



CATHEDRAL

2019 Q1 INTERIM REPORT

FINANCIAL HIGHLIGHTS

Dollars in 000's except per share amounts

	Three months ended March 31	
	2019	2018
Revenues	\$ 37,242	\$ 40,157
Adjusted gross margin % ⁽¹⁾	7%	12%
Adjusted EBITDAS ⁽¹⁾	\$ 1,874	\$ 3,443
Diluted per share	\$ 0.04	\$ 0.07
As % of revenues	5%	9%
Cash flow - operating activities	\$ (854)	\$ 2,132
Earnings (loss) before income taxes	\$ (3,568)	\$ 345
Basic and diluted per share	\$ (0.07)	\$ 0.01
Net earnings (loss)	\$ (3,624)	\$ 294
Basic and diluted per share	\$ (0.07)	\$ 0.01
Equipment additions - cash basis	\$ 1,963	\$ 4,474
Weighted average shares outstanding		
Basic (000s)	49,468	49,401
Diluted (000s)	49,469	49,586

	March 31	December 31
	2019	2018
Working capital	\$ 27,554	\$ 30,599
Total assets	\$ 133,393	\$ 121,770
Loans and borrowings excluding current portion	\$ 7,000	\$ 7,000
Shareholders' equity	\$ 84,622	\$ 89,143

(1) Refer to "NON-GAAP MEASUREMENTS"

MANAGEMENT'S DISCUSSION & ANALYSIS

This Management's Discussion & Analysis ("MD&A") for the three months ended March 31, 2019 should be read in conjunction with the annual audited consolidated financial statements and notes thereto for the year ended December 31, 2018, as well as the MD&A in the 2018 Annual Report of Cathedral Energy Services Ltd. (the "Company" or "Cathedral"). This MD&A has been prepared as of May 9, 2019. Dollar amounts are in '000's except for day rates and per share amounts.

2019 Q1 KEY TAKEAWAYS

Revenues decreased 7% from \$40,157 in 2018 Q1 to \$37,242 in 2019 Q1 with the decline attributed to Canadian operations which were expected.

Adjusted gross margin decreased to 7% from 12% in 2018 Q1. This decline was primarily attributed to higher equipment rentals, field labour, trucking and repairs.

Adjusted EBITDAS decreased 46% from \$3,443 in 2018 Q1 to \$1,874 in 2019 Q1. Adjusted EBITDAS margin decreased to 5% of revenues in 2019 Q1 from 9% in 2018 Q1.

Reorganized management within our U.S. business unit.

Mud lube version of our nDurance™ mud motor bearing section has been commercialized in 2 sizes.

OUTLOOK

On a quarter-over-quarter basis, 2019 Q1 U.S. rig activity was down 3% and there are mixed views for activity levels for the balance of 2019. Take away issues in the Permian are expected to be resolved in late 2019 and into 2020. The U.S. market is expected to continue to grow its overall production and that will require an increase in oilfield services spending, including services provided by Cathedral. Industry analysts are cautiously optimistic of improved Canadian drilling activity in H2 of 2019 (in comparison to 2019 Q1 activity levels) and this coincides with post breakup work awarded to Cathedral and discussions with clients. Despite an improvement in WTI and a narrowing of WCS differential in 2019 Q1, producers have not made significant upward adjustments to their capital programs for 2019. Investors are messaging to producers that they need to live within their cash flow and use free cash flow to pay down debt as well as returning value to shareholder by way of repurchasing shares and implementing or increasing dividends.

Cathedral's senior management is disappointed with the quarterly financial results and execution within our U.S. operations. In response to these issues, we have appointed our Canadian Operations Manager, Clayton Lagore, to lead our U.S. business unit replacing both the previous Operations Manager and Sales Manager. Clayton's background has provided him with extensive knowledge of the drilling industry and general business acumen. Clayton joined Cathedral in 2006 and was appointed Canadian Operations Manager in 2008. Prior to joining Cathedral, Clayton worked with major oilfield service companies and owned and operated a number of independent directional drilling businesses which he and his teams built up and sold to larger entities. Clayton has relinquished his responsibilities for the Canadian business unit and Randy Pustanyk, our EVP, will oversee the Canadian business unit. The Company has taken advantage of certain U.S. staff departures to re-assign existing staff and this will result in a material reduction in overhead. We are expecting improved financial results for our U.S. business unit in the back half of 2019. The U.S. market is our primary focus and our intention is to continue to grow our market share.

Testing of our mud lube version of our nDurance™ bearing section has been very successful and this has resulted in Cathedral commercializing our mud lube bearing section in 2 sizes. Introducing a mud lube bearing assembly, in addition to our sealed bearing design, is aimed at increasing reliability and reducing operating costs in specific applications (Permian, Eagleford and Haynesville) where downhole temperatures are higher and which negatively impacts performance of traditional oil seal bearing designs. The Company will be able to modify existing assets, at a minimal cost, to build out quantities as required, negating the need for significant capital investment.

Our patented "Double Bend" and "Double Pad" motor designs are currently in field testing. Both motor designs are based upon substantially the same principles and are expected to significantly reduce drag, stick slip and rotary torque as well as extending the length of laterals that can be drilled with a conventional bottom hole assembly ("BHA") as compared to using a rotary steerable system. The ability to drill longer laterals with a conventional BHA is expected to result in significant savings to Cathedral's clients. We have a number of U.S. operators that are interested in testing this new technology and we will continue to seek additional testing opportunities.

With regard to MWD technology, we continue to be on track to introduce our next generation FUSION(tm) Dual Telemetry (DT) tool in 2019. In addition, a priority is to improve the data rates of our previously commercialized FUSION Linear Pulse ("LP") tool. Further increases in the speed at which surveys are transmitted on FUSION LP are anticipated in Q2 and Q3.

On behalf of Management and the Board of Directors, we would like to thank Jay Zammit for his contributions to Cathedral over the past twenty years. Commencing with Cathedral as private company, Jay has contributed his experience and sage advice over these many years. Jay began his association as a securities lawyer and then in 2003 joined the Board of Directors. After over two decades of service, Jay has made the decision to reduce his work load, pursue personal interests and thus is retiring from the Cathedral board. Management and the Board of Directors would like to take a moment to thank Jay for all he has done as a member of the board including his role on various committees. His contributions will be missed.

2019 CAPITAL PROGRAM

During the three months ended March 31, 2019, the Company invested \$1,963 (2018 - \$4,474) in equipment. The following table details the current period's net equipment additions:

	Three months ended March 31, 2019
Equipment additions:	
Motors	\$ 965
MWD	930
Other	68
Total cash additions	1,963
Less: proceeds on disposal of equipment (excluding capital lease settlements)	(3,962)
Net equipment additions ⁽¹⁾	\$ (1,999)

(1) See "NON-GAAP MEASUREMENTS"

Cathedral's 2019 capital budget approved by the Board of Directors in December 2018 was for net equipment additions of approximately \$4,000 and \$1,700 of intangible additions related to technology development. Subject to operating results and industry outlook, equipment lost-in-hole will be replaced and funded from the proceeds received.

RESULTS OF OPERATIONS – THREE MONTHS ENDED MARCH 31

Effective January 1, 2019, the Company adopted IFRS 16 Leases ("IFRS 16") (see discussion under "New and Future Accounting Policies"). As a result of this new accounting policy, which was adopted retrospectively without restatement of comparative results, expenditures which previously were reported as cost of sales ("COS") or selling, general and administrative ("SGA") expenses are now classified as lease debt obligation repayments and interest expense and the related right of use asset is depreciated against net income on a straight-line basis. As interest and depreciation are excluded from Adjusted EBITDAS (refer to Non-GAAP measurements), Adjusted EBITDAS for 2019 was higher in comparison to 2018 in the amount of \$825. Previously this \$825 was classified as rent expense (being \$683 in COS amounts and \$142 in SGA amounts).

Revenues	2019	2018
Canada	\$ 7,364	\$ 10,637
United States	29,878	29,520
Total	\$ 37,242	\$ 40,157

Revenues 2019 Q1 revenues were \$37,242, which represented a decrease of \$2,915 or 7% from 2018 Q1 revenues of \$40,157.

Canadian revenues (excluding motor rental revenues) decreased to \$6,446 in 2019 Q1 from \$9,698 in 2018 Q1; a 34% decrease. This decrease was the result of: i) a 31% decrease in activity days to 874 in 2019 Q1 from 1,272 in 2018 Q1 and ii) an 3% decrease in the average day rate to \$7,375 in 2019 Q1 from \$7,624 in 2018 Q1.

The average active land rig count in Canada was down 37% in 2019 Q1 compared to 2018 Q1 (source: Baker Hughes). Cathedral's activity levels were roughly in line with this decline. The decrease in day rates was due to a reduction in equipment damage recoveries and lower net base rate related to market pressures.

U.S. revenues (excluding motor rental revenues) increased slightly to \$29,426 in 2019 Q1 from \$29,131 in 2018 Q1; a 1% increase. This increase was the net result of: i) a 9% decrease in activity days to 2,269 in 2019 Q1 from 2,498 in 2018 Q1; and ii) an 11% increase in the average day rate to \$12,969 in 2019 Q1 from \$11,662 in 2018 Q1 (when converted to Canadian dollars).

The average active land rig count for the U.S. was up 9% in 2019 Q1 compared to 2018 Q1 (source: Baker Hughes). The Company experienced a decline in activity days resulting in a decrease in market share compared to 2018 Q1. These declines were related to reductions in client's drilling programs to stay within their cash flow as well as some operational issues. Day rates in USD increased 6% to \$9,756 USD in 2019 Q1 from \$9,231 USD in 2018 Q1 due to increase in recoveries of 3rd party equipment rentals from clients.

Motor rentals in Canada declined slightly while U.S. rentals increased. Combined rental revenues increased to \$1,370 in 2019 compared to \$1,328 a 3% increase.

Gross margin and adjusted gross margin Gross margin for 2019 Q1 was negative compared to 6% in 2018 Q1. Adjusted gross margin (see Non-GAAP Measurements) for 2019 Q1 was \$2,596 or 7% compared to \$4,762 or 12% for 2018 Q1.

Adjusted gross margin, as a percentage of revenue, decreased due to higher equipment rentals, field labour, trucking and repairs. The field labour increased due to industry pressures to retain staff. Rentals increased primarily due to rental of RSS (rotary steerable systems), most of which was rebilled to customers as discussed previously in U.S. day rate section.

Depreciation of equipment allocated to cost of sales increased to \$4,445 in 2019 Q1 from \$2,215 in 2018 Q1 due to changes in estimate of useful life made effective October 1, 2018. Depreciation included in cost of sales as a percentage of revenue was 12% for 2019 Q1 and 6% in 2018 Q1.

Selling, general and administrative expenses ("SG&A") SG&A expenses were \$3,855 in 2019 Q1; an increase of \$28 compared with \$3,827 in 2018 Q1. As a result of the implementation of IFRS 16 there was a decrease of \$142 related to amounts previously classified as rent, but currently classified as lease repayments and interest. Depreciation increased \$672 on the related right of use assets set up under IFRS 16.

Additionally, there were reductions in SG&A wages and related benefits and burdens. As a percentage of revenue, SG&A was 10% in 2019 Q1 compared to 10% in 2018 Q1.

Technology group expenses Technology group expenses are related to new product development and supporting and upgrading existing technology. Technology group expenses consist of salaries and related benefits and burdens as well as shop supplies. Technology group activities spent on new product development are capitalized as intangible assets. Total technology group costs were \$982 in 2019 Q1; an increase of \$151 compared with \$831 in 2018 Q1. The portion of total technology group costs related to new product development was \$230 and this amount has been capitalized as intangible assets (2018 Q1 - \$230). Technology group costs not related to new product development were \$752 in 2019 Q1; an increase of \$151 compared with \$601 in 2018 Q1. Technology group costs increased primarily due to wage increases.

Gain on disposal of equipment During 2019 Q1, the Company had a gain on disposal of equipment of \$2,793 compared to \$3,008 in 2018 Q1. These gains mainly relate to equipment lost-in-hole. Proceeds from clients on lost-in-hole equipment are based on amounts specified in service agreements and, in most cases; these proceeds exceed the net book value of the equipment and result in a gain. The timing of lost-in-hole recoveries is not in the control of the Company and therefore can fluctuate significantly from quarter-to-quarter. In 2019 Q1, the Company received proceeds on lost-in-hole recoveries from clients of \$3,962 (2018 Q1 - \$3,775).

Finance costs Finance costs consist of interest expenses on operating loans, long-term debt and bank charges of \$143 for 2019 Q1 versus \$45 for 2018 Q1. The change was due to increase in average debt levels outstanding in 2019 Q1.

Finance costs lease liability Beginning in 2019 Q1, there was \$262 related to IFRS 16 (2018 Q1 - \$nil) (see discussion under "New and Future Accounting Policies").

Foreign exchange The Company had a foreign exchange gain of \$542 in 2019 Q1 compared to a loss of \$(697) in 2018 Q1 due to the fluctuations of the Canadian dollar relative to the U.S. dollar. The Company's foreign operations are denominated in USD and therefore, upon consolidation, gains and losses due to fluctuations in the foreign currency exchange rates are recorded as other comprehensive income on the balance sheet as a component of equity. However, gains and losses in the Canadian entity on U.S. denominated intercompany balances continue to be recognized in the statement of comprehensive income (loss). Included in the 2019 Q1 foreign currency loss are unrealized gain of \$527 (2018 Q1 - loss of \$669) related to intercompany balances.

Income tax In 2018 Q4, Cathedral derecognized \$13,059 of deferred tax assets due to a recent history of tax losses within Cathedral's Canadian entity. As a result of this, for periods like 2019 Q1 where there are losses in the Canadian entity that are not recognized the effective tax rate is not meaningful. Income tax expense is booked based upon expected annualized effective rates based upon the statutory rates of 27% for Canada and 23% for the U.S.

LIQUIDITY AND CAPITAL RESOURCES

Overview On an annualized basis, the Company's principal source of liquidity is cash generated from operations and proceeds from equipment lost-in-hole. In addition, the Company has the ability to fund liquidity requirements through its credit facility and the issuance of debt and/or equity. Cash flow - operating activities in 2019 Q1 decreased to a loss of \$(854) from \$2,132 in 2018 Q1. This decrease was primarily due to decreased net earnings and the positive impact of changes in working capital in 2018 Q1. This use of cash reduced the Company's cash balances.

Working capital At March 31, 2019 the Company had working capital of \$27,554 (December 31, 2018 - \$30,599). \$2,048 of the decrease in working capital relates to increase in current portion of lease liabilities due to the adoption of IFRS 16.

Credit facility The Company's credit facility (the "Facility") consists of a \$5 million operating facility and a \$15 million extendible revolving credit facility and expires December 31, 2020. The Facility is secured by a general security agreement over all present and future personal property. The Facility provides a definition of EBITDA ("Credit Agreement EBITDA") to be used in calculation of financial covenants.

The financial covenants associated with the amended Facility are:

Consolidated funded debt to consolidated Credit Agreement EBITDA ratio shall not exceed 3.0:1; and
Consolidated interest coverage ratio shall not be less than 2.5:1.

The Facility bears interest at the financial institution's prime rate plus 0.75% to 2.25% or bankers' acceptance rate plus 1.75% to 3.00% with interest payable monthly. Interest rate spreads for the Facility depend on the level of funded debt compared to the 12 month trailing Credit Agreement EBITDA. The Facility provides a means to lock in a portion of the debt at interest rates through bankers' acceptance ("BA") based on the interest rate spread on the date the BA was entered into.

Compliance with Facility covenants

Based on current available information, Cathedral expects to comply with all covenants for the next twelve months.

At March 31, 2019, the Company had drawn \$7,000 of its revolving credit facility, \$nil of its operating facility and had \$5,036 in cash. At March 31, 2019, the Company had consolidated funded debt of \$2,804 which includes five outstanding letters of credit ("LOC") which are included in the funded debt calculation. For the trailing twelve months ended March 31, 2019, Credit Agreement EBITDA was \$12,357.

The calculation of the financial covenants under the Facility as at March 31, 2019 is as follows:

Covenant	Actual Ratio	Required Ratio
Consolidated funded debt to consolidated Credit Agreement EBITDA ratio	0.2:1	3.0:1 (maximum)
Consolidated interest coverage ratio	22.8:1	2.5:1 (minimum)

Contractual obligations In the normal course of business, the Company incurs contractual obligations and those obligations are disclosed in the Company's annual financial statements for the year ended December 31, 2018.

As at March 31, 2019, the Company's commitment to purchase equipment is approximately \$762. Cathedral anticipates expending these funds in 2019 Q2 and Q3.

The Company has issued the following five LOC:

- two securing rent payments on property leases and renew annually with the landlords. The first LOC is \$700 CAD for the first ten years of the lease and then reduces to \$500 for the last five years of the lease. The second LOC is currently for \$542 USD and increases annually based upon annual changes in rent;
- \$75 USD issued for U.S. workers compensation coverage; and
- two securing the Company's corporate credit cards in the amounts of \$75 CAD and \$175 USD.

Share capital At May 9, 2019, the Company has 49,468,117 common shares and 2,959,500 options outstanding with a weighted average exercise price of \$1.03.

CONTROLS AND PROCEDURES

The Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO") are responsible for designing disclosure controls and procedures ("DC&P") and internal controls over financial reporting ("ICFR") as defined in National Instrument 52-109 Certification of Disclosure in Issuer's Annual and Interim Filings ("52-109"), or causing them to be designed under their supervision, in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP.

Cathedral's DC&P have been designed to provide reasonable assurance that material information relating to Cathedral is made known to the CEO and the CFO by others and that information required to be disclosed by Cathedral in its annual filings, interim filings or other reports filed or submitted by Cathedral under securities legislation is recorded, processed, summarized and reported within the time periods specified in applicable securities legislation.

Because of their inherent limitations, DC&P and ICFR may not prevent or detect all misstatements, errors or fraud. Control systems, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control systems are met.

The CEO and CFO have concluded that there have been no changes in internal controls for the period ended on March 31, 2019 that have materially affected, or are reasonably likely to materially affect, Cathedral's ICFR.

RISK FACTORS

The MD&A for the year ended December 31, 2018, which is included in the Company's 2018 Annual Report, includes an overview on risk factors associated with the Company and its operating entities. Those risk factors remain in effect as at March 31, 2019.

GOVERNANCE

The Audit Committee of the Board of Directors has reviewed this MD&A and the related unaudited condensed consolidated interim financial statements and recommended they be approved to the Board of Directors. Following a review by the full Board, the MD&A and financial statements were approved.

NEW AND FUTURE ACCOUNTING POLICIES

i) The Company has adopted IFRS 16 Leases ("IFRS 16") effective January 1, 2019.

The Company utilized the modified retrospective approach in application of the standard. This resulted in the recognition of a lease liability and a corresponding recognition of a right-of-use asset. The Company has chosen to recognize the right-of-use asset on January 1, 2019 at a value equal to the related liability of the lease. The Company also used the exemption for any capital leases recognized prior to January 1, 2019 under the previous standards and to only apply IFRS 16 to contracts that were previously identified as leases. As such, the Company did not apply the standard to any contracts not previously identified as containing a lease. Exemptions were utilized for short-term leases where the term is 12 months or less and for leases of low value items. As well, the classification of cash flows were impacted as the presentation of operating lease payments previously shown as operating cash flows will be split into financing (principal portion) and financing (interest portion) cash flows under IFRS 1616.

The modified retrospective approach does not require restatement of prior period financial information. Accordingly, comparative information in the Company's financial statements are not restated.

As lease payments are made there is a reduction to the principal portion of the lease liability as well as an amount allocated to finance costs. The finance cost is expensed over the lease term. The right of use asset is depreciated over the shorter of the asset's useful life and the lease term on a straight-line basis. Cathedral uses a single discount rate for a portfolio of leases with reasonably similar characteristics.

ii) The Company also adopted IFRS Interpretations Committee ("IFRIC") issued IFRIC 23 Uncertainty over Income Tax Treatments ("IFRIC 23") which clarifies the accounting for uncertainties in income taxes. The adoption of this standard did not have any material impact on the Company's financial statements.

There were no other new or amended standards issued during the three months ended March 31, 2019 that are applicable to the Company in future periods.

SUMMARY OF QUARTERLY RESULTS

Three month periods ended	Mar 2019	Dec 2018	Sep 2018	Jun 2018	Mar 2018	Dec 2017	Sep 2017	Jun 2017
Revenues	\$ 37,242	\$ 43,127	\$ 42,570	\$ 34,973	\$ 40,157	\$ 38,402	\$ 36,015	\$ 34,355
Adjusted EBITDAS ⁽¹⁾	\$ 1,874	\$ 3,412	\$ 6,190	\$ (985)	\$ 3,443	\$ 5,606	\$ 3,909	\$ 2,363
Adjusted EBITDAS ⁽¹⁾ per share - diluted	\$ 0.04	\$ 0.07	\$ 0.13	\$ (0.02)	\$ 0.07	\$ 0.11	\$ 0.08	\$ 0.05
Net earnings (loss)	\$ (3,624)	\$ (17,858)	\$ 3,001	\$ (2,498)	\$ 294	\$ (4,490)	\$ 1,810	\$ 186
Net earnings (loss) per share - basic and diluted	\$ (0.07)	\$ (0.36)	\$ 0.06	\$ (0.05)	\$ 0.01	\$ (0.09)	\$ 0.04	\$ -

(1) Refer to MD&A: see "NON-GAAP MEASUREMENTS"

FORWARD LOOKING STATEMENTS

This MD&A contains certain forward-looking statements and forward-looking information (collectively referred to herein as "forward-looking statements") within the meaning of applicable Canadian securities laws. All statements other than statements of present or historical fact are forward-looking statements. Forward-looking statements are often, but not always, identified by the use of words such as "anticipate", "achieve", "believe", "plan", "intend", "objective", "continuous", "ongoing", "estimate", "outlook", "expect", "may", "will", "project", "should" or similar words suggesting future outcomes. In particular, this MD&A contains forward-looking statements relating to, among other things: take away issues in the Permian are expected to be resolved in late 2019 and into 2020; the U.S. market is expected to continue to grow its overall production and that will require an increase in oilfield services spending, including services provided by Cathedral; industry analysts are cautiously optimistic of improved Canadian drilling activity in H2 of 2019; expecting improved financial results for our U.S. business unit in the back half of 2019; the U.S. market is our primary focus and our intention is to continue to grow our market share; the ability to drill longer laterals with a conventional BHA is expected to result in significant savings to Cathedral's clients; further increases in the speed at which surveys are transmitted on mud pulse are anticipated in Q2 and Q3; projected capital expenditures and commitments and the financing thereof; and Cathedral expects to comply with all covenants during 2019.

The Company believes the expectations reflected in such forward-looking statements are reasonable as of the date hereof but no assurance can be given that these expectations will prove to be correct and such forward-looking statements should not be unduly relied upon.

Various material factors and assumptions are typically applied in drawing conclusions or making the forecasts or projections set out in forward-looking statements. Those material factors and assumptions are based on information currently available to the Company, including information obtained from third party industry analysts and other third party sources. In some instances, material assumptions and material factors are presented elsewhere in this MD&A in connection with the forward-looking statements. You are cautioned that the following list of material factors and assumptions is not exhaustive. Specific material factors and assumptions include, but are not limited to:

- the performance of Cathedral's businesses, including current business and economic trends;
- oil and natural gas commodity prices and production levels;
- alternatives to and changing demand for hydrocarbon products;
- performance obligation to clients;
- capital expenditure programs and other expenditures by Cathedral and its customers;
- currency exchange and interest rates;
- the ability of Cathedral to service its debt;
- the ability of Cathedral to retain and hire qualified personnel;
- the ability of Cathedral to obtain parts, consumables, equipment, technology, and supplies in a timely manner to carry out its activities;
- the ability of Cathedral to maintain good working relationships with key suppliers;
- the ability of Cathedral to market its services successfully to existing and new customers and reliance on major customers;
- risks associated with technology development and intellectual property rights;
- the ability of Cathedral to maintain safety performance;
- the ability of Cathedral to obtain timely financing on acceptable terms;
- the ability to obtain sufficient insurance coverage to mitigate operational risks;
- risks associated with acquisitions and business development efforts;
- environmental risks;
- risks associated with information technology systems;
- changes under governmental regulatory regimes and tax, environmental and other laws in Canada and U.S.; and
- competitive risks.

Forward-looking statements are not a guarantee of future performance and involve a number of risks and uncertainties some of which are described herein. Such forward-looking statements necessarily involve known and unknown risks and uncertainties, which may cause the Company's actual performance and financial results in future periods to differ materially from any projections of future performance or results expressed or implied by such forward-looking statements. These risks and uncertainties include, but are not limited to, the risks identified in this MD&A and in the Company's Annual Information Form under the heading "Risk Factors". Any forward-looking statements are made as of the date hereof and, except as required by law, the Company assumes no obligation to publicly update or revise such statements to reflect new information, subsequent or otherwise.

All forward-looking statements contained in this MD&A are expressly qualified by this cautionary statement. Further information about the factors affecting forward-looking statements is available in the Company's current Annual Information Form that has been filed with Canadian provincial securities commissions and is available on www.sedar.com.

NON-GAAP MEASUREMENTS

Cathedral uses certain performance measures throughout this document that are not defined under GAAP. Management believes that these measures provide supplemental financial information that is useful in the evaluation of Cathedral's operations and are commonly used by other oilfield companies. Investors should be cautioned, however, that these measures should not be construed as alternatives to measures determined in accordance with GAAP as an indicator of Cathedral's performance. Cathedral's method of calculating these measures may differ from that of other organizations, and accordingly, may not be comparable.

The specific measures being referred to include the following:

- i) "Adjusted gross margin" - calculated as gross margin plus non-cash items (depreciation and share-based compensation); is considered a primary indicator of operating performance (see tabular calculation);
- ii) "Adjusted gross margin %" - calculated as adjusted gross margin divided by revenues and is considered a primary indicator of operating performance (see tabular calculation);
- iii) "Adjusted EBITDAS" - defined as earnings before Interest, taxes, depreciation, amortization, share-based compensation, unrealized foreign exchange on intercompany balances, write-down of equipment, write-down of inventory and non-recurring expenses (including severance). Management believes that Adjusted EBITDAS provides supplemental information to net earnings in evaluating the results of the Company's business activities before considering certain charges, how it was financed and how it was taxed; and
- iv) "Net equipment additions" – is equipment additions expenditures less proceeds from equipment lost down-hole. Cathedral uses net equipment additions to assess net cash flows related to the financing of Cathedral's equipment additions.

The following tables provide reconciliations from GAAP measurements to non-GAAP measurements referred to in this MD&A:

Adjusted gross margin

	Three months ended March 31	
	2019	2018
Gross margin	\$ (1,891)	\$ 2,507
Add non-cash items included in cost of sales:		
Depreciation	4,445	2,215
Share-based compensation	42	40
Adjusted gross margin	\$ 2,596	\$ 4,762
Adjusted gross margin %	7%	12%

Adjusted EBITDAS

	Three months ended March 31	
	2019	2018
Earnings (loss) before income taxes	\$ (3,568)	\$ 345
Add:		
Depreciation included in cost of sales	4,445	2,215
Depreciation included in selling, general and administrative expenses	751	36
Share-based compensation included in cost of sales	42	40
Share-based compensation included in selling, general and administrative expenses	107	93
Finance costs	143	45
Finance costs lease liabilities	262	-
Subtotal	2,182	2,774
Unrealized foreign exchange (gain) loss on intercompany balances	(527)	669
Non-recurring expenses	219	-
Adjusted EBITDAS	\$ 1,874	\$ 3,443

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

March 31, 2019 and December 31, 2018

Dollars in '000s

(unaudited)

	March 31 2019	December 31 2018
Assets		
Current assets:		
Cash	\$ 5,036	\$ 6,875
Trade receivables	31,343	35,583
Prepaid expenses	1,724	1,691
Inventories	11,093	11,750
Total current assets	49,196	55,899
Equipment (note 3)	57,700	61,068
Intangible assets	2,820	2,827
Right of use asset (note 4)	21,799	-
Deferred tax assets	1,878	1,976
Total non-current assets	84,197	65,871
Total assets	\$ 133,393	\$ 121,770
Liabilities and Shareholders' Equity		
Current liabilities:		
Operating loan (note 5)	\$ -	\$ 188
Trade and other payables	18,381	23,868
Current taxes payable	964	991
Lease liabilities, current (note 4)	2,137	89
Provision for settlements, current	160	164
Total current liabilities	21,642	25,300
Loans and borrowings (note 5)	7,000	7,000
Provision for settlements, long-term	280	327
Lease liabilities, long-term (note 4)	19,849	-
Total non-current liabilities	27,129	7,327
Total liabilities	48,771	32,627
Shareholders' equity:		
Share capital (note 6)	88,155	88,155
Contributed surplus	10,559	10,410
Accumulated other comprehensive income	11,206	12,252
Deficit	(25,298)	(21,674)
Total shareholders' equity	84,622	89,143
Total liabilities and shareholders' equity	\$ 133,393	\$ 121,770

See accompanying notes to condensed consolidated interim financial statements.

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (LOSS)

Three months ended March 31, 2019 and 2018

Dollars in '000s except per share amounts
(unaudited)

	Three months ended March 31	
	2019	2018
Revenues (note 7)	\$ 37,242	\$ 40,157
Cost of sales:		
Direct costs	(34,646)	(35,395)
Depreciation	(4,445)	(2,215)
Share-based compensation	(42)	(40)
Total cost of sales	(39,133)	(37,650)
Gross margin	(1,891)	2,507
Selling, general and administrative expenses:		
Direct costs	(2,997)	(3,698)
Depreciation	(751)	(36)
Share-based compensation	(107)	(93)
Total selling, general and administrative expenses	(3,855)	(3,827)
Technology group expenses	(5,746)	(1,320)
Gain on disposal of equipment	(752)	(601)
Earnings (loss) from operating activities	2,793	3,008
Finance costs	(3,705)	1,087
Finance costs lease liabilities	(143)	(45)
Finance costs lease liabilities	(262)	-
Foreign exchange gain (loss)	542	(697)
Earnings (loss) before income taxes	(3,568)	345
Income tax recovery (expense):		
Current	-	(162)
Deferred	(56)	111
Total income tax expense	(56)	(51)
Net earnings (loss)	(3,624)	294
Other comprehensive income (loss):		
Foreign currency translation differences for foreign operations	(1,046)	1,195
Total comprehensive income (loss)	\$ (4,670)	\$ 1,489
Net earnings (loss) per share		
Basic and diluted (note 6)	\$ (0.07)	\$ 0.01

See accompanying notes to condensed consolidated interim financial statements.

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

Three months ended March 31, 2019 and 2018

Dollars in '000s

(unaudited)

	Share capital	Contributed surplus	Accumulated other comprehensive income	Retained earnings (deficit)	Total shareholders' equity
Balance at December 31, 2017	\$ 88,059	\$ 9,801	\$ 8,144	\$ (4,613)	\$ 101,391
Total comprehensive income (loss) for three months ended March 31, 2018	-	-	1,195	294	1,489
Issue of shares upon exercise of options	43	(12)	-	-	31
Share-based compensation	-	133	-	-	133
Total contributions by and distributions to shareholders	43	121	-	-	164
Balance at March 31, 2018	\$ 88,102	\$ 9,922	\$ 9,339	\$ (4,319)	\$ 103,044
Balance at December 31, 2018	\$ 88,155	\$ 10,410	\$ 12,252	\$ (21,674)	\$ 89,143
Total comprehensive income for three months ended March 31, 2019	-	-	(1,046)	(3,624)	(4,670)
Share-based compensation	-	149	-	-	149
Balance at March 31, 2019	\$ 88,155	\$ 10,559	\$ 11,206	\$ (25,298)	\$ 84,622

See accompanying notes to condensed consolidated interim financial statements.

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

Three months ended March 31, 2019 and 2018

Dollars in '000s

(unaudited)

	Three months ended March 31	
	2019	2018
Cash provided by (used in):		
Operating activities:		
Earnings (loss) before income taxes	\$ (3,624)	\$ 294
Items not involving cash		
Depreciation	5,196	2,251
Share-based compensation	149	133
Income tax expense	56	51
Gain on disposal of equipment	(2,793)	(3,008)
Finance costs	143	45
Finance costs lease liabilities	262	-
Unrealized foreign exchange (gain) loss on intercompany balances	(527)	669
Cash flow - continuing operations	(1,138)	435
Changes in non-cash operating working capital	287	2,903
Income taxes paid	(3)	(1,206)
Cash flow - operating activities	(854)	2,132
Investing activities:		
Equipment additions	(1,963)	(4,474)
Intangible asset additions	(385)	(301)
Proceeds on disposal of equipment	3,962	3,775
Changes in non-cash investing working capital	(1,262)	(2,294)
Cash flow - investing activities	352	(3,294)
Financing activities:		
Change in operating loan	(188)	(399)
Repayments on loans and borrowings	(574)	(11)
Interest paid	(405)	(45)
Payment on settlements	(40)	(196)
Proceeds on share issuance from exercise of share options	-	31
Advances of loans and borrowings	-	2,500
Restricted cash	-	1,514
Cash flow - financing activities	(1,207)	3,394
Effect of exchange rate on changes on cash	(130)	57
Change in cash and cash equivalents	(1,839)	2,289
Cash, beginning of period	6,875	2,683
Cash, end of period	\$ 5,036	\$ 4,972

See accompanying notes to condensed consolidated interim financial statements.

NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

Three months ended March 31, 2019 and 2018

Dollars in '000s except per share amounts
(unaudited)

1. Reporting entity

Cathedral Energy Services Ltd. (the "Company" or "Cathedral") is a company domiciled in Canada. The Company is a publicly traded company listed on the Toronto Stock Exchange under symbol "CET". The consolidated financial statements of the Company as at and for the period ended March 31, 2019 comprise the Company and its 100% owned subsidiary, Cathedral Energy Services Inc. ("INC"), (together referred to as "Cathedral"). INC is incorporated in the United States of America ("U.S.") and its functional currency is U.S. dollars ("USD").

The Company and INC are primarily involved and engaged in the business of providing directional drilling services to oil and natural gas companies in western Canada and the U.S.

2. Basis of preparation

(a) Statement of compliance

These unaudited condensed consolidated interim financial statements have been prepared in accordance with International Accounting Standard 34, *Interim Financial Reporting* ("IAS 34") ("IFRS" or "GAAP").

Accordingly, certain information and footnote disclosures normally included in the annual financial statements prepared in accordance with IFRS, as issued by the International Accounting Standards Board ("IASB"), have been omitted or condensed. It also requires management to exercise judgment in applying the Company's accounting policies. These unaudited condensed consolidated interim financial statements should be read in conjunction with the Company's consolidated financial statements for the year ended December 31, 2018, which are included in the Company's 2018 Annual Report.

The unaudited condensed consolidated interim financial statements were authorized for issue by the Board of Directors on May 9, 2019.

(b) Basis of measurement

The unaudited condensed consolidated interim financial statements have been prepared on the historical cost basis.

(c) Functional and presentation currency

These unaudited condensed consolidated interim financial statements are presented in Canadian dollars ("CAD"), which is the Company's functional currency. All financial information presented in dollars has been rounded to the nearest thousand except for share and per share amounts.

(d) Significant accounting policies

These unaudited condensed interim consolidated financial statements have been prepared in accordance with IFRS and using the same accounting policies as outlined in note 3 of the consolidated financial statements for the year ended December 31, 2018. The accounting policies have been applied consistently by the Company, except as described below.

i) The Company has adopted IFRS 16 Leases ("IFRS 16") effective January 1, 2019.

The Company utilized the modified retrospective approach in application of the standard. This resulted in the recognition of a lease liability and a corresponding recognition of a right-of-use asset. The Company has chosen to recognize the right-of-use asset on January 1, 2019 at a value equal to the related liability of the lease. The Company also used the exemption for any capital leases recognized prior to January 1, 2019 under the previous standards and to only apply IFRS 16 to contracts that were previously identified as leases. As such, the Company did not apply the standard to any contracts not previously identified as containing a lease. Exemptions were utilized for short-term leases where the term is 12 months or less and for leases of low value items. As well, the classification of cash flows were impacted as the presentation of operating lease payments previously shown as operating cash flows will be split into financing (principal portion) and financing (interest portion) cash flows under IFRS 16.

The modified retrospective approach does not require restatement of prior period financial information. Accordingly, comparative information in the Company's financial statements are not restated.

As lease payments are made there is a reduction to the principal portion of the lease liability as well as an amount allocated to finance costs. The finance cost is expensed over the lease term. The right of use asset is depreciated over the shorter of the asset's useful life and the lease term on a straight-line basis. Cathedral uses a single discount rate for a portfolio of leases with reasonably similar characteristics.

ii) The Company also adopted IFRS Interpretations Committee ("IFRIC") issued IFRIC 23 Uncertainty over Income Tax Treatments ("IFRIC 23") which clarifies the accounting for uncertainties in income taxes. The adoption of this standard did not have any material impact on the Company's financial statements.

There were no other new or amended standards issued during the three months ended March 31, 2019 that are applicable to the Company in future periods.

Financial Statement Impact

The recognition of the present value of minimum lease payments using the Company's incremental borrowing rate on January 1, 2019 resulted in an addition of \$22,356 in right of use assets and lease liabilities. There were no adjustments to opening retained earnings. The Company has recognized lease liabilities in relation to lease arrangements previously disclosed as operating lease commitments. Upon recognition, the Company's average incremental borrowing rate used in measuring lease liabilities was 4.7%. The leases recognized were all for rental of office and shop locations.

Future Accounting Pronouncements

There were no other new or amended standards issued during the period ended March 31, 2019 that are applicable to the Company in future periods.

NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

3. Equipment

During the period, there were additions to drilling equipment of \$1,963 (2018 - \$4,474).

4. Right of use asset and lease liabilities

<i>Right of use asset</i>	Real Property
Balance, December 31, 2018	\$ -
Initial recognition	22,356
Additions	-
Disposals	-
Depreciation	(672)
Exchange adjustments	115
Balance, March 31, 2019	\$ 21,799

Lease liabilities

At December 31, 2018, the Company had lease liabilities of \$89 related to existing vehicle capital leases.

<i>Lease liabilities</i>	Vehicles	Real Property	Total
Balance, December 31, 2018	\$ 89	\$ -	\$ 89
Initial recognition January 1, 2019		22,356	22,356
Interest	1	262	263
Payments	(11)	(826)	(837)
Exchange adjustments	(1)	116	115
Subtotal	\$ 78	\$ 21,908	\$ 21,986
Less current portion	(78)	(2,059)	(2,137)
Lease liabilities, long-term	\$ -	\$ 19,849	\$ 19,849

The maturity analysis of the undiscounted contractual balances of the lease liabilities is as follows:

In one year or less	\$ 3,070
In more than one year, but not more than five years	11,591
In more than five years	12,510
Total	\$ 27,171

The amount recorded in the unaudited interim consolidated statements of earnings for the three months ended March 31, 2019 in relation to short-term leases was \$38.

5. Operating loan and Loans and borrowings

	March 31 2019	December 31 2018
Current liabilities:		
Operating loan	\$ -	\$ 188
Non-current liabilities:		
Secured revolving term loan	7,000	7,000
Total	\$ 7,000	\$ 7,000

The Company's credit facility (the "Facility") consists of a \$5 million operating facility and a \$15 million extendible revolving credit facility and expires December 31, 2020. The Facility is secured by a general security agreement over all present and future personal property. The Facility provides a definition of EBITDA ("Credit Agreement EBITDA") to be used in calculation of financial covenants.

The financial covenants associated with the amended Facility are:

- Consolidated funded debt to consolidated Credit Agreement EBITDA ratio shall not exceed 3.0:1; and
- Consolidated interest coverage ratio shall not be less than 2.5:1.

The Facility bears interest at the financial institution's prime rate plus 0.75% to 2.25% or bankers' acceptance rate plus 1.75% to 3.00% with interest payable monthly. Interest rate spreads for the Facility depend on the level of funded debt compared to the 12 month trailing Credit Agreement EBITDA. The Facility provides a means to lock in a portion of the debt at interest rates through bankers' acceptance ("BA") based on the interest rate spread on the date the BA was entered into.

Compliance with Facility covenants

Based on current available information, Cathedral expects to comply with all covenants for the next twelve months.

NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

At March 31, 2019, the Company had drawn \$7,000 of its revolving credit facility, \$nil of its operating facility and had \$5,036 in cash. At March 31, 2019, the Company had consolidated funded debt of \$2,804 which includes five outstanding letters of credit ("LOC") which are included in the funded debt calculation. For the trailing twelve months ended March 31, 2019, Credit Agreement EBITDA was \$12,357.

The calculation of the financial covenants under the Facility as at March 31, 2019 is as follows:

Covenant	Actual Ratio	Required Ratio
Consolidated funded debt to consolidated Credit Agreement EBITDA ratio	0.2:1	3.0:1 (maximum)
Consolidated interest coverage ratio	22.8:1	2.5:1 (minimum)

6. Share capital

Authorized: An unlimited number of common shares and an unlimited number of preferred shares (issuable in series).

Common shares issued:

	Three months ended March 31, 2019	
	Number	Amount
Issued, beginning of period	49,468,117	\$ 88,155
Issued on exercise of options	-	-
Issued, end of period	49,468,117	\$ 88,155

Basic earnings (loss) per share

The calculation of basic earnings per share for the three months ended March 31, 2019 was based on the profit (loss) attributable to common shareholders of \$(3,624) (2018 – \$294) and a weighted average number of common shares outstanding as follows:

Weighted average number of ordinary shares

	Three months ended March 31,	
	2019	2018
Issued, beginning of period	49,468,117	49,383,951
Effect of share options exercised	-	17,111
Weighted average number of common shares at end of period	49,468,117	49,401,062

Diluted earnings (loss) per share

The calculation of diluted earnings per share for the three months ended March 31, 2019 and 2018 was based on profit attributable to common shareholders of \$294 for 2018 Q1 (no diluted calculation in 2019 Q1 as the Company incurred a loss) and a weighted average number of common shares outstanding after adjustment for the effects of all dilutive potential common shares as follows:

Weighted average number of common shares (diluted)

	Three months ended March 31,	
	2019	2018
Weighted average number of common shares (basic)	49,468,117	49,401,062
Effect of share options on issue	1,324	185,436
Weighted average number of common shares (diluted) at end of period	49,469,441	49,586,498

At March 31, 2019, 3,040,500 options (2018 – 714,000 options) were excluded from the diluted weighted average number of common shares calculation as their effect would have been anti-dilutive. The average market value of the Company's common shares for purposes of calculating the dilutive effect of share options was based on quoted market prices for the period during which the options were outstanding.

7. Revenue

a) Disaggregation of revenue

The following table reconciles revenue by geographic location:

	Three months ended March 31,	
	2019	2018
Canada	\$ 7,364	\$ 10,637
United States	29,878	29,520
Total	\$ 37,242	\$ 40,157

b) Seasonality of operations

A portion of the Company's operations are carried on in western Canada where activity levels in the oilfield services industry are subject to a degree of seasonality. Operating activities in western Canada are generally lower during "spring breakup" which normally commences in mid to late March and continues through to May. Operating activities generally decrease in the fall and peak in the winter months from December until mid to late March. Additionally, volatility in the weather and temperatures not only during this period, but year round, can create additional unpredictability in operational results. Activity levels in the oil and natural gas basins in the U.S. are not subject to the seasonality to the same extent that it occurs in the western Canada region.

NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

8. Commitments

In the normal course of business, the Company incurs contractual obligations and those obligations are disclosed in the Company's MD&A for the year ended December 31, 2018. As at March 31, 2019, the Company had a commitment to purchase approximately \$762 of equipment. Cathedral anticipates expending these funds 2019 Q2 and Q3 based upon current delivery lead times.

The Company has issued the following five standby letters of credit ("LOC"):

- two LOC securing rent payments on property leases and renew annually with the landlords. The first LOC is \$700 CAD for the first ten years of the lease and then reduces to \$500 for the last five years of the lease. The second LOC is currently for \$542 USD and increases annually based upon annual changes in rent;
- one LOC \$75 USD issued for U.S. workers compensation coverage; and
- two LOC securing the Company's corporate credit cards in the amounts of \$75 CAD and \$175 USD.