

**VITAL ENERGY INC.**  
**MANAGEMENT DISCUSSION and ANALYSIS**  
**September 30, 2018**

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Vital Energy Inc. (the “Company” or “Vital”) is a public company and is incorporated in the Province of Alberta, Canada. The Company’s activities are the exploration for, development and production of oil and natural gas properties in Western Canada.

*The discussion and analysis that follows is a summary of Vital’s activities and results for the three and nine months ended September 30, 2018, its financial position as at September 30, 2018 and its future prospects. This Management’s Discussion and Analysis is dated as of November 26, 2018 and provides information on the activities of the Corporation and should be read in conjunction with the condensed interim financial statements for the three and nine months ended September 30, 2018 and the annual audited financial statements for the year ended December 31, 2017. All amounts are expressed in accordance with International Financial Reporting Standards (“IFRS”) and in Canadian dollars unless otherwise stated. Additional information is available on the Company’s website at [www.vitalenergyoil.com](http://www.vitalenergyoil.com) or on Sedar’s website at [www.sedar.com](http://www.sedar.com).*

### **Forward-Looking Statements**

*Certain statements contained in this document constitute "forward-looking statements". When used in this document, the words "may", "would", "could", "will", "intend", "plan", "propose", "anticipate", "believe", used by any of the Company’s management, are intended to identify forward-looking statements. Such statements reflect the Company’s forecasts, estimates and expectations, as they relate to the Company’s current views based on their experience and expertise with respect to future events and are subject to certain risks, uncertainties and assumptions. Many factors could cause the Company’s actual results, performance or achievements to be materially different from any future results, performance or achievements that may be expressed or implied by such forward-looking statements. Given these risks and uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements. The Company does not intend, and does not assume any obligation, to update any such factors or to publicly announce the result of any revisions to any of the forward-looking statements contained herein to reflect future results, events or developments unless required by law.*

*Actual results achieved will vary from the information provided herein as a result of numerous known and unknown risks and uncertainties and other factors. Such factors include, but are not limited to: risks associated with the Company’s stage of development; competitive conditions; share price volatility; risks associated with crude oil and natural gas exploration and development; risks related to the inherent uncertainty of reserves and resources estimates; possible imperfections in title to properties; the volatility of crude oil and natural gas prices and markets; environmental regulation and associated risks; loss of key personnel; operating and insurance risks; the inability to add reserves; risks associated with industry conditions; the ability to obtain additional financing on acceptable terms if at all; non operator activities; the inability of investors in certain jurisdictions to bring actions to enforce judgments; equipment unavailability; potential conflicts of interest; risks related to operations through subsidiaries; risks related to foreign operations; currency exchange rate risks and other factors, many of which are beyond the control of the Company. Accordingly, there is no representation by the Company that actual results achieved during the forecast period will be the same in whole or in part as that forecast. Further, the Company undertakes no obligation to update or revise any forward-looking statement or statements to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events, except as required by applicable securities laws.*

*Financial outlook information contained in this MD&A about prospective results of operations, financial position or cash flows is based on assumptions about future events, including economic conditions and proposed courses of action, based on management's assessment of the relevant information currently available. Readers are cautioned that such financial outlook information contained in this MD&A should not be used for purposes other than for which it is disclosed herein.*

### **Non-IFRS Measures**

*The financial data presented herein has been prepared in accordance with IFRS. The Company has also used certain measures of financial reporting that are commonly used as benchmarks within the oil and natural gas production industry in the following MD&A discussion. The measures are widely accepted measures of performance and value within the industry and are used by investors and analysts to compare and evaluate oil and natural gas exploration and producing entities. Most notably, these measures include "operating netback" and "funds flow from (used in) operations". Operating netback is a benchmark used in the crude oil and natural gas industry to measure the contribution of oil and natural gas sales and is calculated by deducting royalties and operating expenses from revenues. Funds flow from (used in) operations is cash flow from operating activities before changes in non-cash working capital, and is used to analyze operations, performance and liquidity. These measures are not defined under IFRS and should not be considered in isolation or as an alternative to conventional IFRS measures. These measures and their underlying calculations are not necessarily comparable or calculated in an identical manner to a similarly titled measure of another entity. When these measures are used, they are defined as "non IFRS" and should be given careful consideration by the reader.*

### **Note Regarding Boe and Mcf**

*In this MD&A, barrels of oil equivalent ("boe") is derived by converting gas to oil in the ratio of six thousand cubic feet ("Mcf") of gas to one barrel ("bbl") of oil (6 Mcf: 1 bbl) and one thousand cubic feet of gas equivalent ("Mcf") are derived by converting oil to gas in the ratio of one bbl of oil to six Mcf (1 bbl: 6 Mcf). Boe and Mcf may be misleading, particularly if used in isolation. A boe conversion of 6 Mcf of natural gas to 1 bbl of oil, or a Mcf conversion ratio of 1 bbl of oil to 6 Mcf of natural gas is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the well head.*

*Other terms used in this report are as follows:*

*boe - barrel of oil equivalent*

*boe/d – barrel of oil equivalent per day*

*WTI – West Texas Intermediate (a light oil reference price)*

*WCS – Western Canadian Select (a heavy oil reference price)*

### **Description of the Business**

Vital Energy Inc. (the "Company" or "Vital") is a public company whose shares trade on the TSXV under the symbol "VUX". Vital is incorporated in the Province of Alberta, Canada and its activities consist of exploration for, development and production of primarily light and medium gravity crude oil in Western Canada.

The Company operates from its head office in Calgary, Alberta located at Suite 888, 940 6<sup>th</sup> Avenue S.W., Calgary, Alberta, T2P 3T1.

## Overall Performance

### Highlights

- Production was 272 boe/d (“boe per day”) in the third quarter of 2018 versus 239 boe/d in the second quarter of 2018. The increase in production is primarily attributable to increased production in the Baxter Lake, Standard Hill and Gull Lake areas.
- Overall the company produced 25,075 boe in the third quarter of 2018 versus 21,791 boe in the second quarter of 2018 and again the increase in overall sales production was primarily from the Baxter Lake, Standard Hill and Gull Lake areas.
- Production operating costs in the third quarter of 2018 were \$17.07 per boe as compared to \$19.22 per boe incurred in the second quarter of 2018. The second quarter production costs reflect workover costs of \$6.01 per boe for the work performed at Baxter Lake and Gull Lake while workover costs were \$2.26 per boe in the third quarter.
- Average crude oil and natural gas price realized by the Company in the third quarter of 2018 was \$58.01 per boe as compared to \$56.61 per boe for the second quarter of 2018.
- The Company’s 2018 third quarter production was weighted 87% crude oil to 13% natural gas.

### Selected Financial Information

Selected financial information for the periods ended and as at September 30 is as follows:

	<b>2018</b>	2017	<b>2018</b>	2017
	<b>Three months ended Sept. 30</b>		<b>Nine months ended Sept. 30</b>	
Revenue	<b>\$1,454,524</b>	\$902,689	<b>\$3,536,376</b>	\$2,415,830
Net and comprehensive income (loss)	<b>\$18,117</b>	(\$236,976)	<b>(\$229,612)</b>	(\$653,835)
Net loss per share	<b>\$0.00</b>	\$0.00	<b>(\$0.01)</b>	(\$0.01)
Total assets as at Sept 30	<b>\$13,745,891</b>	\$12,569,382	<b>\$13,745,891</b>	\$12,569,382
Total non-current liabilities as at September 30	<b>\$1,163,369</b>	\$1,071,402	<b>\$1,163,39</b>	\$1,071,402

The revenue and net and comprehensive loss for the three and nine months ended September 30, 2018 has improved from the comparable period in 2017 as there was a significant increase in the realized price of oil.

### Properties

#### *Gull Lake*

In one of the Company’s core areas of operations, Gull Lake, Saskatchewan, Vital is the designated operator and maintains a 50% working interest. The property is covered with 3D seismic data and has 8 wells producing, or capable of producing, crude oil from the Roseray, Cantuar and Upper Shaunovan formations. This project has a salt water disposal facility and a gas collection pipeline system. In the Company’s opinion, there remains drilling opportunities on these lands. A new well drilled and completed in the third quarter of 2018 was equipped and put on production in the fourth quarter. Another new well was drilled and cased in the second quarter of 2018 and is currently standing pending further evaluation for a completion plan.

Vital's net daily oil and natural gas production for the first nine months of 2018 was 161 boe/d as compared to 140 boe/d for the comparable period in 2017. This increase in production is mainly attributable to the well drilled in the second quarter of 2017 being on production for nine months in 2018.

In order to better evaluate the oil development potential, the Company has utilized the 3D seismic survey which covers all of its Gull Lake lands. As of December 31, 2017, GLJ assigned 257,500 boe of proven oil and natural gas reserves net to the Company and 140,700 boe of probable oil reserves net to the Company.

#### *Pennant*

Vital is the Operator and maintains a 100% working interest in 14 contiguous sections of land. To date one (1) vertical well and six (6) horizontal wells have been drilled. Four of the horizontal wells and the vertical well are on production and a well drilled in January 2018 is awaiting completion. 3D seismic coverage on about 35% of Vital's lands indicates there may potentially be additional drilling locations.

On March 20, 2017, the Company entered into a Carried Working Interest Agreement regarding the development of lands in the Pennant area. Under the Agreement, the Carried Working Interest Partner ("Partner") would advance by December 31, 2017 up to \$10,500,000 for the drilling, completion, equipping and all testing facilities for seven (7) horizontal wellbores, construction of five (5) lease pads and associated road works. In addition, the Partner would advance up to \$500,000 for the acquisition of petroleum and natural gas leases.

In exchange, the Company would pay 80% of the net profits from the seven (7) horizontal wells to the Partner until such time as the Partner has recovered 180% of their investment. At that time, the carried working interest will convert to a 5% gross overriding royalty.

As at September 30, 2018, the Partner had advance \$1,700,840 for the drilling, completion and equipping of the first well which was drilled in November 2017. To date of this report, there have been no further wells drilled under this agreement. The partner failed to drill 7 wells or to advance \$10,500,000 before December 2017, therefore the partner is technically in default under the terms of the amended carried working interest agreement.

The company's crude oil production was 55 boe/d for the third quarter of 2018 as compared to 51 boe/d from this area in the second quarter of 2018.

#### Non-core

In addition to its core properties, Vital has land holdings, primarily in the Sullivan Lake Area located in central Alberta, which may have additional drilling opportunities that Vital may drill or seek third party farmouts or joint ventures with other industry partners.

In the Lloydminster heavy oil area of Alberta (Baxter Lake) and Saskatchewan (Standard Hill) certain wells were suspended or shut in as production rates were allowed to decline due to not being economic. As oil prices improved in the second quarter of 2018, one of such suspended wells in Baxter Lake and one in Standard Hill area were reactivated and brought back on production after remedial work. Further reactivation of suspended wells is considered if oil prices continue to improve. Higher oil prices are needed in order to justify any further drilling activities on the Baxter Lake properties.

## **Outlook**

#### Pennant

The company has five (5) producing oil wells on the lands. The medium gravity crude oil is being produced from the Upper Shaunovan formation and geology indicates that the entire land block may be prospective. The Company has acquired additional 3D seismic data and now has coverage on about 35% of the lands.

The 3D seismic data confirms the geology and indicates that further drilling activities on the lands may be justified.

With the additional lands acquired in April 2017 and April 2018, Vital currently owns a 100% working interest in fourteen (14) contiguous sections of lands in Pennant Project Area (approximately 8,977 net acres or 3,633 net hectares). In addition to the 14-15 horizontal well that was drilled, completed and put on production in the fourth quarter of 2017, Vital drilled another horizontal well 15-20 in the first quarter of 2018. The 15-20 well is currently awaiting a finalized completion program which will be determined based on production performance of the 14-15 well. Vital is the Operator of the Pennant Area project.

#### Gull Lake

In 2015 the Company expended a significant amount of its capital installing water injection facilities and other infrastructure on the Gull Lake property. The result has been to lower operating costs and increased netbacks. Additional drilling locations have been identified by geological and 3D seismic interpretation and mapping.

In May 2017, a vertical test well was drilled at 2-29-13-19W3M and was completed and placed on production in late July 2017. This test well was targeting oil production from the Roseray, Cantuar and Upper Shaunavon formations and is currently producing 24-degree API medium gravity oil from the Upper Shaunavon formation. Vital drilled an offset well to the 2-29 well in the second quarter of 2018. The 6-29 well has oil shows in the targeted Upper Shaunavon formation and is being evaluated for completion. Two of Vital's partners are not participating in the drilling of the 6-29 well. As a result, Vital has increased their interest in the 6-29 well from 50% to 84.335%. Another offset well at 1-29-13-19W3 was drilled and completed in the third quarter of 2018, equipped and put on production in the fourth quarter. Vital plans to drill still another offset well at 3-29-13-19W3 in the fourth quarter. Vital is the designated Operator of the Gull Lake Project Area and maintains a 50% working interest in the balance of the Gull Lake project lands.

Vital has a good land inventory and has identified additional potential drilling locations on its "Core Properties" at Gull Lake and Pennant, S.W. Saskatchewan. The pace of the drilling programs will be determined by the prevailing price of oil and available financing.

#### Baxter Lake

As oil prices trended upwards in the first quarter of 2018, Vital re-evaluated the potential and economic viability of performing remedial work to reactivate certain wells in the Baxter Lake area. Commencing May 2018, Vital performed remedial work on certain wells resulting in increased oil production in June 2018.

### Discussion of Operations

Details of quarterly pricing in 2018 and 2017 are as follows:

<b>2018</b>	<b>Q3</b>	<b>Q2</b>	<b>Q1</b>	
WTI - \$US/bbl	69.50	67.88	62.87	
WCS Benchmark –US\$/bbl	47.25	48.61	38.59	
WCS Dollar Differential –US\$/bbl	22.25	19.27	24.28	
WCS % Differential	32%	28%	39%	
<b>2017</b>	<b>Q4</b>	<b>Q3</b>	<b>Q2</b>	<b>Q1</b>
WTI - \$US/bbl	55.40	48.21	48.29	51.91
WCS Benchmark –US\$/bbl	43.14	38.26	37.16	37.33
WCS Dollar Differential –US\$/bbl	12.26	10.05	11.13	14.58
WCS % Differential	22%	21%	23%	28%

A review of oil pricing reflects the Corporation's realized sales price is lower than the WCS benchmark price as the Corporation sells lower gravity oil than used in setting the WCS benchmark price. The following is a summary of Corporation's realized oil pricing:

<b>2018</b>			
	<b>Q3</b>	<b>Q2</b>	<b>Q1</b>
Revenue	\$1,454,524	\$1,233,688	\$848,464
# bbls	25,075	21,791	19,746
Bbls/d	272	239	219
Revenue per bbl	\$58.01	\$56.61	\$42.97
WCS -\$C per bbl	\$61.76	\$62.75	\$48.76
Differential to WSC price	6.1%	9.8%	11.9%

<b>2017</b>			
	<b>Q3</b>	<b>Q2</b>	<b>Q1</b>
Revenue	\$902,689	\$747,881	\$765,260
# bbls	21,487	18,667	19,924
Bbls/d	234	205	221
Revenue per bbl	\$42.05	\$40.06	\$38.40
WCS -\$C per bbl	\$47.91	\$49.96	\$49.36
Differential to WSC price	12.2%	19.8%	22.2%

The Company's net and comprehensive income of \$18,117 for the three months ended September 30, 2018 was an improvement over the 2018 second quarter loss of \$236,976. The improvement in the third quarter as opposed to the second quarter results from increased sales production and improved oil pricing.

Revenue for the nine months ended September 30, 2018 was \$3,536,676 as compared to \$2,415,830 for the same period in 2017. This increase in revenue of \$1,120,846 reflects increased sales production of 6,568 boe and an increased sales price per boe oil of \$12.85.

Crown royalties were 16% of revenue in the first three months+ of 2018 as compared to 9% for the comparable period in 2017. The increase in royalties reflects increased production and oil prices.

The production operating costs for the nine months ended September 30, 2018 were \$1,178,260 as compared to \$1,195,674 for the same period in 2017. With increased production in 2018, the Corporation has been able to reduce operating costs even while performing workovers at Baxter Lake and Standard Hill in the second quarter of 2018.

The depletion and depreciation expense for the nine months ended September 30, 2018 was \$1,071,451 as compared to \$866,240 for the same period in 2017. The increase of \$205,211 reflects a larger depletion base in 2018 and increased production in 2018. Depletion is calculated on a unit-of production basis.

The following tables detail the Corporation's operational netback for the three and nine months ended September 30th:

	<b>Three months ended September 30, 2018</b>		<b>Nine months ended September 30, 2018</b>	
		<b>Per boe</b>		<b>Per boe</b>
Production (boe)	25,075		66,653	
Average daily production (boe/d)	272		244	
Petroleum and natural gas revenue	\$1,454,524	\$58.01	\$3,536,676	\$53.06
Royalties	\$302,763	\$12.07	\$579,162	\$8.69
Production operating costs	\$427,971	\$17.07	\$1,178,260	\$17.68
<b>Operational netback</b>	<b>\$723,790</b>	<b>\$28.86</b>	<b>\$1,779,254</b>	<b>\$26.69</b>

	<b>Three months ended September 30, 2017</b>		<b>Nine months ended September 30, 2017</b>	
		<b>Per boe</b>		<b>Per boe</b>
Production (boe)	21,466		60,085	
Average daily production (boe)	233		220	
Petroleum and natural gas revenue	\$902,689	\$42.05	\$2,415,830	\$40.21
Royalties	\$85,155	\$3.96	\$229,662	\$3.82
Production operating costs	\$468,466	\$21.82	\$1,195,674	\$19.90
<b>Operational netback</b>	<b>\$349,068</b>	<b>\$16.27</b>	<b>\$990,494</b>	<b>\$16.49</b>

In comparing the three-month periods, the overall operational netback per boe is higher in 2018 due to increased oil prices and a decrease in production costs per boe primarily from increased production in 2018. Again, royalties were higher per boe in the third quarter of 2018 because of increased production and oil prices.

#### Quarterly results

The third quarter income was \$18,117 being an improvement of \$255,093 over the 2017 third quarter loss of \$236,976. The revenue of \$1,454,524 earned in the third quarter of 2018 was \$551,835 higher than the comparable period in 2017. This reflects an increase in 2018 third quarter production of 3,609 boe and an increase in the average selling price of \$15.96 per boe as compared to the third quarter of 2017.

Production operating costs were \$427,971 in the third quarter of 2018 compared to \$468,466 in the third quarter of 2017 a decrease of \$40,495. The costs of the increased production in the 2018 third quarter were buffered by lower repairs and maintenance costs as compared to the third quarter of 2017.

Depletion and depreciation was \$389,597 for the third quarter of 2018 compared to \$363,429 for the second quarter in 2018. The increase in the expense of \$26,168 reflects the increase in production in the third quarter of 2018.

General and administrative expenses are as follows:

	Three Months Ended		Nine Months Ended	
	September 30		September 30	
	2018	2017	2018	2017
Wages and employee benefits	\$ 130,889	\$ 77,449	\$ 313,484	\$ 232,792
Professional fees	13,678	41,373	67,868	94,395
Consulting fees	86,964	40,802	267,419	134,852
User fees	16,238	10,676	40,433	41,153
Rental	17,276	33,586	44,637	59,080
Office	1,295	(1,501)	54,788	40,880
Travel and entertainment	-	2,256	3,192	6,843
	<b>\$ 266,340</b>	<b>\$ 204,641</b>	<b>\$ 791,821</b>	<b>\$ 609,995</b>

Wages and employee benefits have increased in the third quarter with the hiring of an executive officer.

Consulting fees increased by \$132,567 for the nine months ended September 30, 2018 as compared to the same period in 2017. The increase is attributable one additional consultant being engaged commencing January 2018.

Rent costs for the nine months ended September 30<sup>th</sup> have decreased by \$14,437 in 2018 from 2017 as a new lease was signed at a reduced rate in the second quarter of 2017.

The remainder of the general and administrative costs are comparable period over period.

Finance costs in 2018 were \$103,142 as compared to \$146,647 in 2017. The 2017 expense includes \$18,000 of financing fees.

## Share capital

### Authorized

Unlimited number of voting Class A, B and C common shares

Unlimited number of non-voting Class D, E and F common shares

Unlimited number of non-voting, non-cumulative, redeemable Class A preferred shares

Unlimited number of non-voting, cumulative, redeemable Class B preferred shares

### Issued and outstanding – Class A common shares

	# of shares	Amount
<b>Balance, December 31, 2016 &amp; 2017 and Sept. 30, 2018</b>	<b>60,499,971</b>	<b>\$29,565,885</b>

As of the date of this report, there have been no changes in share capital.

### Share-based compensation

The Company has established a stock option plan (the "Plan") which is administered by the Board of Directors, allowing the Board of Directors to grant stock options. The Company adopted a 10% Rolling Stock Option Plan, which allows for the granting of stock options for the purchase of up to 10% of the outstanding shares of the Company.

Additionally, options may not be granted to any one person, any one consultant or any persons performing investor relations duties in any twelve-month period which could, when exercised, result in the issuance of shares exceeding 5%, 2% or 2% respectively of the issued and outstanding shares of the Company. All options granted under the Plan shall expire no later than the tenth anniversary of the date the options were granted.

The exercise price of the options is to be determined by the Board of Directors, subject to any applicable Exchange approval, at the time any option is granted. In no event shall such exercise price be lower than the exercise price permitted by any applicable Exchange. Vesting of the options is at the discretion of the Board of Directors. A summary of the status of the stock option plan and changes is presented below:

	<b>September 30, 2018</b>		<b>December 31, 2017</b>	
	#	Weighted average exercise price	#	Weighted average exercise price
<b>Outstanding, beginning of year</b>	<b>4,200,000</b>	<b>\$ 0.25</b>	<b>4,650,000</b>	<b>\$ 0.25</b>
Forfeited	-	0.25	(450,000)	0.25
<b>Outstanding, end of period</b>	<b>4,200,000</b>	<b>\$ 0.25</b>	<b>4,200,000</b>	<b>\$ 0.25</b>
<b>Exercisable, end of period</b>	<b>4,200,000</b>	<b>\$ 0.25</b>	<b>4,200,000</b>	<b>\$ 0.25</b>

The details of the options outstanding at September 30, 2018 are as follows:

<b>Options outstanding</b>	<b>Weighted average exercise price</b>	<b>Options exercisable</b>	<b>Weighted average years to expiry</b>
4,200,000	0.25	4,200,000	6.00

## **Liquidity and Capital Resources**

As at September 30, 2018, the Company had cash and cash equivalents of \$1,291,761 and working capital of \$48,720 (December 31, 2017 - \$891,877) before the inclusion of the debentures payable of \$2,175,000. This level of working capital will not be sufficient for the next twelve months in order to sustain current operations in this low oil price environment. The Corporation anticipates that the revenue generated from the wells recently drilled or where workovers were completed should be sufficient to sustain operations for the next twelve months. The terms of the debentures may need to be re-negotiated or re-financed. There can be no assurance that the Company will be able to repay or re-negotiate the debentures when they become due. If that were to occur, the Company may not be able to continue its operations and the amounts realizable for the assets could be less than the amounts reflected in the September 30, 2018 interim financial statements. The debentures are convertible at the option of the holders. If the debentures were converted, it could result in dilution of existing shareholdings.

The Company anticipates drilling three more wells (2 net wells) on their properties in the second half of 2018. The Company believes they will be able to finance the capital expenditures from operations and from an agreement entered into with a drilling company ("Supplier") which will provide beneficial financing terms. Under the agreement, the Supplier has agreed to drill and complete up to five wells. The Company is not obligated to drill the five wells and the Supplier will only receive their actual cost plus 12% for the work completed. The cost of the well may be paid in twelve (12) equal instalments. The Company believes

that the cash flows from the wells drilled and current working capital on hand should be sufficient to pay for the wells under this program. The decrease in working capital from December 31, 2017 to September 30, 2018 of \$888,157 is largely explained by the payment of suppliers' invoices related to the well drilled with the carried interest partner.

As discussed in the *Properties* section, the Company entered into a Carried Working Interest Agreement in 2017 on the Pennant lands. As of the date of this report, there are no plans for any further drilling under this agreement other than the one well drilled in December 2017.

For the nine months ended September 30, 2018, cash and cash equivalents decreased by \$776,600 (2017 – increase of \$73,585). This was a result of cash being provided by operations in the amount of \$658,268 (2017 – \$214,402), financing activities utilizing \$1,271,001 (2017 - \$nil) and investing activities using cash of \$163,867 (2017 –\$140,817). The cash used in financing activities of \$1,271,001 is primarily a timing issue related to the Carried Interest Partner where expenditures were paid on their behalf.

## Debentures

In December 2017, the Company extended for one year \$2,075,000 of the debentures originally issued on December 23, 2015 to December 23, 2018 and repaid one debenture in the amount of \$50,000. The extended debentures have the same terms as the debentures originally issued in December 2015 being 8% per annum, interest payable quarterly, secured and convertible. The debentures are convertible at the holder's option into common shares of the Company at a conversion price of \$0.10 per common share.

On December 28, 2017, the Company issued an 8% secured convertible debenture in the principal amount of \$100,000 to a director. The debenture will mature one year from the date of issuance, is secured against the property of the Company and interest is paid quarterly. The debenture is convertible at the holder's option into common shares of the Company at a conversion price of \$0.10 per common share.

## Related party transactions

Transactions with related parties are incurred in the normal course of business and are measured at the exchange amount which is the amount of consideration established and approved by the related parties. Related party transactions are as follows:

For the nine months ended September 30, 2018, the Company incurred \$185,000 (2017 - \$139,500) in consulting fees paid to officers or companies controlled by an officer and a director.

The debentures are payable to directors. Interest expense of \$130,142 (2017 - \$128,647) is included in finance costs in the Condensed Interim Statements of Comprehensive Loss related to this debt.

## Summary of Quarterly Results (unaudited)

Fiscal Quarter Ended - \$	September 30, 2018	June 30, 2018	March 31, 2018	December 31, 2017
Revenue	\$1,454,524	\$1,233,688	\$848,464	\$820,192
Net (income) loss	(\$18,117)	\$38,919	\$208,810	\$214,969
Net loss per share	\$0.00	\$0.00	\$0.01	\$0.00

<b>Fiscal Quarter Ended - \$</b>	<b>September30, 2017</b>	<b>June 30, 2017</b>	<b>March 31, 2017</b>	<b>December 31, 2016</b>
Revenue	\$902,689	\$747,881	\$765,260	852,428
Net loss	\$236,976	\$183,714	\$233,145	40,887
Net loss per share	\$0.00	\$0.00	\$0.01	0.00

Generally, the quarterly results are comparable quarter over quarter.

### **Off-Balance Sheet Arrangements**

There are no off-balance sheet arrangements as at September 30, 2018.

### **Critical Accounting Estimates and Policies**

The Company's significant accounting policies are disclosed in note 3 to the audited financial statements for the year ended December 31, 2017. The changes in accounting policies for 2018 are disclosed in note 3 to the unaudited condensed financial statements for the three months ended March 31, 2018. Amendments to IFRS 2, Share-based Payments, introduces accounting requirements for cash-settled share-based payments that follow the same approach as used for equity-settled share-based payments. They introduced an exception into IFRS 2 so that a share-based payment where the entity settles the share-based payment arrangement net is classified as equity-settled in its entirety, provided the share-based payment would have been classified as equity-settled had it not included the net settlement feature. Finally, they clarify the accounting treatment in situations where a cash-settled share-based payment changes to an equity-settled share-based payment because of modifications of the terms and conditions. This amendment was effective for reporting periods beginning on or after January 1, 2018. On adoption, this new standard did not have a significant impact on the financial statements.

### **Accounting standards issued but not yet applied**

The standards and interpretations that are issued but not yet effective up to the date of issuance of the Corporation's financial statements are listed below:

#### **IFRS 16 Leases**

IFRS 16 was issued in January 2016 and specifies how an IFRS reporter will recognize, measure, present and disclose leases. The standard provides a single lessee accounting model, requiring lessees to recognize assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value. Lessors continue to classify leases as operating or finance, with IFRS 16's approach to lessor accounting substantially unchanged from its predecessor, IAS 17. The Corporation is still assessing the impact of this new standard.

This standard is effective for reporting periods beginning on or after January 1, 2019.

### **Financial Instruments and Other Instruments**

The Company's financial instruments consist of cash and cash equivalents, trade and other receivables, deposits, accounts payable and accrued liabilities and debentures. It is management's opinion that the

Company is not exposed to significant interest, currency or credit risks arising from these financial instruments and that the fair value of these financial instruments approximates their carrying values, as applicable.

## **Risks and Uncertainties**

The risks and uncertainties set out below and elsewhere in this MD&A are not the only ones facing the Company. Additional risks and uncertainties not presently known to the Company or that the Company currently considers immaterial may also impair the business and operations of the Company and cause the price of the Common Shares to decline. If any of the following risks actually occur, the Company's business may be harmed and the financial condition and results of operations may suffer significantly. In that event, the trading price of the Common Shares could decline and holders of Common Shares may lose all or part of their investment.

### *Stage of Development*

An investment in the Company is subject to certain risks related to the nature of the Company's business and its stage of development. There are numerous factors which may affect the success of the Company's business which are beyond the Company's control including local, national and international economic and political conditions. The Company's business involves a high degree of risk which a combination of experience, knowledge and careful evaluation may not overcome. The Company has had no earnings to date and there can be no assurance that the Company's business will be successful or profitable or that additional commercial quantities of crude oil and natural gas will be discovered by the Company. The Company has not paid any dividends and it is unlikely to pay dividends in the immediate or foreseeable future.

### *Additional Funding Requirements*

The Company's cash on hand and cash flow may not be sufficient to fund its ongoing activities at all times. From time to time, the Company may require additional financing in order to carry out its oil and gas acquisition, exploration and development activities. Failure to obtain such financing on a timely basis could cause the Company to forfeit its interest in certain properties, miss certain acquisition opportunities and reduce or terminate its operations, and may affect the Company's ability to expend the capital required to replace its reserves or to maintain its production. There can be no assurance that additional debt or equity financing will be available to meet these requirements or, if available, on terms acceptable to the Company. This may be complicated by the limited market liquidity for the shares of smaller companies, restricting access to some institutional investors. Continued uncertainty in domestic and international credit markets could also materially affect the Company's ability to access sufficient capital for its capital expenditures and acquisitions. Furthermore, if additional financing is raised through the issuance of equity, control of the Company may change and the shareholders may suffer dilution. The Company may also consider asset dispositions or farm-out or joint venture arrangements in order to fund or implement its exploration and development activities; however, there can be no assurance that the Company will be able to secure such dispositions or arrangements on acceptable terms or at all. The inability of the Company to access sufficient capital for its operations and/or to secure acceptable alternative arrangements may have a material adverse effect on the Company's ability to execute its business strategy and on its business, financial condition, results of operations and prospects.

### *Competitive Conditions*

The oil and natural gas industry is highly competitive and the Company competes with a substantial number of other companies that have greater resources. Many of these companies explore for, produce and market oil and natural gas, carry on refining operations and market the resultant products on a worldwide basis. The primary areas in which the Company encounter substantial competition are in locating and acquiring desirable leasehold acreage for drilling and development operations, locating and acquiring attractive producing oil and natural gas properties, and obtaining purchasers and transporters of the oil and natural gas they produce. Many of these competitors have financial, technical and other resources substantially

greater than those of the Company. To the extent that these companies enjoy technological advantages, they may be able to implement new technologies more rapidly than the Company. There is also competition between producers of oil and natural gas and other industries producing alternative energy and fuel. The inability to acquire desirable properties, assets or service providers as a result of competition may have a material adverse effect on the Company's business, financial condition, results of operations and trading price of the Common Shares.

#### *Crude Oil and Natural Gas Exploration and Development*

Crude oil and natural gas exploration involves a high degree of risk and there is no assurance that expenditures made on future exploration or development activities by the Company will result in discoveries of crude oil, condensate or natural gas that are commercially or economically feasible. It is difficult to project the costs of implementing any exploratory drilling program due to the inherent uncertainties of drilling in unknown formations, the shortages of and delays in the availability of drilling rigs and equipment, the costs associated with encountering various drilling conditions such as over pressured zones and tools lost in the hole, and changes in drilling plans and locations as a result of prior exploratory wells or additional seismic data and interpretations thereof.

The Company's operations are subject to all the risks normally associated with the exploration, development and operation of crude oil and natural gas properties and the drilling of crude oil and natural gas wells, including encountering unexpected formations or pressures, mechanical failures, premature declines of reservoirs, environmental damage, blow outs, cratering, fires and spills, all of which could result in personal injuries, loss of life and damage to property of the Company and others. In accordance with customary industry practice the Company does maintain insurance coverage, but are not fully insured against all risks, nor are all such risks insurable. Environmental regulation is becoming increasingly stringent and costs and expenses of regulatory compliance are increasing.

Exploration, appraisal and development of crude oil and natural gas reserves is speculative and involves a significant degree of risk. Few properties that are explored are ultimately developed into new reserves. If at any stage the Company is precluded from pursuing its exploration or development program, or such program is otherwise not continued, the Company's business, financial condition and/or results of operations and, accordingly, the trading price of the Common Shares is likely to be materially adversely affected.

#### *Volatility of Crude Oil and Natural Gas Prices and Markets*

The Company's financial condition, operating results and future growth are dependent on the prevailing prices for crude oil and natural gas production. Historically, the markets for crude oil and natural gas have been volatile and such markets are likely to continue to be volatile in the future. Prices for crude oil and natural gas are subject to large fluctuations in response to relatively minor changes to the demand for crude oil and natural gas, whether the result of uncertainty or a variety of additional factors beyond the control of the Company. The Company must periodically negotiate contracts with a limited number of potential purchasers. The price negotiated is influenced by the size of the crude oil or natural gas stream, the nature of the crude oil or natural gas and its location when produced. Any substantial decline in the prices of crude oil and natural gas could have a material adverse effect on the Company and the level of its crude oil and natural gas reserves. Additionally, the economics of producing from some wells may change as a result of lower prices, which could result in a suspension of production. No assurance can be given that crude oil and natural gas prices will be sustained at levels which will enable the Company to operate profitably. From time to time the Company may avail itself of forward sales or other forms of hedging activities with a view to mitigating its exposure to the risk of price volatility.

#### *Loss of Key Personnel*

The Company depends to a large extent on the efforts and continued employment of the Management Team, who has developed the operations of the Company. The loss of the services of these officers and other key personnel could adversely affect the Company's business, and the Company does not maintain key man insurance on any of these persons. The success of drilling operations and other activities integral to its

business will depend in part on the ability to attract and retain experienced geologists, engineers and other professionals. Competition for experienced geologists, engineers and some other professionals is extremely intense. The Company's ability to compete in the oil and natural gas exploration and production industry will be harmed to the extent that the Company is unable to retain and attract experienced technical personal.

#### *Operating and Insurance Risks*

The operations of the Company are subject to hazards and risks inherent in drilling for, producing and transporting crude oil and natural gas. These risks include, among others, fires, explosions, geologic formations with abnormal pressures, collapses of casing surrounding the drill pipe in wells, mechanical failures, failure of oilfield drilling and service tools, uncontrollable flows of underground natural gas, oil and formation water, changes in below ground pressure in a formation that causes the surface to collapse or crater, pipeline ruptures and cement failures, and environmental hazards such as leaks, spills and toxic discharges. These risks can cause substantial losses resulting from personal injury or loss of life, damage and destruction of property and equipment, pollution and other environmental damage, regulatory investigations and penalties, and suspension of operations. As protection against operating hazards and in accordance with customary industry practices, the Company maintains insurance coverage against some, but not all, potential losses because the insurance coverage is not available or because premium costs are considered too high. Losses could occur for uninsured risks or in amounts exceeding the insurance coverage and these losses could have a materially adverse effect on the Company's business, financial condition, results of operations and trading price of the Common Shares.

#### *Equipment Unavailability*

The Company does not own the drilling rigs and related equipment required to develop its oil and gas properties and relies on third parties to provide drilling and other oil field services. Demand is high for equipment and services in the geographic areas that the Company has selected for exploration and development. This demand may reduce the availability of that equipment and services and could delay the Company's exploration, development and exploitation activities. The leases under which the Company develops properties provide time periods during which it must generate production of oil or gas or the lease expires. Any delay that prevented completion of drilling on leased property during the term of the lease would require additional expenditures by the Company to renew the lease or possibly the loss of any benefit from past development expenditures and future production revenue. In addition, the high demand for equipment and services increases the costs to the Company of the equipment and associated supplies and personnel. Any substantial delays to gain access to equipment and services or material increases in costs could adversely affect the Company's business and financial condition and have a material adverse effect on the Company's business, financial condition, results of operations and trading price of the Common Shares.