

HIGH ARCTIC ENERGY SERVICES INC.



CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

**FOR THE THREE AND SIX MONTH PERIODS ENDED
JUNE 30, 2018**

High Arctic Energy Services Inc.

Consolidated Statements of Financial Position

As at June 30, 2018 and December 31, 2017

Unaudited - Canadian \$ Million

	Notes	June 30, 2018	December 31, 2017
Assets			
Current assets			
Cash and cash equivalents		28.1	22.1
Accounts receivable	4	40.7	40.4
Short term investments	5	1.9	2.4
Inventory	6	10.7	10.0
Income taxes receivable		1.1	1.3
Prepaid expenses		1.4	0.9
		<u>83.9</u>	<u>77.1</u>
Non-current assets			
Property and equipment	7	178.1	182.9
Deferred tax asset		7.3	7.0
		<u>185.4</u>	<u>190.0</u>
Total assets		<u>269.3</u>	<u>267.0</u>
Liabilities			
Current liabilities			
Accounts payable and accrued liabilities	8	22.6	21.5
Dividend payable	12	0.9	0.9
Deferred revenue	11	0.5	1.0
		<u>24.0</u>	<u>23.4</u>
Non-current liabilities			
Finance lease obligation	9	0.4	0.5
Unfavourable lease liability	10	2.9	3.1
Deferred tax liability		10.3	9.2
		<u>13.6</u>	<u>13.8</u>
Total liabilities		<u>37.6</u>	<u>36.2</u>
Shareholders' equity	14	<u>231.7</u>	<u>230.8</u>
Total liabilities and shareholders' equity		<u>269.3</u>	<u>267.0</u>
Commitments and contingencies	20		

See accompanying notes to these consolidated financial statements.

Approved on behalf of the Corporation by:

(signed) "Joe Oliver" Director

(signed) "Michael Binnion" Director

High Arctic Energy Services Inc.

Consolidated Statements of Changes in Equity

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million

	Notes	Share capital	Contributed surplus	NCIB Equity	Accumulated other comprehensive income	Retained earnings (deficit)	Total shareholders' equity
Balance at January 1, 2018		186.1	9.4	-	18.5	16.8	230.8
Net earnings		-	-	-	-	6.2	6.2
Dividends	12	-	-	-	-	(5.2)	(5.2)
Other comprehensive income - foreign currency translation gain		-	-	-	7.0	-	7.0
Other comprehensive income - loss on short term investments	5	-	-	-	(0.5)	-	(0.5)
Purchase of common shares for cancellation	14	(4.7)	(0.6)	-	-	-	(5.3)
Liability for share repurchase commitment	8,14	-	-	(2.2)	-	-	(2.2)
Share-based payment transactions		0.2	0.7	-	-	-	0.9
Balance at June 30, 2018		181.6	9.5	(2.2)	25.0	17.8	231.7

	Notes	Share capital	Contributed surplus	NCIB Equity	Accumulated other comprehensive income	Retained earnings (deficit)	Total shareholders' equity
Balance at January 1, 2017		185.5	9.1	-	28.6	7.0	230.2
Net earnings		-	-	-	-	14.0	14.0
Dividends	12	-	-	-	-	(5.3)	(5.3)
Other comprehensive income - foreign currency translation loss		-	-	-	(4.6)	-	(4.6)
Other comprehensive income - loss on short term investments	5	-	-	-	(1.0)	-	(1.0)
Share-based payment transactions		0.3	(0.2)	-	-	-	0.1
Balance at June 30, 2017		185.8	8.9	-	23.0	15.7	233.4

See accompanying notes to these consolidated financial statements.

High Arctic Energy Services Inc.

Consolidated Statements of Cash Flows

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million

	Notes	Three Months Ended June 30		Six Months Ended June 30	
		2018	2017	2018	2017
Net earnings for the period		1.8	5.0	6.2	14.0
Adjustments for non-cash items:					
Depreciation	7	6.4	6.5	12.8	12.9
Amortization for onerous lease		(0.1)	(0.1)	(0.2)	(0.2)
Share-based compensation	15	0.2	0.1	0.8	0.1
Gain on sale of property and equipment	7	(0.2)	-	(0.2)	-
Foreign exchange (gain) loss		0.3	-	0.7	(0.1)
Deferred income tax expense (recovery)		0.2	(2.4)	0.4	(0.6)
		8.6	9.1	20.5	26.1
Net changes in items of working capital	19	7.3	22.3	0.2	0.4
Net cash generated from operating activities		15.9	31.4	20.7	26.5
Investing activities					
Additions of property and equipment	7	(1.3)	(1.8)	(3.9)	(4.4)
Disposal of short term investments	5	-	-	-	0.6
Disposal of property and equipment	7	0.4	-	0.5	0.1
Net changes in items of working capital	19	(0.1)	0.2	(0.3)	0.2
Net cash used in investing activities		(1.0)	(1.6)	(3.7)	(3.5)
Financing activities					
Long-term debt proceeds	13	-	0.6	-	8.2
Long-term debt repayments	13	-	(20.0)	-	(26.1)
Dividend payments	12	(2.6)	(2.7)	(5.2)	(5.3)
Purchase of common shares for cancellation	14	(4.3)	-	(5.3)	-
Issuance of common shares, net of costs	14	0.1	0.1	0.1	0.1
Capital lease obligation payments	9	(0.1)	(0.1)	(1.1)	(0.3)
Net cash used in financing activities		(6.9)	(22.1)	(11.5)	(23.4)
Effect of exchange rate changes		0.4	(0.7)	0.5	(0.8)
Net change in cash and cash equivalents		8.4	7.0	6.0	(1.2)
Cash and cash equivalents - beginning of period		19.7	19.1	22.1	27.3
Cash and cash equivalents - end of period		28.1	26.1	28.1	26.1
Cash paid for:					
Interest		0.1	0.3	0.2	0.7
Income taxes		5.0	6.6	5.7	7.4

See accompanying notes to these consolidated financial statements.

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million, except per share amounts

1 Nature of Business

High Arctic Energy Services Inc. ("High Arctic" or "the Corporation") is incorporated under the laws of Alberta, Canada and is a publicly traded corporation listed on the Toronto Stock Exchange under the symbol "HWO". The head office of the Corporation is located at 700 – 2nd Street S.W. Suite 500, Calgary, Alberta, Canada, T2P 2W1. High Arctic's business is to provide contract drilling, completion services, equipment rentals and other oilfield services to the oil and natural gas industry in Papua New Guinea ("PNG") and Canada.

As of June 30, 2018, 21,916,634 common shares of the Corporation were owned by FBC Holdings S.A.R.L. representing 42.1% of the outstanding common shares.

2 Basis of Preparation

The consolidated financial statements ("Financial Statements") of the Corporation have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") applicable to the preparation of interim financial statements, including IAS 34 – Interim Financial Reporting ("IAS 34"). These Financial Statements should be read in conjunction with High Arctic's consolidated financial statements for the year ended December 31, 2017 wherein the Corporation's significant accounting policies were presented in Note 3. The significant accounting policies have been consistently applied in the preparation of these Financial Statements except for Note 3 Changes in Accounting Policies – "Impact of Adoption of IFRS 15".

The Financial Statements of High Arctic for the three and six months ended June 30, 2018 were approved by the Board of Directors on August 9, 2018.

3 Changes in Accounting Policies

Impact of Adoption of IFRS 15

The Corporation has adopted, as of January 1, 2018, all the requirements of IFRS 15, *Revenue from Contracts with Customers* replacing IAS 11, *Construction Contracts*, IAS 18, *Revenue* and several revenue related interpretations. The Corporation has elected to adopt the standard using the modified retrospective approach, which requires the cumulative effect of adopting IFRS 15 to be recognized in retained earnings as of January 1, 2018. Adoption of this standard did not result in a cumulative adjustment as there is no change to the timing or amount of revenue recognition under the new policy. The main area of change is the additional disclosure requirements.

The following outlines the Corporation's revenue recognition policy under IFRS 15:

Revenue Recognition

Revenue is measured based on the consideration specified in a contract with a customer based upon an agreed transaction price with a customer. The Corporation's revenue is primarily generated from short term or spot market contracts. Long term contracts are those with a term greater than one year. Revenue from the rendering of services is recognized as the Corporation satisfies its performance obligations in contracts with customers, which is generally over time, as the Corporation provides its services on a per billable day or hourly basis.

A portion of the Corporation's revenue is lease revenue and not within the scope of IFRS 15 as a portion of the revenue received represents the customer's ability to direct the use of the Corporation's asset. The Corporation has applied judgement to determine the amount of revenue that relates to lease revenue when lease rates were not specifically identified in contracts based on an expected cost-plus margin.

The Corporation recognizes the incremental costs of obtaining a contract as an expense when incurred if the related contract is one year or less. The Corporation's revenue transactions do not contain significant financing components and the Corporation does not adjust transaction prices for the effects of a significant financing component when the period between the transfer of the promised service to the customer and the payment by the customer is less than one year. The Corporation does not disclose information related to performance obligations that have an original duration of one year or less.

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million, except per share amounts

4 Accounts Receivable

The Corporation applies the simplified approach to providing for expected credit losses as prescribed by IFRS 9, which permits the use of lifetime expected credit loss provision for all trade receivables.

	June 30, 2018	December 31, 2017
Less than 31 days	27.3	18.0
31 to 60 days	4.2	13.7
61 to 90 days	4.4	5.7
Greater than 90 days	4.9	3.1
Allowance for doubtful accounts	(0.1)	(0.1)
Total	40.7	40.4

The Corporation's accounts receivable are denominated in the following currencies:

Canadian dollar (in millions)	13.0	16.1
United States dollar (in millions) (2018 - US \$20.5; 2017 - US \$19.4)	27.7	24.3
Total	40.7	40.4

High Arctic determined the loss provision percentages used in the provision matrix based on historical credit loss experience as well as Historical Global Default rates for investment grade and speculative grade companies as published by Standard and Poor's. The expected credit losses also incorporate forward looking information.

Total receivable	Less than 31 days	31 to 60 days	61-90 days	Over 90 days	Total
Investment grade receivables	24.2	3.5	4.3	4.6	36.6
Non-investment grade receivables	3.1	0.7	0.1	0.3	4.2
Total receivables	27.3	4.2	4.4	4.9	40.8
Expected credit loss for investment grade	0.04%	0.06%	0.10%	0.30%	0.50%
Expected credit loss for non-investment grade	0.75%	1.00%	2.00%	4.00%	7.75%
Investment grade expected credit loss provision	(0.01)	-	-	(0.01)	(0.02)
Non-investment grade expected credit loss provision	(0.02)	(0.01)	-	(0.01)	(0.04)
Total allowance for doubtful accounts	(0.03)	(0.01)	-	(0.02)	(0.06)

5 Short Term Investments

High Arctic periodically invests in the common shares and debt instruments of certain publicly traded oil and gas service companies. As at June 30, 2018, the investments are presented at a fair value of \$1.9 million (December 31, 2017 - \$2.4 million) which is \$1.9 million (December 31, 2017 - \$1.4 million) less than the original cost. The difference in fair value of \$1.9 million has been included in accumulated other comprehensive income. For the three and six months ended June 30, 2018, an increase in fair value of \$0.2 million and decrease in fair value of \$0.5 million, respectively, have been included in other comprehensive income.

Short term investments consist of the following:

	June 30, 2018	December 31, 2017
Investments in equity securities	1.9	2.4
Total	1.9	2.4

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million, except per share amounts

6 Inventory

As at June 30, 2018 the Corporation had inventory of \$10.7 million (December 31, 2017 - \$10.0 million), which is primarily comprised of parts and materials related to maintenance, recertification and refurbishment of rigs and rig-related equipment. During the three and six months ended June 30, 2018, the Corporation did not recognize an impairment on inventory items (2017 – nil).

7 Property and Equipment

The following tables provide a continuity of the property and equipment costs, net of impairment and accumulated depreciation, and provide details of the effects of foreign currency translation for the six months ended June 30, 2018 and year ended December 31, 2017.

Cost:	Vehicles	Oilfield Equipment	Computer hardware and office equipment	Land & Building	Work-in- progress	Total
Balance, January 1, 2017	13.6	325.8	3.0	13.3	1.4	357.1
Additions	-	-	-	-	6.8	6.8
Finance lease obligation (note 9)	0.7	-	-	-	-	0.7
Disposals	(3.3)	(5.4)	-	-	-	(8.7)
Transfers	0.2	5.9	0.2	-	(6.3)	-
Effect of foreign exchange	(0.1)	(11.8)	-	-	-	(11.9)
Balance, December 31, 2017	11.1	314.5	3.2	13.3	1.9	344.0
Additions	-	-	-	-	3.9	3.9
Disposals	(0.4)	(0.2)	(0.1)	-	-	(0.7)
Transfers	-	3.9	0.2	-	(4.1)	-
Effect of foreign exchange	-	8.4	-	-	-	8.4
Balance, June 30, 2018	10.7	326.6	3.3	13.3	1.7	355.6

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million, except per share amounts

Accumulated depreciation and impairments:	Computer hardware and office equipment					Total
	Vehicles	Oilfield Equipment	Land & Building	Work-in-progress		
Balance, January 1, 2017	9.5	135.6	2.4	0.4	-	147.9
Depreciation for the year	1.2	23.8	0.5	0.4	-	25.9
Disposals	(3.1)	(4.6)	-	-	-	(7.7)
Effect of foreign exchange	(0.1)	(4.9)	-	-	-	(5.0)
Balance, December 31, 2017	7.5	149.9	2.9	0.8	-	161.1
Depreciation for the period	0.4	12.2	0.1	0.1	-	12.8
Disposals	(0.3)	(0.1)	-	-	-	(0.4)
Effect of foreign exchange	-	4.0	-	-	-	4.0
Balance, June 30, 2018	7.6	166.0	3.0	0.9	-	177.5

Carrying amounts of property and equipment:

At December 31, 2017	3.6	164.6	0.3	12.5	1.9	182.9
At June 30, 2018	3.1	160.6	0.3	12.4	1.7	178.1

8 Accounts Payable and Accrued Liabilities

	June 30, 2018	December 31, 2017
Accounts payable	8.7	5.4
Accrued liabilities	8.6	11.0
Accrued payroll	1.6	2.6
NCIB share repurchase (note 14)	2.2	-
Income taxes payable	0.8	0.7
Current portion - finance lease obligation (note 9)	0.2	1.2
Current portion - unfavourable lease liability (note 10)	0.4	0.4
Onerous lease liability	0.1	0.2
Total	22.6	21.5

9 Finance Lease Obligation

During 2017, the Corporation recognized vehicles under a finance lease arrangement with lease terms of three years. As at June 30, 2018, future minimum lease payments totaled \$0.6 million, of which \$0.2 million has been included in the current portion of finance lease obligations as part of accounts payable and accrued liabilities and the remaining \$0.4 million has been disclosed as a non-current liability (December 31, 2017 – \$0.5 million).

During 2016, the Corporation received certain equipment under a finance lease with a purchase option after a twelve month lease term as well as an option to extend the lease term by an additional twelve months. The fair value of the equipment of \$2.5 million has been included with property and equipment with a corresponding lease obligation liability that is reduced by the principal portion of the monthly payments related to the principal of the lease.

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million, except per share amounts

During the first quarter of 2018, the Corporation exercised the option to purchase the leased equipment upon expiry of the lease term for \$0.9 million (December 31, 2017 - \$1.0 million).

10 Unfavourable Lease

On August 31, 2016, High Arctic acquired the Production Services Division of Tervita. The acquisition was accounted for as a business combination using the acquisition method of accounting whereby the assets acquired and the liabilities assumed are recorded at estimated fair value on the acquisition date. The Corporation assumed a real estate lease as part of the Tervita acquisition that was assessed to be unfavourable as the contracted lease rates were unfavourable relative to market rates, resulting in an unfavourable lease liability of \$3.3 million as at June 30, 2018, of which \$0.4 million has been included in the current portion of accounts payable and accrued liabilities and the remaining \$2.9 million has been disclosed as a non-current liability (December 31, 2017 - \$3.1 million).

11 Deferred Revenue

Pursuant to contracts primarily related to the provision of drilling rigs, the Corporation has received payments that will be recognized as revenue in future periods over the life of the related contracts. As at June 30, 2018, \$0.5 million will be recognized as revenue in the next twelve months and has been disclosed as a current liability (December 31, 2017 - \$1.0 million) with no amounts remaining as a non-current liability (December 31, 2017 - nil).

12 Dividend Payable

Dividends are recorded as a liability on the date of declaration by the Corporation's Board of Directors. During the six months ended June 30, 2018, the Corporation declared dividends of \$5.2 million (2017 - \$5.3 million), of which \$0.9 million was payable as of June 30, 2018 (December 31, 2017 - \$0.9 million). Since June 30, 2018, a monthly dividend of \$0.0165 per share has been declared for a total of \$0.9 million.

13 Long-Term Debt

In the first quarter of 2017, High Arctic renewed its existing credit facility. As at June 30, 2018, High Arctic's credit facilities consisted of a \$45.0 million revolving loan facility which matures on August 31, 2019. The facility is renewable with the lender's consent and is secured by a general security agreement over the Corporation's assets.

The available amount under the \$45.0 million revolving loan facility is limited to 60% of the net book value of the Canadian fixed assets plus 75% of acceptable accounts receivable (85% for investment grade receivables), plus 90% of insured receivables, less priority payables as defined in the loan agreement. As at June 30, 2018, no amounts were outstanding on the credit facility (December 31, 2017 - nil) and total credit available to draw was \$45.0 million.

The Corporation's loan facilities are subject to three financial covenants, which are reported to the lender on a quarterly basis:

Covenants	Required	June 30, 2018
Funded debt to EBITDA ⁽¹⁾ ⁽⁴⁾	2.50 : 1 Maximum	0.01 : 1
Current ratio ⁽²⁾	1.25 : 1 Minimum	3.50 : 1
Fixed charge coverage ratio ⁽³⁾	1.25 : 1 Minimum	34.57 : 1

⁽¹⁾ Funded debt to EBITDA is defined as the ratio of consolidated Funded Debt to the aggregate covenant EBITDA for the trailing four quarters.

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million, except per share amounts

- (2) Current ratio is defined as the ratio of consolidated current assets to consolidated net current liabilities (excluding current portion of long-term debt and other debt, if any).
- (3) Fixed charge coverage ratio is defined as covenant EBITDA less cash taxes, dividends, distributions and unfunded capital expenditures divided by the total of principal payments on long term debt and capital leases, in which principal payments means the total principal amount of the loan outstanding at the end of the quarter amortized over a 7-year period.
- (4) EBITDA for the purposes of calculating the covenants, "covenant EBITDA," is defined as net income plus interest expense, current tax expense, depreciation, amortization, future income tax expense (recovery), share-based compensation expense less gains from foreign exchange and sale or purchase of assets.

There have been no changes to these financial covenants subsequent to June 30, 2018 and the Corporation remains in compliance with the financial covenants under its credit facility as at June 30, 2018.

14 Share Capital and Other Components of Equity

(a) Share Capital

Authorized – an unlimited number of common shares and an unlimited number of preferred shares.

Issued:	Six months ended June 30, 2018		Year ended December 31, 2017	
	Shares	\$	Shares	\$
Balance, beginning of year	53,331,039	186.0	53,174,369	185.4
Issuance of shares upon exercise of options (note 15)	43,000	0.2	150,070	0.6
Normal course issuer bid (note 14)	(1,367,427)	(4.7)	-	-
Vested restricted shares (note 15)	20,000	0.1	6,600	-
Common shares outstanding	52,026,612	181.6	53,331,039	186.0
Unvested restricted shares outstanding (note 15)	-	-	20,000	0.1
Total common and restricted shares outstanding	52,026,612	181.6	53,351,039	186.1

Issuance of Shares

For the six months ended June 30, 2018 a total of 43,000 (year ended December 31, 2017 – 150,070) stock options were exercised for shares of the Corporation (see note 15).

Normal Course Issuer Bid

In September 2017, the Corporation received approval from the Toronto Stock Exchange to acquire for cancellation up to 2,902,733 common shares, representing 5 percent of the Corporation's issued and outstanding common shares under a Normal Course Issuer Bid ("the Bid"). The Bid commenced on September 19, 2017 and is valid for one year. During the six months ended June 30, 2018, the Corporation repurchased 1,367,427 common shares under the Bid at an average price of \$3.91 per share, for a total repurchase cost of \$5.3 million.

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million, except per share amounts

The following table summarizes the share repurchase activities during the period:

	Six months ended June 30, 2018
Shares repurchased	1,367,427
Amounts charged to	
Share capital	4.7
Contributed surplus	0.6
Share repurchase cost	5.3

Under an automatic repurchase plan agreement with an independent broker, the Corporation has recorded the following liability for share repurchases that may take place during its internal blackout period:

	June 30, 2018
Amounts charged to	
NCIB Equity	2.2
Liability for share repurchase commitment	2.2

(b) Per Share Amounts

The following table summarizes the weighted average number of common shares used in calculating basic and diluted earnings per share. All potentially dilutive instruments such as options, RSUs, PSUs, DSUs and the restricted shares issued under the Executive and Director Share Incentive Plan are considered.

	Six months ended June 30, 2018		Six months ended June 30, 2017	
	Number of Shares	Earnings per Share	Number of Shares	Earnings per Share
Weighted average number of common shares used in basic earnings per share	52,922,012	\$0.12	53,204,339	\$0.26
Dilution effect of options, DSUs, RSUs and PSUs	486,636	-	417,320	-
Weighted average number of common shares used in diluted earnings per share	53,408,648	\$0.12	53,621,659	\$0.26
	Three months ended June 30, 2018		Three months ended June 30, 2017	
	Number of Shares	Earnings per Share	Number of Shares	Earnings per Share
Weighted average number of common shares used in basic earnings per share	52,518,391	\$0.04	53,232,296	\$0.09
Dilution effect of options, DSUs, RSUs and PSUs	470,504	-	331,938	-
Weighted average number of common shares used in diluted earnings per share	52,988,895	\$0.04	53,564,234	\$0.09

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million, except per share amounts

For the six months ended June 30, 2018, 460,800 stock options (2017 – nil) were excluded in the calculation of diluted earnings per share as the effect would have been anti-dilutive.

15 Share-based Compensation

The Corporation has various equity based compensation plans under which the Corporation may issue up to 5,202,661 common shares (being 10% of all outstanding shares) as at June 30, 2018. The following table summarizes the Corporation's outstanding grants for each equity based compensation plan.

	June 30, 2018	December 31, 2017
Stock Options	1,993,800	2,020,800
Employee and Director Share Units	-	20,000
Restricted Share Units	177,307	106,269
Performance Share Units	208,933	100,430
Deferred Share Units	154,928	52,541
Balance, end of period	<u>2,534,968</u>	<u>2,300,040</u>
Common shares available for grants	5,202,661	5,335,104
Percentage used of total available	<u>49%</u>	<u>43%</u>
Remaining common shares available for grants	<u>2,667,693</u>	<u>3,035,064</u>

Stock Option Plan

The Corporation has a Stock Option Plan under which options to purchase common shares may be granted to directors, management and certain employees. At June 30, 2018, a total of 1,993,800 options are outstanding and expire at various dates up to 2023, at amounts that range from \$2.83 to \$5.32 per share. These options are exercisable over a term of 5 years and are generally subject to a three year vesting period with 40% exercisable by the holder after the first anniversary date, 70% after the second anniversary date and 100% after the third anniversary date. The options have an average remaining contractual life of 2.5 years and 1,260,800 options are currently vested and eligible to be exercised.

	Number of Options	Weighted Average Exercise Price \$/Share
Total Outstanding January 1, 2017	1,851,600	4.04
Granted	605,000	3.91
Exercised	(150,070)	3.14
Forfeited	(167,130)	4.27
Expired	(118,600)	5.13
Total Outstanding December 31, 2017	<u>2,020,800</u>	<u>3.99</u>
Granted	265,000	3.86
Exercised	(43,000)	2.66
Forfeited	(235,000)	3.92
Expired	(14,000)	5.29
Total Outstanding June 30, 2018	<u>1,993,800</u>	<u>4.00</u>

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million, except per share amounts

The options exercised in 2018 had a weighted average market price of \$3.90 per share on the date of exercise.

Exercise Price Range	Options Outstanding			Exercisable Options	
	Number of Options	Remaining Contractual Life (Years)	Weighted Average Exercise Price (\$)	Number of Options	Weighted Average Exercise Price (\$)
\$2.83 to \$3.39	415,000	0.4	3.29	415,000	3.29
\$3.46 to \$3.67	185,000	2.3	3.57	179,000	3.57
\$3.75 to \$4.77	941,000	4.1	3.79	229,000	3.80
\$4.92 to \$5.32	452,800	1.2	5.24	437,800	5.25

Share-based compensation associated with stock options is a non-cash item and is measured in accordance with a prescribed formula. Share-based compensation expense recognized by the Corporation for the Stock Option Plan for the six months ended June 30, 2018 was \$0.1 million (2017 – less than \$0.1 million). The fair values of stock options granted have been estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions:

Period of Grant	Six months ended June 30, 2018	Six months ended June 30, 2017
Average fair value per option granted	0.70	0.83
Average expected life (years)	3.7	3.0
Expected volatility (%)	35	36
Expected forfeiture rate (%)	19	27
Average risk-free interest rate (%)	1.90	0.85
Expected distribution yield (%)	5.1	3.9

Performance Share Unit Plan

On May 10, 2017, the Corporation's shareholders approved a Performance Share Unit Plan (the "PSUP"). Under the PSUP the Corporation is able to grant share units to employees which upon vesting will be settled through the issuance of common shares of the Corporation.

At the discretion of the Board of Directors, certain vesting criteria may be applied to the share units granted. Under the PSUP, the Corporation intends to grant share units which have performance vesting conditions, referred to as Performance Share Units ("PSUs") and other units which, unless otherwise directed by the Board of Directors, vest one third on each of the first, second and third anniversaries from the date of grant, referred to as Restricted Share Units ("RSUs").

The number of RSUs and PSUs outstanding are proportionately adjusted for any dividends declared on the Corporation's common shares during the period the RSUs and PSUs are outstanding.

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million, except per share amounts

	RSUs	PSUs	Total
Total Outstanding January 1, 2017	-	-	-
Granted	105,000	99,999	204,999
Reinvested dividends	1,269	431	1,700
Total Outstanding December 31, 2017	106,269	100,430	206,699
Granted	77,500	150,000	227,500
Reinvested dividends	3,621	3,777	7,398
Forfeited	(10,083)	(45,274)	(55,357)
Total Outstanding June 30, 2018	177,307	208,933	386,240

During the six months ended June 30, 2018, 150,000 Performance Share Units (“PSUs”) and 77,500 Restricted Share Units (“RSUs”) were granted. For the six months ended June 30, 2018 the Corporation incurred \$0.3 million of share-based compensation expense (2017 – nil) related to the 386,240 units issued under the PSUP and an amount of \$0.9 million remains to be amortized in future periods in respect of the PSUP plan.

Deferred Share Units

In 2017, the Corporation’s shareholders approved a deferred share unit plan (the “DSU”) for non-employee members of the Board of Directors. Under the terms of the plan, DSUs awarded will vest immediately and may be settled through the issuance of common shares of the Corporation upon the holder ceasing to serve as a member of the Board of Directors and is not an employee of the Corporation.

The number of DSUs outstanding are proportionately adjusted for any dividends declared on the Corporation’s common shares during the period the DSUs are outstanding.

	Six months ended June 30, 2018	Year ended December 31, 2017
Total Outstanding January 1, 2018	52,541	-
Granted	100,000	52,500
Reinvested dividends	2,387	41
Total Outstanding June 30, 2018	154,928	52,541

For the six months ended June 30, 2018, the Corporation incurred share-based compensation expense of \$0.4 million related to the 154,928 DSUs outstanding (2017 – nil).

Executive and Director Share Incentive Plan

Prior to the establishment of the PSUP the Corporation maintained an Executive and Director Share Incentive Plan (“EDSIP”) that was approved by the shareholders in 2010. Upon approval of the PSUP, no further grants were made under the EDSIP and the plan was terminated during the second quarter of 2018 upon the release of the remaining EDSIPs under the plan.

During the six months ended June 30, 2018, 20,000 shares issued under the EDSIP vested and were released. For the six months ended June 30, 2018, the Corporation incurred share-based compensation expense of less than \$0.1 million (2017 – less than \$0.1 million) related to the EDSIP and no amounts remain to be amortized in future periods. A forfeiture rate of nil has been assumed in the share-based compensation expense assumptions with the expense adjusted when actual forfeitures occur.

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million, except per share amounts

Cash Settled Restricted Shares Units

Prior to the establishment of the PSUP, the Corporation issued cash settled restricted share units ("CSRSUs") to certain employees. For the six months ended June 30, 2018, the Corporation incurred \$0.1 million of share-based compensation expense (2017 – less than \$0.1 million) related to the 140,000 CSRSUs outstanding and an amount of \$0.1 million (before recognizing a reduction for any future forfeitures and effect of future revaluation) remains to be amortized in future periods in respect of the CSRSUs.

16 Revenue

The following table includes a reconciliation of disaggregated revenue by reportable segment (Note 23). Revenue has been disaggregated by primary geographic location, type of service provided and the amount that relates to lease revenue.

Revenue by Geography Three months ended June 30, 2018	Drilling Services	Production Services	Ancillary Services	Inter-Segment Elimination	Total
Canada	-	16.0	0.7	-	16.7
PNG	8.8	-	-	-	8.8
Revenue from contracts with customers	8.8	16.0	0.7	-	25.5
Operating lease revenue	14.4	2.0	6.1	(0.9)	21.6
Total revenue	23.2	18.0	6.8	(0.9)	47.1

Revenue by Geography Three months ended June 30, 2017	Drilling Services	Production Services	Ancillary Services	Inter-Segment Elimination	Total
Canada	-	15.2	1.4	-	16.6
PNG	12.7	-	-	-	12.7
Revenue from contracts with customers	12.7	15.2	1.4	-	29.3
Operating lease revenue	15.6	1.6	5.4	(0.8)	21.8
Total revenue	28.3	16.8	6.8	(0.8)	51.1

Revenue by Geography Six months ended June 30, 2018	Drilling Services	Production Services	Ancillary Services	Inter-Segment Elimination	Total
Canada	-	37.3	1.8	-	39.1
PNG	21.0	-	-	-	21.0
Revenue from contracts with customers	21.0	37.3	1.8	-	60.1
Operating lease revenue	25.7	4.0	12.8	(1.8)	40.7
Total revenue	46.7	41.3	14.6	(1.8)	100.8

Revenue by Geography Six months ended June 30, 2017	Drilling Services	Production Services	Ancillary Services	Inter-Segment Elimination	Total
Canada	-	36.0	3.0	-	39.0
PNG	29.9	-	-	-	29.9
Revenue from contracts with customers	29.9	36.0	3.0	-	68.9
Operating lease revenue	32.7	3.3	12.6	(1.6)	47.0
Total revenue	62.6	39.3	15.6	(1.6)	115.9

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million, except per share amounts

17 Expenses

Oilfield services expenses by nature:	Three months ended June 30		Six months ended June 30	
	2018	2017	2018	2017
Personnel costs and personnel related costs	16.7	17.6	36.4	39.5
Drilling rig rental costs	4.3	4.2	9.1	9.4
Material and supplies costs	3.1	6.0	7.9	12.7
Equipment operating and maintenance costs	3.5	3.4	8.6	7.7
Other	1.1	1.2	2.4	2.4
Total	28.7	32.4	64.4	71.7

General and administrative expenses by nature:	Three months ended June 30		Six months ended June 30	
	2018	2017	2018	2017
Personnel costs and personnel related costs	3.3	3.4	6.6	6.9
Professional, legal and consulting fees	0.5	0.4	0.7	0.9
Facility costs	0.1	0.1	0.2	0.2
Leases	0.2	0.2	0.5	0.4
Other	0.4	0.3	0.8	0.5
Total	4.5	4.4	8.8	8.9

18 Other Expenses

During the second quarter of 2018, the Corporation closed its Blackfalds facility and consolidated these operations with its Acheson facility in an effort to reduce costs and better position the operations closer to areas of field activity. High Arctic incurred \$0.6 million in expenses associated with the facility closure, of which majority relate to severance and equipment hauling expenses.

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million, except per share amounts

19 Supplemental Cash Flow Information

Changes in non-cash working capital is comprised of:

	Note	Three months ended June 30		Six months ended June 30	
		2018	2017	2018	2017
Accounts receivable	4	9.8	38.5	2.9	11.9
Inventory and prepaid expenses		(0.7)	(1.3)	(0.7)	(1.7)
Accounts payable and accrued liabilities	9	(0.8)	(13.1)	(2.0)	(10.1)
Income taxes payable		(0.7)	(0.2)	0.2	2.4
Deferred revenue	11	(0.4)	(1.4)	(0.5)	(1.9)
Total		7.2	22.5	(0.1)	0.6
Related to:					
Operating activities		7.3	22.3	0.2	0.4
Investing activities		(0.1)	0.2	(0.3)	0.2
		7.2	22.5	(0.1)	0.6

20 Commitments and Contingencies

Inventory

As part of the Corporation's contractual rig management and operations, the Corporation has been supplied an inventory of spare parts with a total value of \$9.0 million by a customer and a third-party supplier for the Corporation's operations in PNG. The inventory is owned by these parties and has not been recorded on the books of High Arctic. At the end of the contracts, the Corporation must return an equivalent amount of inventory to these parties. The Corporation recorded a provision of \$0.7 million during 2016 within accrued liabilities to account for a potential shortfall in inventory, which may require cash settlement.

Finance and Operating Lease Obligations

The Corporation has entered into long-term premise leases for operating facilities. These leases are operating leases and the remaining length of the lease terms are up to fourteen years. All the premise leases have renewal terms which allow the Corporation to renew the lease for various lengths at the market rates negotiated at the time of renewal. The minimum lease payments for the next fourteen years as at June 30, 2018 are:

	1 Year	2-3 Years	4-5 Years	Beyond 5 Years	Total
Facility and equipment lease commitments	1.7	2.6	1.9	8.3	14.5
Total lease commitments	1.7	2.6	1.9	8.3	14.5

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million, except per share amounts

21 Capital Disclosures

The Corporation's capital structure is comprised of shareholders' equity and long term debt less cash and cash equivalents.

	June 30, 2018	December 31, 2017
Shareholder's equity	231.7	230.8
Long-term debt	-	-
Cash and cash equivalents	(28.1)	(22.1)
Total Capitalization	203.6	208.7

The Corporation's goal is to have a capital structure that will provide the capital to meet the needs of its business and instil confidence with investors, creditors and capital markets.

Financing decisions for the foreseeable future will be governed largely by managing the available cash and liquidity available under the Corporation's credit facilities based on the timing and extent of expected operating and capital cash outlays. Future equity and debt financings are a possibility to raise capital for new business opportunities.

22 Financial Instruments and Risk Management

Fair Value of Financial Assets and Liabilities

Cash and cash equivalents include cash and term deposits and are classified as financial assets at fair value through profit and loss. Cash and cash equivalents are measured at fair value and unrealized gains or losses related to changes in fair value are reported in income. Accounts receivable, and other receivables are classified as assets at amortized cost using the effective interest method, less impairment allowance, if any. Any gains or losses on the realization of loans and receivables are included in earnings. The fair value of accounts and other receivables approximate their carrying values due to the short-term nature of these instruments.

The Corporation's short-term investments are designated as financial assets at fair value through other comprehensive income and are initially recognized at fair value on the settlement date, net of directly attributable transaction costs. Future changes in fair value are recognized in other comprehensive income (OCI), net of tax and are not recycled into income. Financial assets at fair value comprise listed Canadian public company investment. These assets are carried at fair value on the Consolidated Statements of Financial Position. Fair value is determined by quoted prices in active markets for identical assets (Level 1).

Accounts payable, accrued liabilities, dividends payable and the long-term debt are designated as other liabilities and are recorded at amortized cost.

Financial and Other Risks

The Corporation is exposed to financial risks arising from its financial assets and liabilities. The financial risks include market risk relating to interest rate risk, foreign currency risk, commodity price risk, risks of foreign operations, income tax risk, credit risk and liquidity risk.

Market Risk

Market risk is the risk that the fair value or future cash flows of financial assets or liabilities will fluctuate due to movements in market rates of interest, foreign currency exchange rates and commodity prices.

Other Price Risk

Other price risk is the risk that the fair value or future cash flows of financial instruments will fluctuate as a result of changes in market prices (other than those arising from interest rate risk or foreign currency risk) whether those changes are caused by factors specific to the individual financial instrument, its issuer or factors affecting all

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million, except per share amounts

similar financial instruments in the market or a market segment. Exposure to other price risk is primarily in short term investments where changes in quoted prices on investments in equity securities impact the underlying value of investments.

Interest Rate Risk

Interest rate risk is the risk that the value of a financial instrument will fluctuate as a result of changes in market interest rates. The Corporation is exposed to interest rate risk as the long term debt is a floating rate credit facility and fluctuates in response to changes in the prime interest rates.

Foreign Currency Risk

Foreign currency risk is the risk that a variation in the exchange rate between Canadian and foreign currencies will affect the Corporation's results. The majority of the Corporation's international revenue and expenses are transacted in U.S. dollars and the Corporation does not actively engage in foreign currency hedging. For the six months ended June 30, 2018, a \$0.10 change in the value of the Canadian dollar relative to the U.S. dollar would have resulted in a \$0.8 million change in net earnings for the year as a result of changes in foreign exchange.

Credit Risk and Customers

Credit risk is the risk of a financial loss occurring as a result of a default by a counter party on its obligation to the Corporation. The Corporation's financial instruments that are exposed to credit risk consist primarily of accounts receivable and cash balances held in banks. The Corporation mitigates credit risk by regularly monitoring its accounts receivable position and depositing cash in properly capitalized banks. The Corporation also institutes credit reviews prior to commencement of contractual arrangements.

The Corporation's accounts receivable are predominantly with customers who explore for and develop petroleum reserves and are subject to normal industry credit risks. The Corporation assesses the credit worthiness of its customers on an ongoing basis and monitors the amount and age of balances outstanding. The Corporation applies the simplified approach to providing for expected credit losses prescribed by IFRS 9, which permits the use of the lifetime expected loss provision for all trade receivables. The Corporation uses the historical default rates within the industry between investment grade and non-investment grade customers as well as forward looking information to determine the appropriate loss allowance provision.

The Corporation views the credit risks on these amounts as normal for the industry. The carrying amount of accounts receivable represents the maximum credit exposure on this balance. The Corporation has a wide range of customers comprised of small independent, intermediate and large multinational oil and gas producers. Notwithstanding its large customer base, the Corporation provides services to three large multinational/regional customers (2017 – four) which individually accounted for greater than 10% of its consolidated revenues during the six months ended June 30, 2018. Sales to these three customers were approximately \$41.4 million, \$13.6 million and \$11.1 million for the six months ended June 30, 2018 (2017 - \$30.4 million, \$14.7 million and \$9.6 million). As at June 30, 2018, these three customers represented 53%, 12% and 6%, respectively, of outstanding accounts receivable (December 31, 2017 – three customers represented a total of 60%). Management has assessed the three customers as creditworthy and the Corporation has had no history of collection issues with these customers.

Liquidity Risk

Liquidity risk is the risk that the Corporation will not be able to meet its financial obligations as they fall due. The Corporation's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due. The Corporation's processes for managing liquidity risk include preparing and monitoring capital and operating budgets, coordinating and authorizing project expenditures, and authorization of contractual agreements. The Corporation seeks to manage its financing based on the results of these processes. The following are the contractual maturities of financial liabilities in their future fair value amounts:

June 30, 2018	Beyond 5				Total
	1 Year	2-3 Years	4-5 Years	Years	
Accounts payable	22.6	-	-	-	22.6
Dividends payable	0.9	-	-	-	0.9
Total	23.5	-	-	-	23.5

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million, except per share amounts

December 31, 2017	Beyond 5				
	1 Year	2-3 Years	4-5 Years	Years	Total
Accounts payable	21.5	-	-	-	21.5
Dividends payable	0.9	-	-	-	0.9
Total	22.4	-	-	-	22.4

23 Operating Segments

The Corporation determines its operating segments based on internal information reviewed by the Board of Directors to allocate resources and assess performance. The Corporation's reportable operating segments, as determined by management, are strategic operating units that offer different products and services. The accounting policies for each reportable segment are the same as those described in Note 3 of High Arctic's consolidated financial statements for the year ended December 31, 2017. The Corporation operates in two geographic areas and four operating segments as follows:

Drilling Services

This segment currently consists of the Corporation's drilling services provided in PNG.

Production Services

This segment currently consists of the Corporation's well servicing and snubbing services provided in Canada.

Ancillary Services

Ancillary services segment consists of High Arctic's oilfield rental equipment in Canada and PNG as well as its Canadian nitrogen and compliance consulting services.

Corporate

The Corporate segment provides management and administrative services to all of the Corporation's operations and subsidiaries.

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million, except per share amounts

Three months ended June 30, 2018	Drilling Services	Production Services	Ancillary Services	Corporate	Inter- Segment Elimination	Total
Revenue	23.2	18.0	6.8	-	(0.9)	47.1
Expenses						
Oilfield Services	12.6	14.7	2.3	-	(0.9)	28.7
General and administrative	1.7	1.5	0.2	1.1	-	4.5
Depreciation	2.4	2.5	1.5	-	-	6.4
Share-based compensation	-	-	-	0.3	-	0.3
	16.7	18.7	4.0	1.4	(0.9)	39.9
Operating earnings (losses) for the period	6.5	(0.7)	2.8	(1.4)	-	7.2
Other expenses	-	-	-	0.6	-	0.6
Foreign exchange loss	-	-	-	0.3	-	0.3
Gain on sale of assets	-	-	-	(0.2)	-	(0.2)
Interest and finance expense	-	-	-	0.1	-	0.1
Earnings (losses) before income tax	6.5	(0.7)	2.8	(2.2)	-	6.4
Property and equipment	66.5	78.0	33.4	0.2	-	178.1
Total assets less deferred tax assets	111.9	99.5	48.4	2.2	-	262.0
Three months ended June 30, 2017	Drilling Services	Production Services	Ancillary Services	Corporate	Inter- Segment Elimination	Total
Revenue	28.3	16.8	6.8	-	(0.8)	51.1
Expenses						
Oilfield Services	16.1	14.4	2.7	-	(0.8)	32.4
General and administrative	1.4	1.7	0.4	0.9	-	4.4
Depreciation	2.5	2.4	1.6	-	-	6.5
Share-based compensation	-	-	-	-	-	-
	20.0	18.5	4.7	0.9	(0.8)	43.3
Operating earnings (losses) for the period	8.3	(1.7)	2.1	(0.9)	-	7.8
Foreign exchange gain	-	-	-	(0.2)	-	(0.2)
Interest and finance expense	-	-	-	0.3	-	0.3
Earnings (losses) before income tax	8.3	(1.7)	2.1	(1.0)	-	7.7
Property and equipment	75.0	85.5	36.3	0.2	-	197.0
Total assets less deferred tax assets	128.5	96.8	45.1	3.4	-	273.8

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million, except per share amounts

Six months ended June 30, 2018	Drilling Services	Production Services	Ancillary Services	Corporate	Inter- Segment Elimination	Total
Revenue	46.7	41.3	14.6	-	(1.8)	100.8
Expenses						
Oilfield Services	27.1	33.9	5.2	-	(1.8)	64.4
General and administrative	3.2	3.0	0.5	2.1	-	8.8
Depreciation	4.8	5.2	2.8	-	-	12.8
Share-based compensation	-	-	-	0.9	-	0.9
	35.1	42.1	8.5	3.0	(1.8)	86.9
Operating earnings (losses) for the period	11.6	(0.8)	6.1	(3.0)	-	13.9
Other expenses	-	-	-	0.6	-	0.6
Foreign exchange loss	-	-	-	0.7	-	0.7
Gain on sale of assets	-	-	-	(0.2)	-	(0.2)
Interest and finance expense	-	-	-	0.2	-	0.2
Earnings (losses) before income tax	11.6	(0.8)	6.1	(4.3)	-	12.6
Property and equipment	66.5	78.0	33.4	0.2	-	178.1
Total assets less deferred tax assets	111.9	99.5	48.4	2.2	-	262.0
Six months ended June 30, 2017	Drilling Services	Production Services	Ancillary Services	Corporate	Inter- Segment Elimination	Total
Revenue	62.6	39.3	15.6	-	(1.6)	115.9
Expenses						
Oilfield Services	34.7	33.1	5.5	-	(1.6)	71.7
General and administrative	2.5	3.2	0.9	2.3	-	8.9
Depreciation	5.0	4.7	3.2	-	-	12.9
Share-based compensation	-	-	-	0.1	-	0.1
	42.2	41.0	9.6	2.4	(1.6)	93.6
Operating earnings (losses) for the period	20.4	(1.7)	6.0	(2.4)	-	22.3
Foreign exchange gain	-	-	-	(0.3)	-	(0.3)
Interest and finance expense	-	-	-	0.7	-	0.7
Earnings (losses) before income tax	20.4	(1.7)	6.0	(2.8)	-	21.9
Property and equipment	75.0	85.5	36.3	0.2	-	197.0
Total assets less deferred tax assets	128.5	96.8	45.1	3.4	-	273.8

High Arctic Energy Services Inc.

Notes to the Consolidated Financial Statements

For the three and six months ended June 30, 2018 and 2017

Unaudited - Canadian \$ Million, except per share amounts

2018	PNG	Canada	Total
Revenue for the three months ended June 30, 2018	27.7	19.4	47.1
Revenue for the six months ended June 30, 2018	55.3	45.5	100.8
Total assets less deferred tax assets at June 30, 2018	173.3	88.7	262.0

2017	PNG	Canada	Total
Revenue for the three months ended June 30, 2017	32.1	19.0	51.1
Revenue for the six months ended June 30, 2017	71.5	44.4	115.9
Total assets less deferred tax assets at June 30, 2017	159.3	114.5	273.8