



# Strategies for the long term

CLEARWATER SEAFOODS INCOME FUND



2006 Second Quarter Report

# Letter to Unit Holders

HALIFAX, August 11/CNW/ - (TSX:CLR.UN):

- Distributions are reinstated at \$0.05 per unit per month (\$0.60 per unit annualized) retroactive to July 2006.
- Year-to-date cash available for distribution was \$24.8 million versus \$7.5 million in 2005.
- Gross profit margins improved \$14 million Year-to-date compared to 2005 as a result of fewer vessel disruptions, higher volumes and stronger margins, particularly in the scallop business as well as significant cash foreign exchange income.
- Improved leverage from 3.5 times earnings before interest, tax, depreciation and amortization (EBITDA) as of December 31, 2005 to 2.6 times EBITDA as of end of the second quarter 2006.

During the second quarter of 2006 Clearwater's sales and net earnings were \$81.3 million and \$11.5 million respectively versus sales of \$69.7 million and net earnings of \$1.4 million in 2005.

Gross profit for the second quarter of 2006 was \$23.3 million, an improvement of \$8.7 million over 2005. The most significant factor contributing to the improvement in gross profit for the quarter was the sales mix, with the second quarter of 2006 continuing to reflect the impact of a stronger contribution from the scallop business due to higher volumes, strong market prices and fewer vessel disruptions.

As a result distributable cash increased in the second quarter to \$16.5 million versus \$0.6 million in the second quarter 2005.

The Trustees have decided to reinstate distributions to unit holders on record as of August 31, 2006 at a rate of \$0.05 per unit per month, \$0.60 per unit when annualized when annualized retroactive to July 2006 (for total distributions when annualized of approximately \$31.7 million). In making this decision they have considered the current financial results which have improved over the same period in 2005, on-going capital expenditure requirements and cash on hand, which has been reserved

to complete funding of the vessel under construction, leverage and expectations regarding future earnings. Future earnings can be impacted by a number of factors including but not limited to, total allowable catch levels, selling prices, weather, exchange rates and fuel costs.

- Current financial results - Earnings have improved in 2006 with the rolling four quarters EBITDA and distributable cash as of the second quarter 2006 reaching \$72 million and \$44 million respectively as compared to \$56 million and \$27 million realized in calendar 2005.
- Capital expenditures - Clearwater currently has two significant capital projects – the clam vessel it expects to complete in 2006 and an Argentine vessel it plans to construct for 2008. Clearwater has retained cash over the past quarters to reduce leverage and has sufficient cash to fully fund the new clam vessel. It intends to use the excess cash on its balance sheet going forward to complete the construction of the clam vessel. It plans to fund construction of the Argentine vessel through reserves from distributable cash prior to delivery, which will fully fund construction of that vessel and with the delivery of that vessel, will result in a fleet of freezer processor vessels that has an average age of approximately 8 years with long remaining life spans.
- Leverage - Leverage has been decreasing over the past few quarters and now stands at 2.6 times EBITDA as compared to 3.5 times at December 31, 2005. Clearwater's intention is to continue to reduce debt levels in a measured manner over time.
- Expectations regarding future earnings – Clearwater expects that despite the ongoing challenge of foreign

exchange, leverage and the short-term negative impact of making continued improvements in the clam business, a positive outlook for the business and fewer vessel disruptions should provide the potential for continued improvements.

A number of challenges that were faced in 2005 continued into 2006 including foreign exchange and high fuel costs and are expected to be on going. We also continue to reorganize the clam business, with the plant closure in North Sydney in the second quarter. Other challenges experienced in the prior year that have not impacted 2006 and are not expected to recur relate to delays with two new scallop vessels, additional refit costs in the clam and scallop businesses and the impact of the repositioning of the sales channels in China. The business has operated closer to normal in the first half of 2006, which is evident in the results. The core business is healthy and with the strength of our quota ownership and our significant investment in developing effective and efficient harvesting and production processes the long-term outlook for the business is positive. Our strategy continues to have a long-term focus, developing and maintaining the strong foundations Clearwater was built upon.

Despite the ongoing challenge of foreign exchange, leverage and continued improvements in our clam business, a positive outlook for the scallop business and fewer vessel disruptions should provide the potential for continuous improvements in 2006 compared to 2005.

For an analysis of Clearwater and Clearwater Seafoods Income Fund's (the "Fund") results for the quarter, please see the discussion and analysis included with this report.

## FINANCIAL HIGHLIGHTS

<b>CLEARWATER</b>				
	13 weeks ended	13 weeks ended	26 weeks ended	26 weeks ended
(\$000's except per unit amounts)	July 1, 2006	July 2, 2005	July 1, 2006	July 2, 2005
Sales	\$ 81,312	\$ 69,712	\$ 151,661	\$ 137,071
Net earnings	\$ 11,507	\$ 1,371	\$ 12,486	\$ 3,016
Basic and diluted net earnings per unit	\$ 0.22	\$ 0.03	\$ 0.24	\$ 0.06
Distributable cash <sup>1</sup>	\$ 16,459	\$ 612	\$ 24,752	\$ 7,541
Distributions paid or payable <sup>2</sup>	\$ -	\$ 9,121	\$ -	\$ 18,244
Distributions paid per unit on unsubordinated units	\$ -	\$ 0.21	\$ -	\$ 0.42
Weighted Average Units outstanding				
Limited Partnership Units	52,788,843	52,788,843	52,788,843	52,788,843
Fully diluted	56,870,476	56,870,476	56,870,476	56,870,476
<b>The Fund</b>				
	13 weeks ended	13 weeks ended	26 weeks ended	26 weeks ended
(\$000's except per unit amounts)	July 1, 2006	July 2, 2005	July 1, 2006	July 2, 2005
Net earnings	\$ 6,514	\$ 812	\$ 7,661	\$ 1,714
Basic and diluted net earnings per unit	\$ 0.22	\$ 0.03	\$ 0.26	\$ 0.06
Distributable cash <sup>1</sup>	\$ -	\$ 6,176	\$ -	\$ 12,352
Distributions paid or payable	\$ -	\$ 6,176	\$ -	\$ 12,352
Weighted Average Units outstanding				
Trust Units <sup>3</sup>	29,407,626	29,407,626	29,407,626	29,407,626
Special Trust Units	23,381,217	23,381,217	23,381,217	23,381,217

1. Please refer to the Distributable cash definition in the MD&A for detailed reconciliations of these amounts. The Fund receives distributions from Clearwater and in turn distributes them to its unitholders. As such, distributable cash for the Fund is equal to the distributions received and paid.
2. Subordination on 9,352,487 million units expired on December 31, 2005. No distributions were paid on these units in 2005.
3. Clearwater's Partnership Agreement provides that as long as Clearwater Fine Foods Incorporated ("CFFI") owns more than 45% of the units of the Fund on a fully diluted basis, they have the right to appoint 4 of the 7 directors of CS ManPar. CFFI currently owns 46.71% and therefore CFFI has the right to nominate the majority of the board of directors. Therefore the Fund does not consolidate the results of Clearwater's operations but rather accounts for the investment using the equity method. Due to the limited amount of information that this would provide on the underlying operations of Clearwater, the financial highlights of Clearwater are also enclosed.



Colin MacDonald  
Chief Executive Officer  
Clearwater Seafoods Limited Partnership  
August 11, 2006

## 2006 SECOND QUARTER CONFERENCE CALL AND WEBCAST

Clearwater will review its first quarter financial results via conference call on Tuesday May 9, 2006 at 4:00 p.m. Eastern Time (5:00 p.m. Atlantic). The call will be chaired by Colin MacDonald, Clearwater's Chief Executive Officer, and he will be joined by Robert Wight, the Chief Financial Officer. You can access the call by dialling 800-814-4853 or 416-644-3434. A replay will be available through September 11, 2006 at 877-289-8525 or 416-640-1917 using pass code 21196907 (pound key). To listen to the webcast of this event, please enter <http://www.newswire.ca/en.webcast/viewEvent.cgi?eventID=1546160> in your web browser.

## ABOUT CLEARWATER

Clearwater is recognized for its consistent quality, wide diversity and reliable delivery of premium seafood, including scallops, lobster, clams, cold water shrimp, crab and groundfish.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion and Analysis ("MD&A") was prepared effective August 11, 2006.

The Audit Committee and the Board have reviewed and approved the contents of this MD&A as well as the related 2006 second quarter news release.

This MD&A should be read in conjunction with the interim and annual financial statements, and the annual information form, which are available on Sedar at [www.sedar.com](http://www.sedar.com) as well as Clearwater's website, [www.clearwater.ca](http://www.clearwater.ca).

As of December 31, 2005, Clearwater's management evaluated the effectiveness of its disclosure controls and procedures, as defined under the rules adopted by the Ontario Securities Commission in multilateral instrument 52-109. This evaluation was performed under the supervision of, and with the participation of the Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"). Based on the evaluation of disclosure controls and procedures, the CEO and CFO have concluded that Clearwater's disclosure controls and procedures are effective.

The audited financial statements for December 31, 2005 and the first quarter April 1, 2006 have been restated with respect to the accounting for an inflation bond. In management's opinion this does not impact the overall process for the disclosure controls and procedures. It is limited to the accounting applied to inflation adjusted bonds and was accounted for incorrectly based on the interpretation of mark-to-market information provided by a third party. Subsequently, management has developed additional controls regarding the accounting for the inflation bonds and believe them to be effective as of the date of this release.

The review and evaluation of disclosure controls and procedures is an on-going process managed by the CEO and CFO to ensure compliance with security rules and regulations.

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## COMMENTARY REGARDING FORWARD-LOOKING STATEMENTS

*This Report may contain forward-looking statements. Such statements involve known and unknown risks, uncertainties, and other factors outside management's control including but not limited to total allowable catch levels, selling prices, weather, exchange rates and fuel costs that could cause actual results to differ materially from those expressed in the forward-looking statements. The Fund does not assume responsibility for the accuracy and completeness of the forward-looking statements and does not undertake any obligation to publicly revise these forward-looking statements to reflect subsequent events or circumstances.*

## EXPLANATION OF YEAR-TO-DATE RESULTS

*Consolidated Operating Results for the 26-week periods ended July 1, 2006 and July 2, 2005 in thousands of Canadian dollars.*

The results of operations of the Fund are entirely related to Clearwater's performance and therefore the commentary below is on the operations of Clearwater. The statement of earnings disclosed below reflects the unaudited interim earnings of Clearwater for the 26-week periods ended July 1, 2006 and July 2, 2005.

	2006	2005
Sales	\$ 151,661	\$ 137,071
Cost of goods sold	107,025	106,371
	44,636	30,700
	29.4%	22.4%
Administration and selling	17,621	17,366
Loss (gain) on disposal and other, net	2,931	(2,077)
Other income	(3,697)	(657)
Foreign exchange and derivative contracts income	(7,668)	(3,190)
Bank interest and charges	437	345
Interest on long-term debt	6,836	5,741
Depreciation and amortization	7,673	7,618
Reduction in foreign currency translation account	1,697	526
	25,830	25,672
Earnings before income taxes and minority interest	18,806	5,028
Income taxes	3,094	805
Earnings before minority interest	15,712	4,223
Minority interest	3,226	1,207
Net earnings	\$ 12,486	\$ 3,016

## Net Earnings

Net earnings increased by \$9.5 million in 2006 due primarily to higher gross profit, realized foreign exchange income and higher other income.

	2006	2005	Change
Net earnings	\$ 12,486	\$ 3,016	\$ 9,470
Explanation of changes in earnings:			
Higher gross profit			13,936
Higher cash foreign exchange and derivative income			5,926
Higher other income			3,040
Lower gains on disposal and other			(5,008)
Higher income tax expense			(2,289)
Higher minority interest expense			(2,019)
Higher non-cash foreign exchange and derivative expense			(1,448)
Higher interest			(1,187)
Higher reduction in foreign currency translation account			(1,171)
All other			(310)
			\$ 9,470

Net sales to customers for the year-to-date by product category were as follows:

	2006	2005	Change	%
Scallops	\$ 54,317	\$ 39,201	\$ 15,116	39%
Lobster	35,233	33,194	2,039	6%
Clams	29,757	21,840	7,917	36%
Cold water shrimp	15,558	18,841	(3,283)	(17%)
Groundfish and other	8,165	14,656	(6,491)	(44%)
Crab	4,260	4,770	(510)	(11%)
Hedging program	4,371	4,569	(198)	(4%)
	\$ 151,661	\$ 137,071	\$ 14,590	11%

Scallops, which represent one of our more profitable species, have grown to represent 36% of sales year-to-date of 2006 compared to 31% of annual 2005 sales and 29% of the comparative year-to-date 2005 sales. Scallop sales increased primarily due to 46% higher volumes, increases in the selling price for each species and a heavier weighting of Argentine scallops in 2006 when compared to 2005. Despite the higher cost of

fuel, harvesting costs were lower per pound due to higher catch rates.

Lobster sales increased compared to the prior year due to modest increases in volumes. A combination of our new raw lobster product and the application of technology that provides an effective method to sort and grade our live lobster, has allowed us to purchase live product on a more selective basis and utilize the product we have more efficiently.



Clam sales increased due primarily to higher volumes with stable selling prices in Canadian dollars. We have been increasing our selling prices, which have offset the negative impact of lower exchange rates for U.S. dollars and Japanese Yen against the Canadian dollar. Higher volumes over last year related to the fact that in 2005 there were significant disruptions and refit costs incurred in the clam business as well as the repositioning of the sales channels away from a single importer in the Chinese market. The business operated without these disruptions in 2006. In 2005 we began a process of reorganizing our clam business to respond to the challenges of currency and to take advantage of opportunities that will arise when the new vessel arrives in late 2006. As a result we may continue to see some short-term disruptions in this business. As previously disclosed, we are focused on increasing prices to offset the impact of foreign exchange, reducing our costs through harvesting and processing efficiencies and growing our volumes with results expected to be realized over time.

Clearwater's fleet of in excess of 20 vessels used approximately 32 million litres of marine fuel oil in 2005. A change of one cent in the price of marine fuel oil results in a change of approximately \$320,000 to annual harvesting expenses.

During the quarter, it was announced that the North Sydney plant would be sold to a local group of community and business leaders whose mandate and commitment will be to find alternative opportunities for the plant. Due to the impact of the weakening of the US dollar, the increasing cost of metal cans, the effect of fuel on freight costs and intense US based competition in the

canned clam market, it is uneconomic to maintain a plant in North Sydney to process these clams. This plant was used for the canning of clams, which represent approximately 3% of annual sales and the processing of masago that represents approximately 1% of annual sales. However, we do not expect the decision to exit this plant to have any impact on sales of these products as we have sufficient inventories to supply our customers and have contracted out the production of these products to ensure a continued supply. Exiting the plant triggered a \$3.1 million loss that includes a \$2.2 million dollar non-cash write down and approximately \$0.9 million in other related exit costs. However, going forward these changes are estimated to result in annual savings of approximately \$1 million per year.

In the first quarter of 2006 we began negotiations on a new collective agreement with the Union at our Highland plant in Glace Bay, Nova Scotia. These negotiations are currently at a standstill and the plant has not operated since March 2006. The disruption has and will impact groundfish sales for 2006 but should not have a material impact on earnings.

Coldwater shrimp sales are lower compared to the prior year as lower volumes and lower selling prices per pound were realized in part due to catch mix.

In summary, gross profit was greater by \$13.9 million due primarily to higher earnings in the scallop business as a result of higher volumes despite the continued negative impact of foreign exchange.

Foreign exchange reduced sales and margins by approximately \$13.8 million year-to-date in 2006.

Currency	2006		2005	
	% sales	Rate	% sales	Rate
US dollars	41.5%	1.209	49.2%	1.316
Japanese Yen	8.8%	0.010	7.9%	0.012
Euros	26.5%	1.418	16.0%	1.578
UK pounds	5.3%	2.038	5.3%	2.308
Canadian dollar and other	17.9%		21.6%	
	100.0%		100.0%	



Clearwater maintains an active hedging program to provide a higher degree of certainty to future Canadian dollar cash flows with respect to sales. As of July 1, 2006 the following economic hedges were in place:

Economic Hedge	Year scheduled to expire	Amount	Average rate	% of 2005 sales for related period
US	2006	\$64.1 million	1.12	81%
Euro	2006	\$ 9 million	1.48	24%
US	2007	\$16.5 million	1.16	11%
Euro	2007	\$ 4 million	1.43	7%

Clearwater utilizes a number of financial instruments as part of its hedging strategy that do not qualify for hedge accounting. Please refer to the notes to the financial statements for a list of the contracts outstanding at quarter end.

Due to the increasing complexity of applying the accounting standards as well as the coming requirement to report the change in the mark-to-market as other comprehensive income once the Comprehensive Income Accounting Standard is adopted in 2007; beginning the second quarter of 2006 Clearwater is no longer designating contracts as hedges for accounting purposes. As a result it is recording the fair value of these contracts as an asset (\$1.9 million at April 1, 2006) with the offsetting gain deferred and recognized on the exercise date of the original contract. As of April 1, 2006 all contracts thereafter opened will be marked-to-market each reporting period and any gains or losses, both realized and unrealized, will be included in foreign exchange income.

**Administration and selling costs** were consistent with 2005 on a comparative basis. In 2006 we expect to continue to invest further in developing markets for our products, particularly in Asia.

**Loss (gain) on disposal of licenses and other** is an expense in 2006 versus an income item in 2005. The 2006 figure includes a gain of approximately \$0.4 million on the sale of non-core fishing quotas compared to a gain of approximately \$2.5 million in 2005. The current year

also includes a non-cash write down of the plant and related assets in North Sydney of approximately \$2.2 million and a provision for the related exit costs of approximately \$0.9 million.

**Other income** is higher in 2006 as it includes approximately \$0.8 million in additional royalty income from the rental of quota along with increased export rebates and investment income. 2005 also included a write down on an investment.

**Foreign exchange and derivative contracts** produced income of \$7.7 million in the first half of 2006 versus \$3.2 million in 2005. Year-to-date in 2006, foreign exchange includes approximately \$3.2 million of unrealized exchange losses on currency swaps and foreign exchange option accruals partially offset by unrealized exchange gains on long term debt. From a cash perspective, the business generated \$10.0 million of cash from foreign exchange management in the first half of 2006 versus \$4.1 million in the first half of 2005. A significant portion of foreign exchange realized income relates to option income. Please refer to note 6 in the financial statements for a detailed listing of all derivatives and their fair values. As of July 1, 2006, if all derivative contracts were settled by Clearwater, for which there is no intention to do so, Clearwater would have made a payment of \$2.6 million (December 31, 2005 received a payment of \$8.2 million). Please refer to note 8 in the financial statements for a detailed listing of items included in foreign exchange and derivative contracts.

Other income detail	26 weeks ended 2006	26 weeks ended 2005
Investment income	\$ (776)	\$ (313)
Export rebate	(858)	(457)
Quota rental and royalties	(1,316)	(515)
Other	(747)	628
	\$ (3,697)	\$ (657)

Detailed schedule of foreign exchange and derivative contract income:

Foreign exchange and derivative contract detail year-to-date	26 weeks ended 2006	26 weeks ended 2005
Realized gain		
Foreign exchange cash option income	(8,309)	(3,675)
Other realized	(1,700)	(408)
	(10,009)	(4,083)
Unrealized loss (gain)		
Foreign exchange on balance sheet	(10,655)	(808)
Mark to market on options and expandable contracts	4,048	989
Mark to market on interest and currency swap contracts	8,948	712
	2,341	893
<b>Total gain</b>	<b>\$ (7,668)</b>	<b>\$ (3,190)</b>

**Bank interest and interest on long-term debt** increased due to higher average outstanding debt balances in 2006. Until such time as construction is complete on the new clam vessel the related interest costs are being capitalized. In the first half of 2006, \$1,107,500 of interest was capitalized (2005 - \$597,000). As of July 1, 2006 Clearwater has used economic hedges to term out and fix substantially all its interest rate exposures. Included in interest expense related to 2006 is \$2.4 million of interest related to the Iceland bond. Interest exposure on this bond has been hedged and the cash payment on the related swaps was \$932,000 for the second quarter 2006 (\$1.8 million year-to-date).

The **reduction in foreign currency translation account** is a non-cash adjustment, which relates to the reduction of Clearwater's net investment in its subsidiary in Argentina.

**Minority interest** relates to earnings from Clearwater's investment in its subsidiaries in Argentina and Newfoundland and Labrador.

**Income taxes** have increased compared to the prior year and are estimated to be approximately \$4 to \$5 million for the 2006 fiscal year.

## DISTRIBUTABLE CASH AND CASH DISTRIBUTIONS

Distributable cash is not a recognized measure under Canadian Generally Accepted Accounting Principles

("GAAP") and therefore is unlikely to be comparable to similar measures presented by other companies. Management believes that distributable cash is a useful supplemental measure as it provides an indication of cash available for distribution. This provides guidance to readers seeking to assess the sustainability of distributions by comparing distributions paid to the amount of distributable cash. In addition, as distributable cash is a measure frequently analysed for income trusts we have calculated the amount in order to assist readers in facilitating this review. Distributable cash should not be construed as an alternative to net earnings determined in accordance with GAAP as an indicator of performance, as a measure of liquidity or as a measure of cash flows and management does not use this measure as a performance measure of earnings.

Clearwater's business is seasonal in nature with the result being that generally lower amounts of distributable cash are generated in the first half of the year as compared to the latter half.

During the first half of 2006, Clearwater generated \$24.8 million of distributable cash compared to \$7.5 million in 2005. Please refer to the distributable cash reconciliation included in this document for detailed reconciliations of these amounts.

The significant factors contributing to the increase from 2005 include:

- Increase in gross profit due primarily to higher

earnings from the scallop business as a result of higher volumes and higher selling prices for each species with fewer vessel disruptions;

- Increase in realized foreign exchange income.

Offset by:

- Higher minority interest in earnings from Clearwater's investment in its subsidiaries in Newfoundland and Labrador and Argentina.
- Higher cash taxes.

On December 31, 2005 subordination on 9,352,487 units expired, as a result all units (52,788,843 units) will participate in any future distributions.

The Trustees have decided to reinstate distributions to unit holders on record as of August 31, 2006 at a rate of \$0.05 per unit per month, \$0.60 per unit when annualized retroactive to July 2006 (for total distributions when annualized of approximately \$31.7 million). In making this decision they have considered the current financial results which have improved over the same period in 2005, on-going capital expenditure requirements and cash on hand, which has been reserved to complete funding of the vessel under construction, leverage and expectations regarding future earnings. Future earnings can be impacted by a number of factors including but not limited to, total allowable catch levels, selling prices, weather, exchange rates and fuel costs.

- Current financial results - Earnings have improved in 2006 with the rolling four quarters EBITDA and distributable cash as of the second quarter 2006 reaching \$72 million and \$44 million respectively as compared to \$56 million and \$27 million realized in calendar 2005.
- Capital expenditures - Clearwater currently has two significant capital projects – the clam vessel it expects to complete in 2006 and an Argentine vessel it plans to construct for 2008. Clearwater has retained cash over the past quarters to reduce leverage and has sufficient cash to fully fund the new clam vessel. It intends to use the excess cash on its balance sheet going forward to complete the construction of the clam vessel. It plans to fund construction of the Argentine vessel through reserves from distributable cash prior to delivery, which will fully fund construction of that vessel and with the delivery of that vessel, will result in a fleet of freezer processor vessels that has

an average age of approximately 8 years with long remaining life spans.

- Leverage - Leverage has been decreasing over the past few quarters and now stands at 2.6 times EBITDA as compared to 3.5 times at December 31, 2005. Clearwater's intention is to continue to reduce debt levels in a measured manner over time.
- Expectations regarding future earnings – Clearwater expects that despite the ongoing challenge of foreign exchange, leverage and the short-term negative impact of making continued improvements in the clam business, a positive outlook for the business and fewer vessel disruptions should provide the potential for continued improvements.

## LIQUIDITY AND CAPITAL RESOURCES

Earnings before interest, tax, depreciation and amortization ("EBITDA") and leverage are not recognized measures under Canadian GAAP and therefore are unlikely to be comparable to similar measures presented by other companies. Management believes EBITDA and leverage to be useful terms when discussing liquidity. In addition, as EBITDA and leverage are measures frequently analysed for public companies we have calculated the amount in order to assist readers in facilitating this review. EBITDA should not be construed as an alternative to net earnings determined in accordance with GAAP as an indicator of performance, as a measure of liquidity or as a measure of cash flows and management does not use this measure as a performance measure of earnings. Please refer to the section on definitions and reconciliations for calculation of the EBITDA and leverage referred to in this document.

As at July 1, 2006 the Fund owns 55.71% (July 2, 2005-55.71%) of the outstanding partnership units of Clearwater. However, as Clearwater Fine Foods Incorporated ("CFFI") has maintained the right to nominate the majority of the board of directors of Clearwater at the time of the initial investment by the Fund, the assets and liabilities at acquisition have been recorded using the book values as recorded by CFFI.

As at July 1, 2006 the Fund and Clearwater had similar capital structures as illustrated in the next table:

	Fund	Clearwater
<b>Units</b>		
Publicly Listed Trust Units	29,407,626	
Class A Partnership Units		29,407,626
<b>Units Held solely by Clearwater Fine Foods Incorporated</b>		
Special Trust Units	23,381,217	
Class B Partnership Units		23,381,217
	52,788,843	52,788,843
<b>Convertible debentures/Class C Partnership Units</b>		
Convertible debentures	\$ 49,341,000	
Class C Partnership Units		\$ 49,341,000

The **Special Trust Units** issued by the Fund were issued solely to provide voting rights to Clearwater Class B Partnership units held by CFFI. The right of 9,352,487 Class B Partnership units to receive distributions was subordinated to the rights of the Class A units until December 31, 2005.

In June 2004, 4,081,633 **Class C Units** were issued by Clearwater (indirectly) to the Fund concurrently with the issue by the Fund of \$50 million of Convertible Debentures. The Class C Units are non-voting and redeemable and retractable at a price of \$12.25 per unit. These units exist under an agreement whereby they will be converted, redeemed or retracted in a manner that corresponds to any conversion, redemption or repurchase of the Convertible Debentures of the Fund and in a manner that ensures that the distributions on the Class C Units will be able to (indirectly) fund the ongoing interest payments on the Convertible Debentures. The Class C Units are classified in accordance with their component parts: the value ascribed to the holder's option to convert to units, \$882,000, has been classified as equity and the remaining portion of the units has been classified as debt.

The \$50 million of **Convertible Debentures** issued by the Fund are unsecured and subordinated, bear interest at 7% and are due on December 31, 2010. They are convertible at any time up to maturity at the option of the holder into trust units of the Fund at a conversion price of \$12.25 per trust unit. The Debentures pay interest semi-annually in arrears on June 30 and December 31. The Debentures are not redeemable before December 31, 2007. Subject to regulatory approval, the Fund may satisfy its obligation to repay the principal amount of the Debentures on redemption or at maturity, in whole or in part, by delivering that number of trust units equal to the amount due divided by 95% of the market price of the trust units at that time, plus accrued interest in cash.

As previously noted, Clearwater's intention is to continue to reduce debt levels in a measured manner over time. As part of this strategy the Fund intends to file a notice of intention with the Toronto Stock Exchange ("TSX") to make a normal course issuer bid for a portion of its convertible debentures by which it would acquire up to \$5 million principal amount of convertible debentures in the 12-month period from the date of approval by the TSX. This repurchase will be accompanied by a similar repurchase of Class C Partnership units.

In addition to the Convertible Debentures/Class C Partnership Units, Clearwater has three additional primary debt facilities. These facilities include approximately \$85 million in **five and ten year notes** in Canadian and U.S. dollars from a syndicate of five institutional lenders, 2,460 million ISK (approximately Canadian \$39 million) in **five-year bonds** and a \$60 million **revolving term debt facility** from a syndicate of banks.

In September 2005 Clearwater obtained 2,460 million ISK (approximately Canadian \$39 million as of July 1, 2006) from the Icelandic bond market. The bonds yield 6.7%, are adjusted for the Iceland consumer price index ("CPI"), have a face value of 2,460 million ISK, mature in 2010 and are unsecured. These bonds have been fully swapped into Canadian, U.S., Euro and Pound Sterling debt with floating interest rates. The bond is measured at fair value for changes in foreign exchange with the interest and CPI valued using the effective interest rate method. The non-cash accrual for the interest and inflation adjustment are recorded using the effective interest rate method with the expense being recorded as interest expense on long term debt on the income statement and as an increase to the value of the bond on the balance sheet. The cash interest paid along with the change in the mark-to-market value of the related swaps are classified as foreign exchange and derivative income on the income statement and as a net liability on the balance sheet.

Please refer to note 3 of the financial statements on long-term debt and note 6 on financial instruments.

In addition, during the third quarter of 2005 Clearwater added an additional lender to its syndicate of five and ten year notes and added an additional US \$25 million of available credit under the notes of which US \$5 million has been drawn down. The proceeds from these new facilities were used to reduce the amount outstanding under the revolving term debt facility.

The revolving term debt facility is available to Clearwater until May 2008. This facility is renewable on an annual basis. During the first quarter of 2006, Clearwater determined it did not require access to the full facility and therefore reduced the amount available under the facility from \$115 million to \$60 million. As a result, Clearwater expects to realize lower standby fees going forward. The facility is part of a master netting agreement and was in a cash position of \$13,104,000 as at July 1, 2006. The cash position was a result of the positive operating results, the timing of capital expenditures and the continued suspension of distributions that commenced in the fourth quarter of 2005.

Clearwater's debt facilities contain various covenants and Clearwater is in compliance with these covenants. Management believes the available credit will be sufficient to meet its cash requirements.

During the quarter funded debt (net of cash balances) has increased by approximately \$8.5 million. Capital expenditures, the majority of which related to the new clam vessel currently under construction, and the seasonal investments in inventories, net of the positive earnings for the quarter, are the significant reasons for the increase in net long-term debt. Year-to-date capital expenditures have been fully funded by cash flows and in addition debt levels have been reduced by \$5.6 million. This has resulted in leverage levels improving from 3.5 times EBITDA at December 31, 2005 to 2.6 times as at July 1, 2006.

**Cash flow** generated by Clearwater's operations along with its banking facilities are used to fund current operations, seasonal working capital demands, capital expenditures, other commitments and distributions to Unitholders. Due to the seasonality in Clearwater's business, sales and gross profit are typically higher in the second half of the calendar year than in the first half of the year. Inventories reach a seasonal peak in the summer due to better weather for harvesting, resulting in seasonal demands on working capital. These primarily relate to the segments of the business that purchase product from independent fishermen. These purchases cannot be controlled as efficiently as raw materials harvested by Clearwater's own fleet of vessels.

**Capital expenditures** were \$15.9 million year-to-date (2005 - \$23.3 million). Of this amount, \$15.1 million (2005 - \$21.9 million) was considered return on investment ("ROI") capital and \$0.8 million (2005 - \$1.4 million) was maintenance capital. ROI and maintenance capital are tracked on a project-by-project basis with the

### Summarized cash flow information

For the 13 and 26 week periods ending July 1, 2006 and July 2, 2005. See statements of cash flows for more detail.

	13 weeks ended 2006	13 weeks ended 2005	26 weeks ended 2006	26 weeks ended 2005
Cash flow from operations				
(before change in working capital)	\$ 18,112	\$ 2,960	\$ 28,810	\$ 11,201
Investing, Financing, and other activities				
Distributions to unitholders	-	(9,121)	-	(18,244)
Capital expenditures (net of proceeds on sale)	(7,449)	(5,596)	(14,926)	(20,285)
Investment (reduction) in working capital	(16,967)	(4,871)	(6,867)	6,377
Other investing activities	(283)	(54)	904	543
Distributions to minority partners	(1,849)	-	(2,418)	(869)
Other	(89)	(187)	96	(329)
	(26,637)	(19,829)	(23,211)	(32,807)
Decrease (Increase) in long term debt, net of cash	\$ (8,525)	\$ (16,869)	\$ 5,599	\$ (21,606)

only ROI project currently in process being the new clam vessel. Significant expenditures that are expected to have an average return in excess of average cost of capital are classified as ROI, and expenditures that have less than the cost of capital are classified as maintenance. In addition, Clearwater is reviewing a replacement for one of the vessels in Argentina that will occur in 2008.

As previously announced Clearwater is currently in the process of constructing a **new factory freezer clam vessel**. The total estimated cost of the vessel, including owner supplied materials and related costs, is expected to be approximately \$48 million, of which \$38.6 million has been spent to date. Clearwater expects the new vessel to be delivered in late 2006 and begin harvesting in 2007. Once

operational, this new vessel is expected to reduce harvesting costs, greatly improve the quality and range of products offered and increase its harvesting capacity. Two exciting and key innovations in this vessel, which support these goals, are its state-of-the-art energy management system and its advanced on-board processing systems. The energy management system is expected to result in significantly reduced fuel consumption. The advanced on-board processing systems are expected to improve product quality and yield as well as provide the flexibility to produce a greater variety of products. Construction costs required to complete the vessel will be funded by drawing down cash balances or on debt facilities as required.

## EXPLANATION OF SECOND QUARTER RESULTS

Consolidated Operating Results for the thirteen weeks comprising the second quarter, in thousands of Canadian dollars.

The results of operations of the Fund are entirely related to Clearwater's performance and therefore the commentary below is on the operations of Clearwater. The statement of earnings disclosed below reflects the unaudited interim earnings of Clearwater for the 13-week periods ended July 1, 2006 and July 2, 2005.

	2006	2005
Sales	\$ 81,312	\$ 69,712
Cost of goods sold	57,981	55,160
Gross profit	23,331	14,552
	28.7%	20.9%
Administration and selling	8,932	8,705
Loss (gain) on disposal of licenses and other, net	2,815	(2,068)
Other income	(2,608)	(258)
Foreign exchange and derivative income	(8,698)	(1,691)
Bank interest and charges	216	183
Interest on long-term debt	3,152	2,799
Depreciation and amortization	3,702	3,727
Reduction in foreign currency translation account	345	328
	7,856	11,725
Earnings before income taxes and minority interest	15,475	2,827
Income taxes	2,189	790
Earnings before minority interest	13,286	2,037
Minority interest	1,779	666
Net earnings	\$ 11,507	\$ 1,371



## Net Earnings

Net earnings increased by \$10.1 million in the second quarter of 2006 due primarily to higher gross profits and realized foreign exchange earnings as outlined below.

	2006	2005	Change
Net earnings	\$ 11,507	\$ 1,371	\$ 10,136
Explanation of changes in earnings:			
Higher gross profit			8,779
Higher cash foreign exchange income			6,523
Higher other income			2,350
Higher non-cash foreign exchange income			484
Change in loss/gain on disposal and other, net			(4,883)
Higher income tax expense			(1,399)
Higher minority interest expense			(1,113)
Higher interest expense			(386)
All other			(219)
			\$ 10,136

Net sales to customers for the quarter by product category were as follows:

	2006	2005	Change	%
Scallops	\$ 28,174	\$ 19,646	\$ 8,528	43%
Lobster	20,705	19,723	982	5%
Clams	15,711	10,969	4,742	43%
Cold water shrimp	8,268	8,353	(85)	(1%)
Groundfish and other	3,597	5,858	(2,261)	(39%)
Crab	3,172	3,483	(311)	(9%)
Hedging program	1,685	1,680	5	-%
	\$ 81,312	\$ 69,712	\$ 11,600	17%

Scallop sales, which represent one of our more profitable species, were up due primarily to 62% higher volumes. Volumes were higher in part due to fewer vessel disruptions and strong catch rates in 2006. In the second quarter of 2005 the two Argentine vessels were on refit and we had not taken delivery of the last two vessels for the Canadian fleet.

Lobster sales were consistent with the second quarter of 2005. A slight increase in volumes was offset by a

decrease in selling prices. A combination of our new raw lobster product and the application of technology that provides an effective method to sort and grade our live lobster, has allowed us to purchase live product on a more selective basis and utilize the product we have more efficiently.

Clam sales increased in the quarter compared to the second quarter in 2005 due to increased volumes with stable pricing in Canadian dollars. We have been



Currency	2006		2005	
	% sales	Rate	% sales	Rate
US Dollars	42.5%	1.169	49.2%	1.308
Japanese Yen	10.3%	0.010	8.4%	0.012
Euros	24.7%	1.427	14.2%	1.550
UK pounds	5.1%	2.051	5.0%	2.301
Canadian dollar and other	17.4%		23.2%	
	100.0%		100.0%	

increasing our selling prices, which have offset the negative impact of lower exchange rates for U.S. dollars and Japanese Yen against the Canadian dollar. Higher volumes over the past year related to the fact that in 2005 there were significant disruptions and refit costs incurred in the clam business as well as the repositioning of the sales channels away from a single importer in the Chinese market. The business operated without these disruptions in 2006. In 2005 we began a process of reorganizing our clam business to respond to the challenges of currency and to take advantage of opportunities that will arise when the new vessel arrives in late 2006. As a result we may continue to see some short-term disruptions in this business. As previously disclosed, we are focused on increasing prices to offset the impact of foreign exchange, reducing our costs through harvesting and processing efficiencies and growing our volumes with results expected to be realized over time.

During the quarter, it was announced that the North Sydney plant would be sold to a local group of community and business leaders whose mandate and commitment will be to find alternative opportunities for the plant. Due to the impact of the weakening of the US dollar, the increasing cost of metal cans, the effect of fuel on freight costs and intense US based competition in the canned clam market, it is uneconomic to maintain a plant in North Sydney to process these clams. This plant was used for the canning of clams, which represent approximately 3% of annual sales and the processing of masago that represents approximately 1% of annual sales. However, we do not expect the decision to exit this plant to have any impact on sales of these products as we have sufficient inventories to supply our customers and have contracted out the production of these products to ensure a continued supply.

Exiting the plant triggered a \$3.1 million loss that includes a \$2.2 million dollar non-cash write down and approximately \$0.9 million in other costs. However, going forward these changes are estimated to result in annual savings of approximately \$1 million per year.

Coldwater shrimp sales are consistent as a result of higher volumes offset by lower selling prices, however margins were lower partially as a result of product mix.

In the first quarter of 2006 we began negotiations on a new collective agreement with the Union at our Highland plant in Glace Bay, Nova Scotia. These negotiations are currently at a standstill and the plant has not operated since March 2006. The disruption has and will impact groundfish sales for 2006 but should not have a material impact on earnings.

In summary, gross profit for the quarter was \$8.8 million higher than in 2005 primarily due to higher sales volumes of scallops and clams.

We received about 14 cents less for each U.S. dollar in the second quarter of 2006, which resulted in our receiving approximately \$4.1 million less when converted to Canadian dollars. In addition, exchange rates on Euros, Japanese Yen and Pounds Stirling were lower in 2006, which impacted sales and resulted in our receiving approximately \$1.7 million, \$1.7 million and \$0.5 million less respectively when converted to Canadian dollars. The total impact of lower exchange rates in the second quarter was \$8.0 million dollars.

Clearwater maintains an active hedging program to provide a higher degree of certainty to future Canadian dollar cash flows. For additional detail please refer to the year-to-date analysis as well as note 6 in the financial statements.

Other income detail for the quarter	2006	2005
Investment income	\$ (278)	\$ (243)
Export rebate	(440)	(249)
Quota rental and royalties	(1,312)	(41)
Other	(578)	275
	\$ (2,608)	\$ (258)

Foreign exchange and derivative contract detail for the quarter	2006	2005
Realized gain		
Foreign exchange cash option income	\$ (6,081)	\$ (1,386)
Other realized	(1,437)	391
	(7,518)	(995)
Unrealized (gain)/loss		
Foreign exchange on balance sheet	(5,350)	(1,318)
Mark to market on options and expandable contracts	1,587	(90)
Mark to market on interest and currency swap contracts	2,583	712
	(1,180)	(696)
Total gain	\$ (8,698)	\$ (1,691)

**Loss (gain) on disposal of licenses and other, net** is an expense in 2006 versus an income item in 2005. The 2006 figure includes a gain of approximately \$0.4 million on the sale of non-core fishing quotas compared to a gain of approximately \$2.5 million in 2005. The current quarter also includes a non-cash write down of the plant and related assets from the North Sydney plant of approximately \$2.2 million and a provision for the related costs of approximately \$0.9 million.

**Other income** is higher in 2006 as it includes approximately \$1.3 million in additional royalty income from the rental of quota along with higher export rebates when compared to the prior year.

**Foreign exchange and derivative contract** income produced \$8.7 million in 2006 versus \$1.7 million in 2005. From a cash perspective, the business generated \$7.5 million of cash from foreign exchange management in 2006 versus \$1.0 million in 2005.

**Interest on long-term debt** was higher in 2006 as a result of higher debt levels.

**Income taxes** were \$2.2 million as compared to \$0.8 million in 2005. Income taxes have increased due to the improved earnings of taxable subsidiaries.

## OUTLOOK

Clearwater's sales and gross profit for the second quarter of 2006 and year-to-date have improved compared to 2005. Improvements are due in part to the fact that the business has operated closer to normal during the first half of the year. In 2005 we experienced a number of one-time negative impacts including vessel disruptions and refits, repositioning of the sales channel in the Chinese market as well as the late delivery and maintenance required for the two new FAS scallop vessels. In 2006 our clam business will continue to be under stress until the arrival of the new clam vessel. In the meantime, Clearwater will continue to operate two older clam vessels that are nearing the end of their useful lives, and consequently are expected to incur high maintenance costs.

Distributable cash generated has improved compared to the first half in 2005 with \$24.5 million of distributable cash generated versus \$7.5 million in 2005. Despite the ongoing challenge of foreign exchange and leverage, a positive outlook for the business and fewer vessel disruptions should provide the potential for improvements in 2006 as compared to 2005.

The Trustees have decided to reinstate distributions to unit holders on record as of August 31, 2006 at a rate of \$0.05 per unit per month, \$0.60 per unit when annualized retroactive to July 2006 (for total distributions when annualized of approximately \$31.7 million). In making this decision they have considered the current financial results which have improved over the same period in 2005, on-going capital expenditure requirements and cash on hand, which has been reserved to complete funding of the vessel under construction, leverage and expectations regarding future earnings. Future earnings can be impacted by a number of factors, including but not limited to, total allowable catch levels, selling prices, weather, exchange rates and fuel costs.

- Current financial results - Earnings have improved in 2006 with the rolling four quarters EBITDA and distributable cash as of the second quarter 2006 reaching \$72 million and \$44 million respectively as compared to \$56 million and \$27 million realized in calendar 2005.

- Capital expenditures - Clearwater currently has two significant capital projects – the clam vessel it expects to complete in 2006 and an Argentine vessel it plans to construct for 2008. Clearwater has retained cash over the past quarters to reduce leverage and has sufficient cash to fully fund the new clam vessel. It intends to use the excess cash on its balance sheet going forward to complete the construction of the clam vessel. It plans to fund construction of the Argentine vessel through reserves from distributable cash prior to delivery, which will fully fund construction of that vessel and with the delivery of that vessel, will result in a fleet of freezer processor vessels that has an average age of approximately 8 years with long remaining life spans.
- Leverage - Leverage has been decreasing over the past few quarters and now stands at 2.6 times EBITDA as compared to 3.5 times at December 31, 2005. Clearwater's intention is to continue to reduce debt levels in a measured manner over time.
- Expectations regarding future earnings – Clearwater expects that despite the ongoing challenge of foreign exchange, leverage and the short-term negative impact of making continued improvements in the clam business, a positive outlook for the business and fewer vessel disruptions should provide the potential for continued improvements.

Foreign exchange and increases in fuel costs are expected to continue to impact the future results of the company. However, we expect to see improvements in the business for the remainder of the year compared to the prior year. The core business is healthy and with the strength of our quota ownership and effective and efficient harvesting and production processes the long-term outlook for the business is positive. Our strategy is for the long-term health and growth of the company continuing to develop and maintain the strong foundations Clearwater was built upon.

## SUMMARY OF QUARTERLY RESULTS

The following financial data provides historical data for the ten most recently completed quarters.

(IN 000'S EXCEPT PER UNIT AMOUNTS)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
<b>Fiscal 2006</b>				
Sales	\$ 70,349	\$81,312		
Net earnings	979	11,507		
Basic earnings per unit	0.02	0.22		
Fiscal 2005				
Sales	\$ 67,359	\$ 69,712	\$ 93,548	\$ 84,220
Net earnings	1,645	1,371	12,136	4,721
Basic earnings per unit	0.03	0.03	0.23	0.09
Fiscal 2004				
Sales	\$ 72,741	\$ 85,038	\$ 88,835	\$ 98,845
Net earnings (loss)	(2,978)	8,760	15,138	16,553
Basic earnings (loss) per unit	(0.06)	0.17	0.29	0.31

Clearwater's business is seasonal in nature with sales typically higher in the second half of the calendar year than in the first half of the year, a trend illustrated in the results above.

For a more detailed analysis of each quarter results please refer to our quarterly reports and our annual reports, which contain an analysis of the fourth quarter.

## DEFINITIONS AND RECONCILIATIONS

### Distributable Cash

*Distributable cash is not a recognized measure under Canadian Generally Accepted Accounting Principles ("GAAP") and therefore is unlikely to be comparable to similar measures presented by other companies. Management believes that distributable cash is a useful supplemental measure as it provides an indication of cash available for distribution to readers seeking to assess the sustainability of distributions by comparing distributions*

*paid to the amount of distributable cash. In addition, as distributable cash is a measure frequently analyzed for income trusts we have calculated the amount in order to assist readers in facilitating this review. Distributable cash should not be construed as an alternative to net earnings determined in accordance with GAAP as an indicator of performance, as a measure of liquidity or as a measure of cash flows and management does not use this measure as a performance measure of earnings.*

### Reconciliation of distributable cash

	13 weeks ended	13 weeks ended	26 weeks ended	26 weeks ended
(\$000's except per unit amounts)	July 1, 2006	July 2, 2005	July 1, 2006	July 2, 2005
Cash flow from operating activities	\$ 1,145	\$ (1,911)	\$ 21,943	\$ 17,578
Add (deduct):				
Change in non-cash working capital <sup>A</sup>	16,967	4,871	6,867	(6,377)
Minority share EBITDA, int., taxes <sup>B</sup>	(2,249)	(1,264)	(4,125)	(1,674)
Proportionate maint. capital <sup>C</sup>	(341)	(685)	(722)	(1,596)
Gain (loss) on disposal P,P,E /licenses <sup>D</sup>	677	(399)	789	(390)
Distributable cash	\$ 16,459	\$ 612	\$ 24,752	\$ 7,541
Distributions <sup>E</sup>	\$ -	\$ 9,121	\$ -	\$ 18,244
Payout ratio	- %	1,490%	- %	242%

- A. Change in non-cash working capital is excluded as changes in working capital are financed using Clearwater's debt facilities.
- B. Minority share in EBITDA, interest and taxes represents cash flows attributable to the minority interest in certain non-wholly owned subsidiaries. It is the minority partners' interest in the earnings before interest, taxes, depreciation and amortization of the subsidiaries less their proportionate share of the interest and taxes.
- C. Proportionate maintenance capital represents capital expenditures that are related to sustaining existing assets rather than expansion or productivity improvement.
- D. Gains and losses on property, plant and equipment are added back (deducted) as during the course of operating the business Clearwater will typically realize gains and losses from the turnover of assets, which occurs frequently due to Clearwater's focus on innovation. During the second and third quarters of 2005 gains of \$5.6 million were excluded from the calculation of distributable cash as it pertains to the sale of a licence that did not relate to the typical turnover of assets. During the second quarter of 2006, \$479,000 of gains on sales of licences and \$3.1 million of losses associated with the exiting of a plant were excluded from the calculation of distributable cash.
- E. There have been no distributions for the first and second quarters of 2006. 2005 first quarter distributions consisted of payments of 21 cents/unit on 43,436,356 unsubordinated units (no payments were made on 9,352,487 subordinated units).

Clearwater's business is seasonal in nature with the result being that lower amounts of distributable cash are generated in the first half of the year as compared to the latter half.

## Gross Profit

Gross profit consists of sales less harvesting, production, distribution, and manufacturing costs.

### Earnings before interest, tax, depreciation and amortization

Earnings before interest, tax, depreciation and amortization ("EBITDA") is not a recognized measure under Canadian GAAP and therefore is unlikely to be comparable to similar measures presented by other companies. Management

believes EBITDA to be a useful term when discussing liquidity. In addition, as EBITDA is a measure frequently analysed for public companies we have calculated the amount in order to assist readers in facilitating this review. EBITDA should not be construed as an alternative to net earnings determined in accordance with GAAP as an indicator of performance, as a measure of liquidity or as a measure of cash flows and management does not use this measure as a performance measure of earnings.

### Reconciliation of the current quarter and preceding three quarters EBITDA

(\$000's)	July 1, 2006	December 31, 2005
Net earnings	\$ 29,343	\$ 19,873
Add (deduct):		
Minority interest	5,416	3,398
Income taxes	5,264	2,975
Reduction in foreign currency translation	2,407	1,236
Depreciation and amortization	15,455	15,400
Interest on long term debt	13,545	12,450
Bank interest and charges	878	786
<b>EBITDA</b>	<b>\$ 72,308</b>	<b>\$ 56,118</b>

## Leverage

Leverage is not a recognized measure under Canadian GAAP and therefore is unlikely to be comparable to similar measures presented by other companies. Management believes leverage to be a useful term when discussing liquidity. In addition, as leverage is a measure frequently analysed for public companies we have calculated the amount in order to assist readers in facilitating this review.

Leverage should not be construed as an indicator of performance, as a measure of liquidity or as a measure of cash flows and management does not use this measure as a performance measure of earnings.

Leverage is calculated by dividing the current and preceding three quarters EBITDA by the total debt on the balance sheet for the period

(\$000's)	July 1, 2006	December 31, 2005
EBITDA	\$ 72,308	\$ 56,118
Total debt	185,056	194,445
Leverage	2.6	3.5

**CONSOLIDATED BALANCE SHEETS**

(IN THOUSANDS OF DOLLARS)

	July 1, 2006 (UNAUDITED)	December 31, 2005 (AS RESTATED) (SEE NOTE 7)
<b>ASSETS</b>		
Investment in Clearwater Seafoods Limited Partnership (note 2)	336,995	329,271
<b>LIABILITIES AND UNITHOLDERS' EQUITY</b>		
Convertible debentures (note 3)	49,341	49,278
<b>UNITHOLDERS' EQUITY</b>		
Trust units (note 4)	299,336	299,336
Cumulative earnings	83,546	75,885
Cumulative distributions	(95,228)	(95,228)
	287,654	279,993
	<b>\$ 336,995</b>	<b>\$ 329,271</b>

See accompanying notes to consolidated financial statements



**CONSOLIDATED STATEMENTS OF EARNINGS AND CUMULATIVE EARNINGS**

13 AND 26 WEEK PERIODS ENDED JULY 1, 2006 AND JULY 2, 2005  
 (IN THOUSANDS OF DOLLARS)  
 (UNAUDITED)

	13 weeks ended		26 weeks ended	
	2006	2005	2006	2005
Equity in earnings of Clearwater Seafoods				
Limited Partnership	\$ 6,541	\$ 839	\$ 7,717	\$ 1,766
Interest income	877	877	1,755	1,755
Interest expense	(904)	(904)	(1,811)	(1,807)
Net earnings	\$ 6,514	\$ 812	\$ 7,661	\$ 1,714
Cumulative earnings at beginning of period	77,032	67,779	75,885	66,877
Cumulative earnings at end of period	\$ 83,546	\$ 68,591	\$ 83,546	\$ 68,591
Basic and diluted net earnings per trust unit	\$ 0.22	\$ 0.03	\$ 0.26	\$ 0.06

See accompanying notes to consolidated financial statements

**CONSOLIDATE STATEMENTS OF CASH FLOWS**

13 AND 26 WEEK PERIODS ENDED JULY 1, 2006 AND JULY 2 2005  
 (IN THOUSANDS OF DOLLARS)  
 (UNAUDITED)

	13 weeks ended		26 weeks ended	
	2006	2005	2006	2005
<b>Cash flows from operating activities</b>				
Net earnings	\$ 6,514	\$ 812	\$ 7,661	\$ 1,714
Items not involving cash				
Equity in earnings of Clearwater Seafoods Limited Partnership, net of cash distributions received of nil, 26 weeks - nil				
(2005 - \$6,179, 26 weeks - \$12,355)	(6,541)	5,340	(7,717)	10,589
Other	27	27	56	52
	-	6,179	-	12,355
<b>Cash flows used in financing activities</b>				
Distributions to unitholders	-	(6,179)	-	(12,355)
Increase (decrease) in cash	-	-	-	-
Cash - beginning of period	-	-	-	-
Cash - end of period	\$ -	\$ -	\$ -	\$ -

See accompanying notes to consolidated financial statements

## CLEARWATER SEAFOODS INCOME FUND

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(TABULAR AMOUNTS EXPRESSED IN THOUSANDS OF DOLLARS)  
(UNAUDITED)

#### 1 Basis of Presentation

Clearwater Seafoods Income Fund (the "Fund") is a limited purpose, open-ended trust established under the laws of the Province of Ontario. The Fund was created to acquire and indirectly hold the securities of Clearwater Seafoods Limited Partnership ("Clearwater").

The unaudited interim period consolidated financial statements have been prepared by the Fund in accordance with Canadian Generally Accepted Accounting Principles. The preparation of financial data is based on accounting policies and practices consistent with those used in the preparation of the audited annual consolidated financial statements. These unaudited interim period consolidated financial statements do not contain all the disclosures required in annual audited financial statements by Canadian Generally Accepted Accounting Principles, and accordingly should be read together with the audited annual consolidated financial

statements and the accompanying notes included in the Fund's 2005 Annual Report.

These consolidated financial statements consolidate the accounts of the Fund and its subsidiary, Clearwater Seafoods Holdings Trust ("CSHT"). CSHT owns 55.71% (December 31, 2005 – 55.71%) of the units of Clearwater. However, as the Fund does not have the right to nominate the majority of the board of directors, it does not consolidate the results of Clearwater's operations but rather accounts for the investment using the equity method. Under this method, the cost of the investment is increased by the Fund's proportionate share of Clearwater's earnings and reduced by any distributions paid to the Fund by Clearwater and amortization of the purchase price discrepancy. Due to the limited amount of information that this provides on the underlying operations of Clearwater the financial statements of Clearwater are also enclosed.

#### 2 Investment in Clearwater Seafoods Limited Partnership

The investment in Clearwater Seafoods Limited Partnership consists of the following:

	July 1, 2006	December 31, 2005 (as restated) (see note 7)
Investment in Class A Partnership units, at cost	\$ 298,454	\$ 298,454
Investment in Class C Partnership units	50,000	50,000
Add: Cumulative equity in net earnings	83,769	76,045
Less: Cumulative distributions received	(95,228)	(95,228)
	<b>\$ 336,995</b>	<b>\$ 329,271</b>

Included in equity in earnings in the quarter is \$130,000, 26 weeks – \$761,000 (2005 –\$75,000, 26 weeks - \$86,000) for amortization and other adjustments relating to purchase price discrepancies recognized by the Fund in accounting for its investment in Clearwater using the equity method.

Details of the allocation of the excess of the Fund's cost over the historical cost of the assets recorded by Clearwater are as follows:

	July 1, 2006	December 31, 2005
Intangible assets		
Licences – indefinite lives	\$ 189,260	\$ 189,260
Customer relationships and other	548	578
Goodwill	14,240	14,240
Long-term liabilities	588	606
Cumulative foreign currency translation account	(6,596)	(7,435)
	<b>\$ 198,010</b>	<b>\$ 197,249</b>

### 3 Convertible Debentures

On June 15, 2004 the Fund completed an offering for \$50 million of 7% convertible unsecured subordinated debentures, which are due December 31, 2010.

The convertible debentures are convertible at any time up to maturity at the option of the holder into trust units of the Fund at a conversion price of \$12.25 per trust unit. The debentures pay interest semi-annually in arrears on June 30 and December 31, commencing December 31, 2004. The debentures are not redeemable before December 31, 2007. On and after December 31, 2007, but before December 31, 2008, the debentures may be redeemed at the option of the Fund provided that the market price of the trust units is not less than 125% of the conversion price. On and after December 31, 2008, the debentures may be redeemed at the option of the Fund at a price equal to their principal amount plus accrued interest. Subject to regulatory approval, the Fund may satisfy its obligation to repay the principal amount of the debentures on redemption or at maturity, in whole or in part, by delivering that number of trust units equal to the amount due divided by 95% of the market price of the trust units at that time, plus accrued interest in cash.

The convertible debentures are classified in accordance with their component parts: the value ascribed to the holder's option to convert to units has been classified as equity and the remaining portion of the convertible debenture has been classified as debt.

The estimated fair value of the Fund's convertible debentures at July 1, 2006 was \$45,875,000 based on the quoted market value of the debentures Clr.db on the Toronto Stock Exchange.

### 4 Trust Units and Special Trust Units

The Declaration of Trust provides that an unlimited number of units and an unlimited number of Special Trust Units may be issued. Each unit is transferable and represents an equal undivided beneficial interest in any distributions of the Fund and in the net assets of the Fund in the event of termination or winding up of the Fund. All units have equal rights and privileges. Each unit entitles the holder thereof to participate equally in the distributions and to one vote at all meetings of unitholders for each whole unit held. The issued units are not subject to future calls or assessments. Units are redeemable at any time at the option of the holder at amounts related to market price at the time, subject to a maximum of \$50,000 in aggregate cash redemptions by the Fund in any particular month. This limitation may be waived at the discretion of the Trustees of the Fund. Redemption in excess of this amount, assuming no waiving of the limitation, shall be paid by way of a distribution in specie of assets of the Fund, namely notes of Clearwater Seafoods Holdings Trust.

The Special Trust Units have been issued solely to provide voting rights to Clearwater Class B units ("CSLP Exchangeable Units"). Special Trust Units were issued in conjunction with the CSLP Exchangeable Units and cannot be transferred separately from them. Special Trust Units entitle the holders thereof to the number of votes at any meeting of unitholders of the Fund equal to the number of units which may be obtained upon exchange of the CSLP Exchangeable Units to which they relate and do not otherwise entitle the holder to any rights with respect to the Fund's property or income.

The right of the holders of 40% of the CSLP Exchangeable Units, or 9,352,487 units, to receive distributions from Clearwater were subordinated to the rights of holders of Class A limited partnership units of Clearwater ("CSLP Ordinary Units") until December 31, 2005 at which time all subordination agreements expired. CSLP Exchangeable Units that are no longer subject to subordination may at any time thereafter at the option of the holder be exchanged on a one-for-one basis for units of the Fund.

CSLP Exchangeable Units that were subject to subordination, as described above, were not during such period of subordination exchangeable into units of the Fund, and their entitlement to distributions from Clearwater in respect of any month during such period was subordinated until CSLP Ordinary Units and CSLP Exchangeable Units, that at the time were not subject to subordination, received distributions of at least \$0.0958 per unit in respect of such month.

	Units	Special Trust Units	Total \$ (in 000's)
Balance December 31, 2005, no change to July 1, 2006	29,407,629	23,381,217	\$ 299,336

As at July 1, 2006 there were in total 52,788,843 units outstanding (December 31, 2005 – 52,788,843).

## 5 Guarantees

The Fund guarantees Clearwater's term credit facility (see note 3(d) to Clearwater's financial statements). The guarantee is limited to the value of the convertible debentures and the value of the units held in Clearwater. As of July 1, 2006 and December 31, 2005 there was no balance outstanding on the term credit facility.

## 6 Comparative Figures

The comparative figures have been reclassified in accordance with the current year presentation for interest income and interest expense in the consolidated statement of earnings and cumulative earnings.

## 7 Restatement

During the preparation of the second quarter 2006 interim financial statements, Clearwater discovered an error relating to its financial statements for the year ended December 31, 2005 and quarter ended April 1, 2006. The senior unsecured bond and the accrued interest reported on the previously released financial statements did not reflect adjustments for the change in the Icelandic Consumer Price Index for the periods reported.

The comparative figures in these financial statements have been restated to reflect the required adjustments by the Fund related to its equity interest in Clearwater to properly account for the inflation adjusted bonds within Clearwater. The adjustments are non-cash and relate to accounting for the bonds using the effective interest method. As disclosed in the notes to the financial statements, Clearwater has derivative agreements that effectively hedge the economic impact from inflation adjustments. These non-cash entries will be offset by non-cash adjustments related to the derivative agreements.

Summary of adjustments from reported to restated figures:

<b>As of December 31, 2005</b>			
Consolidated balance sheet			
	As previously reported	Adjustments	As restated
Investment in Clearwater Seafoods			
Limited Partnership	\$ 329,921	\$ (650)	\$ 329,271
Cumulative earnings	76,535	(650)	75,885

CLEARWATER SEAFOODS LIMITED PARTNERSHIP

CONSOLIDATED BALANCE SHEETS  
(IN THOUSANDS OF DOLLARS)

	July 1, 2006 (UNAUDITED)	December 31, 2005 (AS RESTATED) (see note 12)
<b>ASSETS</b>		
<b>Current Assets</b>		
Cash	\$ 14,885	\$ 9,726
Accounts receivable	49,272	54,912
Inventories	59,915	43,419
Prepays and other	7,122	6,458
	<u>131,194</u>	<u>114,515</u>
Other long-term assets	10,063	10,643
Property, plant and equipment	158,398	151,945
Licences and licence agreements	102,768	103,181
Goodwill	10,378	10,378
	<u>\$ 412,801</u>	<u>\$ 390,662</u>
<b>LIABILITIES AND UNITHOLDERS' EQUITY</b>		
<b>Current Liabilities</b>		
Checks issued in excess of funds on deposit	\$ 727	\$ -
Accounts payable and accrued liabilities	50,456	36,597
Income taxes payable	4,005	2,144
Current portion of long-term debt (note 3)	971	1,008
	<u>56,159</u>	<u>39,749</u>
Long-term debt (note 3)	184,085	193,437
Future income taxes	8,175	7,958
Due to joint venture partner	2,093	2,023
Minority interest	2,989	2,181
<b>UNITHOLDERS' EQUITY</b>		
Partnership units (note 4)	173,133	173,133
Cumulative earnings	162,372	149,886
Cumulative distributions	(162,620)	(162,620)
Cumulative foreign currency translation account (note 5)	(13,585)	(15,085)
	<u>159,300</u>	<u>145,314</u>
	<u>\$ 412,801</u>	<u>\$ 390,662</u>

See accompanying notes to consolidated financial statements

CLEARWATER SEAFOODS LIMITED PARTNERSHIP

CONSOLIDATED STATEMENTS OF EARNINGS AND CUMULATIVE EARNINGS

13 AND 26 WEEK PERIODS ENDED JULY 1, 2006 AND JULY 2, 2005  
(IN THOUSANDS OF DOLLARS)  
(UNAUDITED)

	13 weeks ended		26 weeks ended	
	2006	2005	2006	2005
Sales	\$ 81,312	\$ 69,712	\$ 151,661	\$ 137,071
Cost of goods sold	57,981	55,160	107,025	106,371
Gross profit	23,331	14,552	44,636	30,700
Administration and selling	8,932	8,705	17,621	17,366
Loss (gain) on disposal of licences and other	2,815	(2,068)	2,931	(2,077)
Other income (note 7)	(2,608)	(258)	(3,697)	(657)
Foreign exchange and derivative contracts (note 8)	(8,698)	(1,691)	(7,668)	(3,190)
Bank interest and charges	216	183	437	345
Interest on long-term debt	3,152	2,799	6,836	5,741
Depreciation and amortization	3,702	3,727	7,673	7,618
Reduction in foreign currency translation account (note 5)	345	328	1,697	526
	7,856	11,725	25,830	25,672
Earnings before the undernoted	15,475	2,827	18,806	5,028
Income taxes	2,189	790	3,094	805
Earnings before minority interest	13,286	2,037	15,712	4,223
Minority interest	1,779	666	3,226	1,207
Net earnings	\$ 11,507	\$ 1,371	\$ 12,486	\$ 3,016
Cumulative earnings at beginning of period	150,865	131,658	149,886	130,013
Cumulative earnings at end of period	\$ 162,372	\$ 133,029	\$ 162,372	\$ 133,029
Basic and diluted net earnings per unit	\$ 0.22	\$ 0.03	\$ 0.24	\$ 0.06

See accompanying notes to consolidated financial statements



CLEARWATER SEAFOODS LIMITED PARTNERSHIP

CONSOLIDATED STATEMENTS OF CASH FLOWS

13 AND 26 WEEK PERIODS ENDED JULY 1, 2006 AND JULY 2, 2005  
(IN THOUSANDS OF DOLLARS) (UNAUDITED)

	13 weeks ended		26 weeks ended	
	2006	2005	2006	2005
<b>Cash flows from (used in) operating activities</b>				
Net earnings	\$ 11,507	\$ 1,371	\$ 12,486	\$ 3,016
Items not involving cash				
Depreciation and amortization	3,702	3,727	7,673	7,618
Unrealized foreign exchange gain on long-term debt	(5,304)	(607)	(10,656)	(97)
Future income taxes (recovery)	123	(368)	(945)	18
Reduction in foreign currency translation account	345	328	1,697	526
Minority interest	1,779	666	3,226	1,207
Unrealized foreign exchange loss (gain) on currency option contracts	1,586	(89)	4,048	990
Unrealized loss on currency and interest swap contracts	1,605	-	7,118	-
Accrued interest and inflation on long-term bonds payable	1,125	-	2,374	-
Loss (gain) on disposal of property, plants, equipment, licences and other	1,644	(2,068)	1,789	(2,077)
	18,112	2,960	28,810	11,201
Change in non-cash operating working capital	(16,967)	(4,871)	(6,867)	6,377
	1,145	(1,911)	21,943	17,578
<b>Cash flows from financing activities</b>				
Proceeds from long-term debt	-	15,856	-	21,452
Reduction of long-term debt	(1,055)	(791)	(1,167)	(916)
Other	(89)	(187)	96	(329)
Distributions to minority partners	(1,849)	-	(2,418)	(869)
Distributions to unitholders	-	(9,121)	-	(18,244)
	(2,993)	5,757	(3,489)	1,094
<b>Cash flows from (used in) investing activities</b>				
Increase in other long-term assets	(283)	(54)	904	543
Purchase of property, plants, equipment, licences and other	(8,342)	(8,317)	(15,863)	(23,290)
Proceeds on disposal of property, plants, equipment, licences and other	893	2,721	937	3,005
	(7,732)	(5,650)	(14,022)	(19,742)
Increase (decrease) in cash	(9,580)	(1,804)	4,432	(1,070)
Cash - beginning of period	23,738	162	9,726	(572)
Cash - end of period	\$ 14,158	\$ (1,642)	\$ 14,158	\$ (1,642)
Cash consists of cash and checks issued in excess of funds on deposit.				
<b>Supplementary cash flow information</b>				
Interest paid	\$ 4,743	\$ 4,219	\$ 7,300	\$ 5,750
Income taxes (received) paid	(137)	2,090	673	3,918
<b>Change in non-cash working capital consists of changes in the following accounts:</b>				
Accounts receivable	(490)	4,940	5,640	20,181
Inventories	(17,953)	(21,628)	(16,496)	(14,966)
Foreign exchange on option contracts	(1,586)	89	(4,048)	(990)
Prepays and other	(2,133)	(784)	(664)	(1,423)
Accounts payable and accrued liabilities	5,050	12,870	6,840	5,665
Income taxes payable	145	(358)	1,861	(2,090)
	\$ (16,967)	\$ (4,871)	\$ (6,867)	\$ 6,377

There were no material non-cash transactions during the quarters presented  
See accompanying notes to consolidated financial statements

## CLEARWATER SEAFOODS LIMITED PARTNERSHIP

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(TABULAR AMOUNTS EXPRESSED IN THOUSANDS OF DOLLARS)

(UNAUDITED)

#### 1 Basis of Presentation

Clearwater Seafoods Limited Partnership ("Clearwater") is a limited partnership that acquired the seafood business of Clearwater Fine Foods Incorporated ("CFFI") on July 30, 2002.

The unaudited interim period consolidated financial statements have been prepared by Clearwater in accordance with Canadian Generally Accepted Accounting Principles ("GAAP"). The preparation of financial data is based on accounting policies and practices consistent with those used in the preparation of the audited annual consolidated financial statements. These unaudited interim period consolidated financial statements do not contain all the disclosures required in annual audited financial statements by Canadian GAAP, and accordingly should be read together with the audited annual consolidated financial statements and the accompanying notes included in Clearwater Seafoods Income Fund's (the "Fund") 2005 Annual Report.

As CFFI maintained the right to nominate the majority of the board of directors both before and after the acquisition of its seafoods business by Clearwater Seafoods Limited Partnership the acquisition was accounted for using the book values of the assets and liabilities as recorded by CFFI.

#### 2 Seasonality

Due to the seasonal nature of the business, gross profit is typically higher in the second half of the calendar year than the first half of the year.

#### 3 Long-Term Debt

	July 1, 2006	Dec. 31, 2005 (as restated) (see note 12)
Notes payable (a)		
Canadian dollars	\$ 63,000	\$ 63,000
United States dollars	23,324	23,296
Class C Partnership Units (b)	49,341	49,280
Bond payable (c)	39,535	46,873
Marine mortgage, due in 2017 (d)		
Canadian	2,275	2,792
Danish Kroner	1,700	1,771
Yen	1,443	1,570
Term loan, due in 2091 (e)	3,500	3,500
Other loans	1,938	2,363
	<b>185,056</b>	<b>194,445</b>
Less current portion	971	1,008
	<b>\$ 184,085</b>	<b>\$ 193,437</b>

(a) Notes payable, Senior secured notes issued in four series:

\$43,000,000 Canadian Series A Notes issued in 2003, bearing interest at 6.4% payable semi-annually, maturing December 8, 2008.

\$15,000,000 U.S. dollar Series B Notes issued in 2003, bearing interest at 5.65% payable semi-annually, maturing December 8, 2008.

\$20,000,000 Canadian Series C Notes issued in 2003, bearing interest at 7.23% payable semi-annually, maturing December 8, 2013.

\$5,000,000 U.S. dollar Series D Notes issued in 2005, bearing interest at 6.12% payable semi-annually, maturing December 8, 2013. Clearwater has an additional \$20,000,000 U.S. dollar available to draw on this facility until December 31, 2007.

The notes are secured by mortgages and charges on all of the present and future property and assets of Clearwater and certain of its wholly owned subsidiaries, the interests of the Fund in Clearwater Seafoods Holdings Trust ("CSHT") and all the issued shares of CS ManPar Inc., the general partner of Clearwater. The security arrangement is guaranteed by an inter-creditor agreement with the banking syndicate members participating in the term credit facility disclosed in section (f) of this note.

(b) In June 2004, 4,081,633 Class C units were issued concurrently with the issue by the Fund of \$50 million of Convertible Debentures and are held by the Fund through CSHT. The Class C units are redeemable and retractable at a price of \$12.25 per unit and are due December 31, 2010. These units exist under an agreement whereby they will be converted, redeemed or retracted in a manner that corresponds to any conversion, redemption or repurchase of the Convertible Debentures of the Fund and in a manner that ensures that the distributions on the Class C units will be able to fund the ongoing interest payments on the Convertible Debentures. The Class C units are classified in accordance with their component parts: the value ascribed to the holders option to convert to Class A units has been classified as equity and the remaining portion of the units has been classified as debt. Interest on the debt is calculated by applying an interest rate of approximately 7.3% to the outstanding debt component. The difference between actual cash payments, which will approximate 7.02%, and interest expense is added to the debt component of the units.

(c) Senior unsecured bond in the amount of 2,460,000,000 ISK due September 27, 2010 at a fixed rate of 6.7% accrued annually and paid at maturity. Both the bond and the interest are adjusted for changes in the Icelandic Consumer Price index ("CPI"). Clearwater has entered into a number of swap agreements to economically fix the currency and CPI exposure associated with the debt. There are also interest rate swap agreements in place.

Clearwater has no intention to unwind the swap agreements, however the agreements do not qualify for hedge accounting and therefore the gains and losses related to the fair value of these hedges are taken into income during the period.

The swap agreements have effectively resulted in the following:

- \$25,000,000 Canadian dollar liability with an effective interest rate of 8.72%
- \$5,000,000 U.S. dollar liability with an effective interest rate of 9.43%
- \$4,707,502 U.S. dollar liability with an effective interest rate of 8.51%
- 3,000,000 Pound Sterling liability with an effective interest rate of 9.65%
- 2,500,000 Euro liability with an effective interest rate of 8.02%

Interest expense on the bond is recorded using the effective interest rate method that takes into account estimated future Icelandic inflation rates. Interest accrued related to the second quarter of 2006 was \$1.1 million (nil 2005) and \$2.4 million year-to-date (nil 2005). As previously noted interest exposure on this bond has been hedged and the cash payment on the related swaps was \$932,000 for the second quarter 2006 (\$1.8 million year-to-date).

Refer to note 6(c) for further information on the related swaps.

(d) Marine mortgage payable in the principal amount of CDN \$4,549,000 (December 31, 2005 - \$5,583,000), DKK 17,871,000 (December 31, 2005 – DKK 19,262,000) and YEN 297,671,000 (December 31, 2005 – 317,516,000) bearing interest at UNIBOR plus 1% payable semi-annually, 50% of which represents Clearwater's proportionate share. Principal payments are required annually with CDN \$517,000, DKK 1,391,000 and YEN 19,845,000 due in 2007, CDN \$776,000, DKK 2,087,000 and YEN 29,767,000 due in 2008-2012, CDN \$152,000 due in 2013, DKK 2,087,000 and YEN 29,767,000 due in 2013-2014, DKK 1,871,000 due in 2015, YEN 29,767,000 due in 2015-2016 and YEN 9,923,000 due in 2017, 50% of which represents Clearwater's proportionate share. The loan matures in 2017 and is secured by a first mortgage over the related vessel and covenants concerning certain fishing licences.

(e) Term loan, payable in 2091. In connection with this loan Clearwater makes a royalty payment of \$275,000 per annum in lieu of interest.

(f) Term credit facility with available credit of up to \$60 million (December 31, 2005 \$115 million), maturing in May 2008. In May 2007 the banking syndicate at the request of Clearwater may extend the credit for an additional two years until May 2009. This facility is part of a master netting agreement and on July 1, 2006 was in a net cash position of CDN \$13,104,000, (December 31, 2005 CDN, \$7,859,000). The facility bears interest at rates ranging from prime plus 0.5 – 1.25% and Libor plus 1.5 - 2.25% and has no scheduled repayments. The facility is secured by mortgages and charges on all of the present and future property and assets of Clearwater and of certain of its wholly-owned subsidiaries, the interests of the Fund in CSHT, the interests of CSHT in Clearwater and all the issued shares of CS ManPar Inc., and is subject to the maintenance of certain financial covenants. As part of the master netting arrangement, bank account balances associated with the facility are netted with the term credit facility balance.

Clearwater's debt facilities contain various covenants. Clearwater is in compliance with all debt covenants at July 1, 2006.

Principal repayments required in each of the next five years are approximately as follows:

2006	\$	971
2007		1,204
2008		60,878
2009		1,009
2010		89,254

#### 4 Partnership Units

Clearwater is authorized to issue an unlimited number of Class A limited partnership units, an unlimited number of Class B general partnership units, issuable in series, an unlimited number of Class C limited partnership units and an unlimited number of Class Y general partnership units, issuable in series. Each unit (other than the Class Y units) entitles the holder thereof to one vote, except in certain situations as described pursuant to the Limited Partnership Agreement governing Clearwater. Each issued Class B unit is accompanied by a Special Trust Unit issued by the Fund entitling the holder to receive notice of, to attend and to vote at meetings of unitholders of the Fund.

The right of 40% of the holders of Class B units, or 9,352,487 units, to receive distributions from Clearwater was subordinated to the rights of holders of Class A units until December 31, 2005. Class B units that were subject to such subordination were entitled to receive distributions from Clearwater only quarterly, rather than monthly, and only after distributions of at least \$0.0958 per unit in respect of each month during such quarter have first been paid to the holders of Class A units and Class B units that at the time are not subject to such subordination. Class B units that are no longer subject to subordination may at any time thereafter at the option of the holder thereof be exchanged for units of the Fund whereupon CSHT will be issued Class A units and the Class B units that were so exchanged will be cancelled.

In June 2004, 4,081,633 Class C units in the amount of \$50 million were issued concurrently with the issue by the Fund of \$50 million of Convertible Debentures and are held by the Fund through CSHT. The Class C units are non-voting, redeemable and retractable at a price of \$12.25 per unit. These units exist under an agreement whereby they will be converted, redeemed or retracted in a manner that corresponds to any conversion, redemption or repurchase of the Convertible Debentures of the Fund and in a manner that ensures that the distributions on the Class C units will be able to fund the ongoing interest payments on the Convertible Debentures. Class C Partnership units are classified in accordance

with their component parts: the value ascribed to the holder's option to convert to units has been classified as equity and the remaining portion of the units has been classified as debt.

Distributions on the Class C Partnership units take priority over the Class A and B units and are included in interest expense on long term debt.

	Class A Units	Class B Units	\$ (in 000's)
Balance December 31, 2005, no change			
to July 1, 2006	29,407,626	23,381,217	\$ 173,133

As at July 1, 2006 there were in total 52,788,843 units outstanding (December 31, 2005 - 52,788,843).

## 5 Cumulative Foreign Currency Translation Account

The reduction in the foreign currency translation account is a non-cash adjustment, which relates to the reduction of Clearwater's net investment in its 80% owned subsidiary in Argentina. The cumulative translation account largely arose because of the significant devaluation of the peso in Argentina versus the Canadian dollar in 2001. It is Clearwater's desire to continue to manage its exposure to Argentine pesos by repatriating its capital as quickly as possible while not impairing local operations. Dividends declared have resulted in a reduction in Clearwater's net investment in that subsidiary and accordingly, a proportionate share of the cumulative translation account has been recognized in earnings. Clearwater anticipates that continued repayments of its advances to and the payment of dividends from the subsidiary in Argentina may result in additional reduction of the cumulative translation account in the future. The cumulative translation account is included in the Unitholders Equity section of the balance sheet and the remaining balance at July 1, 2006 is \$13,585,000 (December 31, 2005 - \$15,085,000).

## 6 Financial Instruments

In the ordinary course of business, Clearwater enters into derivative financial instruments to reduce underlying fair value and cash flow risks associated with foreign currency and interest rates.

Forward exchange contracts are used by Clearwater in the management of its foreign currency exposures. Clearwater manages its exposure to fluctuations in exchange rates on United States dollar and European Euro denominated revenues using forward exchange contracts.

July 1, 2006 and December 31, 2005 Clearwater had outstanding forward contracts as follows (as converted to Canadian dollars at contracted rates):

Currency	Notional Amount	Average Exchange Rate	Maturity	Fair Value Asset (liability)
<b>United States dollar</b>				
July 1, 2006	57,100	1.114	2006	(32)
	10,000	1.134	2007	243
December 31, 2005	62,000	1.257	2006	6,516
<b>Euro</b>				
July 1, 2006	9,000	1.476	2006	393
	4,000	1.430	2007	(29)
December 31, 2005	12,000	1.498	2006	1,334

Although Clearwater has no intention of settling these contracts, at July 1, 2006, if it settled these contracts it would have received a payment of \$575,000 (December 31, 2005 - \$7,850,000). The liability or asset recorded is included in accounts payable and accrued liabilities or prepaids and other, as appropriate and the resulting loss or gain is included in income.

Clearwater has also entered into foreign currency options and expandable forward contracts as at July 1, 2006 and December 31, 2005 with estimated quoted market values as follows:

Currency	Notional Amount	Average Exchange Rate	Maturity	Fair Value Asset (liability)
<b>United States dollar</b>				
July 1, 2006	71,500	1.134 – 1.191	2006	(163)
	90,000	1.100 – 1.180	2007	(823)
	7,000 – 34,000	1.127 – 1.271	2006	492
	6,500 – 24,000	1.187 – 1.202	2007	363
December 31, 2005	170,000	1.172 – 1.255	2006	(1,214)
	20,000	1.180 – 1.135	2007	161
	22,500 – 45,000	1.229 – 1.271	2006	1,951
	17,500 – 35,000	1.187 – 1.202	2007	315
<b>Japanese Yen</b>				
July 1, 2006	1,000,000	0.01125	2006	-
	1,000,000	0.01047	2007	(64)
December 31, 2005	1,000,000	0.01125	2006	(12)
<b>Euro</b>				
July 1, 2006	29,000	1.375 – 1.478	2006	(932)
	15,000	1.390 – 1.413	2007	(897)
December 31, 2005	29,000	1.215 – 1.478	2006	(741)
<b>Sterling</b>				
July 1, 2006	20,700	2.013 – 2.101	2007	(1,114)
December 31, 2005	5,000	2.020	2006	(157)

Although Clearwater has no intention of settling these contracts prior to maturity, at July 1, 2006, if it settled these contracts it would have made a payment of \$3,138,000 (December 31, 2005 - received a payment of \$303,000). The above market values represent the potential net asset/liability in the event the contracts were closed. The liability or asset recorded is included in accounts payable and accrued liabilities or prepaids and other, as appropriate and the resulting loss or gain is included in income.

## (b) Credit risk

Clearwater is exposed to credit risk in the event of non-performance by counter parties to its derivative financial instruments, but does not anticipate non-performance by any of the counter parties as Clearwater only deals with highly rated financial institutions.

Clearwater has significant accounts receivable from customers operating in the United States, Europe and Asia. Clearwater has a policy of utilizing a combination of credit reporting agencies, credit insurance, letters of credit and secured forms of payment to mitigate customer specific credit risk and country specific credit risk.

## (c) Interest rate risk and fair values

As indicated in the note entitled "Long-Term Debt" Clearwater uses cross currency and interest rate swaps to hedge its exposures to changes in foreign currencies and interest rates. The terms of the swap agreements related to the Icelandic bonds also effectively hedge the changes in the CPI. These agreements do not qualify for hedge accounting. Although Clearwater has no intention of settling these contracts prior to maturity, at July 1, 2006, if it settled these contracts it would have made a payment of \$7,690,678 (December 31, 2005 made a payment of \$563,000). The liability is included in accounts payable and accrued liabilities and the resulting non-cash loss is included in income. See note 3(c) for additional information relating to the swaps. The Icelandic Krona has declined substantially and reduced the value of the Iceland bond in Canadian currency and has had a corresponding impact on the related swaps.

The carrying value of cash, accounts receivable and accounts payable and accrued liabilities approximate fair value.

## 7 Other Income

Other income detail:

	13 weeks ended		26 weeks ended	
	2006	2005	2006	2005
Investment income	\$ (278)	\$ (243)	\$ (776)	\$ (313)
Export rebate	(440)	(249)	(858)	(457)
Quota rental and royalties	(1,312)	(41)	(1,316)	(515)
Other (income)/expense	(578)	275	(747)	628
	<u>\$ (2,608)</u>	<u>\$ (258)</u>	<u>\$ (3,697)</u>	<u>\$ (657)</u>



## 8 Foreign exchange and derivative contracts

Foreign exchange and derivative contract detail:

	13 weeks ended		26 weeks ended	
	2006	2005	2006	2005
Realized gain				
Foreign exchange cash option income	\$ (6,081)	\$ (1,386)	\$ (8,309)	\$ (3,675)
Other	(1,437)	391	(1,700)	(408)
	(7,518)	(995)	(10,009)	(4,083)
Unrealized (gain)/loss				
Foreign exchange on balance sheet	(5,350)	(1,318)	(10,655)	(808)
Mark to market on options and expandables	1,587	(90)	4,048	989
Mark to market on interest and currency swaps	2,583	712	8,948	712
	(1,180)	(696)	2,341	893
Total gain	\$ (8,698)	\$ (1,691)	\$ (7,668)	\$ (3,190)

## 9 Segmented Information

### (a) General information

Clearwater operates primarily within one industry, that being the harvesting, procurement, processing, and sale of seafood with no separately reportable business segments. The products are sold primarily to customers in the United States, Asia, Europe, and Canada.

### (b) Net sales to customer by product category

	13 weeks ended		26 weeks ended	
	2006	2005	2006	2005
Scallops	\$ 28,174	\$ 19,646	\$ 54,317	\$ 39,201
Lobster	20,705	19,723	35,233	33,194
Clams	15,711	10,969	29,757	21,840
Cold water shrimp	8,268	8,353	15,558	18,841
Groundfish and other	3,597	5,858	8,165	14,656
Crab	3,172	3,483	4,260	4,770
Hedging program	1,685	1,680	4,371	4,569
	\$ 81,312	\$ 69,712	\$ 151,661	\$ 137,071

(c) Geographical information

	13 weeks ended		26 weeks ended	
	2006	2005	2006	2005
Sales				
United States	\$ 23,087	\$ 24,856	\$ 40,123	\$ 44,218
Europe				
France	17,093	8,238	34,925	18,315
Denmark	4,645	1,321	6,833	6,208
UK	5,334	4,431	10,153	8,899
Other	2,681	4,600	7,096	9,076
Asia				
Japan	7,346	8,056	12,767	13,777
Other	8,107	3,943	13,633	9,366
Canada	11,334	12,449	21,760	22,129
Other, including hedging program	1,685	1,818	4,371	5,083
	\$ 81,312	\$ 69,712	\$ 151,661	\$ 137,071

	July 1, 2006	Dec 31, 2005
<b>Property, plant, equipment, licences and goodwill</b>		
Canada	\$ 252,605	\$ 246,503
Argentina	17,920	18,295
Other	1,019	706
	\$ 271,544	\$ 265,504

## 10 Related Party Transactions

Clearwater had the following transactions and balances with CFFI during the second quarter and year-to-date periods of 2006 and 2005.

	13 weeks ended		26 weeks ended	
	2006	2005	2006	2005
<b>Transactions</b>				
Charge by CFFI for use of a corporate airplane	50	21	102	34
Charged to CFFI for rent and other services	54	52	108	106
Charged by CFFI for management fee	50	-	100	-
<b>Balances, as at July 1, 2006 and December 31, 2005</b>			July 1, 2006	Dec. 31, 2005
Receivable from CFFI			520	639

In addition Clearwater was charged approximately \$38,000 for vehicle leases in the second quarter of 2006 (2005 - \$61,000) and year-to-date \$75,000 (2005 - \$ 103,000) and approximately \$10,000 for other services (2005 - \$10,000) by companies controlled by a relative of an officer of Clearwater, year-to-date \$19,000 (2005 - 29,000).

These transactions are in the normal course of operations and have been recorded at the exchange amount.

## 11 Comparative figures

The comparative figures have been reclassified in accordance with the current year presentation in the consolidated statement of earnings and cumulative earnings.

## 12 Restatement

During the preparation of the second quarter 2006 interim financial statements, Clearwater discovered an error relating to its financial statements for the year ended December 31, 2005 and the quarter ended April 1, 2006. The senior unsecured bond and accrued interest reported on the previously released financial statements did not reflect adjustments for the change in the Icelandic Consumer Price Index for the periods reported.

The comparative figures in these financial statements have been restated to reflect the required adjustments by Clearwater to properly account for inflation adjusted bonds. The adjustments are non-cash and relate to accounting for the bonds using the effective interest method. As disclosed in the notes to the financial statements Clearwater has derivative agreements that effectively hedge the economic impact from inflation adjustments. These non-cash entries will be offset by non-cash adjustments related to the derivative agreements.

Summary of adjustments from reported to restated figures:

<b>As of December 31, 2005</b>			
Consolidated balance sheet			
	As previously reported	Adjustments	As restated
Other long-term assets	\$ 10,397	\$ 246	\$ 10,643
Long-term debt	192,024	1,413	193,437
Cumulative earnings	151,053	(1,167)	149,886

Further information can be found in the disclosure documents filed by Clearwater Seafoods Income Fund with the securities regulatory authorities available at [www.sedar.com](http://www.sedar.com) or at its website ([www.clearwater.ca](http://www.clearwater.ca)).

For further information, please contact: Robert Wight, Chief Financial Officer, Clearwater at (902) 457-2369, or Tyrone Cotie, Director of Corporate Finance and Investor Relations, Clearwater, at (902) 457-8181.

## CORPORATE INFORMATION

### TRUSTEES OF CLEARWATER SEAFOODS INCOME FUND

**Bernard Wilson**  
Former Vice Chairman  
Pricewaterhouse Coopers

**Brian Crowley**  
Founding President  
Atlantic Institute for Market Studies

**Thomas D. Traves**  
President and Vice-Chancellor,  
Dalhousie University

### DIRECTORS OF CS MANPAR INC., MANAGING PARTNER OF CLEARWATER SEAFOODS LIMITED PARTNERSHIP

**Bernard Wilson**  
Former Vice Chairman  
Pricewaterhouse Coopers  
Chairman, Audit Committee

**Hugh K. Smith**  
Vice-President,  
Municipal Group of Companies  
Chairman, Corporate Governance and  
Compensation Committee

**Thomas D. Traves**  
President and Vice-Chancellor,  
Dalhousie University

**Brian Crowley**  
Founding President  
Atlantic Institute for Market Studies

**Brendan Paddick**  
Chief Executive Officer  
Columbus Communications Inc.

**John C. Risley**  
Chairman, CS ManPar Inc.

**Colin E. MacDonald**  
Chief Executive Officer, CS ManPar Inc.

### OFFICERS OF CS MANPAR INC.

**John C. Risley**  
Chairman

**Colin E. MacDonald**  
Chief Executive Officer

**Eric R. Roe**  
Chief Operating Officer

**Michael D. Pittman**  
Vice-President, Fleet

**Robert D. Wight**  
Vice-President, Finance  
and Chief Financial Officer

**Stan Spavold**  
Corporate Secretary

### INVESTOR RELATIONS

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Halifax, Nova Scotia

### UNITS LISTED

Toronto Stock Exchange  
Unit symbol: CLR.UN  
Convertible Debenture symbol: CLR.DB

### TRANSFER AGENT

Computershare Investor Services Inc.