

Allon Therapeutics Inc.

Every  
71 seconds  
someone  
develops  
Alzheimer's

First Quarter Report  
March 31, 2008



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## Corporate Profile

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Allon Therapeutics Inc. is a Canadian biotechnology company developing drugs that protect against neurodegenerative conditions such as Alzheimer's disease, mild cognitive impairment and schizophrenia-related cognitive impairment. Allon has two technology platforms derived from neuroprotective proteins that are formed naturally in the brain. Compounds from these two platforms have demonstrated broad efficacy in numerous pre-clinical models of neurodegenerative diseases. Allon launched two Phase II clinical trials in 2006 and began a third trial in the third quarter of 2007.

- As part of the Company's program to develop AL-108 as a disease-modifying treatment for Alzheimer's disease, a phase II trial is currently evaluating AL-108 in patients with amnesic mild cognitive impairment, a precursor to Alzheimer's.
- AL-108 is also being evaluated as a treatment for schizophrenia-related cognitive impairment, a condition considered the most significant roadblock for schizophrenia patients' return to productivity.
- AL-208 is being evaluated as a treatment for the mild cognitive impairment experienced by patients who undergo coronary artery bypass graft (MCI-CABG) surgery. The Company expects to have efficacy data from this trial in the middle of 2008.

The Company is listed on the Toronto Stock Exchange under the trading Symbol "NPC" (Neuro Protection Company) and based in Vancouver.

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## Letter to Shareholders

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Dear Shareholders:

I am very pleased to report that our company has met all of our clinical and financial objectives for the First Quarter, highlighted by human clinical trial results demonstrating that AL-108 improved the memory function of patients with amnesic mild cognitive impairment (aMCI), a precursor to Alzheimer's disease.

The top-line data from our Phase IIa clinical trial establishes the potential for AL-108 to become the first drug to impact the progression of Alzheimer's. This achievement is the most important to date for Allon — and it has given us a strong position from which to negotiate a development and commercialization partnership with a major pharmaceutical company. We are optimistic that we will complete a partnership in 2008 that fully values the significant potential of our technology.

We will announce full results from the Phase IIa trial during the summer and then take the next step in our Alzheimer's program by beginning a Phase IIb trial in late 2008 evaluating AL-108 in patients with mild-to-moderate Alzheimer's.

Our other clinical development programs are all also proceeding on schedule. We expect to report data around mid-year from our Phase II trial evaluating AL-208 as a treatment for mild cognitive impairment (MCI) in patients who have undergone coronary artery bypass graft (CABG) surgery. Our Phase II trial evaluating AL-108 as a treatment for schizophrenia cognitive impairment continues to enrol patients and we expect to report data from this trial by the end of the year.

Our Phase I clinical trial evaluating the pharmacokinetics of AL-108 (intranasal administration) and AL-208 (intravenous administration) in the blood and cerebrospinal fluid of healthy adult subjects and Alzheimer's patients will be completed and we expect to release results during the Second Quarter.

Subsequent to the end of the First Quarter, we announced results of preclinical studies that demonstrated the potential of our product candidate AL-309 as a treatment for peripheral neuropathy. Millions of people suffer from peripheral neuropathy, a condition in which nerve damage leads to pain, discomfort, numbness and muscle weakness. Among the major causes of neuropathy are diabetes and cancer chemotherapy.

These preclinical results are significant because they confirm a completely new drug development path for our company. AL-309 is the lead candidate in Allon's second neuroprotection technology platform, derived from the brain protein Activity-Dependent Neurotrophic Factor (ADNF). Our clinical-stage drugs AL-108 and AL-208 are derived from our first neuroprotection platform, based on the brain protein Activity-Dependent Neuroprotective Protein (ADNP). ADNP and ADNF are different proteins yielding drugs based on different molecules, with different therapeutic mechanisms and distinct commercial opportunities.

We are now working on finalizing preclinical studies to compile additional data that will enable the Company to file an Investigational New Drug application with the United States Food and Drug Administration for approval to begin evaluating AL-309 in human clinical trials.

I look forward to reporting our continued progress.

Respectfully,



Gordon C. McCauley  
President & CEO

# FINANCIAL INFORMATION

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## MANAGEMENT'S DISCUSSION & ANALYSIS

*The following information should be read in conjunction with the unaudited interim financial statements as at and for the three months ended March 31, 2008 and the 2007 audited consolidated financial statements and their accompanying notes and management's discussion and analysis for the year ended December 31, 2007. The financial statements listed have been prepared in accordance with Canadian generally accepted accounting principles. All dollar amounts are expressed in Canadian dollars unless otherwise specified. Additional information relating to Allon Therapeutics Inc. ("Allon" or the "Company"), including Allon's Annual Information Form (AIF) can be obtained from SEDAR at [www.sedar.com](http://www.sedar.com).*

May 15, 2008

## OVERVIEW

Allon Therapeutics Inc. ("the Company") is a clinical-stage Canadian biotechnology company developing drugs that protect against neurodegenerative conditions which impact the body's central nervous system. The Company has Phase II clinical programs in Alzheimer's disease (AD), in schizophrenia cognitive impairment and in mild cognitive impairment associated with coronary artery bypass graft (MCI-CABG) surgery. The Company is listed on the Toronto Stock Exchange under the trading symbol "NPC" (Neuro Protection Company<sup>TM</sup>) and based in Vancouver.

On February 26, 2008, the Company announced top-line results demonstrating statistically significant human efficacy of its drug AL-108 in a Phase IIa clinical trial in patients with amnesic mild cognitive impairment (aMCI), a precursor to Alzheimer's disease. Statistically significant efficacy was achieved on key endpoints that measured short-term, working and recognition memory, three types of memory that are clinically relevant in AD. The trial also demonstrated that AL-108 was safe and well tolerated by patients. Allon intends to follow this success with a Phase IIb clinical trial to begin in late 2008 in patients with mild-to-moderate Alzheimer's disease.

The Company has two additional on-going human efficacy trials from which data is expected to be released in 2008:

- A Phase II study in schizophrenia cognitive impairment is evaluating the potential of AL-108 to be used as a treatment for the debilitating cognitive impairment suffered by most schizophrenia patients. The efficacy shown by the aMCI trial is relevant in schizophrenia cognitive impairment because the aMCI results show an effect in regions of the brain that are implicated in schizophrenia.

- A Phase II study in MCI-CABG is evaluating the potential for AL-208 to be used as a treatment for the ischemic damage that results from heart bypass surgery as well as other neurodegenerative indications, where intravenous or systemic delivery is preferable.

The Company's compounds are derived from two proprietary technology platforms, activity-dependent neuroprotective protein (ADNP) and activity-dependent neurotrophic factor (ADNF) both of which are important for normal brain function. The Company's clinical compounds, AL-108 and AL-208, are both derived from the ADNP platform as is the pre-clinical candidate AL-408. Two additional pre-clinical compounds, AL-309 and AL-209, are derived from the ADNF platform.

The following table summarizes the development status of each of our research and development programs:

Platform	Compound	Stage of Development	Status
ADNP	AL-108	Phase IIa clinical trial amnesic mild cognitive impairment	Top-line results show efficacy February 26, 2008
		Phase II clinical trial schizophrenia cognitive impairment	Enrolment initiated Q3 2007, top-line data expected Q4 2008
		Phase IIb clinical trial mild-to-moderate Alzheimer's	Commencement Q4 2008
		Phase I human CSF pharmacokinetic study	Dosing completed, data expected Q2 2008
	AL-208	Phase II clinical trial MCI-CABG	Randomization initiated Q1 2007, top-line data expected mid-2008
		Phase I human CSF pharmacokinetic study	Dosing completed, data expected Q2 2008
AL-408	Pre-clinical stage	Pre-clinical pharmacology studies ongoing	
ADNF	AL-309	Pre-clinical stage	Pre-clinical pharmacology and toxicology ongoing
	AL-209	Pre-clinical stage	Pre-clinical pharmacology studies ongoing

## FIRST QUARTER 2008 ACHIEVEMENTS

- Completed patient dosing and released top-line results showing a positive impact on memory function in its AL-108 Phase II human efficacy trial in amnesic mild cognitive impairment, a precursor to Alzheimer's disease;
- Continued enrolment in a Phase II clinical trial evaluating AL-108 a treatment for schizophrenia cognitive impairment in collaboration with Treatment Units for Research of Neurocognition on Schizophrenia (TURNIS);
- Continued enrolment in a Phase II human efficacy trial evaluating the Company's product AL-208 as a treatment for the mild cognitive impairment that commonly occurs following coronary artery bypass graft surgery;
- Initiated a Phase I human clinical trial and completed patient dosing to evaluate the pharmacokinetics of AL-108 and AL-208 in healthy adults and Alzheimer's patients;
- Released pre-clinical study results demonstrating that AL-108 reduces physical brain damage associated with the pathological hallmarks of Alzheimer's disease.

## RESULTS OF OPERATIONS

The Company reported a net loss of \$4,349,737 (\$0.07 per share) for the three months ended March 31, 2008 compared to a net loss of \$2,818,519 (\$0.06 per share) for the three months ended March 31, 2007, representing a quarter over quarter increased loss of \$1,531,218.

Research and development costs accounted for \$3,764,608 of the Company's \$4,599,149 operating expenses and included costs for Allon's three Phase II clinical trials, a Phase I clinical trial, pre-clinical studies to prepare for a Phase IIb in Alzheimer's and to advance pipeline products. During Q1 2008, the Company completed its AL-108 Phase IIa clinical trial in aMCI and released top-line data demonstrating statistically significant efficacy. The Company expects to complete patient dosing in its Phase II clinical trial in MCI-CABG and to release results in mid-2008. With the completion of the AL-108 clinical trial in aMCI and AL-208 clinical trial in MCI-CABG in Q2 2008, the Company expects research and development and overall expenses to significantly decrease during the second quarter and remainder of 2008.

## EXPENSES

### RESEARCH AND DEVELOPMENT

For the three months ended March 31, 2008, research and development expenses were \$3,764,608 compared to \$2,111,945 for the three months ended March 31, 2007. Quarter over quarter research and development expenses increased by \$1,652,663 largely due to the initiation and completion of patient dosing in a Phase I clinical trial, purchase of sufficient drug product to conduct current and planned projects for 2008 and undertaking of additional pre-clinical work in preparation for a Phase IIb study in Alzheimer's. These increases were partly offset by decreased costs associated with the AL-108 Phase IIa clinical trial which was completed in the quarter and for which top-line data was released on February 26, 2008.

The Company completed patient assessment and follow up of for the Phase IIa human clinical trial evaluating AL-108 as a treatment for aMCI, a precursor to Alzheimer's disease. Dosing for this trial was completed in December 2007 and positive top-line results, demonstrating statistically significant human efficacy, were released on February 26, 2008.

In collaboration with the United States National Institute of Mental Health-funded project, TURNS, enrolment has proceeded in a Phase II clinical trial evaluating AL-108 as a treatment for schizophrenia cognitive impairment. Management expects that this trial will be completed and results released in Q4 2008.

During Q1 2008, significant advancements were made towards the completion of enrolment in the randomized portion of its Phase II human clinical trial evaluating AL-208 as a treatment for MCI-CABG surgery. Management expects to release results from this clinical trial in mid-2008.

In January 2008, a Phase I human clinical trial was initiated to evaluate the cerebrospinal fluid (CSF) and plasma pharmacokinetics (PK) of the Company's drugs AL-108 and AL-208 in healthy adult subjects and AD patients. Patient dosing was completed during Q1 2008 and management expects to release data from this trial in Q2 2008.

During Q1 2008, pre-clinical data was presented that demonstrates that AL-108 reduces the physical brain damage associated with the pathological hallmarks of AD and improves the behavioral capacity to learn and retain memory. The Company also continued to advance pre-clinical studies to determine the effectiveness of AL-108 as a treatment for Parkinson's disease.

During Q1 2007, the Company began enrolling patients in a Phase IIa human efficacy trial evaluating AL-108 as a treatment for aMCI. The Company further advanced the development of AL-108 by announcing a collaboration with TURNS, filing an IND and obtaining approval to investigate AL-108 in a Phase II clinical trial as a potential treatment for schizophrenia cognitive impairment. The Company announced results of a Phase Ib clinical trial confirming that AL-108 was safe and well tolerated in healthy elderly subjects after seven days of dosing and also announced that Allon had received funding from MJFF to study AL-108 in pre-clinical models of Parkinson's disease.

The Company advanced its AL-208 compound by confirming the drug's safety profile at 300mg, the highest dose tested in the open label portion of the Phase II human clinical trial evaluating AL-208 as a treatment for MCI-CABG. During Q1 2007, the Company began enrolling patients in the randomized portion of this clinical trial.

### **Clinical stage compounds:**

#### **AL-108**

AL-108 is an intranasally formulated, eight amino acid neuroprotective peptide from the ADNP platform. The Company has two Phase II clinical programs, evaluating AL-108 as a treatment for Alzheimer's disease and schizophrenia cognitive impairment. Development costs for AL-108 were \$2.5 million during the three months ended March 31, 2008.

#### ***Alzheimer's disease***

On February 26, 2008, the Company released top-line results of a Phase IIa clinical trial showing that AL-108 has a positive impact on memory function in patients with aMCI, a precursor to Alzheimer's. Statistically significant efficacy was achieved on key endpoints that measured short-term, working

and recognition memory, three types of memory that are clinically relevant in AD. The trial also demonstrated that AL-108 was safe and well tolerated by patients.

A significant, dose-dependent and durable improvement was seen in two key cognitive tests, delayed-match-to-sample and digit span, tests that are widely recognized and validated as effective measures of memory function. The high dose (15 mg twice daily) group showed a 62.4% improvement from baseline ( $p=0.038$ , versus placebo) in the delayed-match-to-sample test by the end of the trial. Similarly, the high dose group showed a 17.2% increase from baseline ( $p=0.028$ , versus placebo) in the digit span test.

The trial was a double-blind, randomized, placebo-controlled, multiple-dose study to evaluate the safety, tolerability and effect on cognitive function of AL-108 after 12 weeks of intranasal administration in patients with aMCI.

The trial was conducted at 15 sites in the United States in 144 patients aged 55 to 85 years and evenly divided between genders. Three groups of patients received either placebo, low dose of AL-08 (5 mg once a day) or high dose (15 mg twice a day) intranasally for 12 weeks. A Phase IIb study in mild-to-moderate Alzheimer's patients is expected to begin in Q4 2008.

### ***Schizophrenia cognitive impairment***

During the fiscal year ended December 31, 2007, the Company entered into a collaboration with TURNS to investigate AL-108 as a potential treatment for schizophrenia cognitive impairment in a Phase II clinical trial. During Q1 2008, the Company continued enrolling patients and expects to complete the trial and release results during the second half of 2008.

The trial is a multicenter ascending dose, double-blind, placebo-controlled study of AL-108 in chronic schizophrenia funded and managed by TURNS. TURNS was created by the U.S. National Institute of Mental Health to identify drugs that improve cognition and that can be combined with anti-psychotic drugs that control the psychotic episodes that characterize schizophrenia.

### **AL-208**

AL-208 is an intravenously delivered, eight amino acid peptide from the ADNP platform currently in a Phase II clinical trial for MCI-CABG. Development costs for AL-208 were \$0.6 million during the three months ended March 31, 2008.

During Q1 2008, the Company advanced the AL-208 Phase II clinical trial in MCI-CABG with continued progression of enrolment in the randomized portion of the trial. In total, approximately 200 patients will be treated with AL-208 (or placebo) during surgery. Follow up cognitive assessments are conducted several weeks after surgery, to determine the impact of AL-208 on cognitive function compared to patients in the control group.

The results of this trial will indicate AL-208's potential as a treatment for MCI-CABG as well as other neurodegenerative indications where intravenous or systemic delivery is preferable to support further clinical development in acute neurodegenerative diseases such as MCI-CABG, stroke and traumatic brain injury. Results are expected in the middle of 2008.

## **Pre-clinical stage compounds:**

### **AL-309**

AL-309 is a D-amino acid derivative of AL-209 from the ADNF platform. Pre-clinical studies are currently being conducted to determine the potential of AL-309 as a treatment for neuropathies caused by diabetes and chemotherapy. Subsequent to the end of Q1 2008, the Company presented pre-clinical data that demonstrates the potential of AL-309 as a treatment for diabetic neuropathy.

AL-309 has demonstrated efficacy in animal models related to Alzheimer's disease, neuropathy and fetal alcohol syndrome. Pre-clinical studies confirmed that AL-309 passes through both the intestinal wall and blood brain barrier and that effective concentrations can be detected for extended periods of time. These results confirm the potential of AL-309 as a treatment for neurodegenerative disease.

### **AL-209**

AL-209 is a nine amino acid peptide that has demonstrated potent neuroprotective effects in a number of neurodegenerative disease models such as AD, fetal alcohol syndrome and amyotrophic lateral sclerosis (ALS). AL-209 is currently in pre-clinical development

### **AL-408**

AL-408 is a D-amino acid derivative of AL-108. It has demonstrated neuroprotective effects in neurodegenerative animal models of Alzheimer's disease and fetal alcohol syndrome. Furthermore, the compound has also shown to be orally bioavailable, which makes it a potential drug candidate for chronic neurodegenerative disease indications.

## **GENERAL AND ADMINISTRATIVE**

For the three months ended March 31, 2008, general and administrative expenses were \$696,052 compared to \$631,142 for the three months ended March 31, 2007, representing a \$64,910 increase. The increase primarily results from the addition of personnel and modest increases in overhead.

The increases were offset by decreases in stock based compensation expense and lower legal fees. Stock based compensation was affected by a change in estimate detailed further under Stock Based Compensation in this notes to the financial statements.

## **AMORTIZATION**

Amortization expense for the three months ended March 31, 2008 was \$138,489 compared to \$136,430 for the three months ended March 31, 2007. Tangible assets and intellectual property are depreciated on a straight-line basis. The \$2,059 increase primarily resulted from the capitalization and amortization of a milestone payment in Q4 2007 associated with the advancement of AL-108 in a Phase II clinical trial indicated for AD.

## **OTHER (INCOME)/EXPENSES**

For the three months ended March 31, 2008, the Company recognized other income of \$249,412 compared to other income of \$60,998 for the three months ended March 31, 2007. The \$188,414 increase is primarily due to the recognition of a foreign exchange gain on translation during Q1 2008 compared to a loss recorded during the same period in 2007.

Foreign exchange translation gains were \$149,828 for the three months ended March 31, 2008 compared to translation losses of \$48,353 for the three months ended March 31, 2007. The increase primarily resulted from a modest weakening of the Canadian dollar relative to the US dollar during the quarter, which impacts the translation of US dollar balances to Canadian dollars. The Company's policy is to maintain sufficient US denominated cash, cash equivalent and short-term investment balances to match its anticipated US dollar operating expenses. Foreign exchange risk is detailed further in Note 9 of the Company's Financial Statements.

The Company earned interest revenue of \$108,664 and incurred other expenses of \$9,857 for a total of interest and other income of \$98,807 for the three months ended March 31, 2008 compared to interest revenue of \$109,351 for the three months ended March 31, 2007. Though the Company generally maintained higher cash and short-term investment balances during the three months ended March 31, 2008, this was offset by lower interest rates in both Canada and the US.

## QUARTERLY INFORMATION

The following is selected quarterly financial information for the Company, for the eight most recently completed quarters:

(in thousands, except per share data)

	<b>Mar 31, 2008</b>	<b>Dec 31, 2007</b>	<b>Sep 30, 2007</b>	<b>Jun 30, 2007</b>
Interest and other income	\$ 99	\$ 162	\$ 246	\$ 132
Research and development expenses	\$ 3,765	\$ 3,294	\$ 2,128	\$ 1,557
Net and comprehensive loss for the quarter	\$ (4,350)	\$ (4,069)	\$ (3,242)	\$ (2,552)
Loss per share - basic and diluted	\$ (0.07)	\$ (0.07)	\$ (0.05)	\$ (0.05)
	<b>Mar 31, 2007</b>	<b>Dec 31, 2006</b>	<b>Sep 30, 2006</b>	<b>Jun 30, 2006</b>
Interest income	\$ 109	\$ 65	\$ 66	\$ 59
Research and development expenses	\$ 2,112	\$ 2,873	\$ 1,487	\$ 1,230
Net and comprehensive loss for the quarter	\$ (2,819)	\$ (3,579)	\$ (1,976)	\$ (1,984)
Loss per share - basic and diluted	\$ (0.06)	\$ (0.09)	\$ (0.06)	\$ (0.06)

During the quarter ended June 30, 2006, the Company completed dosing for its AL-208 Phase Ib multiple ascending dose clinical trial, initiated in Q1 2006, and began patient enrolment for a Phase II clinical trial for AL-208 indicated for MCI post-CABG. The Company completed preparatory work for a Phase Ib multiple ascending dose clinical trial for AL-108, indicated for AD and scheduled to commence in Q3 2006.

During the quarter ended September 30, 2006, the final expenses for a Phase Ib clinical trial of AL-208 were incurred the Company continued enrolment in the safety portion of its Phase II clinical trial for AL-208. A Phase 1b multiple-ascending dose clinical trial was initiated in AL-108 to evaluate its safety and tolerability as a treatment for AD. Subsequent to the end of the quarter, on November 1, 2006 the Company announced that dosing was completed. Allon also incurred expenses in preparation for a Phase IIa clinical trial of AL-108, expected to begin in the fourth quarter of 2006.

During the quarter ended December 31, 2006, dosing was completed for a Phase Ib multiple, ascending dose clinical trial of AL-108 and for the safety portion of a Phase II clinical trial for AL-208 indicated for MCI post-CABG. The Company filed an IND, received approval and began a Phase IIa

clinical trial of AL-108, indicated for MCI, an Alzheimer's related condition. The Company also completed a \$10.0 million equity financing.

During the quarter ended March 31, 2007, patient enrolment was initiated for a Phase IIa trial of AL-108 indicated for Alzheimer's and The Company filed an IND enabling it to proceed in a Phase II clinical trial to evaluate AL-108 as a treatment for schizophrenia cognitive impairment. The Company released results from an AL-108 Phase Ib clinical trial confirming that administrations of multiple doses of AL-108 were safe and well tolerated in healthy, elderly adults. On completion of the safety portion of the AL-208 Phase II MCI-CABG Allon commenced enrolment for the randomized portion of the study.

During the quarter ended June 30, 2007 the Company continued to advance its AL-108 and AL-208 Phase II human efficacy trials and continued preparations for its Phase II clinical trial of AL-108 for schizophrenia cognitive impairment. This trial is expected to commence in the United States during Q3 2007. The Company confirmed the oral bioavailability of its AL-309 drug compound which has shown potential as a treatment for chronic central nervous system diseases and injuries. The Company also completed a \$15.7 million bought deal equity financing.

During the quarter ended September 30, 2007 the Company significantly advanced its Phase II clinical programs towards delivery of human efficacy data in 2008. Patient screening was completed for the AL-108 Phase IIa human efficacy trial in Alzheimer's and completion of enrolment was announced subsequent to the end of the quarter. The Company continued its collaboration with the NIMH funded project TURNS and NARSAD, marked by the commencement of patient enrolment in the Phase II trial for AL-108 in schizophrenia cognitive impairment. The Company continued enrolling patients and made minor changes to the trial design intended to improve the rate of enrolment for its Phase II human efficacy trial for AL-208 in MCI-CABG. Further, the Company advanced pre-clinical work on its AL-309 compound.

During the quarter ended December 31, 2007, enrolment and dosing were completed in the Phase IIa clinical trial in aMCI, a precursor to AD. The Company also continued enrolment in its two other ongoing Phase II trials in schizophrenia cognitive impairment with AL-108 and in MCI-CABG with AL-208.

During the quarter ended March 31, 2008, the Company completed patient dosing and released top-line results showing a positive impact on memory function in its AL-108 Phase IIa clinical trial in aMCI. The Company continued enrolment in its two remaining Phase II clinical trials, evaluating AL-108 in schizophrenia cognitive impairment and AL-208 in MCI-CABG, and initiated a Phase I clinical trial to evaluate the pharmacokinetics of AL-108 and AL-208 in healthy adults and AD patients. During the quarter, the Company also advanced pre-clinical studies in AL-309 to evaluate this compound as a potential treatment for neuropathy.

## **LIQUIDITY**

The Company devotes its resources primarily to funding its research and development programs. Revenue is currently derived from interest earned on cash and short-term investment balances. At March 31, 2008, the Company had accumulated a deficit of \$38,486,604. Losses are expected to continue in the short-term as the Company invests in research and development, pre-clinical studies and clinical trials. Since inception, the Company has been financed primarily from public and private sales of equity, the exercise of stock options and warrants, interest earned on cash balances and short-term investments.

At March 31, 2008 the Company had cash and short-term investments of \$9,088,483 compared to \$13,126,865 at December 31, 2007. Short-term investments are held in high-grade, liquid commercial paper and other low risk investments which are recorded at fair value. The Company has no exposure to liquidity or other risks associated with certain Asset-Backed Securities. At March 31, 2008 maturities on investments ranged from 30 days to 2 months.

During the quarter ended June 30, 2007 management completed a bought deal financing, issuing 13,059,933 units (the "Units"), comprised of one share and one half share purchase warrant at a price of \$1.20 per Unit. An additional 103,699.5 warrants were also purchased as part of the transaction resulting in gross proceeds of \$15,671,920. Each whole warrant entitles the holder thereof to purchase one common share at an exercise price of \$1.65 for a term of 24 months, expiring on May 29, 2009. The Company requires working capital of \$3,320,945 and commitments for the remainder of 2008 and \$312,000 to fund commitments in 2009 and expects cash on hand and interest revenue to fund operations to the middle of 2009.

At March 31, 2008, the Company had 2,898,350 stock options exercisable at prices ranging from \$.001 to \$1.72 per share and 12,880,541 warrants outstanding and exercisable at prices ranging from \$1.00 to \$1.65. If all outstanding stock options and warrants were exercised, proceeds of \$2,023,679 and \$17,192,424 would be generated respectively.

## **CAPITAL RESOURCES**

Working capital at March 31, 2008 was \$7,733,000 compared to \$11,859,461 million at December 31, 2007. The working capital decrease is a result of the Company's investment in research and development associated with the completion of the AL-108 clinical trial in aMCI, the progression of the Company's remaining two Phase II clinical trials and other research and development initiatives.

Management expects cash on hand and interest revenue to fund operations to the middle of 2009. Additional funding requirements beyond mid 2009 will largely depend on research and development initiatives undertaken by the Company. Such funding may be obtained from the issuance of shares in association with an external financing or, subject to share price, be obtained from the issuance of shares from the exercise of outstanding options or warrants. The Company also has two products in clinical development available for potential partnerships and out-licensing opportunities.

While advancing its clinical development program, management entered into contracts that will remain in effect over several reporting periods. These commitments are performance based with payment subject to the achievement of clinical trial milestones and may be cancelled with written notice. The total current and planned commitments account for \$3,873,888 million of the \$9,088,483 cash and short-term investments on hand towards the completion of its Phase II clinical trials, capital expenditures and other research and development initiatives. The Company had no off-balance sheet arrangements during Q1 2008.

## Schedule of contractual and planned commitments as of December 31, 2007

(in thousands)

	2008	2009	2010	2011-2012	Total
AL-108 Phase IIa Clinical Trial, Alzheimer's	\$ 74	\$ -	\$ -	\$ -	\$ 74
AL-108 Phase II Clinical Trial, schizophrenia	\$ 151	\$ -	\$ -	\$ -	\$ 151
AL-208 Phase II Clinical Trial, MCI-CABG	\$ 327	\$ -	\$ -	\$ -	\$ 327
Pre-Clinical initiatives	\$ 2,341	\$ 302	\$ 231	\$ -	\$ 2,874
Capital and Licensing	\$ 318	\$ 10	\$ 10	\$ 20	\$ 339
Other	\$ 61	\$ -	\$ -	\$ -	\$ 61
Total Company Commitments	\$ 3,272	\$ 312	\$ 241	\$ 20	\$ 3,846

### OUTSTANDING SHARE CAPITAL

At March 31, 2008, the Company had 59,016,666 common shares outstanding. Each common share entitles the holder to one vote per share. At March 31, 2008, there were 4,771,600 options outstanding, of which 2,898,350 were exercisable into an equivalent number of the Company's common shares at exercise prices ranging from \$0.001 to \$1.72. The Company also had 12,880,541 warrants outstanding, entitling holders to purchase one common share of the Company for each warrant held. Warrant exercise prices range from \$1.00 to \$1.65 and warrants may be exercised from dates ranging from current to May 29, 2009.

Allon's shares are listed on the Toronto stock exchange and held by a broad base of investors, none of whom exercise significant influence. See Note 6 of the Company's financial statements for more detail regarding outstanding share capital.

### RELATED PARTY TRANSACTIONS

During the three months ended March 31, 2008, the Company paid a Board member \$12,500 to provide consulting services to assist the Company with general research and the advancement of its drug development programs. The Board member was paid \$12,500 for consulting services for the three months ended March 31, 2007. The Company plans to retain these services throughout 2008.

On February 2, 2007, the Company received \$145,657, from a Senior Officer of the Company, as reimbursement for principle and interest on a loan of \$143,155 granted during the fourth quarter of 2006. The loan was subject to an annual interest rate of 5.25%, consistent with market rates at the time of the loan.

### FIRST QUARTER

For the three months ended March 31, 2008, the Company recorded a net loss of \$4,349,737 (\$0.07 per share), compared to \$2,818,519 (\$0.06 per share) for the same period ended March 31, 2007. Research and development expenses for the three months ended March 31, 2008 were \$3,764,608 compared to \$2,111,945 for the same period ended March 31, 2007. Research and development expenses associated with the progression of the clinical development program are the Company's most significant expense. The increased research and development costs primarily relate to the addition of a Phase I clinical trial, the three clinical Phase II clinical trials in AL-108 and AL-208 increased pre-clinical studies and timing of purchase of drug product. During Q1 2008, the Company completed one of its three Phase II clinical trials and incurred the majority of expenses associated with its Phase I clinical trial. The Company expects to complete a second Phase II clinical trial in mid-

2008 and therefore anticipates significant decreases in R&D expenditures in the second quarter and remainder of 2008.

## **DISCLOSURE CONTROLS AND PROCEDURES**

Disclosure controls and procedures are designed to provide reasonable assurance that material information required to be disclosed in the prescribed filings and reports filed with the Canadian securities regulatory authorities is recorded, processed, summarized and reported on a timely basis. Controls are also designed to provide reasonable assurance that information required to be disclosed is assimilated and communicated to senior management in a timely manner so that appropriate decisions can be made regarding public disclosure. The Company's Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of our disclosure controls and procedures and concluded that they provide reasonable assurance that material information relating to the Company was made known to them and reported as required.

## **INTERNAL CONTROLS OVER FINANCIAL REPORTING**

Management has designed internal controls over financial reporting (ICFR) to provide reasonable assurance regarding the reliability of the Company's financial reporting and the preparation of financial statements in accordance with Canadian generally accepted accounting principles. Management, including the Company's Chief Executive Officer and Chief Financial Officer, is responsible for establishing and maintaining adequate ICFR, which has been developed based on the framework established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Regardless of how well an internal control system is designed and operated, it can provide only reasonable, not absolute, assurance that all misstatements due to error or fraud will be detected or prevented from occurring in the financial statements due to the inherent limitations of any internal control system. During the three months ended March 31, 2008, there were no significant changes in the Company's internal controls over financial reporting that have materially affected or are reasonably likely to affect the Company's internal controls over financial reporting.

## **CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements as well as the reported amount of revenues and expenses during the reporting periods. 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 were made. Actual results may differ from these estimates under different assumptions or conditions. Significant areas requiring management estimates include the valuation and useful life of technology, licenses and patents, clinical trial accounting, accruals for long-term research and development initiatives and valuation of stock based compensation.

## **VALUATION AND AMORTIZATION OF INTANGIBLE ASSETS**

The Company's intangible assets are comprised of purchased technology, patents and licenses. The cost of the Company's intangible assets is amortized on a straight-line basis over the estimated useful life ranging from 15 to 17 years. Factors considered in estimating the useful life of intangible assets include the expected use of the asset by the Company, legal, regulatory and contractual provisions that may limit the useful life, and the effects of competition.

Management evaluates the recoverability of the net book value of its intangible assets on an annual basis based on the expected utilization of the underlying technologies. If the carrying value of the underlying technology exceeds the estimated net recoverable value, calculated based on undiscounted estimated future cash flows, the carrying value will be written down to its fair value, based on the related estimated discounted cash flows. The ultimate amount recoverable will be dependent on the successful development and commercialization of products based on these rights. To date, management has not written down any intangible assets.

## **CLINICAL TRIAL ACCOUNTING**

Clinical trial expenses relating to service agreements with contract research organizations, investigators, contractors and other service providers who conduct certain product development activities that compliment our efforts towards developing our drug candidates are recorded based on the estimated amount of work completed for each trial. During internal reviews, contractual terms and obligations, patient enrolment, correspondence and discussions with service providers are considered in order to estimate the amount of clinical trial expense for an accounting period.

## **RESEARCH AND DEVELOPMENT COSTS**

Research and development costs consist of direct and indirect expenditures related to the Company's clinical and pre-clinical drug development programs. Research and development costs are expensed as incurred unless they meet generally accepted accounting criteria for deferral and amortization. Costs are assessed to determine if they have met the relevant criteria for deferral and amortization at each reporting date. To date, no development costs have been deferred.

## **STOCK BASED COMPENSATION**

Stock based compensation is accounted for in accordance with section 3870 of the CICA handbook. When equity based instruments such as stock options are issued, an estimate of fair value is derived using the Black-Scholes pricing model. The application of this pricing model requires management to estimate several variables, including the period for which the instrument is expected to be outstanding, price volatility of the Company's stock over the relevant timeframe, the determination of a relevant risk free interest rate and an assumption regarding the Company's future dividend rate policy. Changes in one or more assumptions could materially impact the value derived for these equity instruments.

During Q1 2008, the Company revised its estimate of the expected exercise dates from three years to five years for options granted to employees. The impact of this revision increased the fair value of options granted and overall stock based compensation expense to be booked during the vesting period, for each option granted. However the immediate impact was to reduce the quarterly stock

based compensation expense incurred for each option as the affected options are amortized over a period of five years instead of three.

## **NEW ACCOUNTING POLICIES**

On January 1, 2008, the Company adopted three new accounting standards issued by the CICA: Handbook Section 1535, *Capital Disclosures* (Section 1535), Handbook Section 3862, *Financial Instruments – Disclosures* (Section 3862), and Handbook Section 3863, *Financial Instruments – Presentation* (Section 3863). Section 1535 requires the disclosure of the Company's objectives, policies and processes for identifying and managing capital. Sections 3862 and 3863 replace Section 3861 and require the disclosure of information with regards to the significance of financial instruments for the Company's financial position and performance, the nature and extent of risks arising from financial instruments to which the Company is exposed and how the Company manages those risks. Additional disclosure regarding the adoption and effect of these accounting changes on the Company's financial statements is detailed further in Notes 3, 9 and 10 of the Q1 2008 Interim Financial Statements.

## **FUTURE CHANGES IN ACCOUNTING POLICY**

### **International Financial Reporting Standards**

On February 13, 2008, the Accounting Standards Board confirmed that the use of International Financial Reporting Standards (IFRS) will be required, for fiscal years beginning on or after January 1, 2011, for publicly accountable profit-oriented enterprises. After that date, IFRS will replace Canadian GAAP for those enterprises. The Company is currently assessing the impact of these new accounting standards on its consolidated financial statements.

## **FINANCIAL INSTRUMENTS**

Management invests surplus cash balances in short-term high-grade, liquid commercial paper and other low risk, Canadian and US dollar investments. Funds are invested within the guidelines of the Company's investment policy, which mandates preservation of capital and maintaining liquidity while seeking the best available return. The Company has no known exposure to credit or liquidity risk associated with current events in the US and Canadian money markets.

The Company has designated its short-term investments as held-for-trading and measures these assets at fair value based on market value. Though investments may occasionally be sold prior to maturity, most investments are held to maturity, thereby minimizing risk of losses associated with these instruments. During Q1 2008, there were no gains or losses realized on short-term investments. At March 31, 2008 the Company had \$6,062,549 invested in short-term investments.

## **RISKS AND UNCERTAINTIES**

As previously described, cash on hand, together with expected interest income is expected to be sufficient to fund operations to the middle of 2009. Funding needs may, however, vary depending on a number of factors including progress in research and development, the cost associated with completing clinical trials and the regulatory approval process and the costs of enforcing and prosecuting patent claims and other intellectual property rights.

In general, prospects for companies in the biopharmaceutical industry may be regarded as uncertain given the nature of the industry, therefore, investments in such companies should be regarded as

highly speculative. In the future, the Company will need to raise additional funds to continue research and development and clinical trials necessary for market approval. The Company cannot guarantee that financing will be available or that terms for additional financing will be favourable.

This discussion and analysis and other sections of the financial statements contain forward looking statements, which are based on the Company's current expectations and assumptions and are subject to a number of risk factors and uncertainties that could cause actual results to differ materially from those anticipated. Given these risk factors and uncertainties, readers are cautioned not to place undue reliance on such forward-looking information.

Additional information relating to Allon Therapeutics Inc. is disclosed in the Company's Annual Information Form which is filed on SEDAR at [www.sedar.com](http://www.sedar.com).

# ALLON THERAPEUTICS INC.

Consolidated Balance Sheets  
(Unaudited, 2008) and (Audited, 2007)

March 31, 2008 and December 31, 2007

	2008	2007
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 3,025,934	\$ 3,610,590
Short-term investments	6,062,549	9,516,275
Accounts receivable	52,834	66,702
Prepaid expenses and deposits	287,084	260,953
	<u>9,428,401</u>	<u>13,454,520</u>
Property and equipment	47,334	54,232
Intangible assets	6,021,611	6,151,208
	<u>6,068,945</u>	<u>6,205,440</u>
	<u>\$15,497,346</u>	<u>\$19,659,960</u>

## Liabilities and Shareholders' Equity

Current liabilities:		
Unearned revenue (note 5)	\$ 30,317	\$ 68,216
Accounts payable and accrued liabilities	1,665,084	1,526,843
	<u>1,695,401</u>	<u>1,595,059</u>
Shareholders' equity:		
Share capital (note 6)	50,832,635	50,832,635
Additional paid-in capital	1,455,914	1,369,133
Deficit	(38,486,604)	(34,136,867)
	<u>13,801,945</u>	<u>18,064,901</u>
	<u>\$15,497,346</u>	<u>\$19,659,960</u>

Basis of presentation (note 1)

See accompanying notes to consolidated financial statements.

Approved on behalf of the Board:



Frank A. Holler  
Director



C. Michael O'Brian  
Director

# ALLON THERAPEUTICS INC.

Consolidated Statements of Operations, Comprehensive Loss and Deficit  
(Unaudited)

Three months ended March 31, 2008 and 2007

	2008	2007
Expenses:		
Research and development	3,764,608	2,111,945
General and administrative	696,052	631,142
Amortization	138,489	136,430
	<u>4,599,149</u>	<u>2,879,517</u>
Other expense / (income):		
Interest and other income	(98,807)	(109,351)
Foreign exchange loss / (gain)	(149,828)	48,353
Loss / (gain) on short-term investments	(777)	-
	<u>(249,412)</u>	<u>(60,998)</u>
Net and comprehensive loss for the period	(4,349,737)	(2,818,519)
Deficit, beginning of period	(34,136,867)	(21,455,517)
Deficit, end of period	<u>\$ (38,486,604)</u>	<u>\$(24,274,036)</u>
Net loss per share:		
Basic and diluted (note 8)	\$ (0.07)	\$ (0.06)

See accompanying notes to consolidated financial statements.

# ALLON THERAPEUTICS INC.

Consolidated Statements of Cash Flows  
(Unaudited)

Three months ended March 31, 2008 and 2007

	2008	2007
Cash provided by (used in):		
Operations:		
Net and comprehensive loss for the period	\$ (4,349,737)	\$(2,818,519)
Items not involving cash:		
Amortization	138,489	136,430
Stock-based compensation	86,781	95,859
Unrealized (loss) / gain on short-term investments	(777)	363
Change in non-cash operating working capital	88,856	34,523
	(4,036,388)	(2,551,344)
Investments:		
Redemption of short-term investments	3,759,110	4,520,398
Additions to short-term investments	(305,384)	(5,918,685)
Purchase of property, equipment and intangibles	(1,994)	(5,384)
	3,451,732	(1,403,671)
Financing:		
Proceeds from issuance of common shares, net of share issue costs	-	14,320
	-	14,320
Decrease in cash and cash equivalents for the period	(584,656)	(3,940,695)
Cash and cash equivalents, beginning of period	3,610,590	10,369,753
Cash and cash equivalents, end of period	\$ 3,025,934	\$ 6,429,058
Supplementary information:		
Cash received during the period for:		
Interest	\$ 118,089	\$ 77,412

See accompanying notes to consolidated financial statements.

# ALLON THERAPEUTICS INC.

Notes to Consolidated Financial Statements  
(Unaudited)

Three months ended March 31, 2008 and 2007

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## 1. Basis of presentation:

Allon Therapeutics Inc. ("Allon" or the "Company") is a public company incorporated under the Canada Business Corporations Act. Allon is a biopharmaceutical company engaged in the development of drugs to treat neurodegenerative diseases and disorders.

The eventual profitability of the Company and its ability to continue as a going concern is dependent upon many factors, including obtaining appropriate financing as required, successful development of its products, and receiving regulatory approvals. In addition, the biotechnology industry is subject to rapid and substantial technological change which could reduce the marketability of the Company's technology. The Company will be required to obtain additional sources of financing in order to continue its research activities, its issuance and maintenance of patents, realize returns on its assets and discharge its liabilities in the normal course of business.

## 2. Significant accounting policies:

These unaudited interim consolidated financial statements are prepared following accounting policies and methods of their application consistent with the Company's audited annual financial statements and notes for the year ended December 31, 2007 except as described in note 3. These unaudited interim consolidated financial statements do not include all note disclosures required by Canadian generally accepted accounting principles ("Canadian GAAP") for annual financial statements, and therefore should be read in conjunction with the annual audited consolidated financial statements for the year ended December 31, 2007 included in the Company's 2007 Annual Report. The results of operations for the three months ended March 31, 2008 are not necessarily indicative of the results for the full year.

### (a) Comparative figures:

Certain prior period amounts have been reclassified to conform to the current presentation of financial statements.

## 3. New accounting policy:

Effective January 1, 2008, the Company adopted three new accounting standards issued by the Canadian Institute of Chartered Accountants (CICA): Handbook Section 1535, *Capital Disclosures* (Section 1535), Handbook Section 3862, *Financial Instruments – Disclosures* (Section 3862), and Handbook Section 3863, *Financial Instruments – Presentation* (Section 3863).

### a) Financial instruments – disclosure and presentation:

Sections 3862, Financial Instruments - Disclosures ("Section 3862") and 3863, Financial Instruments – Presentation ("Section 3863") replace Handbook Section 3861, Financial Instruments – Disclosure and Presentation ("Section 3861"), revising and enhancing its disclosure requirements, and carrying forward unchanged its presentation requirements.

# ALLON THERAPEUTICS INC.

Notes to Consolidated Financial Statements  
(Unaudited)

Three months ended March 31, 2008 and 2007

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### 3. New accounting policy (continued):

Section 3862 requires entities to provide disclosures in their financial statement that enable users to evaluate the significance of financial instruments on the Company's financial position and its performance, the nature and extent of risks arising from financial instruments to which the Company is exposed during the period and at the balance sheet date and how the Company manages those risks.

Section 3863 establishes standards for presentation of financial instruments and non-financial derivatives. It deals with the classification of financial instruments, from the perspective of the issuer, between liabilities and equities, the classification of related interest, dividend, losses and gains, and circumstances in which financial assets and financial liabilities are offset.

The adoption of these standards did not have any impact on the classification and valuation of the Company's financial instruments. Disclosures resulting from the adoption of these Handbook Sections are detailed further in Note 9 of these interim consolidated financial statements.

#### (b) Capital disclosures:

Section 1535, Capital Disclosures ("Section 1535") specifies the disclosure of (i) an entity's objectives, policies and processes for managing capital; (ii) quantitative data about what the entity regards as capital; (iii) whether the entity has complied with any capital requirements; and (iv) if it has not complied, the consequences of such non-compliance. These additional disclosures are detailed further in Note 10.

### 4. Future changes in accounting policy:

#### International Financial Reporting Standards

On February 13, 2008, the Accounting Standards Board confirmed that the use of International Financial Reporting Standards (IFRS) will be required for fiscal years beginning on or after January 1, 2011, for publicly accountable profit-oriented enterprises. After that date, IFRS will replace Canadian GAAP for those enterprises. The Company is currently assessing the impact of these new accounting standards on its consolidated financial statements.

# ALLON THERAPEUTICS INC.

Notes to Consolidated Financial Statements  
(Unaudited)

Three months ended March 31, 2008 and 2007

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## 5. Unearned revenue:

On January 24, 2007 the Company announced that it received a grant from The Michael J. Fox Foundation for Parkinson's Research ("MJFF") to evaluate the effectiveness of AL-108 in pre-clinical models of Parkinson's disease. During 2007, Allon received \$214,289 and incurred expenses for all but \$68,216 which was recorded as unearned revenue at December 31, 2007, to be applied against future research expenses as incurred. During the quarter ended March 31, 2008, Allon incurred expenses of \$37,899 against the MJFF grant leaving a balance of \$30,317 in unearned revenue. The Company anticipates using the remaining grant balance in Q2 2008.

## 6. Share capital:

### (a) Authorized:

Unlimited voting common shares without par value

Unlimited preferred shares, issuable in series

### (b) Equity Financing:

On May 29 and June 22, 2007, Allon closed a bought deal equity financing. The financing consisted of 13,059,933 units (the "Units"), comprised of one share and one half share purchase warrant priced at \$1.20 per Unit and 103,699.5 warrants priced at \$0.16 per whole warrant for total gross proceeds of \$15,688,512 less issue costs of \$1,264,421 for net proceeds of \$14,424,091.

### (c) Warrants:

A total of 6,633,666 share purchase warrants were issued in conjunction with the Q2 2007 equity financing. Each warrant entitles the holder thereof to purchase one common share at an exercise price of \$1.65 for a term of 24 months following the date of issue. Included in the total warrants issued were 103,699.5 warrants issued for \$16,592, which approximates the fair value of the warrants at the time of issue and which is recorded as additional paid in capital.

As part of a private placement, the Company issued 5,625,000 share purchase warrants on November 14, 2006 and 637,500 share purchase warrants on November 29, 2006 for a total of 6,262,500 share purchase warrants relating to this share issuance. Each warrant entitles the holder, on exercise, to purchase one share of the Company at a price of \$1.00 for a period of 24 months following the date of issue.

At March 31, 2008 the Company had warrants outstanding to acquire 12,880,541 common shares at prices ranging from \$1.00 to 1.65 which would result in proceeds of \$17,192,424 if they were exercised in full.

# ALLON THERAPEUTICS INC.

Notes to Consolidated Financial Statements  
(Unaudited)

Three months ended March 31, 2008 and 2007

## 6. Share capital (continued):

(d) Additional paid in capital:

Additional paid in capital increased by \$86,781 to \$1,455,914 as a result of stock based compensation booked during the three month period ended March 31, 2008.

## 7. Stock-based compensation:

The Company recognized \$86,781 in compensation expense for the three months ended March 31, 2008 and \$95,859 for the same period ended March 31, 2007, both relating to awards granted to employees and non-employees under its stock option plan.

Stock options:

The Company's Stock Option Plan, "the Plan", provides for the granting of options for the purchase of common shares of the Company at the fair market value of the Company's stock at the grant date. Stock options are granted to both employees and non-employees. The Company's Board of Directors has discretion as to the number, vesting period, and expiry dates of stock options granted.

The Plan is based on a rolling percentage of options issuable of up to 10% of the Company's outstanding common shares. As of March 31, 2008, the Company had 59,016,666 common shares issued and outstanding resulting in current authorization to issue a maximum of 5,901,667 options under the Plan.

During the three months ended March 31, 2008, the Company did not grant any options compared to 50,000 options granted at \$1.00 during the three months ended March 31, 2007.

Stock option activity for the three months ended March 31, 2008 and March 31, 2007:

	Common shares under option	Weighted avg exercise price
Outstanding, December 31, 2006	3,708,497	\$ 0.76
Granted	50,000	1.00
Outstanding, March 31, 2007	3,758,497	\$ 0.76
Exercisable, March 31, 2007	2,492,447	\$ 0.63
Outstanding, December 31, 2007	4,771,600	\$ 0.85
Outstanding, March 31, 2008	4,771,600	\$ 0.85
Exercisable, March 31, 2008	2,898,350	\$ 0.70

# ALLON THERAPEUTICS INC.

Notes to Consolidated Financial Statements  
(Unaudited)

Three months ended March 31, 2008 and 2007

## 7. Stock-based compensation (continued):

The following table summarizes stock options outstanding at March 31, 2008 and March 31, 2007:

Exercise price	Options outstanding			Options exercisable		
	Number of common shares	Weighted average remaining contractual life	Weighted average exercise price	Number exercisable	Weighted average exercise price	
\$ 0.001 – 0.40	1,439,100	5.95	\$ 0.12	1,439,100	\$ 0.12	
\$ 1.00 – 1.72	3,332,500	7.90	1.16	1,459,250	1.27	
March 31, 2008 Total	4,771,600	7.77	\$ 0.85	2,898,350	\$ 0.70	
\$ 0.001 – 0.40	1,468,497	6.95	\$ 0.12	1,468,497	\$ 0.12	
\$ 1.00 – 1.72	2,290,000	8.14	1.18	1,023,950	1.38	
March 31, 2007 Total	3,758,497	7.93	\$ 0.76	2,492,447	\$ 0.63	

The fair value of share based awards is determined using the Black-Scholes option pricing model. Like other accepted option valuation models, the Black-Scholes model was developed to estimate fair value of freely tradable, fully transferable options without vesting restrictions, which significantly differs from the Company's stock option awards. The Black-Scholes option pricing model is also based on several highly subjective assumptions including the expected life of the option, expected future stock price volatility and fair value of the Company's stock at the date of grant of the stock options. Changes in these assumptions can materially affect the estimated fair value of the Company's stock options.

The estimated fair value of options granted to the Company's employees and directors is calculated at the grant date and amortized on a straight line basis over the vesting period of the options. The fair value of each option granted to non-employees is estimated as of the balance sheet date.

# ALLON THERAPEUTICS INC.

Notes to Consolidated Financial Statements  
(Unaudited)

Three months ended March 31, 2008 and 2007

## 7. Stock-based compensation (continued):

The following table summarizes assumptions used in the Black-Scholes option pricing model for the respective three month periods ending March 31, 2008 and March 31, 2007:

	Employees & Directors		Contractors	
	2008	2007	2008	2007
Dividend yield	0%	0%	0%	0%
Expected volatility	80%	88%	71%	58%
Risk free interest rate	3.72%	3.59%	3.31%	3.41%
Expected remaining life in years	2.06	1.51	3.77	3.30
Fair value per share	\$0.45	\$0.47	\$0.69	\$0.61

## 8. Net loss per common share:

The following table sets forth the computation of loss per common share:

	Three months ended 2008	Three months ended 2007
Net loss for the period	\$ (4,349,737)	\$ (2,818,519)
Weighted average number of common shares outstanding	59,016,666	45,912,405
Net loss per common share	(0.07)	(0.06)

## 9. Financial Instruments:

The Company's financial instruments consists of cash and cash equivalents, short-term investments, accounts receivable, accounts payable and accrued liabilities. The fair values of cash, accounts receivable, accounts payable and accrued liabilities approximate carrying value because of the short-term nature of these instruments. Cash equivalent and short-term investments are classified as held for trading and their fair value is determined directly by reference to quoted market prices.

### (a) Credit risk:

Cash equivalent and short-term investments are held in high-grade, liquid commercial paper and other low risk investments with no exposure to liquidity or other risk associated with Asset-Backed Securities. These financial instruments are classified as held for trading as they may periodically be traded before their maturity date. However, the majority of these financial instruments are held to maturity and would not result in a significant risk of fair value

# ALLON THERAPEUTICS INC.

Notes to Consolidated Financial Statements  
(Unaudited)

Three months ended March 31, 2008 and 2007

## 9. Financial Instruments (continued):

changes if held to maturity. At March 31, 2008 maturities on investments ranged from 30 days to two months.

(b) Liquidity risk:

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they come due. The company manages its liquidity risk by continuously monitoring forecasted and actual cash flows, as well as anticipated investing and financing activities. The majority of the Company's financial liabilities are due within ninety days. The company does not have long-term financial liabilities.

(c) Market risk:

Market risk is the risk that changes in market prices, such as foreign currency exchange rates and interest rates will affect the Company's income or the value of the financial instruments held.

(d) Foreign currency and interest rate risk:

The Company's primary risks are exposure to foreign currency exchange and interest rate risk. These risks arise from the Company's holdings of US and Canadian dollar denominated cash, accounts payable, cash equivalents, and short-term investments. Changes arising from these risks could impact the Company's reported interest income or foreign exchange gains or losses. The Company limits its exposure to foreign currency risk by holding US denominated cash, cash equivalents and short-term investments in amounts of up to 100% of forecasted twelve month US dollar expenditures, thereby creating a natural hedge against foreign currency fluctuations and limiting foreign currency risk to translation of US dollar balances at the balance sheet date.

Accounts exposed to foreign exchange and interest rate risk for the periods ended March 31:

	2008			2007		
	Cdn \$ Balance	US \$ <sup>1</sup> Balance	Total	Cdn \$ Balance	US \$ <sup>1</sup> Balance	Total
Cash and equivalents	\$ 568,943	\$2,456,991	\$3,025,934	\$ 810,082	\$5,618,976	\$6,429,058
Accounts payable	308,822	379,678	688,500	240,408	584,190	824,598
Short-term investments	4,205,140	1,857,409	6,062,549	1,398,287	-	1,398,287
Total	\$5,082,905	\$4,694,078	\$9,776,983	\$2,448,777	\$6,203,166	\$8,651,943

(1) All US balances are shown in Canadian dollar equivalents.

# ALLON THERAPEUTICS INC.

Notes to Consolidated Financial Statements  
(Unaudited)

Three months ended March 31, 2008 and 2007

## 9. Financial Instruments (continued):

(e) Foreign currency exchange risk sensitivity analysis:

The following table details the Company's sensitivity analysis to a 10% strengthening in the US Dollar on foreign currency denominated monetary items and adjusts their translation at the balance sheet date for a 10% change in foreign currency rates. For a 10% weakening of the US Dollar against the Canadian Dollar, there would be an equal and opposite impact on net and comprehensive loss for the period.

Change in foreign exchange gain/(loss) resulting from currency fluctuations at March 31:

	2008	2007
	10% Foreign Currency Strengthening	10% Foreign Currency Strengthening
Cash and equivalents	\$ 239,356	\$ 486,660
Accounts payable	36,988	50,597
Short-term investments	180,956	-
Embedded derivatives	9,857	-
Total	\$ 467,147	\$ 537,257

## 10. Management of capital:

The Company's objective is to maintain a sufficient capital base so as to sustain future research and development and business initiatives and to maintain investor, creditor and market confidence. The Company considers the items included in the consolidated shareholders' equity, cash and cash equivalents and short-term investments as capital and may issue new shares or raise debt in order to maintain its capital structure. However, at this time, the Company has not utilized debt facilities as part of its capital management program. The Company is a research and development stage company and as such funds are primarily invested in research and development initiatives and no dividends are issued to shareholders. The Company does not foresee implementing a dividend program in the near future. Neither Allon nor its subsidiary are subject to any externally exposed capital requirements and the Company does not use financial ratios to manage capital.

# ALLON THERAPEUTICS INC.

Notes to Consolidated Financial Statements  
(Unaudited)

Three months ended March 31, 2008 and 2007

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## **11. Related party transactions:**

During the three months ended March 31, 2008, Allon paid one of its Board members \$12,500 to provide consulting services to assist the Company with general research and the advancement of its drug development programs. The Company plans to retain these services throughout 2008.

During the first quarter of 2007, the Company received \$145,657, from a Senior Officer of the Company, as reimbursement for principle and interest on a loan of \$143,155 granted during the fourth quarter of 2006. The loan was subject to an annual interest rate of 5.25%, consistent with market rates at the inception of the loan.



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## Corporate Office

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**Allon Therapeutics Inc.**

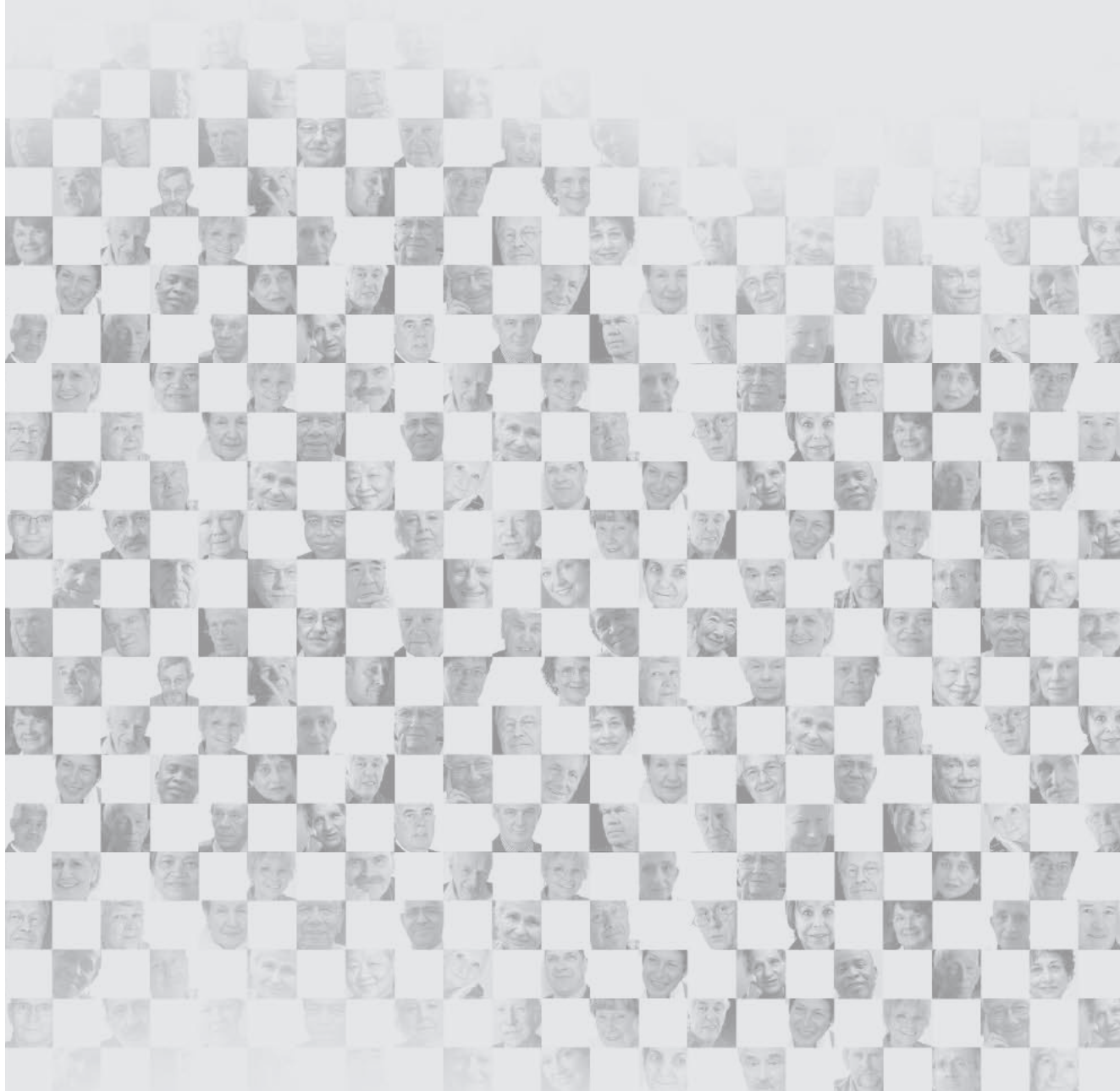
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