2004 Annual Report

Inex Pharmaceuticals Corporation

Contents

www.inexpharm.com

Corporate Profile

INEX is a Canadian biopharmaceutical company developing and commercializing proprietary drugs and drug delivery systems to improve the treatment of cancer.

INEX has a pipeline of product candidates under two technology platforms that are in various stages of development.

INEX has advanced its lead anticancer drug, Marqibo™, from research through development and it is the Company's primary focus.

INEX is in the process of planning a phase 3 clinical program for Marqibo. In January 2005 the US Food and Drug Administration declined INEX's application for accelerated approval of Marqibo. INEX is now focused on a path to standard approval.

Since 1996, INEX shares have been trading on the Toronto Stock Exchange under the symbol "IEX".

At December 31, 2004 INEX had a cash position of Cdn$30 million and 62 full-time employees.

Highlights

2004 Achievements

Lead product – Marqibo™

- Filed a New Drug Application (NDA) with the US Food and Drug Administration (FDA) seeking accelerated marketing approval for Marqibo as treatment for patients with relapsed non-Hodgkin's lymphoma (NHL). While the filing of the NDA is a significant achievement, on January 15, 2005, the FDA issued a non-approvable letter for Marqibo.
- Signed a strategic partnership with Enzon Pharmaceuticals, Inc. for the development and North American commercialization of Marqibo. On March 17, 2005, Enzon terminated the Marqibo partnership based on the FDA's "non-approvable" decision and Marqibo no longer being a strategic fit for their product pipeline.
- Filed New Drug Submission with Health Canada
- Promising Marqibo data presented at two prominent medical meetings:

American Society of Clinical Oncology

Positive follow-up data where Marqibo was used as part of a combination regimen in the first-line treatment of patients with NHL.

Pharmacokinetics trial in patients with metastatic melanoma.

American Society of Hematology

Additional analysis of Marqibo as a single agent treatment for NHL.

Follow-up data from first-line combination therapy NHL trial.

Initial data from a dose escalation trial evaluating Marqibo in combination with the anticancer drug dexamethasone for the treatment of patients with relapsed acute lymphoblastic leukemia (ALL).

Product Pipeline

- INX-0125 (sphingosomal vinorelbine)

Completed manufacture of the first clinical scale batch of INX-0125 in preparation for filing an Investigational New Drug (IND) application.

- INX-0076 (sphingosomal topotecan)

Initiated formulation studies for INX-0076 after re-acquiring worldwide rights to the product following GlaxoSmithKline's termination of their development agreement.

- INX-0167

Presented promising preclinical data from INX-0167, a product candidate in the targeted immunotherapy platform, showing promising anti-tumor activity when used in combination with monoclonal antibodies.

Corporate

- Added Timothy M. Ruane to the executive team as Senior VP Corporate Development

2005 Milestones

Lead product – Marqibo™

- Finalize Marqibo clinical development strategy for standard approval
- File Special Protocol Assessment with FDA
- Seek development and commercialization partners for Marqibo
- Continue ongoing phase 2 studies in first-line NHL and relapsed ALL

Product Pipeline

- INX-0125 (sphingosomal vinorelbine)

File an Investigational New Drug application to start phase 1 clinical trial.

- INX-0076 (sphingosomal topotecan)

Complete formulation studies to determine future development strategy.

- Targeted Immunotherapy

Evaluate various strategic options to create value from this promising early-stage technology.

Corporate

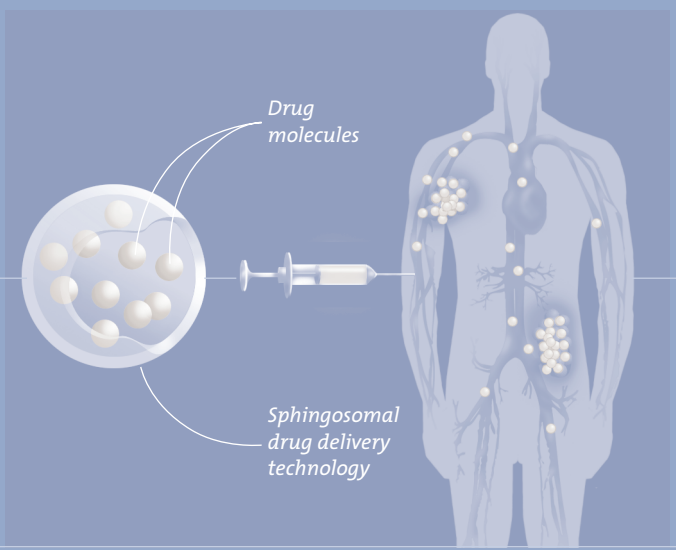
- Maintain burn rate of approximately $1 million per month
- Extract value from pipeline assets through business development initiatives

Product Pipeline

			Research	Preclinical	Phase 1	Phase 2	Phase 3
Targeted Chemotherapy Platform	Marqibo™	(sphingosomal vincristine)					●
	INX-0125	(sphingosomal vinorelbine)				●	
	INX-0076	(sphingosomal topotecan)				●	
Targeted Immunotherapy Platform	INX-0167	With monoclonal antibodies	●				
	INX-0204	Vaccine programs	●				

Targeted Chemotherapy Platform

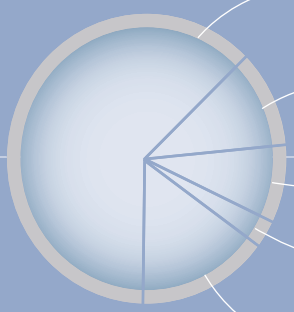
INEX's Targeted Chemotherapy



Drug molecules are encapsulated inside INEX's sphingosomal delivery technology to create a new proprietary drug.

The advantages of encapsulation include extended circulation of the drug in the bloodstream and accumulation at tumor sites. The encapsulated drug is then released from the sphingosomes over an extended period of time, which increases the drug's effectiveness.

Cancers Treated with Vincristine



62% | *Non-Hodgkin's lymphoma*

11% | *Acute lymphoblastic leukemia*

9% | *Multiple myeloma*

3% | *Hodgkin's disease*

15% | *Other*

In the US there are approximately 85,000 patients treated annually with vincristine.

Vincristine is the active ingredient in Marqibo. Clinical trials for Marqibo are currently underway for the treatment of non-Hodgkin's lymphoma and acute lymphoblastic leukemia.

Data source: Tandem Research Anticancer and Tumor Audit Oct 2000-Sept 2001.

President's Message

OVERVIEW

INEX is focused on designing a clinical program to obtain marketing approval for its lead product Marqibo™

Although INEX achieved a great deal in 2004, we unfortunately did not achieve our ultimate goal of a successful FDA review for accelerated approval of our lead anticancer product, Marqibo, as a treatment for relapsed aggressive non-Hodgkin's lymphoma (NHL).

On December 1, 2004 external advisors to the FDA, called the Oncologic Drugs Advisory Committee (ODAC), recommended against accelerated approval for Marqibo on the basis of data from our pivotal phase 2 clinical trial and comparison to available therapy. The FDA agreed with ODAC's recommendation and in January 2005 issued a "not approvable" letter.

Based on the ODAC decision, we took decisive action to restructure our workforce and resources to focus on Marqibo and set our course to obtain standard marketing approval. This restructuring lowers our burn rate for 2005 to approximately $1 million per month and provides us with financial resources to fund operations until approximately the end of 2006 at this burn rate.

In addition to Marqibo, we have budgeted to advance our product pipeline including filing an application to start a phase 1 clinical trial for INX-0125 (sphingosomal vinorelbine) and continuing preclinical work for INX-0076 (sphingosomal topotecan). We are also reviewing our development strategy for our Targeted Immunotherapy pipeline and evaluating various strategic initiatives for this highly promising early stage technology.

MARQIBO™

Marqibo consists of the off-patent anticancer drug vincristine encapsulated in INEX's proprietary sphingosomal drug delivery technology. The encapsulation provides extended circulation of the drug in the blood stream and promotes accumulation and extended drug release at cancer sites, which increases the effectiveness and reduces the side effects of the encapsulated anticancer drug. The commercial strategy is to target Marqibo at several types of cancer in which vincristine is now used.

Our numerous phase 2 clinical trials have confirmed that Marqibo is an active anticancer agent. In these trials, we have treated more than 500 patients with a variety of cancers including NHL, leukemia, Hodgkin's disease and some pediatric cancers, which provides a solid safety and efficacy database to build on. Our pivotal phase 2 trial of 119 patients demonstrated an overall response rate of 25% among NHL patients who had relapsed or had failed to respond after an average of four previous therapies. The response rate increased to 46% for patients who had failed to respond or had relapsed after only two previous therapies.

THE PATH AHEAD

When the FDA's official "not approvable" letter arrived in mid-January 2005, it was the beginning of our new path forward.

The FDA letter provided us with guidance on our next steps. In the clinical section, the FDA will require us to complete randomized controlled trials where we can compare Marqibo to other drugs used to treat specific types of cancer. It also encouraged a meeting with the FDA to discuss trial designs that would be suitable for re-applying for approval.

In addition to comments on the clinical section of the NDA, the FDA listed deficiencies in the chemistry, manufacturing and controls section that related primarily to the packaging, labeling and product specifications. We feel these deficiencies are easily addressed with minimal investment. There were no deficiencies mentioned for the nonclinical section of the NDA. Therefore, we believe we have a New Drug Application that is essentially two-thirds complete and our future investment will be to complete clinical trials necessary to re-apply for standard FDA approval.

Our current focus for trial designs are in NHL and acute lymphoblastic leukemia (ALL) as Marqibo has demonstrated promising activity in both these indications. After completing initial clinical trial designs with leading medical experts, we anticipate meetings with the FDA to obtain feedback that will enable us to complete a detailed clinical development plan. This plan will be the basis for submission of Special Protocol Assessments (SPAs), in which we will ask the FDA to endorse our trial designs as a basis for approval.

An SPA is an FDA process that allows for formal FDA agreement on trial design and endpoints. Based upon feedback from the FDA, we will determine the most viable path forward for Marqibo. We should be in a position to provide this guidance by mid-year.

The design of the Marqibo phase 3 clinical trials will also give us firm ground on which to seek new commercialization partnerships for Marqibo. Although Marqibo was no longer a strategic fit for our former North American marketing partner, Enzon Pharmaceuticals, we feel there are a number of companies for whom the phase 3 program and market opportunity for Marqibo would be a good fit.

Timothy Ruane, who joined our management team as Senior Vice-President, Corporate Development, in late December 2004, is managing our Marqibo partnering strategy and other business development initiatives. Mr. Ruane joined us from ILEX Oncology, Inc. where as Senior Vice-President, Business Management, he was responsible for all commercial operations of the company including marketing, sales and business development. ILEX was recently acquired by Genzyme Corporation in a transaction that closed on December 21, 2004. Mr. Ruane provides a new dimension to our leadership team and will make important contributions to our business strategy as we move forward.

PIPELINE INITIATIVES

While the primary focus at INEX is on Marqibo, our second product INX-0125 (sphingosomal vinorelbine) has demonstrated in preclinical studies that it has excellent potential as a cancer therapy. Accordingly, during the first half of 2005, we will be filing an Investigational New Drug application with regulatory authorities in the US and a Clinical Trial Agreement in Canada to begin evaluating INX-0125 in human clinical trials.

In addition, we are completing formulation studies for another product in our pipeline, INX-0076 (sphingosomal topotecan), prior to making a decision to proceed to clinical trials.

Marqibo, INX-0125 and INX-0076 are all based on INEX's Targeted Chemotherapy technology platform. For our second technology platform, Targeted Immunotherapy, we are considering various strategic initiatives to create value from this promising early stage technology.

We are also evaluating other options for the company as we continue to plan the path forward for Marqibo and our pipeline candidates.

In summary, we remain steadfast in our confidence that Marqibo warrants the resources we are investing in it. Key information on a viable plan going forward will be uncovered as we work with medical experts and the FDA.

The path ahead will be challenging but I am confident it will yield an important new treatment option for oncologists and their patients and build back significant value for shareholders.

On behalf of the Board of Directors and our executive team, I extend our appreciation to our shareholders for their support and to our employees who have risen to INEX's new challenges with enthusiasm and determination.

I look forward to updating you on our progress in the weeks and months ahead.

David J. Main
President and Chief Executive Officer
March 17, 2005

Management's Discussion and Analysis of Financial Condition and Operations

March 17, 2005 | *This discussion and analysis should be read in conjunction with our audited consolidated financial statements and related notes herein that are prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"). Additional information relating to Inex Pharmaceuticals Corporation ("INEX" or the "Company"), including our Annual Information Form is on the System for Electronic Document Analysis and Retrieval (SEDAR) at www.sedar.com.*

OVERVIEW

Our business strategy is to focus on the development and commercialization of proprietary drugs and drug delivery systems to improve the treatment of cancer by taking approved conventional chemotherapy drugs (Targeted Chemotherapy) or novel compounds (Targeted Immunotherapy) and using them in combination with our proprietary drug delivery technology.

Targeted Chemotherapy | Each of our Targeted Chemotherapy drug candidates consist of an already approved anticancer agent encapsulated in our proprietary sphingosomal drug delivery technology. The encapsulated agent is carried through the bloodstream and delivered to disease sites where it is released to carry out its therapeutic action. When used in free (unencapsulated) form, a chemotherapeutic drug circulates indiscriminately throughout the body, diluting the drug's effectiveness and causing toxic side effects in the patient's healthy tissues. Our proprietary sphingosomal drug delivery technology permits the loading of a high concentration of a therapeutic agent in a lipid envelope, promotes accumulation of the drug in tumors and prolongs the release of the drug at disease sites. As a result, compared to free form drugs, drugs encapsulated in our proprietary drug delivery technology have been shown in preclinical models to deliver more of the therapeutic agent to a targeted disease site over a longer period of time, thus increasing the efficacy of the drug while at the same time reducing toxicity in healthy, non-targeted tissues. Drugs designed to be used with our proprietary drug delivery technology may have a competitive advantage in the pharmaceutical marketplace because of these performance characteristics.

Our primary focus is on our lead Targeted Chemotherapy product, Marqibo™ (formerly known as Onco TCS), as this is our most advanced product candidate.

In addition to Marqibo, we are also developing two additional Targeted Chemotherapy products, INX-0125 and INX-0076. INX-0125 is the sphingosomal encapsulation of the chemotherapy drug vinorelbine. We are completing preclinical development of INX-0125 and expect to file an Investigational New Drug application in 2005 to begin a phase 1 clinical trial. Vinorelbine is used to treat breast and lung cancers.

INX-0076 is the sphingosomal encapsulation of the chemotherapy drug topotecan. INX-0076 was being developed in partnership with GlaxoSmithKline (GSK). However, in September 2004, GSK terminated the partnership due to technical problems encountered with the manufacturing of clinical trial materials. In 2005, our focus for INX-0076 is continued formulation development to determine the future development strategy for the drug.

Targeted Immunotherapy | Our second technology platform, Targeted Immunotherapy, induces the body's immune system to fight cancer and infectious disease by delivering drugs that stimulate an immune response directed at the appropriate target cells. This early-stage research platform has the potential to provide us with several different proprietary drugs for development.

INX-0204 (formerly OligoVax) and INX-0167 are our two early-stage product candidates under this platform.

As a result of our December 2004 restructuring, we are reviewing our strategy for the development of our Targeted Immunotherapy platform products, and are considering various strategic initiatives for this highly promising early-stage technology.

Current focus and business strategy | While we focus on moving Marqibo into phase 3 clinical trials, we will seek to generate long-term sustained growth by advancing a pipeline of new proprietary products. We intend to pursue the commercialization of our products through alliances with international pharmaceutical companies. A typical pharmaceutical alliance would bring up-front and milestone payments to us plus funding from the partner to cover all or a portion of on-going development costs as well as a share of revenues based on net product sales. Generally, we would expect to negotiate a higher share of revenues from such an alliance if the dedicated product is in late-stage clinical trials as compared with early-stage development. Depending on available cash resources, however, we may seek to partner our product candidates at an earlier stage of development. Where reasonable commercial terms can be secured, we may license our delivery technology to another company for combination and development with the partner's therapeutic compound.

Recent significant events | The following are recent significant events related to our lead product, Marqibo:

- In January 2004, we entered into a partnership with Enzon Pharmaceuticals, Inc. ("Enzon") for North American commercialization rights for Marqibo
- In March 2004 we submitted our New Drug Application (NDA) seeking accelerated marketing approval for Marqibo as a treatment for patients with relapsed aggressive non-Hodgkin's Lymphoma (NHL), to the US Food and Drug Administration (FDA). In May 2004, the FDA accepted our NDA for review
- In November 2004 we filed a New Drug Submission (NDS) for Marqibo with the Therapeutics Products Directorate (TPD) of Health Canada
- On December 1, 2004, the FDA's Oncologic Drugs Advisory Committee (ODAC) voted against supporting accelerated approval for Marqibo as a treatment for relapsed aggressive NHL on the basis of data from our pivotal phase 2 clinical trial. Since it was evident after the vote by the ODAC that the FDA would not grant accelerated approval to Marqibo, we announced December 14, 2004 that we were restructuring and reducing costs to extend our financial resources to allow the continued development of Marqibo
- In mid-January 2005, we received the FDA's official decision rejecting accelerated approval for Marqibo on the basis of the pivotal phase 2 clinical trial data
- On March 17, 2005, we announced that we had reached an agreement with Enzon to terminate the development and commercialization partnership agreement for Marqibo effective immediately

The following are recent significant events related to our product pipeline and other matters:

- In July 2004, we presented preclinical data from INX-0167, a new product in our Targeted Immunotherapy platform, showing promising anti-tumor activity when used in combination with monoclonal antibodies
- In September 2004, we reported the termination of a partnership with GlaxoSmithKline (GSK) of one of our early-stage pipeline drugs, INX-0076. GSK had experienced technical manufacturing problems
- In December 2004, Timothy Ruane joined our management team as senior vice-president, business development
- During the year we completed the manufacture of our first clinical scale batch of INX-0125
- In the first half of 2005, we expect to file an Investigational New Drug application (IND) with the FDA and a Clinical Trial Agreement with Health Canada seeking approval to commence human clinical trials for INX-0125

ODAC votes against accelerated approval for Marqibo | On September 27, 2004, we announced that the FDA's Oncologic Drugs Advisory Committee (ODAC) would review Marqibo at its scheduled meeting December 1, 2004. On December 1, 2004, the ODAC voted against supporting accelerated approval for Marqibo as a treatment for relapsed aggressive non-Hodgkin's lymphoma (NHL) on the basis of data from our pivotal phase 2 clinical trial and comparison to available therapy.

Since it was evident after the vote by the ODAC that the FDA would not grant accelerated approval to Marqibo, we announced December 14, 2004 that we were restructuring and reducing costs to extend our financial resources to allow the continued development of Marqibo, including the design and launch of phase 3 clinical trials that would, if positive, support regular approval from the FDA. We reduced our workforce from 165 to 62 employees and reduced expenditures to approximately $1 million per month for 2005. Subsequently, the FDA's official decision was received in mid-January 2005 rejecting accelerated approval for Marqibo.

The pivotal phase 2 trial and numerous other phase 2 trials have confirmed that Marqibo is an active anticancer agent that warrants continued development. Therefore, the design and preparation for phase 3 clinical trials to seek standard approval from the FDA and other regulatory agencies is our main focus in 2005.

Until the FDA's decision, our clinical and regulatory strategy for Marqibo had been to seek accelerated approval with the data from the pivotal phase 2 trial in the relapsed aggressive NHL patient population and at the same time generate clinical data in other settings where free (unencapsulated) vincristine has historically been used.

Enzon partnership and termination | On January 19, 2004 we entered into a strategic partnership with Enzon to develop and commercialize Marqibo. Under the terms of this agreement, Enzon received the exclusive North American commercialization rights for Marqibo for all indications. In exchange, we received a non-refundable US$12.0 million up-front payment. We retained all commercialization rights for Marqibo outside of North America.

Enzon and INEX had shared equally the development costs incurred in seeking marketing approvals in North America for Marqibo.

On March 16, 2005 we reached an agreement with Enzon to terminate our strategic partnership effective immediately. Following the December 1, 2004 Oncologic Drugs Advisory Committee vote to not support accelerated approval for Marqibo resulting in a delay in the commercialization of Marqibo, Enzon advised us that Marqibo was no longer a strategic fit for their pipeline. Up to December 31, 2004, Enzon had contributed $6.1 million (US$4.8 million) as their share of Marqibo development costs. In addition, as part of the termination, we expect to receive Enzon's estimated share of future development expenses and certain milestone payments totaling US$5.0 million. See the "Subsequent events" note in the accompanying financial statements for additional details.

As a result of the strategic partnership entered into with Enzon, in February 2004 we made a US$3.0 million cash milestone payment to Elan under the terms of the agreement entered into in April 2003. The FDA's acceptance of our Marqibo NDA in May 2004 triggered a second payment to Elan of US$2.5 million. A third and final milestone payment of US$2.5 million is contingent upon the successful completion of regulatory approval for Marqibo and can be settled, at our option, with cash or common shares of the Company. After the final payment is made, we will have no further milestone or royalty obligations to Elan.

Marqibo new trial designs | Subsequent to the FDA's January 2005 decision, we are now evaluating phase 3 trial designs for Marqibo. If results from these trials are positive, it would form the basis for the filing of a new NDA for standard approval for Marqibo.

Our current focus for trial designs are in NHL and acute lymphoblastic leukemia (ALL) as Marqibo has demonstrated promising activity in both these indications. After completing initial clinical trial designs and consulting with medical experts, we anticipate holding meetings with the FDA to obtain feedback that will enable us to complete a detailed clinical development plan. This plan will be the basis for submission of Special Protocol Assessments (SPAs), in which we will ask the FDA to endorse our trial designs as a basis for approval.

The SPA is a FDA process that allows for formal FDA agreement on trial design and endpoints. Based upon feedback from the FDA, we will determine the most viable path forward for Marqibo.

The discussions with medical experts and the FDA will provide us with a strong basis on which to negotiate commercialization partnerships for Marqibo. We anticipate beginning partnership discussions in 2005.

Marqibo additional clinical trial results | During 2004, we continued to collect follow-up data on patients enrolled in a phase 2 trial, originally initiated in the first quarter of 2001, in which Marqibo was substituted for vincristine in standard combination therapy as a first-line treatment for patients with aggressive NHL. The current standard first-line treatment for the aggressive form of NHL is the four-drug "CHOP" chemotherapy combination, comprising the drugs cyclophosphamide, doxorubicin hydrochloride, vincristine and prednisone. Patients diagnosed with B-cell lymphoma received the Marqibo formulation of CHOP along with the monoclonal antibody drug, Rituxan® (rituximab).

Interim results from this trial have been presented in December 2002, June 2004 and December 2004. The most recent December 2004 results were presented at the Annual Meeting of the American Society of Hematology (ASH) in San Diego, California. Results were presented from 68 evaluable patients. Sixty-three patients, or 93%, responded to the therapy. Sixty-two patients had their tumors completely eliminated for a complete response rate of 91.2% and one patient's tumor volume decreased by more than 50% for a partial response rate of 1.5%.

Investigators also presented positive patient survival data. At a median follow-up of 30 months, median progression-free survival and median overall survival had not yet been reached. Overall survival was 96% (three deaths) and progression-free survival was 82% (twelve relapses).

Also at ASH, we presented interim data from a clinical trial that demonstrated Marqibo's activity against tumors in patients with relapsed acute lymphoblastic leukemia (ALL).

Interim results were presented from a phase 1/2 dose escalating clinical trial in which Marqibo, in combination with the anticancer agent dexamethasone, was evaluated in fourteen patients with relapsed or refractory ALL. Four of the fourteen patients (29%) achieved complete responses when treated with Marqibo and dexamethasone, while two other patients showed hematologic improvement. All of the patients tolerated the treatment well considering the high doses of Marqibo administered on a weekly basis. Three of the four responding patients went on to receive stem cell transplants. The trial is continuing to enroll and treat patients.

INX-0125 (sphingosomal vinorelbine) | In April 2003, we announced that we had selected INX-0125 as the next product to be developed in our Targeted Chemotherapy pipeline based on promising preclinical efficacy data. Vinorelbine, an approved chemotherapeutic drug that is off-patent in the US, is a member of the vinca alkaloids class of drugs that also includes vincristine (the active drug in Marqibo) and vinblastine. Vinorelbine has been shown to have activity in cancers other than those treated by vincristine and has the potential to be made more effective and less toxic when encapsulated in our drug delivery technology. INX-0125 demonstrated increased tumor inhibition in three preclinical human xenograft tumor models (colon, breast and prostate) relative to doses of unencapsulated vinorelbine that resulted in equivalent levels of toxicity. Vinorelbine is used to treat breast and lung cancers.

In 2004, toxicology studies were completed for INX-0125 in preparation for filing an Investigational New Drug (IND) application. In the first half of 2005, we expect to file an IND with the FDA and a Clinical Trial Agreement with Health Canada seeking approval to commence human clinical trials for INX-0125.

INX-0076 (sphingosomal topotecan) | Camptothecins are a class of compounds used in a number of chemotherapy treatments and topotecan is a drug in the camptothecin class. In preclinical studies, we demonstrated that our sphingosomal drug delivery technology can protect camptothecin drugs from degradation in the bloodstream and can preferentially accumulate at tumor sites, thus increasing efficacy and reducing dosing requirements compared to the free drug. On November 20, 2001, we announced that we had entered into a development and license agreement with GSK under which we granted a worldwide license of our proprietary delivery technology to GSK for use with camptothecins and its analogs. The first drug to be developed under the agreement was the combination of our drug delivery technology and the GSK camptothecin compound topotecan hydrochloride, currently marketed by GSK as Hycamtin®.

In April 2003, GSK filed an IND application with the FDA asking for approval to begin human clinical trials evaluating INX-0076. Due to a number of technical problems experienced by GSK in manufacturing the necessary supply of materials needed for clinical trials, GSK saw a delay in the commencement of the planned clinical trials and subsequently terminated the agreement in September 2004. We are now completing formulation development for INX-0076 that will address manufacturing issues and we will determine further development options for INX-0076 in 2005.

INX-0167 | INX-0167 is a new product from our Targeted Immunotherapy platform that has demonstrated in preclinical studies the capacity to stimulate the immune system and significantly enhance the anti-tumor activity of monoclonal antibodies. We presented data from these studies on July 18, 2004 in Montreal at the 12th International Congress of Immunology and the 4th Annual Conference of the Federation of Clinical Immunological Societies. The data demonstrated that treatment with the monoclonal antibody rituximab (Rituxan®) alone prolonged median survival by 25% over control, and INX-0167 alone was able to prolong survival by 110% over control. However, combining rituximab and INX-0167 produced a synergistic response prolonging median survival by over 500% over control.

INX-0167 presents a significant opportunity given the increasing use of monoclonal antibodies to treat cancer. Monoclonal antibodies currently represent a multi-billion dollar opportunity in the cancer treatment market. As a result of our December 2004 restructuring, we are reviewing our development strategy for our Targeted Immunotherapy platform products including both INX-0167 and INX-0204 (OligoVax), and are considering various strategic initiatives for this highly promising early-stage technology.

New Senior Vice-President, Corporate Development | In December 2004, Timothy Ruane joined our management team as senior vice-president, business development. Mr. Ruane joined us from ILEX Oncology, Inc. ("ILEX") where as senior vice-president, business management he was responsible for all commercial operations of the company including marketing, sales and business development. ILEX was recently acquired by Genzyme Corporation in a transaction that closed on December 21, 2004. Mr. Ruane provides a new dimension to our leadership team and will make important contributions to our business strategy as we move forward.

Development stage company | INEX commenced operations in July 1992 and has devoted its resources primarily to fund its research and development programs. We have been unprofitable since inception and have not received any revenues other than from research and development collaborations, license fees and milestone payments. We had a cumulative deficit of $212.9 million at December 31, 2004. No material net income is expected for the foreseeable future as we continue to invest in product research and development, preclinical studies, clinical trials and regulatory compliance. We will require substantial additional funds to carry out our business strategy and there can be no assurance that we will be able to raise these funds. See Risks and uncertainties.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The significant accounting policies that we believe to be most critical in fully understanding and evaluating our financial results are stock-based compensation, revenue recognition and valuation and amortization of medical technology. These accounting policies require us to make certain estimates and assumptions. We believe that the estimates and assumptions upon which we rely are reasonable based upon information available to us at the time that these estimates and assumptions are made. Actual results may differ from our estimates. Areas where critical accounting estimates are made include revenue recognition, the valuation and amortization of medical technology and amounts recorded as stock-based compensation. Our critical accounting estimates affect our net loss calculation and the balance sheet value of our medical technology.

Revenue recognition | Our primary sources of revenue have been derived from research and development collaborations services, and licensing fees comprised of initial fees and milestone payments. Payments received under collaborative research and development agreements, which are non-refundable, are recorded as revenue as services are performed and as the related expenditures are incurred pursuant to the agreement and provided collectability is reasonably assured. Initial fees and milestone payments which require our ongoing involvement are deferred and amortized into income over the estimated period of our ongoing involvement as we fulfill our obligations related to the various elements within the licensing and development agreements. Any upfront license payments received under an agreement whereby we also provide research and development services are recognized as revenue over the term of the research and development period.

Our revenue recognition policy is in accordance with the guidelines provided in Emerging Issues Committee (EIC) -141, *Revenue Recognition, Non-Refundable Fees* and EIC-142, *Revenue Arrangements with Multiple Deliverables*. These consensuses are consistent with the US generally accepted accounting principles outlined in SAB-104, *Revenue Recognition* and the Emerging Issues Task Force (EITF) consensus regarding EITF Issue 00-21.

The revenue that we recognize is a critical accounting estimate because of the volume and nature of the revenues we receive. The research and development collaboration and licensing agreements that we have entered into contain multiple revenue elements that are to be recognized for accounting in accordance with our revenue recognition policy. We need to make estimates as to what period the services will be delivered with respect to up-front licensing fees and milestone payments received because these payments are deferred and amortized into income over the estimated period of our ongoing involvement. The actual period of our ongoing involvement may differ from the estimated period determined at the time the payment is initially received and recorded as deferred revenue. This may result in a different amount of revenue that should have been recorded in the period and a longer or shorter period that the revenue should be deferred and amortized into. Our revenue for the year ended December 31, 2004 was $14.6 million and deferred revenue at December 31, 2004 was $11.2 million. In light of the termination of the development and commercialization agreement with Enzon announced on March 17, 2005, we will be reviewing the recognition of any deferred review related to this agreement in the first quarter of 2005.

Valuation and amortization of medical technology | Our intangible assets are comprised of purchased or licensed medical technology. At December 31, 2004, our Elan medical technology (net book value of $8.6 million) represented almost all of the balance sheet value of our medical technology.

The costs of our medical technology are amortized on a straight-line basis over the estimated useful life of the technology ranging from nine to 12 years. Factors considered in estimating the useful life of medical technology include:

- our expected use of the asset
- legal, regulatory and contractual provisions that may limit the useful life
- the effects of obsolescence, demand, competition and other economic factors
- the level of maintenance expenditures required to obtain the expected future cash flows from the medical technology

We review the carrying value of our medical technology on an annual basis and if we determine that successful development of products to which medical technology costs relate is not reasonably certain, or that deferred medical technology costs exceed the recoverable value based on future potential undiscounted cash flows, such excess costs are charged to operations. The costs incurred to establish and maintain patents for intellectual property developed internally are expensed in the period incurred.

The valuation of medical technology is a critical accounting estimate because of the long-term nature of and risks and uncertainties related to the development of our medical technology. Significant judgment is exercised and assumptions are made when determining whether the carrying value of the medical technology may or may not be recoverable based on future potential undiscounted cashflows. Any significant changes to our assessment could possibly result in an impairment loss of our medical technology. During our recent review of the oligonucleotide therapeutic technology licenses purchased from Lynx Therapeutics, Inc. in March 1998, it became apparent that although certain of our oligonucleotide technology continues to be useful in our Targeted Immunotherapy platform technology, this application relies on the immune stimulating properties of such molecules and is no longer based on an antisense mechanism. The Lynx medical technology relates to the use of oligonucleotides for antisense applications and is therefore of no future value to us. As a result an impairment loss of $3.4 million, the net book value of the Lynx medical technology as at September 30, 2004, has been included in amortization expense in the year ended December 31, 2004.

Due to the long-term nature and risks and uncertainties related to the development of our product candidates, the actual useful life of our medical technology may differ from our initial estimate of the useful life that the medical technology is amortized over. We licensed the Elan medical technology from Elan Corporation, plc ("Elan") relating to Marqibo in April 2001 for a cost of $18.4 million (US$12.0 million) and the useful life was estimated then to be three years ending in the second quarter of 2004. Based on events early in 2004, such as the completion of our phase 2 pivotal trial evaluating Marqibo, the filing of a NDA seeking marketing approval for Marqibo and the signing of the commercialization agreement with Enzon Pharmaceuticals, Inc. ("Enzon"), management has, effective on January 1, 2004, revised the estimated useful life of the Elan medical technology to approximate the average remaining legal and economic life of the key patents in North America of approximately 10 years. Accordingly, the remaining net book value of the Elan medical technology of $2.1 million on January 1, 2004 and any subsequent additions to this technology are being amortized over the period ending in the fourth quarter of 2013. Total additions to Elan medical technology in 2004, based on milestone payments made to Elan to maintain a license to some of their intellectual property, were $7.3 million (US$5.5 million).

In light of the FDA's decision not to grant accelerated approval for Marqibo and Enzon's termination of our partnership with them, we reviewed the net book value of the Elan medical technology. Based on future potential undiscounted cash flows for Marqibo, we believe that the net book value of the Elan medical technology is not impaired.

The amortization expense recorded on medical technology in 2004, including the impairment loss on the Lynx medical technology, was $4.9 million.

Stock-based compensation | We adopted the fair value method of accounting for all employee and non-employee stock-based compensation in the fourth quarter of 2003 pursuant to the amended recommendations of the Canadian Institute of Chartered Accountants (CICA) Handbook Section 3870 *Stock-based Compensation and Other Stock-based Payments*. The stock based compensation that we record is a critical accounting estimate because of the value of compensation recorded, the volume of our stock option activity, and the many assumptions that are required to be made to calculate the compensation expense. The amended recommendations of CICA Handbook Section 3870 provide that a company may apply the rules on a prospective basis or a retroactive basis and that a company may choose to voluntarily adopt the amended recommendations in 2003 rather than on the required adoption date of January 1, 2004.

We applied this change in accounting on a retroactive basis, with restatement of prior periods, to all awards granted since the establishment of our Incentive Stock Option Plan in 1993 and Share Incentive Plan in 1996. We chose this alternative because we feel that this gives the reader of the financial statements the greatest comparability to prior periods and to future periods when stock based compensation expense is required to be recorded in our financial statements. We also chose this alternative to be consistent with the stock based compensation accounting requirements in other jurisdictions.

Compensation expense is recorded for stock options issued to employees and non-employees using the fair value method. We must calculate the fair value of stock options issued and amortize the fair value to stock compensation expense over the vesting period, and adjust the amortization for stock option forfeitures and cancellations. We use the Black-Scholes model to calculate the fair value of stock options issued which requires that certain assumptions including the expected life of the option and expected volatility of the stock be estimated at the time that the options are issued. We amortize the fair value using the accelerated method over the vesting period of the options, generally a period of four years. This accounting estimate is reasonably likely to change from period to period as further stock options are issued and adjustments are made for stock option forfeitures and cancellations.

The Black-Scholes model is not the only permitted model to calculate the fair value of stock options issued pursuant to Handbook Section 3870. A different model, such as the binomial model, as well as any changes to the assumptions made may result in a different stock compensation expense calculation. We recorded stock compensation expense in 2004 of $0.8 million. This included a $1.2 million credit for the cancellation of severed employees unvested options (see Restructuring costs).

CHANGES IN ACCOUNTING POLICIES

We adopted the CICA's approved amendment to Handbook Section 3860, *Financial Instruments – Disclosure and Presentation*, during the fourth quarter of 2004. The amendment requires obligations that may be settled, at the issuer's option, by a variable number of the issuer's own equity instruments to be presented as liabilities. The amendment becomes effective for fiscal years beginning on or after November 1, 2004 but as encouraged by the CICA we chose to adopt the amendment in the fourth quarter of 2004. As required under Handbook Section 3860, this change in accounting has been applied to our exchangeable and development notes (the "Notes") on a retroactive basis with restatement and has impacted the financial statements as follows:

- The fair values of the options to convert the Notes to equity, in the aggregate amount of $5.9 million and calculated using the Black-Scholes option pricing model, are considered a discount on the Notes, with a corresponding credit to additional paid-in capital. The debt discount for each draw on the Notes is being amortized, based on an effective yield basis, over the term of that draw. The amortization of the debt discount is included in interest expense in the loss for the period
- The remaining amount of the Notes' fair value is now presented on our consolidated balance sheet as debt, whereas they were originally reported as equity
- Interest expense on the Notes is now presented as an expense in the consolidated statements of operations whereas it was previously recorded directly to the Company's deficit account and presented in the consolidated statements of shareholders' equity
- The Notes are payable in US dollars and together with accrued interest are translated to Canadian dollars on each reporting date. Any change in the US/Canadian currency exchange rate gives rise to a foreign currency translation gain or loss to be included in other income (losses) for the period

In respect of the Notes, we recorded an unrealized foreign exchange gain in other income of $3.1 million in 2004 and $8.4 million in 2003. Amortization of debt discount of $1.1 million was included in interest on exchangeable and development notes in both the year ended December 31, 2004 and the year ended December 31, 2003.

Expected changes in accounting policies | The recommendations of the new Accounting Guideline 15, *Consolidation of Variable Interest Entities*, became effective for interim or fiscal periods beginning on or after November 1, 2004 and will be adopted in 2005.

SELECTED FINANCIAL INFORMATION

The following is selected financial information for our 2004, 2003 and 2002 fiscal years:

(in millions of Cdn$ except per share data)	2004	2003 restated [1]	2002 restated [1]
Total revenues	**$ 14.6**	$ 3.5	$ 8.0
Research and development expenses	**26.8**	30.7	36.3
General and administrative expenses	**9.3**	8.8	9.4
Restructuring costs	**5.1**	–	–
Amortization	**6.6**	8.9	8.9
Total loss	**(33.7)**	(39.7)	(48.6)
Loss per share [2]	**(0.88)**	(1.11)	(1.48)
Total assets	**49.4**	65.8	83.8
Total long-term liabilities	**38.7**	37.8	41.5
Deficit	**(212.9)**	(179.2)	(139.5)
Total shareholders' (deficiency) equity	**(12.6)**	19.5	30.2

[1] The above selected financial information has been restated for 2003 and 2002 to reflect our adoption of the CICA's approved amendment to Handbook Section 3860, *Financial Instruments – Disclosure and Presentation*, as discussed in detail in Changes in accounting policies.

[2] Diluted loss per share has not been presented for since our stock options and exchangeable and development notes are antidilutive.

The factors that have caused period to period variations in our revenues, expenses and loss per year between 2004 and 2003 are explained in detail in Results of operations. The most significant factor causing the period to period variations between 2003 and 2002 was a decline in spending on the pivotal phase 2 trial for Marqibo and other preclinical pharmacokinetic and toxicology studies. The decrease in total revenues in 2003 was primarily due to the loss of research and development collaboration revenue as a result of Elan's announcement in June 2002 to focus its development efforts outside of oncology, which ultimately led to us entering into a Termination Agreement with Elan in April 2003.

SUMMARY OF QUARTERLY RESULTS

The following table presents our unaudited consolidated quarterly results of operations for each of our last eight quarters. This data has been derived from our unaudited consolidated financial statements, which were prepared on the same basis as our annual audited consolidated financial statements and, in our opinion, include all adjustments necessary, consisting solely of normal recurring adjustments, for the fair presentation of such information.

(in millions of Cdn$ except per share data)

	Mar 31 2003	June 30 2003	Sept 30 2003	Dec 31 2003	Mar 31 2004	June 30 2004	Sept 30 2004	Dec 31 2004
Revenue	$ 2.4	$ 0.1	$ 0.8	$ 0.2	$ 3.7	$ 3.3	$ 3.3	$ 4.3
Net loss [1]	(7.7)	(8.9)	(11.4)	(11.7)	(6.5)	(7.3)	(5.2)	(14.7)
Loss per share [1, 2]	(0.23)	(0.27)	(0.31)	(0.30)	(0.17)	(0.19)	(0.14)	(0.38)

[1] Other than the fourth quarter of 2004, the above quarterly information has been restated to reflect our adoption of the CICA's approved amendment to Handbook Section 3860, *Financial Instruments – Disclosure and Presentation*, as discussed in detail in Changes in accounting policies.

[2] Diluted loss per share has not been presented since our stock options and exchangeable and development notes are antidilutive.

Quarterly trends | A discussion of revenue increases in 2004 over 2003 can be found in Results of operations.

Fourth quarter | The increase in net loss in the fourth quarter over the third quarter of 2004 is largely due to the payment of year-end employee bonuses of approximately $0.6 million, the recording of restructuring costs of $5.1 million and an impairment loss of $3.4 million on the Lynx medical technology which are discussed in detail in Results of operations.

RESULTS OF OPERATIONS

For the fiscal year ended December 31, 2004, our net loss was $33.7 million ($0.88 per common share). For the fiscal year ended December 31, 2003, our restated net loss was $39.7 million ($1.11 per common share). The net loss in 2004 differed from our expectations due to the impact of our change in accounting policy for our exchangeable and development notes of $1.2 million, the recording of $5.1 million in restructuring costs and recording a $3.4 million impairment loss on our Lynx medical technology.

Revenue | Revenue from research and development collaborations, licensing fees and milestone payments was $14.6 million for 2004 as compared to $3.5 million for 2003.

Revenue from research and development collaborations was $6.1 million in 2004 as compared to nil in 2003. This was a result of revenue recorded from Enzon in relation to ongoing development expenses pursuant to a strategic partnership agreement to jointly develop and commercialize Marqibo. See the "Collaborative Agreements" note in the accompanying financial statements for details on the strategic partnership agreement signed with Enzon on January 19, 2004.

Licensing fees and milestone revenue is shown in the following table:

(in millions of Cdn$)		2004		2003
Enzon revenue [1]				
Amortization of up-front payment	**$**	**4.7**	$	–
Accrual of anniversary payment		**2.0**		–
GSK revenue [2]				
Amortization of initial license fee		**0.5**		0.5
Milestone payments		**1.3**		3.0
Total	**$**	**8.5**	$	3.5

[1] Amortization of the up-front US$12.0 million payment received from Enzon at the start of our strategic partnership in January 2004 and accrual of the earned portion of a US$1.75 million anniversary payment due from Enzon on January 19, 2005.

[2] The GSK revenue was earned pursuant to an agreement to develop GSK's anticancer drug, topotecan hydrochloride, with our proprietary sphingosomal drug delivery technology. However, GSK had experienced a number of technical problems in manufacturing the necessary supply of materials needed for clinical trials, and these problems delayed the program. As a result of the termination by GSK of the agreement on September 1, 2004, we will not be receiving any further payments under this agreement and all revenue received and deferred under the agreement has now been amortized into income.

We expect that the principal sources of revenue for the next several years will be interest income and payments under future licensing and collaborative research and development agreements. Such payments may be conditional upon us achieving certain milestones under such agreements. If the research and development work related to the payments received from such agreements were to cease or the expected research and development terms were revised to become shorter in future periods, we could recognize the related revenue in earlier periods than expected. Conversely, if the expected research and development terms were revised to become longer in future periods, we could recognize the related revenues in later periods than currently estimated. See Risks and uncertainties.

On March 17, 2005 we announced an agreement with Enzon to terminate our strategic partnership effective immediately. In addition to collaboration revenue of US$1.6 million due from Enzon at December 31, 2004, as part of the termination, we expect to receive Enzon's estimated share of future development expenses and certain milestone payments totaling US$5.0 million. See the "Subsequent events" note in the accompanying financial statements for additional details. Beyond the Enzon agreement we do not currently have any sources of collaboration or milestone revenue. Based on Enzon's termination of the Marqibo development agreement, we are now in the process of evaluating our partnering options for the worldwide development and commercialization of Marqibo and plan to initiate partnering discussions in 2005.

Expenses / Research and development | Research and development expenses decreased to $26.8 million for the year ended December 31, 2004 from $30.7 million in the same period in 2003. The decline is mainly the result of a significant decline in spending on pre-commercial manufacturing, clinical trials and other activities related to the NDA for Marqibo since most of this work was completed in 2003. Partially offsetting the overall decrease in research and development expenses was an increase in spending on INX-0125 (sphingosomal vinorelbine) development and preclinical studies. In the first half of 2005, we expect to file an Investigational New Drug application with the FDA and a Clinical Trial Agreement with Health Canada seeking approval to commence human clinical trials for INX-0125.

Salary expense for research and development personnel in 2004 was $0.6 million lower than in 2003 and was in line with a slight reduction in our personnel up until December 17, 2004 when we restructured and reduced our workforce from a total of 165 employees to 62 employees (see Restructuring costs). Our internal research and development staff was 41 at December 31, 2004 (total staff 62) as compared to 123 at December 31, 2003 (total staff 170).

We expect to continue incurring substantial research and development expenditures in the future due to the continuation and expansion of research and development programs for our pipeline of product candidates. As we progress with the planning of our Marqibo phase 3 trials, we will continue to evaluate our options and projected spend for the implementation of this program.

As a result of workforce reductions and budgeted spending cuts, we currently estimate that research and development expenses in 2005 will be less than half the $26.8 million expensed in 2004.

General and administrative | General and administrative expenses increased to $9.3 million for the year ended December 31, 2004 as compared to $8.8 million in the same period in 2003. This is attributed to increased recruiting costs incurred in preparation for the expected commercialization of Marqibo.

We expect general and administrative expenses in 2005 to fall by at least 30%, largely as a result of workforce reductions in December 2004. We do not expect Enzon's termination of our strategic partnership to have a significant impact on our general and administrative expenses in 2005 and beyond.

Restructuring costs | Net restructuring costs for the year ended December 31, 2004 were $5.1 million as compared to nil for the comparable period. In December 2004, following the December 1, 2004 Oncologic Drugs Advisory Committee vote to not support accelerated approval for Marqibo we scaled back certain of our activities and implemented a workforce reduction of 62% or 103 employees. The following table summarizes restructuring costs recorded in the consolidated statement of operations for the year ended December 31, 2004:

(in millions of Cdn$)		
Employee severance compensation	$	5.6
Cancellation of unvested stock options for severed employees [1]		(1.2)
Laboratory equipment impairment loss [2]		0.7
Total restructuring costs	$	5.1

[1] The cancellation of unvested stock options for severed employees resulted in the reversal of the stock-based compensation expense previously recorded on those options of $1.2 million.

[2] The scaling back of activities rendered a portion of our laboratory equipment surplus to requirements. At this time we have completed only a preliminary inventory of surplus equipment and have not yet obtained independent valuations for such equipment. The impairment loss is based on our estimate of the fair value of this surplus laboratory equipment as compared to its net book value.

See the "Restructuring costs" note in the accompanying financial statements for additional details.

Amortization | Amortization expense was $6.6 million for the year ended December 31, 2004. This compares with $8.9 million for the comparable period in 2003. The change in the estimated useful life of the Marqibo medical technology that was licensed from Elan in April 2001 reduced amortization expense by $5.4 million. At the time the medical technology was licensed, the useful life was estimated at three years. Based on developments earlier in 2004 and our expectations of reaching product commercialization, commencing in the first quarter of 2004 the estimated useful life of this medical technology has been extended for an additional 10 years. During our recent review of our Lynx medical technology it became apparent that this technology was of no future value to us. As a result, an impairment loss of $3.4 million, the net book value of the Lynx medical technology as at September 30, 2004, has been included in amortization expense in 2004 and partially offsets the reduction in amortization expense on the Marqibo medical technology. See Critical accounting policies and estimates above and the "Medical technology" note in the accompanying financial statements for additional details on the change to the estimated useful life of the medical technology licensed from Elan and the impairment loss recorded on the Lynx medical technology.

In 2005 we expect amortization expense to be approximately $2.0 million.

Other Income/Losses | Interest income was $0.9 million for the year ended December 31, 2004 as compared to $1.5 million for the year ended December 31, 2003. The decrease is a result of a decrease in the average cash, cash equivalents and short-term investments held throughout 2004 as compared to the prior year, and slightly lower average interest rates during 2004. We anticipate that in future years interest income will continue to fluctuate in relation to cash balances and interest yields. See Risks and uncertainties.

Interest expense on the US dollar denominated exchangeable and development notes (the "Notes") was $3.9 million for the year ended December 31, 2004 which was the same as the $3.9 million for the year ended December 31, 2003. The increase in interest expense due to compounding was offset by a decrease in the US to Canadian dollar foreign exchange rate. The interest expense accrued on the Notes is not payable until the Notes mature in April 2007.

Other income for the year ended December 31, 2004 was $2.5 million as compared to $7.6 million in the comparable period in 2003. Other income is largely the result of unrealized foreign exchange gains on our US dollar denominated exchangeable and development notes. This income is partially offset by foreign exchange losses on holdings of cash and short-term investments. We expect continued fluctuation in Canada/US dollar exchange rates in future years. See Risks and uncertainties.

Capital expenditures | Capital expenditures were $1.2 million, none of which were funded by capital leases, during the year ended December 31, 2004, as compared to $1.2 million including $0.2 million funded by capital leases in 2003. During the year ended December 31, 2004, we used certain of our capital assets to raise long-term debt financing, net of security deposit, of $1.1 million. We anticipate minimal capital expenditures in 2005.

LIQUIDITY AND CAPITAL RESOURCES

Since our incorporation, we have financed our operations through the public and private sales of common shares, the issuance of an exchangeable note and development note, revenues from research and development collaborations with corporate partners, interest income on funds available for investment, and government grants and tax credits. From incorporation through December 31, 2004 we had received approximately $178.1 million in net proceeds from the issuance of common shares.

At December 31, 2004, we had cash, cash equivalents and short-term investments of approximately $30.0 million as compared to $50.8 million at December 31, 2003. See Risks and uncertainties. Cash used in operating activities was $12.0 million during 2004 compared to cash used in operations of $35.0 million in the same period in the prior year. The use of cash in operating activities, in the year ended December 31, 2004, reflects:

- the decrease in our loss for the period, after adjustments for items not involving cash, to $29.8 million as compared to $32.9 million in the comparable period in 2003
- the increase in deferred revenue of $15.9 million resulting from the payment received from Enzon in the year ended December 31, 2004 as compared to nil in the comparable period in 2003
- net increase in non-cash working capital items of $2.0 million for the period as compared to net decrease of $2.0 million in the comparable period in 2003

The net changes in non-cash working capital items reflect an increase in accounts payable and accrued liabilities in 2004 as compared to 2003 of $4.1 million due largely to the accrual of termination payments resulting from our December 2004 staff reductions and an increase in accounts receivable and accrued revenue.

Net cash used in investing activities was $5.1 million in 2004 compared to net cash provided of $22.1 million in 2003. The acquisition of medical technology in 2004 includes payments of $7.3 million (US$5.5 million) to Elan. These payments were recorded as an addition to medical technology. We also recorded deferred partnership costs of $1.2 million in 2004, relating to the Enzon partnership agreement, in other long-term assets. Proceeds on maturing short-term investments, net of purchases, were $4.7 million compared to $23.1 million during the same period in the prior year. For both periods, net proceeds were due to the maturity of short-term investments that were reinvested with less than 90 day terms due to the interest yields available in the market place at that time.

Net cash provided by financing activities was $1.0 million for the year ended December 31, 2004 compared to $26.7 million for the year ended December 31, 2003. In July 2003 we received net proceeds from an offering of common shares of approximately $25.6 million. Proceeds received from the issuance of common shares on the exercise of stock options through our employee stock option plan was $0.8 million for the year ended December 31, 2004 and $0.6 million for the comparable period in 2003.

The following table lists our contractual obligations as at December 31, 2004. We expect to fund these expenditures out of cash reserves, except for the exchangeable and development notes which may, at our option, be repaid with common shares and are discussed further in Outstanding share data below.

Contractual obligations		Payments due by period			
(in millions of Cdn$)	Total	In the next year	2-3 years	4-5 years	After 5 years
Long-term debt	$ 1.9	$ 0.9	$ 1.0	$ –	$ –
Exchangeable and development notes [1]	40.2	–	40.2	–	–
Capital lease obligations	0.3	0.1	0.2	–	–
Operating leases	3.3	1.1	2.2	–	–
Research expenditures [2]	0.7	0.2	0.3	0.2	–
Total	$ 46.4	$ 2.3	$ 43.9	$ 0.2	$ –

[1] "Exchangeable and development notes" means the principal and accrued interest amounts outstanding at the balance sheet date for the exchangeable and development notes.

[2] "Research expenditures" means research and license funding commitments to third parties that are subject to our right to terminate any such funding upon providing advance notice.

We believe that our current funds on hand, anticipated final payments from Enzon, government grants, and expected interest income, will be sufficient to finance our operations and capital needs for approximately two years. See Risks and uncertainties.

Off-balance sheet arrangements | We do not have any off-balance sheet arrangements.

OUTSTANDING SHARE DATA

As of February 28, 2005, we had 38,566,788 common shares outstanding and we had outstanding options to purchase 4,706,505 common shares.

Between April 2001 and September 2002, we issued to Elan an exchangeable note and a development note (the "Notes") in aggregate principal sum of US$27.0 million and with a cumulative interest rate of 7% per year. On April 15, 2004, we announced that the Notes then totaling $41.9 million (US$32.0 million) including accrued interest, had been assigned by Elan to a group of institutional investors. The terms and conditions of the Notes remained unchanged. Effective April 27, 2004, the exchangeable note can be converted, at the holders' option, into our common shares at US$5.71 per share and the development note can be converted at US$5.07 per share. Upon maturity at April 27, 2007, repayment of both notes can be made, at our sole discretion, in cash, or by the issuance of our common shares based on the market price of our shares at the time of maturity, or by any combination of cash and common shares. As at December 31, 2004, the Notes plus accrued interest totaled $40.3 million (US$33.5 million).

The total maximum number of common shares for which we currently have regulatory approval to issue in respect of the exchangeable and development notes, is 7,342,614, being the maximum number issuable if the Notes are converted by the holder immediately before maturity on April 27, 2007. If such shares are insufficient to settle all amounts outstanding under the Notes, we would be required to obtain shareholder approval to issue additional common shares or pay the remaining amounts due in cash.

Pursuant to the termination agreement signed with Elan in April 2003, we made a US$3.0 million milestone cash payment to Elan triggered by the signing of our partnership agreement with Enzon and a second milestone cash payment of US$2.5 million triggered by the FDA's acceptance of our NDA filing for Marqibo. A third and final milestone payment of US$2.5 million is contingent upon the successful completion of regulatory approval for Marqibo and can be settled, at our option, with cash or our common shares. See the "Acquisition" note in the accompanying financial statements for additional details.

RISKS AND UNCERTAINTIES

Our risks and uncertainties are discussed in further detail in our Annual Information Form which can be found at www.sedar.com.

We believe that our current funds on hand, anticipated final payments from Enzon, government grants, and expected interest income, will be sufficient to finance our operations and capital needs for approximately two years. In arriving at this estimate of the sufficiency of our cash resources, we have made certain assumptions about the phase 3 clinical trials for Marqibo, and we have assumed that significant costs will not begin to be incurred until the second half of 2005 at the earliest and only if we have entered into arrangements with a new development partner for Marqibo. Any material change in these assumptions will affect this cash reserve estimate. Our funding needs may vary further depending on a number of other factors including:

- the extent to which we pursue the continued development of our Marqibo and non-Marqibo, Targeted Chemotherapy product pipeline and the cost of any clinical trials pursued
- the extent to which we can extract significant value from our Targeted Immunotherapy technology and from our other non-core technologies
- the decisions, and the timing of decisions, made by health regulatory agencies regarding our technology and products
- our ability to attract and retain corporate partners, and their effectiveness in carrying out the development and ultimate commercialization of our product candidates
- our decision to in-license or acquire additional products for development
- competing technological and market developments
- prosecuting and enforcing our patent claims and other intellectual property rights

Substantial additional funds would be required to complete the phase 3 clinical trials for Marqibo and to continue with the active development of our other Targeted Chemotherapy and Targeted Immunotherapy products. We will seek to obtain additional funds for these purposes through a variety of sources including public or private equity or debt financing, collaborative arrangements with pharmaceutical companies and government grants. There can be no assurance that additional funding will be available at all or on acceptable terms to permit further development of our products. In addition, we have not established bank financing arrangements and there can be no assurance that we will be able to establish such arrangements on satisfactory terms. Also, our outstanding exchangeable and development notes which, together with accrued interest, would total US$39.2 million at maturity in April 2007, may hinder our ability to raise additional funding. If we settle these notes at maturity through the issuance of common shares our issued share capital will be diluted.

If adequate funding is not available, we may be required to delay, reduce or eliminate one or more of our research or development programs. We may need to obtain funds through arrangements with collaborators or others that may mean relinquishing greater or all rights to product candidates at an early stage of development or on less favorable terms than we would otherwise seek. Insufficient financing may also mean relinquishing rights to some of our technologies that we would otherwise develop or commercialize.

In addition, we are exposed to market risk related to changes in interest and foreign currency exchange rates, each of which could adversely affect the value of our current assets and liabilities. We invest our cash reserves in a diverse portfolio of liquid, high-grade investment securities with varying terms to maturity (not exceeding two years), selected with regard to the expected timing of expenditures for continuing operations and prevailing interest rates. We do not believe that the results of operations or cash flows would be affected to any significant degree by a sudden change in market interest rates relative to our investment portfolio, due to the relative short-term nature of the investments. We purchase goods and services in both Canadian and US dollars and have historically earned a significant portion of our revenues in US dollars. Foreign exchange risk related to operating costs is primarily managed by satisfying non-Canadian denominated expenditures with cash flows or assets denominated in the same currency. We do not have any protection against the foreign exchange risk related to our US dollar denominated exchangeable and development notes and maturing on April 27, 2007. As at December 31, 2004, we do not have any forward currency contracts or other financial derivatives in place to hedge exchange risk.

FORWARD-LOOKING STATEMENTS

This discussion and analysis, contains forward-looking statements which may not be based on historical fact, including without limitation statements containing the words "believes", "may", "plan", "will", "estimate", "continue", "anticipates", "intends", "expects", and similar expressions. Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, events or developments to be materially different from any future results, events or developments expressed or implied by such forward-looking statements. Such factors include, among others:

- our stage of development
- our lack of product revenues
- our additional capital requirements
- risks associated with the completion of our clinical trials and obtaining regulatory approval to market our products
- our ability to protect our intellectual property
- our dependence on collaborative partners

These factors should be considered carefully and readers are cautioned not to place undue reliance on such forward-looking statements. We disclaim any obligation to update these factors or to publicly announce the result of any revisions to any of the forward-looking statements contained above to reflect future results, events or developments.

Management's Responsibility for Financial Reporting

The financial statements contained in this annual report have been prepared by management in accordance with generally accepted accounting principles and have been approved by the Board of Directors. The integrity and objectivity of these financial statements are the responsibility of management. In addition, management is responsible for all other information in the annual report and for ensuring that this information is consistent, where appropriate, with the information contained in the financial statements.

In support of this responsibility, management maintains a system of internal controls to provide reasonable assurance as to the reliability of financial information and the safe-guarding of assets. The financial statements include amounts which are based on the best estimates and judgments of management.

The Board of Directors is responsible for ensuring that management fulfills its responsibility for financial reporting and internal control and exercises this responsibility principally through the Audit Committee. The Audit Committee consists of three directors not involved in the daily operations of the Company. The Audit Committee meets with management and meets independently with the external auditors to satisfy itself that management's responsibilities are properly discharged and to review the financial statements prior to their presentation to the Board of Directors for approval.

The external auditors, KPMG LLP, conduct an independent examination, in accordance with generally accepted auditing standards, and express their opinion on the financial statements. Their examination includes a review of the Company's system of internal controls and appropriate tests and procedures to provide reasonable assurance that the financial statements are, in all material respects, presented fairly and in accordance with accounting principles generally accepted in Canada. The external auditors have free and full access to the Audit Committee with respect to their findings concerning the fairness of financial reporting and the adequacy of internal controls.

David J. Main
President and
Chief Executive Officer

Ian C. Mortimer
Vice President, Finance and
Chief Financial Officer

Auditors' Report to the Shareholders

We have audited the consolidated balance sheets of Inex Pharmaceuticals Corporation as at December 31, 2004 and 2003, and the consolidated statements of operations, shareholders' equity (deficiency), and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2004 and 2003 and the results of its operations and the cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

KPMG llp
Chartered Accountants, Vancouver, Canada,
February 8, 2005, except for notes 11(a) and 21, which are as of March 17, 2005

Consolidated Balance Sheets

(Expressed in Canadian dollars)
December 31, 2004 and 2003

	2004	2003
		Restated–note 3
ASSETS		
Current assets:		
Cash and cash equivalents *(note 5)*	$ **30,045,776**	$ 46,107,754
Short-term investments *(note 5)*	**—**	4,732,287
Accounts receivable	**2,163,629**	436,062
Government grant receivable	**—**	70,000
Accrued revenue *(note 21)*	**1,999,766**	—
Prepaid expenses and other assets	**333,363**	649,511
	34,542,534	51,995,614
Long-term investment *(note 6)*	**691,410**	2,001,166
Property and equipment *(note 7)*	**4,125,111**	5,313,178
Medical technology *(note 8)*	**8,648,146**	6,178,225
Other long-term assets *(note 15)*	**1,398,367**	296,328
	$ **49,405,568**	$ 65,784,511
LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIENCY)		
Current liabilities:		
Accounts payable and accrued liabilities *(note 20(c))*	$ **9,944,457**	$ 4,835,501
Current portion of obligations under capital leases	**107,282**	174,131
Current portion of long-term debt	**825,428**	365,906
Current portion of deferred revenue	**2,208,000**	503,310
	13,085,167	5,878,848
Obligations under capital leases *(note 14)*	**156,380**	264,911
Long-term debt *(note 15)*	**1,045,202**	781,096
Exchangeable and development notes *(note 10)*	**37,522,788**	36,737,933
Deferred lease inducements *(note 7)*	**414,699**	440,699
Deferred revenue *(notes 11(a))*	**8,947,715**	—
Deferred dilution gain *(note 6)*	**852,672**	2,162,428
	62,024,623	46,265,915
Shareholders' equity (deficiency):		
Share capital *(note 9)*	**180,237,917**	179,097,330
Additional paid-in capital	**20,069,127**	19,627,483
Deficit	**(212,926,099)**	(179,206,217)
	(12,619,055)	19,518,596
	$ **49,405,568**	$ 65,784,511

Commitments and contingencies *(note 16)*
Subsequent event *(note 21)*

See accompanying notes to consolidated financial statements.

Approved on behalf of the Board:

David J. Main
Director

Darrell J. Elliott
Director

Consolidated Statements of Operations

(Expressed in Canadian dollars) Years ended December 31, 2004 and 2003	2004	2003
		Restated–note 3
Revenue:		
Research and development collaborations *(note 11(a))*	**$ 6,091,405**	$ —
Licensing fees and milestone payments *(notes 11(a) and 11(c))*	**8,538,181**	3,542,904
	14,629,586	3,542,904
Expenses:		
Research and development *(note 12)*	**26,827,547**	30,741,073
General and administrative	**9,324,798**	8,798,307
Restructuring costs *(note 13)*	**5,113,153**	—
Amortization	**6,585,041**	8,931,162
	47,850,539	48,470,542
Loss before other income (losses)	**(33,220,953)**	(44,927,638)
Interest income	**902,629**	1,478,824
Interest on exchangeable and development notes *(notes 3 and 10)*	**(3,909,007)**	(3,880,936)
Other income	**2,507,449**	7,633,878
Dilution gain from Protiva Biotherapeutics Inc. *(note 6)*	**1,309,756**	1,351,167
Equity in loss of Protiva Biotherapeutics Inc. *(note 6)*	**(1,309,756)**	(1,351,167)
Loss for the year	**$ (33,719,882)**	$ (39,695,872)
Weighted average number of common shares outstanding	**38,522,011**	35,625,564
Loss per common share	**$ (0.88)**	$ (1.11)

See accompanying notes to consolidated financial statements.

Consolidated Statements of Shareholders' Equity (Deficiency)

(Expressed in Canadian dollars)
Years ended December 31, 2004 and 2003

	Number of shares	Share capital	Additional paid-in capital	Deficit	Total shareholders' equity (deficiency)
Balance, December 31, 2002 *(restated – note 3)*	32,974,762	$ 152,617,301	$ 17,054,344	$ (139,510,345)	$ 30,161,300
Net loss *(restated – note 3)*	—	—	—	(39,695,872)	(39,695,872)
Stock-based compensation	—	—	2,944,183	—	2,944,183
Issuance of common shares pursuant to exercise of options	422,671	927,207	(371,044)	—	556,163
Issuance of common shares pursuant to public offering	5,012,200	27,316,490	—	—	27,316,490
Share issuance costs	—	(1,763,668)	—	—	(1,763,668)
Balance, December 31, 2003 *(restated – note 3)*	38,409,633	179,097,330	19,627,483	(179,206,217)	19,518,596
Net loss	—	—	—	(33,719,882)	(33,719,882)
Stock-based compensation	—	—	823,488	—	823,488
Issuance of common shares pursuant to exercise of options	157,155	1,140,587	(381,844)	—	758,743
Balance, December 31, 2004	38,566,788	$ 180,237,917	$ 20,069,127	$ (212,926,099)	$ (12,619,055)

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows

(Expressed in Canadian dollars)
Years ended December 31, 2004 and 2003

	2004	2003
		Restated–note 3
Cash provided by (used in):		
Operations:		
Loss for the year	$ (33,719,882)	$ (39,695,872)
Items not involving cash:		
Amortization of property and equipment	1,680,414	1,806,052
Impairment loss on property and equipment *(note 13)*	727,157	—
Amortization of medical technology	4,904,627	7,125,110
Amortization of deferred revenue	(5,222,460)	(524,268)
Amortization of deferred lease inducements	(125,039)	(110,891)
Amortization of other long-term assets	205,227	—
Increase in deferred lease inducements	99,039	—
Interest on exchangeable and development notes	3,909,007	3,880,936
Unrealized foreign exchange (gain) loss on exchangeable and development notes	(3,124,152)	(8,374,430)
Dilution gain from Protiva Biotherapeutics Inc.	(1,309,756)	(1,351,167)
Equity in loss of Protiva Biotherapeutics Inc.	1,309,756	1,351,167
Stock-based compensation expense	823,488	2,944,183
Increase in deferred revenue	15,874,865	—
Net change in non-cash working capital *(note 19)*	1,967,165	(2,017,066)
	(12,000,544)	(34,966,246)
Investments:		
Acquisition of property and equipment	(1,219,504)	(1,021,501)
Acquisition of medical technology	(7,374,548)	—
Acquisition of other long-term assets	(1,196,363)	—
Proceeds on maturity of short-term investments, net	4,732,287	23,096,569
	(5,058,128)	22,075,068
Financing:		
Issuance of common shares pursuant to:		
Public offering, net of issue costs	—	25,552,822
Exercise of options	758,743	556,163
Proceeds from long-term debt, net of security deposit and financing costs	1,056,304	850,674
Repayment of long-term debt	(642,973)	—
Repayment of obligations under capital leases	(175,380)	(241,088)
	996,694	26,718,571
Increase (decrease) in cash and cash equivalents	(16,061,978)	13,827,393
Cash and cash equivalents, beginning of year	46,107,754	32,280,361
Cash and cash equivalents, end of year	$ 30,045,776	$ 46,107,754

Supplementary cash flow information *(note 20(a))*

See accompanying notes to consolidated financial statements.

Notes to the Consolidated Financial Statements

1 | OPERATIONS:

Inex Pharmaceuticals Corporation (the "Company"), incorporated under the laws of the Province of British Columbia, Canada, is a biopharmaceutical company developing and commercializing proprietary drugs and drug delivery systems that improve the treatment of cancer. The Company's product candidates utilize both already approved, conventional pharmaceuticals in combination with its drug delivery technology, and novel oncology compounds known as oligonucleotide pharmaceuticals.

The Company commenced operations in July 1992 and has devoted its resources primarily to fund its research and development programs. The Company has incurred losses since inception and has not received any revenues other than from research and development collaborations, license fees and milestone payments. The Company has a cumulative deficit of $212.9 million as at December 31, 2004 (2003 – $179.2 million). Losses are expected to continue for the foreseeable future as the Company continues to invest in product research and development, preclinical studies, clinical trials and regulatory compliance and other pipeline candidates.

Since its incorporation, the Company has financed its operations through the public and private sales of its common shares, the issuance of exchangeable and development notes payable, revenues from research and development collaborations with corporate partners, interest income on funds available for investment, and government grants and tax credits. As at December 31, 2004 the Company has cash, cash equivalents and short-term investments of approximately $30.0 million.

Management believes that the current funds on hand and anticipated income sources should be sufficient to finance its operations and capital needs for approximately two years. The Company's funding needs may, however, vary depending upon a number of factors including, among others, progress of the Company's research and development programs, the Company's ability to attract and retain corporate partners, the number and breadth of these programs, costs associated with completing clinical studies and the regulatory approval process, and protecting the Company's intellectual property rights.

2 | SIGNIFICANT ACCOUNTING POLICIES:

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles and reflect the following significant accounting policies:

a | *Basis of consolidation:*

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Inex Pharmaceuticals, Inc. ("IPI"), Inex Pharmaceuticals (USA), Inc. ("Inex USA"), Inex International Holdings Ltd. ("Inex Holdings"), and IE Oncology Company Ltd. ("IE Oncology"), held through Inex Holdings.

In addition, the consolidated financial statements reflect the results of operations of the Company's investment in Protiva Biotherapeutics Inc. ("Protiva") using the equity method of accounting.

All significant intercompany transactions and balances have been eliminated on consolidation.

b | Use of estimates:

The preparation of the financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions about future events that affect the reported amounts of assets, liabilities, revenue and expenses as at the end or during the reporting period. Management believes that the estimates used are reasonable and prudent, however, actual results could differ from those estimates. Significant areas requiring the use of management estimates relate to the determination of the valuation of the long-term investment, medical technology, the useful lives of assets for amortization, recognition of revenue, stock-based compensation, components of the exchangeable and development notes, and the amounts recorded as accrued liabilities.

c | Cash and cash equivalents:

Cash and cash equivalents are all highly liquid instruments with an original maturity of three months or less when purchased. The carrying value of cash and cash equivalents approximates their market value.

d | Short-term investments:

Short-term investments are recorded at cost plus accrued interest. The carrying value of short-term investments approximates their market value.

e | Long-term investment:

Long-term investment in a company over which the Company has significant influence is accounted for using the equity method. The Company provides for impairment losses whenever events or changes in circumstances indicate that a decline in value below the carrying amount is other than temporary. No provisions for impairment losses with respect to this investment have been made to date.

f | Property and equipment:

Property and equipment are recorded at cost less impairment losses, accumulated amortization, related government grants and investment tax credits. The Company records amortization using the straight-line method over the estimated useful lives of the capital assets as follows:

	Rate
Laboratory equipment	5 years
Computer hardware	5 years
Computer software	2 years
Office equipment	2 years
Furniture and fixtures	5 years

Leasehold improvements are amortized over the lesser of their estimated useful lives or the lease term.

g | Medical technology:

The costs of acquiring or licensing medical technology from arm's length third parties are capitalized. Costs are amortized on a straight-line basis over the estimated useful life of the technology ranging from nine to 12 years.

The costs incurred in establishing and maintaining patents for intellectual property developed internally are expensed in the period incurred.

h | Valuation of long-lived assets:

If management determines that the carrying value of property and equipment or medical technology exceeds the recoverable value based on future undiscounted cash flows, such assets are written down to their fair values.

In the fourth quarter of 2004, the Company wrote-down its Lynx medical technology to nil (note 8) and recorded an impairment loss on its laboratory equipment of $727,157 (note 13).

i | Leases and lease inducements:

Leases entered into are classified as either capital or operating leases. Leases which substantially transfer all benefits and risks of ownership of property to the Company are accounted for as capital leases. At the time a capital lease is entered into, an asset is recorded together with its related long-term obligation to reflect the purchase and financing.

All other leases are accounted for as operating leases wherein rental payments are expensed as incurred.

Lease inducements represent leasehold improvements paid for by the landlord and are amortized on a straight-line basis over the term of the lease and are recorded as a reduction of rent expense.

j | Deferred dilution gains:

Gains that arise on the dilution of the Company's interest in the development stage company, Protiva, for which realization is not assured, are deferred. The dilution gains are amortized to income as Protiva continues to develop the technology transferred from the Company, to the extent of the Company's share in Protiva's net loss each period (note 6). Dilution losses are recognized immediately.

k | Revenue recognition:

The Company earns revenue from research and development collaboration services, licensing fees and milestone payments. Payments received under collaborative research and development agreements, which are non-refundable, are recorded as revenue as services are performed and the related expenditures incurred pursuant to the terms of the agreement and provided collectibility is reasonably assured. Non-refundable upfront license fees from collaborative licensing and development arrangements are recognized as the Company fulfills its obligations related to the various elements within the agreements, in accordance with the contractual arrangements with third parties and the term over which the underlying benefit has been conferred. Revenues associated with multiple element arrangements are attributed to the various elements based on their relative fair value. Any upfront license payments received under an agreement whereby the Company also provides research and development services are recognized as revenue over the term of the research and development period. Revenue earned under contractual arrangements upon the occurrence of specified milestones is recognized as the milestones are achieved and collection of payment is reasonably assured.

Cash or other compensation received in advance of meeting the revenue recognition criteria is recorded as deferred revenue on the consolidated balance sheet. Revenue meeting recognition criteria but not yet received or receivable is recorded as accrued revenue on the consolidated balance sheet.

l | Research and development expenditures:

Research costs are charged as an expense in the period in which they are incurred. Development costs are charged as an expense in the period incurred unless the Company believes a development project meets specified criteria for deferral and amortization. No development costs have been deferred to date.

m | Loss per share:

Loss per share is calculated based on the weighted average number of common shares outstanding. Diluted loss per share does not differ from basic loss per share since the effect of the Company's stock options and the exchangeable and development notes are antidilutive.

n | Government assistance and investment tax credits:

Government assistance provided for current expenses is included in the determination of income for the year, as a reduction of the expenses to which it relates. Government assistance provided for the acquisition of property and equipment is deducted from the cost of the related assets. Investment tax credits are accounted for under the cost reduction method whereby they are netted against the expense or asset to which they relate. Government assistance and investment tax credits are recorded when the Company has incurred the qualifying expenditures and there is reasonable assurance the government assistance or tax credits will be realized.

o | Foreign currency translation:

For the Company and its integrated subsidiaries (IPI, Inex USA, Inex Holdings and IE Oncology), monetary assets and liabilities are translated into Canadian dollars at the rate of exchange prevailing at the balance sheet date. Non-monetary assets and liabilities are translated at historical exchange rates. Revenue and expenses are translated at the average rate of exchange for the month in which such transactions occur. Exchange gains and losses are included in loss for the year.

p | Future income taxes:

Income taxes are accounted for using the liability method of tax allocation. Future income taxes are recognized for the future income tax consequences attributable to differences between the carrying values of assets and liabilities and their respective income tax bases and for loss carryforwards. Future income tax assets and liabilities are measured using substantively enacted or enacted income tax rates expected to apply to taxable income in the years in which temporary differences are expected to be recovered or settled. The effect on future income tax assets and liabilities of a change in rates is included in earnings in the period that includes the substantive enactment date. Future income tax assets are recognized in the financial statements if realization is considered to be more likely than not.

q | Financial instruments:

For certain of the Company's financial instruments, including cash and cash equivalents, short-term investments, accounts receivable, government grant receivable and accounts payable and accrued liabilities, the carrying amounts approximate fair value due to their relative short-term nature. The obligations under capital leases bear interest at rates that, in management's opinion, approximate the current interest rates and therefore, approximate their fair value. Management believes that the carrying value of the exchangeable and development notes approximate their fair value.

The Company purchases goods and services in both Canadian and US dollars and earns a significant portion of its revenues in US dollars. Foreign exchange risk is managed primarily by satisfying non-Canadian denominated expenditures with cash flows or assets denominated in the same currency. As at December 31, 2004, the Company does not have any forward currency contracts or other financial derivatives in place to hedge exchange risk.

r | Stock-based compensation:

The Company grants stock options to employees, directors and consultants pursuant to a share incentive plan described in note 9(b). Compensation expense is recorded for stock options issued to employees and non-employees using the fair value method with a corresponding increase in additional paid-in capital. Any consideration received on exercise of stock options or the purchase of stock is credited to share capital.

Under the fair value based method, stock-based payments to non-employees are measured at the fair value of the equity instruments issued, and the awards are periodically remeasured during the vesting period as the options are earned. Any changes therein are recognized over the period, and in the same manner as if the Company had paid cash instead of paying with or using equity instruments. The fair value of stock-based awards to employees is typically measured at the grant date and amortized over the vesting period.

s | Comparative figures:

Certain prior year comparative figures have been reclassified to conform to the current year's presentation.

3 | CHANGE IN ACCOUNTING POLICIES:

In the fourth quarter of 2004, the Company adopted the amended recommendations of the Canadian Institute of Chartered Accountants ("CICA") Handbook Section 3860, *Financial Instruments – Disclosure and Presentation*. This change in accounting has been applied to the Company's exchangeable and development notes (the "Notes") (note 10) on a retroactive basis with restatement and has impacted the financial statements as follows:

a | The fair values of the options to convert the Notes to equity, in the aggregate amount of $5,943,374 and calculated using the Black-Scholes option pricing model, are considered a discount on the Notes, with a corresponding credit to additional paid-in capital. The debt discount for each draw on the Notes is being amortized, on an effective yield basis, over the term of that draw. The amortization of the debt discount is included in interest on exchangeable and development notes in the loss for the period. As the Notes were originally reported as equity, there was no requirement to account for the fair values of the options to convert the Notes.

b | The remaining amount of the Notes' fair value is now presented on the Company's consolidated balance sheet as debt, whereas they were originally reported as equity.

c | Interest expense on the Notes is now presented as an expense in the consolidated statements of operations whereas it was previously recorded directly to the Company's deficit account and presented in the consolidated statements of shareholders' equity.

d | The Notes are payable in US dollars and together with any accrued interest to date will be translated to Canadian dollars at each reporting date. Any change in the US/Canadian currency exchange rate gives rise to a foreign currency translation gain or loss included in other income (losses) for the period.

As a result of the retroactive change in accounting policy, the 2003 financial statements have been restated as follows:

	As originally reported	As restated
Consolidated Statement of Operations		
Interest on exchangeable and development notes [(i)]	$ –	$ (3,880,936)
Other income (losses)	(740,552)	7,633,878
Net loss	(44,189,366)	(39,695,872)
Loss per share	(1.32)	(1.11)
Consolidated Balance Sheet		
Exchangeable and development notes (classified as debt) *(note 10)*	–	36,737,933
Total liabilities	9,527,982	46,265,915
Additional paid-in capital	13,684,109	19,627,483
Exchangeable and development notes (classified as equity) *(note 10)*	48,243,515	–
Deficit	(184,768,425)	(179,206,217)
Total shareholders' equity	56,256,529	19,518,596

[(i)] Interest on exchange and development notes was originally reported as a $2,797,037 charge to the deficit in the consolidated statement of shareholders' equity and did not appear in the consolidated statement of operations.

4 | ACQUISITION:

On April 3, 2003, the Company entered into a Termination Agreement (the "Termination Agreement") to regain 100% ownership of its lead product candidate, Marqibo, by reacquiring the 19.9% interest in IE Oncology, a joint venture company, held by Elan Corporation, plc ("Elan"). The reacquisition was prompted by Elan's announcement in 2002 to undertake a significant financial restructuring program that required a focus on therapeutic areas outside oncology.

Under the Termination Agreement, there were no advance cash payments or ongoing royalties payable to Elan. The purchase price payable by the Company for Elan's interest in IE Oncology is to be satisfied through three milestone payments to Elan totaling US$8,000,000, some of which may be paid in shares valued at the then current market price. The milestone payments are payable if and when certain commercial and regulatory events occur. The outcome of these events, and the likelihood that the contingent consideration will become payable by the Company, could not be determined beyond reasonable doubt at the date of acquisition. The signing of the partnership agreement with Enzon (note 11(a)) was the first such event and triggered the US$3,000,000 milestone payment to Elan pursuant to the Termination Agreement. Acceptance of the Company's New Drug Application filing for Marqibo by the US Food and Drug Administration in May 2004 triggered an additional US$2,500,000 payment to Elan. Both payments have been recorded by the Company as medical technology and will be amortized over the remaining useful life of the medical technology, which is estimated to be 10 years. A further US$2,500,000 will become due to Elan if the Company obtains regulatory approval for Marqibo.

In addition, as part of the Termination Agreement, the Company retains a fully paid-up license to Elan's intellectual property related to Marqibo. Elan has no further financial obligations to the Company under the original joint venture agreements. The reacquisition terms take into consideration that the Company has assumed Elan's 19.9% funding obligation since July 1, 2002 and Elan will not be responsible for further reimbursement of any past development costs. In addition, Elan's obligation to purchase US$2,000,000 of the Company's common shares upon filing of a New Drug Application has been cancelled. The exchangeable note and the development note (note 10) remain outstanding and the terms and conditions remain in effect.

The April 3, 2003 acquisition was accounted for as a step purchase using the purchase method of accounting, and accordingly, 100% of the assets, liabilities and operations of IE Oncology have been included in the consolidated financial statements of the Company from April 3, 2003, the date of acquisition. The purchase cost of Elan's 19.9% interest in IE Oncology at the date of acquisition consisted solely of the contingent consideration of up to US$8,000,000 described above, and will be recorded if and when the milestone triggering events occur.

5 | CASH EQUIVALENTS AND SHORT-TERM INVESTMENTS:

At December 31, 2004, cash and cash equivalents include commercial paper bearing a weighted average interest rate of 2.4% (2003 – 2.7%). Included in cash and cash equivalents is $8,415,828 (US$7,001,520) denominated in US dollars (2003 – $583,072 (US$ 449,728)).

The Company did not hold any short-term investments as at December 31, 2004. Short-term investments as at December 31, 2003, include commercial paper bearing a weighted average interest rate of 2.8% with initial maturities greater than 90 days, all of which matured by February 2004. At December 31, 2003, there were no short-term investments denominated in US dollars. All of the Company's short-term investments were held to maturity. Short-term investments include securities issued from a variety of corporations and financial institutions, the largest of which represented 9% as at December 31, 2003.

All held-to-maturity securities are due within one year and the fair values approximate carrying value.

6 | LONG-TERM INVESTMENT:

Long-term investment represents the Company's investment in Protiva. On January 18, 2001, the Company transferred certain intellectual property rights and capital assets relating to its gene delivery technology to Protiva in exchange for 4,550,000 common shares of Protiva resulting in approximately 98% ownership of Protiva. The investment was recorded in the accounts of the Company at $44,317, the carrying value of the assets transferred.

During 2001, Protiva issued common shares and Series 1 class A preferred shares to outside investors. In addition, Protiva issued 184,255 Series 1 class A preferred shares to the Company in settlement of a $309,550 advance. During 2002, Protiva issued Series 2 class A preferred shares to outside investors. As a result of these share issuances, the Company no longer had the right to elect the majority of the board of directors of Protiva effective on August 31, 2001 and the Company's ownership in Protiva was reduced to 34% effective July 31, 2002. Accordingly, effective September 1, 2001, the Company ceased consolidating Protiva and began accounting for it using the equity method. The issuances of shares by Protiva resulted in dilution gains of $2,213,887 and $4,599,684 in 2002 and 2001, respectively, which have been deferred by the Company and are being amortized to income as further research and development costs are incurred.

During the year ended December 31, 2004, the Company recovered costs of approximately $229,500 (2003 – $151,250) from Protiva with respect to providing research support services. At December 31, 2004, included in accounts receivable of the Company is $38,411 (2003 – $43,769) due from Protiva.

7 | PROPERTY AND EQUIPMENT:

2004	Cost	Accumulated amortization and impairment	Net book value
Laboratory equipment *(note 13)*	**$ 6,852,560**	**$ 5,342,433**	**$ 1,510,127**
Leasehold improvements	**4,945,381**	**3,206,840**	**1,738,541**
Computer hardware and software	**1,949,347**	**1,402,479**	**546,868**
Office equipment	**1,288,716**	**1,232,932**	**55,784**
Furniture and fixtures	**913,265**	**639,474**	**273,791**
	$ 15,949,269	**$ 11,824,158**	**$ 4,125,111**

2003	Cost	Accumulated amortization and impairment	Net book value
Laboratory equipment	$ 5,763,607	$ 3,960,822	$ 1,802,785
Leasehold improvements	4,936,836	2,795,756	2,141,080
Computer hardware and software	1,177,158	843,802	333,356
Office equipment	1,941,263	1,306,196	635,067
Furniture and fixtures	910,898	510,008	400,890
	$ 14,729,762	$ 9,416,584	$ 5,313,178

The original cost of leasehold improvements are recorded before applying lease inducements of $1,214,235 (2003 – $1,115,196), resulting in a net cost of $3,731,146 (2003 – $3,821,640). These lease inducements were deferred and are amortized as described in note 2(i). Included in laboratory equipment and office equipment are assets under capital leases with an original cost of $1,118,644 (2003 – $1,118,644) and accumulated amortization of $797,340 (2003 – $626,373).

8 | MEDICAL TECHNOLOGY:

2004	Cost	Accumulated amortization and impairment	Net book value
Lynx medical technology	**$ 9,710,266**	**$ 9,710,266**	**$ –**
Elan medical technology *(note 4 and note 11(b))*	**25,771,147**	**17,186,372**	**8,584,775**
Other medical technology	**65,650**	**2,279**	**63,371**
	$ 35,547,063	**$ 26,898,917**	**$ 8,648,146**

2003	Cost	Accumulated amortization and impairment	Net book value
Lynx medical technology	$ 9,710,266	$ 5,583,402	$ 4,126,864
Elan medical technology *(note 4 and note 11(b))*	18,462,249	16,410,888	2,051,361
	$ 28,172,515	$ 21,994,290	$ 6,178,225

The Lynx medical technology was recorded upon the purchase of the oligonucleotide therapeutic business of Lynx Therapeutics, Inc. by the Company in March 1998 and relates to the use of oligonucleotides for antisense applications. During the Company's recent review of the technology licenses purchased from Lynx, it became apparent that although the Company is continuing to use oligonucleotides in its Targeted Immunotherapy platform technology, this application relies on the immune stimulating properties of such molecules and is no longer based on an antisense mechanism. The Lynx medical technology is therefore of no future value to the Company. As a result an impairment loss of $3,398,592, the net book value of the Lynx medical technology as at September 30, 2004, has been included in amortization expense in the year ended December 31, 2004.

The Company licensed the Elan medical technology from Elan Corporation, plc ("Elan") relating to Marqibo in April 2001 for a cost of $18,462,249 (US$12,015,000) and the useful life was estimated then to be three years ending in the second quarter of 2004. Based on events early in 2004, such as the completion of the Company's pivotal phase 2 trial evaluating Marqibo, the filing of the New Drug Application seeking marketing approval for Marqibo and the signing of the commercialization agreement with Enzon, management has, effective January 1, 2004, revised the estimated useful life of the Elan medical technology to approximate the average remaining legal and economic life of the key patents in North America of approximately 10 years. Accordingly, the remaining net book value of the Elan medical technology of $2,051,361 on January 1, 2004 and any subsequent additions to this technology are being amortized over the period ending in the fourth quarter of 2013.

9 | SHARE CAPITAL:

a | Authorized:

100,000,000 common shares without par value.

25,000,000 preferred shares without par value.

b | Stock-based compensation:

The Company established the 1996 Share Incentive Plan whereby the Company may grant options to employees, directors and consultants. The exercise price of the options is determined by the Company's Board of Directors but will be at least equal to the closing market price of the common shares on the day preceding the date of grant and the term may not exceed 10 years. Options granted are also subject to certain vesting provisions, but generally vest over four years. During the year ended December 31, 2004, the shareholders of the Company approved an increase to the number of shares reserved for issuance under the 1996 Share Incentive Plan by 900,000 (2003 – 485,000) thereby increasing the maximum common shares available under this plan to 5,818,322 (2003 – 4,918,322), of which 963,961 (2003 – 183,165) common shares remain available for future allocation. Prior to the adoption of the 1996 Share Incentive Plan the Company had in place the 1993 Employee Incentive Stock Option Plan. No further options are issuable under the 1993 Employee Incentive Stock Option Plan.

Stock option transactions with respect to the 1996 Share Incentive Plan and 1993 Employee Incentive Stock Option Plan for the respective years and the number of share options outstanding are summarized as follows:

	Number of optioned common shares	Weighted average exercise price
Balance, December 31, 2002	4,602,629	$ 4.94
Options granted	768,197	5.73
Options exercised	(422,671)	1.32
Options forfeited	(208,418)	6.11
Balance, December 31, 2003	4,739,737	5.34
Options granted	708,184	1.38
Options exercised	(157,155)	4.83
Options forfeited	(592,761)	6.00
Balance, December 31, 2004	4,698,005	$ 4.68

The following table summarizes information pertaining to the Company's stock options outstanding at December 31, 2004:

	Options outstanding December 31, 2004			Options exercisable December 31, 2004	
Range of Exercise prices	Number of options outstanding	Weighted average remaining contractual life (years)	Weighted average exercise price	Number of options exercisable	Weighted average exercise price
$0.66 to $0.70	615,184	10.0	$ 0.70	175,000	$ 0.70
$1.10 to $1.90	317,725	3.3	1.22	317,725	1.22
$2.00 to $3.90	196,342	4.0	3.25	194,311	3.24
$4.00 to $4.95	1,078,859	3.4	4.54	941,663	4.50
$5.00 to $5.95	1,558,434	4.8	5.45	1,325,662	5.33
$6.00 to $6.98	260,740	3.0	6.61	238,791	6.61
$7.00 to $7.97	420,227	4.4	7.11	397,820	7.11
$8.05 to $12.50	250,494	2.1	9.73	237,953	9.81
$0.70 to $12.50	4,698,005	4.7	$ 4.68	3,828,925	$ 5.01

The stock options expire at various dates from March 8, 2005 to December 14, 2014.

The fair value of each option is estimated as at the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions:

	2004	2003
Dividend yield	**0.0%**	0.0%
Expected volatility	**99.6%**	70.7%
Risk-free interest rate	**3.7%**	3.5%
Expected average option term	**4.9 years**	4.53 years

There were no options issued to non-employees during the years ended December 31, 2004 and December 31, 2003. The weighted average fair value of the options granted to employees during the year ended December 31, 2004 was $0.92 (2003 – $3.33) per option.

10 | EXCHANGEABLE AND DEVELOPMENT NOTES:

	2004	2003
		Restated–note 3
Exchangeable note, net of financing costs of $62,172 *(note 11(b))*	**$ 14,379,858**	$ 15,515,276
Accrued interest on exchangeable note	**4,091,543**	3,108,836
Unamortized discount on exchangeable note	**(618,697)**	(879,010)
Development note	**18,030,000**	19,447,500
Accrued interest on development note	**3,752,835**	2,514,886
Unamortized discount on development note	**(2,112,751)**	(2,969,555)
	$ 37,522,788	$ 36,737,933

Elan provided the Company with a US$12,015,000 exchangeable note to fund the Company's share of IE Oncology's licensing cost of the Elan medical technology (note 11(b)). Elan also provided the Company with a US$15,000,000 development note facility of which US$9,834,508 and US$5,165,492 were drawn down in each of 2002 and 2001, respectively, to partially fund the Company's share of IE Oncology's expenditures. Interest on the exchangeable and development notes (together "the Notes") accrues at 7% per annum, but no payment of interest or principal is required until maturity on April 27, 2007.

Effective April 27, 2004, the exchangeable note can be converted, at the holders option, into common shares of the Company at US$5.71 per share and the development note can be converted at US$5.07 per share. Upon maturity on April 27, 2007, repayment of the outstanding principal and interest on the Notes can be made, at the Company's sole discretion, in cash or by issuance of the Company's common shares based on the market price of the shares at the time of maturity.

In April 2004, Elan assigned the Notes to a group of institutional investors. The terms and conditions of the Notes remain unchanged.

In April 2004, the Company received regulatory approval to issue a total of 7,342,614 shares to provide for full coverage on the conversion of the Notes at the option of the holders, including all cumulative interest to the maturity date of April 27, 2007.

11 | COLLABORATIVE AGREEMENTS:

a | Enzon Pharmaceuticals, Inc. ("Enzon")

On January 19, 2004, the Company entered into a strategic partnership with Enzon Pharmaceuticals, Inc. ("Enzon") to develop and commercialize Marqibo (formerly referred to as Onco TCS). On March 16, 2005, the Company signed an agreement with Enzon to terminate the strategic partnership with the Company (see note 21).

Under the terms of the strategic partnership, Enzon received the exclusive North American commercialization rights for Marqibo for all indications. In exchange, the Company received a non-refundable US$12.0 million up-front payment in January 2004.

There were multiple elements to the partnership agreement with Enzon. The up-front non-refundable US$12,000,000 payment received from Enzon had been attributed to the various elements within the agreement and has been deferred and is being amortized into revenue in accordance with the Company's revenue recognition policy. US$2,000,000 of the up-front payment was amortized into the Company's revenue over the first half of 2004, and the remaining up-front payment of US$10,000,000 is being recognized as revenue equally over six years. At December 31, 2004, $11,155,715 (US$8,420,678) of the up-front payment is recorded as deferred revenue and $4,741,882 (US$3,579,322) is recognized as licensing fees and milestone payments revenue for the year.

The Company recorded $6,091,405 (US$4,816,213) of research and development collaborations revenue from Enzon for Enzon's equal share of the ongoing development costs of Marqibo.

The Company incurred costs of $1,196,364 associated with entering into the partnership with Enzon. These costs were deferred and were being amortized into expense over the same period as the US$12,000,000 up-front payment that they relate to. At December 31, 2004, $996,970 of these costs were recorded as other assets and $199,394 were recognized as an expense in the statement of operations for the year.

b | Elan Corporation, plc ("Elan"):

On April 27, 2001, the Company and Elan entered into an agreement to form a joint venture, IE Oncology, for the development and commercialization of the Company's lead product, Marqibo. Pursuant to the joint venture agreement, the Company held an 80.1% interest and Elan held a 19.9% interest in IE Oncology. As part of this transaction, IE Oncology licensed certain medical technology from Elan (note 8). The Company's share of IE Oncology's licensing cost of the Elan medical technology was funded by an US$12,015,000 exchangeable note (note 10), payable to Elan. Also, on April 27, 2001, under the terms of its agreement with Elan, the Company issued 1,322,644 common shares to Elan for net cash proceeds of $7,696,284. On April 3, 2003, the Company entered into a Termination Agreement (note 4) to regain 100% ownership of its lead product candidate, Marqibo, by reacquiring the 19.9% interest of IE Oncology held by Elan. On January 19, 2004, the Company entered into a strategic partnership with Enzon Pharmaceuticals, Inc. to develop and commercialize Marqibo.

c | GlaxoSmithKline ("GSK"):

The Company and GSK entered into an agreement in November 2001 to develop GSK's anticancer drug, topotecan hydrochloride, with the Company's proprietary sphingosomal drug delivery technology. However, GSK had experienced a number of technical problems in manufacturing the necessary supply of materials needed for clinical trials, and these problems delayed the program. The Company announced on August 4, 2004 that GSK had decided to terminate the agreement to develop INX-0076. The termination took effect on September 1, 2004. In September, upon the delivery of certain documentation required under the agreement, GSK made a final milestone payment of US$0.75 million. This was the only payment from GSK in 2004 and brings the total up-front and milestone payments since the agreement's inception to US$6.0 million.

During the year ended December 31, 2004, the Company has recorded revenue of $1,796,528 (US$1,305,556) (2003 – $2,921,400 (US$2,000,000)) for milestone payments received from GSK under the agreement.

d | Esperion Therapeutics, Inc. ("Esperion"):

The Company entered into a licensing agreement with Esperion dated March 16, 1999, and subsequently amended on October 23, 2000, under which Esperion licensed certain of the Company's intellectual property for the treatment of atherosclerosis. Under this agreement the Company is entitled to license fees and milestone payments, aggregating US$6,550,000. As at December 31, 2004 and 2003, the Company had received an aggregate of $531,980 (US$350,000) from the Esperion licensing agreement, of which nil was received in 2004 (2003 – nil). In addition, the Company is entitled to royalties on product revenue, if any, on products utilizing the licensed intellectual property.

e | Aradigm Corporation ("Aradigm"):

The Company entered into a licensing agreement with Aradigm on December 8, 2004, under which Aradigm licensed certain of the Company's sphingosomal technology for delivery of Ciprofloxacin using Aradigm's device to meet requirements of the Canadian Department of National Defence. Under this agreement, the Company is entitled to license fees and milestone payments aggregating US$5,700,000. As at December 31, 2004, the Company had not received any payments under the agreement. In addition, the Company is entitled to royalties on product revenue, if any, on products utilizing the licensed intellectual property.

12 | GOVERNMENT GRANTS:

Government grants of $361,581 (2003 – $282,619) have been netted against research and development expenses.

13 | RESTRUCTURING COSTS:

In December 2004, following the December 1, 2004 Oncologic Drugs Advisory Committee vote to not support accelerated approval for Marqibo as a treatment for relapsed aggressive non-Hodgkin's lymphoma, the Company scaled back certain of its activities and implemented a workforce reduction of approximately 62% or 103 employees. The following table summarizes restructuring costs recorded in the consolidated statement of operations for the year ended December 31, 2004:

		2004
Employee severance compensation [(i)]	$	5,599,992
Cancellation of unvested stock options for severed employees [(ii)]		(1,213,996)
Laboratory equipment impairment loss [(iii)]		727,157
	$	5,113,153

[(i)] In accordance with EIC 134 – *Accounting for Severance and Termination Benefits*, the Company has recorded a severance compensation expense for former employees of $5,599,992 of which $396,579 was paid in December 2004, leaving a balance of $5,203,413 included in accounts payable and accrued liabilities at December 31, 2004. As at February 8, 2005, a further $4,163,472 had been paid out and the remaining balance at that date in the amount of $1,039,941 will be paid out over the next 2 years.

[(ii)] The cancellation of unvested stock options for severed employees resulted in the reversal of the stock-based compensation expense previously recorded on those options in the amount of $1,213,996.

[(iii)] The scaling back of activities has also rendered a portion of the Company's laboratory equipment surplus to requirements. The Company is currently completing an inventory of surplus equipment and has not yet obtained independent valuations for such equipment. Based on Management's estimates of the fair value of this surplus laboratory equipment, in accordance with Handbook section 3063 – *Impairment of Long-Lived Assets,* an impairment loss of $727,157 has been recognized.

14 | OBLIGATIONS UNDER CAPITAL LEASES:

The Company has laboratory equipment and office equipment under capital leases expiring at various dates through 2008. Future minimum payments under capital leases are as follows:

Year ending December 31:		
2005	$	121,480
2006		67,753
2007		67,753
2008		39,233
		296,219
Amount representing interest at approximately 7.3% to 9.3%		32,557
		263,662
Current portion		107,282
Long-term portion	$	156,380

Interest expense relating to obligations under capital leases for the year ended December 31, 2004 was $27,219 (2003 – $37,288).

15 | LONG-TERM DEBT:

The Company entered into a $3,200,000 equipment financing credit facility on December 18, 2003. Pursuant to draw-downs under this facility, the Company issued promissory notes to the lender as follows:

Draw-down date		Principal sum	Interest rate
December 18, 2003	$	1,147,002	5.25%
Total draw-downs at December 31, 2003		1,147,002	
March 31, 2004		727,074	4.23%
June 30, 2004		639,527	5.48%
Total draw-downs at December 31, 2004	$	2,513,603	

The promissory notes are to be repaid monthly over a three year period commencing the first day of the month following the date of draw-down. The promissory notes are collateralized by property and equipment with a net book value $991,930 (2003 – $954,291) and a non-interest bearing security deposit of $589,125 (2003 – $268,828) included in other long-term assets, that may be applied to the final monthly payments. The Company incurred $17,500 in financing costs on the arrangement, which is included in other long-term assets and is being amortized over the term of the debt through a charge to interest expense.

The future minimum payments are as follows:

Year ending December 31:		
2005	$	900,453
2006		900,453
2007		179,700
		1,980,606
Amount representing interest at 4.23% to 5.48%		109,976
		1,870,630
Current portion		825,428
Long-term portion	$	1,045,202

16 | COMMITMENTS AND CONTINGENCIES:

a | The Company is committed to future research and development expenses related to its clinical trials and research and development programs. In addition, the Company is committed to future research expenditures and license fees for the next five years of $227,000 annually from 2005 to 2006 and $93,000 annually from 2007 to 2009. In the case of certain of the research agreements, the Company has the right to terminate the research funding upon providing notice in advance of a predetermined period.

b | The Company has entered into various licensing agreements whereby, for access to intellectual property, it has agreed to pay royalties on future licensing and product revenue on certain products utilizing the in-licensed intellectual property.

c | The Company has entered into several long-term supply agreements that in some cases include minimum annual purchase commitments of new materials for its product candidates. The Company is committed to future minimum purchases for the next five years of $38,000 in 2005 and nil from 2006 to 2009. The Company has also committed to additional minimum annual purchase commitments that come into effect pending the outcome of certain future regulatory and commercialization events.

d | The Company has entered into an operating lease agreement for lab and office premises. The annual rent and operating costs are approximately $1,212,000. The lease expires in 2012 but can be terminated, at the Company's option, in 2007. The Company also has the option to extend the lease to 2017 and then to 2022, in which case rent would be adjusted to reflect the fair market rate as at the time of those extensions.

e | The Company entered into a Technology Partnerships Canada ("TPC") agreement with the Canadian Federal Government on November 12, 1999. Under this agreement, TPC agreed to fund 27% of the costs incurred by the Company, prior to March 31, 2004, in the development of certain oligonuncleotide product candidates up to a maximum contribution from TPC of $9,329,912. As at December 31, 2004, a cumulative contribution of $3,701,571 (2003 – $3,663,615) has been earned under this agreement. The Company does not expect any further funding under this agreement. In return for the funding provided by TPC, the Company agreed to pay royalties on the share of future licensing and product revenue, if any, that is received by the Company on its oligonuncleotide product candidates covered by the funding under the agreement. These royalties are payable until a certain cumulative payment amount is achieved or until a pre-specified date. In addition, until a cumulative amount equal to the funding actually received under the agreement has been paid to TPC, the Company agreed to pay royalties on the share of future product revenue, if any, for Marqibo that is received by the Company.

17 | INCOME TAXES:

Income tax expense (recovery) varies from the amounts that would be computed by applying the combined Canadian federal and provincial income tax rate of 35.6% (2003 – 37.6%) to loss before income taxes as shown in the following table:

	2004	2003
Computed taxes (recoveries) at Canadian federal and provincial tax rates	**$ (12,004,278)**	$ (14,926,000)
Differences due to lower tax rates in foreign jurisdictions	**1,094,101**	12,294,000
Permanent and other differences	**(1,260,823)**	(1,391,000)
Change in valuation allowance	**12,171,000**	4,023,000
Income tax expense	**$ –**	$ –

As at December 31, 2004, the Company has investment tax credits available to reduce Canadian federal income taxes and provincial income taxes of future years, which expire as follows:

	Federal investment tax credits	Provincial investment tax credits
2005	$ 75,000	$ –
2006	1,116,000	–
2007	1,653,000	–
2008	1,986,000	–
2009	1,512,000	–
2010	1,327,000	604,000
2011	2,516,000	1,225,000
2012	4,558,000	1,837,000
2013	4,262,000	2,100,000
2014	3,526,000	1,800,000
	$ 22,531,000	$ 7,566,000

At December 31, 2004, the Company has scientific research and experimental development expenditures of approximately $60,270,000 available for indefinite carryforward and $12,170,000 of net operating losses which can be used to offset future taxable income in Canada. These losses expire in 2011.

At December 31, 2004, the Company has net operating losses relating to its foreign subsidiaries of $2,840,000 for United States income tax purposes and $70,180,000 for Barbados income tax purposes. These losses expire in various amounts commencing in 2010.

Significant components of the Company's future tax assets as of December 31 are shown below:

	2004	2003
Future tax assets:		
Non-capital loss carryforwards	**$ 7,081,000**	$ 2,610,000
Research and development deductions	**21,456,000**	17,629,000
Book amortization in excess of tax	**1,196,000**	332,000
Share issue costs	**558,000**	965,000
Tax value in excess of accounting value in investment	**1,557,000**	1,557,000
Revenue recognized for tax purposes in excess of revenue recognized for accounting purposes	**3,186,000**	179,000
Provincial investment tax credits	**2,695,000**	2,286,000
Total future tax assets	**37,729,000**	25,558,000
Valuation allowance	**(37,729,000)**	(25,558,000)
Net future tax assets	**$ –**	$ –

The potential income tax benefits relating to these future tax assets have not been recognized in the accounts as their realization did not meet the requirements of "more likely than not" under the liability method of tax allocation. Accordingly, no future tax assets have been recognized as at December 31, 2004 and 2003.

18 | SEGMENTED INFORMATION:

The Company utilizes novel therapeutic compounds and proprietary drug delivery systems to commercialize improved therapies for the treatment of cancer and operates in one industry segment. The Company's revenue from research and development collaborations, licensing fees and milestone payments was earned from major collaborators based in the US.

The following information regarding the amounts of property and equipment and medical technology by geographic segments is based on the location of the physical assets, or based on the ownership rights for intangible assets:

	2004	2003
Property and equipment and medical technology:		
Barbados	$ 8,584,775	$ 2,051,361
Canada	4,188,482	9,440,042
	$ 12,773,257	$ 11,491,403

19 | NET CHANGE IN NON-CASH WORKING CAPITAL ITEMS:

	2004	2003
Accounts receivable	$ (1,727,567)	$ 280,322
Government grant receivable	70,000	32,849
Accrued revenue	(1,999,766)	–
Prepaid expenses and other assets	515,542	(332,726)
Accounts payable and accrued liabilities	5,108,956	(1,981,782)
Accrued interest on short-term investments	–	(15,729)
	$ 1,967,165	$ (2,017,066)

20 | SUPPLEMENTARY INFORMATION:

	2004	2003
a | Supplementary cash flow information:		
Income taxes paid	$ –	$ –
Interest paid	27,219	37,288
Non-cash transactions:		
Property and equipment acquired by assumption of capital lease obligations	–	203,406
b | Foreign exchange gain (loss):	$ 2,507,449	$ 7,601,045
c | Accounts payable and accrued liabilities is comprised of the following:		
Trade accounts payable	$ 1,118,402	$ 1,175,118
Research and development accruals	3,018,159	2,734,161
Professional fee accruals	274,162	187,213
Restructuring cost accruals	5,203,413	–
Other accrued liabilities	330,321	739,009
	$ 9,944,457	$ 4,835,501

21 | SUBSEQUENT EVENT:

On March 17, 2005, the Company announced that it had reached an agreement with Enzon that terminated the strategic partnership with the Company (see note 11(a)) effective immediately. Following the December 1, 2004 Oncologic Drugs Advisory Committee vote to not support accelerated approval for Marqibo as a treatment for relapsed aggressive non-Hodgkin's lymphoma, resulting in a delay in the commercialization of Marqibo, Enzon advised the Company that Marqibo is no longer a strategic fit for Enzon's pipeline.

The Company has received payment for Enzon's share of development costs invoiced to December 31, 2004 and, as part of the termination, expects to receive Enzon's estimated share of future development expenses and certain milestone payments totaling US$5,000,000 of which US$1,663,699 (CDN$1,999,766) is included as accrued revenue in the consolidated balance sheet for the year ended December 31, 2004. Any payments received will be net of any applicable taxes attributable to the payment.

Corporate Directory

Board of Directors

Darrell J. Elliott [2, 3]
Chairman of the Board (INEX)
Senior Vice President
MDS Capital Corp.
Vancouver, BC

David J. Main, M.B.A. [2]
President and
Chief Executive Officer
Inex Pharmaceuticals Corporation
Burnaby, BC

Pieter R. Cullis, Ph.D.
Vancouver, BC

K. Michael Forrest [1, 2]
Hillsborough, CA

Gary Frashier [2, 3]
President & Principal
Management Associates
San Antonio, TX

James Hudson [1]
Vancouver, BC

M. Blake Ingle, Ph.D. [3]
General Partner
Inglewood Ventures LP
San Diego, CA

Donald J. McCarren, Ph.D. [3]
President
D&A Consulting, Inc.
Louden, TN

James J. Miller, Ph.D. [1, 2]
Managing Director
NDI Capital
Vancouver, BC

[1] *Audit Committee*

[2] *Corporate Governance and Nominating Committee*

[3] *Executive Compensation & Human Resources Committee*

Management

David J. Main, M.B.A.
President and
Chief Executive Officer

Alexandra D. J. Mancini, M.Sc.
Senior Vice President,
Clinical and Regulatory Affairs

Thomas B. MacRury, Ph.D.
Senior Vice President,
Commercial Operations

Timothy M. Ruane, M.B.A.
Senior Vice President,
Corporate Development

Ian C. Mortimer, M.B.A.
Vice President, Finance and
Chief Financial Officer

Transfer Agent and Registrar

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Communications concerning transfer requirements, lost certificates, estate transfers, changes of address and other similar inquiries should be addressed to the Transfer Agent and Registrar.

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Company Contact

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Stock Listing

Inex Pharmaceuticals Corporation Common Shares are traded on the Toronto Stock Exchange under the symbol IEX.

Dividends

The company has not paid any cash dividends on the common stock since its inception.

Annual General Meeting

The Annual General meeting of shareholders will be held at 1:30 p.m. (PST) on May 10, 2005 at the Hyatt Regency Hotel, 655 Burrard Street, Vancouver, British Columbia, Canada.

Inex Pharmaceuticals Corporation

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