Pediapharm inc.

Canada's Leading Pediatric Pharmaceutical Company

MANAGEMENT DISCUSSION AND ANALYSIS
FOR THE THREE MONTH PERIOD ENDED JUNE 30, 2014

DATED AUGUST 28, 2014

SCOPE OF THIS MANAGEMENT DISCUSSION & ANALYSIS AND NOTICE TO INVESTORS

This management discussion and analysis of financial position and results of operations ("MD&A"), is prepared as of August 28, 2014, and complements the unaudited condensed interim consolidated financial statements of Pediapharm Inc. ("Pediapharm" or the "Company"), which include Pediapharm Licensing Inc., its wholly owned subsidiary, for the three month period ended June 30, 2014, which are compared to the three month period ended June 30, 2013.

All financial information has been prepared in accordance with International Financial Reporting Standards ("IFRS") and all amounts are in Canadian dollars unless otherwise indicated. The condensed interim consolidated financial statements and related notes have been prepared in accordance with IAS 34, Interim Financial Reporting, as issued by the International Accounting Standards Board. They do not contain all the information required to be disclosed in annual financial statements. Certain information and notes usually provided in the annual financial statements have been omitted or condensed when not deemed essential to the understanding of the interim financial information of the Company. Therefore, this MD&A should be read in conjunction with the information contained in the audited consolidated financial statements of the Company and the notes thereto for the fifteen month period ended March 31, 2014.

The unaudited condensed interim consolidated financial statements and the MD&A have been reviewed by the audit committee and approved by the Company's Board of Directors on August 28, 2014. These documents and more information about the Company are available on SEDAR at www.sedar.com.

FORWARD LOOKING STATEMENTS

Certain statements made in this MD&A are forward-looking statements or information. The Company is hereby providing cautionary statements identifying important factors that could cause the Company's actual results to differ materially from those projected in the forward-looking statements. Any statements that express, or involve discussions as to, expectations, beliefs, plans, objectives, assumptions or future events or performance (often, but not always, through the use of words or phrases such as "may", "is expected to", "anticipates", "estimates", "intends", "plans", "projection", "could", "vision", "goals", "objective" and "outlook") are not historical facts and may be forward-looking and may involve estimates, assumptions and uncertainties which could cause actual results or outcomes to differ materially from those expressed in the forward-looking statements. In making these forward-looking statements, the Company has assumed that the current market will continue and grow and that the risks listed below will not adversely impact the business of the Company. By their nature, forward looking statements involve numerous assumptions, inherent risks and uncertainties, both general and specific, which contribute to the possibility that the predicted outcomes may not occur or may be delayed. The risks, uncertainties and other factors, many of which are beyond the control of the Company that could influence actual results include, but are not limited to: future capital requirements and dilution; intellectual property protection and infringement risks; competition (including potential for generic competition); reliance on key management personnel;. Pediapharm's ability to implement its business plan; regulatory approval by the Canadian Health authorities; product reimbursement by third party payers; patent litigation or patent expiry; litigation risk; stock price volatility; government regulation; potential third party claims. The Company's expected revenue in the Future Outlook section is based on historical revenue growth. Further, unless otherwise noted, any forward-looking statement speaks only as of the date of this MD&A, and, except as required by applicable law, the Company does not undertake any obligation to update any forward-looking statement to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events. New factors emerge from time to time, and it is not possible for management to predict all such factors and to assess in advance the impact of each such factor on the business of the Company, or the extent to which any factor or combination of factors may cause actual results to differ materially from those contained in any forward-looking statement.

KEY HIGHLIGHTS-PERIOD ENDED JUNE 30, 2014

- Total revenues for the three-month period ended June 30, 2014 increased by 30% compared to the three-month period ended March 31, 2014. This supports management's view that, despite the previously announced termination of the Sanofi agreement, the Company is achieving substantial growth with its existing portfolio of products;

- NYDA®, a breakthrough treatment for head lice and its eggs, is a major contributor to the revenue growth and is on track to reach over $2,000,000 in revenue in the year ended March 31, 2015 ("fiscal 2015");

- The Company has over $5,750,000 of working capital as of June 30, 2014;

- As a result of its on-going business development efforts, Pediapharm has several potential product acquisitions and licensing agreements under due diligence review;

- The Easyhaler®-budesonide filing is currently under review by Health Canada after clearing the screening process in July 2014;

- On April 4, 2014, the Company entered into an exclusive supply and distribution agreement with Merz Pharma Canada, Ltd. regarding the Canadian rights to CUVPOSA™ (glycopyrrolate) oral solution intended for pediatric chronic severe drooling (sialorrhea) associated with neurologic conditions such as cerebral palsy. Pediapharm believes that CUVPOSA™ will most likely be the first product to be officially approved in Canada to treat that disease and as such, the Company is hoping to be granted a Special Access Program and a priority review from Health Canada.

- Termination of promotional sales agreements with Sanofi Canada ("Sanofi") for Suprax® and Allerject™, effective June 30, 2014. While this was disappointing news for the Company, Pediapharm knows this was not due to its own performance, as revenues for these products had experienced significant growth. In fact, the Company had tremendous success in more than doubling the revenues from Suprax® within 4 years. Furthermore, Suprax® is expected to be in a shortage situation until September 2015, as can be seen on Health Canada's website named www.drugshortage.ca.

SUBSEQUENT EVENTS

On July 2, 2014, the Company entered into its first asset purchase agreement by acquiring the Canadian rights of naproxen suspension from Hoffman La Roche (Roche). Roche will retain the Naprosyn™ trademark and retains all product rights to the other oral dosage forms under this brand. This product in its suspension form is only available under prescription (Rx) and is indicated for the treatment of osteoarthritis, rheumatoid arthritis, ankylosing spondylitis, and juvenile rheumatoid arthritis. Due to the significant unmet medical need, it will be reintroduced to the market as *Pediapharm naproxen suspension*.

On July 24, 2014, Pediapharm announced that a Special Access Program' (SAP) from Health Canada has been initiated for Naproxen suspension. This program allows physicians to prescribe the product to their patients when no commercially alternatives are available. This program has been initiated at the request of physicians mainly treating patients suffering of Juvenile Rheumatoid Arthritis (JRA). The product will be made available through Pediapharm and the SAP will be in place until the availability of Pediapharm Naproxen Suspension, which is expected to be in the first quarter of 2015 (calendar year).

FUTURE OUTLOOK

Despite the termination of the agreement with Sanofi, the Company strives to achieve revenue growth in fiscal 2015. The Company's focus remains to execute its commercial plan with existing products, such as NYDA®, a revolutionary treatment indicated for eradication of head lice and its eggs. NYDA® is on track to reach over $2,000,000 in revenue in fiscal 2015 and has the potential to achieve peak revenues of $6,000,000 to $8,000,000 by fiscal 2018.

The Company has four products presently under review with Health Canada or in the process of being filed for approval from Health Canada. The following represents a list of these products: Easyhaler®-budesonide, Pediapharm Naproxen suspension, Cesinex® and CUVPOSA™. The 2 most advanced files are Easyhaler®-budesonide and Pediapharm Naproxen suspension with an estimated product launch by March 2015. Easyhaler®-budesonide will be competing in a market of $195 million and Pediapharm Naproxen suspension in a market of $76 million, including $8 million of the suspension form.

The Company's core strategy regarding business development remains to acquire exclusive licensing agreements (commonly known as "in-licensing"), as well as products currently marketed in Canada, such as the aforementioned recent acquisition from Hoffmann-La Roche Limited. Before the end of fiscal 2015, Pediapharm expects to sign more license agreements and strives to acquire another product currently marketed in Canada. This strategy will put Pediapharm in a strong position to further sustain its future growth. Simultaneously, the Company is seeking for a Canadian commercial agreement, similar to the aforementioned Sanofi agreement, in order to optimize its short-term revenues and profits.

In summary, Pediapharm has a strong working capital position with over $5,750,000 as of June 30, 2014. With the excellent sales momentum of its current marketed products portfolio, including NYDA®, the Company continues to make positive steps towards generating positive cash flow. The Company is in the process of assessing more exclusive licensing agreements and potential product acquisitions, and strives to add more products to its portfolio within this fiscal year and for years to come. Pediapharm is a growth company in the high-margin specialty pharmaceutical industry.

CORPORATE STRUCTURE OF PEDIAPHARM

Pediapharm was incorporated in 2003 under the federal laws of Canada and commenced its operations in late 2007. The head office and registered and records office of Pediapharm are both located at 225 - 1 Place du Commerce, Verdun, Québec, H3E 1A2. Pediapharm has one wholly-owned subsidiary, Pediapharm Licensing Inc., which was incorporated in 2011 under the laws of Ontario and was granted a drug establishment license by Health Canada. The registered office of Pediapharm Licensing Inc. is located at 4 Innovation Drive, Dundas, Ontario L9H 7P3. The Board of Directors of the Company has decided, following the amalgamation with Chelsea Acquisition Corporation completed on December 10, 2013, to change the Company's financial year-end from December 31 to March 31. Pursuant to section 4.8 of National Instrument 51-102 – *Continuous Disclosure Obligations*, the Company has filed on SEDAR a Notice of Change in Year End providing information about the length and filing dates of its annual audited financial statements and interim financial statements for both its transition year and subsequent financial years.

BUSINESS OVERVIEW OF PEDIAPHARM

Pediapharm is a specialty pharmaceutical corporation that distributes innovative prescription medicines used to treat pathological conditions that mainly affect children from infancy to eighteen (18) years of age. The products that Pediapharm distributes originate from transactions whereby Pediapharm either acquires intellectual property rights through a licensing agreement (commonly known as "in-licensing") that enables

Pediapharm to register the drug products with Health Canada in order to commercialize them. As such, Pediapharm does not produce, manufacture or develop products, but rather licenses finished products and sells them. Pediapharm may also acquire products that are already commercialized in Canada. Pediapharm also commercializes non-prescription products (non-prescription drugs, medical devices, diagnostic products) that are innovative and fulfill unmet medical needs of children.

Pediapharm presently does not develop any of its own products or own any patents, but may eventually partner in low-risk novel formulation development of known drugs in order to make them more amenable for pediatric use.

SELECTED FINANCIAL INFORMATION

FINANCIAL POSITION ANALYSIS

ASSETS

At June 30, 2014, total assets were $7,111,701 as opposed to $8,597,175 at March 31, 2014. Cash has decreased to $5,341,288 as a result of the operating loss, the investment in new assets and the reduction of accounts payable and accrued liabilities. Accounts receivable is up by $221,137 mainly due to higher revenues of the three months ended June 30, 2014 compared with the revenues of the three months ended March 31, 2014. Inventories were down by $88,101, mostly explained by timing of receipts and shipments of goods.

LIABILITIES

At June 30, 2014, total current liabilities were $518,092 compared with $1,371,534 at March 31, 2014. The substantial decrease is primarily due to the payment of invoices that were related to the amalgamation with Chelsea Acquisition Corporation and the listing on the TSX Venture Exchange. Deferred revenue, which consists of amounts received from commission and product sales in advance of revenue recognition, has also decreased substantially from $264,327 to $84,039 as a result of revenue recognition timing.

EQUITY

At June 30, 2014, Shareholders' equity was $6,585,960 compared with $7,220,948 as at March 31, 2014, mostly due to the comprehensive loss for the period and the expenses related to vesting of previously issued stock options.

STOCK OPTIONS

On January 22, 2014, the Company’s Board of Directors approved the grant of 3,585,000 stock options to certain directors, officers and employees of the Company. The options were issued with an exercise price of $0.46 per share and have a term of ten (10) years. In addition, the options have varied vesting provisions such that they vest either over three (3) or four (4) years.

On February 17, 2014, the Company’s Board of Directors approved the grant of 225,000 stock options to an officer of the Company under its employee stock option plan. The options were issued with an exercise price of $0.46 per share, have a term of ten (10) years and have vesting provisions such that they vest over four (4) years.

On May 1, 2014, the Company’s Board of Directors approved the grant of 100,000 stock options to an Investor Relations firm. The options were issued with an exercise price of $0.36 per share for a period of one year. The options granted vest monthly in 12 equal tranches starting on the grant date.

OPERATING RESULTS ANALYSIS

	June 30, 2014 (3 months)	June 30, 2013 (3 months)
Revenue	885,260	851,376
Selling and administrative expenses	1,716,187	1,104,535
Net loss	(812,707)	(359,745)
Cash flow from (used in) operating activities	(1,570,481)	(238,095)
Cash flow from (used in) investing activities	(179,758)	(13,038)
Cash flow from (used in) financing activities	-	9,002

FINANCIAL INFORMATION COMPARISON

REVENUE
For the three months ended June 30, 2014, revenues reached $885,260 compared with revenues of $851,376 in the three months ended June 30, 2013. While there was a very strong revenue growth from NYDA®, it was somewhat offset by a reduction of revenue from sales of Suprax®, as a result of the termination of the Company's promotional sales agreements with Sanofi Canada for Suprax® and Allerject™, effective June 30, 2014.

SELLING AND ADMINISTRATIVE EXPENSES
For the three months ended June 30, 2014, selling and administrative expenses were $1,716,187 (2013 - $1,104,535). The Company has deployed additional efforts in selling & marketing as well as in business development to capitalize on the Company's existing portfolio as well as future products and/or license agreements. Furthermore, the Company has added key management personnel such as the Chief Financial Officer and the newly appointed Vice President, Marketing and Sales, in support of the expected revenue and profit growth. Expenses related to the listing on the TSX Venture Exchange also had an impact when comparing both periods.

COMPREHENSIVE LOSS
The comprehensive loss for the three months ended June 30, 2014 was $812,707 compared to the $359,745 in the three months ended June 30, 2013. The additional efforts in marketing & sales as well as business development are the main reasons for the increased loss. Furthermore, expenses related to the listing on the TSX Venture Exchange also had an impact when comparing both periods.

CASH FLOW ANALYSIS

Operating activities
For the three months ended June 30, 2014, cash flows used in operating activities was $1,570,481 compared with $238,095 for the three months ended June 30, 2013. In addition to the comprehensive loss of $812,707, the increase is due to the payment of expenses, with accounts payable and accrued liabilities going from $1,100,315 on March 31, 2014 to $433,303 on June 30, 2014.

Investing activities
Most of the investing activities for Pediapharm involve the purchase of licenses, as well as the amortization

charges as per Pediapharm's accounting policies.

For the three months ended June 30, 2014, the Company purchased intangible assets in the amount of $167,301. The majority of this amount included a down payment for a licensing/distribution agreement.

Financing activities
For the three months ended June 30, 2014 and 2013, there was no significant activity to report.

SUMMARY OF ANNUAL RESULTS

The following tables set out financial performance highlights for the past three fiscal years.

	Fifteen months ended March 31, 2014	Twelve months ended December 31, 2012	Twelve months ended December 31, 2011
Revenues	$4,681,776	$2,490,503	$1,711,318
Selling and Administrative Expenses	$6,216,605	$4,570,472	$3,678,148
Total comprehensive loss	($4,079,633)	($2,246,068)	($3,588,064)
Cash flow from (used in) operations	($2,010,333)	($1,932,622)	($1,495,206)
Cash & cash equivalents, end of period	$7,092,224	$599,551	$807,801
Assets	$8,597,175	$1,705,991	$1,725,357
Long-term liabilities	$4,693	$10,284,499	$8,428,951
Dividends	$0	$0	$0

SUMMARY OF QUARTERLY RESULTS

Prior to becoming a reporting issuer on December 10, 2013, the Company did not prepare quarterly financial statements. Therefore, the Company is able to provide the last six quarters only.

	Quarter ended	Quarter ended	Quarter ended	Quarter ended	Quarter ended	Quarter ended
	30-Jun-14	31-Mar-14	31-Dec-13	30-Sep-13	30-Jun-13	31-Mar-13
Revenues	$885,260	$677,969	$1,237,538	$1,094,596	$851,376	$821,413
Selling and Administrative Expenses	$1,716,187	$1,772,634	$1,289,916	$1,061,867	$1,104,535	$1,031,633
Total comprehensive loss	($812,707)	($1,566,442)	($1,703,124)	($111,010)	($359,744)	($339,314)
Cash flow from (used in) operations	($1,570,481)	($426,833)	($1,020,399)	($251,593)	($238,095)	($264,997)
Cash & cash equivalents, end of period	$5,341,288	$7,092,224	$6,104,636	$508,046	$346,935	$586,520
Assets	$7,111,701	$8,597,175	$8,262,599	$3,011,612	$1,849,834	$1,962,317
Long-term liabilities	$7,649	$4,693	$573,896	$9,384,684	$8,944,297	$10,428,765
Dividends	$0	$0	$0	$0	$0	$0

LIQUIDITY, CAPITAL RESOURCES AND SOURCES OF FINANCING

Pediapharm finished the three-month period ended June 30, 2014 with cash amounting to $5,341,288, which is in excess of future expected cash outflows for at least the next twelve months. There are no substantial debt or contractual commitment for the next twelve months.

RELATED PARTY TRANSACTIONS

Transactions with related parties during the period and amounts due or from these parties as at June 30, 2014 are disclosed in the consolidated financial statements. All related party transactions, unless otherwise disclosed, occurred in the normal course of operations.

In the three months ended June 30, 2014, the Company paid management fees in the amount of $37,500 (2013 - $0) to a company owned by the current Chief Financial Officer of the Company.

In the three months ended June 30, 2014, the Company paid management fees in the amount of $7,000 (2013 - $0) to a Director of the Company for a project outside of the regular duties of a Director.

In the three months ended June 30, 2014, the Company paid consulting fees in the amount of $0 (2013 - $12,550) to a firm of which a Director of the Company is a partner.

CAPITAL RESOURCES

Pediapharm manages its capital structure and brings about adjustments related to changes in the economic environment and underlying risks of its assets. To preserve or modify its capital structure and to carry on the development and commercialization of technology and fulfill its various financial obligations, Pediapharm may issue additional shares or negotiate new loans.

CONTRACTUAL COMMITMENTS

The future minimum payments required under a long-term operating lease for office space are as follows:

	$
2015	65,604
2016	79,605
2017	70,760

DESCRIPTION OF THE SECURITIES

Pediapharm authorized share capital consists of an unlimited number of Pediapharm Common Shares. As of August 28, 2014, Pediapharm has 72,055,856 shares outstanding. There have been no dividends declared during the current period.

OFF -BALANCE SHEET ARRANGEMENTS

The Company has no off-balance sheet arrangements.

SIGNIFICANT ACCOUNTING POLICIES

The Company prepares its consolidated financial statements in accordance with IFRS, which require management to make estimates and assumptions that affect the amounts of its assets and liabilities, the information provided with regard to future assets and liabilities as well as the amounts of revenues and expenses for the relevant periods.

The elements in the financial statements that require more use of estimates include valuation of stock options and warrants and impairment of fixed and intangible assets. Actual results may differ from these estimates, but management believes they will not result in material changes versus the results being presented. Readers are invited to refer to the audited consolidated financial statements for the period ended March 31, 2014 for a full description of the significant accounting policies of the Company at that date.

FUTURE CHANGES IN ACCOUNTING POLICIES

The IASB previously published versions of IFRS 9, *Financial Instruments*, that introduced new classification and measurement requirements in 2009 and 2010 and a new hedge accounting model in 2013. In July 2014, the IASB released the final version of IFRS 9, *Financial Instruments*, which replaces earlier versions of IFRS 9 issued and completes the IASB's project to replace IAS 39, *Financial Instruments: Recognition and Measurement*. The standard is effective for annual periods beginning on or after January 1st, 2018, with earlier application permitted. Pediapharm is currently evaluating the impact of the standard on its consolidated financial statements. There are no other IFRS or International Financial Reporting Interpretation Committee interpretations that are not yet effective that would be expected to have a material impact on Pediapharm.

Readers are referred to the more detailed information described in other disclosure documents filed with the applicable Canadian securities regulatory authorities and available at www.sedar.com .

Management of Pediapharm Inc.