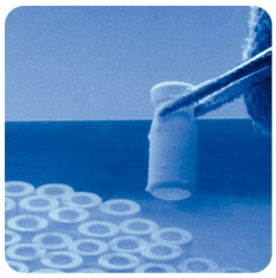

First Quarter Results

Transition Therapeutics Inc.

2002

To Our Shareholders,

During the first quarter of fiscal 2002, Transition Therapeutics Inc. was extremely active. We focused our efforts and resources on increasing shareholder value through advancement of our research programs and pursuing partnership opportunities with several pharmaceutical and biotechnology companies.

The proposed merger announced with Waratah Pharmaceuticals Inc. (”Waratah”) subsequent to the quarter-end was a direct result of that activity. After exploring several strategic opportunities to further enhance shareholder value, we announced an agreement in principle to combine the business and operations of Transition and Waratah by way of a plan of arrangement.

The proposed merger, announced October 29, 2001 is expected to complement and strengthen our management expertise, enhance our cash position, increase market awareness and decrease shareholder risk through the addition of another strong technology to our existing product portfolio for the treatment of Multiple Sclerosis (MS) and diabetes. Waratah's novel Islet Neogenesis Therapy (I.N.T.™) for the treatment of insulin dependent diabetes represents a new paradigm in the treatment of diabetes and has the potential to replace insulin injections and diabetes-related transplants through the administration of certain growth factors which stimulate the regeneration of insulin-secreting islet cells. The addition of this new technology to Transition's already strong product pipeline will further increase the Company's probability of clinical success and the achievement of profitable operations.

Under the terms of the agreement in principle, it is proposed that shareholders of Waratah receive 0.8333 common shares of Transition for each one share of Waratah held. Transition shares will remain unchanged and no additional consideration or benefit will be made available to any shareholder. The combined company will have a strengthened Board of Directors with expertise in small biotech and large pharmaceutical companies as well as in capital markets and regulatory compliance. Stephen Brand, Waratah's current President and Chief Scientific Officer, will continue in the same position for the combined company and I will be Chief Executive Officer. Transition expects that the transaction will be completed by December 31, 2001 subject to negotiation of a definitive agreement, due diligence, formal valuations, regulatory approvals, shareholder approval and fairness opinions for both companies. The provisions of Ontario Securities Commission rule 61-501 applicable to the related party aspects of the transaction will be complied with.

Financial Highlights

During the first quarter of fiscal 2002, Transition continued to optimize its financial structure. At September 30, 2001, Transition had working capital of $7.5 million, including cash and short-term deposits of $7.0 million, compared to working capital of $7.9 million at June 30, 2001. Management is committed to preserving its cash through a disciplined cost management program that strictly controls all non-programmed spending.

The net loss for the first quarter of fiscal 2002 increased to $522,197 or ($0.02) per share from $208,925 or ($0.02) per share for the same quarter in fiscal 2001. Research and development expenses increased to $346,872 for the three months ended September 30, 2001 from $85,037 in the first quarter of fiscal 2001. This increase is a result of additional research and the growth in scientific personnel required to quickly advance the Company's MS, diabetes and restenosis programs. General and administrative expenses were $253,932 for the first quarter of fiscal 2002 compared to $116,035 in the

To Our Shareholders,

first quarter fiscal 2001. The increase was required to support research and development activities, enhance Company awareness and comply with regulatory requirements.

Transition continues to advance its research programs, and expects to file an Investigational New Drug submission for lead compounds in MS and diabetes products in June 2002. As a Company committed to building shareholder value, we will continue to identify and capitalize on new and existing opportunities that will ensure the achievement of our strategic goal: making Transition a successful global biotechnology company.

On behalf of the Board, I thank everyone at Transition for continuing to support this Company through talent and dedication. I look forward to reporting on a successful merger of Transition and Waratah and on the exciting advancements of the combined company in the months ahead.

Tony Cruz
President & CEO
Transition Therapeutics Inc.

MANAGEMENT'S DISCUSSION & ANALYSIS

The following information should be read in conjunction with the unaudited interim financial statements and the related notes included herein as well as the 2001 audited financial statements and the related notes, which are prepared in accordance with Canadian generally accepted accounting principles. Except for historical information, the following report includes statements which are forward looking. Readers are cautioned that the actual results may differ materially from the results projected in any forward statements.

Overview

Transition Therapeutics Inc. (the "Company") is a Canadian biotechnology company developing products for the treatment of Multiple Sclerosis ("MS"), diabetes and restenosis. The Company commenced operations in July 1998, and has devoted its resources primarily to fund its research and development programs. The Company has not generated positive cash flow from operations since inception and is considered to be in the development stage. All revenue has been generated from interest income on surplus funds and the sale of reagents. The Company has incurred a cumulative deficit since inception on July 6, 1998 to September 30, 2001 of $2,805,789. Losses are expected to continue for the next several years as the Company invests in research and development, pre-clinical studies, clinical trials and regulatory compliance.

Results of operations

For the three months ended September 30, 2001, the Company recorded a net loss of $522,197 ($0.02 per common and Class B share) compared to a net loss of $208,925 ($0.02 per common share) for the three months ended September 30, 2000. The increase in the loss from fiscal 2001 is due to the net effect of higher expenditures, which were partially offset by higher interest income.

Revenue

Interest income for the three months ended September 30, 2001 was $90,162 as

compared to interest expense of $1,115 for the three months ended September 30, 2000. Interest income resulted from increased cash and cash equivalents and short-term investments. Those balances increased by $6,880,820 between September 30, 2000 and September 30, 2001 primarily due to the completion of a private placement financing in October, 2000 and the Company's initial public offering in February, 2001, which raised combined net proceeds of $9,401,246. Interest income is expected to decline during the second quarter of fiscal 2002 due to lower cash balances resulting from ongoing expenditures and from lower yields on cash and cash equivalents and short term investments.

Research and development, net

Research and development expenses increased to $346,872 for the three months ended September 30, 2001 from $85,037 for the same period in fiscal 2001. The primary reasons for the increase in expenditures included: an increase in research sponsorship agreements; the hiring of four new scientists and a Director of Clinical Development and Manufacturing; the addition of two new laboratory facilities; and an increase in patent costs to broaden the Company's patent position. Research and development expenses are expected to increase during the second and third quarters of fiscal 2002 as the Company completes pre-clinical toxicity studies for its MS interferon combination therapy.

General and administrative expenses

General and administrative expenses increased to $253,932 for the three months ended September 30, 2001 from $116,035 for the same period in fiscal 2001. The primary reasons for the increase in expenditures included: the addition of a Director of Finance, and incurring expenditures for regulatory and investor relations activities. The Company anticipates a similar level of general and administrative expenses for the second quarter of fiscal 2002 as were incurred in the first quarter of fiscal 2002.

Financing activities

During August, 2001 the Company raised net proceeds of $117,188 from the issuance of 93,750 common shares through the exercise of share purchase warrants. As at September 30, 2001, the Company has 3,578,750 share purchase warrants outstanding, and if exercised would generate maximum cash proceeds to the Company of $4,473,437.

In the future, the Company will need to raise additional funds to continue to advance its research and development programs, to continue pre-clinical studies and to fund potential future clinical trials. The Company intends to seek such funds through public or private placements, corporate collaborations or partnership arrangements and from other sources.

Liquidity and capital resources

The Company's cash and cash equivalents plus short-term investments and the Company's working capital position were $7,005,925 and $7,452,994 respectively at September 30, 2001, down from June 30, 2001 balances of $7,604,138 and $7,880,155. The decreases resulted primarily from the net loss during the three months ended September 30, 2001 and the decrease in accounts payable and accrued liabilities offset by the proceeds of the issuance of common shares on the exercise of share purchase warrants.

Capital expenditures

During the three months ended September 30, 2001, the Company's capital expenditures were $25,600, as compared to $828 for the three months ended September 30, 2000. During the three months ended September 30, 2001, the primary capital expenditures were office equipment and furniture to support the increased staffing levels. The Company does not anticipate any significant capital expenditures during the second quarter of fiscal 2002.

Risks and uncertainties

Prospects for companies in the biopharmaceutical industry are generally regarded as uncertain given the nature of the industry and, accordingly, investments in such companies should be regarded as speculative. The Company's technologies are currently in the research and development stage, which is the riskiest stage for a company in the biopharmaceutical industry. It is not possible to predict, based upon studies in animals, whether a new therapeutic or device will prove to be safe and effective in humans. The Company has not introduced a product into the market and there is no assurance that research and development programs conducted by the Company will result in any commercially viable products.

The Company has incurred losses and anticipates that its losses will increase as it continues its research and development and potential future clinical trials and eventually seeks regulatory approval for the sale of its products. If a product is approved for sale, there is no assurance that the Company will generate adequate funds to continue development or will ever achieve profitable operations. There are many factors such as competition, proprietary rights, patent protection and the regulatory environment, that can influence the Company's ability to be profitable.

From time to time, the Company will seek additional funding through public or private placements, corporate collaborations or partnership arrangements. The Company's ability to access the capital markets or to enlist partners is mainly dependent on the progress of its research and development and regulatory approval of its products. There is no assurance that additional funding will be available on acceptable terms, if at all.

To continue the Company's research and development programs and to conduct future clinical trials, the Company will rely upon employees, collaborators and other third party relationships. There is no assurance that the Company will be able to maintain or establish these relationships as required.

Market prices for securities of biotechnology companies may be highly volatile and subject to significant fluctuation and may not necessarily be related to the operating or other performances of such companies.

Outlook

On October 29, 2001, the Company announced that it has reached an agreement in principle with Waratah Pharmaceuticals Inc. ("Waratah") to combine the business and operations of the two companies by way of a plan of arrangement. Shareholders of Waratah will receive 0.8333 common shares of the Company for each share of Waratah held. The Company's shares will remain unchanged. The Company and Waratah have appointed a joint interim executive committee to provide strategic guidance in merging the operations of the two companies. It is anticipated that the effective date of this

transaction will be December 31, 2001 subject to negotiation of a definitive agreement, due diligence, formal valuations, regulatory approvals, shareholder approval and fairness opinions for both companies. The provisions of Ontario Securities Commission rule 61-501 applicable to the related party aspects of the transaction will be complied with. It is anticipated that this proposed transaction will be accounted for using the purchase method with the Company identified as the acquirer.

The combined company intends to file Investigational New Drug ("IND") submissions with the regulatory authorities in 2002 for both the Company's MS interferon combination therapy and Waratah's Islet Neogenesis Therapy (I.N.T.™) for Type I diabetes. Upon successful review of the INDs by regulatory authorities, Phase I or Phase I/II clinical trials will commence.

The combined company also intends to continue the development of the combined product pipeline and seek corporate partners who are interested in establishing licensing, co-development and other such relationships.

CONSOLIDATED BALANCE SHEETS

	Unaudited September 30, 2001 $	Audited June 30, 2001 $
ASSETS		
Current		
Cash and cash equivalents	4,005,925	4,604,138
Short-term investments	3,000,000	3,000,000
Interest receivable	168,050	122,436
GST receivable	19,507	117,969
Accrued accounts receivable	12,000	12,000
Investment tax credits receivable	152,538	131,400
Deposits on collaborations	130,111	102,874
Prepaid expenses and other assets	226,692	217,381
Total current assets	**7,714,823**	**8,308,198**
Capital assets, net	321,911	312,989
	8,036,734	**8,621,187**
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current		
Accounts payable and accrued liabilities	232,272	398,486
Current portion of leasehold inducement	3,698	3,698
Current portion of obligation under capital leases	25,859	25,859
Total current liabilities	**261,829**	**428,043**
Leasehold inducement	28,046	28,970
Obligation under capital leases	63,861	76,167
Total liabilities	353,736	533,180
Commitments [*note 7*]		
Subsequent events [*note 10*]		
Shareholders' equity		
Share capital [*notes 3 and 4*]	10,488,787	10,371,599
Deficit	(2,805,789)	(2,283,592)
Total shareholders' equity	**7,682,998**	**8,088,007**
	8,036,734	**8,621,187**

See accompanying notes

CONSOLIDATED STATEMENTS OF LOSS AND DEFICIT

Unaudited	Three-month period ended September 30, 2001 $	Three-month period ended September 30, 2000 $	Cumulative since inception on July 6, 1998 $
REVENUE			
Product	-	-	58,021
EXPENSES			
Research and development, net [*note 5*]	346,872	85,037	1,578,436
General and administrative	253,932	116,035	1,556,817
Amortization	11,555	6,738	52,224
	612,359	207,810	3,187,477
Loss before the undernoted	(612,359)	(207,810)	(3,129,456)
Interest income (expense)	90,162	(1,115)	323,667
Net loss for the period	**(522,197)**	**(208,925)**	**(2,805,789)**
Deficit, beginning of period	(2,283,592)	(529,808)	-
Deficit, end of period	**(2,805,789)**	**(738,733)**	**(2,805,789)**
Net loss per common and Class B share	**(0.02)**	**(0.02)**	

See accompanying notes

CONSOLIDATED STATEMENTS OF CASH FLOWS

Unaudited	Three-month period ended September 30, 2001 $	Three-month period ended September 30, 2000 $	Cumulative since inception on July 6, 1998 $
OPERATING ACTIVITIES			
Net loss for the period	(522,197)	(208,925)	(2,805,789)
Add (deduct) items not involving cash			
Amortization	16,678	6,738	68,732
Amortization of leasehold inducement	(924)	(924)	(5,236)
Write-off of accrued accounts receivable	-	-	64,528
	(506,443)	(203,111)	(2,677,765)
Net change in non-cash working capital balances related to operations [*note 6*]	(171,052)	6,963	(439,096)
Cash used in operating activities	**(677,495)**	**(196,148)**	**(3,116,861)**
INVESTING ACTIVITIES			
Purchase of short-term investments	-	-	(4,240,000)
Maturity of short-term investments	-	-	1,240,000
Purchase of capital assets	(25,600)	(828)	(273,912)
Cash used in investing activities	**(25,600)**	**(828)**	**(3,273,912)**
FINANCING ACTIVITIES			
Repayment of obligation under capital leases	(12,306)	(3,512)	(27,011)
Proceeds from issuance of special warrants, net	-	-	4,914,941
Proceeds from issuance of common shares, net	117,188	60	5,508,768
Cash provided (used) in financing activities	**104,882**	**(3,452)**	**10,396,698**
Net increase (decrease) in cash and cash equivalents during the period	**(598,213)**	**(200,428)**	**4,005,925**
Cash and cash equivalents, beginning of period	4,604,138	285,533	-
Cash and cash equivalents, end of period	**4,005,925**	**85,105**	**4,005,925**

See accompanying notes

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

Transition Therapeutics Inc. [the "Company"] is a biopharmaceutical development company, incorporated on July 6, 1998 under the Business Corporations Act (Ontario). The Company is engaged in the business of developing products for the treatment of Multiple Sclerosis, diabetes and restenosis. To date, the Company has not earned significant revenues and is considered to be in the development stage.

The continuation of the Company's research and development activities and the commercialization of the targeted therapeutic products is dependant on the Company's ability to complete its research and development programs, achieve future profitable operations and finance its cash requirements.

These consolidated financial statements include the accounts of Transition Therapeutics Leaseholds Inc., its wholly-owned subsidiary, incorporated on March 10, 2000 under the Business Corporations Act (Ontario).

Information with respect to the June 30, 2001 balance sheet is derived from the Company's audited consolidated financial statements. These consolidated financial statements have been prepared using the same accounting principles used in the audited consolidated financial statements for the period ended June 30, 2001, except for the accounting principle discussed in Note 2. Certain information and note disclosures normally included in financial statements prepared in accordance with Canadian generally accepted accounting principles have been omitted. It is suggested that these interim consolidated financial statements should be read in conjunction with the consolidated financial statements for the year ended June 30, 2001.

2. CHANGE IN ACCOUNTING POLICY

Loss per common and Class B share

In the first quarter of fiscal 2002, the Company retroactively adopted the new recommendations of the CICA relating to loss per share. Pursuant to the new recommendations, basic loss per common and Class B share is determined by dividing the net loss attributable to common shares and Class B shares by the weighted average number of common and Class B shares outstanding during the period. Contingently returnable common shares are excluded when determining the weighted average number of common and Class B shares outstanding. Fully diluted loss per common and Class B share is in accordance with the treasury stock method and is based on the weighted average number of common and Class B shares and dilutive common and Class B share equivalents outstanding during the period. The fully diluted loss per common and Class B share has not been presented as it is anti-dilutive.

The weighted average number of shares used in the computation of basic loss per common and Class B share for the three months ended September 30, 2001 is 23,356,107 (three months ended September 30, 2000 - 12,545,099).

For the three months ended September 30, 2001, 1,172,901 (three months ended September 30, 2000 - 1,204,901) contingently returnable common shares were excluded from the basic loss per common and Class B share calculation.

3. SHARE CAPITAL

[a] Authorized

Unlimited common shares

On October 10, 2000, the Company subdivided the outstanding and issued common shares on the basis of 3.25649 common shares for each issued and outstanding common share. All share and loss per share figures have been retroactively adjusted to reflect this change.

[b] Issued and outstanding and changes during the period

Common Shares	#	$
Balance, June 30, 2001	19,975,000	6,968,948
Exercise of share purchase warrants	93,750	117,188
Balance, September 30, 2001	**20,068,750**	**7,086,136**

Class B Shares	#	$
Balance, June 30, 2001 and September 30, 2001	**4,500,000**	**3,402,651**
Total common and Class B shares, September 30, 2001	**24,568,750**	**10,488,787**

[c] Stock options and share purchase warrants

Share purchase warrants	#
Share purchase warrants outstanding, June 30, 2001	3,672,500
Share purchase warrants exercised	(93,750)
Share purchase warrants outstanding, September 30, 2001	**3,578,750**

The maximum possible cash proceeds to the Company from the exercise of the share purchase warrants are $4,473,437.

Stock options	#
Stock options outstanding, June 30, 2001	1,435,000
Stock options issued	200,000
Stock options outstanding, September 30, 2001	**1,635,000**

The maximum possible cash proceeds to the Company from the exercise of the stock options are $1,829,500.

4. STOCK-BASED COMPENSATION PLAN

A summary of options outstanding as at September 30, 2001 under the Company's Stock Option Plan is presented below:

Exercise Price $	Number of Outstanding Options #	Expiry date	Number of Exercisable Options #
0.80	**640,000**	October 24, 2005	**231,200**
1.25	**765,000**	February 27, 2006	**356,656**
1.25	**10,000**	June 18, 2006	**1,104**
1.35	**20,000**	June 13, 2006	**5,000**
1.30	**25,000**	September 23, 2006	**25,000**
1.55	**25,000**	September 18, 2006	**3,124**
1.67	**150,000**	July 8, 2006	**30,000**
	1,635,000		**652,084**

5. RESEARCH AND DEVELOPMENT PROJECTS

Treatment of Multiple Sclerosis

	$
Cumulative research and development expenses as at June 30, 2001	212,563
Research and development expenses for the three-month period ended September 30, 2001	102,738
Cumulative research and development expenses	**315,301**

Treatment of Diabetes and Obesity

	$
Cumulative research and development expenses as at June 30, 2001	148,311
Research and development expenses for the three-month period ended September 30, 2001	46,688
Cumulative research and development expenses	**194,999**

Treatment of Restenosis

	$
Cumulative research and development expenses as at June 30, 2001	116,056
Research and development expenses for the three-month period ended September 30, 2001	35,945
Cumulative research and development expenses	**152,001**

Treatment of Scarring/Wound Healing

	$
Cumulative research and development expenses as at June 30, 2001	452,354
Research and development expenses for the three-month period ended September 30, 2001	48,288
Cumulative research and development expenses	**500,642**

Discovery and Manufacturing Program

	$
Cumulative research and development expenses as at June 30, 2001	244,448
Research and development expenses for the three-month period ended September 30, 2001	113,213
Cumulative research and development expenses	**357,661**

6. CONSOLIDATED STATEMENTS OF CASH FLOWS

The net change in non-cash working capital balances related to operations consists of the following:

	Three-month period ended September 30, 2001 $	Three-month period ended September 30, 2000 $
Share subscriptions receivable	-	21,163
Interest receivable	(45,614)	-
GST receivable	98,462	(3,920)
Accrued accounts receivable	-	(24,291)
Investment tax credit receivable	(21,138)	-
Deposits on collaborations	(27,237)	-
Prepaid expenses and other assets	(9,311)	(2,850)
Accounts payable and accrued liabilities	(166,214)	16,834
	(171,052)	**6,936**
Supplemental cash flow information		
Interest paid	1,081	129

7. COMMITMENTS

[a] As at September 30, 2001, the Company is committed to aggregate expenditures of $145,005 [June 30, 2001 - $263,745] under its collaboration agreements.

8. SEGMENTED INFORMATION

The Company considers itself to be in one business segment, that is, the research and development of therapeutic agents and operates in Canada.

9. COMPARATIVE CONSOLIDATED FINANCIAL STATEMENTS

The comparative consolidated financial statements have been reclassified from statements previously presented to conform to the presentation of the 2001 consolidated financial statements.

10. SUBSEQUENT EVENTS

On October 29, 2001, the Company announced that it has reached an agreement in principle with Waratah to combine the business and operations of the two companies by way of a plan of arrangement. Shareholders of Waratah will receive 0.8333 common shares of the Company for each share of Waratah held. The Company's shares will remain unchanged. The Company and Waratah have appointed a joint interim executive committee to provide strategic guidance in merging the operations of the two companies. It is anticipated that the effective date of this transaction will be December 31, 2001 subject to negotiation of a definitive agreement, due diligence, formal valuations, regulatory approvals, shareholder approval and fairness opinions for both companies. The provisions of Ontario Securities Commission rule 61-501 applicable to the related party aspects of the transaction will be complied with. It is anticipated that this proposed transaction will be accounted for using the purchase method with the Company identified as the acquirer.

Stock Symbol

TTH

Exchange

CDNX

Fiscal Year End

June 30

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