

**MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITIONS AND RESULTS OF OPERATIONS**

YEAR ENDED DECEMBER 31, 2007

INFORMATION REGARDING FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements. These statements involve known and unknown risks, uncertainties and other factors which may cause our actual results, performance or achievements to be materially different from any future results, performances or achievements expressed or implied by the forward-looking statements. Forward-looking statements include, but are not limited to, statements about:

- the marketing and sales of our products and services;
- the declaration and distribution of any future dividends;
- our ability to sustain licensing and other contract-based revenues;
- the impact of our contracts with the NIH and The Wellcome Trust on future business;
- the value of, and expenses associated with, our intellectual property;
- the impact of our restructuring efforts;
- the requirements of pharmaceutical and biotechnology companies;
- the benefits of knockout mice programs and, in particular, our technologies and products, to the pharmaceutical industry;
- the increasing competition we face in the field of knockout mice from both commercial and government organizations;
- failures in the drug discovery, development and approval processes by our partners and collaborators;
- our ability to successfully execute our business plan and to meet contractual obligations, in view of the Company's limited staff; and
- liquidity and capital resources.

In some cases, you can identify forward-looking statements by terms such as "may," "will," "should," "could," "would," "expects," "plans," "anticipates," "believes," "estimates," "projects," "predicts," "potential" and similar expressions intended to identify forward-looking statements. These statements reflect our current views with respect to future events and are based on assumptions and subject to risks and uncertainties. Given these uncertainties, you should not place undue reliance on these forward-looking statements. These forward-looking statements represent our estimates and assumptions only as of the date of this report.

You should read this report completely and with the understanding that our actual future results may be materially different from what we expect. We qualify all of our forward-looking statements by these cautionary statements.

YOU SHOULD READ THE FOLLOWING DISCUSSION AND ANALYSIS IN CONJUNCTION WITH OUR FINANCIAL STATEMENTS AND THE NOTES ACCOMPANYING THE FINANCIAL STATEMENTS.

1. Overview

Deltagen (or the “Company” or “We”) is a provider of research tools to the biopharmaceutical industry and to the academic research community. Deltagen has generated an inventory of “knockout mice” in which a single gene has been deleted (“knocked out”). The knockout mice have been analyzed to determine the phenotypic changes associated with that gene deletion. This phenotypic data has been organized in an integrated database known as DeltaBase. DeltaBase contains phenotypic data on 750 different knockout mouse lines. In addition to those 750 knockout mouse lines, Deltagen has approximately 150 additional knockout mouse lines that have not been characterized phenotypically. Deltagen also has approximately 450 knockout lines at the embryonic stem (ES) cell stage.

Our customers and partners/collaborators have included some of the world’s largest pharmaceutical companies, including GlaxoSmithKline plc, Merck & Co., Inc., Pfizer Inc., Eli Lilly and Company and Schering-Plough Research Institute.

We have historically generated revenue from our DeltaBase and DeltaOne products and programs.

DeltaBase is our proprietary database that provides information, based on knockout mouse studies, on gene function and validated gene targets for drug discovery. Each knockout mouse underwent a standardized, detailed and extensive analysis in order to determine the function and role that a particular gene plays in the mouse and that gene’s suitability as a drug target.

DeltaOne offers access to our portfolio of knockout mice and/or accompanying phenotypic data, as well as any corresponding intellectual property, on a gene-by-gene basis.

We derive substantially all of our revenues from a narrow and limited range of sources. Substantially all of our revenues are currently derived from the licensing of knockout mouse lines and related phenotypic data to the biopharmaceutical industry and academic institutions under our DeltaOne program. Because of continuing consolidation in the biopharmaceutical industry and the finite number of knockout lines in the Company’s inventory, significant uncertainty exists with respect to the Company’s future revenues.

Our operating results have fluctuated in the past and are likely to do so in the future, and we do not believe that period-to-period comparisons of our operating results are a good indication of our future performance.

2. Critical Accounting Policies and Estimates

The consolidated financial statements of Deltagen for the three-month period and the year ended December 31, 2007 are unaudited, but have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”). These consolidated financial statements have been prepared so that they present fairly, in the opinion of management, the Company’s financial position and its results of operations and its cash flows for the period presented.

Under our revenue recognition policy, revenues are recognized when a definitive agreement with a determinable price exists, product delivery and/or invoicing (in each case where there is reasonable assurance of meeting customer-specified criteria) have occurred, and collectibility is reasonably assured. A change in our revenue recognition policy or changes in the terms of contracts under which we recognize revenues could have an impact on the amount and timing of our recognition of revenues.

The preparation of consolidated financial statements in conformity with GAAP requires the Company to make estimates and assumptions that affect the amounts that are reported in the consolidated financial statements and accompanying disclosures. Although these estimates are based on the Company’s best knowledge of current events and actions that the Company may undertake in the future, actual results may differ materially from the estimates.

3. Results of Operations

The Company's consolidated revenues for the quarter and the year ended December 31, 2007 totaled \$2.028 million and \$3.413 million, respectively. The revenues in the fourth quarter were attributable primarily to license fees associated with the provision of knockout mice and related phenotypic data to The Wellcome Trust (the "Trust") pursuant to orders placed by the Trust on May 29, 2007 and September 13, 2007 together with orders by other customers under the Company's DeltaOne™ program.

The Company had interest income of \$0.029 million and \$0.159 million for the quarter and the year ended December 31, 2007, respectively.

Total consolidated expenses for the quarter and the year ended December 31, 2007 were \$1.127 million and \$3.666 million, respectively. The operating expenses in the fourth quarter were attributable to third-party royalty and commission expenses (\$0.611 million), as well as labor costs and other general and administrative expenses (\$0.516 million). The fourth quarter labor costs include the second of three annual installment payments made in December 2007 to the Company's officers (\$0.220 million in the aggregate) in accordance with the Company's dividend-related retention bonus plan, as discussed previously in Management's Discussion and Analysis of Financial Conditions and Results of Operation for Full-Year 2006.

Net income before provision for income taxes for the quarter ended December 31, 2007 was \$0.931 million. Net loss before provision for income taxes for the year ended December 31, 2007 was \$0.093 million.

As of December 31, 2007, the Company had \$3.065 million in consolidated cash and cash equivalents and \$2.625 million in accounts receivable, following distribution of a dividend of \$0.05 per share in May 2007 to the Company's shareholders (totaling \$1.936 million) and dividends to former Xenopharm, Inc. ("Xenopharm") shareholders in August 2007 (totaling \$0.026 million) and in November 2007 (totaling \$0.245 million). These dividend payments reduced in the aggregate cash holdings of the Company by approximately \$2.028 million in 2007. The Xenopharm-related dividends are discussed in greater detail in the "Major Events" section below. The accounts receivable amount includes approximately \$1.237 million relating to tax credits expected to be received from the French government by the Company's wholly-owned subsidiary, Deltagen Europe, S.A.

4. Major Events during 2007

The Wellcome Trust:

The Company received on May 29, 2007 an order from the Trust, a United Kingdom-based, independent charitable organization that funds research to improve human and animal health, for seventeen of the Company's knockout mouse lines and related phenotypic data. This order was the first to be received by the Company from the Trust and was worth \$0.850 million. The Company received on September 13, 2007 a second order worth \$1.000 million from the Trust for twenty of the Company's knockout mouse lines and related phenotypic data. The knockout mouse lines will be made available to the academic research community. The Company will retain exclusive rights to make these ordered knockout lines available to commercial organizations.

The Company received \$0.463 million and \$0.675 million pursuant to the Trust orders during the fourth quarter and calendar year 2007, respectively. The Company expects to receive the balance of the license fees relating to the Trust orders (\$1.175 million) in installment payments in the first and second quarters of 2008, contingent upon satisfaction of specified acceptance milestones.

Dividend Distributions:

The Company distributed on May 31, 2007 a dividend of \$0.05 per share to the Company's shareholders of record as of the close of business on May 21, 2007. The Company also distributed dividends in August and November 2007 to certain former Xenopharm shareholders in connection with the issuance of shares of the Company's common stock relating to Xenopharm earnout shares, as discussed in greater detail immediately below.

Xenopharm Earnout Shares and Dividends:

In an Agreement and Plan of Merger and Reorganization dated February 15, 2002 by among the Company, XP Acquisition Corporation and Xenopharm (the "Merger Agreement"), entered into in connection with the Company's acquisition of Xenopharm, the Company agreed to issue shares of the Company's common stock to the former Xenopharm shareholders (the "XP Holders") upon the occurrence of certain events. On March 14, 2004, pursuant to and in satisfaction of a certain condition of the Merger Agreement, the XP Holders had rights to receive an aggregate of 131,572 shares of the Company's common stock (the "XP Earnout Shares"). These XP Earnout Shares were not issued to the XP Holders at such time, notwithstanding the requirement to do so. In addition to receipt of the XP Earnout Shares, the XP Holders were entitled to receive the cash dividend of \$0.20 per share distributed by the Company on December 28, 2006 ("2006 Dividend") with respect to the XP Earnout Shares. The Company's Board approved the issuance and delivery of the XP Earnout Shares to the XP Holders in accordance with the provisions of the Merger Agreement, and upon such issuance, payment of a cash dividend of \$0.20 per share to the XP Holders with respect to the XP Earnout Shares. The XP Earnout Shares and the related dividends, which totaled approximately \$0.026 million, were distributed in August 2007.

In August 2007, the Company received a letter from certain XP Holders asserting the XP Holders' right to receive certain other earnout shares (the "Additional XP Earnout Shares") under the Merger Agreement. In October 2007, the Company entered into a settlement agreement (the "Settlement Agreement") with the stockholder representative of the XP Holders. Under the Settlement Agreement, Deltagen agreed to issue to the XP Holders, in accordance with the Merger Agreement, the Additional XP Earnout Shares, totaling up to 1,054,021 shares of the Company's common stock, and to pay to the XP Holders all prior and future dividends of the Company with respect to the Additional XP Earnout Shares, subject to the Company having received a release of liability ("Release") on or before January 23, 2008 (the "Deadline") with respect to the Merger Agreement from at least 75% of the XP Holders, on a ratable basis (the "Threshold"). The Threshold was met on October 24, 2007, when the Company received a Release from approximately 93% of the XP Holders. In November 2007, Deltagen issued the Additional XP Earnout Shares and distributed a dividend payment of \$0.25 per share with respect to the Additional XP Earnout Shares ("XP Dividends") to those XP Holders that had executed and delivered a Release. The XP Dividends related to the Company's 2006 Dividend (\$0.20 per share) and the \$0.05 per share dividend distributed in May 2007. The Company issued in November 2007 981,123 shares and distributed \$245,280.75 in XP Dividends to the XP Holders that had returned a Release by such time. One of the XP Holders returned a Release on the Deadline and is eligible to receive certain Additional XP Earnout Shares, as discussed in greater detail in the "Subsequent Events" section below.

Company's Mid-Year Restructuring:

In June 2007, the Company implemented certain restructuring changes to reduce the fixed operating expenses of the Company. The Company terminated the employment of Dr. Shera Kash, the Company's Vice President of Operations, effective June 30, 2007. The Company implemented effective July 1, 2007 changes to the coverages under the Company's insurance policies, suspension of review and audit activities by the Company's auditors and termination of the Company's offsite storage contracts. In addition, the Company implemented a new management and director compensation plan (the "Comp Plan") for the twelve-month period from July 1, 2007 through June 30, 2008 (the "Period"). Under the Comp Plan, the base salaries of the Company's officers were reduced by 50%. The officers would be eligible to receive original base salary restoration amounts and bonuses in the event that the Company realizes a profit during the Period. In the

aggregate, the Company's officers are eligible to share 32% of the Company's first \$0.969 million in profits (original base pay restoration), 20% of the next \$0.980 million in profits and 10% of any profits in excess of the foregoing amounts. Portions of these amounts may be paid to the officers in interim payments during the Period. The Comp Plan does not affect the amounts of any severance-related payments due under the officers' employment agreements. The Board also may adjust the Comp Plan in the event that there are unanticipated events that materially impact the forecasted expenses of the Company. The Comp Plan also reduced annual director's fees from \$40,000 each to a base director fee of \$15,000 each. The directors are eligible to each receive 0.5% of the Company's profits (if any), up to a maximum bonus of \$10,000 each. In connection with the Company's restructuring, two of the Company's directors, Lawrence Hill and Philippe O. Chambon, resigned from the Company's Board of Directors effective June 30, 2007.

Xenopharm Patents Issued:

Xenopharm is an exclusive licensee under certain technologies relating to the metabolism of foreign compounds, known as xenobiotics, invented by Professor David Moore et al. and assigned to the Baylor College of Medicine. Two United States patents, U.S. Patent No. 7,186,879 and U.S. Patent No. 7,193,125, directed to modulation of xenobiotic metabolism, issued in March 2007. The patents' claims cover transgenic mice having reduced constitutive androstane receptor (CAR) activity, including CAR knockout mice, as well as "humanized" mice expressing a human CAR receptor. These mice are useful in screening methods to identify compounds that modulate, activate or inhibit CAR activity, compounds likely to have CAR-mediated toxicity, and analogs of these compounds with less potential toxicity. In particular, the humanized mice are useful as predictors of drug toxicity and metabolism, including drug-drug interactions, in the human body.

Marketing in Asia:

In March 2007, the Company entered into a marketing agreement with TransGenic Inc. of Japan ("TransGenic") under which TransGenic became the Company's exclusive sales and marketing representative in Japan, China and South Korea for the Company's knockout mouse lines and related phenotypic data. The Company had previously been represented in Asia by Mitsubishi Corporation.

5. Subsequent Events

Additional Xenopharm Earnout Shares and Dividends:

The Company received on the Deadline a Release from one of the XP Holders that is eligible to receive Additional XP Earnout Shares in the amount of 21,522 shares of the Company's common stock and payment of \$5,380.50 in dividends. The Company expects to issue these shares and distribute these dividends in February 2008.

RISK FACTORS AFFECTING FUTURE OPERATING RESULTS

There are numerous risks and uncertainties related to both our business and our industry that could cause actual results or events to differ materially from those indicated by forward-looking statements.

For a list of additional risk factors that may affect our future operating results, refer to the "Risk Factors" section of "Management's Discussion and Analysis of Financial Conditions and Results of Operations" for the year ended December 31, 2005, as posted on the Company's website (www.deltagen.com). The risk factors listed there are not the only ones we face and additional risks and uncertainties not presently known to us or that we currently deem immaterial also may impair or otherwise affect our business operations.