

**Form 51-102FI**

**PHEROMONE SCIENCES CORP.**

**Management's Discussion and Analysis of Results of Operations and Financial condition for the nine month period ending July 31, 2006.**

The following discussion and analysis should be read in conjunction with the first quarter unaudited financial statements and related notes dated July 31, 2006. This discussion and analysis provides an update to the Management's Discussion and Analysis ("MD&A") and financial statements contained in the audited, October 31, 2005 year end report and financial statements.

The information in this MD&A contains forward-looking statements

The information contained in this report is made as of August 28, 2006.

**Performance Summary and Update**

On May 25, 2006 the Company announced it had received TSX approval for the joint venture and financing agreement with Sertonex Inc. (Sertonex) of London Ontario and Sertoli Technologies Inc. (STI) of Tucson Arizona. The purpose of the joint venture is to develop a commercially viable treatment for Type 1 human diabetes using transplanted devices containing pig cells.

Under the terms of the agreement, Pheromone has the exclusive right to acquire 100% of the project by providing funding of up to \$3,500,000 in three stages. The first financing of \$1,000,000 was due within 90 days of Exchange approval, the second financing of \$1,000,000 within 6 months of Exchange approval, and the third financing of \$1,500,000 within 12 months of Exchange approval. As each stage of the project is financed, Pheromone acquires one third of the project by issuing 1,157,500 shares to each of the two shareholders of Sertonex, Dr. David White and Mr. Justin Leushner.

On May 25, 2006 the Company also announced it had completed a private placement financing for gross proceeds of \$3,229,100. The funds will be used to fund research on the diabetes project and for operating expenses.

With the financing completed, the company exercised its option under the joint venture agreement to concurrently close the first two stages and acquire 67% of the project effective August 9, 2006. For payment Dr. White and Mr. Leushner each received 2,315,000 common shares of Pheromone, subject to timed and performance earn out escrow agreements Mr. Leushner has joined the board of directors of the Company and Dr. White has been engaged as the principal researcher on the project and Chair of Pheromone's Scientific Advisory Board.

## **Performance Summary and Update** (Cont'd...)

As part of the agreement, STI exclusively licensed to Pheromone all patents, and patent applications for the therapeutic use of Sertoli cell technology, the key component of the diabetes research. In exchange, Pheromone issued to STI 6,527,500 common shares and must pay STI a licensing fee of \$1,142,312 by May 9, 2007, and certain other future royalties on income related to the patents. The payment shares are subject to a 3 year timed escrow agreement. STI is controlled by Research Corporation Technologies, Inc., a not for profit organization setup to facilitate the commercialization of bio medical research. Mr. Charles R. Allard of Edmonton, Alberta has joined the board of directors on behalf of STI.

On June 14, 2006 the Company incorporated a wholly owned US subsidiary in the state of Nevada, called Sertocell Biotechnology (US) Inc., to remove cross-border issues related to pursuing USFDA approvals, US patents, and future joint venture arrangements with US based pharmaceutical companies.

To help guide the diabetes research efforts the Company has established a new Scientific Advisory Board chaired by Dr. David White. Dr. White is Pheromone's principal researcher on its diabetes project and the lead author on the only published study of the clinical trial of diabetes treatment using transplanted pig cells. He is a noted immunologist, formerly a professor at Cambridge University in England and now Professor of Xenotransplantation at the University of Western Ontario. Also on the advisory board are Dr. Norman Wong, co-founder of Resverlogix and a Professor in the Departments of Medicine and Biochemistry & Molecular Biology at the University of Calgary, and Dr. Jannette Dufour, an expert in Sertoli cells who is now an Assistant Professor in the Department of Cell Biology and Biochemistry at Texas Tech University Health Sciences Center.

To assist the Board of Directors in commercializing the research findings, the Company has established a Business Advisory Board. Three former Company directors were appointed: Andrew Saxton, William Milligan and Chris Neuman.

In this quarter the Company also started receiving cash royalty payments from the July 2004 sale of its fertility monitor technology to HealthWatchSystems Inc. in July 2004. The product is branded as OV-Watch™, and is sold on the Internet and in selected markets in the USA. Further details of the transaction are contained in the October 31<sup>st</sup>, 2004 Year-End Financial Statement Foot Notes, Note Number 12.

## **Results of Operations**

The Company continues to focus on research and development and as such has incurred losses since its inception. For the nine month period ending July 31, 2006 the company recorded a loss of \$1,332,944 or \$0.04 per share versus a loss of \$316,408 or \$0.01 per share in the prior year. Of the current loss recorded for the period, \$1,013,192 is related to the non-cash expense from stock based compensation. Not including stock based compensation, the net loss for the period would be \$319,752. General and administrative expenses for the nine month period ending July 31, 2005 were \$336,950.

### **Summary of Quarterly Results**

		1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
2004	Net Income (loss)	(180,113)	(164,542)	(96,942)	73,223
	Net Income (loss) per share	(0.01)	(0.01)	(0.01)	0.01
2005	Net Income (loss)	(80,737)	(158,248)	(77,423)	(117,156)
	Net Income (loss) per share	(0.01)	(0.01)	(0.01)	(0.01)
2006	Net Income (loss)	(98,315)	(1,127,233)	(107,385)	
	Net Income (loss) per share	(0.01)	(0.04)	(0.01)	

### **Outstanding Share Data**

As at August 28, 2006, the Company has 50,305,483 common shares issued and outstanding. The Company also has a total of 2,660,000 outstanding stock options comprised of 2,470,000 options priced at \$0.40 a share, 40,000 at \$0.16 per share, and 150,000 at \$0.13 per share. There are 4,036,375 outstanding warrants exercisable at \$0.60 per share until May 16, 2008. All warrants are subject to a hold period ending either September 6, 2006 or September 16, 2006.

### **Liquidity and Capital Resources**

As at July 31, 2006, the Company had cash and short-term investments of \$3,174,945 compared to \$374,338 as at October 31, 2005. Short-term investments consist of money market funds and guaranteed investment certificates. Cash used for operations in the period was \$493,806 compared to \$191,794 for the period ended July 31, 2005. As at July 31, 2006, the Company had no long-term obligations.

### **Financing**

In May, 2006, the Company issued 8,072,750 units at \$0.40 per unit for gross proceeds of \$3,229,100 pursuant to a non brokered private placement. Each unit consists of one common share and one-half of one common share purchase warrant. Each warrant entitles the holder to acquire one common share at \$0.60 until May 16, 2008. The Company has the right to force the exercise of the warrants if the stock trades at a 10-day moving average above \$1.00 per share. In connection with the placement, the company paid finder's fees of \$119,385 and administration fees of \$3,200.

### **Transactions with Related Parties**

During the nine month period ended July 31, 2006, the Company paid management consulting fees in the amount of \$40,000 to a company controlled by Devinder Randhawa, the Chief Executive Officer of the Company. Management consulting fees of \$24,697 were paid to a company controlled by a director, Justin Leushner, for services provided to the Company. Patrick Groening, the Chief Financial Officer of the Company, received \$30,000 for his services.

These transactions are in the normal course of operations and are measured at the exchange amount, which is the amount of consideration established and agreed to by the parties. Amounts due to related parties are non-interest bearing, unsecured and have no specific repayment terms.

### **Subsequent Events**

Subsequent to July 31, 2006, the Company:

- a) Exercised its option to acquire a two-thirds portion of Sertonex Inc. in exchange for issuing to the Sertonex shareholders 4,630,000 common shares. The shares are subject to a three year escrow agreement with 10% of the shares released immediately and 15% of the original total released every six months thereafter. The shares are also subject to an earn out escrow agreement where half of the shares released from the time escrow are contingent on meeting certain milestones related to regulatory approvals of the diabetes product technology.
- b) Closed an intellectual property licensing agreement with Sertoli Technologies Inc. in exchange for 6,527,500 common shares of Pheromone and an obligation for an additional payment of \$1,142,312 by May 9, 2007. The shares are subject to a three year escrow agreement with 10% of the shares released immediately and 15% of the original total released every six months thereafter.

### **Additional Information**

Additional information relating to the Company is available on SEDAR at [www.sedar.com](http://www.sedar.com).