Celtic Exploration Ltd.

Q1

INTERIM REPORT FOR
THE THREE MONTHS ENDED
MARCH 31, 2006 (UNAUDITED)

HIGHLIGHTS

($ thousands, unless otherwise indicated)	2006	2005	Change
	Three months ended March 31		
FINANCIAL			
Revenue, net of royalties	$ **27,782**	$ 14,099	97%
Funds from operations	$ **20,538**	$ 10,489	96%
Funds from operations per share			
Basic ($/share)	$ **0.71**	$ 0.41	73%
Diluted ($/share)	$ **0.69**	$ 0.39	77%
Net earnings	$ **7,301**	$ 3,018	142%
Earnings per share			
Basic ($/share)	$ **0.25**	$ 0.12	108%
Diluted ($/share)	$ **0.24**	$ 0.11	118%
Capital expenditures, net of dispositions	$ **42,354**	$ 23,623	79%
Total assets	$ **288,839**	$ 155,257	86%
Bank debt	$ **72,000**	$ 33,550	115%
Working capital deficiency, excluding bank debt	**13,107**	9,727	35%
Bank debt, net of working capital	$ **85,107**	$ 43,277	97%
Shareholders' equity	$ **133,592**	$ 79,861	67%
Common shares issued and outstanding (thousands)			
Basic	**29,027**	25,891	12%
Diluted	**31,384**	27,948	12%
OPERATIONS			
Production			
Oil (bbls/d)	**3,617**	2,269	59%
Natural gas (mcf/d)	**14,322**	8,856	62%
Combined (BOE/d)	**6,004**	3,745	60%
Production per million shares (BOE/d)	**207**	145	43%
Realized sales prices, before financial derivatives			
Oil ($/bbl)	$ **62.62**	$ 53.91	16%
Natural gas ($/mcf)	$ **10.44**	$ 8.33	25%
Combined ($/BOE)	$ **62.66**	$ 52.35	20%
Operating netbacks, after financial derivatives			
Oil ($/bbl)	$ **37.12**	$ 35.80	4%
Natural gas ($/mcf)	$ **7.59**	$ 5.05	50%
Combined ($/BOE)	$ **40.49**	$ 33.64	20%
Drilling activity			
Total wells	**32**	22	45%
Working interest wells	**20.5**	15.5	32%
Success rate on working interest wells	**73%**	63%	16%
Undeveloped land			
Gross acres	**318,549**	240,052	33%
Net acres	**199,228**	145,330	37%

MESSAGE TO SHAREHOLDERS

Celtic Exploration Ltd. ("Celtic" or the "Company") is pleased to report to shareholders the Company's activities in the first quarter of 2006. During the first quarter, Celtic drilled 32 (20.5 net) wells with an overall success rate of 73%.

The majority of the Company's drilling activity in the first quarter took place in the deep basin of west central Alberta where 21 (14.4 net) wells were drilled with an overall success rate of 82%.

At Swan Hills, five oil wells and one natural gas well were drilled at 100% working interest. All six wells are currently on production at a combined rate of approximately 400 BOE per day. Oil production from this area is 41° API and fetches premium light oil pricing. Production from the oil wells is expected to increase in the summer when the associated solution gas is tied-in. The natural gas well marks Celtic's first production in the Swan Hills area from the Gilwood formation. The Company will continue to keep two rigs operating throughout the summer targeting Beaverhill Lake light oil.

At Virginia Hills, Celtic drilled five wells at working interests ranging from 9.4% to 45.0%, resulting in two natural gas wells and one oil well. These are the first wells drilled by the Company in this new exploration area.

At Lator, the Company tested a 100% working interest Cretaceous natural gas well at a stabilized rate of 1.8 mmcf per day (300 BOE per day). This well is expected to come on production during the summer and a follow-up location is planned.

At Fox Creek, Celtic drilled a horizontal well in 2005 confirming an extension of the eastern edge of the Beaverhill Lake pool. In the first quarter of 2006, the Company drilled a second step-out well which also proved successful. Celtic has a third location planned for the second quarter.

At Kaybob South, Celtic acquired seven sections (4,480 acres) of land at a Crown sale in January 2006, bringing the Company's total land holdings in the area to nine sections (5,760 acres). As a follow-up to the initial two wells drilled in 2005, Celtic drilled two more wells in the first quarter that are now completed and, subsequent to March 31, 2005 and prior to break-up, the Company drilled another two wells in order to gain sufficient information before the Crown land sale in early May. At this land sale, Celtic acquired additional acreage and has resumed drilling and completion operations. Natural gas production from the first well has now commenced and tie-ins are proceeding on the remaining five wells that have been drilled to date. Celtic estimates that it will have production of approximately 1,200 to 1,500 BOE per day on this acreage prior to down spacing the property in late fall.

In west central Alberta, the Company is currently evaluating new exploration prospects that, if successful, could lead to meaningful development activity later in 2006 and in 2007. Celtic continues to assemble lands in these new areas and will be in a position to discuss the specifics of these prospects after all of the necessary land positions have been acquired.

In east central Alberta, prior to break-up, Celtic drilled the first well of a nine-well program in the Ashmont area. The Company has commenced testing five potential natural gas zones encountered in the well and the remainder of the drilling program is expected to continue at the end of May, subject to suitable weather conditions.

At Chime, the Company divested its non-operated, lower working interest properties for proceeds of $9.5 million. Celtic's share of natural gas production, with associated liquids, included in this disposition was made up of approximately 130 BOE/d. The proceeds from this sale of assets is being re-directed towards undeveloped Crown land acquisitions on new, higher working interest prospects in west central Alberta.

At March 31, 2006, Celtic's undeveloped land holdings increased by 37% compared to the corresponding period of the previous year, to over 199,000 net acres. In addition to the increase in its undeveloped land position, the Company continues to add significantly to its drilling inventory as a result of successful exploration and development activity.

Celtic remains optimistic that the remainder of 2006 will continue to see strong production and cash flow growth. Given the Company's new bank credit facility of $100 million and commodity price risk management contracts in place, the Company remains in a solid financial position to carry out its planned capital expenditure program.

MANAGEMENT'S DISCUSSION AND ANALYSIS

INTRODUCTION

The Company was incorporated on April 16, 2002 as Desco Exploration Ltd. and completed its initial public offering on June 27, 2002. On September 30, 2002, the Company changed its name to Celtic Exploration Ltd. ("Celtic" or "the Company"). Celtic's head office is based in Calgary, Alberta, Canada. Common shares of the Company are listed and posted for trading on the Toronto Stock Exchange under the symbol "CLT."

The following management's discussion and analysis ("MD&A") should be read in conjunction with the Company's unaudited interim financial statements for the three months ended March 31, 2006 and the audited financial statements and related notes for the year ended December 31, 2005. This MD&A is effective May 8, 2006. The accompanying financial statements of Celtic have been prepared by management and approved by the Company's Audit Committee and Board of Directors. These financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). Additional information relating to Celtic can be found on the SEDAR website at www.sedar.com.

Non-GAAP Financial Measurements This document contains the terms "funds from operations" and "operating netbacks" which do not have a standardized meaning prescribed by Canadian GAAP, and therefore may not be comparable with the calculation of similar measures by other companies. Funds from operations and operating netbacks are used by Celtic as key measures of performance. Funds from operations and operating netbacks are not intended to represent operating profits, nor should they be viewed as an alternative to cash flow provided by operating activities, net earnings or other measures of financial performance calculated in accordance with GAAP. The reconciliation between net earnings and funds from operations can be found in the statement of cash flows included in the audited financial statements. Operating netbacks are determined by deducting royalties, production expenses and transportation and selling expenses from oil and gas sales revenue. The Company calculates funds from operations per share using the same method and shares outstanding, which are used in the determination of earnings per share.

Other Measurements All dollar amounts are referenced in Canadian dollars, except when noted otherwise. Where amounts are expressed on a barrel of oil equivalent ("BOE") basis, natural gas volumes have been converted to oil equivalence at six thousand cubic feet per barrel. The term BOE may be misleading, particularly if used in isolation. A BOE conversion ratio of six thousand cubic feet per barrel is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. References to oil in this discussion include crude oil and natural gas liquids ("NGLs"). NGLs include condensate, propane, butane and ethane.

Critical Accounting Estimates Management is required to make judgments, assumptions and estimates in the application of generally accepted accounting principles that have a significant impact on the financial results of the Company.

Capitalized costs relating to the exploration and development of oil and gas reserves, along with estimated future capital expenditures required in order to develop proved reserves, are depleted and depreciated on a unit-of-production basis using estimated proved reserves.

The carrying value of property, plant and equipment is reviewed at least annually for impairment. Impairment occurs when the carrying value of the assets is not recoverable by the future undiscounted cash flows. The cost recovery ceiling test is based on estimates of proved reserves, production rates, oil and gas prices, future costs and other relevant assumptions. By their nature, these estimates are subject to measurement uncertainty and the impact on the financial statements could be material.

Liability recognition for asset retirement obligations associated with oil and gas well sites and facilities are determined using estimated costs discounted based on the estimated life of the asset. These capitalized costs are amortized on a unit-of-production basis, consistent with depletion and depreciation. Over time, the liability is accreted up to the actual expected cash outlay to perform the abandonment and reclamation.

In order to recognize stock-based compensation expense, the Company estimates the fair value of stock options granted using assumptions related to interest rates, expected life of the option, volatility of the underlying security and expected dividend yields. These assumptions may vary over time.

The determination of the Company's income and other tax liabilities requires interpretation of complex laws and regulations often involving multiple jurisdictions. All tax filings are subject to audit and potential reassessment after the lapse of considerable time. Accordingly, the actual income tax liability may differ significantly from that estimated and recorded on Celtic's financial statements.

Changes in Accounting Policies and Practices Details outlining Celtic's accounting policies are contained in the notes to the financial statements. There have been no changes in the Company's accounting policies and practices in 2006, compared to the previous year.

Disclosure Controls and Procedures Disclosure controls and procedures are designed to provide reasonable assurances that all relevant information is gathered and reported to senior management, including the Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO"), on a timely basis in order that appropriate decisions can be made regarding public disclosure. As at March 31, 2006, the CEO and the CFO have evaluated the effectiveness of Celtic's disclosure controls and procedures as defined in Multilateral Instrument 52-109 of the Canadian Securities Administrators and have concluded that such disclosure controls and procedures are effective.

GROWTH STRATEGY

Celtic expects to continue to grow by implementing its dual-prong strategy to acquire assets with exploitation potential and, at the same time, implement its full-cycle exploration program. This strategy has proved successful to date, as is evidenced by Celtic's rapid growth since commencing active oil and gas operations in September 2002. To complement this strategy, the Company has assembled a team of experienced and qualified personnel and is well positioned financially to act quickly on new opportunities. Celtic believes that its growth strategy will continue to increase funds from operations per share, net asset value per share and production per share.

RESULTS OF OPERATIONS

2006 First Quarter Highlights The quarter ended March 31, 2006 was another successful quarter in the execution of the Company's growth strategy. Highlights for the first quarter of 2006 are as follows:

- Drilled 32 (20.5 net working interest) wells during the quarter resulting in 11 (8.9 net) oil wells, 10 (5.8 net) natural gas wells and 1 (0.2 net) coal bed methane well, for an overall success rate, based on net wells, of 73%;
- Reported net earnings of $7.3 million (up 142%) and earnings per share (diluted) of $0.24, an increase of 118% compared to $0.11 in the first quarter of 2005;
- Reported funds from operations of $20.5 million (up 96%) and funds from operations per share (diluted) of $0.69, an increase of 77% from $0.39 in the previous year;
- Generated an average operating netback of $40.49 per BOE, up 20% from $33.64 per BOE in 2005; and
- Increased average daily production by 60% to 6,004 BOE per day, up from 3,745 BOE per day in the first quarter of 2005, and achieved daily average production per million shares of 207 BOE per day, up 43% in 2006 compared to 145 BOE per day in the previous year.

Production Oil and gas production in the first quarter of 2006 increased 60% to average 6,004 BOE per day compared to 3,745 BOE per day in the first quarter of 2005. Average production in the fourth quarter of 2005 was 5,094 BOE per day. Production per million shares outstanding in the first quarter of 2006 averaged 207 BOE per day, up 43% from 145 BOE per day in the same period of 2005.

Revenue and Royalties Revenue, after royalties, for the three months ended March 31, 2006 was $27.8 million, an increase of 97% compared to $14.1 million in the same period of the previous year. Royalties in the first quarter of 2006 averaged 21.5% of sales compared to 18.7% in the corresponding period of 2005. Celtic continues to achieve lower royalties than industry standard through its participation in royalty incentive programs available for deep drilling and horizontal re-activation wells.

The combined average product price received for oil and gas sales, before financial derivative contracts, for the quarter ended March 31, 2006 was $62.66 per BOE, an increase of 20% compared to the first quarter of the previous year.

Expenses For the three-month period ended March 31, 2006, production expenses were $5.3 million ($9.82 per BOE), transportation and selling expense was $0.4 million ($0.83 per BOE), general and administrative expenses were $0.6 million ($1.20 per BOE), interest expense was $0.7 million, and depletion, depreciation and amortization expenses were $9.8 million ($18.20 per BOE). In the previous year, for the three-month period ended March 31, 2005, production expenses were $2.8 million ($8.19 per BOE), transportation and selling expense was $0.3 million ($0.81 per BOE), general and administrative expenses were $0.6 million ($1.72 per BOE), interest expense was $0.2 million, and depletion, depreciation and amortization expenses were $5.7 million ($16.87 per BOE).

Taxes For the three months ended March 31, 2006, Celtic provided for a provision of future income taxes in the amount of $3.2 million. This amount differs from the expected provision for income taxes of $3.8 million based on the statutory combined income tax rate of 35.62% due to the differences between the resource allowance deduction and non-deductible Crown charges and non-taxable Provincial tax credits (Alberta Royalty Tax Credit). An analysis of the income tax provision is included in the notes to the financial statements.

Net Earnings and Funds from Operations Net earnings for the three months ended March 31, 2006 was $7.3 million ($0.25 per share, basic and $0.24 per share, diluted), an increase of 142% from $3.0 million ($0.12 per share, basic and $0.11 per share, diluted) in the same period of the previous year. In addition, funds from operations were $20.5 million ($0.71 per share, basic and $0.69 per share, diluted), an increase of 96% compared to $10.5 million ($0.41 per share, basic and $0.39 per share, diluted) for the three months ended March 31, 2005.

Capital Expenditures During the three-month period ended March 31, 2006, Celtic spent $52.7 million on exploration and development activity and property acquisitions. Drilling and completion operations accounted for $33.0 million, equipment and facility expenditures were $7.7 million and $11.8 million was spent on land and seismic. The Company continues to invest in land and seismic in order to build on its inventory of prospects for future drilling. Proceeds from disposition of assets in the first quarter of 2006 amounted to $10.3 million and includes the disposition of non-operated and low-working-interest properties at Chime, Alberta for proceeds of $9.5 million.

Drilling Activity During the three months ended March 31, 2006, Celtic drilled 32 (20.5 net) wells compared to 22 (15.5 net) wells in the first quarter of the previous year, with an overall success rate of 73% on net wells drilled. The split between development drilling and exploratory drilling was 74% and 26%, respectively. The average vertical depth of net wells drilled was 2,225 metres, 16% deeper than the average drilling depth of 1,910 metres in the first three months of 2005.

CAPITAL RESOURCES AND LIQUIDITY

Source of Funds Investment funding for capital expenditures incurred in the first quarter of 2006 was provided by bank debt and cash provided by operating activities.

The Company has recently put in place a committed term loan facility, whereby the maximum amount available to be drawn is $100.0 million. At March 31, 2006, Celtic had drawn $72.0 million, leaving significant unused credit lines available to fund working capital deficiency and future capital expenditures.

Celtic expects to fund future capital expenditures through the use of a combination of cash provided by operating activities and bank debt, supplemented by new equity share offerings, as required.

Working Capital The capital-intensive nature of Celtic's activities creates a working capital deficiency position during periods with high levels of capital investment. However, during such periods, the Company maintains sufficient unused bank credit lines to satisfy such working capital deficiencies. At March 31, 2006, the working capital deficiency amount plus outstanding bank debt represented 85% of the Company's maximum authorized bank borrowing credit limit.

The oil and gas industry has a pre-arranged monthly clearing day for payment of revenues from all buyers of oil and natural gas. This occurs on the 25th day following the month of sale. As a result, the Company's production revenues are collected in an orderly fashion. Celtic monitors its revenue counterparty credit positions to mitigate any potential credit losses. To the extent that the Company has joint venture partners in its activities, it must collect the partners' share of capital expenditures and operating expenses on a monthly basis. Exceptions are in the event that the partners' share of a capital project is a significant amount. In this case, Celtic will collect such amounts from its partners in advance of expenditures taking place in accordance with standard industry operating procedures. At March 31, 2006, the Company did not have any material accounts receivable that were deemed uncollectible.

Accounts payable consist of amounts payable to suppliers relating to head office and field operating and investing activities. These invoices are processed within the Company's normal payment period.

Celtic actively manages the pace of its capital spending program by monitoring forecasted production and commodity prices and resulting cash flows. Should circumstances affect cash flow in a detrimental way, the Company is capable of reducing capital investment levels.

Share Information The Company is authorized to issue an unlimited number of common shares and an unlimited number of preferred shares. As at March 31, 2006, there were 29.0 million common shares outstanding. There were no preferred shares outstanding. As at March 31, 2006, directors, employees and consultants have been granted options to purchase 2.4 million common shares of the Company at an average exercise price of $7.02 per share. Detailed information regarding the Company's stock options outstanding is contained in the notes to the financial statements.

Contractual Obligations Celtic has a committed term loan credit facility with Canadian financial institutions. The authorized borrowing amount under this facility is $100.0 million, of which $72.0 million was outstanding at March 31, 2006. Interest under this facility is payable monthly. Additional disclosure relating to bank debt is provided in the notes to the financial statements.

From time to time, the Company enters into agreements to transport and market oil and gas production. In addition, the Company has entered into agreements with third parties that provides employees with access to specialized computer software and information including production and reserves data, geological data, accounting systems and land management systems.

As a normal course of business, the Company leases office space, vehicles for field personnel and office equipment such as computers, printers and photocopiers.

Related-party Transactions The Company has retained the law firm of Borden Ladner Gervais LLP to provide Celtic with legal services. William C. Guinan, a director, chairman and corporate secretary of Celtic, is a partner of this law firm. The Company expects to continue using the services of this law firm from time to time.

SUPPLEMENTAL QUARTERLY INFORMATION

The Company has been successful in providing strong growth in funds from operations and net earnings. The following table summarizes key financial and operating information for the past eight quarters:

($ thousands, except per unit amounts)	**2006 Q1**	2005 Q4	2005 Q3	2005 Q2	2005 Q1	2004 Q4	2004 Q3	2004 Q2
Revenue, net of royalties ($)	**27,782**	26,647	22,186	13,645	14,099	13,086	13,986	11,976
Funds from operations ($)	**20,538**	18,674	17,082	10,724	10,489	9,559	10,155	8,472
Per share – basic ($/share)	**0.71**	0.65	0.59	0.39	0.41	0.37	0.39	0.33
Per share – diluted ($/share)	**0.69**	0.62	0.57	0.38	0.39	0.36	0.38	0.32
Net earnings ($)	**7,301**	7,062	5,729	2,455	3,018	3,278	3,594	2,582
Per share – basic ($/share)	**0.25**	0.24	0.20	0.09	0.12	0.13	0.14	0.10
Per share – diluted ($/share)	**0.24**	0.24	0.19	0.09	0.11	0.12	0.14	0.10
Total assets ($)	**288,839**	242,113	207,074	178,574	155,257	135,984	122,416	114,246
Bank debt, net of working capital ($)	**85,107**	63,426	42,003	29,589	43,277	30,073	20,572	19,225
Production (BOE/d)	**6,004**	5,094	5,081	3,751	3,745	3,524	3,744	3,543
Production per million shares (BOE/d)	**207**	176	176	136	145	136	145	137
Realized sales price ($/BOE)	**62.66**	66.95	63.60	53.57	52.35	49.03	48.86	45.07
Operating netback ($/BOE)	**40.49**	35.37	37.95	33.42	33.64	31.62	31.02	27.98
Netback as a percentage of sales	**65%**	53%	60%	62%	64%	64%	63%	62%

Factors that have caused variations over the quarters:

- The majority of the Company's production growth has been the result of the Company's successful exploration and development drilling activities.
- Oil and gas property acquisitions completed in 2004 and 2005 also contributed to production growth:
  - The $3.4 million acquisition of a property at Morse River completed in April 2004 added approximately 120 bbls per day of oil production.
  - In 2005, Celtic completed the acquisition of complementary oil and gas properties in the Swan Hills/Virginia Hills area of west central Alberta for approximately $2.5 million, adding approximately 350 BOE/d (73% oil and 27% natural gas).
- Revenue, funds from operations and earnings growth is primarily the result of production growth and increases in commodity prices.

BUSINESS RISKS

Celtic's exploration and production activities are concentrated in the Western Canadian Sedimentary Basin, where activity is highly competitive and includes a variety of different-sized companies ranging from smaller junior producers, intermediate and senior producers and royalty trust organizations, to the much larger integrated petroleum companies. Celtic is subject to a number of risks which are also common to other organizations involved in the oil and gas industry. Such risks include finding and developing oil and gas reserves at economic costs, estimating amounts of recoverable reserves, production of oil and gas in commercial quantities, marketability of oil and gas produced, fluctuations in commodity prices, financial and liquidity risks and environmental and safety risks.

In order to reduce exploration risk, Celtic employs highly qualified and motivated professional employees who have demonstrated the ability to generate quality proprietary geological and geophysical prospects. To maximize drilling success, Celtic explores in areas that afford multi-zone prospect potential, targeting a range of shallower low-to-moderate-risk prospects with some exposure to select deeper high-risk prospects with high-reward opportunities.

Celtic has retained an independent engineering consulting firm that assists the Company in evaluating recoverable amounts of oil and gas reserves. Values of recoverable reserves are based on a number of variable factors and assumptions such as commodity prices, projected production, future production costs and government regulation. Such estimates may vary from actual results.

The Company mitigates its risk related to producing hydrocarbons through the utilization of the most advanced technology and information systems. In addition, Celtic strives to operate the majority of its prospects, thereby maintaining operational control. The Company does rely on its partners in jointly owned properties that Celtic does not operate.

Celtic is exposed to market risk to the extent that the demand for oil and gas produced by the Company exists within Canada and the United States. External factors beyond the Company's control may affect the marketability of oil and gas produced. These factors include commodity prices and variations in the Canada-United States currency exchange rate, which in turn respond to economic and political circumstances throughout the world. Oil prices are affected by worldwide supply and demand fundamentals, while natural gas prices are affected by North American supply and demand fundamentals. Celtic may periodically use physical fixed-price contracts and financial futures and options contracts to hedge its exposure against the potential adverse impact of commodity price volatility.

Exploration and production for oil and gas is very capital intensive. As a result, the Company relies on equity markets as a source of new capital. In addition, Celtic utilizes bank financing to support ongoing capital investment. Funds from operations also provide Celtic with capital required to grow its business. Equity and debt capital is subject to market conditions and availability may increase or decrease from time to time. Funds from operations also fluctuate with changing commodity prices.

Oil and gas exploration and production can involve environmental risks such as pollution of the environment and destruction of natural habitat, as well as safety risks such as personal injury. The Company conducts its operations with high standards in order to protect the environment and the general public. Celtic maintains insurance coverage for comprehensive and general liability as well as limited pollution liability. The amount and terms of this insurance are reviewed on an ongoing basis and adjusted as necessary to reflect current corporate requirements, as well as industry standards and government regulations.

BUSINESS OUTLOOK

Advisory Regarding Forward-looking Statements Certain information with respect to Celtic contained herein, including management's assessment of future plans and operations, contains forward-looking statements. These forward-looking statements are based on assumptions and are subject to numerous risks and uncertainties, certain of which are beyond Celtic's control, including the impact of general economic conditions, industry conditions, volatility of commodity prices, currency exchange rate fluctuations, imprecision of reserve estimates, environmental risks, competition from other explorers, stock market volatility and ability to access sufficient capital. As a result, Celtic's actual results, performance or achievement could differ materially from those expressed in, or implied by, these forward-looking statements and, accordingly, no assurance can be given that any events anticipated by the forward-looking statements will transpire or occur. In addition, the reader is cautioned that historical results are not necessarily indicative of future performance.

2006 Forecast Celtic is optimistic about its future prospects. The Company was successful in establishing a production base during the early months after commencing operations that provides a cash flow stream that can be reinvested in Celtic's ongoing exploration and development activity. Celtic is opportunity driven and is confident that it can continue to grow the Company's production base by building on its current inventory of development prospects and by adding new exploration prospects. Celtic will endeavour to maintain a high-quality product stream that, on a historical basis, receives a superior price with reasonably low production costs. In addition, the Company takes advantage of royalty incentive programs in order to further increase netbacks. Celtic will continue to focus its exploration efforts in areas of multi-zone potential for light-gravity crude oil and liquids-rich natural gas.

Celtic's Board of Directors has approved an initial capital expenditure budget in the amount of $120 million for 2006. This capital spending will be financed by funds from operations and bank credit lines.

After forecasting risked production discoveries, timing of production on-stream dates resulting from the Company's planned capital expenditures for 2005 and estimated decline rates on existing volumes, Celtic expects production in 2006 to average between 7,200 and 7,600 BOE/d (55% oil and 45% gas). This represents a 63% to 72% increase from average production of 4,423 BOE/d in 2005.

The Company's commodity price assumptions for 2006 are US$65.00 per barrel for WTI oil, US$8.00 per mmbtu for natural gas and a U.S./Canadian exchange rate of US$0.870.

After giving effect to the aforementioned production and commodity price assumptions and taking into account commodity risk price management contracts in place (as outlined in detail in the notes to the financial statements), funds from operations for 2006 is forecasted to be approximately $96.3 million or $3.31 per share ($3.17 per share, diluted) and net earnings is forecasted to be approximately $30.2 million or $1.04 per share ($1.00 per share, diluted). Changes in forecasted commodity prices can have a significant effect on estimated funds from operations and net earnings.

Bank debt, net of working capital, is estimated to reach $87.2 million by the end of 2006, or approximately 0.9 times forecasted 2006 funds from operations.

Celtic's capital expenditure budget for 2006 will see the Company participate at high working interests in the drilling of approximately 80 to 90 wells during the year. Celtic continues to pursue property acquisitions that would complement its existing asset base, and completion of such acquisitions would be over and above the Company's planned capital expenditure budget.

Celtic is excited about the growth prospects being generated in the Company and remains optimistic about the Company's ability to deliver continued per share growth in production, funds from operations and earnings. Given the Company's strong inventory of drilling locations, we look forward to continued growth in 2006.

ADDITIONAL INFORMATION

Additional information relating to Celtic is filed on SEDAR and can be viewed on their website at www.sedar.com. Further information relating to the Company is also available on its website at www.celticex.com.

On behalf of the Board of Directors

David J. Wilson
President and Chief Executive Officer
May 8, 2006

BALANCE SHEET

($ thousands)	As at March 31, 2006 [Unaudited]	As at December 31, 2005 [Audited]
ASSETS		
Current assets		
Cash and cash equivalents	$ 3,505	$ 1,812
Accounts receivable	25,237	22,582
Prepaid expenses	79	288
Financial derivative contracts	157	–
Assets held for disposal	9,450	–
	38,428	24,682
Other assets	1,361	1,160
Property, plant and equipment *(Note 2)*	249,050	216,271
	$ 288,839	$ 242,113
LIABILITIES		
Current liabilities		
Accounts payable and accrued liabilities	$ 51,535	$ 46,408
Bank debt *(Note 3)*	72,000	41,700
	123,535	88,108
Asset retirement obligation *(Note 4)*	4,609	4,294
Future income taxes *(Note 6b)*	27,103	23,864
	$ 155,247	$ 116,266
SHAREHOLDERS' EQUITY		
Share capital *(Note 5)*	$ 90,007	$ 89,812
Contributed surplus	1,794	1,545
Retained earnings	41,791	34,490
	$ 133,592	$ 125,847
	$ 288,839	$ 242,113

The accompanying notes form an integral part of these financial statements.

ON BEHALF OF THE BOARD OF DIRECTORS:

Director

Director

STATEMENT OF OPERATIONS AND RETAINED EARNINGS

Three months ended March 31, *($ thousands, except per share amounts)*	2006 [Unaudited]	2005 [Unaudited]
REVENUE		
Oil and natural gas	$ 33,875	$ 17,668
Royalties, net	(7,287)	(3,293)
Realized gain on financial derivatives	1,036	–
Unrealized gain (loss) on financial derivatives *(Note 9e)*	158	(276)
	$ 27,782	$ 14,099
EXPENSES		
Production	$ 5,305	$ 2,762
Transportation and selling	446	273
Interest	659	233
General and administrative	646	581
Stock-based compensation *(Note 5)*	265	202
Depletion, depreciation and amortization	9,834	5,687
Accretion of asset retirement obligation *(Note 4)*	57	38
	$ 17,212	$ 9,776
Earnings before taxes	$ 10,570	$ 4,323
Capital tax	30	37
Future income taxes *(Note 6a)*	3,239	1,268
Net earnings	$ 7,301	$ 3,018
Retained earnings, beginning of period	34,490	16,226
Retained earnings, end of period	$ 41,791	$ 19,244
Earnings per share		
Basic	$ 0.25	$ 0.12
Diluted *(Note 7)*	$ 0.24	$ 0.11

The accompanying notes form an integral part of these financial statements.

STATEMENT OF CASH FLOWS

Three months ended March 31, ($ thousands)	2006 [Unaudited]	2005 [Unaudited]
OPERATING ACTIVITIES		
Net earnings	$ 7,301	$ 3,018
Items not affecting cash:		
Depletion, depreciation and amortization	9,834	5,687
Accretion of asset retirement obligation	57	38
Stock-based compensation	265	202
Unrealized loss (gain) on financial derivatives	(158)	276
Future income taxes	3,239	1,268
Funds from operations	$ 20,538	$ 10,489
Change in non-cash operating working capital *(Note 10)*	1,633	(5,458)
Cash provided by operating activities	$ 22,171	$ 5,031
FINANCING ACTIVITIES		
Increase in bank debt	$ 30,300	$ 10,150
Issue of common shares, net of costs	178	205
Cash provided by financing activities	$ 30,478	$ 10,355
INVESTING ACTIVITIES		
Property, plant and equipment expenditures	$ (52,464)	$ (21,706)
Property, plant and equipment acquisitions	(232)	(1,947)
Property, plant and equipment dispositions	10,342	30
Change in other assets	(201)	–
Change in non-cash investing working capital *(Note 10)*	(8,402)	8,189
Cash used in investing activities	$ (50,957)	$ (15,434)
Net change in cash and cash equivalents	$ 1,692	$ (48)
Cash and cash equivalents, beginning of period	1,813	62
Cash and cash equivalents, end of period	$ 3,505	$ 14

The accompanying notes form an integral part of these financial statements.

NOTES TO THE INTERIM FINANCIAL STATEMENTS

For the interim period ended March 31, 2006
(All tabular amounts in thousands, unless otherwise stated)
(Unaudited)

NOTE 1 NATURE OF BUSINESS AND BASIS OF PRESENTATION

Celtic Exploration Ltd. ("Celtic" or the "Company") was incorporated under the *Business Corporations Act* (Alberta) on April 16, 2002 as Desco Exploration Ltd. The Company changed its name to Celtic Exploration Ltd. on September 30, 2002. Celtic is an oil and natural gas exploration, development and production company based in Calgary, Alberta, Canada. The Company's operations are focused in Western Canada, primarily in Alberta.

The interim financial statements of the Company have been prepared following the same accounting policies and methods of computation as the financial statements of the Company for the year ended December 31, 2005. The disclosure below is incremental to that included in the annual financial statements. In this regard, these interim financial statements should be read in conjunction with the financial statements and notes thereto for the year ended December 31, 2005.

These financial statements are stated in Canadian dollars and have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from these estimates.

NOTE 2 PROPERTY, PLANT AND EQUIPMENT

At March 31, 2006	**Cost**	**Accumulated depletion, depreciation and amortization**	**Net book value**
Oil and gas properties, plant and equipment	$ 312,902	$ 67,076	$ 245,826
Asset retirement obligation costs	4,427	1,591	2,836
Head office assets	638	250	388
	$ 317,967	$ 68,917	$ 249,050

At December 31, 2005	**Cost**	**Accumulated depletion, depreciation and amortization**	**Net book value**
Oil and gas properties, plant and equipment	$ 270,555	$ 57,388	$ 213,167
Asset retirement obligation costs	4,168	1,471	2,697
Head office assets	632	225	407
	$ 275,355	$ 59,084	$ 216,271

At March 31, 2006, oil and gas properties with a cost of $26.9 million (December 31, 2005 – $16.7 million) relating to undeveloped properties have been excluded from the depletion and depreciation calculation.

Future capital costs required to develop proved reserves in the amount of $10.0 million (2005 – $12.0 million) are included in the depletion and depreciation calculation.

Celtic does not capitalize any interest or general and administrative expenses that are not directly related to exploration and development activities. During the three months ended March 31, 2006, the Company capitalized $0.1 million (2004 – $0.1 million) with respect to employee salaries directly relating to exploration and development activities.

NOTE 3 BANK DEBT

	March 31, 2006	December 31, 2005
Demand operating loan	$ 52,000	$ 21,700
Bankers' acceptances	20,000	20,000
	$ 72,000	$ 41,700

Celtic has a committed term credit facility with Canadian financial institutions. The authorized borrowing amount under this facility is $100.0 million. Interest is payable monthly for borrowings through direct advances. Interest rates fluctuate based on a pricing grid and range from bank prime to bank prime plus 1.5%, depending upon the Company's then current debt to cash flow ratio of between less than one times and greater than three times. At March 31, 2006, interest was payable at bank prime. Under the credit facility, borrowings through the use of bankers' acceptances are also available. The Company has a fixed-rate bankers' acceptance in the amount of $20.0 million maturing on April 17, 2006 at an aggregate interest rate of 4.6%. Security is provided for by a floating charge debenture over all assets in the amount of $250.0 million, general assignment of book debts and a fixed charge on the Company's major producing petroleum and natural gas properties.

Repayments of principal are not required provided that the borrowings under the facility do not exceed the authorized borrowing amount and the Company is in compliance with all covenants, representations and warranties. The credit facility revolves until May 4, 2007, at which time the banks will complete their annual reviews.

NOTE 4 ASSET RETIREMENT OBLIGATION

The following table provides a reconciliation of the carrying amount of the obligation associated with the retirement of oil and gas properties:

	March 31, 2006	December 31, 2005
Asset retirement obligation, beginning of year	$ 4,294	$ 3,307
Liabilities incurred, net of liabilities disposed	258	797
Liabilities settled	–	(44)
Revisions to estimated liabilities	–	21
Accretion expense	57	213
Asset retirement obligation, end of year	$ 4,609	$ 4,294

The key assumptions, on which the carrying amount of the asset retirement obligations is based, include a credit-adjusted risk-free rate of 8.5% and an inflation rate of 2.2%. The total undiscounted amount of the estimated cash flows required to settle the obligations was $13.6 million (December 31, 2005 – $12.4 million). The expected timing of payment of the cash flows required to settle the obligations ranges from 5.8 years to 51.2 years.

NOTE 5 SHARE CAPITAL

Authorized Unlimited number of common shares.
Unlimited number of preferred shares.

Issued The following table summarizes the changes in common shares outstanding up to the period ended March 31, 2006:

	Common shares	Amount
Balance, December 31, 2004	25,835	$ 59,446
Issued for cash on exercise of stock options	138	550
Amount relating to exercised options previously recorded as contributed surplus	–	63
Issued for cash through private placement	3,000	30,750
Share issue costs, after future income taxes	–	(997)
Balance, December 31, 2005	28,973	$ 89,812
Issued for cash on exercise of stock options	55	178
Amount relating to exercised options previously recorded as contributed surplus	–	17
Balance, March 31, 2006	**29,028**	**$ 90,007**

(a) Stock options Celtic has a stock option plan that provides for granting of stock options to directors, officers, employees and consultants. Stock options granted under the stock option plan have a maximum term of five years to expiry. Vesting is determined by the Company's board of directors. However, the majority of the options granted vest equally over a three-year period commencing on the first anniversary date of the grant. The exercise price of each stock option granted is determined as the closing market price of the common shares on the Toronto Stock Exchange on the day of grant. Each stock option granted permits the holder to purchase one common share of the Company at the stated exercise price.

The following table summarizes the changes in stock options outstanding up to the period ended March 31, 2006:

	Number of options	Average exercise price
Balance, December 31, 2004	1,928	$ 5.28
Granted	466	11.22
Exercised	(138)	3.99
Forfeited	–	–
Balance, December 31, 2005	2,256	$ 6.58
Granted	155	12.25
Exercised	(55)	3.63
Forfeited	–	–
Balance, March 31, 2006	**2,356**	**$ 7.02**

The Company uses the fair-value method to record stock-based compensation expense with respect to stock options granted. The fair value of each option granted is estimated on the date of grant using the Black-Scholes option pricing model with weighted average assumptions for grants as follows:

	2006	2005
Risk-free interest rate	**3.44%**	3.29%
Expected life (years)	**3.0**	3.0
Expected volatility	**31%**	33%
Expected dividend yield	**0%**	0%
Fair value of options granted during the period ($/share)	**2.43**	2.28

The following table summarizes information regarding stock options outstanding at March 31, 2006:

Range of exercise prices per share	Number of options outstanding	Weighted average remaining term in years	Weighted average exercise price per share for options outstanding	Number of options exercisable	Weighted average exercise price per share for options exercisable
$ 2.01 to $ 3.50	455	1.5	$ 3.04	455	$ 3.04
$ 3.51 to $ 5.00	120	1.9	$ 4.06	120	$ 4.06
$ 5.01 to $ 6.50	748	2.6	$ 5.80	207	$ 5.70
$ 6.51 to $ 8.00	382	3.4	$ 7.72	127	$ 7.72
$ 8.01 to $ 9.50	30	3.6	$ 8.65	10	$ 8.65
$ 9.51 to $11.00	185	4.0	$ 10.69	63	$ 10.68
$11.01 to $12.50	436	4.6	$ 11.81	–	$ –
Total	2,356	3.0	$ 7.02	982	$ 4.88

NOTE 6 INCOME TAXES

(a) Future income tax expense The provision for income taxes differs from the expected amount calculated by applying the combined federal and provincial corporate income tax rate as a result of the following:

Three months ended March 31,	2006	2005
Earnings before taxes	**$ 10,570**	$ 4,323
Statutory combined federal and provincial income tax rate	**35.62%**	37.62%
Expected income taxes	**3,765**	1,626
Increase (decrease) resulting from:		
Non-deductible Crown payments	**645**	542
Non-deductible stock-based compensation costs	**94**	72
Non-taxable provincial royalty credits (ARTC)	**(15)**	(30)
Allowable resource allowance deduction	**(800)**	(744)
Benefit relating to changes in future income tax rates	**(452)**	(200)
Other adjustments	**2**	2
Provision for future income taxes	**$ 3,239**	$ 1,268

(b) Future income tax liability The components of future income taxes are as follows:

	March 31, 2006	December 31, 2005
Future income tax liabilities:		
Property, plant and equipment	$ 29,322	$ 26,072
Unrealized financial derivative gains	53	–
Future income tax assets:		
Asset retirement obligation costs	(1,561)	(1,455)
Share issue costs	(666)	(708)
Other income tax assets	(45)	(45)
Future income taxes	$ 27,103	$ 23,864

NOTE 7 EARNINGS PER SHARE

The Company uses the treasury stock method to determine the dilutive effect of stock options and other dilutive instruments. Under this method, only "in-the-money" dilutive instruments impact the calculations in computing diluted earnings per share.

In computing diluted earnings per share, 0.9 million (2005 – 1.0 million) shares were added to the 29.0 million (2005 – 25.8 million) weighted average number of common shares outstanding during the year for the dilutive effect of stock options.

NOTE 8 COMMITMENTS

The Company is committed to payments under a rental agreement for office space as follows:

	Amount
2006	$ 192
2007	506
2008	506
2009	506
2010	506
2011	169
	$ 2,385

Rental leases relating to office space expire on April 30, 2011.

NOTE 9 FINANCIAL INSTRUMENTS

(a) Fair values of financial assets and liabilities Financial instruments of the Company consist mainly of cash and cash equivalents, receivables, payables and bank debt. At March 31, 2006, there were no significant differences between the carrying amounts reported on the balance sheets and their estimated fair values.

(b) Credit risk The majority of the Company's accounts receivable is in respect of oil and gas operations. Celtic generally extends unsecured credit to these third parties, and therefore, the collection of accounts receivable may be affected by changes in economic or other conditions and may accordingly impact the Company's overall credit risk. Celtic has not experienced any material credit loss in the collection of receivables in 2006.

(c) Interest rate risk The Company is exposed to fluctuations in interest rates on its bank debt. Interest rate risk is mitigated through short-term fixed-rate borrowings using bankers' acceptances.

(d) Foreign exchange rate risk The Company is exposed to the risk of changes in the Canadian/U.S. dollar exchange rate on sales of commodities that are denominated in U.S. dollars or directly influenced by U.S. dollar benchmark prices.

(e) Commodity risk management From time to time, the Company may use financial derivative instruments to manage its exposure to fluctuations in commodity prices and foreign currency exchange rates. Under the terms of certain financial derivative contracts, Celtic may be required to provide security from time to time depending on the underlying market value of those contracts.

The Company accounts for financial derivative instruments using the Canadian accounting standard outlined in the *CICA Handbook Accounting Guideline 13, "Hedging Relationships."* This guideline addresses the identification, designation and effectiveness of financial contracts for the purpose of applying hedge accounting. Under this guideline, financial derivative contracts must be designated to the underlying revenue or expense stream that they are intended to hedge, and tested to ensure they remain sufficiently effective. For transactions that do not qualify as designated hedges, the Company applies a fair-value method of accounting by initially recording an asset or liability, and recognizing changes in the fair value of the derivative instrument in income.

The following is a summary of oil sales price derivative contracts in effect as at March 31, 2006 that have fixed future sales prices (fixed oil prices are based on the West Texas Intermediate ["WTI"] Index):

Daily quantity	Remaining term of contract	Fixed price per barrel (bbl)
750 bbls/d	April 1 to December 31, 2006	US$61.20
300 bbls/d (costless collar)	April 1 to December 31, 2006	US$60.00 (floor) US$65.20 (cap)
750 bbls/d (costless collar)	April 1 to December 31, 2006	US$60.00 (floor) US$70.10 (cap)

The fair value of the above oil contracts, mark-to-market at March 31, 2006, is an unrealized loss of $2.3 million.

The following is a summary of natural gas sales price derivative contracts in effect as at March 31, 2006 that have fixed future sales prices (fixed natural gas prices are based on the New York Mercantile Exchange ["NYMEX"] Index):

Daily quantity	Remaining term of contract	Fixed price per mmbtu
4,000 mmbtu/d	April 1 to October 31, 2006	US$10.01
4,000 mmbtu/d	November 1 to December 31, 2006	US$11.03
10,000 mmbtu/d	January 1 to March 31, 2007	US$10.47
10,000 mmbtu/d (costless collar)	April 1 to December 31, 2007	US$7.50 (floor) US$12.40 (cap)

The fair value of the above natural gas contracts, mark-to-market at March 31, 2006, is an unrealized gain of $2.5 million.

In addition to financial derivative instruments, the Company may, from time to time, enter into physical fixed-price sales contracts in order to manage its exposure to fluctuations in commodity prices and foreign currency exchange rates. The following is a summary of natural gas physical fixed-price sales contracts in effect as at March 31, 2006 that have fixed future sales prices (fixed natural gas prices are based on the AECO-C and NIT Index):

Daily quantity	Remaining term of contract	Fixed price per gigajoule (GJ)
6,000 GJ/d	April 1 to October 31, 2006	CA$9.77
6,000 GJ/d	November 1 to December 31, 2006	CA$10.84

NOTE 10 SUPPLEMENTAL CASH FLOW INFORMATION

Changes in non-cash working capital, excluding bank debt:

Three months ended March 31,	2006	2005
Accounts receivable	$ (2,655)	$ (1,265)
Prepaid expenses	209	25
Assets held for disposal	(9,450)	–
Accounts payable and accruals	5,127	3,971
Change in non-cash working capital	$ (6,769)	$ 2,731
Relating to:		
Operating activities	$ 1,633	$ (5,458)
Investing activities	(8,402)	8,189
Change in non-cash working capital	$ (6,769)	$ 2,731

During the reporting period, the Company made the following cash outlays in respect of interest expense and capital taxes:

Three months ended March 31,	2006	2005
Interest expense	$ 702	$ 306
Capital tax	10	60

Celtic
Exploration Ltd.

CORPORATE INFORMATION

BOARD OF DIRECTORS

Robert J. Dales [2, 3, 4]
President, Valhalla Ventures Inc.

William C. Guinan [1, 5]
Partner, Borden Ladner Gervais LLP

Eldon A. McIntyre [2, 3, 4]
President, Jarrod Oils Ltd.

Neil G. Sinclair [2, 4, 5]
President, Sinson Investments Ltd.

David J. Wilson [3, 5]
President & Chief Executive Officer,
Celtic Exploration Ltd.

OFFICERS

David J. Wilson
President & Chief Executive Officer

Sadiq H. Lalani
Vice President,
Finance & Chief Financial Officer

Alan G. Franks
Vice President, Operations

Michael R. Shea
Vice President, Land

David C. Morgenstern
Vice President, Exploration

1 Chairman of the Board
2 Member of the Audit Committee
3 Member of the Reserves Committee
4 Member of the Compensation Committee
5 Member of the Disclosure Committee

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STOCK EXCHANGE LISTING

Toronto Stock Exchange
Trading symbol "CLT"

ABBREVIATIONS

bbls	*barrels*
mbbls	*thousand barrels*
bbls/d	*barrels per day*
BOE	*barrels of oil equivalent*
mBOE	*thousand barrels of oil equivalent*
BOE/d	*barrels of oil equivalent per day*
mcf	*thousand cubic feet*
mmcf	*million cubic feet*
bcf	*billion cubic feet*
mmcf/d	*million cubic feet per day*
mmbtu	*million British Thermal Units*
GJ	*gigajoules*
AECO-C	*Alberta Energy Company "C" Meter Station of the Nova Pipeline System*
API	*American Petroleum Institute*
ARTC	*Alberta Royalty Tax Credit*
CICA	*Canadian Institute of Chartered Accountants*
WTI	*West Texas Intermediate*

CONVERSION OF UNITS

Imperial = *Metric*
1 acre = *0.4 hectares*
2.5 acres = *1 hectare*
1 bbl = *0.159 cubic metres*
6.29 bbls = *1 cubic metre*
1 foot = *0.3048 metres*
3.281 feet = *1 metre*
1 mcf = *28.2 cubic metres*
0.035 mcf = *1 cubic metre*
1 mile = *1.61 kilometres*
0.62 miles = *1 kilometre*
1 mmbtu = *1.054 GJ*
0.949 mmbtu = *1 GJ*
Natural gas is equated to oil
on the basis of 6 mcf = *1 BOE.*