

Pediapharm Inc.

Condensed Consolidated Interim Financial
Statements (unaudited)
(expressed in Canadian dollars)

For the three and six month periods ended
September 30, 2014 and 2013

Notice to Reader

The accompanying unaudited condensed interim consolidated financial statements of PEDIAPHARM INC. (the "Corporation") for the periods of three and six months ended on September 30, 2014 and 2013 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 Corporation's audit committee. These unaudited condensed interim consolidated financial statements have not been reviewed by the Corporation's auditors.

Pediapharm Inc.

Condensed Interim Consolidated Statement of Financial Position

(unaudited)

(expressed in Canadian dollars)

	As at September 30, 2014 \$	As at March 31, 2014 \$
Assets		
Current assets		
Cash and cash equivalents	4,401,313	7,092,224
Accounts receivable	488,022	427,727
Prepaid expenses	21,298	55,376
Inventories	353,602	348,144
	<u>5,264,235</u>	<u>7,923,471</u>
Property and equipment	73,205	22,504
Intangible assets		
Product & licencing rights	833,721	643,826
Other	7,594	7,374
	<u>841,315</u>	<u>651,200</u>
	<u>6,178,755</u>	<u>8,597,175</u>
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	582,368	1,100,315
Deferred revenue	4,040	264,327
Current portion of long-term debt		6,892
	<u>586,408</u>	<u>1,371,534</u>
Long-term debt	6,688	4,693
	<u>593,096</u>	<u>1,376,227</u>
Shareholders' Equity		
Share capital	20,779,567	20,779,567
Contributed surplus	1,267,366	903,012
Deficit	<u>(16,461,274)</u>	<u>(14,461,631)</u>
	<u>5,585,659</u>	<u>7,220,948</u>
	<u>6,178,755</u>	<u>8,597,175</u>

Approved by the Board of Directors on November 28, 2014

(Sylvain Chretien)

Director

(Normand Chartrand)

Director

Sylvain Chretien

Normand Chartrand

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

Pediapharm Inc.

Condensed Interim Consolidated Statement of Comprehensive Loss

(unaudited)

(expressed in Canadian dollars)

		For the 3-month period ended September 30, 2014 \$	For the 3-month period ended September 30, 2013 \$	For the 6-month period ended September 30, 2014 \$	For the 6-month period ended September 30, 2013 \$
Revenue		928,257	1,094,596	1,806,992	1,945,972
Expenses (income)					
Selling and administrative	5, 8	2,121,969	1,061,868	3,831,630	2,166,403
Finance costs	4	218	141,995	487	251,433
Foreign exchange losses (gains)		6,884	1,842	7,580	794
Interest income		(13,877)	(99)	(33,062)	(1,903)
		2,115,194	1,205,606	3,806,635	2,416,727
Loss and comprehensive loss for the period		(1,186,937)	(111,010)	(1,999,643)	(470,755)
Loss per share from continuing operations attributable to equity holders of the Company					
Basic and diluted		(0.02)	(0.01)	(0.03)	(0.06)
Weighted average number of common shares outstanding		72,055,856	8,160,000	72,055,856	8,160,000

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

Pediapharm Inc.

Condensed Interim Consolidated Statement of Changes in Equity

(unaudited)

(expressed in Canadian dollars)

	Share capital \$	Contributed surplus \$	Deficit \$	Total shareholders' equity (deficiency) \$
Balance – April 1, 2013	1,000	979,467	(10,525,494)	(9,545,027)
Loss and comprehensive loss for the period	-	-	(470,752)	(470,752)
Share-based compensation – Stock option plan	-	54,800	-	54,800
Balance – September 30, 2013	<u>1,000</u>	<u>1,034,267</u>	<u>(10,996,246)</u>	<u>9,960,979</u>
Balance – April 1, 2014	20,779,567	903,012	(14,461,631)	7,220,948
Loss and comprehensive loss for the period	-	-	(1,999,643)	(1,999,643)
Share-based compensation – Stock option plan	-	364,354	-	364,354
Balance – September 30, 2014	<u>20,779,567</u>	<u>1,267,366</u>	<u>(16,461,274)</u>	<u>5,585,659</u>

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

Pediapharm Inc.

Condensed Interim Consolidated Statement of Cash Flows

(unaudited)

(expressed in Canadian dollars)

Note	For the 3-month period ended September 30, 2014 \$	For the 3-month period ended September 30, 2013 \$	For the 6-month period ended September 30, 2014 \$	For the 6-month period ended September 30, 2013 \$
Cash flows from				
Operating activities				
Loss for the period	(1,186,937)	(111,010)	(1,999,643)	(470,755)
Adjustments for				
Depreciation of property and equipment	4,313	1,682	6,051	1,377
Amortization of intangible assets	22,160	20,070	44,035	39,451
Amortization of financing fees related to term loans		4,685		(1,131)
Share-based compensation expense	186,635	27,402	364,354	54,803
Interest on long-term debt		117,457		240,626
Interest income	(13,876)	(99)	(33,062)	(1,903)
Amortization of warrants		19,855		39,709
Unrealized foreign exchange loss	6,884	1,842	7,580	794
Deferred share units				10,500
	(980,821)	81,884	(1,610,685)	(86,529)
Changes in non-cash operating working capital items	7 146,708	(299,831)	(809,909)	(313,854)
Interest paid	(1,710)	(33,745)	(4,896)	(89,713)
Interest received	13,876	99	33,062	1,903
	(821,947)	(251,593)	(2,392,428)	(488,193)
Investing activities				
Purchases of property and equipment	(44,297)	(1,502)	(56,754)	(10,173)
Purchases of intangible assets	(66,848)	(834)	(234,149)	(5,200)
	(111,145)	(2,336)	(290,903)	(15,373)
Financing activities				
Proceeds from long-term debt and warrants, net of issuance costs		416,883		425,886
		416,883		425,886
Foreign exchange impact on cash	(6,883)	(1,842)	(7,580)	(794)
Net change in cash and cash equivalents during the period	(939,975)	161,112	(2,690,911)	(78,474)
Cash and cash equivalents – Beginning of period	5,341,288	346,934	7,092,224	586,520
Cash and cash equivalents – End of period	4,401,313	508,046	4,401,313	508,046

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

Pediapharm Inc.

Notes to Condensed Consolidated Interim Financial Statements (unaudited)

September 30, 2014 and 2013

(expressed in Canadian dollars)

1 Incorporation and nature of activities

Pediapharm Inc. (the “Company”) was incorporated under the Canada Business Corporations Act and offers sales and marketing services to the pharmaceutical industry, particularly related to pediatric care. 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 Stock Exchange.

The Board of Directors of the Company 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.

2 Basis of presentation and summary of significant accounting policies

Basis of presentation

The key accounting policies applied in the preparation of these condensed interim consolidated financial statements are consistent with those disclosed in Note 2 of the Corporation’s consolidated financial statements for the year ended March 31, 2014. These policies have been consistently applied to all periods presented. These condensed consolidated interim financial statements should be read in conjunction with the Corporation’s most recent annual consolidated financial statements for the year ended March 31, 2014.

These consolidated interim financial statements have been prepared in accordance with Part I of the CPA Canada Handbook (referred to as IFRS) as issued by the International Accounting Standards Board (IASB) applicable to the preparation of interim financial statements, IAS 34, *Interim Financial Reporting*.

The policies applied in these consolidated financial statements are based on IFRS issued and outstanding as of November 28, 2014.

The accompanying condensed interim consolidated financial statements were prepared on a going concern basis under the historical cost convention.

3 Share-based compensation

On September 4, 2014, the Company’s Board of Directors approved the grant of 180,000 stock options to a director of the Company who was appointed on June 2, 2014. The options were issued with an exercise price of \$0.30 per share and have a term of ten (10) years. The options vest the following way: 1/3 on September 4, 2014, 1/3 on September 4, 2015 and 1/3 on September 4, 2016.

Pediapharm Inc.

Notes to Condensed Consolidated Interim Financial Statements (unaudited)

September 30, 2014 and 2013

(expressed in Canadian dollars)

On September 4, 2014, the Company's Board of Directors also approved the grant of 80,000 stock options to a new employee who is not an officer of the Company. The options were issued with an exercise price of \$0.30 per share and have a term of ten (10) years. The options vest the following way: 1/4 on September 4, 2015, 1/4 on September 4, 2016, 1/4 on September 4, 2017 and 1/4 on September 4, 2018.

For the three month period ended September 30, 2014, the share-based compensation expense with respect to options amounted to \$186,635 (three month period ended September 30, 2013 – \$27,402) and is included in administrative expenses in the consolidated statement of comprehensive loss.

For the six month period ended September 30, 2014, the share-based compensation expense with respect to options amounted to \$364,354 (six month period ended September 30, 2013 – \$54,803) and is included in administrative expenses in the consolidated statement of comprehensive loss.

As at September 30, 2014, a total of 2,768,919 common shares remained authorized for issuance under the stock incentive plan.

All options granted become immediately exercisable in the event of any change of control of the Company.

4 Finance costs

	For the three-month periods ended September 30,		For the six-month periods ended September 30,	
	2014 \$	2013 \$	2014 \$	2013 \$
Interest on long-term debt	218	117,457	487	222,210
Financing fees		24,538		29,223
	218	141,995	487	251,433

Pediapharm Inc.

Notes to Condensed Consolidated Interim Financial Statements (unaudited)

September 30, 2014 and 2013

(expressed in Canadian dollars)

5 Employee benefit expense

a)

	For the three-month periods ended September 30,		For the six-month periods ended September 30,	
	2014	2013	2014	2013
	\$	\$	\$	\$
Salaries and benefits	512,336	397,300	1,003,984	793,714
Share-based compensation	95,598	6,066	197,311	12,132
	<u>607,934</u>	<u>403,366</u>	<u>1,201,295</u>	<u>805,846</u>

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

	For the three-month periods ended September 30,		For the six-month periods ended September 30,	
	2014	2013	2014	2013
	\$	\$	\$	\$
Key management compensation				
Salaries, short-term employee benefits and consulting fees	236,141	150,144	474,756	300,508
Share-based compensation	91,037	14,666	167,043	29,332
	<u>327,178</u>	<u>164,810</u>	<u>641,799</u>	<u>329,840</u>

Key management compensation is included in administrative expenses.

Pediapharm Inc.

Notes to Condensed Consolidated Interim Financial Statements (unaudited)

September 30, 2014 and 2013

(expressed in Canadian dollars)

6 Related party transactions

Transactions with related parties during the period and amounts due or from these parties as at September 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 September 30, 2014, the Company paid management fees in the amount of \$37,500 (2013 - \$22,500) to a company owned by the current Chief Financial Officer of the Company. In the six months ended September 30, 2014, the Company paid management fees in the amount of \$75,000 (2013 - \$22,500) to a company owned by the current Chief Financial Officer of the Company.

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

In the three months ended September 30, 2014, the Company paid consulting fees in the amount of \$0 (2013 - \$19,664) to a firm of which a Director of the Company is a partner. In the six months ended September 30, 2014, the Company paid consulting fees in the amount of \$0 (2013 - \$32,214) to a firm of which a Director of the Company is a partner.

Pediapharm Inc.

Notes to Condensed Consolidated Interim Financial Statements (unaudited)

September 30, 2014 and 2013

(expressed in Canadian dollars)

7 Cash flows

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

	For the three-month periods ended September 30,		For the six-month periods ended September 30,	
	2014 \$	2013 \$	2014 \$	2013 \$
Decrease (increase) in				
Accounts receivable and prepaid expenses	171,201	(504,342)	(26,217)	(320,212)
Inventories	(93,559)	98,740	(5,458)	(435,820)
Increase (decrease) in				
Accounts payable and accrued liabilities	149,065	129,215	(517,947)	672,078
Deferred revenue	(79,999)	(23,444)	(260,287)	(229,900)
	<u>146,708</u>	<u>(299,831)</u>	<u>(809,909)</u>	<u>(313,854)</u>

8 Selling and administrative expenses

	For the three-month periods ended September 30,		For the six-month periods ended September 30,	
	2014 \$	2013 \$	2014 \$	2013 \$
Sales and marketing expenses	1,235,941	708,047	2,204,069	1,487,360
Business development & regulatory affairs	337,678	115,132	618,817	234,339
General administrative	548,350	238,689	1,008,744	444,704
	<u>2,121,969</u>	<u>1,061,868</u>	<u>3,831,630</u>	<u>2,166,403</u>

Pediapharm Inc.

Notes to Condensed Consolidated Interim Financial Statements (unaudited)

September 30, 2014 and 2013

(expressed in Canadian dollars)

9 Subsequent events

On October 8, 2014, Pediapharm and Laboratorios SALVAT S.A., Ltd. ("SALVAT") announced they have entered into an agreement to grant Pediapharm the exclusive Canadian rights to a novel patented formulation of Ciprofloxacin 0.3% and Fluocinolone Acetonide 0.025% otic solution.