



NEWS RELEASE – for Immediate Release

Source: Patheon Inc.

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PATHEON REPORTS THIRD QUARTER 2008 RESULTS

Revenue advances 18% (12% in local currencies) over prior year

TORONTO, Canada, (September 5, 2008) – Patheon (TSX:PTI) today announced its results for the third quarter ended July 31, 2008 with revenue of \$195.0 million, 18% higher than last year (12% in local currencies), and EBITDA before repositioning expenses of \$24.7 million versus \$20.6 million in the prior year. The current year EBITDA growth was achieved after absorbing incremental costs of \$3.3 million related to a previously announced early retirement program in Cincinnati, a \$1.3 million non-cash foreign exchange loss (versus a \$3.6 million gain in the prior year) and operating expenses associated with a wide range of initiatives related to the restructuring of the Company.

“This quarter we experienced strong revenue growth from a broad base of existing customers. In addition we continued to improve the underlying profitability of the operations, the benefits of which are somewhat masked by our near term restructuring actions,” said Wes Wheeler, President and Chief Executive Officer, Patheon Inc. “Our focus this quarter was to implement people, process and operational changes to build a great company. Many of these initiatives required additional spending in the quarter. To date we’ve invested in global training of staff in our Patheon Advantage™ (LeanSixSigma) program, reduced headcount with severance programs to streamline operations, continued to build our executive team and entered into an agreement to change the terms of our Preferred Shares that will simplify our financial reporting and will eliminate a major source of foreign exchange volatility. All of these initiatives are important elements of our turnaround strategy.”

Third Quarter 2008 Operating Results from Continuing Operations

Consolidated revenue increased 18% (12% in local currencies) to \$195.0 million over the prior year consolidated revenue of \$164.8 million.

Commercial Manufacturing revenues increased 15% year-over-year to \$157.3 million driven by strong growth in Europe's existing business base. Revenue increased at all North America locations with the exception of Cincinnati, which was impacted by customer related raw material supply constraints.

Pharmaceutical Development Services (PDS) Q3 2008 revenues increased 32% year-over-year to \$37.7 million, with both North America and Europe experiencing strong growth as a result of higher order backlog from contracts signed in the second quarter. "The PDS business growth is a clear demonstration that we offer a unique blend of services that our customers require. We offer talented staff that includes 100 PhD's in six development facilities, most of which are co-located with sophisticated commercial manufacturing equipment" said Wes Wheeler.

Consolidated EBITDA before repositioning expenses was \$24.7 million for an EBITDA margin of 12.7% in the third quarter, compared with \$20.6 million for an EBITDA margin of 12.5% in the same period last year. The current period includes non-cash net foreign exchange losses on U.S. dollar denominated debt in Canada of \$1.3 million compared with a gain of \$3.6 million for the same period last year. Additional costs were incurred during the quarter in connection with recruiting executive and senior management positions, consulting fees related to new operational and strategic initiatives, and severance costs.

EBITDA before repositioning expenses for the global commercial operations was \$21.7 million in the third quarter of 2008, \$6.8 million higher than the same period in 2007. EBITDA growth was achieved across all regions with the exception of Cincinnati, reflecting the benefits of revenue growth and cost saving initiatives. Cincinnati was impacted by customer-related raw material supply constraints and a \$3.3 million charge for an early retirement program, the benefits of which will begin in the fourth quarter of 2008.

EBITDA before repositioning expenses for the global PDS operations was \$13.9 million in the third quarter of 2008, \$7.5 million higher than the same period in 2007. The PDS operations benefited from strong growth in all regions.

Repositioning expenses for the quarter were \$6.7 million attributable to severance accruals for the planned 2009 consolidation of the York Mills and Whitby operations in Canada, and downsizing expense related to establishing the Caguas, Puerto Rico site as a satellite plant to the Manati operation.

Third Quarter Year to Date 2008 Operating Results from Continuing Operations

Consolidated revenue grew 15% year-over-year (9% in local currencies) to \$545.1 million vs. \$472.3 million for the prior year. Consolidated EBITDA before repositioning expenses was \$57.9 million reflecting an EBITDA margin of 10.6% year to date, compared with \$60.5 million for an EBITDA margin of 12.8% in the same period last year. This included non-cash net foreign exchange losses on U.S. dollar denominated debt in Canada of \$4.1 million compared with a gain of \$4.8 million for the same period

last year. As noted above, these results also reflect additional costs incurred in connection with recruiting executive and senior management positions, consulting fees related to new operational and strategic initiatives, and severance costs.

Commercial manufacturing revenues increased 14% year-over-year to \$442.4 million reflecting growth from the existing customer base in the European and Canadian operations. The growth performance more than offset the loss of two products due to a product market withdrawal and the decision by a customer to repatriate a product. EBITDA before repositioning expenses from the Commercial operations was \$53.4 million year to date, \$8.9 million higher than the same period in 2007. This EBITDA growth included a benefit of \$4.7 million related to weakness of the US dollar, steady improvement in performance in Europe, Canada and Puerto Rico, partially offset by higher energy costs, other restructuring activities and the third quarter results of Cincinnati.

PDS revenues grew 24% year-over-year to \$102.7 million reflecting continued broad based growth in all regions. Further growth capacity is currently coming online due to the completion of a new PDS lab facility in Research Triangle Park, N.C., the recently launched clinical packaging operations and a new intermediate scale solid dose pilot facility in Cincinnati. EBITDA before repositioning expenses from the global PDS operations was \$29.4 million year to date, \$8.4 million higher than the same period in 2007. This reflected the benefit of volume gains in all regions.

Restructuring Activities

Repositioning expenses were \$17.3 million during the nine-month period compared to \$8.1 million for the same period last year attributable to changes in executive and senior management, the previously announced workforce reduction in Swindon and the ongoing York Mills/Whitby consolidation and restructuring of the Puerto Rico operations. The early retirement costs at Cincinnati were included in operating costs, as noted above.

The Company is making significant headcount reductions to increase productivity and drive future profitability. Severance expenses booked year-to-date, planned divestitures and completed divestitures will account for a total headcount reduction relative to October 2007 of approximately 850 or 16% of the Patheon workforce.

Update on Restructuring the Canadian Operations

The Company's plan to close its York Mills facility is on track to transfer the facility's commercial production and development services to the Whitby facility by mid-2009. In the third quarter 2008 the company booked a severance accrual of \$4.4 million for employee related repositioning expenses at York Mills and Whitby. The consolidation of the York Mills and Whitby operations will provide the company with an efficient plant structure in Canada, the benefits of which will begin to be realized in the second half of 2009.

Update on Carolina Facilities

The Carolina operations are classified as a discontinued operation, with related assets and liabilities being classified as held for sale. Based on discussions with interested third parties, it has been determined that the carrying value of the assets is impaired. The loss from discontinued operations for the three months ended July 31, 2008 includes an impairment charge of \$7.7 million to write down the Carolina assets to their fair market value less estimated disposition costs.

Outlook

Due to normal summer shutdowns, particularly in Europe, revenues for the fourth quarter of 2008 are expected to be lower than revenues for the third quarter of 2008 and could be subject to fluctuations in the strength of the U.S. dollar.

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.

Convertible Preferred Shares

The Company is also announcing today that it has entered into an agreement with JLL Patheon Holdings, LLC under which JLL has agreed to waive its right to the mandatory redemption provision of the Company's convertible preferred shares. In consideration JLL will receive 400,000 restricted voting shares of the Company. The Patheon Board of Directors has also agreed to a limited waiver of the standstill provision under the investor agreement with JLL that will allow JLL to acquire restricted voting shares in the open market over 12 months equal to no more than 1% of the equity of the Company including the restricted voting shares issuable under the convertible preferred shares.

“The change in the terms of the agreement allows Patheon to reclassify to equity from a combination of debt and equity the full value of the preferred shares. This eliminates both a non-cash accretive interest charge and a significant foreign exchange exposure, and results in a revised financial statement presentation that clarifies the true financial nature of the convertible preferred shares. It also eliminates a potential cash redemption of the preferred shares in 2017 that would have been at least \$185 million” said Eric Evans, Chief Financial Officer of Patheon.

The change in terms will result in a deemed repayment of the debt and equity components of the convertible preferred shares. Based on current market conditions the Company anticipates that it will recognize in the fourth quarter a non-cash gain of approximately \$28 million on the deemed repayment of the debt component. The agreement will result in a net increase in shareholders' equity of approximately \$152 million.

The agreement is subject to TSX approval and is expected to be completed during the fourth quarter. Additional details on the Agreement can be found in the Company's third quarter MD&A.

Notes

The consolidated results for the third quarter of 2008 and comparative prior periods presented in this news release reflect the results for the Company's continuing operations. The results for Niagara-Burlington operations, which were divested at the end of the first quarter 2008 and the Carolina, Puerto Rico operations have been segregated and presented separately as discontinued operations in the consolidated financial statements. All amounts are in U.S. dollars unless otherwise indicated.

ABOUT PATHEON

Patheon Inc. (TSX:PTI; www.patheon.com) is a leading global provider of contract development and manufacturing services to the global pharmaceutical industry. Patheon prides itself in providing the highest quality products and services to more than 300 of the world's leading pharmaceutical and biotechnology companies. Patheon's services range from preclinical development through commercial manufacturing of a full array of dosage forms including parenteral, solid, semi-solid and liquid forms. Patheon uses many innovative technologies including single-use disposables, Liquid-Filled Hard Capsules and a variety of modified release technologies.

Patheon's comprehensive range of fully integrated Pharmaceutical Development Services includes pre-formulation, formulation, analytical development, clinical manufacturing, scale-up and commercialization. Patheon can take customers direct to clinic with global clinical packaging and distribution services and Patheon's Quick to Clinic™ programs can accelerate early phase development project to clinical trials while minimizing the consumption of valuable API.

Patheon's integrated development and manufacturing network of 11 facilities, and 6 development centers across North America and Europe, strives to ensure that customer products can be launched with confidence anywhere in the world.

Caution Concerning Forward-Looking Statements

This news release contains forward-looking statements which reflect management's expectations regarding the Company's future growth, results of operations, performance (both operational and financial) and business prospects and opportunities. Wherever possible, words such as "plans", "expects" or "does not expect", "forecasts", "anticipates" or "does not anticipate", "believes", "intends" and similar expressions or statements that certain actions, events or results "may", "could", "would", "might" or "will" be taken, occur or be achieved have been used to identify these forward-looking statements. Although the forward-looking statements contained in this press release reflect management's current assumptions based upon information currently available to

management and based upon what management believes to be reasonable assumptions, the Company cannot be certain that actual results will be consistent with these forward-looking statements. Current material assumptions relate to customer volumes, regulatory compliance and foreign exchange rates. Forward-looking statements necessarily involve significant known and unknown risks, assumptions and uncertainties that may cause the Company's actual results, performance, prospects and opportunities in future periods to differ materially from those expressed or implied by such forward-looking statements. These risks and uncertainties include, among other things: the inability to complete transactions as a result of failure to satisfy closing conditions, including receipt of regulatory approvals, regulatory approval of and market demand for client products; credit and client concentration; the ability to identify and secure new contracts; regulatory matters, including compliance with pharmaceutical regulations; international operations risks; exposure to foreign currency risks; competition; product liability claims; intellectual property; environmental, health and safety risks; substantial financial leverage; interest rates; proposed divestiture of the Carolina site; initiatives to reduce operating expenses; use of non-GAAP financial measures, significant shareholders; risks associated with information systems; and supply arrangements. Although the Company has attempted to identify important risks and factors that could cause actual actions, events or results to differ materially from those described in forward-looking statements, there may be other factors and risks that cause actions, events or results not to be as anticipated, estimated or intended. There can be no assurance that forward-looking statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. Accordingly, readers should not place undue reliance on forward-looking statements. These forward-looking statements are made as of the date of this news release and, except as required by law, the Company assumes no obligation to update or revise them to reflect new events or circumstances.

Webcast Conference Call with Analysts

Patheon Inc. will host a webcast conference call with financial analysts on its third quarter 2008 results on Friday, September 5, 2008 at 10:00 a.m. (Eastern Time). The call will begin with a brief presentation, followed by a question-and-answer period with investment analysts. Interested parties are invited to access the live call, via telephone, in listen-only mode, at (416) 644-3414 (Toronto and International) or toll free at (800) 733-7571 (U.S., including Puerto Rico). Listeners are encouraged to dial in five to 15 minutes in advance to avoid delays. A live audio webcast will also be available via the web at www.patheon.com. An archived version of the Q3 webcast will be available on www.patheon.com for three months.

Consolidated Statements of Loss

(unaudited)

	Three months ended July 31,			Nine months ended July 31,		
	2008	2007	%	2008	2007	%
(in thousands of U.S. dollars, except loss per share)	\$	\$	Change	\$	\$	Change
Revenues	194,976	164,737	18.4%	545,145	472,325	15.4%
Operating expenses	168,977	147,722	14.4%	483,165	416,652	16.0%
Foreign exchange loss (gain) on debt (note 7)	1,281	(3,634)	-135.3%	4,105	(4,790)	-185.7%
Repositioning expenses (note 6)	6,685	1,189	462.2%	17,332	8,131	113.2%
Depreciation and amortization	12,034	9,390	28.2%	33,890	28,935	17.1%
Amortization of intangible assets	471	471	0.0%	1,413	1,414	-0.1%
Foreign exchange loss on foreign operations	-	-		-	858	
Interest	8,342	7,356	13.4%	24,117	21,659	11.3%
Refinancing expenses	-	-		-	13,471	
Earnings (loss) from continuing operations before income taxes	(2,814)	2,243	-225.5%	(18,877)	(14,005)	-34.8%
Provision for income taxes	1,721	5,608	-69.3%	4,344	14,886	-70.8%
Loss from continuing operations	(4,535)	(3,365)	-34.8%	(23,221)	(28,891)	19.6%
(as a % of revenues)	-2.3%	-2.0%		-4.3%	-6.1%	
Loss from discontinued operations (note 2)	(10,147)	(59,704)	83.0%	(15,124)	(58,188)	74.0%
Net loss for the period	(14,682)	(63,069)	76.7%	(38,345)	(87,079)	56.0%
Basic and diluted loss per share						
From continuing operations	(5.0¢)	(3.7¢)	-35.1%	(25.6¢)	(31.1¢)	17.7%
From discontinued operations	(11.2¢)	(64.2¢)	82.6%	(16.7¢)	(62.6¢)	73.3%
	(16.2¢)	(67.9¢)	76.1%	(42.3¢)	(93.7¢)	54.9%
Average number of shares						
outstanding during period - basic and diluted (in thousands)	90,742	92,959	-2.4%	90,667	92,956	-2.5%

see accompanying notes

Consolidated Balance Sheets

(unaudited)

	As at July 31, 2008	As at October 31, 2007
<i>(in thousands of U.S. dollars)</i>	\$	\$
Assets		
Current		
Cash and cash equivalents	34,054	30,557
Accounts receivable	146,302	127,691
Inventories	83,884	85,991
Prepaid expenses and other	11,411	11,887
Current assets held for sale (note 2)	1,546	16,151
Total current assets	<u>277,197</u>	<u>272,277</u>
Capital assets		
Intangible assets	478,859	479,682
Deferred costs	5,357	6,770
Future tax assets	7,092	8,878
Goodwill	34,318	31,039
Investments	3,375	3,658
Long-term assets held for sale (note 2)	2,178	946
	1,942	26,367
	<u>810,318</u>	<u>829,617</u>
Liabilities and Shareholders' equity		
Current		
Bank indebtedness	20,834	8,224
Accounts payable and accrued liabilities	170,001	159,335
Income taxes payable	7,759	4,684
Current portion of long-term debt	11,984	11,719
Current liabilities related to assets held for sale (note 2)	17	7,743
Total current liabilities	<u>210,595</u>	<u>191,705</u>
Long-term debt		
Deferred revenues	208,390	203,615
Future tax liabilities	25,185	25,994
Convertible preferred shares - debt component	43,634	47,397
Other long-term liabilities	151,205	139,916
Long-term liabilities related to assets held for sale (note 2)	20,968	22,069
Total liabilities	<u>659,997</u>	<u>632,432</u>
Shareholders' equity		
Convertible preferred shares - equity component	15,925	15,925
Restricted voting shares	392,395	391,967
Contributed surplus	6,164	4,049
Deficit	(324,595)	(286,250)
Accumulated other comprehensive income	60,432	71,494
Total shareholders' equity	<u>150,321</u>	<u>197,185</u>
	<u>810,318</u>	<u>829,617</u>

see accompanying notes

Consolidated Statements of Changes in Shareholders' Equity

(unaudited)

	Nine months ended July 31,	
	2008	2007
(in thousands of U.S. dollars)	\$	\$
Convertible preferred shares - equity component		
Balance at beginning of period	15,925	-
Shares issued during the period, net of issue costs	-	15,925
Balance at end of period	15,925	15,925
Restricted voting shares		
Balance at beginning of period	391,967	400,721
Shares issued during the period, net of issue costs	428	24
Balance at end of period	392,395	400,745
Contributed surplus		
Balance at beginning of period	4,049	3,829
Stock options	2,115	168
Balance at end of period	6,164	3,997
Deficit		
Balance at beginning of period	(286,250)	(189,900)
Adjustment related to change in accounting policy	-	(1,749)
Net loss for the period	(38,345)	(87,079)
Balance at end of period	(324,595)	(278,728)
Accumulated other comprehensive income		
Balance at beginning of period	71,494	36,081
Transition adjustment	-	(762)
Other comprehensive income (loss) for the period	(11,062)	16,958
Balance at end of period	60,432	52,277
Total shareholders' equity at end of period	150,321	194,216

see accompanying notes

Consolidated Statements of Comprehensive Loss

(unaudited)

	Three months ended July 31,		Nine months ended July 31,	
	2008	2007	2008	2007
(in thousands of U.S. dollars)	\$	\$	\$	\$
Net loss for the period	(14,682)	(63,069)	(38,345)	(87,079)
Other comprehensive income (loss), net of income taxes				
Change in foreign currency gains on investments in subsidiaries, net of hedging activities ¹	(810)	5,545	(4,596)	12,642
Foreign currency losses on investments in subsidiaries, net of hedging activities reclassified to consolidated statement of loss ²	-	-	-	2,793
Change in value of derivatives designated as foreign currency and interest rate cash flow hedges ³	1,248	370	(2,115)	1,201
(Gains) losses on foreign currency and interest rate cash flow hedges reclassified to consolidated statement of loss ⁴	(1,116)	(399)	(4,351)	322
Other comprehensive income (loss) for the period	(678)	5,516	(11,062)	16,958
Comprehensive loss for the period	(15,360)	(57,553)	(49,407)	(70,121)

see accompanying notes

The amounts disclosed in other comprehensive income have been recorded net of income taxes as follows:

¹Net of an income tax expense of nil (2007 - nil).

²Net of an income tax expense of nil (Nine months ended July 31, 2007, recovery of \$1,935,000).

³Net of an income tax expense of \$363,000 and income tax recovery of \$168,000 for the three and nine months ended July 31, 2008, respectively. (Three and nine months ended July 31, 2007, recovery of \$116,000).

⁴Net of an income tax recovery of \$135,000 and \$204,000 for the three and nine months ended July 31, 2008, respectively. (Three and nine months ended July 31, 2007, recovery of \$323,000 and \$343,000, respectively).

Consolidated Statements of Cash Flows

(unaudited)

	Three months ended July 31,		Nine months ended July 31,	
	2008	2007	2008	2007
(in thousands of U.S. dollars)	\$	\$	\$	\$
Operating activities				
Net loss from continuing operations	(4,535)	(3,365)	(23,221)	(28,891)
Add (deduct) charges to operations not requiring a current cash payment				
Depreciation and amortization	12,505	9,861	35,303	30,349
Foreign exchange loss (gain) on debt	1,893	(3,634)	4,717	(4,790)
Foreign exchange loss on foreign operations	-	-	-	858
Accreted interest on convertible preferred shares	3,861	3,481	11,289	3,481
Other non-cash interest	161	126	421	1,506
Employee future benefits, net of contributions	(313)	(65)	(1,878)	323
Future income taxes	(3,240)	2,980	(8,794)	3,146
Amortization of deferred revenues	(504)	(547)	(1,513)	(1,516)
Other	838	463	2,183	970
	<u>10,666</u>	<u>9,300</u>	<u>18,507</u>	<u>5,436</u>
Net change in non-cash working capital balances related to continuing operations	5,156	(20,272)	(8,949)	(27,715)
Increase in deferred revenues	623	2,057	2,101	2,057
Cash provided by (used in) operating activities of continuing operations	<u>16,445</u>	<u>(8,915)</u>	<u>11,659</u>	<u>(20,222)</u>
Cash provided by (used in) operating activities of discontinued operations	<u>(349)</u>	<u>5,591</u>	<u>(6,545)</u>	<u>15,640</u>
Cash provided by (used in) operating activities	<u>16,096</u>	<u>(3,324)</u>	<u>5,114</u>	<u>(4,582)</u>
Investing activities				
Additions to capital assets	(15,200)	(8,186)	(34,050)	(20,600)
Proceeds on sale of capital assets	-	-	12,089	-
Net increase in investments	(926)	(293)	(1,311)	(177)
Increase in deferred pre-operating costs	-	(1,116)	-	(2,827)
Cash used in investing activities of continuing operations	<u>(16,126)</u>	<u>(9,595)</u>	<u>(23,272)</u>	<u>(23,604)</u>
Cash provided by (used in) investing activities of discontinued operations	<u>-</u>	<u>(339)</u>	<u>10,439</u>	<u>(792)</u>
Cash used in investing activities	<u>(16,126)</u>	<u>(9,934)</u>	<u>(12,833)</u>	<u>(24,396)</u>
Financing activities				
Increase in bank indebtedness	3,728	9,078	11,801	7,762
Increase in long-term debt	7,882	6,812	23,822	182,652
Repayment of long-term debt	(8,408)	(7,018)	(23,984)	(319,605)
Issue of convertible preferred shares	-	-	-	150,000
Convertible preferred share issue cost - equity component	-	-	-	(1,213)
Issue of restricted voting shares	403	-	428	24
Cash provided by financing activities of continuing operations	<u>3,605</u>	<u>8,872</u>	<u>12,067</u>	<u>19,620</u>
Cash used in financing activities of discontinued operations	<u>(6)</u>	<u>(101)</u>	<u>(179)</u>	<u>(467)</u>
Cash provided by financing activities	<u>3,599</u>	<u>8,771</u>	<u>11,888</u>	<u>19,153</u>
Effect of exchange rate changes on cash and cash equivalents	<u>(279)</u>	<u>(1,555)</u>	<u>(672)</u>	<u>(402)</u>
Net increase (decrease) in cash and cash equivalents during the period	<u>3,290</u>	<u>(6,042)</u>	<u>3,497</u>	<u>(10,227)</u>
Cash and cash equivalents, beginning of period	<u>30,764</u>	<u>46,538</u>	<u>30,557</u>	<u>50,723</u>
Cash and cash equivalents, end of period	<u>34,054</u>	<u>40,496</u>	<u>34,054</u>	<u>40,496</u>

see accompanying notes

Notes to Unaudited Consolidated Financial Statements for the Three and Nine Months Ended July 31, 2008
(Dollar information in tabular form is expressed in thousands of U.S. dollars)

1. Accounting policies

Basis of presentation

The accompanying unaudited consolidated financial statements have been prepared by the Company in accordance with Canadian generally accepted accounting principles on a basis consistent with those followed in the most recent audited consolidated financial statements except as noted below. These consolidated financial statements do not include all the information and footnotes required by generally accepted accounting principles for annual financial statements and therefore should be read in conjunction with the audited consolidated financial statements and notes for the year ended October 31, 2007.

The preparation of the consolidated financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect: the reported amounts of assets and liabilities; the disclosure of contingent assets and liabilities at the date of the consolidated financial statements; and the reported amounts of revenue and expenses in the reporting period. Management believes that the estimates and assumptions used in preparing its consolidated financial statements are reasonable and prudent, however, actual results could differ from those estimates.

Changes in accounting policy

Effective November 1, 2007, the Company adopted the Canadian Institute of Chartered Accountants (“CICA”) accounting standards Section 3862 “Financial Instruments – Disclosure”, Section 3863 “Financial Instruments – Presentation”, Section 1535 “Capital Disclosures” and Section 1506 “Accounting Changes”. The adoption of the new standards resulted in additional disclosures with regard to financial instruments and the Company’s objectives, policies and process for managing capital (notes 8 and 9). The new standards have no impact on the classification and valuation of the Company’s consolidated financial instruments.

Recently issued accounting pronouncements

(a) 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 and is currently evaluating the effects of adopting the new requirements of this standard.

(b) 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 and is currently evaluating the effects of adopting the new requirements of this standard.

(c) 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

Notes to Unaudited Consolidated Financial Statements for the Three and Nine Months Ended July 31, 2008
(Dollar information in tabular form is expressed in thousands of U.S. dollars)

consistency with this new standard. The new and amended standards are effective for the Company beginning November 1, 2008. The Company is currently assessing the impact of these standards on its consolidated financial statements.

(d) 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.

2. Discontinued operations and assets held for sale

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 completed the sale of its Niagara-Burlington commercial 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) in Ontario. Pharmetics offered employment to all of the commercial manufacturing employees at the two sites and continues to manufacture and supply all of the products manufactured at these sites. Proceeds from the divestiture, net of transaction costs and including post closing adjustments, were \$10,492,000. The Company recorded a loss of \$601,000 on the disposal.

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 its site in Whitby. In accordance with this plan, on April 15, 2008 the Company completed the sale of the York Mills property for net proceeds of \$11,864,000 and has entered into a lease for up to two years in order to facilitate the decommissioning process.

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

The results of the Niagara-Burlington and Carolina operations have been reported as discontinued operations. Because the business in the York Mills, Toronto facility is being transferred within the existing site network, its results of operations are included in continuing operations. All prior period amounts have been reclassified to conform to the current period presentation.

In the third quarter of 2008, the Company recorded an impairment charge of \$7,700,000 to write down the carrying value of the Carolina operations long-lived assets to their fair value less estimated disposition costs, based on discussions with third parties interested in purchasing the facilities. In the third quarter of 2007, the Company recorded an impairment charge of \$61,609,000. This included a charge of \$48,580,000 to write down the carrying value of the Carolina long-lived depreciable assets to their estimated fair value and a charge of \$13,029,000 to write down the carrying value of the Niagara-Burlington operations’ long-lived assets to their fair value less estimated disposition costs.

The results of discontinued operations for the three and nine months ended July 31, 2008 and 2007 are as follows:

Notes to Unaudited Consolidated Financial Statements for the Three and Nine Months Ended July 31, 2008
(Dollar information in tabular form is expressed in thousands of U.S. dollars)

	Three months ended July 31,		Nine months ended July 31,	
	2008	2007	2008	2007
	\$	\$	\$	\$
Revenues	1,689	21,270	16,849	66,386
Operating expenses	4,092	17,841	22,946	55,530
Repositioning expenses	24	277	190	988
Asset impairment charge	7,700	61,609	7,700	61,609
Depreciation and amortization	-	748	45	2,452
Amortization of intangible assets	-	760	324	4,180
Loss on disposal of discontinued operations	-	-	601	-
Interest	20	8	32	40
Loss before income taxes	(10,147)	(59,973)	(14,989)	(58,413)
Provision for (recovery of) income taxes	-	(269)	135	(225)
Net loss for the period	(10,147)	(59,704)	(15,124)	(58,188)

As at July 31, 2008, the assets and liabilities held for sale relate to the Carolina operations. As at October 31, 2007, the assets held for sale and the related liabilities included the Niagara-Burlington and Carolina operations and the land and buildings at York Mills. In accordance with Section 3475 of the CICA Handbook, long-lived assets held for sale are measured at the lower of their carrying amount or fair value less cost to sell.

Assets held for sale and the related liabilities are as follows:

	As at July 31,	As at October 31,
	2008	2007
	\$	\$
Current assets		
Accounts receivable	317	7,486
Inventories	707	8,045
Prepaid expenses and other	522	620
Total current assets	1,546	16,151
Long-term assets		
Capital assets	1,942	24,403
Intangible assets	-	1,948
Future tax assets	-	16
Total long-term assets	1,942	26,367
Current liabilities		
Accounts payable and accrued liabilities	-	7,743
Current portion of long-term debt	17	-
Total current liabilities	17	7,743
Long-term liabilities		
Long-term debt	20	213
Other long-term liabilities	-	1,523
Total long-term liabilities	20	1,736

3. Convertible preferred shares and restricted voting shares

Notes to Unaudited Consolidated Financial Statements for the Three and Nine Months Ended July 31, 2008
(Dollar information in tabular form is expressed in thousands of U.S. dollars)

The following table summarizes information on convertible preferred shares, and restricted voting shares and related matters at July 31, 2008:

	Outstanding	Exercisable
Class I preferred shares series C and D outstanding	150,000	
Restricted voting shares outstanding	90,749,388	
Restricted voting share stock options	6,169,770	3,192,093

Please refer to note 11 "Subsequent Events" with regard to an agreed waiver in the mandatory redemption provision in the Class I preferred shares series C and D.

4. Segmented information

The Company is organized and managed as a single business segment, being the provider of commercial manufacturing and pharmaceutical development services.

Canadian and foreign continuing operations consist of:

	Manufacturing location			Total
	Three months ended July 31, 2008			
	Canada	USA	Europe	
	\$	\$	\$	\$
Revenues by client's billing location:				
Canada	5,503	129	2,923	8,555
USA	39,763	36,025	9,614	85,402
Europe	12,468	1,374	79,846	93,688
Other geographic areas	1,456	164	5,711	7,331
Total revenues	59,190	37,692	98,094	194,976
Capital assets	117,378	114,009	247,472	478,859
Goodwill	3,375	-	-	3,375

	Manufacturing location			Total
	Three months ended July 31, 2007			
	Canada	USA	Europe	
	\$	\$	\$	\$
Revenues by client's billing locations:				
Canada	4,515	554	36	5,105
USA	35,223	34,255	4,257	73,735
Europe	7,669	1,272	74,670	83,611
Other geographic areas	1,221	153	912	2,286
Total revenues	48,628	36,234	79,875	164,737
Capital assets	105,699	110,965	233,662	450,326
Goodwill	3,239	-	-	3,239

Notes to Unaudited Consolidated Financial Statements for the Three and Nine Months Ended July 31, 2008
(Dollar information in tabular form is expressed in thousands of U.S. dollars)

	Manufacturing location			
	Nine months ended July 31, 2008			
	Canada	USA	Europe	Total
	\$	\$	\$	\$
Revenues by client's billing location:				
Canada	14,838	616	3,029	18,483
USA	106,220	112,787	31,184	250,191
Europe	39,535	3,356	218,491	261,382
Other geographic areas	3,473	1,737	9,879	15,089
Total revenues	164,066	118,496	262,583	545,145

	Manufacturing location			
	Nine months ended July 31, 2007			
	Canada	USA	Europe	Total
	\$	\$	\$	\$
Revenues by client's billing locations:				
Canada	10,741	903	895	12,539
USA	104,917	117,305	11,016	233,238
Europe	26,732	2,227	190,050	219,009
Other geographic areas	2,791	292	4,456	7,539
Total revenues	145,181	120,727	206,417	472,325

Revenues are attributed to countries based on the location of the client's billing address, capital assets are attributed to the country in which they are located, and goodwill is attributed to the country in which the entity to which the goodwill pertains is located.

Revenue information by service activity is as follows:

	Three months ended July 31,			
	2008		2007	
	\$		\$	
Commercial manufacturing - prescription	146,046	75%	124,950	76%
Commercial manufacturing - over-the-counter	11,227	6%	11,229	7%
Development services	37,703	19%	28,558	17%
	194,976	100%	164,737	100%

	Nine months ended July 31,			
	2008		2007	
	\$		\$	
Commercial manufacturing - prescription	397,754	73%	357,498	76%
Commercial manufacturing - over-the-counter	44,645	8%	31,694	6%
Development services	102,746	19%	83,133	18%
	545,145	100%	472,325	100%

Notes to Unaudited Consolidated Financial Statements for the Three and Nine Months Ended July 31, 2008
(Dollar information in tabular form is expressed in thousands of U.S. dollars)

5. Stock-based compensation

The Company has an incentive stock option plan. Persons eligible to participate in the plan are directors, officers, and key employees of the Company and its subsidiaries or any other person engaged to provide ongoing management or consulting services to Patheon and its subsidiaries. The plan provides that the maximum number of shares that may be issued under the plan is 7.5% of the sum, at any point in time, of the issued and outstanding restricted voting shares of the Company and the aggregate number of restricted voting shares issuable upon exercise of the conversion rights attaching to the issued and outstanding Class I Preferred Shares, Series C of the Company. As of July 31, 2008, the total number of restricted voting shares issuable under the plan was 9,426,970 of which there are stock options outstanding to purchase 6,169,770 shares. The exercise price of restricted voting shares subject to an option is determined at the time of grant and the price cannot be less than the weighted average market price of the restricted voting shares of Patheon on the Toronto Stock Exchange during the two trading days immediately preceding the grant date. Options generally expire seven to ten years after the grant date and are also subject to early expiry in the event of death, resignation, dismissal or retirement of an optionee. Options generally vest over one to three years, with one-third vesting on each of the first, second and third anniversaries of the grant date for those vesting over three years.

For the purposes of calculating the stock-based compensation expense, the fair value of stock options is estimated at the date of the grant using the Black-Scholes option pricing model and the cost is amortized over the vesting period. During the three and nine months ended July 31, 2008, the Company granted 357,140 and 3,560,876 options, respectively. The weighted average fair value of the options granted for the three and nine months ended July 31, 2008 was \$1.75 and \$1.39, respectively. No options were granted in the third quarter of 2007. The weighted average fair value of 100,000 options granted for the nine months ended July 31, 2007 was \$1.92. The following assumptions were used in arriving at the fair value of options issued during the three and nine months ended July 31, 2008:

	Three months ended July 31, 2008	Nine months ended July 31, 2008
Risk free interest rate	3.6%	3.7%
Expected volatility	43%	43%
Expected weighted average life of options	5 years	5 years
Expected dividends yield	0%	0%

Stock-based compensation expense recorded in the three months ended July 31, 2008 was \$626,000 (2007 - \$74,000). Stock-based compensation expense recorded in the nine months ended July 31, 2008 was \$2,115,000 (2007 - \$168,000).

6. Repositioning expenses

The Company has incurred a number of expenses associated with operational improvements, cost reduction initiatives and in connection with changes in executive management. During the first half of fiscal 2007, the Company also incurred professional fees and other costs in connection with its review of strategic and financial alternatives.

The following is a summary of expenses associated with these initiatives (collectively “repositioning expenses”) for the three and nine months ended July 31:

Notes to Unaudited Consolidated Financial Statements for the Three and Nine Months Ended July 31, 2008
(Dollar information in tabular form is expressed in thousands of U.S. dollars)

	Three months ended July 31,		Nine months ended July 31,	
	2008	2007	2008	2007
	\$	\$	\$	\$
Employee-related expenses	6,832	771	16,800	2,319
Consulting, professional and project management costs	(147)	418	532	2,558
Strategic alternatives review	-	-	-	3,254
	6,685	1,189	17,332	8,131

As at July 31, 2008, \$9,014,000 of the repositioning expenses are unpaid and are recorded in accounts payable and accrued liabilities. Repositioning expenses paid during the three and nine months ended July 31, 2008 amounted to \$3,581,000 and \$14,427,000 respectively.

7. Other information

Foreign exchange

During the three months ended July 31, 2008, the foreign exchange gain on operating exposures, (including benefits from cash flow hedges and the revaluation of all foreign currency denominated working capital), recorded in operating expenses was \$135,000 (2007 loss - \$309,000). During the three months ended July 31, 2008, the Company recorded a foreign exchange loss on the revaluation of certain U.S. dollar denominated debt, net of hedging activities, in its Canadian legal entity of \$1,281,000 (2007 gain - \$3,634,000). During the nine months ended July 31, 2008, the foreign exchange gain on operating exposures recorded in operating expenses was \$3,923,000 (2007 loss - \$1,695,000) and, the foreign exchange loss on the revaluation of certain U.S. dollar denominated debt was \$4,105,000 (2007 gain -\$4,790,000).

Employee future benefits

The employee future benefit expense in connection with defined benefit pension plans and other post retirement benefit plans for the three months ended July 31, 2008 was \$1,213,000 (2007 – \$1,630,000). For the nine months ended July 31, 2008, the employee future benefit expense was \$4,025,000 (2007 – \$4,624,000).

8. Financial instruments and risk management

Categories of financial assets and liabilities

Under Canadian generally accepted accounting principles financial instruments are classified into one of the following five categories: held-for-trading, held to maturity investments, loans and receivables, available-for-sale financial assets and other financial liabilities. The Company has also designated certain of its derivatives as effective hedges. The carrying values of the Company's financial instruments, including those held for sale on the consolidated balance sheet are classified into the following categories:

Notes to Unaudited Consolidated Financial Statements for the Three and Nine Months Ended July 31, 2008
(Dollar information in tabular form is expressed in thousands of U.S. dollars)

	As at July 31,	As at October 31,
	2008	2007
	\$	\$
Held for trading ⁽¹⁾	34,054	30,557
Loans and receivables ⁽²⁾	146,302	127,691
Loans and receivables - held for sale ⁽²⁾	317	7,486
Other financial liabilities ⁽³⁾	570,173	527,493
Other financial liabilities - held for sale ⁽³⁾	37	7,956
Derivatives designated as effective hedges ⁽⁴⁾ - gain/(loss)	(5,379)	1,459
Derivatives designated as held for trading ⁽⁵⁾ - loss	-	(2,699)

⁽¹⁾ Includes cash and cash equivalents.

⁽²⁾ Includes accounts receivable.

⁽³⁾ Includes bank indebtedness, accounts payable and accrued liabilities, income taxes payable, long-term debt, and the debt component of the convertible preferred shares.

⁽⁴⁾ Includes the Company's foreign exchange forward contracts and interest rate swaps, both of which are effective hedges.

⁽⁵⁾ Includes the Company's foreign exchange forward contracts that are not considered to be an effective hedge for accounting purposes.

The Company has determined the estimated fair values of its financial instruments based on appropriate valuation methodologies; however, considerable judgment is required to develop these estimates. The fair values of the Company's financial instruments are not materially different from their carrying value, with the exception of the Company's senior secured term loan of \$148,125,000 and the debt component of the convertible preferred shares of \$151,205,000. Based on current interest rates for debt with similar terms and maturities, the fair market value of the senior secured term loan and the debt component of the convertible preferred shares is estimated to be \$114,135,000 and \$123,559,000, respectively.

As at July 31, 2008, the carrying amount of the financial assets that the Company has pledged as collateral for its long-term debt facilities was \$94,148,000 (October 31, 2007 – \$103,376,000).

Foreign exchange forward contracts, interest rate swaps and other hedging arrangements

The Company utilizes financial instruments to manage the risk associated with fluctuations in foreign exchange and interest rates. The Company formally documents all relationships between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions.

As at July 31, 2008, the Company's Canadian operations had entered into foreign exchange forward contracts to sell an aggregate amount of US\$58,739,000. These contracts hedge the Canadian operations' expected exposure to U.S. dollar denominated cash flows and mature at the latest on October 28, 2009, at an average exchange rate of \$1.0215 Canadian. The mark-to-market value on these financial instruments as at July 31, 2008 was an unrealized loss of \$189,000, which has been recorded in accumulated other comprehensive income in shareholders' equity. In the third quarter of 2008, the Company's Canadian operations terminated a foreign exchange contract to purchase US\$45,000,000. The foreign exchange contract was classified as held for trading and was used by the Canadian operations to hedge a net U.S. dollar balance sheet exposure. This US dollar balance sheet exposure will be eliminated once the waiver in the mandatory redemption provisions on the convertible preferred shares has been completed. Please refer to note 11 "Subsequent Events".

As at July 31, 2008, the Company's U.K. operations had entered into foreign exchange forward contracts to sell an aggregate amount of US\$2,100,000 and €4,400,000. These contracts hedge the Swindon, U.K. operation's expected

Notes to Unaudited Consolidated Financial Statements for the Three and Nine Months Ended July 31, 2008
(Dollar information in tabular form is expressed in thousands of U.S. dollars)

exposure to U.S. dollar and euro denominated cash flows and mature at the latest on November 10, 2008, at average exchange rates of £0.5058 and £0.7865 respectively. The mark-to-market value on these financial instruments as at July 31, 2008 was an unrealized gain of \$20,000, which has been recorded in accumulated other comprehensive income in shareholders' equity.

As at July 31, 2008, the Company has designated \$133.8 million of U.S. dollar denominated debt as a hedge against its net investment in its subsidiaries in the U.S.A. and Puerto Rico. The exchange gains and losses arising from this debt, from the date so designated, are recorded in accumulated other comprehensive income in shareholders' equity.

The Company has entered into interest rate swap contracts to convert all of the interest costs on its senior secured term loan from a floating to a fixed rate of interest until June 30, 2010. The mark-to-market value of these financial instruments at July 31, 2008 was an unrealized loss of \$5,210,000 which has been recorded in accumulated other comprehensive income in shareholders' equity.

Risks arising from financial instruments and risk management

The Company's activities expose it to a variety of financial risks; market risk (including foreign exchange and interest rate), credit risk and liquidity risk. The Company's overall risk management program focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the Company's financial performance. The Company uses derivative financial instruments to hedge certain risk exposures. The Company does not purchase any derivative financial instruments for speculative purposes.

Risk management is the responsibility of the corporate finance function. The Company's domestic and foreign operations along with the corporate finance function, identify, evaluate and, where appropriate, hedge financial risks. Material risks are monitored and are discussed with the audit committee of the board of directors.

Foreign exchange risk

The Company operates in Canada, U.S.A, Puerto Rico, Italy, France and the U.K. The functional currency of the parent company is Canadian dollars and the reporting currency is U.S. dollars. Foreign exchange risk arises because the amount of the local currency receivable or payable for transactions denominated in foreign currencies may vary due to changes in exchange rates ("transaction exposures") and because the non U.S. dollar denominated financial statements of the Company may vary on consolidation into Canadian dollars and the subsequent revaluation into the reporting currency of U.S. dollars ("translation exposures").

The most significant transaction exposures arise in the Canadian operations. The balance sheet of the Canadian operations includes U.S. dollar denominated debt, including the debt component of the convertible preferred shares. The Canadian operations are required to revalue the Canadian dollar equivalent of the U.S. dollar denominated debt at each period end. Part of this debt is designated as an effective hedge against the Company's investments in subsidiaries in the U.S.A. and Puerto Rico and the related foreign exchange gains and losses are recorded in other comprehensive income. Foreign exchange gains and losses from the remaining debt are recorded in earnings. As of July 31, 2008, fluctuations of +/-5% would, everything else being equal, have an effect on loss from continuing operations before taxes of approximately +/- \$5.3 million, prior to hedging activities.

In addition, approximately 70% of revenues of the Canadian operations and approximately 10% of its operating expenses are transacted in U.S. dollars. As a result, the Company may experience transaction exposures because of volatility in the exchange rate between the Canadian and U.S. dollar. Based on the Company's current U.S. denominated net inflows, as of July 31, 2008, fluctuations of +/-5% would, everything else being equal, have an effect on loss from continuing operations before taxes for the three and nine months ended July 31, 2008 of approximately +/- \$1.6 million and +/- \$4.6 million, respectively, prior to hedging activities.

Notes to Unaudited Consolidated Financial Statements for the Three and Nine Months Ended July 31, 2008
(Dollar information in tabular form is expressed in thousands of U.S. dollars)

The objective of the Company's foreign exchange risk management activities is to minimize transaction exposures and the resulting volatility of the Company's earnings. The Company manages this risk by entering into foreign exchange forward contracts. The U.S. dollar debt exposure is also partially hedged by U.S. denominated cash and accounts receivable in the Canadian operations. As of July 31, 2008, approximately 29% of the U.S. dollar debt exposure is hedged and the Company has entered into forward foreign exchange contracts to cover approximately 80% of its Canadian-U.S. dollar cash flow exposures for its 2008 fiscal year and 30% for its fiscal year 2009. With the exception of the hedges against the Company's investments in the U.S.A. and Puerto Rico noted above, the Company does not currently hedge translation exposures.

Interest rate risk

The Company's interest rate risk primarily arises from its floating rate debt, in particular its senior secured term loan in North America and its Italian mortgages. At July 31, 2008, \$234.6 million of the Company's total debt portfolio, is subject to movements in floating interest rates. A +/-100 basis points change in interest rates would, everything else being equal, have an effect on the loss from continuing operations before income taxes for the three and nine month ended July 31, 2008 of approximately +/-\$.6 million and +/-\$.8 million, respectively, prior to hedging activities.

The objective of the Company's interest rate management activities is to minimize the volatility of the Company's earnings. In order to manage this risk, the Company has entered into interest rate swaps to convert the interest expense on its senior secured term loan, until June 2010, from a floating interest rate to a fixed interest rate. As at July 31, 2008, taking the interest rate swap into account, \$86.4 million of the Company's debt portfolio is subject to floating interest rates.

Credit risk

Credit risk arises from cash and cash equivalents held with banks and financial institutions, derivative financial instruments (foreign exchange forward contracts and interest rate swaps with positive fair values), as well as credit exposure to clients, including outstanding accounts receivable. The maximum exposure to credit risk is equal to the carrying value of the financial assets.

The objective of managing counter party credit risk is to prevent losses in financial assets. The Company assesses the credit quality of the counter parties, taking into account their financial position, past experience and other factors. Management also monitors the utilization of credit limits regularly. In cases where the credit quality of a client does not meet the Company's requirements, a cash deposit is received before any services are provided. As at July 31, 2008 the Company held deposits of \$18,712,000.

The carrying amount of accounts receivable are reduced through the use of an allowance account and the amount of the loss is recognized in the income statement within operating expenses. When a receivable balance is considered uncollectible, it is written off against the allowance for accounts receivable. Subsequent recoveries of amounts previously written off are credited against operating expenses in the income statement.

Notes to Unaudited Consolidated Financial Statements for the Three and Nine Months Ended July 31, 2008
(Dollar information in tabular form is expressed in thousands of U.S. dollars)

The following table sets forth details of the age of receivables that are not overdue as well as an analysis of overdue amounts and related allowance for the doubtful accounts:

	As at July 31, 2008
	\$
Total accounts receivable	147,387
Less: Allowance for doubtful accounts	(1,085)
Total accounts receivable, net	146,302
Of which:	
Not overdue	123,381
Past due for more than one day but for not more than three months	22,622
Past due more for than three months but for not more than six months	1,084
Past due for more than six months but not for more than one year	168
Past due for more than one year	132
Less: Allowance for doubtful accounts	(1,085)
Total accounts receivable, net	146,302

Liquidity risk

Liquidity risk arises through excess of financial obligations over available financial assets due at any point in time. The Company's objective in managing liquidity risk is to maintain sufficient readily available reserves in order to meet its liquidity requirements at any point in time. The Company achieves this by maintaining sufficient cash and cash equivalents and through the availability of funding from credit facilities. As at July 31, 2008 the Company was holding cash and cash equivalents of \$34,054,000 and had undrawn lines of credit available to it of \$65,556,000.

The contractual maturities of the Company's financial liabilities were presented in the Company's consolidated financial statements for the year ended October 31, 2007.

9. Management of Capital

The Company defines capital that it manages as the aggregate of its shareholders' equity and interest bearing debt, including the debt and equity components of the convertible preferred shares. The Company's objectives when managing capital are to ensure that the company will continue as a going concern, so that it can provide products and services to its customers and returns to its shareholders.

As at July 31, 2008, total managed capital was \$542,734,000 (October 31, 2007 - \$560,659,000), comprised of shareholders' equity of \$150,321,000 (October 31, 2007 - \$197,185,000), the debt component of the convertible preferred shares of \$151,205,000 (October 31, 2007 - \$139,916,000), where the associated accreted interest expense is a non-cash charge and cash interest-bearing debt of \$241,208,000 (October 31, 2007 - \$223,558,000). The Company has no obligation to pay cash dividends on the convertible preferred shares until after October 31, 2009, at which time the Company can elect to pay a cash dividend or increase the liquidation preference and conversion rate of the convertible preferred shares.

The Company manages its capital structure in a manner to ensure that the total of interest bearing debt that requires a cash interest payment is not greater than four times the Company's cash earnings from continuing operations for

Notes to Unaudited Consolidated Financial Statements for the Three and Nine Months Ended July 31, 2008
(Dollar information in tabular form is expressed in thousands of U.S. dollars)

the previous twelve months. For purposes of measuring the Company's success in meeting the above stated criteria, cash earnings from continuing operations is defined as the net earnings (loss) from continuing operations before any deduction for repositioning expenses, depreciation and amortization, amortization of intangible assets, asset impairment charges, foreign exchange loss on foreign operations, interest, refinancing expenses and income taxes. As at July 31, 2008 and October 31, 2007 the above capital management criteria can be illustrated as follows:

	July 31, 2008	October 31, 2007
	\$	\$
Interest bearing debt requiring a cash interest payment	241,208	223,558
Cash earnings from continuing operations for the previous twelve months	81,559	84,147
Ratio	2.96	2.66

10. Related party transactions

Revenues from companies controlled by a director and significant shareholder of the Company were in the amount of \$180,000 and \$289,000 for the three and nine months ended July 31, 2008, respectively. The revenues were \$52,000 and \$735,000 for the three and nine months ended July 31, 2007, respectively. These transactions were conducted in the normal course of business and are recorded at the exchanged amount. Accounts receivable at July 31, 2008 include a balance of \$105,000 (October 31, 2007 - \$392,000) resulting from these transactions.

As at July 31, 2008, the Company has an investment of \$2,141,000 (October 31, 2007 - \$739,000) representing an 18% interest in two Italian companies (collectively referred to as "BSP Pharmaceuticals") whose largest investor is an officer of the Company. These companies will specialize in the manufacturing of cytotoxic pharmaceutical products. On July 2, 2008 the Company signed a shareholders' agreement with the other investors in BSP Pharmaceuticals, the terms of which provide the Company with significant influence over the strategic operating, investing and financing policies of BSP Pharmaceuticals. As a result, the Company is now accounting for its investment in BSP Pharmaceuticals using the equity method. Accordingly, for the three and nine months ended July 31, 2008, the Company has recorded an investment loss of \$78,000.

Management services and other fees charged to BSP Pharmaceuticals under a management services agreement were \$500,000 and \$1,287,000 for the three and nine months ended July 31, 2008, respectively. The management fees were \$423,000 and \$1,109,000 for the three and nine months ended July 31, 2007, respectively. Accounts receivable at July 31, 2008 include a balance of \$173,000 (October 31, 2007 - \$1,593,000) 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.

11. Subsequent event

Convertible Preferred Shares

On September 5, 2008 the Company announced that it has entered into an agreement (the "JLL Agreement") with JLL Patheon Holdings, LLC, ("JLL") under which JLL has agreed to waive the requirement, under the terms of the convertible preferred shares. In consideration of this waiver, the Company has agreed to issue to JLL 400,000 restricted voting shares, representing approximately 0.4% of the currently outstanding restricted voting shares. The Company also has agreed to provide a limited waiver of the standstill provisions of the investor agreement with JLL

Notes to Unaudited Consolidated Financial Statements for the Three and Nine Months Ended July 31, 2008
(Dollar information in tabular form is expressed in thousands of U.S. dollars)

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, following the elimination of such obligation, 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 will result in a change in accounting treatment for the convertible preferred shares. The convertible preferred shares are currently treated as a compound financial instrument that contains both debt and equity components, with the related non-cash accretive interest expense. Completion of the JLL Agreement will result in the full carrying value of the convertible preferred shares being classified within shareholders' equity on the Company's balance sheet and no further accretive interest expense will be recorded in the consolidated statement of loss. Paid-in-kind dividend equivalents (or cash dividends, if the Company so elects after October 27, 2009) on the convertible preferred shares will be reported below net loss to arrive at a loss attributable to the restricted voting shareholders.

The debt and equity components of the convertible preferred shares reported on the Company's consolidated balance sheet at July 31, 2008 amounted to \$151.2 million and \$15.9 million, respectively and the related non-cash accretive interest expense recorded in the consolidated statement of loss for the three and nine months ended July 31, 2008 amounted to \$3.9 million and \$11.3 million, respectively. Had the JLL Agreement been signed at the beginning of the 2008 fiscal year, the Company would have recorded, as a charge to equity, paid-in-kind dividends on the convertible preferred shares for the three and nine months ended July 31, 2008 of \$3.5 million and \$10.2 million respectively.

The change in terms will result 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, for accounting purposes. The deemed consideration received will be allocated to the respective components based on their relative fair values at the date of the transaction. Based on current market conditions, the Company anticipates that it will recognize in the fourth quarter a non-cash gain of approximately \$28 million on the deemed repayment of the debt component. The JLL agreement will result in a net increase in shareholders' equity of approximately \$152 million.

The reclassification of the convertible preferred shares to shareholders' equity will also eliminate entirely the unhedged 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 three and nine months ended July 31, 2008 amounted to \$1.3 million and \$4.1 million respectively.

It is expected that the closing will occur during the Company's fiscal fourth quarter, subject to satisfaction of the conditions set out in the JLL Agreement. The closing is subject to a number of customary closing conditions, including TSX approval of the issuance of restricted voting shares to JLL Holdings. Either party may terminate the JLL Agreement if the closing does not occur on or prior to October 31, 2008.

12. Comparative amounts

Certain comparative amounts have been re-stated and reclassified to conform with current accounting policies and the current period presentation for discontinued operations.

Patheon Inc.

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

The following management discussion and analysis of financial condition and results of operations ("MD&A") of Patheon Inc. ("Patheon" or "the Company") for the three-month and nine-month periods ended July 31, 2008 and 2007 should be read in conjunction with the Company's consolidated financial statements and related notes contained in this interim report. All amounts are in US dollars unless otherwise indicated. This MD&A is dated as of September 5, 2008.

The purpose of this 2008 third quarter report is to provide an update to the information contained in the Company's Management's Discussion and Analysis section of the Company's 2007 Annual Report, which contains a more comprehensive discussion of the Company's strategy, capabilities to deliver results, risks and key performance indicators. Management assumes that the reader of this document has access to the MD&A section of the Company's 2007 Annual Report. This document and other information can be downloaded in portable document format (PDF) from the Company's web site at www.patheon.com or from the SEDAR web site for Canadian regulatory filings at www.sedar.com. To request a printed copy, the reader may also contact Patheon's transfer agent, Computershare Investor Services Inc., at 1-800-564-6253 or via email at service@computershare.com, or Patheon at www.patheon.com.

Use of Non-GAAP Financial Measures

Except as otherwise indicated, references in this MD&A to "EBITDA before repositioning expenses" are to earnings from continuing operations before repositioning expenses, asset impairment charges, depreciation and amortization, foreign exchange losses reclassified from other comprehensive income, interest, refinancing expenses, and income taxes. "EBITDA margin before repositioning expenses" is EBITDA before repositioning expenses divided by revenues. EBITDA before repositioning expenses and EBITDA margin before repositioning expenses are measures of earnings or earnings margin not recognized by generally accepted accounting principles in Canada ("Canadian GAAP"). 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, and other non-GAAP measures should not be construed as alternatives to net earnings determined in accordance with Canadian GAAP as indicators of performance. The Company has included these measures because it believes that this information is used by certain investors to assess the financial performance of the Company, in particular the operating earnings before non-cash charges and large and non-recurring costs.

Overview of Patheon

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

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

Patheon provides manufacturing services for a broad range of products in many dosage forms and packaging formats in accordance with client specifications. Depending on the particular client, Patheon may be responsible for most or all aspects of the manufacturing and packaging process, from sourcing excipient raw materials and

packaging components to delivering the finished product in consumer-ready form to the client. Typically, Patheon's clients supply the active pharmaceutical ingredients ("API") used in the production process.

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

At July 31, 2008, there were a total of 364 ongoing projects being carried out by Patheon's pharmaceutical development services ("PDS"). This total includes stability and process optimization work on some products that have already been launched. The Company is working on seven drug candidates at the New Drug Application ("NDA") stage. The Company did not launch any products developed on behalf of a client into commercial production during the third quarter of 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 Six Sigma program called "Patheon Advantage".

Within the overall market, pharmaceutical companies are increasingly adopting outsourcing as a strategic approach as they focus on restructuring their own networks and reassess their structures. Pharmaceutical companies are also increasingly forming strategic outsourcing arrangements with service providers. There is also an emergence of specialty pharmaceutical and biotech companies which require both development and manufacturing services, but are not investing in their own facilities. The Company is using its position as a comprehensive provider of commercial manufacturing and development services to take advantage of these market trends and to establish and maintain long-term, strategic relationships with customers on a global basis.

Key Performance Drivers

Several key performance drivers for the Company were identified in Patheon's 2007 Annual Report:

- (i) Generating higher-quality revenues

The Company's strategy is to focus resources and capital by increasing the percentage of revenues generated by higher margin R_x manufacturing and pharmaceutical development services.

- (ii) Improving capacity utilization and operating efficiency

The Company's operating sites' cost structures are largely fixed in the short term, with the result that fluctuations in manufacturing activity can have a significant impact on profit margins. The Company continues to focus on improving capacity utilization at all of its sites by entering into new commercial manufacturing agreements with new and existing clients. The Company also continues to evaluate how best to utilize the amount of available capacity in its network.

The Company continues to improve operating efficiencies through an operational excellence program with initiatives focused on a global procurement program, a workforce reduction program and a manufacturing efficiency review process. As part of this initiative, in 2008 the Company has also launched “Patheon Advantage”, a Lean Six Sigma program. The program works by empowering site professionals and employees to analyze their own processes, and identify the root causes of waste, variation and errors. The result is expected to be a reduction in cycle times and waste from variable processes. This program has been successfully introduced in the North American operations and will be implemented in the European operations in the fourth quarter of 2008.

(iii) Mitigating the impact of foreign exchange fluctuations

Because the Company’s client service contracts in North America are primarily denominated in U.S. dollars, the profitability of the Company’s Canadian operations can be impacted by significant changes in the foreign exchange trading relationship between the Canadian and U.S. dollar. Approximately 70% of revenues and approximately 10% of operating expenses of the Canadian operations are transacted in U.S. dollars.

To help mitigate these exposures, the Company enters into forward foreign exchange contracts.

An update on the Company’s interim performance relating to these key issues is provided in the sections below entitled “Recent Developments” and “Results of Operations”.

Recent Developments

Restructuring the Canadian Site Network

On April 17, 2007 the Company announced that as part of its strategy to focus on developing and manufacturing R_x 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 received on closing, net of transaction costs and including post closing adjustments, 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.

Restructuring the 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 has 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.

The Carolina operations are classified as a discontinued operation, with the related assets and liabilities being classified as held for sale. Based on discussion with interested third parties, it has been determined that the carrying value of the assets is impaired. The loss from discontinued operations for the three months ended July 31, 2008 includes an impairment charge of \$7.7 million to write down the Carolina assets to their fair market value less estimated disposition costs.

New Leadership

Under the leadership of Wes Wheeler, the new Chief Executive Officer, the Company has made changes to its executive management team and is undertaking a series of operational initiatives to reduce operating expenses and increase manufacturing efficiency, including launching the Patheon Advantage program. These programs are expected to make the Company more competitive, reduce operating costs and improve long-term profitability. As part of these initiatives, during the third quarter of 2008, the Company incurred charges of \$3.3 million relating to an early retirement program in Cincinnati. Costs associated with this program have been charged to operating expenses. Savings from the program will start in the fourth quarter of 2008.

During the third quarter of 2008 the Company has unveiled a new brand image, featuring a new logo, new company colors and a new slogan that reflect Patheon's vision to become the best provider of manufacturing and development services to the pharmaceutical industry. The Company has also made a decision to re-locate its global headquarters to Research Triangle Park, North Carolina.

Convertible Preferred Shares

On September 5, 2008 the Company announced that it has entered into an agreement (the "JLL Agreement") with JLL Patheon Holdings, LLC, ("JLL") under which JLL has agreed to waive the requirement, under the terms of the convertible preferred shares. In consideration of this waiver, the Company has agreed to issue to JLL 400,000 restricted voting shares, representing approximately 0.4% of the currently outstanding restricted voting shares. The Company also has 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, following the elimination of such obligation, 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 will result in a change in accounting treatment for the convertible preferred shares. The convertible preferred shares are currently treated as a compound financial instrument that contains both debt and equity components, with the related non-cash accretive interest expense. Completion of the JLL Agreement will result in the full carrying value of the convertible preferred shares being classified within shareholders' equity on the Company's balance sheet and no further accretive interest expense will be recorded in the consolidated statement of loss. Paid-in-kind dividend equivalents (or cash dividends, if the Company so elects after October 27, 2009) on the convertible preferred shares will be reported below net loss to arrive at a loss attributable to the restricted voting shareholders.

The debt and equity components of the convertible preferred shares reported on the Company's consolidated balance sheet at July 31, 2008 amounted to \$151.2 million and \$15.9 million, respectively and the related non-cash accretive interest expense recorded in the consolidated statement of loss for the three and nine months ended July 31, 2008 amounted to \$3.9 million and \$11.3 million, respectively. Had the JLL Agreement been signed at the beginning of

the 2008 fiscal year, the Company would have recorded , as a charge to equity, paid-in-kind dividends on the convertible preferred shares for the three and nine months ended July 31, 2008 of \$3.5 million and \$10.2 million respectively.

The change in terms will result 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, for accounting purposes. The deemed consideration received will be allocated to the respective components based on their relative fair values at the date of the transaction. Based on current market conditions, the Company anticipates that it will recognize in the fourth quarter a non-cash gain of approximately \$28 million on the deemed repayment of the debt component. The JLL agreement will result in a net increase in shareholders' equity of approximately \$152 million.

The reclassification of the convertible preferred shares to shareholders' equity will also eliminate entirely the unhedged 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 three and nine months ended July 31, 2008 amounted to \$1.3 million and \$4.1 million respectively.

It is expected that the closing will occur during the Company's fiscal fourth quarter, subject to satisfaction of the conditions set out in the JLL Agreement. The closing is subject to a number of customary closing conditions, including TSX approval of the issuance of restricted voting shares to JLL Holdings. Either party may terminate the JLL Agreement if the closing does not occur on or prior to October 31, 2008.

The JLL Agreement is a "related party transaction" within the meaning of Multilateral Instrument 61-101 – *Protection of Minority Securityholders in Special Transactions*. The negotiation of the JLL Agreement by the Company was supervised by a Special Committee of independent directors. Based upon, among other things, the recommendations of, and discussions with management of the Company and the advice of its legal and financial advisors, the Special Committee unanimously determined that entering into the JLL Agreement is in the best interests of the Company and recommended that the Board approve the agreement.

Results of Operations

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

Results of Consolidated Operations

	Three months ended July 31,			Nine months ended July 31,		
	2008	2007	%	2008	2007	%
(in thousands of U.S. dollars)	\$	\$	Change	\$	\$	Change
Revenues	194,976	164,737	18.4%	545,145	472,325	15.4%
Operating expenses	168,977	147,722	14.4%	483,165	416,652	16.0%
Foreign exchange loss (gain) on debt	1,281	(3,634)	-135.3%	4,105	(4,790)	-185.7%
EBITDA before repositioning expenses:	24,718	20,649	19.7%	57,875	60,463	-4.3%
<i>(as a percentage of revenues)</i>	<i>12.7%</i>	<i>12.5%</i>		<i>10.6%</i>	<i>12.8%</i>	
Repositioning expenses	6,685	1,189	462.2%	17,332	8,131	113.2%
Depreciation and amortization	12,034	9,390	28.2%	33,890	28,935	17.1%
Amortization of intangible assets	471	471	0.0%	1,413	1,414	-0.1%
Foreign exchange loss on foreign operations	-	-		-	858	
Interest	8,342	7,356	13.4%	24,117	21,659	11.3%
Refinancing expenses	-	-		-	13,471	
Earnings (loss) from continuing operations before income taxes	(2,814)	2,243	-225.5%	(18,877)	(14,005)	-34.8%
Provision for income taxes	1,721	5,608	-69.3%	4,344	14,886	-70.8%
Loss from continuing operations	(4,535)	(3,365)	-34.8%	(23,221)	(28,891)	19.6%
<i>(as a percentage of revenues)</i>	<i>-2.3%</i>	<i>-2.0%</i>		<i>-4.3%</i>	<i>-6.1%</i>	
Loss from discontinued operations	(10,147)	(59,704)	83.0%	(15,124)	(58,188)	74.0%
Net loss for the period	(14,682)	(63,069)	76.7%	(38,345)	(87,079)	56.0%

Revenues by Geographic Region and Service Activity

U.S.\$ '000	Three months ended July 31,			Nine months ended July 31,		
	2008	2007	%	2008	2007	%
(in thousands of U.S. dollars)	\$	\$	Change	\$	\$	Change
<u>North America</u>						
Commercial Manufacturing						
Prescription	61,230	54,704	12%	169,555	176,627	-4%
Over-the-counter	8,956	10,058	-11%	38,332	28,512	34%
	70,186	64,762	8%	207,887	205,139	1%
Development Services	26,696	20,100	33%	74,675	60,769	23%
	96,882	84,862	14%	282,562	265,908	6%
<u>Europe</u>						
Commercial Manufacturing						
Prescription	84,816	70,246	21%	228,199	180,871	26%
Over-the-counter	2,271	1,171	94%	6,313	3,182	98%
	87,087	71,417	22%	234,512	184,053	27%
Development Services	11,007	8,458	30%	28,071	22,364	26%
	98,094	79,875	23%	262,583	206,417	27%
<u>TOTAL</u>						
Commercial Manufacturing						
Prescription	146,046	124,950	17%	397,754	357,498	11%
Over-the-counter	11,227	11,229	0%	44,645	31,694	41%
	157,273	136,179	15%	442,399	389,192	14%
Development Services	37,703	28,558	32%	102,746	83,133	24%
CONSOLIDATED REVENUES	194,976	164,737	18%	545,145	472,325	15%

Three Months Ended July 31, 2008 Compared with Three Months Ended July 31, 2007

Revenues

Consolidated revenues from continuing operations for the three-month period ended July 31, 2008 increased 18%, or \$30.2 million, to \$195.0 million from \$164.7 million in the same period in 2007. On a consolidated basis, compared with the third quarter of 2007, R_x revenues increased by 17%, PDS revenues increased by 32% and OTC revenues were unchanged.

For the three-month period ended July 31, 2008, revenues excluding the Puerto Rico operations were \$181.4 million, compared with \$153.5 million in the same period last year, representing an increase of 18%.

Prescription manufacturing and development services represented 94% of revenues, compared with 93% for the comparable period in 2007.

Production volumes for the three-months ended July 31, 2008 were 3% lower than for the three-months ended April 30, 2008 based on standard pack size. The reduction principally reflects lower production volumes in Cincinnati, which was constrained by the availability of client supplied API during the third quarter.

Geographically, in North America, revenues increased in the third quarter by \$12.0 million or 14% over the same period a year ago. This reflected strong PDS revenues in Canada and Cincinnati and increases in the level of commercial manufacturing revenues from a broad range of existing clients in all locations with the exception of the Cincinnati.

In Europe, revenues for the third quarter of 2008 increased by \$18.2 million or 23% over the same period in 2007. The increase reflects higher commercial manufacturing revenues from the existing business base in all locations, in particular in the Ferentino, Italy and Bourgoin-Jallieu, France facilities. PDS revenues in Swindon, U.K. and Ferentino, Italy also showed strong growth. Reported revenues increased as a result of the strengthening of the European currencies, in particular the euro, which strengthened approximately 15% against the U.S. dollar relative to the same period last year, increasing reported revenues by approximately \$10.1 million. Had European currencies remained constant to the rates of the prior year, European revenues would have been 10% higher than the same period in 2007.

Operating Expenses

Operating expenses comprise processing costs (principally materials, employee, and other site-related costs), marketing, sales, service, corporate support, administrative expenses and foreign exchange gains and losses relating to operating activities. In the third quarter of 2008, operating expenses were \$169.0 million, being \$21.3 million higher than the same period a year ago. Operating expenses were impacted by increased volumes, higher utility costs and the continued strengthening of European and Canadian currencies relative to the U.S. dollar. Operating expenses in the third quarter of 2008 include a charge of \$3.3 million incurred in connection with the early retirement program in Cincinnati and incremental costs in connection with the initiatives being put in place by the new leadership team. Operating expenses as a percentage of revenues were 87%, compared with 90% in the same period a year ago.

Foreign Exchange Loss on Debt

The net foreign exchange loss of \$1.3 million recorded in the quarter ended July 31, 2008 related to the revaluation of U.S. dollar denominated debt in the Canadian legal entity. This compares with a gain of \$3.6 million reported in the comparable period in 2007. The reported loss in 2008 is net of foreign exchange gains from a US\$45 million forward foreign exchange contract put in place to reduce the impact of this exposure. This foreign exchange exposure will be eliminated once the mandatory redemption provision of the Company's convertible preferred shares has been completed (see "Recent Developments"). In anticipation of this change, the Company unwound the US\$45 million forward exchange contract in July 2008.

EBITDA Before Repositioning Expenses and EBITDA Margin Before Repositioning Expenses

On a consolidated basis in the third quarter of 2008, EBITDA before repositioning expenses, representing earnings from continuing operations before repositioning expenses, asset impairment charges, depreciation and amortization, foreign exchange losses reclassified from other comprehensive income, interest, refinancing expenses, and income taxes was \$24.7 million, compared with \$20.6 million in the same period a year ago. EBITDA margin before repositioning expenses was 12.7% in the three-month period ending July 31, 2008, compared with 12.5% in the same period a year ago. EBITDA before repositioning expenses for the three months ended July 31, 2008 includes a charge of \$3.3 million in connection with the Cincinnati early retirement program.

For the three-month period ended July 31, 2008 EBITDA before repositioning expenses excluding the Puerto Rico operations was \$29.6 million, compared with \$30.1 million in the same period last year. This represents an EBITDA margin before repositioning expenses of 16.3% in the three month period, compared with 19.6% in the same period last year.

On a year-over-year basis the decline in the value of the U.S. dollar relative to the Canadian dollar has had a significant negative impact on the profitability of the Canadian operations, where approximately 70% of the revenues are denominated in U.S. dollars. The U.S. dollar also declined in value relative to the European currencies; this has had the impact of increasing the value of earnings in the European operations once translated into U.S. dollars. After taking into account all foreign exchange related factors, including the benefits of the Company's cash flow hedging program and the change in foreign exchange gains and losses on the revaluation of monetary assets and liabilities, the negative impact on EBITDA before repositioning expenses in the third quarter of 2008 relative to the same period last year was approximately \$4 million.

In Canada, EBITDA before repositioning expenses from the commercial operations was \$9.9 million in the third quarter of 2008, being \$2.9 million higher than the same period last year. The improvement reflects increased revenues from the existing client base across all the Canadian operations. The negative impact on EBITDA before repositioning expenses of a 6% decline in the value of the U.S. dollar, relative to the Canadian dollar in the same period last year, was entirely offset by benefits from the Company's cash flow hedging program and foreign exchange gains on the revaluation of U.S. dollar denominated monetary assets and liabilities.

In the U.S.A. (including Puerto Rico), EBITDA before repositioning expenses for the commercial operations was a loss of \$8.4 million in the third quarter of 2008, compared with a loss of \$6.8 million in the same period last year. The result reflects a loss reported by Cincinnati, which was impacted by API supply constraints, a mix of lower margin business and a charge of \$3.3 million in connection with an early retirement program. The decline in Cincinnati was offset in part by a reduction in the losses in Puerto Rico, which benefitted from increased volumes and cost savings from the headcount reductions.

In Europe, EBITDA before repositioning expenses from the commercial operations was \$20.1 million in the third quarter of 2008, being \$5.4 million higher than the same period a year ago. This reflects revenue gains in all operations and cost saving benefits from the headcount reduction program in Swindon, U.K. The strengthening European currencies relative to the U.S. dollar compared with the same period last year, plus the benefits of foreign exchange gains on the revaluation of foreign currency denominated assets and liabilities, had the impact of increasing EBITDA before repositioning expenses by approximately \$1.8 million.

EBITDA before repositioning expenses from the global PDS operations was \$13.9 million in the third quarter of 2008, being \$7.5 million higher than the same period in 2007. The global PDS operations benefited from strong revenue growth in all locations. In Canada, the negative impact on EBITDA before repositioning expenses of a 6% decline in the value of the U.S. dollar, relative to the Canadian dollar in the same period last year, was entirely offset by benefits from the Company's cash flow hedging program and foreign exchange gains on the revaluation of U.S. dollar denominated monetary assets and liabilities.

Corporate costs in the third quarter of 2008 were \$10.9 million, compared with \$0.7 million in the same period last year. Additional costs relative to the prior year were incurred in connection with recruiting for senior and executive management positions, consulting fees related to new operational and strategic initiatives, costs in connection with the relocation of the global headquarters and higher stock-based compensation expenses. Costs also include a net foreign exchange loss of \$1.3 million arising from the revaluation of U.S. dollar denominated debt held in the Canadian legal entity. This compares with a gain of \$3.6 million recorded in the same period last year. The strengthening Canadian dollar had the impact of increasing the U.S. dollar translated values of Canadian costs by approximately \$0.8 million.

Repositioning Expenses

During the third quarter of 2008 the Company incurred \$6.7 million of expenses in connection with the continuing restructuring of the Puerto Rico operations and the consolidation of the York Mills and Whitby operations in Canada that was identified in the initial strategic plan.

Depreciation and Amortization Expense

Depreciation and amortization expense was \$12.0 million in the third quarter of 2008, compared with \$9.4 million in the third quarter of 2007. The increase reflects an accelerated depreciation charge related to certain assets impacted by the consolidation of the Canadian site network, additional depreciation expenses in Swindon, U.K. in connection with the recently completed lyophilized cephalosporin capacity and from the impact of the strengthening European and Canadian currencies relative to the U.S. dollar.

Amortization of Intangible Assets

Amortization of intangible assets was \$0.5 million in the third quarter of 2008, being comparable with the charge in the third quarter of 2007. The amortization of intangible assets relates to the Caguas operations in Puerto Rico.

Interest Expense

Interest expense for the third quarter of 2008 was \$8.3 million, compared with \$7.4 million in the third quarter of 2007. The increase in interest costs principally reflects the translation impact of the strengthening euro against the U.S. dollar on euro denominated interest costs in the Italian operations and from an increase in the non-cash accretive interest charge in respect of the debt component of the convertible preferred shares, which amounted to \$3.9 million in the third quarter of 2008.

Loss Before Income Taxes from Continuing Operations

The Company reported a loss before income taxes from continuing operations of \$2.8 million in the third quarter of 2008, compared with earnings of \$2.2 million in the same period a year ago.

Income Taxes

The Company recorded an income tax charge of \$1.7 million in the third quarter of 2008, compared with a charge of \$5.6 million in the same period last year. The income tax expenses in 2008 and 2007 principally reflects high tax rates in Italy where the Company reported significant profits compounded by tax losses in Puerto Rico and Canada, where the tax benefit after valuation reserve has not been recognized. The accreted interest expense on the convertible preferred shares of \$3.9 million (third quarter of 2007 - \$3.5 million) is not deductible for tax purposes. During the third quarter of 2008, the Company recorded a future income tax recovery of \$3.0 million relating to prior period research and development tax credits in the Swindon, U.K. operations that have only recently been approved for assessment.

Loss and Loss Per Share from Continuing Operations

The Company recorded a loss from continuing operations in the third quarter of 2008 of \$4.5 million, compared with a loss of \$3.4 million in the same period last year. The loss per share was 5.0¢, compared with a loss of 3.7¢ per share a year earlier. The loss in 2008 included after tax repositioning expenses of \$6.7 million or 7.4¢ per share. The loss in 2007 included after tax repositioning expenses of \$1.2 million or 1.3¢ per share and after tax refinancing expenses of \$12.6 million, or 13.5¢ per share.

Loss and Loss Per Share from Discontinued Operations

Discontinued operations in the third quarter of 2008 consist of the results of the Carolina, Puerto Rico operations. The comparable results for 2007 include both the Carolina and Niagara-Burlington operations. Financial details of the operating activities are disclosed in note 2 in the interim consolidated financial statements. The loss from discontinued operations in the third quarter of 2008 was \$10.1 million, or 11.2¢ compared with a loss of \$59.7 million, or 64.2¢ in the same period last year. The results for the third quarter of 2008 include a \$7.7 million asset impairment charge to reduce the carrying value of the Carolina site assets to their fair market value less estimated disposition costs (see “Recent Developments”). The prior year results include a much larger asset impairment charge of \$61.6 million, of which \$48.6 million related to the Carolina operations and \$13.0 million to the Niagara-Burlington operations.

Net Loss and Loss Per Share

The Company recorded a net loss in the third quarter of 2008 of \$14.7 million, or 16.2¢ per share, compared with a loss of \$63.1 million or 67.9¢ per share in the same period last year.

Because the Company reported a loss in the three and nine month periods ended July 31, 2008 and 2007, there is no impact of dilution.

Nine Months Ended July 31, 2008 Compared with Nine Months Ended July 31, 2007

Revenues

Consolidated revenues from continuing operations for the nine-month period ended July 31, 2008 increased 15%, or \$72.8 million, to \$545.1 million from \$472.3 million in the same period in 2007. R_x revenues increased by 11%, OTC revenues increased by 41% and PDS revenues increased by 24%.

For the nine-month period ended July 31, 2008, revenues excluding the Puerto Rico operations were \$506.9 million, compared with \$425.3 million in the same period last year, representing an increase of 19%.

Prescription manufacturing and development services represented 92% of revenues during the nine-month period ended 2008, compared with 93% for the comparable period in 2007. The decline reflects the impact of increased OTC revenues in the Canadian and Cincinnati operations.

Geographically, in North America, revenues increased by \$16.6 million or 6% over the same period a year ago, an increase driven primarily by the Canadian commercial manufacturing operations and from PDS operations in both Canada and Cincinnati. Revenues in Puerto Rico were lower than prior year, reflecting a year-over-year reduction in volumes during the first half of 2008.

In Europe, revenues increased by \$56.2 million or 27% over the same period in 2007. The year-over-year increase reflects higher manufacturing revenues from all operations as a result of additional volume requirements from the existing client base. Reported revenues increased as a result of the strengthening of the European currencies, in particular the euro, which strengthened approximately 14% against the U.S. dollar relative to the same period last

year, increasing reported revenues by approximately \$25.9 million. Had European currencies remained constant to the rates of the prior year, European revenues would have been 15% higher than the same period in 2007.

Operating Expenses

Operating expenses comprise processing costs (principally materials, employee and other site-related costs), marketing, sales, service, corporate support, administrative expenses and foreign exchange gains and losses relating to operating activities. Operating expenses were \$483.2 million during the nine-month period ended 2008, being \$66.5 million higher than the same period a year ago. Operating expenses were impacted by increased volumes, higher utility costs, incremental costs in connection with hiring the new leadership team and the strengthening of European and Canadian currencies relative to the U.S. dollar. Operating expenses in the third quarter of 2008 include a charge of \$3.3 million incurred in connection with the early retirement program in Cincinnati and incremental costs in connection with the initiatives being put in place by the new leadership team. Operating expenses as a percentage of revenues were 88.6% during the nine-month period ended 2008, comparable with virtually the same percentage, 88.2% in the same period a year ago.

Foreign Exchange Loss on Debt

The net foreign exchange loss of \$4.1 million recorded in the nine-months ended July 31, 2008 related to the revaluation of U.S. dollar denominated debt in the Canadian legal entity. This compares with a gain of \$4.8 million reported in the comparable period in 2007. The reported loss in 2008 is net of foreign exchange gains from a forward foreign exchange contract put in place to reduce the impact of this exposure.

EBITDA Before Repositioning Expenses and EBITDA Margin Before Repositioning Expenses

On a consolidated basis, EBITDA before repositioning expenses, representing earnings from continuing operations before repositioning expenses, asset impairment charges, depreciation and amortization, foreign exchange losses reclassified from other comprehensive income, interest, refinancing expenses, and income taxes was \$57.9 million, compared with \$60.5 million in the same period a year ago. EBITDA margin before repositioning expenses was 10.6% in the nine-month period ending July 31, 2008, compared with 12.8% in the same period a year ago. EBITDA before repositioning expenses for the nine months ended July 31, 2008 includes a charge of \$3.3 million in connection with the Cincinnati early retirement program.

For the nine-month period ended July 31, 2008 EBITDA before repositioning expenses excluding the Puerto Rico operations was \$72.7 million, compared with \$78.1 million in the same period last year. This represents an EBITDA margin before repositioning expenses of 14.3% during the nine-month period ended 2008, compared with 18.4% in the same period last year.

On a year-over-year basis, the decline in the value of the U.S. dollar relative to the Canadian dollar has had a significant negative impact on the profitability of the Canadian operations, where approximately 70% of the revenues are denominated in U.S. dollars. The U.S. dollar also declined in value relative to the European currencies; this has had the impact of increasing the value of earnings in the European operations once translated into U.S. dollars. Had foreign exchange rates remained the same as those in the same period last year, EBITDA before repositioning expenses for the nine-months ended July 31, 2008 would have been approximately \$8 million higher than was reported. This takes into account all foreign exchange related factors, including the benefits of the Company's cash flow hedging program and the change in foreign exchange gains and losses on the revaluation of monetary assets and liabilities.

In Canada, EBITDA before repositioning expenses from the commercial operations was \$26.2 million during the nine-month period ended 2008, being \$3.7 million higher than the same period last year. Steady growth in commercial revenues, especially in Whitby, was offset by a 12% decline in the value of the U.S. dollar, relative to the Canadian dollar in the same period last year, which reduced EBITDA before repositioning expenses by

approximately \$1.3 million, net of the benefits from the Company's cash flow hedging program and foreign exchange gains on the revaluation of U.S. dollar denominated monetary assets and liabilities.

In the U.S.A. (including Puerto Rico), EBITDA before repositioning expenses for the commercial operations was a loss of \$15.1 million during the nine-month period ended 2008, compared with a loss of \$11.1 million in the same period last year. The result reflects a decline in profitability in the Cincinnati operations, which in the third quarter of 2008 were impacted by API supply constraints, a mix of lower margin business and a charge of \$3.3 million in connection with an early retirement program. The decline in Cincinnati was offset in part by a reduction in the losses in Puerto Rico, which benefitted from increased volumes and cost savings from the headcount reductions.

In Europe, EBITDA before repositioning expenses from the commercial operations was \$42.3 million during the nine-month period ended 2008, being \$9.2 million higher than the same period a year ago. The improvement reflects increased commercial manufacturing revenues in all operations and cost savings in the third quarter in Swindon, U.K. as a result of headcount reductions. In Italy this has been offset in part by a change in mix to lower margin products. In the first quarter the Swindon, U.K. operations were also affected by additional operating costs in anticipation of the launch of Ceftobiprole[®]. The strengthening European currencies relative to the U.S. dollar compared with the same period last year, plus the benefits of foreign exchange gains on the revaluation of foreign currency denominated assets and liabilities, had the impact of increasing EBITDA before repositioning expenses by approximately \$6.0 million.

EBITDA before repositioning expenses from the global PDS operations was \$29.4 million during the nine-month period ended 2008, being \$8.4 million higher than the same period in 2007. This reflected the benefit of volume gains in the Canadian, Cincinnati and Italian operations, offset in part by the negative impact of the strengthening Canadian dollar, which reduced profitability in the Canadian operations by approximately \$2.4 million. The Swindon, U.K. operations were also impacted by one time charges arising from raw material losses which occurred during the first quarter of 2008.

Corporate costs during the nine-month period ended 2008 were \$25.0 million, compared with \$5.1 million in the same period last year. Additional costs relative to prior year were incurred in connection with recruiting for senior and executive management positions, consulting fees related to new operational and strategic initiatives, costs in connection with the relocation of the global headquarters and higher stock-based compensation expenses. The costs also include net foreign exchange losses of \$4.1 million, compared to a gain of \$4.8 million in the prior period, arising from the revaluation of U.S. dollar denominated debt held in the Canadian legal entity. The strengthening Canadian dollar had the impact of increasing the U.S. dollar translated values of Canadian costs by approximately \$2.2 million.

Repositioning Expenses

The Company incurred \$17.3 million of expenses during the nine-month period ended July 31, 2008 in connection with changes in senior and executive management, a workforce reduction initiative in Swindon, U.K. and the continuing restructuring of the Puerto Rico and Canadian networks. In the comparable period in 2007, the Company incurred \$8.1 million in repositioning expenses, which included consulting fees associated with a manufacturing efficiency review, work force reductions in particular in Puerto Rico, and costs incurred in connection with the Company's strategic alternatives review.

Depreciation and Amortization Expense

Depreciation and amortization expense was \$33.9 million during the nine-month period ended July 31, 2008, compared with \$28.9 million in the same period in 2007. The increase reflects an accelerated depreciation charge related to certain assets impacted by the consolidation of the Canadian site network, additional depreciation expenses in Swindon, U.K. in connection with the recently completed lyophilized cephalosporin capacity and from the impact of the strengthening European and Canadian currencies relative to the U.S. dollar.

Amortization of Intangible Assets

Amortization of intangible assets was \$1.4 million during the nine-month period ended July 31, 2008, being comparable with the charge in 2007. The amortization of intangible assets relates to the Caguas operations in Puerto Rico.

Foreign Exchange Loss on Foreign Operations

In the second quarter of 2007, the Company recorded a net foreign exchange loss on foreign operations of \$0.9 million. This reflected the recognition of net foreign exchange translation losses previously recorded in accumulated other comprehensive income, arising from a change in the Company's internal capital structure.

Interest Expense

Interest expense was \$24.1 million during the nine-month period ended July 31, 2008, compared with \$21.7 million in the first nine-months of 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 for the nine months ended July 31, 2008 of \$11.3 million 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 on euro denominated interest costs in the Italian operations.

Loss Before Income Taxes from Continuing Operations

The Company reported a loss before income taxes from continuing operations of \$18.9 million in the first nine-months of 2008, compared with a loss of \$14.0 million in the same period a year ago.

Income Taxes

The Company recorded an income tax charge of \$4.3 million during the nine-month period ended July 31, 2008, compared with a charge of \$14.9 million in the same period last year. The income tax expense in 2008 principally reflects high tax rates in Italy where the Company reported significant profits, compounded by tax losses in Puerto Rico and Canada, where the tax benefit after valuation reserve has not been recognized. In addition, the accreted interest expense on the convertible preferred shares of \$11.3 million is not deductible for tax purposes. During the first quarter of 2008, the Company booked a future income tax recovery of \$2.0 million relating to a reduction in tax rates in Italy that the Company will benefit from commencing in fiscal 2009 and in the third quarter of 2008, the Company recorded a future income tax recovery of \$3.0 million relating to prior period research and development tax credits in the U.K. that have only recently been approved for assessment.

The 2007 income tax 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.

Loss and Loss per Share from Continuing Operations

The Company recorded a loss from continuing operations of \$23.2 million during the nine-month period ended July 31, 2008, compared with a loss of \$28.9 million in the same period last year. The loss per share was 25.6¢ during the nine-month period ended July 31, 2008, compared with a loss of 31.1¢ per share a year earlier. The loss in 2008 included after tax repositioning expenses of \$16.4 million or 18.1¢ per share. The loss in 2007 included after tax repositioning expenses of \$7.1 million or 7.7¢ per share and after tax refinancing expenses of \$12.6 million, or 13.5¢ per share.

Loss and Loss per Share from Discontinued Operations

Discontinued operations in the nine-month period ended July 31, 2008 and the comparable results for 2007 include the Carolina operations and the Niagara-Burlington operations up to the end of the first quarter 2008. Financial

details of the operating activities are disclosed in note 2 in the interim consolidated financial statements. The loss from discontinued operations in the first nine months of 2008 was \$15.1 million, or a loss per share of 16.7¢, compared with a loss of \$58.2 million, or 62.6¢ in the same period last year. The loss in 2008 includes a charge of \$0.6 million in connection with the final divestiture of the Niagara-Burlington operations and an impairment charge of \$7.7 million relating to assets of the Carolina operations. The loss in 2007 includes an asset impairment charge of \$48.6 million relating to the Carolina operations and \$13.0 million, relating to the Niagara-Burlington operations.

Net Loss and Loss Per Share

The Company recorded a net loss of \$38.3 million during the nine-month period ended July 31, 2008, or 42.3¢ per share, compared with a loss of \$87.1 million or 93.7¢ per share in the same period last year.

Because the Company reported a loss in the nine months ended July 31, 2008 and 2007, there is no impact of dilution.

Liquidity and Capital Resources

Summary of Cash Flows

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

Summary of Cash flows

(in thousands of U.S. dollars)	Three months ended July 31,		Nine months ended July 31,	
	2008	2007	2008	2007
	\$	\$	\$	\$
Net loss from continuing operations	(4,535)	(3,365)	(23,221)	(28,891)
Depreciation and amortization	12,505	9,861	35,303	30,349
Foreign exchange loss (gain) on debt	1,893	(3,634)	4,717	(4,790)
Foreign exchange loss on foreign operations	-	-	-	858
Accreted interest on convertible preferred shares	3,861	3,481	11,289	3,481
Other non-cash interest	161	126	421	1,506
Employee future benefits, net of contributions	(313)	(65)	(1,878)	323
Future income taxes	(3,240)	2,980	(8,794)	3,146
Amortization of deferred revenues	(504)	(547)	(1,513)	(1,516)
Other	838	463	2,183	970
Working capital	5,156	(20,272)	(8,949)	(27,715)
Increase in deferred revenues	623	2,057	2,101	2,057
Cash provided by (used in) operating activities of continuing operations	16,445	(8,915)	11,659	(20,222)
Cash used in investing activities of continuing operations	(16,126)	(9,595)	(23,272)	(23,604)
Cash provided by financing activities of continuing operations	3,605	8,872	12,067	19,620
Net increase(decrease) in cash and cash equivalents from discontinued operations	(355)	5,151	3,715	14,381
Other	(279)	(1,555)	(672)	(402)
Net increase (decrease) in cash and cash equivalents during the period	3,290	(6,042)	3,497	(10,227)

Cash Provided by (Used in) Operating Activities

Cash provided by operating activities from continuing operations was \$16.4 million in the third quarter of 2008 compared with a usage of \$8.9 million in the comparable period in 2007. On a year-to-date basis cash provided by operating activities from continuing operations was \$11.7 million, compared with a usage of \$20.2 million in the same period last year. The improvement in cash flows reflects a reduction in losses before non-cash charges, along with a decrease in investments in working capital in the third quarter of 2008.

Cash used in operating activities from discontinued operations was \$0.3 million and \$6.5 million in the third quarter and the first nine months of 2008, respectively. During the comparable periods in 2007, the Company reported cash inflows of \$5.6 million and \$15.6 million, respectively. The deterioration reflects reduced earnings in the Carolina operations. In addition, the amount reported for the second and third quarter of 2007 included a net \$4.1 million of cash inflows from the operations of the Niagara-Burlington OTC manufacturing business, which was sold on January 31, 2008.

Cash Used in Investing Activities

Cash used in investing activities from continuing operations in the third quarter of 2008 was \$16.1 million, compared with cash usage of \$9.6 million in the same period a year ago. On a year-to-date basis cash used in investing activities from continuing operations was \$23.3 million compared with \$23.6 million in the same period last year. Cash inflows in 2008 include net proceeds received on sale of the Company's York Mills property of \$11.9 million, which was transacted in the second quarter. Capital expenditures were \$15.2 million and \$34.1 million for the three months and nine months ended July 31, 2008, respectively. The increase in expenditures relative to the prior year principally relates to facility expansions at the Toronto Region and Whitby operations.

Cash provided by investing activities from discontinued operations during the nine-month period ended July 31, 2008 was \$10.4 million, compared with a cash usage of \$0.8 million in the same period last year. The cash inflow in 2008 principally reflects net proceeds after transaction costs from the sale of the Niagara-Burlington operations of \$10.5 million.

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

Cash used in Investing Activities

	Three months ended July 31,		Nine months ended July 31,	
	2008	2007	2008	2007
(in thousands of U.S. dollars)	\$	\$	\$	\$
Additions to capital assets				
Sustaining	(4,990)	(3,146)	(12,121)	(8,351)
Project-related	(10,210)	(5,040)	(21,929)	(12,249)
Total additions to capital assets	(15,200)	(8,186)	(34,050)	(20,600)
Proceeds on sale of capital assets	-	-	12,089	-
Net increase in investments	(926)	(293)	(1,311)	(177)
Increase in deferred pre-operating costs	-	(1,116)	-	(2,827)
Cash used in investing activities of continuing operations	(16,126)	(9,595)	(23,272)	(23,604)
Cash provided (used in) investing activities of discontinued operations	-	(339)	10,439	(792)
Cash used in investing activities	(16,126)	(9,934)	(12,833)	(24,396)

Cash Provided by Financing Activities

Cash provided by financing activities was \$3.6 million and \$11.9 million, for the three and nine months ended July 31, 2008, respectively. The amounts for the comparable periods a year ago were \$8.8 million and \$19.2 million, respectively. The cash flows in 2008 reflect drawings and repayments on existing credit facilities.

In the second quarter of 2007, the Company completed, through private placement, the issuance of \$150 million of convertible preferred shares of the Company to JLL Partners and entered into new credit facilities in the aggregate amount of \$225 million, comprising a seven-year \$150 million term loan and a five-year \$75 million revolving facility. The net proceeds from the JLL Partners investment and term loan were used to repay the Company's obligations under its North American and U.K. credit facilities.

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

Cash Provided by Financing Activities

(in thousands of U.S. dollars)	Three months ended July 31,		Nine months ended July 31,	
	2008	2007	2008	2007
	\$	\$	\$	\$
Increase in bank indebtedness	3,728	9,078	11,801	7,762
Increase in long-term debt	7,882	6,812	23,822	182,652
Repayment of long-term debt	(8,408)	(7,018)	(23,984)	(319,605)
Issue of convertible preferred shares	-	-	-	150,000
Convertible preferred share issue cost-equity component	-	-	-	(1,213)
Issue of restricted voting shares	403	-	428	24
Cash provided by financing activities of continuing operations	3,605	8,872	12,067	19,620
Cash used in financing activities of discontinued operations	(6)	(101)	(179)	(467)
Cash provided by financing activities	3,599	8,771	11,888	19,153

Financing Arrangements and Ratios

There have been no changes to the Company's financing arrangements during the nine-month period ended July 31, 2008.

Total cash interest bearing debt, at July 31, 2008 was \$241.2 million, being \$17.7 million higher than at October 31, 2007. Total interest bearing debt at July 31, 2008, including the debt component of the convertible preferred shares of \$151.2 million, was \$392.4 million. At July 31, 2008, the Company's consolidated ratio of interest-bearing debt to shareholders' equity was 261%, compared with 184% at October 31, 2007. The increase reflects a combination of increased debt and a reduction in shareholders' equity, arising from the losses and a reduction in accumulated other comprehensive income.

The Company has entered into an agreement with JLL under which JLL has agreed to waive its right to the mandatory redemption provision of the Company's convertible preferred shares (See "Recent Developments"). Once the waiver has been completed the debt component of the convertible preferred shares will be classified within shareholders' equity. Had the waiver been in effect at July 31, 2008 the Company's consolidated ratio of interest-bearing debt to shareholders' equity would have been 80%.

Adequacy of Financial Resources

As at July 31, 2008, the Company had cash balances of \$34.1 million and \$65.6 million in undrawn credit facilities available to it and was in compliance with all covenant requirements under its financing arrangements. The Company believes that, subject to usual business risks, its financial resources are sufficient to fund projected capital expenditures, debt service requirements and employee future benefit obligations in the normal course of business. There have been no material changes to the contractual obligations under the financing arrangements disclosed in the MD&A section of the Company's 2007 Annual Report that are outside the normal course.

Critical Accounting Policies and Estimates

Changes in and Significant New Accounting Policies

Effective November 1, 2007 the Company adopted the Canadian Institute of Chartered Accountants 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 interim consolidated financial statements only.

General

Patheon's significant accounting policies are described in note 2 to the 2007 audited consolidated financial statements. The most critical of these policies are those related to revenue recognition, deferred revenues, impairment of long-lived depreciable assets, convertible preferred shares, employee future benefits, and income taxes, (notes 2, 4, 13, 15, 16 and 18 of the 2007 audited consolidated financial statements).

The preparation of the consolidated financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect: the reported amounts of assets and liabilities; the disclosure of contingent assets and liabilities at the date of the consolidated financial statements; and the reported amounts of revenue and expenses in the reporting period. Management believes that the estimates and assumptions used in preparing its consolidated financial statements are reasonable and prudent; however, actual results could differ from those estimates.

The Company's accounting policies have been reviewed and discussed with the Company's Audit Committee.

Revenue Recognition

The Company recognizes revenue for its commercial manufacturing and pharmaceutical development services when services are completed in accordance with specific agreements with its clients and when all costs connected with providing these services have been incurred, the price is fixed or determinable and collectability is reasonably assured. Client deposits on pharmaceutical development services in progress are included in accounts payable and accrued liabilities.

The Company does not receive any fees on signing of contracts. In the case of pharmaceutical development services, revenue is recognized on the achievement of specific milestones in accordance with the respective development service contracts. In the case of commercial manufacturing services, revenue is recognized when services are complete and the product has met rigorous quality assurance testing.

Deferred Revenues

The costs of certain capital assets are reimbursed to the Company by the pharmaceutical companies that are to benefit from the improvements in connection with the manufacturing and packaging agreements in force. These reimbursements are recorded as deferred revenues and are recognized as income over the remaining minimum term of the agreements. \$0.5 million and \$1.5 million were recognized as earnings in the three months and nine months ended July 31, 2008, respectively. The Company received \$0.6 million and \$2.1 million in capital reimbursements in the three months and nine months ended July 31, 2008, respectively.

Impairment of Long-Lived Depreciable Assets

On an ongoing basis, 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 net earnings.

Convertible Preferred Shares

On April 27, 2007 the Company issued \$150.0 million of convertible preferred shares. The shares are considered to be a compound financial instrument that contains both a debt component and an equity component.

On issuance of the convertible preferred shares, the fair value of the debt component is determined by discounting the expected future cash flows using a market interest rate for a non-convertible debt instrument with similar terms. The resulting value is carried as debt on an amortized cost basis until extinguished on conversion or redemption. The remainder of the proceeds is allocated as a separate component of shareholders' equity, net of transaction costs. Transaction costs are apportioned between the debt and equity components based on their respective carrying amounts when the instrument was issued.

Currently, the interest cost recognized in respect of the debt component represents the accretion of the liability, over its expected life using the effective interest method, to the amount that would be payable if redeemed. The accretive interest expense for the three months and nine months ended July 31, 2008 was \$3.9 million and \$11.3 million, respectively.

The Company has announced that it has entered into an agreement with JLL under which JLL has agreed to waive its right to the mandatory redemption provision of the Company's convertible preferred shares (See "Recent Developments"). Once the waiver has been completed the debt component of the convertible preferred shares will be classified within shareholders' equity.

Income Taxes

In accordance with Canadian GAAP, the Company uses the liability method of accounting for future income taxes and provides for future income taxes for significant temporary timing differences.

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 \$34.3 million have been recorded at July 31, 2008. The future tax assets are primarily composed of accounting provisions related to pension and post-retirement benefits not currently deductible for tax purposes, the tax benefit of net operating loss carry forwards related to the U.K., 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.

Future tax liabilities of \$43.6 million have been recorded at July 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.

Employee Future Benefits

The Company provides to certain retired employees pensions and post-employment benefits, including medical benefits and dental care. The determination of the obligation and expense for defined benefit pensions and post-employment benefits is dependent on the selection of certain assumptions used by actuaries in calculating such amounts. Those assumptions are disclosed in note 15 to the Company's 2007 audited consolidated financial statements.

Risk Management

The following are updates to certain risks and uncertainties described in the Company's Management's Discussion and Analysis for the year ended October 31, 2007, available on SEDAR (www.sedar.com) or on Patheon's website (www.patheon.com).

Foreign Currency

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

The Company's Canadian operations negotiate sales contracts for payment in both U.S. and Canadian dollars, and materials and equipment are purchased in both U.S. and Canadian dollars. The majority of its non-material costs (including payroll, facilities' costs and costs of locally sourced supplies and inventory) are denominated in Canadian dollars. Approximately 70% of revenues of the Canadian operations and approximately 10% of its operating expenses are transacted in U.S. dollars. As a result, the Company may experience trading and translation gains or losses because of volatility in the exchange rate between the Canadian dollar and the U.S. dollar. Based on the Company's current U.S. denominated net inflows, for each one-cent change in the Canadian-U.S. rate, the impact on annual pre-tax earnings, excluding any hedging activities, is approximately \$1.2 million.

In addition certain sales contracts in Swindon, U.K. are denominated in euros and U.S. dollars. This exposes the UK operations to certain limited trading and translation gains or losses because of volatility in the exchange rate between U.K. sterling, the euro and the U.S. dollar.

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

At July 31, 2008 the Company's Canadian operations had outstanding foreign exchange forward contracts to sell US\$58.7 million at an average exchange rate of \$1.0215 Canadian. The contracts mature at the latest on October 28, 2009 and cover approximately 80% of the Company's expected foreign exchange exposure for the 2008 fiscal year and 30% for fiscal 2009. The mark-to-market value at July 31, 2008 that is recorded in accumulated other comprehensive income is an unrealized loss of \$0.2 million. In July 2008 the Company's Canadian operations terminated a foreign exchange contract to purchase US\$45.0 million. The foreign exchange contract was classified as held-for-trading and was used by the Canadian operations to hedge a U.S. dollar balance sheet exposure. This U.S. dollar balance sheet exposure will be eliminated once the waiver in the mandatory redemption provisions on the convertible preferred shares has been completed (See "Recent Developments").

As at July 31, 2008, the Company's U.K. operations had entered into foreign exchange forward contracts to sell an aggregate amount of US\$2.1 million and €4.4 million. These contracts hedge the Swindon, U.K operation's expected exposure to U.S. dollar and euro denominated cash flows and mature at the latest on November 10, 2008, at an average exchange rate of £0.5058 and £0.7865, respectively. The mark-to-market value on these financial instruments as at July 31, 2008 was an unrealized gain of \$20,000, which has been recorded in accumulated other comprehensive income in shareholders' equity.

Translation gains and losses related to the carrying value of the Company's foreign operations and certain foreign currency denominated debt held by the Company and designated as a hedge against the carrying value of certain foreign subsidiaries, are included in accumulated other comprehensive income in shareholders' equity. At July 31, 2008, the Company had designated \$133.8 million of U.S. dollar denominated debt as a hedge against its investment in its U.S.A. and Puerto Rico subsidiaries.

Interest Rate Exposure

The Company has exposure to movements in interest rates. The Company has entered into interest rate swaps to convert the interest expense on its senior secured term loan from a floating interest rate to a fixed interest rate until June 30, 2010. The mark-to-market value of these financial instruments at July 31, 2008 was an unrealized loss of \$5.2 million which has been recorded in accumulated other comprehensive income in shareholders' equity. Taking this interest rate swap into account, at July 31, 2008, 78% of the Company's total debt portfolio, including the debt component of the convertible preferred shares, was not subject to movements in floating interest rates. Assuming no change to the structure of the debt portfolio, a 1% change in floating interest rates has an impact on annual pre-tax earnings of approximately \$0.9 million.

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, 2007 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. There have been no changes, since this last formal assessment, that have materially affected, or are reasonably likely to materially affect the Company's disclosure controls and procedures.

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.

Seasonal Variability of Results

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

Selected Quarterly Financial Information

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

Quarterly Consolidated Financial Information

<i>Quarter ended (in thousands of U.S. dollars, except per share amounts)</i>	REVENUES	EBITDA	NET LOSS	BASIC AND		BASIC AND
		REPOSITIONING BEFORE EXPENSES	CONTINUING FROM OPERATIONS	PER SHARE FROM CONTINUING OPERATIONS	NET LOSS	
	\$	\$	\$	\$	\$	\$
2008						
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)
2006						
October 31	150,521	14,667	(23,324)	(\$0.25)	(22,416)	(\$0.24)

Additional Information

Share Capital

As of July 31, 2008, the Company had 90,749,388 restricted voting shares outstanding and 150,000 each of Class I Preferred Shares, Series C (convertible preferred shares) and Series D (special voting preferred shares). Each Class I Preferred Shares, Series C was convertible into 232.9569 Patheon restricted voting shares. As at July 31, 2008 the Company had 6,169,770 stock options outstanding, of which 3,192,093 were exercisable.

The Company has entered into an agreement with JLL under which JLL has agreed to waive its right to the mandatory redemption provision of the Company's convertible preferred shares. For further information please refer to the "Recent Developments" section of this MD&A.

Related Party Transactions

Revenues from companies controlled by a director and significant shareholder of the Company were in the amount of \$0.2 million and \$0.3 million for the three and nine months ended July 31, 2008, respectively. The revenues were \$0.1 million and \$0.7 million for the three and nine months ended July 31, 2007, respectively. These transactions were conducted in the normal course of business and are recorded at the exchanged amount. Accounts receivable at July 31, 2008 include a balance of \$1.0 million (October 31, 2007 - \$0.4 million) resulting from these transactions.

As at July 31, 2008, the Company has an investment of \$2.1 million (October 31, 2007 - \$0.7 million) representing an 18% interest in two Italian companies (collectively referred to as "BSP Pharmaceuticals") whose largest investor is an officer of the Company. BSP Pharmaceuticals specializes in the manufacturing of cytotoxic pharmaceutical products. On July 2, 2008 the Company signed a shareholders' agreement with the other investors in BSP Pharmaceuticals, the terms of which provide the Company with significant influence over the strategic operating, investing and financing policies of BSP Pharmaceuticals. As a result the Company is now accounting for its

investment in BSP Pharmaceuticals using the equity method. Accordingly, for the three and nine months ended July 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 were \$0.5 million and \$1.3 million for the three and nine months ended July 31, 2008, respectively. The management fees were \$0.4 million and \$1.1 million for the three and nine months ended July 31, 2007, respectively. Accounts receivable at July 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.

Public Securities Filings

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

Outlook

Due to normal summer shut downs, particularly in Europe, revenues for the fourth quarter of 2008 are expected to be lower than revenues for the third quarter of 2008 and are subject to fluctuations in the strength of the U.S. dollar.

These expectations are based on internal management forecasts which 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 three and six months ended April 30, 2008 that it anticipated that revenues for the third quarter of 2008 would be slightly higher than the second quarter of 2008. Revenues reported in the third quarter of 2008 exceeded second quarter revenues by \$9.0 million, representing an increase of 4.8%.

FORWARD-LOOKING STATEMENTS

This MD&A contains forward-looking statements which reflect management's expectations regarding the Company's future growth, results of operations, performance (both operational and financial) and business prospects and opportunities. Wherever possible, words such as "plans", "expects" or "does not expect", "forecasts", "anticipates" or "does not anticipate", "believes", "intends" and similar expressions or statements that certain actions, events or results "may", "could", "would", "might" or "will" be taken, occur or be achieved have been used to identify these forward-looking statements. Although the forward-looking statements contained in this MD&A reflect management's current assumptions based upon information currently available to management and based upon what management believes to be reasonable assumptions, the Company cannot be certain that actual results will be consistent with these forward-looking statements. Current material assumptions relate to customer volumes, regulatory compliance and foreign exchange rates. Forward-looking statements necessarily involve significant known and unknown risks, assumptions and uncertainties that may cause the Company's actual results, performance, prospects and opportunities in future periods to differ materially from those expressed or implied by such forward-looking statements. These risks and uncertainties include, among other things: the inability to complete transactions as a result of the failure to satisfy the closing conditions, including the receipt of regulatory approvals, regulatory approval of and market demand for client products; credit and client concentration; the ability to identify and secure new contracts; regulatory matters, including compliance with pharmaceutical regulations; international operations risks; exposure to foreign currency risks; competition; product liability claims; intellectual

property; environmental, health and safety risks; substantial financial leverage; interest rates; proposed divestiture of the Carolina site; initiatives to reduce operating expenses; use of non-GAAP financial measures, significant shareholders; risks associated with information systems; and supply arrangements. Although the Company has attempted to identify important risks and factors that could cause actual actions, events or results to differ materially from those described in forward-looking statements, there may be other factors and risks that cause actions, events or results not to be as anticipated, estimated or intended. There can be no assurance that forward-looking statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. Accordingly, readers should not place undue reliance on forward-looking statements. These forward-looking statements are made as of the date of this MD&A and, except as required by law, the Company assumes no obligation to update or revise them to reflect new events or circumstances.

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