



ADVANCING THERAPY.  
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## | Q3 2005 Financial Report |

It has been another busy quarter for the team here at MIGENIX as we prepared for a very active year ahead on the clinical front. With our significant transformation over the past three years, we have now achieved several important steps in building our business. Here are some of the highlights of our third fiscal quarter:

- Enrollment was initiated in a Phase II monotherapy study of MX-3253 (celgosivir) for the treatment of chronic Hepatitis C Virus (“HCV”) infections and preparations were advanced for a planned Phase II combination study.
- A Special Protocol Assessment (SPA) was filed with the U.S. FDA by Cadence Pharmaceuticals, our partner in the MX-226 program for the prevention of catheter-related infections. Preparations are being made to begin a pivotal Phase III study.
- Preparatory work was advanced to initiate a Phase I/II study for MX-4509 in Alzheimer’s patients looking for biomarkers as an initial indication of neurodegenerative activity.

Enrollment in the MX-3253 Phase II HCV monotherapy study has reached approximately 40 patients. Tolerability, safety, and HCV viral loads at various time points during the study will be evaluated. We plan to start a Phase II combination study (MX-3253 in combination with interferon and ribavirin) around mid-year calendar 2005. Results from the monotherapy study are expected in the third quarter of calendar 2005 and, interim results from the combination study are expected around the end of this calendar year or early next year. In preclinical HCV models, MX-3253 has shown synergistic effects with interferon and ribavirin.

Cadence Pharmaceuticals, our partner on the MX-226 program for catheter-related infections, submitted a Special Protocol Assessment (SPA) to the US FDA for a confirmatory Phase III clinical study. Once approved, the SPA will provide a written agreement that if the study is performed according to the protocol, and the results are successful, a New Drug Application (NDA) can be submitted. Although there is never a guarantee from the FDA, an SPA does provide more certainty in the NDA marketing approval process. We anticipate Cadence will get SPA approval in the second quarter and will begin the pivotal Phase III study around mid-year (calendar 2005).

The latest-stage product candidate from our degenerative disease portfolio is MX-4509. We are preparing to initiate a Phase I/II clinical study of MX-4509 mid-year calendar 2005. This study will be in Alzheimer’s patients as a representative neurodegenerative group and will evaluate safety and biomarkers as an initial indication of activity. We expect the biomarker data from this trial will be applicable to several potential neurodegenerative indications including Friedreich’s ataxia, which provides a possible near-term opportunity for a new clinical indication. Friedreich’s ataxia, the most common recessive neurodegenerative disease, has the potential to be an Orphan indication, is 100% fatal, affects children usually between the ages of 5 and 15, and there is no current treatment. From the clinical perspective, the disease has clear clinical endpoints and could therefore involve less complicated trials than other neurodegenerative diseases. We expect data from the Phase I/II study in the fourth quarter of this year and the preclinical data needed for Friedreich’s ataxia by the first quarter of calendar 2006.

Regarding MX-594AN, our acne product, discussions with multiple parties continue and we remain optimistic about a partnership for this important asset.

With our pipeline in place and many clinical and preclinical activities ongoing in the near-term, this will be a very important year for MIGENIX, where several of the expected milestones have the potential to take our business to the next level. On behalf of the entire MIGENIX team, we thank you for your continued support.

Sincerely,

“Jim DeMesa”

Jim DeMesa, MD  
President and CEO  
March 16, 2005



The following should be read in conjunction with the audited consolidated financial statements and management's discussion & analysis of financial condition and results of operations for the year ended April 30, 2004; and the interim unaudited consolidated financial statements for the three and nine months ended January 31, 2005, including the related notes therein. All amounts unless indicated otherwise are expressed in Canadian dollars. The discussion and analysis contained in this Management Discussion & Analysis is as of March 16, 2005. Additional information on the Company including the Company's Annual Information Form is available on SEDAR at [www.sedar.com](http://www.sedar.com).

## **BUILDING THE PRODUCT PIPELINE**

As part of the long-term strategy to build value, the Company on an ongoing basis investigates in-licensing and/or acquisition opportunities to expand its product pipeline with solid technology and promising product opportunities. Since May 2002, five in-licensing and acquisition transactions have been completed including the August 31, 2004 acquisition of San Diego based MitoKor, Inc ("MIGENIX SD").

The Company pursuant to an April 15, 2004 definitive agreement completed the acquisition of MIGENIX SD by way of an Agreement and Plan of Merger and Reorganization whereby MIGENIX SD merged with MBI Acquisition Corp., an indirect wholly owned subsidiary of the Company.

MIGENIX SD was a private biotechnology company focused on the research and development of drugs for the treatment of major medical conditions related to mitochondrial dysfunction. The most advanced program in the MIGENIX SD portfolio is MX-4509 (see "DEVELOPMENT PROGRAMS - MX-4509: Treatment of Neurodegenerative Diseases"). The MIGENIX SD pre-clinical programs include opportunities in arthritis, Friedreich's ataxia, Parkinson's disease, retinitis pigmentosa, glaucoma, stroke/ischemia reperfusion injury, and obesity, although not all of these opportunities are currently being actively developed (see "DEVELOPMENT PROGRAMS - Other Research and Development Programs"). Adding MIGENIX SD's clinical and preclinical product candidates for neurological, metabolic, and degenerative diseases broadens the Company's therapeutic focus and increases the commercial opportunities available to MIGENIX. The acquisition of MIGENIX SD also brings license agreements with Pfizer and Wyeth providing the potential for future revenues and funding for current patent related costs.

Total consideration paid by the Company to acquire MIGENIX SD was approximately \$6.9 million consisting of:

- 5,388,691 common shares as upfront consideration valued at approximately \$6 million;
- 4,000,000 Series E convertible redeemable preferred shares for up to US\$4 million in potential future milestones upon the achievement of certain product development or other milestones related to the MIGENIX SD portfolio (see "LIQUIDITY AND CAPITAL RESOURCES" and "OUTSTANDING SHARE DATA"). The Series E preferred shares were recorded at their aggregate redemption value of US\$1;
- \$0.9 million of transaction related costs; and
- a US\$25,000 cash payment.

The \$6.9 million purchase consideration has been allocated based on the fair value of the tangible assets, intangible assets and liabilities acquired as at August 31, 2004, resulting in approximately: \$5.8 million in intangible assets, \$1 million in net working capital, and \$0.1 million in other non-current assets.

Additionally as part of the transaction MIGENIX assumed warrants for the purchase of 128,862 common shares with a weighted average exercise price of US\$13.53 with expiry dates through June 22, 2011. The estimated fair value of the assumed warrants is nominal and no value has been included in the purchase consideration in respect of them.

## **NAME and TRADING SYMBOL CHANGES**

On September 9, 2004, the Company changed its name to MIGENIX Inc. (previously "Micrologix Biotech Inc.") having obtained shareholder approval for the change. The Company's common shares now trade under the symbol "MGI" (previously "MBI") on the Toronto Stock Exchange and "MGIFF" (previously "MGIXF") in the over the counter market (pink sheets) in the United States.

On September 24, 2004 MitoKor Inc. changed its name to MIGENIX Corp.

## **DEVELOPMENT PROGRAMS**

### ***MX-226: Prevention of Catheter-Related Infections***

On August 2, 2004 MIGENIX entered into a Collaboration and License Agreement for the development and commercialization of MX-226 with Cadence Pharmaceuticals, Inc., ("Cadence"; formerly Strata Pharmaceuticals Inc.) a private, hospital-focused specialty pharmaceutical company based in San Diego. Under the terms of the agreement Cadence have the exclusive rights to market and sell MX-226 in North America and Europe. Consideration to MIGENIX in exchange for these rights is as follows:

- \$2.6 million in up-front payments, consisting of a \$2.0 million (US\$1.5 million) license fee and a \$0.6 million (US\$0.5 million) equity investment in MIGENIX common shares at \$1.08 per common share including a premium to market. See "RESULTS OF OPERATIONS - Revenues" for accounting treatment of these up-front payments.
- up to US\$30 million in development and commercialization milestone payments; and
- a double-digit royalty on net sales



In addition, Cadence will fund the clinical, regulatory, and commercialization costs related to MX-226 and will assume responsibility for manufacturing. MIGENIX and Cadence have formed a Joint Development Management Committee to oversee the development of MX-226.

By mid-year calendar 2005, Cadence plans to initiate a pivotal Phase III trial with MX-226 under a Special Protocol Assessment ("SPA") to support the submission of a New Drug Application ("NDA") for marketing approval in the United States. Cadence has submitted its request for the SPA to the US Food and Drug Administration ("FDA") and is working towards obtaining the SPA. The SPA is for a confirmatory pivotal Phase III trial using, as the primary endpoint, prevention of local catheter site infections, which achieved statistical significance in a Phase III study completed in July 2003. Local catheter site infections are associated with catheter colonization and catheter-related bloodstream infections. In the Phase III trial catheter colonization, considered to be a precursor to catheter-related bloodstream infections, was also reduced by a statistically significant amount. An SPA is a process that provides for an official FDA evaluation of Phase III clinical study protocols and provides trial sponsors with a written agreement that the proposed design and analysis of the studies would be adequate to support a license application submission (such as an NDA) if the study is performed according to the SPA and the results are successful. There can be no assurance that an SPA will guarantee approval of the product but it does make the process more predictable.

Cadence's decision to conduct a Phase III trial pursuant to an SPA was one of the regulatory options available to advance MX-226 following the completion of the Phase III trial in July 2003 and subsequent meetings with the FDA. In the meetings with the FDA the opportunity to submit an NDA for catheter-related bloodstream infections based on data from the one Phase III study was another option available, which Cadence is not currently pursuing.

#### ***MX-594AN: Treatment of Acne***

In order to meet the objective of advancing the MX-594AN program while managing the Company's cash resources MIGENIX is pursuing a development and commercialization partner for the further development of MX-594AN. Discussions and due diligence activities with potential partners are continuing. The Company did not enter into a license agreement before the end of calendar 2004 as originally forecasted. Furthermore it is not known whether a license agreement can be completed under terms acceptable to the Company (see "RISKS and UNCERTAINTIES"). The Company is delaying certain MX-594AN development work until a partner is secured, because we believe decisions about the program are best made with the input of the partner.

#### ***MX-3253: Treatment of Chronic Hepatitis C virus ("HCV") Infections***

MIGENIX's development plan for MX-3253 includes two initial Phase II clinical studies: a monotherapy study and a combination therapy study. This is the general approach taken in the development of most HCV drugs as the current "gold standard" treatment regime for HCV uses a combination therapy approach (combination of pegylated interferon and ribavirin) which is effective in only about 40 to 50% of patients with genotype 1 HCV (the most common type in North America).

Enrollment of patients in the Phase II monotherapy study started in October 2004 and has reached approximately 40 patients with results from the trial forecasted for the third quarter of calendar 2005. This study is an open-label, randomized, dose-response, 12-week monotherapy study being conducted in Canada and it is planned to enroll approximately 60 treatment naïve or interferon-intolerant HCV patients divided into three dosage groups. The study will provide the first safety, tolerability, and dosage information in HCV patients, as well as evaluate viral load reductions as an assessment of the early anti-viral activity of MX-3253 on its own. Regarding viral load reductions in the Phase II monotherapy trial there is a broad range of potential outcomes. These include results ranging from little or no reduction to large decreases in viral load. Assuming MX-3253 is well tolerated in the monotherapy study with no serious adverse reactions all results within this range would allow us to advance MX-3253 as a combination therapy since preclinical studies have demonstrated synergistic activity between MX-3253, interferon and ribavirin.

The Phase II combination study which is planned to start around mid-year calendar 2005 will explore the efficacy of MX-3253 in combination with products currently on the market, in addition to the safety and tolerability of the drug combinations in HCV patients. We are forecasting to have interim (12 week treatment) data from the combination study around the end of calendar 2005 and completed efficacy data (24 week treatment) around mid-year calendar 2006. Preparations for the trial are progressing. Prior to enrolling patients in the trial the Company will need to complete various activities including, but not limited to: regulatory submissions, obtaining various approvals, site contracts, securing the supply of the products to be used in combination with MX-3253 and manufacturing of MX-3253.

#### ***MX-4509: Treatment of Neurodegenerative Diseases***

MX-4509 is an orally-administered drug candidate which was acquired as part of the acquisition of MIGENIX SD (see "BUILDING THE PRODUCT PIPELINE" above). MX-4509 was well tolerated in a Phase I clinical trial and has demonstrated activity in animal models used for assessing drugs for Alzheimer's disease and neuroprotection.

A Phase I/II study in Alzheimer's patients of MX-4509 as a neurodegenerative agent is planned to start by mid-year calendar 2005, looking at biomarkers as an indication of the activity of MX-4509. Preparations for the Phase I/II trial are progressing. Prior to enrolling patients in the trial the Company will need to complete various activities including, but not limited to: regulatory submissions, obtaining various approvals and site contracts. Results from the Phase I/II study are forecasted for the fourth quarter calendar 2005.

Our plan is to generate clinical and non-clinical data that will allow us to advance MX-4509 into further clinical trials for one or more of three potential indications: Alzheimer's disease, Parkinson's disease, and/or Friedreich's ataxia. A strategy we are evaluating is the potential for MX-4509 in Friedreich's ataxia (niche market opportunity, 100% fatal, with no treatment available) and obtaining an



Orphan Drug designation, providing us the chance for a less complex development path to market. We may also conduct a dose ranging Phase I study in healthy volunteers to further study the pharmacokinetics and safety of various doses of MX-4509.

### **Other Research and Development Programs**

Activities in the MX-2401 program (an intravenous drug candidate being developed for the treatment of serious, hospital-acquired Gram-positive infections) have focused on manufacturing process development in preparation for the GLP non-clinical studies required to initiate clinical development and certain confirmatory pre-clinical studies. As a result of program prioritization, the Company is delaying some MX-2401 development work in order to focus resources on more advanced programs (MX-3253 and MX-4509). The Company is pursuing several opportunities that would provide funding for this program.

Lead identification and optimization work in the Company's pre-clinical non-nucleoside HCV program has resulted in the identification of a lead series of compounds. Compounds in the lead series have been shown to inhibit the target enzyme, do not indiscriminately bind to RNA, and are active *in vitro* in both the BVDV virus and HCV replicon assays (surrogate models for HCV).

Work in the Company's other preclinical programs, including the programs acquired as part of the MIGENIX SD acquisition, are focused on advancing existing compounds into *in vivo* models of efficacy and pharmacology. Some of the programs are being advanced solely with the Company's resources, whereas other programs are proceeding with minimal internal resources through testing services funded by third parties such as NIH (HBV program) and the Foundation for Fighting Blindness (retinitis pigmentosa), as well as by an external service provider providing chemistry services that were part of the MIGENIX SD assets acquired. The Company is pursuing opportunities for funding programs that are not being fully advanced at this time and we may terminate some of these programs in the future.

### **CRITICAL ACCOUNTING POLICIES**

The Company's unaudited interim consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"). These accounting principles require the Company to make certain estimates and assumptions. The Company believes that the estimates and assumptions upon which it relies are reasonable based upon information available at the time that these estimates and assumptions are made. Actual results could differ from these estimates. Areas of significant estimates include recognition of revenue, amortization of intangible assets and the review of the carrying value of intangible assets.

The significant accounting policies that the Company believes are the most critical in fully understanding and evaluating the reported financial results include the following:

#### Revenue recognition

Revenue to date has primarily been derived from licensing fees (which are comprised of initial fees) and research and development collaboration payments from licensing arrangements. Initial fees received which require the Company's ongoing involvement are deferred and amortized into income over the term of the underlying product development period. A change in the underlying product development period from the originally estimated period may result in a longer or shorter period that the initial fees are amortized into income, decreasing or increasing income respectively. Research and development collaboration revenues generally compensate the Company for non-clinical and clinical expenses related to development programs under collaborative/licensing agreements for certain product candidates of the Company, and are recognized as revenue when the research and development activities are performed under the terms of the agreements.

#### Research and development costs

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

Under US GAAP, costs to purchase rights to unproven technology which may not have alternate future uses are expensed as research and development. Under Canadian GAAP, the purchase cost of such rights is generally capitalized as an intangible asset. Any change in the future use or impairment of unproven technology may have a material impact on the Company's Canadian GAAP financial statements.

#### Intangible assets

Intangible assets are comprised of patents, trademarks, technology licenses and acquired technology and include technology licenses and acquired technology acquired in exchange for equity instruments issued by the Company. Intangible assets are amortized on a straight-line basis over the estimated useful life of the underlying technologies of ten years. The Company determines the estimated useful lives for intangible assets based on a number of factors such as legal, regulatory or contractual limitations; known technological advances; anticipated demand; and the existence or absence of competition. The Company reviews the carrying value of its intangible assets on a quarterly basis to determine if there has been a change in any of these factors. A significant change in these factors may warrant a revision of the expected remaining useful life of the intangible asset, resulting in accelerated amortization or an impairment charge, which would impact earnings.



Stock-based compensation

The Company grants stock options to executive officers and directors, employees, consultants and advisory board members pursuant to its stock option plans. The Company records all stock-based awards to the Company's executive officers, directors and employees granted, modified or settled since May 1, 2003, and all stock-based awards to non-employees granted, modified or settled since May 1, 2002, at fair value. The fair value of stock options is estimated at the date of grant using the Black-Scholes Option Pricing Model and is amortized over the vesting terms of the stock options. The Company discloses the proforma effects to the loss and loss per common share for the period as if the fair value method had been used for awards to executive officers, directors and employees granted, modified or settled during the period May 1, 2002 to April 30, 2003.

**SELECTED QUARTERLY FINANCIAL DATA (Unaudited)**

The following table provides summary financial data for our last eight quarters:

<i>(Expressed in thousands, except per share amounts)</i>	Three months ended,			
	January 31, 2005 ("Q3/05")	October 31, 2004 ("Q2/05")	July 31, 2004 ("Q1/05")	April 30, 2004 ("Q4/04")
Revenue	\$181	\$2,152	\$-	\$ -
Operating Loss	\$(3,270)	\$(919)	\$(3,256)	\$(3,954)
Net Loss	\$(3,162)	\$(964)	\$(3,138)	\$(3,816)
Basic and diluted loss per common share	\$(0.05)	\$(0.02)	\$(0.06)	\$(0.07)
Weighted average number of common shares outstanding	59,794	59,641	53,635	51,384

	Three months ended,			
	January 31, 2004 ("Q3/04") <sup>(1)</sup>	October 31, 2003 ("Q2/04") <sup>(1)</sup>	July 31, 2003 ("Q1/04") <sup>(1)</sup>	April 30, 2003 ("Q4/03")
Revenue	\$926	\$654	\$1,392	\$1,842
Operating Loss	\$(1,871)	\$(3,535)	\$(3,240)	\$(4,324)
Net Loss	\$(1,737)	\$(3,512)	\$(3,154)	\$(4,406)
Basic and diluted loss per common share	\$(0.04)	\$(0.08)	\$(0.07)	\$(0.10)
Weighted average number of common shares outstanding	46,691	46,691	46,566	46,312

(1) The Operating Loss, Net Loss and Basic and diluted loss per common share figures for Q1/04, Q2/04 and Q3/04 have been adjusted from those originally reported to reflect the Company's adoption in April 2004 (effective May 1, 2003) of the amendments to the recommendations of the CICA Handbook section 3870, Stock-Based Compensation and Other Stock-Based Payments.

The primary factors affecting the magnitude of the Company's operating losses and net losses have been research and development expenses (particularly clinical program development costs) not funded by a partner, licensing revenues, and write-downs in intangible assets. The operating loss and net loss in Q2/05 was significantly lower than previous quarters as a result of \$2.1 million in licensing revenue from the collaboration and license agreement with Cadence entered into during Q2/05 (see "Revenues" below). The operating loss and net loss in Q3/04 were significantly lower than previous quarters as a result of \$0.8 million in previously deferred revenue being recorded as licensing revenue following the termination of the MX-226 license Agreement with Fujisawa Healthcare in January 2004, the completion of the MX-594AN Phase IIb trial in Q2/04 (not funded by a partner) and no active clinical trials during the period. The operating loss and net loss in Q4/03, Q2/04 and Q4/04 include intangible asset write-downs of approximately, \$0.7 million, \$0.2 million and \$0.9 million, respectively.



## RESULTS OF OPERATIONS

### Overview

The loss for the three months ended January 31, 2005 ("Q3/05") was \$3.2 million (\$0.05 per common share) compared with a loss of \$1.7 million (\$0.04 per common share) for the same period last year ("Q3/04") and a loss of \$1.0 million (\$0.02 per common share) for the three months ended October 31, 2004 ("Q2/05"). The increase in the Q3/05 loss compared to Q3/04 and Q2/05 is principally attributable to the MX-226 licensing revenues in Q3/04 and Q2/05 (see "Revenues" below) and increased research and development activity in Q3/05 (see "Research and Development Expenses" below). The Q3/05 loss attributable to the MIGENIX SD operations and programs acquired on August 31, 2004 (see "BUILDING THE PRODUCT PIPELINE"; and "DEVELOPMENT PROGRAMS – MX-4509: Treatment of Neurodegenerative Diseases") is \$0.9 million (\$nil in Q3/04; \$0.6 million in Q2/05).

The loss for the nine months ended January 31, 2005 ("YTD Fiscal 2005") is \$7.3 million (\$0.13 per common share) as compared to \$8.4 million (\$0.18 per common share) for the same period last year ("YTD Fiscal 2004"). The decrease in the YTD Fiscal 2005 loss compared to the YTD Fiscal 2004 loss is principally attributable to MX-226 licensing revenue (see "Revenues" below). The YTD Fiscal 2005 loss attributable to the MIGENIX SD operations and programs is \$1.5 million (\$nil in YTD Fiscal 2004).

MIGENIX has been unprofitable since its formation and has incurred a cumulative deficit of \$93.1 million to January 31, 2005.

### Revenues

Licensing revenues for Q3/05 were \$nil (\$0.9 million for Q3/04; \$2.1 million for Q2/05) and were \$2.1 million for YTD Fiscal 2005 (\$1.2 million for YTD Fiscal 2004). The Q2/05 and YTD Fiscal 2005 licensing revenues are pursuant to the August 2004 collaboration and license agreement with Cadence and include the \$2.0 million upfront fee and a \$0.1 million premium on the equity investment made by Cadence (see "DEVELOPMENT PROGRAMS - MX-226: Prevention of Catheter-Related Infections").

Research and development collaboration revenues for Q3/05 were \$0.2 million (\$nil for Q3/04; \$0.1 million for Q2/05) and were \$0.2 million for YTD Fiscal 2005 (\$1.8 million for YTD Fiscal 2004). Research and development collaboration revenues for YTD Fiscal 2004 were principally pursuant to the MX-226 license agreement with Fujisawa Healthcare which ended in January 2004.

### Research and Development Expenses

Research and development expenses were \$2.2 million in Q3/05 (\$1.7 million in Q3/04; \$1.7 million in Q2/05) and were \$6.1 million for YTD Fiscal 2005 (\$8.3 million for YTD Fiscal 2004).

Clinical development program costs were \$0.8 million of research and development expenses in Q3/05 (\$0.4 million in Q3/04; \$0.4 million in Q2/05) and were \$1.3 million in YTD Fiscal 2005 (\$3.8 million in YTD Fiscal 2004). The decrease in clinical program development costs for YTD Fiscal 2005 compared with YTD Fiscal 2004 is due to decreases in costs in the MX-226 (Phase III trial completed in Q1/04 and Cadence is now responsible for the development of MX-226 in North America and Europe; see "DEVELOPMENT PROGRAMS - MX-226: Prevention of Catheter-Related Infections") and in the MX-594AN (Phase IIb trial completed in Q2/04; see "DEVELOPMENT PROGRAMS - MX-594AN: Treatment of Acne") programs. Total clinical development costs for MX-226 were \$nil for YTD Fiscal 2005 compared with \$1.6 million for YTD Fiscal 2004. Total clinical development costs for MX-594AN were \$0.1 million for YTD Fiscal 2005 compared with \$1.9 million for YTD Fiscal 2004. These decreases were partially offset by increases in the MX-3253 and MX4509 programs. YTD Fiscal 2005 costs in the MX-3253 program were \$0.5 million (YTD Fiscal 2004: \$nil) (Phase II monotherapy trial started in Q2/05; see "DEVELOPMENT PROGRAMS - MX-3253: Treatment of Chronic HCV Infections") and \$0.5 million (YTD Fiscal 2004: \$nil) of costs in the MX-4509 program (preparations for the Phase I/II trial; see "DEVELOPMENT PROGRAMS - MX-4509: Treatment of Neurodegenerative Diseases").

Personnel costs were \$0.9 million of research and development expenses in Q3/05 (\$1.0 million in Q3/04; \$0.9 million in Q2/05) and were \$2.5 million for YTD Fiscal 2005 (\$2.8 million for YTD Fiscal 2004).

Other research and development expenses including non-clinical programs were \$0.5 million of research and development expenses in Q3/05 (\$0.3 million in Q3/04; \$0.4 million in Q2/05) and were \$2.3 million for YTD Fiscal 2005 (\$1.7 million for YTD Fiscal 2004). The increase for YTD Fiscal 2005 as compared to YTD Fiscal 2004 is principally due to manufacturing process development activities in the MX-2401 program during Fiscal 2005 (see "DEVELOPMENT PROGRAMS - Other Research and Development Programs" above).

### General and Corporate Expenses

General and corporate expenses for Q3/05 were \$0.9 million (\$0.9 million in Q3/04; \$1.1 million in Q2/05) and were \$2.9 million for YTD Fiscal 2005 (\$2.7 million for YTD Fiscal 2004). Personnel costs were \$0.5 million of general and corporate expenses in Q3/05 (\$0.6 million in Q3/04; \$0.6 million in Q2/05) and were \$1.7 million of general and corporate expenses for YTD Fiscal 2005 (\$1.8 million for YTD Fiscal 2004).

### Capital Asset Expenditures and Amortization

Expenditures in Q3/05 for capital assets were \$nil (\$nil in Q3/04) bringing YTD Fiscal 2005 capital asset expenditures to \$0.2 million (\$0.3 million for YTD Fiscal 2004 including \$0.2 million in capital assets acquired through a capital lease). Amortization expense for Q3/05 is \$0.1 million (Q3/04: \$0.1 million; Q2/05: \$0.1 million) bringing YTD Fiscal 2005 amortization to \$0.3 million (\$0.3 million for YTD Fiscal 2004).



**Intangible Asset Expenditures, Write-Downs and Amortization**

Expenditures in Q3/05 for intangible assets were \$0.1 million (\$0.1 million for Q3/04). YTD Fiscal 2005 intangible asset expenditures are \$0.4 million (\$0.5 million for YTD Fiscal 2004) before the \$5.8 million in intangible assets acquired on the acquisition of MIGENIX SD (see "BUILDING THE PRODUCT PIPELINE"). Amortization expense for Q3/05 is \$0.2 million (Q3/04: \$0.1 million; Q2/05: \$0.2 million) bringing YTD Fiscal 2005 amortization to \$0.5 million (\$0.3 million for YTD Fiscal 2004). There have been no significant write-downs of intangible assets during YTD Fiscal 2005 (\$0.2 million YTD Fiscal 2004).

**Other Income and Expenses**

Interest income during YTD Fiscal 2005 was \$0.3 million compared to \$0.5 million during YTD Fiscal 2004. The decrease for YTD Fiscal 2005 is primarily due to lower average interest rates and cash balances during the period. The Company had a foreign exchange loss of \$0.1 million during YTD Fiscal 2005 (\$0.2 million during YTD Fiscal 2004) as a result of the impact of the declining value of the U.S. dollar as compared to the Canadian dollar on the Company's U.S. dollar denominated monetary assets.

**LIQUIDITY AND CAPITAL RESOURCES**

At January 31, 2005, MIGENIX had cash, cash equivalents and short-term investments of \$15.5 million (October 31, 2004: \$19.2 million; April 30/04: \$21.7 million) and net working capital of \$13.8 million (October 31, 2004: \$16.5 million; April 30, 2004: \$19.1 million). The decrease in net working capital from April 30, 2004 is primarily attributable to the YTD Fiscal 2005 loss of \$6.2 million (excluding non-cash amortization and stock-based compensation) which was partially offset by the Cadence equity investment (\$0.5 million) and the net cash acquired on the acquisition of MIGENIX SD (\$0.6 million).

MIGENIX has financed its operations primarily through the sale of equity securities and through January 31, 2005, the Company has raised approximately \$107 million in net proceeds. Licensing and collaboration revenues have also been an important source of funding for the Company. As part of the collaboration and license agreement with Cadence the Company received \$2.1 million in licensing revenue (see "REVIEW of OPERATIONS - Revenues"). MIGENIX reviews its funding options on a regular basis and intends to seek additional equity and non-equity funding as required to support its operations (see "RISKS and UNCERTAINTIES").

The Company uses redeemable/convertible preferred shares to facilitate the acquisition and in-licensing of new technologies and drug candidates including the MIGENIX SD acquisition completed in August 2004 (See "BUILDING THE PRODUCT PIPELINE"; and "OUTSTANDING SHARE DATA"). The preferred shares provide the Company with a vehicle to structure acquisitions and in-licensing transactions so as to lower the immediate cash cost to the Company, to pay milestones in the future in cash and/or common shares (at the Company's option) based on the achievement of pre-determined product development milestones. MIGENIX anticipates that it will continue to use preferred shares in this manner in the future.

In addition to the milestone payments associated with the Company's preferred shares the Company may in the future pursuant to license and acquisition agreements have to pay the following in respect of the lipopeptide, polyene, oligonucleotide and celgosivir programs: (i) up to additional US\$3 million cash if certain drug development milestones are achieved; and (ii) royalties on product sales and/or sub-licensing revenues.

As at January 31, 2005, the Company had the following contractual obligations and commitments <sup>(1)</sup>:

<b>Contractual Obligations (1)</b>					
Payments due by period (Expressed in thousands of dollars)	<b>Total</b>	<b>Less than 1 year</b>	<b>1 – 3 years</b>	<b>4 – 5 years</b>	<b>After 5 years</b>
Capital Lease Obligations	84	62	22	-	-
Operating Leases	129	129	-	-	-
Purchase Obligations (2)	2,480	2,480	-	-	-
<b>Total Contractual Obligations</b>	<b>2,693</b>	<b>2,671</b>	<b>22</b>	<b>-</b>	<b>-</b>

(1) Excludes contingent milestone and royalty obligations pursuant to the Company's preferred shares and under license and acquisition agreements (see "LIQUIDITY AND CAPITAL RESOURCES" above and "OUTSTANDING SHARE DATA" below).

(2) Represents obligations under research, manufacturing, and service agreements



## OUTSTANDING SHARE DATA

As at March 16, 2005, there are:

- 60,988,428 (January 31, 2005: 60,980,928; April 30, 2004: 54,820,901) common shares outstanding;
- 14,600,000 (January 31, 2005: 14,600,000; April 30, 2004: 10,600,000) convertible redeemable preferred shares outstanding consisting of 350,000 Series A, 1,000,000 Series B, 5,250,000 Series C, 4,000,000 Series D and 4,000,000 Series E preferred shares. The 4,000,000 Series E preferred shares were issued on August 31, 2004 as part of the MIGENIX SD acquisition (see "BUILDING THE PRODUCT PIPELINE"). The outstanding preferred shares represent US\$14.6 million (January 31, 2005: US\$14.6 million; April 30, 2004: US\$10.6 million) in potential future milestone payments in the lipopeptide/MX-2401 (US\$675,000), polyene (US\$675,000), oligonucleotide/MX-1121 (US\$5,250,000), celtosivir/MX-3253 (US\$4,000,000) and MIGENIX SD (US\$4,000,000) programs. These preferred shares are to be redeemed or converted from time to time upon the achievement of specified drug development and other milestones in the respective programs. During the next 12 months the Company estimates that 100,000 preferred shares (US\$100,000) could become convertible or redeemable pursuant to these milestones which would result in a charge of US\$100,000 to research and development expenses. Each series of preferred shares includes provision for the Company to redeem the entire series for US\$1, in which event any development milestones achieved subsequent to such redemption would be payable in cash; and
- stock options outstanding for the purchase of 4,009,575 (January 31, 2005: 4,116,300; April 30, 2004: 3,895,475) common shares at an average exercise price per common share of \$1.43 (January 31, 2005; \$1.45; April 30, 2004: \$1.57)

As at January 31, 2005 and March 16, 2005, there are:

- warrants outstanding for the purchase of 5,980,526 (April 30, 2004: 5,851,664) common shares as follows:
  - [i] 5,851,664 (April 30, 2004: 5,851,664) common shares at a weighted average exercise price per common share of \$1.56 (range of \$1.25 to \$3.00), expiring between December 5, 2005 and December 3, 2007, of which warrants for the purchase of 1,970,414 common shares have an exercise feature allowing the warrant holders to elect to satisfy their obligation to pay the exercise price to the Company by accepting a lesser number of common shares; and
  - [ii] 128,862 (April 30, 2004: nil) common shares at a weighted average net exercise price per common share of US\$13.53 (range of US\$13.21 to US\$17.75), expiring between June 21, 2006 and June 22, 2011. These warrants were assumed by the Company as part of the MIGENIX SD acquisition. If these warrants are exercised the warrant holders would be entitled to receive up to US\$88,659 in milestone payments (milestones are the same as those for the Series E preferred shares – see "BUILDING THE PRODUCT PIPELINE"), payable at the Company's option, in cash and/or common shares

## OFF-BALANCE SHEET ARRANGEMENTS

The Company does not have any off-balance sheet arrangements.

## RELATED PARTY TRANSACTIONS

During Q3/05 and YTD Fiscal 2005, the Company incurred legal fees of \$nil and \$0.4 million respectively (\$0.1 million and \$0.3 million, respectively for Q3/04 and YTD Fiscal 2004) inclusive of sales taxes, payable to a law firm where the Secretary of the Company is a partner. This amount is payable under normal trade terms.

## RISKS AND UNCERTAINTIES

MIGENIX believes that its funds on hand at January 31, 2005, together with program prioritization and cost management efforts and expected interest income, should be sufficient for its operating and capital needs for approximately the next 12 to 15 months before any equity or non-equity financings. MIGENIX will need to raise additional funds in support of its operations (see "LIQUIDITY and CAPITAL RESOURCES") and there is no assurance that such funds can be obtained. Our anticipated annual burn rate is in the \$13 million to \$15 million range. To meet this burn rate and/or maintain a sufficient cash position to fund its operations MIGENIX may need to delay certain planned development work including the MX-3253 and/or MX-4509 clinical trials, may sell or out-license certain development programs, and/or reduce other expenditures. Our future cash flows and capital requirements will depend on many factors, including, but not limited to, the following: the progress of our research and development programs including: clinical trials and the magnitude and scope of these activities; our ability to establish and maintain corporate collaborations and licensing arrangements including for our MX-594AN acne drug candidate; the amount of milestone based licensing payments, if any, from Cadence, Spring Bank, Pfizer and Wyeth; the time and costs involved in obtaining regulatory approvals; the time and costs involved in scaling up the commercial manufacturing of our products; the amount of government and/or grant funding obtained; the costs involved in preparing, filing, prosecuting, maintaining, defending and enforcing patent claims; our strategy to develop, acquire or license new technologies and products and other factors not within our control.

Without a partner and/or additional funding, the development of MX-594AN will be further delayed (see "DEVELOPMENT PROGRAMS – MX-594AN: Treatment of Acne). Failure to partner could result in the sale or termination of the MX-594AN program. If the Company is not successful in out-licensing the MX-594AN program, terminates the program and/or determines that the carrying value of the program should be written down, this would not have a significant impact on operating results.



No product candidates being developed by MIGENIX have been approved to be marketed commercially. The Company's business entails significant risks, including the costs, time and uncertainties involved to obtain the required regulatory approvals to market new drugs, the uncertainties involved in preclinical and clinical testing to obtain the information required for regulatory approvals and for marketing of new drugs, the availability of capital and corporate alliances, managing and maintaining corporate collaborations, the degree of patent and other intellectual protection, intense competition and technological change. There can be no assurance that MIGENIX's research and development activities will result in any commercially viable products.

**Forward-looking Statements**

This Management's Discussion & Analysis of Financial Condition and Results of Operations ("MD&A") contains forward-looking statements within the meaning of the United States Private Securities Litigation Reform Act of 1995. All statements other than statements of historical fact may be deemed to be forward-looking statements. Forward-looking statements frequently, but not always, use the words "intends", "plans", "believes", "anticipates" or "expects" or similar words; that events "will", "may", "could" or "should" occur; and/or include statements concerning our strategies, goals, plans and expectations. Forward-looking statements in this MD&A include, but are not limited to: having results from the current Phase II MX-3253 monotherapy study in the third quarter calendar 2005; starting the MX-3253 Phase II combination therapy study around mid-year calendar 2005 and having interim efficacy data (12 weeks treatment) around the end of calendar 2005 with completed efficacy data (24 weeks treatment) around mid-year calendar 2006; Cadence initiating a MX-226 confirmatory pivotal Phase III trial under a Special Protocol Assessment mid-year calendar 2005; starting a Phase I/II study of MX-4509 in mid-2005 in Alzheimer's patients, with results expected in the fourth quarter calendar 2005; the Company's anticipated annual burn rate being in the \$13 million to \$15 million range; up to US\$100,000 in milestones being achieved and payable in the next 12 months pursuant to the Company's preferred shares; and the Company's funds at January 31, 2005 together with program prioritization, cost management efforts and expected interest income being sufficient for approximately 12 to 15 months of operations. These forward-looking statements involve a number of significant risks and uncertainties that could cause actual results, achievements and/or other events to differ materially from those reflected in the forward-looking statements. These factors include, but are not limited to: the possibility that favourable relationships with licensees/collaborators cannot be established or, if established, will be abandoned by the licensees/collaborators before completion of product development; our early stage of development; uncertainties as to the requirement that a drug be found to be safe and effective after extensive clinical trials and the possibility that the results of such trials, if commenced and completed, will not establish the safety or efficacy of our products; risks relating to requirements for approvals by government agencies such as the FDA and/or Health Canada before products can be tested in clinical trials and ultimately marketed; the possibility that such government agency approvals will not be obtained in a timely manner or at all or will be conditioned in a manner that would impair our ability to advance development and/or market the product successfully; the possibility that we will not be able to raise adequate capital to fund our operations through the process of developing and testing a successful product or the risk that future financings will be completed with unfavourable terms; the fact that our technology is in the research stage and therefore the potential benefits for human therapy are unproven; the possibility that we will not successfully develop any products; the possibility that advances by competitors will cause our proposed products not to be viable, the risk that our patents could be invalidated or narrowed in scope by judicial actions or that our technology could infringe the patent or other intellectual property rights of third parties; the possibility that any products successfully developed by us will not achieve market acceptance; and other risks and uncertainties which may not be described herein. For further information concerning these and other risks and uncertainties in the MD&A, see the Company's Annual Information Form and Annual Report on Form 20-F. These risks and uncertainties should be considered when evaluating forward-looking statements, and undue reliance should not be placed upon forward-looking statements.

The Company's actual results, performance or achievement could differ significantly from those expressed in, or implied by, forward-looking statements. Accordingly, MIGENIX cannot assure that any of the events anticipated by our forward-looking statements will occur, or if they do, what impact they will have on our results of operations and financial condition.

Forward-looking statements are based on the beliefs, opinions and expectations of MIGENIX' management at the time they are made, and we do not assume any obligation to update our forward-looking statements if those beliefs, opinions, or expectations, or other circumstances, should change. Readers should not place undue reliance on forward looking statements.

**CONSOLIDATED BALANCE SHEETS**

As at	January 31, 2005	April 30, 2004
(Unaudited—in thousands of Canadian dollars)	\$	\$
<b>ASSETS</b>		
<b>Current</b>		
Cash and cash equivalents	3,809	4,382
Short-term investments	11,643	17,336
Amounts receivable	249	73
Prepaid expenses and deposits	1,159	269
<b>Total current assets</b>	<b>16,860</b>	<b>22,060</b>
Long-term investments	1	1
Other assets (note 4)	-	463
Capital assets	1,228	1,358
Intangible assets (note 5)	7,718	2,178
	<b>25,807</b>	<b>26,060</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Current</b>		
Accounts payable and accrued liabilities	2,975	2,944
Current portion of capital lease obligation	62	58
<b>Total current liabilities</b>	<b>3,037</b>	<b>3,002</b>
Capital lease obligation	22	68
<b>Total liabilities</b>	<b>3,059</b>	<b>3,070</b>
<b>Shareholders' equity</b>		
Common shares (note 6[a][i])	115,215	108,517
Preferred shares (note 6[a][ii])	-	-
Contributed surplus	586	262
Deficit	(93,053)	(85,789)
<b>Total shareholders' equity</b>	<b>22,748</b>	<b>22,990</b>
	<b>25,807</b>	<b>26,060</b>

See accompanying notes

On behalf of the Board:

"Jim DeMesa"

"Colin Mallet"

Director

Director

**CONSOLIDATED STATEMENTS OF LOSS AND DEFICIT**

(Unaudited—in thousands of Canadian dollars except per share amounts)	Three months ended January 31, <i>(restated – note 3)</i>		Nine months ended January 31, <i>(restated – note 3)</i>	
	2005 \$	2004 \$	2005 \$	2004 \$
<b>REVENUE</b>				
Licensing (note 8[a])	-	926	2,089	1,154
Research and development collaboration	181	-	244	1,818
	181	926	2,333	2,972
<b>EXPENSES</b>				
Research and development	2,214	1,729	6,147	8,260
General and corporate	913	892	2,887	2,665
Amortization	308	176	728	529
Write-down of intangible assets	16	-	16	164
	3,451	2,797	9,778	11,618
<b>Operating loss for the period</b>	<b>(3,270)</b>	<b>(1,871)</b>	<b>(7,445)</b>	<b>(8,646)</b>
<b>Other income (expense)</b>				
Interest income	98	132	311	477
Foreign exchange gain (loss)	10	2	(130)	(234)
	108	134	181	243
<b>Loss for the period</b>	<b>(3,162)</b>	<b>(1,737)</b>	<b>(7,264)</b>	<b>(8,403)</b>
Deficit, beginning of period	(89,891)	(80,236)	(85,789)	(73,570)
<b>Deficit, end of period</b>	<b>(93,053)</b>	<b>(81,973)</b>	<b>(93,053)</b>	<b>(81,973)</b>
<b>Basic and diluted loss per common share</b> (note 6[d])	<b>(0.05)</b>	<b>(0.04)</b>	<b>(0.13)</b>	<b>(0.18)</b>
<b>Weighted average number of common shares outstanding</b> (in thousands – note 6[d])	<b>59,794</b>	<b>46,691</b>	<b>57,690</b>	<b>46,649</b>

See accompanying notes

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

	Three months ended January 31,		Nine months ended January 31,	
	<i>(restated – note 3)</i>		<i>(restated – note 3)</i>	
	2005	2004	2005	2004
	\$	\$	\$	\$
<i>(Unaudited—in thousands of Canadian dollars)</i>				
<b>OPERATING ACTIVITIES</b>				
Loss for the period	(3,162)	(1,737)	(7,264)	(8,403)
Items not affecting cash:				
Amortization	308	176	728	529
Stock based compensation	73	24	324	210
Write-down of intangible assets	16	-	16	164
Gain on disposal of capital assets	-	-	(3)	(1)
Changes in non-cash working capital items relating to operating activities:				
Accrued interest on short-term investments	10	290	111	302
Amounts receivable	(115)	1,200	(79)	2,878
Prepaid expenses and deposits	(216)	37	(302)	188
Accounts payable and accrued liabilities	(586)	(208)	170	(1,782)
Deferred revenue	-	(925)	-	(1,153)
<b>Cash (used in) operating activities</b>	<b>(3,672)</b>	<b>(1,143)</b>	<b>(6,299)</b>	<b>(7,068)</b>
<b>FINANCING ACTIVITIES</b>				
Issuance of common shares, net of issue costs	-	-	543	75
Proceeds on exercise of stock options	-	-	1	2
Repayment of capital lease obligation	(15)	(14)	(43)	(36)
<b>Cash (used in) provided by financing activities</b>	<b>(15)</b>	<b>(14)</b>	<b>501</b>	<b>41</b>
<b>INVESTING ACTIVITIES</b>				
Funds from short-term investments	4,700	8,690	19,401	21,646
Purchase of short-term investments	(4,459)	(6,888)	(13,819)	(17,732)
Other asset expenditures	-	-	(491)	-
Purchase of capital assets	(2)	(8)	(172)	(135)
Intangible asset expenditures	(65)	(86)	(351)	(473)
Acquisition of business, net of cash acquired (note 4)	-	-	635	-
Proceeds on disposal of capital assets	-	-	22	1
<b>Cash provided by investing activities</b>	<b>174</b>	<b>1,708</b>	<b>5,225</b>	<b>3,307</b>
<b>(Decrease) increase in cash and cash equivalents</b>	<b>(3,513)</b>	<b>551</b>	<b>(573)</b>	<b>(3,720)</b>
Cash and cash equivalents, beginning of period	7,322	1,901	4,382	6,172
<b>Cash and cash equivalents, end of period</b>	<b>3,809</b>	<b>2,452</b>	<b>3,809</b>	<b>2,452</b>
<b>Supplemental cash flow information</b>				
Issuance of common shares for acquisition of a business (note 4)	-	-	5,999	-
Issuance of preferred shares for acquisition of a business (note 4)	-	-	-	-
Issuance of common shares in settlement of accounts payable and accrued liabilities	155	-	155	-
Increase in capital lease obligation	-	-	-	176

See accompanying notes

## NOTES TO CONSOLIDATED INTERIM FINANCIAL STATEMENTS

Nine months ended January 31, 2005 (Unaudited—Canadian dollars)

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### 1. BASIS OF PRESENTATION

The accompanying unaudited interim consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles for interim financial statements. The accounting policies used in the preparation of these unaudited interim consolidated financial statements are consistent with the Company's most recent annual audited consolidated financial statements for the year ended April 30, 2004. These unaudited interim consolidated financial statements and notes do not include all disclosures required for annual financial statements and should be read in conjunction with the annual audited consolidated financial statements of the Company.

In the opinion of management, all adjustments (including reclassification and normal recurring adjustments) necessary to present fairly the financial position, results of operations and cash flows have been made. Interim results are not necessarily indicative of results for a full year.

### 2. SIGNIFICANT ACCOUNTING POLICIES

#### Consolidation

These consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, MIGENIX Corp., M&M Holdings Inc. and Micrologix Biotech (USA) Inc., incorporated under the laws of the State of Delaware, USA. Micrologix Biotech (USA) Inc. is inactive, M&M Holdings Inc. was incorporated April 1, 2004 to acquire MitoKor Inc. (note 4) and MIGENIX Corp. is the former MitoKor Inc. entity merged with the Company's former subsidiary, MBI Acquisition Corp. (note 4). Intercompany accounts and transactions have been eliminated on consolidation.

#### Foreign exchange

The accounts of the Company and its integrated foreign subsidiaries are translated using the temporal method of accounting for the translation of foreign currency amounts into Canadian dollars. Under this method, monetary assets and liabilities expressed in foreign currencies are translated at rates of exchange in effect at the balance sheet date. All other assets and liabilities are translated at the rates prevailing at the dates the assets were acquired or liabilities incurred. Revenue and expense items are translated at the average exchange rate during the period. Exchange gains and losses are included in the determination of loss for the period.

### 3. CHANGE IN ACCOUNTING POLICY

#### Stock-based compensation

In accordance with the amended recommendations of the Canadian Institute of Chartered Accountants ("CICA") Handbook Section 3870, *Stock-based Compensation and Other Stock-based Payments*, the Company adopted a change in its accounting for employee stock-based awards during the year ended April 30, 2004 and accordingly, compensation expense was recognized prospectively for stock-based awards made to executive officers, directors and employees beginning May 1, 2003. Prior to the adoption of this method, the Company had been disclosing in the notes to its financial statements the pro-forma effect of accounting for stock options awarded to executive officers, directors and employees under the fair value

method. As this change was implemented in the fourth quarter of Fiscal 2004, the previously reported figures for the three and nine months ended January 31, 2004 have been restated resulting in an increase of \$10,000 in research and development expenses and an increase of \$9,000 in general and corporate expenses for the three months ended January 31, 2004 (\$69,000 and \$122,000 respectively, for the nine months ended January 31, 2004). This had no impact on the basic and diluted loss per common share for the three and nine months ended January 31, 2004.

#### 4. ACQUISITION OF MITOKOR, INC.

On August 31, 2004, the Company through its wholly owned subsidiary M&M Holdings Inc. acquired 100% of the issued and outstanding common and preferred shares of MitoKor, Inc ("MitoKor"). The acquisition was completed by way of an Agreement and Plan of Merger and Reorganization whereby MitoKor merged with, MBI Acquisition Corp., an indirect wholly owned subsidiary of the Company.

MitoKor was a private biotechnology company focused on the research and development of drugs for the treatment of major medical conditions related to mitochondrial dysfunction. Mitochondria are present in nearly all animal and plant cells and are essential to human life. Mitochondrial dysfunction is a significant contributing factor to over 75 diseases.

MitoKor's most advanced program MITO-4509 (now designated MX-4509), is an orally-administered drug candidate which has demonstrated activity in animal models of Alzheimer's disease and other neurodegenerative conditions, and was well tolerated in a Phase I clinical trial. MitoKor's pre-clinical programs include opportunities in arthritis, Friedreich's ataxia, retinitis pigmentosa, glaucoma, stroke/ischemia reperfusion injury and obesity. Additionally MitoKor has license agreements with Pfizer (note 8[b]) and Wyeth (note 8[c]).

Total consideration paid by the Company to acquire MitoKor was approximately \$6,900,000 comprised of the following:

	<u>\$(000's)</u>
Cash	33
Common shares (note 6[a][i])	5,999
Preferred shares (below)	-
Transaction costs	<u>868</u>
Total purchase consideration	<u>6,900</u>

As part of the consideration the Company issued 4,000,000 Series E preferred shares (note 6[a][iii]) which represent up to US\$4,000,000 in potential future milestone payments related to the MitoKor technologies over the 36 month period ending August 31, 2007 (as specified in the merger agreement).

Additionally, the Company assumed MitoKor preferred warrants that if exercised by the warrant holders would result in the Company issuing approximately 128,862 common shares and potentially having to pay an additional US\$88,659 in milestone payments (note 6[c][ii]). The estimated fair value of the assumed warrants is nominal and no value has been included in the purchase consideration in respect of them.

Transaction costs (as above) include costs previously recorded as other assets on the balance sheet prior to the completion of the acquisition.

#### 4. ACQUISITION OF MITOKOR, INC. (cont'd)

The purchase price was allocated based on the fair value of the tangible and intangible assets and liabilities acquired as at August 31, 2004, resulting in the following allocation:

	<u>\$(000's)</u>
Assets acquired:	
Cash	935
Amounts receivable	97
Prepaid expenses	588
Other non-current assets	109
Capital assets	23
Intangible assets (Acquired technology)	<u>5,792</u>
Total assets acquired	<u>7,544</u>
Less: liabilities assumed	
Current liabilities	(644)
Net assets acquired	<u><u>6,900</u></u>

The transaction has been accounted for using the purchase method of accounting for business combinations. These consolidated financial statements include MitoKor's results of operations for the period September 1, 2004 through January 31, 2005.

On September 24, 2004 MitoKor changed its name to MIGENIX Corp.

#### 5. INTANGIBLE ASSETS

	<b>Cost</b> <b>\$ (000's)</b>	<b>Accumulated</b> <b>Amortization</b> <b>\$ (000's)</b>	<b>Net Book</b> <b>Value</b> <b>\$ (000's)</b>
<b>January 31, 2005</b>			
Acquired technology (note 4)	6,915	510	6,405
Technology licenses	798	612	186
Patents	1,550	425	1,125
Trademarks	2	-	2
	<u>9,265</u>	<u>1,547</u>	<u>7,718</u>
<b>April 30, 2004</b>			
Acquired technology	1,123	168	955
Technology licenses	798	577	221
Patents	1,300	318	982
Trademarks	28	8	20
	<u>3,249</u>	<u>1,071</u>	<u>2,178</u>

## 6. SHARE CAPITAL

### [a] Issued and outstanding

#### [i] Common shares

	Number of Shares (000's)	Amount \$ (000's)
<b>Balance, April 30, 2004</b>	54,821	108,517
Issued pursuant to acquisition of a business (note 4)	5,389	5,999
Issued pursuant to fee payable on acquisition of a business (note 4)	152	155
Issued pursuant to license agreement (note 8[a])	617	543
Issued for cash pursuant to exercise of stock options	2	1
<b>Balance, January 31, 2005</b>	<b>60,981</b>	<b>115,215</b>

On September 8, 2004 the Company obtained shareholder approval to eliminate the maximum number of common shares which the Company is authorized to issue.

#### [ii] Preferred shares

	Number of Shares (000's)	Amount \$ (000's)
Series A	350	-
Series B	1,000	-
Series C	5,250	-
Series D	4,000	-
<b>Balance, April 30, 2004</b>	<b>10,600</b>	<b>-</b>
Series E issued pursuant to acquisition of a business (below)	4,000	-
<b>Balance, January 31, 2005</b>	<b>14,600</b>	<b>-</b>

On September 8, 2004 the Company obtained shareholder approval to eliminate the maximum number of preferred shares which the Company is authorized to issue.

#### Series E Preferred Shares

On August 31, 2004 the Company issued 4,000,000 Series E preferred shares as part of the consideration for the acquisition of MitoKor Inc. (note 4). Upon the achievement of any of the milestones specified in the MitoKor merger agreement, the corresponding number of Series E preferred shares for such milestone will, at the Company's option, be converted into common shares and/or be redeemed for cash. As the achievement of the specified milestones is uncertain, the Series E preferred shares have been recorded at an aggregate value of US\$1. The Company at its option may at any time redeem the then outstanding Series E preferred shares for an aggregate value of US\$1 and any milestone payments that become payable after such redemption, if any, would be payable in cash.

If the Company elects to convert any of the Series E preferred shares into common shares the conversion will be based upon the average closing price of the Company's common

shares on the Toronto Stock Exchange for the 10 trading days prior to the applicable conversion date.

**[b] Stock options**

[i] Stock option transactions and the number of stock options outstanding with respect to both the 1996 and 2000 Stock Option Plans are summarized as follows:

	Number of Common Shares (000's)	Weighted Average Exercise Price \$
<b>Balance, April 30, 2004</b>	3,895	1.57
Options granted	406	1.09
Options exercised	(2)	(0.81)
Options forfeited/expired	(183)	(3.29)
<b>Balance, January 31, 2005</b>	<b>4,116</b>	<b>1.45</b>

The stock options expire at various dates between March 9, 2005 and December 5, 2012.

[ii] The following table summarizes information about options outstanding with respect to both the 1996 and 2000 Stock Option Plans at January 31, 2005:

Range of Exercise Prices \$	Options Outstanding			Options Exercisable	
	Outstanding (000's)	Weighted Average Exercise Price \$	Weighted Average Remaining Contractual Life (years)	Exercisable (000's)	Weighted Average Exercise Price \$
0.55-0.71	102	0.64	5.2	84	0.63
0.72-1.07	2,023	0.89	5.7	1,290	0.86
1.08-1.59	1,321	1.50	5.3	1,110	1.56
1.60-2.30	361	1.84	5.4	231	1.85
2.31-3.40	89	3.00	3.2	89	3.00
3.41-5.37	111	4.61	1.7	111	4.61
5.38-8.00	109	5.92	3.0	109	5.92
	<b>4,116</b>	<b>1.45</b>	<b>5.3</b>	<b>3,025</b>	<b>1.57</b>

[iii] Stock-based Compensation Expense

The Company recorded stock based compensation expense of \$73,000 and \$324,000, respectively for the three and nine months ended January 31, 2005 (\$24,000 and \$210,000, respectively for the three and nine months ended January 31, 2004) relating to stock options granted to executive officers, directors, and employees since May 1, 2003 (note 3) and to consultants since May 1, 2002. This expense has been allocated on the same basis as cash compensation resulting in \$25,000 and \$128,000, respectively (2004 - \$11,000 and \$76,000, respectively) being allocated to research and development and \$48,000 and \$196,000, respectively (2004 - \$13,000 and \$134,000, respectively) being allocated to general and

corporate for the three and nine months ended January 31, 2005. The estimated fair value of the stock options granted was determined using the Black-Scholes option pricing model with the following weighted average assumptions:

	Three months ended January 31,		Nine months ended January 31,	
	2005	2004	2005	2004
Annualized volatility	79.4%	n/a	81.6%	91.6%
Risk-free interest rate	3.5%	n/a	3.5%	3.4%
Expected life of options in years	5.0	n/a	5.0	5.0
Dividend yield	0.0%	n/a	0.0%	0.0%

The weighted average fair value of stock options granted during the three months ended January 31, 2005 was \$0.52 (no options were granted in the three months ended January 31, 2004) and was \$0.74 for the nine months ended January 31, 2005 (2004 - \$1.11). The estimated fair value of stock options is amortized to expense over the vesting period of the stock options.

The Black-Scholes pricing model was developed for use in estimating the fair value of traded options which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly variable assumptions including the expected stock price volatility. Because the Company's stock options have characteristics significantly different from those of traded options, and because changes in the input assumptions can materially affect the fair value estimate, the Black-Scholes model does not necessarily provide a reliable single measure of the fair value of the Company's stock options.

[iv] Pro-forma Information – Stock-based Compensation

Pro-forma disclosure is required to reflect the impact on the Company had it elected to adopt the fair value method of accounting for options granted to executive officers, directors and employees effective May 1, 2002. If the computed fair values of stock options granted May 1, 2002 to April 30, 2003 had been amortized to expense over their vesting periods, the loss and loss per common share would have been:

(thousands, except per share amounts)	Three months ended January 31,		Nine months ended January 31,	
	2005	2004	2005	2004
Loss for the period as reported	(3,162)	(1,737)	(7,264)	(8,403)
Compensation charge related to stock options granted to executive officers, directors and employees during the period May 1, 2002 to April 30, 2003	(26)	(26)	(77)	(78)
Pro-forma loss for the period	(3,188)	(1,763)	(7,341)	(8,481)
Pro-forma basic and diluted loss per common share	(0.05)	(0.04)	(0.13)	(0.18)

## 6. SHARE CAPITAL (continued)

### [c] Warrants

As at January 31, 2005, the Company had warrants outstanding for the purchase of 5,980,526 (April 30, 2004: 5,851,664) common shares as follows:

[i] 5,851,664 (April 30, 2004: 5,851,664) common shares at a weighted average exercise price per common share of \$1.56 (range of \$1.25 to \$3.00), expiring between December 5, 2005 and December 3, 2007, of which warrants for the purchase of 1,970,414 common shares have an exercise feature allowing the warrant holders to elect to satisfy their obligation to pay the exercise price to the Company by accepting a lesser number of common shares; and

[ii] 128,862 (April 30, 2004: nil) common shares at a weighted average net exercise price per common share of US\$13.53 (range of US\$13.21 to US\$17.75), expiring between June 21, 2006 and June 22, 2011. These warrants were assumed as part of the acquisition of MitoKor and if exercised and the maximum milestone payments associated with the Series E Preferred shares (note 4) are achieved could result in the payment to the warrant holders of US\$88,659 in milestone payments, payable at the Company's option, in cash and/or common shares.

### [d] Loss per common share

(thousands, except per share amounts)	Three months ended January 31,		Nine months ended January 31,	
	2005	2004	2005	2004
		<i>(restated -note 3)</i>		<i>(restated -note 3)</i>
<b>Numerator:</b>				
Loss for the period	(3,162)	(1,737)	(7,264)	(8,403)
<b>Denominator:</b>				
Weighted average number of common shares outstanding including escrowed shares	60,981	47,878	58,877	47,836
Less: weighted average number of escrowed shares outstanding	(1,187)	(1,187)	(1,187)	(1,187)
Weighted average number of common shares outstanding	59,794	46,691	57,690	46,649
<b>Basic and diluted loss per common share</b>	(0.05)	(0.04)	(0.13)	(0.18)

## 7. SEGMENTED INFORMATION

The Company operates primarily in one business segment with operations located in Canada and the United States. During the three months ended January 31, 2005, 32%, 38% and 30% of total revenue was derived from three collaborators in the United States [92%, 5% and 3%, respectively for the nine months ended January 31, 2005]. At January 31, 2005, included in amounts receivable are \$58,000, \$36,000 and \$65,000 due from these three research collaborators, respectively. During the three and nine months ended January 31, 2004, 100% of total revenue was derived from one collaborator in the United States. At April 30, 2004 there was \$nil included in amounts receivable related to this collaborator.

## 8. COLLABORATIVE DEVELOPMENT, LICENCING AND ROYALTY AGREEMENTS

### **[a] Cadence Pharmaceuticals Inc (“Cadence”; formerly Strata Pharmaceuticals Inc)**

Further to an exclusive negotiation period entered into on June 3, 2004, the Company and Cadence on August 2, 2004 entered into a collaboration and license agreement for the North American and European rights to the Company's product candidate for the prevention of catheter-related infections. Pursuant to the terms of the agreement the Company received: (i) an up-front fee of \$1,979,000 (US\$1,500,000) of which \$267,000 (US\$200,000) was received during the three months ended July 31, 2004 as a non-refundable exclusivity fee; and (ii) an equity investment of \$665,000 (US\$500,000) priced at a premium to market. As part of the agreement, the Company is also entitled to receive development and commercialization milestone payments up to US\$30,000,000 and a double-digit royalty on net sales of the product (a portion of certain manufacturing development costs incurred by Cadence up to US\$2,000,000 are to be deducted from royalties). In addition, Cadence is responsible for and will fund the clinical, regulatory, and commercialization costs related to the product candidate and will assume responsibility for manufacturing. The agreement also provides for a Joint Management Development Committee with representatives from both the Company and Cadence.

As the Company will have limited involvement in the ongoing development of the product the licensing fee of \$1,979,000 (inclusive of the exclusivity fee) and the \$110,000 premium on the equity investment were recognized as licensing revenue during the three months ended October 31, 2004. The exclusivity fee of \$267,000 had previously been recorded as deferred revenue at July 31, 2004.

On August 2, 2004, the Company issued 617,284 common shares to Cadence pursuant to the equity investment (note 6[a][i]).

### **[b] Pfizer Inc**

In November 1998, MitoKor (note 4) entered into a collaborative research and development agreement with Pfizer to discover and develop molecules that affect selected mitochondrial targets, focusing on the treatment and prevention of neurodegenerative disease. Under the terms of the agreement, Pfizer funded research performed by MitoKor for a specific number of full time researchers through May 2002. Concurrent with the research and development agreement, MitoKor also entered into a license and royalty agreement with Pfizer pursuant to which MitoKor granted Pfizer an exclusive license to sell certain products developed in connection with the collaborative research and development agreement in exchange for event-based milestone and royalty payments specified in the license and royalty agreement. To date, no milestone payments or royalty income has been received associated with the agreement.

## 8. COLLABORATIVE DEVELOPMENT, LICENCING AND ROYALTY AGREEMENTS

### [c] Wyeth

MitoKor (note 4) is a party to a license agreement with Wyeth. Under the agreement, Wyeth holds an exclusive, worldwide license, as well as options to obtain a license under certain of the Company's patents to develop certain estrogens and estrogen-like compounds for the treatment of human neurodegenerative disease, including Alzheimer's disease and certain other dementias. Wyeth has funded a Phase III clinical trial evaluating the use of estrogens to delay the onset and slow the progression of Alzheimer's disease and certain other dementias in post-menopausal women. The agreement provides for option exercise fees, preclinical and clinical milestone payments and royalty and other payments following the commercial approval of any products developed and launched by Wyeth under this agreement. Wyeth is obligated to use commercially reasonable efforts to develop and commercialize one or more products under this agreement. Wyeth retains the right to terminate this agreement on a product-by-product basis. Written notice requirements are either 90 days or 360 days depending on the country and the status of Wyeth's product marketing efforts. If the agreement is so terminated by Wyeth, the licensed patent rights revert to the Company. To date, no milestone payments or royalty income has been received associated with the agreement.

## 9. RELATED PARTY TRANSACTIONS

All transactions with related parties are recorded at their exchange amounts and accounts payable are subject to normal trade terms. During the three and nine months ended January 31, 2005, the Company incurred legal fees of approximately \$41,000 and \$431,000 respectively [\$100,000 and \$262,000, respectively for the three and nine months ended January 31, 2004] inclusive of sales taxes, payable to a law firm where the Secretary of the Company is a partner. Included in accounts payable and accrued liabilities at January 31, 2005, is approximately \$168,000 [2004 - \$120,000] owed to this law firm.