



CATHEDRAL

2017 Q1 INTERIM REPORT

FINANCIAL HIGHLIGHTS

Dollars in 000's except per share amounts

	Three months ended March 31	
	2017	2016
Revenues	\$ 38,323	\$ 18,744
Adjusted gross margin % ⁽¹⁾	22%	26%
Adjusted EBITDAS ⁽¹⁾	\$ 6,796	\$ 1,476
Diluted per share	\$ 0.16	\$ 0.04
As % of revenues	18%	8%
Funds from continuing operations ⁽¹⁾	\$ 3,989	\$ 167
Diluted per share	\$ 0.09	\$ -
Gain on disposal of foreign subsidiary	\$ -	\$ 10,865
Earnings before income taxes	\$ 3,972	\$ 11,010
Basic and diluted per share	\$ 0.09	\$ 0.30
Diluted per share	\$ 0.09	\$ 0.30
Net earnings	\$ 2,581	\$ 9,683
Basic and diluted per share	\$ 0.06	\$ 0.27
Diluted per share	\$ 0.06	\$ 0.27
Equipment additions - cash basis	\$ 1,570	\$ 268
Weighted average shares outstanding		
Basic (000s)	42,606	36,295
Diluted (000s)	42,761	36,295

	March 31	December 31
	2017	2016
Working capital	\$ 29,710	\$ 39,324
Total assets	\$ 124,460	\$ 136,017
Loans and borrowings excluding current portion	\$ 84	\$ 26,322
Shareholders' equity	\$ 106,186	\$ 90,772

(1) Refer to "NON-GAAP MEASUREMENTS"

MANAGEMENT'S DISCUSSION & ANALYSIS

This Management's Discussion & Analysis ("MD&A") for the three months ended March 31, 2017 should be read in conjunction with the annual audited consolidated financial statements and notes thereto for the year ended December 31, 2016, as well as the MD&A in the 2016 Annual Report of Cathedral Energy Services Ltd. (the "Company" or "Cathedral"). This MD&A has been prepared as of May 11, 2017. Dollar amounts are in '000's except for day rates and per share amounts.

2017 Q1 KEY TAKEAWAYS

Revenues increased 105% from \$18,744 in 2016 Q1 to \$38,323 in 2017 Q1.

Adjusted EBITDAS increased 360% from \$1,476 in 2016 Q1 to \$6,796 in 2017 Q1. Adjusted EBITDAS margin increased to 18% of revenues in 2017 Q1 from 8% in 2016 Q1.

In January, the Company completed the sale of its Flowback and Production testing ("F&PT") assets for net proceeds of \$17,241.

On February 15, 2017, the Company closed a bought deal public offering and insider private placement financing for total gross proceeds of \$14,130. As a consequence of this financing and the sale of the F&PT assets, the Company had no bank debt at March 31, 2017 (excluding letters of credit).

The Company has increased its capital program for 2017 to a committed amount of \$6,800 and may increase capital spending further based on operating cash flow availability in subsequent quarters in 2017. These funds are focused on increasing the capacity of existing equipment and replacing equipment previously lost down hole.

OUTLOOK

What a difference a year can make! In 2016 Q1 we were suffering from the impact of oil prices that had hit a bottom in the \$26 USD bbl range in February. In the first quarter of 2016 we had an average of 10 active jobs running in the United States ("U.S.") and five running in Canada. For the first quarter of 2017 our average job count was almost three times 2016 levels. We have had to make a tremendous shift from shrinking our business throughout most of 2016 to a rapid ramp up starting in late 2016 and into 2017. Ramping up our business has also had many challenges including making sure we have equipment and people available and also ensuring we maintain a high service quality with our customers. We were very pleased with revenue growth and margins achieved in 2017 Q1, on a year-over-year basis, and compared to 2016 Q4.

Despite increased activity levels, we are still challenged on pricing in an environment where there is upward pressure on our costs. Although customers concede that their service related costs will increase in 2017, they are trying to defer price increases as long as possible. At the same time, competitive pressure remains intense as there is still a large amount of directional drilling equipment capacity in the market. Some competitors appear willing to work at low margins in order generate some cash contribution or are pricing aggressively in an effort to gain market share. We expect pricing levels will improve modestly throughout 2017. We have been able to achieve price increases with our some of our longer term clients starting in late Q1 and into Q2. Our customer value proposition is delivering "Better Performance Every Day" which is supported by our proprietary equipment, great people, engineering services and size and scale. This strategy positioned us well during the industry downturn and as activity levels have improved. We are confident our performance matters approach will prevail long term. Competing based on price alone is not a sustainable strategy for our competitors going forward.

Another challenge we are facing, in part due to the competitive dynamics, is that customers are pushing our equipment harder than has been the case in the past to improve drilling times. This has resulted in above average equipment damage and equipment lost-in-hole. In most cases we can recover these costs from customers, however, these losses and damages are impacting our available equipment capacity short-term while the equipment is repaired or replaced. Through our Drilling Engineering Services and Sales teams, we are working with customers to improve drilling practices and are also being more selective with customers we work with. In addition, we are investing capital to improve our equipment capacity and capabilities.

On the expense side we are still focused on cost management and also trying to ensure our expense increases lag price increases. Most of our expenses relate to labour and we are seeing labour cost pressure as the industry ramps up and as a consequence of a tight labour pool resulting from people leaving the industry over the past two years. Our suppliers are in similar positions and also expecting price increases to help them ramp up.

We continue to manage our business cautiously with the expectation we will see continued commodity price volatility going forward. With the increased rig count and productivity of North American shale wells, oil production and inventories are increasing which has put pressure on prices. However, despite the WTI oil price volatility, the rig count in the U.S., our primary market, has been increasing. As goes the outlook on oil prices, so goes the rig count and directional drilling industry activity levels.

An exciting development in 2017 Q1 was the commercial introduction of our downhole generator. The downhole generator uses mud flow to create power for the Measurement-While-Drilling ("MWD") equipment thereby reducing battery use and the associated battery costs. The downhole generator also facilitates improved Electro-Magnetic ("EM") MWD data transmission to improve EM performance and allow it to be used in difficult formations and areas where competitor technologies have limitations.

We are fortunate that the business improvement areas we focused on in the face of adversity over the past two years have set us up favorably to capitalize on an upturn in our industry. Many of the strategic initiatives we have been working on over the last two years have been focused on making sure we can ramp up our business effectively. On the sales side, we have strategies to help us secure higher pricing for our services. On the operations side, we are looking at ways to better manage our labor pool, keep our expenses in line and continue to deliver high quality service. Our technology group continues to make equipment improvements to our existing equipment and explore new products aimed at revenue generation and expense and capital cost reductions.

We remind our shareholders that Q2 is typically a lower revenue quarter for the Canadian oil field services industry, including Cathedral, due to lower activity levels in Canada as a result of spring break-up.

2017 CAPITAL PROGRAM

During the three months ended March 31, 2017 the Company invested \$1,036 (2016 - \$268) in equipment. The following table details the current period's net equipment additions:

	Three months ended March 31, 2017
Equipment additions:	
Growth capital ⁽¹⁾	\$ 492
Maintenance capital ⁽¹⁾	38
Replacement capital ⁽¹⁾	506
Total cash additions	1,036
Less: proceeds on disposal of equipment (excluding capital lease settlements)	(2,250)
Net equipment additions ⁽¹⁾	\$ (1,214)

(1) See "NON-GAAP MEASUREMENTS"

Cathedral's 2017 capital budget ("capex") reviewed by the Board of Directors in December 2016 was for expenditures of \$3,400 with \$350 for growth capital and \$1,500 for replacement and \$1,550 for maintenance capital. Based on improved activity levels and operating cash flow, on May 11, 2017, the Board of Directors approved a revised capex program of \$10,000 of net equipment additions⁽¹⁾ for the year.

The \$10,000 capex plan for 2017 is comprised of \$5,200 of replacement and maintenance capital and \$4,800 of growth capital. The \$5,200 amount, is substantially related for investment to replace items that have been lost-in-hole over the past two years and for equipment upgrades and replacements to improve the capacity of Cathedral's existing MWD and motor fleet. Over the past 2 years, Cathedral deferred replacement and maintenance capital expenditures in the face of low equipment utilization and in order to pay down debt. Subject to operating results and industry outlook, on a go forward basis equipment lost-in-hole will be replaced funded from the proceeds received. As such, Cathedral's total capex in any year may exceed the above noted capex. The 2017 capital budget will be reviewed quarterly based on anticipated future activity levels and operating cash flow. Cathedral intends to finance its 2017 capital budget from cash flow from operations, proceeds from assets lost-in-hole, working capital (cash) and credit facility availability.

RESULTS OF OPERATIONS – THREE MONTHS ENDED MARCH 31

Revenues	2017		2016
Canada	\$	10,466	\$ 5,663
United States		27,857	13,081
Total	\$	38,323	\$ 18,744

Revenues 2017 Q1 revenues were \$38,323, which represented an increase of \$19,579 or 105% from 2016 Q1 revenues of \$18,744. Both Canada and United States U.S. operations had increases due to increases in drilling activity. In late 2016, due to a limited supply of the Company's proprietary motors, the Company made the decision to reduce the number of rental motors available in both Canada and the U.S. in favor of redirecting motors on jobs where both equipment and staff are deployed and the total cash flow contribution is typically higher. As a consequence motor rental revenue in both Canada and the U.S. were less in 2017 Q1 compared to 2016 Q1.

Canadian revenues (excluding motor rental revenues) increased to \$9,307 in 2017 Q1 from \$3,354 in 2016 Q1; a 178% increase. This increase was the result of: i) a 184% increase in activity days to 1,423 in 2017 Q1 from 501 in 2016 Q1; net of ii) a 2% decrease in the average day rate to \$6,540 in 2017 Q1 from \$6,695 in 2016 Q1. Partially offsetting the revenue increase was a decrease of \$1,150 in motor rental revenue. Motor rental revenues for 2017 Q1 were \$1,159 (2016 Q1 - \$2,309).

The average active land rig count in Canada was up 87% in 2017 Q1 compared to 2016 Q1. The increase in the Company's activity days relative to the active rigs drilling was a result of sales and marketing efforts and the Company demonstrating performance on client jobs. The decrease in day rates was in part due to type of work performed, but mainly due to decreases in day rates charged to customers, which were a result of competitive pressure, and pricing concessions provided to customers to secure work. Many of these customer pricing concessions were carried forward from late 2016.

U.S. Directional Drilling revenues (excluding motor rental revenues) increased to \$27,578 in 2017 Q1 from \$11,977 in 2016 Q1; a 130% increase. This increase was the result of: i) a 162% increase in activity days to 2,565 in 2017 Q1 from 979 in 2016 Q1; net of ii) a 12% decrease in the average day rate to \$10,752 in 2017 Q1 from \$12,234 in 2016 Q1 (when converted to Canadian dollars). All U.S. operating areas saw increases in activity days.

The average active land rig count for the U.S. was up 36% in 2017 Q1 compared to 2016 Q1. Again, due to efforts of sales and marketing staff and performance on client jobs, the Company was able to increase market share compared to 2016 Q1. Day rates in USD fell to \$8,117 USD in 2017 Q1 from \$8,906 USD in 2016 Q1; a 9% decline. U.S. day rates decreases were partially offset by the U.S. division providing footage drilling services to certain clients, which can result in higher relative day rates. U.S. motor rental revenues for 2017 Q1 were \$279 compared to \$1,104 in 2016 Q1.

Gross margin and adjusted gross margin Gross margin for 2017 Q1 was 15% compared to 10% in 2016 Q1. Adjusted gross margin (see Non-GAAP Measurements) for 2017 Q1 was \$8,486 or 22% compared to \$4,949 or 26% for 2016 Q1.

Adjusted gross margin, as a percentage of revenue, decreased due to increases in field labour rates, higher equipment rentals and slightly higher equipment repairs on a percentage of revenue basis. These increases were offset by a reduction in the fixed component of cost of sales which were 13% lower on a percentage of revenue basis in 2017 Q1 compared to 2016 Q1. The decrease in the fixed component of cost of sales as a percentage of revenue was mostly attributable to increase in revenues, however there were increases in costs largely related to salaries and other labour related costs.

Depreciation allocated to cost of sales decreased to \$2,606 in 2017 Q1 from \$3,111 in 2016 Q1. Depreciation included in cost of sales as a percentage of revenue was 7% for 2017 Q1 and 17% in 2016 Q1.

Selling, general and administrative expenses ("SG&A") SG&A expenses were \$3,823 in 2017 Q1; a decrease of \$448 compared with \$4,271 in 2016 Q1. As a percentage of revenue, SG&A was 10% in 2017 Q1 compared to 23% in 2016 Q1.

Excluding the non-cash items of depreciation and share-based compensation, SG&A was \$3,751 in 2017 Q1 compared to \$4,188 in 2016 Q1, a decrease of \$437 or 10%. SG&A decreased primarily due to work force reductions. Additionally, 2016 Q1 had costs related to severance that were not incurred in 2017 Q1. Staffing costs included in SG&A include executive, sales, accounting, human resources, payroll, safety, technology support and related support staff. As well, there were year-over-year reductions in virtually every SG&A item due to efforts to reduce expenditures in 2016.

Gain on disposal of equipment During 2017 Q1, the Company had a gain on disposal of equipment of \$2,014 compared to \$891 in 2016 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.

Finance costs Finance costs consist of interest expenses on operating loans, loans and borrowings and bank charges of \$302 for 2017 Q1 versus \$379 for 2016 Q1. The decrease in finance costs relate to repayments of loans in 2017 Q1 partially offset by increases in the interest rates.

Foreign exchange The Company had a foreign exchange gain of \$218 in 2017 Q1 compared to a gain of \$2,354 in 2016 Q1 due to the fluctuations of the Canadian dollar relative to the U.S. dollar. The Company's foreign operations are denominated in a currency other than the Canadian dollar 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 2017 Q1 foreign currency gains are unrealized gain of \$192 (2016 Q1 - \$2,364) related to intercompany balances.

Gain on disposal of foreign subsidiary During 2016 Q1, the Company completed the sale of its wholly-owned Barbados subsidiary for net proceeds of \$nil which resulted in a non-cash gain on sale of \$10,865. The subsidiary held the Company's investment in Venezuela and this sale completed Cathedral's exit from carrying on a business in Venezuela.

Net loss from discontinued operations In 2016 Q4, the Company made the decision to sell its F&PT assets and focus its attention and resources fully on the directional drilling business where it believes it has a strong competitive advantage and better future growth prospects. The proceeds from this sale were used to pay down debt. As such, operating results for the F&PT business have been included in the statements of comprehensive income and statements of cash flows as discontinued operations. For 2017 Q1, the net loss from discontinued operations was \$(118) compared to \$(1,420) net loss for 2016 Q1.

Income tax For 2017 Q1, the Company had an income tax expense of \$1,273 compared to recovery of \$93 in 2016 Q1. Excluding adjustments to prior years' tax provisions, the effective tax rate was 32% for 2017 Q1. Excluding the non-cash gain on disposal of foreign subsidiary but including

the loss from discontinued operations, the effective tax rate was 30% for 2016 Q1. Income tax expense is booked based upon expected annualized effective rates.

LIQUIDITY AND CAPITAL RESOURCES

Overview On an annualized basis the Company's principal source of liquidity is cash generated from operations. In addition, the Company has the ability to fund liquidity requirements through its credit facility and the issuance of debt and/or equity. For the three months ended March 31, 2017, the Company had funds from continuing operations (see Non-GAAP Measurements) of \$3,989 (2016 –\$167). The increase in funds related to continuing operations is due to the increase in activity levels.

During 2017 Q1 the Company completed two major transactions that had a material impact on its outstanding debt. In January, the Company completed the sale of its F&PT assets for net proceeds of \$17,241. On February 15, 2017, the Company closed a bought deal public offering and insider private placement financing for total gross proceeds of \$14,130. As a result of these transactions, in 2017 Q1 the Company reduced its loans and borrowings by \$26,315 which included a complete repayment of revolving term loan of \$26,250. Cash balances as at March 31, 2017 were \$3,783.

Working capital At March 31, 2017 the Company had working capital of \$29,710 (December 31, 2016 - \$39,324) and a working capital ratio of 2.7 to 1 (December 31, 2016 – 3.3 to 1). The decrease in working capital level was primarily due to the sale of F&PT assets held for sale which had been classified as a current asset at December 31 in the amount of \$17,241. Partially offsetting this was an increase in trade receivables of \$8,084 from December 31, 2016. Upon closing of the F&PT sale on January 16, 2017, \$17,200 of the revolving term loan was repaid. The Company continues to retain a good accounts receivable aging profile with 89% of receivables under 60 days at March 31, 2017.

Credit facility The Company has a committed revolving credit facility (the "Facility") that expires in December 2018. The Facility is secured by a general security agreement over all present and future personal property.

The current Facility has been amended seven times. These amendments have certain restrictions, including, but not limited to; paying dividends, utilization of the accordion feature, enhanced lender financial reporting and a cap on any litigation settlement payments without lender approval. As well, effective 2016 Q1, the Company includes lost-in-hole equipment proceeds in the definition of Bank EBITDA (as defined in the credit agreement).

The financial covenants associated with the amended Facility are as follows:

Quarter ending:	Maximum Funded Debt to Bank EBITDA Ratio	Minimum Debt Service Ratio
March 31, 2017	3.5:1	2.0:1
June 30, 2017	3.5:1	2.5:1
September 30, 2017	3.5:1	3.0:1
December 31, 2017	3.25:1	3.0:1
March 31, 2018 and thereafter	3.0:1	3.0:1

Additionally, there is a minimum working capital ratio of 1.25:1.

The Seventh Amending Agreement, dated January 16, 2017, reduced the aggregate commitment to \$23,000 after \$17,200 was repaid upon the sale of F&PT assets and the maturity date was extended to December 2018.

After the amendments discussed above, the Facility bears interest at the bank's prime rate plus 0.50% to 5.00% or bankers' acceptance rate plus 1.75% to 6.25% with interest payable monthly. Interest rate spreads for the Facility depend on the level of funded debt to the 12 month trailing Bank 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.

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

At March 31, 2017, the Company had cash balances in excess of outstanding letters of credit and capital lease obligations. As such its Funded debt to bank EBITDA ratio ("Funded debt ratio") was negative (i.e. net cash balance). As such, the Funded debt ratio has been met, but is not meaningful ("NM") for presentation. For the three months ended March 31, 2017 Bank EBITDA was \$7,021.

The Company's financial ratios at March 31, 2017 were:

Ratio	Actual	Required
Funded debt to Bank EBITDA ratio	NM	3.5:1 Maximum
Debt service ratio	6.8:1	2.0:1 Minimum
Working capital ratio	2.7:1	1.25:1 Minimum

Contractual obligations 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, 2016. As at March 31, 2017, the Company had a commitment to purchase approximately \$810 of equipment.

Share capital At May 11, 2017, the Company has 48,916,451 common shares and 2,411,750 options outstanding with a weighted average exercise price of \$1.47.

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, 2017 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, 2016, which is included in the Company's 2016 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, 2017.

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

There were no other new or amended standards issued during the three months ended March 31, 2017 that are applicable to the Company in future periods. A description of standards and interpretations that will be adopted by the Company in future periods can be found in the notes to the consolidated financial statements for the year ended December 31, 2016.

SUMMARY OF QUARTERLY RESULTS

Three month periods ended	Mar 2017	Dec 2016	Sep 2016	Jun 2016	Mar 2016	Dec 2015	Sep 2015	Jun 2015
Revenues	\$ 38,323	\$ 28,009	\$ 19,489	\$ 14,624	\$ 18,744	\$ 21,161	\$ 26,366	\$ 21,920
Total Adjusted EBITDAS ⁽¹⁾	\$ 6,796	\$ 3,829	\$ 2,173	\$ (1,638)	\$ 1,476	\$ (169)	\$ 3,013	\$ (1,237)
Adjusted EBITDAS ⁽¹⁾ per share - diluted	\$ 0.16	\$ 0.11	\$ 0.06	\$ (0.05)	\$ 0.04	\$ (0.00)	\$ 0.08	\$ (0.03)
Net earnings (loss)	\$ 2,581	\$ (6,420)	\$ (2,126)	\$ (6,916)	\$ 9,683	\$ (10,500)	\$ (8,852)	\$ (15,266)
Net earnings (loss) per share - basic and diluted	\$ 0.06	\$ (0.18)	\$ (0.06)	\$ (0.19)	\$ 0.27	\$ (0.29)	\$ (0.24)	\$ (0.42)
Dividends declared per share	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 0.04	\$ 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: expect pricing levels will improve modestly throughout 2017; expectation we will see continued commodity price volatility going forward; many of the aspects of our business that we focused on in the face of adversity over the past two years have set us up favorably to capitalize on an upturn in our industry; have strategies to help us secure higher pricing for our services; looking at ways to better manage our labor pool, keep our expenses in line and continue to deliver high quality service; technology group continues to make equipment improvements to our existing equipment and explore new products aimed at revenue generation and expense and capital cost reductions; and Cathedral expects to comply with all covenants during 2017.

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;
- capital expenditure programs and other expenditures by Cathedral and its customers;
- 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;
- currency exchange and interest rates;
- risks associated with foreign operations;
- risks associated with acquisitions and business development efforts;
- environmental risks;
- 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 and Annual Report which have been filed with Canadian provincial securities commissions and are 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 oil and gas service 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; is considered a primary indicator of operating performance (see tabular calculation);
- iii) "Total Adjusted EBITDAS" - defined as earnings before share of income/loss from associate, write-down/recovery on investment in associate finance costs, unrealized foreign exchange on intercompany balances, unrealized foreign exchange due to hyper-inflation accounting, taxes, non-recurring gains and losses on disposal of equipment (see non-GAAP measurement), depreciation, write-down of goodwill, write-down of equipment, write-down of inventory and share-based compensation; is considered an indicator of the Company's ability to generate funds flow from operations prior to consideration of how activities are financed, how the results are taxed and measured and non-cash expenses (see tabular calculation). This measure includes both discontinued F&PT operations and continuing Directional Drilling operations;
- iv) "Adjusted EBITDAS from discontinued operations" – Total Adjusted EBITDAS as calculated above from discontinued F&PT operations only;
- v) "Adjusted EBITDAS from continuing operations" – Total Adjusted EBITDAS as calculated above for ongoing Directional Drilling as well as corporate administrative costs;
- vi) "Funds from operations" - calculated as cash provided by operating activities before changes in non-cash working capital and income taxes paid less current tax expense; is considered an indicator of the Company's ability to generate funds flow from operations on an after tax basis but excluding changes in non-cash working capital which is financed using the Company's operating loan (see tabular calculation);
- vii) "Growth equipment additions" or "Growth capital" – is capital spending which is intended to result in incremental revenues or decreased operating costs. Growth capital is considered to be a key measure as it represents the total expenditures on equipment expected to add incremental revenues and funds flow to the Company;
- viii) "Maintenance equipment additions" or "Maintenance capital" – is capital spending incurred in order to refurbish or replace previously acquired other than "replacement equipment additions" described below. Such additions do not provide incremental revenues. Maintenance capital is a key component in understanding the sustainability of the Company's business as cash resources retained within Cathedral must be sufficient to meet maintenance capital needs to replenish the assets for future cash generation;
- ix) "Replacement equipment additions" or "Replacement capital" – is capital spending incurred in order to replace equipment that is lost downhole. Cathedral recovers lost-in-hole costs including previously expensed depreciation on the related assets from customers. Such additions do not provide incremental revenues. The identification of replacement equipment additions is considered important as such additions are financed by way of proceeds on disposal of equipment (see discussion within the MD&A on "gain on disposal of equipment");
- x) "Infrastructure equipment additions" or "Infrastructure capital" – is capital spending incurred on land, buildings and leasehold improvements. Infrastructure capital is a component in understanding the sustainability of the Company's business as cash resources retained within Cathedral must be sufficient to meet maintenance capital needs;
- xi) "Non-recurring gains and losses on disposal of equipment" – are disposals of equipment that do not occur on a regular or periodic basis. Unlike the lost-in-hole recoveries, the proceeds from these gains are not used on equivalent replacement property. These are often on non-field equipment such as land and buildings;
- xii) "Net equipment additions" – is equipment additions expenditures less proceeds on the regular disposal of equipment (the proceeds on sale of land and buildings have been excluded). Cathedral uses net equipment additions to assess net cash flows related to the financing of Cathedral's equipment additions; and
- xiii) "Net debt" – is loans and borrowing less working capital. Management uses net debt as a metric to shows the Company's overall debt level.

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	
	2017	2016
Gross margin	\$ 5,865	\$ 1,827
Add non-cash items included in cost of sales:		
Depreciation	2,606	3,111
Share-based compensation	15	11
Adjusted gross margin	\$ 8,486	\$ 4,949
Adjusted gross margin %	22%	26%

Total Adjusted EBITDAS

		Three months ended March 31	
		2017	2016
Earnings before income taxes	\$	3,972	\$ 11,010
Add:			
Depreciation included in cost of sales		2,606	3,111
Depreciation included in selling, general and administrative expenses		25	34
Share-based compensation included in cost of sales		15	11
Share-based compensation included in selling, general and administrative expenses		47	49
Finance costs		302	379
Subtotal		6,967	14,594
Unrealized foreign exchange gain on intercompany balances		(192)	(2,364)
Write-down of inventory		-	277
Gain on disposal of foreign subsidiary		-	(10,865)
Non-recurring expenses		127	436
Adjusted EBITDAS from continuing operations		6,902	2,078
Adjusted EBITDAS from discontinued operations		(106)	(602)
Total Adjusted EBITDAS	\$	6,796	\$ 1,476

Funds from operations

		Three months ended March 31	
		2017	2016
Cash flow - operating activities	\$	(568)	\$ 4,156
Add (deduct):			
Changes in non-cash operating working capital		6,105	(4,235)
Income taxes paid (recovered)		(893)	120
Current tax recovery (expense)		(655)	126
Funds from operations	\$	3,989	\$ 167

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

March 31, 2017 and December 31, 2016

Dollars in '000s

(unaudited)

	March 31 2017	December 31 2016
Assets		
Current assets:		
Cash	\$ 3,783	\$ 1,898
Trade receivables	34,329	26,245
Current taxes recoverable	-	1,336
Prepaid expenses	1,421	1,611
Inventories	7,768	8,037
Assets held for sale (note 5)	-	17,241
Total current assets	47,301	56,368
Equipment (note 4)	66,256	68,158
Intangible assets	2,013	1,978
Deferred tax assets	8,890	9,513
Total non-current assets	77,159	79,649
Total assets	\$ 124,460	\$ 136,017
Liabilities and Shareholders' Equity		
Current liabilities:		
Operating loan	\$ -	\$ 2,105
Trade and other payables	14,766	12,837
Current taxes payable	220	-
Loans and borrowings (note 6)	382	459
Provision for settlements, current (note 7)	2,223	1,643
Total current liabilities	17,591	17,044
Loans and borrowings (note 6)	84	26,322
Provision for settlements, long-term (note 7)	599	1,879
Total non-current liabilities	683	28,201
Total liabilities	18,274	45,245
Shareholders' equity:		
Share capital (note 8)	87,617	74,481
Contributed surplus	9,679	9,620
Accumulated other comprehensive income	11,009	11,371
Deficit	(2,119)	(4,700)
Total shareholders' equity	106,186	90,772
Total liabilities and shareholders' equity	\$ 124,460	\$ 136,017

See accompanying notes to condensed consolidated interim financial statements.

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

Three months ended March 31, 2017 and 2016

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

	Three months ended March 31	
	2017	2016
Revenues	\$ 38,323	\$ 18,744
Cost of sales:		
Direct costs	(29,837)	(13,795)
Depreciation	(2,606)	(3,111)
Share-based compensation	(15)	(11)
Total cost of sales	(32,458)	(16,917)
Gross margin	5,865	1,827
Selling, general and administrative expenses:		
Direct costs	(3,751)	(4,188)
Depreciation	(25)	(34)
Share-based compensation	(47)	(49)
Total selling, general and administrative expenses	(3,823)	(4,271)
	2,042	(2,444)
Gain on disposal of equipment	2,014	891
Earnings (loss) from operating activities	4,056	(1,553)
Finance costs	(302)	(379)
Foreign exchange gain	218	2,354
Write-down of inventory	-	(277)
Gain on disposal of foreign subsidiary (note 9)	-	10,865
Earnings before income taxes	3,972	11,010
Income tax recovery (expense):		
Current	(655)	126
Deferred	(618)	(33)
Total income tax recovery (expense)	(1,273)	93
Net earnings from continuing operations	2,699	11,103
Net loss from discontinued operations (note 5)	(118)	(1,420)
Net earnings	2,581	9,683
Other comprehensive income (loss):		
Foreign currency translation differences for foreign operations	(362)	(3,205)
Foreign currency translation gain on disposal of foreign subsidiary	-	1,348
Total comprehensive income	\$ 2,219	\$ 7,826
Net earnings from continuing operations per share		
Basic and diluted	\$ 0.06	\$ 0.31
Net loss from discontinued operations per share		
Basic	\$ (0.00)	\$ (0.04)
Net earnings per share		
Basic and diluted	\$ 0.06	\$ 0.27

See accompanying notes to condensed consolidated interim financial statements.

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

Three months ended March 31, 2017 and 2016

Dollars in '000s

(unaudited)

	Share capital	Contributed surplus	Accumulated other comprehensive income	Retained earnings (deficit)	Total shareholders' equity
Balance at December 31, 2015	\$ 74,481	\$ 9,470	\$ 11,577	\$ 1,079	\$ 96,607
Total comprehensive income (loss) for three months ended March 31, 2016	-	-	(3,205)	9,683	6,478
Accumulated other comprehensive income recognized in income on sale of subsidiary	-	-	1,348	-	1,348
Transactions with shareholders, recorded directly in equity contributions by and distributions to shareholders for three months ended March 31, 2016:					
Share-based compensation	-	60	-	-	60
Total contributions by and distributions to shareholders	-	60	-	-	60
Balance at March 31, 2016	\$ 74,481	\$ 9,530	\$ 9,720	\$ 10,762	\$ 104,493
Balance at December 31, 2016	\$ 74,481	\$ 9,620	\$ 11,371	\$ (4,700)	\$ 90,772
Total comprehensive income (loss) for three months ended March 31, 2017	-	-	(362)	2,581	2,219
Transactions with shareholders, recorded directly in equity contributions by and distributions to shareholders for three months ended March 31, 2017:					
Issue of shares from bought deal public offering and insider private placement	13,131				13,131
Issue of shares upon exercise of options	5	(1)			4
Share-based compensation	-	60	-	-	60
Total contributions by and distributions to shareholders	13,136	59	-	-	13,195
Balance at March 31, 2017	\$ 87,617	\$ 9,679	\$ 11,009	\$ (2,119)	\$ 106,186

See accompanying notes to condensed consolidated interim financial statements.

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

Three months ended March 31, 2017 and 2016

Dollars in '000s

(unaudited)

	Three months ended March 31	
	2017	2016
Cash flow provided by (used in):		
Operating activities:		
Net earnings from continuing operations	\$ 2,699	\$ 11,103
Items not involving cash:		
Depreciation	2,631	3,145
Total income tax (recovery) expense	1,273	(93)
Unrealized foreign exchange gain on intercompany balances	(192)	(2,364)
Finance costs	302	379
Share-based compensation	62	60
Gain on disposal of equipment	(2,014)	(891)
Write-down of inventory	-	277
Gain on disposal of foreign subsidiary (note 9)	-	(10,865)
Cash flow - continuing operations	4,761	751
Cash flow - discontinued operations (note 5)	(117)	(710)
Changes in non-cash operating working capital	(6,105)	4,235
Income taxes (paid) recovered	893	(120)
Cash flow - operating activities	(568)	4,156
Investing activities:		
Equipment additions	(1,036)	(268)
Intangible asset additions	(79)	(45)
Proceeds on disposal of equipment	2,393	1,205
Proceeds on disposal of discontinued operations	17,252	-
Changes in non-cash investing working capital	196	646
Cash flow - investing activities	18,726	1,538
Financing activities:		
Change in operating loan	(2,105)	(2,088)
Repayments on loans and borrowings	(26,313)	(2,603)
Proceeds on share issuance from bought deal public offering and insider private placement	13,131	-
Proceeds on share issuance from exercise of share options	4	-
Payments on settlement	(668)	-
Interest paid	(305)	(134)
Cash flow - financing activities	(16,256)	(4,825)
Effect of exchange rate on changes in cash	(17)	(95)
Change in cash	1,885	774
Cash, beginning of period	1,898	1,426
Cash, end of period	\$ 3,783	\$ 2,200

See accompanying notes to condensed consolidated interim financial statements.

NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

Three months ended March 31, 2017 and 2016

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 year ended December 31, 2016 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.

During 2016 Q1, the Company disposed of its 100% interest in Directional Plus International Inc. ("DPI"). See note 9 for further details.

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, 2016, which are included in the Company's 2016 Annual Report.

The unaudited condensed consolidated interim financial statements were authorized for issue by the Board of Directors on May 11, 2017.

(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, 2016. The accounting policies have been applied consistently by the Company.

Future Accounting Pronouncements

There were no other new or amended standards issued during the period ended March 31, 2017 that are applicable to the Company in future periods. A description of standards and interpretations that will be adopted by the Company in future periods can be found in the notes to the consolidated financial statements for the year ended December 31, 2016.

3. Seasonality of operations

A significant 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.

4. Equipment

During the period, there were additions to drilling equipment of \$1,036 (2016 - \$268).

5. Assets held for sale and discontinued operations

On December 16, 2016, the Company entered into an agreement to sell the fixed assets of its Flowback and Production Testing ("F&PT") cash generating unit. As such, the net realizable value of the F&PT equipment has been reclassified as assets held for sale on the consolidated balance sheet and the related operations have been presented as discontinued operations for 2017 and 2016. The sale closed on January 15, 2017, and as at December 31, 2016 the assets were written down to their estimated net realizable value of \$17,241.

NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

Operating results related to this division have been included in loss from discontinued operations on the consolidated statements of comprehensive income (loss). Comparative periods have been reclassified to include this division as discontinued operations. The following table provides information with respect to amounts included in the statements of operations related to discontinued operations.

	Three months ended March 31	
	2017	2016
Revenues	\$ 370	\$ 2,351
Cost of sales:		
Direct costs	(421)	(2,395)
Depreciation	(11)	(1,121)
Total cost of sales	(432)	(3,516)
Gross margin	(62)	(1,165)
Selling, general and administrative expenses:		
Direct costs	(66)	(666)
Share-based compensation	3	(2)
Total selling, general and administrative expenses	(63)	(668)
	(125)	(1,833)
Gain (loss) on disposal of property and equipment	10	1
Finance costs	(3)	(7)
Loss before income taxes	(118)	(1,839)
Income tax recovery:		
Deferred	-	419
Total income tax recovery	-	419
Net loss from discontinued operations	\$ (118)	\$ (1,420)

The following table provides information with respect to amounts included in the statements of cash flows related to discontinued operations.

	Three months ended March 31	
	2017	2016
Cash provided by (used in):		
Operating activities:		
Net loss from discontinued operations	\$ (118)	\$ (1,420)
Items not involving cash		
Depreciation	11	1,121
Share-based compensation	(3)	2
Deferred tax recovery	-	(419)
Gain on disposal of property and equipment	(10)	(1)
Finance costs	3	7
Cash flow - discontinuing operations	\$ (117)	\$ (710)

6. Loans and borrowings

	March 31	December 31
	2017	2016
Current liabilities:		
Current portion of finance lease liabilities	\$ 382	\$ 459
Non-current liabilities:		
Finance lease liabilities	\$ 84	\$ 72
Secured revolving term loan	-	26,250
Total	\$ 84	\$ 26,322

Terms and debt repayment schedule

The Company has a committed revolving credit facility (the "Facility") that expires in December 2018. The Facility is secured by a general security agreement over all present and future personal property.

The current Facility has been amended seven times. These amendments have certain restrictions, including, but not limited to; paying dividends, utilization of the accordion feature, enhanced lender financial reporting and a cap on any litigation settlement payments without lender approval. As well, effective 2016 Q1, the Company includes lost-in-hole equipment proceeds in the definition of Bank EBITDA (as defined in the credit agreement).

NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

The financial covenants associated with the amended Facility are as follows:

Quarter ending:	Maximum Funded Debt to Bank EBITDA Ratio	Minimum Debt Service Ratio
March 31, 2017	3.5:1	2.0:1
June 30, 2017	3.5:1	2.5:1
September 30, 2017	3.5:1	3.0:1
December 31, 2017	3.25:1	3.0:1
March 31, 2018 and thereafter	3.0:1	3.0:1

Additionally, there is a minimum working capital ratio of 1.25:1.

The Seventh Amending Agreement, dated January 16, 2017, reduced the aggregate commitment to \$23,000 after \$17,200 was repaid upon the sale of F&PT assets and the maturity date was extended to December 2018.

After the amendments discussed above, the Facility bears interest at the bank's prime rate plus 0.50% to 5.00% or bankers' acceptance rate plus 1.75% to 6.25% with interest payable monthly. Interest rate spreads for the Facility depend on the level of funded debt to the 12 month trailing Bank 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.

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

At March 31, 2017, the Company had cash balances in excess of outstanding letters of credit and capital lease obligations. As such its Funded debt to bank EBITDA ratio ("Funded debt ratio") was negative (i.e. net cash balance). As such, the Funded debt ratio has been met, but is not meaningful ("NM") for presentation. For the three months ended March 31, 2017 Bank EBITDA was \$7,021.

The Company's financial ratios at March 31, 2017 were:

Ratio	Actual	Required
Funded debt to Bank EBITDA ratio	NM	3.5:1 Maximum
Debt service ratio	6.8:1	2.0:1 Minimum
Working capital ratio	2.7:1	1.25:1 Minimum

7. Provision for settlements

In 2016 Q2, the Company entered into a Settlement Agreement and Release (the "Settlement Agreement") in respect of two wage and hour lawsuits (the "Collective Actions") that were filed against the Company's wholly owned subsidiary, INC. The Collective Actions alleged that INC employed or contracted Measurement While Drilling ("MWD") and Directional Drilling ("DD") operators were entitled to recover unpaid or incorrectly calculated overtime wages under the Fair Labor Standards Act ("FLSA").

The Settlement Agreement resolved all claims from INC employed and contracted MWD and DD operators. Under the terms of the Settlement Agreement, the parties established an initial settlement fund of up to \$3,400 USD. The final determination of the settlement fund amount was based on the number of claimants that participated in the settlement at the end of December 2016, which under the terms of the Settlement Agreement is confidential. The settlement fund payments will be paid quarterly by the Company over a three-year period with the final payment due on or before September 2019. The quarterly payments may be accelerated in the event Cathedral meets certain financial targets over the payment period and can be deferred if a scheduled payment would put Cathedral in violation of its credit facility covenants subject to not more than three payments being deferred. Any FLSA settlement fund payments made by Cathedral exceeding \$200 USD are subject to the approval of Cathedral's banking syndicate.

In 2017 Q1, the Company entered into a confidential settlement agreement with one of its U.S. clients related to a down-hole drilling incident, which impacted two of their wells in December 2013. The settlement is payable based on an initial payment in 2017 Q1 and the remainder in quarterly installments concluding in 2021.

Any settlement fund payments made by Cathedral are subject to the approval of Cathedral's banking syndicate. During 2017 Q1, payments on both settlements of \$668 were made.

8. 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, 2016		Year ended December 31, 2015	
	Number	Amount	Number	Amount
Issued, beginning of period	36,295,380	\$ 74,481	36,295,380	\$ 74,481
Issued on bought deal and private placement	12,616,071	13,131	-	-
Issued on exercise of options	5,000	5	-	-
Issued, end of period	48,916,451	\$ 87,617	36,295,380	\$ 74,481

Issuance of common shares

5,000 common shares were issued as a result of the exercise of vested options arising from grants to employees in 2015. Options were exercised at an average strike price of \$0.75 per option. All issued shares are fully paid.

11,500,000 shares were issued on February 15, 2017 on a bought deal basis (the "Bought Deal") and concurrent with the Bought Deal, 1,116,071 shares were issued to certain directors and officers on an insider private placement basis. Shares were issued at \$1.12 per share. There were \$999

NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

in share issue costs that have been deducted against the gross proceeds of \$14,130.

Basic earnings per share

The calculation of basic earnings per share for the three months ended March 31, 2017 was based on the profit attributable to common shareholders of \$2,581 (2016 – \$9,683) and a weighted average number of common shares outstanding of 42,606,249 (2016 – 36,295,380); calculated as follows:

Weighted average number of ordinary shares

	Three months ended March 31,	
	2017	2016
Issued, beginning of period	36,295,380	36,295,380
Effect of bought deal and private placement	6,308,036	-
Effect of share options exercised	2,833	-
Weighted average number of common shares at end of period	42,606,249	36,295,380

Diluted earnings per share

The calculation of diluted earnings per share for the three months ended March 31, 2017 and 2016 was based on profit attributable to common shareholders of \$2,581 (2016 – \$9,683) and a weighted average number of common shares outstanding after adjustment for the effects of all dilutive potential common shares of 42,760,810 (2016 – 36,295,380) calculated as follows:

Weighted average number of common shares (diluted)

	Three months ended March 31,	
	2017	2016
Weighted average number of common shares (basic)	42,606,249	36,295,380
Effect of share options on issue	154,561	-
Weighted average number of common shares (diluted) at end of period	42,760,810	36,295,380

At March 31, 2017, 1,855,250 options (2016 – 1,781,832 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.

During the three months ended March 31, 2017, the Company granted 1,141,250 share options. The following table sets out the assumptions used in applying the Black-Scholes model for the options issued as well as the resulting fair value:

	2017 Q1
Number of options issued	1,141,250
Exercise price	\$ 1.13
Fair value per option (weighted average)	\$ 0.52
Expected annual dividend per share	\$ -
Risk-free interest rate (weighted average)	0.8%
Expected share price volatility (weighted average)	101.9%
Forfeiture rate per annum	10.0%

9. Gain on disposal of foreign subsidiary

During 2016 Q1, the Company completed the sale of its DPI foreign subsidiary for net proceeds of \$nil plus assumption of obligations of DPI which resulted in a non-cash gain on sale of \$10,865. DPI held the Company's investment in Venezuela and this sale completes Cathedral's exit from carrying on a business in Venezuela.

10. Commitments

In the normal course of business, the Company incurs contractual obligations and those obligations are disclosed in the Company's consolidated financial statements for the year ended December 31, 2016. As at March 31, 2017, the Company's commitment to purchase equipment is approximately \$810.

The Company has issued three standby letters of credit, two of which relate to property leases and renew annually to landlords. The first letter of credit is \$700 for the first ten years of the lease and then reduces to \$500 for the last five years of the lease. The second letter of credit is for \$542 USD and increases annually based upon annual changes in rent. The final letter of credit is for \$75 USD issued in relation to U.S. workers' compensation coverage.