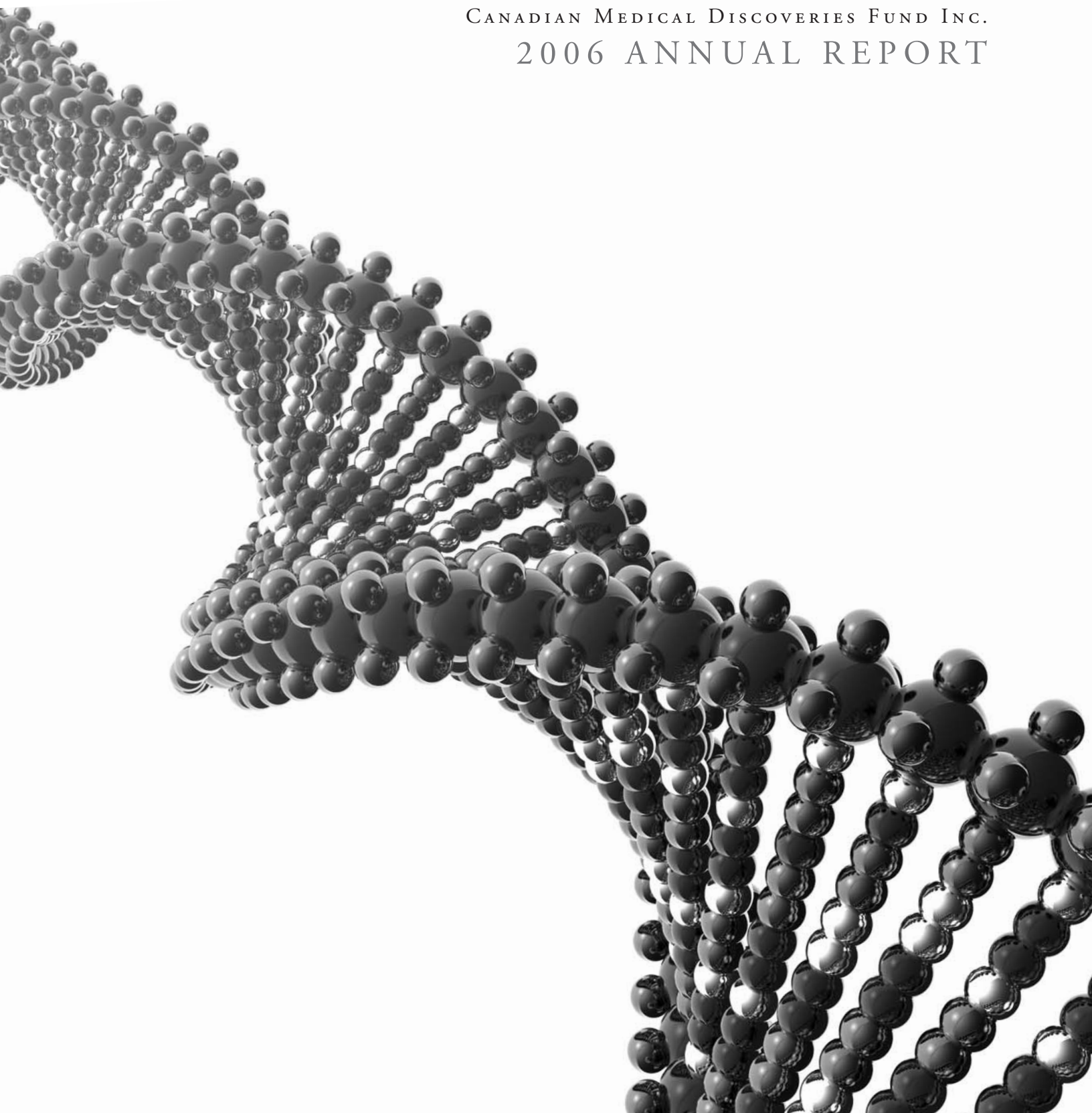




CANADIAN MEDICAL DISCOVERIES FUND INC.
2006 ANNUAL REPORT



MANAGEMENT DISCUSSION OF FUND PERFORMANCE

This annual management report of fund performance contains financial highlights and accompanies the audited annual financial statements of Canadian Medical Discoveries Fund Inc. (the "Fund"). You may request a copy of the Fund's unaudited interim or audited annual financial statements, the current proxy voting policies and procedures or quarterly portfolio disclosure at no cost by calling our toll free number 1-866-299-7929, by writing to us at Canadian Medical Discoveries Funds, BCE Place, 181 Bay Street, Suite 3740, Toronto, Ontario, M5J 2T3, or by visiting our website at www.cmdf.com.

The annual management report of fund performance and accompanying financial statements have been approved by the Board of Directors. The financial statements were audited by Ernst & Young LLP, the external auditors of the Fund.

The Fund's proxy voting disclosure record for the period ended June 30, 2006 will be available free of charge upon request at any time after August 31, 2006, by visiting our website at www.cmdf.com.

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MANAGEMENT DISCUSSION OF FUND PERFORMANCE

August 31, 2006

INVESTMENT OBJECTIVE AND STRATEGIES

The Fund's investment objective is to achieve long-term capital appreciation through investment in eligible Canadian businesses engaged in the health sciences sector, with emphasis on those businesses involved in early-stage commercialization of research or product development. The health sciences sector encompasses a broad range of scientific disciplines and industries that relate to or have an impact on health care including, without limitation, life sciences, biotechnology, diagnostics, medical devices, drug discovery and development, health care delivery services and e-health. The manager of the Fund, Medical Discovery Management Corp. (the "Manager", or, "MDMC") will seek investments in a variety of product development initiatives as well as businesses with products, technologies or services in different stages of development.

RISK FACTORS

An investment in the Fund is highly speculative in nature. The Labour-Sponsored Investment Fund ("LSIF") program was launched to kick-start the venture capital market in Ontario and across Canada. Essentially, the federal and provincial governments provided investors with a tax credit to direct money into promoting the growth of businesses by creating a new source of financing in the market segment. Over the years, the LSIF program has evolved beyond the tax credit into an opportunity for investors to access private equity investments to which they otherwise would typically not have access. Investments in LSIFs are highly speculative in nature and suitable only for investors able to make a long-term investment with no guarantee of returns in the near or long-term. Some of the more specific risks associated with the Fund are listed below.

Availability of Suitable Investments

There is no assurance that suitable investments in eligible Canadian health sciences businesses will be found to fulfill the investment objectives of the Fund.

Legislative Changes

On September 30, 2005 the Ontario Government announced its plan to end its involvement with the LSIF program and eliminate the Ontario tax credits. For the next three RRSP seasons (2006, 2007 and 2008 taxation years) the Ontario tax credits will remain the same, followed by reductions for the 2009 and 2010 taxation years. The Ontario government does not currently intend to offer any provincial tax credits to investors beyond the 2011 RRSP season. On March 23, 2006 a number of measures relating to the transition of the labour sponsored fund program and Ontario Act which were developed in consultation with the labour sponsored investment fund industry were announced in the 2006 Ontario budget. These proposed measures which, among other things, loosened the investment restrictions relating to investments made pursuant to the Ontario Act received Royal Assent on May 18, 2006 and are now law.

Nature of Portfolio Companies

The business of the Fund is to make eligible investments in small businesses directly, many of which will have a limited operating history. These investments may require a number of years in order to mature and generate the returns expected by the Fund and investors. A significant portion of the investment portfolio of the Fund will be comprised of investments in private companies. These investments are likely to mature and generate returns at different times, which could create an irregular pattern in the net asset value of the Class A Shares. In addition, losses on unsuccessful private company investments are often realized before gains on successful private companies are realized. An investment in Class A Shares is highly speculative in nature and suitable only for investors able to make a long-term investment.

Many of the investee companies are developing products or services which require significant additional development, testing and investment prior to any final commercialization. The likelihood of the long-term success of the Fund must be considered in light of the expenses, difficulties and delays frequently encountered in connection with the development of new technology, and the competitive and regulatory environments of the biotechnology industry.

Industry Concentration

Since the focus of the Fund is on investments in companies engaged in or providing services to the health sciences sector, the Net Asset Value of the Fund may be more volatile than that of portfolios with a more conventional diversified investment focus. However, the Fund attempts to diversify its investment portfolio by investing in a variety of product development initiatives and by investing in businesses which are in different stages of development. The value of the investment portfolio may fluctuate as a result of factors affecting the health sciences sector generally.

External Factors

The value of the investments fluctuates with general economic conditions including the level of interest rates, corporate earnings, economic activity, the Canadian dollar and other factors. The risks associated with such fluctuations may be amplified for investors as emerging businesses are often affected by external events to a greater degree than larger, more established businesses. In addition, eligible health sciences businesses, by virtue of their size and stage of development, will be affected more than larger, more mature entities by external events, including downturns in general economic conditions.

Valuation of Investments

The principal investments of the Fund are private companies for which no quoted market value exists. Since no formal market exists, the market values of investee companies are based on the historic carrying cost or estimates of the fair mar-

ket value of the assets of the investee companies and may not reflect amounts for which they can actually be sold. The daily valuation process is subjective to a degree and, to the extent that actual valuations differ from estimates, existing investors may gain a benefit or suffer a loss. All public investments are valued at their respective market values, extracted through public exchanges.

Liquidity of Class A Shares

No formal market exists at present through which Class A Shares may be sold and none is expected to develop. There are restrictions on the transfer and redemption of Class A Shares and shareholders may not be able to dispose of Class A Shares other than through the redemption of shares by the Fund. Except in limited circumstances, no Class A Shares may be redeemed before the expiration of at least eight years from the date on which such shares were issued. Investors who redeem prior to the expiry of the eight year holding period must repay the tax credit they received upon purchase of the shares as well as incur an early redemption penalty fee.

Penalty Taxes and Revocation of Registration

If the Fund does not comply with the investment requirements of the Ontario Act (the "Ontario Act") or the Income Tax Act, Canada (the "Federal Tax Act"), it will be subject to penalty taxes, other penalties and possible revocation of registration under such acts. The investment performance of the Fund may be adversely affected if the Fund becomes subject to such special taxes and penalties.

Follow on Financings

It is likely that the Fund's investee companies will require additional financing to support their continued development and fully implement their business strategies. The ability of the investee company to raise capital is sometimes dependent upon the cyclical nature of the capital markets. To the extent that such capital cannot be raised at all, or on commercially favourable terms, or the Fund does not or is unable to par-

ticipate in any such subsequent rounds of financing, this could have a material adverse effect on the value of the investment.

RESULTS OF OPERATIONS

The net asset value of the Fund at August 31, 2006 was \$192.41 million. There were 28,534,252 Class A shares outstanding.

Revenue

The Fund had revenue of \$1.3 million for the year ended August 31, 2006 compared to \$1.4 million for the year ended August 31, 2005. This revenue is composed of primarily interest and dividend income earned on the venture investments and marketable securities.

Investment Performance

For the year ended August, 31 2006, the Fund generated a negative investment performance. The annual return for Class A Shares was -13.48%. The LSIF Peer Group Average performance, as tracked by Globefund representing the average of the 119 LSIFs in Canada, for the year ended August 31, 2006 was -0.94%. The Fund's performance was largely a result of value erosion with the Fund's investment portfolio together with normal operating costs. The Fund took several write downs of value in its private company portfolio throughout the year which impacted the negative performance. Offsetting these charges were gains in some of the publicly-traded securities and increased valuations as a result of substantial arm's length financings completed at new valuations on some of the portfolio's private investee companies. The companies contributing positively include Systems Xcellence Inc. (SXC-T), AnorMED Inc. (AOM-T), MethylGene Inc. (MYG-T) and NeuroMed Pharmaceuticals Inc. During the year, the Fund partially or fully exited its positions at a gain in AnorMED Inc. (AOM-T) (\$3.1 million), Neurocrine Biosciences Inc. (NBIX-N) (\$4.1 million), and Systems Xcellence Inc. (SXC-T) (\$10.3 million). Positions disposed of at a loss include Hemosol Corp. (-\$1.6 million), Migenix Inc. (-\$0.8 million) and Nexia Biotechnologies Inc. (-\$1.2 million)

together with Ellipsis Neurotherapeutics Inc. (-\$0.6 million) and IDx Inc. (-\$0.9 million) in corporate action related transactions. During the year, the Fund made approximately \$9.3 million of follow-on investments in Resonant Medical Technologies Inc., Targanta Therapeutics Corp., GeminX Biotechnologies Inc., Cytochroma Inc., NeuroMed Pharmaceuticals and ViOptix Canada Inc.

Expenses and Liabilities

On an absolute basis, operating expenses decreased during the fiscal year 2006 as compared to the prior year. The average daily net assets for the year were almost \$43 million less than the comparative 2005 period due in large part to \$18 million in net redemptions for the year. Any operating expenses calculated as a percentage of the net assets of the Fund, such as management fees and some administration fees, have decreased accordingly.

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RELATED PARTY TRANSACTIONS

The Manager may be deemed to be a related party. Please refer to the section titled "Management Fees" which outlines the 2006 and 2005 fees paid to these related parties.

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RECENT DEVELOPMENTS

CHANGE OF CONTROL OF THE MANAGER

On December 14, 2005, Fairway Asset Management Corp. ("Fairway", formerly Impax Capital Corp.) signed an agreement to, indirectly, acquire all of the issued and outstanding shares of the Manager, MDMC. This change received securities regulatory approval in January 2006. Under new management, MDMC is committed to

improving the Fund's performance and will do so by focusing on reducing the operating costs and streamlining the marketing and investment initiatives of the Fund.

FAIRWAY AND JOVIAN PARTNERSHIP

In May 2006, Jovian Capital Corporation ("Jovian") through its wholly-owned subsidiary Jovian Asset Management Inc. acquired 100% of the

Class A Shares and 49% of the Class C Shares in Fairway, parent company to MDMC.

Jovian is a publicly-traded management and holding company listed on the TSX Venture Exchange (JVN). Jovian has interests in a variety of financial service firms specializing in wealth and asset management. The Jovian group of companies operates as a national financial services organization with approximately \$12 billion of client assets.



FINANCIAL HIGHLIGHTS

The following tables show selected key financial information about the Fund, which are intended to help you understand the Fund's financial performance for the last five years. This information is derived from the Fund's annual audited financial statements.

The Fund's net asset value (NAV) per share

For the years ended August 31,	2006	2005	2004	2003	2002
Net asset value, beginning of year ⁽¹⁾	\$ 7.79	\$ 8.68	\$ 10.10	\$ 9.35	\$ 11.16
INCREASE (DECREASE) FROM OPERATIONS:					
Total revenue	0.04	0.04	0.09	0.15	0.25
Total expenses	(0.38)	(0.35)	(0.45)	(0.43)	(0.44)
Realized gains (losses) for the year	(0.43)	(0.17)	0.25	(0.77)	0.66
Unrealized gains (losses) for the year	(0.25)	(0.36)	(0.99)	1.91	(2.16)
Total increase (decrease) from operations ⁽²⁾	(1.02)	(0.84)	(1.10)	0.86	(1.69)
Net asset value, end of year ⁽¹⁾	\$ 6.74	\$ 7.79	\$ 8.68	\$ 10.10	\$ 9.35

⁽¹⁾ Net asset value is based on the actual number of shares outstanding at the relevant times.

⁽²⁾ The increase (decrease) from operations is based on the weighted average number of shares outstanding over the financial year.

RATIOS AND SUPPLEMENTARY DATA

For the years ended August 31,

	2006	2005	2004	2003	2002
Net assets (000's) ⁽¹⁾	\$ 192,407	\$ 239,685	\$ 294,089	\$ 344,042	\$ 315,318
Number of shares outstanding ⁽¹⁾	28,534,252	30,779,619	33,892,055	34,054,870	33,728,363
Management expense ratio ⁽²⁾	4.84%	4.28%	4.61%	4.59%	4.30%
Portfolio turnover rate ⁽³⁾	12.93%	15.79%	15.86%	23.39%	8.89%
Trading expense ratio ⁽⁴⁾	0.07%	0.21%	0.31%	0.28%	0.79%
Closing market price or pricing NAV ⁽¹⁾	\$ 6.74	\$ 7.79	\$ 8.68	\$ 10.10	\$ 9.35

⁽¹⁾ This information is provided as at the last business day of the year shown.

⁽²⁾ Management expense ratio includes all fees, expenses, capital taxes, and Goods and Services Tax and is expressed as an annualized percentage of the average net assets administered during the year.

⁽³⁾ The Fund's portfolio turnover rate indicates how active the Fund's portfolio advisor manages its portfolio investments. A portfolio turnover rate of 100% is equivalent to the Fund buying and selling all of the securities in its port-

folio once in the course of the year. The higher a fund's portfolio turnover rate in a year, the greater the trading costs payable by the fund in the year, and the greater the chance of an investor receiving taxable capital gains in the year. There is not necessarily a relationship between a high turnover rate and the performance of a fund.

⁽⁴⁾ The trading expense ratio represents total commissions and other portfolio transaction costs expressed as an annualized percentage of daily average net assets during the year.

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MANAGEMENT FEES

The management fee is based on 3% of the daily net asset value calculated and charged monthly in arrears. The services received in exchange for the management fee include but are not limited to:

- Provision of office facilities and personnel, financial reporting, marketing, registrar, transfer agency and other shareholder administrative services;
- Retention and supervision of investment advisors;
- Assistance with the formulation and refinement of the investment objectives, restrictions, policies and procedures of the Fund as well as the identification and evaluation of potential eligible investments, the negotiation of the terms and conditions attributable to the investments, the monitoring of the business and

financial performance of the investments and the provision of management assistance and advice to the investments as may be considered necessary;

- Preparation and filing of all prospectus documents, information documents, notices and other material in connection with the meetings of shareholders of the Fund.

ADMINISTRATION FEES

The Fund has retained Talvest (LSVC) Inc. ("Talvest") to provide or cause to be provided ongoing marketing, registrar, transfer agency and other shareholder administration services. The fee paid by the Fund to Talvest for the services that Talvest provides is 0.85% per annum of the net asset value of the Fund less the amount of the fees payable for liquid portfolio management services.

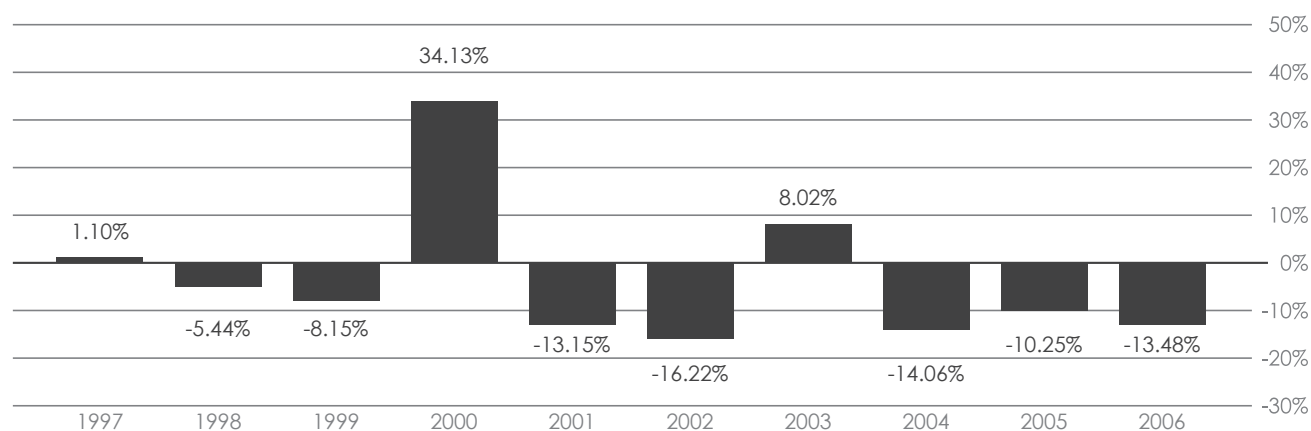
PAST PERFORMANCE

The performance information shown does not take into account sales, redemption, distribution or other optional charges that would have reduced returns on performance. The Fund's past performance is no guarantee of how it will perform in the future.

YEAR-BY-YEAR RETURNS (%)

The following bar chart shows the Fund's performance for the years ended August 31 in each of the years shown. It shows in percentage terms how an investment made in the Fund on September 1st (the first day of the Fund's financial year) would have increased or decreased by the end of the fiscal year on August 31.

CANADIAN MEDICAL DISCOVERIES FUND INC.



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ANNUAL COMPOUND RETURNS

The table below summarizes the annual compound total returns to August 31, 2006 for the periods indicated. As a basis of comparison, the LSIF industry average compound returns, as posted on www.globefund.com, for the same periods

have also been provided. The LSIF industry average is the most representative broad-based securities market index as it includes all the Ontario-based LSIFs.

Fund Name	1 Year	3 Year	5 Year	10 Year	Since Inception
Canadian Medical Discoveries Fund Inc.	- 13.48%	- 12.61%	- 9.59%	- 4.70%	- 3.26%
LSIF industry average*	- 0.94%	0.19%	- 4.04%	0.50%	N/A

* Source: www.globefund.com as at August 31, 2006

SUMMARY OF INVESTMENT PORTFOLIO

Below is a summary of the Fund's investment portfolio as at August 31, 2006 [dollar amounts in thousands]

Investment Classification	Fair Value of Investments \$	% of Net Asset Value %
Drug Discovery & Development	83,746	43.5%
Medical Equipment & Technology	38,275	19.9%
Health Care Delivery & Information Technology	18,562	9.7%
Intellectual Property & Early Stage	21,968	11.4%
	162,551	84.5%

TOP 25 POSITIONS AS A PERCENTAGE OF THE NET ASSET VALUE

Investment	Sector Classification
Cash and Short-Term Investments	Cash and Short-Term Investments
Systems Xcellence Inc.	Health Care Delivery & IT
GeminX Biotechnologies Inc.	Drug Discovery & Development
University Medical Discoveries Inc.	Intellectual Property & Early Stage
Viron Therapeutics Inc.	Drug Discovery & Development
ActivBiotics (Ontario) Inc.	Drug Discovery & Development
Ambit Bioscience (Canada) Corporation	Drug Discovery & Development
Praxim SA	Medical Equipment & Technology
Tm Bioscience Corporation	Medical Equipment & Technology
MedTech Partners Inc.	Intellectual Property & Early Stage
Killix Ltd.	Medical Equipment & Technology
MedInnova Partners Inc.	Intellectual Property & Early Stage
Resonant Medical Technologies Inc.	Medical Equipment & Technology
PainCeptor Pharma (Ontario) Corporation	Drug Discovery & Development
NeuroMed Pharmaceuticals Ltd.	Drug Discovery & Development
Twinstrand Therapeutics Inc.	Drug Discovery & Development
Targanta Therapeutics Inc., Preferred and Common Shares	Drug Discovery & Development
IsoTis S.A.	Medical Equipment & Technology
Renovis Inc.	Medical Equipment & Technology
Trillium Therapeutics Inc.	Drug Discovery & Development
Protiva Biotherapeutics, Preferred Shares	Medical Equipment & Technology
Excel-Tech Ltd.	Medical Equipment & Technology
AdipoGenix (Canada) Inc., 8% Convertible Debenture	Drug Discovery & Development
PharmAthene Canada Inc., Preferred Shares	Drug Discovery & Development
Cytochroma Inc., Preferred Shares	Drug Discovery & Development

Top 25 Holdings As A Percentage Of Total Net Assets

83.2%

The summary of investment portfolio may change due to ongoing portfolio transactions of the Fund. A quarterly update is available by calling 1-866-299-7929, writing to BCE

Place, 181 Bay Street, Suite 3740, P.O. Box 750, Toronto, ON, M5J 2T3, or by visiting www.cmdf.com.

2006 ANNUAL FINANCIAL STATEMENTS

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The accompanying financial statements of Canadian Medical Discoveries Fund Inc. (the "Fund") are the responsibility of management. They have been prepared in accordance with Canadian generally accepted accounting principles using information available and include certain amounts that are based on management's best estimates and judgments.

Management has developed and maintains a system of internal controls to provide reasonable assurance that all assets are safeguarded and to produce relevant, reliable and timely financial information, including the accompanying financial statements.

The Board of Directors discharges its duties relating to the financial statements primarily through the activities of its Audit & Valuation Committee, which is comprised of members of the Board of

Directors. The Committee has the responsibility for determining the net asset value of the Fund, including the net asset value of the Class A shares of the Fund, as well as meeting with management and the external auditors to review both the financial statements and the results of the audit examination. The external auditors have unrestricted access to the Audit & Valuation Committee. The Committee also considers, for review by the Board of Directors and approval of the shareholders, the engagement or re-appointment of the external auditors.

These financial statements have been approved by the Board of Directors and have been audited by Ernst & Young LLP, Chartered Accountants, on behalf of the shareholders. The auditors' report outlines the scope of their audit and their opinion on the financial statements.



Steven J. Hawkins
President & Chief Executive Officer
Medical Discovery Management Corporation

October 10, 2006



Jason Mackey
Chief Financial Officer
Medical Discovery Management Corporation

AUDITORS' REPORT

To the Shareholders of
Canadian Medical Discoveries Fund Inc.

We have audited the statement of investment portfolio of Canadian Medical Discoveries Fund Inc. as at August 31, 2006 and the statements of financial position as at August 31, 2006 and 2005 and the statements of operations, changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of ma-

terial misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the investment portfolio of the Fund as at August 31, 2006 and the financial position as at August 31, 2006 and 2005 and the results of its operations, the changes in its net assets and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Ernst + Young LLP

Toronto, Canada,
October 10, 2006.

Chartered Accountants

STATEMENTS OF FINANCIAL POSITION

As at August 31,
[in thousands of dollars, except share and per share amounts]

	2006	2005
ASSETS		
Venture investments, at estimated fair value	\$ 162,551	\$ 217,164
Marketable securities, at estimated fair value	30,289	21,023
Cash	765	1,677
Accrued interest receivable	65	–
Prepaid expenses and other receivables	123	739
Subscriptions receivable	–	5
Amounts receivable for portfolio assets sold	–	870
Income taxes receivable	–	8
Total assets	193,793	241,486
LIABILITIES		
Accrued expenses	1,199	1,552
Redemptions payable	103	199
Taxes payable	25	–
Other accrued liabilities	59	50
Total liabilities	1,386	1,801
Net assets	\$ 192,407	\$ 239,685
Class A shares outstanding	28,534,252	30,779,619
Net asset value per Class A share	\$ 6.74	\$ 7.79

See accompanying notes

On behalf of the Board:



Director
Gordon A. McMillan



Director
Steven J. Hawkins

STATEMENTS OF OPERATIONS

Years ended August 31,
[in thousands of dollars, except share and per share amounts]

	2006	2005
INVESTMENT INCOME		
Interest income from marketable securities	\$ 862	\$ 880
Interest income from venture investments	157	539
Dividend income	234	-
Other income	73	21
	1,326	1,440
EXPENSES		
Management fees ^[note 1]	7,208	8,583
Administration fees ^[note 1]	2,019	2,434
Audit and related fees	308	230
Legal fees	296	266
Shareholder reporting costs	286	251
Directors fees and expenses	121	62
Custodian fees	48	19
Capital tax recovery	(11)	(173)
Other expenses	564	-
	10,839	11,672
Net operating loss before income taxes	(9,513)	(10,232)
Recovery of income taxes ^[note 4]	-	(56)
Net operating loss	(9,513)	(10,176)
Net realized loss on venture investments	(12,665)	(5,659)
Net change in unrealized depreciation on venture Investments	(7,289)	(11,881)
Net loss on investments	(19,954)	(17,540)
Decrease in net assets from operations	\$ (29,467)	\$ (27,716)
Decrease in net assets from operations per Class A share	(1.01)	(0.86)

See accompanying notes

STATEMENTS OF CHANGES IN NET ASSETS

Years ended August 31,
[in thousands of dollars]

	2006	2005
Decrease in net assets from operations	\$ (29,467)	\$ (27,716)
Capital transactions		
Proceeds from issue of Class A shares ^[note 3]	1,918	5,103
Amounts paid for Class A shares redeemed ^[note 3]	(19,466)	(31,215)
Commissions and other share issuance costs on Class A shares	(263)	(576)
	(17,811)	(26,688)
Decrease in net assets for the year	(47,278)	(54,404)
Net assets, beginning of year	239,685	294,089
Net assets, end of year	\$ 192,407	\$ 239,685

See accompanying notes

STATEMENTS OF CASH FLOWS

Years ended August 31,
[in thousands of dollars]

	2006	2005
OPERATING ACTIVITIES		
Net operating loss	\$ (9,513)	\$ (10,176)
Net change in non-cash working capital balances related to operations	1,044	930
Cash used in operating activities	(8,469)	(9,246)
FINANCING ACTIVITIES		
Proceeds from issue of Class A shares	1,918	5,103
Amounts paid for Class A shares redeemed	(19,466)	(31,215)
Commissions and other share issuance costs paid	(263)	(576)
Cash used in financing activities	(17,811)	(26,688)
INVESTING ACTIVITIES		
Proceeds on disposal of venture investments	50,966	25,626
Purchase of venture investments	(16,308)	(46,779)
Proceeds on disposal of marketable securities	30,535	154,475
Purchase of marketable securities	(39,825)	(96,300)
Cash provided by investing activities	25,368	37,022
Net increase (decrease) in cash during the year	(912)	1,088
Cash, beginning of year	1,677	589
Cash, end of year	\$ 765	\$ 1,677

See accompanying notes

STATEMENT OF INVESTMENT PORTFOLIO

As at August 31, 2006

[in thousands of dollars, except share amounts]

Venture investments	Maturity Date/ Expiration Date	Par value/ Number of shares	%	\$
Drug discovery and development - at cost				
2056273 Ontario Inc., Common		75		2,708
ActivBiotics (Ontario) Inc., Class A Voting		40		-
ActivBiotics (Ontario) Inc., Class C Non-voting Preferred		9,727,626		6,179
AdipoGenix (Canada) Inc., Common		10		-
AdipoGenix (Canada) Inc., 8% Convertible Debenture	On demand	3,040,750		3,041
Adnavance Technologies Inc., Class A Preferred		3,290,514		1,810
Adnavance Technologies Inc., Warrants	1/31/2014	3,161,874		-
Aegera Therapeutics Inc., Class A Preferred		4,615,510		4,970
Aegera Therapeutics Inc., Class D Preferred		414,106		365
Aegera Therapeutics Inc., Common		441,113		238
Ambit Bioscience (Canada) Corporation, Class A		4		-
Ambit Bioscience (Canada) Corporation, Class C		11,628,107		6,081
Cytochroma Inc., Class A Preferred		700,000		700
Cytochroma Inc., Class B Preferred		400,000		1,000
Cytochroma Inc., 12% Convertible Debenture	10/12/2006	1,452,000		1,452
GeminX Biotechnologies Inc., Class B Preferred		945,274		1,189
GeminX Biotechnologies Inc., Series A Preferred		7,136,641		8,505
GeminX Biotechnologies Inc., Warrants	(various to 8/6/2014)	408,117		-
Inimex Pharmaceuticals Inc., Special Voting Stock		4,900,038		-
Inimex Pharmaceuticals Inc., 12% Convertible Debenture	6/29/2007	500,000		500
Inimex Veterinary Research Ltd., Class A Preferred		4,900,038		2,000
MethylGene Inc., Common		709,699		2,900
NeuroMed Pharmaceuticals Ltd., Special Voting Stock		2,693,835		-
NeuroMed Pharmaceuticals Ltd., Series B-1 Exchangeable Shares		160,057		571
NeuroMed Pharmaceuticals Ltd., Series B-2 Exchangeable Shares		120,043		429
NeuroMed Pharmaceuticals Ltd., Series C-1 Exchangeable Shares		625,000		818
NeuroMed Pharmaceuticals Ltd., Series C-2 Exchangeable Shares		543,478		784
NeuroMed Pharmaceuticals Ltd., Series D Special Voting Stock		1,232,713		1,988
NeuroMed Pharmaceuticals Ltd., Common Exchangeable Shares		12,544		2

Venture investments	Maturity Date/ Expiration Date	Par value/ Number of shares	%	\$
Drug discovery and development - at cost (cont'd)				
NeuroMed Pharmaceuticals Inc., Series B-1 Special Voting Stock		160,057		-
NeuroMed Pharmaceuticals Inc., Series B-2 Special Voting Stock		120,043		-
NeuroMed Pharmaceuticals Inc., Series C-1 Special Voting Stock		625,000		-
NeuroMed Pharmaceuticals Inc., Series C-2 Special Voting Stock		543,478		-
NeuroMed Pharmaceuticals Inc., Series D Special Voting Stock		1,232,713		-
NeuroMed Pharmaceuticals Inc., Canadian Special Voting		12,544		-
NPS Pharmaceuticals Inc., Common		6,900		105
NPS Pharmaceuticals Inc., Options (CAD)	4/15/2009	1,296		-
NPS Pharmaceuticals Inc., Options (USD)	(various to 6/13/2013)	27,000		-
Nysa Membrane Technologies Inc., Class A Preferred		13,055		600
PainCeptor Pharma Corp., Class A Special Voting		5,973,333		-
PainCeptor Pharma Corp., Class B Special Voting		4,177,154		-
PainCeptor Pharma Corp., Class C Special Voting		1,388,418		-
PainCeptor Pharma (Ontario) Corporation, Class A Preferred Exchangeable		5,973,333		2,261
PainCeptor Pharma (Ontario) Corporation, Class B Preferred Exchangeable		4,177,154		1,739
PainCeptor Pharma (Ontario) Corporation, Class C Preferred Exchangeable		1,388,418		526
PharmAthene Canada Inc., Class C Non-voting Preferred		2,591,654		2,907
PharmAthene Canada Inc., 8% Convertible Debenture	7/13/2007	2,000,000		2,275
PharmAthene Canada Inc., Warrants	10/7/2014	1,243,994		-
Protiva Biotherapeutics, Series 1 Class A Preferred		8,999,995		1,801
Protiva Biotherapeutics, Series 2 Class A Preferred		5,999,994		1,201
Protiva Biotherapeutics, Series 5 Class A Preferred		1,099,991		220
Protiva Biotherapeutics, 15% Convertible Debenture	11/30/2006	900,000		900
Protiva Biotherapeutics, 15% Promissory Note	11/30/2006	378,666		379
Protiva Biotherapeutics, 18% Promissory Note	5/31/2007	750,000		750
Protiva Biotherapeutics, Warrants	8/31/2006	1,642,856		-
Star Bio Investments Inc., Common		158,580		3,960
Targanta Therapeutics Inc., Class A Preferred Exchangeable		1,375,758		1,250
Targanta Therapeutics Inc., Class B Preferred Exchangeable		1,831,050		1,000
Targanta Therapeutics Inc., Common		500,000		1,000
Targanta Therapeutics Inc., 8% CDN Convertible Promissory Note	10/24/2006	291,250		291

Venture investments	Maturity Date/ Expiration Date	Par value/ Number of shares	%	\$
Drug discovery and development - at cost (cont'd)				
Targanta Therapeutics Inc., 8% USD Convertible Promissory Note	10/24/2006	1,750,000		2,043
Targanta Therapeutics Corp., Series A Special Voting		1,375,758		-
Targanta Therapeutics Corp., Series B Special Voting		1,831,050		-
Targanta Therapeutics Corp., Common Special Voting		500,000		-
Transition Therapeutics Inc., Common		3,686,967		2,048
Trillium Therapeutics Inc., Class A Preferred		1,879,700		2,500
Trillium Therapeutics Inc., Common		1,000,000		770
Trillium Therapeutics Inc., Warrants	(various to 12/19/2008)	563,910		-
Twinstrand Therapeutics Inc., Series 1 Class C Preferred		886,330		1,343
Twinstrand Therapeutics Inc., Series 1 Class D Preferred		125,190		162
Twinstrand Therapeutics Inc., Series 2 Class C Preferred		1,377,779		2,480
Twinstrand Therapeutics Inc., Series 2 Class D Preferred		110,000		99
Twinstrand Therapeutics Inc., Warrants	(various to 5/31/2009)	754,703		-
Viron Therapeutics Inc., Class A Preferred		997,729		7,004
Drug discovery and development - at cost			47.2	89,844
Unrealized depreciation				(6,098)
Drug discovery and development - at estimated fair value			51.5	83,746

Medical equipment and technology - at cost

Agrisoma Biosciences, Common		673,638		2,164
Excel-Tech Ltd., Common		1,352,465		3,000
IsoTis S.A., Common		2,956,638		8,065
Praxim SA, Series 1 Preferred		191,556		5,000
Praxim SA, Series 2 Preferred		130,000		1,442
Renovis Inc., Common		202,548		2,712
Resonant Medical Inc., Series A Preferred		235,849		500
Resonant Medical Technologies Inc., Class A Exchangeable		1,179,245		2,500
Resonant Medical Technologies Inc., Class B Preferred Exchangeable		797,872		1,875
SMC Ventures Inc., Class A Common		622,450		-
Spectral Diagnostics Inc., Common		196,078		500
Spectral Diagnostics Inc., Common, restricted		2,045,918		962
Spectral Diagnostics Inc., Zero Coupon Promissory Note	12/31/2010	1,156,250		962
Spectral Diagnostics Inc., \$0.47 strike Warrants	6/8/2011	231,250		-
Tm Bioscience Corporation, Common		5,828,264		8,381
Tm Bioscience Corporation, Deferred Common Share		540		-
Tm Bioscience Corporation, Options	(various to 2/1/2010)	12,424		-
Tm Bioscience Corporation, Warrants	(various to 11/12/2007)	1,421,919		-

Venture investments	Maturity Date/ Expiration Date	Par value/ Number of shares	%	\$
Medical equipment and technology - at cost (cont'd)				
ViOptix Inc., Series X Preferred		1		-
ViOptix Canada Inc., Class C Preferred		9,104,524		3,385
ViOptix Canada Inc., 8% Convertible Debenture	10/11/2014	1,991,700		1,992
ViOptix Canada Inc., 12% Promissory Note	9/10/2006	75,000		84
ViOptix Canada Inc., Class A Voting		400		-
Xillix Ltd., Variable Rate Convertible Debenture	12/31/2010	5,000,000		5,000
Medical equipment and technology - at cost			25.5	48,524
Unrealized depreciation				(10,249)
Medical equipment and technology - at estimated fair value			23.6	38,275
Health care delivery and information technology - at cost				
Lifemark Health, Limited Partnership Units		33,030		330
Network Health Inc., Class A Common		707,681		1,283
Network Health Inc., Class B Common		707,681		-
Systems Xcellence Inc., Common		1,035,086		4,002
Health care delivery and information technology - at cost			2.9	5,615
Unrealized appreciation				12,947
Health care delivery and information technology - at estimated fair value			11.4	18,562
Intellectual property and early stage - at cost				
LPBP Inc., Class A Common		350,331		-
MedInnova Partners Inc., Common		50,000		-
MedInnova Partners Inc., Class B Preferred		10,500,000		10,500
MedTech Partners Inc., Common		50,000		-
MedTech Partners Inc., Non-voting Preferred Class A		13,000,000		13,000
MEF Finance Corp., Common		50		50
Neuroscience Development Inc., Common		50,000		-
Neuroscience Development Inc., Class A Preferred		1,700,000		1,700
T2C2/Bio, Limited Partnership Units		5,000		4,931
University Medical Discoveries Inc., Common		1,000,000		-
University Medical Discoveries Inc., Non-voting Preferred		149,000,000		14,900
Working Ventures CMDF Queen's Scientific Breakthrough Fund Inc., Class A Preferred		137,952		1,380
Intellectual property and early stage - at cost			24.4	46,461
Unrealized depreciation				(24,493)
Intellectual property and early stage - at estimated fair value			13.5	21,968
Venture investments - at cost			100.0	190,444
Unrealized depreciation of venture investments				(27,893)
Venture investments - at estimated fair value^[1]			100.0	162,551
[1] Venture investments - at estimated fair value is comprised of				
Public companies				36,283
Private companies				126,268
				162,551

Marketable securities	Cost \$	Par value \$	Fair value \$
SHORT-TERM INVESTMENTS			
Issuer			
Lancaster Short Term Investment Fund*	30,289	30,289	30,289
Total marketable securities - at estimated fair value	30,289	30,289	30,289
Total investments - at estimated fair value			192,840
Other liabilities			
[consisting of cash, receivables, prepaid expenses less liabilities]			(433)
Net assets			192,407

* Lancaster Short Term Investment Fund earns interest at variable rates based on actual yield achieved and is redeemable upon demand. During 2006, the interest rate on the short term investment ranged between 2.63% and 4.28%.

See accompanying notes

NOTES TO FINANCIAL STATEMENTS

(in thousands of dollars except share amounts)
August 31, 2006

1. CORPORATE STATUS AND ACTIVITIES

Canadian Medical Discoveries Fund Inc. (the "Fund", or, "CMDF") is a venture capital investment corporation sponsored by The Professional Institute of the Public Service of Canada (the "Sponsor"). The Fund is a labour-sponsored investment fund ("LSIF") corporation under the Community Small Business Investment Funds Act, Ontario (the "Ontario Act") and is a prescribed labour-sponsored venture capital corporation under the Income Tax Act, Canada (the "Tax Act"). The Fund is also a qualifying fund pursuant to the Labour-Sponsored Venture Capital Corporations Act, Saskatchewan (the "Saskatchewan Act"). The Fund is subject to investment restrictions under federal and certain provincial legislation.

The Fund's primary objective is to achieve long-term capital appreciation through investment in eligible Canadian businesses engaged in the health sciences sector, with emphasis on those businesses involved in early-stage commercialization of research or product development. The Fund seeks to achieve its investment objective through a number of investment strategies.

MANAGEMENT AND ADMINISTRATION ARRANGEMENTS

Fairway Asset Management Corp. ("Fairway", formerly Impax Capital Corp.), indirectly, acquired all of the issued and outstanding shares of the manager of the Fund, Medical Discovery Management Corp. ("MDMC" or the "Manager") and became the sole shareholder of MDMC in January 2006. In May 2006, Jovian Capital Corporation ("Jovian") acquired an indirect non-control-

ling interest in MDMC through its wholly-owned subsidiary, Jovian Asset Management, when it acquired 100% of the Class A Shares and 49% of the Class C Shares of Fairway Asset Management Corp., formerly Impax Capital Corp., parent company to MDMC. Jovian is a publicly-traded company listed on the TSX Venture Exchange (JVN). Jovian is a management and holding company with interests in a variety of financial service firms specializing in wealth and asset management. The Jovian group of companies operates as a national financial services organization.

The Fund has retained MDMC pursuant to a management agreement dated December 1, 2004 (the "Management Agreement"). The Management Agreement has an initial term of ten years and shall be automatically extended for successive one year periods on each anniversary date of the agreement. Either party may terminate further automatic extensions by providing written notice to the other party. The Manager is entitled to receive a fee of 3% of the average daily net asset value of the Fund calculated and charged monthly in arrears. The services received in consideration of the management fee include services which are reasonably required in respect of the daily operations and management of the affairs of the Fund.

The Manager is also entitled to a performance fee equal to 25% of all Realized Income earned from each Portfolio Company, calculated at the end of each fiscal quarter of the Fund in respect of Realized Income received in that quarter. Before a performance fee is earned with respect to a full or partial disposition of a particular Portfolio Company, the Fund must have first fully recouped an amount equal to all cash the Fund invested in that Portfolio Company. Before a performance fee is paid, the Portfolio Income at the

end of the particular fiscal quarter must exceed the Threshold Amount calculated as at the end of the fiscal quarter. In the event that, after the payment of all such performance fees, the Portfolio Income at that time would then be reduced below the Threshold Amount calculated as at the end of that fiscal quarter, then the amount of performance fees that are paid at that time shall be limited to the amount that permits the Portfolio Income to meet the Threshold Amount calculated as at the end of that fiscal quarter.

For the purposes of the performance fee:

The Fund is deemed to have acquired (i) each investment in a Portfolio Company held at November 30, 2004 for cash equal to its fair value at November 30, 2004 as determined by the Fund's Valuation Committee, and (ii) each investment in a Portfolio Company after November 30, 2004 for the actual cash amounts invested.

"Realized Income" is the amount by which all cash (net of commissions and other costs) received by the Fund in respect of each Portfolio Company exceeds the Fund's cash investment in that particular Portfolio Company;

"Portfolio Company" means a business in which the Fund has made an investment which comprises part of the Fund's venture investment portfolio;

"Portfolio Income" means all distributions or revenue received or receivable by the Fund and all realized and unrealized gains and losses on investments in all Portfolio Companies after November 30, 2004 less all Performance Fees paid after November 30, 2004;

"Threshold Amount" means the sum of all Quarterly Threshold Amounts after November 30, 2004. The **"Quarterly Threshold Amount"** is, in each fiscal quarter, the amount of Portfolio Income that, when annualized, would provide a rate of return equal to the greater of 6% and the average of the quoted 5-year Government of Canada bond rate on the first day of the fiscal quarter and the eleven immediately preceding fiscal quarters, of the average daily amount invested in the venture investment portfolio.

No performance fee has been paid or is payable to the Manager as of the fiscal year ended August 31, 2006.

The Fund has retained Talvest (LSVC) Inc. (the "Administrator") by agreement (the "Administration Agreement"), which terminates on December 31, 2006, to provide ongoing marketing, registrar, transfer agency and other shareholder administration services (including services associated with the printing and mailing of the annual prospectus) and preparation of shareholder reporting information. The Administrator receives a fee calculated and charged monthly based on an annual fee of 0.85% of the net asset value of the Fund, less the fee paid for the administration of the Fund's liquid asset portfolio. Effective January 15, 2003, the Fund retained TD Asset Management Inc. to administer the Fund's liquid asset portfolio at a fee of 0.05% of its market value.

RESEARCH-ORIENTED INVESTMENT FUND ELIGIBILITY

The Fund issued its Class A shares as a Research-Oriented Investment Fund ("ROIF") pursuant to the Ontario Act for the 2006 taxation year. The 5% ROIF tax credit is applicable to purchases of Class A shares, in addition to the 15% provincial tax credits. As a result of issuing Class A shares as a ROIF, the Fund must hold at least 50% of its investments, measured on a cost basis as a percentage of its capital available for investment (as defined in the Ontario Act), in specified research business investments. A specified research business investment is, generally, a business which incurs at least 50% of its total expenses as scientific research and experimental development expenses at a permanent establishment in Canada.

2. SIGNIFICANT ACCOUNTING POLICIES

VENTURE INVESTMENTS

Venture investments are recorded at the estimated fair value which is determined on a going concern basis or, if appropriate, assuming an orderly disposition over a reasonable period of time. The valuation process uses, as much as possible, objective measures, but it is still based on assumptions and includes inherent uncertainties. Actual values realized when the Fund ultimately disposes of an investment will vary from the current estimated fair value and the variation may be material.

Specified derivative transactions, investments and positions not otherwise addressed below will be valued in accordance with the principles set out in National Instrument 81-102.

Public Companies

Venture investments in securities having quoted market values and which are publicly traded on a recognized stock exchange, and are not otherwise restricted or thinly traded, are recorded at values based on the quoted market prices on the dates of the statements of financial position. Warrants and options to purchase additional securities in public companies are valued using widely accepted financial valuation models. Purchases and sales of investments in public companies are recorded on a trade-date basis.

Private Companies

Venture investments in securities not having quoted market values ("private companies") are originally recorded at cost. They are re-valued if a substantial arm's length transaction establishes a different value. Warrants and options to purchase additional securities in private companies are valued at their original cost. Where performance of an investment varies adversely from the Fund's expectations, it is written down to its estimated fair value where appropriate.

The process of valuing venture investments for which no published market exists is inevitably based on inherent uncertainties and the resulting values may differ from values that would have been used had a ready market existed for the venture investments.

Purchases and sales of investments in private companies are recorded as at the date the Fund obtains a legal right to demand the securities purchased or to collect the proceeds of a sale.

Debt Instruments and Convertible Securities

The fair value of convertible securities is generally determined as the greater of their principal amount plus accrued interest and their estimated fair value as if they have been converted, with such estimated fair value being determined on the basis described above.

Venture investments in debt instruments are valued at their principal amount, with accrued interest or discounts earned included in interest receivable. Where payments are in arrears or there are other indications that it is unlikely the Fund will fully realize on the investment, a write down or other provision is made.

Other Securities

Investments in limited partnerships and Community Small Business Investment Funds are valued based on the Fund's pro-rata share of the estimated fair value of their underlying investments.

MARKETABLE SECURITIES

Marketable securities consist of short-term, interest bearing investments which have a term to maturity of less than one year at the date of acquisition. Marketable securities are recorded at cost plus accrued interest, which approximates fair value.

Purchases and sales of marketable securities are recorded on a trade-date basis.

PERFORMANCE FEES

Performance fees are recorded as a payable to the Manager when a performance fee is actually due and payable under the terms of the Management Agreement.

The net asset value of the Class A shares recognizes a contingent performance fee payable, if any, based on the assumption that all the venture investments are liquidated at the estimated fair value as at the date of the financial statements.

INDEPENDENT VALUATOR

The Fund has engaged its auditors, with the assistance of a qualified business valuator on the audit team, to provide an opinion that the fair value per Class A share, at each fiscal year end of the Fund, is not materially different from the net asset value determined by the Audit & Valuation Committee.

INCOME RECOGNITION

Interest and other income are recorded on an accrual basis. Dividend income is recorded when and as declared.

SALES COMMISSIONS AND OTHER SHARE ISSUANCE COSTS

Sales commissions and other share issuance costs are treated as capital transactions and reflected in the statements of changes in net assets. Fees paid by shareholders on the early redemption of shares are credited to other income.

MANAGEMENT'S ESTIMATE

The preparation of financial statements in conformity with Canadian generally accepted accounting principles ("GAAP") requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Management believes that the estimates used in preparing its financial statements are reasonable and prudent; however, actual results could differ from these estimates.

3. SHARE CAPITAL

The following is a description of the authorized and issued share capital:

AUTHORIZED

Class A Shares

Unlimited number of Class A shares, issuable at net asset value to individuals only, discretionary dividend entitlement, voting, entitled to elect a minority of the Directors of the Fund, restrictions on transfer and redemption, redeemable at the net asset value less any redemption fee.

A holder of Class A shares may require the Fund to redeem his or her Class A shares if the redemption occurs more than eight years after the date of issue of the Class A shares. Class A shares may also be redeemed at any time prior to the expiry of the eight-year period if an amount generally equal to the federal and provincial tax credits is withheld from the net asset value less any redemption fee attributable to the shares on the redemption date and the withheld tax credits are paid to the appropriate federal and provincial authorities. A Class A shareholder may also require the Fund to redeem his or her Class A shares prior to the expiry of the eight-year period without withholding of the federal and provincial tax credits in certain designated circumstances.

In any financial year, the Fund is not required to, but may at its option if sufficient liquid assets are available, redeem Class A shares having an aggregate redemption price exceeding 20% of the net asset value of the Fund at the beginning of the year. Any unsatisfied redemption requests during a fiscal year will be honoured prior to any redemption requests submitted in a subsequent fiscal year. The Fund is entitled to suspend the right of Class A shareholders to redeem shares or delay the payment date of the redemption amount with the prior consent of the Ontario Securities Commission.

Class B Shares

25,000 Class B shares, issuable only to the Sponsor of the Fund, non-participating, voting, entitled to elect two-thirds majority of the Directors of the Fund, redeemable at the purchase price.

Class C Shares

Unlimited number of Class C shares, issuable in series, entitled to receive dividends at the discretion of the Board of Directors, non-voting.

SHARE ACTIVITY

The following table shows the share activity for the years ended August 31:

	# of Class A Shares
Balance at August 31, 2004	33,892,055
Issued during the year	596,517
Redeemed during the year	(3,708,953)
Balance at August 31, 2005	30,779,619
Issued during the year	239,702
Redeemed during the year	(2,485,069)
Balance at August 31, 2006	28,534,252

At August 31, 2006 and 2005, there was 1 Class B share outstanding which was issued for nominal consideration

4. INCOME TAXES

Under the Tax Act, no income taxes are payable by the Fund on dividends received from Canadian corporations and income taxes payable on capital gains will be fully refundable on a formula basis when shares of the Fund are redeemed or capital gains dividends are paid or deemed to be paid by the Fund to its shareholders. Taxes payable on investment income earned by the Fund will be partially refundable upon the payment or deemed payment of dividends by the Fund to the shareholders.

The Fund records the refundable portion of its income taxes as an asset, as it intends to recover all of its refundable income taxes through the

deemed payment of a dividend by capitalizing the appropriate amount of its income and/or realized capital gains pro rata to the stated capital account for its Class A Shares. If, and to the extent, the Fund increases the stated capital of the Class A Shares, the holder of the shares will be deemed to have received a dividend and/or a realized capital gain and the adjusted cost base of the shareholder's shares will be increased by the amount of any deemed dividend.

The Fund's provision for (recovery of) income taxes consists of Large Corporations Tax.

The Tax Act and the Ontario Act set minimum levels of qualifying venture investments for the Fund. If the minimum level of qualifying venture invest-

ments is not met under each statute, the Fund will be subject to defined taxes and penalties.

As at August 31, 2006, the Fund has non-capital losses of approximately \$48,000 (2005 - \$55,000) that expire at various times up to the year 2026 and that may be carried forward and used to reduce taxable income in future years. As at August 31, 2006, the Fund has available capital losses of approximately \$56,000 (2005 - \$41,000) that may be carried forward indefinitely to offset future taxable capital gains. The benefit, if any, of these losses has not been recognized in the financial statements.

The tax amounts reflected in these financial statements are based on management's best estimate of the amounts that will ultimately be assessed. This determination is based on numerous factors such as the pace at which the Fund makes qualifying venture investments, the amount of share capital raised and redeemed, and the net income and the undistributed net realized gains (losses) on sales of investments by the Fund. Should actual events not agree with the estimates made by management of the Fund, material adjustments to the tax amounts may be required.

The Federal Tax and Ontario Acts contain restrictions on the nature and amount of short-term investments, bonds and venture investments held by the Fund. In the event that the minimum investment requirements are not met, the Fund may be subject to defined income tax penalties.

5. STAGES OF DEVELOPMENT OF INVESTMENT PORTFOLIO

The Fund categorizes its investment portfolio into the stages presented below. The stages are defined by the Fund as:

- Seed: Companies in this stage perform scientific proof of concept projects which often emerge from academic research or innovations
- Early: Companies in this stage generally have products in the preclinical or early clinical development phases also known as Phase I or Phase II trials
- Late: Companies in this stage have products which are in Phase III trials, in the registration phase or are on the market
- Public: Companies in this stage are traded on a recognized stock exchange and can be in any of the stages described above

Stage of Development	Number of Companies	Cost of Venture Investments \$	% of Total Investment Portfolio at Cost %	Fair Value of Investments \$	% of Total Investment Portfolio at Fair Value %
Seed	8	46,460	24.4%	21,969	13.5%
Early	22	74,267	39.0%	69,245	42.6%
Late	10	32,118	16.9%	31,742	19.5%
Public	10	37,599	19.7%	39,595	24.4%
	50	190,444	100.0%	162,551	100.0%

6. COMMISSION CHARGES ON PORTFOLIO TRANSACTIONS

Total commission paid in respect of portfolio transactions during the year was \$164 (2005 - \$194).

7. COSTS OF DISTRIBUTION

Total costs of distribution of the Fund's securities consist of commission charges of \$115 (2005 - \$394) and share issue costs of \$148 (2005 - \$182).

8. NON-MONETARY TRANSACTIONS

In the normal course of business, the Fund completed various non monetary transactions whereby the Fund disposed of or received investments in exchange for consideration other than cash. The gain or loss is determined based on the fair value of the consideration received. The fair value of the asset given up was \$16,087 (2005 - \$11,533) and the fair value of the consideration received was \$15,429 (2005 - \$11,533) resulting in a loss of \$658 (2005 - \$nil) which is included in the net realized loss on venture investments in the Statements of Operations.

9. COMMITMENTS

In the normal course of business, the Investment Committee of the Fund approves investments. The actual funding of these investments is contingent upon agreements being finalized or the investee companies achieving certain milestones. As at August 31, 2006, there were a total of \$1,890 (2005 - \$1,427 and US\$3,425) of further approved investments for which funding has not been completed.

10. CONTINGENT LIABILITY

As a result of the performance fee agreement which became effective on December 1, 2004, the Manager is entitled to a performance fee of \$nil based on the realized gains as at August 31, 2006 (2005 - \$105). No amount has been recognized as payable in the financial statements in

2006 or 2005 since, before the performance fee can be paid, Portfolio Income must exceed the Threshold Amount.

11. COMPARATIVE FINANCIAL STATEMENTS

The comparative financial statements have been reclassified from statements previously presented to conform to the presentation of the 2006 financial statements.

12. STATEMENT OF PORTFOLIO TRANSACTIONS

The Fund will provide, without charge, a Statement of Portfolio Transactions (unaudited) upon request by any shareholder of the Fund to the Manager c/o Felcom Data Services Inc. at 26 Wellington Street East, Suite 206, Toronto, Ontario M5E 1S2.

13. SUBSEQUENT EVENTS

Proposed Amalgamation

On September 27, 2006, the Board of Directors of Canadian Medical Discoveries Fund Inc. and Canadian Medical Discoveries Fund II Inc. ("CMDF II"), also managed by the Manager, approved a plan of arrangement to amalgamate CMDF and CMDF II. Subject to regulatory and shareholder approval, the amalgamation would occur either in late 2006 or early 2007.

Appointment of New Investment Advisor

On October 6, 2006, CMDF and CMDF II announced the appointment of Jove Investment Management Inc. ("Jove") as the Investment Advisor to the Funds. Jove has a strong team of professionals that specialize in life sciences investment management. MDMC is responsible for the payment of all fees payable to Jove.

Change of Control of the Manager

As previously discussed in Note 1, Jovian acquired an indirect non-controlling interest in MDMC on

May 9, 2006. Jovian, through its wholly owned subsidiary, has agreed to acquire the balance of the securities of Fairway, and thereby, indirectly own 100% of the securities of the Manager. This indirect change of control of MDMC, which is subject to customary approvals, is anticipated to be completed in December of 2006.

MDMC has provided the management of the CMDF Funds since their inception, beginning with CMDF in 1994, and will continue to manage the CMDF Funds under the existing management agreements.

Change of Service Provider

On October 9, 2006, MDMC entered into an agreement with Felcom Data Services Inc. ("Felcom"), a wholly-owned subsidiary of Jovian, pursuant to which Felcom is to provide certain shareholder and administrative services to the Fund (such services previously provided by Talvest (LSVC) Inc.), including services related to marketing, processing of orders, maintaining of shareholder records, preparing shareholder reporting, and fund accounting and reporting services. MDMC is responsible for the payment of all fees related to the services provided by Felcom.



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