PetroShale
Calgary • Denver

Consolidated Interim Financial Statements

As at March 31, 2016
and for the three months ended March 31, 2016 and 2015

In accordance with National Instrument 51-102 released by the Canadian Securities Administrators, the Company discloses that its auditors have not reviewed these unaudited interim consolidated financial statements as at and for the three months ended March 31, 2016.

PetroShale
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CONSOLIDATED INTERIM STATEMENTS OF FINANCIAL POSITION
(Unaudited)

As at (thousands of Canadian dollars)	NOTE	**March 31, 2016**	**December 31, 2015**
ASSETS			
Current assets			
Cash and cash equivalents		$ 3,622	$ 822
Accounts receivable		2,447	3,461
Prepaid expenses		244	222
		6,313	4,505
Non-current assets			
Restricted cash	9	98	104
Property, plant and equipment	3,4	119,976	123,943
		120,074	124,047
		$126,387	$128,552
LIABILITIES			
Current liabilities			
Accounts payable and accrued liabilities		$ 18,837	$ 18,212
Senior loan	6	29,371	30,082
Subordinated loan	6	77,854	75,408
		126,062	123,702
Non-current liabilities			
Decommissioning obligation	5	822	834
Total liabilities		126,884	124,536
SHAREHOLDERS' EQUITY			
Share capital	7	35,658	35,658
Contributed surplus		3,372	3,344
Deficit		(42,594)	(39,114)
Accumulated other comprehensive income		3,067	4,128
		(497)	4,016
Commitments	9		
Subsequent Events	13		
		$126,387	$128,552

See accompanying notes to the consolidated financial statements.

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CONSOLIDATED INTERIM STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS
(Unaudited)

(thousands of Canadian dollars, except per share amounts)	NOTE	Three months ended March 31, 2016	2015
Revenue			
Oil and natural gas revenue		$ 4,004	$ 3,002
Royalties		(822)	(673)
		3,182	2,329
Expenses			
Production and operating		1,509	789
General and administrative		755	612
Depletion and depreciation	4	1,987	1,495
Finance		2,763	1,901
Foreign exchange gain		(380)	-
Share-based compensation	7	28	70
		6,662	4,867
Net loss for the year		(3,480)	(2,538)
Currency translation adjustment		(1,061)	760
Comprehensive loss for the year		$(4,541)	$(1,778)
Net loss per share, basic and diluted	8	**$ (0.10)**	**$ (0.07)**

See accompanying notes to the consolidated financial statements.

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CONSOLIDATED INTERIM STATEMENTS OF CHANGES IN EQUITY

For the three months ended March 31, 2016 and 2015
(Unaudited)

(thousands of Canadian dollars, except share amounts)

	Non Voting Common Shares		Voting Common Shares				Accumulated Other Comprehensive	
	Shares	Amount	Shares	Amount	Contributed Surplus	Deficit	Income	Total
Balances, December 31, 2014	6,700,000	$ -	27,507,574	$ 35,658	$ 3,111	$ (30,167)	$ 1,681	$ 10,283
Share-based compensation	-	-	-	-	70	-	-	70
Net loss for the period	-	-	-	-	-	(2,538)	-	(2,538)
Other comprehensive income for the period	-	-	-	-	-	-	760	760
Balances, March 31, 2015	6,700,000	$ -	27,507,574	$ 35,658	$ 3,181	$ (32,705)	$ 2,441	$ 8,575
Balances, December 31, 2015	6,700,000	$ -	27,507,574	$ 35,658	$ 3,344	$ (39,114)	$ 4,128	4,016
Share-based compensation	-	-	-	-	28	-	-	28
Net loss for the period	-	-	-	-	-	(3,480)	-	(3,480)
Other comprehensive loss for the period	-	-	-	-	-	-	(1,061)	(1,061)
Balances, March 31, 2016	6,700,000	$ -	27,507,574	$ 35,658	$ 3,372	$ (42,594)	$ 3,067	$ (497)

See accompanying notes to the consolidated financial statements.

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CONSOLIDATED INTERIM STATEMENTS OF CASH FLOWS
(Unaudited)

(thousands of Canadian dollars)	Three months ended March 31, 2016	2015
Operating Activities		
Net loss for the period	$ (3,480)	$ (2,538)
Items not affecting cash:		
Depletion and depreciation	1,987	1,495
Accretion of decommissioning obligation	5	2
Amortization of loan fees	52	233
Share-based compensation	28	70
Decommissioning expenditures	-	(1)
Change in non-cash working capital (note 11)	1,519	928
	111	189
Investing Activities		
Acquisition of property, plant and equipment	(3,286)	(1,956)
Additions to property, plant and equipment	(2,900)	(7,164)
Change in non-cash working capital (note 11)	(1,487)	(9,315)
	(7,673)	(18,435)
Financing Activities		
Proceeds from subordinated loan, net	7,688	21,980
Proceeds from senior loan, net	635	315
Change in non-cash working capital (note 11)	2,387	-
	10,710	22,295
Change in cash and cash equivalents	3,148	4,049
Effect of foreign exchange rates	(348)	33
Cash and cash equivalents, beginning of period	822	339
Cash and cash equivalents, end of period	$ 3,622	$ 4,421

See accompanying notes to the consolidated financial statements.

1. BUSINESS AND NATURE OF OPERATIONS

PetroShale Inc. (the "Company") is an oil company engaged in the acquisition, development and consolidation of interests in the North Dakota Bakken.

The Company's head office is located at Suite 3900, 350-7th Avenue SW, Calgary, Alberta.

2. BASIS OF PREPARATION

These consolidated interim financial statements and the notes thereto should be read in conjunction with the Company's audited consolidated financial statements as at and for the year ended December 31, 2015, and do not include all of the information required for full annual financial statements.

These consolidated interim financial statements are unaudited and have been prepared in accordance with IAS 34 – "Interim Financial Reporting" using accounting policies consistent with International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board ("IASB") and interpretations of the International Financial Reporting Interpretations Committee ("IFRIC").

The accounting policies applied for the consolidated interim financial statements as at and for the three months ended March 31, 2016 are consistent with those applied for the financial statements as at and for the most recent audited period.

These financial statements have been prepared using the historical cost basis.

The Company's reporting and measurement currency is the Canadian dollar. The functional currency of the Company's US subsidiary is the US dollar, and its results and balance sheet items are translated to Canadian dollars for purposes of these consolidated financial statements, in accordance with the Company's foreign currency translation accounting policy.

These consolidated interim financial statements were approved by the Company's Board of Directors on May 19, 2016.

IFRS 9 - "Financial Instruments" is the result of the first phase of the IASB's project to replace IAS 39 - "Financial Instruments: Recognition and Measurement". The new standard replaces the current multiple classification and measurement models for financial assets and liabilities with a single model that has only two classification categories: amortized cost and fair value. The standard will come into effect on January 1, 2018 with early adoption permitted. The extent of the impact of the adoption of IFRS 9 has not yet been determined.

IFRS 11 – "Accounting for Acquisitions of Interests in Joint Operations" has been amended to provide guidance on accounting for acquisitions of an interest in a joint operation that constitutes a business. IFRS 11 is effective for annual periods beginning on or after January 1, 2016 with early adoption permitted. The Company has determined that this amended accounting standard will not have a significant impact on its consolidated financial statements.

IFRS 15 – "Revenue from Contracts with Customers" was issued in May 2014 to replace IAS11 – "Construction Contracts" and IAS 18 – "Revenue" and related interpretive guidance. IFRS 15 provides a single, principles based model to be applied to all contracts with customers as well as new disclosure requirements with the objective of a more structured approach, improving comparability across entities and industries. Under IFRS 15, an entity will recognize revenue at the amount to which it expects to be entitled in exchange for goods or services on their transfer. IFRS 15 is effective for annual periods beginning on or after January 1, 2018 with earlier adoption permitted and is to be applied retrospectively. The extent of the impact of the adoption of IFRS 15 is not expected to be material.

(tabular amounts in $000's of Canadian dollars, unless otherwise noted)

IFRS 16 – "Leases" is effective for annual periods beginning on or after January 1, 2019 with earlier adoption permitted, and is to be applied retrospectively. The extent of the impact of adoption of this new standard on the Company has not been fully assessed at this time, but is not expected to be material.

3. ACQUISITIONS

During the three months ended March 31, 2016, through various transactions, the Company purchased oil and gas leases in its focus area in North Dakota. This represents various working interests in potential drilling units with associated proved undeveloped and probable reserves. The aggregate consideration for these leases was approximately US$2.4 million. There were no assumptions of liabilities associated with these purchases.

4. PROPERTY, PLANT AND EQUIPMENT

	Other	Developed and Producing Assets	Total
Balances as at December 31, 2014	$ 57	$ 74,979	$ 75,036
Acquisitions	-	26,602	26,602
Additions	-	17,338	17,338
Dispositions	-	(2,378)	(2,378)
Impairment	-	(114)	(114)
Depletion and depreciation	(19)	(9,887)	(9,906)
Effect of foreign exchange rate	9	17,356	17,365
Balances as at December 31, 2015	47	123,896	123,943
Acquisitions	-	3,286	3,286
Additions	-	2,940	2,940
Depletion and depreciation	(5)	(1,982)	(1,987)
Effect of foreign exchange rate	(2)	(8,204)	(8,206)
Balances as at March 31, 2016	$ 40	$ 119,936	$ 119,976

Depletion, Depreciation, and Future Development Costs

For the three months ended March 31, 2016 and 2015, the Company recorded $2.0 million and $1.5 million, respectively, of depletion and depreciation expense, which reflected an estimated US$217.1 million and US$121.4 million, respectively of future development costs associated with proven plus probable reserves.

(tabular amounts in $000's of Canadian dollars, unless otherwise noted)

Impairment Charges

As at December 31, 2015 the Company determined that indicators of impairment existed for its CGUs due to the decline in current and forward commodity prices for both oil and natural gas. The Company performed an impairment test on each of its CGUs as at December 31, 2015, using a discount rate of 10% and future commodity price estimates applicable at the time (see Note 8 to the Company's December 31, 2015 Consolidated Financial Statements.) This resulted in an impairment expense recorded in the three month period ended December 31, 2015 of $114,000 (December 31, 2014 - $906,000.)

An assessment was made as at March 31, 2016 as to whether there were any facts or circumstances which suggested there is a trigger for impairment of the Company's Developed and Producing assets. The Company does not believe any such facts or circumstances existed. For the three months ended March 31, 2016 and 2015, the Company recognized no impairment expense.

Disposition

During the year ended December 31, 2015, the Company disposed of the working interest oil and gas properties which had been included in its Canadian non-core CGU for non-cash proceeds of $447,000, on the assumption of the decommissioning liability by the purchaser.

5. DECOMMISSIONING OBLIGATION

Balance as at December 31, 2014	$	892
Acquisition of petroleum and natural gas properties		70
Additions		97
Dispositions		(447)
Obligations Settled		(3)
Revisions of estimated cash flows		107
Accretion		6
Effect of foreign exchange rate		112
Balance as at December 31, 2015		834
Additions		1
Revisions of estimated cash flows		39
Accretion		5
Effect of foreign exchange rate		(57)
Balance as at March 31, 2016	$	822

The Company's decommissioning obligation consists of remediation obligations resulting from its ownership interests in petroleum and natural gas assets. The total obligation is estimated based on the Company's net working interest in wells and related facilities, estimated costs to return these sites to their original condition, costs to plug and abandon the wells and the estimated timing of the costs to be incurred in future years.

As at December 31, 2015, the Company had disposed of all of its Canadian working interest assets and, as a result, has reflected a disposition of the related decommissioning obligation.

The total undiscounted amount of estimated future cash flows required to settle the obligation as at March 31, 2016 is $1.5 million (December 31, 2015 – $1.6 million) which includes an inflation factor of 1.7% (December 31, 2015 – 1.7%) on the costs of decommissioning and assumes that the liabilities are settled over approximately the next 35 years in accordance with estimates prepared by independent engineers. The estimated future cash flows as at March 31, 2016 have been discounted at the risk-free interest rate of 2.6% (December 31, 2015 – 2.8%).

6. DEBT

Senior Loan

The Company's senior loan is a revolving credit facility with a borrowing base of US$22.5 million (Cdn$29.4 million, assuming the March 31, 2016 foreign exchange rate) as at March 31, 2016. This facility is due on demand, but has a renewal date of July 16, 2016, at which point, at the bank's option, it may be renewed on terms to be agreed upon at that time, or converted to a non-revolving term facility for a term to be determined by the bank. This facility is secured by all of the Company's assets and bears interest at the bank's prime lending rate plus 1% or the relevant bankers acceptance fee plus 2.75% if drawn in Canadian dollars, or the bank's U.S. dollar base rate plus 0.50% or U.S. dollar LIBOR rate plus 3.75% if drawn in U.S. dollars. A standby fee of 0.50% per annum is applied to any undrawn balance. The borrowing base is subject to a borrowing base test performed at least twice annually by the bank, based on reserve reports associated with the Company's U.S. petroleum and natural gas properties. A decrease in the borrowing base could result in the requirement to make a repayment to the bank. The next borrowing base review is scheduled prior to the current renewal date.

The credit facility is subject to financial and non-financial covenants applied to the Company, on a consolidated basis. The financial covenants consist of: (i) a consolidated cash flow to interest expense ratio, as defined in the loan agreement, which is not to be less than 2.50 to 1 on a rolling four-quarter basis, with any equity injections included in the calculation of consolidated cash flow and interest expense excluded from the definition of consolidated cash flow; and (ii) a requirement that total debt not exceed the borrowing base by more than 133%, while excluding the subordinated loan from the definition of total debt. The facility was drawn approximately US$22.5 million as at March 31, 2016.

In 2015, management obtained a waiver from the consolidated cash flow to interest expense covenant from the senior lender on the condition that interest payments under the subordinated loan are deferred until such time as the covenant is back in compliance, or as otherwise agreed to with the senior lender. Interest payments under the subordinated loan have been deferred commencing April 1, 2015. The consolidated cash flow to interest expense ratio at March 31, 2016 was 11.8 to 1, and therefore the Company is in compliance with this covenant as at that date, and is also in compliance with all of its other covenants under the senior loan as at March 31, 2016.

Subordinated Loan

The Company has a secured, subordinated, revolving credit facility which may be drawn in US dollars and which has a capacity of US$80.0 million effective as at April 1, 2016 (Cdn$104.0 million, assuming the March 31, 2016 foreign exchange rate). The maturity date of the facility is December 31, 2017. The credit facility bears interest at a rate of 12% per annum, with interest payments due monthly, and includes a 2.5% loan origination fee. The credit facility is provided by two significant shareholders of the Company, one of whom is also a director and the CEO. This loan is secured by all of the assets of the Company, but subordinated to the senior loan facility. Among certain non-financial covenants, the subordinated loan requires the Company to comply with the financial covenants required by the senior loan agreement. Thus, a default under the terms of the senior loan would create a default under the subordinated loan agreement. This facility was drawn US$60.0 million as at March 31, 2016 and as at December 31, 2015 was drawn US$54.4 million.

(tabular amounts in $000's of Canadian dollars, unless otherwise noted)

Accrued liabilities as at March 31, 2016 includes deferred interest payable and origination fees of US$6.6 million (Cdn $8.6 million, assuming the March 31, 2016 foreign exchange rate; December 31, 2015 – Cdn $6.7 million).

In consideration for the increase in capacity of the facility to US$80.0 million, the extension of the term to December 31, 2017 and the continued deferral of interest payments (for the term of the subordinated loan or until such time as the bank permits cash interest to be paid, if earlier), the Company issued 2.0 million common share purchase warrants to the subordinated lenders effective April 25, 2016, pro rata to their participation in the revised commitment amount. Each warrant will entitle the holder to exercise and purchase one common share of the Company at $0.75 for a period of two years from the date of issuance. The loan origination fee of 2.5% will be paid on the increased commitment amount under the facility.

7. SHARE CAPITAL

a) Share capital

The Company's authorized share capital includes unlimited Class A preferred shares with rights and privileges to be determined by the Board of Directors prior to issuance, unlimited common non-voting shares, convertible into common voting shares on a 1 for 1 basis, and unlimited common voting shares. As at March 31, 2016, the Company had 27,507,574 common shares (December 31, 2015 – 27,507,574) and 6,700,000 non-voting common shares issued and outstanding (December 31, 2015 – 6,700,000.)

The following table reflects the Company's outstanding common shares as at March 31, 2016:

	Number of Voting and Non-Voting Shares	Share Capital
Balance as at December 31, 2015 and March 31, 2016	34,207,574	$ 35,658

b) Stock options

The following table presents stock option transactions for the periods ended March 31, 2016 and December 31, 2015:

	Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term
Balance as at December 31, 2014	2,275,205	$ 1.16	3.15
Granted	20,000	1.11	4.70
Balance as at December 31, 2015	2,295,205	1.16	2.16
Balance as at March 31, 2016	2,295,205	$ 1.16	1.91

(tabular amounts in $000's of Canadian dollars, unless otherwise noted)

As at March 31, 2016, the following stock options were outstanding:

Exercise Prices	Weighted Average Remaining Contractual Term	Number of Outstanding Options	Weighted Average Exercise Price	Number of Options Exercisable
$0.70	2.65	943,264	$0.70	628,838
$1.11	3.50	20,000	$1.11	6,667
$1.40	2.95	275,000	$1.40	141,666
$1.50	0.96	1,056,941	$1.50	1,056,941
	1.91	2,295,205	$1.16	1,834,112

The Company uses the fair value method to account for all share-based awards granted to employees, officers and directors. The estimated fair value of stock option grants was determined using the Black-Scholes option pricing model and is recorded as a charge to income over the vesting period with a corresponding increase to contributed surplus.

c) Warrants

Subsequent to March 31, 2016, the Company received regulatory approval and issued 2 million common share purchase warrants to the Company's subordinated lenders (see Note 6). Each warrant will entitle the holder to exercise and acquire one common share for $0.75 for a period of two years from the date of grant.

8. NET LOSS PER COMMON SHARE

The following table presents the Company's net loss per common share:

(thousands, except for share and per share data)	Three months ended March 31, 2016	2015
Net loss for the period	$ (3,480)	$ (2,538)
Weighted average number of basic common shares	34,207,574	34,207,574
Net loss per weighted average basic and diluted common share	$ (0.10)	$ (0.07)

9. COMMITMENTS

The Company has an outstanding letter of credit in favor of an energy regulator in North Dakota in the amount of US$75,000. As security, the Company has set aside an equivalent amount in cash at the financial institution that issued the letter of credit.

The Company is committed to monthly rental payments for office space of US$7,500 until August 2017.

(tabular amounts in $000's of Canadian dollars, unless otherwise noted)

10. RELATED PARTY TRANSACTIONS

Related party transactions are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

The Company has a secured, subordinated, revolving credit facility which is provided by two significant shareholders of the Company, one of whom is also a director and the CEO. See further details in Note 6 – Debt - Subordinated loan. During the three month period ended March 31, 2016, fees related to this facility were amortized to finance expense in the amount of US$38,000 (March 31, 2015 – US$188,000). During the three month period ended March 31, 2015, the Company paid US$1.3 million in cash interest and origination fees on the subordinated loan. No cash interest has been paid on this loan since April 1, 2015, with interest being accrued since that date, including US$1.7 million during the three months ended March 31, 2016. The Company has accrued a total of US$6.6 million of interest which is reflected in accounts payable at March 31, 2016. The lenders of this facility agreed to enhance its terms as at April 1, 2016. As partial consideration for extending the term of the subordinated loan, increasing the facility capacity and agreeing to continue to defer cash interest payments, the Company granted 2 million common share purchase warrants to the subordinated lenders, pro rata to their participation in the revised commitment amount. Each warrant entitles the holder to acquire one common share at $0.75 for a period of two years from the date of issuance.

11. SUPPLEMENTAL CASH FLOW DISCLOSURES

Changes in non-cash working capital is comprised of:

	Three months ended March 31, 2016	2015
Source/(use) of cash:		
Accounts receivable	$ 1,014	$ 931
Prepaid expenses	(22)	(178)
Accounts payable	625	(7,818)
	$ 1,617	$ (7,065)
Related to operating activities	$ 1,519	$ 928
Related to investing activities	(1,487)	(9,315)
Related to financing activities	2,387	-
Difference due to foreign exchange	(802)	1,322
	$ 1,617	$ (7,065)
Interest paid	$ 317	$ 1,666
Income taxes paid	nil	nil

(tabular amounts in $000's of Canadian dollars, unless otherwise noted)

12. SEGMENT DISCLOSURES

The Company operates in one industry segment, the production of petroleum and natural gas and the exploration for and development of oil and natural gas properties.

The Company and its subsidiaries operated in two geographical segments during the periods reported below, Canada and the United States. The Company disposed of the majority of its Canadian assets as at June 30, 2015.

	Three months ended March 31,	
	2016	**2015**
Revenue, net of royalties		
United States	$ 3,171	$ 2,259
Canada	11	70
	$ 3,182	$ 2,329
Net loss for the period		
United States	$ (3,349)	$ (2,363)
Canada	(131)	(175)
	$ (3,480)	$ (2,538)

	March 31, 2016	December 31, 2015
Property, plant and equipment		
United States	$ 119,286	$123,241
Canada	690	702
	$ 119,976	$123,943

13. SUBSEQUENT EVENTS

a) On April 1, 2016, the Company agreed to make amendments to its subordinated loan agreement extending its maturity date to December 31, 2017 and its total capacity to US$80.0 million. In connection with these amendments, the Company agreed to grant 2 million common share purchase warrants to the subordinated lenders. See Notes 6 and 7.

b) Subsequent to March 31, 2016, the Company acquired additional acreage in its core focus area as well as an interest in a producing well, for aggregate consideration of approximately US$4.0 million.