



Q3

Quarterly Report

Third Quarter - Fiscal 2003

Labopharm

Highlights

THIRD QUARTER HIGHLIGHTS

Completed Treatment Stage for US Phase III Clinical Trials for Once-Daily Tramadol

- Labopharm conducted two, double-blind, multi-centre, randomized trials to evaluate the full 24-hour efficacy and safety of the Company's version of once-daily tramadol in reducing moderate to moderately severe pain in patients suffering from osteoarthritis
- Following extensive consultation with the Food & Drug Administration (FDA), protocols for the trials were tailored to meet that organization's requirements for extended-release analgesics
- Data from trials will be combined with data from the previously completed European regulatory submission to form the basis of the Company's NDA submission to the FDA

Concluded Definitive Marketing Agreements for Once-Daily Tramadol for Italy, Spain and Portugal

- Gruppo Angelini (Italy) and Esteve S.A. (Spain and Portugal) will have exclusive rights to market and sell once-daily tramadol in their respective jurisdictions
- Labopharm will supply Angelini and Esteve with finished, packaged product through Labopharm Europe Limited
- Labopharm is finalizing a definitive agreement for France, with Aventis France S.A., and is actively engaged in discussions to establish additional marketing channels for the remainder of Europe, as well as the United States

Completed Equity Financing for Gross Proceeds of \$23,200,520

- Labopharm issued 4.74 million shares at a price of \$4.90 per share
- Proceeds from the offering will be used to support the anticipated commercialization of once-daily tramadol, to advance development of new programs within Labopharm's pipeline, as well as for working capital and general corporate purposes

HIGHLIGHTS SUBSEQUENT TO THIRD QUARTER END**Secured Marketing Agreement for 14 Eastern European Countries**

- CSC Pharmaceuticals will have exclusive rights to market and sell once-daily tramadol in Austria, Bulgaria, Croatia, Czech Republic, Estonia, Federal Republic of Yugoslavia (Serbia and Montenegro), Hungary, Latvia, Lithuania, Macedonia, Poland, Romania, Slovakia and Slovenia
- Countries covered by agreement represent a population totalling 128 million (more than 16% of total European population)
- Labopharm will supply CSC with product through Labopharm Europe Limited

Presented Results of European Phase III Clinical Trial for Once-Daily Tramadol at the Prestigious OsteoArthritis Research Science International (OARSI) World Congress in Berlin, Germany

- Labopharm's once-daily tramadol formulation:
 - Achieved the primary end point of the study, providing a statistically and clinically significant reduction in pain associated with osteoarthritis
 - Demonstrated a superior adverse events profile compared with that of the comparator, a twice-daily formulation of tramadol currently marketed in Europe
 - Provided sustained pain relief for a full 24-hour period, matching the twice-daily formulation dosed twice per day
- Two-thirds of the patients receiving Labopharm's once-daily tramadol required a dose of 200 mg or less per day to achieve effective pain relief



President's Message to Shareholders

The third quarter of fiscal 2003 unfolded on plan, led by continued advancement toward the commercialization of our once-daily formulation of tramadol. We passed a number of key milestones for this program during the quarter and remain well positioned to launch our first product and generate our first revenue from commercial sales next year. Our financial results for the quarter were in line with our expectations and reflect our significant clinical progress with once-daily tramadol in the United States and the ramp up of commercialization activity in Europe in anticipation of regulatory approval there.

US Phase III Trials for Once-Daily Tramadol Nearing Completion During the third quarter, we completed the treatment stage for our two, pivotal, Phase III clinical trials in the United States that were designed to test the efficacy and safety of Labopharm's once-daily tramadol. We expect to report results from these trials before year end. The results from these trials will be combined with data from our phase III European trial and other studies to form the basis of our new drug application (NDA) to the US Food and Drug Administration. We are at an advanced stage in our negotiation with potential US partners and look forward to concluding these discussions.

European Commercialization Plan for Once-Daily Tramadol Remains on Track Our commercialization plan for once-daily tramadol in Europe remains on track as we concluded definitive marketing agreements with Gruppo Angelini for Italy and with Esteve S.A. for Spain and Portugal during the quarter. Subsequent to quarter end, we secured a licensing and distribution agreement with Austria-based CSC Pharmaceuticals for 14 eastern European countries. The countries covered by this partnership represent a population totalling 128 millions (more than 16% of the European population) – a sizeable market opportunity for once-daily tramadol. With this agreement, we have now secured marketing partnerships for our once-daily formulation of tramadol for 18 countries in Europe, including three of the five largest pharmaceutical markets in that region – France, Italy and Spain. As part of our global commercialization plan for once-daily tramadol,

we continue to actively pursue marketing partners for other key European markets in addition to our efforts in the US and other markets globally.

Recently, we presented the data from our European Phase III trial at the prestigious OsteoArthritis Research Science International (OARSI) World Congress in Berlin, Germany. The double-blind, randomized, parallel-group, non-inferiority study of patients with moderate to severe osteoarthritis of the knee was designed to show that the efficacy and safety of Labopharm's once-daily formulation of tramadol was equally as effective as that of an extended release, twice-daily formulation of tramadol currently marketed in Europe.

Labopharm's once-daily formulation of tramadol achieved the primary end point of the study, providing a statistically and clinically significant reduction in pain associated with osteoarthritis and demonstrating the non-inferiority of once-daily tramadol compared to the twice-daily formulation as measured by the percentage change in the WOMAC Osteoarthritis Index Pain subscale. Pain ratings improved by 58% for each of the versions of tramadol, with the results being statistically significant. Furthermore, pain relief was achieved from the first week of treatment and was maintained, with further improvement, over the duration of the study. Two-thirds of the patients receiving Labopharm's once-daily tramadol required a dose of 200 mg or less per day to achieve effective pain relief.

Secondary end points of the study were daily efficacy rating, pain ratings over a 24-hour period, patient and investigator global ratings, other WOMAC (stiffness and functional disability) scores, and incidence of adverse events. Labopharm's once-daily formulation of tramadol also demonstrated an improvement in all secondary end points. The proportion of patients in the once-daily tramadol group reporting mild to no pain 24 hours following dosing (73%) was the same as the proportion of twice-daily tramadol patients reporting mild to no pain 12 hours following dosing. Pain ratings over a 24-hour period were similar for the once-daily tramadol and twice-daily tramadol groups, indicating that Labopharm's once-daily tramadol provided pain relief for a full 24-hour period. Patients and investigators rated both once-daily tramadol and twice-daily tramadol effective to very effective in 85% of cases. WOMAC stiffness and functional disability scores demonstrated similar efficacy results for both the once-daily tramadol and twice-daily tramadol groups.

The adverse events profile of Labopharm's once-daily tramadol was superior to that of the twice-daily tramadol product, with a lower incidence of key adverse events. Fewer patients in the once-daily tramadol group experienced dizziness/vertigo (26% compared to 37%), vomiting (8% compared to 14%) and headache (13% compared to 18%). Furthermore, the severity of each of the adverse events was less for the once-daily tramadol group. Both the once-daily tramadol group and twice-daily tramadol group experienced similar occurrences of nausea,

constipation and weakness. A greater number of patients in the once-daily tramadol group experienced somnolence (drowsiness) (30% compared to 21%).

With the final pieces of the puzzle falling into place for Europe, we are ramping up pre-commercialization manufacturing activity, and finalizing logistical details to support the commercial launch.

Continued Progress in Other Key Development Programs As we prepare for the commercialization of once-daily tramadol, we are continuing to advance other product development programs in our pipeline. These products all represent solid commercial opportunities that we expect to drive long-term growth.

Our in-house programs are advancing well. Subsequent to quarter-end we advanced once-daily oxybutynin, indicated for the treatment of urinary incontinence, into the clinic. We recently completed clinical batch manufacturing and initiated pilot pharmacokinetic studies with results expected in the first quarter of 2004.

We also made strong progress with another of our in-house products. DDS-2003 is a currently marketed product that does not have optimal delivery characteristics. Labopharm is developing a novel approach to overcome these inherent delivery issues. The development of a prototype formulation and validation in animal models is ongoing, and manufacturing process selection has been initiated in preparation for clinical trial batch manufacturing. Clinical trials are expected to commence in the first quarter of 2004.

Looking to our partnered programs, Allegra-D® continues to progress as scheduled. Last quarter we completed the technology transfer to a third party and, in collaboration with our partner Aventis, are now manufacturing the three US, new drug application batches, that will move the program forward.

Strengthened Intellectual Property Our core Contramid® technology forms the basis for a number of the products in our pipeline. Our intellectual property protection around Contramid® was strengthened in the third quarter when the US Patent and Trademark Office granted us a fundamental patent. The product-by-process patent extends our existing intellectual property protection of Contramid®, the technology's process of manufacture and its use in controlled-release pharmaceutical products. The patent, the seventh issued on Contramid® in the US, extends the patent protection on our technology through 2020.

Strengthened Financial Position To support the anticipated commercialization of once-daily tramadol, as well as the continued development of products across our pipeline, we completed an equity offering of \$23,200,520 during the quarter. Our strengthened financial position will ensure we have the resources

in place to execute our commercialization strategy for once-daily tramadol, including the conclusion of additional marketing partnerships worldwide.

Positioned for Success in 2004 In the first nine months of this year we have continued to make steady progress toward the commercialization of our first product, achieving a number of significant milestones. Over the near term we expect to meet the final pre-commercialization milestones in preparation for the launch of once-daily tramadol, first in Europe, and subsequently in the US.

Commercialization of once-daily tramadol represents the first in a string of many opportunities to realize the value of our pipeline and our Contramid® technology. In 2004, we fully expect to generate our first revenue from product sales and begin to turn toward profitability. The commercialization of Tramadol will, in turn, fund additional development across our pipeline, putting Labopharm further down the path toward establishing additional value-creating milestones for the other products in its portfolio, all with their own potential for reward. In 2004 we may have as many as six, separate products in the clinic, which represents a strong investment in Labopharm's future. We look forward to keeping you updated on our progress as we move through the balance of the year and into 2004.

(signed)

James R. Howard-Tripp
President and
Chief Executive Officer
October 29, 2003

Management's Discussion and Analysis

The following information should be read in conjunction with Labopharm Inc.'s ("the Company") unaudited interim Consolidated Financial Statements as of September 30, 2003 and Notes included herewith, which are prepared in accordance with Canadian generally accepted accounting principles for interim financial statements, as well as the audited Consolidated Financial Statements and Management's Discussion and Analysis for the ten-month period ended December 31, 2002.

To the extent any statements made in this document contain information that is not historical, these statements are essentially forward-looking and are subject to risks and uncertainties. Actual results, levels of activity, performance, or achievements could differ materially from those projected herein and depend on a number of factors, including the successful and timely completion of clinical studies, the uncertainties related to the regulatory process, and the commercialization of the drug thereafter.

OVERVIEW

Labopharm specializes in the development of pharmaceutical products incorporating its proprietary controlled-release technologies. As a specialty pharmaceutical company focused on drug delivery, the Company's business model differs from conventional biotech and pharma business models. Many of Labopharm's potential products are drugs that are already on the market, to which the Company applies its technologies to form new products with improved release profiles and performance. As a result, Labopharm's products should have shorter development timelines, lower development costs and, through the marketing resources of the Company's partners, could achieve faster market penetration than is typically the case with more traditional biotech or pharmaceutical business models.

The Company currently generates revenue from collaborations with international pharmaceutical companies in which Labopharm's controlled-release technologies are used to enhance the therapeutic benefits of its partners' branded products, and late-stage licensing of oral controlled-release products using its core technology, Contramid®.

PRODUCT DEVELOPMENT

The third quarter was highlighted by the achievement of key milestones on the path toward commercialization of the Company's lead in-house product, a once-daily version of the analgesic tramadol hydrochloride. During the quarter, Labopharm also made progress on a number of the key in-house and partnered products in its pipeline.

In-House Products

Once-Daily Tramadol

During the quarter, Labopharm completed the treatment stage for two pivotal Phase III clinical trials in the US. The trials, designed to assess the efficacy and safety of once-daily tramadol, are part of the Company's global regulatory strategy for once-daily tramadol. In January, Labopharm initiated two double blind, multi-centre, randomized trials in the US to evaluate the efficacy of once-daily tramadol in reducing moderate to moderately severe pain in patients suffering from osteoarthritis. The subject population, which included more than 1,000 men and women aged 40 to 75, was conducted at more than 100 centres. The Company expects to have the trial results in the fourth quarter of 2003. The US trial data, in conjunction with the data from the European Phase III and other studies, will form the basis of a New Drug Application (NDA) filing to the FDA. Tramadol is currently available in the US only in immediate-release forms that require dosing four- to six-times daily.

Labopharm's clinical trial strategy focused on conducting pharmacokinetic and efficacy studies concurrently in both Europe and the United States to advance tramadol more rapidly through regulatory filings and on commercialization in key global markets. To date, the Company has enrolled more than 1,800 patients in various clinical studies as part of its global once-daily tramadol program, and has fully completed its clinical program for Europe.

During the quarter, Labopharm, through its wholly-owned subsidiary, Labopharm Europe Limited, finalized definitive marketing agreements for once-daily tramadol in Italy with Gruppo Angelini and in Spain and Portugal with Esteve S.A. Gruppo Angelini is a privately-held international conglomerate with pharmaceutical, consumer products, and machinery divisions, comprising 20 operating companies. Esteve S.A. is a privately-held, international chemical-pharmaceutical company with a 75-year operating history and facilities in Spain, Portugal, Mexico, and China. Labopharm's agreements with these two partners supplement its existing relationship with Aventis France S.A. for marketing of once-daily tramadol in France, Europe's largest tramadol market. Under the terms of the revenue sharing agreements, Labopharm granted its marketing partners the exclusive rights to market and sell once-daily tramadol in their respective countries. The Company will supply each partner with

finished, packaged product through Labopharm Europe Limited, and will be responsible for obtaining regulatory approval in each country. Labopharm is actively engaged in discussions to establish marketing channels for other jurisdictions in the EU, other countries in Europe, the United States, and the rest of the world.

In the third quarter, Labopharm also began ramping up the commercial-scale manufacturing process with a third-party manufacturer in preparation for the commercialization of once-daily tramadol in Europe. Simultaneously, the Company also initiated registration batch manufacturing in preparation for an NDA filing to the US Food and Drug Administration.

Subsequent to quarter end, Labopharm presented the European Phase III trial data at the prestigious OsteoArthritis Research Science International (OARSI) World Congress in Berlin, Germany. The double-blind, randomized, parallel-group, non-inferiority study of patients with moderate to moderately severe osteoarthritis of the knee was designed to show that the efficacy and safety of Labopharm's once-daily formulation of tramadol was equally as effective as that of an extended release, twice-daily formulation of tramadol currently marketed in Europe. Labopharm's once-daily formulation of tramadol achieved both the primary and secondary end points of the study, providing a statistically and clinically significant reduction in pain associated with osteoarthritis. Pain relief was achieved and maintained from the first week of treatment, with further improvement over the duration of the 12-week study. Two-thirds of the patients receiving Labopharm's once-daily tramadol required a dose of 200 mg or less per day to achieve effective pain relief. Additionally, the adverse events profile of Labopharm's once-daily tramadol was superior to that of the twice-daily tramadol product, with a lower incidence of key adverse events.

Once-Daily Oxybutynin

Subsequent to quarter-end, Labopharm completed clinical batch manufacturing and initiated pilot pharmacokinetic studies for once-daily oxybutynin. The Company expects to have results of the studies in the first quarter of 2004.

DDS-2003

DDS-2003 is a currently marketed product that does not have optimal delivery characteristics. Labopharm is developing a novel approach to overcome these inherent delivery issues. Development and prototype validation in animal models is ongoing and manufacturing process selection has been initiated in preparation for clinical trial batch manufacturing.

Partnered Products Labopharm's pipeline also includes several partnered products, the principal one being Allegra-D®. Labopharm is developing a new formulation of Allegra-D® with Aventis. During the quarter, in collaboration with its partner, the Company completed manufacturing process scale-up. NDA batch manufacturing is ongoing and progressing according to schedule.

TECHNOLOGY PROGRAMS

Labopharm is expanding its portfolio to include additional novel drug delivery technologies, the principal candidate being micelles. Labopharm is developing novel nano-carrier systems based on polymeric micelles for both systemic and targeted delivery of water-insoluble drugs. Proof-of-principle studies with the Company's leading micelles technology have been completed and formal development of products is now being initiated.

FINANCIAL RESULTS

Change in Fiscal Year-End In 2002, the Company changed its financial year-end from February 28 to December 31. Accordingly, the consolidated statements of loss, cash flow, and deficit for the third quarter ended September 30, 2003, are compared to the quarter ended August 31, 2002.

Financing During the quarter, the Company issued to a syndicate of underwriters a total of 4,734,800 common shares, including the over-allotment option, at a price of \$4.90 for total gross proceeds of \$23,200,520. The net proceeds of \$21.8 million from the offering will be used to support the anticipated commercialization of once-daily tramadol, including both the product launch in Europe and the submission of a regulatory filing in the United States, and to advance development of new programs within Labopharm's pipeline, as well as for working capital and general corporate purposes.

Operating Revenue For the third quarter ended September 30, 2003, operating revenue was \$216,900 compared with \$436,800 for the quarter ended August 31, 2002. During the quarter, the Company started to recognize a portion of the up-front payments it received from Gruppo Angelini and Esteve S.A. as licensing revenue. These up-front payments will be recognized over the terms of the respective agreements.

No revenue was recognized on research and development contracts during the quarter, as there were no milestones payments allowing revenue recognition made during the period. The comparative period of the quarter ended August 31, 2002, included revenue from the Axcan and Medpointe agreements. For the nine-month period ended September 30, 2003, revenue from research and development contracts

generated \$599,700 in revenue, primarily from the Medpointe agreement, compared with \$196,000 in the comparative nine-month period ended August 31, 2002.

Investment income for the quarter ended September 30, 2003 was \$209,300 compared with \$325,300 for the quarter ended August 31, 2002. For the nine-month period ended September 30, 2003 investment income totalled \$594,300 compared with \$1,032,100 in the comparative period. The decrease in investment income is in part due to lower investments, but also because of lower returns due to the general market conditions.

Research and Development Expenses Research and development expenses (net of tax credits) for the third quarter ended September 30, 2003 were \$5,977,100 compared with \$2,435,300 for the quarter ended August 31, 2002. The significant increase is primarily attributable to the costs associated with the two Phase III studies in the US. The increase in research and development expenses in the current quarter was also the result of an increase in the number of employees and related costs required to expand the Company's product portfolio and accelerate development.

For the nine-month period ended September 30, 2003, research and development expenses totalled \$19,545,000, of which approximately \$16.1 million were primarily related to clinical studies mainly for the Phase III trials conducted during the period. For the nine-month period ended August 31, 2002, research and development expenses totalled \$7,583,300, of which approximately \$4.6 million were related to clinical trials. Accordingly, research and development costs not related to clinical trials totalled approximately \$3.4 million in the current nine-month period, compared with approximately \$3.0 million in the previous period. This increase in costs is attributable to the growth in the Company's research and development activities, including an increase in R&D personnel to support an advancing product portfolio. Additionally, in April 2003 the Company moved into new laboratories, thereby incurring increased depreciation charges in the current year for its new research and development equipment and the R&D portion of the building accounted for as a capital lease.

Selling, General and Administrative Expenses Selling, general and administrative expenses for the third quarter ended September 30, 2003 were \$1,917,200 compared with \$1,485,200 for the quarter ended August 31, 2002. As the Company prepares the launch of its first commercial product, infrastructure has been added to meet this objective. Business development resources were added to secure commercial agreements with worldwide partners. As the necessary resources were put in place, operating costs for Labopharm Europe Limited moved significantly higher versus the comparative period. Consulting and professional fees also increased due to the negotiation and drafting of commercial agreements, in addition to reviewing,

maintaining and improving the patent portfolio for the Company's products and technology in various territories. Higher costs were also incurred for the depreciation of the new building accounted for as a capital lease. Selling, general and administrative expenses for the nine-month period ended September 30, 2003 were \$5,832,400 compared with \$4,832,600 for the nine-month period ended August 31, 2002 reflecting the pre-commercialization activities described above.

Increased finance charges of \$211,500 for the quarter ended September 30, 2003 and \$357,300 for the nine-month period, primarily include interest on the capital lease of the Company's new facilities, which commenced during May 2003.

Net Loss Net loss for the third quarter ended September 30, 2003 was \$7,888,900, or \$0.22 per share, compared with \$3,491,800, or \$0.11 per share for the quarter ended August 31, 2002. For the nine-month period ended September 30, 2003, net loss was \$24,533,100 or \$0.76 per share compared with \$11,211,900 or \$0.36 per share for the comparative period. The increase reflects the multiple concurrent Phase III clinical trials for once-daily tramadol, and the general increase in the Company's costs as it moves closer to the global commercialization of tramadol, and continues to build its pipeline of products.

Liquidity and Capital Resources Cash and investments at the end of the third quarter ended September 30, 2003 were \$28,837,100 compared with \$32,480,600 as of December 31, 2002. The major use of funds during the nine-month period included \$22,279,500 used for operations, primarily for research and development activities and \$3,251,200 invested in property, plant and equipment coinciding with the Company's relocation into its new facilities with GMP manufacturing capabilities. The financing completed during the third quarter ended September 30, 2003 generated net proceeds of \$21.8 million, increasing the Company's liquidity and capital resources accordingly. Accounts receivables totalled \$1,782,800 on September 30, 2003 and included amounts receivable for commodities tax, from R&D contracts and from the sale of raw materials. Accounts payable and accrued liabilities increased from \$3,923,900 on December 31, 2002 to \$5,258,000 on September 30, 2003 due to the general increase in the Company's activities and to the timing of the payments of the various Phase III studies. Deferred revenue totalled \$493,100 as at September 30, 2003 and represented the portion of the payments from Gruppo Angelini and Esteve S.A. received at the signing of the agreements, which will be recognized over the terms of the respective agreements.

Under the Company's current operating plan, management believes that the Company's current cash, cash equivalents, and investments, together with milestone payments from existing and anticipated commercial agreements, should be sufficient to finance its operations and capital needs into 2005, by which time it expects to generate

a positive cash flow from its operations. However, in light of the inherent uncertainties associated with research and development programs, scale-up and commercialization of products, ability to enter into collaborative research and development agreements, the results of clinical testing, receipt of regulatory approval of certain products, and ability to secure licensing agreements, it may be necessary for the Company to either (i) raise additional funds for the continuing development and marketing of its products, or (ii) delay or scale-back its development programs. Furthermore, additional financing may also be required for business acquisitions or to acquire additional products or technologies.

RISKS AND UNCERTAINTIES

The field of drug delivery systems is still a relatively new and rapidly expanding market that brings therapeutic benefits to patients and offers good commercial potential for pharmaceutical companies. Labopharm's success in this market will depend, in the short and medium term, on the applicability of its Contramid® technology and its competitiveness with other available technologies. However, no product incorporating Contramid® has yet been fully developed and marketed. There has also been rapid and considerable evolution of technology within the drug delivery system industry and the competitive advantages of new systems developed by competitors could challenge those of Contramid®.

Labopharm places great importance on the protection of its intellectual property and has a portfolio of patents and patent applications. There is no guarantee that these patents are valid, or that the Company's patent applications will be approved, or that the Company will be successful in defending them.

Labopharm's success also depends, in large measure, on its ability to conclude licensing, development, manufacturing, and marketing agreements with other pharmaceutical companies for products to which its drug delivery systems would be applied. The Company has certain agreements with pharmaceutical companies. There is no assurance that partners will not withdraw from agreements at a later date or that products will successfully reach the market.

The development of pharmaceutical products is a process that requires large investments and can take years to complete. Projects can be abandoned by partners and/or the Company for a variety of reasons or regulatory authorities can refuse to approve new products.

With respect to manufacturing Contramid®, the Company has an agreement with Cerestar, a European manufacturer of starch and starch derivatives. Labopharm relies on the manufacture of Contramid® as a key ingredient in its products.

Any interruption in supply could affect the ability of the Company to continue development of key products.

Labopharm expects to generate significant revenue from the licensing agreements and alliances it has concluded and that it expects to conclude with pharmaceutical companies. The form in which revenue is generated could vary greatly depending on the conditions of the agreement. There is no assurance that revenue will be generated through these agreements unless key milestones are achieved. The principal forms of revenue are achieved through milestone payments, which are lump-sum payments made at key stages of product development, as well as through product sales and royalties.

Until it begins to generate significant revenue according to the terms of its strategic alliances, the Company foresees continued losses, primarily as a result of its research and development activities.

The price of Labopharm's common shares is subject to fluctuation. Factors such as strategic alliances, research results and clinical studies, questions regarding patents, and any number of other factors could considerably influence the price of Labopharm's common shares.

Labopharm relies on key personnel and if the Company is unable to retain key personnel and hire additional scientific, sales and marketing, and other key personnel, it may not be able to successfully achieve its goals.

The Company operates internationally, and a substantial portion of its expense activities and capital expenditures are in Canadian dollars, whereas its potential revenues under currently signed agreements are primarily in US dollars or Euros. A significant adverse change in foreign currency exchange rates could have a material effect on the Company's consolidated results of operations, financial position or cash flows.

Consolidated Statements of Loss (Unaudited)

(Thousands of dollars except for per share data and number of shares)

For periods of:

	Three months ended		Nine months ended	
	Sept. 30, 2003	August 31, 2002	Sept. 30, 2003	August 31, 2002
	\$	\$	\$	\$
OPERATING REVENUE				
Research and development contracts	-	111.5	599.7	196.0
Licensing	7.6	-	7.6	-
Investment income	209.3	325.3	594.3	1,032.1
	216.9	436.8	1,201.6	1,228.1
OPERATING EXPENSES				
Research and development expenses [note 6]	5,977.1	2,435.3	19,545.0	7,583.3
Selling, general and administrative expenses	1,917.2	1,485.2	5,832.4	4,832.6
Finance charges	211.5	8.1	357.3	24.1
	8,105.8	3,928.6	25,734.7	12,440.0
NET LOSS	(7,888.9)	(3,491.8)	(24,533.1)	(11,211.9)
BASIC AND DILUTED LOSS PER SHARE	(0.22)	(0.11)	(0.76)	(0.36)
Weighted average number of common shares outstanding	35,070,373	31,040,003	32,420,480	30,926,949

Consolidated Statements of Cash Flows (Unaudited)

(Thousands of dollars)

For periods of:

	Three months ended		Nine months ended	
	Sept. 30, 2003	August 31, 2002	Sept. 30, 2003	August 31, 2002
	\$	\$	\$	\$
OPERATING ACTIVITIES				
Net loss	(7,888.9)	(3,491.8)	(24,533.1)	(11,211.9)
Items not affecting cash				
Depreciation of property, plant and equipment	334.5	107.2	721.6	288.6
Amortization of intangible assets	76.3	25.2	193.7	249.6
Loss on disposal and write-off of property, plant and equipment	-	-	-	8.4
	(7,478.1)	(3,359.4)	(23,617.8)	(10,665.3)
Net change in non-cash working capital items	(2,030.8)	(874.0)	1,338.3	(328.4)
	(9,508.9)	(4,233.4)	(22,279.5)	(10,993.7)
INVESTING ACTIVITIES				
Acquisition of investments	(18,074.0)	(9,577.1)	(20,845.9)	(17,223.2)
Disposals and maturities of investments	15,278.4	16,453.1	33,519.2	27,930.9
Acquisition of property, plant and equipment	(333.4)	(171.8)	(3,251.2)	(533.5)
Acquisition of intangible assets	(98.4)	(85.8)	(188.9)	(359.1)
	(3,227.4)	6,618.4	9,233.2	9,815.1
FINANCING ACTIVITIES				
Repayment of capital leases obligations	(74.5)	(16.0)	(102.1)	(48.0)
Proceeds from issuance of capital stock	23,336.4	22.9	23,553.5	2,236.8
Issuance costs of capital stock	(1,375.3)	(1.8)	(1,375.3)	(302.6)
	21,886.6	5.1	22,076.1	1,886.2
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	9,150.3	2,390.1	9,029.8	707.6
Cash and cash equivalents, beginning of period	1,597.7	175.7	1,718.2	1,858.2
Cash and cash equivalents, end of period	10,748.0	2,565.8	10,748.0	2,565.8

See accompanying notes.

Consolidated Balance Sheets

(Thousands of dollars)	As at Sept. 30, 2003 (Unaudited)	As at December 31, 2002 (Audited)
	\$	\$
ASSETS		
Current assets		
Cash and cash equivalents	10,748.0	1,718.2
Short-term investments	16,660.1	22,294.3
Accounts receivable	1,782.8	1,251.6
Research and development tax credits receivable	697.5	568.3
Prepays and other assets	138.3	426.8
	<u>30,026.7</u>	26,259.2
Property, plant and equipment [note 3]	10,738.0	2,020.0
Intangible assets	1,939.4	1,944.2
Long-term investments	1,429.0	8,468.1
	<u>44,133.1</u>	38,691.5
LIABILITIES		
Current liabilities		
Accounts payable and accrued liabilities	5,258.0	3,923.9
Deferred revenue	493.1	117.0
Current portion of obligations under capital leases [note 4]	139.9	7.8
	<u>5,891.0</u>	4,048.7
Obligations under capital leases [note 4]	5,967.7	13.5
	<u>11,858.7</u>	4,062.2
SHAREHOLDERS' EQUITY		
Capital stock [note 5]	111,567.9	88,014.4
Deficit	(79,293.5)	(53,385.1)
	<u>32,274.4</u>	34,629.3
	<u>44,133.1</u>	38,691.5

Consolidated Statements of Deficit (Unaudited)

(Thousands of dollars)	Sept. 30, 2003	August 31, 2002
	\$	\$
For periods of nine months ended:		
BALANCE, beginning of period	(53,385.1)	(35,095.7)
Issuance costs of capital stock	(1,375.3)	(302.6)
Net loss	(24,533.1)	(11,211.9)
BALANCE, end of period	(79,293.5)	(46,610.2)

See accompanying notes.

Notes to Consolidated Financial Statements

As at September 30, 2003

1. STATUTES OF INCORPORATION AND NATURE OF ACTIVITIES

The Company, incorporated under the *Companies Act (Québec)* is specialized in the development of drugs using advanced controlled-release technologies and the development of pharmaceutical products incorporating its proprietary technologies. The Company carries on business in Canada and Ireland and substantially all of the Company's assets are located in Canada. In 2002, the Company changed its fiscal year end from February 28 to December 31. Accordingly, the consolidated statements of loss, cash flow, and deficit, for the nine-month period ended September 30, 2003 are compared to the nine-month period ended August 31, 2002.

The Company's strategy is to develop products internally in order to form strategic alliances or licensing agreements with national or international pharmaceutical companies that have the necessary resources and distribution networks to market and sell the pharmaceutical products incorporating the Company's proprietary technologies. To date, the Company has financed its cash requirements primarily through share issuances, investment tax credits, collaborative research contracts and interest income. The future profitability of the Company is dependent upon such factors as the success of the clinical trials, the approval by regulatory authorities of products developed by the Company and the ability of the Company to obtain the necessary financing to complete its projects through licensing and research agreements. It may be necessary for the Company to raise additional funds until profitability is achieved.

2. BASIS OF PRESENTATION AND ACCOUNTING POLICIES

The unaudited interim consolidated financial statements of the Company have been prepared in accordance with generally accepted accounting principles (GAAP) in Canada for interim financial statements. Accordingly, they do not include all of the information and notes required by GAAP for annual financial statements and should be read in conjunction with the audited consolidated financial statements for the ten-month period ended December 31, 2002 and the accompanying notes, included in the Company's annual report.

The accounting policies used in preparation of these interim consolidated financial statements are the same as those used in the preparation of the Company's most recent annual consolidated financial statements, and are set forth in notes 2 and 3 of the audited financial statements for the ten-month period ended December 31, 2002 included in the Company's annual report.

3. PROPERTY, PLANT AND EQUIPMENT

	Cost	Accumulated depreciation	Net book value
	\$	\$	\$
September 30, 2003			
Laboratory equipment	3,466,476	1,286,440	2,180,036
Computer hardware and software	785,700	387,955	397,745
Furniture and office equipment	692,611	269,934	422,677
Leasehold improvements	122,275	-	122,275
	5,067,062	1,944,329	3,122,733

Assets under capital leases

Building	7,524,417	204,673	7,319,744
Laboratory and office equipment	359,146	63,603	295,543
	12,950,625	2,212,605	10,738,020

December 31, 2002

Laboratory equipment	1,913,973	991,021	922,952
Computer hardware and software	443,374	288,549	154,825
Furniture and office equipment	320,580	213,419	107,161
Leasehold improvements	360,061	329,037	31,024
Assets under construction	738,380	-	738,380
	3,776,368	1,822,026	1,954,342

Assets under capital leases

Laboratory equipment	94,712	28,998	65,714
	3,871,080	1,851,024	2,020,056

During the nine-month period ended September 30, 2003, a building for \$5,970,000 and laboratory and office equipment for \$218,385 were acquired through capital leases (laboratory equipment for \$57,387 in 2002). The building is amortized using the straight-line method over the term of the fifteen-year lease.

4. CAPITAL LEASE OBLIGATIONS

	September 30, 2003	December 31, 2002
	\$	\$
Building, repayable in monthly instalments of \$70,833 until May 2008, \$83,333 from June 2008 to May 2013, and \$95,833 from June 2013 to April 2018, including interest calculated at 14.6%.	14,677,823	—
Various leases for laboratory equipment, repayable in monthly instalments totalling \$9,544 including interest ranging from 7.0% to 13.5%, with transfer of ownership at maturity from May to July 2005.	204,017	25,080
	14,881,840	25,080
Interest included in instalments	8,774,206	3,710
	6,107,634	21,370
Current portion	139,895	7,827
	5,967,739	13,543

5. CAPITAL STOCK

Authorized

Unlimited number of preferred shares, non-participating, non-voting, without par value
Unlimited number of common shares, voting, without par value

Issued

35,928,331 common shares (December 31, 2002 – 31,058,081)

Capital Stock transactions

On July 15 2003, the Company issued 4,500,000 common shares and on August 18, 2003, the over-allotment option was exercised on 234,800 additional common shares. The total consideration was \$23,200,520 in cash. The share issue expenses amounted to \$1,375,259.

Stock option plan

The changes to the number of stock options granted by the Company and their weighted average exercise price, for the nine-month period ended September 30, 2003, are as follows:

	#	\$
Balance, beginning of period	3,460,825	4.24
Granted	200,000	4.28
Exercised	(135,450)	2.61
Expired	(489,800)	4.09
Forfeited	(41,200)	5.74
Balance, end of period	2,994,375	4.33
Options eligible to be exercised, end of period	2,064,100	4.03

5. CAPITAL STOCK (CONT'D)

No compensation cost has been recognized for stock options granted to employees and directors during the nine-month period ended September 30, 2003. Pro forma information regarding net loss has been determined as if the Company had accounted for stock options granted under the fair value method. The fair value of these options was estimated at the date of grant using a Black-Scholes option pricing model with the following weighted average assumptions; volatility factor of the expected market price of the Company's common shares of 0.92 (2002 - 0.94); a risk-free interest rate of 4.0% (2002 - 3.5%); an expected life of the options of 4 years (2002 - 3.4 years); and a dividend yield of nil. The weighted average fair-value of stock options granted during the nine-month period ended September 30, 2003 under the Black-Scholes option pricing model and the above assumptions amounted to \$2.86 (2002 -\$1.91) per option.

Had compensation cost been determined based on the fair value at the date of grant of the options granted, the fair value of the options would have been amortized over the vesting period of the options and the Company's net loss and basic and diluted loss per share for the nine-month period ended September 30, 2003 would have been amended as follows:

		Three months ended		Nine months ended	
		Sept. 30, 2003	Aug. 31, 2002	Sept. 30, 2003	Aug. 31, 2002
		\$	\$	\$	\$
Net loss	As reported	(7,888,925)	(3,491,848)	(24,533,083)	(11,211,971)
	Pro forma	(8,064,974)	(3,778,017)	(25,564,156)	(11,504,444)
Basic and diluted					
loss per share	As reported	(0.22)	(0.11)	(0.76)	(0.36)
	Pro forma	(0.23)	(0.12)	(0.79)	(0.37)

6. RESEARCH AND DEVELOPMENT EXPENSES

Research and development expenses are presented net of tax credits of \$655,307 and \$519,807 for the nine-month periods ended September 30, 2003 and August 31, 2002.

7. COMMITMENTS

The Company has entered into long-term supply agreements with third party manufacturers in anticipation of the commercialization of its products. These agreements include cancellation clauses under which the Company would have to reimburse certain equipment and set-up costs and/or purchase minimum quantities of products. Management has estimated that minimum commitments to terminate these agreements would be approximately \$1,600,000.

8. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform with the presentation in the current period.

General Information

Officers

Donald Buxton
Chairman of the Board (Non-Executive)

James R. Howard-Tripp
President and Chief Executive Officer

Sylvie Bouchard, MD, PhD.
Vice-President, Clinical Development

Lisane Dostie, LLB
General Counsel and Corporate Secretary

Allan Mandelzys, PhD., MBA
Vice-President, Business Development

Damon Smith, BSc., PhD.
Vice-President, Research and Development

Warren Whitehead, CMA
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All amounts in this report are in Canadian dollars, unless otherwise stated.