



Allon Therapeutics Inc. 1ST QUARTER REPORT MARCH 31 2011

Q1



FINANCIAL INFORMATION

MANAGEMENT'S DISCUSSION & ANALYSIS

The following information should be read in conjunction with the unaudited condensed consolidated interim financial statements and accompanying notes as at and for the three months ended March 31, 2011 and with the audited consolidated financial statements and accompanying notes for the year ended December 31, 2010. The unaudited condensed consolidated interim financial statements have been prepared in accordance with IAS 34 Interim Financial Reporting. 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.

June 2, 2011

FORWARD LOOKING STATEMENTS

This Management's Discussion & Analysis (MD&A) contains forward-looking statements that reflect the current view of the Company with respect to future events and financial performance. The forward-looking statements in this MD&A include, but are not limited to, statements regarding: the status of the Company's research and development programs; the Company's expectation regarding the progress of its clinical and pre-clinical programs; the sufficiency of the Company's financial resources to fund operations into 2012; and the Company's future funding requirements. Forward-looking statements include, but are not limited to, those statements set out in this MD&A under "Overview", "Results of Operations", "Liquidity and Capital Resources", "Critical Accounting Policies and Estimates" and "Risks and Uncertainties". The forward-looking statements in this MD&A are based on the Company's current expectations, estimates, projections and assumptions made in light of its experience and its perception of historical trends. Any such forward-looking statements are subject to a number of risks and uncertainties that could cause actual results to differ materially from current expectations. The Company cautions readers that should certain risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary significantly from those expected. The risks that could cause actual results to differ from current expectations include inherent risks in the biopharmaceutical industry, general economic conditions, government regulations, status of healthcare reimbursements, competition, failure of third parties and subcontractors, failure to recruit or retain required management and employees, reliance on collaborative partners, potential for clinical trial liability, inadequate protection of intellectual property rights, uncertainty in the Company's future financial condition and the impact of foreign currency exchange rates. For additional information with respect to certain of these risk factors, reference should be made to the "Risks and Uncertainties" section of this MD&A, to the notes to the unaudited interim consolidated financial statements as at and for the three months ended March 31, 2011, to the "Risk Factors" section in the Company's most recent Annual Information Form, and continuous disclosure materials filed from time to time with Canadian securities regulatory authorities, which are available online at www.sedar.com.

The forward-looking information contained in this MD&A is expressly qualified by this cautionary statement. The Company disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, other than as required by law, rule or regulation. You should not place undue reliance on forward-looking statements.

OVERVIEW

Allon Therapeutics Inc. is a clinical-stage biotechnology company developing treatments for major neurodegenerative conditions. Allon's drug, davunetide, is proceeding in a Phase 2/3 clinical trial in an orphan

indication, progressive supranuclear palsy (PSP), under a Special Protocol Assessment (SPA) with the United States Food and Drug Administration (FDA). This pivotal trial is based upon statistically significant human efficacy demonstrated in amnesic mild cognitive impairment (aMCI), a precursor to Alzheimer’s disease (AD), and in cognitive impairment associated with schizophrenia (CIAS) as well as positive biomarker data.

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. Because the two platforms are based on different proteins, the drugs from each are different molecules with different therapeutic mechanisms and distinct commercial opportunities. Clinical-stage drug, davunetide, is derived from ADNP, while preclinical stage drug AL-309 is derived from ADNF. Davunetide is targeted at PSP (a type of frontotemporal dementia), Alzheimer’s disease, CIAS and Parkinson’s disease. ADNF drug candidate AL-309 is targeted for the treatment of peripheral neuropathies and has characteristics that allow it to be developed for multiple routes of administration based on bioavailability studies using oral, intranasal, or subcutaneous administration.

Status of research and development programs

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

| Platform | Compound | Stage Development | Status |
|-----------------|-----------------|--|--|
| ADNP | davunetide | Phase 2/3 clinical trial in progressive supranuclear palsy (PSP) | Study commenced in Q4 2010 under SPA |
| | | Pilot clinical trial in PSP and other types of FTD | Study completed in Q4 2010. Met primary endpoint |
| | | Phase 2 clinical trial in CIAS | Study completed. Data released in Q4 2009 |
| | | Phase 1 human cerebrospinal fluid (CSF) pharmacokinetic clinical trial | Study completed. Data released in Q3 2008 |
| | | Phase 2a clinical trial in amnesic mild cognitive impairment | Study completed. Data released in Q1 2008 |
| | | Phase 2a clinical trial in MCI-CABG | Study completed. Data released in Q3 2008 |
| ADNF | AL-309 | Preclinical stage | Preclinical pharmacology and toxicology ongoing |

FIRST QUARTER 2011 ACHIEVEMENTS

- The Company announced it had reached agreement with the FDA on a SPA for a pivotal Phase 2/3 clinical trial to evaluate the Company's lead neuroprotective drug candidate, davunetide, as a potential treatment for PSP, a rapidly-progressing and fatal degenerative brain disease. Enrolment in the study began in the fourth quarter of 2010 under the SPA.
- A research project funded by the Michael J. Fox Foundation (MJFF) for Parkinson's Research found that intranasal davunetide treatment significantly improved motor function and brain pathology in a mouse model which replicates certain characteristics of Parkinson's disease (PD), a progressive neurodegenerative disease. Treatment with davunetide caused a 38% improvement in motor performance and coordination relative to controls.
- The Company was issued an important Japanese patent covering the composition of matter of davunetide and other peptides in its neuroprotection drug platform. The patent granted by the Japan Patent Office covers the polypeptide and nucleotide composition of matter for davunetide, its parent protein ADNP and other derivatives of ADNP.
- The Company was granted a patent in the United States covering the treatment of fetal alcohol syndrome, developed as a result of in-utero exposure to alcohol, with davunetide or derivatives and combinations of all other compounds in the Company's neuroprotection drug platform.

RESULTS OF OPERATIONS

Allon reported a net loss of \$2,974,076 (\$0.04 per share) for the three months ended March 31, 2011, compared to a net loss of \$3,120,340 (\$0.04 per share) for the three months ended March 31, 2010, representing a decrease in net loss of \$146,264. This decrease in net loss is explained in the following description of significant variances from the comparable period in 2010.

RESEARCH AND DEVELOPMENT

For the three months ended March 31, 2011, research and development expenses were \$2,013,795 compared to \$2,264,529 for the three months ended March 31, 2010. Despite an increase in clinical trial activities related to PSP during the first quarter of 2011, research and development expenses were lower compared to the first quarter of 2010. This resulted from additional costs in the first quarter of 2010 related to a Phase 1 clinical trial initiated and completed within the quarter to evaluate the pharmacokinetic profile of davunetide. Details of the Company's clinical programs are provided below.

Progressive Supranuclear Palsy (PSP)

PSP is one of several types of FTD in which the pathology is known to involve impairment of the brain protein tau. During the first quarter of 2011, the Company reached agreement with the FDA on a SPA for a pivotal Phase 2/3 clinical trial to evaluate davunetide as a potential treatment for PSP. Enrolment in the study began in the fourth quarter of 2010.

The FDA and the European Union have granted Orphan Drug Designation to davunetide for the treatment of PSP, and in April, 2010, the FDA also granted Fast Track status to davunetide for the treatment of PSP. Fast Track status is designed to facilitate development and expedite review of a drug candidate that treats a serious or life-threatening condition and addresses an unmet medical need.

For the three months ended March 31, 2011, the Company incurred \$1.3 million in development costs for davunetide (2010 - \$1.7 million).

Parkinson's disease (PD)

On February 2, 2011, the Company announced that a research project funded by the Michael J. Fox Foundation for Parkinson's Research found that intranasal davunetide treatment significantly improved motor function and brain pathology in a mouse model which replicates certain characteristics of PD, a progressive neurodegenerative disease. In the study, performed at the University of California, Los Angeles (UCLA), α -synuclein mice were treated with davunetide daily for two months. At the end of the treatment period, these mice and various control groups were tested for motor function, coordination and activity. The davunetide treated α -synuclein mice showed a 38% decrease in the number of errors per step in the beam traversal test, a measure of motor function. Further pre-clinical development is ongoing.

Cognitive impairment associated with schizophrenia (CIAS)

In May 2010, data from preclinical studies that demonstrated that davunetide improved cognitive performance in a model of schizophrenia was published. The research found that treatment with davunetide improved schizophrenia-like symptoms, such as hyperactivity and memory deficits, in a model where the condition is dependent on reduced expression of the microtubule-associated protein, stable tubule-only polypeptide.

On March 30, 2010, the Company released top-line results from an imaging study of schizophrenia patients showing that 12 weeks of treatment with davunetide resulted in a statistically significant increase in levels of a biomarker that is an important indicator of brain cell health. Statistically significant ($p=0.0170$) increase in levels of N-acetyl aspartate (NAA) were measured in the brains of the schizophrenia patients treated with davunetide using magnetic resonance spectroscopy (MRS). NAA is an informative biomarker because decreased levels of NAA occur in schizophrenia, and in numerous other neurodegenerative conditions such as brain injury, stroke, and Alzheimer's disease.

On December 7, 2009, the Company released results of a Phase 2a clinical trial showing that davunetide intranasal has a positive impact on the ability of schizophrenia patients to carry out important activities in their daily lives. Statistically significant efficacy ($p=0.015$) was achieved on the University of California at San Diego Performance-based Skills Assessment. The drug was also evaluated with the MATRICS (Measurement and Treatment Research to Improve Cognition in Schizophrenia) composite battery of tests which was the primary outcome. Davunetide intranasal did not show significance on this measure. The trial was largely funded and managed by the Treatment Units for Research on Neurocognition and Schizophrenia (TURNs). The Company did not incur any significant expenses related to this project in 2011.

AL-309

AL-309 is a D-amino acid derivative of AL-209 from the ADNF platform. In February 2010, the Company presented pre-clinical data that demonstrates the potential of AL-309 as a treatment for peripheral neuropathy. The preclinical data has shown AL-309 to be effective at reducing nerve damage and pain in animal models for peripheral neuropathy caused by diabetes and cancer chemotherapy, two of the most common causes of the disease. The Company did not incur any significant expenses related to this project in the first quarter of 2011. The Company has AL-309 related drug supplies of \$258,596 to be used in future clinical trials. These drug supplies are recorded as non-current assets in the condensed consolidated interim financial statements for the three months ended March 31, 2011.

GENERAL AND ADMINISTRATIVE

For the three months ended March 31, 2011, general and administrative expenses were \$850,885 compared to \$853,131 for the three months ended March 31, 2010. There was not a significant change in general and administrative expenses.

OTHER (INCOME)/EXPENSES

The Company's other income and expenses are primarily comprised of interest income and foreign exchange losses. The Company earned interest revenue of \$4,900 during the three months ended March 31, 2011 compared to \$8,754 for the same period in 2010. Reduced interest earnings resulted from lower interest rates and lower cash balances during 2011 compared to the same period in 2010.

Foreign exchange loss was \$ 114,296 for the three months ended March 31, 2011. This compared to loss of \$11,434 for the same period in 2010. The Company's foreign exchange exposure is primarily limited to the translation of U.S. dollar balances in cash and short-term investment accounts to Canadian dollars. The foreign exchange losses for both 2011 and 2010 resulted from the decline of the U.S. dollar against the Canadian dollar. The Company has higher U.S. dollar holdings in 2011 compared to the same period in 2010 which resulted in higher foreign exchange losses in 2011.

QUARTERLY INFORMATION

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

(in thousands, except per share data)

| | Mar 31, 2011 | Dec 31, 2010 ⁽¹⁾ | Sep 30, 2010 ⁽¹⁾ | Jun 30, 2010 ⁽¹⁾ |
|------------------------------------|--------------|-----------------------------|-----------------------------|-----------------------------|
| Interest income and other income | \$ 5 | \$ 3 | \$ 5 | \$ 43 |
| Research and development expenses | \$ 2,014 | \$ 6,444 | \$ 1,750 | \$ 1,779 |
| Net loss for the quarter | \$ (2,974) | \$ (7,956) | \$ (2,737) | \$ (2,712) |
| Loss per share – basic and diluted | \$ (0.04) | \$ (0.10) | \$ (0.04) | \$ (0.03) |

| | Mar 31, 2010 | Dec 31, 2009 ⁽¹⁾ | Sep 30, 2009 ⁽¹⁾ | Jun 30, 2009 ⁽¹⁾ |
|------------------------------------|--------------|-----------------------------|-----------------------------|-----------------------------|
| Interest income and other income | \$ 9 | \$ 20 | \$ 16 | \$ 32 |
| Research and development expenses | \$ 2,265 | \$ 1,435 | \$ 716 | \$ 542 |
| Net loss for the quarter | \$ (3,120) | \$ (2,576) | \$ (1,551) | \$ (1,205) |
| Loss per share – basic and diluted | \$ (0.04) | \$ (0.03) | \$ (0.02) | \$ (0.02) |

(1) Information was prepared in accordance with Canadian generally accepted accounting principles.

During the quarter ended June 30, 2009, the Company formed a special Steering Committee consisting of leading neurologists and psychiatrists to help the Company design and conduct a Phase 2 human clinical trial that will evaluate the Company's drug, davunetide, as a potential treatment for FTD. Also during the quarter, the European Patent Office issued a notice of allowance for a patent covering the composition and method of use of the Company's neuroprotective compound, davunetide, as a treatment for Alzheimer's disease.

During the quarter ended September 30, 2009, the Company released top-line results from a Phase 2a clinical trial showing that the Company's drug, davunetide, has a positive impact on the ability of schizophrenia patients to carry out important activities in their daily lives. Statistically significant efficacy (p=0.015) was achieved on the University of California at San Diego Performance-based Skills Assessment. The drug was also evaluated with the Measurement and Treatment Research to Improve Cognition in Schizophrenia composite battery of tests which was the primary outcome. Davunetide did not show significance on this measure.

During the quarter ended December 31, 2009, the Company was issued a Canadian patent covering the chemical composition of the Company's preclinical-stage peptide AL-209 and its use in protecting against Alzheimer's disease and other degenerative diseases. The Company also presented the Phase 2a clinical data evaluating davunetide in schizophrenia-related cognitive impairment at the American College of Neuropsychopharmacology annual meeting.

During the quarter ended March 31, 2010, the Company's drug, *davunetide*, was granted Orphan Drug Status in the U.S. and the European Union for the treatment of PSP. The Company also completed a number of clinical activities including: a Phase 1 clinical trial of *davunetide* which demonstrated that the intranasal dose range can be broadened and confirmed *davunetide*'s safety profile; released positive results from an imaging study of schizophrenia patients; and released preclinical data demonstrating the potential of AL-309 as a treatment for peripheral neuropathy. Furthermore, the Company entered into a standby equity distribution agreement with YA Global Master SPV Ltd., which may provide up to \$10 million of equity capital over three years.

During the quarter ended June 30, 2010, the Company's drug, *davunetide*, was granted Fast Track status by the FDA for the treatment of PSP. Furthermore, data from preclinical studies were published demonstrating that *davunetide* improved cognitive performance in a model of schizophrenia.

During the quarter ended September 30, 2010, the Company was chosen as the "Most Innovative Development Company" in the New Economy 2010 Pharmaceutical & Healthcare Awards sponsored by New Economy Magazine.

During the quarter ended December 31, 2010, the Company initiated a pivotal Phase 2/3 clinical trial with *davunetide* in patients with PSP under an SPA. The Company also entered into a \$10.2 million Convertible Revenue and Royalty Interest agreement with Isar. The Company was awarded two non-taxable grants totaling approximately \$500,000 from the United States government under the Qualifying Therapeutic Discovery Project program and was given a grant totaling \$625,000 from the Michael J. Fox Foundation for Parkinson's Research. The Company also released results from the successfully completed pilot clinical trial in PSP and other types of FTD and validated the trial design for the pivotal Phase 2/3 clinical trial.

During the quarter ended March 31, 2011, the Company continued enrolling patients for the pivotal Phase 2/3 clinical trial with *davunetide* for PSP. The Company also completed a research project, funded by the Michael J. Fox Foundation for Parkinson's Research, and found that intranasal *davunetide* treatment significantly improved motor function and brain pathology in a mouse model which replicates certain characteristics of Parkinson's disease.

LIQUIDITY AND CAPITAL RESOURCES

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 consolidated shareholders' equity and long-term debt as capital and may issue new shares or raise debt in order to maintain its capital structure. 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 imposed capital requirements and the Company does not use financial ratios to manage capital.

Revenue is currently derived from interest earned on cash balances. At March 31, 2011, the Company had accumulated a deficit of \$72,503,543. Losses are expected to continue in the near future 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 and related instruments.

The condensed consolidated interim financial statements for the three months ended March 31, 2011 have been prepared under the assumption that the Company will continue as a going concern. The going concern basis of presentation assumes that the Company will continue in operation for the foreseeable future and be able to realize its assets and discharge its liabilities and commitments in the normal course of business. The eventual profitability of the Company and its ability to continue as a going concern is dependent upon many factors, including its ability to obtain sufficient financing, the successful development of its products, and receiving

regulatory approvals. Furthermore, the biotechnology industry is subject to rapid and substantial technological change which could reduce the marketability of the Company's technology.

In addition to its existing cash resources, the Company has access to funds under the Standby Equity Distribution Agreement (SEDA), subject to certain conditions, to fund its business for the next 12 months from the balance sheet date. However, if the SEDA is not available for any reason, there is significant doubt that the Company's existing cash resources will allow the Company to continue as a going concern based on management's planned expenditures for the next 12 months. The Company anticipates accessing additional capital in next 12 months. Management believes that it will secure additional financing in sufficient time to continue to execute its planned expenditures without interruption. However, there can be no assurance that the capital will be available as necessary to meet these continuing expenditures, or if the capital is available, that it will be on terms acceptable to the Company. The issuance of common shares by the Company could result in significant dilution in the equity interest of existing shareholders. The Company will continue to require additional sources of financing in the future to continue its research activities, realize returns on its assets and discharge its liabilities in the normal course of business. There can be no assurance that the Company will be able to raise any capital through any type of offerings.

The condensed consolidated interim financial statements do not reflect adjustments that would be necessary if the going concern assumption was not appropriate. If the going concern basis was not appropriate for these financial statements, then adjustments would be necessary in the carrying value of the assets and liabilities, the reported revenue and expenses and the balance sheet classifications used.

For the three months ended March 31, 2011, operating activities used cash of \$2,965,475 compared to \$4,543,442 used in operations for the three months ended March 31, 2010. Cash used in operating activities reflects the net loss of \$2,974,076 for the three months ended March 31, 2011, adjusted for non-cash items including amortization of tangible and intangible assets, stock-based compensation and changes in non-cash working capital.

For the three months ended March 31, 2011, investing activities used cash of \$3,878 compared to \$182 used for the three months ended March 31, 2010. The amounts for both 2011 and 2010 represented purchase of small amounts of fixed assets.

For the three months ended March 31, 2011, financing activities generated cash of \$182,997 compared to nil for the three months ended March 31, 2010. The financing activity in 2011 resulted from the Company's first draw down under the standby equity distribution agreement (SEDA) entered into with YA Global Master SPV Ltd. (Yorkville) in March 2010. Under the terms of the agreement, Yorkville has committed to provide up to \$10 million of equity capital over three years, if and when drawn by the Company at the Company's discretion. The Company can terminate this agreement at any time without payment of additional fees. Newly issued common shares are priced at a 5% discount to the 5-day weighted average share price of the Company's shares at the time of draw down and are subject to a minimum price set by the Company in advance.

CONTRACTUAL OBLIGATIONS

While advancing its clinical and pre-clinical programs, the Company has entered into contracts that will remain in effect over several reporting periods. The total current and future commitments account for \$1,793,107 of the \$5,073,928 cash on hand. The Company has no off-balance sheet arrangements.

Schedule of contractual and planned commitments as of March 31, 2011

(in thousands)

| | 2011 | 2012 | 2013 | 2014-2015 | Total |
|---------------------------|----------|--------|--------|-----------|----------|
| Pre-clinical Initiatives | \$ 211 | \$ 355 | \$ - | \$ - | \$ 566 |
| Clinical Initiatives | \$ 803 | \$ 108 | \$ 91 | \$ 8 | \$ 1,010 |
| Capital and Licensing | \$ - | \$ 15 | \$ 15 | \$ 29 | \$ 59 |
| Other | \$ 78 | \$ 61 | \$ 6 | \$ 12 | \$ 158 |
| Total Company Commitments | \$ 1,092 | \$ 539 | \$ 112 | \$ 50 | \$ 1,793 |

OUTSTANDING SHARE CAPITAL

At March 31, 2011, the Company had 78,523,161 common shares outstanding. Each common share entitles the holder to one vote per share. At March 31, 2011, there were 7,282,100 options outstanding, of which 4,471,770 options were exercisable into an equivalent number of the Company's common shares at exercise prices ranging from \$0.001 to \$1.72.

The Company'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 7 of the Company's financial statements for more detail regarding outstanding share capital.

RELATED PARTY TRANSACTIONS

During the first quarter of 2011, the Company paid one of its Board members \$12,500 for consulting services provided to the Company in relation to general research and advancement of the Company's drug development programs. The Company plans to retain these services on a continuing basis.

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 the Company's 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 *IAS 34 Interim Financial Reporting*.

During the three months ended March 31, 2011, 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 the unaudited condensed consolidated financial statements in conformity with International Financial Reporting Standards requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements as well as the reported amount of revenues and expenses and related disclosures of the reporting periods. The reported amounts and note disclosures are determined using management's best estimates based on assumptions that reflect the most probable set of economic conditions and planned course of action. Significant areas requiring the use of management estimates relate to the assessment for impairment and useful lives of intangible assets, determination of fair value in relation to the convertible royalty and revenue financing agreement, clinical trial accounting including the determination of useful lives of clinical drug supplies, accrued liabilities, research and development costs and determination of the fair value of share-based compensation. Management believes that the estimates and assumptions are reasonable based upon information available at the time that these estimates and assumptions were made. Actual results could differ from those estimates used in the preparation of the financial statements. For a full description of all of the Company's significant accounting policies and estimates, see Note 3 to the Company's interim consolidated financial statements for the period ended March 31, 2011.

The Company's financial statements have been prepared under the assumption that the Company will continue as a going concern. The eventual profitability of the Company and its ability to continue as a going concern is dependent upon many factors, including its ability to obtain sufficient financing, the 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's existing cash resources, along with the funds available under the SEDA financing arrangement, are sufficient, in management's opinion, to fund its business for the next twelve months to the first quarter of 2012 in accordance with the Company's current business plan. The Company will be required to obtain additional sources of financing in the future to continue its research activities, realize returns on its assets and discharge its liabilities in the normal course of business. There is no guarantee that the Company will be able to raise any capital through any type of offerings.

CONVERSION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS

Effective January 1, 2011, Canadian publicly listed entities are required to prepare their financial statements in accordance with International Financial Reporting Standards ("IFRS"). Due to the requirement to present comparative financial information, the effective transition date is January 1, 2010. The Company's financial statements for the three months ended March 31, 2011 are the first reporting period to be prepared in accordance with IFRS.

The principal impacts of the transition to IFRS on the Company's financial statements are the revaluation of non-monetary assets and liabilities of the Company's U.S. subsidiary and adjustments related to share-based payments. The impacts of the transition to IFRS are set out in Note 11 to the condensed consolidated interim financial statements for the first quarter of 2011.

To ensure accurate and efficient reporting under IFRS, the Company developed a conversion implementation plan in 2009, which was designed to identify differences between previous Canadian GAAP and IFRS that affect the Company and any required changes to accounting processes and controls (including information technology systems). No significant impacts were identified in relation to the Company's information systems or day-to-day accounting processes and controls. The Company reviewed its disclosure controls and procedures and updated these as required to ensure that they are appropriate for reporting under IFRS. Reporting in accordance with IFRS has now been embedded into the Company's systems and procedures.

RISKS AND UNCERTAINTIES

As previously described, if the SEDA is not available for any reason, there is significant doubt that the Company's existing cash resources will allow the Company to continue as a going concern based on management's planned expenditures for the next 12 months. Management believes that it will secure additional financing in sufficient time to continue to execute its planned expenditures without interruption. However, there can be no assurance that the capital will be available as necessary to meet these continuing expenditures, or if the capital is available, that it will be on terms acceptable to the Company. The issuance of common shares by the Company could result in significant dilution in the equity interest of existing shareholders.

The Company will continue to require additional sources of financing in the future to continue its research and development activities. Funding needs 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. The Company cannot guarantee that financing will be available or that terms for additional financing will be favourable.

The Company's primary market risk is the exposure to foreign currency exchange rate fluctuations. This risk arises from the Company's holdings of foreign currency denominated cash, accounts payable, cash equivalents, and short-term investments. Changes in foreign currency exchange rates can create significant foreign exchange gains or losses to the Company. The Company's current foreign currency risk is primarily with the U.S. dollar. The Company has minimal exposure to interest rate risks as it does not have long-term liabilities requiring interest payments.

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. Additional information with respect to these and other risks affecting the Company is described in the section "Risk Factors" in the Company's most recent Annual Information Form filed with Canadian securities regulatory authorities. Reference should also be made to the notes to the unaudited condensed consolidated financial statements for the three months ended March 31, 2011 and to the Company's other continuous disclosure materials filed from time to time with Canadian securities regulatory authorities, which are available online at www.sedar.com

Unaudited Condensed Consolidated Interim Financial Statements of

ALLON THERAPEUTICS INC.

Three month periods ended March 31, 2011 and 2010
(All Amounts Expressed in Canadian dollars)

ALLON THERAPEUTICS INC.

Unaudited Condensed Consolidated Statements of Financial Position

(All amounts expressed in Canadian dollars)

| | <i>Note</i> | March 31, 2011 | December 31, 2010 | January 1, 2010 |
|---|-------------|-------------------|----------------------|--------------------|
| Assets | | | | |
| Current assets: | | | | |
| Cash and cash equivalents | | \$ 5,073,928 | \$ 7,860,284 | \$ 11,002,859 |
| Accounts receivables | | 37,592 | 143,846 | 22,438 |
| Prepaid expenses and deposits | | 1,003,190 | 855,680 | 430,878 |
| Drug supplies | | 205,354 | 205,503 | 3,676,522 |
| | | 6,320,064 | 9,065,313 | 15,132,697 |
| Non-current assets: | | | | |
| Property and equipment | 4 | 27,407 | 29,044 | 42,567 |
| Intangible assets | 5 | 4,319,820 | 4,460,092 | 5,000,523 |
| Drug supplies | | 258,596 | 258,596 | 273,261 |
| | | \$ 10,925,887 | \$ 13,813,045 | \$ 20,449,048 |
| Liabilities and Shareholders' Equity | | | | |
| Current liabilities: | | | | |
| Trade and other payables | | \$ 1,672,292 | \$ 1,731,018 | \$ 2,290,906 |
| Deferred income | 6 | 84,021 | 159,543 | - |
| | | 1,756,313 | 1,890,561 | 2,290,906 |
| Non-current liabilities: | | | | |
| Financial liability | 7 | 176,088 | 180,628 | - |
| Shareholders' equity: | | | | |
| Share capital | 7 | 69,293,559 | 69,110,562 | 69,110,562 |
| Contributed surplus | | 12,362,950 | 12,308,459 | 2,376,849 |
| Cumulative translation adjustment | | (159,480) | (147,699) | - |
| Accumulated Deficit | | (72,503,543) | (69,529,466) | (53,329,269) |
| | | 8,993,486 | 11,741,856 | 18,158,142 |
| | | \$ 10,925,887 | \$ 13,813,045 | \$ 20,449,048 |

Corporate information and going concern (note 1)

See accompanying notes to condensed consolidated financial statements.

Approved on behalf of the Board:

"Frank Holler"
Frank A. Holler, Director

"Michael O'Brian"
C. Michael O'Brian, Director

ALLON THERAPEUTICS INC.

Unaudited Condensed Consolidated Statements of Comprehensive Loss
(All amounts expressed in Canadian dollars)

Three month periods ended March 31, 2011 and 2010

| | 2011 | 2010 |
|--|-----------------------|-----------------------|
| Expenses: | | |
| Research and development | \$ 2,013,795 | \$ 2,264,529 |
| General and administrative | 850,885 | 853,131 |
| | <u>2,864,680</u> | <u>3,117,660</u> |
| Other expense (income): | | |
| Interest and other income | (4,900) | (8,754) |
| Foreign exchange loss | 114,296 | 11,434 |
| | <u>109,396</u> | <u>2,680</u> |
| Loss for the period | <u>(2,974,076)</u> | <u>(3,120,340)</u> |
| Other comprehensive loss: | | |
| Foreign currency translation differences for foreign operation | 11,781 | 173,375 |
| Total comprehensive loss for the period | <u>\$ (2,985,857)</u> | <u>\$ (3,293,715)</u> |
| Loss per share: | | |
| Basic and diluted (note 9) | <u>\$ (0.04)</u> | <u>\$ (0.04)</u> |

See accompanying notes to condensed consolidated financial statements.

ALLON THERAPEUTICS INC.

Unaudited Condensed Consolidated Statements of Changes in Shareholders' Equity
(All amounts expressed in Canadian dollars)

Three month periods ended March 31, 2011 and 2010

| | Share capital | | Contributed surplus | Currency translation adjustment | Deficit | Total shareholders' equity |
|---|-------------------|----------------------|---------------------|---------------------------------|-----------------------|----------------------------|
| | Number | Value | | | | |
| Balance, January 1, 2010 | 78,066,666 | \$ 69,110,562 | \$ 2,376,849 | \$ - | \$ (53,329,269) | \$18,158,142 |
| Stock based compensation | - | - | 11,508 | - | - | 11,508 |
| Currency translation adjustment | - | - | - | (173,375) | - | (173,375) |
| Net loss for the period | - | - | - | - | (3,120,340) | (3,120,340) |
| Balance, March 31, 2010 | 78,066,666 | 69,110,562 | 2,388,357 | (173,375) | (56,449,609) | 14,875,935 |
| Balance, January 1, 2011 | 78,066,666 | 69,110,562 | 12,308,459 | (147,699) | (69,529,467) | 11,741,855 |
| Shares issued pursuant to Standby Equity Distribution Agreement | 456,495 | 200,000 | - | - | - | 200,000 |
| Share issue costs | - | (17,003) | - | - | - | (17,003) |
| Stock based compensation | - | - | 54,491 | - | - | 54,491 |
| Currency translation adjustment | - | - | - | (11,781) | - | (11,781) |
| Net loss for the period | - | - | - | - | (2,974,076) | (2,974,076) |
| Balance, March 31, 2011 | 78,523,161 | \$ 69,293,559 | \$12,362,950 | \$ (159,480) | \$(72,503,543) | \$ 8,993,486 |

See accompanying notes to condensed consolidated financial statements.

ALLON THERAPEUTICS INC.

Unaudited Condensed Consolidated Statements of Cash Flows
(All amounts expressed in Canadian dollars)

Three month periods ended March 31, 2011 and 2010

| | 2011 | 2010 |
|---|---------------------|---------------------|
| Cash provided by (used in): | | |
| Operating activities: | | |
| Net loss for the period | \$ (2,974,076) | \$ (3,120,340) |
| Adjustments for: | | |
| Amortization and depreciation | 131,335 | 136,780 |
| Share-based compensation | 54,491 | 11,508 |
| Change in non-cash operating items | (177,225) | (1,571,390) |
| | <u>(2,965,475)</u> | <u>(4,543,442)</u> |
| Investing activities: | | |
| Purchase of property and equipment | (3,878) | (182) |
| | <u>(3,878)</u> | <u>(182)</u> |
| Financing activities: | | |
| Proceeds from issuance of common shares, net of share issue costs of \$17,003 | 182,997 | - |
| | <u>182,997</u> | <u>-</u> |
| Decrease in cash and cash equivalents | (2,786,356) | (4,543,624) |
| Cash and cash equivalents, beginning of period | 7,860,284 | 11,002,859 |
| Cash and cash equivalents, end of period | <u>\$ 5,073,928</u> | <u>\$ 6,459,235</u> |

See accompanying notes to condensed consolidated financial statements.

ALLON THERAPEUTICS INC.

Notes to the Unaudited Condensed Consolidated Financial Statements
(All amounts expressed in Canadian dollars unless otherwise stated)

1. Corporate information and going concern:

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 accompanying financial statements have been prepared under the assumption that the Company will continue as a going concern. The going concern basis of presentation assumes that the Company will continue in operation for the foreseeable future and be able to realize its assets and discharge its liabilities and commitments in the normal course of business. The eventual profitability of the Company and its ability to continue as a going concern is dependent upon many factors, including its ability to obtain sufficient financing, the successful development of its products, and receiving regulatory approvals. Furthermore, the biotechnology industry is subject to rapid and substantial technological change which could reduce the marketability of the Company's technology.

In addition to its existing cash resources, the Company has access to funds under the Standby Equity Distribution Agreement (SEDA), subject to certain conditions (see Note 7), to fund its business for the next 12 months from the balance sheet date. However, if the SEDA is not available for any reason, there is significant doubt that the Company's existing cash resources will allow the Company to continue as a going concern based on management's planned expenditures for the next 12 months. The Company anticipates accessing additional capital in the next 12 months. Management believes that it will secure additional financing in sufficient time to continue to execute its planned expenditures without interruption. However, there can be no assurance that the capital will be available as necessary to meet these continuing expenditures, or if the capital is available, that it will be on terms acceptable to the Company. The issuance of common shares by the Company could result in significant dilution in the equity interest of existing shareholders. The Company will continue to require additional sources of financing in the future to continue its research activities, realize returns on its assets and discharge its liabilities in the normal course of business. There can be no assurance that the Company will be able to raise any capital through any type of offerings.

These condensed consolidated interim financial statements do not reflect adjustments that would be necessary if the going concern assumption was not appropriate. If the going concern basis was not appropriate for these financial statements, then adjustments would be necessary in the carrying value of the assets and liabilities, the reported revenue and expenses and the balance sheet classifications used.

2. Statement of compliance and basis of presentation:

(a) Statement of compliance:

These condensed consolidated interim financial statements have been prepared in accordance with International Accounting Standard ("IAS") 34, Interim Financial Reporting. These are the Company's first International Financial Reporting Standards ("IFRS") condensed consolidated interim financial statements for part of the period covered by the first IFRS annual financial statements and IFRS 1, First-time Adoption of International Financial Reporting Standards, has been applied. The condensed consolidated interim financial statements do not include all of the information required for full annual financial statements.

ALLON THERAPEUTICS INC.

Notes to the Unaudited Condensed Consolidated Financial Statements
(All amounts expressed in Canadian dollars unless otherwise stated)

An explanation of how the transition to IFRSs has affected the reported financial position, financial performance and cash flows of the Company is provided in note 11. This note includes reconciliations of equity and total comprehensive loss for comparative periods and of equity at the date of transition reported under previous Canadian Generally Accepted Accounting Principles ("Canadian GAAP") to those reported for those periods and at the date of transition under IFRSs.

These condensed consolidated interim financial statements were approved and authorized for issue by the Board of Directors on June 2, 2011.

(b) Basis of presentation:

These condensed consolidated interim financial statements have been prepared on a historical cost basis and are presented in Canadian dollars which is the Company's functional currency.

(c) Use of estimates:

The preparation of the condensed consolidated interim financial statements in conformity with IFRSs requires management to make estimates and assumptions that affect the application of accounting policies and the amounts reported in these condensed consolidated interim financial statements and notes. The reported amounts and note disclosures are determined using management's best estimates based on assumptions that reflect the most probable set of economic conditions and planned course of action. Significant areas requiring the use of management estimates relate to the assessment for impairment and useful lives of intangible assets, determination of fair value in relation to the convertible royalty and revenue financing agreement, determination of useful lives of clinical drug supplies, estimation of accrued liabilities, research and development costs and determination of the fair value of stock-based compensation. Actual results could differ from those estimates used in the preparation of the financial statements.

3. Significant accounting policies:

The accounting policies set out below have been applied consistently to all periods presented in these condensed consolidated interim financial statements and in preparing the opening IFRS statement of financial position at 1 January 2010 for the purposes of the transition to IFRSs, unless otherwise indicated.

(a) Basis of consolidation:

The consolidated interim financial statements include the accounts of the Company and its wholly owned U.S. subsidiary, over which the Company exercises control. Inter-company balances and transactions are eliminated in preparing the consolidated financial statements.

(b) Foreign currency:

The functional and reporting currency of the Company is the Canadian dollar. Transactions which are denominated in other currencies are translated into their Canadian dollar equivalents at exchange rates prevailing at the transaction date. The carrying values of monetary assets and liabilities denominated in foreign currencies are adjusted at each balance sheet date to reflect exchange rates prevailing at that date. The foreign currency gain or loss on monetary items is the difference between amortized cost in the functional currency at the beginning of the period adjusted for effective interest and payments during

ALLON THERAPEUTICS INC.

Notes to the Unaudited Condensed Consolidated Financial Statements
(All amounts expressed in Canadian dollars unless otherwise stated)

the period, and the amortized cost in the foreign currency translated at the exchange rate at the end of the period. Foreign exchange gains and losses are recognized in earnings.

The functional currency of the Company's U.S. subsidiary is the U.S. dollar. The assets and liabilities of foreign operation are translated to Canadian dollars at exchange rates at the reporting date. The income and expenses of foreign operation are translated to Canadian dollars at exchange rates at the quarterly average exchange rate. Any exchange difference is recognized in other comprehensive income.

(c) Cash and cash equivalents:

Cash and cash equivalents consist of highly liquid investments, with minimal interest rate risk and having an initial term to maturity of three months or less when acquired.

(d) Property and equipment:

Property and equipment are measured at cost less accumulated depreciation and accumulated impairment losses. Cost includes expenditure that is directly attributable to the acquisition of the asset.

Property and equipment is depreciated from the date of acquisition, using the straight-line method less its residual value over the estimated useful lives of the assets as follows:

| Assets | Rate |
|-------------------------|------|
| Furniture and equipment | 20% |
| Computer hardware | 45% |
| Computer software | 45% |

Depreciation methods, useful lives and residual values are reviewed at each annual reporting date and adjusted if appropriate.

(e) Intangible assets:

Intangible assets acquired as part of a group of other assets are initially recognized and measured at cost. The cost of a group of intangible assets acquired in a business combination that meet the specified criteria for recognition apart from goodwill, is allocated to the individual assets acquired based on their relative fair values. Costs incurred to establish and maintain patents for intellectual property developed internally are expensed in the period incurred.

Intangible assets with finite useful lives are amortized over their estimated useful lives from the date they are available for use. The amortization methods and estimated useful lives of intangible assets, which are reviewed annually, are as follows:

| Assets | Basis | Rate |
|--------------------|---------------|-------------|
| Licenses | Straight-line | 15-17 years |
| Patents | Straight-line | 15-17 years |
| Medical technology | Straight-line | 15 years |

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Notes to the Unaudited Condensed Consolidated Financial Statements
(All amounts expressed in Canadian dollars unless otherwise stated)

(f) Impairment:

Non-financial assets are tested for impairment annually, or whenever events or changes in circumstances indicate that an asset's carrying amount may be less than its recoverable amount. Management uses judgment to estimate these inputs and any changes to these inputs could have a material impact on the impairment calculation. For impairment testing, non-financial assets that do not generate independent cash flows are grouped together into cash-generating units (CGUs), which represents the level at which largely independent cash flows are generated. An impairment loss is recognized in earnings to the extent that the carrying value of an asset, CGU or group of CGU's exceeds its estimated recoverable amount. The recoverable amount of an asset, CGU or group of CGU's is the greater of its value in use and its fair value less cost to sell. Value in use is calculated as the present value of the estimated future cash flows discounted at appropriate discount rates. An impairment loss relating to a specific asset reduces the carrying value of the asset. An impairment loss relating to a group of CGU's is allocated on a pro-rata basis to reduce the carrying value of the assets in the units comprising the group. A previously recognized impairment loss related to non-financial assets is assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss related to non-financial assets is reversed if there is a subsequent increase in recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying value does not exceed the carrying value that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.

(g) Research and development expenditures:

Research expenditures are expensed in the period incurred. Product development expenditures are expensed in the period incurred unless the product candidate meets strict accounting criteria for deferral and amortization. The Company's policy is to amortize deferred product development expenditures over the expected future life of the product once product revenues or royalties are recorded. No product development expenditures have been deferred to date.

(h) Revenue recognition:

Revenue arising from cash and investments yielding interest is recognized when reasonable assurance exists regarding measurement and collectability, resulting in interest being recognized on a time proportional basis.

Grant revenue is recognized when there is reasonable assurance of compliance with grant conditions and the grant is collectible. Grant amounts received prior to compliance with grant conditions are initially recorded as deferred income. Grants received to directly offset expenses incurred for a specific project are credited to expense on a systematic basis in the same periods in which the expenses are recognized.

(i) Share-based compensation:

The Company uses the fair-value based method of accounting for share-based compensation for all awards of shares and share options granted. The resulting compensation expense, based on the fair value of the awards granted, is recorded in expenses with a corresponding increase in contributed surplus.

ALLON THERAPEUTICS INC.

Notes to the Unaudited Condensed Consolidated Financial Statements
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Under the fair value based method, share-based awards to employees are measured at the fair value of the equity instrument issued as of the grant date using the Black-Scholes model and estimated forfeitures. For awards with graded vesting, the fair value of each tranche is recognized over its respective vesting period. At each reporting date, the Company reassesses its estimates of the number of awards that are expected to vest and recognizes the impact of any revision in the statement of comprehensive income with a corresponding adjustment to equity.

The Company grants stock options to employees, directors and consultants pursuant to a compensation plan, which is described in note 8. Any consideration received on exercise of stock options or the purchase of stock is credited to share capital.

(j) Loss per share:

Loss per common share is calculated by dividing the net loss for the period by the weighted average number of common shares outstanding during the period. Diluted per share amounts do not differ from basic share amounts as the effect of outstanding options is anti-dilutive for all periods presented.

(k) Income taxes:

The Company uses the asset and liability method of accounting for income taxes. Under the asset and liability method, deferred income tax assets and liabilities are recognized for the deferred tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases ("temporary differences") and loss carryforwards. Deferred tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on future tax assets and liabilities of a change in tax rates is generally recognized in income in the period that includes the date of enactment or substantive enactment. Deferred income tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

(l) Financial instruments:

Financial instruments are classified into one of five categories: fair value through profit or loss, held-to-maturity, loans and receivables, available-for-sale financial assets, or other financial liabilities. All financial instruments, including derivatives, are initially measured at fair value plus transaction costs, with subsequent measurement based upon classification.

Compound instruments are bifurcated and presented in the financial statements in their component parts. The equity component is assigned the residual amount after deducting from the fair value of the instrument as a whole the amount separately determined for the liability component. The liability component is considered floating rate with no accretion recorded.

For each financial instrument, subsequent measurement and accounting for changes in fair value are dependent on the initial classification. Financial assets at fair value through profit or loss are measured at fair value with changes in fair value recognized in net income. Available-for-sale financial instruments are measured at fair value with changes in fair value recorded in other comprehensive income until the investment is derecognized or impaired at which time the amounts would be recorded in net income.

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Notes to the Unaudited Condensed Consolidated Financial Statements
(All amounts expressed in Canadian dollars unless otherwise stated)

For other financial liability, subsequent adjustments to expected cash flows are recorded if and when they occur through adjustments to the related expense.

The Company's accounts receivable are classified as loans and receivables, which are measured at amortized cost. Accounts payable, accrued liabilities and the financial liability associated with the Company's convertible royalty and revenue obligations are classified as other financial liabilities and are measured at amortized cost.

4. Property and equipment:

| March 31, 2011 | Cost | Accumulated depreciation | Net book value |
|-------------------------|-------------------|--------------------------|------------------|
| Computer hardware | \$ 90,201 | \$ 72,917 | \$ 17,284 |
| Furniture and equipment | 46,890 | 38,992 | 7,898 |
| Computer software | 21,556 | 19,331 | 2,225 |
| | <u>\$ 158,647</u> | <u>\$ 131,240</u> | <u>\$ 27,407</u> |

| December 31, 2010 | Cost | Accumulated depreciation | Net book value |
|-------------------------|-------------------|--------------------------|------------------|
| Computer hardware | \$ 97,588 | \$ 79,739 | \$ 17,849 |
| Furniture and equipment | 46,208 | 37,630 | 8,578 |
| Computer software | 21,556 | 18,939 | 2,617 |
| | <u>\$ 165,352</u> | <u>\$ 136,308</u> | <u>\$ 29,044</u> |

5. Intangible assets:

Intangible assets include acquired licenses, patents and medical technology acquired relating to the development of drugs to treat neurological diseases and disorders. There was no addition to intangible assets during the three months ended March 31, 2011. The decline in carrying value resulted from the impact of foreign exchange of \$14,701 and amortization expense of \$125,571.

| March 31, 2011 | Cost | Accumulated amortization | Net book value |
|----------------------|---------------------|--------------------------|---------------------|
| Medical technology | \$ 6,643,362 | \$ 2,878,822 | \$ 3,764,540 |
| Patents and licenses | 922,809 | 367,529 | 555,280 |
| | <u>\$ 7,566,171</u> | <u>\$ 3,246,351</u> | <u>\$ 4,319,820</u> |

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Notes to the Unaudited Condensed Consolidated Financial Statements
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| December 31, 2010 | Cost | Accumulated amortization | Net book value |
|----------------------|---------------------|--------------------------|---------------------|
| Medical technology | \$ 6,643,362 | \$ 2,768,098 | \$ 3,875,264 |
| Patents and licenses | 946,603 | 361,775 | 584,828 |
| | <u>\$ 7,589,965</u> | <u>\$ 3,129,873</u> | <u>\$ 4,460,092</u> |

6. Deferred income and government grants:

At March 31, 2011, the Company has \$84,021 of deferred income related to a grant received from the Michael J. Fox Foundation for Parkinson's Research to conduct pre-clinical research in Parkinson's disease. The Company expects to conduct this research in 2011.

7. Share capital:

(a) Authorized:

Unlimited voting common shares without par value

Unlimited preferred shares, issuable in series

(b) Convertible royalty and revenue financing:

In November 2010, the Company entered into a financing agreement with Isar Pharma K/S (Isar), a wholly owned limited partnership of Nordic Biotech Venture Fund II K/S. Under the terms of the agreement, Isar paid the Company U.S. \$10.0 million (Cdn \$10.2 million) in return for a convertible royalty and revenue obligation on davunetide. Isar can elect to convert its interest into common shares of Allon at any time at a conversion price of U.S. \$0.44 (Cdn \$0.45) which represents a 10 percent premium to the 10-day volume weighted average price of Allon prior to closing. The Company can generally force conversion at the conversion price over the next three years when the share price is two times the conversion price, or during the following 4 years when the share price is three times the conversion price. Until conversion, the Company has agreed to pay to Isar the greater of an 8 percent royalty from sales of davunetide or 20 percent of what it receives for commercializing the product. The Company will also pay 20 percent of all non-royalty revenue received in a partnership. The payment obligations decrease proportionately as the investment is converted. The number of shares issuable on conversion is limited to a maximum of 19.99 percent of the Company's outstanding shares at any time unless and until the Company's shareholders resolve both to allow conversions beyond 19.99 percent and to terminate the shareholder rights plan.

This financing agreement was accounted for as a compound instrument and is presented in the financial statements in its component parts. The equity component was assigned the residual amount after deducting from the fair value of the instrument as a whole the amount separately determined for the liability component. An amount of \$0.2 million was included in long term liabilities as the liability component of the financing agreement and was calculated as the present value of the estimated future royalty payments discounted at a rate applicable to biotechnology companies at a similar stage of

ALLON THERAPEUTICS INC.

Notes to the Unaudited Condensed Consolidated Financial Statements
(All amounts expressed in Canadian dollars unless otherwise stated)

development. An amount of \$9.7 million, representing the value of the right of conversion, was included in shareholders' equity as the equity component of the financing agreement and was calculated as the difference between the liability component and the amount of the investment by Isar, net of transaction costs of \$0.3 million. The liability component is classified as other financial liabilities and is accounted for at amortized cost. The distribution payment stream related to the liability component is considered to be a non-financial variable specific to the Company and as a result, it does not meet the criteria for a derivative. The Company's accounting policy is to treat this instrument as a variable-rate debt. Any subsequent changes to the cash flows will only be reflected in income when the related change is realized.

To estimate the fair value of the liability component of the financing agreement, the Company used a probability weighted discounted cash flow model based on estimated timing and amount of future cash flows, discounted using a risk adjusted cost of capital of 47% determined by management after considering all available market and industry information including the Company's market capitalization. Future cash flows were estimated by utilizing external market research to estimate market size and pricing assumptions. If the discount rate were to increase by 1%, the liability component would decrease by approximately \$5,400. If estimated future revenues were to decrease by 10%, the liability component would decrease by approximately \$18,500.

(c) Standby equity distribution agreement:

On March 2, 2010, the Company entered into a standby equity distribution agreement (SEDA) with YA Global Master SPV Ltd., a fund managed by Yorkville Advisors, LLC (Yorkville). Under the terms of the agreement, Yorkville has committed to provide up to \$10 million of equity capital over three years, if and when drawn by the Company at the Company's discretion. The Company can terminate the agreement at any time without payment of any additional fees. Newly issued common shares will be priced at a 5% discount to the 5-day weighted average share price of the Company's shares at the time of draw down, and are subject to a minimum price set by the Company in advance. In January 2011, the Company initiated its first draw down under the SEDA of \$200,000. According to the SEDA provisions, Yorkville subscribed for common shares at a 5% discount to the five-day weighted average price of Allon shares for the period ending on January 12, 2011.

8. Share-based compensation:

The Company recognized \$54,491 in share-based compensation expense for the three months ended March 31, 2011 compared to \$11,508 for the three months ended March 31, 2010. Share-based compensation expenses comprised awards granted to employees and non-employees under the Company's stock option plan.

The Company's Stock Option Plan ("the Plan"), provides for the granting of options for the purchase of common shares of the Company at a purchase price not less than 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.

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Notes to the Unaudited Condensed Consolidated Financial Statements
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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, 2011, the Company had 78,523,161 common shares issued and outstanding resulting in current authorization to issue a maximum of 7,852,316 options under the Plan.

Stock option activity from December 31, 2009 to March 31, 2011 is as follows:

| | Common shares under option | Weighted average exercise price |
|--------------------------------|-------------------------------|------------------------------------|
| Outstanding, December 31, 2009 | 7,152,100 | \$ 0.76 |
| Granted | 312,500 | 0.40 |
| Exercised | - | - |
| Cancelled | (432,500) | 0.90 |
| Outstanding, December 31, 2010 | 7,032,100 | \$ 0.74 |
| Granted | 250,000 | 0.41 |
| Exercised | - | - |
| Cancelled | - | - |
| Outstanding, March 31, 2011 | 7,282,100 | \$ 0.73 |

At March 31, 2011, the Company has 4,471,770 stock options exercisable at weighted average exercise price of \$0.71. At December 31, 2010, the Company has 4,471,770 stock options exercisable at weighted average exercise price of \$0.71.

The following table summarizes stock options outstanding at March 31, 2011:

| 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 – 0.41 | 3,479,600 | 6.29 | \$ 0.26 | 2,175,937 | \$ 0.20 |
| \$ 1.00 – 1.72 | 3,802,500 | 5.29 | 1.16 | 2,295,833 | 1.20 |
| | 7,282,100 | 5.77 | \$ 0.73 | 4,471,770 | \$ 0.71 |

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 subjective assumptions including the expected life of the option and expected future stock price volatility. Changes in these assumptions can materially affect the estimated fair value of the Company's stock options.

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Notes to the Unaudited Condensed Consolidated Financial Statements
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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 non-employee awards are estimated each reporting period until the final measurement date.

The following table summarizes assumptions used in the Black-Scholes option pricing model for employees and directors for the respective three month periods ending March 31, 2011 and March 31, 2010. There were no stock option award to employees and directors during the three months ended March 31, 2010.

| | Employees & Directors | |
|-------------------------|-----------------------|------|
| | 2011 | 2010 |
| Dividend yield | 0% | n/a |
| Expected volatility | 72% | n/a |
| Risk free interest rate | 3.04% | n/a |
| Expected life in years | 8.00 | n/a |
| Fair value per share | \$0.30 | n/a |
| Forfeiture rate | 4.85% | n/a |

9. Net loss per common share:

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

| | Three months ended | |
|--|--------------------|----------------|
| | March 31, 2011 | March 31, 2010 |
| Net loss for the period | \$ (2,974,076) | \$ (3,120,340) |
| Weighted average number of common shares outstanding | 78,523,161 | 78,066,666 |
| Net loss per common share | \$ (0.04) | \$ (0.04) |

10. Related party transactions:

During the three months ended March 31, 2011, the Company paid one of its Board members \$12,500 (three months ended March 31, 2010 - \$50,000) for consulting services provided to the Company in relation to general research and advancement of the Company's drug development programs performed outside of his capacity as a director. The Company plans to retain these services on a continuing basis.

11. Transition to International Financial Reporting Standards:

As stated in note 2(a), these are the Company's first condensed consolidated interim financial statements prepared in accordance with IFRS.

The accounting policies set out in note 3 have been applied in preparing the interim financial statements for the three months ended March 31, 2011, the comparative information presented in these interim financial statements for both the three months ended March 31, 2010 and year ended December 31, 2010 and in the

ALLON THERAPEUTICS INC.

Notes to the Unaudited Condensed Consolidated Financial Statements
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preparation of the opening IFRS statement of financial position at January 1, 2010 (the Company's date of transition).

IFRS 1, First-Time Adoption of International Financial Reporting Standard, permits those companies adopting IFRS for the first time to take certain exemptions from the full requirements of IFRS at the time of transition. The following are the initial IFRS 1 mandatory elections and optional exemptions applied by the Company upon initial adoption of IFRS from Canadian GAAP:

(i) Estimates:

Hindsight is not used to create or revise estimates. The estimates previously made by the Company under Canadian GAAP were not revised for application of IFRS except where necessary to reflect any differences in accounting policies.

(ii) Share-based payments:

The Company has elected to apply IFRS 2, Share-based Payments, to all equity instruments granted after November 7, 2002 that had not vested as of the Transition Date and elected not to apply the standard to any equity instruments issued prior to this date.

(iii) Business combinations:

The Corporation has elected to prospectively apply IFRS 3, Business Combinations, from the Transition Date, rather than retrospectively restating all business combinations that have occurred prior to the Transition Date.

(iv) Currency translation differences:

The Company has elected to reset its historical cumulative translation gains and losses to nil at the Transition Date, rather than to retrospectively apply IAS 21, The Effects of Changes in Foreign Exchange Rates.

In preparing its opening IFRS statement of financial position, the Company has adjusted amounts reported previously in financial statements prepared in accordance with Canadian GAAP. An explanation of how the transition from Canadian GAAP to IFRSs has affected the Company's accounting policies, statement of financial position, and statement of comprehensive income for periods previously reported under Canadian GAAP, but subsequent to the Transition Date to IFRS, is set out in the following tables and the notes that accompany the tables. The adoption of IFRS did not change the Company's actual cash flows, but has resulted in changes to the Company's statements of financial position and comprehensive loss.

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Notes to the Unaudited Condensed Consolidated Financial Statements
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Reconciliation of Assets, Liabilities and Equity

| Note | Previous GAAP | Effect of transition to IFRSs | IFRSs | Previous GAAP | Effect of transition to IFRSs | IFRSs | Previous GAAP | Effect of transition to IFRSs | IFRSs |
|---|---------------------|-------------------------------|---------------------|---------------------|-------------------------------|---------------------|---------------------|-------------------------------|---------------------|
| | January 1, 2010 | | | March 31, 2010 | | | December 31, 2010 | | |
| ASSETS | | | | | | | | | |
| Current Assets: | | | | | | | | | |
| Cash and cash equivalents | \$11,002,859 | \$ - | \$ 11,002,859 | \$ 6,459,236 | \$ - | \$ 6,459,236 | \$ 7,860,284 | \$ - | \$ 7,860,284 |
| Accounts Receivable | 22,438 | - | 22,438 | 29,659 | - | 29,659 | 143,846 | - | 143,846 |
| Prepaid expenses and deposits | 430,878 | - | 430,878 | 291,172 | - | 291,172 | 855,680 | - | 855,680 |
| Drug supplies | 3,922,156 | (245,634) | 3,676,522 | 3,957,311 | (363,507) | 3,593,804 | 218,560 | (13,057) | 205,503 |
| | 15,378,332 | (245,634) | 15,132,697 | 10,737,377 | (363,507) | 10,373,870 | 9,078,370 | (13,057) | 9,065,313 |
| Non-Current Assets: | | | | | | | | | |
| Property and equipment | 42,567 | - | 42,567 | 35,567 | - | 35,567 | 29,044 | - | 29,044 |
| Intangible assets | 5,114,429 | (113,906) | 5,000,523 | 4,984,832 | (133,440) | 4,851,392 | 4,596,040 | (135,948) | 4,460,092 |
| Drug supplies | 327,938 | (54,678) | 273,261 | 327,938 | (63,830) | 264,108 | 327,938 | (69,342) | 258,596 |
| | \$20,863,266 | \$(414,218) | \$20,449,048 | \$16,085,714 | \$(560,777) | \$15,524,936 | \$14,031,392 | \$(218,347) | \$13,813,045 |
| LIABILITIES & SHAREHOLDER'S EQUITY | | | | | | | | | |
| Current Liabilities | | | | | | | | | |
| Trade and other payables | \$ 2,290,906 | \$ - | \$ 2,290,906 | \$ 649,001 | \$ - | \$ 649,001 | \$ 1,731,018 | \$ - | \$ 1,731,018 |
| Deferred revenue | - | - | - | - | - | - | 159,543 | - | 159,543 |
| | 2,290,906 | - | 2,290,906 | 649,001 | - | 649,001 | 1,890,561 | - | 1,890,561 |
| Non-Current liabilities | | | | | | | | | |
| | - | - | - | - | - | - | 180,628 | - | 180,628 |
| Shareholders' equity: | | | | | | | | | |
| Share capital | 69,110,562 | - | 69,110,562 | 69,110,562 | - | 69,110,562 | 69,110,562 | - | 69,110,562 |
| Contributed surplus | 2,252,685 | 124,163 | 2,376,849 | 2,303,631 | 84,726 | 2,388,357 | 12,231,641 | 76,818 | 12,308,459 |
| Cumulative translation adjustment | - | - | - | - | (173,375) | (173,375) | - | (147,699) | (147,699) |
| Deficit | (52,790,887) | (538,381) | (53,329,269) | (55,977,480) | (472,128) | (56,449,609) | (69,382,000) | (147,466) | (69,529,466) |
| | 18,572,360 | (414,218) | 18,158,142 | 15,436,713 | (560,777) | 14,875,936 | 11,960,203 | (218,347) | 11,741,856 |
| | \$20,863,266 | \$(414,218) | \$20,449,048 | \$16,085,714 | \$(560,777) | \$15,524,936 | \$14,031,392 | \$(218,347) | \$13,813,045 |

ALLON THERAPEUTICS INC.

Notes to the Unaudited Condensed Consolidated Financial Statements
(All amounts expressed in Canadian dollars unless otherwise stated)

Reconciliation of Comprehensive Income

| | Note | Three months ended March 31, 2010 | | | Year ended December 31, 2010 | | |
|--|------|-----------------------------------|-------------------------------|---------------------|------------------------------|-------------------------------|----------------------|
| | | Previous GAAP | Effect of transition to IFRSs | IFRSs | Previous GAAP | Effect of transition to IFRSs | IFRSs |
| Expenses: | | | | | | | |
| Research and development | f | \$ 2,167,911 | \$ 96,618 | \$ 2,264,529 | \$ 12,140,132 | \$ 483,952 | \$12,624,084 |
| General and administrative | f | 852,407 | 724 | 853,131 | 3,766,596 | 13,810 | 3,780,406 |
| Amortization | f | 136,780 | (136,780) | - | 545,108 | (545,108) | - |
| | | 3,157,098 | (39,438) | 3,117,660 | 16,451,836 | (47,346) | 16,404,490 |
| Other expense (income): | | | | | | | |
| Interest and other income | | (8,754) | | (8,754) | (61,383) | | (61,383) |
| Foreign exchange loss/ (Gain) | g | 38,249 | (26,815) | 11,434 | 200,660 | (343,569) | (142,909) |
| | | 29,495 | (26,815) | 2,680 | 139,277 | (343,569) | (204,292) |
| Net loss for the period | | \$ 3,186,593 | (66,253) | \$ 3,120,340 | \$ 16,591,113 | \$ (390,915) | \$ 16,200,198 |
| Other comprehensive expense | | | | | | | |
| Foreign currency translation | g | \$ - | \$ 173,375 | \$ 173,375 | \$ - | \$ 147,699 | \$ 147,699 |
| Net and comprehensive loss for the period | | \$ 3,186,593 | \$ 107,122 | \$ 3,293,715 | \$ 16,591,113 | \$ (243,216) | \$16,347,897 |
| Net loss per share: | | | | | | | |
| Basic and diluted | | \$ 0.04 | | \$ 0.04 | \$ 0.21 | | \$ 0.21 |

ALLON THERAPEUTICS INC.

Notes to the Unaudited Condensed Consolidated Financial Statements
(All amounts expressed in Canadian dollars unless otherwise stated)

Under its previous GAAP, non-monetary assets and liabilities of the Company's U.S. subsidiary were translated using the temporal method. Under IFRSs, all assets and liabilities of the Company's U.S. subsidiary are translated using the current rate method. The impact arising from the change is summarized as follows:

a) Drug supplies – current:

| | January 1, 2010 | March 31, 2010 | December 31, 2010 |
|-------------------------------|-----------------|----------------|-------------------|
| Drug Supplies at USD | \$ 3,498,118 | \$ 3,537,905 | \$ 206,617 |
| Temporal rate | 1.1212 | 1.1185 | 1.0578 |
| Drug Supplies at CAD | | | |
| per Cdn GAAP | 3,922,156 | 3,957,311 | 218,560 |
| | January 1, 2010 | March 31, 2010 | December 31, 2010 |
| Drug Supplies at USD | \$ 3,498,118 | \$ 3,537,905 | \$ 206,617 |
| Current rate | 1.0510 | 1.0158 | 0.9946 |
| Drug Supplies at CAD per IFRS | 3,676,522 | 3,593,804 | 205,503 |
| Adjustment | (245,634) | (363,507) | (13,057) |

b) Intangible assets:

| | January 1, 2010 | March 31, 2010 | December 31, 2010 |
|--------------------------|-----------------|----------------|-------------------|
| Intangible assets at USD | \$ 649,251 | \$ 633,939 | \$ 588,002 |
| Temporal rate | 1.2264 | 1.2264 | 1.2264 |
| Intangible assets at CAD | | | |
| per Cdn GAAP | 796,269 | 777,396 | 720,776 |
| | January 1, 2010 | March 31, 2010 | December 31, 2010 |
| Intangible assets at USD | \$ 649,251 | \$ 633,939 | \$ 588,002 |
| Current rate | 1.0510 | 1.0158 | 0.9946 |
| Intangible assets at CAD | | | |
| per IFRS | 682,364 | 643,955 | 584,827 |
| Adjustment | (113,905) | (133,440) | (135,949) |

ALLON THERAPEUTICS INC.

Notes to the Unaudited Condensed Consolidated Financial Statements
(All amounts expressed in Canadian dollars unless otherwise stated)

c) Drug supplies – non-current

| | January 1, 2010 | March 31, 2010 | December 31, 2010 |
|-----------------------------------|-----------------|----------------|-------------------|
| Drug Supplies at USD | \$ 260,000 | \$ 260,000 | \$ 260,000 |
| Temporal rate | 1.2613 | 1.2613 | 1.2613 |
| Drug Supplies at CAD per Cdn GAAP | 327,938 | 327,938 | 327,938 |

| | January 1, 2010 | March 31, 2010 | December 31, 2010 |
|-------------------------------|-----------------|----------------|-------------------|
| Drug Supplies at USD | \$ 260,000 | \$ 260,000 | \$ 260,000 |
| Current rate | 1.0510 | 1.0158 | 0.9946 |
| Drug Supplies at CAD per IFRS | 273,260 | 264,108 | 258,596 |
| Adjustment | (54,678) | (63,830) | (66,342) |

d) Under its previous GAAP, the company used a straight-line approach to amortization of share-based compensation expense. In addition, adjustments for forfeitures were made as they occurred. Under IFRSs, share options that vest in installments are amortized accordingly in an accelerated format. In addition, estimates of forfeitures are required on initial recognition with adjustments to actual forfeitures on vesting date. The impact arising from the change is summarized as follows:

| | Accumulated as of January 1, 2010 | For the three months ended March 31, 2010 | For the year ended December 31, 2010 |
|---|-----------------------------------|---|--------------------------------------|
| Share based compensation per Cdn GAAP | \$ 450,409 | \$ 50,947 | \$ 247,667 |
| Adjustments for: | | | |
| Accelerated vesting | 121,136 | (39,859) | (48,883) |
| Forfeiture | 3,027 | 420 | 1,538 |
| Total adjustments | 124,163 | (39,439) | (47,346) |
| Share based compensation per IFRS | 574,573 | 11,508 | 200,321 |
| Accumulated adjustment to Contributed Surplus | 124,163 | 84,724 | 76,818 |

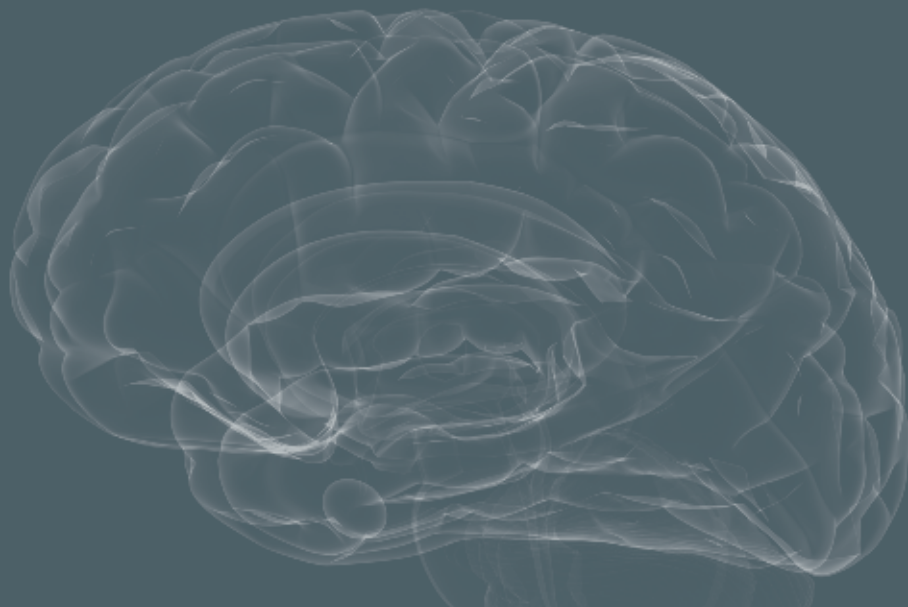
ALLON THERAPEUTICS INC.

Notes to the Unaudited Condensed Consolidated Financial Statements
(All amounts expressed in Canadian dollars unless otherwise stated)

- e) The cumulative effect of all of the above adjustments has resulted in an increase in accumulated deficit of \$538,381 as at January 1, 2010, \$472,128 as at March 31, 2010 and \$147,466 as at December 31, 2010.
- f) Under its previous GAAP, the Company presents its expenses by function, with the exception of depreciation/amortization of property, plant and equipment and intangibles. Under IFRS, depreciation and amortization expenses are allocated to the relevant functional areas of research and development (R&D) and general and administrative (G&A) expenses. Furthermore, adjustments related to share based compensation as describe in d) above were also allocated to the relevant functional areas of R&D and G&A. The impact arising from the change is summarized as follows:

| | Three months ended March 31, 2010 | Year ended December 31, 2010 |
|--|--------------------------------------|---------------------------------|
| Amortization related to R&D | \$ 131,466 | \$ 526,006 |
| Share based compensation adjustment to R&D | (34,848) | (42,054) |
| Total adjustment to R&D | \$ 96,618 | \$ 483,952 |
| Amortization related to G&A | \$ 5,314 | \$ 19,102 |
| Share based compensation adjustment to G&A | (4,590) | (5,292) |
| Total adjustment to G&A | \$ 724 | \$ 13,810 |

- g) Under its previous GAAP, the Company used the temporal method of translation for its U.S. subsidiary whereby only monetary assets and liabilities are translated to the reporting currency at current rates of exchange and the effect of the translation is reported as a foreign exchange gain or loss. Under the current rate method used in IFRS, all assets and liabilities are translated to the reporting currency at current rates of exchange and the effect of the translation is reported as other comprehensive income or loss.



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