TOURMALINE
OIL CORP.

# MANAGEMENT'S DISCUSSION AND ANALYSIS AND CONSOLIDATED FINANCIAL STATEMENTS

**FOR THE YEARS ENDED DECEMBER 31, 2018 AND DECEMBER 31, 2017**

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# MANAGEMENT’S DISCUSSION AND ANALYSIS

### For the years ended December 31, 2018 and December 31, 2017

This management’s discussion and analysis (“MD&A“) should be read in conjunction with Tourmaline Oil Corp.’s consolidated financial statements and related notes for the years ended December 31, 2018 and December 31, 2017. Both the consolidated financial statements and the MD&A can be found at www.sedar.com. This MD&A is dated March 5, 2019.

The financial information contained herein has been prepared in accordance with International Financial Reporting Standards (“IFRS”) and sometimes referred to in this MD&A as Generally Accepted Accounting Principles (“GAAP”) as issued by the International Accounting Standards Board (“IASB”).

All dollar amounts are expressed in Canadian currency, unless otherwise noted.

Certain financial measures referred to in this MD&A are not prescribed by IFRS. See “Non-GAAP Financial Measures” for information regarding the following non-GAAP financial measures used in this MD&A: “cash flow”, “operating netback”, “working capital (adjusted for the fair value of financial instruments)”, “net debt", “adjusted EBITDA”, “total debt” and “total capitalization”.

Additional information relating to Tourmaline can be found at www.sedar.com or at www.tourmalineoil.com.

Forward-Looking Statements - Certain information regarding Tourmaline set forth in this document, including management's assessment of the Company’s future plans and operations, contains forward-looking statements that involve substantial known and unknown risks and uncertainties. The use of any of the words "anticipate", "continue", "estimate", "expect", "may", "will", "project", "should", "believe" and similar expressions are intended to identify forward-looking statements. Such statements represent Tourmaline's internal projections, forecasts, estimates or beliefs concerning, among other things, an outlook on the estimated amounts and timing of capital investment or expenditures, anticipated future debt, expenses, production, cash flow and revenues or other expectations, beliefs, plans, objectives, assumptions, intentions or statements about future events or performance. These statements are only predictions and actual events or results may differ materially. Although Tourmaline believes that the expectations reflected in the forward-looking statements are reasonable, it cannot guarantee future results, levels of activity, performance or achievement since such expectations are inherently subject to significant business, economic, competitive, political and social uncertainties and contingencies.

In particular, forward-looking statements included in this MD&A include, but are not limited to, statements with respect to: the size of, and future net revenues and cash flow from, crude oil, condensate, NGL (natural gas liquids) and natural gas reserves; future prospects; the focus of and timing of capital expenditures; expectations regarding the ability to raise capital and to continually add reserves through acquisitions and development; access to debt and equity markets; projections of market prices and costs; the performance characteristics of the Company's crude oil, condensate, NGL and natural gas properties; crude oil, condensate, NGL and natural gas production levels and product mix; the payment of dividends and the timing and amount thereof; Tourmaline's future operating and financial results; capital investment programs; supply and demand for crude oil, condensate, NGL and natural gas; future royalty rates; drilling, development and completion plans and the results therefrom; future land expiries; dispositions and joint venture arrangements; amount of operating, transportation and general and administrative expenses; treatment under governmental regulatory regimes and tax and environmental laws and regulations; and estimated tax pool balances. In addition, statements relating to "reserves" are deemed to be forward-looking statements, as they involve the implied assessment, based on certain estimates and assumptions, that the reserves described can be profitably produced in the future.

These forward-looking statements are subject to numerous risks and uncertainties, most of which are beyond the Company's control, including the impact of general economic conditions; volatility and uncertainty in market prices for crude oil, condensate, NGL and natural gas; industry conditions; currency fluctuation; imprecision of reserve estimates; liabilities inherent in crude oil, condensate, NGL and natural gas operations; environmental, political, social and regulatory risks; incorrect assessments of the value of acquisitions and exploration and development programs; competition; the lack of availability of qualified personnel or management and skilled labour; changes in income tax and environmental laws and regulations and incentive programs relating to the oil and gas industry; hazards such as fire, explosion, blowouts, cratering, and spills, any of which could result in substantial damage to wells, production facilities, other property and the environment or in personal injury; stock market volatility; ability to access sufficient capital from internal and external sources; the receipt of applicable regulatory or third-party approvals; and the other risks considered under "Risk Factors" in Tourmaline's most recent annual information form available at www.sedar.com.

With respect to forward-looking statements contained in this MD&A, Tourmaline has made assumptions regarding: prevailing and future commodity prices and royalty regimes and tax laws; future well production rates and reserve volumes; availability of skilled labour; timing and amount of capital expenditures; future exchange rates; the impact of increasing competition; conditions in general economic and financial markets; availability of drilling and related equipment and services; effects of regulation by governmental agencies; future operating costs; decommissioning obligations; and ability to market crude oil, condensate, natural gas and NGL successfully. Without limitation of the foregoing, future dividend payments, if any, and the level thereof is uncertain, as the Company's dividend policy and the funds available for the payment of dividends from time to time will be dependent upon, among other things, cash flow, financial requirements for the Company's operations and the execution of its growth strategy, fluctuations in working capital and the timing and amount of capital expenditures, debt service requirements and other factors beyond the Company's control. Further, the ability of Tourmaline to pay dividends will be subject to applicable laws (including the satisfaction of the solvency test contained in applicable corporate legislation) and contractual restrictions contained in the instruments governing its indebtedness, including its credit facility.

Management has included the above summary of assumptions and risks related to forward-looking information provided in this MD&A in order to provide readers with a more complete perspective on Tourmaline's future operations and such information may not be appropriate for other purposes. Tourmaline's actual results, performance or achievement could differ materially from those expressed in, or implied by, these forward-looking statements and, accordingly, no assurance can be given that any of the events anticipated by the forward-looking statements will transpire or occur, or if any of them do so, what benefits, if any, that the Company will derive therefrom. Readers are cautioned that the foregoing lists of factors are not exhaustive.

These forward-looking statements are made as of the date of this MD&A and the Company disclaims any intent or obligation to update publicly any forward-looking statements, whether as a result of new information, future events or results or otherwise, other than as required by applicable securities laws.

Boe Conversions - Per barrel of oil equivalent amounts have been calculated using a conversion rate of six thousand cubic feet of natural gas to one barrel of oil equivalent (6:1). Barrel of oil equivalents (boe) may be misleading, particularly if used in isolation. A boe conversion ratio of 6 mcf:1 bbl is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. In addition, as the value ratio between natural gas and crude oil based on the current prices of natural gas and crude oil is significantly different from the energy equivalency of 6:1, utilizing a conversion on a 6:1 basis may be misleading as an indication of value.

## PRODUCTION

| | Three Months Ended December 31, | | | Years Ended December 31, | | |
|---|---|---|---|---|---|---|
| | **2018** | **2017** | **Change** | **2018** | **2017** | **Change** |
| Natural gas *(mcf/d)* | **1,347,778** | 1,306,935 | 3% | **1,305,025** | 1,221,529 | 7% |
| Crude oil *(bbl/d)* | **7,182** | 6,730 | 7% | **7,173** | 5,893 | 22% |
| Condensate (*bbl/d*) | **17,133** | 15,534 | 10% | **15,318** | 12,885 | 19% |
| NGL *(bbl/d)* | **27,623** | 23,222 | 19% | **25,049** | 19,959 | 26% |
| Oil equivalent *(boe/d)* | **276,568** | 263,309 | 5% | **265,044** | 242,325 | 9% |
| Natural gas % | **81%** | 83% | | **82%** | 84% | |

Production for the three months ended December 31, 2018 increased 5% up to an average of 276,568 boe/d compared to 263,309 boe/d for the same quarter of 2017. For the year ended December 31, 2018, average production increased 9% to 265,044 boe/d in 2018 from 242,325 boe/d for the same period of 2017. The full-year average production was within the 2018 published guidance of 265,000 – 270,000 boe/d.

The increase in production year over year can primarily be attributed to the Company's successful exploration and production ("E&P") program, which included 212.8 wells drilled (net). The growth in oil, condensate and NGL production is primarily the result of increased drilling in the Spirit River/Peace River High Charlie Lake oil plays, and strong condensate recoveries from new wells commencing production as the liquids-rich Montney Turbidite and Gundy areas are developed in northeast British Columbia.

Full-year average production guidance for 2019 remains at 300,000 boe/d as previously disclosed in the Company's November 7, 2018 press release.

## REVENUE AND REALIZED GAINS (LOSSES)

| | Three Months Ended December 31, | | | Years Ended December 31, | | |
|---|---|---|---|---|---|---|
| *(000s)* | **2018** | **2017** | **Change** | **2018** | **2017** | **Change** |
| Natural gas | | | | | | |
| Sales from production | **$ 237,685** | $ 227,539 | 4% | **$ 894,944** | $ 1,053,409 | (15)% |
| Realized gain on risk management activities | **172,714** | 92,722 | 86% | **418,217** | 226,500 | 85% |
| Realized gain (loss) on financial instruments | **(22,283)** | 4,672 | (577)% | **(13,259)** | 6,456 | (305)% |
| | **388,116** | 324,933 | 19% | **1,299,902** | 1,286,365 | 1% |
| Oil | | | | | | |
| Sales from production | **25,496** | 41,360 | (38)% | **167,910** | 125,563 | 34% |
| Realized gain on risk management activities | **5,171** | 453 | 1,042% | **10,480** | 1,786 | 487% |
| Realized gain (loss) on financial instruments | **31,828** | (2,015) | 1,680% | **(17,523)** | 1,517 | (1,255)% |
| | **62,495** | 39,798 | 57% | **160,867** | 128,866 | 25% |
| Condensate | | | | | | |
| Sales from production | **85,525** | 103,915 | (18)% | **413,770** | 303,469 | 36% |
| Realized gain on risk management activities | **1,267** | – | 100% | **1,737** | – | 100% |
| | **86,792** | 103,915 | (16)% | **415,507** | 303,469 | 37% |
| NGL | | | | | | |
| Sales from production | **58,084** | 58,460 | (1)% | **229,933** | 164,911 | 39% |
| Total | | | | | | |
| Sales from production | **406,790** | 431,274 | (6)% | **1,706,557** | 1,647,352 | 4% |
| Realized gain on risk management activities | **179,152** | 93,175 | 92% | **430,434** | 228,286 | 89% |
| Realized gain (loss) on financial instruments | **9,545** | 2,657 | 259% | **(30,782)** | 7,973 | (486)% |
| Total revenue from commodity sales and realized gains (losses) on risk management activities and financial instruments | **$ 595,487** | $ 527,106 | 13% | **$ 2,106,209** | $ 1,883,611 | 12% |

Total sales from production for the three months ended December 31, 2018 decreased 6% to $406.8 million from $431.3 million for the same quarter of 2017. The decrease is due to the significant decline in oil benchmark prices during the fourth quarter of 2018 which was partially offset by the increase in production for the quarter. Sales from production for the year ended December 31, 2018 increased 4% to $1,706.6 million from $1,647.4 million in 2017. The increase reflects higher oil, condensate and NGL revenue from increased production volumes which was partially offset by lower natural gas revenue due to the decline in Canadian benchmark natural gas prices in 2018 compared to 2017.

The fourth quarter of 2018 included a gain on risk management activities of $179.2 million (for the year ended December 31, 2018 - $430.4 million) compared to a gain of $93.2 million for the same period of the prior year (for the year ended December 31, 2017 – gain of $228.3 million). Included in realized gains on risk management activities are all the premiums that Tourmaline receives from selling gas to markets outside Alberta and British Columbia and the premium on physical commodity contract prices compared to benchmark pricing. Since the third quarter of 2016, Tourmaline has significantly diversified the markets where its natural gas is sold. These markets include Malin, PG&E City Gate, Chicago, and as of the fourth quarter of 2017, Dawn, Ontario, all of which during the quarter had higher natural gas prices compared to AECO. As a result, the Company's realized gains on risk management activities for natural gas have increased significantly due to this market diversification strategy.

Total revenue from commodity sales and realized gains for the three and twelve month periods ending December 31, 2018 is higher due to the significant increase in oil, condensate and NGL production combined with generally higher realized prices when compared to the same periods of 2017. Total revenue from commodity sales and realized gains excludes the effect of unrealized gains or losses on commodity contracts until these gains and losses are realized.

**BENCHMARK OIL AND GAS PRICES:**

| | Three Months Ended December 31, | | | Years Ended December 31, | | |
|---|---|---|---|---|---|---|
| | **2018** | **2017** | **Change** | **2018** | **2017** | **Change** |
| Natural gas | | | | | | |
| NYMEX Last Day *(USD$/mcf)* | **$ 3.64** | $ 2.93 | 24% | **$ 3.09** | $ 3.11 | (1)% |
| AECO 5A *(CAD$/mcf)* | **$ 1.57** | $ 1.70 | (8)% | **$ 1.51** | $ 2.17 | (30)% |
| West Coast Station 2 (*CAD$/mcf*) | **$ 0.63** | $ 0.54 | 17% | **$ 1.18** | $ 1.48 | (20)% |
| Sumas (*USD$/mmbtu*) | **$ 7.88** | $ 2.67 | 195% | **$ 3.52** | $ 2.62 | 34% |
| ATP 5A Day Ahead (*CAD$/mcf*) | **$ 2.76** | $ 1.26 | 119% | **$ 2.20** | $ 2.14 | 3% |
| Chicago City Gate (*USD$/mmbtu*) | **$ 3.68** | $ 2.86 | 29% | **$ 3.02** | $ 2.90 | 4% |
| Ventura (*USD$/mmbtu*) | **$ 3.63** | $ 4.85 | (25)% | **$ 2.96** | $ 3.32 | (11)% |
| PG&E Malin (*USD$/mmbtu*) | **$ 4.10** | $ 2.67 | 54% | **$ 2.76** | $ 2.73 | 1% |
| PG&E City Gate (*USD$/mmbtu*) | **$ 4.59** | $ 3.06 | 50% | **$ 3.35** | $ 3.23 | 4% |
| Dawn (*USD$/mmbtu*) | **$ 3.79** | $ 2.93 | 29% | **$ 3.12** | $ 3.04 | 3% |
| Oil and condensate | | | | | | |
| NYMEX *(USD$/bbl)* | **$ 59.34** | $ 55.30 | 7% | **$ 64.90** | $ 50.85 | 28% |
| Edmonton Par *(CAD$/bbl)* | **$ 48.07** | $ 66.68 | (28)% | **$ 69.14** | $ 62.49 | 11% |
| Edmonton Condensate (*CAD$/bbl*) | **$ 64.94** | $ 73.61 | (12)% | **$ 79.45** | $ 67.07 | 18% |

**CURRENCY – EXCHANGE RATES:**

| | Three Months Ended December 31, | | | Years Ended December 31, | | |
|---|---|---|---|---|---|---|
| | **2018** | **2017** | **Change** | **2018** | **2017** | **Change** |
| CAD/USD$ (1) | **$ 0.7567** | $ 0.7870 | (4)% | **$ 0.7719** | $ 0.7711 | –% |

*(1) Average rates for the period.*

**TOURMALINE REALIZED PRICES [(1)]:**

| | Three Months Ended December 31, | | | Years Ended December 31, | | |
|---|---|---|---|---|---|---|
| | **2018** | **2017** | **Change** | **2018** | **2017** | **Change** |
| Natural gas *($/mcf)* | **$ 3.13** | $ 2.70 | 16% | **$ 2.73** | $ 2.89 | (6)% |
| Oil *($/bbl)* | **$ 94.58** | $ 64.28 | 47% | **$ 61.44** | $ 59.91 | 3% |
| Condensate (*$/bbl*) | **$ 55.06** | $ 72.71 | (24)% | **$ 74.32** | $ 64.53 | 15% |
| NGL *($/bbl)* | **$ 22.86** | $ 27.36 | (16)% | **$ 25.15** | $ 22.64 | 11% |
| Oil equivalent *($/boe)* | **$ 23.40** | $ 21.76 | 8% | **$ 21.77** | $ 21.30 | 2% |

*(1) Realized prices include sales from production, realized gain on risk management activities and realized gain (loss) on financial instruments.*

The realized average natural gas price for the three months ended December 31, 2018 was $3.13/mcf, which is 16% higher than the same period of the prior year. The increase reflects higher natural gas benchmark prices, outside of AECO, in the quarter and higher realized gains on risk management activities. For the year ended December 31, 2018, the realized natural gas price was $2.73/mcf, or 6% lower than the same period of the prior year. The lower natural gas price reflects the significant decrease in Canadian benchmark natural gas index prices experienced during the year, which was partially offset by higher realized gains on risk management activities as the Company continues to diversify sales markets.

Realized oil prices increased by 47% for the three months ended December 31, 2018. The realized price for the fourth quarter of 2018 included a realized gain on financial instruments of $31.8 million compared to a loss of $2.0 million on financial contracts in the fourth quarter of 2017. The realized gain in the fourth quarter of 2018 was the result of the unwinding of a proportion of the Company's financial oil contracts to take advantage of the significant gain that had been realized. Since unwinding these positions, forward crude oil prices have recovered and Tourmaline has systematically entered into hedges to protect future oil cash flows. For the twelve months ended December 31, 2018, the realized oil price increased by 3% compared to the prior year. The increase is related to the higher benchmark prices experienced during the year and was partially offset by realized losses on financial instruments during the first three quarters of the year.

For the three months ended December 31, 2018, the realized price of condensate was $55.06/bbl which is 24% lower than the same period of the prior year. The decrease is due to the decline in benchmark prices experienced during the fourth quarter of 2018. For the year ended December 31, 2018, the realized price of condensate increased by 15% to $74.32/bbl compared to the prior year which is consistent with the increase in the benchmark price for condensate during the year.

NGL prices for the fourth quarter of 2018 decreased 16% from $27.36/bbl to $22.86/bbl, when compared to the same quarter of 2017. For the year ended December 31, 2018, the realized NGL price increased 11% from $22.64/bbl to $25.15/bbl when compared to the prior year. The increase in NGL pricing is consistent with the higher benchmark oil price for the year ended December 31, 2018.

## ROYALTIES

| | Three Months Ended December 31, | | Years Ended December 31, | |
|---|---|---|---|---|
| *(000s)* | **2018** | **2017** | **2018** | **2017** |
| Natural gas | **$ (2,416)** | $ 3,020 | **$ (3,431)** | $ 26,041 |
| Oil, condensate and NGL | **17,796** | 18,093 | **80,800** | 54,597 |
| Total royalties | **$ 15,380** | $ 21,113 | **$ 77,369** | $ 80,638 |
| Royalties as a percentage of commodity sales | **3.8%** | 4.9% | **4.5%** | 4.9% |

For the quarter ended December 31, 2018, the average effective royalty rate decreased to 3.8% from 4.9% in the fourth quarter of 2017. For the year ended December 31, 2018, the average effective royalty rate decreased to 4.5% from 4.9% in the prior year. The decrease in the royalty rate in both periods is primarily due to lower natural gas royalties as Canadian natural gas index prices were lower in 2018 compared to 2017. Natural gas crown royalties in 2018 were $62.0 million down from $138.3 million in 2017 reflecting the significant natural gas price decline. Crown royalties are offset by gas cost allowance ("GCA") received from the Crown, to account for expenses incurred to process and transport the Crown's portion of natural gas production. In 2018, Tourmaline received $39.8 million in GCA which is a 5% increase over the $38.0 million received in 2017. This increase is consistent with the increase in natural gas production over the year. Also offsetting natural gas crown royalties are credits for the New Well Royalty Reduction Program and the Natural Gas Deep Drilling Program in Alberta, as well as the Deep Royalty Credit Program in British Columbia.

On January 1, 2017, the Company adopted the Modernized Royalty Framework (the "MRF") introduced by the Alberta Government in 2016. This new royalty regime is applicable to all new wells drilled beginning January 1, 2017, and all other wells drilled prior to January 1, 2017 will follow the old framework for a further 10 years. The Company believes that the MRF is generally consistent with the initial goal of incentivizing the use of technology to improve productivity and rewards producers deploying the most competitive operating practices. Under the MRF, if commodity prices stay consistent, the Company anticipates an increase in the corporate royalty rate but based on the Company's current development plans and operational practices, the increase is not expected to be significant.

The Company expects its royalty rate for 2019 to be approximately 5%. The small increase over the 2018 effective royalty rate is expected due to higher forecast commodity prices in 2019. The royalty rate is sensitive to commodity prices, and as such, an increase in commodity prices will increase the actual rate.

## COMMODITY MARKETING

| | Three Months Ended December 31, | | | Years Ended December 31, | | |
|---|---|---|---|---|---|---|
| *(000s)* | **2018** | **2017** | **Change** | **2018** | **2017** | **Change** |
| Marketing revenue | **$ 5,563** | $ 9,969 | (44)% | **$ 24,670** | $ 14,232 | 73% |
| Marketing purchases | **(5,153)** | (8,661) | (41)% | **(23,497)** | (13,348) | 76% |
| | **$ 410** | $ 1,308 | (69)% | **$ 1,173** | $ 884 | 33% |

During the second quarter of 2017, the Company commissioned the Mulligan marketing terminal in the Gordondale area of Alberta. The throughput from the marketing terminal is comprised of Tourmaline produced oil and NGL volumes as well as oil and NGL volumes purchased from third parties. The revenue and purchases from third parties, which have grown significantly in 2018, are recorded gross for financial statement presentation purposes. Any gains or losses on the sale of third-party product related to the price differential are recorded in marketing revenue.

For the three months ended December 31, 2018, marketing revenue and marketing purchases decreased 44% and 41%, respectively, compared to the three months ended December 31, 2017. This decrease can be attributed to the decline in the price of oil in the fourth quarter of 2018.

## OTHER INCOME

| | Three Months Ended December 31, | | | Years Ended December 31, | | |
|---|---|---|---|---|---|---|
| *(000s)* | **2018** | **2017** | **Change** | **2018** | **2017** | **Change** |
| Other income | **$ 7,644** | $ 13,729 | (44)% | **$ 34,176** | $ 35,342 | (3)% |

Other income decreased from $13.7 million in the fourth quarter of 2017 to $7.6 million for the same quarter of 2018. For the year ended December 31, 2018, other income decreased from $35.3 million in 2017 to $34.2 million in 2018. The decrease in other income in the fourth quarter of 2018 is due to a decrease in water disposal income as well as a decrease in processing income which is the result of Tourmaline increasing its production and displacing third party production at Company-owned processing facilities.

## OPERATING EXPENSES

| | Three Months Ended December 31, | | | Years Ended December 31, | | |
|---|---|---|---|---|---|---|
| *(000s) except per-unit amounts* | **2018** | **2017** | **Change** | **2018** | **2017** | **Change** |
| Operating expenses | **$ 85,185** | $ 74,644 | 14% | **$ 322,387** | $ 282,494 | 14% |
| Per boe | **$ 3.35** | $ 3.08 | 9% | **$ 3.33** | $ 3.19 | 4% |

Operating expenses include all periodic lease and field-level expenses and excludes income recoveries from processing third-party volumes. For the fourth quarter of 2018, total operating expenses were $85.2 million compared to $74.6 million in 2017, an increase of 14% over a production base increase of 5% for the same period. Operating costs for the year ended December 31, 2018 were $322.4 million, compared to $282.5 million for the same period of 2017, reflecting a 14% increase in total costs over a 9% increase in production.

On a per-boe basis, the costs increased from $3.08/boe for the fourth quarter of 2017 to $3.35/boe in the fourth quarter of 2018. For the year ended December 31, 2018, operating costs were $3.33/boe, up from $3.19/boe in the prior year. The increase in per-boe costs is related to the significant increase in oil, condensate and NGL production which have higher associated operating costs per-boe.

The Company's operating costs for 2019 are forecast to average approximately $3.45/boe. The slight increase over 2018 per-boe costs takes into consideration higher anticipated property taxes and operating expenses attributable to a continuously increasing liquids portfolio, which carry higher operating costs. Actual cash costs can change, however, depending on a number of factors, including the Company's actual production levels.

## TRANSPORTATION

| | Three Months Ended December 31, | | | Years Ended December 31, | | |
|---|---|---|---|---|---|---|
| *(000s) except per unit amounts* | **2018** | **2017** | **Change** | **2018** | **2017** | **Change** |
| Natural gas transportation | **$ 68,413** | $ 52,897 | 29% | **$ 251,596** | $ 191,296 | 32% |
| Oil and NGL transportation | **23,833** | 20,028 | 19% | **88,775** | 67,877 | 31% |
| Total transportation | **$ 92,246** | $ 72,925 | 26% | **$ 340,371** | $ 259,173 | 31% |
| Per boe | **$ 3.63** | $ 3.01 | 21% | **$ 3.52** | $ 2.93 | 20% |

Transportation costs for the three months ended December 31, 2018 were $92.2 million, compared to $72.9 million for the same period of 2017. Transportation costs for the year ended December 31, 2018 were $340.4 million, compared to $259.2 million for the same period of 2017. Both periods reflect increased costs related to higher production volumes as well as an increased diversification of sales points.

On a per-boe basis, the costs increased to $3.63/boe for the fourth quarter of 2018 (year ended December 31, 2018 - $3.52/boe) from $3.01/boe in the fourth quarter of 2017 (year ended December 31, 2017 - $2.93/boe). The increase in per-unit costs in 2018 reflects an increased focus on diversifying markets where Tourmaline sells its natural gas and receives a premium to AECO. In the fourth quarter of 2017, Tourmaline began selling natural gas at Dawn, Ontario, further diversifying its sales markets. At Dawn, the Company received a higher price for its natural gas when compared to the AECO benchmark price. Also, in the second quarter of 2018, Tourmaline added an additional 100 mmcf/d of transportation capacity to access the Malin and PG&E markets. The increased proportion of natural gas sold outside Alberta and the increased distance transported resulted in higher per-boe fuel and transportation costs.

## GENERAL & ADMINISTRATIVE EXPENSES ("G&A")

| | Three Months Ended December 31, | | | Years Ended December 31, | | |
|---|---|---|---|---|---|---|
| *(000s) except per-unit amounts* | **2018** | **2017** | **Change** | **2018** | **2017** | **Change** |
| G&A expenses | **$ 19,864** | $ 21,383 | (7)% | **$ 84,071** | $ 74,571 | 13% |
| Administrative and capital recovery | **(2,479)** | (2,886) | (14)% | **(9,410)** | (8,353) | 13% |
| Capitalized G&A | **(6,619)** | (7,847) | (16)% | **(27,321)** | (25,608) | 7% |
| Total G&A expenses | **$ 10,766** | $ 10,650 | 1% | **$ 47,340** | $ 40,610 | 17% |
| Per boe | **$ 0.42** | $ 0.44 | (5)% | **$ 0.49** | $ 0.46 | 7% |

Total G&A expenses for the fourth quarter of 2018 were $10.8 million compared to $10.7 million for the same quarter of the prior year. On a per-boe basis, G&A expenses for the three months ended December 31, 2018 decreased to $0.42/boe from $0.44/boe reflecting the higher production in the fourth quarter of 2018.

For the year ended December 31, 2018, G&A expenses were $47.3 million compared to $40.6 million for the same period in 2017. For the year ended December 31, 2018, G&A expenses per-boe increased to $0.49/boe compared to $0.46/boe in 2017. The increase in total G&A expenses and the per-boe expense is primarily due to staff additions to manage the larger production, reserve and land base as well as higher third-party service provider fees and increased industry marketing initiatives.

G&A expenses for 2019 are expected to average approximately $0.45/boe with the higher forecast production. Actual costs per boe can change, however, depending on a number of factors including the Company's actual production levels.

## SHARE-BASED PAYMENTS

| | Three Months Ended December 31, | | Years Ended December 31, | |
|---|---|---|---|---|
| *(000s)* | **2018** | **2017** | **2018** | **2017** |
| Share-based payments | **$ 8,484** | $ 8,840 | **$ 31,578** | $ 38,262 |
| Capitalized share-based payments | **(3,589)** | (4,420) | **(13,349)** | (19,131) |
| Total share-based payments | **$ 4,895** | $ 4,420 | **$ 18,229** | $ 19,131 |

The Company uses the fair-value method for the determination of non-cash related share-based payments expense. During the fourth quarter of 2018, 127,000 stock options were granted to employees, officers and directors at a weighted-average exercise price of $19.14.

The Company recognized $4.9 million of share-based payment expense in the fourth quarter of 2018 compared to $4.4 million in the fourth quarter of 2017. Capitalized share-based payments for the fourth quarter of 2018 were $3.6 million compared to $4.4 million for the same quarter of the prior year.

For the year ended December 31, 2018, share-based payment expense totalled $18.2 million and a further $13.3 million in share-based payments were capitalized (for the year ended December 31, 2017 - $19.1 million and $19.1 million, respectively).

Share-based payments are lower in 2018 compared to 2017 which reflects options with a lower fair value being expensed in 2018 compared to 2017.

## DEPLETION, DEPRECIATION AND AMORTIZATION ("DD&A")

| | Three Months Ended December 31, | | Years Ended December 31, | |
|---|---|---|---|---|
| *(000s) except per unit amounts* | **2018** | **2017** | **2018** | **2017** |
| Total depletion, depreciation and amortization | **$ 212,037** | $ 202,726 | **$ 798,666** | $ 774,258 |
| Less mineral lease expiries | **(20,774)** | (15,467) | **(52,798)** | (36,615) |
| Depletion, depreciation and amortization | **$ 191,263** | $ 187,259 | **$ 745,868** | $ 737,643 |
| Per boe | **$ 7.52** | $ 7.73 | **$ 7.71** | $ 8.34 |

DD&A expense was $191.3 million for the fourth quarter of 2018 compared to $187.3 million for the same period of 2017. The per-unit DD&A rate for the fourth quarter of 2018 was $7.52/boe compared to $7.73/boe for the same quarter of 2017.

For the year ended December 31, 2018, DD&A expense was $745.9 million (year ended December 31, 2017 - $737.6 million) with a DD&A rate of $7.71/boe (year ended December 31, 2017 - $8.34/boe). The decrease in per-boe depletion in 2018 over the same periods of 2017 can be attributed to lower future development costs per well, thereby adding a higher proportion of reserves with lower associated future development costs, resulting in a lower depletion rate.

Mineral lease expiries for the three months and year ended December 31, 2018 were $20.8 million and $52.8 million, respectively (December 31, 2017 – $15.5 million and $36.6 million, respectively). The Company prioritizes drilling on what it believes to be the most cost-efficient and productive acreage, and with such a large land base, the Company has chosen to not continue some of the expiring sections of land. Tourmaline expects to continue to see mineral lease expiries of a similar magnitude on a go-forward basis but attempts to mitigate all expiries through land swaps, asset dispositions or drilling to maintain the lease.

## FINANCE EXPENSES

| | Three Months Ended December 31, | | | Years Ended December 31, | | |
|---|---|---|---|---|---|---|
| *(000s)* | **2018** | **2017** | **Change** | **2018** | **2017** | **Change** |
| Interest on loans and borrowings | **$ 14,347** | $ 12,550 | 14% | **$ 51,722** | $ 44,286 | 17% |
| Capitalized borrowing costs | **(2,816)** | – | 100% | **(2,816)** | – | 100% |
| Accretion expense | **1,481** | 1,505 | (2)% | **5,613** | 5,334 | 5% |
| Foreign exchange (gain) loss on U.S. denominated debt | **88,692** | 2,342 | 3,687% | **143,250** | (82,746) | 273% |
| Realized (gain) loss on cross-currency swaps | **(88,692)** | (2,342) | (3,687)% | **(143,250)** | 82,746 | (273)% |
| Realized loss on interest rate swaps | **789** | 427 | 85% | **2,495** | 2,975 | (16)% |
| Transaction costs on property acquisitions | **–** | – | –% | **75** | 133 | (44)% |
| Total finance expenses | **$ 13,801** | $ 14,482 | (5)% | **$ 57,089** | $ 52,728 | 8% |

Finance expenses for the three months ended December 31, 2018 totaled $13.8 million compared to $14.5 million for the same period of 2017. The average bank debt outstanding and the average effective interest rate on the debt was $1,538.3 million and 3.32% for the three months ended December 31, 2018 compared to $1,597.6 million and 2.82% for the same period of 2017.

For the year ended December 31, 2018, finance expenses totaled $57.1 million compared to $52.7 million for the same period of 2017. The average bank debt outstanding and the average effective interest rate on the debt for the year ended December 31, 2018 was $1,516.1 million and 3.03% compared to $1,554.5 million and 2.52% for the same period of 2017, respectively.

The increase in the effective interest rate for the three and twelve months ended December 31, 2018 compared to the same periods in 2017 reflects the increase in the Bank of Canada prime rate over the same periods resulting in an increase in interest expense. In the fourth quarter of 2018, the Company recorded $2.8 million in capitalized borrowing costs related to long-term capital projects which lowered finance expense for the three months ended December 31, 2018 compared to the same period of the prior year.

For the year ended December 31, 2018, the Company drew from the credit facility in U.S. dollars, as permitted under the credit facility, which when repaid created a foreign exchange loss due to the weakening of the Canadian dollar over the same period. Concurrent with the draw of U.S. dollar denominated borrowings, the Company entered into cross-currency swaps to manage the foreign currency risk resulting from holding U.S. dollar denominated borrowings. This transaction allows the Company to take advantage of the interest rate spread between CDOR and LIBOR without taking on foreign exchange risk.

## DEFERRED INCOME TAXES

For the three months ended December 31, 2018, the provision for deferred income tax expense was $74.8 million compared to $41.9 million for the same period in 2017. The increase is primarily due to higher pre-tax earnings recorded in the fourth quarter of 2018 compared to the respective period in 2017.

For the year ended December 31, 2018, the provision for deferred income tax expense was $165.4 million compared to a deferred income tax expense of $151.8 million for the same period in 2017. The increase is due to the income before taxes of $567.1 million for the year ended December 31, 2018 compared to the income before taxes of $498.8 million for the year ended December 31, 2017.

## CASH FLOW FROM OPERATING ACTIVITIES, CASH FLOW AND NET EARNINGS

| | Three Months Ended December 31, | | | Years Ended December 31, | | |
|---|---|---|---|---|---|---|
| *(000s) except per unit amounts* | **2018** | **2017** | **Change** | **2018** | **2017** | **Change** |
| Cash flow from operating activities | **$ 329,997** | $ 299,793 | 10% | **$ 1,269,491** | $ 1,182,900 | 7% |
| Per share [(1)] | **$ 1.21** | $ 1.11 | 9% | **$ 4.67** | $ 4.39 | 6% |
| Cash flow [(2)] | **$ 391,532** | $ 348,227 | 12% | **$ 1,303,462** | $ 1,205,758 | 8% |
| Per share [(1)(2)] | **$ 1.44** | $ 1.29 | 12% | **$ 4.80** | $ 4.47 | 7% |
| Net earnings | **$ 190,895** | $ 88,079 | 117% | **$ 401,418** | $ 346,773 | 16% |
| Per share [(1)] | **$ 0.70** | $ 0.33 | 112% | **$ 1.48** | $ 1.29 | 15% |
| Operating netback per boe [(2)] | **$ 15.82** | $ 14.80 | 7% | **$ 14.12** | $ 14.27 | (1)% |

*(1) Per share amounts have been calculated using the weighted average number of diluted common shares.*

*(2) See "Non-GAAP Financial Measures".*

Cash flow for the three months ended December 31, 2018 was $391.5 million or $1.44 per diluted share compared to $348.2 million or $1.29 per diluted share for the same period of 2017. For the year ended December 31, 2018, cash flow was $1,303.5 million or $4.80 per diluted share, compared to $1,205.8 million or $4.47 per diluted share in the prior year.

The Company had after-tax net earnings for the three months ended December 31, 2018 of $190.9 million or $0.70 per diluted share compared to after-tax net earnings of $88.1 million or $0.33 per diluted share for the same period of 2017. For the year ended December 31, 2018, the after-tax net earnings were $401.4 million or $1.48 per share compared to after-tax net earnings of $346.8 million or $1.29 per share for the year ended December 31, 2017. The increase in both cash flow and after-tax net earnings for full year 2018 reflects higher realized oil, condensate and NGL prices and an increase in production over full year 2017. Realized gains on divestitures in 2018 of $65.5 million also contributed to the higher net earnings compared to realized gains on divestitures in 2017 of $22.7 million.

## CAPITAL EXPENDITURES

| | Three Months Ended December 31, | | Years Ended December 31, | |
|---|---|---|---|---|
| *(000s)* | **2018** | **2017** | **2018** | **2017** |
| Land and seismic | **$ 1,915** | $ 4,326 | **$ 16,068** | $ 34,000 |
| Drilling and completions | **237,594** | 234,747 | **784,862** | 898,579 |
| Facilities | **123,717** | 85,311 | **428,841** | 404,133 |
| Property acquisitions | **23,143** | 20,136 | **24,953** | 47,486 |
| Property dispositions | **(942)** | (595) | **(72,176)** | (4,595) |
| Other | **9,767** | 8,308 | **31,889** | 27,013 |
| Total cash capital expenditures | **$ 395,194** | $ 352,233 | **$ 1,214,437** | $ 1,406,616 |

The 2018 fourth quarter E&P expenditures were $363.2 million compared to $324.4 million for the same quarter of 2017. Total capital invested for the fourth quarter of 2018 was $395.2 million (net of $0.9 million in dispositions) compared to $352.2 million (net of dispositions) for the same period of 2017.

During 2018, the Company invested $1,214.4 million of cash consideration (net of dispositions), compared to $1,406.6 million (net of dispositions) in 2017. Expenditures on E&P were $1,229.8 million in 2018 compared to $1,336.7 million for 2017. The drilling and completions costs of $784.9 million in 2018 include 40.2 fewer net wells drilled and 50.8 fewer net wells completed when compared to 2017.

Facilities expenditures in 2018 include construction costs for the Doe Sour Gas Plant commissioned in September 2018. Other costs incurred were associated with the Gundy Deep Cut Gas Plant, expected to be commissioned in June 2019 as well as costs related to the Edson Gas Plant expansion.

The following table summarizes the drill, complete and tie-in activities for the periods:

| | **Year Ended December 31, 2018** | | **Year Ended December 31, 2017** | |
|---|---|---|---|---|
| | **Gross** | **Net** | **Gross** | **Net** |
| Drilled | **241.00** | **212.78** | 290.00 | 252.97 |
| Completed | **237.00** | **207.91** | 292.00 | 258.70 |
| Tied-in | **228.00** | **204.95** | 287.00 | 255.90 |

E&P capital expenditures in 2019 are forecast to be $1.2 billion. The Company expects drilling and completions costs of approximately $880.0 million, facilities expenditures (including equipment, pipelines, tie-ins and major facilities) of $340.0 million, as well as, land and seismic expenditures of $5.0 million. The capital budget is closely monitored and will continue to be adjusted as required depending on cash flow available.

**Acquisitions and Dispositions**

2018

On February 28, 2018, the Company completed the sale of a number of non-core undeveloped assets across all three cash-generating units ("CGUs") for proceeds of approximately $71.2 million, before customary closing adjustments.

On October 17, 2018, the Company acquired assets in the Peace River High area for total cash consideration of $21.2 million for producing properties, land and reserves.

2017

On July 20, 2017, the Company completed an asset swap in NEBC allowing for the consolidation in the Sundown complex. The Company exchanged predominantly Exploration and Evaluation ("E&E") assets and cash consideration of $19.0 million for producing properties, land and reserves.

## LIQUIDITY AND CAPITAL RESOURCES

On May 15, 2018, the Company issued 1,000,000 flow-through common shares at a price of $30.00 per share, for total consideration of $30.0 million. The proceeds were used to temporarily reduce bank debt and then to fund the Company's 2018 exploration program.

On December 5, 2017, the Company issued 1,300,000 flow-through common shares at a price of $31.20 per share, for total consideration of $40.6 million. The proceeds were used to temporarily reduce bank debt and fund the Company's exploration and development program.

The Company has a covenant-based, unsecured, five-year extendible revolving credit facility in place with a syndicate of banks, in the amount of $1.8 billion with a maturity date of June 2023. The maturity date may, at the request of the Company and with consent of the lenders, be extended on an annual basis. The revolving credit facility includes an expansion feature ("accordion") which allows the Company, upon approval from the lenders, to increase the facility amount by up to $500.0 million by adding a new financial institution or by increasing the commitment of its existing lenders. The revolving credit facility can be drawn in either Canadian or U.S. funds and bears interest at the agent bank's prime lending rate, banker's acceptance rates or LIBOR (for U.S. borrowings), plus applicable margins.

Under the terms of the revolving credit facility, Tourmaline has provided its covenant that, on a rolling four-quarter basis: (i) the ratio of adjusted EBITDA to interest expense must exceed 3:1, and (ii) the ratio of total debt to total capitalization must not exceed 0.6:1. At December 31, 2018, adjusted EBITDA for the purposes of the above noted covenant calculations was $1,359.9 million (December 31, 2017 - $1,252.4 million), on a rolling four-quarter basis.

The Company has a $950.0 million term loan with a syndicate of banks. The term loan can be drawn in either Canadian or U.S. funds and bears interest at the agent bank's prime lending rate, banker's acceptance rates or LIBOR (for U.S. borrowings), plus 157.5 basis points with a maturity date of June 2023. The maturity date may, at the request of the Company and with consent of the lenders, be extended on an annual basis. The covenants for the term loan are the same as those under the Company's current credit facility and the term loan ranks equally with the obligation under the Company's credit facility.

The Company also has a covenant based, unsecured, operating credit facility with a Canadian bank in the amount of $50.0 million. The operating credit facility has a maturity date of June 2019, which may, at the request of the Company and with consent of the lender, be extended on an annual basis. The covenants are the same as the revolving credit facility.

In addition, the Company has a letter of credit facility payable on demand in the amount of $50.0 million with a Canadian bank. Tourmaline has outstanding letters of credit in the amount of $9.5 million (December 31, 2017 - $17.6 million), which reduce the credit available on the facility.

The Company's aggregate borrowing capacity is $2.85 billion at December 31, 2018. As at, and for the years ending December 31, 2018 and December 31, 2017, the Company is in compliance with all debt covenants.

As at December 31, 2018, the Company had negative working capital of $242.0 million, after adjusting for the fair value of financial instruments (the unadjusted working capital deficiency was $228.4 million) (December 31, 2017 – $202.5 million and $219.2 million, respectively). As at December 31, 2018, the Company had $947.8 million in long-term debt outstanding and $528.3 million drawn against the revolving credit facility for total bank debt of $1,476.1 million (net of prepaid interest and debt issue costs) (December 31, 2017 - $1,534.8 million). Net debt at December 31, 2018 was $1,718.1 million (December 31, 2017 - $1,737.2 million). As at December 31, 2018, the Company also has $1,364.4 million in unutilized borrowing capacity.

For 2019, management intends to continue to diligently monitor and adjust the capital budget based on expected cash flow and as such management believes the Company has sufficient resources to fund its 2019 exploration and development program. Management is dedicated to keeping a strong balance sheet, which has proven to be very important, especially in times of depressed commodity prices.

On December 30, 2018, the Company paid a quarterly cash dividend of $27.3 million ($0.10 per share). Total dividends paid for 2018 were $100.6 million ($0.37 per share) (2017 – nil).

## SHARES AND STOCK OPTIONS OUTSTANDING

As at March 5, 2019, the Company has 272,042,659 common shares outstanding and 20,305,667 stock options granted and outstanding.

## COMMITMENTS AND CONTRACTUAL OBLIGATIONS

In the normal course of business, Tourmaline is obligated to make future payments. These obligations represent contracts and other commitments that are known and non-cancellable.

| *(000s)* | **1 Year** | **2-3 Years** | **4-5 Years** | **>5 Years** | **Total** |
|---|---|---|---|---|---|
| Operating leases | $ 5,937 | $ 8,212 | $ 6,932 | $ 10,705 | $ 31,786 |
| Firm transportation and processing agreements | 387,110 | 816,230 | 674,861 | 1,869,830 | 3,748,031 |
| Capital commitments (1) | 124,447 | 540,288 | 9,292 | 79,015 | 753,042 |
| Revolving credit facility (2) | – | – | 629,271 | – | 629,271 |
| Term debt (3) | 36,599 | 73,197 | 1,001,942 | – | 1,111,738 |
| | $ 554,093 | $ 1,437,927 | $ 2,322,298 | $ 1,959,550 | $ 6,273,868 |

*(1) Includes drilling commitments, power commitments, and capital spending commitments under the joint arrangement in the Spirit River complex of $300.0 million per year until at least 2020. The capital spending commitment can be deferred to future periods in the event of an economic downturn, and as agreed upon by both parties. In 2018, an economic downturn event, as defined in the joint arrangement in the Spirit River complex had occurred resulting in capital spending being deferred to future periods.*

*(2) Includes interest expense at an annual rate of 3.76% being the rate applicable to outstanding debt on the credit facility at December 31, 2018.*

*(3) Includes interest expense at an annual rate of 3.86% being the applicable rate on the term debt at December 31, 2018.*

## OFF BALANCE SHEET ARRANGEMENTS

The Company has certain lease arrangements, all of which are reflected in the commitments and contractual obligations table, which were entered into in the normal course of operations. All leases are treated as operating leases whereby the lease payments are included in operating expenses or general and administrative expenses depending on the nature of the lease.

## FINANCIAL RISK MANAGEMENT

The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Board has implemented and monitors compliance with risk management policies.

The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to market conditions and the Company's activities.  The Company's financial risks are discussed in note 5 of the Company's consolidated financial statements for the year ended December 31, 2018.

As at December 31, 2018, the Company has entered into certain financial derivative contracts in order to manage commodity risk.  These instruments are not used for trading or speculative purposes.  The Company has not designated its financial derivative contracts as effective accounting hedges, even though the Company considers all commodity contracts to be effective economic hedges.  Such financial derivative commodity contracts are recorded on the consolidated statement of financial position at fair value, with changes in the fair value being recognized as an unrealized gain or loss on the consolidated statement of income and comprehensive income. The contracts that the Company entered into in 2018 are summarized in note 5 of the Company's consolidated financial statements for the year ended December 31, 2018.

The following table provides a summary of the unrealized gains and losses on financial instruments for the year ended December 31, 2018):

| | **Three Months Ended December 31,** | | **Years Ended December 31,** | |
|---|---|---|---|---|
| *(000s)* | **2018** | **2017** | **2018** | **2017** |
| Unrealized gain (loss) on financial instruments | **$ 79,576** | $ (11,143) | **$ 16,633** | $ 67,440 |

The Company has entered into physical contracts to manage commodity risk.  These contracts are considered normal sales contracts and are not recorded at fair value in the consolidated financial statements.  Physical contracts in place at December 31, 2018 have been summarized in note 5 of the Company's consolidated financial statements for the year ended December 31, 2018.

Financial derivative and physical delivery contracts entered into subsequent to December 31, 2018 are detailed in note 5 of the Company's consolidated financial statements for the year ended December 31, 2018.

## APPLICATION OF CRITICAL ACCOUNTING ESTIMATES

Certain accounting policies require that management make appropriate decisions with respect to the formulation of estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Management reviews its estimates on a regular basis.  The emergence of new information and changed circumstances may result in actual results or changes to estimates that differ materially from current estimates. The Company's use of estimates and judgments in preparing the consolidated financial statements is discussed in note 1 of the consolidated financial statements for the year ended December 31, 2018.

## DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROLS OVER FINANCIAL REPORTING

The Company's Chief Executive Officer and Chief Financial Officer have designed, or caused to be designed under their supervision, disclosure controls and procedures ("DC&P"), as defined by National Instrument 52-109 – *Certification of Disclosure in Issuers' Annual and Interim Filings* ("NI 52-109"), to provide reasonable assurance that: (i) material information relating to the Company is made known to the Company's Chief Executive Officer and Chief Financial Officer by others, particularly during the periods in which the annual and interim filings are being prepared; and (ii) information required to be disclosed by the Company in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time period specified in securities legislation.

The Company's Chief Executive Officer and Chief Financial Officer have designed, or caused to be designed under their supervision, internal controls over financial reporting ("ICFR"), as defined by NI 52-109, to provide reasonable assurance regarding the reliability of the Company's financial reporting and the preparation of financial statements for external purposes in accordance with GAAP.

The Company's Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of the Company's DC&P and ICFR. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that, as at December 31, 2018, the Company's DC&P and ICFR are effective.

There were no changes in the Company's DC&P or ICFR during the period beginning on October 1, 2018 and ending December 31, 2018 that have materially affected, or are reasonably likely to materially affect, the Company's DC&P or ICFR. It should be noted that a control system, including the Company's disclosure and internal controls and procedures, no matter how well conceived can provide only reasonable, but not absolute, assurance that the objectives of the control system will be met and it should not be expected that the disclosure and internal controls and procedures will prevent all errors or fraud.

The Company uses the guidelines as set forth in the Committee of Sponsoring Organizations of the Treadway Commission 2013 Internal Control-Integrated Framework.

## BUSINESS RISKS AND UNCERTAINTIES

Tourmaline monitors and complies with current government regulations that affect its activities, although operations may be adversely affected by changes in government policy, regulations or taxation. In addition, Tourmaline maintains a level of liability, property and business interruption insurance which is believed to be adequate for Tourmaline's size and activities, but is unable to obtain insurance to cover all risks within the business or in amounts to cover all possible claims.

See "Forward-Looking Statements" in this MD&A and "Risk Factors" in Tourmaline's most recent annual information form for additional information regarding the risks to which Tourmaline and its business and operations are subject.

## IMPACT OF ENVIRONMENTAL REGULATIONS

The oil and gas industry is currently subject to regulation pursuant to a variety of provincial and federal environmental legislation, all of which is subject to governmental review and revision from time to time. Such legislation provides for, among other things, restrictions and prohibitions on the spill, release or emission of various substances produced in association with certain oil and gas industry operations, such as sulphur dioxide and nitrous oxide. In addition, such legislation sets out the requirements with respect to oilfield waste handling and storage, habitat protection and the satisfactory operation, maintenance, abandonment and reclamation of well and facility sites. Compliance with such legislation can require significant expenditures and a breach of such requirements may result in suspension or revocation of necessary licenses and authorizations, civil liability and the imposition of material fines and penalties.

The use of fracture stimulations has been ongoing safely in an environmentally responsible manner in western Canada for decades. With the increase in the use of fracture stimulations in horizontal wells, there is increased communication between the oil and natural gas industry and a wider variety of stakeholders regarding the responsible use of this technology. This increased attention to fracture stimulations may result in increased regulation or changes of law which may make the operation of the Company's business more expensive or prevent the Company from conducting its business as currently conducted. Tourmaline focuses on conducting transparent, safe and responsible operations in the communities in which its people live and work.

## CHANGES IN ACCOUNTING POLICIES

The following pronouncements as issued by the International Accounting Standards Board ("IASB") have been adopted by the Company effective January 1, 2018.

**IFRS 9 – Financial Instruments** replaces the existing guidance in IAS 39 *Financial Instruments: Recognition and Measurement*. The new standard includes revised guidance on the classification and measurement of financial instruments, including a new expected credit loss model for calculating impairment on financial assets, and the new general hedge accounting requirements. It also carries forward the guidance on recognition and derecognition of financial instruments from IAS 39.

The three principal classification categories under the new standard for financial instruments are: measured at amortized cost, fair value through other comprehensive income ("FVOCI") and fair value through profit and loss ("FVTPL"). The classification of financial instruments under IFRS 9 is generally based on the business model in which a financial instrument is managed and its contractual cash flow characteristics. The previous categories under IAS 39 of held to maturity, loans and receivables and available for sale have been removed.

IFRS 9 replaces the "incurred loss" model in IAS 39 with an "expected loss" model. The new impairment model applies to financial instruments measured at amortized cost, and contract assets and debt investments measured at FVOCI. Under IFRS 9, credit losses will be recognized earlier than under IAS 39.

Cash and cash equivalents, accounts receivable, prepaid expenses and deposits, accounts payable and accrued liabilities, and bank debt continue to be measured at amortized cost and are now classified as "amortized cost". There were no changes to the Company's classifications of its financial instrument assets and liabilities as FVTPL. None of the Company's financial instruments have been classified as FVOCI.

The Company did not formerly apply hedge accounting to its financial instruments and has not elected to apply hedge accounting to any of its financial instruments upon adoption of IFRS 9. There was no impact to the Company as a result of adopting the new standard.

**IFRS 15 – Revenue from Contracts with Customers** establishes a comprehensive framework for determining whether, how much and when revenue is recognized. It replaces existing revenue recognition guidance, including IAS 18 *Revenue*, IAS 11 *Construction Contracts* and IFRIC 13 *Customer Loyalty*

*Programmes*. The Company has adopted IFRS 15 using the modified retrospective approach on January 1, 2018. Based on the Company's review of contracts with customers and its assessment of various revenue streams using the IFRS 15 five step model, there were no material changes to net income, the timing of revenue recognized, income statement line classification or to opening retained earnings as at January 1, 2018. Tourmaline has expanded disclosures in the notes to its consolidated financial statements as prescribed by IFRS 15, including disclosing the Company's disaggregated revenue streams by product type. As a result of adopting IFRS 15 the Company's revenue recognition policy is now:

**Revenue Recognition:**

Revenue from the sale of crude oil, condensate, natural gas and natural gas liquids is recorded when control of the product is transferred to the buyer based on the consideration specified in the contracts with customers. This usually occurs when the product is physically transferred at the delivery point agreed upon in the contract and legal title to the product passes to the customer. The Company evaluates its arrangements with third parties and partners to determine if the Company acts as the principal or as an agent. In making this evaluation, the Company considers if it obtains control of the product delivered or services provided, which is indicated by the Company having the primary responsibility for the delivery of the product or rendering of the service, having the ability to establish prices or having inventory risk. If the Company acts in the capacity of an agent rather than as a principal in a transaction, then the revenue is recognized on a net-basis, only reflecting the fee, if any, realized by the Company from the transaction.

## STANDARDS ISSUED BUT NOT YET ADOPTED

The following pronouncement from the IASB will become effective for financial reporting periods beginning January 1, 2019 and have not yet been adopted by the Company. This new standard permits early adoption with transitional arrangements depending upon the date of initial application.

**IFRS 16 – Leases** sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract, i.e. the customer ("lessee") and the supplier ("lessor") and replaces the previous leases standard, IAS 17-Leases and IFRIC 4-Determining whether an Arrangement contains a Lease and related interpretations. IFRS 16 is effective for annual reporting periods beginning on or after January 1, 2019. The standard is required to be adopted either retrospectively or using a modified retrospective approach. The modified retrospective approach does not require restatement of prior period financial information as it recognizes the cumulative effect of IFRS as an adjustment to opening retained earnings and applies the standard prospectively. On January 1, 2019, the Company will adopt IFRS 16 and plans to use the modified retrospective approach.

On adoption, the Company currently intends on applying the following practical expedients permitted under the standard. Some expedients are available on a lease-by-lease basis, while others are applicable by class of underlying asset.

- Any leases with terms ending within 12 months of January 1, 2019 will be recognized as short-term leases and included in the short-term lease disclosure. These leases will not be recognized on the statement of financial position on initial adoption.

- The Company will exclude initial direct costs from the measurement of the right-of-use asset on transition for any leases with associated initial direct costs.
- Short-term leases and leases of low value assets that have been identified at January 1, 2019, will not be recognized on the statement of financial position. Payments for these leases will be disclosed in the notes to the financial statements.

The Company has completed an initial assessment, but not yet finalized, the potential impact on its consolidated financial statements. The full impact of applying IFRS 16 on the financial statements in the period of initial application will depend on multiple factors and conditions, including but not limited to, the Company's borrowing rate at January 1, 2019, the composition of the Company's lease portfolio at that date and the Company's latest assessment of whether it will exercise any lease renewal or termination options.

Thus far, the most significant impact identified is that the Company will now recognize new assets and liabilities on its Statement of Financial Position for its real estate, vehicle, and IT leases. In addition, the nature of the expenses related to those leases will change. Straight-line operating lease expense will be replaced with a depreciation charge for right-of-use assets and interest expense on lease liabilities.

The Company continues to review all existing contracts in detail. The full extent of the impact has not yet been determined. The Company continues to remain focused on developing and implementing policies, internal controls, information systems and business and accounting processes.

## NON-GAAP FINANCIAL MEASURES

This MD&A or documents referred to in this MD&A make reference to the terms "cash flow", "operating netback", "working capital (adjusted for the fair value of financial instruments)", "net debt", "adjusted EBITDA", "total debt", and "total capitalization" which are not recognized measures under GAAP, and do not have a standardized meaning prescribed by GAAP. Accordingly, the Company's use of these terms may not be comparable to similarly defined measures presented by other companies. Management uses the terms "cash flow", "operating netback", "working capital (adjusted for the fair value of financial instruments)" and "net debt", for its own performance measures and to provide shareholders and potential investors with a measurement of the Company's efficiency and its ability to generate the cash necessary to fund a portion of its future growth expenditures or to repay debt. Investors are cautioned that the non-GAAP measures should not be construed as an alternative to net income determined in accordance with GAAP as an indication of the Company's performance. The terms "adjusted EBITDA", "total debt", and "total capitalization" are not used by management in measuring performance but are used in the financial covenants under the Company's credit facility. Under the Company's credit facility "adjusted EBITDA" means generally net income or loss, excluding extraordinary items, plus interest expense and income taxes and adjusted for non-cash items and gains or losses on dispositions, "total debt" means generally the sum of debt plus subordinated debt, Tourmaline currently does not have any subordinated debt, and "total capitalization" means generally the sum of the Company's shareholders' equity and all other indebtedness of the Company including bank debt, all determined on a consolidated basis in accordance with GAAP.

## Cash Flow

A summary of the reconciliation of cash flow from operating activities (per the statement of cash flow), to cash flow, is set forth below:

| | Three Months Ended December 31, | | Years Ended December 31, | |
|---|---|---|---|---|
| *(000s)* | **2018** | **2017** | **2018** | **2017** |
| Cash flow from operating activities (per GAAP) | **$ 329,997** | $ 299,793 | **$ 1,269,491** | $ 1,182,900 |
| Change in non-cash working capital | **61,535** | 48,434 | **33,971** | 22,858 |
| Cash flow | **$ 391,532** | $ 348,227 | **$ 1,303,462** | $ 1,205,758 |

## Operating Netback

Operating netback is calculated on a per-boe basis and is defined as revenue (excluding processing income) less royalties, transportation costs and operating expenses, as shown below:

| | Three Months Ended December 31, | | Years Ended December 31, | |
|---|---|---|---|---|
| *($/boe)* | **2018** | **2017** | **2018** | **2017** |
| Revenue, excluding processing income | **$ 23.40** | $ 21.76 | **$ 21.77** | $ 21.30 |
| Royalties | **(0.60)** | (0.87) | **(0.80)** | (0.91) |
| Transportation costs | **(3.63)** | (3.01) | **(3.52)** | (2.93) |
| Operating expenses | **(3.35)** | (3.08) | **(3.33)** | (3.19) |
| Operating netback | **$ 15.82** | $ 14.80 | **$ 14.12** | $ 14.27 |

## Working Capital (Adjusted for the Fair Value of Financial Instruments)

A summary of the reconciliation of working capital to working capital (adjusted for the fair value of financial instruments) is set forth below:

| | As at December 31, | |
|---|---|---|
| *(000s)* | **2018** | **2017** |
| Working capital (deficit) | **$ (228,403)** | $ (219,168) |
| Fair value of financial instruments – short-term (ass) liability | **(13,640)** | 16,684 |
| Working capital (deficit) (adjusted for the fair value of financial instruments) | **$ (242,043)** | $ (202,484) |

## Net Debt

A summary of the reconciliation of net debt is set forth below:

| | As at December 31, | |
|---|---|---|
| *(000s)* | **2018** | **2017** |
| Bank debt | **$(1,476,099)** | $(1,534,757) |
| Working capital (deficit) | **(228,403)** | (219,168) |
| Fair value of financial instruments – short-term (asset) liability | **(13,640)** | 16,684 |
| Net debt | **$(1,718,142)** | $(1,737,241) |

## SELECTED QUARTERLY INFORMATION

| | 2018 | | | | 2017 | | | |
|---|---|---|---|---|---|---|---|---|
| *($000s, unless otherwise noted)* | **Q4** | **Q3** | **Q2** | **Q1** | **Q4** | **Q3** | **Q2** | **Q1** |
| **PRODUCTION** | | | | | | | | |
| Natural gas *(mcf)* | **123,995,544** | 115,321,116 | 117,429,708 | 119,585,930 | 120,238,014 | 109,246,506 | 108,879,426 | 107,494,272 |
| Oil and NGL*(bbls)* | **4,778,286** | 4,164,796 | 4,172,997 | 4,236,320 | 4,184,707 | 3,587,572 | 3,287,567 | 3,079,321 |
| Oil equivalent *(boe)* | **25,444,210** | 23,384,982 | 23,744,615 | 24,167,308 | 24,224,376 | 21,795,323 | 21,434,138 | 20,995,033 |
| Natural gas *(mcf/d)* | **1,347,778** | 1,253,490 | 1,290,436 | 1,328,733 | 1,306,935 | 1,187,462 | 1,196,477 | 1,194,380 |
| Oil and NGL *(bbls/d)* | **51,938** | 45,270 | 45,857 | 47,070 | 45,486 | 38,995 | 36,127 | 34,215 |
| Oil equivalent *(boe/d)* | **276,568** | 254,185 | 260,930 | 268,526 | 263,309 | 236,905 | 235,540 | 233,278 |
| **FINANCIAL** | | | | | | | | |
| Total revenue from commodity sales and realized gains (losses) on risk management activities and financial instruments | **595,487** | 496,711 | 463,845 | 550,166 | 527,106 | 410,591 | 479,269 | 466,645 |
| Cash flow from operating activities | **329,997** | 314,191 | 283,155 | 342,148 | 299,793 | 266,525 | 278,577 | 338,005 |
| Per diluted share | **1.21** | 1.15 | 1.04 | 1.26 | 1.11 | 0.99 | 1.03 | 1.25 |
| Cash flow [(1)] | **391,532** | 287,421 | 272,261 | 352,248 | 348,227 | 251,327 | 313,271 | 292,933 |
| Per diluted share | **1.44** | 1.06 | 1.00 | 1.30 | 1.29 | 0.93 | 1.16 | 1.09 |
| Net earnings | **190,895** | 55,296 | 25,639 | 129,588 | 88,079 | 50,580 | 108,580 | 99,534 |
| Per basic share | **0.70** | 0.20 | 0.09 | 0.48 | 0.33 | 0.19 | 0.40 | 0.37 |
| Per diluted share | **0.70** | 0.20 | 0.09 | 0.48 | 0.33 | 0.19 | 0.40 | 0.37 |
| Total assets | **10,732,457** | 10,429,505 | 10,186,188 | 10,212,446 | 10,181,528 | 9,916,804 | 9,630,468 | 9,612,395 |
| Working capital (deficit) | **(228,403)** | (411,687) | (192,116) | (232,695) | (219,168) | (352,068) | (130,337) | (355,097) |
| Working capital (deficit)(adjusted for the fair value of financial instruments) [(1)] | **(242,043)** | (341,960) | (130,834) | (206,988) | (202,484) | (350,112) | (134,212) | (337,191) |
| Cash capital expenditures | **395,194** | 409,919 | 191,773 | 217,551 | 352,233 | 465,466 | 189,532 | 399,385 |
| Dividends paid | **27,304** | 27,103 | 24,488 | 21,687 | – | – | – | – |
| Total outstanding shares *(000s)* | **272,043** | 272,043 | 272,084 | 271,084 | 271,084 | 269,784 | 269,784 | 269,169 |
| **PER UNIT** | | | | | | | | |
| Natural *gas ($/mcf)* | **3.13** | 2.54 | 2.25 | 2.97 | 2.70 | 2.52 | 3.19 | 3.15 |
| Oil and NGL *($/bbl)* | **43.40** | 48.91 | 47.93 | 46.08 | 48.31 | 37.63 | 40.01 | 41.73 |
| Revenue *($/boe)* | **23.40** | 21.24 | 19.53 | 22.76 | 21.76 | 18.84 | 22.36 | 22.23 |
| Operating netback *($/boe)* [(1)] | **15.82** | 13.15 | 12.10 | 15.25 | 14.80 | 12.27 | 15.36 | 14.59 |

*(1) See Non-GAAP Financial Measures.*

The oil and gas exploration and production industry is cyclical in nature. The Company's financial position, results of operations and cash flows are principally impacted by production levels and commodity prices, particularly natural gas prices.

On an annual basis, the Company has had continued production growth over the last two years. The Company's average annual production has increased from 185,672 boe per day in 2016 to 242,325 boe per day in 2017 and 265,044 boe per day in 2018. The production growth can be attributed primarily to the Company's exploration and development activities, and from acquisitions of producing properties.

The Company's cash flow was $731.8 million in 2016, $1,205.8 million in 2017, and $1,303.5 million in 2018. The increase in cash flow in 2018 over 2017 reflects the significant increase in production partially offset by commodity price volatility. Commodity price fluctuations can indirectly impact expected production by changing the amount of funds available to reinvest in exploration, development and acquisition activities in the future. Changes in commodity prices impact revenue and cash flow available for exploration, and also the economics of potential capital projects as low commodity prices can potentially reduce the quantities of reserves that are commercially recoverable. The Company's capital program is dependent on cash flow generated from operations and at times, access to capital markets.

## SELECTED ANNUAL INFORMATION

| *($000s unless otherwise noted)* | **2018** | **2017** | **2016** |
|---|---|---|---|
| **PRODUCTION** | | | |
| Natural gas *(mcf)* | **476,334,125** | 445,858,218 | 355,939,830 |
| Oil and NGL *(bbls)* | **17,352,100** | 14,139,167 | 8,632,548 |
| Oil equivalent *(boe)* | **96,741,121** | 88,448,870 | 67,955,853 |
| Natural gas *(mcf/d)* | **1,305,025** | 1,221,529 | 972,513 |
| Oil and NGL *(bbls/d)* | **47,540** | 38,737 | 23,586 |
| Oil equivalent *(boe/d)* | **265,044** | 242,325 | 185,672 |
| **FINANCIAL** | | | |
| Total revenue from commodity sales and realized gains (losses) on risk management activities and financial instruments | **2,106,209** | 1,883,611 | 1,219,160 |
| Cash flow from operating activities | **1,269,491** | 1,182,900 | 696,901 |
| Per diluted share | **4.67** | 4.39 | 2.97 |
| Cash flow [(1)] | **1,303,462** | 1,205,758 | 731,801 |
| Per diluted share | **4.80** | 4.47 | 3.12 |
| Net earnings (loss) | **401,418** | 346,773 | (31,971) |
| Per basic share | **1.48** | 1.29 | (0.14) |
| Per diluted share | **1.48** | 1.29 | (0.14) |
| Total assets | **10,732,457** | 10,181,528 | 9,357,523 |
| Working capital (deficit) | **(228,403)** | (219,168) | (223,781) |
| Working capital (deficit) (adjusted for the fair value of financial instruments) [(1)] | **(242,043)** | (202,484) | (184,264) |
| Cash capital expenditures (net) | **1,214,437** | 1,406,616 | 1,933,289 |
| Dividends paid | **100,580** | – | – |
| Basic outstanding shares *(000s)* | **272,043** | 271,084 | 268,596 |
| **PER UNIT** | | | |
| Natural gas *($/mcf)* | **2.73** | 2.89 | 2.51 |
| Oil and NGL *($/bbl)* | **46.47** | 42.24 | 37.68 |
| Revenue *($/boe)* | **21.77** | 21.30 | 17.94 |
| Operating netback *($/boe)* | **14.12** | 14.27 | 11.50 |

*(1) See Non-GAAP Financial Measures.*