



Cathedral

Energy Services Income Trust

2007 Q2 INTERIM REPORT

FINANCIAL HIGHLIGHTS

\$ in '000's except per Trust Unit amounts

	Three months ended		Six months ended	
	June 30		June 30	
	2007	2006	2007	2006
Revenues	\$ 24,985	\$ 26,204	\$ 67,697	\$ 64,886
EBITDA ⁽¹⁾	\$ 4,837	\$ 8,370	\$ 19,249	\$ 23,737
Per Trust Unit – diluted	\$ 0.15	\$ 0.27	\$ 0.61	\$ 0.76
Income before taxes	\$ 1,112	\$ 5,033	\$ 12,145	\$ 17,435
Net Income (loss)	\$ (2,415)	\$ 4,963	\$ 7,372	\$ 15,825
Per Trust Unit – basic	\$ (0.08)	\$ 0.16	\$ 0.24	\$ 0.52
Per Trust Unit – diluted	\$ (0.08)	\$ 0.16	\$ 0.23	\$ 0.50
Cash distributions declared per Trust Unit	\$ 0.21	\$ 0.185	\$ 0.42	\$ 0.345
Distributable income ⁽²⁾	\$ 3,132	\$ 6,251	\$ 16,203	\$ 20,472
Cash distributions declared	\$ 6,600	\$ 5,667	\$ 13,130	\$ 10,505
Payout ratio ⁽³⁾	211%	91%	81%	51%
Property and equipment additions and corporate acquisitions:				
Paid or payable in cash	\$ 4,483	\$ 6,255	\$ 10,288	\$ 15,038
Paid or payable in Trust Units	-	-	-	1,500
	<u>\$ 4,483</u>	<u>\$ 6,255</u>	<u>\$ 10,288</u>	<u>\$ 16,538</u>
Weighted average Trust Units outstanding:				
Basic ('000)	31,405	30,595	31,219	30,372
Diluted ('000)	31,893	31,438	31,744	31,339

	June 30 2007	December 31 2006
Working capital	\$10,795	\$15,051
Long-term debt and capital lease obligations excluding current portion	\$15,543	\$15,552
Unitholders' equity	\$73,690	\$76,223

⁽¹⁾ EBITDA is defined as earnings before interest on long-term debt and capital lease obligations, taxes, non-cash compensation expense and depreciation and amortization and is provided to assist investors in determining the ability of the Trust to generate cash from operations. EBITDA does not have any standardized meaning within Canadian Generally Accepted Accounting Principles and therefore may not be comparable to similar measures presented by other companies and/or trusts.

⁽²⁾ Distributable income is defined as funds from operations before changes in non-cash working capital less required principal repayments on long-term debt and capital lease obligations and maintenance capital expenditures. Distributable income does not have any standardized meaning within Canadian Generally Accepted Accounting Policies and therefore may not be comparable to similar measures presented by other trusts. Distributable income is a main performance measurement used by management and investors to evaluate the performance of the Trust.

⁽³⁾ Cash distributions declared as a percentage of distributable income.

MANAGEMENT'S DISCUSSION & ANALYSIS

This Management's Discussion & Analysis ("MD&A") for the three and six months ended June 30, 2007 should be read in conjunction with the annual audited consolidated financial statements and notes thereto for the year ended December 31, 2006, as well as the MD&A in the Trust's 2006 Annual Report, and with the unaudited interim consolidated financial statements for the three months and six months ended June 30, 2007. This MD&A has been prepared as of August 2, 2007. Dollar amounts are in '000's except for day rates and per Trust Unit amounts.

FORWARD-LOOKING INFORMATION

Certain statements in this MD&A including (i) statements that may contain words such as "anticipate", "could", "expect", "seek", "may", "intend", "will", "believe", "should", "project", "forecast", "plan" and similar expressions, including the negatives thereof, (ii) statements that are based on current expectations and estimates about the markets in which the Trust/Cathedral operates and (iii) statements of belief, intentions and expectations about developments, results and events that will or may occur in the future, constitute "forward-looking statements" and are based on certain assumptions and analysis made by the Trust/Cathedral. Forward-looking statements in this MD&A include, but are not limited to, statements with respect to future capital expenditures, including the amount, nature and timing thereof; oil and natural gas prices and demand; other development trends within the oil and natural gas industry; business strategy; expansion and growth of the Trust's/Cathedral's business and operations and other such matters. Such forward-looking statements are subject to important risks and uncertainties, which are difficult to predict and that may affect the Trust's/Cathedral's operations, including, but are not limited to: the impact of general economic conditions; industry conditions; government and regulatory developments; oil and natural gas product supply and demand; competition; and the Trust's/Cathedral's ability to attract and retain qualified personnel. The Trust's/Cathedral's actual results, performance or achievements could differ materially from those expressed in, or implied by, these forward-looking statements and, accordingly, no assurance can be given that any of the events anticipated by the forward-looking statements will transpire or occur, or if any of them do transpire or occur, what benefits the Trust/Cathedral will derive therefrom. Subject to applicable law, the Trust disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

All forward-looking statements contained in this document are expressly qualified by this cautionary statement. Further information about the factors affecting forward-looking statements is available in the Trust's current Annual Information Form and Annual Report which have been filed with Canadian provincial securities commissions and are available on www.sedar.com.

NON-GAAP FINANCIAL MEASUREMENTS

This MD&A refers to certain financial measurements that do not have any standardized meaning within Canadian Generally Accepted Accounting Principles ("GAAP") and therefore may not be comparable to similar measures provided by other companies and/or trusts. These measures are provided to assist investors in determining the Trust's ability to generate cash from operations and to provide additional information regarding the use of its cash resources. The specific measures being referred to include the following i) "EBITDA" - defined as earnings before interest on long-term debt and capital lease obligations, taxes, non-cash compensation expense and depreciation and amortization; ii) "distributable income" - defined as cash flow from operations before changes in non-cash working capital less required principal repayments on long-term debt and capital lease obligations and maintenance capital expenditures; iii) "gross margin" - calculated as revenues less operating expenses; iv) "maintenance capital expenditures" - refers to capital expenditures required to maintain existing levels of service but excludes replacement cost of lost-in-hole equipment to the extent the replacement equipment is financed from the proceeds on disposal of the equipment lost-in-hole; and v) "payout ratio" - calculated as cash distributions declared divided by distributable income.

OVERVIEW

Despite a significant decline in drilling activity in western Canada, the Trust was able to increase revenues on a Q2 year-to-date basis from \$64,886 in 2006 to \$67,697 in 2007 – 4.3% increase. The major items contributing to these results have been the strong performance of the U.S. operations, exposure to drilling for oil, particularly in southeastern Saskatchewan, and the provision of specialty directional drilling services that has resulted in an increase in the average day rate obtained for such services. For Q2, revenues declined \$1,219 or 4.7% from \$26,204 in 2006 to \$24,985 in 2007. EBITDA for the six months ended June 30, 2007 was \$19,249 which compares to \$23,737 in 2006 - an 18.9% decrease. As a result of recording a non-cash \$3,318 (\$0.10 per diluted Trust Unit) provision for future income taxes related to the tax legislation included in Bill C-52, the Budget Implementation Act, 2007 (the "Bill"), that was substantively enacted in 2007 Q2 which results in the taxation of existing income and royalty trusts, other than real estate investment trusts, at effective rates similar to Canadian corporations, the Trust incurred a net loss for 2007 Q2 of \$2,415 or \$0.08 per diluted Trust Unit (2006 net income was \$4,963 or \$0.16 per diluted Trust Unit). On a 2007 Q2 year-to-date basis, the Trust's net income was \$7,372 (\$0.23 per diluted Trust Unit) which compares to \$15,825 (\$0.50 per diluted Trust Unit) in 2006.

RESULTS OF OPERATIONS - THREE MONTHS ENDED JUNE 30, 2007

Revenues Traditionally, Q2 results are affected by seasonal fluctuations related to spring break-up. In 2007 Q2, the seasonality factor was further impacted by lower Canadian drilling activity as a result of concerns related to natural gas commodity prices. Continued strength in the directional drilling portion of the Trust's operations resulted in 2007 Q2 revenues of \$20,453 from the directional drilling division. Directional drilling activity days decreased 5.8% or 134 to 2,194, however the average day rate received for providing directional drilling services increased 10.1% on a quarter-over-quarter basis to \$9,160 (2006 - \$8,322). The largest portion of the increase in the average day rate is related to a shift towards providing premium services such as underbalanced and Steam-Assisted Gravity Drainage ("SAGD") drilling services as opposed to an increase in the overall base day rate. In the Canadian market the Trust's 2007 Q2 activity levels decreased by



16% which was significantly less than the overall decline in drilling activity in the Canadian market. Despite the decline in natural gas drilling in western Canada, the Trust was able to minimize the market decline from prior year activity levels due to the continuing strength of the Trust's client base and involvement in multi-well programs. The Rocky Mountain region of the United States remains a very active area and the Trust's U.S. operations have now been expanded into North Dakota. The Trust's revenues from the U.S. were \$9,640 in 2007 Q2, which represents an increase of \$1,139 or 13.4% on a quarter-over-quarter basis. Due to demand in the U.S. market, 5 Measurement-While-Drilling ("MWD") systems were transferred to the U.S. at the end of Q1 and the Trust now has 23 MWD systems in the U.S. market. The Trust's geographic diversification, by way of providing directional drilling services in southeast Saskatchewan and U.S., has been a significant factor in its ability to organically grow its revenues within the directional division.

The continued decline in natural gas drilling expenditures in the western Canada market resulted in lower revenues for both of the Trust's production testing and wireline divisions. The Trust's production testing division, Tier One, contributed \$1,340 in revenues during 2007 Q2 which is a 39.9% decline from 2006 Q2 revenues. Advance Wireline and Xtreme Wireline combined to generate revenues of \$3,079 for 2007 Q2 compared to \$4,228 for 2006 Q2, a 27.2% quarter-over-quarter decline. Late in 2007 Q2, one wireline unit was transferred from the Canadian operations to the newly formed U.S. division of Advance Wireline but revenue generating operations did not commence until 2007 Q3. A second wireline unit will be transferred to the U.S. operation in mid 2007 Q3.

Gross margin The gross margin for 2007 Q2 was 44.2% which compares to 50.2% in 2006 Q2. The decrease is attributed to a number of factors including: i) shift to providing more horizontal drilling services (versus directional) which provide a lower gross margin than from directional drilling; ii) increases in directional field labour rates; iii) increase in wireline field labour costs as a percentage of revenues due to the continuation of the Trust's build out of its wireline fleet and related field staff that will enable the Trust to take advantage of increased activity levels; and iv) offsetting the previous items was an increase in the average day rate for directional drilling services.

General and administrative expenses General and administrative expenses increased from \$5,311 in 2006 Q2 to \$6,082 in 2007 Q2 – an increase of \$771. The increase was primarily related to increased personnel and office/shop rental costs. As a percentage of revenues, general and administrative expenses were 24.3% in 2007 Q2 and 20.3% in 2006

Depreciation and amortization Depreciation for 2007 Q2 was \$2,943 which compares to \$2,577 in 2006 Q2. This increase is related to expansion of the Trust's depreciable asset base over the past 12 months. As a percentage of revenues, depreciation amounted to 11.8% for 2007 and 9.8% for 2006.

Interest expense Interest expense related to long-term debt and capital leases increased from \$226 in 2006 Q2 to \$260 in Q2 2007 due to the combined net effect of: i) an increase in the average level of debt outstanding; and ii) a decrease in the effective interest rate on the related debt.

Foreign exchange The Trust's foreign exchange loss increased from \$66 in 2006 Q2 to \$237 in 2007 Q2. The increased foreign exchange loss is due to: i) the U.S. dollar weakening against the Canadian dollar to a larger extent in 2007 Q2 versus 2006 Q2; and ii) an overall increase in the Trust's U.S. operations which has resulted in an increase in the Trust's net monetary assets that are denominated in U.S. dollars.

Non-cash compensation expense For 2007 Q2 the Trust had non-cash compensation expense of \$522 which compares to \$534 for the comparable quarter in 2006. The value of Trust Unit options is being amortized against income over their three-year vesting period.

Gain on disposal of property and equipment During 2007 Q2 the Trust had a gain on disposal of property and equipment of \$187, which compares to \$710 in 2006 Q2. These gains are mainly due to recoveries of lost-in-hole equipment costs including previously expensed depreciation on the related assets. The timing of lost-in-hole recoveries is not in the control of the Trust and therefore can fluctuate significantly from quarter-to-quarter.

Taxes In 2007 Q2 tax legislation included in Bill C-52, the Budget Implementation Act, 2007 (the "Bill"), was substantively enacted and this will result in the taxation of existing income and royalty trusts, other than real estate investment trusts, at effective rates similar to Canadian corporations. Substantive enactment of the Bill resulted in the recognition of future income tax amounts based on estimated net taxable temporary differences of \$10,533 which are expect to reverse after 2010 and for which no tax has previously been recorded in the Trust's financial statements. Accordingly, a non-cash future income tax expense and net future income tax liability of \$3,318 (\$0.10 per diluted Trust Unit) were recognized in 2007 Q2. In the Trust's 2007 Q1 MD&A this amount was estimated to be approximately \$3,800.

RESULTS OF OPERATIONS – SIX MONTHS ENDED JUNE 30, 2007

Revenues 2007 Q2 year-to-date revenues were \$67,697 which represented an increase of \$2,811 or 4.3% over 2006 Q2 year-to-date revenues of \$64,886. Ongoing activity reductions in the Canadian markets were offset by continued growth and expansion in the U.S. operations.

The directional drilling division revenues have increased from \$43,946 in 2006 to \$50,387 in 2007. This increase is the result of: i) an increase in activity days from 5,310 in 2006 to 5,517 in 2007; and ii) an increase in the average day rate from \$8,275 in 2006 to \$9,134 in 2007. The decrease in Canadian activity days from 3,435 to 3,194 were more than offset by the growth in U.S. activity days from 1,875 to 2,323. The U.S. Q2 year-to-date revenues increased from \$15,361 in 2006 to \$20,363 in 2007, a 32.6% increase.

The continued decline in natural gas drilling expenditures in the western Canada market resulted in lower revenues for both of the Trust's production testing and wireline divisions. The Trust's production testing division, Tier One, contributed \$5,806 in revenues during 2007 Q2



year-to-date which is a 21.3% decline from 2006 revenues of \$7,382. Advance Wireline and Xtreme Wireline combined to generate revenues of \$10,145 for 2007 Q2 year-to-date which compares to \$12,417 for 2006 which represents an 18.3% decline.

Gross margin The gross margin (revenues less operating expenses) for 2007 was 48.0%, which compares to 52.2% in 2006. The decrease is attributed to a number of factors including: i) shift to providing more horizontal drilling services (versus directional) which provide a lower gross margin than from directional drilling; ii) increases in directional field labour rates; iii) increase in wireline field labour costs as a percentage of revenues due to the continuation of the Trust's build out of its wireline fleet and related field staff that will enable the Trust to take advantage of increased activity levels; and iv) offsetting the previous items was an increase in the average day rate for directional drilling services.

General and administrative expenses General and administrative expenses increased from \$10,573 in 2006 to \$13,014 in 2007 – an increase of \$2,441. The increase was related to the Trust's directional/horizontal drilling business and the contributing factors to that increase were the result of increased personnel and office/shop rental costs as well as an overall increase in directional drilling activity levels both in western Canada and the Rocky Mountain region of the U.S. As a percentage of revenues, general and administrative expenses were 19.2% in 2007 and 16.3% in 2006.

Depreciation and amortization Depreciation and amortization for 2007 was \$5,699 compared to \$4,906 in 2006. The \$793 increase is related to the Trust's investment in property and equipment over the past 12 months. As a percentage of revenues, depreciation and amortization amounted to 8.4% for 2007 and 7.6% for 2006.

Interest expense Interest on long-term debt has increased from \$436 in 2006 to \$523 in 2007. The major factor contributing to this increase is that late in 2006 Q3 the Trust accessed an additional \$3,000 of its available non-reducing revolving term loan facility; proceeds of which were used to finance the Trust's acquisition of land and buildings. Other interest expense has increased mainly due to the increased utilization of the Trust's operating line of credit.

Foreign exchange The Trust's foreign exchange loss has increased from \$58 in 2006 to \$284 in 2007. The increased foreign exchange loss is due to: i) the U.S. dollar weakening against the Canadian dollar to a larger extent in 2007 Q2 versus 2006 Q2; and ii) an overall increase in the Trust's U.S. operations which has resulted in an increase in the Trust's net monetary assets that are denominated in U.S. dollars.

Non-cash compensation expense Non-cash compensation expense for 2007 was \$882 which compares to \$960 in 2006. The Trust Unit options granted are valued using the Black-Scholes option pricing model and such value is being amortized against income over their three-year vesting period.

Gain on disposal of property and equipment During 2007 Q2 YTD the Trust had a gain on disposal of property and equipment of \$184 which compares to \$710 in 2006. These gains are mainly due to recoveries of lost-in-hole equipment costs, including previously expensed depreciation on the related assets. The timing of lost-in-hole recoveries is not in the control of the Trust and therefore can fluctuate significantly from quarter-to-quarter and year-to-year basis.

Taxes For 2007, the Trust had a tax expense of \$4,773 (effective tax rate of 39.3%) which compares to \$1,610 (effective tax rate of 9.2%) in 2006. As noted in the above discussion under the result of operations for the three months ended June 30, 2007, the 2007 Q2 tax provision includes a non-cash adjustment of \$3,318 (\$0.10 per diluted Trust Unit) related to the substantive enactment of the previously announced changes to the taxation of income and royalty trusts, other than real estate investment trusts. Removing the 2007 Q2 adjustment noted above the effective tax rate for 2007 Q2 year-to-date is 12.0% which is higher than the 2006 effective tax rate of 9.2% due to the continuing growth in the U.S. operations which are taxed at a higher rate.

LIQUIDITY AND CAPITAL RESOURCES

The Trust's principal source of liquidity is cash generated from operations. The Trust also has the ability to fund liquidity requirements through its credit facility and the issuance of debt and/or equity. At June 30, 2007, the Trust had an operating line of credit with a major Canadian bank in the amount of \$12,500 (December 31, 2006 - \$12,500) of which \$2,230 (December 31, 2006 - \$6,460) was drawn. In addition, the Trust has a non-reducing revolving term loan facility in the amount of \$25,000 (December 31, 2006 - \$25,000) of which \$15,000 (December 31, 2006 - \$15,000) was drawn as at June 30, 2007. In addition, at June 30, 2007 the Trust had obligations under capital leases in the amount of \$545 (December 31, 2006 - \$664) and other long-term debt of \$271 (December 31, 2006 - \$171).

Operating activities Cash flow from operating activities for the three and six months ended June 30, 2007 was \$14,297 (2006 - \$13,645) and \$24,073 (2006 - \$21,782) respectively. The Trust has a strong working capital position at June 30, 2007 at \$10,795 which compares to \$15,051 at December 31, 2006.

Investing activities Cash used in investing activities for the three and six months ended June 30, 2007 amounted to \$5,320 and \$8,346, respectively which compares to \$7,191 and \$14,841 for the same period in 2006. During 2007 Q2 the Trust invested an additional \$4,483 (2006 - \$6,255) for a total Q2 year-to-date \$10,288 (2006 - \$15,038) increase in property and equipment. For 2007 Q2 the major items added to property and equipment were 5 MWD systems, expansion of mud motor and drilling collar fleet, progress payments on upgrade of low pressure production testing units to higher pressure units and the addition of 3 slickline units. At June 30, 2007, the Trust's operating entities had 73 MWD systems, 19 production testing units and 28 wireline units. All of the 2007 Q2 year-to-date additions to property and equipment have been financed from cash flow from operations except for \$173 of automotive equipment additions. Fluctuations in non-cash working capital related to investing activities are a function of when proceeds on disposal of property and equipment are received and when payments for property and equipment purchases are made.



Financing activities Cash used in financing activities for the three and six months ended June 30, 2007 amounted to \$9,670 and \$16,500, respectively, which compares to \$4,876 and \$6,847 for the same periods in 2006. Distributions paid to Unitholders for 2007 Q2 amounted to \$6,585 (2006 – \$5,502) bringing year-to-date distributions for the six months ended June 30, 2007 to \$14,642 (2006 – \$10,014). The increase in distributions paid are related to a combination of: i) increases in the per Trust Unit “regular” distribution level; ii) the payment of a “special” \$0.05 per Trust Unit cash distribution declared in December 2006 (\$1,549) and payable January 15, 2007; and iii) an increase in the number of Trust Units outstanding. Since January 2006 the Trust has increased its per Trust Unit distribution level from \$0.05 per Trust Unit to \$0.07 per Trust Unit for June 2007 – a 40% increase. Cash distributions paid have been financed from cash flow from operations and management currently expects future cash distributions will also be financed from cash flow from operations. For the six months ended June 30, 2007 financing cash inflows resulted from: i) \$2,392 (2006 - \$2,394) cash received on the exercise of Trust Unit options, and ii) an \$173 increase in new long-term debt. Offsetting these inflows were cash outflows of: i) a \$4,230 reduction in bank indebtedness (2006 – cash provided by bank indebtedness was \$1,110); and ii) a \$193 (2006 - \$337) repayment of long-term debt and capital lease obligations. At August 2, 2007, the Trust had 31,499,350 Trust Units and 2,395,173 Trust Unit options outstanding.

Contractual obligations In the normal course of business, the Trust incurs contractual obligations and those obligations are disclosed in the Trust’s MD&A for the year ended December 31, 2006. As at June 30, 2007 the Trust’s commitment to purchase property and equipment is approximately \$5,236. Included in this commitment is \$3,360 related to the cost of building a new mud motor repair facility in Nisku, Alberta of which approximately \$3,000 is expected to be financed by way of a draw on the Trust’s non-reducing revolving term loan facility. The remaining commitments are expected to be financed from cash flows from operations.

CONTROLS AND PROCEDURES

Management is responsible for establishing and maintaining adequate disclosure controls and internal control over financial reporting. Internal control over financial reporting is a process designed to provide reasonable, but not absolute, assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external reporting purposes in accordance with GAAP. Internal control over financial reporting may not prevent or detect fraud or misstatements because of limitations inherent in any system of internal control. There were no significant changes in the design or effectiveness of the Trust’s disclosure controls or internal controls over financial reporting in the second quarter of 2007.

CHANGES IN ACCOUNTING POLICIES

Effective January 1, 2007, The Trust adopted the Canadian Institute of Chartered Accountants (“CICA”) section 3855, “Financial Instruments – Recognition and Measurement”, section 3865, “Hedges”, and section 1530, “Comprehensive Income”. These standards have been adopted prospectively. For the 6 months ended June 30, 2007, the adoption of these standards did not have an effect on the Trust’s consolidated financial statements. A general summary of these accounting standards were included in the Trust’s 2006 annual MD&A.

BUSINESS RISKS

The MD&A for the year ended December 31, 2006, which is included in the Trust’s 2006 Annual Report, includes an overview on business risks associated with the Trust and its operating entities. Those business risks remain in effect as at June 30, 2007.

DISTRIBUTABLE INCOME

Distributable income is calculated as follows:

	Three months ended June 30		Six months ended June 30	
	2007	2006	2007	2006
Cash flows from operating activities	\$14,297	\$13,645	\$ 24,073	\$ 21,782
Add: - changes in non-cash operating working capital ⁽¹⁾	(11,071)	(7,193)	(7,683)	(814)
Less: - required principal repayments on long-term debt and capital lease obligations	(83)	(157)	(176)	(337)
- maintenance capital expenditures	(11)	(44)	(11)	(159)
Distributable income	\$ 3,132	\$ 6,251	\$ 16,203	\$ 20,472
Cash distributions declared	\$ 6,600	\$ 5,667	\$ 13,130	\$ 10,505
Payout ratio	211%	91%	81%	51%

⁽¹⁾ Changes in non-cash operating working capital have been added back as such changes are financed using the Trust’s bank indebtedness/line of credit facility. In addition, if changes in non-cash operating capital were excluded it would introduce cash flow variability and affect underlying cash flow from operating activities.

Cathedral’s operations in western Canada are subject to seasonality as activity levels in the oilfield services industry are generally lower during “spring breakup” which normally commences in late March and continues through to May. It is the Trust’s policy to pay consistent distributions throughout the year despite the seasonality of a portion of Cathedral’s business.

As a result of the Trust’s equipment being relatively new and the extensive maintenance program for its equipment (such repairs and maintenance cost are expensed in operating expenses), expenditures for maintenance capital are currently minimal. Current maintenance capital expenditure levels may not be indicative of future maintenance capital expenditure levels.



The Administrator of the Trust (Cathedral Energy Services Ltd.) reviews the level and nature of distributions on an on-going basis giving consideration to current performance, historical and future trends in the business and the expected sustainability of those trends as well as required long-term debt repayments, maintenance capital expenditures required to sustain performance and future growth capital expenditures. Currently cash distributions declared are less than distributable income as the Trustees, on the recommendation of management of the Administrator, have decided to retain a portion of distributable income to finance capital expenditures and debt repayment. It is not management's intent to distribute 100% of distributable income. Distributable income is not a standardized measure under Canadian GAAP and distributable income cannot be assured. The Trust's calculation of distributable income may differ from similarly titled measures used by other trusts. Distributable income is a main performance measurement used by management and investors to evaluate the performance of the Trust.

EBITDA:

EBITDA is calculated as follows:

	Three months ended June 30		Six months ended June 30	
	2007	2006	2007	2006
EBITDA as reported	\$ 4,837	\$ 8,370	\$19,249	\$23,737
Deduct: - depreciation and amortization	2,943	2,577	5,699	4,906
- interest – long-term debt and capital lease obligations	260	226	523	436
- non-cash compensation expense	522	534	882	960
- provision for taxes	3,527	70	4,773	1,610
Net income (loss) for the period	\$ (2,415)	\$ 4,963	\$ 7,372	\$15,825

GOVERNANCE

The Audit Committee of the Board of Directors of the Administrator has reviewed this MD&A and the related unaudited interim consolidated financial statements and recommended they be approved to the Board of Directors. Following a review by the full Board, the MD&A and financial statements were approved.

OUTLOOK

Industry analysts continue to forecast strong oil prices for the balance of 2007 and into 2008 but a significant amount of uncertainty exists with respect to the timing of a rebound in natural gas prices. This uncertainty has created a situation in which producers (in particular, Canadian producers) have reconsidered the current economics of drilling natural gas wells which in turn has resulted in the significant decline in drilling activity in western Canada on a year-over-year basis.

During Q3 the Trust expects to add 5 MWD systems to its Canadian fleet to replace the systems transferred to the U.S. On the technology forefront we continue to push forward the development of our 2nd generation Electro-Magnetic ("EM") MWD system and initial field testing during 2007 Q2 was very successful. The 2nd generation EM-MWD system will increase the tools capabilities by allowing it to operate at deeper levels and at lower operating costs.

The Trust's wireline and production testing divisions have been affected by the decline in drilling activity in western Canada and a rebound in their revenue generation ability will be tied to natural gas prices. During 2007 Q3 the Trust's new formed U.S. wireline operations will start to produce revenues and a second wireline unit will be transferred from the Canadian wireline fleet to the U.S. operations in mid August 2007. On the production testing side of the Trust's business, we continue to expand into the high-end testing market including critical sour service work.

With the capital expenditure budget for 2007 the Trust expects to exit 2007 with 78 MWD systems, 28 wireline units and 19 production testing units.

The Trust continues to actively pursue opportunities to offer an expanded range of services to its customers, increase its market share, enter new geographic territories, and make strategic acquisitions.



SUMMARY OF QUARTERLY RESULTS

Three month period ended (\$ in 000's except per Trust Unit amounts)	June 2007	Mar 2007	Dec 2006	Sep 2006	Jun 2006	Mar 2006	Dec 2005	Sept 2005
Revenues	\$ 24,985	\$42,712	\$35,327	\$38,041	\$26,204	\$38,682	\$32,101	\$22,826
EBITDA	4,837	14,412	13,046	16,010	8,370	15,367	12,090	9,026
Net income (loss)	(2,415)	9,787	8,127	11,396	4,963	10,862	7,762	6,179
Net income (loss) per Trust Unit – basic	(0.08)	0.32	0.26	0.37	0.16	0.36	0.26	0.21
Net Income (loss) per Trust Unit – diluted	(0.08)	0.31	0.26	0.36	0.16	0.35	0.25	0.21
Cash distributions declared per Trust Unit	0.21	0.21	0.26	0.20	0.185	0.16	0.1375	0.0925

CONSOLIDATED BALANCE SHEETS

\$ in 000's

	June 30 2007 (unaudited)	December 31 2006
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 781	\$ 1,554
Accounts receivable	25,923	37,693
Inventory	3,810	3,050
Prepaid expenses and deposits	572	892
	31,086	43,189
Property and equipment	65,820	61,488
Intangibles	662	736
Goodwill	19,775	19,775
Other assets	110	33
	\$ 117,453	\$ 125,221
LIABILITIES AND UNITHOLDERS' EQUITY		
Current liabilities:		
Bank Indebtedness	\$ 2,230	\$ 6,460
Accounts payable and accrued liabilities	15,295	16,446
Distribution payable to Unitholders	2,204	3,717
Taxes payable	289	1,232
Current portion of capital lease obligations	193	212
Current portion of long-term debt	80	71
	20,291	28,138
Capital lease obligations	352	452
Long-term debt	15,191	15,100
Future income taxes (note 4)	7,929	5,308
	43,763	48,998
Unitholders' equity (note 5):		
Unitholders' capital	47,326	44,667
Contributed surplus	1,728	1,162
Retained earnings	24,636	30,394
	73,690	76,223
	\$ 117,453	\$ 125,221



CONSOLIDATED STATEMENTS OF OPERATIONS AND RETAINED EARNINGS

\$ in 000's except per Trust Unit amounts
(unaudited)

	Three months ended June 30		Six months ended June 30	
	2007	2006	2007	2006
Revenues	\$ 24,985	\$ 26,204	\$ 67,697	\$ 64,886
Expenses :				
Operating	13,950	13,042	35,172	31,020
General and administrative	6,082	5,311	13,014	10,573
Depreciation and amortization	2,943	2,577	5,699	4,906
Interest – long-term debt and capital lease obligations	260	226	523	436
Interest – other	66	125	162	208
Foreign exchange loss	237	66	284	58
Non-cash compensation expense	522	534	882	960
	24,060	21,881	55,736	48,161
	925	4,323	11,961	16,725
Gain on disposal of property and equipment	187	710	184	710
Income before taxes	1,112	5,033	12,145	17,435
Taxes:				
Current	1,062	946	2,050	1,581
Future (reduction) (note 4)	2,465	(876)	2,723	29
	3,527	70	4,773	1,610
Net income (loss) for the period	(2,415)	4,963	7,372	15,825
Retained earnings, beginning of period	33,651	27,789	30,394	21,765
Less: Distributions declared	(6,600)	(5,667)	(13,130)	(10,505)
Retained earnings, end of period	\$ 24,636	\$ 27,085	\$ 24,636	\$ 27,085
Net income (loss) per Trust Unit:				
Basic	\$ (0.08)	\$ 0.16	\$ 0.24	\$ 0.52
Diluted	\$ (0.08)	\$ 0.16	\$ 0.23	\$ 0.50

CONSOLIDATED STATEMENTS OF CASH FLOWS

\$ in 000's
(unaudited)

	Three months ended June 30		Six months ended June 30	
	2007	2006	2007	2006
Cash provided by (used in):				
Operating activities:				
Net income (loss) for the period	\$ (2,415)	\$ 4,963	\$ 7,372	\$ 15,825
Items not involving cash:				
Depreciation and amortization	2,943	2,577	5,699	4,906
Future taxes (reduction) (note 4)	2,465	(876)	2,723	29
Unrealized foreign exchange gain	(102)	(36)	(102)	(42)
Non-cash compensation expense	522	534	882	960
Gain on disposal of property and equipment	(187)	(710)	(184)	(710)
	3,226	6,452	16,390	20,968
Changes in non-cash operating working capital	11,071	7,193	7,683	814
	14,297	13,645	24,073	21,782
Investing activities:				
Property and equipment additions	(4,483)	(6,255)	(10,288)	(15,038)
Proceeds on disposal of property and equipment	490	1,219	514	1,219
Expenditure on other assets	(110)	-	(110)	-
Changes in non-cash investing working capital	(1,217)	(2,155)	1,538	(1,022)
	(5,320)	(7,191)	(8,346)	(14,841)
Financing activities:				
Distributions paid to Unitholders	(6,585)	(5,502)	(14,642)	(10,014)
Advances under long-term debt	-	-	173	-
Repayment of long-term debt	(27)	(79)	(73)	(155)
Repayment of capital lease obligations	(56)	(78)	(120)	(182)
Proceeds on exercise of Trust Unit options	1,033	868	2,392	2,394
Increase (decrease) in bank indebtedness	(4,035)	(85)	(4,230)	1,110
	(9,670)	(4,876)	(16,500)	(6,847)
Change in cash and cash equivalents	(693)	1,578	(773)	94
Cash and cash equivalents, beginning of period	1,474	607	1,554	2,091
Cash and cash equivalents, end of period	\$ 781	\$ 2,185	\$ 781	\$ 2,185

SELECTED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Three and six months ended June 30, 2007 and 2006

(\$ in 000's except per Trust Unit amounts)

(unaudited)

1. Significant accounting policies:

These unaudited interim consolidated financial statements for the period ended June 30, 2007 do not include all disclosures required in the annual financial statements and should be read in conjunction with the annual consolidated financial statements and notes thereto for the year ended December 31, 2006 included in the Trust's 2006 Annual Report. These unaudited interim consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles and using the same accounting policies as outlined in note 2 of the annual consolidated financial statements for the year ended December 31, 2006 except for the new accounting policies described in note 2.

2. New accounting policies:

Effective January 1, 2007, The Trust adopted the Canadian Institute of Chartered Accountants ("CICA") section 3855, "Financial Instruments – Recognition and Measurement", section 3865, "Hedges", and section 1530, "Comprehensive Income". These standards have been adopted prospectively. For the 3 and 6 months ended June 30, 2007, the adoption of these standards did not have an effect on the Trust's consolidated financial statements.

3. Seasonality of operations:

The majority of Cathedral's operations are carried on in western Canada where activity levels in the oilfield services industry are subject to a degree of seasonality. Operating activities in western Canada are generally lower during "spring breakup" which normally commences in late March and continues through to May. Operating activities generally increase in the fall and peak in the winter months from December till late March. Activity levels in the Rocky Mountain region of the U.S. are not subject the seasonality to the extent that it occurs in the western Canada region.

4. Taxes:

In 2007 Q2 tax legislation included in Bill C-52, the Budget Implementation Act, 2007 (the "Bill"), was substantively enacted and this will result in the taxation of existing income and royalty trusts, other than real estate investment trusts, at effective rates similar to Canadian corporations. Substantive enactment of the Bill resulted in the recognition of future income tax amounts based on estimated net taxable temporary differences of \$10,533 which are expect to reverse after 2010 and for which no tax has previously been recorded in the Trust's financial statements. Accordingly, a future income tax expense and a net future income tax liability of \$3,318 were recognized in 2007 Q2.

5. Unitholders' equity:

(a) Issued Unitholders capital:

	Three months ended June 30, 2007		Six months ended June 30, 2007	
	Number of Trust Units	Amount	Number of Trust Units	Amount
Balance, beginning of period	31,287,041	\$ 46,026	30,970,979	\$ 44,667
Issued on exercise of options	197,506	1,033	513,568	2,392
Contributed surplus on options exercised		267		267
Balance, end of period	31,484,547	\$ 47,326	31,484,547	\$ 47,326

(b) Contributed surplus:

	Three months ended June 30, 2007	Six months ended June 30, 2007
Balance, beginning of period	\$ 1,497	\$ 1,162
Non-cash compensation expense related to Trust Unit option plan	498	833
Less: contributed surplus on options exercised	(267)	(267)
Balance, end of period	\$ 1,728	\$ 1,728



5. Unitholders' equity (continued):

(c) Trust Unit options:

	Three months ended June 30, 2007	Six months ended June 30, 2007
Outstanding, beginning of period	2,631,482	2,869,544
Issued	-	78,000
Forfeited	(12,000)	(12,000)
Exercised	(197,506)	(513,568)
Outstanding, end of period	2,421,976	2,421,976

(d) Trust Unit options:

During the six months ended June, 2007, 78,000 Trust Unit options were granted at an exercise price of \$10.44 and the fair value of these options was \$1.77 per option using the Black-Scholes option pricing method. The following table sets out the assumptions used in applying the Black-Scholes model:

	Date of Issue March 9, 2007
Expected distribution yield	8.05%
Risk-free interest rate	3.94%
Expected volatility	37%
Expected life (in years)	3.5

(e) Retained earnings:

Retained earnings is comprised of the following items:

	June 30 2007	December 31 2006
Accumulated income	\$ 91,869	\$ 84,497
Less: accumulated distributions	(67,233)	(54,103)
	\$ 24,636	\$ 30,394

6. Segmented information:

The Trust, through its directly and indirectly wholly-owned entities, Cathedral Energy Services Ltd. and Cathedral Energy Services Limited Partnership, is engaged in the business of providing selected oilfield services to oil and natural gas exploration entities in western Canada and the Rocky Mountain region of the United States and is viewed as a single operating segment by the chief operating decision maker of Cathedral Energy Services Ltd. for the purpose of resource allocation and assessing performance. Oilfield services are provided in both Canada and the United States. The amounts related to each geographic segment are as follows:

Revenues	Three months ended June 30		Six months ended June 30	
	2007	2006	2007	2006
Canada	\$ 15,345	\$ 17,703	\$ 47,334	\$ 49,525
United States	9,640	8,501	20,363	15,361
	\$ 24,985	\$ 26,204	\$ 67,697	\$ 64,886

Property and equipment, intangibles and goodwill	June 30 2007	December 31 2006
Canada	\$ 74,019	\$ 71,100
United States	12,238	10,899
	\$ 86,257	\$ 81,999

During the three months ended June 30, 2007 one customer accounted for 33% of consolidated revenues (2006 – 19%). During the six months ended June 30, 2007, one customer accounted for 26% (2006 – 15%) of consolidated revenues.



7. Commitments:

In the normal course of business, the Trust incurs contractual obligations and those obligations are disclosed in the Trust's annual financial statements for the year ended December 31, 2006. As at June 30, 2007, the Trust's commitment to purchase property and equipment is approximately \$5,236.

8. Comparative amounts:

Certain comparative amounts have been reclassified to conform to the current year's presentation.

*Cathedral Energy Services Income Trust is a limited purpose trust which owns the securities of Cathedral Energy Services Ltd. and Cathedral Energy Services Limited Partnership (collectively "Cathedral") representing the right to receive cash flow available for distribution from Cathedral. Cathedral is engaged in the business of providing selected oilfield services to oil and natural gas companies in western Canada and the Rocky Mountain region of the United States and currently provides drilling services and related equipment rentals, production testing services and wireline services. Cathedral markets its services under six brand names: **Directional Plus** and **The Directional Company** which provide horizontal and directional drilling services; **CAT Downhole Tools** which provides downhole equipment including drilling jars, shock subs and high performance drilling motors on a rental basis; **Tier One Oil Services** which provides oil and natural gas production testing services; **Advance Wireline** which provides cased hole logging and perforating, complete slickline services and casing integrity inspection logging; and **Xtreme Wireline** which provides slickline services. Cathedral strives to provide its clients with value added technologies and solutions to meet their drilling and production testing requirements. Its mandate is to supply "Best in Class, Best in Service" equipment and personnel to its clients. The trust units trade on the TSX under the symbol: CET.UN. For more information, visit www.cathedralenergyservices.com.*

