March 28, 2016

Monthly Update

Vol. 3 Issue 2

From the desk of Ingram Gillmore, President & CEO

We regularly include the following data populated with estimated monthly results:

Capital *

($k CAD)	Q1 15	Q2 15	Q3 15	Dec-15	Q4 15	**2015**	Jan-16	Feb-16	Q1 16 TD
Drill & Complete	-1,763	1,656	4,899	18	2,109	6,901	113	-28	85
Facilities	1,893	1,957	1,396	299	1,867	7,113	-31	111	80
Land & Seismic	332	332	314	428	462	1,440	-14	-12	-26
A&D	-133	-554	0	0	0	-687	-80	-400	-480
Other	-290	340	-177	-625	-443	-570	-10	-25	-35
TOTAL	**39**	**3,731**	**6,432**	**120**	**3,995**	**14,197**	**-22**	**-354**	**-376**

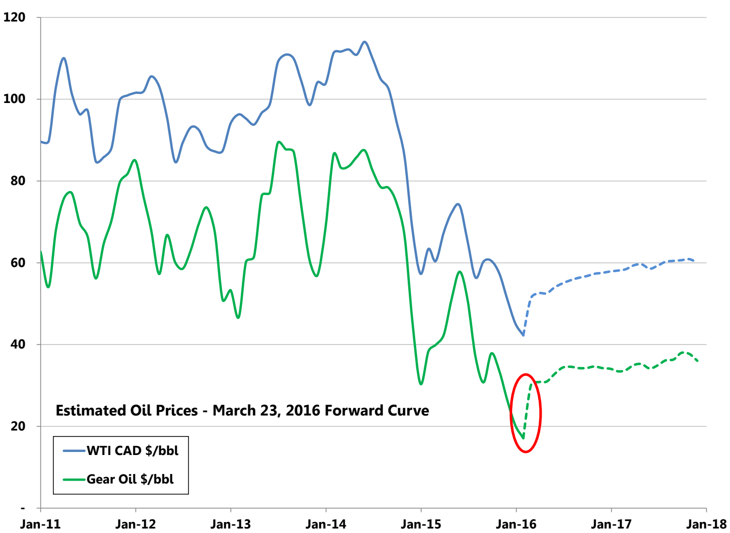
Production (boe/d) *

	Q1 15	Q2 15	Q3 15	Dec-15	Q4 15	2015	Jan-16	Feb-16	Q1 16 TD
Sales	**6,624**	**5,632**	**5,430**	**4,792**	**5,015**	**5,670**	**4,665**	**4,349**	**4,512**
Field	6,332	5,642	5,531	4,791	5,011	5,625	4,560	4,485	4,524

** Estimates based on field data, actuals will vary from estimates due to accruals and adjustments. Such variances may be material.*

This year has been very dynamic so far on the pricing front. I believe that the beginning of the year will go on record as one of the worst streaks of consecutive negative oil prices to ever occur. However, as bad as it seems, this year also apparently provided the shock required to finally jumpstart a true industry response to low prices. Oil focused rig counts are now setting record lows, and some industry observers have gone so far as to predict a price shock to the upside in a few years when the production declines really start to accelerate.

I am not quite ready to plan Gear's future around an upside price shock, but I am pleased to see what the forecast now looks like for Gear's future oil sales.



As you can see, the forecast for Gear's oil revenue per barrel has almost doubled from the record low in February. If you look closer at the chart you should notice that on a percentage basis, the heavy oil price has improved more dramatically than the underlying West Texas light oil price. The main reason for this is because the heavy oil differential, or discount to WTI, was almost 50% in February and it has now improved to a value much closer to 30%.

It is worth noting that although a 30% heavy oil differential is a dramatic improvement from February, it is still materially higher than the 5 year historical average of 22.5%.

So what can we expect for heavy oil differentials for the rest of the year… or for the next five years? I honestly cannot tell you anything for certain. The traditional supply and demand fundamentals do seem to be starting to correct with rig counts at record lows, and refineries completing turnaround season to ramp up for a busy driving season likely catalyzed by very low gasoline prices.

An interesting fact on demand for heavy oil that does not get highlighted often is that heavy oil is a key ingredient in the construction of roadways. In fact Gear has been selling oil to paving firms since 2011 to the tune of approximately $4.5 million of revenue to date. The good news regarding future asphalt demand is that with the recent approval of the United States Federal Funding Act and the Canadian government's recent commitment to larger infrastructure spending, there is expected to be new stability in paving funding across North America for the next 5 years. This increased demand will reverse the previous 10 year trend of decreasing asphalt usage. The forecast from our paving clients is for asphalt consumption to increase over the next few years to 2008 levels. This forecasted increase could translate into 5,000,000 more tonnes of asphalt being consumed per year, which for Gear Energy and other heavy oil producers equates to;

5,000,000 tonnes / 30% residue x 6.3bbls per tonne / 365 days = 287,000 bbl/d

That is 287,000 bbl/d of potentially increased demand for heavy oil that is largely going to be sourced from the PADD II refining region which just happens to be one of the areas most heavily supplied by Western Canadian production. The Gear team are encouraged by the potential for an increased demand for our product and we look forward to assisting in the North American development of new infrastructure.

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