

Management's Discussion & Analysis

The MD&A provides commentary on the results of operations for the periods ended June 30, 2017 and 2016, the financial position as at June 30, 2017, and the outlook of Ceapro Inc. ("Ceapro") based on information available as at August 17, 2017. The following information should be read in conjunction with the unaudited interim condensed consolidated financial statements as at June 30, 2017, and related notes thereto, as well as the audited consolidated financial statements for the year ended December 31, 2016, which are prepared in accordance with International Financial Reporting Standards (IFRS) and the Management's Discussion and Analysis (MD&A) for the year ended December 31, 2016. All comparative percentages are between the periods ended June 30, 2017 and 2016 and all dollar amounts are expressed in Canadian currency, unless otherwise noted. Additional information about Ceapro can be found on SEDAR at www.sedar.com.

Forward-looking Statements

This MD&A offers our assessment of Ceapro's future plans and operations as at August 17, 2017, and contains forward-looking statements. By their nature, forward-looking statements are subject to numerous risks and uncertainties, including those discussed below. Readers are cautioned that the assumptions used in the preparation of forward-looking information, although considered reasonable at the time of preparation, may prove to be imprecise and, as such, undue reliance should not be placed on forward-looking statements. Actual results, performance, or achievements could differ materially from those expressed in, or implied by, these forward-looking statements. No assurance can be given that any of the events anticipated will transpire or occur, or if any of them do so, what benefits Ceapro will derive from them. The Company disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise unless required by law.

Vision, Core Business, and Strategy

Ceapro is incorporated under the Canada Business Corporations Act; and its wholly-owned subsidiaries, Ceapro Technology Inc., Ceapro Active Ingredients Inc., and Ceapro BioEnergy Inc., are incorporated under the Alberta Business Corporations Act. Ceapro (P.E.I.) Inc. is a wholly-owned subsidiary incorporated in Prince Edward Island. Ceapro USA Inc. is a wholly-owned subsidiary incorporated in the state of Nevada. On April 1, 2016, the Company completed a vertical amalgamation with its wholly-owned subsidiary Ceapro Veterinary Products Inc.

Ceapro is a growth stage biotechnology company. Our primary business activities relate to the development and commercialization of natural products for personal care, cosmetic, human, and animal health industries using proprietary technology, natural, renewable resources, and developing innovation.

Our products include:

- A commercial line of natural active ingredients, including *beta glucan*, *avenanthramides (colloidal oat extract)*, *oat powder*, *oat oil*, *oat peptides*, and *lupin peptides*, which are marketed to the personal care, cosmetic, medical, and animal health industries through our distribution partners and direct sales; and
- Veterinary therapeutic products, including an *oat shampoo*, an *ear cleanser*, and a *dermal complex/conditioner*, which are manufactured and marketed to veterinarians in Japan and Asia, through agreements with Daisen Sangyo Co. Ltd.

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

- A potential platform using our *beta glucan* formulations to deliver compounds used for treatments in both personal and healthcare sectors;
- A variety of novel enabling technologies including Pressurized Gas Expansion drying technology which is currently being tested on oat beta glucan but may have application for multiple classes of compounds;

- The development of a new oat variety and certain technologies to increase the content of avenanthramides to high levels to enable new innovative products to be introduced to new markets including medicinal foods, nutraceuticals, and botanical drugs; and
- *CeaProve*®, a diabetes test meal to screen pre-diabetes and to confirm diabetes diagnosis.

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

- Identifying unique plant sources and technologies capable of generating novel active natural products;
- Increasing sales and expanding markets for our current active ingredients;
- Developing and marketing additional high-value proprietary therapeutic natural products;
- Developing and improving manufacturing technologies to ensure efficiencies; and
- Advancing new partnerships and strategic alliances to develop new commercial active ingredients with various formulations to expand our markets.

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

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

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

To support these objectives, we believe we have strong intellectual and human capital resources and we are developing a strong base of partnerships and strategic alliances to exploit our technology. The current economic environment provides challenges in obtaining financial resources to fully exploit opportunities. To fund our operations, Ceapro relies upon revenues primarily generated from the sale of active ingredients, and the proceeds of public and private offerings of equity securities, debentures, government grants and loans, and other investment offerings.

Risks and Uncertainties

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

The Company has exposure to financial instrument and other risks as follows:

a) Credit risk

Trade and other receivables

The Company makes sales to distributors that are well-established within their respective industries. Based on previous experience, the counterparties had zero default rates and management views this risk as minimal. Approximately 87% of trade receivables are due from one distributor at June 30, 2017 (December 31, 2016 – 86% from two distributors) and all trade receivables at June 30, 2017 and December 31, 2016 are current. These main distributors are considered to have good credit quality and historically have a high quality credit rating.

Other receivables represent amounts due for research program claims, government goods and services taxes, and scientific research and development tax credits. The collectability risk is deemed to be low because of the good quality credit rating of the counter-parties.

Cash and cash equivalents

The Company has cash and cash equivalents in the amount of \$7,079,371 at June 30, 2017 (December 31, 2016 - \$9,150,035) and mitigates its exposure to credit risk on its cash balances by maintaining its bank accounts with Canadian Chartered Banks and investing in low risk, high liquidity investments.

There are no past due or impaired financial assets. The maximum exposure to credit risk is the carrying amount of the Company's trade and other receivables and cash and cash equivalents. The Company does not hold any collateral as security.

b) Liquidity risk

In meeting its financial obligations, the Company may be exposed to liquidity risks if it is unable to collect its trade and other receivables balances in a timely manner, which could in turn impact the Company's long-term ability to meet commitments under its current facilities. In order to manage this liquidity risk, the Company regularly reviews its aged trade receivables listing to ensure prompt collections. There is no assurance that the Company will obtain sufficient funding to execute its strategic business plan.

The following are the contractual maturities of the Company's financial liabilities and obligations:

	within 1 year \$	1 to 3 years \$	3 to 5 years \$	over 5 years \$	Total \$
Accounts payable and accrued liabilities	749,774	-	-	-	749,774
Long-term debt	998,958	874,749	16,483	-	1,890,190
CAAP loan	83,884	167,767	167,767	-	419,418
Total	1,832,616	1,042,516	184,250	-	3,059,382

c) Market risk

Market risk is comprised of interest rate risk, foreign currency risk, and other price risk. The Company's exposure to market risk is as follows:

1. Foreign currency risk

Foreign currency risk arises from the fluctuations in foreign exchange rates and the degree of volatility of these rates relative to the Canadian dollar.

The following table summarizes the impact of a 1% change in the foreign exchange rates of the Canadian dollar against the US dollar (USD) and the Euro on the financial assets and liabilities of the Company.

	Carrying Amount (USD)	Foreign Exchange Risk (USD)	
		-1%	+1%
		Earnings & Equity	Earnings & Equity
Financial assets			
Accounts receivable	1,093,052	10,931	(10,931)
Financial liabilities			
Accounts payable and accrued liabilities	198,560	(1,986)	1,986
Total increase (decrease)		8,945	(8,945)

	Carrying Amount (EURO)	Foreign Exchange Risk (EURO)	
		-1%	+1%
		Earnings & Equity	Earnings & Equity
Financial liabilities			
Long-term debt	332,194	(3,322)	3,322
Total (decrease) increase		(3,322)	3,322

The carrying amount of accounts receivable and accounts payable and accrued liabilities in USD and long-term debt in Euro represents the Company's exposure at June 30, 2017.

2. Interest rate risk

The Company has minimal interest rate risk because its long-term debt agreements are all at fixed rates.

d) Share price risk

Ceapro's share price is subject to equity market price risk, which may result in significant speculation and volatility of trading due to the uncertainty inherent in the Company's business and the technology industry.

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

e) People and process risk

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

Ceapro's consolidated financial statements are prepared within a framework of IFRS selected by management and approved by the Board of Directors. The assets, liabilities, revenues, and expenses reported in the consolidated financial statements depend to varying degrees on estimates made by management. An estimate is considered a critical accounting estimate if it requires management to make assumptions about matters that are highly uncertain and if different estimates that could have been used would have a material impact. The significant areas requiring the use of management estimates relate to provisions made for inventory valuation, amortization of property and equipment, tax liabilities and tax assets, provisions, the assumptions used in determining share-based compensation, and the assumptions used to value royalty obligations. These estimates are based on historical experience and reflect certain assumptions about the future that we believe to be both reasonable and conservative. Actual results could differ from those estimates. Ceapro continually evaluates the estimates and assumptions.

f) Loss of key personnel

Ceapro relies on certain key employees whose skills and knowledge are critical to maintaining the Company's success. Ceapro always strives to identify and retain key employees and always strives to be competitive with compensation and working conditions.

g) Interruption of raw material supply

Interruption of key raw materials could significantly impact operations and our financial position. Interruption of supply could arise from weather-related crop failures or from market shortages. Ceapro attempts to purchase key raw materials well in advance of their anticipated use and is in-licensing technologies from third parties to reduce this risk.

h) Environmental issues

Violations of safety, health, and environmental regulations could limit operations and expose the Company to liability, cost, and reputational impact. In addition to maintaining compliance with national and provincial standards, Ceapro maintains internal safety and health programs.

i) Regulatory compliance

As a natural extract producer, Ceapro is subject to various regulations and violation of these could limit markets into which we can sell. Ceapro has introduced a range of procedures which will ensure that Ceapro is well prepared for new regulations and obligations that may be required.

Future accounting policies not yet adopted

At the date of authorization of the Company's consolidated financial statements, certain new standards and amendments to existing standards have been published by the IASB that are not yet effective, and have not been adopted early by the Company. Information on those expected to be relevant to the Company's consolidated financial statements is provided below.

Management anticipates that all relevant pronouncements will be adopted in the Company's accounting policies for the first period beginning after the effective date of the pronouncement. New standards, interpretations and amendments either not adopted or listed below are not expected to have a material impact on the Company's consolidated financial statements.

IFRS 9 "Financial instruments"

In July 2014, the IASB released the final version of IFRS 9 "Financial instruments", representing the completion of its project to replace IAS 39 "Financial Instruments: Recognition and Measurement". The new standard introduces extensive changes to IAS 39's guidance on the classification and measurement of financial assets and introduces a new "expected credit loss" model for the impairment of financial assets. IFRS 9 also provides new guidance on the application of hedge accounting.

IFRS 9 is effective for reporting periods beginning on or after January 1, 2018. The Company's management is currently assessing the impact on these consolidated financial statements. The extent of the impact has not yet been determined.

IFRS 15 “Revenue from Contracts with Customers”

In May 2014, the IASB released IFRS 15 “Revenue from Contracts with Customers” which presents new requirements for the recognition of revenue, replacing IAS 18 “Revenue”, IAS 11 “Construction contracts”, and several revenue related interpretations. The new standard establishes a control-based revenue recognition model and provides additional guidance in many areas not covered in detail under existing IFRS, including how to account for arrangements with multiple performance obligations, variable pricing, customer refund rights, supplier repurchase options, and other common complexities.

IFRS 15 is effective for reporting periods beginning on or after January 1, 2018. The Company’s management is currently assessing the impact of IFRS 15 on these consolidated financial statements. The extent of the impact has not yet been determined.

IFRS 16 “Leases”

In January 2016, the IASB released IFRS 16 “Leases” replacing IAS 17 “Leases” and related interpretations. The new standard eliminates the classification of leases as either operating or finance leases and requires the recognition of assets and liabilities for all leases, unless the lease term is twelve months or less or the underlying asset has a low value.

IFRS 16 is effective for reporting periods beginning on or after January 1, 2019. The Company’s management has not yet assessed the impact of IFRS 16 on these consolidated financial statements.

Results of Operations Periods Ended June 30, 2017 and 2016

CONSOLIDATED INCOME STATEMENT

<i>\$000s except per share data</i>	Quarters Ended June 30,				Six Months Ended June 30,			
	2017	%	2016	%	2017	%	2016	%
Total revenues	3,174	100%	4,168	100%	6,357	100%	8,231	100%
Cost of goods sold	1,156	36%	1,154	28%	2,628	41%	2,383	29%
Gross margin	2,018	64%	3,014	72%	3,729	59%	5,848	71%
Research and product development	301	9%	(61)	-1%	897	14%	267	3%
General and administration	687	22%	524	13%	1,526	24%	1,020	12%
Sales and marketing	5	0%	1	0%	9	0%	3	0%
Finance costs	21	1%	49	1%	100	2%	147	2%
Income from operations	1,004	32%	2,501	60%	1,197	19%	4,411	54%
Other operating (loss) income	(247)	-8%	(143)	-3%	(428)	-7%	(319)	-4%
Income before tax	757	24%	2,358	57%	769	12%	4,092	50%
Income tax expense	(387)	-12%	(722)	-17%	(381)	-6%	(1,243)	-15%
Net income	370	12%	1,636	39%	388	6%	2,849	35%
Basic net income per common share	0.005		0.026		0.005		0.045	
Diluted net income per common share	0.005		0.025		0.005		0.043	

The following sections discuss the results from operations.

Revenue

\$000s	Quarters Ended June 30,			Six Months Ended June 30,		
	2017	2016	Change	2017	2016	Change
Total revenues	3,174	4,168	-24%	6,357	8,231	-23%

Total sales revenue for the second quarter ended June 30, 2017, amounted to \$3,174,000 compared to \$4,168,000 for the second quarter ended June 30, 2016, which was the highest quarterly sales volume in the Company's history. The 35% difference in product sales volume relates primarily to lower sales of beta glucan.

This was partially offset by an increase in sales volume for the Company's other value driver, avenanthramides. Revenue was also impacted by a higher U.S dollar relative to the Canadian dollar compared to the comparative quarter which positively impacted revenue by approximately \$89,000.

Revenue of \$6,357,000 for the first six months of 2017 was 23% lower than the comparative period. Consistent with the quarterly results, this is due to lower product sales volume caused primarily from lower sales of beta glucan. For the first six months of 2017 revenue was also impacted by a lower U.S dollar relative to the Canadian dollar compared to the comparative period which negatively impacted revenue by approximately \$70,000.

Expenses

COST OF GOODS SOLD AND GROSS MARGIN

\$000s	Quarters Ended June 30,			Six Months Ended June 30,		
	2017	2016	Change	2017	2016	Change
Sales	3,174	4,168	-24%	6,357	8,231	-23%
Cost of goods sold	1,156	1,154	0%	2,628	2,383	10%
Gross margin	2,018	3,014	-33%	3,729	5,848	-36%
Gross margin %	64%	72%		59%	71%	

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

During the second quarter of fiscal 2017, cost of goods sold of \$1,156,000 was consistent with the comparative quarter, however sales decreased by 24%, and the net result was a 33% decrease in the gross margin of \$996,000. The gross margin percentage decreased from 72% in the comparative quarter to 64% in the current quarter which reflects the lower sales volume combined with consistent cost of sales. The decrease in the gross margin percentage was a result of a number of factors including higher production salaries due to the hiring of additional operators and staff to support the operation of both the existing and the new production facility during the commissioning and validation period and to facilitate training of all operators, higher utilities and maintenance costs, and an increase in the cost of materials primarily due to the significant increase in the cost of feedstock. These factors have also resulted in an increase in overhead expenses primarily due to higher overhead expenses allocated over lower inventory produced during commissioning and validation activities during the last few quarters. The lower inventory produced is a combination of time required to be allocated to commissioning and validation activities despite the hiring of additional operators and due to higher processing required with the current inventory of feedstock.

The first six months of fiscal 2017 also reflects a similar decrease in revenue of 23%, while the cost of goods sold increased by 10% or \$245,000, resulting in a 36% decrease in gross margin or a decrease of \$2,119,000. The gross margin percentage decreased from 71% for the first six months of 2016 to 59% for the first six months of 2017 due to the same factors that impacted the second quarter of 2017. The results for the six months ended June 30, 2017 were also impacted by a different sales mix of products between the current period and the comparative period as a higher percentage of lower margin products were sold in the first six months of 2017.

The 59% gross margin percentage for the six months ended June 30, 2017 is lower than the 64% gross margin percentage experienced in second quarter of 2017 which reflects an overall improvement in the gross margin percentage from the first quarter of 2017. The percentage increase is primarily a result of improvements made in the second quarter relating to the processing of new feedstock contributing to an increase in the quantity produced and an improvement on the processing cost.

RESEARCH AND PRODUCT DEVELOPMENT

\$000s	Quarters Ended June 30,			Six Months Ended June 30,		
	2017	2016	Change	2017	2016	Change
Salaries and benefits	155	109		315	221	
Regulatory and patents	8	18		118	100	
Other	138	(188)		464	(54)	
Total research and product development expenditures	301	(61)	593%	897	267	236%

During the second quarter ended June 30, 2017, research and development expenses increased by 593% or \$362,000 in comparison with the same period in 2016. The increase primarily relates to both an increase in other research and development costs and to the recognition of scientific research and development ("SRED") tax credits during the second quarter of 2016 whereas in the current year the Company expects to file the current year SRED claim in the third quarter. The increase in expenditures for the second quarter of fiscal 2017 primarily related to expenditures incurred on the development of the Company's protocol and related mandatory regulatory activities for a pilot clinical study for the development of beta glucan as a cholesterol reducer and due to an increase in expenditures on the Company's Pressurized Gas Expanded ("PGX") Technology project. The increase in expenditures for the six months ended June 30, 2017 primarily related to the beta glucan pilot clinical study, an increase in spending on all of the Company's enabling technologies as well as to the commencement of a research program to study the bio activity of new formulations of the Company's value driver active ingredients.

Research and development expenditures also increased for both the second quarter and the six month period from an increase in salaries and benefits due to additional research and development staff hired throughout 2016. While the Company continued to receive grant funding for some key staff who are working primarily on the Company's PGX Technology project, the funding in 2017 was lower than the comparative period, which also raised the salaries and benefits expense.

Regulatory and patents expense will vary from period to period based on the timing of filings and maintenance payments. While the expense is slightly lower in the second quarter of 2017 compared to the comparative quarter, overall the expense is higher for the six month period ended June 30, 2017 due to patent maintenance on increased patent applications for its enabling technologies.

GENERAL AND ADMINISTRATION

\$000s	Quarters Ended June 30,			Six Months Ended June 30,		
	2017	2016	Change	2017	2016	Change
Salaries and benefits	169	95		563	197	
Consulting	120	64		240	131	
Board of directors compensation	41	51		83	108	
Insurance	35	30		72	61	
Accounting and audit fees	31	36		64	60	
Rent	22	22		44	44	
Public company costs	124	83		209	144	
Travel	38	44		52	71	
Depreciation	31	40		67	78	
Legal	14	10		17	31	
Other	62	49		115	95	
Total general and administration expenses	687	524	31%	1,526	1,020	50%

General and administration expense for the quarter ended June 30, 2017 increased by \$163,000 or 31% from the prior year (the overall increase for the six months ended June 30, 2017 was \$506,000 or 50%). The increase was primarily due to an increase in salaries and benefits expense related to the granting of stock options in January which resulted in an increase in share-based payments of approximately \$72,000 (\$360,000 for the six months ended June 30, 2017). While the share based payment accounting charge impacts net income it has no impact on cash flows. Also in January, the base compensation of the Chief Executive Officer was reviewed for the first time in over four years to better realign the compensation to market. This resulted in an overall increase to consulting fees of approximately \$56,000 (\$109,000 for the six months ended June 30, 2017).

Public company costs also increased by \$41,000 (\$65,000 for the six months ended June 30, 2017), primarily due to significantly higher annual regulatory fees resulting primarily from the Company's higher market capitalization and due to significantly higher publication and postage fees relating to the annual report and information circular for an expanded shareholder base. The increase was also partially due to an increase in communication costs and transfer agency fees.

For both the quarter and six month period ended June 30, 2017, the overall increase in general and administration expense was offset by lower Board of Director Compensation due to a decrease in share-based payment expense relating to directors.

For the six month period ended June 30, 2017, the overall increase in general and administration expense was also offset by lower legal fees as compared to the prior period which was higher because of additional regulatory reporting and costs associated with the amalgamation of the Company's subsidiary in 2016 and lower travel expense as attendance at conferences was lower in the first half of 2017.

SALES AND MARKETING

\$000s	Quarters Ended June 30,			Six Months Ended June 30,		
	2017	2016	Change	2017	2016	Change
Courses, conferences & advertising	4	-		7	1	
Other	1	1		2	2	
Total sales and marketing	5	1	400%	9	3	200%

Marketing expenses are negligible due to the Company's strategy to sell mostly through a distribution network instead of selling directly to end-users. The Company is re-visiting this strategy.

FINANCE COSTS

\$000s	Quarters Ended June 30,			Six Months Ended June 30,		
	2017	2016	Change	2017	2016	Change
Interest on long-term debt	6	11		15	22	
Transaction costs	5	7		9	13	
Royalties	-	-		55	50	
Accretion of CAAP loan	11	12		21	24	
Accretion of convertible	-	19		-	38	
	22	49	-55%	100	147	-32%

Finance costs decreased by 55% or \$27,000 in the second quarter ended June 30, 2017 from \$49,000 in 2016 to \$22,000. The decrease primarily relates to a \$19,000 accretion charge for convertible debentures in the comparative period for which there was no charge in the current period as the convertible debentures were all converted to equity during the year ended December 31, 2016.

Finance costs for the six month period ended June 30, 2017 decreased by \$47,000, from \$147,000 in 2016 to \$100,000, primarily due to the same factor that impacted the quarter.

OTHER OPERATING LOSS

\$000s	Quarters Ended June 30,			Six Months Ended June 30,		
	2017	2016	Change	2017	2016	Change
Foreign exchange loss	59	7		70	45	
Quality management system	41	-		81	-	
Other loss	-	-		1	1	
Plant relocation costs	147	136		276	273	
	247	143	73%	428	319	34%

During the second quarter ended June 30, 2017, other operating loss increased by \$104,000 or 73% from \$143,000 in 2016 to \$247,000.

The increase was partially due to a \$52,000 increase in foreign exchange loss over the comparative quarter. The Company's foreign exchange losses and gains are primarily due to the translation of US dollar denominated accounts receivable, accounts payable, and deferred revenue balances, and from the timing of the realization of these balances. Foreign exchange will fluctuate between the quarters due to fluctuations between the US dollar and the Canadian dollar. The foreign exchange gains and losses are also impacted by the translation of the Company's Euro denominated debt. During the second quarter ended June 30, 2017 the Euro debt translation resulted in a \$21,000 loss compared to a \$23,000 gain in the comparative period.

The increase was also partially due to expenditures on the Company's project to implement an improved quality management system which commenced in the fourth quarter of fiscal 2016. The new system will be designed to focus policies towards consistently meeting or exceeding customer requirements and will also be aligned with the Company's strategic goal of transitioning to nutraceutical and pharmaceutical markets.

The overall increase in other operating loss was also impacted by an \$11,000 increase in plant relocation costs which represent costs incurred relating to the new manufacturing facility that are not directly related to the acquisition and construction of the new manufacturing facility and therefore are not eligible to be capitalized.

During the six month period ended June 30, 2017, other operating loss increased by \$109,000 or 34% from \$319,000 in 2016 to \$428,000. The increase was primarily related to expenditures on the improvement of the Company's quality management system. The increase was also partially related to an increase in foreign exchange loss. Included in the foreign exchange loss for the six month period ending June 30, 2017, was a \$24,000 loss from the translation of the Euro debt compared to a Euro debt translation gain of \$38,000 which offset the overall foreign exchange loss in the comparative period.

DEPRECIATION AND AMORTIZATION EXPENSE

In the six month period ended June 30, 2017, the total depreciation and amortization expense of \$175,000 (2016 - \$191,000) was allocated as follows: \$69,000 to general and administration expense (2016 - \$80,000), \$27,000 to inventory (2016 - \$38,000), and \$79,000 (2016 - \$73,000) to cost of goods sold. The expense is slightly lower than the prior year as the depreciable base of manufacturing equipment currently in use and assets used in the corporate head office is lower than the prior year.

Quarterly Information

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

\$000s except per share data	2017		2016				2015	
	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3
Total revenues	3,174	3,183	2,425	3,018	4,168	4,064	3,435	3,079
Net income	370	18	126	645	1,636	1,213	3,452	1,006
Basic net income per common share	0.005	0.000	0.002	0.009	0.026	0.019	0.056	0.016
Diluted net income per common share	0.005	0.000	0.002	0.008	0.025	0.018	0.052	0.016

Ceapro's quarterly sales and results primarily fluctuate due to variations in the timing of customer orders, different product mixes, and changes in the capacity to manufacture products.

The significant increase to net income in the fourth quarter of 2015 relates to the recognition of net deferred tax assets of \$1,147,000 and an investment tax credit receivable of \$603,000. Management assessed that it was probable that sufficient taxable income would be available in the foreseeable future to realize these assets.

Net income in the first quarter of 2017 includes a non-cash share-based payment accounting charge of \$307,000 primarily relating to the granting of stock options in January 2017. This accounting charge is considerably higher than in any of the comparable quarters presented as options granted during these periods were not as significant.

Liquidity and Capital Resources

CAPITAL EMPLOYED

\$000s	June 30, 2017	December 31, 2016
Non-current assets	16,346	14,998
Current assets	10,678	11,394
Current liabilities	(2,148)	(2,534)
Total assets less current liabilities	24,876	23,858
Non-current liabilities	1,203	1,457
Shareholders' equity	23,673	22,401
Total capital employed	24,876	23,858

Non-current assets increased by \$1,348,000 primarily due to the acquisition of \$1,587,000 of property and equipment net of grants offset by a depreciation provision of \$175,000 and the utilization of \$64,000 of deferred tax assets against taxable income for the period.

Current assets decreased by \$716,000. Cash decreased by \$2,071,000 primarily due to the acquisition of property and equipment which was offset by an increase of \$185,000 in inventories, an increase in trade and other receivables of \$817,000 and an increase in prepaid expenses and deposits of \$353,000 primarily due to an additional deposit made on a new ethanol recycling system.

Current liabilities totaling \$2,148,000 decreased by the net amount of \$386,000 primarily due to the recognition of \$302,000 of deferred revenue and a decrease in trade payables and accrued liabilities of \$219,000 which was offset by an increase in the current portion of long-term debt of \$130,000 and an increase in the current portion of the CAAP loan of \$5,000.

Non-current liabilities totaling \$1,203,000 decreased by the net amount of \$254,000 primarily due to the repayment of and reclassification to current portion of long-term debt of \$596,000 offset by an increase in the discounted CAAP loan in the amount of \$16,000 and the utilization of an additional \$326,000 of deferred tax assets against taxable income for the period which resulted in a net deferred tax liability of \$325,905 at June 30, 2017.

Equity of \$23,673,000 at June 30, 2017 increased by \$1,272,000 from equity of \$22,401,000 at December 31, 2016 due to the recognition of net income of \$388,000 for the six month period ended June 30, 2017, the recognition of share-based compensation of \$396,000, and an increase from the exercise of stock options and warrants of \$488,000.

SOURCES AND USES OF CASH

The following table outlines our sources and uses of funds during the periods ended June 30, 2017 and 2016.

<i>\$000s</i>	Quarters Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Sources of funds:				
Funds generated from operations (cash flow)	975	2,547	1,418	4,002
Changes in non-cash working capital items relating to operating activities	-	-	-	-
Changes in non-cash accounts payable and accrued liabilities relating to investing activities	87	10	-	-
Grant used for capital assets	370	18	393	18
Share issuance	75	83	488	97
	<u>1,507</u>	<u>2,658</u>	<u>2,299</u>	<u>4,117</u>
Uses of funds:				
Purchase of property and equipment	(573)	(778)	(1,181)	(1,254)
Purchase of leasehold improvements	(599)	(964)	(765)	(2,046)
Deposits relating to investing activities	-	-	(421)	-
Changes in non-cash working capital items relating to operating activities	(810)	(1,709)	(1,413)	(835)
Changes in non-cash accounts payable and accrued liabilities relating to investing	-	-	(42)	(159)
Interest paid	(22)	(53)	(49)	(109)
Repayment of long-term debt	(252)	(243)	(499)	(485)
	<u>(2,256)</u>	<u>(3,747)</u>	<u>(4,370)</u>	<u>(4,888)</u>
Net change in cash flows	<u>(749)</u>	<u>(1,089)</u>	<u>(2,071)</u>	<u>(771)</u>

Net change in cash flow was a decrease of \$2,071,000 during the six month period ended June 30, 2017 in comparison with a decrease of \$771,000 for the same period in 2016. The difference primarily relates to comparative period being a record breaking quarter with high margin product sales greater than \$4M which generated an additional \$2,584 cash flows from operations in 2016. The difference is also related to a net negative change in working capital balances of \$835,000 in 2016 as opposed to a negative change in working capital balances in 2017 of \$1,413,000 which reflects an increase in the investment of inventories and the repayment of liabilities in 2017 compared to 2016. The higher operating cash flows generated in 2016 were offset by \$1,354,000 lower expenditures on property and equipment and leaseholds in 2017, as well as more cash generated from equity issuances and grant funding in 2017.

The net change in cash flows from operations also reflects increased spending on research and development expenses. While the Company views increased spending on research and development projects relating to its enabling technologies, research on product development and new applications for its value driving products as an important expenditure that will support value creation and future revenues and profits, during the research stage it has a negative impact on net income and net cash flows from operations. The Company intends to continue to increase investment in research and development.

Capital expenditures during the six months ended June 30, 2017 were lower than the comparative period. In the first six months of 2016 the expenditures related primarily to the construction of the extraction/fractionation part of the new facility. This construction was completed at the end of the third quarter of 2016.

In the first six months of 2017, the property and equipment expenditures related partially to the commissioning and validation of the extraction/fractionation processes, partially to the construction of a pilot scale skid for the Company's PGX technology for which grant funding was recognized, as well as to new equipment improvements made to continuously improve the manufacturing process. The Company also made an additional deposit on the purchase of a custom designed ethanol recovery system and incurred leasehold improvement expenditures relating to design work for the construction necessary to install and house the new ethanol recovery system in the additional new facility space obtained in 2016. The purchase of the ethanol recovery system is expected to be completed in 2017, and the related leasehold improvements and installation is planned for 2018.

The Company has a positive working capital balance of \$8,529,838 at June 30, 2017. Based on current plans, the Company estimates that it has sufficient capital necessary to complete final commissioning activities and validation trials at the newly completed manufacturing facility, to complete the purchase and commence installation of an ethanol recovery system which is expected to improve the Company's manufacturing process, and the capital necessary to proceed with previously disclosed research and development projects and upcoming clinical trials.

The Company also estimates that the cash flows generated by its existing operating activities as well as cash available through other sources will be sufficient to finance its operating expenses, maintain capital investment, and service debt needs.

To meet future requirements, Ceapro may raise additional cash through some or all of the following methods: public or private equity or debt financing, income offerings, capital leases, collaborative and licensing agreements, potential strategic alliances with partners, government programs, and other sources. There can be no assurance that the Company will be able to access capital when needed. The ability to generate new cash will depend on external factors, many beyond the Company's control, as outlined in the Risks and Uncertainties section. Should sufficient capital not be raised, Ceapro may have to delay, reduce the scope of, eliminate, or divest one or more of its discovery, research, or development technology or programs, any of which could impair the value of the business.

Total common shares issued and outstanding as at August 17, 2017 were 75,350,225 (August 23, 2016 – 72,619,781). In addition, 2,495,302 stock options, 4,244,480 warrants, and 660,377 broker unit warrants as at August 17, 2017 (August 23, 2016 – 2,843,335 stock options, 4,716,981 warrants, and 660,377 broker unit warrants) were outstanding that are potentially convertible into an equal number of common shares at various prices.

GRANT FUNDING

a) The Company entered into Canadian Agricultural Adaptation Program ("CAAP") repayable contribution agreements for total possible funding of \$1,339,625 receivable over the years from October 7, 2010 through September 30, 2012. During the year ended December 31, 2012, the Company voluntarily amended the maximum possible funding under the agreement to \$671,068 as a result of lower anticipated project expenditures. The end date for project expenditures was also extended one year to September 30, 2013. All amounts claimed under the program are repayable interest free over eight years beginning in 2014. The Company received or recorded as receivable funding of \$671,068 to December 31, 2013 under this program and no further funds are expected.

- b) During the year ended December 31, 2011, the Company entered into a Contribution Agreement with Alberta Innovates Bio Solutions (AI-Bio Solutions) for a non-repayable grant contribution totaling up to \$1,600,000 towards the construction of a new bio-processing facility and subject to compliance with all terms and conditions of the agreement. In accordance with the agreement, the Company received \$750,000 in 2011, and received \$690,000 in 2013. A final payment of \$160,000 was received in 2016 and has been recorded as a reduction of capitalized expenditures. The project has been completed at December 31, 2016.
- c) During the year ended December 31, 2014, the Company entered into a non-repayable grant agreement with AI-Bio Solutions to provide funding of up to \$198,000 for certain research activities. During the six months ended June 30, 2017 the Company received \$19,800 (year ended December 31, 2016 - \$89,100). An amount of \$19,800 (year ended December 31, 2016- \$89,100) was expended on the research project. The project has been completed at June 30, 2017.
- d) During the year ended December 31, 2015, the Company entered into an agreement under the Growing Forward 2 program to provide non-repayable grant funding for up to \$52,000 for certain research activities. During the year ended December 31, 2016, the Company received or recorded as a receivable \$5,791 (2015 - \$14,083) which has been recorded as a reduction of research and development activities. The project has been completed at December 31, 2016.
- e) During the year ended December 31, 2015, the Company entered into a contribution agreement with AI-Bio Solutions for a non-repayable funding contribution of \$800,000 to implement the scale-up of the Company's Enabling Pressurized Gas Expanded (PGX) Technology. During the year ended December 31, 2015, the Company received \$300,000. During the year ended December 31, 2016, the Company recognized \$17,572 as a reduction of capital expenditures and the balance of \$282,428 remained recorded as deferred revenue at December 31, 2016. During the six months ended June 30, 2017, the Company received an additional \$300,000 and recognized \$364,412 on eligible equipment and \$30,000 on eligible expenses. The balance of the grants received of \$188,016 remains recorded as deferred revenue at June 30, 2017. The Company anticipates receiving an additional \$100,000 during the remainder of 2017 and \$100,000 in 2018.
- f) During the year ended December 31, 2015, the Company entered into a contribution agreement with Industrial Research Assistance Program (IRAP) for non-repayable funding of up to a maximum of \$350,000 for costs incurred on the demonstration and testing of the Company's PGX Technology. During the six months ended June 30, 2017, IRAP and the Company agreed to amend the contribution agreement to increase the non-repayable funding up to a maximum of \$400,000. During the six months ended June 30, 2017, the Company received or recorded as a receivable \$72,880 (2016 - \$137,230) which has been recorded as a reduction of research and project development expenses. The Company anticipates receiving an additional \$10,000 during the remainder of 2017.
- g) During the year ended December 31, 2016, the Company entered into an agreement under the Growing Forward 2 program to provide non-repayable grant funding for up to \$33,000 for certain research activities. During the six months ended June 30, 2017, the Company received \$9,623 (year ended December 31, 2016 - \$7,594) which has been recorded as a reduction of research and development activities. The project has been completed at June 30, 2017.
- h) During the year ended December 31, 2016, the Company entered into a contribution agreement with the German-Canadian Centre for Innovation and Research to provide a non-repayable funding contribution of up to \$247,856 for the advancement of the Company's PGX Technology. During the year ended December 31, 2016, the Company received \$50,000 and recognized \$2,625 as a reduction of research and development expenditures and \$19,038 as a reduction of capital expenditures. The balance was recorded as deferred revenue at December 31, 2016. During the six months ended June 30, 2017, the Company received an additional \$64,196 and recognized \$63,715 as a reduction of research and development expenditures and \$28,818 as a reduction of capital expenditures. The Company anticipates receiving an additional \$134,000 in 2018.

Related Party Transactions

During the six month period ended June 30, 2017, \$Nil (2016 - \$3,000) of interest was earned by a company controlled by an officer and by a close family member of a director from their \$Nil (2016 - \$75,000) investments in the convertible debenture financing.

During the six month period ended June 30, 2017, the Company paid key management salaries, short-term benefits, consulting fees, and director fees totaling \$402,000 (2016 – \$283,000) and share-based payments expense for key management personnel was \$387,000 (2016 - \$40,000).

The amount payable to directors at June 30, 2017 was \$40,000 (2016 - \$80,000). Consulting fees and key management salaries payable to officers included in accounts payable and accrued liabilities at June 30, 2017 was \$Nil (2016 - \$21,000).

These transactions are in the normal course of operations and are measured at the amount of consideration established and agreed to by the related parties.

Commitments and Contingencies

(a) During the year ended December 31, 2011, the Company and its wholly-owned subsidiary, Ceapro Veterinary Products Inc. were served with a statement of claim from AVAC Ltd. alleging damages of \$724,500 pursuant to a product development agreement. The Company and Ceapro Veterinary Products Inc. filed a statement of defense to refute the claim and the evidentiary portion of the trial was completed in January 2015. All written arguments were completed on March 16, 2015 and have been submitted to the presiding judge. The Company believes it has presented strong defenses to the allegations at trial and no provision has been made in the consolidated financial statements for this litigation.

(b) During the year ended December 31, 2012, the Company and its wholly-owned subsidiary, Ceapro Technology Inc. were served with a statement of claim from AVAC Ltd. alleging damages of \$1,470,000 pursuant to two product development agreements. The Company and Ceapro Technology Inc. filed a statement of defense to refute the claim and the evidentiary portion of the trial was completed in January 2015. All written arguments were completed on March 16, 2015 and have been submitted to the presiding judge. The Company believes it has presented strong defenses to the allegations at trial and no provision has been made in the consolidated financial statements for this litigation.

(c) During the year ended December 31, 2012, the Company entered into a licence agreement for a new technology to increase the concentration of avenanthramides in oats. The Company shall pay an annual royalty percentage rate of 2% of sales, payable every January 1st and July 1st, subject to a minimum annual royalty payment according to the schedule below:

<u>Year</u>	<u>Amount</u>
2012	nil
2013	\$12,500
2014	\$37,500
2015	\$50,000
2016	\$50,000

And \$50,000 each year thereafter while the licence agreement remains in force. The agreements remain in force until the patents expire or are abandoned.

The licence agreement for the use of the intellectual property requires future royalty payments based on specific sales and is an executory contract. The licence agreement also does not represent an onerous contract. On this basis, upfront payments required to enter into the agreement are capitalized as a licence asset and all royalty payments under the agreement are recognized as they become due.

(d) During the year ended December 31, 2014, the Company entered into a licence agreement with the University of Alberta for the rights to an enabling pressurized gas expanded technology (PGX) that would allow the development, production, and commercialization of powder formulations that could be used as active ingredients.

In accordance with the agreement and as amended on February 2, 2015, the Company shall pay the following royalties, payable on a semi-annual basis:

- (a) a royalty of 3.5% of net sales generated from the field of pharmaceuticals;
- (b) a royalty of 3.0% of net sales generated from the field of nutraceuticals;
- (c) a royalty of 2.75% of net sales generated from the field of cosmetics;
- (d) a royalty of 1.0% of net sales generated from the field of functional foods;
- (e) a royalty of 3.0% of net sales generated from other fields.

The Company shall pay a minimum annual advance on earned royalties of \$5,000 commencing March 1, 2017 and every year thereafter while the licence agreement remains in force.

The licence agreement for the use of the intellectual property requires future royalty payments based on specific sales and is an executory contract. The licence agreement also does not represent an onerous contract. On this basis, upfront payments required to enter into the agreement are capitalized as a licence asset and all royalty payments under the agreement are recognized as they become due.

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

Outlook

Looking forward, we expect our base business in cosmeceuticals to remain solid. This base business is the foundation to secure a revenue stream to support necessary significant investments in human resources and our product pipeline to enable the transition of Ceapro to a full-fledged biopharmaceutical company serving large nutraceuticals and pharmaceuticals markets with our value drivers' beta glucan and avenanthramides respectively known for their cholesterol reducing and anti-inflammatory properties.

Further, we will actively pursue over the next twelve months an extensive research program with our proprietary PGX platform technology for which we have the worldwide rights for all industrial applications.

We are committed to remain focused on executing our strategic imperatives for growth that will drive significant value to all of our shareholders in the near, mid and long term.

Additional Information

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