
NURTURING GROWTH
CEAPRO ANNUAL REPORT 2006

GOING GREEN

Our approach to this annual report truly embodies Ceapro's commitment to the environment and our practice of "going green".

The 2006 Ceapro Annual Report is certified by the Forest Stewardship Council (FSC). FSC certification is the highest level of recognition in environmentally conscious printing practices, earned by those who use only 100% post consumer paper.

By using 100% post consumer paper, we have conserved approximately 13 million BTUs of energy, 720 kg. of CO_2, 25,000 L. of water and 400 kg. of waste.*

We invite our shareholders to visit our website at http://www.ceapro.com.

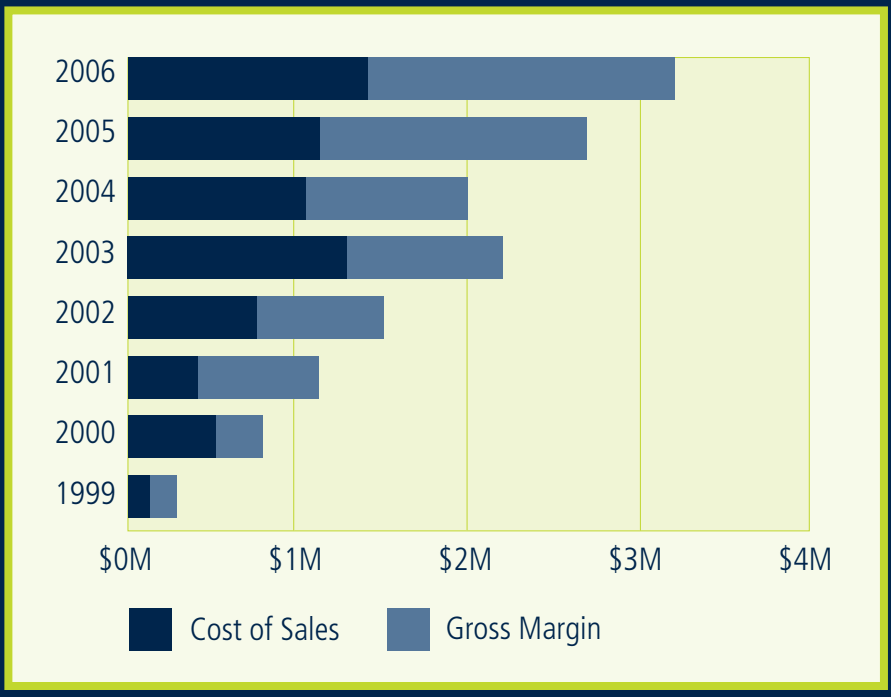
* Environmental impact estimates were made using the Environmental Defense Paper Calculator. For more information visit http://www.papercalculator.org and http://www.fsc.org.

NURTURING GROWTH

Ceapro's achievements during 2006 reflected the Company's diverse strengths and laid the ground for significant further growth. We increased sales, built new manufacturing capacity to fill our customers' orders, paid down our debts, and met our royalty obligations. Strategically we invested in the marketing plans for our own veterinary brand-name, Ceapro Dermatology, and our breakthrough diabetes product, CeaProve®.

HIGHLIGHTS

- Achieved record revenues of $3.3 million
- Increased active ingredient sales by 35%
- Maintained strong gross margins of 57% despite a weaker U.S. dollar and challenging labour market
- Reduced equipment debt by $78,790 or 14%
- Reduced royalty obligations by $373,170
- Readied the markets for CeaProve® and Ceapro Dermatology



DEAR FELLOW SHAREHOLDER:

The pursuit of organic remedies and natural active ingredients is at an all-time high as a response to accelerating consumer demands. This demand carries direct benefits for Ceapro. As a recognized forerunner in natural products, Ceapro's creations are sought by customers ranging from large pharmaceutical corporations to personal-care product manufacturers. Ceapro truly incarnates the vision and practice of "going green."

Our success to-date and for the future lies in understanding consumers' demands, anticipating market trends, and applying our intellectual capital. This capital lies in how to use and develop natural and renewable resources, understanding plant chemistry, and using our expertise in medicine, biology, and process engineering to create innovative solutions.

In 2006 Ceapro's sales and the potential of our technology gathered significant momentum in the marketplace. Revenues reached a record high, exceeding $3.3 million; Ceapro was profitable before R&D expenditures. At the same time we invested heavily in marketing, which has primed Ceapro for major gains – and significant shareholder value creation – in the year ahead.

EXPANDING MARKETS

Ceapro's active ingredient revenue for 2006 rose 35% over 2005. The growth came from increased sales to existing customers and the introduction of new products to new customers. Our gross margins stood at 57% of sales revenue. This performance owed its dynamism in part to greater economies of scale, improvements in process efficiency, and the strength of the relationship we enjoy with our marketing partners.

In 2006 our increased sales of beta glucan were particularly noteworthy. A number of new European clients placed orders ahead of new product introductions. These export sales have continued to increase despite the upward direction of the Canadian dollar over the last few years.

YEARS OF EFFORT REACH FRUITION

The news has spread about the benefits of incorporating Ceapro's active ingredients into diverse categories of products.

Cycles of product adoption exist in the life sciences industry. When Ceapro entered the market several years ago with novel extracts having proven benefits and superior performance, acceptance was not immediate and sales were not substantial. A lag occurred between introduction and acceptance. Based on indications received in 2006 the lag period has ended.

Furthermore, our unique technical and manufacturing abilities have been recognized and are increasingly sought after. For example, researchers at Tufts University in Boston have been exploring the use of oats as a treatment for

atherosclerosis and other diseases where inflammation plays a major role. These researchers demonstrated the potency of avenanthramides. However, to commercialize their technology they require large quantities of the material. They came to the material's leading producer – Ceapro.

BIO-ENERGY INITIATIVE

As specialists in grain processing and extraction technology we have been researching the bio-energy market for years. Our expertise in agro sciences, together with the growing demand for ethanol, makes it clear that there are major opportunities for Ceapro in this market.

Immediately subsequent to year end we formally entered the "green renewable fuels" sector with the establishment of Ceapro BioEnergy Inc. (CBE), a wholly-owned subsidiary aimed at facilitating the production of ethanol and value-added products. The potential impact of this initiative on Ceapro's value creation cannot be overstated.

CBE is conducting a feasibility study to evaluate the application of Ceapro's process technology toward improving the efficiency of ethanol manufacture. The concern in the marketplace is that without subsidies bio-ethanol is not financially viable. Our business strategy is to address that concern head-on. We aim to improve ethanol manufacturing by increasing the value of otherwise unused side-streams which Ceapro regards as excellent raw materials for producing active ingredients and other chemicals.

Our bio-energy initiative holds great promise of showing that the financial benefits of ethanol processing need not be dependent on a single stream of revenue. The opportunity exists for us to take ethanol itself as a raw material and further process it into other high-value goods. This approach perfectly suits Ceapro's fundamental strategy of adding value along the plant processing chain.

Furthermore, there is growing interest in producing ethanol from straw and other cellulose. The technology for producing ethanol from cellulose does not yet exist, but we will have evidence in the year ahead pertaining to Ceapro's ability to work with cellulose fermentation as opposed to grain fermentation. This direction respects the view that food should be used for food – as opposed to food being used for energy generation – and that ethanol should derive from materials not commonly destined for the human food chain. Ceapro's opportunity here is clear and potentially vast, and CBE's feasibility study will reveal the optimal approach for seizing the opportunity.

EXPANDED MANUFACTURING CAPACITY

Subsequent to our fiscal year end, Ceapro was preparing to relocate our production equipment to new, dedicated operating space adjoining our current lease facility. The move will double capacity and cut production times in half, and further enhance production efficiencies and margins.

FURTHER GROWTH IN 2007

The new facility and manufacturing capacity will allow Ceapro to deliver strong corporate growth as we open new doors in our traditional markets and introduce new active ingredients and therapeutic products. For example, in the spring we will launch two new extracts into the global marketplace with the introduction of hydrolyzed oat protein and hydrolyzed lupine protein.

HYDROLYZED PROTEIN

is protein that has been broken down into its component amino acids. While there are many means of achieving this, Ceapro uses proprietary enzymatic processes that produce a superior product for the personal care industry, with a light colour, low odour, and standardized concentration.

Critical to Ceapro's growth prospects are connections to pharmaceutical companies that can use Ceapro technology for bio-medical applications. For instance, we have cultivated a relationship and worked closely with a new client who has developed fifteen over-the-counter skin treatments, all based on Ceapro's beta glucan technology. These products are already in the market in small quantities, and production is in scale-up.

Our core extraction technology will be used as an integrated commercialization engine, one that we expect to generate ever-larger revenues and return on capital. With the aim of broadening our line of natural products, we have developed new technologies that are currently in R&D or pre-commercial stages. These technologies focus on the areas of oral hygiene, wound-care, and diabetes tests for animals. Plus we are broadening our sources of raw materials beyond oats and working with natural sources of active ingredients to benefit the health and vitality of humans and animals.

CEAPROVE®

A significant event for Ceapro's shareholders in 2007 will be the marketing of CeaProve®, our patented diabetes diagnostic. In development for more than twelve years, CeaProve® is now commercialized and entering broad market distribution. Winner of the prestigious Frost & Sullivan Product Innovation Award and recognized as a revolutionary technology, the CeaProve® screening test will be available in commercial quantities this spring.

This important product from Ceapro's pipeline provides a uniquely simple solution for early detection of type-2 diabetes. Diabetes is a metabolic disease that goes undetected for many years despite the presence of disease markers. People at risk are in a condition known as pre-diabetes, a state that can be reversed through a change of diet and an exercise regimen, or by using drugs specifically prescribed for pre-diabetes.

A key challenge has been to identify the condition early. Our product, CeaProve®, can forewarn of the onset of type-2 diabetes five to ten years earlier than standard methods.

The product consists of a meal of calibrated wafers. Forty-five minutes after eating the wafers, the user takes a blood sample with a simple finger-prick and a hand-held glucose meter. The blood sugar analysis from that sample allows detection of diabetes at a pre-disease state and indicates the likelihood of the subject developing the disease over the next five to ten years. Moreover, the test, when repeated at six-month intervals, can also show if dietary and other lifestyle changes are being effective in forestalling the disease.

We are confident that CeaProve® is poised to make a significant contribution to preventive healthcare globally. We will introduce CeaProve® to North American corporations as part of corporate wellness programs, and to healthcare providers internationally for point-of-care diagnosis. We also intend to make CeaProve® available through pharmacies and medical laboratories in Canada.

The disease of diabetes has reached epidemic proportions in many parts of the world. We believe that CeaProve® will become a flagship product in the public eye. The market potential for CeaProve® is tens of millions of tests to be sold annually. Ceaprove®'s function, ease-of-use, and unmistakable benefits represent immense potential value-creation.

OUTLOOK

Ceapro's success will benefit from the following factors:

- a growing base of revenues based on proprietary active ingredients and long-standing distribution partnerships;
- important new technology and products poised to enter markets demonstrated to be receptive for the technology;
- important technology under development in the fields of therapeutics, drug-delivery, and bio-energy.

All members of Ceapro are united in our mission to be a great company for our employees, our customers, and our shareholders by creating exceptional long-term value through leadership in our chosen markets. I am pleased to report that in 2006 we achieved significant success. Like any dynamic and growing organization, we must and will raise the bar for 2007. As entrepreneurial scientists, we look forward to rendering our opportunities into achievements and rewards.

Mark Redmond
President & CEO
Ceapro Inc.
April 3, 2007

MANAGEMENT'S DISCUSSION & ANALYSIS

The MD&A provides commentary on the results of operations for the years ended December 31, 2006 and 2005, financial position as at December 31, 2006 and the outlook of Ceapro Inc. ("Ceapro") based on information available as at March 19, 2007. The following information should be read in conjunction with the consolidated financial statements as at December 31, 2006, and related notes thereto, which are prepared in accordance with Canadian generally accepted accounting principles (Canadian GAAP). All comparative percentages are between the years ended December 31, 2006 and 2005 and all dollar amounts are expressed in Canadian currency, unless otherwise noted. Additional information about Ceapro can be found on SEDAR at www.sedar.com.

FORWARD-LOOKING STATEMENTS

This MD&A offers our assessment of Ceapro's future plans and operations as at March 19, 2007, and contains forward-looking statements. By their nature, forward-looking statements are subject to numerous risks and uncertainties, including those discussed below. You are cautioned that the assumptions used in the preparation of forward-looking information, although considered reasonable at the time of preparation, may prove to be imprecise and, as such, undue reliance should not be placed on forward-looking statements. Actual results, performance or achievements could differ materially from those expressed in, or implied by, these forward-looking statements. No assurance can be given that any of the events anticipated will transpire or occur, or if any of them do so, what benefits Ceapro will derive from them. We disclaim any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

VISION, CORE BUSINESS, AND STRATEGY

Ceapro Inc. (Ceapro) is incorporated under the Canada Business Corporations Act, and its wholly-owned subsidiaries, Ceapro Technology Inc., Ceapro Veterinary Products Inc., Ceapro Active Ingredients Inc., and Ceapro Bioenergy Inc. are incorporated under the Alberta Business Corporations Act. Ceapro is a growth stage biotechnology company. Our primary business activities relate to the development and commercialization of organic products for medical, cosmetic, and animal health industries using proprietary technology and natural, renewable resources. We will also be applying our technology to become an active participant in the bioenergy sector.

Our products include:

- A commercial line of active ingredients, including beta glucan, avenanthramides (colloidal oat extract and Drago-Calm), oat powder, oat oil, and new oat and lupin proteins which are marketed to the personal care and cosmetic industry through an exclusive agreement with our distribution partner, Symrise Inc.; and
- Veterinary therapeutic products, including an oat shampoo, an ear cleanser, and a dermal complex/conditioner, which are marketed to veterinarians in Japan and Asia, through distribution agreements with Daisen Sangyo Co. Ltd., in Canada by Aventix Animal Health, and in the United Kingdom by Pharmavet Ltd. In 2007 we will launch our own brand, Ceapro Dermatology and commence sales to the United States market.

Other products and technologies are currently in the research and development or pre-commercial stage. These new technologies include:

- CeaProve®, a diabetes test meal to identify Type 2 diabetes and pre-diabetes, used to determine dosage levels for diabetes oral therapy, and to monitor the condition of pre-diabetics. We are working towards a Canadian product listing to make CeaProve® available across Canada in 2007.
- A drug-delivery platform using our beta glucan technology to deliver compounds for uses ranging from wound care and therapy, to skin care treatments that reduce the signs of aging.
- An extension to the active ingredients product range offering, through new plant extract products.
- An extension to the existing veterinary products line, though new therapeutic products/formulations.

Our vision is to be a global leader in developing and commercializing products for the human and animal health markets through the use of proprietary technology and renewable resources. We act as innovator, advanced processor and formulator in the development of new products. We deliver our technology to the market through distribution partnerships. Our strategic focus is:

- Increasing sales and expanding markets for active ingredients;
- Developing and marketing additional high-value proprietary therapeutic products;
- Deploying CeaProve® and maximizing product utilization;
- Advancing new technology to a partnering position; and
- Completing a Bio-energy feasibility study.

As a knowledge-based enterprise, we will also expand and strengthen our patent portfolio and build the necessary manufacturing infrastructure to become a global biotechnology company.

Our business growth depends on our ability to access global markets through distribution partnerships. Our marketing strategy emphasizes providing technical support to our distributors and their customers to maximize the value of our technology and product utilization. Our vision and business strategy are supported by our commitment to the following core values:

- Adding value to all aspects of our business;
- Enhancing the health of humans and animals;
- Discovering, extracting, and commercializing new, natural ingredients;
- Producing the highest quality work possible in products, science, and business; and
- Developing personnel through guidance, opportunities, and encouragement.

To support these objectives, we believe we have the requisite resources (intellectual and human capital) and the competitive advantages (partnerships) to exploit our technology. To fund our operations, we rely upon revenues generated from the sale of active ingredients and veterinary therapeutic products, and the proceeds of public and private offerings of equity securities, debentures, and other income offerings.

RISKS AND UNCERTAINTIES

Biotechnology companies are subject to a number of risks and uncertainties inherent in the development of any new technology. General business risks include: uncertainty in product development and related clinical trials and validation studies; the regulatory environment, for example, delays or denial of approvals to market our products; the impact of technological change and competing technologies; the ability to protect and enforce our patent portfolio and intellectual property assets; the availability of capital to finance continued and new product development; and the ability to secure strategic partners for late stage development, marketing, and distribution of our products. To the extent possible, we pursue and implement strategies to reduce or mitigate the risks associated with our business.

As substantially all sales are export sales to two distributors, we are dependent on those distributors to maintain and expand the volume of product sales to existing and new customers.

We have exposure to risk arising from volatility in foreign exchange rates as substantially all sales of our products are denominated in United States currency, while our expenses are primarily denominated in Canadian dollars. We do not currently engage in hedging or use of derivatives to reduce foreign exchange risk.

Ceapro's long-term debt has fixed interest rates over the terms of the obligations. Our exposure to interest rate and inflation risks are expected to be negligible as economic forecasts project a stable outlook for both interest rates and inflation in the near future.

Ceapro's share price is subject to equity market price risk, which may result in significant speculation and volatility of trading due to the uncertainty inherent in our business and the biotechnology industry. There is a risk that future issuance of common shares may result in material dilution of share value, which may lead to further decline in share price. The expectations of securities analysts and major investors about our financial or scientific results, the timing of such results and future prospects, could also have a significant effect on the future trading price of Ceapro's shares.

A variety of factors will affect our future growth and operating results, including the strength and demand for our products, the extent of competition in our markets, the ability to recruit and retain qualified personnel, and our ability to raise capital.

Our financial statements are prepared within a framework of GAAP selected by management and approved by our Board of Directors. The assets, liabilities, revenues, and expenses reported in our financial statements depend to varying degrees on estimates made by management. An estimate is considered a critical accounting estimate if it requires management to make assumptions about matters that are highly uncertain; and if different estimates that could have been used would have a material impact. The significant areas requiring the use of management estimates relate to amortization of property and equipment, the assumptions used in determining stock-based compensation and the discount rate used in determining the employee future benefits obligation. These estimates are based on historical experience and reflect certain assumptions about the future that we believe to be both reasonable and conservative. Actual results could differ from those estimates. We continually evaluate the estimates and assumptions.

DISCLOSURE CONTROLS AND PROCEDURES

Disclosure controls and procedures have been designed to provide reasonable assurance that material information relating to the Company is accumulated and communicated to the Company's management as appropriate to allow timely decisions regarding required disclosure. The Company's Chief Executive Officer and Chief Financial Officer have concluded, based on their evaluation as at December 31, 2006, that the Company's disclosure controls and procedures are effective to provide reasonable assurance that material information related to the Company is made known to them by others within the Company. It should be noted that while the Company's Chief Executive Officer and Chief Financial Officer believe that the Company's disclosure controls and procedures provide a reasonable level of assurance that they are effective, they do not expect that the disclosure controls and procedures will prevent all errors or fraud. A control system, no matter how well conceived or operated, can only provide reasonable, not absolute, assurance that the objectives of the control system are met.

RESULTS OF OPERATIONS

YEARS ENDED DECEMBER 31, 2006, 2005, AND 2004

SELECTED ANNUAL INFORMATION

$000s except per share data	**2006**	2005	2004
Total revenues	**3,310**	2,763	2,420
Net Loss	**(272)**	(57)	(398)
EBITDA	**(79)**	156	(277)
Basic loss per common share	**(0.01)**	(0.00)	(0.01)
Diluted loss per common share	**(0.01)**	(0.00)	(0.01)
Total assets	**2,063**	2,419	1,718
Total liabilities	**1,759**	1,958	1,604

During 2006 there was a 35% increase in active ingredient sales leading to an overall increase of product sales of 23%.

In 2006, the net loss increased by $215,000. Revenues increased $547,000 and gross margin increased $336,000. This was offset by an increase in general and administration of $37,000, higher sales and marketing of $86,000, decreased CeaProve® R&D funding of $205,000, and decreased AVAC Ltd. research funding of $187,750.

EBITDA decreased in the period by $235,000, due to the above factors.

The strong Canadian dollar had an impact on the revenues of Ceapro over the year. Ceapro's revenues are substantially all denominated in United States currency, thus a strong Canadian dollar reduces the value of each sale. The average exchange rate on Ceapro's sales dropped 7% compared to 2005 and 6% compared to 2004. This had a material impact on Ceapro's gross sales.

REVENUE

$000s	**2006**	2005	Change
Product sales			
Active ingredients	**2,917**	2,153	35%
Veterinary therapeutic products	**393**	530	(26%)
	3,310	2,683	23%
Royalties, licenses, and product development fees	**–**	80	(100%)
Total revenues	**3,310**	2,763	20%

PRODUCT SALES

In 2006, active ingredient sales rose $764,000 or 35% as a result of an increase of sales of colloidal oat extract, increased sales of beta-glucan, and increased sales of oat oil offset by lower sales of oat powder. The increase in sales of active ingredients has also been part of Ceapro's continual sales efforts with both the large and mid-size personal care and cosmetic companies. Ceapro continually looks for new and innovative products to add to the current line.

Sales of veterinary therapeutic products were lower year over year due to differences in order timing. There were sales orders filled in Q4 of 2005 but sales orders received in Q4 of 2006 are not being shipped until Q1 of 2007.

ROYALTIES, LICENSES, AND PRODUCT DEVELOPMENT FEES

Royalties, licenses, and product development fees are revenue derived from the addition of new products to existing distribution agreements, activation of new distribution agreements, and scientific and technical services provided to customers for the creation and development of new products. No new royalties or product development fees were received in the current year. The $80,000 earned in 2005 was the final portion of the product development fees, received in 2004, upon delivery of product to the customer for testing.

EXPENSES

COST OF GOODS SOLD AND GROSS MARGINS

$000s	2006	2005	Change
Sales	**3,310**	2,683	
Cost of products sold	**1,414**	1,123	
Gross margin	**1,896**	1,560	22%
Gross margin %	**57%**	58%	

Cost of goods sold is comprised of the direct raw materials required for the specific formulation of products, as well as direct labour, quality control, packaging, and transportation costs. Aside from labour and quality control related expenses, the majority of costs are variable in relation to the volume of product produced or shipped.

For 2006, the gross margin percentage decreased slightly to 57% from 58%, primarily a result of a decrease in the value of the United States dollar, the effects of labor shortages, a greater reliance on overtime hours worked, and the effects of restrictions in the permitted operating hours of the plant. Factors decreasing margins were partly offset due to spreading fixed costs over higher product sales, efficiencies from new equipment installed in recent years, and a different product sales mix with higher sales of high margin products.

GENERAL AND ADMINISTRATION

$000s	2006	2005	Change
Salaries and benefits	**349**	314	
Board of Directors compensation	**97**	102	
Investor relations	**93**	102	
Insurance	**100**	100	
Legal	**33**	96	
Other	**348**	269	
Total general and administration expenses	**1,020**	983	4%

General and administration expense (G&A) for 2006 increased $37,000 primarily due to an increase in consulting fees of $44,000 related to corporate development and transactional advisory services, executive recruitment fees of $27,000, advertising for production employees of $10,000, and increased rent of $11,000 offset by legal fees which decreased $63,000.

SALES AND MARKETING

$000s	2006	2005	Change
Salaries and benefits	**216**	207	
Other	**126**	49	
Total sales and marketing	**342**	256	34%

Sales and marketing expenses increased by 34% largely due to the hiring of a full-time veterinary products marketing manager and a significant investment in creating the Ceapro Dermatology brand and developing marketing plans and materials for Ceapro Veterinary Products for the United States market. These initiatives are expected to impact 2007 sales.

ROYALTIES

$000s	2006	2005	Change
Royalty interest units	**350**	230	
AVAC Royalty	**5**	92	
Less: Recognition of deferred royalty revenue	**(38)**	–	
Total royalties expenses	**317**	322	(2%)

As at December 31, 2006, royalty investors receive royalties equal to 10.59% (2005 – 8.31%) of revenues from product sales and royalty, license, and product development fees of active ingredients, veterinary therapeutic products, and CeaProve® to a maximum of two times the amount invested. AVAC Ltd. receives royalties of up to 5% of revenues from eligible product sales, to a maximum of one and a half the amount invested and royalties of 2.5% of revenues of eligible product sales to a maximum of two times the amount invested. Royalty expense throughout 2007 will vary directly with fluctuations in product sales, royalty, license, and product development fees, product sales mix, and any new royalty interest offerings or AVAC investments that may be completed. During 2006 one of the AVAC royalties was fully earned and accrued. During 2006 the Company commenced the recognition of deferred royalty revenue for royalty interest units issued in 2005 at a rate of one half the amount of the royalty interest expense.

INTEREST

$000s	2006	2005	Change
Interest on callable debt, convertible debentures, and other	**1**	10	
Interest on long-term debt	**45**	41	
Total interest expense	**46**	51	(10%)

Interest expense decreased $5,000 due to lower debt from previous debt repayment.

AMORTIZATION

Amortization expense decreased by $15,000 or 9%, due to a lower net book value of assets.

RESEARCH AND PRODUCT DEVELOPMENT

$000s	2006	2005	Change
Salaries and benefits	**143**	134	
Product development – CeaProve®	**311**	395	
Other	**101**	129	
Research and product development expenditures	**555**	658	(16%)
AVAC investment (Product Innovation)	**–**	(100)	
AVAC investment (CeaProve®)	**(190)**	(395)	
Net research and product development expenses	**365**	163	124%

Net research and product development expenses increased 124% primarily due to a decrease in AVAC investments. In 2005 Ceapro recognized $395,000 of investment under a product pre-commercialization investment agreement that was offset against CeaProve® product development charges. In 2005, $100,000 of active ingredient and animal health product development expenses were offset against funds from AVAC under the Product Innovation Investment agreement.

OTHER INCOME

$000s	2006	2005	Change
AVAC – product innovation investment	**37**	225	
Foreign exchange gains and other	**33**	15	
Total other income	**70**	240	(71%)

Other income was lower in 2006, due to the receipt of $225,000 in 2005 in AVAC product innovation investment for costs that were incurred in 2004. Stronger United States dollar exchange rates versus Canadian dollars at year end resulted in recognized foreign currency gains in the amount of $33,000.

QUARTERLY INFORMATION

The following selected financial information is derived from Ceapro's unaudited quarterly financial statements for each of the last eight quarters, all of which cover periods of three months.

				2006				2005
$000s except per share data	**Q4**	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Total revenues	**704**	762	945	899	608	654	1,032	469
Net (loss) income	**(122)**	(96)	(3)	(51)	123	(125)	101	(156)
Basic (loss) income per share	**(0.00)**	(0.00)	(0.00)	(0.00)	0.00	(0.00)	0.00	(0.00)
Diluted (loss) income per share	**(0.00)**	(0.00)	(0.00)	(0.00)	(0.00)	(0.00)	(0.00)	(0.00)

Ceapro's quarterly sales and results fluctuate due to variations in the timing of product sales. For example, a significant proportion of our annual veterinary therapeutic product sales are in the second quarter of the year.

LIQUIDITY AND CAPITAL RESOURCES

The Company relies upon revenues generated from the sale of active ingredients and veterinary therapeutic products, the proceeds of public and private offerings of equity securities and debentures, and income offerings to support our operations.

During 2006, 429,335 stock options were exercised at prices ranging from $0.17 to $0.25. The amount credited to share capital upon exercise of the options is the cash consideration received, if applicable, plus the fair value of the options at the time they were granted (stock-based compensation).

Total common shares issued and outstanding as at March 19, 2007 were 37,505,505 (March 28, 2006 – 37,098,670). In addition, 3,082,460 stock options (March 28, 2006 – 3,286,795) and 774,066 warrants (March 28, 2006 –

774,066) were outstanding that are potentially convertible into an equal number of common shares at various prices. Shareholders' equity decreased to $303,799 at December 31, 2006 from $461,337 at December 31, 2005.

Ceapro's working capital position decreased to $640,000 at December 31, 2006, a decrease of $363,000 from December 31, 2005. Ceapro continues to pursue additional financing to fund ongoing working capital requirements, and to secure the financial resources required to support the expected increases in sales of existing products, the introduction of new products to existing and new markets, and the development of new technology.

To meet future requirements, we intend to raise additional cash through some or all of the following methods: public or private equity or debt financing, income offerings, capital leases, collaborative and licensing agreements, and joint venture or partnership financing. However, there is no assurance of obtaining additional financing through these arrangements on acceptable terms, if at all. The ability to generate new cash will depend on external factors, many beyond our control, as outlined in the Risks and Uncertainties section. Should sufficient capital not be raised, we may have to delay, reduce the scope of, eliminate, or divest one or more of our discovery, research, or development technology or programs, any of which could impair the value of the business.

SOURCES AND USES OF CASH

The following table outlines our sources and uses of funds during the past two years.

($000s)	**2006**	2005
Sources of funds:		
Funds generated from operations (cash flow)	**(41)**	238
Change in non-cash working capital items	**204**	(666)
Share capital issued, net of costs	**89**	356
Royalty interest proceeds	**–**	457
	252	385
Uses of funds:		
Purchase of property and equipment and deposits	**(245)**	(57)
Decrease in convertible debentures	**–**	(20)
Deferred royalty revenue	**(38)**	–
Change in long-term and callable debt	**(79)**	(70)
Royalties payable	**(17)**	104
	(379)	(43)
Net change in cash	**(127)**	342

FINANCING AND MILESTONES

On April 25, 2005, Ceapro received an investment commitment from AVAC Ltd. for product innovation development in the areas of Veterinary Therapeutics and Active Ingredients based on Alberta cereal by-products of an amount up to $362,250 upon completion of project objectives as outlined and agreed to by both parties. As at December 31, 2006, $362,500 (2005-$325,000) of this commitment has been received or was receivable. Ceapro will pay a 2.5% royalty on certain sales to a maximum of $75,000 per quarter to a maximum of two times the amount received from AVAC. These payments will commence when the royalty payments on other AVAC agreements (dated May 13, 2002, March 26, 2004, and March 14, 2006) are fully satisfied.

In the year ended December 31, 2005, the Company received a commitment for financial assistance totaling $800,000 for pre-market activities of CeaProve® (a health and wellness product) upon completion of project objectives as outlined and agreed to by both parties. As of December 31, 2006, $510,000 of this commitment was received. The Company is obligated to pay a royalty (to a maximum of one and a half times the financial assistance received) on sales generated from CeaProve® on the following basis: 0% of net sales and net Sub-licensing revenues earned until royalty payments have been fully satisfied under the Investment Agreement dated March 24, 2004, and 5% thereafter until repaid to a maximum of $125,000 per quarter. No royalties were incurred or payable during the current year.

During 2006, the Company received a commitment from Agriculture Financial Services Corporation to provide equipment financing for the expansion of the Company's manufacturing capacity. The commitment is for a $750,000 5 year term loan amortized over ten years at an interest rate of 8.25%. The Company expects to begin draw down on this facility in Q1 2007 with payments commencing after draw downs begin on the loan.

The Company has received conditional approval for an award of up to $300,000 from the Federal Government Biofuels Opportunities for Producers Initiative (BOPI) program. The non-repayable funding will support a feasibility study for the construction and operation of a biorefinery and processing plant.

RELATED PARTY TRANSACTIONS

During 2006, $118,098 (2005-$60,580) of royalties were earned by employees and Directors from their investment in previous Ceapro royalty offerings. Directors and employees invested $195,000 (2005- $190,250) in the sale of royalty interest units and lawsuit interests. At December 31, 2006, $25,107 (2005-$13,336) of royalties were payable to employees and Directors. Included in accounts receivable at December 31, 2006 is $150,000 (2005-$50,000) due from a Director for legal fees associated with the Saskatchewan litigation. Prepaid expenses included $44,066 (2005-$25,884) of Director fees paid for the term ending May 31, 2007. 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 related parties.

LEGAL PROCEEDINGS

The Company is the plaintiff in legal proceedings claiming that in 1998 the Saskatchewan Government Growth Fund ("SGGF") and others improperly gained control of Canamino Inc. ("Canamino") a wholly -owned subsidiary of the Company at that time. The claim alleges that Ceapro has suffered damages for its loss of investment in Canamino and loss of reputation in the capital markets. It is expected that this matter will go to trial commencing November 19, 2007.

Legal fees and other direct costs associated with the lawsuit have been, and continue to be, financed and funded by Lawsuit Contributors who have, and continue to, purchase direct interests in the proceeds (if any) from the lawsuit; and through agreements with the Company's legal counsel to accept a portion of their fees on a contingency basis. In addition, the Company was required to post a bond relating to legal costs up to $305,000 which was secured by guarantees of the Board of Directors and an Officer of the Company. Consequently, no costs associated with the lawsuit are included in the Company's financial statements.

As of March 19, 2007, it is the opinion of Ceapro's Corporate Counsel that, based on the document production to date and examinations of discovery that have transpired, the most likely outcome of this action is that Ceapro will be successful. Given the uncertainty of the outcome of the proceeding, the direct interests of the Lawsuit Contributors, and the contingency fee arrangement with the Company's legal counsel, no amount has been accrued in the financial statements with respect to this claim.

OUTLOOK

The initiatives undertaken during 2005 have resulted in an increase in product sales making 2006 our best revenue year in Ceapro's history and creating an operating profit before research expenses. We are encouraged with first quarter 2007 sales and look forward to growing revenues throughout 2007. The expansion of sales to existing customers, and the introduction of new products, and sales to new customers are expected to boost sales of active ingredients. Ceapro's export sales have continued to increase despite the significant strengthening of the Canadian dollar over the last few years and indications in early 2007 are that the Canadian dollar will weaken in 2007. This should have a positive impact on sales.

Ceapro has made strides in the development of CeaProve®, our diabetes screening product, identifying new applications in the areas of diabetes monitoring and drug dosage determination. The awareness of the potential of a diabetes epidemic is now very high and the time is right for this product. We anticipate the product will be available for sale in Q2 and the global market potential is huge.

During 2006 significant marketing investments were made in our veterinary product business including the development of our Ceapro Dermatology brand. Some pre-marketing activities have been completed in the United States and we expect to launch the brand in the United States in Q2.

Ceapro BioEnergy Inc. is our new subsidiary that will undertake a feasibility study to examine the feasibility of new biofuel alternatives. This activity is complementary to Ceapro's core strength and allows for the opportunity for Ceapro to integrate all of its extraction processes. The current market conditions are right for this activity.

Finally, we have received approval to begin our planned expansion into the Leduc incubator. This will allow us to produce more products for sale and operate more efficiently to meet our growing sales and new business opportunities. Agriculture Financial Services Corporation has committed to fund $750,000 of the equipment expansion.

We expect 2007 to be a very exciting year for Ceapro.

We intend to implement our operating plans in a measured and responsible manner. We caution that additional investments may be required to continue to grow the business and product lines and availability of these additional investments may affect the pace of growth.

ADDITIONAL INFORMATION

Additional information relating to Ceapro Inc., including a copy of our Annual Report and Proxy Circular, can be found on SEDAR at www.sedar.com.

FINANCIAL STATEMENTS

MANAGEMENT'S REPORT

To the Shareholders of Ceapro Inc.,

The accompanying consolidated financial statements of Ceapro Inc., and all information presented in this annual report, are the responsibility of Management and have been approved by the Board of Directors.

The consolidated financial statements have been prepared by Management in accordance with Canadian generally accepted accounting principles. The financial statements include some amounts that are based on the best estimates and judgments of Management. Financial information used elsewhere in the annual report is consistent with that in the financial statements.

To further the integrity and objectivity of data in the financial statements, Management of the Company has developed and maintains a system of internal controls, which Management believes will provide reasonable assurance that financial records are reliable and form a proper basis for preparation of financial statements, and that assets are properly accounted for and safeguarded.

The Board of Directors carries out its responsibility for the financial statements in the annual report principally through its Audit Committee. The Audit Committee is appointed by the Board, and all of its members are outside and unrelated Directors. The Committee meets periodically with Management and the external auditors to discuss internal controls over the financial reporting process and financial reporting issues, to make certain that each party is properly discharging its responsibilities, and to review quarterly reports, the annual report, the annual financial statements, management discussion and analysis, and the external auditors' report. The Committee reports its findings to the Board for consideration when approving the financial statements for issuance to the shareholders. The Company's auditors have full access to the Audit committee, with and without Management being present.

The financial statements have been audited by the Company's auditors, Stout & Company LLP, the external auditors, in accordance with auditing standards generally accepted in Canada on behalf of the shareholders.

Sincerely,

SIGNED "Mark J. Redmond, Ph. D."
President and Chief Executive Officer

SIGNED "Branko Jankovic, CA"
Chief Financial Officer

AUDITORS' REPORT

To the Shareholders of Ceapro Inc.,

We have audited the consolidated balance sheets of Ceapro Inc. as at December 31, 2006 and 2005, and the consolidated statements of net loss and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2006 and 2005, and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Edmonton, Canada
February 20, 2007

SIGNED "Stout & Company LLP"
Chartered Accountants

CONSOLIDATED BALANCE SHEETS

As at December 31	2006 $	2005 $
ASSETS		
Current Assets		
Cash and cash equivalents	**310,926**	438,045
Accounts receivable	**634,256**	982,347
Inventories	**160,456**	228,158
Prepaid expenses and deposits	**178,751**	90,761
	1,284,389	1,739,311
Deposits on property and equipment	**167,828**	–
Property and equipment (note 3)	**610,629**	679,623
	2,062,846	2,418,934
LIABILITIES		
Current Liabilities		
Accounts payable and accrued liabilities	**335,616**	284,863
Current portion deferred revenue	**105,000**	229,676
Callable debt (note 4)	**36,313**	81,584
Current portion of long-term debt (note 5)	**36,609**	33,519
Currrent portion of royalties payable (note 6)	**130,456**	106,508
	643,994	736,150
Derferred royalty revenue	**369,764**	457,000
Employee future benefits obligation (note 7)	**219,340**	159,946
Long-term debt (note 5)	**400,122**	436,731
Royalties payable (note 6)	**125,827**	167,770
	1,759,047	1,957,597
SHAREHOLDERS' EQUITY		
Share capital (note 8(b))	**2,508,059**	2,414,830
Contributed surplus (note 8(c))	**128,478**	106,888
Deficit	**(2,332,738)**	(2,060,381)
	303,799	461,337
	2,062,846	2,418,934

See accompanying notes

Approved on Behalf of the Board

SIGNED "Edward A. Taylor"
Director

SIGNED "David B. Harvey"
Director

CONSOLIDATED STATEMENTS OF NET LOSS AND DEFICIT

Years ended December 31

REVENUE	2006 $	2005 $
Sales (note 10)	**3,310,323**	2,683,433
Cost of goods sold	**1,413,976**	1,123,606
Gross margin	**1,896,347**	1,559,827
Royalties, licenses, and product development fees	**–**	80,000
	1,896,347	1,639,827
EXPENSES		
General and administration	**1,020,296**	982,887
Royalties	**317,355**	321,692
Sales and marketing	**342,207**	255,773
Amortization	**146,779**	161,550
Interest on long-term debt	**45,133**	41,310
Interest on callable debt, convertible debentures and other	**1,220**	10,386
	1,872,990	1,773,598
Income (loss) from operations	**23,357**	(133,771)
OTHER INCOME (EXPENSES)		
Research and product development	**(365,424)**	(162,833)
Other income (note 11)	**69,710**	239,597
	(295,714)	76,764
Loss before income taxes	**(272,357)**	(57,007)
Income taxes (note 12)		
Current	**164,792**	435,143
Reduction as a result of applying non-capital losses carried forward against the current year's taxable income	**(164,792)**	(435,143)
NET LOSS FOR THE YEAR	**(272,357)**	(57,007)
Deficit, beginning of year	**(2,060,381)**	(2,003,374)
DEFICIT, END OF YEAR	**(2,332,738)**	(2,060,381)
Net loss per common share:		
Basic	**(0.01)**	(0.00)
Diluted	**(0.01)**	(0.00)
Weighted average number of common shares outstanding	**37,188,901**	36,337,657

See accompanying notes

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended December 31

	2006 $	2005 $
OPERATING ACTIVITIES		
Net loss for the year	**(272,357)**	(57,007)
Items not affecting cash and cash equivalents		
Amortization	**146,779**	161,550
Employee future benefits obligation	**59,394**	83,360
Stock based compensation	**25,592**	50,007
	(40,592)	237,910
CHANGES IN NON-CASH WORKING CAPITAL ITEMS		
Accounts receivable	**348,091**	(557,187)
Inventories	**67,702**	117,266
Prepaid expenses and deposits	**(87,990)**	(24,288)
Accounts payable and accrued liabilities	**50,753**	(351,752)
Deferred revenue	**(174,092)**	149,676
	204,464	(666,285)
	163,872	(428,375)
INVESTING ACTIVITIES		
Purchase of property and equipment	**(77,785)**	(121,206)
Deposits on property and equipment	**(167,828)**	–
Restricted cash for the purchase of property and equipment	**–**	64,430
	(245,613)	(56,676)
FINANCING ACTIVITIES		
Repayment of long-term debt	**(33,519)**	(29,750)
Repayment of callable debt	**(45,271)**	(40,712)
Repayment of convertible debentures	**–**	(20,000)
Proceeds from issuance of share capital	**–**	238,817
Proceeds from exercise of stock options	**89,227**	117,944
Deferred royalty revenue	**(37,820)**	–
Proceeds from royalty interest unit offering	**–**	457,000
(Decrease) increase in royalties payable	**(17,995)**	103,531
	(45,378)	826,830
Decrease (increase) in cash and cash equivalents	**(127,119)**	341,779
Cash and cash equivalents at beginning of year	**438,045**	96,266
CASH AND CASH EQUIVALENTS AT END OF YEAR	**310,926**	438,045
Supplementary information		
Interest paid	**46,353**	51,906
Royalties paid	**373,170**	218,161
Cash and cash equivalents consist of:		
Cash on deposit with banks	**165,251**	438,045
US$ term deposit	**145,675**	–
	310,926	438,045

See accompanying notes

1. NATURE OF BUSINESS OPERATIONS

Ceapro Inc. (the "Company") is incorporated under the Canada Business Corporations Act and is listed on the TSX Venture Exchange. The Company's primary business activities relate to the marketing and development of various health and wellness products and technology relating to plant extracts.

2. ACCOUNTING POLICIES

a) Use of estimates

The preparation of consolidated financial statements is in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of the assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. The significant areas requiring the use of management estimates relates to amortization of property and equipment, the assumptions used in determining stock based compensation, and the interest rate used in determining the value of employee future benefits obligation. Actual results could differ from those estimates.

b) Principles of consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Ceapro Technology Inc., Ceapro Veterinary Products Inc., Ceapro Active Ingredients Inc., and Ceapro BioEnergy Inc.

c) Cash and cash equivalents

Cash and cash equivalents are defined as amounts on deposit with banks and short term deposits with maturities of three months or less.

d) Revenue recognition

Revenue from the sale of health and wellness products is recognized as revenue at the time the products are shipped to customers.

The sale of royalty interests are recorded as deferred royalty revenue and are matched to future royalty expenses.

Royalty, licenses, and product development fees are recorded in accordance with the terms of the applicable agreements.

e) Inventories

Inventory of raw materials is valued at the lower of cost and replacement cost on a first-in, first-out basis.

Inventory of work-in-process and finished goods is valued at the lower of cost and net realizable value on an average cost basis.

f) Property and equipment

Property and equipment are recorded at cost and are amortized over their estimated useful lives as follows:

Manufacturing equipment	20% declining balance
Office equipment	20% declining balance
Computer equipment	30% declining balance

g) Research and product development expenditures

Research costs are expensed when incurred. Product development costs are also expensed when incurred unless they are significant and meet generally accepted criteria for deferral. Costs are reduced by government grants and investment tax credits where applicable.

h) Foreign currency

Monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at year end exchange rates and non-monetary assets at the exchange rates prevailing when the assets were acquired. Foreign currency denominated revenue and expense items are translated at the rate of exchange in effect at the time of the transaction. Foreign currency gains or losses arising on translation are included in income.

i) Income taxes

The liability method is used for determining income taxes. Under this method, future income tax assets and liabilities are recognized for the estimated tax recoverable or payable that would arise if assets and liabilities were recovered or settled at the financial statement carrying amounts. Future tax assets and liabilities are measured using substantively enacted tax rates expected to apply to taxable income in the year in which temporary differences are expected to be recovered or settled. Changes to these balances, including changes due to changes in income tax rates, are recognized in income in the period in which they occur. The amount of the future income tax assets recognized is limited to the amount that is more likely than not to be realized.

j) Lease Obligations

Leases are classified as capital or operating leases. A lease that transfers substantially all of the benefits and risks incidental to the ownership of property is classified as a capital lease. At the inception of a capital lease, an asset

and an obligation are recorded at an amount equal to the lesser of the present value of the minimum lease payments and the property's fair value at the beginning of the lease. All other leases are accounted for as operating leases wherein payments are expense as incurred.

k) Government assistance

Government assistance is periodically granted to the Company under available government incentive programs. Government assistance relating to research and development expenditures is recorded as a reduction of the expenditures when received.

l) Investment tax credits

Investment tax credits relating to qualifying scientific research and experimental development expenditures are accrued provided there is a reasonable assurance that the credits will be realized. When recorded, the investment tax credits are accounted for as a reduction of the related expenditures.

m) Net loss per common share

Net loss per common share is calculated based on the weighted average number of common shares outstanding during the year. Diluted net loss per common share reflects the assumed conversion of all dilutive securities using the treasury stock method. When the Company is in a net loss position, stock options and warrants are anti-dilutive.

n) Stock based compensation

Stock based compensation of employees, directors, officers, and consultants is recorded in accordance with the fair value method.

o) Employee future benefits

The Company accrues its obligations under an employee defined retirement benefit plan and related costs, net of plan assets. The cost of retirement benefits earned by employees is determined using the accumulated benefit method and management's best estimate of expected plan investment performance and retirement ages of employees. Past service costs relating to plan amendments are accrued and recognized in the year the amendments occur.

p) Impairment of long-lived assets

In the event that facts and circumstances indicate that the carrying value of the long-lived assets may be impaired, the Company performs a recoverability evaluation. If the evaluation indicates that the carrying value is not recoverable from undiscounted cash flows attributable to the assets, then an impairment loss is measured by comparing the carrying amount of the asset to its fair value.

3. PROPERTY AND EQUIPMENT

	2006		
	Cost $	**Accumulated Amortization $**	**Net Book Value $**
Manufacturing equipment	**964,280**	**431,389**	**532,891**
Computer and office equipment	**186,650**	**108,912**	**77,738**
	1,150,930	**540,301**	**610,629**

	2005		
	Cost $	Accumulated Amortization $	Net Book Value $
Manufacturing equipment	908,142	308,434	599,708
Computer and office equipment	165,004	85,089	79,915
	1,073,146	393,523	679,623

4. CALLABLE DEBT

	2006 $	2005 $
Loan, payable at $4,166 per month, principal and interest at 8%, secured by specific manufacturing equipment carrying value of $153,502 (2005 -$191,877) and a general security agreement, due November, 2007.	**36,313**	81,584

5. LONG-TERM DEBT

	2006 $	2005 $
Loan, payable at $6,161 per month, principal and interest at 8.85%, secured by a general security agreement, due January, 2010.	**436,731**	470,250
Less current portion	**36,609**	33,519
	400,122	436,731

Estimated principal payments due in the next four years are as follows:

	$
2007	36,609
2008	39,983
2009	43,669
2010	316,470
	436,731

Subsequent to the year-end the Company has been approved for a $750,000 term loan with Agricultural Financial Services Corporation to purchase equipment and services related to the Company's plant expansion. The loan is for a five-year term, amortized over ten years with an interest rate of 8.25%.

6. ROYALTIES PAYABLE

	2006 $	2005 $
Royalties payable pursuant to financial assistance received (note 6 (a))	**181,751**	223,694
Royalties payable pursuant to royalty interest offering (note 6 (c), (d), and (e))	**74,532**	50,584
	256,283	274,278
Less current portion	**130,456**	106,508
	125,827	167,770

a) In the year ended December 31, 1999, the Company received financial assistance in the amount of $164,882 for the research and development of new products, patents, and markets. The Company is obligated to pay a 5% royalty (to a maximum of two times the financial assistance received) on sales generated from products developed using these funds. The portion of this obligation paid or accrued as at December 31, 2006 was $329,764 (2005 - $325,166). Pursuant to an agreement signed in March 2006, the terms of repayment were amended to allow all royalties payable as at December 31, 2005 in the amount of $223,692 to be repaid $13,981 per quarter commencing March 31, 2006. Royalties incurred subsequent to December 31, 2005 are to be repaid quarterly within 60 days of the quarter end.

b) In the year ended December 31, 2004, the Company received a commitment for financial assistance totaling $250,000 for pre-market activities of CeaProve® (a health and wellness product) upon completion of project objectives as outlined and agreed to by both parties. In the year ended December 31, 2006, $225,000 (2005

- $225,000) of this commitment has been received. The Company is obligated to pay a royalty (to a maximum of two times the financial assistance received) on sales generated from CeaProve® on the following basis: 0% of revenues earned to December 31, 2005, 2.5% of revenues earned to December 31, 2006, and 5% thereafter until repaid. No royalties have been incurred during the current or prior years. The Company has repaid at December 31, 2006 $nil (2005 - $nil) of this obligation. Upon completion of the repayment of the financial assistance received, the Company will be required to repay $19,750 advanced during the year ended December 31, 2002. The portion of this obligation paid or accrued as at December 31, 2006 was $nil (2005 - $nil).

c) In the year ended December 31, 2003, the Company completed a Royalty Income Unit offering through the terms described in an Offering Memorandum. Each royalty interest has a right to receive royalties equal to 0.00001% from the sale or licensing of the Company's active ingredients and animal health products, to a maximum cumulative amount of $2.08 per unit. Proceeds from the offering of $516,348 (before related expenses) represent the sale of a 5.163% royalty interest in the Company's future sales and licensing of active ingredients and animal health products. Maximum royalties payable are two times the amount invested or $1,032,695. The portion of this obligation paid or accrued at December 31, 2006 was $490,055 (2005 - $319,127).

d) In the year ended December 31, 2003, the Company sold a 1.418% royalty interest in the Company's future sales and licensing of active ingredients and animal health products for $141,796. In the year ended December 31, 2004, the Company sold an additional 1.724% royalty interest in the future sales and licensing of active ingredients and animal health products for $172,401. The cumulative royalty interest of 3.142% for $314,197 results in combined maximum royalties of two times the amount invested or $628,394. The portion of this obligation paid or accrued at December 31, 2006 was $343,926 (2005 - $239,917).

e) On December 28, 2005 the Company sold a 2.285% royalty interest in the Company's future sales and licensing of active ingredients, animal health, and CeaProve® products for $457,000. Maximum royalties payable are two times the amount invested or $914,000. The portion of this obligation paid or accrued as at December 31, 2006 was $75,640 (2005 - $nil).

f) In the year ended December 31,2005 , the Company received a commitment for financial assistance totaling $362,250 for product innovation development in the area of Veterinary Therapeutics and Active Ingredients. In the year ended December 31, 2006 $325,000 (2005 - $225,000) of the commitment has been received and $37,250 was receivable at December 31, 2006 (2005 - $100,000). The Company is obligated to pay a 2.5% royalty to a maximum of $75,000 per quarter (to a maximum of two times the financial assistance received or $724,500) on sales generated from products developed using these funds. These payments will commence when the royalty payments on investment agreements in note 6(a) are fully satisfied. The portion of the obligation paid or accrued at December 31, 2006 was $nil (2005 - $nil).

g) In the year ended December 31, 2005, the Company received a commitment for financial assistance totaling $800,000 for pre-market activities of CeaProve® (a health and wellness product) upon completion of project objectives as outlined and agreed to by both parties. As of December 31, 2006 $510,000 of this commitment was received (2005 - $510,000 of commitment was receivable). The Company is obligated to pay a royalty (to a maximum of one and a half times the financial assistance received or $1,200,000) on sales of CeaProve® on the following basis: 0% of net

sales and net sub-licensing revenues earned until royalty payments have been fully satisfied under the investment agreement in note 6(b), and 5% thereafter until repaid to a maximum of $125,000 per quarter. No royalties have been incurred during the current year. The portion of this obligation paid or accrued as at December 31,2006 was nil (2005 - $nil).

7. EMPLOYEE FUTURE BENEFITS OBLIGATION

The Company has an unfunded non-reigstered, non-indexed defined retirement benefit plan for certain senior employees. The retirement benefit is two months' salary for each year they are employed by the Company.

During the year ended December 31, 2005, the plan was amended to clarify the obligation and the date to which the obligations accrue. As a result, past service obligations of $53,453 were recorded in the prior year.

	2006 $	2005 $
Unfunded balance, beginning of year	**159,946**	76,586
Current service cost	**35,117**	22,152
Past service costs	**–**	53,453
Interest costs on accrued obligation	**24,277**	7,755
Unfunded balance, end of year	**219,340**	159,946

Management is required to make a significant estimate regarding the discount rate used to determine the accrued employee future benefit obligation. These significant estimates are of a long-term nature, which is consistent with the nature of the employee future benefits. The discount rate used to determine the accrued benefit obligation as at December 31, 2006 was 4.65% (2005 - 5.58%).

8. SHARE CAPITAL

a) Authorized

Unlimited number of Class A voting common shares
Unlimited number of Class B non-voting common shares

b) Issued - Class A common shares

	2006 $		2005 $	
	Number of Shares	**Amount**	Number of Shares	Amount
Balance at beginning of year	**37,076,170**	**2,414,830**	35,635,284	1,995,443
Changes during the year:				
Equity placements	**–**	**–**	774,066	238,818
Exercise of options	**429,335**	**93,229**	666,820	183,059
Decrease in equity component of convertible debentures	**–**	**–**	–	(2,490)
	37,505,505	**2,508,059**	37,076,170	2,414,830

c) Contributed surplus

The following table summarizes the changes in contributed surplus:

	2006 $	2005 $
Balance at beginning of year	**106,888**	121,997
Stock based compensation expense (note 8 (d))	**25,592**	50,007
Exercise of stock options	**(4,002)**	(65,116)
	128,478	106,888

d) Stock Options

The Company has granted stock options to eligible employees, directors, officers, and consultants under stock option plans that vest over periods ranging from eighteen months to four years and have a maximum term of five years.

The Company accounts for options granted under these plans in accordance with the fair value based method of accounting for stock based compensation. In the current year the Company granted 525,000 (2005 - 400,000) stock options. The application of the fair value based method requires the use of certain assumptions regarding the risk-free market interest rate, expected volatility of the underlying stock and life of the options. The weighted average risk-free rate used in 2006 was 4.23% (2005 - 3.40%), the weighted average expected volatility was 90% (2005 - 110%) which was based on prior trading activity of the Company's shares, and the weighted average expected life of the options was 5 years. The stock based compensation expense recorded during the current year relating to options granted in 2006 and 2005 was $24,850 (2005 - $47,903).

In addition, the Company recorded stock based compensation expense of $742 (2005 - $2,104) relating to options granted in 2003.

A summary of the status of the Company's stock options at December 31, 2006 and 2005 and changes during the years ended on those dates is as follows:

	2006 $		2005 $	
	Number of Options	**Weighted Average Exercise Price**	Number of Options	Weighted Average Exercise Price
Outstanding at beginning of year	**3,286,795**	**0.23**	3,586,115	0.21
Granted	**525,000**	**0.29**	400,000	0.28
Expired	**(300,000)**	**0.28**	(32,500)	0.25
Exercised	**(429,335)**	**0.21**	(666,820)	0.18
Outstanding at end of year	**3,082,460**	**0.24**	3,286,795	0.23
Exercisable at end of year	**2,757,460**	**0.23**	3,081,785	0.19

The following table summarizes information about the Company's stock options outstanding:

		2006	2005
Exercise Price $	Year of Expiration	**Number of Options**	Number of Options
0.30	2011	**225,000**	–
0.27	2011	**150,000**	–
0.28	2010	**175,000**	250,000
0.25	2008	**1,742,292**	1,895,792
0.17	2007	**790,168**	809,003
0.20	2006	**–**	332,000
		3,082,460	3,286,795

e) Warrants

A summary of the status of the Company's warrants at December 31, 2006 and 2005 and changes during the years ended on those dates is as follows:

	2006 $		2005 $	
	Number of Warrants	**Average Exercise Price**	Number of Warrants	Average Exercise Price
Outstanding at beginning of year	**774,066**	**0.59**	–	–
Issued	**–**	**–**	774,066	0.59
Outstanding at end of year	**774,066**	**0.59**	774,066	0.59

The following table summarizes information about the Company's warrants outstanding:

Exercise Prices $	**Expiration Date**	**2006 Number Outstanding**
0.60	March 31, 2007*	682,666
0.75	December 28, 2007	91,400
		774,066

Exercise Prices $	**Expiration Date**	**2005 Number Outstanding**
0.60	September 30, 2006	682,666
0.55	December 28, 2007	91,400
		774,066

*The expiry date on these warrants was extended from September 30, 2006 to March 31, 2007.

f) On March 31, 2005 the Company completed a private placement share offering of 682,666 Units, for aggregate gross proceeds of $204,800. Each Unit was priced at $0.30 and contained one common share of the Company and one common share purchase warrant entitling the holder thereof to acquire one additional common share at an exercise price of $0.40 per share until September 30, 2005 and thereafter at a price of $0.60 per common share until September 30, 2006. The expiry date on these warrants was extended from September 30, 2006 to March 31, 2007.

g) On December 28, 2005 the Company completed a Royalty Income Unit offering through the terms described in an Offering Memorandum, which resulted in proceeds of $ 502,700 (914 units at $550 per unit, net of related expense). Each unit is comprised of 100 Class A common shares of the Company ("common shares"), 100 Class A common share purchase warrants ("warrants"), and 100 royalty interests ("royalty interests"). Each warrant entitles the holder thereof to acquire one Class A common share at an exercise price of $0.55 per share until June 28, 2006 and thereafter at a price of $0.75 per share until December 28, 2007. Each royalty interest is a right to receive royalties equal to .000025% of the proceeds received by the Company from the sale or licensing of its active ingredients, animal health products, and CeaProve®, up to a maximum cumulative amount of amount of $10.00 per unit. Proceeds of $457,000 related to royalty interest units and $45,700 for common shares.

9. CONTINGENCIES AND COMMITMENTS

a) The Company is the plaintiff in legal proceedings claiming that in 1998 the Saskatchewan Government Growth Fund ("SGGF") and others improperly gained control of Canamino Inc. ("Canamino"), a wholly-owned subsidiary of the Company at that time. The claim alleges that Ceapro has suffered damages for its loss of investment in Canamino and loss of reputation in the capital markets. It is expected that this matter will go to trial in the fall of 2007.

Legal fees and other direct costs associated with the lawsuit have been, and continue to be, financed and funded by Lawsuit Contributors who have purchased, and continue to purchase, direct interests in the proceeds (if any) from the lawsuit; and through agreements with the Company's legal counsel to accept a portion of their fees on a contingency basis. In addition, the Company was required to post a bond relating to legal costs up to $305,000 which was secured by guarantees of the Board of Directors and an Officer of the Company. Consequently, no costs associated with the lawsuit are included in the Company's consolidated financial statements.

As of March 19, 2007, it is the opinion of Ceapro's Corporate Counsel that, based on the document production to date and examinations of discovery that have transpired, the most likely outcome of this action is that Ceapro will be successful. Given the uncertainty of the outcome of the proceeding, the direct interests of the Lawsuit Contributors, and the contingency fee arrangement with the Company's legal counsel, no amount has been accrued in the consolidated financial statements with respect to this claim.

b) In the normal course of operations the Company may be subject to litigation and claims from customers, suppliers and former employees. Management believes that adequate provisions have been recorded in the accounts where required. Although it is not possible to estimate the extent of potential costs, if any, management believes that the ultimate resolution of such contingencies would not have a material adverse effect on the financial position of the Company.

10. SALES

Substantially all sales are export sales to two distributors of the Company's products. The Company is therefore economically dependent on those distributors to maintain and expand the volume of product sales to existing and new customers.

11. OTHER INCOME

Other income is comprised of:

	2006 $	2005 $
Product Innovation Investment (note 6(f))	**37,250**	225,000
Foreign exchange gains	**32,828**	3,920
Other	**(368)**	10,677
	69,710	239,597

12. INCOME TAXES

a) Non-capital losses

The Company has accumulated non-capital losses carried forward for income tax purposes of approximately $2,198,300, the benefit of which has not been reflected in these consolidated financial statements. These losses may be applied against future taxable income within the limitations prescribed by the Income Tax Act and expire as follows:

	$
2007	682,600
2008	570,800
2015	293,400
2026	651,500
	2,198,300

b) Capital losses

The Company has accumulated capital losses of approximately $6,807,000, which can be carried forward indefinitely to offset future capital gains.

c) Scientific research and experimental development (SR&ED)

The Company has accumulated an SR&ED expenditure pool of approximately $1,506,000, which can be carried forward indefinitely to be applied against future taxable income.

The Company has accumulated SR&ED investment tax credits of approximately $156,000. These credits may be applied against future federal income taxes payable and expire as follows:

	$
2007	119,000
2008	16,000
2009	400
2012	20,600
	156,000

d) Temporary differences

A future income tax asset reflects the net effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's future income tax asset is as follows:

Income tax effect of deductible temporary differences:	**2006 $**	2005 $
Non-capital losses and SR&ED expenditures carried forward	**1,190,000**	1,423,000
Net capital losses carried forward	**1,093,000**	1,144,000
SR&ED investment tax credits	**156,000**	194,000
Undepreciated capital cost for tax purposes in excess of net book value	**3,069,000**	3,123,000
Deferred revenue recognized for tax purposes	**152,000**	231,000
Valuation allowance	**(5,660,000)**	(6,115,000)
	–	–

For consolidated financial statement purposes, no future income tax asset has been recorded at December 31, 2006 and 2005 as it is more likely not to be realized.

e) Income tax reconciliation

The Company's consolidated income tax position comprises tax benefits and provisions arising from the respective tax positions of its taxable entities. The Company's income tax provision differs from that calculated by applying statutory rates for the following reasons:

	2006 $	2005 $
Income taxes (recovery) based on federal and provincial statutory income tax rate of 32.50% (2005 - 33.62%)	**(88,516)**	(19,166)
Tax effect of expenses that are not deductible	**110,445**	124,787
Tax effect of current year non-capital losses not recognized	**211,734**	98,662
Tax effect of deferred revenue recognized	**(68,871)**	230,860
Income tax reduction as a result of applying non-capital losses carried forward against current year taxable income	**(164,792)**	(435,143)
	–	–

13. RELATED PARTY TRANSACTIONS

Related party transactions during the years not otherwise disclosed in these consolidated financial statements are as follows:

	2006 $	2005 $
Royalties earned by employees and directors	**118,098**	60,580
Sale of royalty and lawsuit interests to employees and directors	**195,000**	190,250
Amounts payable to employees and directors included in royalties payable	**25,107**	13,336
Amounts receivable from directors included in accounts receivable	**150,000**	50,000
Prepaid expense related to director fees	**44,066**	25,884

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 related parties.

14. SEGMENTED INFORMATION

The Company operates in one industry segment, which is the active ingredient product technology industry. The majority of the revenue is derived from sales in North America. All the assets of the Company, which support the revenues of the Company, are also located in North America. The distribution of revenue by location of customer is as follows:

	2006 $	2005 $
North America	**2,273,867**	1,827,692
Other	**1,036,456**	935,741
	3,310,323	2,763,433

15. FINANCIAL INSTRUMENTS

The estimated fair value of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, callable debt, and current portions of long-term debt and royalties payable are estimated to approximate their carrying value due to their short-term nature.

The fair value of long-term debt, royalties payable, and employee future benefits obligation are estimated to approximate their carrying value using the Company's incremental borrowing rate or discounted cash flow analysis for similar types of borrowing arrangements.

The Company operates internationally, giving rise to exposure to market risks from changes in foreign exchange rates in relation to the resulting accounts receivable and accounts payable and accrued liabilities.

It is management's opinion that the Company is not exposed to significant interest or credit risks from these financial instruments.

16. SUBSEQUENT EVENTS

a) On January 17, 2007, the Company entered into an agreement for advisory services relating to financial communications and investor relations. The initial term of the agreement is for six months and can be extended for further terms. Under the terms of the agreement, the Company has agreed to pay a monthly retainer fee of $5,000 and has granted 100,000 common share options at an exercise price of $0.30 per common share. Vesting of the options occurs upon the Company achieving certain performance and investment milestones. All options vested are exercisable for a period of five (5) years.

b) On February 14, 2007, the Company received conditional approval for an award of up to $300,000 from the Federal Government Biofuels Opportunities for Producers Initiative (BOPI) program. The non-repayable funding will support a feasibility study for the construction and operation of a biorefinery and processing plant.

INVESTOR INFORMATION

DIRECTORS
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Donald Byers
David Harvey
Donald Oborowsky
John Yewchuk
John Zupancic
Mark J. Redmond

OFFICERS
Mark J. Redmond, Ph. D.
President and Chief Executive Officer

Branko Jankovic, CA
Chief Financial Officer

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STOCK INFORMATION
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CHANGE OF ADDRESS

Registered Shareholders should notify the Company's Transfer Agent and Registrar at the address set out above.

Beneficial Owners should contact their respective brokerage firm to give notice of a change of address.

FINANCIAL CALENDAR

The Company's year-end is December 31.

The Annual Report is mailed in May.
Quarterly Reports are mailed in May, August, and November.

INVESTOR RELATIONS

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EQUAL OPPORTUNITY EMPLOYER

Ceapro Inc. is an equal opportunity employer and seeks to attract and retain the best-qualified people regardless of race, religion, national origin, gender, sexual orientation, age, or disability.

Designed by Optamedia Inc.

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