

WELICHEM BIOTECH INC.
(a development stage enterprise)

INTERIM FINANCIAL STATEMENTS
(Unaudited – Prepared by Management)

AUGUST 31, 2009 and 2008

NOTE: These financial statements have not been reviewed or audited by the Company's auditor.

WELICHEM BIOTECH INC.
(a development stage company)
INTERIM BALANCE SHEETS (See Note 1 – BASIS OF PRESENTATION)
(Expressed in Canadian Dollar)
(Unaudited – Prepared by Management)

	August 31, 2009	May 31, 2009
ASSETS		
Current		
Cash and cash equivalents	\$ (34,827)	\$ 141,559
Short-term investments	(18)	619,335
Government grant receivables	-	46,434
Goods and services tax receivable	7,608	5,078
Prepaid expense	<u>12,514</u>	<u>33,499</u>
	(8,521)	845,905
Property and equipment [Note 8]	18,523	19,985
Deposit [Note 9]	<u>15,819</u>	<u>15,819</u>
Total Assets	\$ 19,620	\$ 881,709
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Accounts payable and accrued liabilities	\$ 151,242	\$ 512,697
Shareholder loan	<u>-</u>	<u>-</u>
	151,242	512,697
Shareholders' equity		
Share capital [Note 11]	11,209,286	11,209,286
Share subscriptions received in advance	-	-
Contributed surplus [Note 12]	2,917,993	2,904,605
Deficit	<u>(14,258,901)</u>	<u>(13,744,879)</u>
	<u>(131,623)</u>	<u>369,012</u>
Total Liabilities and Shareholders' Equity	\$ 19,620	\$ 881,709

Nature of operations [Note 2]
Commitments [Note 18]

On behalf of the Board:

“XIANGDONG TAN” Director “GUOQING LI” Director

The accompanying notes are an integral part of these financial statements.

WELICHEM BIOTECH INC.
(a development stage company)
INTERIM STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS AND DEFICIT
(Expressed in Canadian Dollar)
(Unaudited – Prepared by Management)
THREE-MONTH PERIOD ENDED AUGUST 31

	2009	2008 [Restated - see Note 4a]
RESEARCH AND DEVELOPMENT EXPENSES [Notes 4a,13, 15 & 16]	<u>\$ 362,980</u>	<u>\$ 295,758</u>
GENERAL AND ADMINISTRATIVE EXPENSES		
Amortization – Property and equipment	1,462	2,044
Consulting	-	2,710
Director’s fees	-	3,650
Insurance	9,900	10,552
Investor relations	259	1,036
Legal and accounting fees	16,073	25,091
Loan interest	-	4,233
Office and miscellaneous	1,962	7,427
Public Relations Expenses	-	-
Regulatory expenses	24,719	28,268
Rent	21,216	28,827
Telecommunications	2,084	1,814
Travel and related costs	15,343	8,253
Wages and benefits [Notes 13]	<u>43,343</u>	<u>37,472</u>
	<u>136,361</u>	<u>161,377</u>
Loss before other items	<u>(499,341)</u>	<u>(457,135)</u>
OTHER ITEMS		
Foreign exchange loss	(8,317)	(813)
Interest income (expenses)	<u>(6,364)</u>	<u>26,587</u>
	<u>(14,681)</u>	<u>25,774</u>
Loss and comprehensive loss for the year	<u>(514,022)</u>	<u>(431,362)</u>
Deficit, beginning of year, as previously presented	-	(10,769,217)
Cumulative impact of accounting change relating to patent costs [Note 4a]	-	<u>(273,708)</u>
Deficit, beginning of year, as restated	<u>(13,744,879)</u>	<u>(11,042,925)</u>
Deficit, end of year	<u>(14,258,901)</u>	<u>(11,474,287)</u>
Basic and diluted loss per common share [Note 21]	<u>\$ (0.03)</u>	<u>\$ (0.05)</u>
Weighted average number of common shares outstanding [Note 21]	16,815,751	9,336,299

The accompanying notes are an integral part of these financial statements.

WELICHEM BIOTECH INC.
(a development stage company)
INTERIM STATEMENTS OF CASH FLOWS
(Expressed in Canadian Dollar)
(Unaudited – Prepared by Management)
THREE-MONTH PERIOD ENDED AUGUST 31

	2009	2008 [Restated - see Note 4]
CASH FROM (USED IN) OPERATING ACTIVITIES		
Loss for the year	\$ (514,022)	\$ (431,362)
Add back:		
Government Grants	(50,066)	(31,160)
Amortization of property and equipment	1,462	2,044
Stock-based compensation [Note 13(b)]	13,388	-
Changes in non-cash working capital items:		
(Increase) Decrease in goods and services tax receivable	(2,531)	56,732
(Increase) Decrease in government grants receivable	46,434	-
(Increase) Decrease in prepaid expenses	20,985	(21,056)
Increase (Decrease) in accounts payable and accrued liabilities	<u>(361,455)</u>	<u>(438,486)</u>
Cash used in operating activities	<u>(845,805)</u>	<u>(863,288)</u>
CASH FROM (USED IN) INVESTING ACTIVITIES		
Purchase of property and equipment	-	-
(Increase) Decrease in deposits	-	-
(Increase) Decrease in short-term investments	<u>619,353</u>	<u>-</u>
Cash provided by (used in) investing activities	<u>619,353</u>	<u>-</u>
CASH FROM (USED IN) FINANCING ACTIVITIES		
Proceeds (Repayment) from (to) shareholder loan	-	(998,000)
Increase(Decrease) in capital, net of issuance costs	-	(497,000)
Share subscriptions received in advance (net of issuance costs)	-	-
Government assistance received	<u>50,066</u>	<u>31,160</u>
Cash provided by (used in) financing activities	<u>50,066</u>	<u>(1,463,840)</u>
Net increase (decrease) in cash during the year	(176,386)	(2,327,128)
Cash, beginning of year	<u>141,599</u>	<u>4,984,241</u>
Cash, end of year	(\$34,827)	\$ 2,657,113
Supplemental disclosure of cash flow information:		
Cash paid during the year for interest [Note 10]	\$ -	\$ 27,521
Cash paid during the year for income taxes	-	-

The accompanying notes are an integral part of these financial statements.

WELICHEM BIOTECH INC.
(a development stage company)
NOTES TO THE INTERIM FINANCIAL STATEMENTS
(Expressed in Canadian Dollar)
(Unaudited – Prepared by Management)
3-MONTH PERIOD ENDED AUGUST 31, 2009 and 2008

1. BASIS OF PRESENTATION AND GOING CONCERN

These unaudited interim financial statements of Welichem Biotech Inc. (the “Company” or “Welichem”) have been prepared in accordance with Canadian generally accepted accounting principles (“Canadian GAAP”) for interim financial statements on a going concern basis, which presumes that the company will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future. The interim financial statements and related notes do not include all the information required for annual financial statements and should be read in conjunction with the Company’s audited financial statements for the year ended May 31, 2009. The results of operations and comprehensive loss for the interim periods reported are not necessarily indicative of results for the full year.

The Company has incurred significant losses to date, and as at August 31, 2009, the Company has accumulated a deficit of \$14,258,901 resulting from losses in the current and prior years. As the Company is in the early stages of the research and development of its products, the Company’s ability to continue as a going concern is uncertain and is dependent on its ability to obtain sufficient financing and complete development and commercialization of its products and generate profit in the future. The Company announced \$3.75 million dollars in a private placement to finance expected operation in this quarter. There can be no assurance that the Company will be able to obtain sufficient financing to meet future operational need after twelve months. As a result, there is a significant doubt as to whether the Company will be able to continue as a going concern and realize its assets and pay its liabilities as they fall due.

These financial statements do not include any adjustments to the amounts and classifications of assets and liabilities which might be necessary should the Company be unable to continue operations in the normal course of business. Such adjustments could be material.

2. NATURE OF OPERATION

The Company is a biopharmaceutical company that focuses on the research and development and commercialization of new therapeutics for autoimmune / inflammatory diseases and cancer. The new therapeutics, derived from the metabolites of bacterial symbionts of soil living nematodes, target skin disorders such as psoriasis, eczema, cancers and chemotherapy induced neutropenia.

3. SIGNIFICANT ACCOUNTING POLICIES

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:

WELICHEM BIOTECH INC.
(a development stage company)
NOTES TO THE INTERIM FINANCIAL STATEMENTS
(Expressed in Canadian Dollar)
(Unaudited – Prepared by Management)
3-MONTH PERIOD ENDED AUGUST 31, 2009 and 2008

3. SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

Cash and cash equivalents

The Company considers unrestricted cash on hand and in banks, term deposits and guaranteed financial instruments with maturities from the date of purchase 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 and it is classified as held-for-trading.

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.

3. SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

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 August 31, 2009 and 2008, 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 inclusions of common share equivalents securities are anti-dilutive in the three-month period ended August 31, 2009 and 2008.

WELICHEM BIOTECH INC.
(a development stage company)
NOTES TO THE INTERIM FINANCIAL STATEMENTS
(Expressed in Canadian Dollar)
(Unaudited – Prepared by Management)
3-MONTH PERIOD ENDED AUGUST 31, 2009 and 2008

3. SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

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.

4. ADOPTION OF NEW ACCOUNTING POLICIES AND PRONOUNCEMENTS

[a] Early adoption of an accounting standard – 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 2008 and 2009 by \$289,940 and \$273,708 respectively, 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 \$310 previously added to patent rights and applications were expensed and amortization of patent rights and applications were reduced by \$10,483 for the three-month period ended August 31, 2008.

[b] Capital Disclosure

Effective June 1, 2008, the Company adopted the new recommendations of the CICA Handbook Section 1535, *“Capital Disclosure”*. This new accounting standard establishes the requirement for disclosing information about an entity’s capital and how it is managed. Section 1535 requires the disclosure of (i) an entity’s objectives, policies, and processes for managing capital; (ii) quantitative data about what the entity regards as capital; (iii) whether the entity has complied with any capital requirement; and if it has not complied, the consequences of such non-compliance. The disclosure required by the standard is provided in the Note 6 of the financial statements.

4. ADOPTION OF NEW ACCOUNTING POLICIES AND PRONOUNCEMENTS (CONT'D)

[c] Financial instruments

Effective June 1, 2008, the Company also adopted the new recommendations of the CICA Handbook Section 3862, “*Financial Instruments – Disclosure*”, and Section 3863, “*Financial Instruments – Presentation*”. Section 3862 requires entities to provide disclosures in their financial statements that enable users to evaluate the significance of financial instruments on the entity’s financial position and its performance and the nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the balance sheet date, and how the entity manages those risks. Section 3863 establishes standards for presentation of financial instruments and non-financial derivatives. It deals with the classification of financial instruments, from the perspective of the issuers, between liabilities and equities, the classification of related interest, dividends, losses and gains, and circumstances in which financial assets and financial liabilities are offset. The Company has included disclosures recommended by these new Handbook sections in Note 7 to the financial statements.

Section 3862 and Section 3863 relate to disclosure and presentation only and have no significant impact on our financial results for the three-month period ended August 31, 2009.

[d] General Standards of Financial Statement Presentation

Effective June 1, 2008, the Company adopted the new recommendation of the CICA Handbook Section 1400, “*General Standards of Financial Statement Presentation*”. The new accounting standard provides guidance related to management’s responsibility to assess and disclose the ability of an entity to continue as a going concern.

The disclosure required by this standard is provided in the Note 1 of the financial statements.

5. NEW ACCOUNTING PRONOUNCEMENTS

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.

WELICHEM BIOTECH INC.
(a development stage company)
NOTES TO THE INTERIM FINANCIAL STATEMENTS
(Expressed in Canadian Dollar)
(Unaudited – Prepared by Management)
3-MONTH PERIOD ENDED AUGUST 31, 2009 and 2008

5. NEW ACCOUNTING PRONOUNCEMENTS (CONT'D)

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.

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 continues to monitor and assess the impact of convergence of Canadian GAAP and IFRS.

6. CAPITAL DISCLOSURE

The Company manages its capital with the purpose of safeguarding its accumulated capital in order to maintain its ability to continue as a going concern and to advance its research, development and commercialization activities. The capital structure of the Company consists of shareholder’s equity.

The Company manages its capital structure and makes adjustments to it based on economic conditions and the risk characteristics of the underlying assets. The Company, upon approval from its board of directors, will balance its overall capital structure through new shares or debt issuances or by undertaking other activities as deemed appropriate under specific circumstances.

The Company expects that its current capital resources will support its research and development plans and operations into the end of fiscal year 2010. The Company’s overall strategy with respect to capital management remains unchanged from the prior year.

WELICHEM BIOTECH INC.
(a development stage company)
NOTES TO THE INTERIM FINANCIAL STATEMENTS
(Expressed in Canadian Dollar)
(Unaudited – Prepared by Management)
3-MONTH PERIOD ENDED AUGUST 31, 2009 and 2008

7. FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT

[a] Financial instruments

The Company has classified its financial instruments as following:

Financial Instrument	Classification	Measurement	August 31, 2009	May 31, 2009
Cash and cash equivalents	Held-for-trading	Fair value	\$ (34,827)	\$ 141,559
Short-term investments	Held-for-trading	Fair value	(18)	619,335
Government grant and goods and service tax receivables	Loans and receivables	Amortized cost using the effective interest method	7,608	51,512
Accounts payables, accrued liabilities and shareholder loan	Other financial liabilities	Amortized cost using the effective interest method	151,242	512,697

Section 3855 requires that the carrying values of Goods & Services tax receivable, government grant receivables, accounts payable and accrued liabilities, and shareholder loan be measured at the amortized costs using the effective interest method (“EIM”). The carrying amount of GST receivables, government grant receivables, accounts payables and accrued liabilities is a reasonable approximation of their fair value due to the short term nature of these instruments.

The Company did not have any held-to-maturity or available-for-sale financial instruments, nor did it acquire or hold any financial derivatives during the three-month period ended August 31, 2009.

[b] Financial risk management

The Company is exposed to certain financial risks, including credit risk, liquidity risk and market risk.

Credit Risk

Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its contractual obligations and arises principally from the Company’s cash and cash equivalents and other receivables. The Company invests its excess cash principally in highly rated Canadian government bonds and money market fund units to limit the credit risk. At the end of August 31, 2009, the Company sold all its short-term investments for funding operation activities.

WELICHEM BIOTECH INC.
(a development stage company)
NOTES TO THE INTERIM FINANCIAL STATEMENTS
(Expressed in Canadian Dollar)
(Unaudited – Prepared by Management)
3-MONTH PERIOD ENDED AUGUST 31, 2009 and 2008

7. FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANEGEMENT (CONT'D)

[b] Financial risk management (cont'd)

Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they come due. The Company's current capital resources will support its research and development plans and operations into the end of fiscal year 2010. The Company continues to seek additional funds through equity, debt or partnering transactions to lower the liquidity risk of the Company's financial instruments. The Company's annual operating and capital budgets as well as any material transactions outside the ordinary course of business are subject to the approval of the board of directors.

Market Risk

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

The Company does laboratory tests with several U.S. based entities and payments to such suppliers in US dollars. As a result, the Company is subject to fluctuation in exchange rates which can give rise to foreign currency exposure, either favorable or unfavorable. The Company does not engage in any foreign currency hedging activities.

The Company is subject to interest rate risk on its cash and cash equivalents and believes that the results of operations, financial position and cash flows would not be significantly affected by a sudden change in market interest rates relative to the investment interest rates due to the short term nature of the investments.

The Company sold all its short-term investment of government bond at August 31, 2009 and had no investments on other equity instruments of other corporations. Changes in the Company's equity price could impact its ability to raise additional capital.

As of August 31, 2009, the Company has financial instruments denominated in U.S. dollars and is exposed to market risk as following:

US Dollar	August 31, 2009	May 31, 2009
Cash	\$ 5,078	\$ 58,233
Accounts payable and accrued liabilities	-	(390,166)
	\$ 5,078	\$ (331,933)

The Company has completed a sensitivity analysis to estimate the impact on net income for the period which a change in foreign exchange rate during the three-month period ended August 31, 2009 would have had. The result of the sensitivity analysis shows that assuming all other variables remain constant, a 10% weakening or strengthening of the Canadian dollar against the US dollar would result in a decrease/increase of \$557 in the Company's deficit.

WELICHEM BIOTECH INC.
(a development stage company)
NOTES TO THE INTERIM FINANCIAL STATEMENTS
(Expressed in Canadian Dollar)
(Unaudited – Prepared by Management)
3-MONTH PERIOD ENDED AUGUST 31, 2009 and 2008

8. PROPERTY AND EQUIPMENT

	August 31, 2009			May 31, 2009		
	Cost	Accumulated Amortization	Net Book Value	Cost	Accumulated Amortization	Net Book Value
Lab equipment	\$ 67,948	\$ 62,937	\$ 5,011	\$ 67,948	\$ 62,542	\$ 5,406
Office equipment	<u>59,563</u>	<u>46,051</u>	<u>13,512</u>	<u>59,563</u>	<u>44,984</u>	<u>14,579</u>
	\$ 127,511	\$ 108,988	\$ 18,523	\$ 126,233	\$ 107,526	\$ 19,985

9. DEPOSIT

Deposit consists of a term deposit of \$15,819 (2009 - \$14,615) held as collateral for the Company's credit card.

10. SHAREHOLDER LOAN

On November 30, 2007, the Company established a loan facility with Canadian Maple Leaf Investment Ltd. (CMLI), a major shareholder of the Company, that committed to provide funding up to \$1,000,000 to the Company within a six-month period on “as and required” basis. The Company would pay CMLI interest at a rate of Canadian prime rate plus 2% per annum, calculated daily based on the daily closing balance and to be paid at maturity. On June 23, 2008, the Company fully repaid the lender the principal plus interests. Interest expense incurred in fiscal year of 2009 is \$4,233.

WELICHEM BIOTECH INC.
(a development stage company)
NOTES TO THE INTERIM FINANCIAL STATEMENTS
(Expressed in Canadian Dollar)
(Unaudited – Prepared by Management)
3-MONTH PERIOD ENDED AUGUST 31, 2009 and 2008

11. SHARE CAPITAL

	Pre-consolidation Number of Shares	Post-consolidation Number of Shares	Amount
Balance as at May 31, 2008	73,362,992	7,336,299	\$ 8,066,286
Common shares issued in the private placement closed in June 2008, net of share issuance costs (a)	<u>100,000,000</u>	<u>10,000,000</u>	<u>3,143,000</u>
Balance as at May 31, 2009	173,362,992	17,336,299	\$ 11,209,286
Balance as at August 31, 2009	173,362,992	17,336,299	\$ 11,209,286

- a) The Company commenced a private placement in 2008 to issue 100,000,000 units comprising common shares (pre-consolidation) at a price of \$0.05 per share and 50,000,000 warrants (pre-consolidation) exercisable at \$0.10 up to June 20, 2010 in gross proceeds of \$5,000,000 less issuing costs of \$497,000. The gross proceed was received in 2008 and the private placement was completed and shares and warrants were issued in 2009. [Note 13]

12. CONTRIBUTED SURPLUS

	Amount
Balance, May 31, 2008	\$1,465,930
Warrants issued in private placement in June 2008 [Note 15]	1,360,000
Stock-based compensation expense [Note 14(b)]	<u>78,675</u>
Balance, May 31, 2009	\$2,904,605
Stock-based compensation expense [Note 14(b)]	<u>13,388</u>
Balance, August 31, 2009	<u>\$2,917,993</u>

WELICHEM BIOTECH INC.
(a development stage company)
NOTES TO THE INTERIM FINANCIAL STATEMENTS
(Expressed in Canadian Dollar)
(Unaudited – Prepared by Management)
3-MONTH PERIOD ENDED AUGUST 31, 2009 and 2008

13. STOCK OPTIONS

[a] Stock options

On September 25, 2008, the Company granted 4,700,000 stock options (pre-consolidation) at an exercise price of \$0.10 for a period of 5 years expiring on September 24, 2013 with graded vesting schedule of 25% on the grant date and 25% in every 6 month after to its officers, directors, employees, and consultants.

As of August 31, 2009, outstanding and vested (exercisable) stock options which enable holders to acquire the following number of common shares:

Number of Outstanding Options (Pre-consolidation)	Number of Exercisable Options (Pre-consolidation)	Exercise Price	Expiry Date
38,100	38,100	0.22	December 31, 2009
60,000	60,000	0.22	March 15, 2010
166,500	166,500	0.22	May 25, 2010
50,000	50,000	0.23	May 25, 2010
50,000	50,000	0.23	June 1, 2010
0	0	0.10	January 31, 2011
865,000	865,000	0.10	May 7, 2011
0	0	0.15	July 30, 2011
560,000	560,000	0.10	August 31, 2011
0	0	0.20	January 30, 2012
500,000	500,000	0.135	January 31, 2012
<u>3,570,000</u>	<u>1,785,000</u>	0.10	September 25, 2013
5,859,600	4,074,600		

As of August 31, 2009, the weighted average remaining contractual life of the outstanding stock options is 3.17 years, and all the options are currently exercisable at an average price of \$0.19 (pre-consolidation).

The following table summarizes the stock option activity under this Plan:

	Pre-consolidation Number of Options	Weighted Average Exercise Price
Balance, May 31, 2008	5,984,600	0.13
Options granted	4,700,000	0.10
Options cancelled	<u>(1,970,000)</u>	0.15
Balance, May 31, 2009	8,714,600	\$ 0.11
Options granted		
Options cancelled	<u>(2,855,000)</u>	0.11
Options outstanding on August 31, 2009	5,859,600	\$ 0.18
Options exercisable on August 31, 2009	4,074,600	\$ 0.19

WELICHEM BIOTECH INC.
(a development stage company)
NOTES TO THE INTERIM FINANCIAL STATEMENTS
(Expressed in Canadian Dollar)
(Unaudited – Prepared by Management)
3-MONTH PERIOD ENDED AUGUST 31, 2009 and 2008

13. STOCK OPTIONS (CONT'D)

[b] Stock-based compensation

The Company has recorded stock-based compensation costs of \$13,388 for 2010 (Q1 2009 – \$nil). The offsetting amount is recorded as contributed surplus on the balance sheet [Note 13]. This expense has been allocated to general wages and benefits \$7,013 (Q1 2009 - \$nil), research and development wage expenses \$5,438 (Q1 2009 - \$nil) and research and development consulting expenses \$937 (Q1 2009 - \$nil) on the same base as cash compensation.

The fair value of all options granted has been estimated using the Black-Scholes Option Pricing Model with the following weighted average assumptions:

	<u>Sep 25, 2008</u>	<u>Aug 31, 2007</u>
Risk-free interest rate	3.12%	4.2%
Expected life of options	5 years	5 years
Annualized volatility	150%	107%
Dividend rate	Nil	Nil
Fair value per share	\$0.03	\$0.165

Option pricing models require the use of highly subjective estimates and assumptions including the expected stock price volatility. Changes in the underlying assumptions can materially affect the fair value estimates and, therefore, in management's opinion existing models do not necessarily provide reliable measure of the fair value of the Company's stock options.

14. WARRANTS

As of August 31, 2009, 50,000,000 warrants are outstanding. Each warrant entitles the holder to buy one common share at \$0.10 expiring on June 20, 2010.

	<u>Pre-consolidation</u>
Warrants outstanding as at May 31, 2008 and 2007	18,768,000
Warrants issued in connection with the private placement in June 2008	50,000,000
Warrants expired	<u>(18,768,000)</u>
Warrants outstanding as at May 31, 2009	50,000,000
Warrants outstanding as at August 31, 2009	<u>50,000,000</u>

On June 20, 2008, net proceeds (\$4,503,000) of the private placement were allocated between the common shares (\$3,143,000) and the warrants (\$1,360,000). The allocation was calculated by valuing the common shares and the warrants separately and adjusting the resulting amounts on a pro-rata basis so that the sum of the components is equal to the amount of cash received. The estimated fair value of warrants at \$1,360,000 was recorded as contributed surplus on the balance sheet [Note 13].

WELICHEM BIOTECH INC.
(a development stage company)
NOTES TO THE INTERIM FINANCIAL STATEMENTS
(Expressed in Canadian Dollar)
(Unaudited – Prepared by Management)
3-MONTH PERIOD ENDED AUGUST 31, 2009 and 2008

14. WARRANTS (CONT'D)

The assumptions used in the calculation of the fair value of the warrants (using the Black-Scholes Option Pricing Model) were:

Risk-free interest rate	3.524%
Expected life of warrants	2 years
Annualized volatility	208%
Dividend rate	\$Nil

15. RESEARCH AND DEVELOPMENT EXPENSES

	2009	2008
Subcontractors, supplies and materials	\$ 246,741	\$ 205,358
Patent costs	14,731	310
Wages and benefits [Note 13(b)]	<u>105,140</u>	<u>121,250</u>
	<u>\$ 366,612</u>	<u>\$ 326,918</u>
Less:		
Government assistance and other subsidies [Note 16]	<u>\$ (3,632)</u>	<u>\$ (31,160)</u>
	<u>\$ 362,980</u>	<u>\$ 295,758</u>

16. GOVERNMENT ASSISTANCE AND OTHER SUBSIDIES

Under an agreement through the Industrial Research Assistance Program ("IRAP"), the National Research Council of Canada ("NRC") agreed to reimburse certain of the Company's allowable direct expenditures on the evaluation of anti-cancer agents on a cost matching basis. The Company was awarded a financial contribution of up to \$460,693 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 Q1 2010 the Company received grants of \$50,066 out of which \$46,434 was accrued in year 2009.

WELICHEM BIOTECH INC.
(a development stage company)
NOTES TO THE INTERIM FINANCIAL STATEMENTS
(Expressed in Canadian Dollar)
(Unaudited – Prepared by Management)
3-MONTH PERIOD ENDED AUGUST 31, 2009 and 2008

17. SEGMENTED INFORMATION

The Company primarily operates in one reportable operating segment, being the research and development of pharmaceutical products, in Canada.

18. COMMITMENTS

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

2009/10	\$	61,223
2010/11		<u>27,907</u>
	\$	<u>89,130</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 \$781,739 to the CROs when all the work is completed.

19. RELATED PARTY TRANSACTIONS

All related party transactions are recorded at the exchange amount established and agreed by the related parties. There was no related party transaction occurred in 2010.

20. TECHNOLOGY TRANSFER AGREEMENTS

In September 2004, the Company entered into a Technology Transfer Agreement (the “Agreement”) with Celestial Pharmaceuticals (Shenzen) Ltd. (“CPL”), a company located in the People’s Republic of China (the “PRC”). Pursuant to the Agreement, the Company transferred and assigned its rights to certain of its proprietary technologies (“Transferred Technologies”) to CPL on a royalty-free basis to use, develop, improve and upgrade the Transferred Technologies, and to distribute, market and sell products derived or manufactured from the Transferred Technologies in the PRC, Hong Kong, Macau and Taiwan. CPL also subscribed 4,545,455 common shares of the Company for \$1,500,000.

In December 2005, Welichem licensed and assigned to CPL all its rights to develop, improve, upgrade, manufacture, distribute, and market, in and limited to Australia and Asia, of Welichem proprietary technology known as Novel Macrolide compounds with Antibiotic and Anti-neoplastic properties, in exchange for rights and licence granted to the Company with no additional cost for royalty-free use, development, improvement, upgrading, marketing and distribution worldwide of CPL’s proprietary cream formulation known as CPL-1001. In addition, the Company has access to Celestial’s research data on any drug compounds related to the Company’s patents.

WELICHEM BIOTECH INC.
(a development stage company)
NOTES TO THE INTERIM FINANCIAL STATEMENTS
(Expressed in Canadian Dollar)
(Unaudited – Prepared by Management)
3-MONTH PERIOD ENDED AUGUST 31, 2009 and 2008

21. SUBSEQUENT EVENTS

On September 3, 2009 the TSX Venture Exchange approved the Company to consolidate all of the issued and outstanding common shares on the basis of one post-consolidation common share for every ten pre-consolidation common share. Each option, warrant, or other securities of the Company convertible into pre-consolidation common shares that have not been exercised or cancelled prior to the implementation of the share consolidation are adjusted pursuant to the terms thereof on the basis of one post-consolidation common share for every ten pre-consolidation common shares (i.e. the number of common shares issuable decreases while the exercise price increases). The weighted average numbers of common share outstanding and loss per share are recalculated retroactively for all periods presented to reflect the change.

On July 8, 2009 the Company announced a private placement 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 7th, 2011 for gross proceeds of \$3,750,000 less issuing costs of \$375,000. The gross subscription money was received by the Company on September 15, 2009.