UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

FORM 10-Q

☒ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended September 30, 2004

or

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from to

Commission File Number: 0-30235

Exelixis, Inc.
(Exact name of registrant as specified in its charter)

Delaware	**04-3257395**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

170 Harbor Way
P.O. Box 511
South San Francisco, CA 94083
(Address of principal executive offices, including zip code)

(650) 837-7000
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No o

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes ☒ No o

On October 25, 2004, there were 74,812,073 shares of common stock, par value $.001 per share, of Exelixis, Inc. outstanding.

EXELIXIS, INC.

QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2004

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ITEM 1. FINANCIAL STATEMENTS

EXELIXIS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands)

	September 30, 2004 (unaudited)	December 31, 2003 (1)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 47,993	$ 111,828
Short-term investments	82,851	125,264
Other receivables	5,090	3,846
Other current assets	6,532	3,156
Total current assets	142,466	244,094
Restricted cash and investments	16,390	4,838
Property and equipment, net	33,795	33,500
Goodwill	67,364	67,364
Other intangibles, net	3,690	4,136
Other assets	4,164	3,862
Total assets	$ 267,869	$ 357,794
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 1,622	$ 6,151
Other accrued expenses	9,085	8,632
Accrued compensation and benefits	6,330	6,139
Current portion of capital lease obligations	2,177	4,490
Current portion of notes payable and bank obligations	7,177	5,367
Deferred revenue	15,777	21,579
Total current liabilities	42,168	52,358
Capital lease obligations	297	1,790
Notes payable and bank obligations	17,791	14,437
Convertible promissory note and loan	85,000	85,000
Other long-term liabilities	6,838	2,952
Deferred revenue	35,108	39,775
Total liabilities	187,202	196,312
Commitments		
Stockholders' equity:		
Preferred stock	—	—
Common stock	73	71
Additional paid-in-capital	547,251	541,917
Notes receivable from stockholders	—	(53)
Deferred stock compensation, net	—	(33)
Accumulated other comprehensive income	794	1,708
Accumulated deficit	(467,451)	(382,128)
Total stockholders' equity	80,667	161,482
Total liabilities and stockholders' equity	$ 267,869	$ 357,794

(1) The condensed consolidated balance sheet at December 31, 2003 has been derived from the audited financial statement at that date but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements.

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

EXELIXIS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share data)
(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2003	2004	2003
Revenues:				
Contract	$ 10,617	$ 9,310	$ 28,812	$ 28,389
License	2,045	3,129	8,301	9,385
Total revenues	12,662	12,439	37,113	37,774
Operating expenses:				
Research and development	34,054	32,298	102,694	95,054
General and administrative	5,078	4,495	15,356	14,364
Restructuring charge	—	606	2,275	606
Acquired in-process research and development	—	—	395	—
Amortization of intangibles	168	166	501	499
Total operating expenses	39,300	37,565	121,221	110,523
Loss from operations	(26,638)	(25,126)	(84,108)	(72,749)
Other income (expense):				
Interest income	728	1,096	2,426	3,364
Interest expense	(1,285)	(907)	(3,739)	(2,739)
Other income (expense), net	6	(133)	98	741
Total other income (expense)	(551)	56	(1,215)	1,366
Loss before income taxes	(27,189)	(25,070)	(85,323)	(71,383)
Provision (benefit) for income taxes	—	(75)	—	112
Net loss	$ (27,189)	$ (24,995)	$ (85,323)	$ (71,495)
Net loss per share, basic and diluted	$ (0.38)	$ (0.35)	$ (1.19)	$ (1.13)
Shares used in computing basic and diluted net loss per share	72,170	70,994	71,898	63,466

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

EXELIXIS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	Nine Months Ended September 30,	
	2004	2003
	(unaudited)	
Cash flows from operating activities:		
Net loss	$ (85,323)	$ (71,495)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	12,542	12,183
Stock compensation expense, net of reversals	40	744
Non-cash portion of restructuring charge	(150)	—
Acquired in-process research and development	395	—
Amortization of intangibles	501	499
Other	227	372
Changes in assets and liabilities:		
Other receivables	(739)	(246)
Other current assets	(3,170)	(704)
Related-party receivables	142	364
Other assets	(1,384)	29
Accounts payable and other accrued expenses	(2,310)	(559)

Other long-term liabilities	1,718	750
Deferred revenue	(12,185)	(15,416)
Net cash used in operating activities	(89,696)	(73,479)
Cash flows from investing activities:		
Cash from acquisition	860	—
Purchases of property and equipment	(9,183)	(11,142)
Changes in restricted cash	(11,552)	(13,121)
Proceeds from maturities of short-term investments	118,676	155,047
Purchases of short-term investments	(78,158)	(169,187)
Net cash provided by (used in) investing activities	20,643	(38,403)
Cash flows from financing activities:		
Proceeds from issuance of common stock, net	—	74,639
Proceeds from exercise of stock options, net of repurchases	2,531	156
Proceeds from employee stock purchase plan	1,166	991
Repayment of notes from stockholders	53	735
Payments on capital lease obligations	(3,805)	(5,101)
Proceeds from bank obligations	9,366	12,974
Principal payments on notes payable and bank obligations	(3,882)	(2,323)
Net cash provided by financing activities	5,429	82,071
Effect of foreign exchange rates on cash and cash equivalents	(211)	345
Net decrease in cash and cash equivalents	(63,835)	(29,466)
Cash and cash equivalents, at beginning of period	111,828	84,522
Cash and cash equivalents, at end of period	$ 47,993	$ 55,056

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

EXELIXIS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2004
(unaudited)

NOTE 1 Organization and Summary of Significant Accounting Policies

Organization

Exelixis, Inc. (“Exelixis,” “we,” “our,” or “us”) is a biotechnology company whose primary mission is to leverage its biological expertise and integrated drug discovery capabilities to develop high-quality, differentiated pharmaceutical products in the treatment of cancer, metabolism and other serious diseases. We use comparative genomics and model system genetics to find new drug targets and compounds that we believe would be difficult or impossible to uncover using other experimental approaches. Our research is designed to identify novel genes and proteins expressed by those genes that, when changed, either decrease or increase the activity in a specific disease pathway in a therapeutically relevant manner. These genes and proteins represent either potential product targets or drugs that may treat disease or prevent disease initiation or progression. Our most advanced pharmaceutical programs focus on drug discovery and development of small molecules in cancer and metabolism. We also believe that our proprietary technologies are valuable to other industries whose products can be enhanced by an understanding of DNA or proteins, including the agrochemical, agricultural and diagnostic industries.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and pursuant to Form 10-Q and Article 10 of Regulation S-X of the Securities and Exchange Commission (“SEC”). Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In our opinion all adjustments (consisting of normal recurring adjustments) considered necessary for a fair statement of the results of operations and cash flows for the periods presented have been included. Operating results for the three- and nine-month periods ended September 30, 2004 are not necessarily indicative of the results that may be expected for the year ending December 31, 2004, or for any future period. These financial statements and notes should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2003 included in our Annual Report on Form 10-K filed with the SEC on February 20, 2004.

Reclassifications

Certain prior year balance sheet amounts have been reclassified to conform with current year presentation.

Net Loss Per Share

Basic and diluted net loss per share are computed by dividing the net loss for the period by the weighted-average number of shares of common stock outstanding during the period, less shares that are subject to repurchase. The calculation of diluted net loss per share excludes potential common stock because their effect is antidilutive using the treasury method. Potential common stock consists of common stock subject to repurchase, incremental common shares issuable upon the exercise of stock options and warrants and shares issuable upon conversion of convertible debt.

Stock-Based Compensation

We recognize employee stock-based compensation under the intrinsic value method of accounting as prescribed by Accounting Principles Board Opinion 25, "Accounting for Stock Issued to Employees" and related interpretations. Accordingly, we have not recognized compensation expense in our financial statements for the stock options granted to employees that had an exercise price equal to the fair value of the underlying common stock on the date of grant. The following table illustrates the effect on net loss and loss per share if we had applied the fair value recognition provisions of Statement of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock-Based Compensation," as amended by SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure - an amendment of FASB Statement No. 123" (in thousands, except per share amounts):

	Three Months Ended September 30,	
	2004	2003
Net loss:		
As reported	$ (27,189)	$ (24,995)
Add: Stock-based employee compensation expense (reversal) included in reported net loss	(34)	166)
Deduct: Total stock-based employee compensation expense determined under fair value method for all awards	(3,568)	(3,707)
Pro forma net loss	$ (30,791)	$ (28,536)
Net loss per share (basic and diluted):		
As reported	$ (0.38)	$ (0.35)
Pro forma	$ (0.43)	$ (0.40)

	Nine Months Ended September 30,	
	2004	2003
Net loss:		
As reported	$ (85,323)	$ (71,495)
Add: Stock-based employee compensation expense included in reported net loss	38	741
Deduct: Total stock-based employee compensation expense determined under fair value method for all awards	(12,786)	(14,399)
Pro forma net loss	$ (98,071)	$ (85,153)
Net loss per share (basic and diluted):		
As reported	$ (1.19)	$ (1.13)
Pro forma	$ (1.36)	$ (1.34)

Since options vest over several years and additional option grants are expected to be made in future years, the pro forma impact on the results of operations for the three- or nine-month periods ended September 30, 2004 and 2003 is not necessarily representative of the pro forma effects on the results of operations for future periods.

New Accounting Pronouncements

In January 2003, the Financial Accounting Standards Board ("FASB") issued Interpretation No. 46, "Consolidation of Variable Interest Entities" ("FIN 46"). FIN 46 requires an investor with a majority of the variable interests in a variable interest entity ("VIE") to consolidate the entity and also requires majority and significant variable interest investors to provide certain disclosures. A VIE is an entity in which the equity investors do not have a controlling interest, or the equity investment at risk is insufficient to finance the entity's activities without receiving additional subordinated financial support from the other parties. We adopted the remaining provisions of FIN 46 on January 1, 2004, related to variable interests held prior to January 31, 2003, and the adoption did not have a material impact on our financial condition or results of operations.

NOTE 2 Comprehensive Income (Loss)

Comprehensive income (loss) is comprised of net income (loss) and other comprehensive income (loss). Other comprehensive income (loss) includes unrealized gains and losses on available-for-sale securities, unrealized gains and losses on cash flow hedges and cumulative translation adjustments. Comprehensive income (loss) for the three- and nine-month periods ended September 30, 2004 and 2003 are as follows (in thousands):

	Three Months Ended September 30,	
	2004	2003
Net loss	$ (27,189)	$ (24,995)
Decrease (increase) in unrealized gains on available-for-sale securities	198	(323)
Increase in unrealized gains on cash flow hedges	—	(387)
Increase (decrease) in cumulative translation adjustment	(139)	63
Comprehensive loss	$ (27,130)	$ (25,642)

	Nine Months Ended September 30,	
	2004	2003
Net loss	$ (85,323)	$ (71,495)

Decrease in unrealized gains on available-for-sale securities	(497)	(364)
Increase in unrealized gains on cash flow hedges	—	(119)
Increase (decrease) in cumulative translation adjustment	(187)	408
Reclassification of cumulative translation adjustment to income upon liquidation of an investment in a foreign entity	(228)	—
Comprehensive loss	$ (86,235)	$ (71,570)

NOTE 3 Restructurings

During the second quarter of 2004, we implemented a restructuring and consolidation of our research and discovery organizations designed to optimize our ability to generate multiple new, high-quality investigational new drug applications per year and rapidly advance these new drug candidates through clinical development. The restructuring included a reduction in force of 62 employees, the majority of which were research personnel located in South San Francisco, California. We recorded a restructuring charge of $1.7 million during the second quarter of 2004 comprised of involuntary termination benefits, and as of June 30, 2004 approximately $0.7 million of the restructuring charge remained unpaid. As of September 30, 2004, approximately $0.1 million of the restructuring charge remained unpaid and is included under the caption, “Other Accrued Expenses,” on the balance sheet and is summarized in the following table (in thousands):

	Restructuring Liability at June 30, 2004	Cash Payments	Restructuring Liability at September 30, 2004
Severance and benefits	$ 485	$ (426)	$ 59
Legal and other fees	201	(153)	48
	$ 686	$ (579)	$ 107

We do not expect to record any material expenses related to this restructuring in future periods.

During the third quarter of 2003, we implemented a worldwide restructuring of our research and development organization designed to reallocate resources and enhance the efficiency of our operations. The restructuring included a reduction in force of 61 research personnel located in South San Francisco, California and Tübingen, Germany, closure of our Tübingen location and relocation of certain research activities and employees from Tübingen to South San Francisco. The restructuring plan was substantially complete as of March 31, 2004.

In connection with the third quarter 2003 restructuring plan, we recorded a cumulative charge of approximately $1.5 million to date in accordance with Statement of Financial Accounting Standards No. 146, “Accounting for Costs Associated with Exit or Disposal Activities” (“SFAS 146”), of which approximately none and $537,000 were recorded during the three- and nine-month periods ended September 30, 2004, respectively. This charge primarily consists of severance payments, retention bonuses, relocation costs, lease buyout costs and legal and outplacement services fees. The restructuring charge also includes non-cash activity including an impairment of assets of approximately $78,000 and a gain on closure of our Tübingen facility of approximately $228,000 related to the removal from equity of the cumulative currency translation adjustment attributable to the Tübingen location. The current balance of the remaining restructuring liability is included under the caption “Other Accrued Expenses” on the balance sheet and is

summarized in the following table (in thousands):

	Restructuring Liability at December 31, 2003	Restructuring Expenses Incurred During the Period (1)	Cash Payments	Exchange Rate Impact on Liability	Restructuring Liability at September 30, 2004
Severance and benefits	$ 389	$ 81	$ (439)	$ —	$ 31
Legal and other fees	18	128	(100)	(1)	45
Lease buyout costs	—	307	(195)	—	112
Relocation	6	171	(176)	—	1
	$ 413	$ 687	$ (910)	$ (1)	$ 189

(1) Excludes a net gain of $150,000 relating to non-cash items.

We do not expect to record any additional expenses, in future periods, related to the third quarter 2003 restructuring plan.

NOTE 4 Agrinomics LLC

In July 1999, Exelixis Plant Sciences (formerly Agritope, Inc.) and Bayer CropScience (formerly Aventis CropScience USA LP) formed Agrinomics LLC to conduct a research, development and commercialization program in the field of agricultural functional genomics. As a result of our acquisition of Exelixis Plant Sciences, we owned a 50% interest in Agrinomics, while Bayer CropScience owned the remaining 50% interest. In May 2004, we purchased from Bayer its 50% interest in Agrinomics, in exchange for our release of all future obligations of Bayer to Agrinomics under the joint venture agreement. As there is no readily determinable fair market value for Bayer’s 50% interest in Agrinomics or Bayer’s future obligations under the Agrinomics joint venture agreement, we recorded this acquisition as a non-monetary transaction. Accordingly, for accounting purposes, the purchase price was deemed to be zero.

We recorded the assets acquired and the liabilities assumed based on their estimated fair values at the date of acquisition, as determined by us based on valuation techniques in accordance with generally accepted accounting principles. As a result of this transaction, we recorded net tangible liabilities of $450,000, intangible assets of $55,000 and expense associated with the purchase of in-process research and development of $395,000, representing the fair value of two primary research projects that had not yet reached technological feasibility and that have no alternative future use. This transaction is not expected to have a material impact on our financial condition or results of operations.

NOTE 5 Commitments

In July 2004, we entered into an agreement to lease approximately 68,000 square feet of office and laboratory facilities in South San Francisco, California. Pursuant to the terms of the lease, in lieu of a security deposit, we were required to issue a letter of credit with a bank in the amount of $1.6 million. As collateral for the letter of credit, we are required to maintain a securities account at the bank equal to 100% of the letter of credit, which has been recorded in the balance sheet as restricted cash and investments. The lease term is from July 2004 through July 2018 and the future minimum payments under this operating lease are as follows (in thousands):

Year Ending December 31,	
2004	$ —
2005	407
2006	1,223
2007	1,587
2008	1,627
Thereafter	17,989
	$ 22,833

NOTE 6 Subsequent Event - X-Ceptor Acquisition

On September 27, 2004, we entered into a definitive Agreement and Plan of Merger with X-Ceptor Therapeutics, Inc ("X-Ceptor") pursuant to which we acquired X-Ceptor. X-Ceptor, which prior to the merger was a privately held company located in San Diego.

Californi, is focused on the discovery and development of small molecules that modulate nuclear hormone receptors ("NHRs"). NHRs represent a class of clinically and commercially validated gene targets that are implicated in a wide range of metabolic and cardiovascular disorders. The combination of Exelixis' small molecule discovery engine and oncology pipeline with X-Ceptor's proprietary "reverse endocrinology" platform and pipeline of NHR-targeted compounds advances our strategy to diversify into new therapeutic areas and we expect to accelerate our goal to develop and commercialize a diverse, highly differentiated pipeline of products to treat diseases including cancer, metabolic syndrome, lipid disorders, hypertension and congestive heart failure.

On October 18, 2004, we closed the acquisition of X-Ceptor. The transaction is expected to be accounted for under the purchase method of accounting in the fourth quarter of fiscal 2004. The preliminary purchase price of approximately $25.0 million consists of approximately 2.5 million shares of Exelixis common stock, $2.9 million in cash and approximately $2.4 million in transaction costs. We expect to record a substantial portion of the purchase price as purchased in-process research and development, which will be charged to operating expense in the fourth quarter of 2004.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis contains forward-looking statements. These statements are based on our current expectations, assumptions, estimates and projections about our business and our industry, and involve known and unknown risks, uncertainties and other factors that may cause our or our industry's results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied in, or contemplated by, the forward-looking statements. Words such as "believe," "anticipate," "expect," "intend," "plan," "will," "may," "should," "estimate," "predict," "potential," "continue" or the negative of such terms or other similar expressions, identify forward-looking statements. Our actual results and the timing of events may differ significantly from the results discussed in the forward-looking statements. Factors that might cause such a difference include those discussed under the caption "Risk Factors" below, as well as those discussed elsewhere in this quarterly report on Form 10-Q.

This discussion and analysis should be read in conjunction with our financial statements and accompanying notes included in this report and the 2003 audited financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2003, filed with the Securities and Exchange Commission on February 20, 2004. Operating results are not necessarily indicative of results that may occur in future periods. We undertake no obligation to update any forward-looking statement to reflect events after the date of this report.

Overview

Exelixis is a leading genomics-based drug discovery company dedicated to the discovery and development of novel therapeutics across various therapy areas. The company is leveraging its fully integrated gene-to-drug platform to fuel the growth of its proprietary drug pipeline. Exelixis' development pipeline currently covers cancer and metabolism and is comprised of the following compounds: XL119 (becatecarin), for which a Phase 3 clinical trial has been initiated in patients with bile duct tumors; XL784, initially an anticancer compound, which has completed a Phase 1 clinical trial and is currently being developed as a treatment for renal disease; XL647 and XL999, which are currently in Phase 1 clinical trials; XL880, XL820, XL844 and XL184, anticancer compounds that are potential IND candidates; and multiple compounds in pre-clinical development for diseases including cancer, lipid disorders, hyperlipidemia and congestive heart failure.

We have incurred net losses since inception and expect to incur substantial losses for at least the next several years as we continue our research and development activities, including manufacturing and development expenses for compounds in pre-clinical and clinical studies. As of September 30, 2004, we had approximately $147.2 million in cash, cash equivalents, short-term investments and restricted cash and investments. We anticipate that our current cash, cash equivalents, short-term investments and funding we anticipate to receive from current collaborators will enable us to maintain our currently planned operations for at least the next 15 months. Changes to our current operating plan may require us to consume available capital resources significantly sooner than we expect.

We have collaborations with several leading pharmaceutical, biotechnology and agrochemical companies based on the strength of our technologies and biological expertise in order to support the development of our proprietary product candidates. Through these collaborations, we obtain license fees and research funding, together with the opportunity to receive milestone payments and royalties from research results and subsequent product development. In addition, many of our collaborations have been structured strategically to provide us access to technology to more rapidly advance our internal programs. Our collaborations include: Bayer CropScience LP (formerly Aventis USA LP), Bayer Corporation, Bristol-Myers Squibb Company, Cytokinetics, Inc., Dow AgroSciences LLC, Merck

& Co., Inc. (two collaborations), Renessen LLC, Scios Inc., Schering-Plough Research Institute, Inc. and SmithKlineBeecham Corporation (which does business as GlaxoSmithKline).

As our company has matured and our development efforts have intensified, we have restructured the organization as needed to reallocate resources and enhance the efficiency of our operations. We believe that these efforts have strengthened us by enabling us to achieve an appropriate functional balance within the organization. We expect to continue to use corporate partnering as a strategic tool to cultivate our assets, fund our operations and expand the therapeutic and commercial potential of our pipeline.

Recent Developments

Clinical update

Our clinical pipeline continues to advance. The following summarizes the status of our clinical and pre-clinical development pipeline and serves as an update to the disclosures we made in the business section of our Annual Report on Form 10-K for the year ended December 31, 2003. Several compounds in our pipeline, such as XL647, XL999 and others, are Spectrum Selective Kinase Inhibitors™ that target proteins involved in both tumor proliferation and angiogenesis. Each compound has a different inhibition spectrum of receptor tyrosine kinases ("RTKs"), and each has the potential to maximize efficacy through simultaneous inhibition of multiple RTKs.

- XL119 – The Phase 3 trial began dosing patients in North America and is proceeding with additional patient and investigator enrollment in North America and Europe.
- XL784 – We continue to explore the potential of this compound in renal disease, with a goal of pursuing that indication in the clinic in 2005.
- XL647 – We filed an IND for XL647 in February 2004, and we initiated the Phase 1 trial for this novel, orally available compound in June 2004. The trial is on track and continues to enroll additional subjects.
- XL999 – We filed an IND for XL999 in June 2004 and initiated the Phase 1 trial for this proprietary, novel anticancer compound in October 2004.
- XL880 – We anticipate filing an IND application for XL880 in the first half of 2005.
- XL820 – We anticipate filing an IND application for XL820 in the first half of 2005.
- XL844 – We anticipate filing an IND application for XL844 in the first half of 2005.
- XL184 – We anticipate filing an IND application for XL184 in the first half of 2005.

X-Ceptor Acquisition

On September 27, 2004, we entered into a definitive Agreement and Plan of Merger with X-Ceptor Therapeutics, Inc ("X-Ceptor"), which closed on October 18, 2004. X-Ceptor, which prior to the merger was a privately held company located in San Diego, California, is focused on the discovery and development of small molecules that modulate nuclear hormone receptors ("NHRs"). NHRs represent a class of clinically and commercially validated gene targets that are implicated in a wide range of metabolic and cardiovascular disorders. The combination of Exelixis' small molecule discovery engine and oncology pipeline with X-Ceptor's proprietary "reverse endocrinology" platform and pipeline of NHR-targeted compounds advances Exelixis' strategy to diversify into new therapeutic areas and is expected to accelerate the development and commercialization of a diverse, highly differentiated pipeline of products to treat diseases including cancer, metabolic syndrome, lipid disorders, hypertension and congestive heart failure.

The transaction is expected to be accounted for under the purchase method of accounting in the fourth quarter of fiscal 2004. The preliminary purchase price of approximately $25.0 million consists of approximately 2.5 million shares of Exelixis common stock, $2.9 million in cash and approximately $2.4 million in transaction costs.

Results of Operations

Revenues

Total revenues and dollar and percentage changes as compared to the prior year period are as follows (dollar amounts are presented in

millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2003	2004	2003
Total revenues	$ 12.7	$ 12.4	$ 37.1	$ 37.8
Dollar increase (decrease)	$ 0.2		$ (0.7)	
Percentage increase (decrease)	2%		(2) %	

The increase in revenues for the quarter ended September 30, 2004, as compared to the comparable prior year period, was primarily a result of an increase in revenues from compound deliveries under our combinatorial chemistry collaborations and a milestone payment earned under our Bristol-Myers Squibb

collaboration. This increase was partially offset by upfront payments from Bristol-Myers Squibb related to our collaboration being fully amortized in July 2004. The decrease in revenues for the nine months ended September 30, 2004, as compared to the comparable prior year period, was primarily a result of the successful conclusion of our collaboration with Protein Design Labs in May 2003 and upfront payments from Bristol-Myers Squibb being fully amortized in July 2004, partially offset by an increase in revenues from compound deliveries under our combinatorial chemistry collaborations and milestone payments earned under our Bristol-Myers Squibb collaboration.

Research and Development Expenses

Total research and development expenses and dollar and percentage changes, as compared to the prior year period, are as follows (dollar amounts are presented in millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2003	2004	2003
Total R&D expense	$ 34.1	$ 32.3	$ 102.7	$ 95.1
Dollar increase	$ 1.8		$ 7.6	
Percentage increase	5%		8%	

Research and development expenses consist primarily of salaries and other personnel-related expenses, laboratory supplies, consulting and facilities costs. The increase for the three months ended September 30, 2004, as compared to the equivalent period in 2003, resulted primarily from an increase in consulting and professional expenses associated with advancing our clinical and pre-clinical development programs and was partially offset by a decrease in salaries and other personnel related expenses as a result of our restructuring activities during the second quarter of 2004. Consulting and professional expenses increased 52% to $6.2 million and included costs associated with our Phase 3 trial for XL119, Phase 1 trial for XL647, commencing our Phase 1 trial for XL999 and moving XL844, XL820 and XL880 through pre-clinical testing in anticipation of filing IND applications in 2005.

The increase for the nine months ended September 30, 2004, as compared to the equivalent period in 2003, resulted primarily from the following costs:

- Consulting and professional – Consulting and professional costs increased 36% to $14.4 million, due primarily to an increase in activities associated with advancing the company's clinical and pre-clinical development programs. These activities included Phase 3 trial activity for XL119, Phase 1 trial activity for XL647, commencing a Phase 1 trial and filing an IND application for XL999 and moving XL844, XL820, XL880 and XL184 through pre-clinical testing in anticipation of filing IND applications in 2005.

- Facilities – As a result of our expanding drug discovery and development operations, facility and equipment rental expense increased 18% to $14.4 million, due primarily to our expansion into additional buildings in South San Francisco, California.

The table below summarizes the status of our current drug candidates:

Program	Clinical Status
XL119	Phase 3 clinical trial ongoing
XL784	Completed a Phase 1 clinical trial as an anticancer compound and is currently being developed for renal disease
XL647	Phase 1 clinical trial ongoing
XL999	Phase 1 clinical trial initiated in October 2004
XL880	Expect to file an IND application in the first half of 2005

XL820	Expect to file an IND application in the first half of 2005
XL844	Expect to file an IND application in the first half of 2005
XL184	Expect to file an IND application in the first half of 2005

We currently estimate that typical Phase 1 clinical trials last approximately one year, Phase 2 clinical trials last approximately one to two years and Phase 3 clinical trials last approximately two to four years. However, the length of time generally varies substantially according to factors relating to the trial, such as the type and intended use of the product candidate, the trial design and ability to enroll suitable patients.

We expect that research and development expenses will continue to increase in the future as we advance our compounds through development. We currently do not have estimates of total costs to reach the market by a particular drug candidate or in total. Our potential therapeutic products are subject to a lengthy and uncertain regulatory process that may not result in the necessary regulatory approvals, which could adversely affect our ability to commercialize products. In addition, clinical trials of our potential products may fail to demonstrate safety and efficacy, which could prevent or significantly delay regulatory approval.

General and Administrative Expenses

Total general and administrative expenses and dollar and percentage changes as compared to the prior year period are as follows (dollar amounts are presented in millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2003	2004	2003
Total G&A expense	$ 5.1	$ 4.5	$ 15.4	$ 14.4
Dollar increase	$ 0.6		$ 1.0	
Percentage increase	13%		7 %	

General and administrative expenses consist primarily of facility costs, staffing costs to support our research activities and depreciation expense. The increase for the three months ended September 30, 2004, as compared to the equivalent period in 2003, and for the nine months ended September 30, 2004, as compared to the equivalent period in 2003, resulted primarily from increases in salaries and other personnel-related expenses and facility expenses.

Amortization of Intangibles

Intangibles result from our acquisitions of Genomica, Artemis and Agritope (renamed Exelixis Plant Sciences). Total amortization expense related to these intangibles is expected to be $666,000 for the year ending December 31, 2004.

Restructuring Charges

During the second quarter of 2004, we implemented a restructuring and consolidation of our research and discovery organizations designed to optimize our ability to generate multiple new, high-quality investigational new drug applications per year and rapidly advance these new drug candidates through clinical development. The restructuring included a reduction in force of 62 employees, the majority of which were research personnel located in South San Francisco, California. We recorded a restructuring charge of $1.7 million during the second quarter of 2004 comprised of involuntary termination benefits. We do not expect to record any material expenses related to this restructuring in future periods.

In the third quarter of 2003, we implemented a restructuring of our research and development organization designed to reallocate resources and enhance the efficiency of our operations. The restructuring included a reduction in force of 61 research personnel located in South San Francisco, California and Tübingen, Germany, closure of our Tübingen facility and relocation of certain research activities and employees from Tübingen to South San Francisco. The restructuring plan was substantially completed as of March 31, 2004. In connection with this restructuring plan, we recorded a cumulative charge of approximately $1.5 million to date in accordance with Statement of Financial Accounting Standards No. 146, “Accounting for Costs Associated with Exit or Disposal Activities” (“SFAS 146”), of which approximately none and $537,000 were recorded during the three- and nine-month periods ended September 30, 2004, respectively. This charge consists primarily of severance, retention bonuses, relocation, lease buyout costs and legal and outplacement services fees. The restructuring charge also includes non-cash activity, including an impairment of assets of approximately $78,000 and a gain on closure of our Tübingen facility of approximately $228,000 related to the removal from equity of the cumulative currency translation adjustment attributable to the Tübingen location. We do not expect to record any additional expenses associated with this restructuring, as the restructuring plan is substantially complete.

Acquired In-Process Research and Development

In May 2004, we purchased from Bayer CropScience its 50% interest in Agrinomics LLC, our joint venture with Bayer CropScience, in exchange for our release of all future obligations of Bayer to Agrinomics under the joint venture agreement. We recorded the assets acquired and the liabilities assumed based on their estimated fair values at the date of acquisition, as determined by management based on valuation techniques in accordance with generally accepted accounting principles. As a result, we recorded net tangible liabilities of $450,000, intangible assets of $55,000 and expense associated with the purchase of in-process research and development of $395,000, representing the fair value of two primary research projects that had not yet reached technological feasibility and that have no alternative future use. This transaction is not expected to have a material impact on our financial condition or results of operations.

Total Other Income (Expense)

Total other income (expense), dollar and percentage changes as compared to the prior year period are as follows (dollar amounts are presented in millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2003	2004	2003
Total other income (expense)	$ (0.6)	$ 0.1	$ (1.2)	$ 1.4
Dollar decrease	$ (0.6)		$ (2.6)	
Percentage decrease	(1,084) %		(189) %	

Total other income (expense) consists primarily of interest income earned on cash, cash equivalents and short-term investments, offset by interest expense incurred on notes payable, bank obligations and capital lease obligations. The decrease in 2004 from 2003 was the result of a decrease in interest income due to an overall decline in interest rates coupled with an increase in interest expense related to an increase in our long-term debt.

Income Taxes

We have incurred net losses since inception and, consequently, have not recorded any U.S. federal or state income taxes. We recorded a tax benefit of approximately $75,000 and a tax provision of approximately $112,000 during the three- and nine-month periods ended September 30, 2003, respectively. These tax benefits and provision are related to income earned in our foreign operations. Due to the activities under our 2003 restructuring plan, we did not have taxable income from foreign operations for the full year ended December 31, 2003. As a result, we recorded a tax benefit in the fourth quarter of 2003.

Liquidity and Capital Resources

Cash Requirements

To date, we have financed our operations primarily through the sale of equity, payments and loans from collaborators, equipment financing facilities and interest income. In addition, we acquired Genomica in December 2001, including $109.6 million in cash and investments. As of September 30, 2004, we had approximately $147.2 million in cash, cash equivalents, short-term investments and restricted cash and investments.

We have incurred net losses since inception, including a net loss of approximately $85.3 million for the nine months ended September 30, 2004, and expect to incur substantial losses for at least the next several years as we continue our research and development activities, including manufacturing and development expenses for compounds in pre-clinical and clinical studies. We anticipate that our current cash, cash equivalents, short-term investments and funding to be received from current collaborators will enable us to maintain our currently planned operations for at least the next 15 months. It is possible that we will seek additional financing within this timeframe through public or private financing, collaborative relationships or other arrangements. Changes to our current operating plan may require us to consume available capital resources significantly sooner than we expect.

Our future capital requirements will be substantial and will depend on many factors, including:

- payments received under collaborative agreements, licensing agreements and other arrangements;
- the progress and scope of our collaborative and independent clinical trials and other research and development projects;
- future clinical trial results;

- our need to expand our product and clinical development efforts;
- the cost and timing of regulatory approvals;
- the cost of establishing clinical and research supplies of our product candidates;
- our ability to remain in compliance with, or amend or cause to be waived, financial covenants contained in loan and lease agreements with third parties;
- the effect of competing technological and market developments;
- the filing, maintenance, prosecution, defense and enforcement of patent claims and other intellectual property rights;
- the cost of any acquisitions of or investments in businesses, products and technologies, although we currently have no commitments relating to any such transactions; and
- the cost and timing of establishing or contracting for sales, marketing and distribution capabilities.

If our capital resources are insufficient to meet future capital requirements, we will have to raise additional funds. We currently have a shelf registration statement on file with the SEC that allows us to sell common stock from time to time. In addition, we recently filed a universal shelf registration statement with the SEC that allows us, after such registration statement is declared effective by the SEC, to sell from time to time common stock, preferred stock, debt securities and warrants, either individually or in units. However, we may be unable to raise sufficient additional capital when we need it, on favorable terms or at all. The sale of equity or convertible debt securities in the future may be dilutive to our stockholders, and debt-financing arrangements may require us to pledge certain assets and enter into covenants that would restrict certain business activities or our ability to incur further indebtedness and may contain other terms that are not favorable to our stockholders or us. If we are unable to obtain adequate funds on reasonable terms, we may be required to curtail operations significantly or obtain funds by entering into financing, supply or collaboration agreements on unattractive terms.

Sources and Uses of Cash

Our operating activities used cash of approximately $89.7 million and $73.5 million for the nine months ended September 30, 2004 and 2003, respectively. Cash used in operating activities relates primarily to funding net losses, changes in deferred revenue from collaborators, changes in other current assets and changes in accounts payable and other accrued expenses, partially offset by non-cash charges related to depreciation and amortization. We expect to use cash for operating activities for at least the next several years as we continue to incur net losses associated with our research and development activities, including manufacturing and development expenses for compounds in pre-clinical and clinical studies.

Our investing activities provided cash of approximately $20.6 million and used cash of approximately $38.4 million for the nine months ended September 30, 2004 and 2003, respectively. Changes in cash from investing activities are primarily due to purchases and maturities of short-term investments, purchases of property and equipment, and an increase in restricted cash. In the nine months ended September 30, 2004 and 2003, we made purchases of $9.2 million and $11.1 million, respectively, of property and equipment. We expect to continue to make significant investments in research and development and our administrative infrastructure, including the purchase of property and equipment to support our expanding drug discovery and development operations.

Our financing activities provided cash of approximately $5.4 million and $82.1 million for the nine months ended September 30, 2004 and 2003, respectively. Changes in cash from financing activities are primarily due to payments and proceeds associated with equipment financing facilities, bank obligations and cash received for the issuance of common shares pursuant to our employee stock purchase program and the exercise of stock options. In addition, during the nine months ended September 30, 2003, we received net proceeds of $74.7 million from the issuance of 11.3 million shares of common stock in a follow-on public offering. We finance property and equipment purchases through equipment financing facilities, such as capital leases, notes and bank obligations. Over the next several years, we are required to make certain payments on capital leases, notes, bank obligations and loans from collaborators. Under our collaboration agreement with GlaxoSmithKline, we have the option to sell additional shares of common stock to GlaxoSmithKline and draw up to another $30.0 million under a loan facility, which we plan on drawing during the fourth quarter of 2004, for use in our efforts under the collaboration. GlaxoSmithKline may elect to expand the collaboration, upon which the loan facility, as well as development funding and milestone payments, would be significantly expanded.

We believe there have been no significant changes during the nine-month period ended September 30, 2004 to the items that we disclosed as our contractual obligations under Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” in our Annual Report on Form 10-K for the year ended December 31, 2003, except for the operating lease we entered into during July 2004. The following chart details our contractual obligations as of December 31, 2003, with the addition of the operating lease we entered into during July 2004 (in thousands):

		Payments Due by Period			
Contractual Obligations	**Total**	**Less than 1 year (1)**	**1-3 years**	**4-5 years**	**After 5 years**
Minimum purchase obligations	$ 1,500	$ 1,000	$ 500	$ —	$ —
Notes payable and bank obligations	19,804	5,367	10,810	3,627	—
Licensing agreements	5,449	1,010	1,966	1,732	741
Capital lease obligations	6,782	4,899	1,883	—	—
Convertible promissory note and loan	85,000	—	30,000	18,150	36,850
Operating leases (2)	161,187	12,409	25,432	23,925	99,421
Total contractual cash obligations	$ 279,722	$ 24,685	$ 70,591	$ 47,434	$ 137,012

(1) These amounts represent our contractual obligations for the twelve-month period ending December 31, 2004.

(2) These amounts include the operating lease we entered into during July 2004 to lease approximately 68,000 square feet of office and laboratory facilities in South San Francisco, California. The lease term is from July 2004 through July 2018 and the future minimum payments under this operating lease are $22.8 million.

RISK FACTORS

In addition to the factors discussed elsewhere in this report and our other reports filed with the SEC, the following are important factors that could cause actual results or events to differ materially from those contained in any forward-looking statements made by or on behalf of us. The risks and uncertainties described below are not the only ones facing Exelixis. Additional risks and uncertainties not presently known to us or that we currently deem immaterial also may impair our business operations. If any of the following risks or such other risks actually occur, our business could be harmed.

Risks Related to Our Need for Additional Financing and Our Financial Results

If additional capital is not available to us, we would be forced to delay, reduce or eliminate our product development programs or commercialization efforts and we may breach our financial covenants.

We will need to raise additional capital to:

- fund our operations and clinical trials;
- continue our research and development efforts; and
- commercialize our identified product candidates, if any such compounds receive regulatory approval for commercial sale.

We anticipate that our current cash and cash equivalents, short-term investments and funding to be received from current collaborators will enable us to maintain our currently planned operations for at least the next 15 months. Our future capital requirements will be substantial and will depend on many factors, including:

- payments received under collaborative agreements, licensing agreements and other arrangements;
- the progress and scope of our collaborative and independent clinical trials and other research and development projects;
- future clinical trial results;
- our need to expand our product and clinical development efforts;
- the cost and timing of regulatory approvals;
- the cost of establishing clinical and research supplies of our product candidates;
- our ability to remain in compliance with, or amend or cause to be waived, financial covenants contained in loan and lease agreements with third parties;
- the effect of competing technological and market developments;
- the filing, maintenance, prosecution, defense and enforcement of patent claims and other intellectual property rights;
- the cost of any acquisitions of or investments in businesses, products and technologies, although we currently have no commitments relating to any such transactions; and
- the cost and timing of establishing or contracting for sales, marketing and distribution capabilities.

One or more of these factors or changes to our current operating plan may require us to consume available capital resources significantly sooner than we expect. If our capital resources are insufficient to meet future capital requirements, we will have to raise

additional funds. We may be unable to raise sufficient additional capital when we need it, on favorable terms or at all. The sale of equity or convertible debt securities in the future may be dilutive to our existing stockholders, and debt-financing arrangements may require us to pledge certain assets and enter into covenants that would restrict certain business activities or our ability to incur further indebtedness and may contain other terms that are not favorable to our stockholders or us. If we are unable to obtain adequate funds on reasonable terms, we may be required to curtail operations significantly or to obtain funds by entering into financing, supply or collaboration agreements on unattractive terms. If we raise additional funds through collaboration arrangements with third parties, it will be necessary to relinquish some rights to our technologies or our product candidates, or we may be required to grant licenses on terms that are not favorable to us.

In addition, we must raise additional capital in order to stay in compliance with financial covenants contained in agreements with third parties. For example, as part of our collaboration with SmithKlineBeecham Corporation, we entered into a loan and security agreement, dated October 28, 2002, which contains financial covenants pursuant to which our working capital (the amount by which our current assets exceed our current liabilities) must not be less than $25 million and our tangible net worth (our total stockholder equity less goodwill and other intangible assets) must not be less than $10 million. We recently entered into an amendment to the loan and security agreement that allows us to comply with an alterative covenant instead of the covenants relating to working capital and tangible net worth for a period from September 15, 2004 through March 31, 2005. Pursuant to the alternative covenant, our cash and investments (total cash, cash equivalents and investments) must not be less than $50 million. As of September 30, 2004, our working capital was $100.3 million, our tangible net worth was $9.6 million, and our cash and investments were $147.2 million. If we were to default on the financial covenants under the loan and security agreement, SmithKlineBeecham Corporation may, among other remedies, declare immediately due and payable all obligations under the loan and security agreement. As of September 30, 2004, we had borrowed $55.0 million under the loan and security agreement. In addition, in connection with an equipment lease financing transaction with General Electric Capital Corporation, we entered into a lease agreement pursuant to which we are required to maintain minimum unrestricted cash, which is defined as cash on hand, including investments in marketable securities with maturities of less than 24 months, less cash pledged to other parties, of $35 million. As of September 30, 2004, we had unrestricted cash of $59.9 million. If we were to default on this financial covenant, we may be required to pay as liquidated damages the stipulated loss value of the equipment and all rents and other sums then due under the agreement. If we cannot raise additional capital in order to remain in compliance with our financial covenants or if we are unable to renegotiate such covenants and the lendor and lessor exercise their remedies under the agreements, we would not be able to operate under our current operating plan.

We have a history of net losses. We expect to continue to incur net losses, and we may not achieve or maintain profitability.

We have incurred net losses each year since our inception, including a net loss of approximately $85.3 million for the nine months ended September 30, 2004. As of that date, we had an accumulated deficit of approximately $467.5 million. We expect these losses to continue and anticipate negative operating cash flow for the foreseeable future. We have not yet completed the development, including obtaining regulatory approval, of any of our product candidates and, consequently, have not generated revenues from the sale of products. Our only revenues to date are license revenues and revenues under contracts with our partners. The size of our net losses will depend, in part, on the rate of growth, if any, in our license and contract revenues and on the level of our expenses. These losses have had and will continue to have an adverse effect on our stockholders' equity and working capital. Our research and development expenditures and general and administrative expenses have exceeded our revenues to date, and we expect to spend significant additional amounts to fund research and development in order to enhance our core technologies and undertake product development. In 2001, we acquired XL119, a rebeccamycin analogue that was in Phase 2 clinical development. We have initiated a Phase 3 clinical trial for XL119 as a potential treatment for bile duct tumors. We have also conducted a Phase 1 clinical trial for XL784, a potent inhibitor of the ADAM-10 metalloprotease enzyme, and plan to pursue a development path in renal disease. During the first quarter of 2004, we filed an IND application for XL647, a potent inhibitor of RTKs that are implicated in driving tumor proliferation and vascularization, and initiated a Phase 1 clinical trial for XL647 in cancer patients in the second quarter of 2004. In addition, during the second quarter of 2004, we filed an IND application for XL999, a potent inhibitor of RTKs that are implicated in driving tumor proliferation and vascularization, and initiated a Phase 1 clinical trial for XL999 in cancer patients in October 2004. In the last year, we have added multiple potential anticancer compounds to our development pipeline, and we anticipate filing IND applications for product candidates during the next 12 months. As a result, we expect that our operating expenses will increase significantly in the near term, and, consequently, we will need to generate significant additional revenues to achieve profitability. Because of the numerous risks and uncertainties associated with developing small molecule drugs, we are unable to predict the extent of any future losses or when we will become profitable, if at all. Even if we do increase our revenues and achieve profitability, we may not be able to maintain or increase profitability.

Risks Related to Development of Product Candidates

Clinical testing of our product candidates is a lengthy, costly and uncertain process and may fail to demonstrate safety and efficacy, which could prevent or significantly delay regulatory approval.

Clinical trials are inherently risky and may reveal that our product candidates are ineffective or have unacceptable toxicity or other side effects that may significantly decrease the likelihood of regulatory approval of the product candidate. The results of preliminary studies do not necessarily predict clinical or commercial success, and larger later-stage clinical trials may fail to confirm the results observed in the preliminary studies. With respect to our own proprietary compounds in development, we have established timelines for manufacturing and clinical development based on existing knowledge of the compound and industry metrics. However, we cannot provide assurance that any specified timelines with respect to the initiation or completion of clinical studies will be achieved.

We may experience numerous unforeseen events during, or as a result of, clinical testing that could delay or prevent commercialization of our product candidates, including:

- our product candidates may not prove to be efficacious or may cause harmful side effects;
- negative or inconclusive clinical trial results may require us to conduct further testing or to abandon projects that we expect to be promising;
- patient registration or enrollment in our clinical testing may be lower than we anticipate, resulting in the delay or cancellation of clinical testing; and
- regulators or institutional review boards may not authorize, delay, suspend or terminate clinical research for various reasons, including noncompliance with regulatory requirements or their determination that participating patients are being exposed to unacceptable health risks.

If any of these events were to occur and, as a result, we were to have significant delays in or termination of our clinical testing, our expenses could increase and our ability to generate revenue could be impaired, which would adversely impact our financial results.

We have limited experience in conducting clinical trials and may not be able to rapidly or effectively continue the further development of our compounds or meet current or future requirements identified based on our discussions with the FDA. We do not know whether our planned clinical trials will begin on time, will be completed on schedule, or at all, will be sufficient for registration of these compounds or will result in approvable products.

In the second quarter of 2004, we initiated a Phase 3 clinical trial for XL119. We have also completed Phase 1 clinical trials for XL784. In addition, in the second quarter of 2004, we initiated a Phase 1 clinical trial for XL647 and we initiated a Phase 1 trial for XL999 during October 2004. We will have to conduct additional clinical testing in order to meet FDA requirements for regulatory approval of these and other product candidates. The results from the Phase 2 clinical trials for XL119 may not be predictive of results obtained from the Phase 3 clinical trials, and the results from the Phase 1 clinical trials for XL784 may not be predictive of results obtained from any Phase 2 clinical trials.

Completion of clinical trials may take several years or more, but the length of time generally varies substantially according to the type, complexity, novelty and intended use of a product candidate. The duration and the cost of clinical trials may vary significantly over the life of a project as a result of factors relating to the trial, including, among others, the following:

- the number of patients that ultimately participate in the trial;
- the duration of patient follow-up that seems appropriate in view of the results;
- the number of clinical sites included in the trials; and
- the length of time required to enroll suitable patient subjects.

In addition, our research and clinical testing regarding our product candidates may be delayed or abandoned as a result of other compounds subsequently discovered by us, or our competitors, that we believe show significantly improved safety or efficacy in comparison to our product candidates, which could limit our ability to generate revenues, cause us to incur additional expense and materially and adversely affect the market price of our common stock.

Risks Related to Our Dependence on Third Parties

We are dependent on our collaborations with major companies. If we are unable to achieve milestones, develop products or renew or enter into new collaborations, our revenues may decrease and our activities may fail to lead to commercialized products.

Substantially all of our revenues to date have been derived from collaborative research and development agreements. Revenues from research and development collaborations depend upon continuation of the collaborations, the achievement of milestones and royalties derived from any future products developed from our research. If we are unable to successfully achieve milestones or our collaborators fail to develop successful products, we will not earn the revenues contemplated under such collaborative agreements. In addition, some of our collaborations are exclusive and preclude us from entering into additional collaborative arrangements with other

parties in the area or field of exclusivity. Future collaborations may require us to relinquish some important rights, such as marketing and distribution rights.

We currently have collaborative research agreements with, among others, Bayer Corporation, Bristol-Myers Squibb, SmithKlineBeecham Corporation (which does business as GlaxoSmithKline), Dow AgroSciences and Renessen.

Our current collaboration with Bayer Corporation, which is conducted through Genoptera LLC, a jointly-owned limited liability company, is scheduled to expire in 2008, after which it will automatically be extended for one-year terms unless terminated by either party upon 12 months written notice. Our collaboration agreement with Bayer permits Bayer to terminate our collaborative activities prior to 2008 upon the occurrence of specified conditions, such as the failure to agree on key strategic issues after a period of years or the acquisition of us by certain specified third parties. Our agreement with Bayer is subject to termination at an earlier date if two or more of our Chief Executive Officer, Chief Scientific Officer, Agricultural Biotechnology Program Leader and Chief Informatics Officer cease to have a relationship with us within nine months of each other. Our former Chief Scientific Officer, Geoffrey Duyk, M.D., Ph.D., left the company at the end of 2003.

In May 2004, we terminated our collaboration with Bayer CropScience, which was conducted through Agrinomics LLC, a jointly owned limited liability company. The termination of the collaboration was in connection with our purchase of Bayer CropScience's 50% ownership interest in Agrinomics. As a result, we now wholly own Agrinomics. In addition, we entered into a combinatorial chemistry agreement with Bayer CropScience, and Bayer CropScience and its affiliates entered into a number of license and technology agreements with Agrinomics. The agreements are directed to the use of the assets developed or used under the collaborative research agreement. Agrinomics retained the collaborative agreement with Renessen, which expires in December 2005, but has an early termination option, effective December 2004.

Our mechanism of action collaborative agreement with Bristol-Myers Squibb expired in September 2004. Collaborative research under our cancer collaborative agreement with Bristol-Myers Squibb expires in July 2009, though Bristol-Myers Squibb has the option to extend this collaborative research until July 2010. The development program of our alliance with SmithKlineBeecham is scheduled to expire in October 2008, but the alliance is subject to earlier termination at the discretion of SmithKlineBeecham starting in 2005. Research funding under our agreement with Protein Design Labs expired in May 2003. Funding under our arrangement with Dow AgroSciences expired in July 2004. We also have additional agreements providing lower amounts of committed funding with the following chemistry collaborators: Cytokinetics, Inc., Scios Inc., Schering-Plough Research Corporation, and Merck & Co., Inc.

If these existing agreements are not renewed, or terminated early or if we are unable to enter into new collaborative agreements on commercially acceptable terms, our revenues and product development efforts may be adversely affected. For example, our agreement with Pharmacia Corporation terminated by mutual agreement in February 2002, which eliminated the opportunity for us to earn approximately $9.0 million in research revenue in 2002 and 2003. Although we have entered into other collaborations that offset this loss of revenue, we may not be able to enter into new collaborative agreements on similar or superior financial terms than those under our existing arrangements, and the timing of new collaborative agreements may have a material adverse effect on our ability to continue to successfully meet our corporate goals and milestones.

Conflicts with our collaborators could jeopardize the outcome of our collaborative agreements and our ability to commercialize products.

We are conducting proprietary research programs in specific disease, therapeutic modality and agricultural product areas that are not covered by our collaborative agreements. Our pursuit of opportunities in pharmaceutical and agricultural markets could, however, result in conflicts with our collaborators in the event that any of our collaborators take the position that our internal activities overlap with those areas that are exclusive to our collaborative agreements, and we should be precluded from such internal activities. Moreover, disagreements with our collaborators could develop over rights to our intellectual property. In addition, our collaborative agreements may have provisions that give rise to disputes regarding the rights and obligations of the parties, including the rights of collaborators with respect to our internal programs and disease area research. Any conflict with or among our collaborators could lead to the termination of our collaborative agreements, delay collaborative activities, impair our ability to renew agreements or obtain future collaboration agreements or result in litigation or arbitration and would negatively impact our relationship with existing collaborators. Further, if our collaborators fail to develop or commercialize any of our compounds or product candidates, we may not receive any future royalties or milestone payments for such compounds or product candidates.

We have limited or no control over the resources that our collaborators may choose to devote to our joint efforts. Our collaborators may breach or terminate their agreements with us or fail to perform their obligations thereunder. Further, our collaborators may elect not to develop products arising out of our collaborative arrangements, may experience financial difficulties, may undertake business combinations or significant changes in business strategy that adversely affect their willingness or ability to complete their obligations under any arrangement with us or may fail to devote sufficient resources to the development, manufacture, marketing or sale of such

products. Certain of our collaborators could also become competitors in the future. If our collaborators develop competing products, preclude us from entering into collaborations with their competitors, fail to obtain necessary regulatory approvals, terminate their agreements with us prematurely or fail to devote sufficient resources to the development and commercialization of our products, our product development efforts could be delayed and may fail to lead to commercialized products.

We lack the capability to manufacture compounds for clinical trials and rely on third parties to manufacture our product candidates, and we may be unable to obtain required material in a timely manner, at an acceptable cost or at a quality level required to receive regulatory approval.

We currently do not have manufacturing capabilities or experience necessary to produce materials for clinical trials, including XL119, XL784, XL647 and XL999. We rely on collaborators and third-party contractors to produce materials necessary for pre-clinical and clinical testing. We rely on selected manufacturers to deliver materials on a timely basis and to comply with applicable regulatory requirements, including the FDA's current Good Manufacturing Practices, or GMP. These outsourcing efforts with respect to manufacturing clinical supplies result in a dependence on our suppliers to timely manufacture and deliver sufficient quantities of materials produced under GMP conditions to enable us to conduct planned clinical trials and, if possible, to bring products to market in a timely manner.

Our current and anticipated future dependence upon these third-party manufacturers may adversely affect our future profit margins and our ability to develop and commercialize product candidates on a timely and competitive basis. These manufacturers may not be able to produce material on a timely basis or manufacture material at the quality level or in the quantity required to meet our development timelines and applicable regulatory requirements. We may not be able to maintain or renew our existing third-party manufacturing arrangements, or enter into new arrangements, on acceptable terms, or at all. Our third-party manufacturers could terminate or decline to renew our manufacturing arrangements based on their own business priorities, at a time that is costly or inconvenient for us. If we are unable to contract for the production of materials in sufficient quantity and of sufficient quality on acceptable terms, our planned clinical trials may be delayed. Delays in pre-clinical or clinical testing could delay the filing of our IND applications and the initiation of clinical trials.

Our third-party manufacturers may not be able to comply with the GMP regulations, other applicable FDA regulatory requirements or similar regulations applicable outside of the United States. Additionally, if we are required to enter into new supply arrangements, we may not be able to obtain approval from the FDA of any alternate supplier in a timely manner, or at all, which could delay or prevent the clinical development and commercialization of any related product candidates. Failure of our third-party manufacturers or us to obtain approval from the FDA or to comply with applicable regulations could result in sanctions being imposed on us, including fines, civil penalties, delays in or failure to grant marketing approval of our product candidates, injunctions, delays, suspension or withdrawal of approvals, license revocation, seizures or recalls of products and compounds, operating restrictions and criminal prosecutions, any of which could significantly and adversely affect our business.

If third parties on whom we rely do not perform as contractually required or expected, we may not be able to obtain regulatory approval for or commercialize our product candidates.

We do not have the ability to independently conduct clinical trials for our product candidates, and we must rely on third parties, such as contract research organizations, medical institutions, clinical investigators and contract laboratories to conduct our clinical trials. If these third parties do not successfully carry out their contractual duties or regulatory obligations or meet expected deadlines, if the third parties need to be replaced or if the quality or accuracy of the data they obtain is compromised due to the failure to adhere to our clinical protocols or regulatory requirements or for other reasons, our pre-clinical development activities or clinical trials may be extended, delayed, suspended or terminated, and we may not be able to obtain regulatory approval for or successfully commercialize our product candidates.

Materials necessary to manufacture some of our compounds currently under development may not be available on commercially reasonable terms, or at all, which may delay our development and commercialization of these drugs.

Some of the materials necessary for the manufacture of our compounds under development may, from time to time, be available either in limited quantities, or from a limited number of manufacturers, or both. Our contract manufacturers need to obtain these materials for our clinical trials and, potentially, for commercial distribution when and if we obtain marketing approval for these compounds. Suppliers may not sell us these materials at the time we need them or on commercially reasonable terms. If we are unable to obtain the materials needed for the conduct of our clinical trials, product testing and potential regulatory approval could be delayed, adversely impacting our ability to develop the product candidates. Similarly, if we are unable to obtain critical materials after regulatory approval has been obtained for a product candidate, the commercial launch of that product could be delayed or there would be a shortage in supply, which could materially affect our ability to generate revenues from that product. If suppliers increase the price of these materials, the price for one or more of our products may increase, which may make our product less competitive in the

marketplace. If it becomes necessary to change suppliers for any of these materials or if any of our suppliers experience a shutdown or disruption in the facilities used to produce these materials, due to technical, regulatory or other problems, it could harm our ability to manufacture our products. Our inability to obtain critical materials for any reason could substantially impair our development activities or the production, marketing and distribution of any products that we may develop.

Risks Related to Regulatory Approval of Our Product Candidates

Our product candidates are subject to a lengthy and uncertain regulatory process that may not result in the necessary regulatory approvals, which could adversely affect our ability to commercialize products.

Our product candidates, as well as the activities associated with their research, development and commercialization, are subject to extensive regulation by the FDA and other regulatory agencies in the United States and by comparable authorities in other countries. Failure to obtain regulatory approval for a product candidate would prevent us from commercializing that product candidate. We have not received regulatory approval to market any of our product candidates in any jurisdiction and have only limited experience in preparing and filing the applications necessary to gain regulatory approvals. The process of obtaining regulatory approvals is expensive, often takes many years, if approval is obtained at all, and can vary substantially based upon the type, complexity and novelty of the product candidates involved. Before a new drug application can be filed with the FDA, the product candidate must undergo extensive clinical trials, which can take many years and may require substantial expenditures. Any clinical trial may fail to produce results satisfactory to the FDA. The FDA could determine that the design of a clinical trial is inadequate to produce reliable results. The regulatory process also requires pre-clinical testing, and data obtained from pre-clinical and clinical activities are susceptible to varying interpretations, which could delay, limit or prevent regulatory approval. In addition, delays or rejections may be encountered based upon changes in regulatory policy for product approval during the period of product development and regulatory agency review.

Changes in regulatory approval policy, regulations or statutes or the process for regulatory review during the development or approval periods of our product candidates may cause delays in the approval or rejection of an application. Even if the FDA or a comparable authority in another country approves a product candidate, the approval may impose significant restrictions on the indicated uses, conditions for use, labeling, advertising, promotion, marketing and/or production of such product and may impose ongoing requirements for post-approval studies, including additional research and development and clinical trials. These agencies also may impose various civil or criminal sanctions for failure to comply with regulatory requirements, including withdrawal of product approval.

Risks Related to Commercialization of Products

The commercial success of any products that we may develop will depend upon the degree of market acceptance of our products among physicians, patients, health care payors, private health insurers and the medical community.

Our ability to commercialize any products that we may develop will be highly dependent upon the extent to which these products gain market acceptance among physicians, patients, health care payors, such as Medicare and Medicaid, private health insurers, including managed care organizations and group purchasing organizations, and the medical community. If these products do not achieve an adequate level of acceptance, we may not generate material product revenues, and we may not become profitable. The degree of market acceptance of our product candidates, if approved for commercial sale, will depend on a number of factors, including:

- the effectiveness, or perceived effectiveness, of our products in comparison to competing products;
- the existence of any significant side effects, as well as their severity in comparison to any competing products;
- potential advantages over alternative treatments;
- the ability to offer our products for sale at competitive prices;
- relative convenience and ease of administration;
- the strength of marketing and distribution support; and
- sufficient third-party coverage or reimbursement.

If we are unable to establish sales and marketing capabilities or enter into agreements with third parties to market and sell our product candidates, we may be unable to generate product revenues.

We have no experience as a company in the sales, marketing and distribution of pharmaceutical products and do not currently have a sales and marketing organization. Developing a sales and marketing force would be expensive and time-consuming and could delay any product launch, and we could not be certain that we could develop this capacity. However, to the extent that we enter into arrangements with third parties to perform sales, marketing and distribution services, our product revenues are likely to be lower than

if we market and sell any products that we develop ourselves. If we are unable to establish adequate sales, marketing and distribution capabilities, independently or with others, we may not be able to generate product revenues and may not become profitable.

If we are unable to obtain adequate coverage and reimbursement from third-party payors for any products that we may develop, our revenues and prospects for profitability will suffer.

Our ability to commercialize any products that we may develop will be highly dependent on the extent to which coverage and reimbursement for our products will be available from third-party payors, including governmental payors, such as Medicare and Medicaid, and private health insurers, including managed care organizations and group purchasing organizations. Many patients will not be capable of paying for some or all of the products that we may develop themselves and will rely on third-party payors to pay for their medical needs. If third-party payors do not provide coverage or reimbursement for any products that we may develop, our revenues and prospects for profitability will suffer. In addition, even if third-party payors provide some coverage or reimbursement for our products, the availability of such coverage or reimbursement for prescription drugs under private health insurance and managed care plans often varies based on the type of contract or plan purchased.

A primary trend in the United States health care industry is toward cost containment. In December 2003, the President signed into law legislation creating a prescription drug benefit program for Medicare recipients. The prescription drug program established by the legislation may have the effect of reducing the prices that we are able to charge for products we develop and sell through these plans. This prescription drug legislation may also cause third-party payors other than the federal government, including the States under the Medicaid program, to discontinue coverage for products we develop or to lower the amount that they will pay.

Another development that may affect the pricing of drugs is the proposed Congressional action regarding drug reimportation into the United States. The Medicare Prescription Drug Plan legislation gives additional discretion to the Secretary of Health and Human Services to allow drug reimportation from foreign countries into the United States under some circumstances, including countries where the drugs are sold at a lower price than in the United States. Proponents of drug reimportation may attempt to pass legislation, which would directly allow reimportation under certain circumstances. If legislation or regulations were passed allowing the reimportation of drugs, they could decrease the price we receive for any products that we may develop, negatively affecting our revenues and prospects for profitability.

In addition, in some foreign countries, particularly the countries of the European Union, the pricing of prescription pharmaceuticals is subject to governmental control. In these countries, pricing negotiations with governmental authorities can take six to 12 months or longer after the receipt of regulatory marketing approval for a product. To obtain reimbursement or pricing approval in some countries, we may be required to conduct a clinical trial that compares the cost effectiveness of our product candidates or products to other available therapies. The conduct of such a clinical trial could be expensive and result in delays in the commercialization of our product candidates. Third-party payors are challenging the prices charged for medical products and services, and many third-party payors limit reimbursement for newly approved health care products. In particular, third-party payors may limit the indications for which they will reimburse patients who use any products that we may develop. Cost-control initiatives could decrease the price we might establish for products that we may develop, which would result in lower product revenues to us.

Our competitors may develop products and technologies that make our products and technologies obsolete.

The biotechnology industry is highly fragmented and is characterized by rapid technological change. In particular, the area of gene research is a rapidly evolving field. We face, and will continue to face, intense competition from large biotechnology and pharmaceutical companies, as well as academic research institutions, clinical reference laboratories and government agencies that are pursuing research activities similar to ours. Some of our competitors have entered into collaborations with leading companies within our target markets, including some of our existing collaborators. In addition, significant delays in the development of our product candidates could allow our competitors to bring products to market before us, which would impair our ability to commercialize our product candidates. Our future success will depend on our ability to maintain a competitive position with respect to technological advances. Any products that are developed through our technologies will compete in highly competitive markets. Further, our competitors may be more effective at using their technologies to develop commercial products. Many of the organizations competing with us have greater capital resources, larger research and development staffs and facilities, more experience in obtaining regulatory approvals and more extensive product manufacturing and marketing capabilities. As a result, our competitors may be able to more easily develop technologies and products that would render our technologies and products, and those of our collaborators, obsolete and noncompetitive. In addition, there may be product candidates of which we are not aware at an earlier stage of development that may compete with our product candidates.

We may not be able to manufacture our product candidates in commercial quantities, which would prevent us from commercializing our product candidates.

To date, our product candidates have been manufactured in small quantities for pre-clinical and clinical trials. If any of these product candidates are approved by the FDA or other regulatory agencies for commercial sale, we will need to manufacture them in larger quantities. We may not be able to successfully increase the manufacturing capacity, whether in collaboration with third-party manufacturers or on our own, for any of our product candidates in a timely or economic manner, or at all. Significant scale-up of manufacturing may require additional validation studies, which the FDA must review and approve. If we are unable to successfully increase the manufacturing capacity for a product candidate, the regulatory approval or commercial launch of that product candidate may be delayed or there may be a shortage in supply. Our product candidates require precise, high quality manufacturing. Our failure to achieve and maintain these high manufacturing standards, including the incidence of manufacturing errors, could result in patient injury or death, product recalls or withdrawals, delays or failures in product testing or delivery, cost overruns or other problems that could seriously hurt our business.

Risks Related to Our Intellectual Property

If we are unable to adequately protect our intellectual property, third parties may be able to use our technology, which could adversely affect our ability to compete in the market.

Our success will depend in part on our ability to obtain patents and maintain adequate protection of the intellectual property related to our technologies and products. The patent positions of biotechnology companies, including our patent position, are generally uncertain and involve complex legal and factual questions. We will be able to protect our intellectual property rights from unauthorized use by third parties only to the extent that our technologies are covered by valid and enforceable patents or are effectively maintained as trade secrets. We will continue to apply for patents covering our technologies and products as and when we deem appropriate. However, these applications may be challenged or may fail to result in issued patents. In addition, because patent applications can take many years to issue, there may be currently pending applications, unknown to us, which may later result in issued patents that cover the production, manufacture, commercialization or use of our product candidates. Our existing patents and any future patents we obtain may not be sufficiently broad to prevent others from practicing our technologies or from developing competing products. Furthermore, others may independently develop similar or alternative technologies or design around our patents. In addition, our patents may be challenged or invalidated or may fail to provide us with any competitive advantages, if, for example, others were the first to invent or to file patent applications for these inventions.

The laws of some foreign countries do not protect intellectual property rights to the same extent as the laws of the United States, and many companies have encountered significant problems in protecting and defending such rights in foreign jurisdictions. Many countries, including certain countries in Europe, have compulsory licensing laws under which a patent owner may be compelled to grant licenses to third parties (for example, the patent owner has failed to “work” the invention in that country or the third party has patented improvements). In addition, many countries limit the enforceability of patents against government agencies or government contractors. In these countries, the patent owner may have limited remedies, which could materially diminish the value of the patent. Compulsory licensing of life saving drugs is also becoming increasingly popular in developing countries either through direct legislation or international initiatives. Such compulsory licenses could be extended to include some of our product candidates, which could limit our potential revenue opportunities. Moreover, the legal systems of certain countries, particularly certain developing countries, do not favor the aggressive enforcement of patent and other intellectual property protection, which makes it difficult to stop infringement.

We rely on trade secret protection for our confidential and proprietary information. We have taken security measures to protect our proprietary information and trade secrets, but these measures may not provide adequate protection. While we seek to protect our proprietary information by entering into confidentiality agreements with employees, collaborators and consultants, we cannot assure you that our proprietary information will not be disclosed, or that we can meaningfully protect our trade secrets. In addition, our competitors may independently develop substantially equivalent proprietary information or may otherwise gain access to our trade secrets.

Litigation or third-party claims of intellectual property infringement could require us to spend substantial time and money and adversely affect our ability to develop and commercialize products.

Our commercial success depends in part on our ability to avoid infringing patents and proprietary rights of third parties and not breaching any licenses that we have entered into with regard to our technologies. Other parties have filed, and in the future are likely to file, patent applications covering genes and gene fragments, techniques and methodologies relating to model systems and products and technologies that we have developed or intend to develop. If patents covering technologies required by our operations are issued to others, we may have to rely on licenses from third parties, which may not be available on commercially reasonable terms, or at all, and may require us to pay substantial royalties, grant a cross-license to some of our patents to another patent holder or redesign the formulation of a product candidate so that it does not infringe these patents, which may not be possible or could require substantial time and expense.

Third parties may accuse us of employing their proprietary technology without authorization. In addition, third parties may obtain patents that relate to our technologies and claim that use of such technologies infringes these patents. Regardless of their merit, such claims could require us to incur substantial costs, including the diversion of management and technical personnel, in defending ourselves against any such claims or enforcing our patents. In the event that a successful claim of infringement is brought against us, we may be required to pay damages and obtain one or more licenses from third parties. We may not be able to obtain these licenses at a reasonable cost, or at all. Defense of any lawsuit or failure to obtain any of these licenses could adversely affect our ability to develop and commercialize products.

We may be subject to damages resulting from claims that we or our employees have wrongfully used or disclosed alleged trade secrets of their former employers.

Many of our employees were previously employed at universities or other biotechnology or pharmaceutical companies, including our competitors or potential competitors. We may be subject to claims that these employees or we have inadvertently or otherwise used or disclosed trade secrets or other proprietary information of their former employers. Litigation may be necessary to defend against these claims. Even if we are successful in defending against these claims, litigation could result in substantial costs and be a distraction to management. If we fail in defending such claims, in addition to paying money claims, we may lose valuable intellectual property rights or personnel. A loss of key research personnel or their work product could hamper or prevent our ability to commercialize certain product candidates, which could severely harm our business.

Risks Related to Employees, Growth and Location

The loss of key personnel or the inability to attract and retain additional personnel could impair our ability to expand our operations.

We are highly dependent on the principal members of our management and scientific staff, the loss of whose services might adversely impact the achievement of our objectives and the continuation of existing collaborations. However, we do not currently have sufficient executive management and technical personnel to fully execute our business plan. Recruiting and retaining qualified scientific and clinical personnel will be critical to support activities related to advancing our clinical and pre-clinical development programs, and supporting our collaborative arrangements and our internal proprietary research and development efforts. Although we believe we will be successful in attracting and retaining qualified management, competition is intense for experienced technical personnel, and we may be unable to retain or recruit scientists with the expertise or experience necessary to allow us to pursue collaborations, develop our products and core technologies or expand our operations to the extent otherwise possible. Further, all of our employees are employed “at will” and, therefore, may leave our employment at any time.

Our collaborations with outside scientists may be subject to restriction and change.

We work with scientific and clinical advisors and collaborators at academic and other institutions that assist us in our research and development efforts. These scientists and advisors are not our employees and may have other commitments that limit their availability to us. Although our advisors and collaborators generally agree not to do competing work, if a conflict of interest between their work for us and their work for another entity arises, we may lose their services. In addition, although our advisors and collaborators sign agreements not to disclose our confidential information, it is possible that valuable proprietary knowledge may become publicly known through them.

Difficulties we may encounter managing our growth may divert resources and limit our ability to successfully expand our operations.

We have experienced a period of rapid and substantial growth that has placed, and our anticipated growth in the future will continue to place, a strain on our research, administrative and operational infrastructure. As our operations expand, we will need to continue to manage multiple locations and additional relationships with various collaborative partners, suppliers and other third parties. Our ability to manage our operations and growth effectively requires us to continue to improve our reporting systems and procedures as well as our operational, financial and management controls. In addition, recent SEC rules and regulations have increased the internal control and regulatory requirements under which we operate. We may not be able to successfully implement improvements to our management information and control systems in an efficient or timely manner and may discover deficiencies in existing systems and controls.

Our headquarters facilities are located near known earthquake fault zones, and the occurrence of an earthquake or other catastrophic disaster could cause damage to our facilities and equipment, which could require us to cease or curtail operations.

Given our headquarters location in South San Francisco, California, our facilities are vulnerable to damage from earthquakes. We currently do not carry earthquake insurance. We are also vulnerable worldwide to damage from other types of disasters, including fire, floods, power loss, communications failures, terrorism and similar events. If any disaster were to occur, our ability to operate our business at our facilities would be seriously, or potentially completely, impaired. In addition, the unique nature of our research activities could cause significant delays in our programs and make it difficult for us to recover from a disaster. The insurance we maintain may not be adequate to cover our losses resulting from disasters or other business interruptions. Accordingly, an earthquake or other disaster could materially and adversely harm our ability to conduct business.

Risks Related to Environmental and Product Liability

We use hazardous chemicals and radioactive and biological materials in our business. Any claims relating to improper handling, storage or disposal of these materials could be time consuming and costly.

Our research and development processes involve the controlled use of hazardous materials, including chemicals and radioactive and biological materials. Our operations produce hazardous waste products. We cannot eliminate the risk of accidental contamination or discharge and any resultant injury from these materials. Federal, state and local laws and regulations govern the use, manufacture, storage, handling and disposal of hazardous materials. We may be sued for any injury or contamination that results from our use or the use by third parties of these materials, and our liability may exceed our insurance coverage and our total assets. Compliance with environmental laws and regulations may be expensive, and current or future environmental regulations may impair our research, development and production efforts.

In addition, our collaborators may use hazardous materials in connection with our collaborative efforts. In the event of a lawsuit or investigation we could be held responsible for any injury caused to persons or property by exposure to, or release of, these hazardous materials used by these parties. Further, we may

be required to indemnify our collaborators against all damages and other liabilities arising out of our development activities or products produced in connection with these collaborations.

We face potential product liability exposure far in excess of our limited insurance coverage.

We may be held liable if any product our collaborators or we develop causes injury or is found otherwise unsuitable during product testing, manufacturing, marketing or sale. Regardless of merit or eventual outcome, product liability claims could result in decreased demand for our product candidates, injury to our reputation, withdrawal of patients from our clinical trials, substantial monetary awards to trial participants and the inability to commercialize any products that we may develop. These claims might be made directly by consumers, health care providers, pharmaceutical companies or others selling or testing our products. We have obtained limited product liability insurance coverage for our clinical trials in the amount of $10.0 million per occurrence and $10.0 million in the aggregate. However, our insurance may not reimburse us or may not be sufficient to reimburse us for expenses or losses we may suffer. Moreover, insurance coverage is becoming increasingly expensive, and we may not be able to maintain insurance coverage at a reasonable cost or in sufficient amounts to protect us against losses due to liability. If we obtain marketing approval for any of our product candidates in development, we intend to expand our insurance coverage to include the sale of commercial products, but we may be unable to obtain commercially reasonable product liability insurance for any products approved for marketing. On occasion, juries have awarded large judgments in class action lawsuits based on drugs that had unanticipated side effects. In addition, the pharmaceutical and biotechnology industries, in general, have been subject to significant medical malpractice litigation. A successful product liability claim or series of claims brought against us would decrease our cash reserves and could cause our stock price to fall.

Risks Related to Genetic Engineering of Products

Social issues may limit the public acceptance of genetically engineered products, which could reduce demand for our products.

Although our technology is not dependent on genetic engineering, genetic engineering plays a prominent role in our approach to product development. For example, research efforts focusing on plant traits may involve either selective breeding or modification of existing genes in the plant under study. Public attitudes may be influenced by claims that genetically engineered products are unsafe for consumption or pose a danger to the environment. Such claims may prevent our genetically engineered products from gaining public acceptance. The commercial success of our future products will depend, in part, on public acceptance of the use of genetically engineered products, including drugs and plant and animal products.

The subject of genetically modified organisms has received negative publicity, which has aroused public debate. For example, certain countries in Europe are considering regulations that ban products or require express labeling of products that contain genetic modifications or are “genetically modified.” In addition, the European Union has implemented rules that regulate the placing on the market of food and feed products containing or consisting of genetically modified organisms. These rules also provide for the labeling of such products to the final consumer. Adverse publicity has resulted in greater regulation internationally and trade restrictions on

imports of genetically altered products. If similar action is taken in the United States, genetic research and genetically engineered products could be subject to greater domestic regulation, including stricter labeling requirements. To date, our business has not been hampered by these activities. However, such publicity in the future may prevent any products resulting from our research from gaining market acceptance and reduce demand for our products.

Laws and regulations may reduce our ability to sell genetically engineered products that we or our collaborators develop in the future.

We or our collaborators may develop genetically engineered agricultural and animal products. The field-testing, production and marketing of genetically engineered products are subject to regulation by federal, state, local and foreign governments. Regulatory agencies administering existing or future regulations or legislation may prevent us from producing and marketing genetically engineered products in a timely manner or under technically or commercially feasible conditions. In addition, regulatory action or private litigation could result in expenses, delays or other impediments to our product development programs and the commercialization of products. The FDA has released a policy statement stating that it will apply the same regulatory standards to foods developed through genetic engineering as it applies to foods developed through traditional plant breeding. Genetically engineered food products will be subject to premarket review, however, if these products raise safety questions or are deemed to be food additives. Our product candidates may be subject to lengthy FDA reviews and unfavorable FDA determinations if they raise questions regarding safety or our products are deemed to be food additives.

To date, the FDA has not required genetically engineered agricultural products to be labeled as such, provided that these products are as safe and have the same nutritional characteristics as conventionally developed products. The FDA may reconsider or change its policies, and local or state authorities may enact labeling requirements, either of which could have a material adverse effect on our ability or the ability of our collaborators to develop and market products resulting from our efforts.

Risks Related to Our Common Stock

We expect that our quarterly results of operations will fluctuate, and this fluctuation could cause our stock price to decline, causing investor losses.

Our quarterly operating results have fluctuated in the past and are likely to fluctuate in the future. A number of factors, many of which we cannot control, could subject our operating results and stock price to volatility, including:

- recognition of upfront licensing or other fees;
- payments of non-refundable upfront or licensing fees to third parties;
- acceptance of our technologies and platforms;
- the success rate of our discovery efforts leading to milestone payments and royalties;
- the introduction of new technologies or products by our competitors;
- the timing and willingness of collaborators to commercialize our products;
- our ability to enter into new collaborative relationships;
- the termination or non-renewal of existing collaborations;
- the timing and amount of expenses incurred for clinical development and manufacturing of our products;

- the impairment of acquired goodwill and other assets; and
- general and industry-specific economic conditions that may affect our collaborators' research and development expenditures.

A large portion of our expenses, including expenses for facilities, equipment and personnel, are relatively fixed in the short term. In addition, we expect operating expenses to increase significantly during the next year as we move more compounds into clinical development. Accordingly, if our revenues decline or do not grow as anticipated due to the expiration or termination of existing contracts or our failure to obtain new contracts, our inability to meet milestones or other factors, we may not be able to correspondingly reduce our operating expenses. Failure to achieve anticipated levels of revenues could therefore significantly harm our operating results for a particular fiscal period.

Due to the possibility of fluctuations in our revenues and expenses, we believe that quarter-to-quarter comparisons of our operating results are not a good indication of our future performance. As a result, in some future quarters, our operating results may not meet the expectations of stock market analysts and investors, which could result in a decline in the price of our stock.

Our stock price may be extremely volatile.

The trading price of our common stock has been highly volatile, and we believe the trading price of our common stock will remain highly volatile and may fluctuate substantially due to factors such as the following:

- adverse results or delays in clinical trials;
- announcement of FDA approval or non-approval, or delays in the FDA review process, of our or our collaborators' product candidates or those of our competitors or actions taken by regulatory agencies with respect to our, our collaborators' or our competitors' clinical trials;
- the announcement of new products by us or our competitors;
- quarterly variations in our or our competitors' results of operations;
- litigation, including intellectual property infringement lawsuits, involving us;
- failure to achieve operating results projected by securities analysts;
- changes in earnings estimates or recommendations by securities analysts;
- developments in the biotechnology industry;
- sales of large blocks of our common stock or sales of our common stock by our executive officers, directors and significant stockholders;
- departures of key personnel;
- developments concerning current or future collaborations;
- FDA or international regulatory actions;
- third-party reimbursement policies;
- acquisitions of other companies or technologies; and
- general market conditions and other factors, including factors unrelated to our operating performance or the operating performance of our competitors.

These factors and fluctuations, as well as general economic, political and market conditions, may materially adversely affect the market price of our common stock.

In the past, following periods of volatility in the market price of a company's securities, securities class action litigation has often been instituted. A securities class action suit against us could result in substantial costs and divert management's attention and resources, which could have a material and adverse effect on our business.

We are exposed to risks associated with acquisitions.

We have made, and may in the future make, acquisitions of, or significant investments in, businesses with complementary products, services and/or technologies. Acquisitions involve numerous risks, including, but not limited to:

- difficulties and increased costs in connection with integration of the personnel, operations, technologies and products of acquired companies;
- diversion of management's attention from other operational matters;
- the potential loss of key employees;
- the potential loss of key collaborators;
- lack of synergy, or the inability to realize expected synergies, resulting from the acquisition; and
- acquired intangible assets becoming impaired as a result of technological advancements or worse-than-expected performance of the acquired company.

Mergers and acquisitions are inherently risky, and the inability to effectively manage these risks could materially and adversely affect our business, financial condition and results of operations.

For example, we recently completed our acquisition of X-Ceptor. If Exelixis is not successful in integrating X-Ceptor in its operations, the anticipated benefits of the acquisition may not be realized. The dedication of Exelixis' management resources to integration activities may detract attention from the day-to-day business of Exelixis. In addition, key officers and employees of X-Ceptor may leave the company at any time. The failure to retain such key officers and employees may decrease the likelihood of a successful integration.

Future sales of our common stock may depress our stock price.

If our stockholders sell substantial amounts of our common stock (including shares issued upon the exercise of options and warrants) in the public market, the market price of our common stock could fall. These sales also might make it more difficult for us to sell equity or equity-related securities in the future at a time and price that we deemed appropriate. For example, following an acquisition, a significant number of shares of our common stock held by new stockholders may become freely tradable or holders of registration rights could cause us to register their shares for resale. Sales of these shares of common stock held by existing stockholders could cause the market price of our common stock to decline.

Some of our existing stockholders can exert control over us, and their interests could conflict with the best interests of our other stockholders.

Due to their combined stock holdings, our officers, directors and principal stockholders (stockholders holding more than 5% of our common stock), acting together, may be able to exert significant influence over all matters requiring stockholder approval, including the election of directors and approval of significant corporate transactions. In addition, this concentration of ownership may delay or prevent a change in control of our company, even when a change may be in the best interests of our stockholders. In addition, the interests of these stockholders may not always coincide with our interests as a company or the interests of other stockholders. Accordingly, these stockholders could cause us to enter into transactions or agreements that you would not approve of.

Anti-takeover provisions in our charter documents and under Delaware law could make an acquisition of us, which may be beneficial to our stockholders, more difficult and may prevent attempts by our stockholders to replace or remove our current management.

Provisions in our corporate charter and bylaws may discourage, delay or prevent an acquisition of us, a change in control, or attempts by our stockholders to replace or remove members of our current Board of Directors. Because our Board of Directors is responsible for appointing the members of our management team, these provisions could in turn affect any attempt by our stockholders to replace current members of our management team. These provisions include:

- a classified Board of Directors;
- a prohibition on actions by our stockholders by written consent;
- the ability of our Board of Directors to issue preferred stock without stockholder approval, which could be used to institute a “poison pill” that would work to dilute the stock ownership of a potential hostile acquirer, effectively preventing acquisitions that have not been approved by our Board of Directors; and
- limitations on the removal of directors.

Moreover, because we are incorporated in Delaware, we are governed by the provisions of Section 203 of the Delaware General Corporation Law, which prohibits a person who owns in excess of 15% of our outstanding voting stock from merging or combining with us for a period of three years after the date of the transaction in which the person acquired in excess of 15% of our outstanding voting stock, unless the merger or combination is approved in a prescribed manner. Finally, these provisions establish advance notice requirements for nominations for election to our Board of Directors or for proposing matters that can be acted upon at stockholder meetings. These provisions would apply even if the offer may be considered beneficial by some stockholders.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our market risk disclosures set forth in Item 7A of our Annual Report on Form 10-K for the year ended December 31, 2003 have not changed significantly. Our exposure to market risk for changes in interest rates relates primarily to our investment portfolio and our long-term debt. We have estimated the effects on our interest rate sensitive assets and liabilities based on a one percentage point hypothetical adverse change in interest rates as of September 30, 2004 and December 31, 2003. As of September 30, 2004 and December 31, 2003, a decrease in the interest rates of one percentage point would have had a net adverse change in the fair value of interest rate sensitive assets and liabilities of approximately $3.4 million and $2.7 million, respectively.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of disclosure controls and procedures. Based on the evaluation of our disclosure controls and procedures (as defined in Securities Exchange Act of 1934 Rules 13a-15(e) and 15d-15(e)) required by Securities Exchange Act Rules 13a-15(b) or 15d-15(b), our Chief Executive Officer and our Chief Financial Officer have concluded that as of the end of the period covered by this report, our disclosure controls and procedures were effective.

Changes in internal controls. There were no changes in our internal control over financial reporting that occurred during our most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 6. EXHIBITS

(a) Exhibits

The exhibits listed on the accompanying index to exhibits are filed or incorporated by reference (as stated therein) as part of this Quarterly Report on Form 10-Q.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

EXELIXIS, INC.

Date: November 8, 2004

/s/ Frank Karbe
Frank Karbe
Senior Vice President, Chief Financial Officer
(Principal Financial and Accounting Officer)

EXHIBIT INDEX

Number	Exhibit Description
2.1	Agreement and Plan of Merger, dated as of September 27, 2004, by and among Exelixis, Inc., XBO Acquisition Corp., a wholly-owned subsidiary of Exelixis, Inc. and X-Ceptor Therapeutics, Inc.(1)
3.1	Amended and Restated Certificate of Incorporation of Exelixis, Inc.(2)
3.2	Amended and Restated Bylaws of Exelixis, Inc.(3)
4.1	Specimen Common Stock Certificate.(3)
4.2	Fourth Amended and Restated Registration Rights Agreement, dated February 26,1999 among Exelixis, Inc. and Certain Stockholders of Exelixis, Inc.(3)
4.3	Warrant, dated August 17, 1998, to purchase 125,796 post-split shares of Exelixis, Inc. Series A preferred stock in favor of Comdisco, Inc.(3)
4.4	Warrant, dated August 17, 1998, to purchase 15,365 post-split shares of Exelixis, Inc. Series A preferred stock in favor of Greg Stento.(3)
4.5	Warrant, dated January 24, 1996, to purchase 267,857 post-split shares of Exelixis, Inc. Series B convertible stock in favor of MMC/GATX Partnership No. 1.(3)
4.6	Warrant, dated September 25, 1999, to purchase 63,750 post-split shares of Exelixis, Inc. common stock in favor of MMC/GATX Partnership No. 1.(3)
4.7	Warrant, dated November 15, 1999, to purchase 9,000 post-split shares of Exelixis, Inc. common stock in favor of Bristow Investments, L.P.(3)
4.8	Warrant, dated November 15, 1999, to purchase 101,250 post-split shares of Exelixis, Inc. common stock in favor of Slough Estates USA, Inc.(3)
4.9	Warrant, dated November 15, 1999, to purchase 2,250 post-split shares of Exelixis, Inc. common stock in favor of Laurence and Magdalena Shushan Trust.(3)
4.10	Warrant, dated April 1, 2000, to purchase 70, 875 shares of Exelixis, Inc. common stock in favor of Slough Estates USA, Inc.(4)
4.11	Warrant, dated April 1, 2000, to purchase 6,300 shares of Exelixis, Inc. common stock in favor of Bristow Investments, L.P.(4)
4.12	Warrant, dated April 1, 2000, to purchase 1,575 shares of Exelixis, Inc. common stock in favor of Laurence and Magdalena Shushan Family Trust.(4)
4.13	Form of Convertible Promissory Note, dated May 22, 2001, by and between Exelixis, Inc. and Protein Design Labs, Inc.(5)
4.14	Form of Note Purchase Agreement, dated May 22, 2001, by and between Exelixis, Inc. and Protein Design Labs, Inc.(5)
10.1*	Form of Stock Option Agreement under the 2000 Non-Employee Directors' Stock Option Plan.(6)
10.2*	Form of Stock Option Agreement under the 2000 Equity Incentive Plan.(6)
10.3	Second Amendment to Loan and Security Agreement, dated as of September 20, 2004, by and between SmithKlineBeecham Corporation and Exelixis, Inc. (7)
10.4	Registration Rights Agreement, dated October 18, 2004, by and among Exelixis, Inc., X-Ceptor Therapeutics, Inc., and those certain holders of capital stock of X-Ceptor Therapeutics, Inc. listed in Annex I thereto.(8)
10.5	Registration Rights Agreement, dated October 18, 2004, by and among Exelixis, Inc., X-Ceptor Therapeutics, Inc., and those certain holders of capital stock of X-Ceptor Therapeutics, Inc. listed in Annex I thereto.(8)
31.1	Certification required by Rule 13a-14(a) or Rule 15d-14(a).
31.2	Certification required by Rule 13a-14(a) or Rule 15d-14(a).
32.1**	Certification by the Chief Executive Officer and the Chief Financial Officer of Exelixis, Inc., as required by Rule 13a-14(b) or Rule 15d-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. 1350).(9)

(1) Filed as an Exhibit to Exelixis, Inc.'s Current Report on Form 8-K, as filed with the Securities and Exchange Commission on September 28, 2004 and incorporated herein by reference.

(2) Filed as an Exhibit to Exelixis, Inc.'s Quarterly Report on Form 10-Q for the quarter ended June 30, 2004 and incorporated herein by reference.

(3) Filed as an Exhibit to Exelixis, Inc.'s Registration Statement on Form S-1 (File No. 333-30978), as filed with the Securities and Exchange Commission on February 7, 2000, as amended, and incorporated herein by reference.

(4) Filed as an Exhibit to Exelixis, Inc.'s Quarterly Report on Form 10-Q for the quarter ended March 31, 2000 and incorporated herein by reference.

(5) Filed as an Exhibit to Exelixis, Inc.'s Quarterly Report on Form 10-Q for the quarter ended June 30, 2001 and incorporated herein by reference.

*(6) Management contract or compensatory plan.

(7) Filed as on Exhibit to Exelixis, Inc.'s Current Report on Form 8-K, as filed with the Securities and Exchange Commission on September 23, 2004 and incorporated herein by reference.

(8) Filed as on Exhibit to Exelixis, Inc.'s Current Report on Form 8-K, as filed with the Securities and Exchange Commission on October 21, 2004 and incorporated herein by reference.

**(9) This certification accompanies this Quarterly Report on Form 10-Q, is not deemed filed with the SEC and is not to be incorporated by reference into any filing of the Company under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended (whether made before or after the date of this Quarterly Report on Form 10-Q), irrespective of any general incorporation language contained in such filing.

EXELIXIS, INC.
2000 NON-EMPLOYEE DIRECTORS' STOCK OPTION PLAN

STOCK OPTION AGREEMENT
(NONSTATUTORY STOCK OPTION)

Pursuant to your Certificate of Stock Option Grant on the Smith Barney Stock Plan Services website ("the Grant Certificate") and this Stock Option Agreement, Exelixis, Inc. (the "Company") has granted you an option under its 2000 Non-Employee Directors' Stock Option Plan (the "Plan") to purchase the number of shares of the Company's Common Stock indicated in your Grant Certificate at the exercise price indicated in your Grant Certificate. Defined terms not explicitly defined in this Stock Option Agreement but defined in the Plan shall have the same definitions as in the Plan.

The details of your option are as follows:

1. **VESTING**. Subject to the limitations contained herein, your option will vest as provided in your Grant Certificate, provided that vesting will cease upon the termination of your Continuous Service.

2. **NUMBER OF SHARES AND EXERCISE PRICE**. The number of shares of Common Stock subject to your option and your exercise price per share referenced in your Grant **Certificate** may be adjusted from time to time for Capitalization Adjustments, as provided in the Plan.

3. **EXERCISE PRIOR TO VESTING ("EARLY EXERCISE")**. Subject to the provisions of your option, you may elect at any time that is both (i) during the period of your Continuous Service and (ii) during the term of your option, to exercise all or part of your option, including the nonvested portion of your option; provided, however, that:

(a) a partial exercise of your option shall be deemed to cover first vested shares of Common Stock and then the earliest vesting installment of unvested shares of Common Stock;

(b) any shares of Common Stock so purchased from installments that have not vested as of the date of exercise shall be subject to the purchase option in favor of the Company as described in the Company's form of Early Exercise Stock Purchase Agreement; and

(c) you shall enter into the Company's form of Early Exercise Stock Purchase Agreement with a vesting schedule that will result in the same vesting as if no early exercise had occurred.

4. **METHOD OF PAYMENT**. Payment of the exercise price is due in full upon exercise of all or any part of your option. You may elect to make payment of the exercise price in cash or by check or by one or more of the following:

(a) Provided that at the time of exercise the Common Stock is publicly traded and quoted regularly in *The Wall Street Journal*, pursuant to a program developed under Regulation T as promulgated by the Federal Reserve Board that, prior to the issuance of Common Stock, results in either the receipt of cash (or check) by the Company or the receipt of irrevocable instructions to pay the aggregate exercise price to the Company from the sales proceeds.

(b) Provided that at the time of exercise the Common Stock is publicly traded and quoted regularly in *The Wall Street Journal*, by delivery of already-owned shares of Common Stock either that you have held for the period required to avoid a charge to the Company's reported earnings (generally six months) or that you did not acquire, directly or indirectly from the Company, that are owned free and clear of any liens, claims, encumbrances or security interests, and that are valued at Fair Market Value on the date of exercise. "Delivery" for these purposes, in the sole discretion of the Company at the time you exercise your option, shall include delivery to the Company of your attestation of ownership of such shares of Common Stock in a form approved by the Company. Notwithstanding the foregoing, you may not exercise your option by tender to the Company of Common Stock to the extent such tender would violate the provisions of any law, regulation or agreement restricting the redemption of the Company's stock.

5. **WHOLE SHARES**. You may exercise your option only for whole shares of Common Stock.

6. **SECURITIES LAW COMPLIANCE**. Notwithstanding anything to the contrary contained herein, you may not exercise your option unless the shares of Common Stock issuable upon such exercise are then registered under the Securities Act or, if such shares of Common Stock are not then so registered, the Company has determined that such exercise and issuance would be exempt from the registration requirements of the Securities Act. The exercise of your option must also comply with other applicable laws and regulations governing your option, and you may not exercise your option if the Company determines that such exercise would not be in material compliance with such laws and regulations.

7. **TERM**. The term of your option commences on the Date of Grant and expires upon the ***earliest*** of the following:

(a) three (3) months after the termination of your Continuous Service for any reason other than your Disability or death, provided that if during any part of such three- (3-) month period your option is not exercisable solely because of the condition set forth in the preceding paragraph relating to "Securities Law Compliance," your option shall not expire until the earlier of the Expiration Date or until it shall have been exercisable for an aggregate period of three (3) months after the termination of your Continuous Service;

(b) twelve (12) months after the termination of your Continuous Service due to your Disability;

(c) eighteen (18) months after your death if you die either during your Continuous Service or within three (3) months after your Continuous Service terminates; or

(d) the Expiration Date indicated in your Grant Certificate.

8. EXERCISE.

(a) You may exercise your option during its term by delivering a Cash Letter of Authorization or other appropriate form (in a form designated by the Company) together with the exercise price to the Secretary of the Company, or to such other person as the Company may designate, during regular business hours, together with such additional documents as the Company may then require.

(b) By exercising your option you agree that, as a condition to any exercise of your option, the Company may require you to enter into an arrangement providing for the payment by you to the Company of any tax withholding obligation of the Company arising by reason of the exercise of your option.

(c) **TRANSFERABILITY**. Your option is not transferable, except (i) by will or by the laws of descent and distribution, and (ii) to such further extent as permitted by the Rule as to Use of Form S-8 specified in the General Instructions of the Form S-8 Registration Statement under the Securities Act. Your option is exercisable during your life only by you or a transferee satisfying the above-stated conditions. The right of a transferee to exercise the transferred portion of your option after termination of your Continuous Service shall terminate in accordance with your right to exercise your option as specified in your option. In the event that your Continuous Service terminates due to your death, your transferee will be treated as a person who acquired the right to exercise your option by bequest or inheritance. In addition to the foregoing, the Company may require, as a condition of the transfer of your option to a trust or by gift, that your transferee enter into an option transfer agreement provided by, or acceptable to, the Company. The terms of your option shall be binding upon your transferees, executors, administrators, heirs, successors, and assigns. Notwithstanding the foregoing, by delivering written notice to the Company, in a form satisfactory to the Company, you may designate a third party who, in the event of your death, shall thereafter be entitled to exercise your option.

9. OPTION NOT A SERVICE CONTRACT. Your option is not an employment or service contract, and nothing in your option shall be deemed to create in any way whatsoever any obligation on your part to continue in the employ of the Company or an Affiliate, or of the Company or an Affiliate to continue your employment. In addition, nothing in your option shall obligate the Company or an Affiliate, their respective stockholders, Boards of Directors, Officers or Employees to continue any relationship that you might have as a Director or Consultant for the Company or an Affiliate.

10. NOTICES. Any notices provided for in your option or the Plan shall be given in writing and shall be deemed effectively given upon receipt or, in the case of notices delivered by mail by the Company to you, five (5) days after deposit in the United States mail, postage prepaid, addressed to you at the last address you provided to the Company.

11. GOVERNING PLAN DOCUMENT. Your option is subject to all the provisions of the Plan, the provisions of which are hereby made a part of your option, and is further subject to all interpretations, amendments, rules and regulations which may from time to time be promulgated and adopted pursuant to the Plan. In the event of any conflict between the provisions of your option and those of the Plan, the provisions of the Plan shall control.

EXELIXIS, INC.
2000 EQUITY INCENTIVE PLAN

STOCK OPTION AGREEMENT
(INCENTIVE AND NONSTATUTORY STOCK OPTIONS)

Pursuant to your stock option grant as evidenced by the Certificate of Stock Option Grant on the Smith Barney Stock Plan Services website ("the Grant Certificate") and this Stock Option Agreement, Exelixis, Inc. (the "Company") has granted you an option under its 2000 Equity Incentive Plan (the "Plan") to purchase the number of shares of the Company's Common Stock indicated in your Grant Certificate at the exercise price indicated in your Grant Certificate. Defined terms not explicitly defined in this Stock Option Agreement but defined in the Plan shall have the same definitions as in the Plan.

The details of your option are as follows:

1. VESTING. Subject to the limitations contained herein, your option will vest as provided in your Grant Certificate, provided that vesting will cease upon the termination of your Continuous Service.

2. NUMBER OF SHARES AND EXERCISE PRICE. The number of shares of Common Stock subject to your option and your exercise price per share referenced in your Grant Certificate may be adjusted from time to time for Capitalization Adjustments, as provided in the Plan.

3. EXERCISE PRIOR TO VESTING ("EARLY EXERCISE"). Subject to the provisions of your option, you may elect at any time that is both (i) during the period of your Continuous Service and (ii) during the term of your option, to exercise all or part of your option, including the nonvested portion of your option; provided, however, that:

(a) a partial exercise of your option shall be deemed to cover first vested shares of Common Stock and then the earliest vesting installment of unvested shares of Common Stock;

(b) any shares of Common Stock so purchased from installments that have not vested as of the date of exercise shall be subject to the purchase option in favor of the Company as described in the Company's form of Early Exercise Stock Purchase Agreement;

(c) you shall enter into the Company's form of Early Exercise Stock Purchase Agreement with a vesting schedule that will result in the same vesting as if no early exercise had occurred; and

(d) if your option is an incentive stock option, then, as provided in the Plan, to the extent that the aggregate Fair Market Value (determined at the time of grant) of the shares of Common Stock with respect to which your option plus all other incentive stock options you hold

are exercisable for the first time by you during any calendar year (under all plans of the Company and its Affiliates) exceeds one hundred thousand dollars ($100,000), your option(s) or portions thereof that exceed such limit (according to the order in which they were granted) shall be treated as nonstatutory stock options.

4. METHOD OF PAYMENT. Payment of the exercise price is due in full upon exercise of all or any part of your option. You may elect to make payment of the exercise price in cash or by check or by one or more of the following:

(a) In the Company's sole discretion at the time your option is exercised and provided that at the time of exercise the Common Stock is publicly traded and quoted regularly in *The Wall Street Journal*, pursuant to a program developed under Regulation T as promulgated by the Federal Reserve Board that, prior to the issuance of Common Stock, results in either the receipt of cash (or check) by the Company or the receipt of irrevocable instructions to pay the aggregate exercise price to the Company from the sales proceeds.

(b) Provided that at the time of exercise the Common Stock is publicly traded and quoted regularly in *The Wall Street Journal*, by delivery of already-owned shares of Common Stock either that you have held for the period required to avoid a charge to the Company's reported earnings (generally six months) or that you did not acquire, directly or indirectly from the Company, that are owned free and clear of any liens, claims, encumbrances or security interests, and that are valued at Fair Market Value on the date of exercise. "Delivery" for these purposes, in the sole discretion of the Company at the time you exercise your option, shall include delivery to the Company of your attestation of ownership of such shares of Common Stock in a form approved by the Company. Notwithstanding the foregoing, you may not exercise your option by tender to the Company of Common Stock to the extent such tender would violate the provisions of any law, regulation or agreement restricting the redemption of the Company's stock.

5. WHOLE SHARES. You may exercise your option only for whole shares of Common Stock.

6. SECURITIES LAW COMPLIANCE. Notwithstanding anything to the contrary contained herein, you may not exercise your option unless the shares of Common Stock issuable upon such exercise are then registered under the Securities Act or, if such shares of Common Stock are not then so registered, the Company has determined that such exercise and issuance would be exempt from the registration requirements of the Securities Act. The exercise of your option must also comply with other applicable laws and regulations governing your option, and you may not exercise your option if the Company determines that such exercise would not be in material compliance with such laws and regulations.

7. TERM. The term of your option commences on the Date of Grant and expires upon the ***earliest*** of the following:

(a) Immediately if termination of your Continuous Service is for Cause;

(b) three (3) months after the termination of your Continuous Service for any reason other than your Disability or death, provided that if during any part of such three- (3-) month period your option is not exercisable solely because of the condition set forth in the preceding paragraph relating to "Securities Law Compliance," your option shall not expire until the earlier of the Expiration Date or until it shall have been exercisable for an aggregate period of three (3) months after the termination of your Continuous Service;

(c) twelve (12) months after the termination of your Continuous Service due to your Disability;

(d) eighteen (18) months after your death if you die either during your Continuous Service or within three (3) months after your Continuous Service terminates;

(e) the Expiration Date indicated in your Grant Certificate; or

(f) the day before the tenth (10th) anniversary of the Date of Grant.

If your option is an incentive stock option, note that, to obtain the federal income tax advantages associated with an "incentive stock option," the Code requires that at all times beginning on the date of grant of your option and ending on the day three (3) months before the date of your option's exercise, you must be an employee of the Company or an Affiliate, except in the event of your death or Disability. The Company has provided for extended exercisability of your option under certain circumstances for your benefit but cannot guarantee that your option will necessarily be treated as an "incentive stock option" if you continue to provide services to the Company or an Affiliate as a Consultant or Director after your employment terminates or if you otherwise exercise your option more than three (3) months after the date your employment terminates.

8. EXERCISE.

(a) You may exercise the your option during its term by delivering a Cash Letter of Authorization or other appropriate form (in a form designated by the Company) together with the exercise price to the Secretary of the Company, or to such other person as the Company may designate, during regular business hours, together with such additional documents as the Company may then require.

(b) By exercising your option you agree that, as a condition to any exercise of your option, the Company may require you to enter into an arrangement providing for the payment by you to the Company of any tax withholding obligation of the Company arising by reason of (1) the exercise of your option, (2) the lapse of any substantial risk of forfeiture to which the shares of Common Stock are subject at the time of exercise, or (3) the disposition of shares of Common Stock acquired upon such exercise.

(c) If your option is an incentive stock option, by exercising your option you agree that you will notify the Company in writing within fifteen (15) days after the date of any disposition of any of the shares of the Common Stock issued upon exercise of your option that

occurs within two (2) years after the date of your option grant or within one (1) year after such shares of Common Stock are transferred upon exercise of your option.

(d) By exercising your option you agree that the Company (or a representative of the underwriter(s)) may, in connection with the first underwritten registration of the offering of any securities of the Company under the Securities Act, require that you not sell, dispose of, transfer, make any short sale of, grant any option for the purchase of, or enter into any hedging or similar transaction with the same economic effect as a sale, any shares of Common Stock or other securities of the Company held by you, for a period of time specified by the underwriter(s) (not to exceed one hundred eighty (180) days) following the effective date of the registration statement of the Company filed under the Securities Act. You further agree to execute and deliver such other agreements as may be reasonably requested by the Company and/or the underwriter(s) that are consistent with the foregoing or that are necessary to give further effect thereto. In order to enforce the foregoing covenant, the Company may impose stop-transfer instructions with respect to your shares of Common Stock until the end of such period.

9. TRANSFERABILITY. Your option is not transferable, except by will or by the laws of descent and distribution, and is exercisable during your life only by you. Notwithstanding the foregoing, by delivering written notice to the Company, in a form satisfactory to the Company, you may designate a third party who, in the event of your death, shall thereafter be entitled to exercise your option.

10. OPTION NOT A SERVICE CONTRACT. Your option is not an employment or service contract, and nothing in your option shall be deemed to create in any way whatsoever any obligation on your part to continue in the employ of the Company or an Affiliate, or of the Company or an Affiliate to continue your employment. In addition, nothing in your option shall obligate the Company or an Affiliate, their respective shareholders, Boards of Directors, Officers or Employees to continue any relationship that you might have as a Director or Consultant for the Company or an Affiliate.

11. WITHHOLDING OBLIGATIONS.

(a) At the time you exercise your option, in whole or in part, or at any time thereafter as requested by the Company, you hereby authorize withholding from payroll and any other amounts payable to you, and otherwise agree to make adequate provision for (including by means of a "cashless exercise" pursuant to a program developed under Regulation T as promulgated by the Federal Reserve Board to the extent permitted by the Company), any sums required to satisfy the federal, state, local and foreign tax withholding obligations of the Company or an Affiliate, if any, which arise in connection with your option.

(b) Upon your request and subject to approval by the Company, in its sole discretion, and compliance with any applicable conditions or restrictions of law, the Company may withhold from fully vested shares of Common Stock otherwise issuable to you upon the exercise of your option a number of whole shares of Common Stock having a Fair Market Value, determined by the Company as of the date of exercise, not in excess of the minimum amount of tax required to be withheld by law. If the date of determination of any tax withholding

obligation is deferred to a date later than the date of exercise of your option, share withholding pursuant to the preceding sentence shall not be permitted unless you make a proper and timely election under Section 83(b) of the Code, covering the aggregate number of shares of Common Stock acquired upon such exercise with respect to which such determination is otherwise deferred, to accelerate the determination of such tax withholding obligation to the date of exercise of your option. Notwithstanding the filing of such election, shares of Common Stock shall be withheld solely from fully vested shares of Common Stock determined as of the date of exercise of your option that are otherwise issuable to you upon such exercise. Any adverse consequences to you arising in connection with such share withholding procedure shall be your sole responsibility.

(c) You may not exercise your option unless the tax withholding obligations of the Company and/or any Affiliate are satisfied. Accordingly, you may not be able to exercise your option when desired even though your option is vested, and the Company shall have no obligation to issue a certificate for such shares of Common Stock or release such shares of Common Stock from any escrow provided for herein.

12. NOTICES. Any notices provided for in your option or the Plan shall be given in writing and shall be deemed effectively given upon receipt or, in the case of notices delivered by mail by the Company to you, five (5) days after deposit in the United States mail, postage prepaid, addressed to you at the last address you provided to the Company.

13. GOVERNING PLAN DOCUMENT. Your option is subject to all the provisions of the Plan, the provisions of which are hereby made a part of your option, and is further subject to all interpretations, amendments, rules and regulations which may from time to time be promulgated and adopted pursuant to the Plan. In the event of any conflict between the provisions of your option and those of the Plan, the provisions of the Plan shall control.

EXHIBIT 31.1

CERTIFICATION

I, George A. Scangos, Ph.D., Chief Executive Officer of Exelixis, Inc., certify that:

1. I have reviewed this quarterly report on Form 10-Q of Exelixis, Inc.;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 8, 2004

/s/ George A. Scangos
George A. Scangos
President and Chief Executive Officer

EXHIBIT 31.2

CERTIFICATION

I, Frank Karbe, Chief Financial Officer of Exelixis, Inc., certify that:

1. I have reviewed this quarterly report on Form 10-Q of Exelixis, Inc.;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 8, 2004

/s/ Frank Karbe
Frank Karbe
Senior Vice President, Chief Financial Officer

EXHIBIT 32.1

CERTIFICATION

Pursuant to the requirement set forth in Rule 13a-14(b) of the Securities Exchange Act of 1934, as amended, (the "Exchange Act") and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. §1350), George A Scangos, Chief Executive Officer of Exelixis, Inc. (the "Company"), and Frank Karbe, Chief Financial Officer of the Company, each hereby certifies, to his knowledge, that:

1. The Company's Quarterly Report on Form 10-Q for the period ended September 30, 2004 (the "Periodic Report"), to which this Certification is attached as Exhibit 32.1, fully complies with the requirements of Section 13(a) or Section 15(d) of the Exchange Act; and

2. The information contained in the Periodic Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

In Witness Whereof, the undersigned have set their hands hereto as of the 8th day of November 2004.

/s/ George A. Scangos	/s/ Frank Karbe
George A. Scangos, Ph.D.	Frank Karbe
Chief Executive Officer	Chief Financial Officer
(Principal Executive Officer)	(Principal Financial Officer)