

WELICHEM BIOTECH INC.
FORM 51 – 102F2
MANAGEMENT DISCUSSION AND ANALYSIS
Period Ended November 30, 2009

The following discussion and analysis, prepared as of January 23, 2010, should be read together with the Company's audited financial statements for year ended May 31, 2009 and unaudited financial statements for period ended November 30, 2009 and related notes attached thereto, which are prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). All amounts are stated in Canadian dollars unless otherwise indicated.

This Management Discussion & Analysis summarizes the activities of the Company and provides financial information for the three month period ended November 30, 2009. The discussion contains forward-looking statements made by management that involve risks and uncertainties. Such information is considered reasonable by the Company's management at the time of preparation. The actual results may differ materially from those contained in any forward-looking statements.

OVERVIEW

Welichem Biotech Inc., ("Welichem" or "the Company") is dedicated to the research and development of its anti-inflammatory drug candidate, WBI-1001, as a novel topical treatment for inflammatory skin diseases including psoriasis and atopic dermatitis. The main focus is on securing proof of principle of the unique properties of potential drug candidates being developed in the Company's pipeline.

Progress in this quarter was exclusively focused on the planning of obtaining regulatory approval for and initiating the Phase IIb clinical study on atopic dermatitis with the Company's lead drug candidate, WBI-1001. This was done mindful of the company's stringent budgetary constraints.

Development of Welichem's non-steroidal and non-immunosuppressive anti-inflammatory topical treatment (WBI-1001 cream) on inflammatory skin diseases.

As an emerging pharmaceutical research and development company Welichem is focused on taking its lead drug candidate, the non-steroidal and non-immunosuppressive anti-inflammatory compound WBI-1001, to the market as rapidly as possible for the treatment of significant unmet medical needs. To this end, Welichem submitted, in 2009 Q2, a Clinical Trial Applications to the

Therapeutic Products Directorate (TPD) of Health Canada. The TPD's successful authorization enabled Welichem to initiate a Phase IIb, multi-centered, double-blinded and placebo-controlled clinical trial of WBI-1001 on patients with Atopic Dermatitis (a form of eczema). The prime objective of the Phase IIb study is to evaluate the efficacy of topically applied WBI-1001 creams (0.5% or 1.0%), over a total of 12 weeks, to 18-65 year old patients, and to determine the safety and tolerability of the active creams over a 12-week period. Recruitment and treatment are underway in this trial at three Canadian clinical centers. Patient enrollment is expected to be completed by the end of March 2010.

In this quarter, Welichem also planned another Phase II trial on the topical treatment for psoriasis. This Phase IIa study will be a randomized, double-blinded and placebo-controlled trial of WBI-1001 on patients with mild to moderate plaque psoriasis. It is anticipated that patient enrollment for this study will take place in February 2010.

Safe and potent topical therapies for both psoriasis and atopic dermatitis represent significant unmet medical needs. The Company recognizes the potential increased value of a successful outcome to these phase II clinical trials and the value of finding the ideal partner for Welichem to take this drug candidate to market. The previously completed clinical trials of WBI-1001 in patients with AD and plaque psoriasis have provided very encouraging results. Those showing this drug candidate's excellent safety profile and significant efficacy on patients with AD have been accepted for publication in the Archives of Dermatology.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The Company prepared its financial statements in accordance with Canadian generally accepted accounting principles ("GAAP") and the reporting currency is the Canadian dollar. These accounting principles require the Company to make certain estimates and assumptions. Management believes that the estimates and assumptions upon which it relies are reasonable based on information available at the time that these estimates and assumptions are made. Actual results could differ from these estimates. Areas of significant estimates include: amortization of property and equipment, and stock-based compensation. The significant accounting policies that the Company believes are the most critical in fully understanding and evaluating the reported financial results include the following:

Cash and cash equivalents

The Company considers unrestricted cash on hand and in banks, term deposits and guaranteed financial instruments with an original maturity of 90 days or less as cash and cash equivalents. Cash equivalents are classified as held-for-trading investments and measured at fair value.

Short-term investments

The Company considers fixed income investments, marketable securities and other highly liquid financial instruments purchased with a maturity greater than 90 days but less than one year at the date of purchase as short term investments. Short-term investments with a stated maturity date that are not cash equivalents are classified as held-to-maturity investments, except where the Company does not intend to hold to maturity and, therefore, the investment is designated as held-for-trading. Held-to-maturity investments are measured at amortized cost using the effective interest rate method, while held-for-trading investments are recorded at fair value and the resulting gain or loss is recognized in earnings.

Accounts payable and accrued liabilities

Accounts payable and accrued liabilities are typically short-term in nature and classified as other financial liabilities. These liabilities are carried at amortized costs.

Property and equipment

Property and equipment are recorded at cost less accumulated amortization, and are amortized over their expected useful lives on the following basis:

Lab equipment	30% declining balance
Office equipment	30% declining balance
Leasehold improvements	Term of the lease

The Company uses the half year rule in the year of acquisition.

Impairment of long-lived assets

The Company reviews the carrying value of its long-lived assets for existence of facts or changes in circumstances that might indicate a condition of impairment. An impairment loss would be recognized when the estimated undiscounted future projected cash flows expected to result from the use of the asset and its eventual disposition is less than the carrying amount. The amount of the impairment loss

to be recorded is calculated by the excess of the carrying value over its fair value, with fair value being determined using a discounted cash flow analysis.

Stock-based compensation

The Company uses the fair value method for stock-based compensation granted to employees and non-employees of the Company, and all direct awards of stock, in accordance with the CICA Handbook Section 3870 “Stock-Based Compensation and Other Stock-Based Payments”. The fair value of stock options is determined by the Black-Scholes Option Pricing Model with assumptions for risk-free interest rates, dividend yields, volatility factors of the expected market price of the Company’s common shares and an expected life of the options. The fair value of direct awards of stocks is determined by the quoted market price of the Company’s stock.

Foreign currency translation

The Company maintains its accounting records in Canadian dollars. At the transaction date, transactions completed in foreign currencies are translated into Canadian dollars by the use of the exchange rate in effect at that date. Revenues and expenses are translated at the average exchange rate for the year. At the year end, monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the year-end exchange rates. Non-monetary assets and liabilities are translated using historical exchange rates. Exchange gains and losses on translation are included in operations.

Research and development expenses

Research costs are expensed as incurred. Development costs are expensed as incurred unless such development costs meet the criteria under Canadian GAAP for deferral and amortization. Development costs which meet generally accepted criteria for deferral are capitalized and amortized against earnings over the estimated period of benefit. As of November 30, 2009, the Company has not deferred any development costs.

Government assistance and other subsidies

Government assistance and other subsidies are recorded as either a reduction of the cost of the applicable assets or credited in the statement of operations as determined by the terms and conditions of the agreement under which the assistance is provided to the Company when there is reasonable assurance that the Company has complied with all conditions necessary to receive the grants and collectibility is reasonably assured.

Earnings (loss) per share

Basic earnings (loss) per share are computed using the weighted average number of common shares outstanding during the year. Diluted earnings (loss) per share is calculated giving effect to the potential dilution that would occur if securities or other contracts to issue common shares were exercised or converted to common shares using the treasury method. The treasury method assumes that proceeds received from the exercise of stock options and warrants are used to repurchase common shares at the prevailing market rate. Diluted loss per share is equal to the basic loss per share as inclusion of common share equivalents securities are anti-dilutives in the six-month period ended November 30, 2009 and 2008.

Income taxes

Future income taxes are recorded using the liability method. Future tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Future tax assets and liabilities are measured using substantively enacted tax rates expected to apply when the asset is realized or the liability settled. The effect on future tax assets and liabilities of a change in tax rates is recognized in income in the period that substantive enactment or enactment occurs. To the extent that the Company does not consider it more likely than not that a future tax asset will be recovered, it provides a valuation allowance against the excess.

EARLY ADOPTION OF NEW ACCOUNTING POLICY

Goodwill and Intangible Assets:

In fiscal year 2009, the Company chose to early adopt early the CICA issued Section 3064, Goodwill and Intangible Assets, which replace Section 3062, Goodwill and Other Intangible Assets, and Section 3450, Research and Development Costs. The standard provides guidance on the recognition of intangible assets in accordance with the definition of an intangible asset and the criteria for asset recognition as well as classifying the application of the concept of matching revenues and expenses, whether these assets are separately acquired or internally developed. The change as result of early adoption of accounting standard in respect of patent costs has been applied retroactively. The impact of adopting this standard had been to increase the opening deficit and to reduce patent rights and applications at the beginning of 2009 by \$273,708 which is the net book value of patent costs related to periods prior to the date. Furthermore, following the adoption of this standard, additions to patents and trademarks in the amount of \$14,989 previously added to patent rights and applications were expensed and amortization of patent rights and applications were reduced by \$21,318 for the six-month period ended November 30, 2009.

NEW ACCOUNTING PRONUCEMENTS

Section 1582, Business Combinations

This Section establishes the standards for the accounting of business combinations, and stated that all assets and liabilities of an acquired business will be recorded at fair value. Obligations for contingent considerations and contingencies will also be recorded at acquisition date fair value. The standard also states that acquisition-related costs will be expensed as incurred and that restructuring charges will be expensed in the periods after the acquisition date. This standard is equivalent to the International Financial Reporting Standard on business combinations. The Company will be required to adopt this standard prospectively for business combinations with acquisition dates no later than April 1, 2011. The Company is currently assessing the impact of adopting this standard on financial statements.

Section 1601, Consolidated Financial Statements

In January 2009, CICA issued Handbook Section 1601, “*Consolidated Financial Statements*” which replaced the existing standard. This Section establishes the standards for preparing consolidated financial statements and its effective for the Company on April 1, 2011. The Company is assessing the impact of adopting this standard on financial statements.

Section 1602, Non-Controlling Interests

In January 2009, CICA issued Handbook Section 1602, “*Non-Controlling Interests*”. This Section establishes the standards for accounting of non-controlling interests of a subsidiary in the preparation of consolidated financial statements subsequent to a business combination, and effective for the Company on April 1, 2011. The Company is assessing the impact of adopting this standard on financial statements.

Transition to International Financial Reporting Standards

In January 2006, CICA Accounting Standards Board (“AcSB”) adopted a strategic plan for the direction of accounting standards in Canada. As part of that plan, accounting standards in Canada for public companies are expected to converge with International Financial Reporting Standards (“IFRS”) for accounting periods commencing on or after January 1, 2011. The Company is currently in the diagnostic phase of the conversion of our financial statements to IFRS. This phase includes identifying the difference between existing Canadian GAAP and IFRS standards and evaluating their impact on business processes and information systems, as well as assessing resource requirements for the

conversion. The Company expects to complete our analysis over the next three quarters.

By February 28, 2010, when the diagnostic phase is complete, we will prepare a detailed conversion plan in the fourth quarter of fiscal 2010 and thereafter begin execution to this plan. It is currently not possible to fully determine the impact of conversion to IFRS on the financial statements and any potential business impacts, as our diagnostic phase is not complete and as accounting standards and related interpretations continues to change.

RESULTS OF OPERATIONS

Presently, Welichem has no revenues and it is unlikely to be in a position to generate sufficient revenues to meet its ongoing operating and capital expenses for the foreseeable future. Thus the Company has incurred operating losses since inception.

The Company reported a net loss of \$654K in Q2 2010 compared to a net loss of \$461K in Q2 2009. The company had post-consolidation 42,336,299 common shares outstanding at November 30 09 compared to 17,336,299 common shares at November 30, 2008. Its net loss per share in Q2 2010 decreased to ¢2 cent per share from ¢3 cent per share in Q2 2009.

Research and Development Expenses

Research & Development expenses (“R&D”) will generally vary from period to period depending on the scope of clinical development, research programs pursued, stage of clinical trials undertaken, the number of clinical trials that are active during a particular period of time, the rate of patient enrollment, the decisions made to continue the development and testing a product candidate based on supporting safety and efficacy results from clinical trails.

The R&D expenses in this period increased \$311K (or 124%) over the comparative period last year (\$562K in Q2 2010 vs. \$251K in Q2 2009). The major increase of R&D expenses came from the \$311K (or 227%) more subcontracting costs that occurred in this period. Our subcontracting work in this quarter focused on the preparation for WBI-1001 Phase IIb clinical trial as compared with the WBI-1001 Phase IIa clinical trial costs during the comparative period last year.

The Company received a financial contribution of \$461K covering period from year 2006 to year 2009 by NRC – IRAP for research and development of its novel anti-cancer compound, WBI-2100. On April 1, 2009 the Company was granted

another \$93,333 award for the fiscal year of 2009 to 2010. In the six-month period ended on November 30, 2009 the Company received grants of \$93,333 out of which \$46,434 was accrued in fiscal year 2009. .

The 2010 YTD R&D expenses totaled \$955K representing a \$408K (or 75%) increase from the \$547K incurred during the 2009 YTD comparative period. The increase was due to the different stage of development costs and clinical trial activities for the WBI-1001 product. The 2010 YTD R&D expense is estimated \$800K more than 2009 YTD R&D expenses as the clinical studies (a Phase IIb on atopic dermatitis and a Phase IIa on psoriasis) approach at the end of this fiscal year.

General and Administrative Expenses

General and Administrative expenses (“G&A”) decreased \$116K (or 48%) over the comparative period last year (\$127K in Q2 2010 vs. \$244K in Q2 2009).

Factors that contributed to increases for certain administrative expense items for this quarter included:

- i) \$30K of decrease in public relation costs of the Company.
- ii) \$29K of decrease in accounting fees mainly due to over accrual of auditing fee last year.
- iii) \$18K of decrease in legal cost for less financing-related legal consulting this period.
- iv) \$14K of decrease in G&A wages because we paid retroactive salary to the Company’s CEO last year.
- v) \$13K of decrease in rent as we reduced one-third of our office space starting from January 2009.

The 2010 YTD G&A expenses also decreased \$171K (or 42%) to \$234K from \$405K incurred during the 2009 YTD comparative period. The major decrease came from \$38K less G&A wages, \$32K less annual auditing fees, \$30K less public relation costs, \$24K less financing activity related legal costs, and \$21K less rental expenses.

Interest Income

Interest income increased \$7K in Q2 2010 over Q2 2009 and decreased \$26K in 2010 YTD compared to 2009 YTD. The change in interest income was directly related to the net amount of short-term investments in different periods.

LIQUIDITY AND CAPITAL RESOURCES

From its incorporation in 1995, the Company has financed its operations through private sales of equity securities, debt and through interest income, refundable tax credits and government grants.

On September 15, 2009 the Company received a private placement of \$3,750,000 less issuing costs of \$375,000 by issuing 25,000,000 units comprising post-consolidation common shares at a price of \$0.15 per share and 12,500,000 post-consolidation warrants exercisable at \$0.15 up to July 7, 2011 in gross proceeds.

In addition, the Company will continue to fund its operations from a combination of the sales and issuance of equity securities until the Company achieves the licensing or drug commercialization stages.

As of November 30, 2009, the Company had a net working capital of \$2,565,558 (May 31 2009 - \$333,208) with \$545,208 (May 31 2009 - \$141,559) in cash and cash equivalents and \$2,036,459 (May 31 2009 - \$619,335) in short-term investments.

With this private placement fund, together with interest income, the Company anticipates that it has sufficient funds for operations, research and development up to the end of fiscal year 2010.

MATERIAL COMMITMENTS AND CONTRACTUAL OBLIGATIONS

The Company leases lab and office space and is committed to future minimum lease payments as follows:

December 2009 to May 2010	40,965
June 2010 to September 2010	<u>27,907</u>
	<u>\$68,872</u>

The Company is also committed to paying its share of operating costs in connection with its lab and office space. In addition, the Company has signed agreements and contracts with various contract research organizations (CROs) related to its different research and development projects, and will be obliged to pay a total of \$730,476 to the CROs as the work is completed.

RISKS AND UNCERTAINTIES

The Company's business is in the development stage and does not generate cash flow from operations to adequately fund its activities and has thus relied principally on the issuance of securities for financing. There is no assurance that such financing will be available on a timely basis under terms acceptable to the Company.

It should be noted that the Company's funding needs may vary depending upon several factors, including the progress and nature of research and development initiatives, the ability to attract and maintain strategic alliances, the Company's decision to in-license technology, acquisition and unforeseen costs associated with undertaking pre-clinical/clinical studies.

If adequate funding is not available, the Company may be required to delay, reduce or eliminate one or more of its research and development programs or obtain funds through arrangements with corporate partners or others that may require the Company to relinquish some or all rights to product candidates at an earlier stage of development or on less favorable terms than the Company would otherwise seek. Insufficient funding may also require the Company to relinquish rights to certain of its technologies that the Company would otherwise develop itself.

SUMMARY OF ANNUAL INFORMATION

	Year Ended May 31, 2009	Year Ended May 31, 2008 ⁽¹⁾ (restated)	Year Ended May 31, 2007 ⁽¹⁾ (restated)
Loss for the year	(2,701,954)	(2,503,756)	(3,211,552)
Loss per Common Share -basic and fully diluted ⁽²⁾	(0.16)	(0.34)	(0.52)
Total Assets	881,709	5,115,790	1,473,655
Total Current Liabilities	512,697	1,626,499	463,591
Total Long-term Liabilities	0	0	0
Shareholders' Equity	369,012	3,489,291	1,010,064

SUMMARY OF UNAUDITED QUARTERLY INFORMATION

	2 nd Quarter Ended November 30, 2009	1 st Quarter Ended August 31, 2009	4 th Quarter Ended May 31, 2009	3 rd Quarter Ended February 28, 2009 ⁽¹⁾ - restated	2 nd Quarter Ended November 30, 2008 ⁽¹⁾ - restated	1 st Quarter Ended August 31, 2008 ⁽¹⁾ - restated	4 th Quarter Ended May 31, 2008 ⁽¹⁾ - restated	3 rd Quarter Ended February 29, 2008 ⁽¹⁾ - restated
Loss for the period	(653,918)	(514,022)	(1,306,450)	(503,173)	(460,969)	(431,362)	(811,046)	(610,650)
Loss per Common Share – basic and fully diluted ⁽²⁾	(0.02)	(0.03)	(0.08)	(0.03)	(0.03)	(0.05)	(0.11)	(0.09)
Total Assets	2,637,044	19,620	881,709	1,975,409	2,241,809	2,750,942	5,115,790	216,105
Total Liabilities	38,498	151,242	512,697	342,422	141,850	190,014	1,626,499	915,767
Shareholders' Equity	2,598,546	(131,623)	369,012	1,632,987	2,099,959	2,560,928	3,489,291	(699,662)

- (1) Restated due to a change in accounting policy for patent. See note 4 to the financial statements.
- (2) Weighted average numbers of common share outstanding and earnings per share (EPS) are recalculated retroactively for all periods presented to reflect 10-to-1 share consolidation implemented by the Company on September 3, 2009.

OFF BALANCE SHEET ARRANGEMENTS

The Company does not have any off balance sheet arrangements requiring disclosure.

RELATED PARTY TRANSACTIONS

All related party transactions are recorded at the exchange amount established and agreed by the related parties. No related party transactions occurred in Q2 2010.

SUBSEQUENT EVENTS

Subsequent to the Annual and Special General Meeting on November 10, 2009, the Board of Directors appointed Dr. Liren Tang, former Director of Clinical Development as the Company's CEO and President, to replace Dr. Genhui Chen, who will be pursuing other business opportunities.

On December 11, 2009, the Company began to enroll patients in a Phase IIb clinical trial of its lead candidate, WBI-1001. The Phase IIb clinical trial is a double-blinded, placebo-controlled, 12-week-treatment study. The objectives of the trial are to evaluate the efficacy of the creams (0.5% and 1.0% WBI-1001) in comparison to the vehicle and also to evaluate the safety and tolerability of the creams in patients with atopic dermatitis. The study is being conducted at three centers across Canada. It is planned that 150 patients will be enrolled in the trial that is anticipated to be concluded in six to nine months.

OUTSTANDING SHARE DATA

As of January 23, 2010, the Company had the following outstanding securities at post-consolidation basis:

(1) Common shares issued:	42,336,299
(Shares in escrow:	none)
(2) Stock options:	585,960
(3) Warrants:	17,500,000

DISCLOSURE CONTROLS

The Company's Chief Financial Officer and Chief Executive Officer (the "Certifying Officers" are responsible for establishing and maintaining disclosure controls and procedures ("the procedures") which provide reasonable assurance that information required to be disclosed by the Company under provincial securities legislation (the "Required Filings") is reported within the time periods specified. Without limitation, the procedures are designed to ensure that material information relating to the Company is accumulated and communicated to management, including its Certifying Officers, as appropriate to allow for timely decisions regarding the Required Filings.

The Certifying Officers evaluate the effectiveness of the Company's procedures on a regular basis throughout the year and have concluded that the procedures in place as of the end of the period covered by the Required Filings are effective in providing reasonable assurance that material information relating to the Company is accumulated and communicated to management and reported within the time periods specified.

ADDITIONAL INFORMATION

Additional Information relating to the Company is available by accessing the SEDAR website at www.sedar.com.