



PATHEON INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS

for the Year Ended October 31, 2008

Patheon Inc.
Management's Discussion and Analysis
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This management's discussion and analysis of financial condition and results of operations ("MD&A") should be read in conjunction with the Company's consolidated financial statements and related notes and Auditors' Report. The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). All amounts are in U.S. dollars unless otherwise indicated. This information is current to December 12, 2008.

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

NOTE TO READER

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This MD&A contains forward-looking statements which reflect management's expectations regarding Patheon's future growth, results of operations, performance (both operational and financial) and business prospects and opportunities. Where possible words such as "plans," "expects" or "does not expect," "budget," "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 that which management believes to be reasonable assumptions, Patheon cannot be certain that actual results will be consistent with these forward-looking statements. Current material assumptions relate to foreign exchange rates, customer volumes and regulatory compliance. A number of factors could cause actual results, performance, or achievements to differ materially from the results expressed or implied in the forward-looking statements, including those listed in the "Risk Factors" section of this MD&A. These factors should be considered carefully and readers should not place undue reliance on the forward-looking statements. Forward-looking statements necessarily involve significant known and unknown risks, assumptions and uncertainties that may cause Patheon'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: international operations and foreign currency fluctuation; customer demand for Patheon's services; regulatory matters affecting manufacturing and pharmaceutical development services; divestiture of Carolina site; exposure to complex production issues; substantial financial leverage; interest rate risks; potential environmental, health and safety liabilities; credit and customer concentration; competition; rapid technological change; product liability claims; intellectual property; significant shareholder; supply arrangements; pension plans; derivative financial instruments; international operations; and dependence upon key management personnel and executives. (See "Risk Factors".) Although Patheon 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, as noted above, 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, Patheon assumes no obligation to update or revise them to reflect new events or circumstances.

USE OF NON-GAAP FINANCIAL MEASURES

References in this MD&A to "EBITDA before repositioning expenses" are to income (loss) from continuing 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. "EBITDA margin before repositioning expenses" is EBITDA before repositioning expenses as a percentage of revenues.

References in this MD&A to "Adjusted income (loss) from continuing operations" are to income (loss) from continuing operations before after-tax repositioning expenses, refinancing expenses, gain on extinguishment of debt and asset impairment charges.

Since each of these measures 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 earnings (loss) determined in accordance with GAAP as indicators of performance. EBITDA before repositioning expenses 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 EBITDA before repositioning expenses. 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.

COMPANY PROFILE AND STRATEGY

ABOUT PATHEON

Patheon Inc. (“Patheon” or the “Company”) is a public company, amalgamated under the Canada Business Corporations Act, which trades under the symbol PTI on the Toronto Stock Exchange. The Company, organized and managed in two business segments, is a leading global provider of commercial manufacturing and pharmaceutical development services (“PDS”) to the international pharmaceutical and biotechnology industries.

The Company serves more than 300 of the world’s leading pharmaceutical and biotechnology companies and employs more than 4,500 highly-skilled staff in a network of ten modern manufacturing facilities and seven development centres located in North America and Europe, offering more than three million square feet of high quality capacity.

Commercial Manufacturing

Patheon is a leading global provider of contract manufacturing services to the global pharmaceutical industry. The Company delivers products to over 120 countries and offers a full array of services, including manufacturing, logistics and packaging of conventional dosage forms, sterile dosage forms and specialized products.

Patheon's commercial manufacturing activities relate primarily to prescription products in solid, semi-solid, and liquid dosage forms as well as various sterile dosage forms. Conventional dosage forms include both coated and uncoated compressed tablets, hard shell gelatin capsules, powders, ointments, creams, gels, syrups, suspensions, solutions and suppositories. Conventional sterile dosage forms include aseptically (sterile) filled and terminally sterilized liquids and powders in ampoules, vials, bottles or pre-filled syringes. Sterile lyophilized (freeze-dried) products are also manufactured in both vials and ampoules. Patheon also operates a segregated sterile (injectable) cephalosporin powder filling and lyophilisation facility at its Swindon site in the United Kingdom.

In fiscal 2008, Patheon's facilities and development centres were audited by 211 separate customer audit teams, representing both prospective and existing customers. Audits are an important means by which prospective and existing customers gain confidence that Patheon's operations are conducted in accordance with applicable regulatory requirements. These audits contribute to Patheon's ongoing improvement of manufacturing and development practices. In addition to customer audits, Patheon, like all commercial drug manufacturers, is subject to audits by various regulatory authorities. In fiscal 2008, 18 such audits by regulatory authorities were conducted at Patheon's sites in North America and Europe involving multiple products. Responses to audit observations were accepted and product approval was granted with one exception. In this one exception, discussions are on-going with the regulator as additional information was provided for further review.

Pharmaceutical Development

Patheon is a leading global provider of contract development services offering over 40 dosage forms and a broad range of services. The Company’s pharmaceutical development services include: (i) pre-formulation, formulation and development of dosage forms; (ii) development of analytical methods; (iii) manufacture to customer specifications of proposed new drug products during the regulatory drug approval process, including the manufacture of pilot (experimental) batches; (iv) clinical packaging and (v) scale-up and technology transfer services designed to validate commercial-scale drug manufacturing processes. Since the beginning of fiscal 2001, 19 new pharmaceutical products developed on behalf of customers by Patheon's pharmaceutical development services unit have been approved by regulators and launched through Patheon's commercial manufacturing facilities.

In addition to possessing pharmaceutical development capabilities for a broad range of dosage forms, each of Patheon's development centres provides a different specialized pharmaceutical development capability (high-potency, sterile, lyophilisation and controlled-release). During the course of 2008 the Company increased its PDS capacity with new facilities in Milton Park, in Oxfordshire, U.K. and in Research Triangle Park, North Carolina. The Company also completed a new intermediate scale process suite in its Cincinnati facility.

At October 31, 2008, the company was working on a total of 379 of its clients’ projects. This total includes products under development as well as stability and process optimization work on some products that have already been launched. The

Company is working on 12 drug candidates at the New Drug Application (“NDA”) stage. The Company did not launch any new pharmaceutical products developed by Patheon's PDS unit into commercial manufacturing in fiscal 2008.

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 will grow with the market, increase its market share and increase 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 and by 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 with a Lean 6 Sigma program called “Patheon Advantage”.

OVERVIEW OF PHARMACEUTICAL INDUSTRY OUTSOURCING

The global pharmaceutical industry comprises global, regional and national pharmaceutical manufacturers and distributors, biologics companies, specialty pharmaceutical companies, generic companies and emerging biopharma companies.

The focus and operational structures of many global pharmaceutical companies have undergone significant changes in the past few years. Many global pharmaceutical companies are relying on the services of contract product development and commercial manufacturing companies to help them meet growing demand, bring new drugs to market more quickly and operate more effectively. As a result, certain competencies such as dosage form manufacturing and dosage form development are increasingly being outsourced to service providers such as Patheon. Several global pharmaceutical companies have continued to publicly announce their intentions to restructure their site networks to increase operating efficiencies and to outsource more of their production.

In addition, more products are being developed by biotechnology companies. Many of these companies have focused their financial resources on the development and marketing of their products, rather than investing in their own manufacturing capacity. As a result, the demand for third-party dosage form manufacturing services continues to increase as these smaller companies grow in number and relative representation within the industry.

Finally, specialty pharmaceutical companies (pharmaceutical companies focused on in-licensing or acquiring products, rather than new drug discovery) typically operate in a particular niche segment, such as drug delivery systems or product portfolios focused on specific therapeutic categories. These companies are increasingly in-licensing or developing their own branded products for which they may not have the necessary manufacturing capacity or capabilities, and therefore, are turning to third-party service providers to provide manufacturing services.

Global pharmaceutical sales in 2007 were \$712 billion per IMS Health. Patheon's target markets include the global market for the manufacture of finished dosage forms and for dosage form research and development. The size of the finished dosage form manufacturing market, based on publicly available industry sources, is estimated to be approximately \$80 billion, of which approximately \$12 billion is outsourced. Based on a study by an independent third party consultant retained by Patheon, it is estimated that the contract manufacturing market is growing at approximately 3% per year. Similarly, Patheon management estimates that \$1.4 billion of dosage form development is outsourced and the market is growing at a rate of 10% per annum. Specialty pharmaceutical and biotechnology companies are relying increasingly on contract drug development suppliers to assist with complex studies and to help move high-potential new molecular entities through the various stages of evaluation more quickly.

Demand for outsourced pharmaceutical development and commercial manufacturing services is expected to continue to grow. In addition to pressure on pharmaceutical and biotechnology companies to reduce costs, Patheon's management believes that growth of pharmaceutical industry outsourcing will be driven by the following factors:

- growth of the global pharmaceutical industry. According to leading market research firm IMS Health, global pharmaceutical industry revenues have grown from \$354 billion in 2000 to approximately \$712 billion in 2007;
- global research and development expenditures are increasing;
- the number of product candidates in development continues to expand;

- consolidation of the pharmaceutical industry, and supply chain restructuring, are providing new opportunities as companies seek to reduce excess capacity in their manufacturing networks;
- increased demand for specialized manufacturing capabilities in key technical niches (for example, lyophilization); and
- increased demand for back-up sources of supply.

COMPETITORS

Commercial Manufacturing

In North America and Europe, Patheon's competition includes: (i) companies, both public and private, that are not focused on contract manufacturing, but provide this service as part of a range of services to the pharmaceutical industry; (ii) companies that focus on contract manufacturing, but offer services in a limited number of dosage forms; and (iii) large pharmaceutical companies that offer third-party manufacturing services to fill excess capacity. In addition, in Europe there are a large number of privately owned, dedicated outsourcing companies that serve only their local or national markets.

Pharmaceutical Development

The pharmaceutical development services market is composed of a range of participants: (i) a large number of laboratories, which offer only a limited range of development services generally at a small scale; (ii) providers focused on specific technologies and/or dosage forms; and (iii) a few fully integrated companies that can provide the full complement of services necessary to develop, scale-up and manufacture a wide range of dosage forms.

In recent years a number of companies in Asia, particularly India, have been entering the pharmaceutical contract manufacturing market for generic products and the PDS sector and have been proceeding with obtaining FDA approval for some of their plants as well as acquiring additional plants in Europe and North America.

RECENT DEVELOPMENTS

New Leadership

Under the leadership of Wes Wheeler, who joined Patheon in December 2007 as the Chief Executive Officer, the Company has made changes to its executive management team, opened its U.S. headquarters in Research Triangle Park ("RTP"), North Carolina and opened a new European headquarters in Zug, Switzerland. The Company is also undertaking a series of operational initiatives to reduce operating expenses and increase manufacturing efficiency, including launching the Patheon Advantage Lean 6 Sigma program. The Company has established a number of key performance indicators, including on time delivery, batches right first time and inventory turns to measure the benefits of these initiatives. Combined with re-focused sales efforts, these programs are expected to make the Company more competitive, reduce operating costs and improve long-term profitability.

Canadian Site Network

On April 17, 2007 the Company announced that as part of its strategy to focus on developing and manufacturing prescription pharmaceutical products and to improve the Company's profitability, it planned to restructure its network of pharmaceutical manufacturing facilities in Canada.

In connection with this initiative, on January 31, 2008 the Company sold its Niagara-Burlington commercial OTC manufacturing business to Pharmetics Inc. Pharmetics acquired the assets, including equipment, facilities and land at the Company's facilities in Fort Erie and Burlington (Gateway Drive). Pharmetics provided employment to all of the commercial manufacturing employees at the two sites and will continue to manufacture and supply all of the products that were manufactured at these sites. Proceeds from the divestiture, net of transaction costs, were \$10.5 million.

The Company also plans to close its York Mills, Toronto facility and is currently in the process of transferring all commercial production and development services undertaken at its York Mills facility to, primarily, its Whitby facility. In accordance with this plan, on April 15, 2008, the Company completed the sale of the York Mills property for net proceeds of \$11.9

million and has entered into a lease for up to two years in order to facilitate the decommissioning process. The Company anticipates that the transfer of production from York Mills will be completed during the third quarter of the 2009 fiscal year.

Puerto Rico Operations

On December 14, 2007 the Company announced that as a result of its comprehensive review of the Puerto Rico operations, with a focus on eliminating operating losses and developing a long-term plan for the business, it had decided to retain and continue to streamline its facilities in Caguas and Manati, and divest its facility in Carolina, Puerto Rico that specializes in the manufacture of oral cephalosporin solid dosage forms. The decision follows the genericization of Omnicef® in May 2007 and the resulting significant drop in revenues at the Carolina facility.

Subsequent to the end of fiscal 2008, the Company decided to shut down the Carolina, Puerto Rico facility if a timely sale could not be completed. Serious interest had been shown by strategic buyers and negotiations had occurred with multiple parties. However, the Company has determined that eliminating the cash drain of Carolina through an immediate shutdown outweighs the risk of the sale process taking an extended period of time to complete and/or ultimately being unsuccessful. Assuming that a timely sale cannot be completed, the Company expects to close the facility by the end of the first quarter of 2009 and is in the process of filling all remaining customer orders prior to shutdown. Based on assessment and planning to date, the company estimates that severance and other closure costs will be approximately \$3 million.

The Carolina operations are classified as a discontinued operation, with the related assets and liabilities being classified as held for sale. During 2008 it was determined that the carrying value of the assets were impaired and in the third quarter of 2008 the Company recorded an impairment charge of \$7.7 million to write down the Carolina assets to their fair market value less estimated disposition costs. The fair value was based on discussions and negotiations the Company had undertaken with interested third parties.

Convertible Preferred Shares

On September 19, 2008 the Company completed an agreement (the “JLL Agreement”) with JLL Patheon Holdings, LLC, (“JLL”) under which JLL waived the requirement, under the terms of the convertible preferred shares held by JLL, that the Company redeem for cash all of these shares on April 27, 2017, if not previously converted. In consideration of the waiver, the Company issued to JLL 400,000 restricted voting shares, representing approximately 0.4% of the outstanding restricted voting shares. The Company also agreed to provide a limited waiver of the standstill provisions of the investor agreement with JLL to permit JLL to acquire, through the facilities of the Toronto Stock Exchange, over a one-year period, up to 1% of the outstanding restricted voting shares (determined on a partially diluted basis, taking into account the restricted voting shares issuable on conversion of the convertible preferred shares) namely 1,256,929 restricted voting shares.

The Company entered into the JLL Agreement (i) to characterize the convertible preferred shares as equity, rather than as both debt and equity, thereby achieving a simpler financial statement presentation that better reflects the financial nature of the convertible preferred shares; (ii) to reduce foreign exchange volatility in the Company’s financial reporting; and (iii) to eliminate the obligation to redeem the convertible preferred shares for cash of at least \$185 million in April 2017, if they had not been converted into restricted voting shares prior to that date.

The JLL Agreement resulted in a change in accounting treatment for the convertible preferred shares. The convertible preferred shares were previously treated as a compound financial instrument that contained both debt and equity components, with a related non-cash accretive interest expense. With the completion of the JLL Agreement, the full carrying value of the convertible preferred of \$147.7 million, representing their fair value on the closing date, less transaction costs, has been recorded within shareholders’ equity on the Company’s balance sheet and no further accretive interest expense has been recorded in the consolidated statement of loss. The accretive interest charge recorded in 2008 up to the date of the JLL Agreement was \$13.5 million. Paid-in-kind dividend equivalents (or cash dividends, if the Company so elects after October 27, 2009) on the convertible preferred shares are now reported below net loss to arrive at a loss attributable to the restricted voting shareholders. Any paid-in-kind dividend equivalents have the effect of increasing the carrying value of the convertible preferred shares in shareholders’ equity. Paid-in-kind dividends on the convertible preferred shares for the year ended October 31, 2008 were \$1.5 million.

For accounting purposes, the change in terms has resulted in a deemed repayment of the debt and equity components of the convertible preferred shares with the deemed consideration being the fair value of the convertible preferred shares without mandatory redemption requirements, plus the market value of the 400,000 restricted voting shares. The deemed consideration received was allocated to the respective debt and equity components based on their relative fair values at the date of the transaction. In connection with this, in the fourth quarter of 2008, the Company recorded a non-cash gain of \$34.9 million in the consolidated statement of loss on the deemed repayment of the debt component and recorded a non-cash charge in the deficit account in shareholders' equity of \$14.9 million on the deemed repayment of the equity component.

The reclassification of the convertible preferred shares to shareholders' equity has eliminated entirely the un-hedged U.S. dollar denominated debt exposure recorded in the Company's Canadian legal entity. The related foreign exchange losses recorded in the Company's consolidated statement of loss for the year ended October 31, 2008 amounted to \$6.4 million.

JLL Offer to Acquire Patheon's Restricted Voting Shares

On December 8, 2008 JLL announced in a press release its intention to make an unsolicited offer to acquire any or all the outstanding restricted voting shares of Patheon that it does not already own at a price of USD \$2.00 per share in cash which is equivalent to C\$2.54 per share based on the exchange rate on December 5, 2008. JLL holds convertible preferred shares of the Company, which when converted and taken together with its holdings of restricted voting shares, would represent approximately 29% of the restricted voting shares of the Company.

Patheon's Board of Directors has appointed a special committee of independent directors, none of whom is associated with JLL to review and evaluate the proposed unsolicited bid from JLL, and make recommendations to the Board of Directors. Patheon's Board of Directors will advise shareholders of its recommendation with respect to this bid in due course and until such time shareholders have been advised to take no action with respect to the bid. The Company remains very confident in its business plan and continues to run its business as usual.

OVERVIEW OF PERFORMANCE

Consolidated revenues for the year ended October 31, 2008 were \$717.3 million, compared with \$634.1 million in 2007, representing an increase of \$83.1 million, or 13.1%. Had foreign currency exchange rates remained the same as the prior year, revenues would have increased by approximately 9%.

EBITDA before repositioning expenses for the year ended October 31, 2008 was \$82.6 million, representing a decrease of \$1.5 million, or 1.8% compared with 2007. The EBITDA margin before repositioning expenses in 2008 was 11.5% compared with 13.3% in 2007.

EBITDA before repositioning expenses in 2008 included a foreign exchange loss of \$6.4 million related to the revaluation of U.S. dollar denominated debt, net of hedging, in the Canadian legal entity. In 2007 the Company reported a gain of \$12.3 million on this foreign exchange exposure. This foreign exchange exposure was eliminated in September, 2008 due the change in the balance sheet presentation of the convertible preferred shares, arising from the JLL Agreement (see "Recent Developments"). Had foreign currency exchange rates remained the same as the prior year and after eliminating the impact of all foreign exchange gains and losses, EBITDA before repositioning expenses in 2008 would have been approximately \$12.8 million higher than was reported.

EBITDA before repositioning expenses in 2008 was achieved after expenses of \$3.3 million for an early retirement program in Cincinnati and after incurring a number of one-time expenses for hiring new management, launching the Patheon Advantage Lean 6 Sigma program and opening the new U.S. headquarters in RTP, North Carolina. By comparison, EBITDA before repositioning expenses for the year ended October 31, 2007 included a one-time actuarial gain of \$4.3 million arising from a decision to conform certain post retirement benefits in the Canadian operations.

Income from continuing operations for the year ended October 31, 2008 was \$18.1 million, compared with a loss of \$34.8 million in 2007. Income from continuing operations in 2008 included after tax repositioning expenses of \$19.0 million and a gain on extinguishment of debt of \$34.9 million. The loss from continuing operations in 2007 included after tax repositioning expenses of \$13.6 million and after tax refinancing expenses of \$12.6 million.

SELECTED ANNUAL FINANCIAL INFORMATION

The following is selected financial information for the three most recent fiscal years:

	Years ended October 31,		
	2008	2007	2006
<i>(in thousands of U.S. dollars, except loss per share)</i>	\$	\$	\$
Revenues	717,251	634,146	625,296
EBITDA before repositioning expenses	82,646	84,147	64,982
Adjusted income (loss) from continuing operations	2,174	(8,631)	(15,007)
Net loss attributable to restricted voting shareholders	(2,904)	(94,601)	(288,150)
Basic and diluted loss per share	(\$0.03)	(\$1.02)	\$3.10
Total assets	716,583	829,617	826,183
Total long-term liabilities	278,462	440,727	144,246
Cash dividends	-	-	-

The reduction in total long-term liabilities in 2008 compared with 2007 is as a result of the re-classification of the debt component of the convertible preferred shares to shareholders equity (see "Recent Developments"). The carrying value of the debt component of convertible preferred shares at October 31, 2007 was \$139.9 million.

The increase in long-term liabilities in 2007 compared with 2006 was due to the completion of a \$150 million long-term senior secured debt facility and the issue of \$150 million convertible preferred shares to JLL Partners. The proceeds from these financing activities, both of which were completed in April 2007, were used to repay debt facilities in North America and the U.K. In 2006, these debt facilities were classified within current liabilities.

For explanations concerning other significant variances see the reconciliations of EBITDA before repositioning expenses and adjusted income (loss) from continuing operations below and the "Performance Analysis" section on the MD&A.

A reconciliation of EBITDA before repositioning expenses with earnings (loss) from continuing operations as reported in the Company's consolidated financial statements is as follows:

	Years ended October 31,		
	2008	2007	2006
<i>(in thousands of U.S. dollars)</i>	\$	\$	\$
Income (loss) from continuing operations	18,102	(34,768)	(247,215)
Provision for income taxes	1,478	19,657	11,300
Gain on extinguishment of debt	(34,934)	-	-
Gain on sale of fixed assets	(282)	-	-
Foreign exchange loss on foreign operations	-	858	-
Refinancing expenses	-	13,471	7,975
Interest expense, net	30,789	29,119	20,601
Repositioning expenses	19,899	14,467	12,404
Depreciation and amortization	47,594	41,343	43,975
Asset impairment charge	-	-	215,942
EBITDA before repositioning expenses	82,646	84,147	64,982

The asset impairment charge in the year ended October 31, 2006 related principally to an impairment in the carrying value of goodwill and long-lived depreciable assets in the Puerto Rico operations.

A reconciliation of adjusted income (loss) from continuing operations, with income (loss) from continuing operations as reported in the Company's consolidated financial statements is as follows:

	Years ended October 31,		
	2008	2007	2006
<i>(in thousands of U.S. dollars)</i>	\$	\$	\$
Income (loss) from continuing operations	18,102	(34,768)	(247,215)
Repositioning expenses	19,899	14,467	12,404
Income taxes related to repositioning expenses	(893)	(900)	(1,552)
Refinancing expenses	-	13,471	7,975
Income taxes related to refinancing expenses	-	(901)	-
Gain on extinguishment of debt	(34,934)	-	-
Asset impairment charges	-	-	215,942
Income taxes related to asset impairment charges			(2,561)
Adjusted income (loss) from continuing operations	2,174	(8,631)	(15,007)

PERFORMANCE ANALYSIS

RESULTS OF OPERATIONS

The results of operations for Niagara-Burlington and Carolina have been segregated and presented separately as discontinued operations. All comparative amounts have been reclassified to conform to the current period presentation.

In anticipation of the adoption of the new accounting standard Section 3031 "Inventories" on November 1, 2008, the Company has modified its presentation of the consolidated statement of income (loss) to separately present cost of goods sold and selling, general and administrative expenses. This resulted in the inclusion of depreciation within cost of goods sold and selling, general and administrative expenses.

Consolidated Statements of Income (Loss)

	Three months ended October 31,			Years ended October 31,		
	2008	2007	%	2008	2007	%
<i>(in thousands of U.S. dollars, except loss per share)</i>	\$	\$	Change	\$	\$	Change
Revenues	172,106	161,821	6.4%	717,251	634,146	13.1%
Cost of goods sold	130,818	126,890	3.1%	562,370	502,738	11.9%
Gross profit	41,288	34,931	18.2%	154,881	131,408	17.9%
Selling, general and administrative expenses	30,022	28,069	7.0%	121,277	97,525	24.4%
Repositioning expenses	2,567	6,336	-59.5%	19,899	14,467	37.5%
Operating income	8,699	526	1553.8%	13,705	19,416	-29.4%
Interest expense, net	6,672	7,460	-10.6%	30,789	29,119	5.7%
Foreign exchange gain	(1,630)	(5,828)	-72.0%	(1,448)	(8,921)	-83.8%
Refinancing expenses	-	-		-	13,471	
Foreign exchange loss on foreign operations	-	-		-	858	
(Gain) loss on sale of fixed assets	134	-		(282)	-	
Gain on extinguishment of debt	(34,934)	-		(34,934)	-	
Income (loss) from continuing operations before income taxes	38,457	(1,106)		19,580	(15,111)	
Provision for (recovery of) income taxes	(2,866)	4,771		1,478	19,657	
Income (loss) from continuing operations	41,323	(5,877)		18,102	(34,768)	
Loss from discontinued operations	(4,419)	(1,645)	-168.6%	(19,543)	(59,833)	67.3%
Net income (loss) for the period	36,904	(7,522)		(1,441)	(94,601)	98.5%
Dividends on convertible preferred shares (note 13)	1,463	-		1,463	-	
Net income (loss) attributable to restricted voting shareholders	35,441	(7,522)		(2,904)	(94,601)	96.9%
Basic and diluted earnings (loss) per share						
From continuing operations	\$0.44	(\$0.06)		\$0.18	(\$0.37)	
From discontinued operations	(\$0.05)	(\$0.02)		(\$0.21)	(\$0.65)	
	\$0.39	(\$0.08)		(\$0.03)	(\$1.02)	

Revenues and EBITDA before Repositioning Expenses by Business Segment

Previously, the Company was organized and managed as a single business segment, being the provider of commercial manufacturing and pharmaceutical development services. Due to the continued growth of the PDS operations, and a change in the executive management structure, the business has been reorganized into two business segments: Commercial Manufacturing and Pharmaceutical Development Services ("PDS"). These segments are organized around the service activities provided to the company's customers.

<i>(in thousands of U.S. Dollars)</i>	Three months ended October 31,			Year ended October 31,		
	2008	2007	%	2008	2007	%
	\$	\$	Change	\$	\$	Change
Revenues						
Commercial Manufacturing						
North America	70,679	66,390	6%	278,568	271,265	3%
Europe	64,661	62,974	3%	299,167	247,027	21%
Total Commercial Manufacturing	135,340	129,364	5%	577,735	518,292	11%
Pharmaceutical Development Services	36,766	32,457	13%	139,516	115,854	20%
Total Revenues	172,106	161,821	6%	717,251	634,146	13%
EBITDA before repositioning expenses						
Commercial Manufacturing						
North America	11,909	4,988	139%	23,088	16,430	41%
Europe	12,144	3,841	216%	54,408	36,927	47%
Total Commercial Manufacturing	24,053	8,829	172%	77,496	53,357	45%
Pharmaceutical Development Services	12,727	9,343	36%	42,129	30,391	39%
Corporate Costs	(12,009)	5,512		(36,979)	399	
Total EBITDA before repositioning expenses	24,771	23,684	5%	82,646	84,147	-2%

Commercial Manufacturing

Revenues from commercial manufacturing operations for the year ended October 31, 2008 increased by 11%, or \$59.4 million, to \$577.7 million from \$518.3 million in 2007.

The major driver behind the revenue improvement came from the European operations, which reported a \$52.1 million, or 21% increase in revenues. All four of the facilities contributed to this improvement. Reported revenues in the European operations increased as a result of the strengthening of the euro, which on average was 11% stronger against the U.S. dollar relative to 2007. Had European currencies remained constant to the rates of the prior year, European revenues would have been approximately 12% higher than 2007.

Revenues from the North American operations increased by \$7.3 million, or 3%. This reflected revenue increases from the Canadian and Puerto Rico operations, offset in part by a decline in the Cincinnati operations.

EBITDA before repositioning expenses from the commercial manufacturing operations for the year ended October 31, 2008 increased by 45%, or \$24.1 million to \$77.5 million from \$53.4 million in 2007. This represents an EBITDA margin before repositioning expenses of 13.4% compared with 10.3% in 2007.

The improvement in EBITDA before repositioning expenses was driven by the European operations, which reported a \$17.5 million, or 47% increase in EBITDA before repositioning. The improvement reflects benefits from the revenue increases, offset in part by a change in mix to lower margin products in the Italian operations. Had European currencies remained constant to the rates of the prior year and after eliminating the impact of all foreign exchange gains and losses, European EBITDA before repositioning expenses would have been approximately \$8.8 million lower than was reported.

In North America EBITDA before repositioning expenses increased by \$6.7 million, or 41%. EBITDA before repositioning expenses for North America included a one-time charge for an early retirement program in Cincinnati of \$3.3 million. By comparison in 2007 the results of the Canadian operations benefitted from a one-time actuarial gain of \$3.8 million in connection with a curtailment of certain post retirement benefits. North American results reflected a significant

reduction in losses from the Puerto Rico operations arising from the benefits of the restructuring initiatives, offset by a decline in earnings in Cincinnati principally as a result of a mix of lower margin business. Results from the Canadian operations were impacted by a 7% increase in the average value of the Canadian dollar relative to the U.S. dollar during the year. The negative impact of this currency fluctuation was more than offset by gains from the Company's foreign exchange hedging program and gains from the revaluation of working capital. Had the Canadian dollar remained constant to the rates of the prior year and after eliminating the impact of all foreign exchange gains and losses, North American EBITDA before repositioning expenses would have been approximately \$1.6 million lower than was reported.

Pharmaceutical Development Services

PDS revenues for the year ended October 31, 2008 increased by 20%, or \$23.6 million, to \$139.5 million from \$115.9 million in 2007. The increase in revenues reflects the continued strength of the PDS business in all regions, with the Canadian, Cincinnati and Ferentino operations providing the most significant improvements.

EBITDA before repositioning expenses from the PDS operations for the year ended October 31, 2008 increased by 39%, or \$11.7 million to \$42.1 million from \$30.4 million in 2007. This represents an EBITDA margin before repositioning expenses of 30.2% compared with 26.2% in 2007. The improvement reflected the strong revenue growth across all regions. The improvement in EBITDA before repositioning expenses is after the positive impact of an 11% increase in the average value of the euro relative to the U.S. dollar and the negative impact of a 7% increase in the average value of the Canadian dollar relative to the U.S. dollar during the year. Had the euro and Canadian dollar remained constant to the rates of the prior year and after eliminating the impact of all foreign exchange gains and losses, EBITDA before repositioning expenses for the PDS operations would have been approximately \$2.5 million higher than was reported.

Corporate Costs

Corporate costs for year ended October 31, 2008 were \$37.0 million, compared with a net recovery of \$0.4 million in 2007. Corporate costs in 2008 include net foreign exchange losses of \$6.4 million on the revaluation of un-hedged U.S. dollar denominated debt held in the Canadian legal entity; this compares with a gain of \$12.3 million recorded in 2007. This foreign exchange exposure was eliminated during the fourth quarter of 2008 as a result of the change in the balance sheet classification of the convertible preferred shares arising from the JLL Agreement (see "Recent Developments").

Additional corporate costs were incurred in 2008 for the recruitment of senior and executive management positions, consulting fees relating to operational and strategic initiatives and costs relating to the opening of the U.S. headquarters in RTP, North Carolina. There were also additional non-cash costs for stock based compensation programs in connection with these changes.

Repositioning Expenses

In 2008, the Company incurred \$19.9 million of repositioning expenses in connection with changes in senior and executive management, a workforce reduction initiative in Swindon, U.K. and restructuring of the Puerto Rico and Canadian operations.

In 2007, the Company incurred repositioning expenses of \$14.5 million in connection with its site rationalization program in Puerto Rico and Canada, a manufacturing efficiency review and a review of strategic and financial alternatives which culminated in a major refinancing of the Company in April 2007.

Interest Expense

Interest expense in 2008 was \$30.8 million, compared with \$29.1 million in 2007. The increase in interest costs reflects the impact of the financing arrangements that were put in place on April 27, 2007 and includes a non-cash accretive interest charge of \$13.5 million in 2008, compared with \$7.1 million in 2007, in respect of the debt component of the convertible preferred shares. The increase also reflects the translation impact of the strengthening euro against the U.S. dollar in the first three quarters of 2008 on euro denominated interest costs in the Italian operations.

The Company ceased recording the accretive interest charge after the September 19, 2008 completion of the agreement to eliminate the cash redemption requirement on the convertible preferred shares (see "Recent Developments").

Refinancing Expenses

In 2007, refinancing expenses of \$13.5 million were incurred in connection with the Company's refinancing that was completed in April 2007. The expenses were made up of transaction costs for the new credit facilities, transaction costs allocated to the debt portion of the convertible preferred shares and repayment charges in connection with the cancellation of certain of the Company's U.K. debt facilities.

Foreign Exchange Loss on Foreign Operations

In 2007, the Company recorded a loss of \$0.9 million relating to foreign exchange translation losses previously recorded in accumulated other comprehensive income, arising from a change in the Company's internal capital structure.

Gain on Extinguishment of Debt

In 2008, the Company recorded a non-cash gain of \$34.9 million in connection with the JLL Agreement to eliminate the cash redemption requirement on the convertible preferred shares (see "Recent Developments"). The gain reflects the difference between the fair value of the deemed proceeds on settlement of the debt component of the convertible preferred shares and its carrying value.

Income (Loss) Before Income Taxes from Continuing Operations

The Company reported income before income taxes from continuing operations of \$19.6 million for the year ended October 31, 2008, compared with a loss of \$15.1 million in 2007.

Income Taxes

The income tax expense for the year ended October 31, 2008 was \$1.5 million, compared with \$19.7 million in 2007. Both the accretive interest expense on the convertible preferred shares of \$13.5 million and the gain on settlement of the debt component of convertible preferred shares of \$34.9 million are not taxable items. The income tax expense in 2008 is net of a future income tax recovery of \$3.2 million relating to a reduction in tax rates in Italy that the Company will benefit from commencing in fiscal 2009 and a future income tax recovery of \$3.0 million relating to prior period research and development tax credits in the U.K. These benefits were offset by tax losses in Puerto Rico, where the tax benefit has not been recognized.

The income tax charge in 2007 principally reflected high tax rates in Italy where the Company reported increased taxable income, compounded by tax losses in certain entities in Puerto Rico and Canada, where the tax benefit after valuation reserves was not recognized. The 2007 expense included a charge of \$2.1 million in connection with an inter-company dividend payment and a charge of \$1.9 million in connection with the transfer of net foreign exchange losses from accumulated other comprehensive income.

Income (Loss) from Continuing Operations and Earnings (Loss) Per Share from Continuing Operations

The Company recorded income from continuing operations for the year ended October 31, 2008 of \$18.1 million, compared with a loss of \$34.8 million in the same period a year ago. The earnings per share were 18¢ compared with a loss of 37¢ a year earlier. The income in 2008 included after tax repositioning expenses of \$19.0 million, or 21¢ per share, offset by a gain on the settlement of the debt component of convertible preferred shares of \$34.9 million, or 39¢ per share. The loss in 2007 included after tax repositioning expenses of \$13.6 million or 15¢ per share and after tax refinancing expenses of \$12.6 million, or 14¢ per share.

Loss and Loss Per Share from Discontinued Operations

Discontinued operations include the results of the Niagara-Burlington Operations up to their divestiture date of January 31, 2008 and the Carolina Operations. The results from discontinued operations for the years ended October 31, 2008 and 2007 were as follows:

	Three months ended October 31,		Year ended October 31,	
	2008	2007	2008	2007
<i>(in thousands of U.S. dollars)</i>	\$	\$	\$	\$
Revenues	1,045	11,786	17,894	78,172
Cost of goods sold	4,061	15,651	25,439	66,376
Gross profit (loss)	(3,016)	(3,865)	(7,545)	11,796
Selling, general and administrative expenses	907	(1,414)	2,844	10,023
Repositioning expenses	487	(52)	677	936
Operating income (loss)	(4,410)	(2,399)	(11,066)	837
Interest expense, net	9	8	41	48
Asset impairment charge	-	(564)	7,700	61,045
Loss on disposal of discontinued operations	-	-	601	-
Loss before income taxes	(4,419)	(1,843)	(19,408)	(60,256)
Provision for (recovery of) income taxes	-	(198)	135	(423)
Net loss for the period	(4,419)	(1,645)	(19,543)	(59,833)

The net loss from discontinued operations for the year ended October 31, 2008 was \$19.5 million, or 21¢ per share compared with a net loss of \$59.8 million or 65¢ per share in 2007. The loss in 2008 reflects a significant decline in the profitability of the Carolina operations as a result of the 2007 genericization of Omnicef®. In 2008 the Company also recorded an impairment charge of \$7.7 million to write down the carrying value of the Carolina assets to their fair market value, less estimated costs to divest and a charge of \$0.6 million in connection with the final divestiture of the Niagara-Burlington operations.

The net loss in 2007 included an asset impairment charge of \$48.6 million relating to the Carolina operations and \$12.4 million, relating to the Niagara-Burlington operations.

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

The Company recorded a net loss for the year ended October 31, 2008 of \$2.9 million compared with a loss of \$94.6 million in 2007. The net loss attributable to holders of restricted voting shareholders in 2008 is after a non-cash dividend on the convertible preferred shares of \$1.5 million. This represents a pro-rata dividend commencing on September 20, 2008, following the change in accounting treatment for the convertible preferred shares as a result of the completion of the JLL Agreement (see "Recent Developments").

The loss per share attributable to restricted voting shareholders in 2008 was 3¢, compared with \$1.02 in 2007. Because the Company reported a loss in the years ended October 31, 2008 and 2007 there is no impact of dilution.

FOURTH QUARTER RESULTS

Revenues

Consolidated revenues for the three months ended October 31, 2008 were \$172.1 million, compared with \$161.8 million in 2007, representing an increase of \$10.3 million, or 6%. Had foreign currency exchange rates remained the same as the prior year, revenues would have increased by approximately 8%.

Revenues from commercial operations in the fourth quarter of 2008 increased by \$6.0 million, or 5% to \$135.3 million. North American revenues increased by \$4.3 million, or 6% to \$70.7 million, driven by gains in the Puerto Rico operations, which is starting to see the benefits of recently signed business and recovery in volumes from some of its existing products. These gains were offset in part by revenue declines from existing business in the Cincinnati and Canadian operations. The

European commercial operations reported revenues of \$64.7 million, reflecting a modest increase in revenues of \$1.7 million, or 3%, with the Swindon and Bourgoin operations being the major contributors.

PDS revenues in the fourth quarter of 2008 increased by \$4.3 million, or 13% to \$36.8 million. The improvement was driven in large part by increased business in the Canadian operations.

EBITDA before Repositioning Expenses

EBITDA before repositioning expenses for the three months ended year ended October 31, 2008 was \$24.8 million, representing an increase of \$1.1 million, or 5% compared with 2007. EBITDA margin before repositioning expenses in 2008 was 14.4% compared with 14.6% in 2007.

EBITDA before repositioning expenses in the fourth quarter of 2008 included a foreign exchange loss of \$2.3 million related to the revaluation of U.S. dollar denominated debt, net of hedging, in the Canadian legal entity. In the same period last year the Company reported a gain of \$7.5 million on this foreign exchange exposure. Had foreign currency exchange rates remained the same as the prior year and after eliminating the impact of all foreign exchange gains and losses, EBITDA before repositioning expenses in the fourth quarter of 2008 would have been approximately \$5.0 million higher than was reported.

EBITDA before repositioning expenses for the year ended October 31, 2007 included an actuarial gain of \$4.3 million arising from a decision to conform certain post retirement benefits in the Canadian operations.

EBITDA before repositioning expenses from commercial operations in the fourth quarter of 2008 increased by \$15.2 million, or 172% to \$24.1 million. This represents an EBITDA margin before repositioning expenses of 17.8% compared with 6.8% in the same period last year. EBITDA before repositioning expenses from the North American operations increased by \$6.9 million, driven by a significant improvement in the Puerto Rico operations, where the Company slightly exceeded its break-even target for the fourth quarter of 2008. The improvement in earnings in Puerto Rico was offset in part by a decline in profitability in Cincinnati as a result of change in mix in lower margin business. Profitability in the Canadian operations increased despite the benefits of the majority of the one-time actuarial gain that was recorded in 2007, as noted above. In Europe EBITDA before repositioning expenses increased by \$8.3 million driven by improved margins in the Swindon and Bourgoin operations.

EBITDA before repositioning expenses from the PDS operations in the fourth quarter of 2008 increased by \$3.4 million, or 36% to \$12.7 million, with the gains being driven by the increased volumes in Canada.

Corporate costs in the fourth quarter of 2008 were \$12.0 million, compared with a net recovery of \$5.5 million in the same period in 2007. This overall change of \$17.5 million includes the \$9.8 million differential on foreign exchange gains and losses on the un-hedged debt noted above. Additional costs were incurred in the fourth quarter of 2008 in connection with consulting fees relating to operational and strategic initiatives and costs relating to opening the U.S. headquarters. There were also additional non-cash costs for stock based compensation programs.

Income (Loss) from Continuing Operations

Income from continuing operations for the three months ending October 31, 2008 was \$41.3 million compared with a loss of \$5.9 million in the same period last year. The results for the fourth quarter of 2008 include repositioning costs of \$2.6 million, associated with further headcount reductions in Puerto Rico and costs associated with the transfer of production from the York Mills facility to Whitby. The results for fourth quarter of 2008 also include a non-cash gain of \$34.9 million in connection with the JLL Agreement to eliminate the cash redemption requirement on the convertible preferred shares (see "Recent Developments").

Loss from Discontinued Operations

The loss from discontinued operations for the fourth quarter of 2008, reflect the results of the Carolina, Puerto Rico operations. Results for the fourth quarter of 2007 include both the Niagara-Burlington and Carolina operations. The loss from discontinued operations for the three months ended October 31, 2008 was \$4.4 million, compared with a loss of \$1.6

million in the same period last year. The loss in the fourth quarter of 2008 includes costs that the Company has incurred in its process to sell the Carolina business and severance related repositioning expenses of \$0.5 million.

SELECTED QUARTERLY FINANCIAL INFORMATION

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

Quarterly Consolidated Financial Information

Quarter ended (in thousands of U.S. dollars, except per share amounts)	REVENUES	EBITDA BEFORE REPOSITIONING EXPENSES	NET INCOME (LOSS) FROM CONTINUING OPERATIONS	NET INCOME		
				BASIC AND DILUTED EARNINGS (LOSS) PER SHARE FROM CONTINUING OPERATIONS	(LOSS) ATTRIBUTABLE TO RESTRICTED VOTING SHAREHOLDERS	BASIC AND DILUTED EARNINGS (LOSS) PER SHARE
	\$	\$	\$	\$	\$	\$
2008						
October 31	172,106	24,771	41,323	\$0.44	35,441	\$0.39
July 31	194,976	24,718	(4,535)	(\$0.05)	(14,682)	(\$0.16)
April 30	185,997	23,114	(6,471)	(\$0.07)	(8,475)	(\$0.09)
January 31	164,172	10,043	(12,215)	(\$0.14)	(15,188)	(\$0.17)
2007						
October 31	161,821	23,684	(5,877)	(\$0.06)	(7,522)	(\$0.08)
July 31	164,737	20,649	(3,365)	(\$0.04)	(63,069)	(\$0.68)
April 30	160,218	21,140	(21,950)	(\$0.23)	(21,986)	(\$0.24)
January 31	147,370	18,674	(3,576)	(\$0.04)	(2,024)	(\$0.02)

Net income from continuing operations in the quarter ended October 31, 2008 included a gain on the settlement of convertible preferred shares of \$34.9 million, or 39¢ per share. The net loss attributable to restricted voting shareholders in the quarter ended July 31, 2008 included an after tax asset impairment charge of \$7.7 million, or 8¢ per share relating to the Carolina discontinued operations.

The loss from continuing operations in the quarter ended April 30, 2007 included after tax asset refinancing expenses of \$14.9 million, or 16¢ per share. The net loss attributable to restricted voting shareholders in the quarter ended July 31, 2007 included an after tax asset impairment charge of \$61.6 million or, 68¢ per share relating to the Carolina and Niagara Burlington discontinued operations.

SEASONAL VARIABILITY OF RESULTS

Historically, the Company's manufacturing and PDS revenues typically have been lower in the first fiscal quarter, being the three months ending January 31. 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; (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, being the three months ended October 31, are also typically impacted by summer shut downs during August in the European operations.

OUTLOOK

Revenues are expected to decline slightly for the first quarter of fiscal 2009 versus the same quarter last year due to strengthening of the US dollar. EBITDA before repositioning expenses in the first quarter is expected to be comparable with the first quarter of 2008, reflecting the normal seasonality in the business due to the December holiday shutdowns and customer purchasing practices around the calendar yearend. These forecasts are subject to the strength of the U.S. dollar relative to the Canadian dollar, euro and pounds sterling.

These expectations are based on internal management forecasts, which in the case of the revenue forecasts, are based on client purchase orders and forecasts of anticipated demand and other factors. These internal management forecasts were prepared for internal planning purposes and may not be appropriate for forecasting future financial results or for other purposes.

The Company indicated in its MD&A for the year ended October 31, 2008 that revenues from continuing operations for fiscal 2008 would be comparable with 2007. Revenues from continuing operations reported in fiscal 2008 were \$83.1 million higher than 2007, representing an increase of 13.1%. Had foreign currency exchange rates remained the same as the prior year, revenues would have increased by approximately 9%.

The Company indicated in its MD&A for the three and nine months ended July 31, 2008 that it anticipated that revenues for the fourth quarter of 2008 would be lower than revenues for the third quarter of 2008 and were subject to fluctuations in the strength of the U.S dollar. Revenues reported in the fourth quarter of 2008 were \$22.9 million lower than the third quarter of 2008, representing a reduction of 11.7%. Had foreign currency exchange rates remained the same as the prior quarter, revenues would have declined by approximately 7%.

LIQUIDITY AND CAPITAL RESOURCES

Summary of Cash flows

The following table summarizes the cash flows for the periods indicated:

Summary of Cash flows

(in thousands of U.S. dollars)	Three months ended October 31,		Year ended October 31,	
	2008	2007	2008	2007
	\$	\$	\$	\$
Income (loss) from continuing operations	41,323	(5,877)	18,102	(34,768)
Depreciation and amortization	12,291	10,994	47,594	41,343
Foreign exchange loss (gain) on debt	2,298	(7,541)	7,015	(12,331)
Foreign exchange loss on foreign operations	-	-	-	858
Accreted interest on convertible preferred shares	2,164	3,573	13,453	7,054
Gain on extinguishment of debt	(34,934)	-	(34,934)	-
Other non-cash interest	146	151	567	1,657
Employee future benefits, net of contributions	(1,287)	(5,169)	(3,165)	(4,846)
Future income taxes	(3,667)	1,426	(12,461)	4,572
Amortization of deferred revenues	(380)	(505)	(1,893)	(2,021)
Stock-based compensation expense	499	52	2,614	220
Other	(482)	1,065	(414)	1,867
Working capital	5,305	18,812	(3,644)	(8,903)
Increase in deferred revenues	582	8	2,683	2,065
Cash provided by (used in) operating activities of continuing operations	23,858	16,989	35,517	(3,233)
Cash provided by (used in) operating activities of discontinued operations	(2,530)	(816)	(9,075)	14,824
Cash provided by operating activities	21,328	16,173	26,442	11,591
Cash used in investing activities of continuing operations	(21,669)	(15,405)	(44,941)	(39,009)
Cash provided by (used in) investing activities of discontinued operations	(8)	(137)	10,431	(929)
Cash provided by financing activities	(7,286)	(14,932)	4,602	4,221
Other	(6,170)	4,362	(6,843)	3,960
Net decrease in cash and cash equivalents during the period	(13,805)	(9,939)	(10,309)	(20,166)

Cash Provided by Operating Activities

Cash provided by operating activities from continuing operations was \$35.5 million in 2008, compared with cash usage of \$3.2 million in 2007. The improvement reflected an increase in earnings before non-cash charges.

Cash used by operating activities of discontinued operations in 2008 was \$9.1 million, compared with a cash surplus of \$14.8 million in 2007. The reduction principally reflected a deterioration in the profitability of the Carolina operations following the genericization of Omnicef®, the major product manufactured in the facility, in May 2007. The cash flows for 2008 include the results of the Niagara-Burlington operations up to January 31, 2008.

Cash Used in Investing Activities

The following table summarizes the cash used in investing activities for the periods indicated:

Cash used in Investing Activities	Three months ended October 31,		Year ended October 31,	
	2008	2007	2008	2007
<small>(in thousands of U.S. dollars)</small>	\$	\$	\$	\$
Additions to capital assets				
Sustaining	(9,479)	(9,074)	(21,600)	(17,425)
Project-related	(12,273)	(5,474)	(34,202)	(17,723)
Total additions to capital assets	(21,752)	(14,548)	(55,802)	(35,148)
Proceeds on sale of capital assets	87	-	12,176	-
Net increase in investments	(4)	(25)	(1,315)	(202)
Increase in deferred pre-operating costs	-	(832)	-	(3,659)
Cash used in investing activities of continuing operations	(21,669)	(15,405)	(44,941)	(39,009)
Cash provided (used in) investing activities of discontinued operations	(8)	(137)	10,431	(929)
Cash used in investing activities	(21,677)	(15,542)	(34,510)	(39,938)

Cash used in investing activities from continuing operations in 2008 was \$44.9 million, compared with \$39.0 million in 2007. The increase principally reflected higher project related expenditures offset by proceeds on the sale of the York Mills property of \$11.9 million.

Cash provided by investing activities from discontinued operations in 2008 was \$10.4 million and included net proceeds from the divestiture of the Niagara-Burlington operations of \$10.5 million.

The Company's principal ongoing investment activities are sustaining and project-related capital programs at its network of sites. The majority of the Company's capital allocation is normally invested in project-related programs, which are defined as outlays that will generate growth in capacity and revenues, while sustaining expenditures relate to the preservation of existing assets and capacity. The Company invested \$55.8 million in capital expenditures in 2008 compared with \$35.1 million in 2007, of which project-related expenditures were \$34.2 million in 2008 and \$17.7 million in 2007.

During 2008, the Company's major project-related programs (in millions) were:

- Toronto Region expansion of high potency capabilities \$5.6
- Whitby manufacturing and PDS expansion to absorb transfers from York Mills \$11.3
- Completion of the intermediate-scale process suite in Cincinnati, U.S.A. \$4.4

Capital commitments to complete authorized capital projects were \$12.5 million at October 31, 2008. Based on current internal projections, these expenditures are expected to be incurred during the fiscal year ending October 31, 2009. These expenditures will be financed from cash flows from operations, existing cash reserves and credit facilities and from a new capital lease that has been negotiated.

Based on current management assessments, projected related capital expenditures in fiscal 2009 are expected to be similar to the amount spent in 2008. The major project-related capital programs currently anticipated for 2009 consist of:

- Completion of capacity expansions in the Whitby and Toronto Region Operations
- Additional pilot scale lyophilization capacity in Ferentino, Italy
- New ERP system in the Canadian operations.

Cash Provided by Financing Activities

The following table summarizes the cash provided by financing activities for the periods indicated:

Cash Provided by Financing Activities

	Three months ended October 31,		Year ended October 31,	
	2008	2007	2008	2007
(in thousands of U.S. dollars)	\$	\$	\$	\$
Increase (decrease) in bank indebtedness	(8,605)	(4,230)	3,196	3,532
Increase in long-term debt	16,504	15,456	40,326	198,108
Repayment of long-term debt	(14,918)	(17,278)	(38,902)	(336,883)
Issue of convertible preferred shares	-	-	-	150,000
Convertible preferred share issue cost-equity component	(269)	-	(269)	(1,213)
Issue of restricted voting shares	3	-	431	24
Repurchase of restricted voting shares	-	(8,778)	-	(8,778)
Cash provided (used in) by financing activities of continuing operations	(7,285)	(14,830)	4,782	4,790
Cash used in financing activities of discontinued operations	(1)	(102)	(180)	(569)
Cash provided by (used in) financing activities	(7,286)	(14,932)	4,602	4,221

All significant financing activities for the year ended October 31, 2008 reflected drawings and repayments on existing credit facilities.

The principal financing activity for the year ended October 31, 2007 was the issue, through a private placement, of \$150 million of convertible preferred shares of the Company to JLL Partners and the completion of new credit facilities in the aggregate amount of \$225 million, comprising of a seven-year \$150 million term loan and a five-year \$75 million revolving facility. The net proceeds from the JLL Partners investment and the seven-year term loan were used to repay the Company's obligations under its previous North American and U.K. credit facilities. In 2007, the Company also used \$8.8 million of cash to repurchase 2,334,300 of its restricted voting shares under a normal course issuer bid.

Financing Arrangements

\$225 Million Credit Facilities

On April 27, 2007 the Company completed new credit facilities in the aggregate amount of \$225 million, comprising a seven-year \$150 million senior secured term loan and a five-year \$75 million asset based revolving credit facility. The Company is required to make quarterly installment payments of \$375,000 on the term loan facility, along with additional mandatory repayments based on certain excess cash flow measures. Interest on the facilities is at floating rates based on LIBOR, US or CAD prime, or the federal funds effective rate, plus applicable margins. The Company has entered into interest rate swaps to convert the interest expense on the \$150 million senior secured term loan from a floating interest rate to a fixed interest rate. The facilities are secured by substantially all of the assets of the Company's operations in Canada, U.S.A., Puerto Rico and the U.K and the Company's investments in the shares of all other operating subsidiaries. Drawings under the revolving credit facility are limited by the level of accounts receivable and inventories; accordingly at October 31, 2008 the maximum amount available under the revolving facility was \$54.7 million. At October 31, 2008 the balance on the senior secured term loan was \$147.8 million and \$14.8 million was drawn on the revolving credit facility, including letters of credit of \$0.3 million.

The senior secured term loan and the senior secured revolving loan each contain a definition of "Change in Control" which includes the acquisition of ownership, directly or indirectly, beneficially or of record, by any person or group (within the meaning of the US Securities Exchange Act of 1934 and the rules of the US Securities and Exchange Commission) other than Permitted Holders (as defined in the agreements), of equity interests representing more than 40% of the aggregate ordinary voting power represented by the issued and outstanding equity interests of the Company. JLL Holdings is a Permitted Holder. A Change in Control would not be triggered by the acquisition by JLL Holdings of restricted voting shares under its proposed offer announced December 8, 2008 for any and all outstanding restricted voting shares of the Company. If a Change in Control were triggered, it would constitute an "Event of Default" which would entitle the lenders by notice to the Company to terminate the commitments and declare the loans to be due and payable.

Convertible Preferred Shares

The \$150 million 8.5% convertible preferred shares purchased by JLL on April 27, 2007 represent 150,000 units, each consisting of one Class I Preferred Share, Series C (a convertible preferred share) and one Class I Preferred Share, Series D (a special voting preferred share) at a purchase price of \$1,000 per unit.

Until October 27, 2009, no cash dividends will be paid, but the liquidation preference and conversion rate will increase on a quarterly basis by 2.125%. After October 27, 2009, these increases in the liquidation preference and conversion rate will continue until the conversion of the convertible preferred shares, unless the Company elects to pay a cash dividend for any applicable quarter, in which case the Company will pay a cash dividend for such quarter based on an annual dividend rate of 8.5% on the aggregate liquidation preference of the convertible preferred shares.

At October 31, 2008, each convertible preferred share was convertible into 237.9072 Patheon restricted voting shares, as adjusted for any non-cash dividends noted above, at any time at the holder's option. The Company will be entitled to require the holder to convert into restricted voting shares if, at any time after October 27, 2009, the market price of the restricted voting shares on the Toronto Stock Exchange exceeds a price equivalent to US\$7.87 for a period of at least 60 days.

At the time of issue, the Company was required to redeem the convertible preferred shares for cash on April 27, 2017, if not previously converted, at a price equal to the aggregate liquidation preference of the convertible preferred shares, plus accrued and unpaid dividends thereon. This cash redemption requirement was eliminated on September 19, 2008 in accordance with an amending agreement with JLL (see "Recent Developments"). The Company is still required to redeem the convertible preferred shares upon the occurrence of a change of control of Patheon at a price equal to the greater of the aggregate liquidation preference of the convertible preferred shares, plus accrued and unpaid dividends thereon, or the price per share paid to holders of restricted voting shares in the change of control transaction, multiplied by the number of restricted voting shares into which the convertible preferred shares are then convertible.

The convertible preferred shares have the right to vote, together with the holders of the restricted voting shares, on an as-if converted basis, in respect of all matters other than the election of directors. As at October 31, 2008, these convertible preferred shares were convertible into 35.7 million restricted voting shares of the Company, which would represent approximately 28% of the restricted voting shares outstanding as at that date, after giving effect to such conversion. The special voting preferred shares have the right to appoint up to three directors.

Following the elimination of the cash redemption requirements, the convertible preferred shares have been classified as equity, with the carrying value of \$149.2 million being based on the fair market value on September 19, 2008 adjusted upwards for non-cash dividends earned.

Prior to the elimination of the cash redemption on September 19, 2008, the convertible preferred shares were considered to be a compound financial instrument with both a debt and equity component. On issuance, the fair value of the debt component was \$132.9 million. The remainder of the proceeds, attributable to shareholders' equity was \$15.9 million, net of apportioned transaction costs of \$1.2 million. At October 31, 2007 the carrying value of the debt component of the convertible preferred shares was \$139.9 million.

Financing Ratios

Total interest bearing debt at October 31, 2008 was \$219.6 million, being \$143.8 million lower than at October 31, 2007. The amount at October 31, 2007 included the debt component of the convertible preferred shares of \$139.9 million, which was reclassified to be included in equity as a result of the elimination of the cash redemption provision. At October 31, 2008, the Company's consolidated ratio of interest-bearing debt to shareholders' equity was 91%, compared with 184% at October 31, 2007. The decrease principally reflects the reclassification of the debt component of convertible shares to equity.

The following table summarizes the fixed and variable percentages of debt outstanding at October 31, 2008 and 2007, after taking into account the impact of interest rate swap contracts that the Company has entered into, and the applicable interest rates at the end of each quarter in 2008. The amounts at October 31, 2007 include the debt component of the convertible preferred shares.

	% of Debt Outstanding		Interest Rates at End of Each Quarter in 2008			
	2008	2007	Q4	Q3	Q2	Q1
Fixed rate	70%	81%				
Variable rate based on:						
U.S. LIBOR (1 month)	5%	1%	2.58%	2.46%	2.80%	3.14%
Euribor (3 months)	24%	18%	4.76%	4.97%	4.86%	4.37%
U.K. LIBOR	1%	0%	5.84%	5.78%	5.84%	5.58%

Contractual Obligations

Contractual repayments of long-term debt, commitments under operating leases and purchase obligations are as follows:

<i>(in thousands of U.S. dollars)</i>	Payments Due by Period				
	Total	Less Than 1 Year	1-3 Years	4-5 Years	After 5 Years
	-				
Long-term debt	213,467	10,230	20,562	33,074	149,601
Operating leases	14,727	3,288	4,846	2,611	3,982
Purchase obligations	12,532	12,532	-	-	-
Total contractual obligations	240,726	26,050	25,408	35,685	153,583

Long-term debt includes capital lease obligations. Purchase obligations relate to capital commitments to complete authorized capital projects.

Obligations with Respect to Employee Future Benefit Plans

The Company's obligations as at October 31, 2008 with respect to employee future benefit plans were:

<i>(in thousands of U.S. dollars)</i>	Defined Benefit Pension Plans	Other Benefit Plans	Total
Projected benefit obligations	62,508	4,114	66,622
Less plan assets	(49,471)	-	(49,471)
Unfunded amount	13,037	4,114	17,151
Unrecognized past service costs and net actuarial losses	(8,696)	325	(8,371)
Unamortized past service costs	(281)	-	(281)
Amount included in other long-term liabilities	4,060	4,439	8,499

Based on current information available from actuarial estimates, the Company anticipates that contributions required under its defined benefit pension plans for the year ended October 31, 2009 will be approximately \$5.5 million, this compares with contributions of \$6.4 million that were made in the year ended October 31, 2008. Required contributions to defined benefit pension plans in future years will be dependent upon a number of variables, including the long-term rate of return on plan assets. The amount that the Company will be required to contribute to such plans in the future may vary.

Off-balance Sheet Arrangements

The Company does not engage in off-balance sheet accounting to structure any of its financial arrangements. The Company does not have any interests in unconsolidated special-purpose or structured finance entities.

Adequacy of Financial Resources

The Company has long term financing in place with relatively limited covenant requirements and at October 31, 2008, the Company was in compliance with all covenant requirements under its financing arrangements. Based on the Company's internal financial projections, it anticipates that it will remain in compliance with these covenant requirements in fiscal 2009. The Company believes that, subject to usual business risks as further described in the Risk Factors section below, its financial resources are sufficient to fund projected capital expenditures, debt service requirements and employee future benefit obligations in the normal course of business. As at October 31, 2008, the Company had cash balances of \$20.2 million and \$59.2 million in undrawn credit facilities available to it.

ADDITIONAL INFORMATION

Share Capital

As of November 30, 2008, the Company had outstanding 91,149,388 restricted voting shares and 150,000 Class I preferred shares consisting of 150,000 Class I Series C convertible preferred shares and 150,000 Class I Series D special voting shares. At October 31, 2008 the Company had 5,987,965 stock options outstanding of which 2,947,093 were exercisable.

As of November 30, 2008 the Company also had outstanding 150,000 Class I Preferred Share, Series C (a convertible preferred share) and 150,000 Class I Preferred Share, Series D (a special voting preferred share). For further information concerning these preferred shares please see "Liquidity and Financial Resources – Financing Arrangements" above.

Related Party Transactions

Revenues from companies controlled by Mr. Joaquin Viso, a director and significant shareholder of the Company, were in the amount of \$0.3 million in 2008 (2007 - \$0.5 million). These transactions were conducted in the normal course of business and are recorded at the exchanged amount. Accounts receivable at October 31, 2008 includes a balance of \$0.1 million (2007 - \$0.4 million) with respect to these related party transactions.

At October 31, 2008 the Company has an investment of \$1.7 million (2007 - \$0.7 million) representing an 18% interest in two Italian companies (collectively referred to as "BSP Pharmaceuticals") whose largest investor is Mr. Aldo Braca, an officer of the Company. These companies specialize in the manufacturing of cytotoxic pharmaceutical products. The Company accounts for its investment in BSP Pharmaceuticals using the equity method. 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 year ended October 31, 2008, the Company has recorded an investment loss of \$0.1 million.

Management services and other fees charged to BSP Pharmaceuticals under a management services agreement for the year ended October 31, 2008 were \$2.5 million (2007 - \$1.6 million). Accounts receivable at October 31, 2008 include a balance of \$0.2 million (October 31, 2007 – \$1.6 million) 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.

RISK FACTORS, ACCOUNTING POLICIES AND ESTIMATES

RISK FACTORS

Certain risk factors that may affect Patheon are described below. These risks and uncertainties are not the only ones facing Patheon. Additional risks and uncertainties not currently known to Patheon, or that Patheon currently considers immaterial, may also impair the operations of Patheon.

International Operations and Foreign Currency Fluctuations

Patheon's operations are subject to the risks of doing business in several countries in North America and Europe, including, but not limited to, foreign currency fluctuation, varying economic and political conditions, cultures and business practices, tax rates, and costs of compliance with laws of a variety of countries. There can be no assurance that these factors will not have an adverse effect on business, financial conditions and results of operations of Patheon. For example, the strengthening of the U.S. dollar vis-a-vis the euro could have a negative impact on the Company's consolidated financial results.

Customer Demand for Patheon's Services

The amount of customer spending on pharmaceutical development and production has a large impact on the Company's sales and profitability, particularly the amount its customers choose to spend on outsourcing. Consolidation in the industries in which its customers operate may have an impact on such spending as customers integrate acquired operations, including research and development departments and manufacturing. Many of its customers finance their research and development spending from private and public sources. A reduction in spending by its customers on outsourcing of services offered by Patheon could have a material adverse effect on Patheon's business, financial condition and results of operations.

Patheon is dependent on demand for the products it manufactures on behalf of its customers and on the ability of its customers to obtain regulatory approval and successfully market and obtain third party coverage and reimbursement for their products. Demand for customers' products can be adversely affected by, among other things, delays in health regulatory approval, the loss of patent protection, the emergence of competing products, the degree to which private and government drug plans subsidize payment for a particular product and changes in the marketing strategies for such products. Competing generic products often emerge as a product approaches the end of its patent-protection period. Patheon's revenues for fiscal 2006, 2007, and 2008 were negatively impacted by the loss of patent protection for Zocor[®] and the emergence of generic competition for Omnicef[®] in May 2007.

Patheon may be materially adversely affected by any reduction in market demand for any significant products that Patheon manufactures for its customers. There can be no assurance that production volumes of key products and related revenues will be maintained or that changes in product mix will not materially adversely affect profitability.

Regulatory Matters Affecting Manufacturing and Pharmaceutical Development Services

Patheon is required to comply with the regulatory requirements of the national and international regulatory bodies having jurisdiction in the countries where the Company manufactures products or where its customers' products are distributed. In particular, Patheon is subject to laws and regulations concerning good manufacturing practices and drug safety. As a result, most of Patheon's facilities are subject to regulation by the FDA of the United States, and certain of Patheon's facilities are subject to regulation by the Health Products and Food Branch ("HPFB") of Health Canada in Canada, the Medicines and Healthcare Products Regulatory Agency ("MHRA") of the United Kingdom, the European Medicines Evaluation Agency ("EMA") of the European Union, and other regulatory bodies. These regulatory requirements impact many aspects of Patheon's operations, including manufacturing, labelling, packaging, storage and record keeping related to customers' products.

In addition, if new legislation or regulations are enacted or existing legislation or regulations are amended or are interpreted or enforced differently, Patheon may be required to obtain additional approvals or operate according to different manufacturing standards. This may require Patheon to change its manufacturing techniques or make capital improvements to its facilities. There can be no assurance that Patheon will be able to meet all of the applicable regulatory requirements in the future. If Patheon fails to comply with applicable regulatory requirements, it may be subject to warning letters, fines,

suspension or withdrawal of regulatory approvals, product recalls, seizure of products, debarment, exclusion, disgorgement of profits, operating restrictions and criminal prosecution, as well as the loss of contracts and resulting revenue losses. In addition, such failure to comply could expose Patheon to contractual and product liability claims, including claims by customers for reimbursement for lost or damaged active pharmaceutical ingredients, the cost of which could be significant.

Patheon's pharmaceutical development and manufacturing projects often involve products that must undergo safety and clinical evaluations before they are approved as commercial therapeutic products. The regulatory authorities having jurisdiction in the countries in which the Company's customers intend to market their products may delay approval of a product or determine that the product is not approvable. There can be no assurance that the pharmaceutical development projects and their related revenues for Patheon will be maintained. For example, on November 26, 2008, Johnson & Johnson Pharmaceutical Research & Development, L.L.C. ("J&JPRD") announced that it received a Complete Response letter from the FDA regarding its New Drug Application ("NDA") for ceftobiprole for the treatment of complicated skin and skin structure infections, including diabetic foot infections. The FDA indicated that they could not approve the NDA for ceftobiprole at that time. They asked J&JPRD to conduct additional audit work of clinical investigator sites and to address specific questions related to site monitoring. Ceftobiprole has been approved in Canada and in Switzerland and the Committee for Medicinal Products for Human Use of the EMEA has recommended approval of ceftobiprole in the European Union for the treatment of complicated skin and soft tissue infections. These developments may affect volumes of ceftobiprole to be manufactured by Patheon at its Swindon facility.

Pharmaceutical products commercially manufactured by Patheon are subject to ongoing regulatory review following the receipt of marketing authorization. The regulatory authorities having jurisdiction in the country in which the product is marketed may withdraw the marketing authorization, either temporarily or permanently, for health or safety concerns related to the use of the product. The subsequent discovery of previously unknown problems with any of Patheon's customers' products may result in restrictions on the product, including withdrawal of the product from sale. There can be no assurance that production volumes of key products and related revenues for Patheon will be maintained.

Although Patheon believes that it is in compliance, in all material respects, with applicable laws and regulations, there can be no assurance that a regulatory agency or tribunal would not reach a different conclusion concerning the compliance of Patheon's operations with applicable laws and regulations. In addition, there can be no assurance that Patheon will be able to maintain or renew existing permits, licences or other approvals or obtain, without significant delay, future permits, licences or other approvals needed for the operation of its businesses. Any non-compliance by Patheon with applicable laws and regulations, or the failure to maintain, renew or obtain necessary permits and licences, could have an adverse effect on its results of operations and financial condition.

Exposure to Complex Production Issues

The services Patheon offers are highly exacting and complex, due in part to strict regulatory requirements. From time to time, problems may arise in connection with facility operations or during preparation or provision of products, in both cases for a variety of reasons including equipment malfunction, failure to follow specific protocols and procedures, problems with raw materials and environmental factors. Such problems could affect production of a particular batch or series of batches, requiring the destruction of product, or could halt facility production altogether. This could, among other things, lead to increased costs, lost revenue, damage to customer relations, reimbursement to customers for lost active pharmaceutical ingredients, time and expense spent investigating the cause and, depending on the cause, similar losses with respect to other batches or products. If problems are not discovered before the product is released to the market, recall and product liability costs may also be incurred.

Substantial Financial Leverage

Patheon's total interest-bearing debt as at October 31, 2008 was \$219.6 million, and its consolidated financial leverage ratio (the ratio of total interest-bearing debt to equity) was 0.91:1.0.

While the Company believes that its 2007 credit facility together with the investment by JLL have provided it with critical financial certainty and stability going forward, the Company's substantial financial leverage poses risks to it. Debt service requirements in future periods may be higher than in prior years as a result of a number of factors, including increased borrowing and increases in floating interest rates. In addition, the Company may incur substantial fees from time to time in connection with debt amendments or refinancing. If Patheon's cash flow is not sufficient to service its debt and adequately

fund its business, it may be required to seek further additional financing or refinancing, or to dispose of assets. There is no assurance that any of these alternatives could be effected on satisfactory terms, or at all. In addition, Patheon's financial leverage could adversely affect its ability to raise additional capital to fund its operations and could impair its ability to respond to operational challenges, changing business and economic conditions and new business opportunities, and may make it vulnerable in the event of a downturn in its business.

Interest Rate Risks

The Company has exposure to movements in interest rates. The Company has entered into interest rate swaps to convert the interest expense on the \$150 million senior secured term loan from a floating interest rate to a fixed interest rate until June 2010. Taking this interest rate swap into account, as at October 31, 2008, 30% 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 a approximate impact of \$0.7 million on pre-tax income.

Potential Environmental, Health and Safety Liabilities

Patheon's operations are subject to a variety of environmental, health and safety laws and regulations in each of the jurisdictions in which it operates. These laws and regulations govern, among other things, air emissions, wastewater discharges, the handling and disposal of hazardous substances and wastes, soil and groundwater contamination and employee health and safety. Any failure by Patheon to comply with environmental, health and safety requirements could result in the limitation or suspension of production or subject the Company to monetary fines or civil or criminal sanctions, or other future liabilities.

The facilities in Puerto Rico have been utilized over a period of years as manufacturing facilities and have certain known or potential conditions that may require remediation in the future. There can be no assurance that remediation costs will not be material or that these costs will be covered by contractual indemnity or that Patheon will be able to successfully enforce any such indemnity in the future. In the event of the discovery of new or previously unknown contamination at one of its facilities, the Company may be required to take additional, unplanned remedial measures for which no accounting reserves have been recorded.

Credit and Customer Concentration

During the fiscal years ended October 31, 2007 and 2008, no single customer accounted for more than 15% of Patheon's total revenues in its pharmaceutical development services business segment or in its commercial manufacturing business segment. Notwithstanding this, in the fiscal year ended October 31, 2008, Patheon's top twenty customers accounted for approximately 70% of the Company's commercial manufacturing revenue. This customer concentration increases credit risk and other risks associated with particular customers and particular products, including risks related to market demand for customer products, regulatory and other operating risks. The Company's earnings were significantly adversely affected commencing in fiscal 2007 as a result of the significant loss of revenues from products manufactured at the Caguas and Carolina facilities in Puerto Rico, including a product that lost significant market share as a result of stability-related issues and another product that lost significant market share as a result of the emergence of generic competition. Disruptions in the production of major products could materially adversely impact Patheon's results of operations in the future.

Patheon believes that the risks related to its reliance on its major customers are reduced by a number of factors, including:

- (a) the negotiation of long-term manufacturing agreements with these customers;
- (b) the diversity of products and projects undertaken by Patheon: in fiscal 2008, Patheon manufactured approximately 695 products in connection with more than 2,200 stock keeping units across a wide range of therapeutic categories and dosage forms; and
- (c) the expansion of PDS units in both Europe and North America: by increasing the variety of service activities, Patheon is increasing its customer base, thereby lowering the risk of depending on a small number of customers for a significant portion of its revenues.

Competition

Some of Patheon's competitors may have substantially greater financial, marketing, technical or other resources than Patheon. Additional competition may emerge and may, among other things, result in a decrease in the fees paid for services, which would affect the profitability of Patheon.

One of the many factors affecting competition is the current excess of capacity, within the pharmaceutical industry generally, of facilities capable of manufacturing drugs in solid and semi-solid dosage forms. Thus, customers currently have a wide range of supply alternatives for these dosage forms. Another factor is a relatively recent development, where an increasing number of companies in Asia, particularly India, have been entering the pharmaceutical contract manufacturing and pharmaceutical development service sectors over the last few years and have been proceeding with obtaining FDA approval for some of their plants as well as acquiring additional plants in Europe and North America. One or more of these companies may become a significant competitor to Patheon. Patheon may also compete with the internal operations of pharmaceutical and biotechnology companies that choose to source manufacturing services internally.

Competition is driven by know-how, consistency of operational performance, quality, price, value and speed. For this reason, Patheon has introduced a number of performance enhancement programs including "Patheon Advantage™", "One Patheon", and its "Quick to Clinic™," and "Quick to Market™" programs.

Rapid Technological Change

The healthcare industry is characterized by rapid technological change. Demand for the Company's services may change in ways it may not anticipate because of evolving industry standards or as a result of evolving customer needs that are increasingly sophisticated and varied, or because of the introduction by competitors of new services and technologies. Innovations aimed at offering enhanced or new services generally may require a substantial investment before the Company can determine their commercial viability, and Patheon may not have the financial resources to fund such initiatives. Even if Patheon were to succeed in creating new services or technologies, they may not produce revenues in excess of the costs of development and they may be quickly rendered obsolete by changing customer preferences or by technologies or features offered by its competitors.

Product Liability Claims

Patheon may be named as a defendant in product liability lawsuits, which may allege that products or services it has provided have resulted or could result in an unsafe condition or injury to consumers. Such lawsuits could be costly to defend and could result in reduced sales, significant liabilities and diversion of management's time, attention and resources. Even claims without merit could subject Patheon to adverse publicity and require it to incur significant legal fees.

Historically, Patheon has sought to manage this risk through the combination of product liability insurance and contractual indemnities and liability limitations in its agreements with customers and vendors. In the past, Patheon has been able to obtain liability insurance for the operation of its businesses. However, there can be no assurance that existing liability insurance will be adequate or that it will be able to be maintained or that all possible claims that may be asserted against Patheon will be covered by insurance. A partially or completely uninsured claim, if successful and of sufficient magnitude, could have a material adverse effect on Patheon's financial condition and its results of operations.

Intellectual Property

Patheon relies on unpatented proprietary know-how and continuing technological innovation in providing pharmaceutical development and commercial manufacturing services. Although Patheon requires its employees to enter into confidentiality agreements prohibiting them from disclosing its proprietary information or technology, these agreements may not provide meaningful protection for Patheon's trade secrets and proprietary know-how. Further, people who are not party to confidentiality agreements may obtain access to Patheon's trade secrets or know-how. Others may independently develop similar or equivalent trade secrets or know-how. If Patheon's proprietary information is divulged to third parties, including its competitors, Patheon's competitive position could be harmed.

Significant Shareholder

An affiliate of JLL Partners, namely, JLL Holdings, owns convertible preferred shares of the Company with voting rights in respect of matters to be voted on by Patheon shareholders other than the election of directors. As at October 31, 2008, these convertible preferred shares were convertible into approximately 35.7 million restricted voting shares of the Company, which, together with the 1.7 million restricted voting shares held by JLL Holdings as at the same date, would represent approximately 29% of the restricted voting shares outstanding as at the same date, after giving effect to such conversion. JLL Holdings also owns special voting preferred shares that currently entitle it to elect three members of Patheon's Board of Directors.

In connection with the investment by JLL Partners in Patheon shares on April 27, 2007, the Company entered into an investor agreement with JLL Holdings. Under the investor agreement, the Company currently requires the approval of JLL Holdings before the Company undertakes certain actions, including share issuances, the payment of dividends, share repurchases, any merger, consolidation or sale of all or substantially all of the Company's assets or a similar business combination transaction, and the incurrence of certain indebtedness in excess of \$20 million.

The Company and JLL Holdings entered into the JLL Agreement pursuant to which JLL Holdings waived the requirement that the Company redeem for cash all of the convertible preferred shares on April 27, 2017 in exchange for both the issuance of additional restricted voting shares and the ability for JLL Holdings to also acquire, through the facilities of the Toronto Stock Exchange, over a one-year period, up to 1.26 million restricted voting shares.

JLL Partners (through JLL Holdings) exercises significant influence over Patheon as a result of its voting rights and its rights under the afore-mentioned investor-related agreements, and, as a result, JLL Partners may have the ability to influence strategic decisions of Patheon. As a significant shareholder of Patheon, JLL Partners is focussed on the enhancement of shareholder value generally. However, the interests of JLL Partners could conflict with the interests of other shareholders. This concentration of ownership and JLL Partners' rights may prevent a change of control of the Company that might be considered to be in the interests of shareholders. In addition, if Patheon is unable to obtain requisite approvals from JLL Partners, the Company may be prevented from executing critical elements of its business strategy.

Supply Arrangements

In many instances, Patheon relies on its customers to supply the active pharmaceutical ingredients necessary to manufacture pharmaceutical products. Any failure by a customer to supply an active pharmaceutical ingredient for a pharmaceutical product on a timely basis may negatively impact Patheon's ability to produce such product and may negatively impact the revenues that Patheon generates from such product.

Patheon depends on various active pharmaceutical ingredients, components, compounds, raw materials, and energy supplied primarily by third parties. It is possible that any of its supplier relationships could be interrupted due to natural disasters, international supply disruptions caused by geopolitical issues or other events or could be terminated in the future. Any sustained interruption in the Company's receipt of adequate supplies could have an adverse effect on its financial results. In addition, while the Company has processes intended to reduce volatility in component and material pricing, it may not be able to successfully manage price fluctuations. Price fluctuation or shortages may have an adverse effect on the results of operations. For example, in 2008, a significant increase in the price of energy adversely impacted the results of operations.

Pension Plans

Certain of Patheon's employees in Canada, France and the United Kingdom are participants in defined benefit pension plans which it sponsors. As of October 31, 2008, the unfunded pension liability on its pension plans was approximately \$13.0 million. The amount of future contributions to its defined benefit plans will depend upon asset returns and a number of other factors and, as a result, the amount the Company will be required to contribute to such plans in the future may vary. Such cash contributions to the plans will reduce the cash available for the Company's business.

Derivative Financial Instruments

Patheon enters into interest rate swaps and foreign exchange forward contracts to limit its exposure to changes in variable interest rates and in foreign exchange rates. The Company is exposed to credit-related losses which could impact the results of operations in the event of non-performance by the counterparties to such instruments.

Exposure to Foreign Currency Risk

The activities of Patheon 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 and British sterling for the European countries.

Since the European and U.S. operations conduct business principally in their respective local currencies, the exposure to foreign currency gains and losses is not significant. However, revenues and operating expenses of the Canadian operations are transacted in Canadian and U.S. dollars. As a result, significant long-term strengthening of the Canadian dollar against the U.S. dollar could adversely affect the profitability of the Canadian operations of Patheon and its consolidated financial results, subject to the ability to increase prices for services or to reduce costs. Based on the Company's current U.S. denominated net inflows in Canada, as at October 31, 2008, fluctuations of +/- 5% in exchange rates, would, all else being equal, have an effect on EBITDA before repositioning expenses of approximately \$5.3 million, prior to hedging activities.

The Canadian operations carry a significant amount of U.S. dollar denominated debt, all of which has been designated as a hedge against the Company's investments in subsidiaries in the United States and Puerto Rico. There can be no assurances that it will be possible for the Company to engage in hedging transactions in the future or that current or future hedging transactions, if entered into, will eliminate foreign currency risk.

Risks Associated with Information Systems

Patheon relies on information systems in its business to obtain, rapidly process, analyze and manage data to:

- facilitate the manufacture and distribution of thousands of inventory items to and from its facilities;
- receive, process and ship orders on a timely basis;
- manage the accurate billing of and collections from customers;
- manage the accurate accounting for and payment to vendors; and
- schedule and operate its global network of manufacturing and development facilities.

Its results of operations could be adversely affected if these systems are interrupted, damaged by unforeseen events or fail for any extended period of time, including due to the actions of third parties.

Dependence Upon Key Management Personnel and Executives

Patheon is dependent upon the continued support and involvement of a number of key management personnel. The loss of the services of one or more of such personnel could have a material adverse effect on the business. Patheon's ability to manage its business activities and, hence, its success, will depend in large part on the efforts of these individuals. There can be no assurance that Patheon will be able to continue to attract and retain such personnel.

CHANGES IN ACCOUNTING POLICY

New Accounting Policies Adopted in 2008

Effective November 1, 2007 the Company adopted the Canadian Institute of Chartered Accountants (The "CICA") Handbook Section 1535 "Capital Disclosures", Section 3862 "Financial Instruments – Disclosures", Section 3863 "Financial Instruments – Presentation" and Section 1506 "Accounting Changes". The adoption of the new standards resulted in additional disclosures in the notes to the consolidated financial statements only.

Future Changes in Accounting Policies

Inventories

The CICA issued a new accounting standard, Section 3031 “Inventories”, which requires inventory to be measured at the lower of cost and net realizable value. The standard provides guidance on the types of costs that can be capitalized and requires reversal of previous inventory write-downs if economic circumstances have changed to support the higher inventory values. The Company will adopt this standard beginning November 1, 2008 on a prospective basis and the expected impact on the Company’s financial statements will be an increase to inventory of approximately \$2.9 million with a corresponding decrease in the deficit account, after adjusting for income taxes.

Goodwill, Intangible Assets and Financial Statement Concepts

The CICA has issued a new accounting standard, Section 3064 “Goodwill and Intangible Assets”, which clarifies that costs can be deferred only when they relate to an item that meets the definition of an asset, and as a result, start-up costs must be expensed as incurred. Section 1000 “Financial Statement Concepts”, was also amended to provide consistency with this new standard. The new and amended standards are effective for the Company beginning November 1, 2009. The Company has deferred costs of \$5.3 million which will be written off to the deficit account in the beginning of fiscal year 2009. No additional costs were capitalized during fiscal year 2008 and the Company incurred \$2.1 million in amortization charges during the year.

General Standards of Financial Statement Presentation

The CICA amended Section 1400 “General Standards of Financial Statement Presentation”, to include requirements to assess and disclose an entity’s ability to continue as a going concern. The Company will adopt the amendments to this standard beginning November 1, 2008. The adoption of the new standard will result in additional disclosures in the notes to the consolidated financial statements.

International Financial Reporting Standards

In February 2008, the Canadian Accounting Standards Board announced the adoption of International Financial Reporting Standards (“IFRS”) for publicly accountable enterprises. Patheon will be required to adopt IFRS no later than November 1, 2011. The Company is currently evaluating the effects of adopting these standards.

ACCOUNTING ESTIMATES

General

The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. These estimates and assumptions are based upon management’s historical experience and are believed by management to be reasonable under the circumstances. Such estimates and assumptions are evaluated on an ongoing basis and form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results could differ significantly from these estimates.

The following is a summary of certain accounting estimates and policies considered critical by the management of the Company.

Impairment of Long-lived Depreciable Assets

The Company reviews whether there are any indicators of impairment of its capital assets and identifiable intangible assets (“long-lived depreciable assets”). If such indicators are present, the Company assesses the recoverability of the assets or group of assets by determining whether the carrying value of such assets can be recovered through undiscounted future cash flows. If the sum of undiscounted future cash flows is less than the carrying amount, the excess of the carrying amount over

the estimated fair value, based on discounted future cash flows, is recorded as a charge to earnings. The Company did not record an impairment charge in 2008.

Goodwill

Goodwill represents the excess of the purchase price of the Company's interest in subsidiary companies over the fair value of the underlying net identifiable assets arising on acquisitions. Goodwill is not subject to amortization but is subject to an annual review for impairment, or more frequently if events or changes in circumstances indicate that goodwill is impaired. Goodwill impairment is assessed based on a comparison of the fair value of an individual reporting unit to the underlying carrying value of the reporting unit's net assets including goodwill. When the carrying amount of the reporting unit exceeds its fair value, the fair value of the reporting unit's goodwill, determined in the same manner as in a business combination, is compared with its carrying amount to measure the amount of the impairment loss, if any. The Company did not record a goodwill impairment charge in 2008.

Asset Impairment – Discontinued Operations

Long-lived assets held for sale in connection with the Carolina discontinued operations are measured at the lower of their carrying amount or fair value less cost to sell. Fair value reflects management's best estimate of the proceeds it will receive for the assets based on discussions and negotiations with interested parties. In 2008 the Company recorded a charge of \$7.7 million to write down the carrying value of the Carolina long-lived assets to their fair market value, less estimated costs to sell.

Convertible Preferred Shares

The carrying value of the convertible preferred shares recorded in shareholders equity represents their fair value less transaction costs on September 19, 2008, when the JLL Agreement was completed (see "Recent Developments"), plus the value of subsequent paid-in-kind dividends.

The fair value of the preferred shares on September 19, 2008 was determined based on a binomial valuation model which calculates an overall value based on the underlying value drivers of the convertible security; conversion value, fixed income value and option value. The fair value of the preferred shares less transaction costs on September 19, 2008 was deemed to be \$147.7 million.

Reserve for Doubtful Accounts

The Company establishes an appropriate provision for non-collectible or doubtful accounts. Estimates of recoverable amounts are based on best estimates of the amount a customer will settle its obligation for. Actual amounts received may be affected by various factors, including the resolution of amounts owing for disputed services and the customers financial condition. At October 31, 2008 the Company had a reserve for doubtful accounts of \$1.0 million.

Employee Future Benefits

The Company provides defined benefit pension plans to certain employees in its Canadian, UK and French operations and post employment health and dental coverage to certain of its Canadian employees.

The determination of the obligation and expense for defined benefit pensions and other post-employment benefits is dependent on the selection of certain assumptions used by actuaries in calculating such amounts. The assumptions used in determining the accrued benefit obligation and the benefit expense as at and for the year ended October 31, 2008 are as follows:

	Defined Benefit Pension Plans	Other Benefit Plans
	%	%
Accrued benefit obligation		
Discount rate	6.6	7.0
Rate of compensation increase	4.2	-
Benefit costs recognized		
Discount rate	6.1	5.8
Expected long-term rate of return on plan assets	7.3	-
Rate of compensation increase	4.1	-

A 4% to 12% annual rate of increase in the per capita cost of covered health care and dental benefits was assumed for 2008, with the rate assuming to decrease gradually over the next five years to 6% and to remain at that level thereafter. The following table outlines the effects of a one-percentage-point increase and decrease in the assumed health care and dental benefit trend rates.

	Benefit Obligation	Benefit Expense
<i>(in thousands of U.S. Dollars)</i>	\$	\$
Impact of:		
1% increase	555	45
1% decrease	(416)	(49)

Stock Based Compensation

The Company uses the fair value method of accounting for stock-based compensation. The fair value of the options are estimated using the Black-Scholes option pricing model using estimated stock volatility, expected life of the options and the risk-free interest rate.

Income Taxes

The Company follows the liability method of income tax allocation. Under this method, future tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using the substantively enacted tax rates and laws that will be in effect when the differences are expected to reverse.

Preparation of the consolidated financial statements requires an estimate of income taxes in each of the jurisdictions in which the Company operates. The process involves an estimate of the Company's current tax exposure and an assessment of temporary differences resulting from differing treatment of items such as depreciation and amortization for tax and accounting purposes. These differences result in future tax assets and liabilities and are reflected in the consolidated balance sheet.

Future tax assets of \$34.7 million have been recorded at October 31, 2008. This consists primarily of accounting provisions related to pension and post-retirement benefits not currently deductible for tax purposes, the tax benefit of net operating loss carryforwards related to the U.K. operations, unclaimed R&D expenditures and deferred financing and share issue costs. The

Company evaluates quarterly the ability to realize its future tax assets. The factors used to assess the likelihood of realization are the Company's forecast of future taxable income and available tax planning strategies that could be implemented to realize the future tax assets. The future tax assets recorded at October 31, 2008 are net of a valuation allowance of \$22.8 million.

Future tax liabilities of \$39.1 million have been recorded at October 31, 2008. This liability has arisen primarily on tax depreciation in excess of book depreciation.

The Company's tax filings are subject to audit by taxation authorities. Although management believes that it has adequately provided for income taxes based on the information available, the outcome of audits cannot be known with certainty and the potential impact on the financial statements is not determinable.

EFFECTIVENESS OF DISCLOSURE CONTROLS AND INTERNAL CONTROLS

Disclosure controls and procedures are designed to provide reasonable assurance that all relevant information is gathered and reported to senior management, including the Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO"), on a timely basis so that appropriate decisions can be made regarding public disclosure. An evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures was conducted as of October 31, 2008 by and under the supervision of the Company's management, including the CEO and the CFO. Based on this evaluation, the CEO and the CFO have concluded that the Company's disclosure controls and procedures (as defined in Multilateral Instrument 52-109 – Certification of Disclosure in Issuers' Annual and Interim Filings of the Canadian Securities Administrators) are effective to ensure that the information required to be disclosed in reports that the Company files or submits under Canadian securities legislation is recorded, processed, summarized and reported within the time periods specified in such legislation.

Under the supervision of the CEO and CFO, the Company has designed internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP. This design evaluation included documentation activities, management inquiries and other reviews as deemed appropriate by management in consideration of the size and nature of the Company's business. There were no changes in the Company's internal controls over financial reporting during the most recent interim period that have materially affected, or are reasonably likely to materially affect, its internal control over financial reporting.