Canadian Energy
SERVICES L.P.

Interim Report 2006

for period ending March 31, 2006

MANAGEMENT'S DISCUSSION AND ANALYSIS OF CANADIAN ENERGY SERVICES L.P.

The following management's discussion and analysis ("MD&A") of financial condition and results of operations should be read in conjunction with the unaudited financial statements and notes thereto of Canadian Energy Services L.P. ("CES" or the "Partnership") as at and for the 30-day period ended March 31, 2006 included elsewhere in this interim report. The information contained in this MD&A was prepared on May 10, 2006 and incorporates all relevant considerations to that date.

Certain statements in this MD&A may constitute "forward-looking information" which involves known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Partnership, or industry results, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking information. When used in this MD&A, such information uses such words as "may", "would", "could", "will", "intend", "expect", "believe", "plan", "anticipate", "estimate" and other similar terminology. This information reflects the Partnership's current expectations regarding future events and operating performance and speaks only as of the date of this MD&A. Forward-looking information involves significant risks and uncertainties, should not be read as a guarantee of future performance or results, and will not necessarily be an accurate indication of whether or not such results will be achieved. A number of factors could cause actual results to differ materially from the results discussed in the forward-looking information, including, but not limited to, the factors discussed below. Although the forward-looking information contained in this MD&A is based upon what management of the Partnership believes are reasonable assumptions, the Partnership cannot assure investors that actual results will be consistent with this forward-looking information. This forward-looking information is provided as of the date of this MD&A, and, subject to applicable securities laws, the Partnership assumes no obligation to update or revise such information to reflect new events or circumstances.

In particular, this MD&A contains forward-looking information pertaining to the following: capital expenditure programs; supply and demand for drilling fluid systems and industry activity levels; commodity prices; treatment under governmental regulatory regimes; dependence on equipment suppliers and equipment improvements; dependence on personnel; collection of accounts receivable; operating risk liability; expectations regarding market prices and costs; expansion of services in Canada and the United States; development of new technology; acquisition of trucking capacity; and competitive conditions.

The Partnership's actual results could differ materially from those anticipated in the forward- looking information as a result of the following factors: general economic conditions in Canada and the United States; demand for oilfield services during drilling and completion of oil and natural gas wells; volatility in market prices for oil and natural gas and the effect of this volatility on the demand for oilfield services generally; competition; liabilities and risks, including environmental liabilities and risks, inherent in oil and natural gas operations; sourcing, pricing and availability of raw materials, consumables, component parts, equipment, suppliers, facilities, and skilled management, technical and field personnel; ability to integrate technological advances and match advances of competition; availability of capital; uncertainties in weather and temperature affecting the duration of the oilfield service periods and the activities that can be completed; changes in legislation and the regulatory environment, including uncertainties with respect to implementing the Kyoto Protocol; and the other factors considered under "Risk Factors" in the Partnership's final prospects dated February 21, 2006 and "Risks and Uncertainties" in this MD&A.

Without limiting the foregoing, the forward-looking information contained in this MD&A are expressly qualified by this cautionary statement.

Financial Highlights

Financial Results	30-day period ended March 31, 2006 [1]
($000's except per unit amounts)	
Revenue	6,922
Gross margin [2]	1,769
Net earnings	1,279
per unit – basic[4]	0.14
per unit – diluted[4]	0.14
EBITDAC [2]	1,311
Cash flow from operations [2]	1,311
per unit – basic [4]	0.15
per unit – diluted [4]	0.15
Distributions declared	
per unit – Class A Unit	0.0792
per unit – Subordinated Class B Unit	0.0792

Financial Position	March 31, 2006
($000's)	
Working capital	13,471
Total assets	111,746
Long term financial liabilities [3]	6,205
Unitholders' equity	84,306

Partnership Units Outstanding [4]	30-day period ended March 31, 2006 [1]
End of period	8,905,946
Weighted average – basic	8,905,946
Weighted average – diluted	8,905,946

Notes:
[1] From commencement of operations on March 2, 2006
[2] Refer to the "Non-GAAP Measures" on page 5 for further detail.
[3] Long term debt, excluding current portion and including due to Vendors
[4] Includes Class A Units and Subordinated Class B Units (see "Unitholder's Equity" on page 9)

Overview of Financial and Operational Results

Highlights of the first interim period for CES were:

- Revenue of $6.9 million for the 30-day period ended March 31, 2006 was strong, reflecting good industry conditions. Robust drilling activity and the benefits of integrating the acquired businesses contributed to the strong performance.
- Gross margin of $1.8 million or 26% of revenue was generated for the period.
- Selling, general and administrative costs include the impact of fixed public entity costs on the short period and costs incurred in the integration of the two acquired businesses. The integration costs will continue into the second quarter.
- Net earnings of $1.3 million or 18% of revenue was achieved despite the impact of higher costs.
- The Partnership declared its first monthly distribution of $0.0792 per unit to Class A and Subordinated Class B unitholders of record on March 31, 2006. The target payout ratio on an annualized basis is 80% of distributable cash. The actual payout ratio for the first interim period was 57%. The target payout ratio level is the anticipated level for the twelve month calendar period. The payout ratio will vary with the seasonality of the Partnership's cash flow. Periods of higher activity will cause the ratio to decrease, likewise lower activity periods will cause the ratio to increase.
- The integration of the acquired businesses is proceeding successfully with strong customer support, relocation into a common office facility in April, 2006 and the start of harmonization of operational policies and practices.

Overview of the Partnership Formation

The Partnership is a limited partnership formed on January 13, 2006 under the *Limited Partnerships Act* (Ontario). The Partnership was organized in accordance with and is governed by the terms and conditions of a limited partnership agreement dated January 13, 2006 and amended and restated on March 2, 2006 (the "Partnership Agreement"). The Partnership's business and affairs are managed by Canadian Energy Services Inc. (the "General Partner") pursuant to the Partnership Agreement. A copy of the Partnership Agreement is available on the Partnership's SEDAR profile at www.sedar.com.

The General Partner was incorporated on December 9, 2005 under the *Business Corporations Act* (Alberta). The General Partner is responsible for the administration and management of the Partnership and carries out the objects, purposes and business of the Partnership. The General Partner had not carried on any business prior to the date the Partnership commenced operations other than in connection with the Partnership's initial public offering and the acquisition of the drilling fluids businesses and does not hold any material assets other than legal title to certain assets for the sole benefit of the Partnership. The General Partner owns a 0.01% general partnership interest in the Partnership.

The Partnership commenced business operations on March 2, 2006, following the acquisition of the businesses of two private drilling fluid service companies. See "Investing Activities - Business Acquisitions" on page 8. Immediately thereafter, the Partnership completed an initial public offering ("IPO") for net proceeds of $55.4 million. See "Financing Activities" on page 9. CES designs and implements drilling fluid systems for the oil and gas industry, in particular relating to drilling medium to deep vertical and directional wells and horizontal wells in Western Canadian Sedimentary Basin ("WCSB").

30-day Reporting Period and Comparative Information

The following financial information for CES is for the 30-day period from the commencement of operations on March 2, 2006 to the end of the period, March 31, 2006. Readers should note the 30-day period does not represent a complete quarter of operations.

No comparative information or analysis is provided as financial results for the prior period are not available and would not be considered directly comparable due to the complexity of harmonizing the accounting periods and policies for the past financial information of the acquired businesses.

Non-GAAP Measures

The financial statements have been prepared in accordance with Canadian Generally Accepted Accounting Principles ("GAAP"). Certain supplementary information and measures not recognized under GAAP are also provided where management believes they assist the reader in understanding the Partnership's results and will be calculated on a consistent basis. These measures include:

Cash flow or cash flow from operations – cash flow from operations before changes in non-cash working capital
Distributable cash – cash flow from operations less maintenance capital
EBITDAC – earnings before interest, taxes, amortization and unit-based compensation expense
Gross margin – revenue less cost of sales, which represent cost of product and field operating costs
Payout ratio – distributions declared as a percentage of distributable cash

These measures are identified and presented, where appropriate, together with reconciliations to the equivalent GAAP measure. However, they should not be used as an alternative to GAAP measures, because they may not be consistent with calculations of other companies, trusts or partnerships.

Results for the Interim Period

	30-day period ended March 31, 2006
($000's, except per unit amounts)	
Revenue	6,922
Cost of sales	5,153
Gross margin	1,769
% of revenue	26%
Selling, general and administrative expenses	467
Amortization of property and equipment	23
Partnership unit-based compensation	9
Other income	(9)
Net earnings	1,279
per unit – basic	0.14
per unit – diluted	0.14

Revenue and Operating Activities

Revenue for the 30-day period was $6.9 million driven by a strong month of drilling activity and the benefits being realized from integrating the acquired businesses. Drilling activity in the WCSB generally continued to stay strong through to the end of March with the seasonal drop off in activity not occurring until early April. An exception was for southeast Saskatchewan, where drilling activity came to a stop in the 3rd week of March which is traditionally when the municipalities impose road bans.

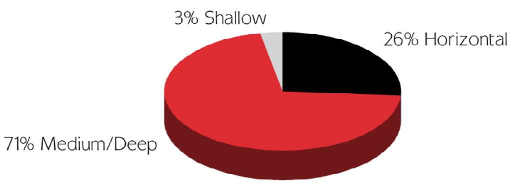
CES continued to focus on the medium to deep and horizontal wells which represented 97% of revenue for the 30-day period.

The Partnership classifies oil and natural gas wells by depth, as follows:

shallow wells:	generally less than 1,000 metres;
medium wells:	generally between 1,000 and 2,500 metres;
deep wells:	generally greater than 2,500 metres; and
horizontal wells:	drilled vertically then horizontally with often multiple lateral legs reaching out 500 to 1,500 metres each.

CES's experience has been that drilling fluid systems profitability increases significantly with the depth and complexity of the well drilled.

The following chart illustrates the Partnership's revenue by well type for the 30-day period ended March 31, 2006:



Organic growth in revenue was generated within the first interim period from cross-selling technologies previously developed for Foothills applications (Envirobond/IFS Invert) to clients who have traditionally used CES for horizontal wells. In addition, cross-selling oilsands technology (Liquidrill/Tarbreak) to existing Foothills clients is being pursued.

Moose Mountain Mud ("MMM") continued to operate as a locally based division of CES providing Liquidrill horizontal technology to customers in southeast Saskatchewan. MMM was very active in the Bakken horizontal play and other carbonate horizontal projects during the 30 day period ended March 31, 2006.

Cost of Sales and Gross Margin

Gross margin of $1.8 million, or 26% of revenue, was generated for the 30-day period. Gross margin represents the profit earned on revenue after deducting the cost of materials, field labour and all related field costs. Margins were slightly lower than expected due to higher input costs.

CES has continued with its initiative to maintain inventory levels of Liquidrill in strategic warehouses throughout the WCSB in order to maximize margins from lowering product costs for use on horizontal wells, including oilsands projects.

Key input costs for CES's business include hydrocarbon base oil and labor costs which are rising throughout the entire industry. The cost of base oil is passed through to the customer on a monthly price schedule. CES is working with its customers to recover labour cost increases through increases in the day rates for field engineering services.

Selling, General and Administrative Expenses

Selling, general and administrative costs for the 30-day period were $467,000. This includes public entity costs which were slightly higher than anticipated.

Cost to the Partnership also reflect a number of one-time costs and the impact of the fixed costs on the short period. The higher level of one-time costs have continued into April as CES completes the integration process.

The operations group in Calgary was expanded to manage the growth of job count in the field. Recruiting for additional accounting and administrative staff was completed in April. Another key accomplishment was the move into a common office space in downtown Calgary in early April.

Other Expense (Income) Items

Amortization was $23,000 for the 30-day period, largely related to the vehicles which are amortized on a straight-line basis over 3 years.

Unit-based compensation was determined using the Black-Scholes option pricing model, expensed over the three year vesting period.

Other income represents interest income earned on short term investments.

Liquidity and Capital Resources

At March 31, 2006 the Partnership had cash and cash equivalents of $6.7 million. Working capital was positive at $13.5 million.

Included in long-term liabilities is an amount of $6.0 million owing to the Vendors on the purchase of the drilling fluids businesses (see "Investing Activities - Business Acquisitions" and "Transactions with Related Parties"). Management is satisfied that the Partnership has sufficient liquidity and capital resources to meet this long-term payment obligation.

CES is in the process of securing a line of credit for $3.0 million for general operating purposes.

Financial instruments of CES include cash and cash equivalents, accounts receivable, accounts payable, accrued liabilities and amounts due to Vendors. As at March 31, 2006 there were no significant differences between the carrying value of these amounts and their estimated fair market value.

Cash Flow from Operating Activities and Distributions

	30-day period ended March 31, 2006
($000's)	
Cash flow from operations, before changes in non-cash working capital items	1,311
Maintenance capital	73
Distributable cash[1]	1,238
Distributions declared	705
Payout ratio	57%

Note:
[1] Refer to the "Non-GAAP Measures" on page 5 for further detail

Distributable cash was $1.2 million. The Partnership declared an initial monthly distribution on March 31, 2006 of $0.0792 per Class A Common limited partnership unit ("Class A Unit") and $0.0792 per Class B subordinated limited partnership unit ("Subordinated Class B Unit") to unitholders of record on March 31, 2006.

Subsequent to the quarter end, CES declared a monthly distribution of $0.0792 per Class A Unit to unitholders of record on April 30, 2006. Distributions on the Subordinated Class B Units are paid on a quarterly basis, subject to the Partnership achieving certain distribution targets on the Class A Units.

Investing Activities

Capital Expenditures
The Partnership incurred $333,000 in capital expenditure for the 30-day period ended March 31, 2006. The majority of the capital expenditure was in respect of the purchase of the land, building and related equipment for the Carlyle, Saskatchewan inventory warehouse facility for approximately $260,000. The remainder of the capital expenditure was for vehicles and other equipment.

Business Acquisitions
On March 2, 2006, the Partnership completed the acquisition of the drilling fluid businesses from Impact Fluid Systems Inc. ("Impact") and Canadian Fluid Systems Ltd. ("CFS") (collectively the "Vendors") for an aggregate purchase price of $80.7 million, subject to working capital adjustments.

The working capital adjustment is calculated based on a minimum working capital amount from each of Impact and CFS. Working capital in excess of this amount is added to the purchase price of the respective businesses. The working capital adjustment is to be determined by CES within a 120-day period from the acquisition date. At the time of closing of the acquisition, the minimum working capital amount was estimated to be $700,000 for each of Impact and CFS for a total of $1.4 million. As a result of the increase in activity and the need to maintain a higher level of working capital in the Partnership, on May 10, 2006, the Vendors and the Partnership agreed to amend the drilling fluid business acquisition agreements to provide for a maximum working capital adjustment of $6.0 million rather than an $8.8 million working capital adjustment that would have been otherwise payable under the acquisition agreements due to the strong performance of the businesses prior to closing.

The purchase price was funded by the payment of $50.6 million in acquisition notes, $6.0 million payable to the Vendors, the issuance of 860,594 Class A Units and the issuance of 2,151,486 Subordinated Class B Units at the initial public offering price of $10 per unit.

The acquisition of the drilling fluid businesses by the Partnership has been accounted for using the purchase method.

	Impact	CFS	Total
Net assets acquired	$000's	$000's	$000's
Current assets	17,040	10,227	27,267
Property and equipment	659	16	675
Goodwill	37,783	38,271	76,054
Current liabilities	(11,717)	(5,153)	(16,870)
Long-term debt	(404)	-	(404)
	43,361	43,361	86,722

	Impact	CFS	Total
Consideration	$000's	$000's	$000's
Acquisition notes	25,301	25,301	50,602
Due to Vendors	3,000	3,000	6,000
Class A Units	4,303	4,303	8,606
Subordinated Class B Units	10,757	10,757	21,514
	43,361	43,361	86,722

The acquisition notes were repaid with proceeds from the initial public offering (the "IPO") (see "Financing Activities").

The payable to the Vendors of $6.0 million will be evidenced at or before the end of the working capital adjustment period by an unsecured promissory note to each Vendor in the amount of $3.0 million. Each note will be for a term of 2 years, and will be non-interest bearing for the first year of the term but shall bear interest at the Royal Bank of Canada prime rate on the second year of the term.

On May 10, 2006 the Partnership agreed to grant an option in favour of the Vendors to convert the promissory note arising from the working capital adjustment to Class A Units at $10 per unit for a period of up to six months from March 2, 2006, the effective date of the acquisitions.

The above business acquisitions were transacted with certain individuals, or entities controlled by them, who as a result of the acquisitions are significant unitholders of the Partnership. These individuals or persons related to them have continued in key management roles with the General Partner. In addition, Rodney L. Carpenter and Thomas J. Simons are officers, directors and significant shareholders of CFS and Impact, respectively, as well as directors of the General Partner.

Pursuant to the 120-day adjustment period, CES is still confirming the fair value of the working capital items and, as a result, the working capital adjustment may differ from the amount estimated, which could change the purchase price and the allocation.

Financing Activities

On March 2, 2006 the Partnership completed the IPO of 5,893,866 Class A Units at a price of $10 per unit for aggregate gross proceeds of $58.9 million before deducting $3.5 million in underwriting commissions and approximately $1.8 million in miscellaneous costs relating to the IPO. Of the net proceeds, $50.6 million was used to repay the acquisition notes issued to each of CFS and Impact in connection with the business acquisitions described under "Investing Activities - Business Acquisitions" and the remaining $3.0 million was retained in the Partnership to fund growth opportunities including the purchase of the Carlyle warehouse facility.

Unitholders' Equity

On March 2, 2006 the Partnership closed the IPO of 5,893,866 Class A Units at a price of $10 per Class A Unit, for aggregate gross proceeds of $58.9 million or net proceeds of approximately $53.6 million after offering expenses and underwriters' commission of $5.3 million.

In connection with the acquisition of the drilling fluid businesses, the Partnership issued an aggregate of 860,594 Class A Units and 2,151,486 Subordinated Class B Units to the Vendors as partial consideration for the acquired businesses. The Subordinated Class B Units issued to CFS and Impact in connection to the acquisitions are non-transferable (except to certain shareholders, associates or affiliates of the respective Vendors) and are only exchangeable into Class A Units on or after March 2, 2009, unless a take-over bid is made for the Class A Units and certain other limited circumstances. Distributions on the Subordinated Class B Units are paid quarterly subject to achieving certain distribution targets on the Class A Units.

The Partnership is authorized to issue an unlimited number of Class A Units and Subordinated Class B Units.

	Number of units	Amount
		($000's)
Class A Units issued pursuant to the IPO	5,893,866	$ 58,939
Class A Units issued as consideration for acquired businesses	860,594	8,606
Subordinated Class B Units issued as consideration for acquired businesses	2,151,486	21,514
Unit issue expenses		(5,336)
Partnership units at March 31, 2006	8,905,946	$ 83,723

Unit Option Plan

The Partnership may provide additional compensation to the General Partner's employees, officers, directors and certain other service providers by issuing options to acquire Class A Units under the Partnerships' Unit Option Plan (the "Unit Option Plan"). As at March 31, 2006, 890,595 Class A Units were reserved for issuance under the Unit Option Plan, of which 315,595 Class A Units remain available for option grants. The 575,000 outstanding options vest as to one-third on each of the first, second and third anniversary dates of the grant (March 2, 2006) and expire on March 2, 2011.

Off-balance Sheet Arrangements

The Partnership does not have any off-balance sheet arrangements.

Transactions with Related Parties

The amount due to the Vendors of $6.0 million represents the amount owing to companies controlled by certain directors, officers and unitholders of the Partnership as the balance owing for the purchase of the assets of CFS and Impact. The amount was determined based on a working capital adjustment pursuant to the respective drilling fluid business acquisition agreements, as amended. It is currently anticipated that this amount will be represented by an unsecured promissory note in favor of each of CFS and Impact that are for a two year term, are non-interest bearing for the first year of the term but shall bear interest at the Royal Bank of Canada prime rate on the second year of the term. The promissory notes will be convertible into Class A Units for a period of six months beginning on March 2, 2006 (refer to "Investing Activities - Business Acquisitions").

In addition, included in current assets, the amount due from the Vendors of $266,000 represents amounts owing from companies controlled by certain directors, officers and unitholders of the Partnership for transactions conducted in the normal course of business at an amount equal to fair market value.

Critical Accounting Policies and Estimates

CES prepares its financial statements in accordance with Canadian GAAP (Generally Accepted Accounting Principles). There were no new accounting policies implemented during the period presented which impact on the Partnership.

As a routine element of the financial statement preparation process, management is required to make estimates and assumptions based on information available as at the financial statement date. These estimates and assumptions affect the reported amounts of assets and liabilities, the possible disclosure of contingent assets and liabilities at the date of the financial statements and the amount of revenue and expense reported for the period.

Although estimates and assumptions must be made during the financial statement preparation process, it is management's opinion that none of the estimates or assumptions were highly uncertain at the time they were made. The most significant estimate in CES's financial statements is the amortization period for property and equipment.

Initial Adoption of Accounting Policies

The Partnership has adopted the following significant accounting policies:

(a) Cash and cash equivalents:

The Partnership considers deposits in banks, certificates of deposit and short-term investments with original maturities of three months or less from the acquisition date as cash and cash equivalents.

(b) Inventory:

Inventory is stated at the lower of cost, determined on a first-in, first-out basis, and net realizable value.

(c) Property and equipment:

Property and equipment are recorded at cost less accumulated amortization. Property and equipment are amortized using the straight-line method over their estimated useful lives at the following rates:

Computer equipment and software	3 years	straight-line method
Vehicles	3 years	straight-line method
Field equipment	5 years	straight-line method
Furniture and fixtures	5 years	straight-line method
Buildings	10 years	straight-line method

The Partnership regularly reviews its property and equipment to eliminate obsolete items.

d) Goodwill:

Goodwill is the residual amount that results when the purchase price of an acquired business exceeds the sum of the amounts allocated to the assets acquired, less liabilities assumed, based on their fair values.

Goodwill is not amortized and is tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. The impairment test is carried out in two steps. In the first step, the carrying amount of the reporting unit is compared with its fair value. When the fair value of a reporting unit exceeds its carrying amount, goodwill of the reporting unit is considered not to be impaired and the second step of the impairment test is unnecessary.

The second step is carried out when the carrying amount of a reporting unit exceeds its fair value, in which case, the implied fair value of the reporting unit's goodwill is compared with its carrying amount to measure the amount of the impairment loss, if any. The implied fair value of goodwill is determined in the same manner as the value of goodwill is determined in a business combination, using the fair value of the reporting unit as if it was the purchase price. When the carrying amount of goodwill exceeds the implied fair value of the goodwill, an impairment loss is recognized in an amount equal to the excess. Impairment provisions are not reversed if there is a subsequent increase in the fair value of goodwill.

(e) Revenue recognition:

The Partnership's revenue is primarily comprised of the sale of products and the provision of services. Revenue on sales of product is recognized based on fixed or determinable prices when the product has been delivered to the well site and the product has been mixed. Revenue from field service charges is recognized based upon agreed daily, hourly or job rates, when the service is performed. Revenue will only be recognized when collection is reasonably assured.

(f) Unit-based compensation:

The Partnership uses the fair value method to account for options granted to employees and directors. Under the fair value method, the fair value of the options is estimated at the grant date using the Black-Scholes option pricing method, and such fair value is expensed over the vesting period, with a corresponding increase in contributed surplus. The amount of compensation expense and contributed surplus is reduced for options that are cancelled prior to vesting. Any consideration received upon the exercise of the unit based compensation together with the amount of non-cash compensation expense recognized in contributed surplus is recorded as an increase in unitholders' capital.

(g) Earnings per unit:

Basic earnings per unit are computed by dividing net earnings by the weighted average number of units outstanding during the year. The Partnership uses the treasury stock method for calculating diluted earnings per unit. Diluted earnings per unit are computed similar to basic earnings per unit except that the weighted average units outstanding are increased to include additional units from the assumed exercise of unit options, if dilutive. The number of additional units is calculated by assuming that outstanding unit options were exercised and that the proceeds from such exercises were used to acquire units of common stock at the average market price during the year.

Management of the Partnership is not aware of any recent accounting pronouncements or developments that will effect the Partnership's financial statements. Management will continue to monitor and assess the impact of accounting pronouncements on the Partnership's financial statements as they become available.

Financial Instruments

The net carrying value of accounts receivable approximates fair value due to the short-term nature of these instruments. The Partnership has a large number of diverse customers, which minimizes overall accounts receivable credit risk.

The carrying value of accounts payable and accrued liabilities and distributions payable approximates the fair value of these financial instruments due to their short-term nature.

The Partnership is exposed to minimal interest rate risk due to limited long-term debt outstanding.

Risk and Uncertainties

The drilling industry is cyclical and the business of CES is directly affected by fluctuations in the level of oil and natural gas exploration and development activity carried on by its clients. Drilling activity is seasonal and, in turn, is directly affected by a variety of factors, including weather, oil and natural gas prices, access to capital markets and government policies including environmental regulations. Any prolonged or significant decrease in energy prices or economic activity, or adverse change in government regulations could have a significant negative impact on exploration and development drilling activity in Canada.

The oil and natural gas drilling season is affected by weather. The industry is generally more active during the winter months of November through March, as the movement of heavy equipment is easier over the frozen ground. Wet weather in the spring and summer can hamper the movement of drilling rigs which has a direct impact upon generating revenue. Conversely, a longer colder winter as well as a dry spring and summer strengthen drilling operations, which would enhance CES's revenue generation. Mitigation of weather risk is difficult and costly as effective derivative products do not yet exist to successfully manage this risk.

The ability of the Partnership to expand its services will depend upon the ability to attract qualified personnel as needed. The demand for skilled oilfield employees and drilling fluid technicians is high, and the supply is limited. The unexpected loss of the Partnership's key personnel or the inability to retain or recruit skilled personnel could have an adverse effect on the Partnership's results. CES addresses this risk by:

- attracting well trained and experienced professionals;
- offering competitive compensation at all levels;
- ensuring a safe working environment with clearly defined standards and procedures; and
- offering its employees both internal and external training programs.

CES takes its environmental responsibilities seriously and has instituted standards, policies and procedures to address this risk area. In addition, the Partnership maintains insurance policies with respect to its operations providing coverage of all material insurable risks.

A concentration of credit risk exists in CES's trade accounts receivable since they are exclusively from companies in the western Canadian oil and gas industry. Significant changes in the oil and gas industry including economic conditions, environmental regulations, government policy and other geopolitical factors may adversely affect CES's ability to realize the full value of its accounts receivable. It is not possible to predict the likelihood or magnitude of this risk. CES attempts to mitigate this risk by performing credit checks on key customers, managing the amount and timing of exposure to individual customers and by review of its credit policies on a regular basis. There were no bad debts in the 30-day period ended March 31, 2006.

Reference should be made to the final prospectus of the Partnership dated February 21, 2006 in respect of the Partnership's IPO, and in particular to the heading "Risk Factors" for further risks associated with the business, operations and structure of the Partnership.

Outlook

The industry outlook remains strong for drilling activity and related services. CES is well positioned for profitable growth in this environment with emphasis on the following areas:

- With natural gas production declining, operators continue to pursue deeper gas where CES technology proves very effective and is widely used.

- Conventional horizontal drilling for oil is very active, driven by high commodity prices. Liquidrill technology remains a leading drilling fluid in the industry.

- Oilsands drilling activity is increasing as drilling contractors build out new rigs that have been specially built for steam assisted gravity drainage ("SAGD") type drilling and the commercial phases of these projects will provide significant opportunities.

- There are increasing opportunities to tender for projects with larger operators. Management attributes this to effective cross selling and positive response to CES having greater critical mass and infrastructure.

BALANCE SHEET

as at March 31, 2006 (stated in thousands of dollars)

		2006
		(unaudited)
ASSETS		
Current assets		
Cash and cash equivalents (note 5)	$	6,745
Accounts receivable		25,678
Due from Vendors (note 14)		266
Inventory		1,645
Prepaid expenses		372
		34,706
Property and equipment (note 6)		986
Goodwill (note 4)		76,054
	$	111,746
LIABILITIES AND UNITHOLDERS' EQUITY		
Current liabilities		
Accounts payable and accrued liabilities	$	20,346
Distributions payable		705
Current portion of long term debt (note 7)		184
		21,235
Long term debt (note 7)		205
Due to Vendors (notes 4, 14)		6,000
		27,440
Unitholders' equity		
Class A Units (note 8)		62,209
Subordinated Class B Units (note 8)		21,514
Contributed surplus		9
Retained earnings		574
		84,306
	$	111,746

Commitments (note 12)
Subsequent Event (note 16)

APPROVED ON BEHALF OF THE BOARD:

Tom Sim

Thomas J. Simons

President & Chief Executive Officer and Director

D M Stewart

D. Michael G. Stewart

Director & Chairman, Audit Committee

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

STATEMENT OF OPERATIONS AND RETAINED EARNINGS

From commencement of operations on March 2, 2006 to March 31, 2006
(stated in thousands of dollars except per unit amounts)

		2006
		(unaudited)
Revenue	$	6,922
Cost of sales		5,153
Gross margin		1,769
Expenses		
Selling, general and administrative expenses		467
Amortization of property and equipment		23
Partnership unit-based compensation		9
		499
Other income		9
Net earnings for the period		1,279
Retained earnings, beginning of period		-
Unitholders' distributions declared		705
Retained earnings, end of period	**$**	**574**
Net earnings per Partnership unit (note 10)		
Basic	$	0.14
Diluted	$	0.14

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

STATEMENT OF CASH FLOW

From commencement of operations on March 2, 2006 to March 31, 2006
(stated in thousands of dollars)

		2006
		(unaudited)
CASH PROVIDED BY (USED IN):		
OPERATING ACTIVITIES:		
Net earnings for the period	$	1,279
Items not involving cash:		
Amortization of property and equipment		23
Partnership unit-based compensation		9
Change in non-cash operating working capital (note 15)		1,970
		3,281
FINANCING ACTIVITIES:		
Units issued for cash, net of issue costs		53,602
Repayment of long-term debt		(15)
Change in non-cash financing working capital (note 15)		812
		54,399
INVESTING ACTIVITIES:		
Repayment of acquisition notes (note 4)		(50,602)
Purchase of property and equipment		(333)
		(50,935)
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS		6,745
Cash and cash equivalents — Beginning of period		-
Cash and cash equivalents — End of period (note 5)	$	6,745
SUPPLEMENTARY CASH FLOW DISCLOSURE		
Interest paid	$	-
Taxes paid	$	-

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

Notes to Financial Statements (in thousands of dollars, except unit and per unit amounts) 17

Canadian Energy Services L.P.
(unaudited)
From commencement of operations on March 2, 2006 to March 31, 2006

1. The Limited Partnership

Canadian Energy Services L.P. (the "Partnership") is a limited Partnership formed on January 13, 2006, pursuant to the *Limited Partnerships Act* (Ontario). The partnership is a "Canadian partnership" as defined in subsection 102(1) of the *Income Tax Act* (Canada) (the "Act") and the terms of a limited partnership agreement dated January 13, 2006, and amended and restated on March 2, 2006 (the "Partnership Agreement"), prohibit the issuance of units to, and the admittance as partners of, persons who are non-residents of Canada for the purposes of the Act.

On March 2, 2006, the Partnership commenced business operations when it acquired the businesses of two private drilling fluid companies. Consideration for the acquisition was comprised of acquisition notes, the issuance of Class A Common limited partnership units ("Class A Units") and the issuance of Class B subordinated limited partnership units ("Subordinated Class B Units"). On March 2, 2006 the acquisition notes were repaid with the proceeds from the Partnership's initial public offering of the 5,893,866 Class A Units.

Canadian Energy Services Inc., the general partner of the Partnership (the "General Partner"), was incorporated on December 9, 2005 under the *Business Corporations Act* (Alberta). The General Partner is authorized to carry on the business of the Partnership and has full power and exclusive authority to administer, manage, control, and operate the business of the Partnership. The Partnership reimburses the General Partner for all direct costs and expenses incurred in the performance of those duties.

The Partnership designs and implements drilling fluid systems for the oil and gas industry, in particular relating to drilling medium to deep vertical and directional wells and horizontal wells in Western Canada.

2. Basis of Presentation

The consolidated financial statements have been prepared by management of the Partnership in accordance with Canadian generally accepted accounting principles.

3. Significant Accounting Policies:

(a) Cash and cash equivalents:

The Partnership considers deposits in banks, certificates of deposit and short-term investments with original maturities of three months or less from the acquisition date as cash and cash equivalents.

(b) Inventory:

Inventory is stated at the lower of cost, determined on a first-in, first-out basis, and net realizable value.

(c) Property and equipment:

Property and equipment are recorded at cost less accumulated amortization. Property and equipment are amortized using the straight-line method over their estimated useful lives at the following rates:

Computer equipment and software	3 years	straight-line method
Vehicles	3 years	straight-line method
Field equipment	5 years	straight-line method
Furniture and fixtures	5 years	straight-line method
Buildings	10 years	straight-line method

The Partnership regularly reviews its property and equipment to eliminate obsolete items.

(d) Goodwill:

Goodwill is the residual amount that results when the purchase price of an acquired business exceeds the sum of the amounts allocated to the assets acquired, less liabilities assumed, based on their fair values.

Goodwill is not amortized and is tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. The impairment test is carried out in two steps. In the first step, the carrying amount of the reporting unit is compared with its fair value. When the fair value of a reporting unit exceeds its carrying amount, goodwill of the reporting unit is considered not to be impaired and the second step of the impairment test is unnecessary.

The second step is carried out when the carrying amount of a reporting unit exceeds its fair value, in which case, the implied fair value of the reporting unit's goodwill is compared with its carrying amount to measure the amount of the impairment loss, if any. The implied fair value of goodwill is determined in the same manner as the value of goodwill is determined in a business combination, using the fair value of the reporting unit as if it was the purchase price. When the carrying amount of goodwill exceeds the implied fair value of the goodwill, an impairment loss is recognized in an amount equal to the excess. Impairment provisions are not reversed if there is a subsequent increase in the fair value of goodwill.

(e) Revenue recognition:

The Partnership's revenue is primarily comprised of the sale of products and the provision of services. Revenue on sales of product is recognized based on fixed or determinable prices when the product has been delivered to the well site and the product has been mixed. Revenue from field service charges is recognized based upon agreed daily, hourly or job rates, when the service is performed. Revenue will only be recognized when collection is reasonably assured.

(f) Unit-based compensation:

The Partnership uses the fair value method to account for options granted to employees and directors. Under the fair value method, the fair value of the options is estimated at the grant date using the Black-Scholes option pricing method, and such fair value is expensed over the vesting period, with a corresponding increase in contributed surplus. The amount of compensation expense and contributed surplus is reduced for options that are cancelled prior to vesting. Any consideration received upon the exercise of the unit based compensation together with the amount of non-cash compensation expense recognized in contributed surplus is recorded as an increase in unitholders' capital.

(g) Income taxes:

The income of the Partnership is taxed at the partner level. As a result, provisions for income and capital taxes are not made by the Partnership. These financial statements include the assets, liabilities, and operations of the Partnership and do not include the assets, liabilities, including income tax, of the partners.

(h) Measurement uncertainty:

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Such estimates include providing for amortization of property and equipment. Actual results could differ from these estimates.

(i) Earnings per unit:

Basic earnings per unit are computed by dividing net earnings by the weighted average number of units outstanding during the year. The Partnership uses the treasury stock method for calculating diluted earnings per unit. Diluted earnings per unit are computed similar to basic earnings per unit except that the weighted average units outstanding are increased to include additional units from the assumed exercise of unit options, if dilutive. The number of additional units is calculated by assuming that outstanding unit options were exercised and that the proceeds from such exercises were used to acquire units of common stock at the average market price during the year.

Notes to Financial Statements (in thousands of dollars, except unit and per unit amounts) 19

(j) Financial instruments:

The net carrying value of accounts receivable approximates fair value due to the short-term nature of these instruments. The Partnership has a large number of diverse customers, which minimizes overall accounts receivable credit risk.

The carrying value of accounts payable and accrued liabilities, amounts due to vendors, and distributions payable approximates the fair value of these financial instruments due to their short-term nature.

The Partnership is exposed to minimal interest rate risk due to limited long-term debt outstanding.

4. Business Acquisitions:

On March 2, 2006 the Partnership completed the acquisition of the drilling fluid businesses from Impact Fluid Systems Inc. ("Impact") and Canadian Fluid Systems Ltd. ("CFS") (collectively the "Vendors") for an aggregate purchase price of $80.7 million, plus an estimated working capital adjustment of $6.0 million. The purchase price was funded by the payment of $50.6 million in acquisition notes, $6.0 million payable to the Vendors, the issuance of 860,594 Class A Units and the issuance of 2,151,486 Subordinated Class B Units at the initial public offering ("IPO") price of $10 per unit. The working capital adjustment is to be determined by the Partnership within a 120-day period from the acquisition date. The acquisition has been accounted for using the purchase method.

	Impact	CFS	Total
Net assets acquired	$	$	$
Current assets	17,040	10,227	27,267
Property and equipment	659	16	675
Goodwill	37,783	38,271	76,054
Current liabilities	(11,717)	(5,153)	(16,870)
Long-term debt	(404)	-	(404)
	43,361	43,361	86,722
Consideration			
Acquisition notes	25,301	25,301	50,602
Due to Vendors	3,000	3,000	6,000
Class A Units	4,303	4,303	8,606
Subordinated Class B Units	10,757	10,757	21,514
	43,361	43,361	86,722

The acquisition notes were repaid with proceeds from the initial public offering (note 8).

The payable to the Vendors will be evidenced by unsecured promissory notes that are for a term of 2 years, at such time they become payable on demand, and are non-interest bearing for the first year of the term but shall bear interest at the Royal Bank of Canada prime rate on the second year of the term. Subsequent to the period end, certain terms of the promissory notes were amended (note 16).

20 Notes to Financial Statements (in thousands of dollars, except unit and per unit amounts)

The above business acquisitions were transacted with certain individuals, or entities controlled by them, who as a result of the acquisitions are significant unitholders of the Partnership. These individuals or persons related to them have continued in key management roles with the General Partner. In addition, Rodney L. Carpenter and Thomas J. Simons are officers, directors and significant shareholders of CFS and Impact, respectively, as well as directors of the General Partner.

Pursuant to the 120-day adjustment period, the Partnership is still confirming the fair value of the working capital items and, as a result, the working capital adjustment may differ from the amount estimated, which could change the purchase price and the allocation.

5. Cash and Cash equivalents:

The major components of cash and cash equivalents are as follows:

Cash	$ 345
Temporary investments	6,400
	$ 6,745

6. Property and Equipment

	Cost	Accumulated Amortization	Net Book Value March 31, 2006
Computer equipment and software	$ 48	$ 1	$ 47
Vehicles	496	14	482
Field equipment	192	5	187
Furniture and fixtures	42	1	41
Buildings	222	2	220
Land	9	-	9
	$ 1,009	$ 23	$ 986

7. Long-term Debt

Vehicle financing loans, repayable in monthly payments of $1.2- $1.7, maturing from January 2007 to July 2009	$ 389
Less current portion	184
	$ 205

Principal payments are as follows for the periods ending March 31:

2007	$ 184
2008	184
2009	21

Notes to Financial Statements (in thousands of dollars, except unit and per unit amounts) 21

8. Unitholders' Equity

The Partnership is authorized to issue an unlimited number of Class A Units and Subordinated Class B Units.

	Number of units	Amount
Class A Units issued pursuant to initial public offering	5,893,866	$ 58,939
Class A Units issued as consideration for acquired businesses	860,594	8,606
Subordinated Class B Units issued as consideration for acquired businesses	2,151,486	21,514
Unit issue expenses		(5,336)
Partnership units at March 31, 2006	8,905,946	$ 83,723

On March 2, 2006 the Partnership closed the IPO of 5,893,866 Class A Units at a price of $10 per Class A Unit, for gross proceeds of approximately $58.9 million or net proceeds of $53.6 million after offering expenses and underwriters' commission of approximately $5.3 million.

In connection with the acquistion of the drilling fluid businesses, the Parnership issued an aggregate of 860,594 Class A Units and 2,151,486 Subordinated Class B Units to the Vendors as partial consideration for the acquired businesses. The Subordinated Class B Units issued to CFS and Impact in connection with the acquisition are non-transferable (except to certain shareholders, associates or affiliates of the respective Vendors) and are only exchangeable into Class A Units on or after March 2, 2009, unless a take-over bid is made for the Class A Units and certain other limited circumstances. Distributions on the Subordinated Class B Units are paid quarterly subject to achieving certain distribution targets on the Class A Units.

9. Partnership Unit Option Plan

The Partnership may provide additional compensation to the General Partner's employees, officers, directors and certain service providers by issuing options to acquire Class A Units under the Partnership's unit option plan (the "Unit Option Plan"). As at March 31, 2006, 890,595 Class A Units were reserved for issuance under the Unit Option Plan, of which 315,595 Class A Units remain available for option grant. The 575,000 outstanding options vest as to one-third on each of the first, second and third anniversary dates of the grant (March 2, 2006) and expire on March 2, 2011.

The following tables summarize information about the Unit Option Plan as at March 31, 2006.

	Options	Average Exercise Price
Outstanding, beginning of period		$ -
Granted at March 2, 2006	575,000	10.00
Exercised	-	-
Expired	-	-
Outstanding, end of period, March 31, 2006	575,000	$ 10.00
Exercisable, end of period, March 31, 2006	-	-

The fair value of the options granted during the period was $331. During the period, compensation costs of $9 were recorded in the statement of operations. The compensation costs were calculated using the Black-Scholes option pricing model, assuming a risk-free interest rate of 4.0%, a dividend yield of 9.5%, an expected volatility of 21% and expected lives of unit options of 5 years.

22 Notes to Financial Statements (in thousands of dollars, except unit and per unit amounts)

10. Earnings Per Unit:

The computations for basic and diluted earnings per unit are as follows:

Net earnings		$ 1,279
Average number of units outstanding:		
	Basic	8,905,946
	Effect of unit options	-
Diluted		8,905,946
Earnings per unit:		
	Basic	$ 0.14
	Diluted	$ 0.14

Unit options to purchase 575,000 partnership units at $10 per unit were outstanding in 2006 but were not included in the computation of diluted earnings per share because the exercise price was greater than the average market price of the Partnership units for the period.

11. Cash Distributions

The Partnership declares monthly distributions of cash to Class A unitholders of record as at the close of business on each monthly distribution record date. In addition, the Partnership pays quarterly distributions on the Subordinated Class B Units to unitholders of record at the close of business on each quarterly distribution record date, subject to acheiving certain distribution targets on the Class A Units. Such distributions are recorded as reductions of equity upon declaration of the distribution. The Partnership has paid distributions to holders of Class A Units and Subordinated Class B Units for the period ended March 31, 2006 in accordance with the following schedule:

Distribution period 2006	Distributions Record Date	Date of Distribution	Per Unit[1]	Total
March 2 - March 31	March 31, 2006	April 13, 2006	$0.0792	$ 705
Total Distributions				**$ 705**

Note:

[1] Monthly distribution paid on Class A Units and quarterly distribution paid on Subordinated Class B Units.

12. Commitments

(a) The Partnership has an agreement regarding a sublease for office space until December 31, 2006 and expects to pay approximately $371 of rent and operating costs in fiscal 2006.

(b) The Partnership has numerous operating vehicle leases and expects to pay approximately $168 in vehicle lease expense in fiscal 2006.

13. Payments to the General Partner

The General Partner will be allocated 0.01% of the taxable income of the Partnership for each fiscal year and 99.9% of the taxable income of the Partnership will be allocated to the holders of Class A Units and Subordinated Class B Units.

Notes to Financial Statements (in thousands of dollars, except unit and per unit amounts) 23

14. Related Party Transactions:

Due from Vendors		
Due from Canadian Fluid Systems Ltd.	$	234
Due from Impact Fluid Systems Inc.		32
	$	266

Due to Vendors		
Due to Canadian Fluid Systems Ltd.	$	3,000
Due to Impact Fluid Systems Inc.		3,000
	$	6,000

Amounts due to the Vendors of $6.0 million represents the balance owing to companies controlled by certain directors, officers and unitholders of the Partnership for the purchase of the businesses of CFS and Impact. The amount was determined based on a working capital adjustment pursuant to the respective drilling fluid business acquisition agreements, as amended. It is currently anticipated that this amount will be represented by unsecured promissory notes in favor of CFS and Impact that are for a two year term, at such time they become payable on demand, and are non-interest bearing for the first year of the term but shall bear interest at the Royal Bank of Canada prime rate on the second year of the term. Subsequent to the period end, certain terms of the promissory notes were amended (note 16).

In addition, included in current assets, the amount due from the Vendors of $266 represents amounts owing from companies controlled by certain directors, officers and unitholders of the Partnership for transactions conducted in the normal course of business at an amount equal to fair value.

15. Supplemental Information:

Components of change in non-cash working capital balances:		
Operating:		
Accounts receivable	$	509
Inventory		(605)
Due from vendor		(266)
Prepaid expenses		(331)
Accounts payable and accrued liabilities		2,663
		1,970
Financing:		
Accounts payable and accrued liabilities		812
	$	2,782

16. Subsequent Event:

The Vendors and the Partnership agreed on May 10, 2006 to amend the drilling fluid business acquisition agreements to provide for (i) a maximum working capital adjustment of $6.0 million rather than an estimated $8.8 million that would have been otherwise payable to the Vendors under the acquisition agreements; and (ii) an option in favour of the Vendors to convert the amounts payable into Class A Units at a conversion price of $10 per unit for a period of up to six months from March 2, 2006, the date of the acquisition. Accordingly, the working capital adjustment payable to the Vendors and reflected as a long term liability of the Partnership has been fixed at $6.0 million in these interim financial statements.

BOARD OF DIRECTORS

Kyle D. Kitagawa [1]
Chairman

Alan D. Archibald [2]

Colin D. Boyer [1,2]

John M. Hooks [2]

D. Michael G. Stewart [1]

Thomas J. Simons

Rodney L. Carpenter

OFFICERS

Thomas J. Simons
President and Chief Executive Officer

Laura A. Cillis
Chief Financial Officer

Kenneth E. Zinger
Chief Operating Officer

Rodney L. Carpenter
Vice President, Business Development

A. David Rosenthal
Vice President, Operations

Kenneth D. Zandee
Vice President, Marketing

Scott R. Cochlan
Corporate Secretary

AUDITORS

Deloitte & Touche LLP
Chartered Accountants, Calgary, AB

BANKERS

Royal Bank of Canada, Calgary, AB

SOLICITORS

Blake, Cassels & Graydon LLP
Calgary, AB

REGISTRAR & TRANSFER AGENT

Computershare Investor Services Inc.,
Calgary, AB and Toronto, ON

STOCK EXCHANGE LISTING

The Toronto Stock Exchange
Trading Symbol: CEU.UN

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1 Member of the Audit Committee

2 Member of the Governance and Compensation Committee