

PAION Q1#2009

Consolidated Financial Interim Report for the First Quarter of 2009

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PAION AG

Key Figures

(all figures in EUR k unless otherwise noted)	Q1 2009	Q1 2008
Revenues	405	1,651
Research and development expenses	-2,616	-1,637
General and administrative expenses	-1,152	-1,035
Selling and marketing expenses	0	-15
Net result for the period	-3,327	-1,178
Earnings per share in EUR for the period (basic)	-0.14	-0.07
Earnings per share in EUR for the period (diluted)	-0.14	-0.07
Net cash from operating activities	-3,573	5,545
Net cash from investing activities	-25	289
Net cash from financing activities	-164	-158
Average number of group employees	30	51

	31 March 2009	31 Dec. 2008
Intangible assets	11,489	11,336
Cash and cash equivalents	32,358	36,072
Equity	28,596	31,528
Non-current liabilities	13,060	13,426
Balance sheet total	45,649	49,313
Equity ratio	62.6%	63.9%

Interim Group Management Report for the Three-Month Period to 31 March 2009

Overview

The loss for the period in the first three months 2009 of EUR -3,327k was EUR 2,149k higher than in the corresponding prior-year period (EUR -1,178k). This increase is mainly due to lower revenues, higher research and development expenses and a lower financial result. Cash and cash equivalents decreased by EUR 3,714k in the first quarter 2009 and amounted to EUR 32,358k compared to EUR 36,072k as of 31 December 2008. Thus the liquidity situation remains solid.

In January 2009 PAION reported the data of its first study with CNS 7056. The Phase I proof of concept study compared intravenous CNS 7056 to placebo and a standard dose of midazolam, the current gold standard for procedural sedation. The anticipated favourable profile was observed and no safety issues were raised. Volunteers treated with increasing doses of CNS 7056 were successfully sedated at the higher dose cohorts as expected and recovered to full consciousness rapidly. Following the proof of concept, PAION prepared in the first quarter 2009 two further studies with CNS 7056. The start of the studies – one Phase Ib and one Phase IIa study – was reported in April 2009. On 11 May 2009 the positive results of the first part of the Phase I trial were reported.

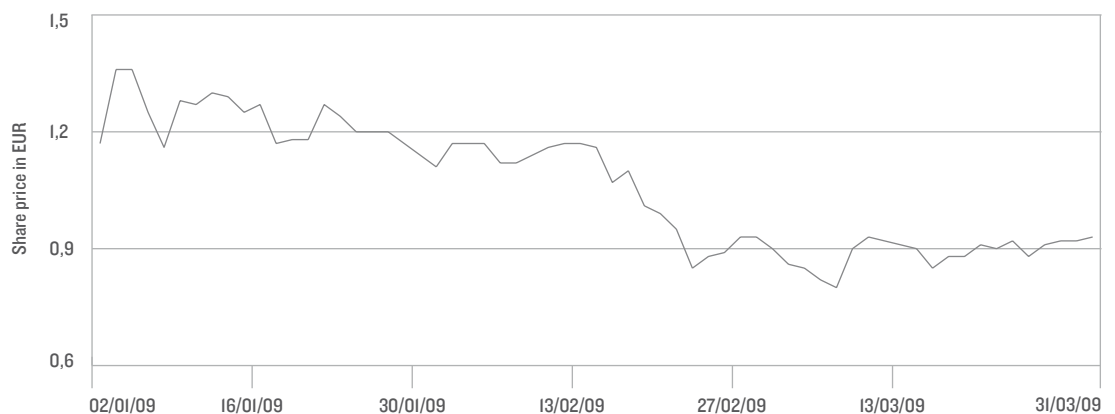
With effect on 19 March 2009 PAION has cancelled the trading of its shares on the Alternative Investment Market (AIM) of the London Stock Exchange. A 40 per cent decline of the number of Depository Interests (DI) since the admission to AIM in June 2008 until the beginning of 2009 and the very low trading volume of PAION shares on AIM led to the conclusion that the additional costs associated with maintaining a second listing on AIM are inappropriate and that it is in the best interests of the company to seek a cancellation of its shares from trading on AIM.

Share Performance

On 6 January 2009 the closing price of PAION share on Xetra was EUR 1.36, also influenced by the general positive market conditions at the beginning of the year. This quote marked the peak price in the first quarter after a closing price of EUR 1.17 at the beginning of 2009. Thereafter the share price decreased steadily. An accelerated decrease occurred on 13 February from EUR 1.17 down to EUR 0.80 on 9 March 2009 which also marked an all-time low on Xetra. This 31.6% decrease was mainly due to general negative market conditions. During this period, worldwide leading indices marked new all-time lows for the year. Furthermore it is assumed, that this development was also intensified by PAION's announcement to de-list from AIM effective of 19 March 2009, underlined by higher selling volumes also on Xetra. Until 31 March 2009 the share price recovered continuously, closing at EUR 0.93. Overall, the share price lost 20.5% on Xetra in the first quarter 2009.

The overall average daily trading volume (Xetra, Frankfurt Stock Exchange resp. all German Stock Exchanges) amounted to 24,644 shares during the first three months of 2009. The trading volume reduced due to lower trading volumes in all securities segments during the first quarter of 2009, compared with the last two quarters in 2008.

Development of the PAION Share Price in the Three-Month Period to 31 March 2009



Overview of Research and Development Activities

a. CNS 7056

CNS 7056 is an innovative short-acting general anaesthetic/sedative that is initially being developed for use in minor medical interventions. Sedatives are used, for example, in endoscopic procedures such as colonoscopies. After intravenous administration to human volunteers CNS 7056 rapidly induces the desired sedation. Importantly, this sedative effect quickly disappears after cessation of administration. This rapid offset of the effect of the substance is due to its metabolism by tissue esterase enzymes that are widely distributed throughout the body. CNS 7056 is being developed as a sedative agent for day case procedures and has additional potential in the indication “induction and maintenance of anaesthesia”. It could also be used as a sedative during artificial respiration in the Intensive Care Unit (ICU).

Clinical Development

In November 2008 PAION reported the successful completion of the first Phase I study with CNS 7056 and published related data on 9 January 2009. In the course of this proof of concept study intravenously administered CNS 7056 was compared to placebo and a standard dose of Midazolam, which is currently the sedative of choice for procedural sedation. The study confirmed the anticipated positive profile of PAION’s drug, with no safety problems occurring. The study comprised increasing dosages of CNS 7056. As expected, volunteers were successfully sedated in the higher dose cohorts and rapidly recovered to full consciousness. During the first quarter of 2009, two further studies were set up: a Phase IIa study (single dose) with patients undergoing endoscopy of the upper gastrointestinal tract and a Phase Ib study (multiple dose) with volunteers undergoing a colonoscopy. On 15 and 20 April the initiation of these trials, which are conducted in the USA and are accordingly billed in US-Dollar, were announced, respectively. On 11 May 2009 the positive results of the first part of the Phase I trial were reported: the effect of CNS 7056 can be reversed by an established antagonist, flumazenil; no re-sedation of the volunteers was observed. These data strengthen the safety profile of CNS 7056.

Cooperation Agreements

CeNeS concluded a licence agreement with Ono Pharmaceuticals in 2007 which allows Ono to develop and market CNS 7056 for the Japanese market.

b. Morphine-6-glucuronide

Morphine-6-glucuronide (M6G), an active morphine metabolite, demonstrated in clinical Phase II and Phase III studies an analgesic effect comparable to morphine, the current “gold standard” for the treatment of severe, postoperative pain. At the same time, the common side effects of morphine administration, such as nausea and vomiting, were significantly reduced with M6G.

Clinical Development

In total, approximately 1,000 patients have already been treated with M6G. In the last Phase III study, however, M6G narrowly failed to demonstrate statistical significance with respect to the incidence and severity of nausea (p-value of 0.052 against a target of <0.050). PAION believes that the positioning and partnering potential of M6G can be optimised and has therefore conducted a more in-depth analysis of the available clinical data. This comprised a total of 769 patients from two Phase II and two Phase III studies and confirmed the analgesic effect of M6G. Furthermore, the data demonstrated a statistically significant reduction in nausea and vomiting. Modelling analyses conducted alongside this meta-analysis to simulate dose-response relationships and pharmacodynamic effects, confirm the product profile of M6G, both in terms of analgesic properties and side effect profile, and in addition reproduce the previously observed longer duration of action of M6G compared to morphine. Based on this model PAION believes that even at increased doses M6G will be better tolerated than equally effective analgesic doses of morphine. In summary, these new analyses support PAION’s view that M6G has a wider therapeutic margin than morphine at equi-analgesic dosages with lower incidence of post-operative nausea and vomiting. PAION believes that these findings will facilitate a data-driven design of a future Phase III programme and will thus increase the probability of success of the clinical development programme and, as such, of out-licensing. Based on these results PAION has re-started the search for a development partner for M6G which was originally initiated by CeNeS.

c. Desmoteplase

Desmoteplase is an intravenously administered substance for dissolving blood clots that is currently being developed for the treatment of acute ischemic stroke.

Clinical Development

So far Desmoteplase was tested in two Phase II studies and one Phase III study for the treatment of ischemic stroke. PAION’s partner, H. Lundbeck A/S, has taken on the further development of Desmoteplase and is supported by PAION in this work. Until market approval Lundbeck plans to perform two additional Phase III studies, recruiting 320 patients each. In December 2008 Lundbeck announced the initiation of this new Phase III program. Unlike the previous studies, this time vessel occlusion must be proven before Desmoteplase is administered.

Cooperation Agreements

Under the extended license agreement, which came into effect in January 2008 and now includes the North American markets, Lundbeck has exclusive global rights to develop and market Desmoteplase. Under this agreement, Lundbeck has agreed to undertake the following:

- Payment of a non-refundable amount of EUR 8 million in advance, on the date the agreement takes effect (payment received in January 2008),
- Assumption of all future costs, especially for clinical development, production development and marketing approval,
- Milestone payments of up to EUR 63 million, of which EUR 38 million are due prior to market approval and EUR 25 million are due upon commencement of marketing activities and the achievement of specific revenue targets, and
- Payment of licence fees (dependent on revenues) which amount to a double-digit percentage, following the deduction of the licence fees PAION has to pay to the original licensor, Bayer Schering Pharma AG.

PAION has reserved the option to co-promote Desmoteplase in Germany, Austria and Switzerland. If PAION decides to exercise this option it will receive a direct share in earnings rather than licence fees based on revenues.

d. CNS 5161

CNS 5161 is an antagonist of the NMDA receptor which may prove beneficial for the treatment of neuropathic pain, i.e. pain caused by irritation or damage of the nervous system. A second potential indication is the treatment of cancer pain.

Clinical Development

PAION completed an open label clinical Phase IIa study using CNS 5161 in December 2008. The study encompassed a total of 24 patients suffering from opioid-resistant cancer pain who were split into six groups receiving ascending higher dosages of CNS 5161 administered six times in total over a period of 24 hours. The primary objective of the study was to define the maximum tolerable dose and to assess the relationship between the plasma concentration of CNS 5161 and changes in pain level. PAION reported the full results on 9 April 2009. Efficacy signals were observed in all but the lowest dose cohort. On the 10-grade numerical pain rating scale (NPRS), mean values dropped by 3.0 points from 6.2 to 3.2 at 32 hours, excluding the first (lowest dose) cohort. This represents approximately a 50% reduction of pain in these patients. EMEA guidelines for neuropathic pain indicate that a 30-50% reduction in pain can be considered a response. The further development of this substance will depend on securing third-party financing.

Cooperation Agreements

In July 2006 CeNeS entered into a development partnership focusing on CNS 5161 with ERGOMED Clinical Research Limited, Frankfurt. This agreement governs the joint development of products at shared costs and income.

e. Solulin

Solulin is an improved variant of the human protein thrombomodulin, an important natural regulator of blood coagulation. Thrombomodulin is capable of inhibiting the activity and formation of thrombin, an endogenous substance which, when produced in excess, can lead to blood clots. In contrast to natural thrombomodulin, which is an integral protein of vascular membranes, Solulin can travel through the blood stream to reach its potential site of action. Animal models demonstrated that Solulin effectively inhibits the formation of blood clots in veins and arteries.

Clinical Development

In 2008 PAION published the results of a clinical Phase I study which involved single and multiple administrations of Solulin. The study was launched mid-2007 and confirmed the substance's good safety profile as well as its anticoagulant mode of action offering good potential to inhibit the activity and formation of thrombin. The tested dosages did not reveal any relevant change in factors seen as key indicators for an increased bleeding propensity. This first clinical study with healthy volunteers focused on safety, tolerability, pharmacokinetics and, as far as can be concluded from laboratory results, also the pharmacological effects of Solulin. As conventional treatments of thrombotic diseases interfere with hemostasis, it is of utmost importance to minimise the bleeding risk inherent in such procedures. Hence, in addition to the regular safety parameters, the study also focused on investigating whether the tested dosages of Solulin had a negative impact on the blood coagulation system. The study revealed that in blood samples taken from the healthy volunteers Solulin was able to dose-dependently block thrombin generation almost completely with a very low impact on hemostasis. Following the completion of the Phase I study and the successful proof of concept, PAION has now initiated the partnering process for the further development of Solulin.

f. Flovagratan

Flovagratan is a substance characterised by a very fast onset of anticoagulation but also very rapid deactivation once intravenous administration is stopped. This is a complementary mode of action to Solulin with an equally fast onset but longer lasting effect. Flovagratan could prove useful as an acute anticoagulant during major surgery such as coronary artery bypass grafting. The substance was previously tested by its originator in two smaller Phase II studies, however in other indications. PAION is conducting additional preclinical studies in preparation for clinical assessment of Flovagratan for the reduction of blood loss during bypass surgery.

Net Assets, Financial Position and Results of Operations

Results of Operations

The loss for the first quarter of 2009 increased by EUR 2,149k year on year to EUR -3,327k. The increase is mainly due to lower revenues, higher research and development expenses and a lower financial result. The revenues of the corresponding prior-year period include a material amount of one-off reimbursements of prior production costs by Lundbeck. The increase of research and development expenses compared to the prior-year period reflects the broader product pipeline of the PAION group, especially the costs for the further development of CNS 7056. The financial result decreased compared to the previous year on the back of lower cash and cash equivalents as well as lower money market interest rates.

	Q1 2009	Q1 2008
	EUR k	EUR k
Revenues	405	1,651
Cost of revenues	-28	-453
Gross profit	377	1,198
Research and development expenses	-2,616	-1,637
General and administrative expenses	-1,152	-1,035
Selling expenses	0	-15
Other income (expenses)	9	-21
Operating expenses	-3,759	-2,708
Operating result	-3,382	-1,510
Financial result	-26	332
Income taxes	81	0
Result for the period	-3,327	-1,178

Revenues of EUR 405k in the first three months of 2009 mainly include the systematic release of deferred income in connection with the license agreement concluded with Lundbeck (EUR 364k) as well as the refund of development expenses by Lundbeck. The revenues in the prior year period furthermore included reimbursements of prior production development costs by Lundbeck according to the licence agreement with Lundbeck.

The cost of revenues incurred in the first quarter of 2009 related as well as in the first quarter 2008 to the development expenses incurred in this period, which were refunded by Lundbeck.

Research and development expenses of EUR 2,616k in the first three months of 2009 increased by EUR 979k compared with the corresponding prior-year period. The increase is primarily attributable to the broader product pipeline compared to the prior year. The main research and development focus was on CNS 7056, M6G and Solulin.

General and administrative expenses remained at the prior-year period level in the first quarter of 2009, amounting to EUR 1,152k (prior-year period: EUR 1,035k).

The financial result for the first three months of 2009 decreased year on year by EUR 358k down to EUR -26k. The main reasons for the decrease are significantly lower money market interest rates as well as the reduction in cash and cash equivalents compared to the prior-year period.

The income taxes are attributable to tax claims for reimbursement of parts of the research and development costs from the British tax authorities.

Net Assets and Financial Position

The total assets as of 31 March 2009 decreased by EUR 3,664k compared to 31 December 2008 and amounted to EUR 45,649k. The decrease was mainly due to a lower equity through the loss of the period and lower cash and cash equivalents. As of 31 March 2009 the equity ratio is 62.6% and is nearly unchanged compared to 31 December 2008 (63.9%). If the subordinate loan borrowed in 2006 and the deferred non-refundable upfront payment from Lundbeck were recognised as economic equity, the equity ratio would increase to 91.2%.

	31 March 2009	31 Dec. 2008	Change
	EUR k	EUR k	EUR k
Non-current assets	11,868	11,746	122
Current assets	33,781	37,567	-3,786
Total assets	45,649	49,313	-3,664
Equity	28,596	31,528	-2,932
Non-current liabilities	13,060	13,426	-366
Current liabilities	3,993	4,359	-366
Total equity and liabilities	45,649	49,313	-3,664

The non-current assets mainly comprise the capitalised development projects of PAION UK Ltd (EUR 11,184k).

The EUR 3,786k decrease in current assets is mainly attributable to the decrease in cash and cash equivalents (EUR 3,714k). The change in cash and cash equivalents stems from the following areas:

	Q1 2009 EUR k	Q1 2008 EUR k
Cash flows from operating activities	-3,573	5,545
Cash flows from investing activities	-25	289
Cash flows from financing activities	-164	-158
Effects of exchange rate changes	48	0
Change in cash and cash equivalents	-3,714	5,676

The negative cash flows from operating activities of EUR 3,573k were mainly due to the loss of the period in the amount of EUR 3,327k.

The negative cash flows from financing activities in the first three months of 2009 and the prior-year period resulted from interest payments for the subordinated loan raised in April 2006.

The decrease of EUR 366k in non-current liabilities is attributable to the proportionate release of the deferred income in connection with the license agreement concluded with Lundbeck.

The decrease of EUR 366k in current liabilities is mainly attributable to the decrease of bonus accruals as well as the decrease of trade liabilities.

Personnel Development

On average, PAION employed 30 employees in the first three months of 2009 (fiscal year 2008: 42 employees).

Risks and Opportunities

Material risks and opportunities relating to future development are presented in detail in the group management report for fiscal year 2008 and have not changed significantly in the first quarter of 2009.

Significant Events Occurring After the Balance Sheet Date

On 9 April 2009 PAION and ERGOMED reported the full data of the Phase IIa study with CNS 5161 in neuropathic cancer pain. The data confirm the efficacy of the substance already at low doses and a good tolerance over a broad dose range.

On 15 April 2009 PAION reported the start of a Phase IIa study with CNS 7056 (single dose). The study will enroll 100 patients undergoing diagnostic endoscopy of the upper gastrointestinal tract.

On 20 April 2009 PAION reported the start of a Phase Ib study with CNS 7056 (repeated dose) in volunteers undergoing colonoscopy. The aim of the study is to examine a variety of (repeated) doses to achieve an overall 30 min sedation time. A further aim of the study is to investigate the effect of an established antagonist, flumazenil. The positive results of this part of the study were reported on 11 May 2009: the effect of CNS 7056 can be reversed by flumazenil and a re-sedation of the volunteers could not be observed. These data strengthen the safety profile of CNS 7056.

Outlook

In 2009 PAION's focus lies on performing the clinical trials with its compound CNS 7056 as well as closing at least one partnering/license agreement. The major part of the research and development expenses is allotted to the Phase Ib and Phase IIa studies with CNS 7056 which were initiated in April 2009. The recruitment of the volunteers and the patients, respectively, is to be completed until end of the year. Furthermore, preclinical studies with Flovagatran are being conducted. These data will be the basis for a decision on the further development of this compound, which will be made in the second half of the year. In the current period only minor costs will be incurred for production development and the production of study medication for future studies.

Since the beginning of 2009 several cost reduction measures were carried out which will lead to sustainable cost savings in the current and future fiscal years. This does not have any impact on the progress of the current projects. In 2009 revenues will result mainly from the proportional release of the deferred income in connection with the milestone payment received from Lundbeck in 2008. Additional revenues are expected from the closing of new cooperation agreements. In total, a negative financial result is expected for the fiscal year.

As of 31 March 2009 PAION's cash and cash equivalents amount to EUR 32.4 million. These provide the necessary flexibility to implement value-generating steps and – based on further optimised cost structures – secure a sufficient cash reach at least until mid 2011. This does not account for further cost reductions, upfront payments, milestone payments and cost reimbursements from existing and future cooperation partners, which could expand the cash reach but may also be used fully or in part for financing additional development activities. The cooperation with Lundbeck alone provides for future milestone payments of up to EUR 63 million, of which up to EUR 38 million will become due prior to market approval.

Aachen, Germany, 13 May 2009

PAION AG

The Management Board

Consolidated Balance Sheet

ASSETS	31 March 2009 EUR	31 Dec. 2008 EUR	31 March 2008 EUR
Non-current assets			
Intangible assets	11,489,018.96	11,336,347.69	118.824,82
Equipment	378,689.69	409,471.11	873.250,54
Other assets	2.16	2.09	0,00
	11,867,710.81	11,745,820.89	992.075,36
Current assets			
Trade receivables	44,537.65	100,449.52	704.472,23
Prepaid expenses and other assets	1,378,865.59	1,395,034.81	1.352.150,05
Cash and cash equivalents	32,358,118.72	36,071,890.73	48.577.689,49
	33,781,521.96	37,567,375.06	50.634.311,77
Total assets	45,649,232.77	49,313,195.95	51.626.387,13

EQUITY AND LIABILITIES	31 March 2009 EUR	31 Dec. 2008 EUR	31 March 2008 EUR
Equity			
Share capital	24,602,919.00	24,602,919.00	16.755.552,00
Capital reserve	88,574,408.37	88,511,062.55	85.823.015,23
Translation reserve	-1,844,905.20	-2,177,128.79	0,00
Loss carryforward	-79,409,073.92	-66,828,608.63	-66.828.608,63
Loss for the period	-3,327,133.63	-12,580,465.29	-1.177.829,10
	28,596,214.62	31,527,778.84	34.572.129,50
Non-current liabilities			
Provisions	1,419,330.90	1,426,929.28	0,00
Financial liabilities	6,832,758.10	6,824,995.87	6.669.917,77
Finance lease liabilities	0.00	0.00	43.439,00
Deferred income	4,807,828.30	5,174,242.44	6.202.831,17
	13,059,917.30	13,426,167.59	12.916.187,94
Current liabilities			
Trade payables	1,454,790.16	1,591,854.98	1.969.369,09
Provisions	547,159.18	867,153.17	289.051,58
Other current financial liabilities	32,010.40	0.00	0,00
Current portion of finance lease liabilities	43,437.00	61,760.00	72.247,00
Other current liabilities	424,186.87	372,824.81	328.423,38
Current portion of deferred income	1,491,517.24	1,465,656.56	1.478.978,64
	3,993,100.85	4,359,249.52	4.138.069,69
Total equity and liabilities	45,649,232.77	49,313,195.95	51.626.387,13

Consolidated Statement of Comprehensive Income

EUR	1 January – 31 March 2009	1 January – 31 March 2008
Revenues	404,950.72	1,651,216.28
Cost of revenues	-28,032.99	-452,626.55
Gross profit	376,917.73	1,198,589.73
Research and development expenses	-2,616,189.81	-1,637,296.69
General and administrative expenses	-1,152,119.92	-1,034,840.51
Selling and marketing expenses	0.00	-15,794.29
Other income (expenses). net	8,984.66	-20,821.28
Operating expenses	-3,759,325.07	-2,708,752.77
Operating result	-3,382,407.34	-1,510,163.04
Financial income	171,087.14	484,405.35
Financial expenses	-196,773.60	-152,071.41
Financial result	-25,686.46	332,333.94
Loss for the period before taxes	-3,408,093.80	-1,177,829.10
Income taxes	80,960.17	0.00
Loss for the period	-3,327,133.63	-1,177,829.10
of which attributable to other shareholders	0.00	0.00
of which attributable to shareholders of PAION AG	-3,327,133.63	-1,177,829.10
Foreign currency translation of subsidiaries	332,223.59	0.00
Other comprehensive income	332,223.59	0.00
Total comprehensive income	-2,994,910.04	-1,177,829.10
of which attributable to other shareholders	0.00	0.00
of which attributable to shareholders of PAION AG	-2,994,910.04	-1,177,829.10
Earnings per share (basic)	-0.14	-0.07
Earnings per share (diluted)	-0.14	-0.07

Consolidated Cash Flow Statement

EUR	1 January – 31 March 2009	1 January – 31 March 2008
Cash flows from operating activities:		
Net result for the period	-3,327,133.63	-1,177,829.10
Reconciliation of net profit (loss) for the period to cash flows from operating activities:		
Amortization/depreciation and non-cash exchange rate changes of fixed assets	-97,005.11	82,423.37
Loss/Profits from the disposal of non-current assets	0.00	1,346.44
Interest expenses and interest income	25,686.46	-332,333.94
Release of investment grants	0.00	-6,108.30
Release of deferred income	-377,369.76	0.00
Expenses from stock option plans	63,345.82	85,742.20
Change in assets and liabilities which are not attributable to investing or financing activities:		
Trade receivables	55,911.87	72,334.10
Prepaid expenses and other assets	68,845.31	-804,830.29
Trade payables	-137,065.26	-325,448.52
Provisions	-338,506.07	-132,365.93
Other current liabilities	51,361.99	9,574.73
Deferred income	36,816.30	7,636,375.64
Non-cash exchange losses/gains	283,748.25	0.00
Interest received	118,412.14	436,019.79
Net cash used in operating activities	-3,572,951.69	5,544,900.19
Cash flows from investing activities:		
Cash paid for investments in intangible assets and equipment	-24,884.81	-31,250.05
Cash received from the sale of intangible assets and equipment	0.00	320,529.05
Net cash used in investing activities	-24,884.81	289,279.00
Cash flows from financing activities:		
Interest paid	-145,555.89	-139,290.88
Payment of finance lease liabilities	-18,856.00	-18,322.00
Net cash used in financing activities	-164,411.89	-157,612.88
Change in cash and cash equivalents	-3,762,248.39	5,676,566.31
Effect of exchange rate changes on cash	48,476.38	0.00
Cash and cash equivalents at beginning of the period	36,071,890.73	42,901,123.18
Cash and cash equivalents at end of the period	32,358,118.72	48,577,689.49
Composition of cash and cash equivalents at the end of the period:		
Cash	32,358,118.72	48,577,689.49

Consolidated Statement of Changes in Equity

EUR	Share capital	Capital reserve	Translation reserve	Loss carryforward	Equity
31 December 2007	16,755,552.00	85,737,273.03	0.00	-66,828,608.63	35,664,216.40
Total comprehensive income	0.00	0.00	0.00	-1,177,829.10	-1,177,829.10
Additional contribution to the capital reserve due to the issue of options	0.00	85,742.20	0.00	0.00	85,742.20
31 March 2008	16,755,552.00	85,823,015.23	0.00	-68,006,437.73	34,572,129.50
Total comprehensive income	0.00	0.00	-2,177,128.79	-11,402,636.19	-13,579,764.98
Issue of shares	7,847,367.00	0.00	0.00	0.00	7,847,367.00
Contribution to the capital reserve	0.00	3,531,315.15	0.00	0.00	3,531,315.15
Cost of raising capital	0.00	-981,364.40	0.00	0.00	-981,364.40
Additional contribution to the capital reserve due to the issue of options	0.00	138,096.57	0.00	0.00	138,096.57
31 December 2008	24,602,919.00	88,511,062.55	-2,177,128.79	-79,409,073.92	31,527,778.84
Total comprehensive income	0.00	0.00	332,223.59	-3,327,133.63	-2,994,910.04
Additional contribution to the capital reserve due to the issue of options	0.00	63,345.82	0.00	0.00	63,345.82
31 March 2009	24,602,919.00	88,574,408.37	-1,844,905.20	-82,736,207.55	28,596,214.62

Selected Explanatory Notes to the Consolidated Interim Financial Statements as of 31 March 2009

General

The quarterly report of PAION AG includes interim consolidated financial statements and an interim group management report in accordance with the provisions of Secs. 37x (3) and 37w (2) to (4) WpHG [“Wertpapierhandelsgesetz”: German Securities Trading Act] in conjunction with Sec. 37y WpHG. The consolidated financial statements were prepared in accordance with the provisions of the International Financial Reporting Standards (IFRSs) for interim financial reporting. The interim group management report was prepared in accordance with the relevant provisions of the German Securities Trading Act.

The interim consolidated financial statements comprise PAION AG as the parent company, registered at Martinstrasse 10–12, 52062 Aachen, Germany, and the wholly-owned subsidiaries, which are fully consolidated:

- PAION Deutschland GmbH, Aachen/Germany
- PAION Holdings UK Ltd, Cambridge/UK
- PAION UK Ltd, Cambridge/UK
- CeNeS Drug Delivery Ltd, Cambridge/UK
- TheraSci Limited, Cambridge/UK
- CeNeS Pharmaceuticals Inc., Norwood/USA
- CeNeS (Bermuda) Ltd, Bermuda

Basis of Accounting

The interim consolidated financial statements have been prepared in accordance with Sec. 315a HGB [“Handelsgesetzbuch”: German Commercial Code] and IFRSs, as adopted by the EU, and the interpretations of the International Financial Reporting Interpretations Committee (IFRIC). All IFRSs issued by the International Accounting Standards Board (IASB), London, UK, which were effective as of the balance sheet date of 31 March 2008 and applied by PAION, were adopted by the European Commission for application in the EU.

The following new announcements were published by the IASB during the reporting period and will be applied as soon as they come into effect if at that point an adoption by the European Commission has taken place.

- IFRIC 18: The IASB published IFRIC 18 Transfers of Assets from Customers in January 2009. IFRIC 18 clarifies the accounting methods for agreements in which a company receives assets or cash from a customer that it must then use to either connect that customer to a network or provide that customer with ongoing access to goods or services (e.g. energy, gas, water). IFRIC 18 must be applied to assets transferred on or after 1 July 2009. This will not have any effects on the Group’s net assets, financial position and results of operations or lead to further disclosures.
- Amendment to IFRS 7 Financial Instruments: Disclosures: On 5 March 2009 the IASB published amendments to IFRS under the title “Improving Disclosures about Financial Instruments – Amendments to IFRS 7”. The amendments relate to disclosures about fair value measurements and liquidity risk. The amendments require that fair value measurement disclosures use a three-level fair value hierarchy and that disclosures are extended. Furthermore the disclosures related about liquidity risks are clarified and extended. For this disclosures are required about maturity of financial liabilities, broken down by non-derivative and derivative financial instruments and the corresponding qualitative disclosures about the management of liquidity risk are changed. The amendments are effective for annual periods beginning on or after 1 January 2009; earlier application would be permitted. In the first year of application, comparative disclosures are not required. The application of these amendments could result in additional disclosure obligations in future consolidated financial statements. The amendments do not have any effects on the Group’s net assets, financial position and results of operations.
- Amendments to IFRIC 9 and IAS 39: On 12 March the IASB published amendments to IFRIC 9 Reassessment of Embedded Derivatives and IAS 39: Financial Instruments: Recognition and Measurement. The amendments clarify the accounting of embedded derivatives in entities that make use of the option to reclassify financial instruments which was published by the IASB in October 2008. The amendments clarify that in case of a reclassification all embedded derivatives have to be measured and if necessary separated. The amendments apply retrospectively and are required to be

applied for annual periods ending on or after 30 June 2009. Since PAION does not own any financial instruments affected by the amendments, the amendments do not have any effects on the Group's net assets, financial position and results of operations.

- On 16 April 2009 the IASB published the collective standard „Improvements to IFRSs“, which implements minor changes to the existing IFRSs. The standard contains 15 amendments to 12 standards. The majority of the amendments must be applied to fiscal years commencing on or after 1 January 2010. This will not have any effects on the Group's net assets, financial position and results of operations or lead to further disclosures.

The provisions of IAS 34, “Interim Financial Reporting”, have been applied. The interim financial statements as of 31 March 2009 should be read in conjunction with the consolidated financial statements as of 31 December 2008.

The preparation of interim consolidated financial statements in accordance with IFRSs requires management to make estimates and assumptions which have an effect on the amount of recognised assets and liabilities, income and expenses and contingent liabilities. Actual amounts may differ from these estimates.

The interim consolidated financial statements do not contain any segment information as no material reportable segments could be identified.

Consolidation Principles

The consolidation principles used in the interim consolidated financial statements as of 31 March 2009 were the same as those used in the consolidated financial statements as of 31 December 2008.

Foreign Currency Translation

The consolidated financial statements are shown in Euro, which is the functional currency of PAION AG and the reporting currency of the Group. Each company within the Group defines its own functional currency. This is the Euro in the case of the German companies, whereas the UK-based companies use Pound Sterling as their functional currency. All items on the respective financial statements of each company are initially converted to the functional currency at the exchange rate applicable on the transaction date. Monetary assets and liabilities denominated in a foreign currency are converted to the functional currency on the reporting date at the exchange rate applicable on that date. All ensuing currency differences are recognised in profit or loss with the exception of exchange rate gains and losses from intra-Group loans classified in accordance with IAS 21 as net investments in foreign business operations; these are recognised in equity.

The assets and liabilities of the foreign companies are converted to Euro on the balance sheet reporting date at the exchange rate applicable on that date. These include any and all goodwill in connection with the acquisition of a foreign company and any and all fair value adjustments to the book values of the foreign company's assets and liabilities. Equity components are converted to Euro at historical rates at the time of initial consolidation. Expenses and income are converted to Euro at average monthly exchange rates. The resulting currency differences are accounted for separately within equity.

Accounting Policies

The accounting policies used in the interim consolidated financial statements as of 31 March 2009 were the same as those used in the consolidated financial statements as of 31 December 2008 except for the changes resulting from the revision of IAS 1.

Tax Effects on Other Comprehensive Income

Because of the negative results of the PAION Group and the existing tax losses carried forward no income taxes are being paid at the moment. In the reporting period the Other Comprehensive Income (foreign currency translation of foreign subsidiaries) does not have any tax effects.

Related Parties

The relationships with related parties have not changed in comparison to those applied in the consolidated financial statements as of 31 December 2008.

Significant Events Occurring After the Balance Sheet Date

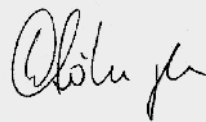
On 9 April 2009 PAION and ERGOMED reported the full data of the Phase IIa study with CNS 5161 in neuropathic cancer pain. The data confirm the efficacy of the substance already at low doses and a good tolerance over a broad dose range.

On 15 April 2009 PAION reported the start of a Phase IIa study with CNS 7056 (single-dose). The study will enroll 100 patients undergoing diagnostic endoscopy of the upper gastrointestinal tract.

On 20 April 2009 PAION reported the start of a Phase Ib study with CNS 7056 (repeated dose) in volunteers undergoing colonoscopy. The aim of the study is to examine a variety of (repeated) doses to achieve an overall 30 min sedation time. A further aim of the study is to investigate the effect of an established antagonist, flumazenil. The positive results of this part of the study were reported on 11 May 2009: the effect of CNS 7056 can be reversed by flumazenil and a re-sedation of the volunteers could not be observed. These data strengthen the safety profile of CNS 7056.

Aachen, Germany 13 May 2009

PAION AG



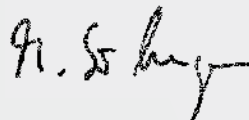
Dr. Wolfgang Söhngen



Alexander Vos



Bernhard Hofer



Dr. Mariola Söhngen



Dr. Gavin Kilpatrick

Review Report

To PAION AG, Aachen:

We have reviewed the interim condensed consolidated financial statements, comprising the balance sheet, statement of comprehensive income, cash flow statement, statement of changes in equity and selected explanatory notes, and the interim group management report of PAION AG, Aachen, for the period from January 1 to March 31, 2009 which are part of the quarterly financial report pursuant to SEC 37x (3) WpHG [“Wertpapierhandelsgesetz”: German Securities Trading Act]. The preparation of the interim condensed consolidated financial statements in accordance with the IFRSS on interim financial reporting as adopted by the EU and of the group management report in accordance with the requirements of the WpHG [“Wertpapierhandelsgesetz”: German Securities Trading Act] applicable to interim group management reports is the responsibility of the Company’s Management. Our responsibility is to issue a report on the interim condensed consolidated financial statements and the interim group management report based on our review.

We conducted our review of the interim condensed consolidated financial statements and the interim group management report in accordance with German generally accepted standards for the review of financial statements promulgated by the Institut der Wirtschaftsprüfer [Institute of Public Auditors in Germany] (IDW) and additionally in accordance with the International Standard on Review Engagements “Review of Interim Financial Information Performed by the Independent Auditor of the Entity” (ISRE 2410). Those standards require that we plan and perform the review to obtain a certain level of assurance in our critical appraisal to preclude that the interim condensed consolidated financial statements are not prepared, in all material respects, in accordance with IFRSS on interim financial reporting as adopted by the EU and that the interim group management report has not been prepared, in all material respects, in accordance with the provisions of the WpHG. A review is limited primarily to making inquiries of company personnel and applying analytical procedures and thus does not provide the assurance that we would obtain from an audit of financial statements. In accordance with our engagement, we have not performed a financial statement audit and, accordingly, we do not express an audit opinion.

Based on our review nothing has come to our attention that causes us to believe that the interim condensed consolidated financial statements are not prepared, in all material respects, in accordance with IFRSS on interim financial reporting as adopted by the EU and that the interim group management report has not been prepared, in all material respects, in accordance with the provisions of the WpHG applicable to interim group management reports.

Cologne, Germany, May 13, 2009
Ernst & Young AG
Wirtschaftsprüfungsgesellschaft
Steuerberatungsgesellschaft

(s) Gockel	(s) Schlöder
Wirtschaftsprüfer	Wirtschaftsprüfer
[German Public Auditor]	[German Public Auditor]

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