

*Condensed Consolidated Financial Statements of*

**CEQUENCE ENERGY LTD.**

*June 30, 2018 and 2017*

# CEQUENCE ENERGY LTD.

## Condensed Consolidated Balance Sheets (Unaudited)(Expressed in thousands of Canadian dollars)

	June 30, 2018 \$	December 31, 2017 \$
<b>ASSETS</b>		
<b>CURRENT</b>		
Cash	3,186	10,971
Accounts receivable (Note 13)	12,253	14,739
Deposits and prepaid expenses	1,078	514
Commodity contracts (Note 13)	-	1,274
	<u>16,517</u>	<u>27,498</u>
Property and equipment (Note 4)	256,152	257,230
	<u>272,669</u>	<u>284,728</u>
<b>LIABILITIES</b>		
<b>CURRENT</b>		
Accounts payable and accrued liabilities	28,684	33,106
Share-based payment liability (Note 11)	148	153
Provisions (Note 10)	1,171	1,466
Commodity contracts (Note 13)	1,154	998
Senior notes (Note 6)	59,761	59,341
	<u>90,918</u>	<u>95,064</u>
Provisions (Note 10)	35,423	37,012
	<u>126,341</u>	<u>132,076</u>
SUBSEQUENT EVENTS (Note 5, 6, 16)		
<b>SHAREHOLDERS' EQUITY</b>		
Shareholders' capital	633,846	633,846
Warrants	1,300	1,300
Contributed surplus	31,222	31,076
Deficit	(520,040)	(513,570)
	<u>146,328</u>	<u>152,652</u>
	<u>272,669</u>	<u>284,728</u>

### APPROVED BY THE BOARD

"Donald Archibald"	Donald Archibald, Director
"Brian Felesky"	Brian Felesky, Director

*The accompanying notes are an integral part of these condensed consolidated financial statements.*

## CEQUENCE ENERGY LTD.

### Condensed Consolidated Statements of Comprehensive Loss (Unaudited)(Expressed in thousands of Canadian dollars except per share amounts)

	Three months ended		Six months ended	
	June 30,		June 30,	
	2018	2017	2018	2017
	\$	\$	\$	\$
<b>REVENUE</b>				
Production revenue (Note 7)	14,677	16,381	27,618	34,626
Gain (loss) on derivative financial instruments (Note 13)	(891)	2,654	(1,772)	7,866
	<b>13,786</b>	<b>19,035</b>	<b>25,846</b>	<b>42,492</b>
<b>EXPENSES</b>				
Operating costs	6,758	5,829	13,147	12,608
Transportation	1,728	1,650	3,168	2,958
Depletion and depreciation (Note 4)	6,310	6,927	11,139	13,858
Impairment (Note 4)	-	96,200	-	96,200
General and administrative	1,487	1,182	2,737	2,232
Finance costs (Note 8)	1,881	1,933	3,777	3,936
Share-based payment (Note 11)	75	366	140	641
Other income (Note 9)	(1,708)	(153)	(1,792)	(293)
	<b>16,531</b>	<b>113,934</b>	<b>32,316</b>	<b>132,140</b>
LOSS BEFORE INCOME TAXES	(2,745)	(94,899)	(6,470)	(89,648)
INCOME TAXES	-	-	-	-
<b>NET LOSS AND COMPREHENSIVE LOSS</b>	<b>(2,745)</b>	<b>(94,899)</b>	<b>(6,470)</b>	<b>(89,648)</b>
Loss per share (Note 12)				
Basic and diluted	(\$0.01)	(\$0.39)	(\$0.03)	(\$0.37)

*The accompanying notes are an integral part of these condensed consolidated financial statements.*

## CEQUENCE ENERGY LTD.

### Condensed Consolidated Statements of Changes in Equity (Unaudited)(Expressed in thousands of Canadian dollars)

	Six months ended June 30,	
	2018	2017
	\$	\$
<b>SHAREHOLDERS' EQUITY</b>		
<b>Shareholders' Capital</b>		
Balance, beginning of period	633,846	633,848
Share issue costs	-	(2)
Balance, end of period	<u>633,846</u>	<u>633,846</u>
<b>Warrants</b>		
Balance, beginning of period	<u>1,300</u>	<u>1,300</u>
Balance, end of period	<u>1,300</u>	<u>1,300</u>
<b>Contributed Surplus</b>		
Balance, beginning of period	31,076	30,085
Share-based payment expense (Note 11)	146	557
Balance, end of period	<u>31,222</u>	<u>30,642</u>
<b>Deficit</b>		
Balance, beginning of period	(513,570)	(414,208)
Net loss	(6,470)	(89,648)
Balance, end of period	<u>(520,040)</u>	<u>(503,856)</u>
<b>TOTAL SHAREHOLDERS' EQUITY</b>	<u><u>146,328</u></u>	<u><u>161,932</u></u>

*The accompanying notes are an integral part of these condensed consolidated financial statements.*

# CEQUENCE ENERGY LTD.

## Condensed Consolidated Statements of Cash Flows (Unaudited)(Expressed in thousands of Canadian dollars)

	Three months ended		Six months ended	
	June 30,		June 30,	
	2018	2017	2018	2017
	\$	\$	\$	\$
<b>CASH FLOWS RELATED TO THE FOLLOWING ACTIVITIES:</b>				
<b>OPERATING</b>				
Net loss	(2,745)	(94,899)	(6,470)	(89,648)
Adjustments for non-cash items:				
Depletion and depreciation expense (Note 4)	6,310	6,927	11,139	13,858
Impairment (Note 4)	-	96,200	-	96,200
Accretion expense on provisions (Note 8)	197	208	406	428
Share-based payment (Note 11)	75	366	140	641
Amortization of transaction costs (Note 8)	120	108	237	214
Accretion expense on senior notes (Note 8)	93	83	183	164
Unrealized (gain) loss on derivative financial instruments (Note 13)	(216)	(2,152)	1,431	(7,610)
Gain on sale of property and equipment (Note 9)	(1,643)	(60)	(1,639)	(120)
Abandonment costs incurred (Note 10)	(301)	(90)	(2,857)	(314)
Net change in non-cash working capital (Note 14)	2,489	(1,665)	1,857	(1,355)
Cash flow from operating activities	4,379	5,026	4,427	12,458
<b>INVESTING</b>				
Property and equipment expenditures (Note 4)	(1,830)	(2,536)	(9,284)	(17,582)
Proceeds from sale of property and equipment, net	1,433	-	1,429	-
Net change in non-cash working capital (Note 14)	(8,747)	(11,146)	(4,357)	(9,082)
Cash flow used in investing activities	(9,144)	(13,682)	(12,212)	(26,664)
<b>FINANCING</b>				
Share issue costs	-	-	-	(2)
Cash settlement of share based payments	-	(203)	-	(203)
Net change in non-cash working capital (Note 14)	-	3	-	-
Cash flow used in financing activities	-	(200)	-	(205)
<b>NET DECREASE IN CASH</b>	<b>(4,765)</b>	<b>(8,856)</b>	<b>(7,785)</b>	<b>(14,411)</b>
<b>CASH, BEGINNING OF PERIOD</b>	<b>7,951</b>	<b>12,223</b>	<b>10,971</b>	<b>17,778</b>
<b>CASH, END OF PERIOD</b>	<b>3,186</b>	<b>3,367</b>	<b>3,186</b>	<b>3,367</b>

The accompanying notes are an integral part of these condensed consolidated financial statements.

# CEQUENCE ENERGY LTD.

## Notes to the Condensed Consolidated Financial Statements

Three and six months ended June 30, 2018 and 2017

**(Unaudited)(All figures expressed in thousands except per share amounts unless otherwise noted)**

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### 1. NATURE AND DESCRIPTION OF THE COMPANY

Cequence Energy Ltd. (the “Company” or “Cequence”) is incorporated under the laws of Alberta with common shares that are widely held and listed on the Toronto Stock Exchange. Cequence is engaged in the acquisition, exploration and production of petroleum and natural gas reserves in Western Canada. The registered office of the Company is located at Suite 1400, 215 – 9<sup>th</sup> Avenue. SW, Calgary, Alberta, T2P 1K3.

These interim condensed consolidated financial statements (“consolidated financial statements”) include all assets, liabilities, revenues and expenses of Cequence and its wholly-owned subsidiary, 1175043 Alberta Ltd.

### 2. SIGNIFICANT ACCOUNTING POLICIES

#### Statement of compliance and authorization

These consolidated financial statements have been prepared in accordance with International Accounting Standard (“IAS”) 34, “Interim Financial Reporting”, as issued by the International Accounting Standards Board (“IASB”). Accordingly, certain information or footnote disclosure normally included in the annual consolidated financial statements prepared in accordance with International Financial Reporting Standards (“IFRS”) have been condensed or omitted.

These consolidated financial statements should be read in conjunction with the Company’s consolidated financial statements for the year ended December 31, 2017.

The consolidated financial statements were authorized for issue by the Company’s Board of Directors on August 10, 2018.

#### Basis of presentation

Except as outlined in Note 3, the consolidated financial statements have been prepared using the same accounting policies and methods as those used in the consolidated financial statements for the year ended December 31, 2017. The consolidated financial statements have been presented in Canadian dollars, which is also the Company’s functional currency, rounded to the nearest thousand, unless otherwise indicated.

#### Going concern

These consolidated financial statements have been prepared on the basis that the Company will continue as a going concern, which asserts that the Company has the ability to realize its assets and discharge its liabilities and commitments in the normal course of business.

As at June 30, 2018, the Company had a working capital deficiency of \$74,401, that included the carrying value of the \$60,000 of senior notes that were refinanced subsequent to June 30, 2018 and are now due on October 3, 2022 (see Note 16). The Company had a \$9,000 Credit Facility with a syndicate of chartered banks that is currently undrawn other than letters of credit outstanding of \$1,590. The Credit Facility is a demand loan with a maturity date of July 31, 2018 which was subsequently extended until September 28, 2018.

# CEQUENCE ENERGY LTD.

## Notes to the Condensed Consolidated Financial Statements

Three and six months ended June 30, 2018 and 2017

**(Unaudited)(All figures expressed in thousands except per share amounts unless otherwise noted)**

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The Company is also in the process of identifying and pursuing alternative financing arrangements, property acquisitions or divestitures, corporate mergers and acquisitions and other recapitalization opportunities to further invest in the Company's ongoing drilling program.

These consolidated financial statements do not reflect the adjustments and classifications of assets, liabilities, revenues and expenses which would be necessary if the Company were unable to continue as a going concern.

### **Basis of consolidation**

The consolidated financial statements include the accounts of the Company and its consolidated subsidiaries, which are the entities over which the Company has control. Control exists when the Company has the power to govern the financial and operating policies of an entity so as to obtain benefit from its activities. All intercompany transactions and balances are eliminated on consolidation.

### **3. CHANGES IN ACCOUNTING POLICIES**

#### **IFRS 15 "Revenue from contracts with customers"**

Cequence adopted IFRS 15 with a date of initial application of January 1, 2018. IFRS 15 replaces existing revenue recognition guidance and provides a single, principles-based five-step model to be applied to all contracts with customers. Cequence used the modified retrospective approach to adopt the new standard, applying the standard retrospectively only to contracts that were not completed contracts on January 1, 2018. Under the transitional provision, the cumulative effect of initially applying IFRS 15 is recognized on the date of initial application as an adjustment to deficit. As a result of applying the requirements of IFRS 15, including the application of certain practical expedients such as the right to invoice method of measuring the Company's progress towards complete satisfaction of its performance obligations, there was no change or adjustments to the Company's consolidated financial statements as a result of the adoption of IFRS 15. Additional disclosure requirements required by IFRS 15 are detailed in Note 7.

Cequence recognizes revenue at a point in time when control of the product has been transferred to the customer and performance obligations have been satisfied. This is generally met when the customer obtains legal title to the product and physical delivery at a delivery point has taken place. Revenue is measured based on the consideration specified in the contracts the Company has with its customers.

Cequence evaluates its arrangements with 3rd parties and partners to determine if the Company acts as the principal or as an agent. In making this evaluation, management considers if it obtains control of the product delivered, which is indicated by the Company having the primary responsibility for the delivery of the product, having the ability to establish prices or having inventory risk. If Cequence acts in the capacity of an agent rather than as a principal in a transaction, then the revenue is recognized on a net-basis, only reflecting the fee, if any, realized by the party from the transaction.

#### **IFRS 9 "Financial Instruments"**

On January 1, 2018, Cequence adopted IFRS 9 as issued by the IASB. IFRS 9 includes a new classification and measurement approach for financial assets and liabilities, and a new expected loss impairment model for financial assets including credit losses. The adoption of IFRS 9 did not have a material impact on Cequence's consolidated financial statements. Additional disclosures related to Cequence's financial assets are included in Note 13. Cequence has revised the description of its accounting policy for financial instruments to reflect the new classifications approach as follows:

# CEQUENCE ENERGY LTD.

## Notes to the Condensed Consolidated Financial Statements

Three and six months ended June 30, 2018 and 2017

**(Unaudited)(All figures expressed in thousands except per share amounts unless otherwise noted)**

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### *Financial Instruments*

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity. Financial assets and financial liabilities are recognized on the consolidated balance sheet at the time the Company becomes a party to the contractual provisions. Upon initial recognition, financial instruments are measured at fair value. Measurement in subsequent periods is dependent on the classification of the financial instrument.

The Company has made the following classifications:

- Fair value through profit or loss: Financial instruments under this classification include cash and commodity contract asset and liabilities.
- Amortized cost: Financial instruments under this classification included accounts receivable, deposits, demand credit facilities, senior notes, accounts payable and accrued liabilities.

IFRS 9 also introduces a new model for the measurement of impairment of financial assets based on expected credit losses which replaces the incurred losses impairment model applied under IAS 39. Under this new model, Cequence's accounts receivable are considered collectible within one year or less; therefore, these financial assets are not considered to have a significant financing component and a lifetime expected credit loss ("ECL") is measured at the date of initial recognition of the accounts receivable.

For accounts receivable, the Company assesses the lifetime ECL applicable to its commodity product sales receivables and joint venture receivables at initial recognition and re-assesses the provision at each reporting date. The majority of the Company's accounts receivable are due from joint venture partners in the oil and gas industry and from marketers of the Company's petroleum and natural gas production. In making an assessment as to whether Cequence's financial assets are credit impaired, the Company considers historical bad debts, the counterparties financial condition, credit rating and total financial exposure. The carrying amounts of receivables are reduced by the amount of the ECL through an allowance account and losses are recognized within general and administrative expense in comprehensive loss.

The Company considers all amounts greater than 90 days past due. These past due accounts are considered to be collectible, except as provided in the allowance for doubtful accounts. When determining whether past due accounts are uncollectible, the Company factors in the past credit history of the counterparties.

### **IFRS 16 "Leases"**

IFRS 16 'Leases' was issued by the IASB in January 2016. IFRS 16 replaces the existing standard IAS 17 and requires the recognition of most leases on the balance sheet. IFRS 16 effectively removes the classification of leases as either finance or operating leases and treats all leases as finance leases for lessees with exemptions for short-term leases where the term is twelve months or less and for leases of low value items. The accounting treatment for lessors remains the same. IFRS 16 is effective January 1, 2019, with earlier application permitted. The Company is in the process of assessing the impact of the adoption of this standard on the Company's consolidated financial statements.



## CEQUENCE ENERGY LTD.

### Notes to the Condensed Consolidated Financial Statements

Three and six months ended June 30, 2018 and 2017

**(Unaudited)(All figures expressed in thousands except per share amounts unless otherwise noted)**

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#### 4. PROPERTY AND EQUIPMENT

**Cost:**

Balance at December 31, 2017	928,935
Additions	9,284
Decommissioning obligation additions and change in estimates	1,683
Disposals	<u>(34,338)</u>
Balance at June 30, 2018	<u>905,564</u>

**Depletion, depreciation and impairment:**

Balance at December 31, 2017	(671,705)
Depletion and depreciation	(11,139)
Disposals	<u>33,432</u>
Balance at June 30, 2018	<u>(649,412)</u>

**Carrying amounts:**

At December 31, 2017	257,230
At June 30, 2018	<u>256,152</u>

Costs subject to depletion include \$849,395 of estimated future capital costs (December 31, 2017 – \$840,601).

The Company's credit facilities are secured by a demand debenture with a first floating charge over all assets of the Company (see Note 5).

#### **Sale of assets**

During the three and six-months ended June 30, 2018, the Company disposed of certain oil and gas properties and associated decommissioning liabilities for proceeds of \$1,433 and \$1,429 prior to closing adjustments. The sales resulted in a gain recognized in comprehensive loss of \$1,643 and \$1,639 for the three and six-month periods ended June 30, 2018.

Assets that were previously held for sale at March 31, 2018 did not receive regulatory approval and have been included in property and equipment balances at June 30, 2018.

#### **Impairment**

At the end of each reporting period, the Company performs an assessment to determine whether there is any indication of impairment or reversal of previously recorded impairments for the cash generating units ("CGU") that comprise oil and gas properties. The assessment of indicators is subjective in nature and requires Management to make judgments based on the information available at the reporting date. Although the market capitalization of the Company continues to be below the net assets of the Company, the Company determined that there were no impairment or impairment reversals for any of the Company's CGUs as at June 30, 2018.

During the six months ended June 30, 2017, the Company recognized impairment expense of \$96,200 related to reductions in the Company's enterprises value and decreases in future crude oil and natural gas prices used to estimate the value in use and fair value less cost to sell of each of the Company's CGUs.

# CEQUENCE ENERGY LTD.

## Notes to the Condensed Consolidated Financial Statements

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**(Unaudited)(All figures expressed in thousands except per share amounts unless otherwise noted)**

### 5. DEMAND CREDIT FACILITIES

As at June 30, 2018, the Company has an extendible revolving term credit facility (the “Credit Facility”) of \$9,000 (December 31, 2017 - \$12,000) with a syndicate of Canadian chartered banks and has drawn \$nil (December 31, 2017 - \$nil) under the facility. The Company has letters of credit outstanding of \$1,590 (December 31, 2017 - \$1,540).

Prime loans and U.S. Base Rate Loans on the facility bear interest at the bank prime rate or U.S. Base Rate, respectively, plus 1.0 percent to 3.5 percent on a sliding scale, depending on the Company’s debt to adjusted EBITDA ratio (ranging from being less than or equal to 1.0:1.0 to greater than 3.5:1.0). Banker’s Acceptances, Libor Loans and letters of credit on the facility bear interest at the Banker’s Acceptance rate, Libor rate or letter of credit rate, as applicable, plus 2.0 percent to 4.5 percent based on the same sliding scale as above. The credit facility is secured by a general assignment of book debts and a \$250,000 demand debenture with a first floating charge over all assets of the Company. The Company is permitted to hedge up to 67 percent of its production under the lending agreement. The Company has a covenant that requires Senior Debt to EBITDA, as defined in the bank agreement, to be less than 3:0 to 1:0. Senior Debt is defined as the sum of Consolidated Debt less the period end balance of the Senior Notes. Consolidated Debt is defined as the sum of the Company’s period end balance of the Credit Facility and Senior Notes. The Company was in compliance with the lender’s covenants at June 30, 2018 and December 31, 2017.

The Credit Facility has a term date of July 31, 2018 and may be extended beyond the initial term, if requested by the Company and accepted by the lenders. If the senior credit facility does not continue to revolve, amounts borrowed under the facility must be repaid on the term date. The Credit Facility is reviewed on a semi-annual basis with the lender holding the right to request an additional review as may be required. The next scheduled review is to take place in September 2018. See Note 16 for the approved extension through to September 28, 2018.

### 6. SENIOR NOTES

	<b>June 30, 2018</b>	December 31, 2017
Senior notes	<b>56,503</b>	56,503
Add transaction costs	<b>3,258</b>	2,838
Total senior notes	<b>59,761</b>	59,341

On October 3, 2013, Cequence issued \$60,000 of unsecured five year term notes (“Senior Notes”) at par with a 9% coupon per annum for gross proceeds net of transaction costs of \$57,974. The Senior Notes are unsecured and are subordinate to Cequence’s credit facilities. The Senior Notes were issued pursuant to a trust indenture with a Canadian trust company, which provides for an additional \$60,000 of unsecured senior notes at a future date, subject to approval of both the lender and the Company on terms to be confirmed at the time of issuance.

The Senior Notes are subject to the same financial covenants as the Company credit facilities as well as other non-financial covenants and restrictive covenants, including restrictions over asset sales, restricted payments and the incurrence of additional indebtedness (see note 15). The Company was in compliance with the senior notes covenants at June 30, 2018 and December 31, 2017.

On July 27, 2018, Cequence entered into a second lien secured loan agreement with the Senior Note lender to refinance the Senior Notes (see Note 16).

## CEQUENCE ENERGY LTD.

### Notes to the Condensed Consolidated Financial Statements

Three and six months ended June 30, 2018 and 2017

**(Unaudited)(All figures expressed in thousands except per share amounts unless otherwise noted)**

#### 7. PRODUCTION REVENUE

Cequence sells its oil, natural gas, and natural gas liquids production pursuant to variable price contracts. The transaction price for variable priced contracts is based on a benchmark commodity price, adjusted for quality, location or other factors, whereby each component of the pricing formula (apart from the benchmark commodity price) can be either fixed or variable, depending on the contract terms. Revenues are typically collected on the 25th day of the month following the prior month's production, with revenue being recorded once the product is delivered to a contractually agreed upon delivery point.

The following table presents Cequence's production disaggregated by revenue source:

	Three months ended		Six months ended	
	2018	June 30, 2017	2018	June 30, 2017
Natural gas	5,568	10,660	12,720	22,298
Crude oil and condensate	9,391	6,080	14,973	13,314
Natural gas liquids	761	568	1,705	1,296
Royalties	(1,043)	(927)	(1,780)	(2,282)
Total	14,677	16,381	27,618	34,626

#### 8. FINANCE COSTS

	Three months ended		Six months ended	
	2018	June 30, 2017	2018	June 30, 2017
Interest expense on demand credit facilities	19	81	64	243
Interest expense on senior notes	1,452	1,453	2,887	2,887
Amortization of transaction costs	120	108	237	214
Accretion expense on senior notes	93	83	183	164
Accretion expense on provisions	197	208	406	428
Total finance costs	1,881	1,933	3,777	3,936

#### 9. OTHER INCOME

	Three months ended		Six months ended	
	2018	June 30, 2017	2018	June 30, 2017
Gain on sale of property and equipment	(1,643)	(60)	(1,639)	(120)
Interest income	(17)	(20)	(57)	(59)
Other	(48)	(73)	(96)	(114)
Total other income	(1,708)	(153)	(1,792)	(293)

## CEQUENCE ENERGY LTD.

### Notes to the Condensed Consolidated Financial Statements

Three and six months ended June 30, 2018 and 2017

**(Unaudited)(All figures expressed in thousands except per share amounts unless otherwise noted)**

#### 10. PROVISIONS

##### Decommissioning liabilities

The following table summarizes the changes in decommissioning liabilities for the six months ended June 30, 2018 and year ended December 31, 2017:

	2018	2017
Balance, beginning of period	38,478	38,161
Property dispositions	(1,116)	(776)
Accretion expense	406	870
Liabilities incurred	-	371
Abandonment costs incurred	(2,857)	(1,079)
Revisions in estimated cash flows	1,402	(185)
Revisions due to change in discount rates	281	1,116
Balance, end of period	36,594	38,478
Current	1,171	1,466
Non-current	35,423	37,012
	36,594	38,478

The Company's decommissioning liabilities result from its ownership in oil and natural gas assets including well sites, facilities and gathering systems. The total estimated, undiscounted cash flows, inflated at 2 percent, required to settle the obligations are \$60,023 (December 31, 2017 - \$63,742). These cash flows have been discounted using a risk-free interest rate of 2.16 percent (December 31, 2017 - 2.20 percent) based on Government of Canada long-term benchmark bonds. The Company expects these obligations to be settled in approximately 1 to 50 years (December 31, 2017 - 1 to 50 years). As at June 30, 2018 and December 31, 2017, no funds have been set aside to settle these liabilities.

#### 11. SHARE-BASED PAYMENT PLANS

The Company has a stock option and RSU plan for directors, officers, employees and consultants of the Company and its subsidiaries. For the three and six months ended June 30, 2018, Cequence recognized share-based payment expense on equity-settled stock options of \$2 and \$146 (2017 - \$300 and \$557) and RSUs of \$73 and (\$6) (2017 - \$66 and \$84).

A summary of the status of the Company's stock option and RSU plans during the six months ended June 30, 2018 and year ended December 31, 2017 is as follows:

Number of Options (000's)	2018	2017
Outstanding, beginning of period	13,220	11,003
Granted	-	5,025
Cancelled/Forfeited	(1,378)	(107)
Expired	(125)	(2,701)
Outstanding, end of period	11,717	13,220

## CEQUENCE ENERGY LTD.

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(Unaudited)(All figures expressed in thousands except per share amounts unless otherwise noted)

<b>Number of RSUs (000's)</b>	<b>2018</b>	2017
Outstanding, beginning of period	<b>2,666</b>	3,010
Granted	-	700
Settled	-	(1,015)
Cancelled/Forfeited	<b>(360)</b>	(29)
Outstanding, end of period	<b>2,306</b>	2,666

#### 12. LOSS PER SHARE

Loss per share has been calculated based on the weighted average number of common shares outstanding during the period. For the three and six months ended June 30, 2018 and 2017, the Company excluded all dilutive instruments as their inclusion would be anti-dilutive. The following table reconciles the denominators used for the basic and diluted loss per share calculations:

	<b>Three months ended</b>		<b>Six months ended</b>	
	<b>2018</b>	<b>June 30, 2017</b>	<b>2018</b>	<b>June 30, 2017</b>
Basic weighted average shares	<b>245,528</b>	245,528	<b>245,528</b>	245,528
Effect of dilutive instruments	-	-	-	-
Diluted weighted average shares	<b>245,528</b>	245,528	<b>245,528</b>	245,528

#### 13. RISK MANAGEMENT

There have been no significant changes to the Company's exposure to risks, or the objectives, policies and processes to manage these risks from December 31, 2017.

##### MARKET RISK

Market risk is the risk that changes in market prices, such as foreign exchange rates, commodity prices, and interest rates will affect the Company's comprehensive loss to the extent the Company has outstanding financial instruments. The objective of the Company is to mitigate market risk exposures within acceptable limits, while maximizing returns.

##### Commodity price risk

The nature of the Company's operations results in exposure to fluctuations in commodity prices. Management continuously monitors commodity prices and initiates instruments to manage exposure to these risks when it deems appropriate. As a means of managing commodity price volatility, the Company enters into various derivative financial instrument agreements and physical contracts. The fair values of the derivative financial instruments are based on mark-to-market assessments and estimates of fair value and are recorded on the consolidated balance sheet as either an asset or liability with the change in fair value recognized in comprehensive loss.

The following table presents all outstanding positions for commodity derivative financial instruments at June 30, 2018:

<b>Term</b>	<b>Product</b>	<b>Type</b>	<b>Volume</b>	<b>Price</b>	<b>Basis</b>
July 1, 2018 to December 31, 2018	Oil	Swap	300 bbl/day	\$71.72	WTI

For the three and six months ended June 30, 2018, realized loss from commodity derivative contracts recognized in comprehensive loss were \$1,107 and \$341 (2017 - \$502 and \$256 gain).

## CEQUENCE ENERGY LTD.

### Notes to the Condensed Consolidated Financial Statements

Three and six months ended June 30, 2018 and 2017

**(Unaudited)(All figures expressed in thousands except per share amounts unless otherwise noted)**

The fair value of the commodity contracts outstanding at June 30, 2018 was a current liability of \$1,154 (December 31, 2017 – current asset of \$1,274 and current liability of \$998).

For the three and six months ended June 30, 2018, the Company recorded an unrealized gain (loss) of \$216 and (\$1,431) from derivative commodity contracts (2017 - \$2,152 and \$7,610 unrealized gain).

As at June 30, 2018, a change in gas price of \$0.50/Gj and oil price of \$1.00/bbl results in a change in the fair value of the commodity contracts of \$nil and \$55 (December 31, 2017 - \$563 and \$109) respectively and a commensurate increase to comprehensive loss.

#### CREDIT RISK

Credit risk is the risk of financial loss to the Company if a counterparty to a financial instrument fails to meet its contractual obligation. The Company is exposed to credit risk with respect to its cash, accounts receivable and commodity contract assets.

The Company's cash is held with a large established financial institution. The majority of the Company's accounts receivable are due from marketers of the Company's petroleum and natural gas production which are typically collected on the 25th day of the month following the prior month's production and from joint venture partners in the oil and gas industry. The Company mitigates its credit risk by entering into contracts with established counterparties that have strong credit ratings and reviewing its exposure to individual counterparties on a regular basis.

As at June 30, 2018, the accounts receivable balance was \$12,253 (December 31, 2017 - \$14,739) of which \$974 (December 31, 2017 - \$956) was past due. The Company considers all amounts greater than 90 days past due. These past due accounts are considered to be collectible, except as provided in the allowance for doubtful accounts. When determining whether past due accounts are uncollectible, the Company factors in the past credit history of the counterparties. The following table provides an aging analysis of the Company's accounts receivables:

Current	30-60 days	60-90 days	90+days	Total
10,138	561	580	974	12,253

At June 30, 2018, the Company has an allowance for doubtful accounts of \$724 (December 31, 2017 – \$659).

#### LIQUIDITY RISK

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they are due. The nature of the oil and gas industry is capital intensive and the Company maintains and monitors a certain level of cash flow to finance operating and capital expenditures. Refer to note 15 for disclosure related to the management of capital.

The expected timing of cash flows relating to financial liabilities as at June 30, 2018 is as follows:

	< 1 Year	1 – 2 Years	2 – 5 Years	Thereafter
Senior notes – principal	-	-	60,000	-
Accounts payable and accrued liabilities	28,684	-	-	-
	28,684	-	60,000	-

## CEQUENCE ENERGY LTD.

### Notes to the Condensed Consolidated Financial Statements

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#### 14. CHANGES IN NON-CASH WORKING CAPITAL

	Three months ended		Six months ended	
	2018	June 30, 2017	2018	June 30, 2017
Accounts receivable	(364)	(1,050)	2,486	1,788
Deposits and prepaid expenses	(376)	(25)	(564)	(106)
Accounts payable and accrued liabilities	(5,518)	(11,733)	(4,422)	(12,119)
Net change in non-cash working capital	<b>(6,258)</b>	<b>(12,808)</b>	<b>(2,500)</b>	<b>(10,437)</b>
Allocated to:				
Operating activities	2,489	(1,665)	1,857	(1,355)
Investing activities	(8,747)	(11,146)	(4,357)	(9,082)
Financing activities	-	3	-	-
	<b>(6,258)</b>	<b>(12,808)</b>	<b>(2,500)</b>	<b>(10,437)</b>

#### 15. CAPITAL MANAGEMENT

Cequence's objectives are to maintain a flexible capital structure in order to meet its financial obligations, execute on strategic opportunities throughout the business cycle and respond to changes in economic conditions. The Company's capital comprises shareholders' equity, demand credit facilities, senior notes and working capital. Cequence manages the capital structure and makes adjustments in light of economic conditions and the risk characteristics of the underlying assets.

In order to maintain or adjust the capital structure, Cequence may issue new common shares, issue new debt or replace existing debt, adjust capital expenditures and acquire or dispose of assets. The Company evaluates its capital structure based on net debt to cash flow from operating activities and the current credit available to Cequence compared to its budgeted capital expenditures.

At June 30, 2018, Cequence has \$60,000 in Senior Notes due on October 3, 2018 which were refinanced as described in Note 16. The Senior Notes contain incurrence covenants that use a Debt to Cashflow test (as defined in the lending agreement) that is in excess of 2.5 times for the preceding four quarters to limit the incurrence of additional debt, the creation of liens in connection with indebtedness, dividends and other distributions, asset sales and other matters, and customary events of default. At June 30, 2018, the Company's Debt to Cashflow ratio was in excess of 2.5 times (December 31, 2017 – 2.4 times). The Company does not currently anticipate initiating an action that would be restricted by the incurrence covenants.

The Company's \$9,000 Credit Facility did not have any amounts drawn and was extended until September 28, 2018 as described in Note 16. The Company's Credit Facility is based on the lenders' review of the Company's oil and natural gas reserves with the next scheduled review expected to be completed in September 2018. The Credit Facility has a covenant that requires Senior Debt to twelve month trailing EBITDA, as defined in the bank agreement, to be less than 3:0 to 1:0. The Company was in compliance with the lender's covenant at June 30, 2018 with a ratio of 0.1 times (December 31, 2017 – 0.1 times).

## CEQUENCE ENERGY LTD.

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The Company continues to review its options to improve its financial leverage including alternative financing arrangements, property acquisitions or divestitures, corporate mergers and acquisitions, other recapitalization opportunities, further adjustments to the capital program, use of risk management contracts or the issuance of additional equity.

#### 16. SUBSEQUENT EVENTS

##### Senior Notes

On July 27, 2018, Cequence entered into a second lien secured loan agreement with the Senior Note lender for a \$60 million loan facility due October 3, 2022 (the "Term Loan") to refinance the existing Senior Notes which were due on October 3, 2018.

Interest will be paid quarterly at the rate of 5% per annum if the 12-month trailing Funds Flow from Operations is equal to or less than \$40 million; and 10% per annum if the 12-month trailing Funds Flow from Operations is greater than \$40 million. Funds Flow from Operations is defined as cash flow from operating activities before decommissioning liability expenditures and net change in non-cash working capital.

Cequence has granted the lender second lien security over all of the Company's assets (with the exception of its Simonette joint venture property) through a \$100,000 demand debenture, which will rank junior in priority to the security securing the obligations under the Company's Credit Facility pursuant to an intercreditor agreement. The Term Loan is subject to a cross default clause and the same financial covenants as the Company's Credit Facility as well as certain other non-financial covenants and restrictive covenants, including restrictions over asset sales, restricted payments, the incurrence of additional indebtedness and other transactions outside of the ordinary course of business.

As part of the refinancing Cequence issued 36.8 share purchase warrants entitling the lender to purchase common shares of the Company at a price of \$0.10 per common share which are exercisable for 4 years from the date of issuance.

At any time prior to the maturity of October 3, 2022, the Company has the option to make voluntary prepayments towards the Term Loan. Subject to restrictions in the intercreditor agreement, there are mandatory repayments related to asset sales and the incurrence of unsecured debt.

The Term Loan is subject to the successful closing of not less than \$5 million under the Rights Offering as described below on or before September 30, 2018.

##### Rights Offering

On July 27, 2018, Cequence filed a Rights Offering Circular for holders of common shares on August 9, 2018 (the "record date") to subscribe for up to 245,527,883 flow-through common shares of the Company at a price of \$0.035 per share (the "Rights Offering") for gross proceeds of up to \$8.6 million. The Company has in place standby commitments from two of its directors that will, collectively, guarantee that at least \$5 million will be raised under the Rights Offering.

Cequence expects that the Rights Offering is expected to close on or about September 13, 2018. There is no assurance that the Rights Offering will close or will close as described.

##### Demand Credit Facilities

Cequence has amended its Credit Facility and extended the maturity date until September 28, 2018. The next scheduled review is to take place in September 2018.