



**DESTINY RESOURCE SERVICES CORP.**  
**2006 Second Quarter Interim Report**  
**As at and for the Three and Six Months Ended June 30, 2006**

**MANAGEMENT'S DISCUSSION AND ANALYSIS ("MD&A")**

*The following discussion and analysis of financial results for the three month and six month periods ended June 30, 2006 ("Q2'06" and "2006 YTD") and June 30, 2005 ("Q2'05" and "2005 YTD") is based on information available until August 10, 2006 (unless otherwise noted) and upon the Company's consolidated interim financial statements for the periods presented, which were prepared in accordance with Canadian generally accepted accounting principles with the exception of a complete set of notes, and should be read in conjunction with the Company's consolidated financial statements and Annual Report for the prior fiscal year ended December 31, 2005.*

*Forward-looking Information*

*Statements in this Management's Discussion and Analysis relating to matters that are not historical facts are forward-looking statements. Such forward-looking statements involve known (see Business Risks section) and unknown risks and uncertainties which may cause the actual results, performances or achievements of the Company to be materially different from any future results implied by such forward-looking statements.*

**REVENUE**

Revenue for Q2'06 at \$16.9 million increased by 14.4% from \$14.8 million in Q2'05. 2006 YTD revenue at \$43.1 million represented a 37.3% increase from \$31.4 million over the same period last year. 53% of revenue for the first half of the current year was represented by one client compared to 57% last year (for additional information refer to the Working Capital section). Commodity prices remain high and exploration is a growing focus within the industry, which in turn has translated into increased overall revenues for the Company.

**GROSS MARGIN**

Gross margin for Q2'06 was \$2.5 million representing 14.8% of revenues compared to \$2.6 million representing 17.3% of revenues over the same quarter last year. Delays in job starts due to government activities, such as military exercises and provincial permitting processes, was the primary cause for the decrease. Costs were incurred for keeping working crews on standby during this time for which no revenues were generated.

Gross margin for 2006 YTD was \$9.8 million representing 22.6% of revenues compared to \$6.6 million representing 20.9% of revenues over the same period last year. The increase in 2006 YTD gross margin dollars compared to 2005 YTD arises from:

- Favourable Q1'06 greater activity levels and modest price increase over Q1'05,
- Offset by delays in job starts causing outlays in costs without any related revenues in Q2'06.

**GENERAL AND ADMINISTRATIVE ("G&A") EXPENSES**

General and administrative expenses, which represent primarily the costs associated with the corporate head office and the lease of the Survey & Mapping division's shop and office, were \$0.9 million for Q2'06 compared to \$0.6 million over the same period last year. 2006 YTD expenses were \$2.6 million compared to \$1.6 million over the same period last year which represented an overall increase of \$1.0 million. Current year to date accruals for the profit sharing plans were \$0.8 million higher than last year (being a full accrual this year compared to only partial last year) and represented 80% of this increase. The remaining difference can be attributed to increased infrastructure costs in response to increased business activities.

The profit sharing plans have been instituted to align the Company's incentive compensation for key employees with the interests of shareholders. The plans, which replace bonuses and the grant of stock options, are intended to have the participating employees more focused on the Company's bottom line performance and to enable the Company to retain and attract operating and executive management in a competitive environment. Awards are made one-half in cash and one-half in shares, to be purchased in the market.

### AMORTIZATION OF PROPERTY AND EQUIPMENT

Amortization of property and equipment increased by \$0.3 million to \$0.8 million for Q2'06 from \$0.5 million over the same period last year. For 2006 YTD this amount was \$1.5 compared to \$0.9 million for 2005 YTD. Amortization is dependant on the timing of additions to property and equipment. Over the last half of 2005, \$4.7 million was invested in purchases of property and equipment. These purchases were amortized at the full rate in 2006. Disposals of property and equipment in 2006 resulted from normal course business activities with no specific noteworthy items.

### INTEREST EXPENSE

Interest expense for 2006 YTD at \$0.1 million was slightly higher than the amount incurred in 2005 YTD. Usage of the operating lines has increased due to higher business activities.

### INCOME TAXES

The Company expects to have a small loss for tax purposes for fiscal 2006 resulting in no current income tax expense for the year. For fiscal 2007 all non-capital tax loss carry-forwards will be fully utilized. The future income tax liability as at June 30, 2006 is at \$1.5 million, increased from the \$0.8 million at the end of Q1'06 to reflect operations.

### SUMMARY OF QUARTERLY RESULTS

A summary of operating results by quarter for the last 2 years is as follows:

<i>(000's, except per share amounts)</i>	<b>Q2 2006</b>	<b>Q1 2006</b>	<b>Q4 2005</b>	<b>Q3 2005</b>	<b>Q2 2005</b>	<b>Q1 2005</b>	<b>Q4 2004</b>	<b>Q3 2004</b>
Total Revenue	<b>16,934</b>	26,199	11,844	21,216	14,793	16,604	7,430	12,200
Income (loss) from continuing operations	<b>504</b>	3,313	1,842	1,325	1,979	2,091	(421)	1,057
Income (loss) from discontinued operations	---	---	---	---	---	---	72	---
Income (loss) for the period	<b>504</b>	3,313	1,842	1,325	1,979	2,091	(349)	1,057
Basic & diluted earnings (loss) per share:								
From continuing operations	<b>0.09</b>	0.59	0.33	0.24	0.36	0.38	(0.16)	0.40
From discontinued operations	---	---	---	---	---	---	0.03	---
For the period	<b>0.09</b>	0.59	0.33	0.24	0.36	0.38	(0.13)	0.40
Number of shares outstanding weighted average								
Basic	<b>5,575</b>	5,575	5,568	5,554	5,548	5,495	2,664	2,636
Diluted	<b>5,596</b>	5,596	5,591	5,567	5,571	5,500	2,664	2,636

The above noted Summary of Quarterly Results highlights the following:

1. The Company's business is seasonal with Q1 and Q3 traditionally being the two strongest quarters and Q2 and Q4 normally being the weakest quarters. The underlying causes of the seasonality are weather conditions, the Company being restricted from entering and conducting work in designated wildlife areas at certain times of the year, and the timing of client capital spending programs.
2. The Company discontinued operations in several businesses in 2003. Amounts in 2004 represent recoveries relating to insurance and bad debts for these discontinued operations.

### LIQUIDITY AND CAPITAL RESOURCES

Destiny's capital requirements consist primarily of working capital necessary to fund operations, capital expenditures related to the purchase and manufacture of operating equipment, payment of dividends and capital to finance strategic acquisitions. Sources of funds available to meet these capital requirements include cash flow from operating activities, external lines of credit, equipment financing, term loans and access to equity markets.

During 2005, the Company increased its bank facility from \$5 million to \$10 million, with the ability to draw to \$18 million during the months of June through September. In addition, the rate on the facility was reduced to bank prime

plus 1%. During 2006, the bank facility maximum is at \$10 million and the rate on this facility has been further reduced by to bank prime plus 0.75%.

The Company believes that it has the capital resources and availability to meet its working capital and capital expenditure requirements and to pay dividends in accordance with its dividend policy for 2006 and beyond.

#### **WORKING CAPITAL**

At June 30, 2006 net working capital was at \$3.2 million compared to \$0.6 million at December 31, 2005. Significant components that contributed to this increase include: funds from operations of \$6.6 million, year to date net capital expenditures of \$1.3 million, and the payment of cash dividends of \$2.7 million.

Approximately 79% of trade accounts receivable at June 30, 2006, (67% at December 31, 2005) were represented by one client. Destiny provides services to this client both directly for the client's own account (for the development of seismic data for the client to sell) and for work for third party exploration and production companies, most of which are substantial oil companies and several of which specify Destiny as their sub-contractor of choice when contracting with Destiny's client. Approximately 75% of trade accounts receivable at June 30, 2006 was less than 60 days old (49% are less than 30 days old). Bad debt expenses for the Company's businesses have been negligible over the past three years.

#### **PROPERTY AND EQUIPMENT**

Property and equipment assets totaled \$11.2 million at the end of Q2'06, compared to \$11.5 million as at December 31, 2005 reflecting a net decrease \$0.3 million for the year. Activity for 2006 consisted of: purchases of \$1.3 million, amortization of \$1.5 million, disposals of less than \$0.1 million.

#### **CONTRACTUAL OBLIGATIONS**

Destiny's future contractual payment obligations are in the form of operating leases on premises and equipment. The Company has no hedging, capital leases or other "off balance sheet" contractual obligations.

	<b>Payments Due by Future Year</b>				
	<b>total</b>	<b>less than 1 year</b>	<b>2 – 3 years</b>	<b>4 - 5 years</b>	<b>After 5 years</b>
Operating Leases	2,064,816	773,962	851,442	439,412	---

#### **SHAREHOLDERS' EQUITY**

Shareholders' equity was \$12.9 million at the end of Q2'06 reflecting an increase of \$1.1 million from year end 2005 of \$11.8 million. The major components within this increase were: net income of \$3.8 million, and cash dividends of \$2.7 million.

As at August 10, 2006, the number of issued and outstanding common shares is 5,575,081 with 53,000 additional common shares reserved for potential future issuance pursuant to options outstanding under the Company's stock option plan.

#### **NEW CANADIAN ACCOUNTING PRONOUNCEMENTS**

The Canadian Institute of Chartered Accountants ("CICA") has issued a number of accounting pronouncements, some of which may impact the Company's reported results and financial position in future periods. See the 2005 Annual Report and the Q1'06 interim report.

#### **BUSINESS RISKS**

Destiny is subject to the risks and variables inherent in the oilfield services industry. Demand for the Company's products and services depend on the exploration, development and production activities of energy companies. These activities are directly affected by factors such as oil and gas commodity prices, weather, changes in legislation,

exchange rates, the general state of domestic and world economies, concerns regarding fuel surpluses or shortages, substitution through imports or alternative energy sources, changes to taxation or regulatory regimes and the broad sweep of international political risks such as war, civil unrest, nationalization and expropriation or confiscation, which are all beyond the control of the Company and cannot be accurately predicted. The oil market is influenced by global supply and demand considerations and by the supply management practices of OPEC. The natural gas market is primarily influenced by North American supply and demand and by the price of competing fuels. The risks associated with external competition are minimized by concentrating Company activities in areas where it has demonstrated technical and operational advantages and by employing highly competent professional staff. Environmental standards and regulations are continually becoming more stringent in this industry and Destiny is committed to maintaining its high standards. Destiny also mitigates business risks by establishing strategic alliances with reputable partners, developing new technologies and methodologies as well as investigating new business opportunities.

The risks inherent in the oilfield services industry could impact the Company's ability to meet its financial covenants on its revolving, bank operating loan facility. Bank lines were drawn by \$4.7 million as at June 30, 2006 and were well below the maximum allowable limit at that time.

### **OUTLOOK**

Destiny believes that it has adequate working capital, cash flow from operations and access to capital to fund ongoing business requirements. Management believes the Company has a cost structure that has sufficient variability to adapt to the volatility of its industry. The Company has experienced management, at all levels of sales, operations and administration, who are motivated to achieve success in both the short- and long-term. The Company provides services principally in connection with the exploration for oil and natural gas.

Destiny periodically encounters expansion opportunities to consider. These involve, in each case, the requirement for capital expenditures beyond the normal course for the Company. Destiny may pursue any or all of these opportunities, and others that may present themselves. In doing so the Company may incur term debt, issue equity, and retain cash that might otherwise be paid as dividends or any combination of the foregoing.

### **DISCLOSURE CONTROLS AND PROCEDURES**

As defined in Multilateral Instrument 52-109, disclosure controls and procedures require that controls and other procedures be designed to provide reasonable assurance that financial and non-financial information required to be disclosed is duly recorded, processed, summarized, accumulated and communicated to management. It must be disclosed on a timely basis and be in accordance with provincial and territorial securities legislation.

The Company has designed and evaluated the effectiveness of its disclosure controls and procedures, as defined, and has concluded they were effective as of the end of the period covered by this report.