



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

For the First Quarter Ended January 31, 2010

Patheon Inc.

Management's Discussion and Analysis of Financial Condition and Results of Operations

The following management discussion and analysis of financial condition and results of operations ("MD&A") of Patheon Inc. ("Patheon" or the "Company") for the three month periods ended January 31, 2010 and 2009 should be read in conjunction with the Company's unaudited interim consolidated financial statements and related notes and the audited consolidated financial statements and MD&A for the year ended October 31, 2009. All amounts are in U.S. dollars unless otherwise indicated. This MD&A is dated as of March 15, 2010.

The purpose of this 2010 first quarter report is to provide an update to the information contained in the Company's MD&A section of the Company's 2009 Annual Report, which contains a more comprehensive discussion of the Company's strategy, capabilities to deliver results, risks and key performance indicators. Management assumes that the reader of this document has access to the MD&A section of the Company's 2009 Annual Report. This document and other information can be downloaded in portable document format ("PDF") from the Company's web site at www.patheon.com or from the SEDAR web site for Canadian regulatory filings at www.sedar.com. To request a printed copy, the reader may also contact Patheon's transfer agent, Computershare Investor Services Inc., at 1-800-564-6253 or via email at service@computershare.com, or Patheon at www.patheon.com.

Use of Non-GAAP Financial Measures

References in this MD&A to "Adjusted EBITDA" are to income (loss) before discontinued operations before repositioning expenses, interest expense, foreign exchange losses reclassified from other comprehensive income, refinancing expenses, gains and losses on sale of fixed assets, gain on extinguishment of debt, income taxes, asset impairment charge, depreciation and amortization. "Adjusted EBITDA margin" is Adjusted EBITDA as a percentage of revenues.

Since Adjusted EBITDA is a non-GAAP measure that does not have a standardized meaning, it may not be comparable to similar measures presented by other issuers. Readers are cautioned that these non-GAAP measures should not be construed as alternatives to net income (loss) determined in accordance with GAAP as indicators of performance. Adjusted EBITDA is used by management as an internal measure of profitability. The Company's major credit facilities also have certain covenant calculations that are based on Adjusted EBITDA. The Company has included these measures because it believes that this information is used by certain investors to assess financial performance of the Company, before non-cash charges and large non-recurring costs. Please see Note 5 of the unaudited interim consolidated financial statements for an Adjusted EBITDA bridge reconciling these amounts to the closest Canadian GAAP measure.

Overview of Patheon

Patheon is focused exclusively on providing commercial manufacturing and pharmaceutical development services ("PDS") to pharmaceutical, biotechnology and specialty pharmaceutical companies located primarily in North America, Europe and Asia. Patheon serves its international clientele from its operating facilities in North America (including Puerto Rico) and Europe.

Patheon commercially manufactures prescription and over-the-counter products in solid, semi-solid and liquid dosage forms. Conventional dosage forms include compressed tablets, hard-shell capsules, powders, ointments, creams, gels, syrups, suspensions, solutions and suppositories. Sterile dosage forms include liquids and powders presented in ampoules, vials, bottles or pre-filled syringes. Sterile lyophilized products are also manufactured in both vials and ampoules.

Patheon provides manufacturing services for a broad range of products in many dosage forms and packaging formats in accordance with client specifications. Depending on the particular client, Patheon

may be responsible for most or all aspects of the manufacturing and packaging process, from sourcing excipient raw materials and packaging components to delivering the finished product in consumer-ready form to the client. Typically, Patheon's clients supply the active pharmaceutical ingredients used in the production process.

The pharmaceutical development services provided by Patheon include most of the pharmaceutical development services typically required by companies conducting clinical trials and preparing for full-scale commercial production of a new drug. In providing its pharmaceutical development services, Patheon is able to: (i) develop an appropriate dosage form; (ii) develop analytical methods; (iii) manufacture the proposed new drug product to client specifications during the regulatory drug approval process; (iv) manufacture pilot batches of proposed new drug products for the regulatory drug approval process; and (v) provide scale-up and technology transfer services designed to validate that a drug can be manufactured commercially.

At January 31, 2010, there were a total of 370 ongoing projects being carried out by Patheon's PDS business. This total includes stability and process optimization work on some products that have already been launched. The Company is working on eight new drug candidates at the new drug application stage on behalf of customers. During the first quarter of 2010, one new product developed by Patheon on behalf of its clients, received regulatory approval.

Vision and Strategy

Patheon's vision is to be the best provider of manufacturing and development services to the pharmaceutical industry. In implementing its strategy, the Company expects to grow with the market, increase its market share and improve efficiency. Growth within the market will be achieved by retaining existing customers with high quality products and service. The Company will also increase market share by diversifying its customer base, expanding capacity and broadening its capabilities in higher value added service offerings. Efficiency has been and continues to be improved by consolidating existing facilities, cost containment and by implementing a system of continuous improvement through a Lean 6 Sigma program called "Patheon Advantage".

Recent Developments

On January 21, 2010, Patheon announced it had begun construction of a new pharmaceutical development center at its existing manufacturing facility in Bourgoin, France. This new addition will enable the Bourgoin site to offer a full range of solid dose services as part of its Pharmaceutical Development Services (PDS) business. The state-of-the-art facility has been designed for the supply of late-phase clinical trial tablet and capsule products, and will be capable of handling batch sizes up to 120 kg. It will consist of a new pilot plant and equipment designed to contain high potency products. Process trains will be scalable to commercial lines, offering clients the ability to produce Phase 3 and commercial product in the same location.

On December 15, 2009, Patheon announced that it had successfully released the first commercial shipments of SUMAVEL DosePro (sumatriptan injection) to Zogenix in anticipation of the planned U.S. commercial product launch scheduled in January 2010. The successful production of this new, needle-free drug product/delivery system is the culmination of joint manufacturing process and equipment development between Patheon and Zogenix. Aseptic drug filling, final product assembly, and packaging of SUMAVEL DosePro needle-free delivery system are performed exclusively by Patheon in its Swindon, U.K. facility with components and assemblies from around the world designed specifically for use in the DosePro technology.

In November, 2009, Patheon completed the expansion of its manufacturing facility in Ferentino, by adding a PDS suite. The facility is dedicated to the manufacture of sterile products including aseptically filled, terminally sterilized liquids and lyophilization. It also includes development and quality control laboratories. The expansion doubles PDS manufacturing capabilities for clinical batches, and analytical laboratory capabilities were doubled to support the subsequent increased volume of projects.

Puerto Rico Operations

The Company announced on December 10, 2009 its plan to consolidate its Puerto Rico operations into its manufacturing site located in Manatí and ultimately close or sell its plant in Caguas. The Company estimates this consolidation will result in total repositioning expenses of \$7.0 million, of which \$2.4 million was booked in the three months ended January 31, 2010. Patheon also booked an impairment charge of \$1.3 million in connection with the consolidation plan. The consolidation will be completed by the end of fiscal 2011, and will also result in accelerated depreciation of Caguas assets of approximately \$7.0 million during fiscal years 2010 and 2011. Because the business in the Caguas facility is being transferred within the existing site network, its results of operations are included in continuing operations.

The Company closed its Carolina facility in Puerto Rico effective January 31, 2009. The Company is currently marketing the remaining assets. Certain transitional activities continue at the facility to ensure proper and compliant closure.

The results of the Carolina operations have been reported in discontinued operations in fiscal years 2010 and 2009.

JLL Offer to Acquire Patheon's Restricted Voting Shares

On November 30, 2009, The Special Committee of the Company's Board of Directors and JLL Patheon Holding, LLC ("JLL") announced that they entered into a settlement agreement in respect of the pending legal actions between the parties, and was confirmed by the courts on December 4, 2009. The settlement provided among other things that: until March 2011, the Board will consist of nine directors who will initially be four nominees of JLL, the Chief Executive Officer of the Company (Wesley P. Wheeler), Joaquín B. Viso and three independent directors. The three independent directors will include two members of the Special Committee, Derek J. Watchorn and Roy T. Graydon, and a new independent director, Brian G. Shaw; JLL agreed not to acquire any additional restricted voting shares ("Shares") of the Company for a one-year period. Thereafter, and until April 27, 2012, JLL will not acquire any additional Shares unless, among other things, the acquisition complies with the standstill provisions of the Investor Agreement between Patheon and JLL and, if the acquisition is to be effected by means of a takeover bid, the bid is subject to an irrevocable condition requiring the valid tender to the bid of at least a majority of the minority held Shares. Also, until April 27, 2012, certain transactions by the Company, including certain rights offerings, issuer bids and related party transactions, would require independent director approval; and finally the Company paid JLL U.S. \$1.5 million in connection with the settlement.

Upon expiry of the JLL Offer on August 26, 2009, JLL had acquired an aggregate of 33,853,508 restricted voting shares that were validly deposited under the Offer. The restricted voting shares taken up and paid for by JLL since the JLL Offer was launched represent approximately 38% of the outstanding restricted voting shares of the Company not already owned by JLL or its affiliates and associates. As of January 31, 2010, with the conversion and the restricted voting shares validly deposited in response to the JLL Offer, JLL now owns an aggregate of 73,523,246 Patheon restricted voting shares, representing approximately 57% of Patheon's total restricted voting shares outstanding.

On July 29, 2009, JLL converted their 150,000 Series C convertible preferred shares of Patheon into a total of 38,018,538 restricted voting shares of Patheon, in accordance with the convertible preferred share terms. As a result of the JLL conversion, the Company no longer pays dividends on the Series C convertible preferred shares.

On March 11, 2009, JLL announced by way of press release that it was commencing its unsolicited offer to acquire any or all of the outstanding restricted voting shares of Patheon that it did not already own at a price of US\$2.00 per share in cash ("JLL Offer"). At this date, JLL held convertible preferred shares of the Company, which when converted and taken together with its holding of restricted voting shares, represented approximately 30% of the restricted voting shares of the Company.

Results of Operations

The results of Carolina operations have been reported as discontinued operations in 2010 and 2009.

Results of Consolidated Operations

	Three months ended January 31,		
	2010	2009	%
<i>(in millions of U.S. dollars, except loss per share)</i>	\$	\$	Change
Revenues	154.8	147.2	5.2%
Cost of goods sold	130.2	116.5	11.8%
Gross profit	24.6	30.7	-19.9%
Selling, general and administrative expenses	28.8	26.3	9.5%
Repositioning expenses	2.4	0.5	380.0%
Operating (loss) income	(6.6)	3.9	-269.2%
Interest expense, net	3.2	4.5	-28.9%
Impairment charge	1.3	-	100.0%
Foreign exchange (gain) loss	(0.4)	1.5	-126.7%
Loss from continuing operations before income taxes	(10.7)	(2.1)	-409.5%
Provision for (benefit from) income taxes	-	(0.6)	-100.0%
Loss before discontinued operations	(10.7)	(1.5)	-613.3%
Loss from discontinued operations	(0.4)	(4.5)	91.1%
Net loss for the period	(11.1)	(6.0)	-85.0%
Dividends on convertible preferred shares	-	3.6	-100.0%
Net loss attributable to restricted voting shareholders	(11.1)	(9.6)	-15.6%

Three Months Ended January 31, 2010 Compared with Three Months Ended January 31, 2009

Operating Income Summary

Revenue for the period was \$154.8 million, up 5.2% from the prior period. Excluding currency fluctuations, current year revenues would have decreased by approximately 1.0%. Revenues from commercial manufacturing increased 8.8% to \$128.1 million from \$117.7 million in the prior period. PDS saw a reduction in revenue of 9.5% to \$26.7 million from \$29.5 million in the prior period.

Gross profit for the period decreased 19.9% to \$24.6 million. Gross profit margin decreased to 15.9% in the first quarter 2010 from 20.9% in the first quarter of 2009. This decrease was due to higher depreciation, production delays due to customer-supplied material shortages, unfavorable foreign exchange impact, and lower PDS volumes on a relatively fixed overhead cost basis. These factors were partially offset by a decrease in cost of goods sold due to the realization this quarter of prior period Canadian Research and Development Investment Tax Credits.

Selling, general and administrative costs were \$28.8 million, up \$2.5 million or 9.5% from prior year. The increase is primarily due to Special Committee costs of \$3.0 million for the three months ended January 31, 2010 compared to \$0.5 million in the same period last year. Selling, general and administrative costs were also impacted by unfavorable foreign exchange, offset by lower compensation and marketing expenses.

Repositioning expenses for the three months ended January 31, 2010 were \$2.4 million in connection with the Caguas closure and consolidation in Puerto Rico as previously reported in the fourth quarter of 2009. During the three months ended January 31, 2009, the Company incurred \$0.5 million in connection with the ongoing shut down and transition of business out of the York Mills facility.

Operating (loss) income for the period decreased to a loss of \$6.6 million or (4.3)% of revenues from income of \$3.9 million or 2.6% of revenues in the same period last year as a result of the factors discussed above.

Interest Expense

Interest expense for the three months ended January 31, 2010 was \$3.2 million, compared with \$4.5 million for the same period of 2009. The decrease in interest expense primarily reflects a \$1.1 million decrease in interest expense from Italy and UK as a result of lower three month Euribor and UK Libor rates, partially offset by weakening of U.S dollar against the Euro and Sterling.

Impairment charge

During the three months ended January 31, 2010, the Company booked an impairment charge of \$1.3 million in connection with the consolidation of its Puerto Rico operations into its manufacturing site located in Manatí, as previously reported in the fourth quarter of 2009. This was to write down the carrying value of the Caguas facility's long-lived assets to their anticipated fair value upon closure of the facility. Since the production in the Caguas facility is being transferred to another existing site, its results of operations are included in continuing operations.

Foreign Exchange (Gains) Losses

Foreign exchange gains for the three months ended January 31, 2010 were \$0.4 million, compared to losses of \$1.5 million for the same period of 2009. The reduction of foreign exchange loss into a gain is primarily due to the effect of the strengthening of the Canadian dollar against the U.S. dollar on the U.S. dollar denominated debt liabilities and favorable hedging contracts in the first quarter of 2010.

Loss from Continuing Operations Before Income Taxes

The Company reported a loss from continuing operations before income taxes of \$10.7 million for the three months ended January 31, 2010, compared to \$2.1 million for the same period of 2009.

Income Taxes

The income tax expense for the three months ended January 31, 2010 was nil, compared with a recovery of \$0.6 million for the same period of 2009. Tax expense in certain European jurisdictions, were offset by recoveries in certain North American jurisdictions in the current quarter. Prior period recovery was due to recognition of an income tax refund.

Loss before Discontinued Operations and Loss Per Share from Continuing Operations

The Company recorded a loss before discontinued operations for the three months ended January 31, 2010 of \$10.7 million, compared with a loss of \$1.5 million in the same period last year. The loss per share before discontinued operations for the quarter was 8.3¢ compared with a loss of 5.6¢ a year earlier, after taking into account the dividends on the convertible preferred shares.

Loss and Loss Per Share from Discontinued Operations

Discontinued operations in the three months ended January 31, 2010 and 2009 include the results of the Carolina, Puerto Rico operations. Financial details of the operating activities are disclosed in Note 3 of the interim unaudited consolidated financial statements. The loss from discontinued operations for the three months ended January 31, 2010 was \$0.4 million, or 0.3¢ per share compared with a loss of \$4.5 million or 5.0¢ per share in the same period of 2009. On-going costs of discontinued operations relate to maintaining the Carolina building for sale.

Net Loss, Loss Attributable to Restricted Voting Shareholders and Loss Per Share

The Company recorded a loss for the three months ended January 31, 2010 of \$11.1 million, or 8.6¢ per share compared with a loss of \$9.6 million, or 10.6¢ per share in the same period of 2009. Prior year results include dividends on the convertible preferred shares of \$3.6 million. Dividends were recorded until July 28, 2009, the date when these preferred shares were converted to restricted voting shares by JLL.

Because the Company reported a loss in the three months ended January 31, 2010 and 2009, there is no impact of dilution.

Revenue and Adjusted EBITDA by Business Segment

The Company is organized and managed in two business segments: commercial manufacturing and PDS. These segments are organized around the service activities provided to the Company's customers.

<i>(in millions of U.S. Dollars)</i>	Three months ended January 31,		
	2010	2009	%
	\$	\$	Change
Revenues			
Commercial Manufacturing			
North America	56.5	55.3	2.2%
Europe	71.6	62.4	14.7%
Total Commercial Manufacturing	128.1	117.7	8.8%
Pharmaceutical Development Services			
	26.7	29.5	-9.5%
Total Revenues	154.8	147.2	5.2%
Adjusted EBITDA			
Commercial Manufacturing			
North America	0.5	5.2	-90.4%
Europe	8.6	10.0	-14.0%
Total Commercial Manufacturing	9.1	15.2	-40.1%
Pharmaceutical Development Services			
	7.4	5.8	27.6%
Corporate Costs	(7.2)	(8.2)	-12.2%
Total adjusted EBITDA	9.3	12.8	-27.3%

Commercial Manufacturing

Revenues from commercial manufacturing operations for the three months ended January 31, 2010 increased by 8.8%, or \$10.4 million, to \$128.1 million from \$117.7 million in the same period of 2009. Had local currencies remained constant to the rates of the prior year, commercial manufacturing revenues would have been approximately 2.0% higher than 2009.

Revenues from the North American operations increased \$1.2 million, or 2.2%. Higher revenues in Cincinnati were offset by lower revenue from Canadian operations. Had the Canadian dollar remained constant to the rates of the prior year, North American revenues would have been flat to 2009.

Revenues from the European operations increased by \$9.2 million or 14.7%. The increase is primarily due to the weakening of the U.S. dollar against the Euro and Sterling and new product introductions. Had European currencies remained constant to the rates of the prior year, European revenues would have been approximately 3.5% higher than the same period of 2009.

Adjusted EBITDA from the commercial manufacturing operations for the three months ended January 31, 2010 decreased by 40.1%, or \$6.1 million to \$9.1 million from \$15.2 million in the same period of 2009. This represents an Adjusted EBITDA margin of 7.1% compared with 12.9% in the same period last year. Had local currencies remained constant to prior year rates and after eliminating the impact of all foreign

exchange gains and losses, commercial manufacturing Adjusted EBITDA would have been approximately \$0.9 million higher than the reported number in the current period.

North American operations reported a decrease of \$4.7 million, or 90.4% in Adjusted EBITDA. The decrease in Adjusted EBITDA was driven by vendor supply issues in Puerto Rico, lower revenues in Canada, and unfavorable product mix, partially offset by stronger EBITDA from stronger revenue results in Cincinnati.

European Adjusted EBITDA decreased by \$1.4 million, or 14.0% for the three months ended January 31, 2010. The decrease is primarily due to unfavorable mix and foreign exchange.

Pharmaceutical Development Services

PDS revenues for the three months ended January 31, 2010 decreased by 9.5%, or \$2.8 million, to \$26.7 million from \$29.5 million in the same period of 2009. This decline was primarily due to lower overall demand for development services due to general market conditions. Had the local currency rates remained constant from the prior year, PDS revenues would have been approximately 13.2% lower.

Adjusted EBITDA from the PDS operations for the three months ended January 31, 2010 increased by 27.6%, or \$1.6 million to \$7.4 million from \$5.8 million in the same period of 2009. The first quarter 2010 PDS Adjusted EBITDA includes \$2.8 million in prior period Canadian Research and Development Investment Tax Credits that were realized this quarter. Had local currencies remained constant to the rates of the prior year and after eliminating the impact of all foreign exchange gains and losses, PDS Adjusted EBITDA would have been approximately \$1.1 million lower than the reported amount.

Corporate Costs

Corporate costs for three months ended January 31, 2010 were \$7.2 million, compared with \$8.2 million for the same period of 2009. This decrease is primarily due to lower compensation, timing of marketing programs, and cost saving initiatives implemented this period. These expense reductions were partially offset by \$3.0 million associated with the Special Committee costs. Prior year was impacted by \$0.5 million of Special Committee costs.

Liquidity and Capital Resources

Summary of Cash Flows

The following table summarizes the Company's cash flows for the periods indicated:

	Three months ended January 31,	
	2010	2009
(in millions of U.S. dollars)	\$	\$
Loss before discontinued operations	(10.7)	(1.5)
Depreciation and amortization	13.1	9.9
Impairment charge	1.3	-
Other non-cash interest	0.1	0.1
Change in other long-term liabilities	(0.3)	(0.9)
Future income taxes	(3.5)	(3.4)
Amortization of deferred revenues	(1.7)	(0.1)
Stock-based compensation expense	0.2	0.5
Other	(0.4)	-
Working capital changes	(2.4)	3.0
Increase (decrease) in deferred revenues	11.2	(0.6)
Cash provided by operating activities of continuing operations	6.9	7.0
Cash used in operating activities of discontinued operations	(0.8)	(3.3)
Cash provided by operating activities	6.1	3.7
Cash used in investing activities of continuing operations	(10.9)	(8.2)
Cash provided by financing activities	4.5	11.2
Other	(1.7)	(2.9)
Net increase in cash and cash equivalents during the period	(2.0)	3.8

Cash Provided by (Used in) Operating Activities

Cash provided by operating activities from continuing operations was \$6.9 million for the three months ended January 31, 2010 compared to \$7.0 million in the same period of 2009. Higher deferred revenues, partially offset by working capital changes were the primary driver of the positive cash flow from operations in the current year. In 2009, lower operating loss and positive working capital contributed to the \$7.0 million in cash from operations.

Cash used in operating activities from discontinued operations was \$0.8 million for the three months ended January 31, 2010 compared to \$3.3 million in the comparable period in 2009. The decrease in cash outflow in 2010 is due to the Carolina facility closing down operations in Q1 2009 and Q1 2010 expenses representing primarily utility costs, insurance and supplies to maintain the building which is held for sale.

Cash Used in Investing Activities

Cash used in investing activities from continuing operations for the three months ended January 31, 2010 was \$10.9 million, compared to \$8.2 million in the same period a year ago. The increased cash outflow in the quarter was primarily driven by increasing production capacity in Cincinnati and the SAP implementation in Canada.

A summary of cash used in investing activities is as follows:

Cash Used in Investing Activities

	Three months ended January 31,	
	2010	2009
(in millions of U.S. dollars)	\$	\$
Total additions to capital assets	(10.2)	(8.5)
Net (increase) decrease in investments	(0.6)	0.3
Investment in intangibles	(0.1)	-
Cash used in investing activities of continuing operations	(10.9)	(8.2)
Cash used in investing activities	(10.9)	(8.2)

Cash Provided by Financing Activities

Cash provided by financing activities was \$4.5 million for the three months ended January 31, 2010, compared to cash provided of \$11.2 million for the same period last year. The cash inflows reflect net drawings on existing credit facilities primarily to fund operations, capital expenditures, and payout of repositioning costs.

During 2009, the Company recorded a capital lease obligation of \$7.9 million related to customer financed equipment. The capital lease relates to a customer contract signed for the Swindon, U.K. site in 2006. The initial lease will be paid down over three years assuming the customer achieves forecast annual production volumes. The remaining obligation at January 31, 2010, recorded as long-term debt, was \$5.9 million.

A summary of cash provided by financing activities is as follows:

Cash Provided by Financing Activities

	Three months ended January 31,	
	2010	2009
(in millions of U.S. dollars)	\$	\$
Increase in short-term borrowings	2.4	0.5
Increase in long-term debt	8.1	19.8
Repayment of long-term debt	(6.0)	(9.1)
Cash provided by financing activities of continuing operations	4.5	11.2
Cash provided by financing activities	4.5	11.2

Financing Arrangements and Ratios

There have been no significant changes to the Company's financing arrangements during the three months ended January 31, 2010.

Total cash interest-bearing debt, at January 31, 2010 was \$250.6 million, being \$0.1 million higher than at October 31, 2009. At January 31, 2010, the Company's consolidated ratio of interest-bearing debt to shareholders' equity was 98.9%, compared with 92.3% at October 31, 2009.

Adequacy of Financial Resources

As of January 31, 2010, the Company had cash balances of \$20.3 million and \$25.6 million in undrawn credit facilities available to it and was in compliance with all covenant requirements under its financing arrangements. The Company believes that, subject to usual business risks, its financial resources are sufficient to fund projected capital expenditures, debt service requirements and employee future benefit obligations in the normal course of business. There have been no material changes to the contractual obligations disclosed in the MD&A section of the Company's 2009 Annual Report that are outside the normal course.

Critical Accounting Policies and Estimates

Accounting policies are consistent with those described in Note 1 of the Company's 2009 Audited Consolidated Financial Statements, other than for developments set out below.

Changes in and Significant New Accounting Policies

The Company had no changes in accounting policy from the previously audited consolidated financial statements for the year ended October 31, 2009.

Change in recoverability of certain Investment Tax Credits

While evaluating the Investment Tax Credits ("ITCs") relating to Scientific Research and Development costs, the Company concluded it would be able to utilize previous periods unrecorded ITCs. Therefore, the Company recorded a decrease of \$2.8 million in the cost of goods sold relating to the utilization of the ITCs in the three months ended January 31, 2010.

Recently issued accounting pronouncements

CICA Section 1582, "Business Combinations," replaces Section 1581, "Business Combinations." Section 1582 improves the relevance, reliability and comparability of the information that a reporting entity provides in its financial statements about a business combination and its effects. This section outlines a variety of changes, including, but not limited to the following: an expanded definition of a business, a requirement to measure all business combinations and non-controlling interests at fair value, and a requirement to recognize future income tax assets and liabilities and acquisition and related costs as expenses of the period. The section applies to annual and interim financial statements for fiscal years beginning on or after January 1, 2011, with early adoption permitted. The Company is currently evaluating the effects of adopting these standards.

In January 2009, the CICA issued Handbook Section 1601, "Consolidations" ("CICA 1601"), and Section 1602, "Non-controlling Interests" ("CICA 1602"). CICA 1601 establishes standards for the preparation of consolidated financial statements. CICA 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. These standards apply to interim and annual consolidated financial statements relating to fiscal years beginning on or after January 1, 2011. The Company is currently evaluating the effects of adopting these standards.

In February 2008, the Canadian Accounting Standards Board announced the adoption of IFRS for publicly accountable enterprises. Patheon will be required to adopt IFRS no later than November 1, 2011. While IFRS uses a conceptual framework similar to Canadian GAAP, there are significant differences on recognition, measurement and disclosures which must be addressed. Determination of the key differences between IFRS and the Company's accounting policies is in progress with an evaluation of the main potential impact on its business practices, systems, disclosure controls and procedures, and internal controls over financial reporting. Changes in accounting policies upon adoption of IFRS are likely and may materially impact the Company's consolidated financial statements.

Risk Management

The following are updates to certain risks and uncertainties described in the Company's MD&A for the year ended October 31, 2009, available on SEDAR (www.sedar.com) or on Patheon's website (www.patheon.com).

Foreign Currency

The Company's business activities are conducted in several currencies – Canadian dollars and U.S. dollars for the Canadian operations, U.S. dollars for the U.S. operations and Euros, U.K. sterling and U.S. dollars for the European operations.

The Company's Canadian operations negotiate sales contracts for payment in both U.S. and Canadian dollars, and materials and equipment are purchased in both U.S. and Canadian dollars. The majority of its non-material costs (including payroll, facilities' costs and costs of locally sourced supplies and inventory) are denominated in Canadian dollars. Approximately 70% of revenues of the Canadian operations and approximately 20% of its operating expenses are transacted in U.S. dollars. As a result, the Company may experience trading and translation gains or losses because of volatility in the exchange rate between the Canadian dollar and the U.S. dollar. Based on the Company's current U.S. denominated net inflows, for each one-percent change in the Canadian-U.S. exchange rate, the impact on annual pre-tax income, excluding any hedging activities, is approximately \$0.2 million.

The Company mitigates its foreign exchange risk by engaging in foreign currency hedging activities using derivative financial instruments. The Company does not purchase any derivative instruments for speculative purposes.

At January 31, 2010, the Company's Canadian operations had outstanding foreign exchange forward contracts to sell US\$26.1 million at an average exchange rate of \$1.150 Canadian. The contracts mature at the latest on October 27, 2010 and cover approximately 33% of the Company's expected foreign exchange exposure for fiscal year 2010. The mark-to-market value at January 31, 2010 that is recorded in accumulated other comprehensive income (loss) is an unrealized gain of \$1.9 million.

Translation gains and losses related to the carrying value of the Company's foreign operations and certain foreign currency denominated debt held by the Company and designated as a hedge against the carrying value of certain foreign subsidiaries, are included in accumulated other comprehensive income (loss) in shareholders' equity. At January 31, 2010, the Company had designated \$87.5 million of U.S. dollar denominated debt as a hedge against its investment in its U.S. and Puerto Rico subsidiaries.

Interest Rate Exposure

The Company has exposure to movements in interest rates. The Company has entered into interest rate swaps to convert the interest expense on its senior secured term loan from a floating interest rate to a fixed interest rate until June 30, 2010. The mark-to-market value of these financial instruments at January 31, 2010 was an unrealized loss of \$3.0 million, which has been recorded in accumulated other comprehensive income (loss) in shareholders' equity. Taking this interest rate swap into account, at January 31, 2010, 38% of the Company's total debt portfolio was subject to movements in floating interest rates. Assuming no change to the structure of the debt portfolio, a 1% change in floating interest rates has an impact on annual pre-tax income of approximately \$1.0 million.

CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

As of January 31, 2010, the Company's management evaluated the effectiveness of the Company's disclosure controls and procedures, as defined under rules adopted by the Canadian Securities Administrators ("CSA"). This evaluation was performed under the supervision of, and with the participation of, the CEO and the Chief Financial Officer ("CFO").

Based on this evaluation, the CEO and the CFO have concluded that the Company's disclosure controls and procedures are effective in providing reasonable assurance that material information relating to the Company and its consolidated subsidiaries is made known to the CEO and the CFO by others within those entities on a timely basis.

Internal Control over Financial Reporting

There was no change in the Company's internal control over financial reporting that occurred during the period beginning on November 1, 2009, and ended on January 31, 2010, that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

The Company filed certifications, signed by the President and CEO and the Executive Vice President and CFO, with the CSA upon filing of the 2010 interim filings. In those filings, the CEO and CFO certify, as required by National Instrument 52-109, the appropriateness of the financial disclosure, the design and effectiveness of the disclosure controls and procedures and the design and effectiveness of internal controls over financial reporting.

Seasonal Variability of Results

Historically, the Company's manufacturing and PDS revenues are lower in the first and fourth fiscal quarters. The Company attributes this to several factors, including: (i) many clients reassess their need for additional product in the last quarter of the calendar year in order to use existing inventories of products; (ii) the lower production of seasonal cough and cold remedies in the first quarter; (iii) many small pharmaceutical and small biotechnology clients involved in PDS projects limit their project activity toward the end of the calendar year in order to reassess progress on their projects and manage cash resources; and (iv) the Patheon-wide plant shut-down during a portion of the traditional holiday period in December and January. Revenues in the fourth fiscal quarter are also typically impacted by summer shut-downs during August in the European operations.

Selected Quarterly Financial Information

The following is selected financial information for the eight most recent quarters:

Quarterly Consolidated Financial Information

<i>Quarter ended (in millions of U.S. dollars, except per share amounts)</i>	REVENUES	EBITDA BEFORE REPOSITIONING EXPENSES	LOSS FROM CONTINUING OPERATIONS	BASIC AND DILUTED LOSS PER SHARE FROM CONTINUING OPERATIONS	LOSS ATTRIBUTABLE TO RESTRICTED VOTING SHAREHOLDERS	BASIC AND DILUTED LOSS PER SHARE
	\$	\$	\$	\$	\$	\$
2010						
January 31	154.8	9.3	(10.7)	(0.08)	(11.1)	(0.09)
2009						
October 31	176.1	27.6	5.8	0.04	4.6	0.04
July 31	164.4	13.5	(5.2)	(0.09)	(9.8)	(0.10)
April 30	167.4	20.2	1.8	(0.02)	(3.2)	(0.04)
January 31	147.2	12.8	(1.5)	(0.06)	(9.6)	(0.11)
2008						
October 31	172.1	24.8	41.7	0.44	35.8	0.39
July 31	195.0	24.7	(3.9)	(0.04)	(14.0)	(0.16)
April 30	186.0	23.1	(6.5)	(0.07)	(8.5)	(0.09)

Additional Information

Share Capital

As of January 31, 2010, the Company had outstanding 129,167,926 restricted voting shares and 150,000 Class I Series D special voting shares. At January 31, 2010, the Company had 4,031,644 stock options outstanding of which 2,535,683 were exercisable.

Related Party Transactions

Revenues from companies controlled by a former director and significant shareholder of the Company were in the amount of \$0.1 million and \$0.3 million for the three months ended January 31, 2010 and 2009, respectively. These transactions were conducted in the normal course of business and are recorded at the exchanged amount. Accounts receivable at January 31, 2010 and October 31, 2009 includes a balance of \$0.1 million and \$0.5 million, respectively, resulting from these transactions.

As of January 31, 2010 and 2009, the Company had an investment of \$2.7 million and \$1.5 million, respectively, representing an 18% interest in two Italian companies (collectively referred to as “BSP Pharmaceuticals”) whose largest investor was an officer of the Company until December 31, 2009. These companies specialize in the manufacturing of cytotoxic pharmaceutical products. On July 2, 2008, the Company signed a shareholders’ agreement with the other investors in BSP Pharmaceuticals, the terms of which provide the Company with significant influence over the strategic operating, investing and financing policies of BSP Pharmaceuticals. As a result, the Company is now accounting for its investment in BSP Pharmaceuticals using the equity method. Accordingly, for the three months ended January 31, 2010 and 2009, the Company recorded investment income of \$0.4 million and a loss of \$0.2 million, respectively.

There were no management fees recorded under a management services agreement with BSP Pharmaceuticals for the three months ended January 31, 2010 and 2009. Accounts receivable at January 31, 2010 and October 31, 2009 include a balance of \$2.1 million and \$1.5 million, respectively, in connection with the management services agreement. These services were conducted in the normal course of business and are recorded at the exchanged amounts.

In connection with certain of BSP Pharmaceuticals’ bank financing, the Company has made commitments that it will not dispose of its interest in BSP Pharmaceuticals prior to January 1, 2011.

Public Securities Filings

Other information about the Company, including the annual information form and other disclosure documents, reports, statements or other information that are filed with Canadian securities regulatory authorities can be accessed through SEDAR at www.sedar.com.

FORWARD-LOOKING STATEMENTS

This MD&A contains forward-looking statements which reflect management’s expectations regarding the Company’s future growth, results of operations, performance (both operational and financial) and business prospects and opportunities. All statements, other than statements of historical fact, are forward-looking statements. Wherever possible, words such as “plans”, “expects” or “does not expect”, “forecasts”, “anticipates” or “does not anticipate”, “believes”, “intends” and similar expressions or statements that certain actions, events or results “may”, “could”, “would”, “might” or “will” be taken, occur or be achieved have been used to identify these forward-looking statements. Although the forward-looking statements contained in this MD&A reflect management’s current assumptions based upon information currently available to management and based upon what management believes to be reasonable assumptions, the Company cannot be certain that actual results will be consistent with these forward-looking statements. Current material assumptions relate to customer volumes, regulatory compliance and foreign exchange rates. Forward-looking statements necessarily involve significant known and unknown risks, assumptions and uncertainties that may cause the Company’s actual results, performance, prospects and opportunities in

future periods to differ materially from those expressed or implied by such forward-looking statements. These risks and uncertainties include, among other things: regulatory approval of and market demand for client products; general economic risks; credit and client concentration; the ability to identify and secure new contracts; regulatory matters, including compliance with pharmaceutical regulations; international operations risks; exposure to foreign currency risks; competition; product liability claims; intellectual property; environmental, health and safety risks; substantial financial leverage; interest rates; initiatives to reduce operating expenses; use of non-GAAP financial measures, significant shareholders; risks associated with information systems; and supply arrangements. For additional information regarding risks and uncertainties that could affect our business, please see the “Description of the Business – Risk Factors” section in our Annual Information Form, and the “Risk Factors” section in our MD&A for the year ended October 31, 2009, both of which are available on SEDAR at www.sedar.com Although the Company has attempted to identify important risks and factors that could cause actual actions, events or results to differ materially from those described in forward-looking statements, there may be other factors and risks that cause actions, events or results not to be as anticipated, estimated or intended. There can be no assurance that forward-looking statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. Accordingly, readers should not place undue reliance on forward-looking statements. These forward-looking statements are made as of the date of this MD&A and, except as required by law, the Company assumes no obligation to update or revise them to reflect new events or circumstances.