Lorus Therapeutics Inc.

LORUS

Working Together™

1999 Annual Report

Science and Business

Many see a vast divide between science and business – separate values, different methods, divergent goals. We couldn't disagree more. Good science and good business have much in common and are at their best when they make each other stronger. Both need rigour, creativity and patience; both are motivated by tangible results and rewards, and at Lorus, both share the ultimate goal of triumph over cancer. > Lorus is science and business working together.™ >


We manage the science that manages cancer.™ Cancer will have no


silver bullet. This war will be won on many fronts. Lorus is leading


the trend to building critical mass in oncology in Canada. Our skill


in sourcing discoveries has yielded us some very promising products.

The Year's Highlights

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- ***Harvard Medical School Agreement – May 1998***

  This agreement deepens the research activity around clotrimazole, and several hundred related analogs. The agreement with Harvard also has the ability to act as a research engine screening new products that will feed the Lorus pipeline. With combined market potential of over CDN$1 billion, the line of novel cytostatic products (which are the property of our 80% owned NuChem Pharmaceuticals) have demonstrated the ability to stop cancer cells from dividing. The Harvard team leader, Dr. J.A. Halperin, is credited with the discovery of the anti-proliferative, anti-angiogenic and anti-metastatic properties of the parent molecule.

- ***Manufacturing Divestiture – December 1998***

  Lorus sold its Virulizin® manufacturing assets to a Canadian pharmaceutical company. This divestiture supports two strategic objectives: the first, to focus on drug development and the second, strict cash control. It also allowed Lorus to relocate to new premises, more supportive of our business.

Shares Outstanding: 42.7 million in this year

Established: 1986

May | June | July | August | September | October |

98

Public since: 1991

Shares Outstanding: 78.7 post GeneSense acquisition

- ***National Cancer Institute Collaboration – March 1999***

  On the basis of the *in vitro* anti-cancer activity of our NuChem compounds, the U.S. National Cancer Institute (NCI) has decided to allocate resources for the further development of NC 381, NC 383 and NC 384. This is an honour bestowed on fewer than 10% of the compounds the NCI evaluates.

- ***Alliance with Faulding Inc. for Virulizin® development – April 1999***

  Virulizin®, our most advanced cancer compound, moved a step closer to the approval phase with this agreement. Lorus and Faulding Canada, a leader in injectible oncology product sales, will collaborate to determine whether to file for approval in Canada this year. The use of Virulizin® as second line therapy on refractory pancreatic cancer patients is our first priority and represents a strong early revenue stream opportunity.

- ***Virulizin® profiled at American Association for Cancer Research (AACR) Annual Meeting – April 1999***

  On the strength of compelling animal and human results (animal work conducted by Changnian Liu, M.D., Ph.D. and Phase I/II trial conducted by Dr. Jules Harris), the AACR chose to feature Virulizin® as one of the most promising treatments for pancreatic cancer. "Our results show that the activity of Virulizin® against pancreatic cancer is comparable to that of the current best chemotherapeutic drug treatment and that it is well tolerated," said Dr. Liu. The vote of confidence from this prestigious organization has renewed our conviction that Virulizin® is both safe and effective, which in turn provides us with confidence going into the next phase of our development program.

- ***Letter of Intent to Acquire GeneSense Technologies – April 1999***

  The merging of Lorus and GeneSense supports the core strategy of Lorus to create one of the leading cancer biopharmaceutical companies in Canada, and furthers our intent to build a diversified pipeline of cancer therapies. Since 1996 GeneSense has focused on antisense technology, which works at the genetic level to interrupt the production of disease-causing proteins. With combined market potential of over CDN$2 billion, these antisense compounds have shown dramatic results in *in vivo* testing. The scientific capability of GeneSense's Dr. Jim A. Wright, who is now Lorus' President and Chief Scientific Officer, and his research team adds scientific depth to Lorus. We will also experience immediate synergies with GeneSense's lab facilities at the Sunnybrook Health Science Centre. This begins an exciting new phase for Lorus.

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Major Corporate Partners:
F.H. Faulding (Canada)

# of late stage products: 5

November | December | January | February | March | April |

Employees: 22

Total estimated annual market potential of proprietary products: >$3.0 billion

- ***HSBC Securities leads CDN$10 million financing for Lorus – Fall 1999***

  In addition to acting as advisor on the GeneSense transaction, HSBC represented Lorus in a major effort to raise funds to finance our research and development program. The reception and support from our shareholders and new investors reflect well on the scientific strengths and market potential of our product pipeline.

- ***Cost reductions – May 1999***

  Our cost vigilance has been richly rewarded through a reduction in general and administrative expenditures in the year. These savings have been achieved through the sale of our manufacturing function (and related staff transfers), our relocation to new offices offering more efficient space, and the constant drive to control expenditures without starving the development process.

Dear Shareholders

My personal goal for Lorus has been to take an organization created on the strength of one idea, and turn it into a mature, enduring force for cancer therapy. This year, we took giant steps toward that goal. There is momentum operating around us now. The world has taken note of the potential of our lead compound, Virulizin®; one of the most exciting antisense discoverers – GeneSense Technologies – has placed their trust in us to realize the possibilities in their work; and new investors have expressed their confidence by pledging millions of new dollars to support our efforts. These and other events of the year are an endorsement of Lorus, our science and our business model.

Delivering on our promises

The commitments we made last year, to our shareholders, investors and employees, are promises that we have kept. Last year we set out to build our product pipeline with breadth and depth, extend our reach through partnering agreements, and move Virulizin® one step closer to approval. All these, we did.

> **A diverse pipeline.** A truly balanced cancer therapy portfolio is not just multiple products but multiple technologies. This is both good science and good risk management. It is good science because cancer is a disease that is best treated with a range of therapies. Cancer cells can be attacked and limited in different ways, using different technologies. It is good business because a company built on the promise of multiple technologies spreads its risk more broadly. With this in mind, our acquisition of GeneSense Technologies and its two promising antisense products adds a third technology group to our pipeline. GTI 2040 has shown wide-ranging anti-cancer activity against a wide spectrum of cancers, with remarkable safety. GTI 2501 has shown a good safety profile and very strong activity against breast and renal cell carcinomas. These two products offer over CDN$2 billion in market potential. Add these antisense compounds to our immunotherapeutic (Virulizin®) and chemotherapeutic (NuChem) technologies and we now have three solid platforms and hundreds of potential anti-cancer products, addressing most of the major cancers.

"A truly balanced cancer therapy portfolio is not just multiple products but multiple technologies. This is both good science and good risk management"

> **An expanding network.** Our business model demands that we be in a constant state of forging new alliances and partnerships – to access new discoveries, to manufacture, to develop and to market our products. This year we added several new partners. Our deepening relationship with *Harvard Medical School* and the laboratory of Dr. J.A. Halperin has progressed into its next stage of preclinical development of two analogs. By February of 1999, the data from preclinical testing were positive with strong anti-cancer activity in several animal studies. *The U.S. National Cancer Institute* has elected to undertake independent animal trials of the NuChem novel compounds on the basis of outstanding *in vitro* results. Our NuChem analogs are manufactured under agreement by *Torcan Chemical* of Aurora, Ontario. *Faulding Canada Inc.* is now working with us to move Virulizin® through its final development stages in Canada and, possibly, Latin America. These alliances further extend our reach upstream into discoveries and downstream into manufacturing and marketing.

> **Advancement of Virulizin®.** It is now well accepted that Virulizin® is an effective immunotherapy with a safety profile superior to the current treatment options for pancreatic cancer. The recognition received from the American Association of Cancer Research and the popular and medical press was deeply gratifying and puts us in a strong position as Virulizin® moves into the approval and marketing stages. In certain countries Virulizin® is already improving the quality of life in cancer patients – that is why we are here.

Evidence that the science works...

The best cancer drugs do more than treat the disease; they are easy for the patient to take, they improve the quality of life, and are cost effective for the payer. That is a tall bill for a molecule that has performed *in vitro* against cancer cells – but it is what we demand. Our skill in sourcing and backing discoveries that meet these criteria has yielded us some products with extraordinary potential. Our antisense compounds have demonstrated complete regression of breast and renal tumors in mice with no signs of re-growth even after treatment is discontinued,

one of our NuChem analogs reduces colorectal cancer tumors in mice within days of oral administration, and Virulizin® is extending survival rates over existing best alternatives. The science is working.

...evidence that the business model works...

Our goal is to become Canada's leading anti-cancer drug development company. This rests on the success of a business model that is now receiving a potent endorsement – from the financial, scientific and pharmaceutical communities. We occupy the space between drug discovery and marketing – we develop drugs that come to us through our strong relationships with the scientific community. We have a balanced product portfolio, diversified across technologies, not just products – we are risk managers. We respect science *and* business and are at home in the lab and the boardroom – we are integrators.

Moving forward with clear intent

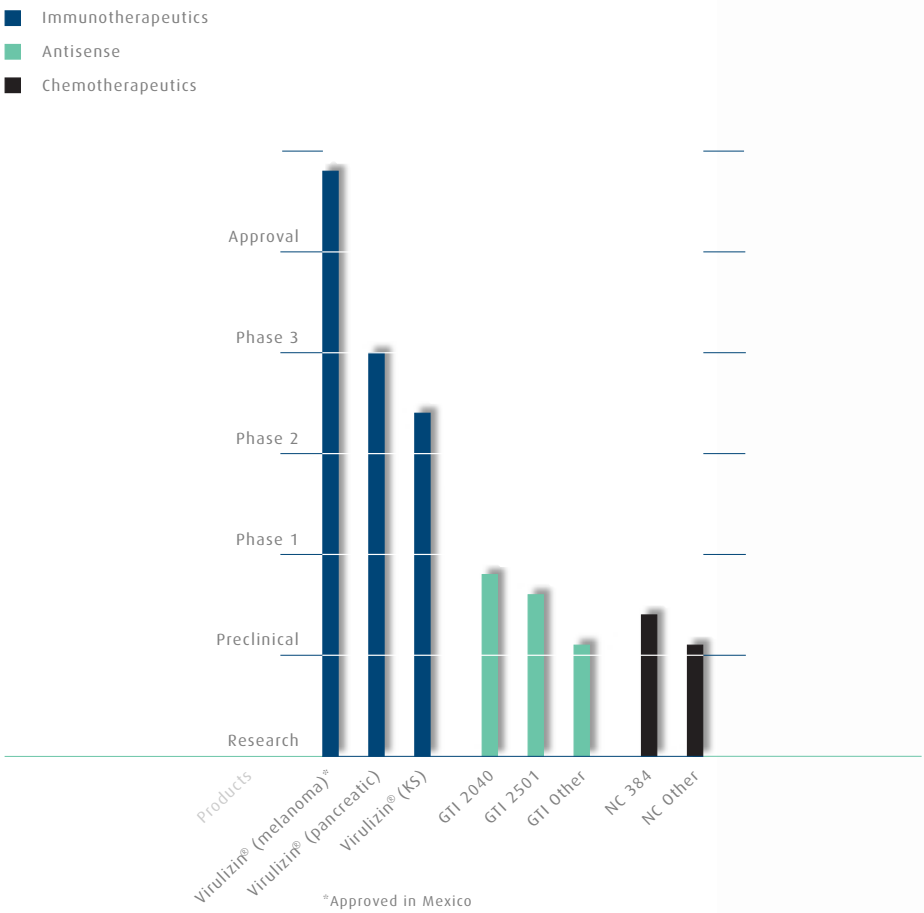
In the year ahead we are planning to move forward with all our major products: a NDS filing for the use of Virulizin® as a second line therapy in pancreatic cancer, the initiation of a Phase I clinical trial for our first antisense drug GTI 2040, the initiation of the toxicity studies for our second antisense drug GTI 2501 and for NC 384 and additional preclinical work on NC 381 and NC 383 as well as some activity in discussions with potential partners for Virulizin®.

> We will, as our first priority, integrate our recent merger with GeneSense Technologies to maximize the benefits of the synergy between Lorus and GeneSense. We will also be cautiously seeking out other opportunities to add to our pipeline and to grow the business. We will not, however, undertake any new initiatives that could slow down or detract from our existing programs.

> I would like to thank our shareholders, employees and corporate partners for their continued support and we look forward to a successful start to the new millennium.

Philippe G. Lacaille (signed)
President and Chief Executive Officer

Product Pipeline



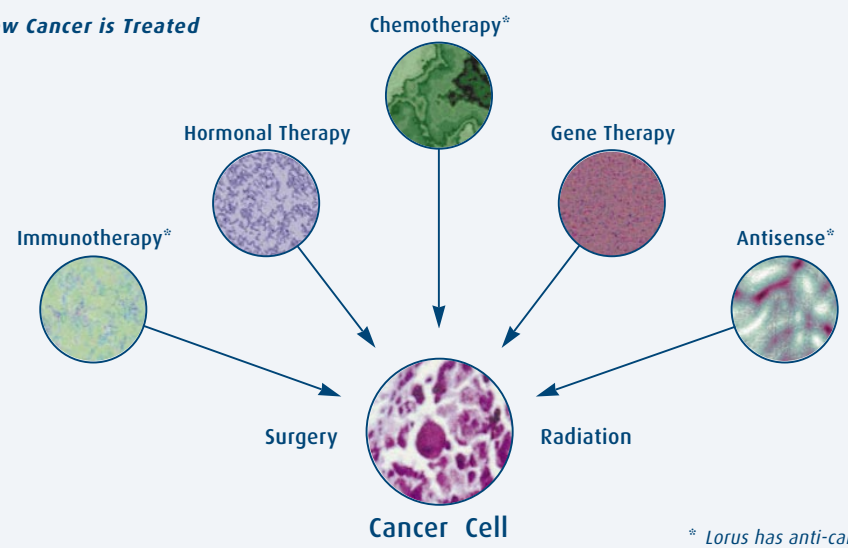
Lorus has successfully built a development pipeline with products that attack cancer using different technologies. These products could eventually be combined to better manage cancer and range from the research stage to marketing approval.

Lorus is the first hub for oncology drugs in Canada

The dramatic rise in the number of promising oncological discoveries is affecting the structure of our sector. Vastly increased competition from the micro and small-cap biotechnology firms for the capital required to fuel drug development is prompting consolidation into entities with critical mass. Companies with balanced pipelines and better risk profiles are better able to attract and manage long term funding and thereby bring new drugs to market. Lorus has embraced this consolidation as a business model to form the first hub for oncology drugs in Canada. The sector now has several key players:

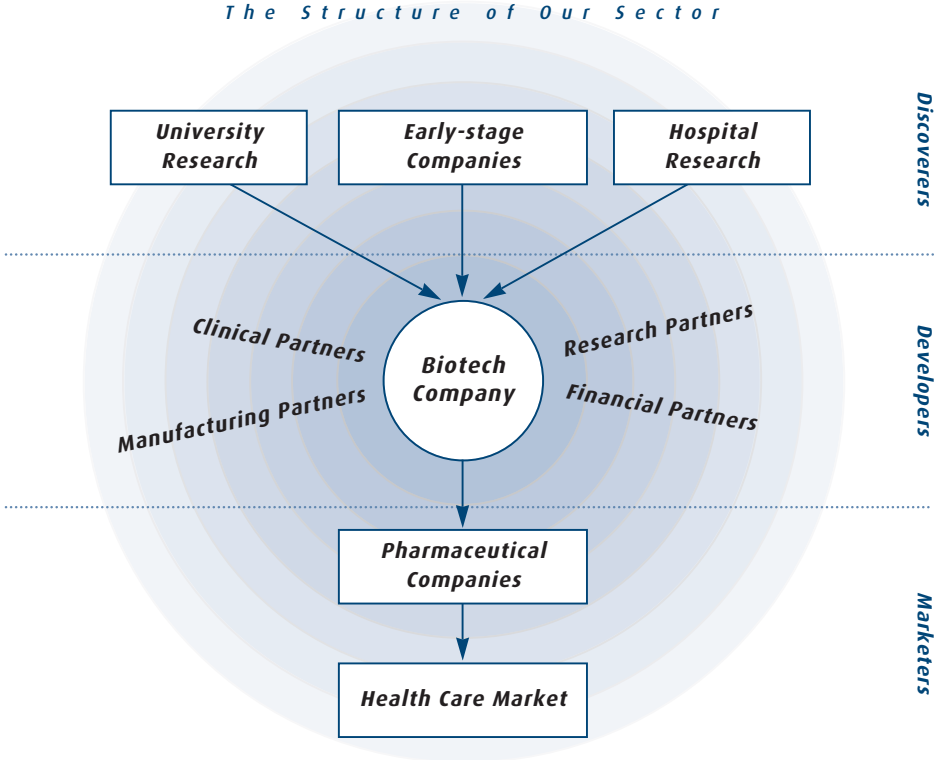
> **Discoverers,** the scientists who labour in universities, hospitals or as independent researchers, are one of the vital sources of new cancer therapy technologies. The pace of

How Cancer is Treated



* *Lorus has anti-cancer products in these areas*

The Structure of Our Sector

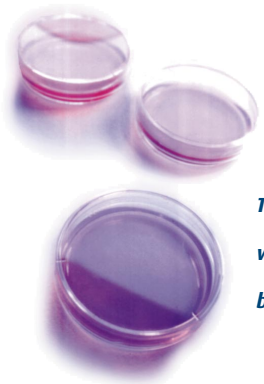


discovery in oncology has increased dramatically in the last 10 years as the number of platform technologies increases. Traditionally, this community has relied on the pharmaceutical companies to take on the research and development processes required to move products to patients.

> **Developers** are a vital link between discovery and distribution. By selecting and backing a portfolio of cancer discoveries and advancing them through Phase II clinical trials, developers are the source of more advanced cancer products – giving development support to scientists and acting as a source of compounds that have progressed through the development cycle. Developers add value by getting compounds to the stage of readiness for the long and expensive process of Phase III clinical trials, international approval and marketing.

> **Marketers,** the traditional multinational pharmaceutical companies that complete the development of, secure international registration for and market cancer drugs, can no longer carry the full burden of funding all the research and development for this flood of new discoveries. These companies must fill their pipelines with late stage drugs that show nearer term revenue potential. They are now relying on the drug developers to source and weed out and advance only the most promising discoveries.

> **Where does Lorus fit?** Through in-licensing of new products, consolidation of small biotechnology firms and forging of strategic partnerships, Lorus is creating a hub for cancer therapies made up of researchers, marketers, manufacturers and founders. Lorus is the first hub for oncology drugs in Canada and is leading the trend to building critical mass in this way. There is enormous value to be unlocked in this space between discovery and distribution as we drive, and benefit from, industry consolidation.



To create an enduring force in cancer drug development you need what Lorus has – a strong intellectual property platform, and the business acumen to make it happen.

It is our intention to become *the* hub for the development of anti-cancer therapies in Canada. We will do this on three key strengths:

❶ *Clear focus*

Our business is cancer therapy; our role is development. The clarity of this focus allows us to make better choices, build a better team of people, accumulate relevant expertise and send a stronger message to the financial community about our value. We will maintain this focus and use it to guide acquisitions, in-licensing and partnering decisions.

❷ *Sound structure*

As we have discussed, our business model is both good management and good science – it is the future of the bio-pharmaceutical industry. Managing our business model requires a unique set of talents – to keep the centre strong and to forge smart alliances that become the spokes in the wheel. We will add to the core team only if it brings a strategic skill vital to keeping the pipeline moving. We will only ally ourselves with researchers, manufacturers and marketers that share our commitment to oncology.

❸ *Depth in science and business*

Success in our business means one thing: shorter time-to-market of safe, efficacious and cost effective anti-cancer therapies. Speed is vital. What does it take to achieve this success? First, we must continue our record of shrewd sourcing and selection of new therapies. To do this we will foster and expand our excellent relationships with the academic and research communities across North America including the U.S. National Cancer Institute and Harvard Medical School. Second, we must use our experience in drug development to keep up the momentum on the most promising products, allocating resources where they will have the most impact.

Lorus Therapeutics Inc.
1999 Annual Report

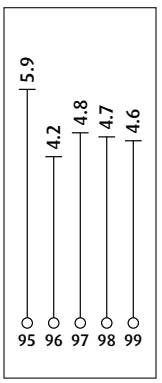
The Business at Work

Science and Business
Working Together™

Management's Discussion and Analysis of Operations and Financial Conditions

The following discussion and analysis for the years ended May 31, 1999, 1998 and 1997 should be read in conjunction with the audited consolidated financial statements of the Company included in this Annual Report.

Loss for the Period
(in millions of dollars)



Lorus Therapeutics Inc. is a Canadian biopharmaceutical company focused on the development of cancer therapies. Lorus' goal is to capitalize on its pre-clinical, clinical and regulatory expertise by developing new drug candidates that can be used, either alone, or in combination, to successfully manage cancer. Through an active acquisition and in-licensing program, Lorus is building a portfolio of promising anti-cancer drugs. Late stage clinical development and marketing will be done in co-operation with strategic pharmaceutical partners.

To date, Lorus has invested a substantial portion of its financial and human resources in the development of Virulizin®, a biological immunotherapeutic drug for the treatment of cancer, and in the development of the NuChem Analogs and their use in the treatment of cancer.

While developing Virulizin® and the NuChem analogs, the Company has incurred net losses in each of the periods covered by this Annual Report. The Company has not been profitable since it was established. Lorus expects that losses will continue until agreements to develop, market and distribute Virulizin® or the NuChem analogs are concluded with a strategic pharmaceutical partner, and sufficient sales are realized.

Results of Operations

Year ended May 31, 1999 ("fiscal 1999") compared to the year ended May 31, 1998 ("fiscal 1998")

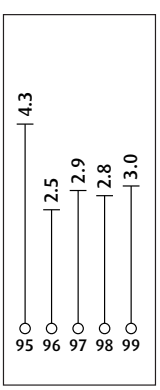
During fiscal 1999, the Company incurred net research and development expenses of $3,004,812 compared to $2,758,203 in fiscal 1998. In fiscal 1999, a decline in spending on Virulizin® development programs was more than offset by increased spending on pre-clinical development, primarily at Harvard Medical School, of the NuChem analogs acquired in December, 1997. Cash refunds of investment tax credits of $186,820 were received in fiscal 1999 compared to $3,496 in fiscal 1998.

General and administrative expenses for fiscal 1999 were $1,701,364 compared to $1,912,235 in fiscal 1998. Spending on legal and regulatory matters and on investor relations increased during the year. Savings resulting from the divestiture of Lorus' manufacturing operations, relocation to more appropriate office facilities and other cost reduction programs during fiscal 1999 offset these increases.

Depreciation and amortization expense decreased to $187,567 in fiscal 1999 from $340,014 in fiscal 1998, due to the sale of the Company's manufacturing assets in December 1998. This transaction resulted in a gain on sale of $443,343 in fiscal 1999.

Interest earned in fiscal 1999 was $144,696 compared with $268,619 in the previous year. The decrease relates to the lower average cash balance during fiscal 1999.

Research and Development Expenses
(in millions of dollars)



The Company's loss for fiscal 1999 was $4,623,481 compared to $4,741,833 for the previous year.

Year ended May 31, 1998 compared to the year ended May 31, 1997 ("fiscal 1997")

During fiscal 1998, the Company incurred net research and development expenses of $2,758,203 compared to $2,887,877 for fiscal 1997.

During fiscal 1998, general and administrative expenses increased to $1,912,235 from $1,511,328 for fiscal 1997. The increase is mainly attributable to a new investor relations program and increased legal costs associated with licensing, due diligence and contracting activity.

During fiscal 1998, interest income increased to $268,619 from $100,952 for fiscal 1997. The increase is attributable to a higher average cash balance during fiscal 1998.

During fiscal 1998, depreciation and amortization decreased to $340,014 from $539,508 for fiscal 1997.

During fiscal 1998, the Company's loss decreased to $4,741,833 from $4,837,761 for fiscal 1997. The primary reason is the decrease in research and development expenses during fiscal 1998.

Liquidity and Capital Resources

Since its inception, Lorus has financed its operating activities through public offerings and private placements of equity securities, refundable investment tax credits and interest income.

Cash Used in Operating Activities

During fiscal 1999, the Company used $4,116,731 to finance its operating activities compared to $4,380,034 in fiscal 1998 and $3,580,920 in fiscal 1997. The decreased cash requirement in fiscal 1999 relates primarily to the decrease in non-cash working capital balances. In fiscal 1998, the increased cash requirement relates to the significant decrease in non-cash working capital balances when compared to fiscal 1997.

Cash Used in Investing Activities

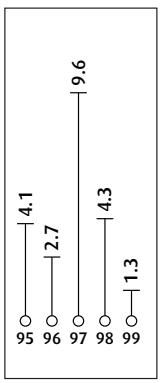
During fiscal 1999, the Company generated $2,410,565 from investing activities compared to $3,864,058 in fiscal 1998 and a net outflow of $7,807,274 in fiscal 1997. The prime reason for the year-to-year fluctuations is the timing of purchases and maturities of short-term investments.

In fiscal 1999, the sale of the Company's manufacturing assets realized proceeds of $665,000 consisting of cash and a note receivable that has been recorded at a discounted carrying value of $433,333 at May 31, 1999. Offsetting this note receivable is a bad debt provision of $317,777, the remaining balance of the note receivable at September 30, 1999 as the purchaser of the assets filed under Section 49 of the Canadian Bankruptcy and Insolvency Act in September 1999. Investment in acquired research and development, represented by the ongoing acquisition costs of patent rights to certain clotrimazole related analogs, was $513,205 in fiscal 1999, $714,750 in 1998 and $0 in 1997.

Purchases of capital assets and capitalized patent expenses were $464,924 in 1999, $202,433 in 1998 and $26,033 in 1997. The fiscal 1999 additions were primarily patent costs, leasehold improvements at the Company's new head-office, and computer hardware and software related to the Year 2000 Issue. In fiscal 1998 and 1997, capital spending was primarily on the in-house cell-culture and analytical laboratory and pilot manufacturing plant equipment. At May 31, 1999 the Company has deferred charges of $160,750 in connection with the proposed acquisition of GeneSense Technologies Inc.

Cash and Short-term Investments

(in millions of dollars)



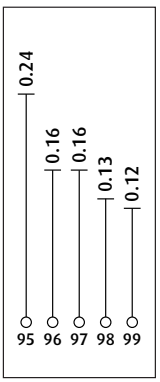
Cash Provided from Financing Activities

During fiscal 1999, the Company generated $1,697,368 from financing activities, compared with $20,215 and $10,480,104 in fiscal 1998 and 1997, respectively. In fiscal 1999, the Company completed a private placement of 5,333,333 common shares and 2,666,667 purchase warrants for net proceeds of $1,216,951. The proceeds were allocated $1,003,618 as to common shares and $213,333 as to warrants. During fiscal 1999, additional financing of $493,406 was generated by the issuance of shares in respect of acquired research and development, and $47,700 was generated by the exercise of stock options. In addition to the foregoing, during fiscal 1999 the Company deferred costs of $60,689 in connection with the October private placement.

During fiscal 1998, the Company incurred a cash inflow from financing activities of $20,215. This compared to a cash inflow of $10,480,104 for fiscal 1997.

During fiscal 1997, the Company completed a $5,000,000 private placement of 3,571,429 common shares (stated capital $1.31 per common share) and 892,857 common share purchase warrants (stated capital $0.09 per one-quarter common share purchase warrant) for net proceeds of $4,871,228. The holder of the common share purchase warrants is entitled to purchase one common share at a price of $1.68 per share at any time on or before April 30, 2002. In addition, if at any time after the two year anniversary of the closing and before the expiry date the closing price of the shares on the Toronto Stock Exchange has been $2.80 or greater for a period of 60 consecutive trading days, the Company will have the right to require the holder to exercise the warrants.

Loss per Common Share
(in dollars)



During fiscal 1997, the Company completed a $3,400,000 private placement of special warrants for net proceeds of $3,131,709. Each special warrant grants the holder the right to acquire, without any additional payment, one common share (stated capital $1.31 per common share) and one-quarter common share purchase warrant (stated capital $0.09 per one-quarter common share purchase warrant). Each common share purchase warrant entitled the holder to acquire one common share of the Company for $1.68 at any time on or before April 30, 1999.

During fiscal 1997, the majority (1,483,300 warrants) of the 1996 common share purchase warrants were also exercised for cash consideration of $2,002,555 or $1.35 per common share. A number (316,600 warrants) of the 1996 dealer common share warrants were also exercised for proceeds of $278,608 or $0.88 per common share. The Company also issued 247,638 common shares upon the exercise of stock options for net proceeds of $196,004.

The precise timing of the application of the Company's working capital depends on several factors. These include: the degree of advancement in the Company's scientific programs; patient enrollment in clinical trials; changes in government regulations; the time required for regulatory authorities to review Lorus' submissions and applications, and the Company's success in negotiating strategic partnerships.

Lorus will require additional funding to complete its research and development activities, to obtain regulatory approvals to market Virulizin® in selected jurisdictions, to broaden the application of its technology and, upon the proposed completion of the GeneSense acquisition, to further the development of the GeneSense technologies. In April 1999, the Company signed an Agency Agreement with HSBC Securities Inc. to raise up to CDN$20 million in a private placement of Special Warrants. In October 1999, Lorus reported that it had closed on CDN$10 million of that financing. These funds will assist the Company in its near-term cash requirements however additional financings will be required. Accordingly, the Company intends to raise additional funds in the future by issuing common shares or other financial instruments or through the formation of strategic partnerships to develop its products.

The Year 2000 Issue

The "Year 2000 Issue" arises because many computer hardware and software systems use only two digits to represent the year. As a result, these systems and programs may not process dates beyond 1999.

Vulnerability to Issue

The Company uses information technology for office administration and accounting purposes, but the Company could perform these functions without the use of information technology. The Company's information systems are not complex and would not be difficult to replace with hardware and software of similar functionality that is available from a number of vendors.

The Company occupies leased premises, and is dependent on building systems not within its control that incorporate technology that could be affected by the Year 2000 Issue. Since the Company has only has 10 employees performing management and administration functions in a single location, its operations could, if necessary, be moved to other premises in the unlikely event that building systems were non-compliant.

The Company makes limited use of technology to interact with third parties, and alternative means of communication could readily be arranged if necessary. Lorus' major suppliers are institutions conducting research on its behalf, entities providing manufacturing services and an outside payroll service provider.

Evaluation of the Company's Situation

Responsibility for overseeing the Company's response to the Year 2000 Issue has been assigned to the Controller (as chief financial officer). Management of the project has been assigned to the Vice President – Industrial Operations. As part of the Year 2000 preparedness program, in July 1998 Lorus upgraded its office administration and accounting systems and its related PC network. Subject to installation of a small number of system enhancements, to be provided at no cost to the Company, the vendor of Lorus' financial accounting system has warranted that the system is Year 2000 compliant. In June 1999, the Company engaged an outside consultant to review and test its PC network for compliance, with positive results. Nevertheless, the Company's contingency plan for these systems ensures that the functions dependent on these systems could be moved to similar systems available from other vendors.

The Company has satisfied itself that the institutions conducting research on its behalf have plans in place to address the Year 2000 Issue. The deliverables from these institutions (primarily reports and laboratory data) are in hard copy (for regulatory filing purposes) as well as electronic format. Accordingly, Lorus believes there is little risk of data loss resulting from the Year 2000 Issue. Lorus has obtained assurances from its vendors of manufacturing services that they will not be adversely affected by the Year 2000 Issue. The Company has confirmed that its payroll service provider is Year 2000 compliant.

Although the Company has received or expects to receive Year 2000 compliance assurances from its vendors, the nature of the Year 2000 Issue is such that no assurances can be given that any service provider will not be adversely affected. In this event, Lorus' contingency plan involves contracting with alternative providers for these services, although there can be no assurances that such services would be available on comparable terms or that these alternative arrangements could be concluded quickly.

Status of Company's Compliance Plan

Lorus has completed canvassing its service providers and expects to have completed its contingency plan by late July 1999. This plan will, of necessity, be dynamic and may change, as the compliance status of affected technology is determined. Remediation and testing of the financial accounting software package will be completed in August 1999. Lorus will avail itself of remediation and upgrades in respect of non-mission-critical software packages, such as spreadsheets and word-processing, as these are made available by vendors prior to year 2000.

Costs of Compliance

To date, Lorus has expended approximately $70,000 on upgraded or replacement computer hardware and software. These expenditures were made for reasons that included, but were not limited to, addressing the Year 2000 Issue. These costs have been capitalized. Based on currently available information, Lorus does not expect further expenditures in connection with the Year 2000 Issue to be material and has budgeted $10,000 for these items.

Forward-Looking Statements

Except for historical information, this annual report contains forward-looking statements that reflect the Company's current expectations regarding future events. These forward-looking statements involve risks and uncertainties, which may cause actual results to differ materially from those statements. Those risks and uncertainties include, but are not limited to, changing market conditions, the successful and timely completion of clinical studies, the establishment of corporate alliances, the impact of competitive products and pricing, new product development, uncertainties related to the regulatory approval process, and other risks detailed from time to time in the Company's quarterly filings, annual reports and 20-F filings.

Auditors' Report

To the Shareholders of Lorus Therapeutics Inc.

We have audited the consolidated balance sheets of Lorus Therapeutics Inc. as at May 31, 1999 and 1998 and the consolidated statements of loss and deficit and cash flows for each of the years in the three year period ended May 31, 1999 and the related consolidated statement of loss and deficit and cash flows for the period from inception on September 5, 1986 to May 31, 1999. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with 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 May 31, 1999 and 1998 and the results of its operations and the changes in its financial position for each of the years in the three year period ended May 31, 1999 and for the period from inception on September 5, 1986 to May 31, 1999 in accordance with generally accepted accounting principles.

We did not audit the consolidated financial statements of Lorus Therapeutics Inc. for the period from inception on September 5, 1986 to May 31, 1994. Those consolidated financial statements were audited by other auditors who issued a report without reservation on July 8, 1994.

KPMG LLP (signed)

Toronto, Canada
October 29, 1999
Chartered Accountants

Consolidated Balance Sheets

(Canadian Dollars)	***1999***	*As at May 31 1998*
Assets		
Current assets		
Cash and cash equivalents	**$ 1,286,599**	$ 1,295,397
Short-term investments	**–**	3,000,000
Accounts receivable	**25,598**	169,126
Note receivable (note 3)	**115,556**	–
Prepaids and supplies	**52,284**	297,904
Total current assets	**1,480,037**	4,762,427
Deferred charges (note 4)	**221,439**	–
Acquired research and development (note 5)	**1,001,479**	663,696
Capital assets (note 7)	**546,994**	491,294
	$ 3,249,949	$ 5,917,417
Liabilities and Shareholders' Equity		
Current liabilities		
Accounts payable and accrued liabilities (note 8)	**$ 1,330,228**	$ 1,132,272
Total current liabilities	**$ 1,330,228**	$ 1,132,272
Shareholders' Equity		
Share capital (note 9)		
Common shares		
(Issued: May 31, 1999 – 42,746,668 May 31, 1998 – 36,785,147)	**38,955,082**	37,191,787
Warrants	**534,762**	540,000
Deficit accumulated during development stage	**(37,570,123)**	(32,946,642)
Total shareholders' equity	**1,919,721**	4,785,145
	$ 3,249,949	$ 5,917,417

Commitments (notes 5 and 11)

Canada and United States accounting policy differences (note 15)

Subsequent event (note 16)

See accompanying notes

On behalf of the Board:

Donald W. Paterson (signed) — Director

Philippe G. Lacaille (signed) — Director

Consolidated Statements of Loss and Deficit

(Canadian Dollars)	*Years ended May 31*			*Period from inception on Sept. 5, 1986 to May 31*
	1999	*1998*	*1997*	*1999*
Expenses				
Research and development	**$ 3,191,632**	$ 2,761,699	$ 2,932,052	$ 26,752,075
Less investment tax credits	**(186,820)**	(3,496)	(44,175)	(2,943,253)
	3,004,812	2,758,203	2,887,877	23,808,822
General and administrative	**1,701,364**	1,912,235	1,511,328	13,782,001
Depreciation and amortization	**187,567**	340,014	539,508	2,296,016
Gain on sale of capital assets (note 3)	**(443,343)**	–	–	(443,343)
Provision for bad debts (note 3)	**317,777**	–	–	317,777
Interest earned	**(144,696)**	(268,619)	(100,952)	(2,191,150)
Net loss for the period	**4,623,481**	4,741,833	4,837,761	37,570,123
Deficit, beginning of period	**32,946,642**	28,204,809	23,367,048	–
Deficit, end of period	**$ 37,570,123**	$ 32,946,642	$ 28,204,809	$ 37,570,123
Loss per common share	**$ 0.12**	$ 0.13	$ 0.16	
Weighted average number of common shares outstanding	**37,857,779**	36,566,787	30,532,767	

See accompanying notes

Consolidated Statements of Cash Flows

(Canadian Dollars)	*Years ended May 31*			*Period from inception on Sept. 5, 1986 to May 31*
	1999	*1998*	*1997*	*1999*
Operating Activities				
Loss for the period	**$ (4,623,481)**	$ (4,741,833)	$ (4,837,761)	$ (37,570,123)
Add items not requiring a current outlay of cash				
Depreciation and amortization	**362,989**	391,068	539,508	2,522,492
Gain on sale of capital assets	**(443,343)**	–	–	(443,343)
Restructuring costs	**–**	–	–	626,040
Net change in non-cash working capital balances related to operations	**587,104**	(29,269)	717,333	1,252,346
Cash used in operating activities	**(4,116,731)**	(4,380,034)	(3,580,920)	(33,612,588)
Investing Activities				
(Purchase) Sale of short-term investments	**3,000,000**	4,781,241	(7,781,241)	–
Note receivable, net of repayments and provision (note 3)	**(115,556)**	–	–	(115,556)
Deferred charges	**(160,750)**	–	–	(160,750)
Acquired research and development	**(513,205)**	(714,750)	–	(1,227,955)
Additions to capital assets	**(464,924)**	(202,433)	(26,033)	(3,064,667)
Proceeds on sale of capital assets	**665,000**	–	–	665,000
Cash provided by (used in) investing activities	**2,410,565**	3,864,058	(7,807,274)	(3,903,928)
Financing Activities				
Deferred charges	**(60,689)**	–	–	(60,689)
Issuance of warrants	**213,333**	–	3,453,138	534,762
Exercise of warrants	**–**	(2,928,271)	(90,992)	–
Issuance of common shares	**1,544,724**	2,948,486	7,117,958	38,329,042
Cash provided by financing activities	**1,697,368**	20,215	10,480,104	38,803,115
Increase (decrease) in cash and cash equivalents during the period	**(8,798)**	(495,761)	(908,090)	1,286,599
Cash and cash equivalents, beginning of period	**1,295,397**	1,791,158	2,699,248	
Cash and cash equivalents, end of period	**$ 1,286,599**	$ 1,295,397	$ 1,791,158	$ 1,286,599

See accompanying notes

Notes to Consolidated Financial Statements

May 31, 1999 and 1998

1. The Corporation and Basis of Presentation

Lorus Therapeutics Inc. ("Lorus" and the "Corporation") is a Canadian biopharmaceutical company focused on the development of cancer therapies. Lorus' goal is to capitalize on its pre-clinical, clinical and regulatory expertise by developing new drug candidates that can be used, either alone, or in combination, to successfully manage cancer. Through an active acquisition and in-licensing program, Lorus is building a portfolio of promising anti-cancer drugs. Late stage clinical development and marketing will be done in co-operation with strategic pharmaceutical partners.

The continuation of the Corporation's research and development activities and the commercialization of the targeted therapeutic products is dependent upon the Corporation's ability to successfully complete its research and development programs and finance its cash requirements through a combination of equity financing and payments from strategic partners. It is not possible to predict the outcome of future research and development programs or the Corporation's ability to fund its cash requirements over the term of the programs (note 16 (a)).

The Corporation's common shares trade in the United States on the National Association of Securities Dealers "Over the Counter" Bulletin Board, and in Canada on The Toronto Stock Exchange and the Montreal Exchange.

2. Significant Accounting Policies

Basis of Presentation

The consolidated financial statements of the Corporation have been prepared by management in accordance with accounting principles generally accepted in Canada and comply in all material respects with accounting principles generally accepted in the United States, except as disclosed in note 15 "Canada and United States Accounting Policy Differences".

Uses of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of expenses during the period. Actual results could differ from those estimates.

Capital Assets

Capital assets are recorded at acquisition cost less any related refundable investment tax credits. Patents include patent registration costs and are amortized from the date of grant. Patent registration costs are expensed when an application is determined to be unsuccessful. The Corporation provides depreciation and amortization at rates which are expected to charge operations with the cost of the assets over their estimated useful lives as follows:

> Furniture and Equipment	straight-line over five years
> Leasehold improvements and pilot plant	straight-line over the term of the lease
> Patents	straight-line over seven years

Foreign Currency Translation

Expenses arising from foreign currency transactions are translated into Canadian dollars at the rates prevailing at the transaction dates. Monetary assets and liabilities are translated into Canadian dollars at the rates prevailing at the balance sheet date. Gains or losses resulting from these transactions are accounted for in the loss of the period and are not significant.

Research and Development

Research costs are charged to expense as incurred. Development costs are expensed as incurred unless they meet the criteria under generally accepted accounting principles for deferral and amortization. Refundable investment tax credits earned on scientific research and development expenditures are recorded as a reduction of the related current period expenses or as a reduction of the related fixed asset.

The Corporation capitalizes the costs of research and development acquired upon the acquisition of patents and licences. These costs are amortized on a straight-line basis over seven years. Unamortized costs related to specific patents and licences will be written off in the period in which the Corporation assesses that the patent or licence has experienced a permanent impairment in value.

Research and development acquired does not necessarily reflect the present or future values of the patents and licences. The amount recoverable is dependent upon the continued advancement of the research and development through clinical trials and ultimately to commercialization. It is not possible to predict the outcome of future research and development programs.

3. *Note Receivable*

In December 1998, the Corporation sold substantially all of its manufacturing assets for total proceeds of $699,000 consisting of $150,000 in cash and a note receivable for $549,000. The Corporation recorded a gain on the disposition of $443,343. The note receivable is unsecured, non-interest bearing and due in 18 monthly installments of $30,500 commencing March 1, 1999.

Subsequent to the asset sale, the debtor of the note receivable filed under Section 49 of the Canadian Bankruptcy and Insolvency Act. As a result, Lorus has written down the note receivable as at May 31, 1999 to its estimated net recoverable amount of $115,556, recording a provision for bad debts of $317,777 in the Consolidated Statement of Loss.

4. *Deferred Charges*

Deferred charges at May 31, 1999 include $160,750 in respect of costs in connection with the proposed acquisition of GeneSense Technologies Inc. (note 16 (b)), and $60,689 in respect of costs associated with the current financing efforts (note 16 (a)). On completion of the acquisition and financing, these costs will be accounted for as an increase in the investment in GeneSense Technologies Inc. and as a reduction in share capital, respectively.

5. *Acquired Research and Development*

In December 1997, the Corporation, through a newly incorporated subsidiary NuChem Pharmaceuticals Inc. ("NuChem"), acquired certain patent rights and a sub-licence to develop and commercialize the anti-cancer application of certain analogs ("NCEs"). Consideration for this acquisition includes a 20% share interest in NuChem, US$350,000 in shares of the Corporation and up to US$3,500,000 in cash. On June 15, 1998 the Corporation issued from treasury, 583,188 common shares of the Corporation in settlement of the US$350,000. As at May 31, 1999 the Corporation had made cash payments of Cdn.$715,000 (US$500,000). The remaining balance of up to US$3,000,000 is payable upon the achievement of certain milestones based on the commencement and completion of clinical trials related to the NCEs. In particular, the milestones and the related amounts payable on the achievement of such milestones are as follows:

Milestone Events

	Contingent amount payable (U.S. dollars)
after completing treatment of the last subject in the first Phase I trial	$ 250,000
after completing treatment of the last subject in the first Phase II trial	500,000
after completing treatment of the last subject in the first Phase III trial	750,000
upon receipt of marketing approval in either the United States, Canada, England or France for the first of the NCEs	1,500,000
	$ 3,000,000

All research and development activities to be undertaken by NuChem are to be funded by the Corporation. As at May 31, 1999, the gross cost of acquired research and development was $1,227,955 (1998 – $714,750) and accumulated amortization was $226,476 (1998 – $51,054).

6. Income Taxes

Carryforward Amounts

As at May 31, 1999, the Corporation had losses of approximately $13,000,000 and unutilized investment tax credits of approximately $2,540,000. To the extent that these amounts are not utilized, they expire as follows:

Year of expiry	*Income tax losses*	*Investment tax credits*
2000	$ 89,000	$ 24,000
2001	15,000	117,000
2002	3,215,000	244,000
2003	1,668,000	1,000
2004	2,022,000	754,000
2005	2,296,000	12,000
2006	3,695,000	364,000
2007		357,000
2008		447,000
2009		220,000
	$ 13,000,000	$ 2,540,000

In addition, the Corporation has accumulated timing differences of approximately $20,353,000. The timing differences consist primarily of scientific research and development expenditures that are available to reduce taxable income in future years. The potential tax benefits that may result from the application of these carry forward amounts in future years have not been recognized in these financial statements.

The tax benefit of the foregoing items amounts to approximately $16,289,000, which has been completely offset by a valuation allowance.

7. Capital Assets

As at May 31	***1999***	*1998*
Cost		
Furniture and equipment	**$ 457,229**	$ 1,117,013
Leasehold improvements and pilot plant	**64,203**	1,011,163
Patents	**388,792**	17,035
	910,224	2,145,211
Accumulated Depreciation		
Furniture and equipment	**(352,284)**	(815,363)
Leasehold improvements and pilot plant	**(6,419)**	(837,337)
Patents	**(4,527)**	(1,217)
	(363,230)	(1,653,917)
	$ 546,994	$ 491,294

8. Accounts Payable and Accrued Liabilities

As at May 31	***1999***	*1998*
Accounts payable	**$ 168,322**	$ 24,605
Accrued liabilities	**1,161,906**	1,107,667
	$ 1,330,228	$ 1,132,272

9. Share Capital

a) Authorized Shares

The Corporation has authorized an unlimited number of common shares.

b) Issued and Outstanding Common Shares

Number of common shares	***1999***	*1998*	*1997*
Balance, beginning of year	**36,785,147**	34,317,426	28,698,459
Exercise of special warrants (notes 9 (e) and (g))	**5,333,333**	2,428,571	–
Exercise of units (note 9 (f))	**–**	–	3,571,429
Exercise of purchase warrants (note 9 (d))	**–**	37,150	1,799,900
Exercise of stock options (note 9 (h))	**45,000**	2,000	247,638
Other issuances (note 5)	**583,188**	–	–
Balance, end of year	**42,746,668**	36,785,147	34,317,426

Common shares – amounts	***1999***	*1998*	*1997*
Balance, beginning of year	**$ 37,191,787**	$ 34,243,301	$ 27,125,343
Exercise of special warrants (notes 9 (e) and (g))	**1,003,618**	2,903,016	–
Exercise of units (note 9 (f))	**–**	–	4,549,799
Exercise of purchase warrants (note 9 (d))	**–**	32,692	2,372,155
Exercise of stock options (note 9 (h))	**47,700**	1,360	196,004
Expiry of warrants (note 9 (d) and (e))	**218,571**	11,418	–
Other issuances (note 5)	**493,406**	–	–
Balance, end of year	**$ 38,955,082**	$ 37,191,787	$ 34,243,301

The legal stated capital of the Corporation is $42,400,436 at May 31, 1999 (1998 – $40,234,294).

c) Issued and Outstanding Common Share Purchase Warrants and Special Warrants

Number of common share purchase warrants and special warrants	***1999***	*1998*	*1997*
Purchase warrants			
Balance, beginning of year	**1,499,999**	1,215,457	2,122,500
Exercise of special warrants (notes 9 (e) and (g))	**3,200,000**	607,142	–
Exercise of units (note 9 (f))	**–**	**–**	892,857
Exercise of purchase warrants (note 9 (d))	**–**	(37,150)	(1,799,900)
Expiry of purchase warrants (note 9 (d) and (e))	**(607,142)**	(285,450)	–
Balance, end of year	**4,092,857**	1,499,999	1,215,457
Special warrants			
Balance, beginning of year	**–**	2,428,571	–
Issuance of special warrants (note 9 (g))	**5,333,333**	–	2,428,571
Exercise of special warrants (note 9 (e) and (g))	**(5,333,333)**	(2,428,571)	–
Balance, end of year	**–**	–	2,428,571
	4,092,857	1,499,999	3,644,028

Stated value of common share purchase warrants and special warrants	***1999***	*1998*	*1997*
Purchase warrants			
Balance, beginning of year	**$ 540,000**	$ 336,562	$ 106,125
Exercise of special warrants (notes 9 (e) and (g))	**213,333**	218,571	–
Exercise of units (note 9 (f))	**–**	**–**	321,429
Exercise of purchase warrants (note 9 (d))	**–**	(3,715)	(90,992)
Expiry of purchase warrants (note 9 (d) and (e))	**(218,571)**	(11,418)	–
Balance, end of year	**$ 534,762**	$ 540,000	$ 336,562
Special warrants			
Balance, beginning of year	**–**	3,131,709	–
Issuance of special warrants (note 9 (e) and (g))	**1,216,951**	–	3,131,709
Exercise of special warrants (note 9 (e) and (g))	**(1,216,951)**	(3,131,709)	–
Balance, end of year	**$ –**	$ –	$ 3,131,709
	$ 534,762	$ 540,000	$ 3,468,271

d) 1996 Special Warrant Offering

During 1997, 1,483,300 purchase warrants and 316,600 dealer purchase warrants, relating to a 1996 special warrant offering, were exercised for cash consideration of $2,281,163. During 1998, the remaining 37,150 dealer purchase warrants were exercised for $32,692 and the remaining 285,450 purchase warrants expired, unexercised.

e) 1997 Special Warrant Offering

On April 30, 1997, the Corporation completed a private placement of 2,428,571 special warrants for gross proceeds of $3,399,999 ($1.40 per special warrant) before deducting expenses of $268,290. Each special warrants granted the holder the right to acquire, without additional payment, one common share (stated capital $1.31 per common share) and one-quarter common share purchase warrant (stated capital $0.09 per one-quarter common share purchase warrant). The one-quarter common share purchase warrants entitled the holder to acquire one common share for $1.68 at any time on or before April 30,1999. On July 8, 1997 the special warrants were converted into 2,428,571 common shares and 607,142 purchase warrants. The purchase warrants expired, unexercised, on April 30, 1999.

f) 1997 Private Placement

On April 30, 1997, the Corporation completed a private placement of 3,571,429 units for gross proceeds of $5,000,000 ($1.40 per unit) before deducting expenses of $128,773. Each unit granted the holder the right to acquire, without additional payment, one common share (stated capital $1.31 per common share) and one-quarter common share purchase warrant (stated capital $0.09 per one-quarter common share purchase warrant). Each whole common share purchase warrants entitled the holder to acquire on common share for $1.68 on or before April 30, 2002. On April 30, 1997 the units were converted into 3,571,429 common shares and 892,857 purchase warrants. In addition, the Corporation will have the right to require the holder of the purchase warrants to exercise the warrants if at any time after April 30, 1999 and before April 30, 2002 the closing price of the shares on the Toronto Stock Exchange has been $2.80 or greater for a period of 60 consecutive days. As at May 31, 1999 all of the purchase warrants related to this offering were outstanding.

g) 1999 Private Placement of Special Warrants

On January 8, 1999, the Corporation completed a private placement of 5,333,333 special warrants for gross proceeds of $1,600,000 ($0.30 per special warrant) before deducting expenses of $383,049. Each special warrant granted the holder the right to acquire, without additional payment, one common share (stated capital $0.272 per common share) and one-half of one Series A purchase warrant (stated capital $0.028 per one-half common share purchase warrant). Each whole common share purchase warrant entitles the holder to acquire one common share for $0.36 at any time on or before January 8, 2000. On May 7, 1999 the special warrants were converted into 5,333,333 common shares and 2,666,667 purchase warrants. In addition, the Corporation granted 483,333 broker warrants and 50,000 compensation options (stated capital $0.12 per broker warrant and compensation option) to agents of the Corporation in connection with the completion of the offering. Each broker warrant and compensation option entitles the holder to acquire one common share for $0.30. As at May 31, 1999 all of the purchase warrants, broker warrants and compensation options related to this offering were outstanding.

h) Stock Option Plan

The Corporation has granted certain options for common shares to directors, officers and employees of the Corporation pursuant to the terms of a Stock Option Plan (the "Plan"). The aggregate number of common shares of the Corporation that may be issued and sold under the Plan is 4,300,000. Stock option transactions for directors, officers and employees for the three years ended May 31, 1999 are summarized as follows:

	1999		1998		1997	
	Options	Weighted-avg. exercise price	Options	Weighted-avg. exercise price	Options	Weighted-avg. exercise price
Outstanding at beginning of year	**2,128,060**	**$ 1.06**	1,991,453	$ 1.16	1,832,727	$ 1.20
Granted	**1,247,565**	**$ 0.49**	537,845	$ 0.89	1,055,404	$ 1.31
Exercised	**(45,000)**	**$ 1.06**	(2,000)	$ 0.68	(247,638)	$ 0.79
Forfeited	**(236,687)**	**$ 1.25**	(399,238)	$ 1.37	(649,040)	$ 1.66
Outstanding at end of year	**3,093,938**	**$ 0.81**	2,128,060	$ 1.06	1,991,453	$ 1.16
Exercisable at end of year	**1,774,461**	**$ 1.00**	1,573,119	$ 1.09	1,268,715	$ 1.14

The following table summarizes information about stock options outstanding at May 31, 1999:

	Options outstanding			Options exercisable	
Range of Exercise prices	Options Outstanding	Weighted-avg. Remaining Contractual Life	Weighted-avg. Exercise Price	Options Exercisable	Weighted-avg. Exercise price
$0.33 to $0.99	2,049,331	1.64 years	$0.59	810,923	$0.71
$1.00 to $1.99	1,016,107	2.21 years	$1.22	935,038	$1.22
$2.00 and above	28,500	0.17 years	$2.00	28,500	$2.00
	3,093,938	1.81 years	$0.81	1,774,461	$1.00

10. Changes in Non-Cash Working Capital Balances

Changes in non-cash working capital balances for each of the periods ended are summarized as follows:

	Years ended May 31			Period from inception on Sept. 5, 1986 to May 31
(Canadian Dollars)	**1999**	1998	1997	1999
(Increase) decrease				
Accounts receivable	**$ 143,528**	$ (25,982)	$ 115,211	$ (25,598)
Prepaids and supplies	**245,620**	(45,130)	74,331	(52,284)
Increase(decrease)				
Accounts payable and accrued liabilities	**197,956**	41,843	527,791	1,330,228
	$ 587,104	$ (29,269)	$ 717,333	$1,252,346

11. Commitments

Under operating leases for premises and equipment, the Corporation is obligated to make minimum annual payments approximately as follows:

2000	$ 90,000
2001	58,000
2002	48,000
2003	53,000
2004	38,000
	$ 287,000

During the year ended May 31, 1999, the amount of payments under operating leases was approximately $117,000 (1998 – $162,000 and 1997 – $152,000).

Under contracts for research and development, the Corporation is committed to make payments of approximately $264,000.

12. Related Party Transactions

During the year ended May 31, 1999, the Corporation paid consulting fees to individuals (or companies controlled by those individuals), who were either officers, directors or shareholders of the Corporation, of $86,000 (1998 – $104,000 and 1997 – $95,000).

The Corporation also incurred professional fees payable to a law firm in which a director of the Corporation is a partner. These fees relate primarily to the issuance of common shares, the proposed acquisition of GeneSense Technologies Inc. (note 17(b)), and consultations in the normal course of business, for an aggregate of $279,000 for the year ended May 31, 1999 (1998 – $162,000 and 1997 – $245,000).

Amounts due to related parties as at May 31, 1999 are $78,000 and are included in accounts payable and accrued liabilities (1998 – $15,000 and 1997 – $117,000).

13. Uncertainty Due to the Year 2000 Issue

The Year 2000 issue arises because many computerized systems use two digits rather than four digits to identify a year. Date-sensitive systems may recognize the year 2000 as 1900 or some other date resulting in errors when information using Year 2000 dates is processed. In addition, similar problems may arise in some systems that use certain dates in 1999 to represent something other than a date. The effects of the Year 2000 issue may be experienced before, on, or after January 1, 2000, and, if not addressed, the impact on operations and financial reporting may range from minor errors to significant systems failure, which could affect the Corporation's ability to conduct normal business operations. It is not possible to be certain that all aspects of the Year 2000 Issue affecting the Corporation, including those related to the efforts of suppliers, or other third parties, will be fully resolved.

14. Financial Instruments

The carrying values of cash and cash equivalents, short-term investments, accounts receivable, notes receivable and accounts payable and accrued liabilities approximate their fair values due to the short-term nature of these instruments.

15. Canada and United States Accounting Policy Differences

These financial statements have been prepared in accordance with generally accepted accounting principles ("GAAP") as applied in Canada. In certain respects, GAAP as applied in the United States differs from that applied in Canada.

(a) Recent Accounting Pronouncements:

In June 1997, the Financial Accounting Standards Board issued SFAS No. 130, "Reporting Comprehensive Income", (SFAS No. 130) which establishes standards for reporting and presentation of comprehensive income. This standard defines comprehensive income as the changes in equity of an enterprise except those resulting from stockholder transactions. Comprehensive loss for the periods presented in these financial statements equalled the loss for the period.

In June 1997, the Financial Accounting Standards Board issued SFAS No. 131, "Disclosures About Segments of an Enterprise and Related Information" (SFAS No. 131). SFAS No. 131 was adopted by the Corporation in 1997. SFAS No. 131 establishes standards for disclosures about operating segments, and services, geographic areas and major customers. The Corporation is organized and operates as one operating segment, the development of cancer therapies.

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" (SFAS No. 133). SFAS No. 133 establishes accounting and reporting standards requiring that every derivative instrument be recorded in the balance sheet as either an asset or liability measured at its fair value. SFAS No. 133, as recently amended, is effective for fiscal years beginning after June 15, 2000. Management believes the adoption of SFAS No. 133 will not have a material effect on the Corporation's financial position or results of operations.

(b) SFAS 123 Pro Forma Information:

SFAS No. 123, "Employee Stock Compensation," encourages, but does not require, the recording of compensation costs for stock options to be valued at fair value. For companies choosing not to adopt the fair value measurement for stock based compensation, the pronouncement requires the Corporation to disclose pro forma net income and earnings per share information as if the Corporation had accounted for its stock options issued in 1995 through 1999 under the fair value method. The Corporation has elected not to adopt the recording of compensation cost for stock options at fair value and, accordingly, a summary of the pro forma impact on the statement of operations is presented in the table below:

	1999	*1998*	*1997*
Loss for the year	**$ 4,623,481**	$ 4,741,833	$ 4,837,761
Compensation expense related to the fair value of stock options	**216,485**	304,771	271,044
Pro forma loss for the period	**$ 4,839,966**	$ 5,046,604	$ 5,108,805
Pro forma loss per common share	**$ 0.13**	$ 0.14	$ 0.17

The fair value of each option granted has been estimated at the date of grant using the Black-Scholes option pricing model with the following assumptions used for options granted in the years ended May 31, 1999, 1998 and 1997: (i) dividend yield of 0%; (ii) expected volatility of 60%; (iii) risk-free interest rate of 5.3%(1998 – 4.5%, 1997 – 5.0%) and (iv) expected lives of 5 years. The Corporation has assumed no forfeiture rate as adjustments for actual forfeitures are made in the year they occur. The weighted-average grant-date fair value of options issued in the years ended May 31, 1999, 1998 and 1997 was $0.28, $0.49 and $0.74, respectively.

16. Subsequent Events

(a) Financing

Subsequent to the year end, the Corporation completed the first tranche of a private placement of 30,303,030 special warrants for gross proceeds of $ 10,000,000 ($0.33 per special warrant) before deducting issue expenses of approximately $1,025,000. The special warrants entitle the holder the right to acquire, without additional payment, one common share of the Corporation. In addition, the Corporation issued 3,030,303 broker warrants to an agent of the Corporation for its services in connection with the completion of the offering.

In the event that the proposed acquisition of GeneSense (note 16 (b)) is not completed within 120 days of the closing date of the private placement, the holders of the special warrants shall be entitled to require the Corporation to repurchase their special warrants at a purchase price equal to the offering price, together with interest thereon.

(b) Proposed Acquisition

The Corporation has entered into a share purchase agreement dated June 11, 1999 to acquire all of the issued and outstanding shares of GeneSense Technologies Inc. ("GeneSense"). The closing of the acquisition is conditional upon Lorus meeting certain conditions including the successful completion of a minimum $10,000,000 debt and/or equity financing on or before the closing date of the acquisition.

The purchase price is being satisfied by an exchange of shares in the ratio of 5.15 Lorus common shares for each GeneSense common share. Upon the closing of the acquisition, Lorus will issue approximately 36,050,000 common shares. In addition, the Corporation will also issue 7,210,000 common shares purchase warrants and 903,825 options in exchange for 1,400,000 common share purchase warrants and 175,500 options of GeneSense which were outstanding immediately prior to the acquisition.

Corporate Governance

The Board of Directors of the Company believes that sound corporate governance practices are essential to the well being of the Company and its shareholders, and that these practices should be reviewed regularly to ensure that they are appropriate. The following is a description of the Company's corporate governance practices prepared by the Board of Directors.

The by-laws of The Toronto Stock Exchange and a policy statement of the Montreal Exchange require that this Statement of Corporate Governance Practices relate the corporate governance practices of the Board of Directors to the "Guidelines for Improved Corporate Governance" contained in the December 1994 Report of The Toronto Stock Exchange Committee on Corporate Governance in Canada (the "TSE Report"). The headings which appear below address the principal matters relating to corporate governance practices discussed in the TSE Report.

In this Statement, the term "unrelated director" has the meaning given to it in the TSE Report – a director who is free from any interest and any business or other relationship which could, or could reasonably be perceived to, materially interfere with the director's ability to act with a view to the best interests of the Company, other than interests arising from shareholding. All unrelated directors of the Company are also "independent directors" given that the Company does not have a significant shareholder.

Mandate of the Board

The mandate of the Board of Directors is to supervise the management of the business and affairs of the Company and to act with a view to the best interests of the Company. In fulfilling its mandate, the Board, among other matters, is responsible for:

- overseeing and evaluating the strategic planning process;
- identifying and implementing appropriate systems to manage the Company's principal risks;
- ensuring that the Company operates within all applicable laws and regulations, and to the highest ethical and moral standards;
- appointing and evaluating senior management;
- developing the Company's communications policy;
- ensuring adequate and timely reporting of financial results and other significant developments and matters to the Company's shareholders; and
- ensuring the integrity of the Company's internal controls and management information systems.

Five meetings of the Board were scheduled for fiscal 1999. There were five meetings of the Board during fiscal 1998. The frequency of meetings as well as the nature of agenda items change depending upon the state of the Company's affairs and in light of the opportunities or risks which the Company faces.

Board Composition

At the Annual and Special Meeting of Shareholders of the Company held on November 18, 1998, a resolution was passed by which the number of directors of the Company and the number of directors to be elected at the Annual Meeting of Shareholders was reduced to seven. The Board of Directors is currently composed of seven members. The Board of Directors believes that six of the current directors are "unrelated directors" and that one director is a "related director" within the meaning of the TSE Report. Accordingly, the Board of Directors is and will be constituted with a majority of individuals who qualify as "unrelated directors" within the meaning of the TSE Report. In deciding whether a particular director is a "related director" or an "unrelated director", the Board of Directors examined the factual circumstances of each director and considered them in the context of all relevant factors. Mr. Philippe Lacaille, the President and Chief Executive Officer of the Company, is a director. The Board believes that his extensive knowledge of the Company's business is beneficial to the other directors and that his participation as a director contributes to the effectiveness of the Board.

Proportionate Representation

Given the absence of a significant shareholder of the Company, the Board believes that the membership of the Board of Directors fairly reflects the investment in the Company by all of its shareholders. The Board believes that all directors make a valuable contribution to the Board and the Company.

Independence from Management

Mr. Lacaille is President and Chief Executive Officer of the Company and serves as a director.

Given that the membership of the Board includes only one director who is an executive officer of the Company, the Board believes that it is sufficiently independent of management.

Board Committees

During fiscal 1999, the Board of Directors had three committees: an Audit Committee, a Corporate Governance and Compensation Committee and an Environmental Committee. Ad hoc committees have also been established

from time to time. The Environmental Committee was dissolved in January, 1999 subsequent to the Company's discontinuance of its manufacturing operations. The responsibilities of the Environmental Committee are now carried out by the Board of Directors with the assistance of management.

Audit Committee

The Audit Committee is composed entirely of unrelated directors. The committee is responsible for reviewing the Company's financial reporting procedures, internal controls and the performance of the Company's external auditors. The committee is also responsible for reviewing quarterly financial statements and the annual financial statements prior to their approval by the Board of Directors. The Audit Committee met four times during the past year. Its members are Mr. Paterson, Mr. Reiter, and Mr. Diamond. Mr. Reiter replaced Mr. Marcus as a member of the Audit Committee as of November, 1998, when Mr. Marcus decided not to stand for re-election as a director of the Company.

Corporate Governance and Compensation Committee

The Corporate Governance and Compensation Committee is composed entirely of unrelated directors. The Committee is responsible for reviewing and making recommendations to the Board on, among other things, the compensation policies and practices for employees and senior executives of the Company, the implementation of succession plans, the evaluation of the performance of the Board and the adequacy of compensation of directors to reflect the responsibilities and risks involved in being an effective director. The Corporate Governance and Compensation Committee held three meetings in fiscal 1998 during which time its members were Mr. Campbell and Mr. Reiter.

Environmental Committee

The Environmental Committee was dissolved in January, 1999 subsequent to the Company's discontinuance of its manufacturing operations. The Environmental Committee was composed of Mr. Peter Campbell, a director of the Company, and a senior officer and several employees of the Company. The mandate of the Environmental Committee was to ensure that the Company's management and employees were aware of and complied with environmental laws, as well as good management practices, to promote environmental awareness among employees, and to encourage practices that protect the environment. The Environmental Committee met and reported monthly to the Company, and on a quarterly basis provided a written report to the Board of Directors. The responsibilities of the Environmental Committee are now carried out by the Board of Directors with the assistance of management.

Decisions Requiring Board Approval

In addition to those matters which must by law be approved by the Board, management is also required to seek Board approval for any material expenditure. Management is also required to consult with the Board before pursuing capital projects or strategic ventures which are beyond the Company's existing businesses. The Board approves all changes in senior management.

Board Performance

It is the responsibility of the Chairperson to ensure the effective operation of the Board. The Chairperson is responsible for ensuring the effectiveness of the process the Board follows and the quality of information provided to directors by management. The Chairperson will also meet at least once each year on an individual basis with every member of the Board to discuss that director's contribution to Board and committee deliberations and any other matters which the individual directors wish to raise with the Chairperson. The Chairperson also oversees the orientation of new directors.

Shareholder Feedback

The Company maintains an investor relations capability which the Board believes is important and highly effective. Every shareholder inquiry receives a prompt response from an appropriate officer of the Company.

Expectations of Management

The information which management provides to the Board is highly important to the ability of the Board to function effectively. Directors must have confidence in the data gathering, analysis and reporting functions of management. The Chairperson of the Board monitors the nature of the information requested by and provided to the Board. Periodically, the Board meets without the presence of the directors who are members of senior management. The Board also meets regularly with the senior officers responsible for the Company's operations to discuss key issues or strategies related to their areas of responsibility. From time to time, the Board has engaged outside advisers at the Company's expense to provide advice to the Board on matters relevant to the Company's activities.

Directors and Officers

Board of Directors

Donald W. Paterson (Chairperson)[1]
President,
Cavandale Corporation, Toronto

Dr. Donald P. Braun
Professor of Medicine and Immunology,
Rush Medical College

Director, Scientific Program Development,
Rush Cancer Institute, Chicago

Peter J. Campbell[2,3]
Executive Advisor, Health Care Industry,
Toronto

A. Ephraim Diamond[1]
Chairman and Chief Executive Officer,
Whitecastle Investments Limited, Toronto

Philippe G. Lacaille
President and Chief Executive Officer,
Lorus Therapeutics Inc., Toronto

Joel S. Marcus[4]
Chief Executive Officer,
Alexandria Real Estate Equities Inc.,
Los Angeles

Bruno Masson
Investment Manager,
SOFINOV (Société Financière D'Innovation), Montréal

Barry J. Reiter[1,2]
Partner,
Tory Tory DesLauriers & Binnington, Toronto
Barristers and Solicitors

1 Member of the audit committee

2 Member of the compensation committee

3 Member of the environmental committee

4 Mr. Marcus ceased to be a director of the Company on November 18, 1998 upon his decision not to stand for re-election.

Executive Officers

Philippe G. Lacaille
President and Chief Executive Officer

Guy Ely, M.D.
Vice President, Research and Development

Wayne D. Cockburn
Vice President, Business Development

Nadir Harjee
Vice President, Industrial Operations

Eckhardt Ferdinandi, Ph.D.
Director of Research

Karin C. Dschankilic, C.A.
Controller

Shane A. Ellis, B.A., LL.M.
Director of Legal Affairs – Corporate Secretary

Medical and Scientific Advisory Board (MSAB)

Dr. Donald P. Braun, Ph.D. (Chairperson)
Professor of Medicine and Immunology,
Rush Medical College

Director, Scientific Program Development,
Rush Cancer Institute, Chicago, Illinois

Dr. Gregory Curt, M.D.
US Department of Health and Human
Services, Betheseda, Maryland

Dr. Jaime de la Garza Salazar, M.D.
Director General, National Cancer
Institute, Mexico City, Mexico

Dr. Phil Gold, CC, M.D., Ph.D.
Professor of Medicine, Physiology and
Oncology, McGill University, Montréal, Québec

Dr. Jules Harris, M.D.
Professor of Medicine and Immunology,
Rush Medical College, Chicago, Illinois

Dr. Robert Kerbel, Ph.D.
Director, Division of Cancer Biology Research,
Sunnybrook Health Sciences Centre,
Toronto, Ontario

Dr. Lesley Seymour, MBBCh, FCP (SA)
Clinical Trials Group,
National Cancer Institute of Canada,
Kingston, Ontario

Shareholder Information

Corporate Counsel

Tory Haythe
Toronto, Canada

Marusyk Miller & Swain
Ottawa, Canada

Auditors

KPMG LLP
Yonge Corporate Centre
4120 Yonge Street, Suite 500
North York, Ontario
M2P 2B8
Tel: (416) 228-7000
Fax: (416) 228-7123

Transfer Agent and Registrar

Inquiries regarding transfer requirements, lost certificates and changes of address should be directed to the transfer agent.

Montreal Trust Company of Canada
151 Front Street West, 8th Floor
Toronto, Canada
M5J 2N1
Tel: (416) 981-9500
Fax: (416) 981-9800

Inquiries and Form 20-F, Annual and Quarterly Reports

Shareholders and prospective shareholders are invited to call or write to us with questions or requests for additional information. The form 20-F for 1998 filed with the Securities and Exchanges Commission, copies of the 1998 Annual Report and future quarterly reports are available from:

Philippe G. Lacaille
Chairman & CEO
7100 Woodbine Avenue
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Canada L3R 5J2
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Fax: (905) 305-1584
E-mail: info@lorusthera.com
Website: http://www.lorusthera.com

Annual Meeting

The 1999 Annual Meeting of Shareholders will be held on Monday, November 29, 1999 at 2:00 p.m. at:

Canadian Bar Association – Ontario
Education and Meeting Centre
Salon 2 & 3
200 – 20 Toronto Street
Toronto, Ontario

LORUS

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