GEAR ENERGY

Monthly Update

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FROM THE DESK OF INGRAM GILLMORE, PRESIDENT & CEO

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

Capital * ($k CAD)	Q4 16	2016	Q1 17	Q2 17	17-Sep	Q3 17	17-Oct	17-Nov	Q4 17	2017 YTD
Drill & Complete	3,083	**9,501**	14,563	3,856	2,650	7,610	2,444	3,076	5,520	**31,549**
Facilities	2,106	**5,064**	3,193	2,718	1,339	3,065	1,837	1,803	3,640	**12,616**
Land & Seismic	978	**1,278**	1,147	262	39	288	322	18	340	**2,037**
A&D	-74	**57,616**	-68	128	-166	1,636	-15	46	31	**1,727**
Other	-100	**-1,479**	-119	-676	-450	-450	0	0	0	**-1,245**
TOTAL	**5,993**	**71,980**	**18,716**	**6,288**	**3,412**	**12,149**	**4,588**	**4,943**	**9,531**	**46,684**

Production (boe/d) *	Q4 16	2016	Q1 17	Q2 17	17-Sep	Q3 17	17-Oct	17-Nov	Q4 17	2017 YTD
Sales	**6,203**	**5,152**	**5,907**	**6,510**	**6,691**	**6,525**	**7,223**	**7,183**	**7,203**	**6,478**
Field	5,942	4,992	6,084	6,468	6,805	**6,646**	7,356	7,355	**7,356**	**6,575**

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

"The report of my death was an exaggeration"

Mark Twain, May 31, 1897

If you have been reading energy headlines the last couple of weeks, you might believe that the Canadian oil industry is about to go the way of the dinosaurs. In particular the reporting on heavy oil pricing this week has been all doom and gloom. Here are a couple of recent headlines as an example:

Canadian Oil Selling For Half Off, And It Could Get Worse

A perfect storm of events has Canadian oil trading at its deepest discount in four years.

http://www.huffingtonpost.ca/2017/12/17/canadian-oil-selling-for-half-off-and-it-could-get-worse_a_23309881/

Canada oil producers exhaust options as pipelines, railroads fill

https://ca.reuters.com/article/businessNews/idCAKBN1EC0GW-OCABS

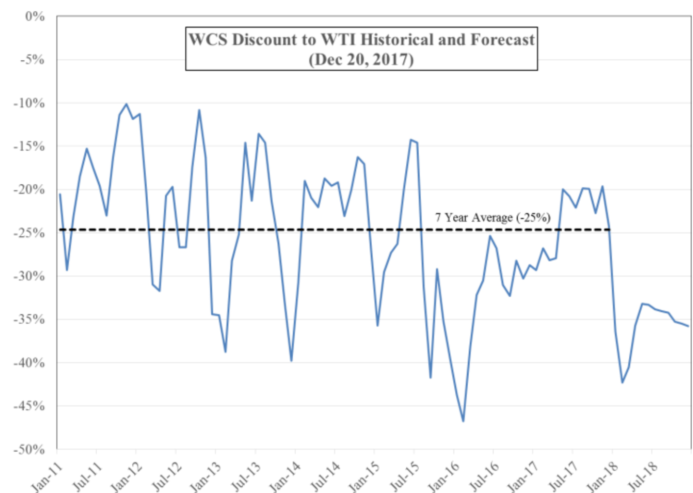
With this kind of macro negativity it is no wonder that I have had inbound calls asking what it all means for Gear Energy. The answer, of course, is complicated, but the short answer is we will keep doing what we always do. We will reinvest our cash flow in projects that target strong returns and help develop future inventory, while always keeping a close eye on the health of the balance sheet.

So what is the longer answer?

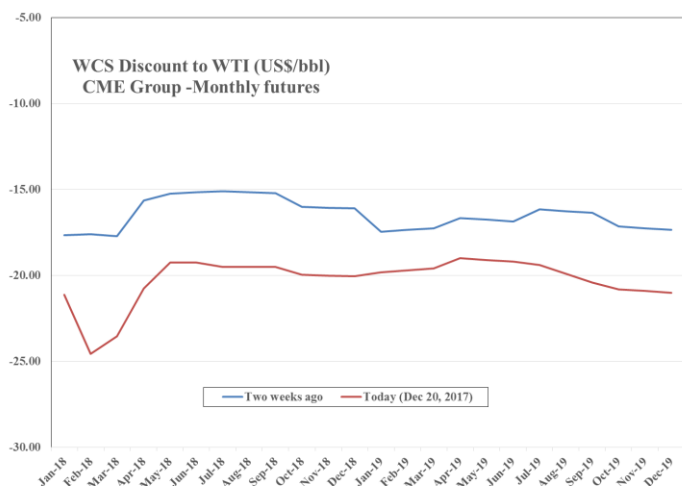
To tackle that we need to step back and review briefly what is currently happening with heavy oil prices.

Essentially, the export capacity for Canadian oil is very tight with supply ramping up from new projects such as Suncor's Fort Hills oil sands project with no new pipeline capacity forecasted to handle these volumes in the near term. The situation was exacerbated recently by the 590,000 bbl/d Keystone pipeline being shut in for a couple of weeks in November to repair a leak. In Canada, basically we are having challenges getting all of our oil to our single market – the United States.

In the past, when this imbalance has occurred, 'crude-by-rail' has taken up the slack and it is likely to do so again. This takes time. Both CN and CP have stated that they have temporary constraints and that there is inevitable delay as they mobilize enough equipment and labour to meet the increased demand from oil shippers. In the meantime we are also hearing that some of the pipelines are being analyzed for potential debottlenecking opportunities. The bottom line on the pricing is that we need to be patient. Over Gear's history we have seen multiple times where the differentials have deviated materially from the normal range of about 25%, and every time they eventually swing back. There has not been a single prolonged period where the differential has materially been below 25% since 2011.



The Keystone outage was the recent catalyst for a very quick and relatively dramatic widening of the discount for Canadian heavy oil prices. As you can see below the current short term forecast has become increasingly negative, with an expectation that things will improve later in 2018. Arguably there is a small silver lining, in the fact that by not supplying as much Canadian oil to the United States, there is going to be some upward pressure on the WTI benchmark prices. With WTI currently around US$58/bbl, that certainly helps to soften the blow of the wider heavy oil discounts.



Despite the negative headlines, the curve right now is still supporting a realized Gear heavy oil price of comfortably more than CDN$40/bbl. Using the recently released 2018 guidance of 10% royalties and $15.50/boe operating costs, the field netback for 2018 with this forward curve would be above $20/boe. At that level we are still able to accomplish our quoted 2018 goals of delivering short term production growth and investing materially in future inventory growth while keeping the balance sheet strong at or below a one times net debt to cash flow ratio. If things do in fact get worse, then we will make adjustments to spending as required. We have always been very hands on with our capital, and now more than ever we need to stay disciplined.

Certain information in this monthly update is forward-looking within the meaning of certain securities laws, and is subject to important risks, uncertainties and assumptions. This forward-looking information may include, among other things, estimated production, expected cash flow and profit from certain assets of Gear, expectations of commodity prices and price differentials, demand for oil, capital expenditure budgets and estimates, royalty rates, operating costs, credit/debt requirements, and drilling inventory and locations. Readers should not rely on such forward-looking information to make investment decisions as the results or events anticipated or predicted in such forward-looking information may differ materially from actual results or events as a result of a number of factors including based on the risk factors as set forth in Gear's most recent annual information form (the "**AIF**"), which is available on this website and at www.sedar.com. Gear has based the forward-looking information on a number of assumptions including the assumptions identified in such monthly updates, which may not be realized. It has also assumed that the risk factors discussed in the AIF will not cause such forward-looking information to differ materially from actual results or events. The forward-looking information in this monthly update describes the expectations of management of Gear as of the respective dates of this monthly update and Gear does not assume any obligation to publicly update or revise them to reflect new events or circumstances, except as may be required pursuant to applicable laws. Readers should not rely on the views of management of Gear as set out in this monthly update to make investment decisions with respect to Gear or other companies in the oil and gas industry and should instead consult with their own investment advisors.

This monthly update may include certain key performance indicators to analyze financial and operating performance such as cash flow from operations, cash flow from operations per debt adjusted share, production per day per thousand debt adjusted shares, operating netbacks, corporate netbacks and net debt, which do not have any standardized meaning prescribed by Canadian generally accepted accounting principles ("**GAAP**") and therefore may not be comparable with the calculation of similar measures for other entities. For additional information on these non-GAAP measures, see Gear's most recent management's discussion and analysis which is available on Gear's website at www.gearenergy.com and at www.sedar.com.

Barrel of oil equivalent ("boe") used in the monthly updates have been based on a conversion ratio of 1 barrel of oil to 6 thousand cubic feet of natural gas. A boe may be misleading, particularly if used in isolation, as such conversion ratio is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.