

Medicago Inc.

Interim Consolidated Financial Statements
(unaudited)
September 30, 2010

Medicago Inc.

Consolidated Balance Sheets (unaudited)

	September 30, 2010 \$	December 31, 2009 \$
Assets		
Current assets		
Cash and cash equivalents	7,197,025	228,039
Short-term investments (note 3)	7,475,360	14,105,198
Accounts receivable	346,910	300,566
Investment tax credits receivable	3,138,826	2,097,274
Grants receivable	-	37,272
Prepaid expenses	67,748	96,848
	<hr/>	<hr/>
	18,225,869	16,865,197
Security deposits on leases agreements , from 0.30% to 1.10%, maturing until September 2011	397,288	50,000
Property, plant and equipment	5,972,535	4,941,092
Intangible assets	<hr/>	<hr/>
	1,581,703	974,045
	<hr/>	<hr/>
	26,177,395	22,830,334
Liabilities		
Current liabilities		
Bank loans	600,000	600,000
Accounts payable and accrued liabilities	2,444,326	2,301,518
Deferred grants	7,222,561	340,203
Current portion of long-term debt	72,414	83,862
	<hr/>	<hr/>
	10,339,301	3,325,583
Long-term debt	<hr/>	<hr/>
	15,548,577	15,404,017
	<hr/>	<hr/>
	25,887,878	18,729,600
Shareholders' Equity		
Share capital (note 4)	53,746,214	48,660,207
Contributed surplus	1,560,777	1,554,679
Other equity components (note 5)		
Stock option plan (note 5a)	1,322,174	956,444
Unit options (note 5b)	882,661	399,536
Warrants (note 5c)	10,933,785	8,919,515
Deficit	(68,171,654)	(56,395,186)
Accumulated other comprehensive income	<hr/>	<hr/>
	15,560	5,539
	<hr/>	<hr/>
	289,517	4,100,734
	<hr/>	<hr/>
	26,177,395	22,830,334
	<hr/>	<hr/>

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

Approved by the Board of Directors

(signed) RANDAL CHASE, PH.D.

Director

(signed) ANDREW J. SHELDON

Director

Medicago Inc.

Interim Consolidated Statements of Earnings and Comprehensive loss For the nine-month period ended September 30, 2010 and 2009 (unaudited)

	Three-month period ended September 30,		Nine-month period ended September 30,	
	2010 \$	2009 \$	2010 \$	2009 \$
Revenues				
Revenues from research agreements	-	-	34,345	-
	<u>-</u>	<u>-</u>	<u>34,345</u>	<u>-</u>
Expenses				
Research and development	3,533,446	2,059,422	8,956,355	5,283,945
Research grants and contributions	(149,649)	(117,589)	(805,553)	(207,513)
Research and development tax credits	(731,857)	(120,284)	(1,041,552)	(393,284)
General and administrative, business development and intellectual property	771,547	866,261	2,866,955	2,614,679
Stock-based compensation	128,221	111,342	370,284	350,649
Exchange (gain) loss	2,789	(16,458)	14,022	(36,396)
Depreciation of property, plant and equipment	242,375	117,434	623,134	332,566
Amortization of intangible assets	23,203	13,297	60,989	40,252
Gain on sale of available-for-sale investments	-	(9,643)	(6,690)	(82,338)
Financial expenses, net (note 6)	284,294	259,037	772,869	681,530
	<u>4,104,369</u>	<u>3,162,819</u>	<u>11,810,813</u>	<u>8,584,090</u>
Loss for period	<u>(4,104,369)</u>	<u>(3,162,819)</u>	<u>(11,776,468)</u>	<u>(8,584,090)</u>
Basic and diluted loss per share (note 10)	<u>(0.03)</u>	<u>(0.03)</u>	<u>(0.09)</u>	<u>(0.09)</u>
Comprehensive Income (loss)				
Loss for period	(4,104,369)	(3,162,819)	(11,776,468)	(8,584,090)
Unrealized gain on available-for-sale investments	10,472	31,593	16,711	207,179
Reclassification of gain on available-for-sale investments realized upon sale to loss for the period	-	(9,643)	(6,690)	(82,338)
	<u>10,472</u>	<u>21,950</u>	<u>(10,021)</u>	<u>124,841</u>
Comprehensive loss for period	<u>(4,093,897)</u>	<u>(3,140,869)</u>	<u>(11,766,447)</u>	<u>(8,459,249)</u>

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

Medicago Inc.

Interim Consolidated Statements of Deficit, Accumulated Other Comprehensive Loss and Contributed Surplus

For the nine-month period ended September 30, 2010 and 2009

(unaudited)

	Nine-month period ended September 30,	
	2010	2009
	\$	\$
Deficit		
Balance – Beginning of period	(56,395,186)	(43,920,364)
Loss for period	(11,776,468)	(8,584,090)
Balance – End of period	<u>(68,171,654)</u>	<u>(52,504,454)</u>
Accumulated other comprehensive income (loss)		
Balance – Beginning of period	5,539	(48,384)
Other comprehensive income	10,021	124,841
Balance – End of period	<u>15,560</u>	<u>76,457</u>
Total deficit and accumulated other comprehensive loss	<u>(68,156,094)</u>	<u>(52,427,997)</u>
Contributed Surplus		
Balance – Beginning of period	1,554,679	1,087,608
Stock options forfeited	2,127	7,883
Unit options forfeited	-	66,640
Warrants forfeited	3,971	392,548
Balance – End of period	<u>1,560,777</u>	<u>1,554,679</u>

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

Medicago Inc.

Interim Consolidated Statements of Cash flows

For the nine-month period ended September 30, 2010 and 2009

(unaudited)

	Three-month period ended September 30,		Nine-month period ended September 30,	
	2010 \$	2009 \$	2010 \$	2009 \$
Cash flows from operating activities				
Loss for the period	(4,104,368)	(3,162,819)	(11,776,468)	(8,584,090)
Items not affecting cash and cash equivalents				
Stock-based compensation costs	128,221	111,342	370,284	350,649
Depreciation and amortization	265,123	130,731	684,123	372,818
Amortization of deferred charges	29,375	29,375	88,125	88,125
Gain on sale of available-for-sale investments	-	(9,643)	(6,690)	(82,338)
Interest capitalized on long-term debt	30,833	33,128	92,498	99,514
	(3,650,361)	(2,867,886)	(10,548,128)	(7,755,322)
Change in non-cash working capital items (note 7a)	5,927,202	(24,323)	6,119,744	(62,139)
	2,276,841	(2,892,209)	(4,428,384)	(7,817,461)
Cash flows from financing activities				
Bank loans contracted	-	-	-	258,870
Long-term debt contracted	-	-	33,608	46,820
Payments on long-term debt	(67,392)	(72,097)	(81,119)	(84,087)
Issuance of units	7,500,000	-	7,500,000	-
Exercise of options	-	-	3,800	-
Exercise of warrants	-	2,018,938	860,875	2,060,063
Issue expenses	(779,729)	-	(779,729)	(83,290)
	6,652,879	1,946,841	7,537,435	2,198,376
Cash flows from investing activities				
Acquisitions of short-term investments	(6,445,907)	-	(9,187,420)	-
Dispositions of short-term investments	4,011,752	922,078	15,486,681	6,871,251
Additions to property, plant and equipment	(616,524)	(358,154)	(1,654,577)	(595,935)
Additions to intangible assets	(232,646)	-	(784,749)	(51,578)
	(3,283,325)	563,924	3,859,935	6,223,738
Net change in cash and cash equivalents	5,646,395	(381,444)	6,968,986	604,653
Cash and cash equivalents – Beginning of period	1,560,630	2,077,444	228,039	1,091,347
Cash and cash equivalents – End of period	7,197,025	1,696,000	7,197,025	1,696,000
Additional information				
Interest paid	243,135	191,952	665,344	658,485

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

Medicago Inc.

Notes to Interim Consolidated Financial Statements

September 30, 2010

(unaudited)

1 Interim financial information

The financial information for the nine-month periods ended September 30, 2010 and 2009 are unaudited. However, in the opinion of management, all adjustments necessary to present fairly the results of these periods have been recorded. The adjustments made were of a normal recurring nature. The results of the interim periods are not necessarily indicative of results which may be expected for any other interim period or for the full year.

The unaudited interim consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles (GAAP), using the same accounting policies as the audited consolidated financial statements for the year ended December 31, 2009. All disclosures required for annual financial statements have not been included in these financial statements. These consolidated financial statements should be read in conjunction with the Company's most recent annual consolidated financial statements.

2 New accounting standards

Future accounting changes

In January 2009, the CICA published the following sections of the CICA Handbook that apply to interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011.

- (a) Section 1582, "Business Combinations", which replaces the former Section 1581 with the same title, establishes accounting standards for a business combination. It provides the Canadian equivalent to International Financial Reporting Standard IFRS3 Revised, "Business Combinations".
- (b) Section 1601, "Consolidated Financial Statements", which replaces the former Section 1600 with the same title, establishes standards for the preparation of consolidated financial statements.
- (c) Section 1602, "Non-Controlling Interests". This new section establishes standards on accounting for non-controlling interests in a subsidiary in consolidated financial statements prepared subsequent to a business combination. It is equivalent to the corresponding provisions of International Accounting Standard IAS 27, "Consolidated and Separate Financial Statements".

The Company is currently evaluating the impact of these new standards on its financial statements.

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Notes to Interim Consolidated Financial Statements

September 30, 2010

(unaudited)

3 Short-term investments

	September 30, 2010 \$	December 31, 2009 \$
Term deposits bearing interest at annual rates ranging from 1.00% to 1.49%, maturing until September 2011	4,095,000	9,600,000
Bonds and discount notes, bearing interest at effective annual rates ranging 3.70% , maturing until June 2012	3,293,446	3,248,485
Money market funds	86,914	1,256,713
	<u>7,475,360</u>	<u>14,105,198</u>

4 Share capital

- Authorized
 - Unlimited number of shares, without par value, of the following classes:
 - Common shares, voting and participating
 - Preferred shares, with rights, privileges and conditions to be determined by the Board of Directors before issuance.

The share capital issued has varied as follows:

	<u>Nine-month period ended September 30, 2010</u>		<u>Year ended December 31, 2009</u>	
	Number	\$	Number	\$
Common shares				
Balance – Beginning of period	114,771,690	48,660,207	90,324,940	37,182,667
Issued pursuant to the payment of a commitment fee	154,393	67,161	-	-
Issued pursuant to a public offering	18,518,520	4,802,771	16,100,000	9,980,328
Issued pursuant to the exercise of warrants	3,443,500	1,072,076	8,346,750	2,853,892
Issued pursuant to the exercise of stock options	18,999	6,225	-	-
Issue expenses *	-	(862,226)	-	(1,356,680)
Balance – End of period	<u>136,907,102</u>	<u>53,746,214</u>	<u>114,771,690</u>	<u>48,660,207</u>

Medicago Inc.

Notes to Interim Consolidated Financial Statements

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* Issue expenses were shared out between common shares and warrants pro rata to their fair value.

- (i) On August 6, 2010, the Company issued 154,393 shares for the payment of a commitment fee of \$75,000 following the execution of a standby equity distribution agreement on May 13, 2010.

The Company granted 200,000 non-transferable warrants to an agent entitling to subscribe, before August 6, 2011, for 200,000 shares at a price of \$0.50. (note 5c).

- (ii) On August 19, 2010, the Company issued 18,518,520 units at a price of \$0.405 per unit for total gross proceeds of \$7,500,000 (the '2010 Offering'). Each unit consists of one common share of the Company and 0.75 common share purchase warrant. Each warrant entitles the holder thereof to purchase one common share at a price of \$0.50 for five years following the issuance of the warrant.

The gross proceeds of the 2010 Public Offering amounting to \$7,500,000 are shared out between the 18,518,520 common shares for a gross amount of \$4,802,771 and the 13,888,890 warrants attached to each unit for a gross amount of \$2,697,229 (note 5c). In connection with this financing, the Company paid a cash compensation equivalent to 6.5% of the gross proceeds of the financing, being \$487,500. The Company also granted non-transferable unit options to the agents entitling to subscribe, before August 19, 2012, for 1,203,704 units at a price of \$0.405 per unit as financing expenses (note 5b). Each unit consists of one common share of the Company and 0.75 common share purchase warrant. Each warrant entitles the holder thereof to purchase one common share at a price of \$0.50. The issue expenses for the Company regarding this financing totalled \$ 1,347,229.

Equity distribution agreement

On May 13, 2010, Medicago has entered into a standby equity distribution agreement (SEDA) with YA Global Master SPV Ltd., a fund managed by Yorkville Advisors, LLC. In accordance with the terms of the SEDA, Medicago will have the right, from time to time during a period of up to 36 months from the date of the SEDA, to issue and sell to YA Global, and YA Global undertakes to acquire from Medicago, common shares for a maximum total consideration of \$10-million upon exercise by Medicago of a drawdown. The maximum amount of a drawdown will be the lesser of \$500,000 or the remaining portion of the commitment amount. The purchase price of the common shares issued under the SEDA will be: (i) 95 per cent of the relevant daily volume-weighted average price per common share for the applicable day if such average daily price is equal to or greater than 20 cents; (ii) 92.5 per cent of the relevant average daily price of the common shares if such average daily price is equal or greater than 15 cents but less than 20 cents; and (iii) 90 per cent of the relevant average daily price of the common shares if such average daily price is equal to or greater than 10 cents but less than 15 cents.

The Company has not used the SEDA since its implementation.

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5 Other equity components

(a) Stock option plan

The following table summarizes the stock option activity since January 1, 2009:

	For the nine-month period ended September 30, 2010			For the year ended December 31, 2009		
	Number	Carrying value \$	Weighted average exercise price \$	Number	Carrying value \$	Weighted average exercise price \$
Outstanding – Beginning of period	7,091,592	956,444	0.55	2,344,595	500,081	0.89
Granted	415,000	-	0.52	4,797,830	-	0.39
Exercised	(18,999)	(2,427)	0.20	-	-	-
Forfeited	(50,981)	(2,127) *	0.38	(50,833)	(7,883) *	0.83
Expired	(308,559)	-	1.11	-	-	-
Compensation costs for the period	-	370,284	-	-	464,246	-
Outstanding – End of period	7,128,053	1,322,174	0.53	7,091,592	956,444	0.55
Options exercisable – End of period	3,551,779		0.59	2,709,094		0.75

* During the nine-month period ended September 30, 2010, 50,981 stock options were forfeited (50,883 in 2009). The corresponding credit amounting to \$2,127 (\$7,883 in 2009) has been recorded as contributed surplus.

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The following table summarizes information about outstanding and exercisable stock options as at September 30, 2010:

Exercise price	Stock options outstanding			Stock options currently exercisable	
	Number	Weighted average remaining contractual life (months)	Weighted average exercise price \$	Number	Weighted average exercise price \$
\$0.20	2,000,317	39	0.20	665,210	0.20
\$0.355	1,420,000	39	0.355	1,189,999	0.355
\$0.37	223,674	35	0.37	149,116	0.37
\$0.52 to \$0.66	1,244,794	60	0.60	528,219	0.65
\$0.72	1,220,033	111	0.72	-	-
\$1.00 to \$1.11	867,147	11	1.01	867,147	1.01
\$1.68	152,088	9	1.68	152,088	1.68
	7,128,053	51	0.53	3,551,779	0.59

Assumptions used in determining stock-based compensation costs

The table below shows the assumptions used in determining stock-based compensation costs under the Black-Scholes option pricing model:

	Nine-month Ended September 30, 2010	For the year Ended December 31, 2009
Dividend yield	Nil	Nil
Expected volatility	121.5%	98.74%
Risk-free interest rate	2.86%	2.01%
Expected life (years)	5.00	4.97
Weighted average fair value of options granted at market price at the date of the grant (\$)	0.44	0.41
Weighted average fair value of options granted at a price higher than the market price at the date of the grant (\$)	-	0.23
Stock-based compensation costs (\$)	370,284	464,246

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(unaudited)

(b) Unit options

The following table summarizes the unit option activity since January 1, 2009:

	For the nine-month period ended September 30, 2010			For the year ended December 31, 2009		
	Number	Carrying value \$	Weighted average exercise price \$	Number	Carrying value \$	Weighted average exercise price \$
Outstanding and exercisable – Beginning of period	1,127,000	399,536	0.72	280,000	66,640	0.50
Granted to the agent pursuant to a public offering	1,203,704	483,125	0.405	1,127,000	399,536	0.72
	-	-	-	(280,000)	(66,640)	0.50
Outstanding and exercisable – End of period	2,330,704	882,661	0.56	1,127,000	399,536	0.72

* During fiscal 2010, 0 unit options expired (280,000 in 2009). The corresponding credit amounting to \$ 0 (\$66,640 in 2009) has been recorded as contributed surplus.

The following table summarizes information about unit options outstanding and exercisable as at September 30, 2010:

Exercise price	Number	Weighted average remaining contractual life (years)
\$0.405	1,203,704	1.88
\$0.72	1,127,000	0.17
	2,330,704	1.05

Medicago Inc.

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(unaudited)

The fair value of unit options was estimated using the Black-Scholes valuation model with the following assumptions:

	2010	2009
Dividend yield	Nil	Nil
Expected volatility	115.39%	119.55%
Risk-free interest rate	1.39%	0.54%
Expected life (years)	2	1
Fair value of unit options granted (\$)	0.401	0.354

(c) Warrants

The following table summarizes the warrant activity since January 1, 2009:

	For the nine-month period ended September 30, 2010			For the year ended December 31, 2009		
	Number	Carrying value \$	Weighted average exercise price \$	Number	Carrying value \$	Weighted average exercise price \$
Outstanding and exercisable – Beginning of period	60,628,946	8,919,515	0.49	64,933,196	8,410,743	0.39
Granted to the subscribers in connection with public offering	13,888,890	2,697,229	0.50	8,050,000	1,611,672	1.00
Agent's fee in connection with Equity Distribution Agreement	200,000	17,216	0.50			
Exercised	(3,443,500)	(211,201)	0.25	(8,346,750)	(491,329)	0.28
Forfeited	(64,750)	(3,971)	0.25	(4,007,500)	(392,548)	0.75
Warrant issue expenses	-	(485,003)	-	-	(219,023)	-
Outstanding and exercisable – End of period	71,209,586	10,933,785	0.50	60,628,946	8,919,515	0.49

Medicago Inc.

Notes to Interim Consolidated Financial Statements

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(unaudited)

The following table summarizes the information relating to warrants outstanding and exercisable as at September 30, 2010:

Exercise price	Number	Weighted average remaining contractual life (years)
\$0.250	2,000,000	0.35
\$0.405	* 45,000,000	0.06
\$0.43	** 7,996,112	0.16
\$0.50	14,088,890	4.83
\$0.700	643,877	0.59
\$1.00	53,888	0.16
\$1.120	1,426,819	0.92
	<u>71,209,586</u>	<u>1.04</u>

* On October 20, 2010, 45,000,000 common share purchase warrants issued in October 2008 expired without being exercised.

** On October 21, 2010, the Company announced a reduction of the exercise price of warrants issued as part of the units offering by way of prospectus completed on November 27, 2009 from \$1.00 to \$0.43.

The fair value of warrants was estimated using the Black-Scholes valuation model with the following weighted average assumptions:

	2010	2009
Dividend yield	Nil	Nil
Expected volatility	118.74%	119.55%
Risk-free interest rate	2.15%	0.54%
Expected life (years)	4.94	1
Fair value of warrants granted (\$)	0.19	0.20

Medicago Inc.

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(unaudited)

6 Financial expenses, net

	Three-month period ended September 30,		Nine-month period ended September 30,	
	2010	2009	2010	2009
	\$	\$	\$	\$
Interest on long-term debt	252,536	236,628	717,295	735,879
Interest and bank charges	23,253	28,794	41,786	64,282
Amortization of deferred financing expenses	29,375	29,375	88,125	88,125
Interest income	(20,870)	(35,760)	(74,337)	(206,756)
	<u>284,294</u>	<u>259,037</u>	<u>772,869</u>	<u>681,530</u>

7 Additional information on cash flows

(a) Change in non-cash working capital items

	Three-month period ended September 30,		Nine-month period ended September 30,	
	2010	2009	2010	2009
	\$	\$	\$	\$
Accounts receivable, grants and financing receivable	(121,520)	(113,211)	(9,072)	(117,705)
Investment tax credits receivable	(731,857)	(120,284)	(1,041,552)	(393,284)
Prepaid expenses	(37,559)	(45,233)	29,100	(63,090)
Accounts payable and accrued liabilities	(189,772)	87,459	258,910	344,994
Deferred grants	7,007,910	166,946	6,882,358	166,946
	<u>5,927,202</u>	<u>(24,323)</u>	<u>6,119,744</u>	<u>(62,139)</u>

(b) Items not affecting cash related to financing and investing activities

	Nine-month Ended September 30, 2010	For the year Ended December 31, 2009
	\$	\$
Acquisition of intangible assets in accounts payable and accrued liabilities	-	116,102

Medicago Inc.

Notes to Interim Consolidated Financial Statements

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(unaudited)

8 Segment information

The Company is organized under one single business segment, being the research and development of vaccines. Substantially all of the Company's property, plant and equipment and intangible assets are located in Canada.

All revenues of the year have been allocated based on the location in which the sale originated. All of them have been generated in Canada.

9 Economic dependence

100% of the revenues for the nine-month period ended September 30, 2010 were with one customer.

10 Loss per share

The following table summarizes the reconciliation of the basic weighted average number of shares outstanding and the diluted weighted average number of shares outstanding used in the diluted earnings per share calculations:

	Three-month period ended September 30,		Nine-month period ended September 30,	
	2010	2009	2010	2009
Basic and diluted weighted average number of shares outstanding	126,782,457	92,369,576	120,290,042	91,022,673
Dilutive effect of stock options	1,168,826	1,710,999	1,520,879	706,144
Dilutive effect of warrants	746,019	14,784,998	6,520,497	1,353,868
Diluted weighted average number of shares outstanding	<u>128,697,302</u>	<u>108,865,573</u>	<u>128,831,418</u>	<u>93,082,685</u>
Excluded from the calculation where exercise price are greater than average market price				
Stock options	3,484,062	2,120,088	3,484,062	3,763,762
Warrants	69,209,586	2,070,696	24,209,586	47,070,696

For the three and nine-month periods ended September 30, 2010 and 2009, the diluted loss per share was the same as the basic net loss per share since the dilutive effect of stock options and warrants was not included in the calculation; otherwise the effect would have been anti-dilutive. Accordingly, the diluted loss per share for those periods was calculated using the basic weighted average number of shares outstanding.