Pediapharm Inc.

Condensed Interim Consolidated Financial Statements (unaudited)

For the three-month periods ended June 30, 2018 and 2017

(expressed in Canadian dollars)

Notice to Reader

The accompanying unaudited condensed interim consolidated financial statements of PEDIAPHARM INC. (the "Company") for the periods of three months ended on June 30, 2018 and 2017 have been prepared by the management and are its responsibility. These unaudited condensed interim consolidated financial statements, together with the accompanying notes, have been reviewed and approved by the members of the Company's audit committee. These unaudited condensed interim consolidated financial statements have not been reviewed by the Company's auditors.

Pediapharm Inc.

Condensed Interim Consolidated Statements of Financial Position (unaudited)

(expressed in Canadian dollars)

	Note	As at June 30, 2018 $	As at March 31, 2018 $
Assets			
Current assets			
Cash and cash equivalents		3,267,600	3,608,506
Accounts receivable		1,240,605	738,454
Prepaid expenses and deferred costs		182,697	98,795
Inventories		1,817,966	2,189,278
		6,508,868	6,635,033
Property and equipment		18,520	20,099
Intangible assets		2,533,238	2,602,330
		9,060,626	9,257,462
Liabilities			
Current liabilities			
Accounts payable and accrued liabilities		2,019,597	1,688,454
Interest payable	3, 4	166,834	165,613
Convertible debentures		20,000	20,000
		2,206,431	1,874,067
Convertible debentures	3	4,457,939	4,345,627
		6,664,370	6,219,694
Shareholders' Equity			
Share capital		25,347,384	25,347,384
Contributed surplus		4,953,143	4,902,565
Deficit		(27,904,271)	(27,212,181)
		2,396,256	3,037,768
		9,060,626	9,257,462

Approved by the Board of Directors on August 27, 2018

_______________*(Sylvain Chretien)*______ Director   ________*(Normand Chartrand)*_________ Director

Sylvain Chretien   Normand Chartrand

The accompanying notes are an integral part of these consolidated financial statements.

Pediapharm Inc.

Condensed Interim Consolidated Statements of Income (Loss) and Comprehensive Income (Loss) (unaudited)

(expressed in Canadian dollars)

	Note	For the 3-month period ended June 30, 2018 $	For the 3-month period ended June 30, 2017 $
Revenue			
Products		3,249,139	2,462,845
Commissions		-	2,705
		3,249,139	2,465,550
Cost of sales		1,511,139	1,178,501
Gross profit		1,738,000	1,287,049
Selling and administrative expenses	5, 8	2,149,219	2,134,515
Depreciation and amortization		1,929	3,088
Foreign exchange loss (gain)		8,998	(12,793)
Operating income (loss)		(422,146)	(837,761)
Financing costs	4	279,146	285,905
Interest income		(9,202)	(5,738)
Net income (loss) and comprehensive income (loss)		(692,090)	(1,117,928)
Net income (loss) per share attributable to shareholders of the Company			
Basic and diluted		(0.008)	(0.014)
Weighted average number of common shares outstanding		87,414,986	78,850,021

The accompanying notes are an integral part of these consolidated financial statements.

Pediapharm Inc.

Condensed Interim Consolidated Statements of Changes in Shareholders' Equity (unaudited)

(expressed in Canadian dollars)

	Note	Share capital				
		Common shares	Amount $	Contributed surplus $	Deficit $	Total shareholders' equity $
Balance – March 31, 2017		72,709,103	21,025,018	3,862,379	(23,591,761)	1,295,636
Loss and comprehensive loss		-	-	-	(1,117,928)	(1,117,928)
Share-based compensation – Stock option plan		-	-	95,753	-	95,753
Issuance of shares for private placement, net of fees	9	14,705,883	4,983,242	-	-	4,983,242
Issuance of warrants for private placement	9		(776,772)	776,772		-
Balance – June 30, 2017		87,414,986	25,231,488	4,734,904	(24,709,689)	5,256,703
Balance – March 31, 2018		87,414,986	25,347,384	4,902,565	(27,212,181)	3,037,768
Loss and comprehensive loss		-	-	-	(692,090)	(692,090)
Share-based compensation – Stock option plan		-	-	50,578	-	50,578
Balance – June 30, 2018		87,414,986	25,347,384	4,953,143	(27,904,271)	2,396,256

Authorized shares

The Company is authorized to issue an unlimited number of common shares without par value.

The accompanying notes are an integral part of these consolidated financial statements.

Pediapharm Inc.

Condensed Interim Consolidated Statements of Cash Flows (unaudited)

(expressed in Canadian dollars)

	Note	For the 3-month period ended June 30, 2018 $	For the 3-month period ended June 30, 2017 $
Cash flows from			
Operating activities			
Net loss for the year		(692,090)	(1,117,928)
Adjustments for			
Depreciation of property and equipment		1,579	2,482
Amortization of intangible assets		76,472	42,430
Share-based compensation expense		50,578	95,753
Interest on convertible debentures	4	166,833	166,833
Convertible debenture interest accretion net of deferred financing cost amortization	4	112,313	119,072
Interest income		(9,202)	(5,738)
		(293,517)	(697,096)
Changes in non-cash operating working capital items	7	116,402	(1,218,335)
Interest paid		(165,613)	(165,000)
Interest received		9,202	5,738
		(333,526)	(2,074,693)
Investing activities			
Purchases of property and equipment		-	(2,368)
Purchases of intangible assets		(7,380)	(295,900)
		(7,380)	(298,268)
Financing activities			
Proceeds from issuance of shares, net of issuance costs	9	-	4,983,242
		-	4,983,242
Net change in cash and cash equivalents during the year		(340,906)	2,610,281
Cash and cash equivalents – Beginning of year		3,608,506	3,241,097
Cash and cash equivalents – End of year		3,267,600	5,851,378

The accompanying notes are an integral part of these consolidated financial statements.

1 Incorporation and nature of activities

Pediapharm Inc. (the "Company") was incorporated under the Canada Business Corporations Act and sells products and offers marketing services, particularly related to pediatric care, to the pharmaceutical industry. The Company is domiciled in Canada, and its registered office is located at 1 Place du Commerce, Suite 225, Verdun, Quebec H3E 1A2. Pediapharm Inc.'s shares are traded on the TSX Venture Exchange.

2 Basis of presentation and summary of significant accounting policies

Basis of presentation

The Company prepares its condensed interim consolidated financial statements in accordance with Canadian generally accepted accounting principles (GAAP) as set out in Part I of the CPA Canada Handbook – Accounting, which incorporates International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB).

The policies applied in these condensed interim consolidated financial statements are based on IFRS issued and outstanding as of August 27, 2018.

The condensed interim consolidated financial statements have been prepared under the historical cost basis, except for certain financial instruments which are measured at fair value. In addition, the condensed interim consolidated financial statements have been prepared using the accrual basis of accounting, except for cash flow information.

Basis of consolidation

Subsidiaries are all entities over which the Company has the power to govern the financial and operating policies to obtain benefits from its activities. Subsidiaries are fully consolidated from the date control is obtained, and they are deconsolidated on the date control ceases. These condensed interim consolidated financial statements include the Company's one inactive subsidiary, Pediapharm Licensing Inc.

New standards adopted by the Company

IFRS 9, Financial Instruments

The IASB previously published versions of IFRS 9 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, 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 1, 2018, with earlier application permitted. The Company assessed the impact of the adoption of IFRS 9 on its consolidated financial statements and determined that there were no significant changes from the adoption of the new standard.

IFRS 15, Revenue from Contracts with Customers

IFRS 15 is effective for annual periods beginning on or after January 1, 2018. IFRS 15 specifies how and when to recognize revenue as well as requires entities to provide users of financial statements with more informative, relevant disclosures. The standard supersedes IAS 18, Revenue, and a number of revenue-related interpretations. The new standard applies to nearly all contracts with customers: the main exceptions are leases, financial instruments and insurance contracts. The Company assessed the impact of adoption of IFRS 15 on its financial statements, by reviewing selected revenue arrangement and assessing the differences in accounting for such contracts under the new guidance as compared with previous revenue accounting standards, and determined that there were no significant changes from the adoption of the new standard. The Company adopted the new guidance using the modified retrospective approach, under which the new guidance was adopted retrospectively with the cumulative effect of initial application of the guidance recognized on April 1, 2018.

New standards not yet adopted by the Company

IFRS 16, Leases

In January 2016, the IASB released IFRS 16. The new standard eliminates the classification of leases as either operating or finance leases and introduces a single accounting model for the lessee under which a lease liability and a right-of-use asset is recognized for all leases with a term of more than 12 months. IFRS 16 also substantially carries forward the lessor accounting requirements; accordingly, a lessor continues to classify its leases as operating leases or finance leases. IFRS 16 supersedes IAS 17, Leases, and related interpretations. IFRS 16 is effective for annual periods beginning on January 1, 2019 for the Company, with earlier application permitted for companies that also apply IFRS 15. The Company is currently evaluating the impact of the new standard on its consolidated financial statements.

There are no other IFRSs or IFRIC Interpretations that are not yet effective that would be expected to have a material impact on the Company.

3 Convertible debentures

On January 31, 2018, the Company announced it had entered into agreements to extend $5,480,000 of the total debentures issued to holders (Holders) in connection with the original private placement. The extension is to be one year in length, making the new maturity date March 30, 2020 (the New Maturity Date). Any such extensions that are not approved by the individual Holders will remain subject to the original terms of the debentures and shall mature on March 30, 2019 (the Original Maturity Date). A total of $20,000 was not extended and will therefore mature on the Original Maturity Date.

The extension of the debentures was not considered as a substantial modification of the terms of the existing financial liabilities and do not result in a derecognition of the original financial liabilities under IAS 39. The impact of the extension of the maturity date results in a gain of $475,702 in the consolidated statement of loss and comprehensive loss (note 13) due to the revaluation of the fair value with the New Maturity Date.

(expressed in Canadian dollars)

The convertible debentures bear interest at a rate of 12% per annum paid quarterly in cash, and they are fully secured by the assets of the Company. The principal amount is convertible at any time at the option of the holder into common shares of the Company at a price of $0.45 per common share, and, upon giving effect to such conversion, all accrued and unpaid interest will be paid in full. The debentures will automatically convert into common shares at the conversion price if, during any 20 consecutive trading days, the common shares trade at a volume weighted average price of at least $0.60 on a total cumulative volume of not less than 2,000,000 shares. The Company may at any time after the second anniversary of the date of issue, which was March 30, 2015, and prior to maturity, repay the principal amount subject to an early repayment fee of 2% of the principal amount repaid. Issuance costs were deducted from the convertible debentures balance and are amortized using the effective interest method.

The convertible debentures are a compound financial instrument under IAS 32, and have both a liability and equity component. The fair value of the consideration for the compound instrument must be split into its liability and equity components. The fair value of the consideration in respect of the liability component is first measured at the fair value of a similar liability that does not have any associated equity conversion option. This becomes the liability component's carrying amount at initial recognition, and the residual amount is allocated to the equity component..

4 Financing costs

	For the 3-month period ended June 30, 2018 $	For the 3-month period ended June 30, 2017 $
Interest on convertible debentures	166,833	166,833
Convertible debenture interest accretion net of deferred financing cost amortization	112,313	119,072
	279,146	285,905

(expressed in Canadian dollars)

5 Employee benefit expense

a) Employees other than the Company's president, chief financial officer and vice-presidents

	Note	For the 3-month period ended June 30, 2018 $	For the 3-month period ended June 30, 2017 $
Salaries and benefits		582,455	497,101
Share-based compensation		11,753	32,837
		594,208	529,938

b) Key management personnel consist of the Company's president, chief financial officer, vice-presidents and Board of Directors.

	Note	For the 3-month period ended June 30, 2018 $	For the 3-month period ended June 30, 2017 $
Key management compensation			
Short-term employee benefits and consulting fees		362,144	384,274
Share-based compensation		38,825	62,915
		400,969	447,189

Key management compensation is included in selling and administrative expenses.

6 Related party transactions

Transactions with related parties during the period and amounts due to or from these parties as at June 30, 2018 and 2017 are disclosed in these condensed interim consolidated financial statements.

All related party transactions, unless otherwise disclosed, occurred in the normal course of operations.

For the three-month period ended June 30, 2018, the Company incurred a total of $12,133 in interest expense on the convertible debentures with 9346-4646 Québec Inc. and two Board members.

(expressed in Canadian dollars)

7 Consolidated statement of cash flows

Changes in non-cash operating working capital items are as follows:

	For the 3-month period ended June 30, 2018 $	For the 3-month period ended June 30, 2017 $
Decrease (increase) in		
Accounts receivable	(502,151)	(705,873)
Prepaid expenses	(83,902)	(22,141)
Inventories	371,312	(415,603)
Increase (decrease) in		
Accounts payable and accrued liabilities	331,143	(74,718)
	116,402	(1,218,335)

8 Selling and administrative expenses

	For the 3-month period ended June 30, 2018 $	For the 3-month period ended June 30, 2017 $
Sales and marketing expenses	1,425,878	1,413,156
Business development and regulatory affairs	214,926	200,793
General administrative	508,415	520,566
	2,149,219	2,134,515

9 Non-brokered private placement

On May 24, 2017, the Company closed a non-brokered private placement of 14,705,883 units at a price of $0.34 per unit for gross proceeds of $5,000,000 with 9346-4626 Québec Inc., a private company operating as Transican (the subscriber). The total gross proceeds were allocated between common shares and warrants for amounts of $4,359,892 and $640,108, respectively.

Each unit comprises one common share in the capital of the Company and ½ of one common share purchase warrant of the Company. Each whole warrant entitles the subscriber to purchase one common share at a price of $0.51 per share until May 24, 2020. The fair value of the warrants, using the Black-Scholes model, was value at $0.0435 per ½ warrant. The assumptions used were expected volatility of 66.5%, a risk free rate of 0.78%, an expected life of three years, and an exercise price of $0.51 per common share. No commissions or fees were paid in connection with the offering, other than $43,035 in legal fees.

As a result of the closing of the transaction, the subscriber has become a new shareholder of the Company as a holder of more than 10% of the issued and outstanding common shares.