# FINANCIAL AND OPERATIONAL HIGHLIGHTS

GEAR ENERGY

| (Cdn$ thousands, except per boe amounts) | Three months ended March 31, 2016 | March 31, 2015 | Dec 31, 2015 |
|---|---|---|---|
| **FINANCIAL** | | | |
| Cash flow from operations [(1)] | **3,985** | 12,210 | 4,682 |
| Per weighted average basic and diluted share | **0.05** | 0.17 | 0.06 |
| Cash flow from operating activities | **3,556** | 12,439 | 3,801 |
| Per weighted average basic and diluted share | **0.04** | 0.18 | 0.05 |
| Net income (loss) | **(1,716)** | (4,357) | (26,501) |
| Per weighted average basic and diluted share | **(0.02)** | (0.06) | (0.35) |
| Capital expenditures | **101** | 171 | 3,993 |
| Net acquisitions [(2)] | **(480)** | (132) | - |
| Net debt outstanding [(1)] | **59,550** | 83,313 | 65,972 |
| Shares outstanding, weighted average, basic | **85,484** | 70,817 | 75,918 |
| Shares outstanding, weighted average, diluted | **85,484** | 70,817 | 75,918 |
| Shares outstanding, end of period | **85,484** | 70,817 | 85,484 |
| **OPERATING** | | | |
| Production | | | |
| Oil and liquids (bbl/d) | **4,192** | 6,466 | 4,819 |
| Natural gas (mcf/d) | **1,459** | 944 | 1,176 |
| Total (boe/d) | **4,435** | 6,624 | 5,015 |
| Average prices | | | |
| Oil and liquids ($/bbl) | **20.90** | 35.93 | 31.68 |
| Natural gas ($/mcf) | **1.52** | 2.15 | 2.10 |
| Oil equivalent ($/boe) | **20.25** | 35.39 | 30.93 |
| Netback ($/boe) | | | |
| Commodity and other sales | **20.25** | 35.39 | 30.93 |
| Royalties | **1.63** | 6.28 | 4.72 |
| Operating costs | **15.34** | 17.91 | 16.63 |
| Operating netback (before hedging) | **3.28** | 11.20 | 9.58 |
| Realized risk management gains | **12.71** | 12.91 | 3.86 |
| Operating netback (after hedging) | **15.99** | 24.11 | 13.44 |
| General and administrative | **3.67** | 2.76 | 2.00 |
| Interest | **1.53** | 1.38 | 1.28 |
| Foreign exchange (gain) loss | **-** | (0.52) | 0.06 |
| Drilling commitments | **1.19** | - | - |
| Corporate netback | **9.60** | 20.49 | 10.10 |
| **TRADING STATISTICS** | | | |
| ($ based on intra-day trading) | | | |
| High | **0.61** | 2.62 | 1.10 |
| Low | **0.25** | 1.38 | 0.40 |
| Close | **0.54** | 1.87 | 0.53 |
| Average daily volume (thousands) | **139** | 245 | 157 |

(1) Cash flow from operations and net debt are non-GAAP measures and are reconciled to the nearest GAAP measures under the heading "*Non-GAAP Measures*" in Gear's MD&A.

(2) Net acquisitions exclude non-cash items for decommissioning liability and deferred taxes and is net of post-closing adjustments.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

This management's discussion and analysis ("MD&A") is Gear Energy Ltd. ("Gear" or the "Company") management's analysis of its financial performance. It is dated May 11, 2016 and should be read in conjunction with the unaudited Financial Statements as at and for the three months ended March 31, 2016 and the audited Financial Statements as at and for the year ended December 31, 2015. Both statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board.

The MD&A contains non-generally accepted accounting principles ("GAAP") measures and forward-looking statements and readers are cautioned that the MD&A should be read in conjunction with Gear's disclosure under "Non-GAAP Measures" and "Forward-Looking Statements" included at the end of this MD&A. All figures are in Canadian dollar thousands unless otherwise noted.

### ABOUT GEAR ENERGY LTD.

Gear is a Canadian exploration and production company with predominantly heavy oil production in East Central Alberta and West Central Saskatchewan. Presently, Gear has 21 employees with 13 staff in the Calgary office and 8 employees located in Gear's operating areas in Alberta, British Columbia, and Saskatchewan. Gear also has a number of contract operators in the field. The Company trades on the Toronto Stock Exchange under the symbol GXE.

Gear is return-driven with a focus on delivering per share growth by pursuing assets with the following characteristics:

- Geographically focused
- Definable resource base with low risk production
- Repeatable projects that are statistically economic
- Multiple producing horizons
- Easy surface access and existing infrastructure
- High operatorship

Gear enhances returns of acquired assets by:

- Drilling and developing on acquired lands
- Focusing on operational and cost efficiencies
- Continually improving operations through innovation and imitation
- Adopting and refining advanced drilling and completing techniques
- Pursuing strategic acquisitions with significant potential synergies

### ECONOMIC ENVIRONMENT

The beginning of 2016 will likely go on record as one of the poorest streaks of oil price weakness ever seen. The combination of continued strong production and record inventories in the United States coupled with the return of Iranian barrels to the global supply resulted in a very weak oil market through February of this year. Fortunately, as expected, Industry response in North America has been dramatic, with rig counts plummeting to record lows and US oil production finally starting to decline. The sentiment upon the exit of the quarter was markedly more positive than the beginning and we are holding a cautious amount of optimism for a general trend towards price strengthening, despite the expectation for continued volatility.

Gear experienced record low pricing levels in the first quarter of 2016, with an average received oil price of $20.90 per barrel. Prices at this level do not support economic capital investment and as such Gear put its drilling plans on hold and focused on the balance sheet and debt repayment throughout the quarter. As we exit the first quarter, pricing has rebounded with the forward curve forecast for WTI averaging US$46 per barrel for the last nine months of the year, an increase of almost 40 per cent from the first quarter average of US$33.45. With the forward sentiment now in excess of Gear's economic threshold of WTI US$40, Gear now intends to spend $10 million on capital expenditures in the year, with the majority of that amount allocated to the drilling of ten low risk horizontal oil wells. Gear currently intends to fully fund the capital program through cash flow. Gear's semi-annual borrowing base review is scheduled to be completed by June 1, 2016. The current reserves based syndicated facility of $60 million is likely to be reduced, primarily as a result of a reduction in the proved developed producing reserves balance. However, the actual amount of the borrowing base reduction is not known as at the date of this MD&A. If required to make repayments under the credit facility as the result of a reduction in its borrowing base, Gear's management believes that the Company has adequate access to capital in the form of alternative debt structures and equity in order to meet these requirements; however, there is no certainty that such debt or equity financing will be available. Gear's capital budget for 2016 remains conservative and flexible and management intends to continue to monitor commodity prices and differentials and may at any time suspend, cancel or alter the 2016 capital program in response to any weakening or strengthening of commodity prices or any changes in its access to capital.

**2016 GUIDANCE**
Table 1 summarizes 2016 guidance estimates.

**Table 1**

| | **2016 Guidance** | Q1 2016 |
|---|---|---|
| Production – Annual (boe/d) | **4,000** | 4,435 |
| Royalty rate (%) | **10** | 8 |
| Operating costs ($/boe) | **15.50 – 16.50** | 15.34 |
| General and administrative expense ($/boe) | **2.95** | 3.67 |
| Interest expense ($/boe) | **1.50** | 1.53 |
| Capital expenditures ($ millions) | **10** | 0.1 |

In March 2016, Gear announced its $10 million 2016 capital development program, consisting of $8 million of drilling and completion activity, $1 million of field optimization projects and $1 million of land, maintenance and other corporate costs. The proposed 10 well drilling program is scheduled to commence in July and is forecast to add approximately 800 boepd of oil production to the December average. Production from new wells is expected to offset any further base declines and provide annual volumes in the range of 4,000 boepd. Royalty rates are expected to increase from Q1 2016 as Gear's crown production reference price matches actual received price. General and administrative costs on a per boe basis are expected to decrease from Q1 2016 which included one-time severance payments.

**METRICS**
Gear measures its performance on its ability to grow value on a debt adjusted per share basis. Table 2 details cash flow from operations, and production per debt adjusted share:

**Table 2**

| | Three months ended | | | |
|---|---|---|---|---|
| | **Mar 31, 2016** | Mar 31, 2015 | % Change | Dec 31, 2015 |
| Cash flow from operations per debt adjusted share (1) | **0.016** | 0.100 | (84) | 0.026 |
| Production, boepd per debt adjusted thousand shares (1) | **0.018** | 0.054 | (67) | 0.028 |

(1) Cash flow from operations per debt adjusted share and production boepd per debt adjusted thousand shares are non-GAAP measures and are reconciled to the nearest GAAP measure below under the heading "*Non-GAAP Measures*".

**2016 FIRST QUARTER FINANCIAL AND OPERATIONAL RESULTS**

**Cash flow from operations**
Cash flow from operations for the three months was $4.0 million, compared to $12.2 million from the first quarter of 2015. This $8.2 million decrease in cash flow is the result of decreased commodity prices, production volumes, gains on risk management contracts and foreign exchange, offset by decreased royalty, operating, general and administrative costs and interest expenses.

The following table details the change in cash flow from operations for 2016 relative to 2015:

**Table 3**

| | Three months ended Mar 31, | |
|---|---|---|
| | $ thousands | $/boe |
| **Q1 2015 Cash flow from operations** (1) | 12,210 | 20.48 |
| Volume variance | (6,814) | - |
| Price variance | (6,109) | (15.14) |
| Cash gains/losses on risk management contracts | (2,569) | (0.20) |
| Royalties | 3,089 | 4.66 |
| Expenses: | | |
| Operating | 4,483 | 2.56 |
| General and administrative | 275 | (0.64) |
| Interest | 210 | (0.14) |
| Foreign exchange | (310) | (0.52) |
| Drilling commitments | (480) | (1.19) |
| **Q1 2016 Cash flow from operations** (1) | 3,985 | 9.87 |

(1) Cash flow from operations is a non-GAAP measure and is reconciled to the nearest GAAP measure below under the heading "*Non-GAAP Measures*".

**Net loss**
For the three months ended March 31, 2016, Gear generated a net loss of $1.7 million compared to a loss of $4.4 million in the same period in 2015. The changes in net income are due to several factors discussed below.

**Production**
Sales production volumes averaged 4,435 boepd in the first quarter of 2016, compared to 6,624 boepd in the same period in 2015. This 33 per cent decrease is the direct result of minimal capital investment in 2015 and 2016. Gear invested $14.9 million to drill 12 wells in 2015 with a 100% success rate. Results from these wells were exceptional, however, the capital investment was not sufficient enough to replace 100 per cent of Gear's base production declines. Through 2015 only 38 per cent of the total cash flow was reinvested into development while 62 per cent was dedicated to strengthening the balance sheet by reducing outstanding debt.

Gear currently has approximately 500 bbl/d of uneconomic production shut-in, which will be re-activated should pricing return to levels under which these wells would be cash flow positive.

**Table 4**

| | | Three months ended | | |
|---|---|---|---|---|
| **Production** | **Mar 31, 2016** | Mar 31, 2015 | % Change | Dec 31, 2015 |
| Oil and NGL (bbl/d) | **4,192** | 6,466 | (35) | 4,819 |
| Natural gas (mcf/d) | **1,459** | 944 | 55 | 1,176 |
| Total production (boe/d) (1) | **4,435** | 6,624 | (33) | 5,015 |
| % Oil and NGL production | **94** | 98 | (4) | 96 |
| % Natural gas production | **6** | 2 | 200 | 4 |

(1) Reported production for a period may include minor adjustments from previous production periods.

Gear is deferring 2016 development activity to the second half of the year and as a result, production volumes are forecasted to decline until the fall. Production guidance for the year is currently 4,000 boe per day. Gas production has increased year over year primarily as a result of increased solution gas conservation efforts within our core oil producing areas.

**Revenue**
Sales of crude oil, natural gas and natural gas liquids for the first quarter of 2016 totaled $8.2 million, a 61 per cent decrease over the first quarter 2015 sales of $21.1 million. This decrease is the result of lower realized commodity prices and lower production volumes. A breakdown of sales by product is outlined in Table 5:

**Table 5**

| **Sales by product** | | Three months ended | | |
|---|---|---|---|---|
| ($ thousands) | **Mar 31, 2016** | Mar 31, 2015 | % Change | Dec 31, 2015 |
| Oil and natural gas liquids | **7,971** | 20,913 | (62) | 14,046 |
| Natural gas | **202** | 183 | 10 | 228 |
| Total revenue | **8,173** | 21,096 | (61) | 14,274 |

**Commodity Prices**
**Table 6**

| | | Three months ended | | |
|---|---|---|---|---|
| **Average Benchmark Prices** | **Mar 31, 2016** | Mar 31, 2015 | % Change | Dec 31, 2015 |
| WTI oil (US$/bbl) (1) | **33.45** | 48.65 | (31) | 42.16 |
| WCS differential (US$/bbl) (2) | **(14.24)** | (14.99) | (5) | (14.49) |
| Cdn$ / US$ exchange rate | **1.37** | 1.23 | 11 | 1.33 |
| WCS (Cdn$/bbl) | **26.39** | 41.76 | (37) | 36.94 |
| AECO natural gas ($/mcf) (3) | **2.11** | 2.95 | (28) | 2.65 |
| **Gear Realized Prices** | | | | |
| WCS (Cdn$/bbl) | **26.39** | 41.76 | (37) | 36.94 |
| Gear differential (4) | **(5.49)** | (5.83) | (6) | (5.26) |
| Oil and NGL ($/bbl) | **20.90** | 35.93 | (42) | 31.68 |
| Natural gas ($/mcf) | **1.52** | 2.15 | (29) | 2.10 |
| Total revenue ($/boe) | **20.25** | 35.39 | (43) | 30.93 |

(1) WTI represents posting price of West Texas Intermediate oil.
(2) WCS represents the differential between the average market price for the benchmark Western Canadian Select heavy oil and WTI.
(3) Represents the AECO 7a monthly index
(4) Includes prior period adjustments.

During the quarter WCS heavy barrels traded at the lowest they ever have since inception of the WCS benchmark. Gear's average realized price dipped as low at $17.11 per bbl during quarter, with the quarter averaging $20.90 per barrel. Fortunately, the forward outlook on pricing has improved with US WTI forecasted to average approximately $46 per barrel for the last nine months of the year and WCS differentials expected to tighten in relation to WTI. Considerable risks continue to exist on heavy oil pricing including supply of US shale oil, supply policy decisions from OPEC, and the general demand for oil. Ongoing concerns regarding worldwide over-supply of crude oil have resulted in the forward outlook on commodity prices into 2016 remaining weak. However, there has been a significant reduction in capital investment in the oil sector which historically has resulted in a re-balancing of oil supply and demand.

US denominated WTI prices for the first quarter decreased by 31 per cent over the same period in 2015 and the WCS differential narrowed slightly on an absolute basis from US$14.99 per barrel to US$14.24 per barrel. However, on a relative basis the WCS differential expanded during the first quarter to a 43 per cent discount from WTI versus a 31 per cent discount during the same period in 2015. These two movements were offset with the weakening of the Canadian dollar and resulted in Gear's realized commodity price decreasing by 43 per cent to $20.25 per boe compared to the prior year.

**Royalties**

In the first quarter of 2016, royalties as a percentage of commodity sales were a record low of 8 per cent, a decrease of 55 per cent from the same period in 2015. This decrease is the result of the decreased pricing environment throughout the first quarter and the fact that Gear's 2015 drilling program focused on wells drilled on crown lands where incentive rates apply on most new horizontally drilled production ranging from 2.5 per cent to 5 per cent.

**Table 7**

| **Royalty expense** | Three months ended | | | |
|---|---|---|---|---|
| ($ thousands except per boe and %) | **Mar 31, 2016** | Mar 31, 2015 | % Change | Dec 31, 2015 |
| Royalty expense | **656** | 3,745 | (82) | 2,178 |
| Royalty expense as a % of Sales | **8.0** | 17.8 | (55) | 15.3 |
| Royalty expense per boe | **1.63** | 6.28 | (74) | 4.72 |

Annualized royalty rates for 2016 are expected to average approximately 10 per cent.

**Operating and Transportation costs**

Operating costs plus transportation for the first quarter of 2016 came in at a record low for the company at $15.34 per boe, representing a 14 per cent decrease over the same period in 2015 and an 8 per cent decrease over the fourth quarter of 2015. Throughout the prior year and the first quarter of 2016 Gear's field staff worked to identify cost saving opportunities across the organization. The reduction in operating costs can be attributed to supplier cost reductions, increased operating efficiencies and decreased labor and fuel costs. In addition, Gear shut-in 250 barrels per day of high operating cost production in early 2015 and then an additional 250 barrels per day in the fall of 2015.

Table 8 below summarizes the operating and transportation expense:

**Table 8**

| **Operating and Transportation expense** | Three months ended | | | |
|---|---|---|---|---|
| ($ thousands except per boe) | **Mar 31, 2016** | Mar 31, 2015 | % Change | Dec 31, 2015 |
| Operating expense | **5,351** | 9,658 | (45) | 6,693 |
| Transportation expense | **841** | 1,017 | (17) | 979 |
| Operating and transportation expense | **6,192** | 10,675 | (42) | 7,672 |
| Operating expense per boe | **13.26** | 16.20 | (18) | 14.51 |
| Transportation expense per boe | **2.08** | 1.71 | 22 | 2.12 |
| Operating and transportation expense per boe | **15.34** | 17.91 | (14) | 16.63 |

Gear anticipates continued stability in operating costs throughout 2016 estimating total costs between $15.50 to $16.50 per boe.

**Operating Netbacks**

Gear's operating netback was $3.28 per boe in the first quarter of 2016 compared to $11.20 per boe in the same period of 2015. The decrease is primarily due to low commodity prices, offset by reductions in royalty and operating costs.

The components of operating netbacks are summarized in Table 9:

**Table 9**

| **Netbacks**<br>($ per boe) | **Q1 2016 Total**<br>**($/boe)** | Q1 2015 Total<br>($/boe) | % Change | Q4 2015 Total<br>($/boe) |
|---|---|---|---|---|
| Total sales | **20.25** | 35.39 | (43) | 30.93 |
| Royalties | **(1.63)** | (6.28) | (74) | (4.72) |
| Operating costs | **(15.34)** | (17.91) | (14) | (16.63) |
| Netback | **3.28** | 11.20 | (71) | 9.58 |

**General and Administrative ("G&A") Expenses and Share-based compensation ("SBC")**
G&A totaled $1.5 million for the three months ended March 31, 2016, a decrease of $0.2 million when compared to the same period in 2015 and an increase of $0.6 million from the fourth quarter of 2015. On a per boe basis, G&A increased by 33 per cent when compared to the same period in 2015 as a result of decreased sales production volumes.

During the first quarter of 2016 $0.1 million of directors' fees were paid for services rendered in 2015. Also included in G&A in the first quarter are $0.3 million of one time severance costs. G&A excluding this one-time cost was $2.95 per boe.

SBC is related to bonus awards through the granting of actual common shares and stock options to Gear's employees. There were 855 thousand options granted during the first quarter of 2016 at an average price of $0.35. In addition, 776 thousand options were forfeited. As at March 31, 2016, a total of 6.5 million options were outstanding or eight per cent of the 85.5 million total common shares outstanding.

Table 10 is a breakdown of G&A and SBC expense:

**Table 10**

| **G&A and SBC expense** | Three months ended | | | |
|---|---|---|---|---|
| ($ thousands except per boe) | **Mar 31, 2016** | Mar 31, 2015 | % Change | Dec 31, 2015 |
| G&A expenses | **1,481** | 1,648 | (10) | 923 |
| SBC expense | **174** | 571 | (70) | 518 |
| G&A expenses per boe | **3.67** | 2.76 | 33 | 2.00 |
| SBC expense per boe | **0.43** | 0.96 | (55) | 1.12 |

**Interest and financing charges**
Interest and financing charges totaled $0.6 million in the first quarter of 2016, a decrease of 25 per cent over the first quarter of 2015. This decrease is primarily attributable to a 31 per cent decrease in average debt levels to $69.7 million in the first quarter of 2016 compared to $101 million in the same period in 2015.

Gear's interest rate on its demand facility is dependent on the second preceding quarter's borrowings on its demand facility in comparison to its earnings before interest, taxes, depletion, depreciation, amortization, and accretion. Gear's current annualized borrowing costs, inclusive of financing charges on its credit facility, approximated 3.5 per cent for the first quarter of 2016.

Table 11 is a breakdown of interest expense:

**Table 11**

| **Interest and financing charges** | Three months ended | | | |
|---|---|---|---|---|
| ($ thousands except per boe) | **Mar 31, 2016** | Mar 31, 2015 | % Change | Dec 31, 2015 |
| Interest expense | **590** | 762 | (23) | 538 |
| Financing charges | **23** | 50 | (54) | 47 |
| Standby and letter of credit fees | **3** | 14 | (79) | 7 |
| Interest and financing charges | **616** | 826 | (25) | 592 |
| Interest and financing charges per boe | **1.53** | 1.38 | 11 | 1.28 |

**Risk Management Contracts**
Gear uses or plans to use a variety of derivative instruments to reduce its exposure to fluctuations in commodity prices, foreign exchange rates and interest rates. All present and future transactions are considered to be effective economic hedges; however, Gear's current contracts and future contracts thereafter may not qualify as effective hedges for accounting purposes. The board of directors has authorized a hedging limit of up to 65 per cent of forecast production, net of royalties, for the current and following calendar year.

Gear's hedging strategy continues to be dynamic to the current economic environment. Gear has a mandate to protect its capital program funding for the current and upcoming year by reducing fluctuations in both its cash flow from operations and assigned loan value on its credit facility. As such, Gear has been incorporating both fixed price swaps and collars into its hedging program for 2016 and 2017. Fixed price swaps give Gear price certainty and entering into collars allows Gear to maintain a loan value on its reserves for its credit facility but still allows for upside participation in crude oil prices should they recover.

Gear's hedging program continues to play a significant role in the company's ability to reduce its debt throughout 2016 and to preserve the balance sheet and provide financial flexibility in the future should prices recover. Gear evaluates hedging opportunities on a regular basis and acknowledges the importance its hedging program plays in the determination of its borrowing base.

Table 12 summarizes Gear's hedged volumes for the remainder of 2016 through the first half of 2017.

**Table 12**

**Financial WTI Crude Oil Contracts**

| **Term** | | **Contract** | **Currency** | **Volume bbl/d** | **Sold Swap $/bbl** | **Sold Call $/bbl** | **Bought Put $/bbl** | **Sold Put $/bbl** |
|---|---|---|---|---|---|---|---|---|
| Jan 1, 2016 | Jun 30, 2016 | Collar | CAD | 250 | - | 87.25 | 65.00 | - |
| Jan 1, 2016 | Jun 30, 2016 | Collar | CAD | 250 | - | 82.50 | 65.00 | - |
| Jan 1, 2016 | Jun 30, 2016 | Collar | USD | 230 | - | 67.65 | 57.00 | - |
| Jan 1, 2016 | Jun 30, 2016 | Collar | USD | 270 | - | 67.50 | 57.00 | - |
| Jan 1, 2016 | Dec 31, 2016 | Swap | CAD | 1,000 | 66.00 | - | - | - |
| Jan 1, 2016 | Dec 31, 2016 | Swap | CAD | 500 | 68.00 | - | - | - |
| Jul 1, 2016 | Dec 31, 2016 | Swap | CAD | 500 | 68.50 | - | - | - |
| Jan 1, 2017 | Jun 30, 2017 | Swap | CAD | 120 | 60.00 | - | - | - |

Subsequent to March 31, 2016, Gear entered into the following risk management contracts:

Financial WTI Crude Oil Contracts

| Term | | Contract | Currency | Volume bbl/d | Sold Swap $/bbl | Sold Call $/bbl | Bought Put $/bbl | Sold Put $/bbl |
|---|---|---|---|---|---|---|---|---|
| Jan 1, 2017 | Jun 30, 2017 | Swap | CAD | 80 | 60.00 | - | - | - |
| Jan 1, 2017 | Dec 31, 2017 | Swap | CAD | 200 | 60.00 | - | - | - |

**Drilling Commitments**

During the first quarter Gear negotiated certain drilling commitments which extend the service period on previously existing contracts and as a result incurred a renegotiation fee of $0.5 million or $1.19 per boe, which has been included in the statement of loss and comprehensive loss.

**Depletion, Depreciation and Amortization Expense ("DD&A")**

DD&A during the first quarter of 2016 was $10.61 per boe compared to $15.94 per boe in the same period in 2015 and $18.56 per boe in the fourth quarter of 2015. The reduction in the DD&A rate is the result of selling volumes from inventory that did not have any carrying value ascribed to them as a result of inventory impairments taken in 2015. Gear records its inventory at the lower of cost and net realizable value.

Table 13

| **DD&A Rate** | Three Months Ended | | | |
|---|---|---|---|---|
| ($ thousands except per boe) | **Mar 31, 2015** | Mar 31, 2015 | % Change | Dec 31, 2015 |
| DD&A | **4,283** | 9,503 | (55) | 8,564 |
| DD&A rate per boe | **10.61** | 15.94 | (33) | 18.56 |
| Impairment charges | **-** | - | - | 10,840 |

**Taxes**

A deferred tax recovery was not recorded in the quarter due to the uncertainty of the recoverability of additional deferred income tax assets in the current low commodity price environment. The deferred income tax asset is primarily influenced by temporary differences relating to the book basis of Gear's property, plant and equipment relative to its tax basis. As at March 31, 2016 Gear's estimated tax pools were $295.3 million ($302.1 million at December 31, 2015). These income tax pools are deductible at various rates and annual deductions associated with the initial tax pools will decline over time. No cash income taxes were paid in 2016 or 2015.

**Capital Expenditures, Acquisitions and Dispositions**

Capital expenditures totaled a nominal $0.1 million in the first quarter of 2016 as compared to $0.2 million in the first quarter of 2015. In response to continued weakness in the price of oil, Gear adopted a conservative approach to its capital program where only unavoidable capital was spent during the quarter. This approach will continue throughout the second quarter, followed by a return to capital investment beginning in July 2016 with the initiation of the budgeted 10 well horizontal drilling program.

In March, Gear released its 2016 capital budget which forecasts a total investment of $10 million: $8 million for drilling and completions, $1 million for field optimization projects and $1 million of land, maintenance and other corporate costs. The 2016 drilling program is scheduled to commence at the beginning of the third quarter in order to take advantage of lower drilling costs in the summer months and is expected to include ten 100 per cent working interest horizontal oil locations; three unlined quads in Wildmere, six single lined horizontals in Paradise Hill and one low risk multi-lateral horizontal well to be drilled into a potential new core area.

In the first quarter of 2016 Gear divested a small non-core property with no associated production and fee titles on another property for combined proceeds of $0.5 million.

A breakdown of capital expenditures and net acquisitions is shown in Table 14:

**Table 14**

| **Capital expenditures** (1) | Three Months Ended | | | |
|---|---|---|---|---|
| ($ thousands) | **Mar 31, 2016** | Mar 31, 2015 | % Change | Dec 31, 2015 |
| Geological and geophysical | **(15)** | 47 | (132) | 48 |
| Drilling and completions | **91** | (1,763) | (105) | 2,109 |
| Production equipment and facilities | **39** | 1,594 | (98) | 1,217 |
| Undeveloped land purchased at crown land sales | **(14)** | 285 | (105) | 413 |
| Other | **-** | 8 | (100) | 206 |
| Total capital expenditures | **101** | 171 | (41) | 3,993 |
| Property acquisitions and dispositions, net(2) | **(480)** | (132) | 264 | - |
| Total capital expenditures and net acquisitions | **(379)** | 39 | (1,072) | 3,993 |

(1) Values are inclusive of changes in estimates from prior periods.
(2) Includes post-closing adjustments.

**Decommissioning Liability**
At March 31, 2016, Gear recorded a decommissioning liability of $57 million ($55 million at December 31, 2015) for the future abandonment and reclamation of Gear's properties. The estimated decommissioning liability includes assumptions in respect of actual costs to abandon wells or reclaim the property, the time frame in which such costs will be incurred as well as annual inflation factors in order to calculate the undiscounted total future liability. The future liability has been discounted at the risk free rate of 1.86 per cent (2.04 per cent at December 31, 2015). Abandonment cost estimates are derived from third party government sources and, as a result, can fluctuate from time to time. The increase in liability is due to the reduction in the risk free rate.

Environmental stewardship is a core value at Gear and abandonment and reclamation investments continue to be made in a prudent and responsible manner with oversight by the Board of Directors. Ongoing abandonment expenditures for all of Gear's assets are funded out of cash flow from operations.

**Capitalization, Financial Resources and Liquidity**
A breakdown of Gear's capital structure is outlined in Table 15, as at March 31, 2016 and December 31, 2015:

**Table 15**

| **Debt** | | |
|---|---|---|
| ($ thousands except ratio amounts) | **Mar 31, 2016** | Dec 31, 2015 |
| Net debt (1) | **59,550** | 65,972 |
| Net debt to annualized cash flow from operations | **3.7** | 3.5 |
| Net debt to annual cash flow from operations | **-** | 1.7 |
| Common shares outstanding | **85,484** | 85,484 |

(1) Net debt is a non-GAAP measure and is reconciled to the nearest GAAP measure below under the heading "*Non-GAAP Measures*".

As a result of minimizing capital spending in the first quarter of 2016, Gear was able to apply essentially all of its cash flow against outstanding debt balances, reducing net debt by 10 per cent from $66 million at December 31, 2015 to $59.6 million at March 31, 2016. Gear continues to believe that a proactive disciplined approach to operations and diligent management of its capital structure provides flexibility to react appropriately to volatile market conditions. Since the beginning of the economic downturn Gear has reduced its outstanding debt balances by almost 40 per cent.

*Syndicated Demand Credit Facilities*
During the second quarter Gear will undergo its regular scheduled review of its syndicated demand credit facilities (the "Credit Facilities"). Gear's borrowing limit under the Credit Facilities is dependent on the Company's reserve values and a forward price determined by Gear's lenders. Gear's proved developed producing reserves balance declined year over year and as such a reduction in Gear's borrowing limit is anticipated by management, the magnitude of which is not currently known. Initial discussions have indicated that, if reduced, Gear's new reserves based credit facilities may include a non-conforming portion that would likely be subject to an increased interest rate and would require repayment within six to twelve months. Gear's management believes that any debt repayment that might be required can be dealt with in an orderly fashion from cash flow, an equity offering and/or a possible debt financing; however, there is no certainty that such debt or equity financing will be available.

The current Credit Facilities bear interest at Canadian bank prime or, at Gear's option, Canadian bankers' acceptances, plus applicable margin and stamping fee. The total stamping fees range, depending on Gear's borrowings on its demand facility in comparison to its earnings before interest, taxes, depletion, depreciation, amortization, and accretion, between 50 bps to 250 bps on Canadian bank prime borrowings and between 175 bps and 375 bps on Canadian dollar bankers' acceptances. The undrawn portion of the Credit Facilities is subject to a standby fee in the range of 20 to 45 bps. In addition, the Credit Facilities are secured by a fixed and floating charge on the assets of Gear and are subject to semi-annual reviews. At March 31, 2016 Gear had $52.1 million drawn on the Credit Facilities, leaving $7.9 million in borrowing capacity. The debt has been classified as current as Gear's borrowings are under a revolving operating demand facility that can be called at any time. As at March 31, 2016, Gear was in compliance with its externally imposed financial covenant.

*Debentures*
On November 10, 2015 Gear completed a bought deal financing and private placement (the "Offering") with a syndicate of underwriters to issue 14.7 million common shares at $0.75 per share and $14.8 million of convertible unsecured subordinated debentures (the "Debentures") for total gross proceeds of $26 million. The Offering closed on November 30, 2015.

The Debentures issued on November 30, 2015 have a maturity date of November 30, 2020 and carry a coupon of 4 per cent per annum, payable semi-annually in arrears on May 31 and November 30 until maturity, commencing May 31, 2016. These Debentures carry an equity conversion feature which is subject to shareholder approval. Gear intends to seek shareholder approval for conversion of the Convertible Debentures at its next annual and special meeting of shareholders scheduled to occur on May 11, 2016. If shareholder approval is received, the Debentures will be convertible at the option of the holder at any time prior to the maturity date at a conversion price of $0.87 per common share such that for every $1,000 principal amount of Debentures a holder will receive approximately 1,149.43 common shares. Holders converting their Debentures will be entitled to receive accrued and unpaid interest thereon for the period from the date of the latest interest payment date to, but excluding, the date of conversion. If shareholder approval is not received on May 11, 2016 the annual interest rate on the Debentures will increase to 6.0 per cent per annum. The Debentures are redeemable on or after November 30, 2018 by Gear if the current market price of Gear's common shares is at least 125 per cent of the conversion price at a redemption price equal to the principal amount plus accrued and unpaid interest up to the date of redemption. On or after November 30, 2019, the Debentures may be redeemed by Gear at a redemption price equal to the principal amount plus accrued and unpaid interest up to the date of redemption. For additional information regarding the Debentures see note 6 "Debentures" in the notes the financial statements for the three months ended March 31, 2016.

Gear typically uses two markets to raise capital: equity and bank debt with the expectation that future capital programs will be financed with cash flow from operations and existing credit capacity. Gear's 2016 capital program is expected to be financed primarily through cash flow from operations. Gear's ability to increase its borrowing capacity is based on its reserves value as determined by its external reserve evaluator.

If Gear undertakes any major acquisitions, management would expect to finance the transactions with a combination of equity and debt in a cost effective manner. Gear will continue to be very active looking at acquisitions that meet its investment criteria.

**Shareholders' Equity**
As at March 31, 2016, 85.5 million Gear common shares were outstanding; this amount remains unchanged as at the date of this MD&A and from December 31, 2015.

As at December 31, 2015, a total of 6.4 million options were outstanding with a weighted average exercise price of $2.83 per share and each option entitled the holder to acquire one Gear common share. As at March 31, 2016, a total of 6.5 million options were outstanding with a weighted average exercise price of $2.43 per share and each option entitled the holder to acquire one Gear common share. As at date of this MD&A, a total of 6.4 million options were outstanding with a weighted average exercise price of $2.43 per share and each option entitled the holder to acquire one Gear common share.

As at March 31, 2016, $14.8 million of Debentures were outstanding; this amount remains unchanged as at the date of this MD&A and from December 31, 2015. If the conversion of the Debentures is approved by Gear shareholders at the annual and special meeting of shareholders to be held on May 11, 2016, the Debentures (at the option of the holder) will be convertible into Gear common shares based on a conversion price of $0.87. As such an aggregate of up to 17,011,494 Gear common shares may be issued on conversion of the Debentures. If shareholder approval is received, Gear will also have the option to satisfy its obligation to repay the principal amount of the Debentures due at maturity or redemption of the Debentures by the issuance of Gear common shares and the number of such common shares will be based on 95% of the weighted average trading price of the common shares prior to the date fixed for maturity or redemption. As the number of common shares to be issued on redemption or maturity is based on a price to be determined at a later date, the maximum number of Gear common shares that may be issued upon such redemption or maturity is not determinable at the present time.

**Environmental Initiatives Impacting Gear**
There are no new material environmental initiatives impacting Gear at this time.

**Contractual Obligations and Commitments**
Gear has contractual obligations in the normal course of operations including purchase of assets and services, operating agreements, transportation commitments, sales commitments, royalty obligations, lease rental obligations and employee agreements. These obligations are of a recurring, consistent nature and impact Gear's cash flows in an ongoing manner. Gear also has contractual obligations and commitments that are of a less routine nature as disclosed in its financial statements.

Gear enters into commitments for capital and decommissioning expenditures in advance of the expenditures being made. At a given point in time, it is estimated that Gear has committed to capital expenditures equal to approximately one quarter of its capital budget by means of giving the necessary authorizations to incur the expenditures in a future period.

As at March 31, 2016, Gear had four contractual commitments:
- lease agreements for its head office and its field office,
- two drilling rig commitments

The lease agreement for Gear's head office commenced November 1, 2013 and expires on July 30, 2016 and the lease agreement for Gear's field office is effective until December 31, 2016. The total annual commitment for both lease agreements is $0.1 million. The first drilling rig commitment is effective until December 31, 2016 with a total commitment of $0.7 million; the second commitment is effective January 1, 2017 through December 31, 2020 with a total commitment of $7.7 million. Total outstanding drilling commitments are $8.4 million. For further information see note 12 to the financial statements.

Gear is involved in litigation and claims arising in the normal course of operations. Management is of the opinion that pending litigation will not have a material impact on Gear's financial position or results of operations.

**Off Balance Sheet Arrangements**
Gear has certain lease agreements that were entered into in the normal course of operations, all of which are discussed in the Contractual Obligations and Commitments section above and disclosed in the notes to the audited Financial Statements. All leases have been treated as operating leases whereby the lease payments are included in operating expenses or G&A expenses depending on the nature of the lease. No asset or liability value has been assigned to these leases on the balance sheet as of March 31, 2016.

**Related Party Transactions**
Other than the payment of compensation to key management personnel, the Corporation has not entered into any related party transactions.

**Non-GAAP Measures**
Management uses certain key performance indicators and industry benchmarks such as cash flow from operations, cash flow from operations per debt adjusted share, production per day per thousand debt adjusted share, operating netbacks ("netbacks") and net debt to analyze financial and operating performance. Management believes that these key performance indicators and benchmarks are key measures of profitability for Gear and provide investors with information that is commonly used by other oil and gas companies. These key performance indicators and benchmarks as presented do not have any standardized meaning prescribed by Canadian GAAP and therefore may not be comparable with the calculation of similar measures for other entities.

*Cash Flow from Operations*
Cash flow from operations is a non-GAAP measure defined as cash flow from operating activities before changes in non-cash operating working capital and decommissioning liabilities settled. Gear evaluates its financial performance primarily on cash flow from operations and considers it a key measure as it demonstrates its ability to generate the cash flow necessary to fund our capital program and repay debt. Cash flow from operations is unlikely to be comparable with the calculation of similar measures for other companies.

Table 16 below reconciles cash flow from operating activities to cash flow from operations.

**Table 16**

| | Three months ended | | |
|---|---|---|---|
| ($ thousands) | **Mar 31, 2016** | Mar 31, 2015 | Dec 31, 2015 |
| Cash flow from operating activities | **3,556** | 12,439 | 3,801 |
| Expenditures on site restoration and reclamation | **151** | 298 | 650 |
| Change in non-cash working capital | **278** | (527) | 231 |
| Cash flow from operations | **3,985** | 12,210 | 4,682 |

*Net Debt*
Net debt is a non-GAAP measure defined as debt less current working capital items, excluding risk management contracts. Gear uses net debt as a key indicator of its leverage and strength of its balance sheet. Net debt is directly tied to Gear's cash flow from operations and capital investment. Net debt is unlikely to be comparable with the calculation of similar measures for other companies.

**Table 17**

| **Capital Structure and Liquidity**<br>($ thousands) | **Mar 31, 2016** | Dec 31, 2015 |
|---|---|---|
| Debt | **52,112** | 55,725 |
| Debentures (at face value) (1) | **14,800** | 14,800 |
| Working capital surplus (2) | **(7,362)** | (4,553) |
| Net debt obligations | **59,550** | 65,972 |

(1) Excludes unamortized portion of issuance costs.
(2) Excludes risk management contracts and the conversion approval option.

At March 31, 2016 and December 31, 2015, Gear had a working capital surplus. When in a deficit position, the Corporation is able to meet obligations as they come due by drawing on the Gear Credit Facility. Gear actively manages its liquidity through strategies such as continuously monitoring forecasted and actual cash flows from operating, financing and investing activities, available credit under existing banking arrangements and opportunities to issue additional equity. Management believes that future cash flows generated from these sources will be adequate to settle Gear's financial liabilities; however, there is no certainty that such debt and equity financing will be available. See "Syndicated Demand Credit Facilities".

*Debt adjusted shares*
Debt adjusted shares are calculated by the weighted average shares plus the share equivalent on Gear's average net debt over the period, assuming that the debt were to be extinguished with a share issuance based on the weighted average share price in the period. Table 18 below reconciles the debt adjusted shares.

**Table 18**

| | | Three months ended | |
|---|---|---|---|
| (thousands, except per share amounts) | **Mar 31, 2016** | Mar 31, 2015 | Dec 31, 2015 |
| Weighted average shares | **85,484** | 70,817 | 75,918 |
| Average share price | **0.40** | 1.78 | 0.67 |
| Average net debt (1) | **62,760** | 90,858 | 68,862 |
| Share equivalent on average net debt | **156,900** | 51,044 | 102,731 |
| Debt adjusted shares | **243,384** | 121,861 | 178,649 |

(1) Average net debt obtained by a simple average between opening and ending net debt for the three and twelve months ended.

**Critical Accounting Estimates**
Gear's financial and operating results incorporate certain estimates including:

- Estimated revenues, royalties and operating expenses on production as at a specific reporting date but for which actual revenues and costs have not yet been determined;
- Estimated capital expenditures on projects that are in progress;
- Estimated DD&A charges that are based on estimates of oil and gas reserves that Gear expects to recover in the future;
- Estimated fair values of derivative contracts that are subject to fluctuation depending upon the underlying commodity prices;
- Estimated decommissioning liabilities that are dependent upon estimates of future costs and timing of expenditures;
- Estimated future recoverable value of property, plant and equipment and any associated impairment charges or recoveries;
- Estimated future utilization of tax pools; and
- Estimated employee stock based compensation costs.

Gear has hired individuals and consultants who have the skills required to make such estimates and ensures that individuals or departments with the most knowledge of the activity are responsible for the estimates. Further, past estimates are reviewed and compared to actual results, and actual results are compared to budgets in order to make more informed decisions on future estimates. For further information on the determination of certain estimates inherent in the financial statements refer to Note 4 "Management Judgments and Estimation Uncertainty" in the audited financial statements for the year ended December 31, 2015.

**Disclosure Controls and Procedures**
Disclosure controls and procedures ("DC&P"), as defined in National Instrument 52-109 Certification of Disclosure in Issuers' Annual and Interim Filings, are designed to provide reasonable assurance that information required to be

disclosed in the Company's annual filings, interim filings or other reports filed, or submitted by the Company under securities legislation is recorded, processed, summarized and reported within the time periods specified under securities legislation and include controls and procedures designed to ensure that information required to be so disclosed is accumulated and communicated to management, including the Chief Executive Officer and the Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

**Internal Controls over Financial Reporting**

Gear's Chief Executive Officer and the Chief Financial Officer are responsible for establishing and maintaining internal control over financial reporting ("ICFR") for Gear. They have, as at March 31, 2016, designed ICFR, or caused it to be designed under their supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS. The control framework Gear's officers used to design the Company's ICFR is the Internal Control - Integrated Framework ("COSO Framework") published by The Committee of Sponsoring Organizations of the Treadway Commission ("COSO").

There were no changes in Gear's ICFR during the three months ended March 31, 2016 that materially affected, or are reasonably likely to materially affect, the Company's ICFR.

**Future Accounting Policy Changes**

As of January 1, 2016 Gear was required to adopt amendments to IFRS 11 *Joint Arrangements*. The amendments to this standard requires entities acquiring an interest in a joint operation to apply the principles of IFRS 3 as it relates to business combinations. As of January 1, 2016 the new standard has been adopted and is not anticipated to have a material impact on Gear.

In May 2014, the IASB issued IFRS 15 *Revenue from Contracts with Customers*, which replaces International Accounting Standard ("IAS") 18 *Revenue*, IAS 11 *Construction Contracts*, and related interpretations. The standard is required to be adopted either retrospectively or using a modified transition approach for fiscal years beginning on or after January 1, 2018, with earlier adoption permitted. IFRS 15 will be applied by Gear on January 1, 2018 and the Company is currently evaluating the impact of the standard on Gear's financial statements.

In July 2014, the IASB completed the final elements of IFRS 9 *Financial Instruments*. The standard supersedes earlier versions of IFRS 9 and completes the IASB's project to replace IAS 39 *Financial Instruments: Recognition and Measurement*. IFRS 9, as amended, includes a principle-based approach for classification and measurement of financial assets, a single 'expected loss' impairment model and a substantially-reformed approach to hedge accounting. The standard will come into effect for annual periods beginning on or after January 1, 2018, with earlier adoption permitted. IFRS 9 will be applied on a retrospective basis by Gear on January 1, 2018 and the Company is currently evaluating the impact of the standard on Gear's financial statements.

In January 2016, the IASB issued IFRS 16 *Leases*, which replaces IAS 17 *Leases*. For lessees applying IFRS 16, a single recognition and measurement model for leases would apply, with required recognition of assets and liabilities for most leases. The standard will come into effect for annual periods beginning on or after January 1, 2019, with earlier adoption permitted if the entity is also applying IFRS 15 *Revenue from Contracts with Customers*. IFRS 16 will be applied by Gear on January 1, 2019 and the Company is currently evaluating the impact of the standard on Gear's financial statements.

**Forward-looking Information and Statements**

This first quarter report contains certain forward-looking information and statements within the meaning of applicable securities laws. The use of any of the words "expect", "anticipate", "continue", "estimate", "objective", "ongoing", "may", "will", "project", "should", "believe", "plans", "intends", "strategy" and similar expressions are intended to identify forward-looking information or statements. In particular, but without limiting the foregoing, this first quarter report contains forward-looking information and statements pertaining to the following: Guidance estimates, expected production, pricing, differentials, royalty rate expectations, expected G&A per boe, planned number of gross and net wells drilled, future operating cost trends, expected net debt to cash flow, financing sources for future capital drilling, estimates of normal course obligations, and a number of other matters, including the amount of future decommissioning costs; future liquidity and financial capacity; future results from operations and operating metrics; future costs, expenses and royalty rates; future interest costs; and future development, exploration, acquisition and development activities (including drilling plans) and related capital expenditures.

The forward-looking information and statements contained in this first quarter report reflect several material factors and expectations and assumptions of Gear including, without limitation: that Gear will continue to conduct its operations in a manner consistent with past operations; the general continuance of current industry conditions; the continuance of existing (and in certain circumstances, the implementation of proposed) tax, royalty and regulatory regimes; the accuracy of the estimates of Gear's reserves and resource volumes; certain commodity price and other cost assumptions; and the continued availability of adequate debt and equity financing and cash flow from operations to fund its planned expenditures. Gear believes the material factors, expectations and assumptions reflected in the forward-looking information and statements are reasonable but no assurance can be given that these factors, expectations and assumptions will prove to be correct.

The forward-looking information and statements included in this first quarter report are not guarantees of future performance and should not be unduly relied upon. The forward-looking information and statements are included herein to provide readers with management's plans and assumptions for budgeting purposes and should not be used for other purposes. Such information and statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking information or statements including, without limitation: changes in commodity prices; changes in the demand for or supply of Gear's products; unanticipated operating results or production declines; changes in tax or environmental laws, royalty rates or other regulatory matters; changes in development plans of Gear or by third party operators of Gear's properties, increased debt levels or debt service requirements; inaccurate estimation of Gear's oil and gas reserve and resource volumes; reduced borrowing capacity under the Credit Facilities; demand for repayment by the lenders of all or a portion of the amount outstanding under the Credit Facilities; inability to obtain alternate sources of debt or equity financing; limited, unfavorable or a lack of access to capital markets; increased costs; a lack of adequate insurance coverage; the impact of competitors; and certain other risks detailed from time to time in Gear's public documents available on SEDAR at www.sedar.com, including under the heading "Risk Factors" in Gear's annual information form for the year ended December 31, 2015.

The forward-looking information and statements contained in this first quarter report are made as of the date of this first quarter report, 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**.**

**Barrels of Oil Equivalent**

Disclosure provided herein in respect of BOEs may be misleading, particularly if used in isolation. A BOE conversion ratio of six Mcf to one Bbl is based on an energy equivalency conversion method primarily applicable at the burner tip and do not represent a value equivalency at the wellhead. Additionally, given that the value ratio based on the current price of crude oil, as compared to natural gas, is significantly different from the energy equivalency of 6:1; utilizing a conversion ratio of 6:1 may be misleading as an indication of value.

## QUARTERLY HISTORICAL REVIEW

| | 2016 | 2015 | | | | 2014 | | |
|---|---|---|---|---|---|---|---|---|
| (Cdn$ thousands, except per share, share, and per boe amounts) | Q1 | Q4 | Q3 | Q2 | Q1 | Q4 | Q3 | Q2 |
| **FINANCIAL** | | | | | | | | |
| Sales of crude oil, natural gas and NGLs | 8,173 | 14,274 | 19,476 | 25,528 | 21,096 | 39,558 | 48,273 | 47,331 |
| Cash flow from operations [1] | 3,985 | 4,682 | 7,416 | 14,900 | 12,210 | 20,602 | 22,580 | 20,661 |
| Per basic | 0.05 | 0.06 | 0.10 | 0.21 | 0.17 | 0.29 | 0.32 | 0.29 |
| Per diluted | 0.05 | 0.06 | 0.10 | 0.21 | 0.17 | 0.29 | 0.31 | 0.29 |
| Cash flow from operating activities | 3,556 | 3,801 | 9,873 | 14,432 | 12,439 | 13,425 | 21,428 | 20,294 |
| Per basic and diluted | 0.04 | 0.05 | 0.14 | 0.20 | 0.18 | 0.19 | 0.30 | 0.28 |
| Net income (loss) | (1,716) | (26,501) | (63,360) | (2,301) | (4,357) | (29,999) | 8,914 | 6,420 |
| Per basic | (0.02) | (0.35) | (0.89) | (0.03) | (0.06) | (0.42) | 0.13 | 0.09 |
| Per diluted | (0.02) | (0.35) | (0.89) | (0.03) | (0.06) | (0.42) | 0.12 | 0.09 |
| Capital expenditures | 101 | 3,993 | 6,433 | 4,286 | 171 | 20,969 | 27,314 | 12,328 |
| Net acquisitions [2] | (480) | - | - | (553) | (132) | (1,027) | 1,451 | 79,086 |
| Net debt outstanding [1] | 59,550 | 65,972 | 71,753 | 71,678 | 83,313 | 98,404 | 94,334 | 87,635 |
| Weighted average shares outstanding, basic (thousands) | 85,484 | 75,918 | 70,817 | 70,817 | 70,817 | 70,817 | 70,798 | 70,293 |
| Weighted average shares outstanding, diluted (thousands) | 85,484 | 75,918 | 70,817 | 70,817 | 70,817 | 71,485 | 72,314 | 71,768 |
| Shares outstanding, end of period (thousands) | 85,484 | 85,484 | 70,817 | 70,817 | 70,817 | 70,817 | 70,817 | 70,734 |
| **OPERATING** | | | | | | | | |
| Production | | | | | | | | |
| Oil and liquids (bbl/d) | 4,192 | 4,819 | 5,295 | 5,492 | 6,466 | 6,836 | 6,529 | 6,004 |
| Natural gas (mcf/d) | 1,459 | 1,176 | 810 | 838 | 944 | 991 | 1,101 | 998 |
| Total (boe/d) | 4,435 | 5,015 | 5,430 | 5,632 | 6,624 | 7,001 | 6,712 | 6,170 |
| Average prices | | | | | | | | |
| Oil and liquids ($/bbl) | 20.90 | 31.68 | 39.58 | 50.72 | 35.93 | 62.39 | 79.72 | 85.88 |
| Natural gas ($/mcf) | 1.52 | 2.10 | 2.60 | 2.31 | 2.15 | 3.57 | 3.89 | 4.52 |
| Oil equivalent ($/boe) | 20.25 | 30.93 | 38.98 | 49.81 | 35.39 | 61.42 | 78.17 | 84.30 |
| Netback ($/boe) | | | | | | | | |
| Commodity and other sales | 20.25 | 30.93 | 38.98 | 49.81 | 35.39 | 61.48 | 78.40 | 84.49 |
| Royalties | 1.63 | 4.72 | 4.88 | 5.96 | 6.28 | 11.02 | 14.97 | 16.35 |
| Operating costs | 15.34 | 16.63 | 17.53 | 18.66 | 17.91 | 19.94 | 21.78 | 21.37 |
| Operating netback (before hedging) | 3.28 | 9.58 | 16.57 | 25.19 | 11.20 | 30.52 | 41.65 | 46.77 |
| Realized risk management gains (losses) | 12.71 | 3.86 | 1.80 | 9.37 | 12.91 | 3.98 | (1.04) | (4.16) |
| Operating netback (after hedging) | 15.99 | 13.44 | 18.37 | 34.56 | 24.11 | 34.50 | 40.61 | 42.61 |
| General and administrative | 3.67 | 2.00 | 2.66 | 3.87 | 2.76 | 1.86 | 3.20 | 4.27 |
| Interest | 1.53 | 1.28 | 1.34 | 1.42 | 1.38 | 1.31 | 1.16 | 1.45 |
| Foreign exchange (gain) loss | - | 0.06 | (0.47) | 0.17 | (0.52) | (0.63) | (0.32) | 0.09 |
| Drilling commitments | 1.19 | - | - | - | - | - | - | - |
| Corporate netback | 9.60 | 10.10 | 14.84 | 29.10 | 20.49 | 31.96 | 36.57 | 36.80 |

(1) Cash flow from operations and net debt are non-GAAP measures and are reconciled to the nearest GAAP measure under the heading "*Non-GAAP Measures*".
(2) Net acquisitions exclude non-cash items for decommissioning liability and deferred taxes and is net of post-closing adjustments.

Quarter over quarter fluctuations in revenue is the result of both the amount of oil volumes sent to sale as well as Gear's received price. Volume fluctuations are the result well productivity and success of deliveries to the sales point. The amount of volumes delivered to sale can be influenced by a variety of factors some of which include weather, truck and rail car availability, as well as pipeline apportionments. Gear's received price is based off of WTI less the WCS differential and is further decremented for the quality differential on its specific grade of oil. Net income is further impacted by royalty and operating expenses. Royalty expenses are directly linked to the price received by Gear and, on crown lands, the productivity of each producing well. Gear's royalty profile changes based on Gear's drilling program as well as well results on its existing producing wells. Operating costs are heavily impacted by weather as well as the productivity of each well. Operating costs are typically higher in the winter months due to increased maintenance and energy costs. Transportation costs are included in operating costs, which fluctuate with the amount of volumes sold.

On April 30, 2014 Gear closed an acquisition of heavy oil assets focused near the company's core producing areas of West Central Alberta and East Central Saskatchewan. The acquired assets included approximately 2,100 boepd of high working interest, operated heavy oil production. The acquisition of these assets resulted in increased sales, cash flow from operations and production in the second quarter of 2014 and thereafter.

## CORPORATE INFORMATION

| DIRECTORS | Head Office |
|---|---|
| Don Gray<br>Chairman<br>Arizona, United States of America | Gear Energy Ltd.<br>2600, 500 – 4th Avenue SW<br>Calgary, Alberta T2P 2V6 |
| Greg Bay<br>Independent Businessman<br>Calgary, Alberta | **Auditors**<br>Deloitte LLP<br>700, 850 2nd Street SW<br>Calgary, Alberta T2P 0R8 |
| Raymond Cej<br>Independent Businessman<br>Calgary, Alberta | **Bankers**<br>National Bank of Canada<br>1800, 311 – 6th Avenue SW<br>Calgary, Alberta T2P 3H2 |
| Harry English<br>Independent Businessman<br>Calgary, Alberta | Alberta Treasury Branches<br>Suite 600, 444 – 7th Avenue SW<br>Calgary, Alberta T2P 0X8 |
| Ingram Gillmore<br>President & CEO, Gear Energy Ltd.<br>Calgary, Alberta | Business Development Bank of Canada<br>444, 7th Avenue SW<br>Calgary, AB T2P 0X8 |
| Peter Verburg<br>President, EIQ Capital Corp.<br>Calgary, Alberta | **Engineering Consultants**<br>GLJ Petroleum Consultants Ltd.<br>4100, 400 – 3rd Avenue SW.<br>Calgary, Alberta T2P 4H2 |
| **OFFICERS**<br>Ingram Gillmore<br>President & CEO | **Legal Counsel**<br>Burnet Duckworth & Palmer LLP<br>2400, 525 – 8th Avenue SW<br>Calgary, Alberta T2P 1G1 |
| Yvan Chretien<br>Vice-President, Land | **Transfer Agent**<br>Computershare<br>600, 530 – 8th Avenue SW<br>Calgary, Alberta T2P 3S8 |
| Bryan Dozzi<br>Vice-President, Engineering | |
| David Hwang<br>Vice-President Finance & CFO | |
| Jason Kaluski<br>Vice-President, Operations | |
| Ted Brown<br>Corporate Secretary | |

**FOR FURTHER INFORMATION PLEASE CONTACT:**

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