



Consolidated Financial Statements of
(Unaudited)

THERATECHNOLOGIES INC.

Nine-month periods ended August 31, 2006 and 2005

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(Unaudited)

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Financial Statements

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THE RATECHNOLOGIES INC.

Consolidated Balance Sheets
(Unaudited)

August 31, 2006, with comparative figures as at November 30, 2005
(in thousands of dollars)

	August 31, 2006	November 30, 2005
		(Audited)
Assets		
Current assets:		
Cash and cash equivalents	\$ 1,547	\$ 1,087
Bonds	16,457	12,515
Accounts receivable	300	258
Tax credits receivable	1,578	978
Research supplies	2,264	1,929
Prepaid expenses	563	425
	22,709	17,192
Bonds	23,406	25,424
Investments in public companies (market value: \$1,130 in 2006; \$1,424 in 2005)	836	836
Property and equipment	1,700	2,072
Other assets (note 2)	8,162	8,121
	\$ 56,813	\$ 53,645
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 5,638	\$ 4,639
Shareholders' equity:		
Capital stock (note 3)	177,509	155,659
Contributed surplus	3,287	2,587
Deficit	(129,621)	(109,240)
	51,175	49,006
	\$ 56,813	\$ 53,645

See accompanying notes to unaudited consolidated financial statements.

THE RATECHNOLOGIES INC.

Consolidated Statements of Earnings
(Unaudited)

Periods ended August 31, 2006 and 2005
(in thousands of dollars, except per share amounts)

	August 31,		August 31,	
	2006	2005	2006	2005
	(3 months)		(9 months)	
Revenues:				
Royalties, technologies and other (note 4)	\$ 5	\$ 20	\$ 187	\$ 14,850
Interest	407	389	1,095	1,292
	412	409	1,282	16,142
Operating costs and expenses:				
Research and development	6,440	3,855	16,086	10,321
Tax credits	(236)	(186)	(620)	(674)
	6,204	3,669	15,466	9,647
General and administrative	1,046	1,387	3,586	4,074
Selling and market development	257	210	689	795
Patents and amortization of other assets	156	208	460	1,057
	7,663	5,474	20,201	15,573
Operating (loss) earnings before undernoted item	(7,251)	(5,065)	(18,919)	569
Proportionate share in loss of companies under significant influence	-	(153)	-	(6,602)
Loss on investments in companies	-	-	-	(2,659)
Net loss	\$ (7,251)	\$ (5,218)	\$ (18,919)	\$ (8,692)
Basic and diluted loss per share (note 3 (c))	\$ (0.16)	\$ (0.15)	\$ (0.45)	\$ (0.24)
Weighted average number of common shares outstanding	46,759,880	35,549,019	42,182,786	35,529,213

See accompanying notes to unaudited consolidated financial statements.

TERATECHNOLOGIES INC.

Consolidated Statements of Deficit
(Unaudited)

Periods ended August 31, 2006 and 2005
(in thousands of dollars)

	August 31,		August 31,	
	2006	2005	2006	2005
	(3 months)		(9 months)	
Deficit, beginning of period	\$ (122,370)	\$ (98,371)	\$ (109,240)	\$ (94,897)
Net loss	(7,251)	(5,218)	(18,919)	(8,692)
Share issue costs	-	-	(1,462)	-
Deficit, end of period	\$ (129,621)	\$ (103,589)	\$ (129,621)	\$ (103,589)

See accompanying notes to unaudited consolidated financial statements.

THE RATECHNOLOGIES INC.

Consolidated Statements of Cash Flows (Unaudited)

Periods ended August 31, 2006 and 2005
(in thousands of dollars)

	August 31,		August 31,	
	2006	2005	2006	2005
	(3 months)		(9 months)	
Cash flows from operating activities:				
Net loss	\$ (7,251)	\$ (5,218)	\$ (18,919)	\$ (8,692)
Adjustments for:				
Depreciation of property and equipment	150	156	443	431
Depreciation of other assets	126	119	351	802
Stock-based compensation	110	90	700	253
Proportionate share in loss of companies under significant influence	—	153	—	6,602
Loss on investments in companies and gains on dilution	—	—	—	2,659
	(6,865)	(4,700)	(17,425)	2,055
Changes in operating assets and liabilities:				
Interest receivable on bonds	224	364	157	410
Accounts receivable	(3)	(44)	(117)	6
Tax credits receivable	(238)	(186)	(600)	(678)
Research supplies	383	242	(576)	(1,496)
Prepaid expenses	75	(101)	(138)	(496)
Accounts payable and accrued liabilities	1,195	(447)	1,041	(1,157)
	1,636	(172)	(233)	(3,411)
	(5,229)	(4,872)	(17,658)	(1,356)
Cash flows from financing activities:				
Share issuance	—	—	21,850	60
Share issue costs	(135)	—	(1,405)	—
	(135)	—	20,445	60
Cash flows from investing activities:				
Addition to property and equipment	(16)	(79)	(161)	(459)
Addition to other assets	(51)	(35)	(165)	(226)
Disposal of other assets	—	—	80	—
Acquisition of bonds	—	(3,542)	(16,082)	(10,931)
Disposal of bonds	5,273	3,133	14,001	14,684
Sale of shares in a private company, net amount	—	2,565	—	2,561
	5,206	2,042	(2,327)	5,629
Net change in cash and cash equivalents	(158)	(2,830)	460	4,333
Cash and cash equivalents, beginning of period	1,705	7,599	1,087	436
Cash and cash equivalents, end of period	\$ 1,547	\$ 4,769	\$ 1,547	\$ 4,769

See note 6 (a) for supplemental cash flow information.

See accompanying notes to unaudited consolidated financial statements.

THE RATECHNOLOGIES INC.

Notes to Consolidated Financial Statements
(Unaudited)

Periods ended August 31, 2006 and 2005
(in thousands of dollars, except per share amounts)

1. Basis of presentation:

The financial statements included in this report are unaudited and reflect normal and recurring adjustments which are, in the opinion of the Company, considered necessary for a fair presentation. These financial statements have been prepared in conformity with Canadian generally accepted accounting principles. The same accounting policies as described in the Company's latest annual report have been used. However, these financial statements do not include all disclosures required under generally accepted accounting principles and, accordingly, should be read in connection with the financial statements and the notes thereto included in the Company's latest annual report. These interim financial statements have not been reviewed by auditors.

2. Other assets:

	August 31, 2006		
	Cost	Accumulated depreciation	Net book value
Intellectual property	\$ 7,670	\$ 2,231	\$ 5,439
Patent costs	1,694	847	847
Research supplies	1,801	-	1,801
Long-term accounts receivable	75	-	75
	<u>\$ 11,240</u>	<u>\$ 3,078</u>	<u>\$ 8,162</u>

	November 30, 2005		
	Cost	Accumulated depreciation	Net book value
Intellectual property	\$ 7,670	\$ 1,941	\$ 5,729
Patent costs	1,754	922	832
Research supplies	1,560	-	1,560
Deferred development costs	70	70	-
	<u>\$ 11,054</u>	<u>\$ 2,933</u>	<u>\$ 8,121</u>

THE RATECHNOLOGIES INC.

Notes to Consolidated Financial Statements, Continued
(Unaudited)

Periods ended August 31, 2006 and 2005
(in thousands of dollars, except per share amounts)

3. Capital stock:

	August 31, 2006	November 30, 2005
		(Audited)
Authorized in unlimited number and without par value:		
Common shares		
Preferred shares issuable in one or more series		
Issued:		
46,759,880 common shares (35,552,985 in 2005)	\$ 177,509	\$ 155,659

During the second quarter of 2006, the Company concluded a public offering for the sale and issue of 11,192,500 common shares, including the over-allotment option, for cash proceeds of \$21,825. The issuance costs amounted to \$1,462.

During the second quarter of 2006, the Company also issued 14,395 common shares to employees for a cash consideration of \$25, in connection with its share purchase plan.

(a) Share option plan:

Changes in outstanding options granted under the Company's stock option plan for the year ended November 30, 2005 and the nine-month period ended August 31, 2006 were as follows:

	Number	Weighted average exercise price
Options as at November 30, 2004 (audited)	2,781,500	\$ 7.28
Granted	535,000	1.59
Cancelled	(1,015,836)	8.33
Options as at November 30, 2005 (audited)	2,300,664	5.50
Granted	832,500	1.68
Cancelled	(192,998)	6.80
Options as at August 31, 2006	2,940,166	\$ 4.33

In September 2006, 350,000 options with an exercise price of \$4.60 expired.

THE RATECHNOLOGIES INC.

Notes to Consolidated Financial Statements, Continued
(Unaudited)

Periods ended August 31, 2006 and 2005
(in thousands of dollars, except per share amounts)

3. Capital stock (continued):

(b) Stock-based compensation and other stock-based payments:

The fair value of the options granted was estimated at the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions:

	2006	2005
Risk-free interest rate	4.08%	3.77%
Expected volatility	50%	51%
Expected average option life in years	6	6
Expected dividend yield	Nil	Nil

Dividend yield was excluded from the calculation, since it is the present policy of the Company to retain all earnings to finance operations and future growth.

The following table summarizes the weighted average fair value of stock options granted during the periods of nine months ended August 31, 2006 and 2005:

	Number	Weighted average grant-date fair value
2006	832,500	\$ 0.88
2005	415,000	0.97

(c) Diluted loss per share:

Diluted loss per share was not presented as the effect of options and warrants would have been anti-dilutive. Furthermore, the exercise of 2,417,666 (2005 - 3,709,829) options and warrants would not have been considered in such computation since their exercise prices were higher than the average market price during the reporting periods of 2006 and 2005.

(d) Warrants:

During the third quarter of 2006, 1,080,000 warrants expired at the exercise price of \$17.30. On August 31, 2006, no warrants were outstanding.

TheraTechnologies Inc.

Notes to Consolidated Financial Statements, Continued
(Unaudited)

Periods ended August 31, 2006 and 2005
(in thousands of dollars, except per share amounts)

4. Royalties, technologies and other:

In December 2004, the Company signed an agreement to terminate three co-development projects using ALZA Corporation's Macroflux® transdermal technology. The Company retains the rights to develop its molecules with all other delivery systems and ALZA retains the commercialization rights to Macroflux® with other molecules. In this regard, the Company received a payment of \$14,640 (US\$12,000).

5. Segmented information:

In 2006, the Company is conducting its activities in one segment, therapeutic peptides. Pursuant to the sale of Celmed BioSciences Inc. on June 20, 2005, the Company no longer conducts activities in cellular therapy. Segmented information for 2005 is as follows:

	Therapeutic peptides	Cellular therapy	Other segments	Intersegment adjustments and eliminations	Total
Third quarter ended August 31, 2005					
Revenues from external customers	\$ 20	\$ —	\$ —	\$ —	\$ 20
Loss from continuing operations	(5,065)	—	(153)	—	(5,218)
Net loss	(5,065)	—	(153)	—	(5,218)
Total assets	57,849	—	907	(509)	58,247
Nine-months ended August 31, 2005					
Revenues from external customers	14,830	—	—	—	14,830
Revenues from companies under significant influence	20	—	—	—	20
Earnings (loss) from continuing operations	569	(6,147)	(455)	(2,659)	(8,692)
Net earnings (loss)	569	(6,147)	(455)	(2,659)	(8,692)
Total assets	57,849	—	907	(509)	58,247

THE RATECHNOLOGIES INC.

Notes to Consolidated Financial Statements, Continued
(Unaudited)

Periods ended August 31, 2006 and 2005
(in thousands of dollars, except per share amounts)

6. Supplemental information:

(a) The following transactions were conducted by the Company and did not impact cash flow:

	August 31, 2006	November 30, 2005
Additions to property and equipment and other assets financed by accounts payable and accrued liabilities	\$ 64	\$ 163
Share issue costs financed by accounts payable and accrued liabilities	57	—

(b) General and administrative expenses include a gain on exchange of \$110 for the nine-month period ended August 31, 2006 (a loss of \$76 for the same period in 2005).