CELEBRATING

20 YEARS OF

BETTER PERFORMANCE EVERY DAY

2017

ANNUAL REPORT

FIVE YEAR FINANCIAL HISTORY

Dollars in 000's except per share amounts

		2017		2016		2015 [5]		2014 [5]		2013 [5]
Revenues	**$**	**147,095**	$	80,866	$	106,243	$	208,655	$	150,850
Adjusted gross margin % [1]		**18%**		22%		18%		21%		22%
Total Adjusted EBITDAS [1]	**$**	**18,674**	$	5,840	$	7,699	$	38,487	$	32,815
Diluted per share	**$**	**0.39**	$	0.16	$	0.21	$	1.06	$	0.91
Cash flow - operating activities	**$**	**2,952**	$	4,140	$	25,931	$	36,941	$	14,026
Gain on disposal / (Write-down of) investment in associate and related assets	**$**	**-**	$	10,865	$	-	$	177	$	(13,070)
Write-downs of goodwill, equipment, intangibles and inventory	**$**	**(8,584)**	$	(277)	$	(12,773)	$	-	$	-
Write-down of deferred taxes related to CRA settlement	**$**	**-**	$	-	$	(10,346)	$	-	$	-
Earnings (loss) before income taxes	**$**	**(382)**	$	(722)	$	(24,894)	$	8,112	$	5,241
Basic and diluted per share	**$**	**(0.01)**	$	(0.02)	$	(0.69)	$	0.22	$	0.14
Net earnings (loss)	**$**	**87**	$	(5,779)	$	(35,342)	$	10,283	$	(1,542)
Basic and diluted per share	**$**	**-**	$	(0.16)	$	(0.97)	$	0.28	$	(0.04)
Cash dividends declared per share [2]	**$**	**-**	$	-	$	0.1200	$	0.3300	$	0.3075
Equipment additions [3]	**$**	**11,322**	$	899	$	6,908	$	30,763	$	28,283
Weighted average shares outstanding										
Basic (000s)		**47,381**		36,295		36,295		36,244		36,171
Diluted (000s)		**47,577**		36,295		36,295		36,255		36,241
Working capital	**$**	**31,016**	$	39,324	$	13,550	$	38,135	$	26,031
Total assets	**$**	**121,630**	$	136,017	$	155,610	$	230,534	$	205,375
Loans and borrowings excluding current portion	**$**	**46**	$	26,322	$	30,477	$	56,142	$	38,462
Shareholders' equity	**$**	**101,391**	$	90,772	$	96,607	$	128,368	$	126,612

(1) Refer to MD&A: see "NON-GAAP MEASUREMENTS"
(2) Quarterly dividend was suspended in November 2015
(3) Equipment additions exclude non-cash additions
(4) Revenues and Adjusted gross margin % for 2012 to 2017 exclude Discontinued Operations. 2012 to 2015 amounts have been restated from prior presentation. Refer to note 10 in the audited financial statements
(5) 2013 to 2015 reclassified for Discontinued Operations

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Annual General Meeting:

Shareholders are invited to attend the Annual General Meeting which will be held at 2:00 pm on May 10, 2018 at our Head Office 6030 – 3 Street SE, Calgary, Alberta.

REPORT TO SHAREHOLDERS

We are very pleased with our corporate, operations and financial achievements in 2017:

- Revenues increased 82% to $147.1 million of which 78% was from United States source.
- Total Adjusted EBITDAS increased 220% to $18.8 million.
- We eliminated our debt in early 2017 and retained a positive cash balance throughout the year.
- We reacted quickly to a significant increase in industry activity levels and we were able to diversify our client base relative to 2016.
- We continued to make improvements in our sales and operations areas to support our value proposition of providing our clients Better Performance Every Day.
- We executed on the beginning of a longer term capital expenditure and business improvement investment plan which will position us for future growth.
- We exceeded our health and safety objectives for the year.
- Based in part to the above financial achievements, our share price gained 170% from the $0.70 range at the beginning of 2017 to the $1.75 range at year end.

As noted in our 2016 annual report, 2016 was a very challenging year for Cathedral from both an operations and financial perspective. 2016 was about continuing to improve our sales and operations capabilities and retaining key clients during a severe industry downturn - while at the same time exercising very conservative fiscal management in order to improve our balance sheet. In contrast, 2017 was all about ramping up our business to meet improving drilling activity levels particularly in the United States (U.S.) which is our primary focus market.

A big achievement for us in 2017 was improving our financial position. At the end of 2016 we had made significant progress on strengthening our balance sheet with the announced divestment of our Flowback and Production Testing ("F&PT") division for proceeds of $17.8 million. The sale was a result of a strategic alternatives process entered into in mid-2016 that was largely precipitated by the commercial banks in our banking syndicate. In hindsight, the sale of the F&PT division proved to be a good decision not only based on the proceeds received but the divesture allowing us to focus all our efforts and resources on our directional drilling business which was ramping up significantly in early 2017. Following the F&PT division divestiture we also completed an equity financing in mid-February for gross proceeds of $14.1 million. As a consequence of the above financing activities and cash flow from operations we were bank debt free and maintained a positive cash balance through to the end of the year.

The strength of our balance sheet and our improving financial performance through 2017 allowed us to attract a new banking syndicate. In December 2017 we announced that we had entered into a new Credit Facility with Alberta Treasury Branches and Export Development Canada (EDC) as lenders. EDC continues to support us as they were a lender in the previous facility.

Going into 2017 we expected to be impacted by three key themes:

- continued commodity price volatility impacting activity levels;
- intense competitive pressure and continued customer attention on drilling costs - impacting pricing; and
- labour availability and vendor supply and price challenges - impacting expenses

Although we experienced commodity price volatility throughout the year, there was a strong increase in activity levels in both the U.S. and Canada. An average WTI oil price for the year of $52 bbl USD supported our previous assertion that WTI pricing in the $50 bbl range and above would translate into improved activity levels in our business.

In 2017 the U.S. active rig count grew from 658 at the beginning of the year to 929 rigs at the end for an average rig count of 876. The U.S. year-over-year rig count growth in 2017 was 80% over the average rig count of 512 in 2016 (source: Baker Hughes). In 2017 our U.S. activity days increased 90% to 9,782 in 2017 from 5,145 in 2016. In 2017 the average Canadian rig count was 206 compared to an average rig count of 129 in 2016 representing a 60% growth. In 2017, our Canadian activity days increased 59% to 3,890 from 2,440 in 2016.

On the pricing side we were able to achieve price increases from our U.S. customers throughout the year. In Canada pricing remained challenging. Our average Canadian day rate in 2017 was $7,106 compared to an average day rate in the U.S. of $11,655 ($8,981 in USD). As is well published, the Canadian energy industry is having challenges based on the political climate and take away capacity for both oil and natural gas. As such Cathedral's continuing focus is on the larger U.S. market where we have better growth prospects and achieve better pricing and cash flow contributions. As our corporate and operational support costs are largely in Canada we also benefit from the USD/CAD exchange rate. In 2017, 78% of our revenues in CAD were derived from the U.S. market.

Over the year, we did experience both labor and supplier challenges. The labor issues were mainly related to the U.S. market were both labor availability and wage escalation were challenges. The supplier challenges were primarily due to the supply chain ramping up in the year resulting in long lead times on some critical items. We are generally able to push through equipment consumable costs and labor price increases to clients' over time, however, the price increases have more recently tended to lag our expense increases. Expense management continues to be a proactive focus area from the top to the very bottom of the Company.

A big challenge for Cathedral since the industry downturn was a change in our client's drilling practices and the downhole drilling environment becoming more severe. Energy companies are demanding wells be drilled, cheaper, longer and faster than wells drilled pre-downturn. The oilfield service industry has risen to this challenge, however, to achieve this equipment is being run harder, longer and in more demanding operating environments. Directional drilling equipment is being pushed harder and faster than in the past resulting in equipment being damaged, more frequent repairs and in part contributing to higher equipment lost-in-hole frequency.

In addition, equipment that worked well pre-2014, particularly drilling motors, is not able to meet the performance challenges post-downturn – energy companies want the latest and greatest equipment on their jobs. To a large degree, directional drilling equipment that was fit for purpose five years ago is quickly becoming obsolete.

Responding to this new drilling environment was a key focus area for us in 2017. Due to equipment damage and equipment lost-in-hole, our job capacity became constrained mid-year. The competitive environment was also such that clients were reluctant to pay for damages even if we could demonstrate the damage was directly caused by their drilling practices.

The positive news is that based on Cathedral having our own equipment expertise and doing our own repairs we are able to react to these demands quickly. Our Drilling Engineering and Sales teams worked with clients to recover equipment damages and assist them with improving their drilling practices to mitigate them. We improved our ability to recover equipment damages and have had very good success recovering funds for equipment lost-in-hole from clients. Our technology development teams worked on equipment modifications and performance enhancements. We aggressively ramped up our capital spending program mid-year to alleviate our equipment constraints and to start developing and funding a new line of high performance motors. In 2017 we invested $11.3 million in new equipment, replacing equipment lost-in-hole and upgrading existing equipment. By late 2017 we were able to reap the benefits of the incremental capital expenditures and other operational improvements.

With our equipment capacity now increasing, the improvements we have made in operations, sales and technology over the past three years and our acute focus on providing our clients *“Better Performance Every Day”* we are positive about our prospects going into 2018.

We thank our employees for their continued dedication and hard work and our customers, vendors and business partners for their support though the trying times over the past couple of years and with supporting the ramp up of our business. Finally, we thank our shareholders for their support and confidence in our business prospects and strategy.

Sincerely,

Signed: *"P. Scott MacFarlane"*

P. Scott MacFarlane

President and Chief Executive Officer

Cathedral Energy Services Ltd.

March 8, 2018

MANAGEMENT'S DISCUSSION & ANALYSIS

This Management's Discussion and Analysis ("MD&A") for the year ended December 31, 2017 provides an analysis of the consolidated results of operations, financial position and cash flows of Cathedral Energy Services Ltd. (the "Company" or "Cathedral") and should be read in conjunction with the audited consolidated financial statements and notes thereto for the year ended December 31, 2017, as well as the Company's 2017 interim MD&A's. This MD&A is intended to assist the reader in the understanding and assessment of significant changes and trends, as well as the risks and uncertainties, related to the results of the operations and financial position of the Company. Currency amounts are in '000's except for day rates and per share amounts. This MD&A is dated March 8, 2018.

CORPORATE OVERVIEW

Cathedral Energy Services Ltd. is incorporated under the Business Corporations Act (Alberta). The Company is publicly traded on the Toronto Stock Exchange under the symbol "CET". The Company together with its wholly owned subsidiary, Cathedral Energy Services Inc. ("INC"), is engaged in the business of providing directional drilling services to oil and natural gas companies in western Canada and the U.S.

In late 2016, the Company made the decision to sell its Flowback and Production Testing ("F&PT") business and focus its resources fully on the directional drilling business where it believes it has a strong competitive advantage and better future growth prospects. A definitive agreement to sell the assets of this division was executed in December 2016 and the sale closed in January 2017.

Cathedral is a trusted partner to North American energy companies requiring high performance directional drilling services. We work in partnership with our customers to tailor our equipment and expertise to meet their specific geographical and technical needs. Our experience, technologies and responsive personnel enable our customers to achieve higher efficiencies and lower project costs.

FINANCIAL HIGHLIGHTS

		2017		2016		2015 [4]
Revenues	**$**	**147,095**	$	80,866	$	106,243
Adjusted gross margin % [1]		**18%**		22%		18%
Adjusted EBITDAS from continuing operations [1]	**$**	**18,796**	$	7,459	$	5,229
Diluted per share	**$**	**0.40**	$	0.21	$	0.14
As % of revenues		**13%**		9%		5%
Total Adjusted EBITDAS [1]	**$**	**18,674**	$	5,840	$	7,699
Diluted per share	**$**	**0.39**	$	0.16	$	0.21
Cash flow - operating activities	**$**	**2,952**	$	4,140	$	25,931
Write-downs of goodwill, equipment, intangibles and inventory	**$**	**(8,584)**	$	(277)	$	(12,773)
Gain on disposal on investment in associate and related assets	**$**	**-**	$	10,865	$	-
Provision for settlements	**$**	**-**	$	(4,217)	$	-
Write-down of deferred taxes related to CRA settlement	**$**	**-**	$	-	$	(10,346)
Loss before income taxes	**$**	**(382)**	$	(722)	$	(24,894)
Basic per share	**$**	**(0.01)**	$	(0.02)	$	(0.69)
Net earnings (loss) from continuing operations	**$**	**229**	$	2,617	$	(28,841)
Basic and diluted per share	**$**	**-**	$	0.07	$	(0.79)
Net earnings (loss)	**$**	**87**	$	(5,779)	$	(35,342)
Basic and diluted per share	**$**	**-**	$	(0.16)	$	(0.97)
Cash dividends declared per share [2]	**$**	**-**	$	-	$	0.12
Equipment additions [3]	**$**	**11,322**	$	899	$	6,908
Weighted average shares outstanding						
Basic (000s)		**47,381**		36,295		36,295
Diluted (000s)		**47,577**		36,295		36,295
Working capital	**$**	**31,016**	$	39,324	$	13,550
Total assets	**$**	**121,630**	$	136,017	$	155,610
Loans and borrowings excluding current portion	**$**	**46**	$	26,322	$	30,477
Shareholders' equity	**$**	**101,391**	$	90,772	$	96,607

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

(2) Quarterly dividend was suspended in November 2015

(3) Equipment additions exclude non-cash additions

(4) 2015 reclassified for Discontinued Operations

FISCAL 2017 KEY TAKEAWAYS

Revenues increased by $66,229 or 82% and Total Adjusted EBITDAS increased $12,834, or 220%;

Adjusted gross margin decreased from 22% to 18% due to increase equipment repairs, equipment rentals and field labour rates;

In December 2016, the Company entered into an agreement for the sale of all its flow back and production testing assets. These assets were presented as Assets held for sale at December 31, 2016 and the related operations were presented as Discontinued Operations. The sale closed in January 2017;

There was a significant decline in the USD/CAD foreign exchange rate year-over-year; for 2017 Q4 the average exchange rate was $1.27 compared to $1.33 for 2016 Q4;

In February 2017, the Company closed a bought deal public offering and insider private placement financing for total gross proceeds of $14,130; and

In December 2017, the Company signed with a new credit facility with a syndicate comprised of Alberta Treasury Branches and Export Development Canada.

OUTLOOK

The response to oil prices pushing into the WTI $60bbl USD range in late 2017 was a sharp increase in the U.S. rig count from 924 at the beginning of January to 978 at the end of February. As goes the outlook for oil prices, so goes the rig count and directional drilling industry activity levels. The improving rig count in early 2018 could signal a good start to the year other than the 10% drop in WTI that occurred the first week in February.

In 2018, our thesis is that oil prices will continue to be volatile and North American rig counts will show flat to slow growth. One factor supporting moderate rig growth is the improved well productivity. It is now taking less wells to get the same productivity as it has in the past due to longer laterals and better completions technology. On this basis, our strategy is that any market share we gain in 2018 will be at the expense of competitors - a challenge we are well prepared for. Any market growth will be icing on the cake.

The U.S. market will continue to be our primary focus in 2018 and we will continue to favor this market in terms of resource and equipment allocation. We intend to continue to develop our Canadian business where we see good prospects from a financial and strategic point of view. Changing supply and demand market dynamics, politics and innovation can change an oil and gas basin's prospects quickly and dramatically. Our business strategy of maintaining an operating presence in all the North American major basins has served us well for this reason.

2017 was challenging in terms of ramping up our business and underpinning this increased activity with a good sales and operations foundation. As we move forward, 2018 is about Cathedral demonstrating leadership in the directional business. 2018 is Cathedral's 20th year in business. Over the past 20 years we have built our business on being innovative, which will continue to be a key tenet going forward.

Based on the knowledge gained in 2016 and 2017 related to the more demanding post downturn drilling environment our equipment is subject to, Cathedral focused its 2017 technology development efforts on design changes to its existing MWD tools and motors with a view to make them more rugged and improve their reliability and performance. There were successes in many areas in 2017 and design upgrades are currently being implemented in our existing equipment fleet.

In late 2017, we embarked on a technology development program to develop a next generation Dual Telemetry (DT) MWD tool. The proposed tool design will incorporate a number of improvements over Cathedral's existing FUSION DT platform and over competitive products. A byproduct of this technology development program is improvements to Cathedral's standalone electromagnetic (EM) and pulse technology platforms. The launch of the new DT platform is anticipated to occur in 2019. This timeline may be impacted by technical challenges and the ability to test prototypes in wellbores. However, improvements identified under the longer term DT development program will be introduced into the existing MWD fleet as they become available.

In early 2018, we will be introducing a new high performance motor. The motor design improves the mud flow characteristics of the motor along with delivering more energy to the drill bit. As drilling penetration rates have increased there are more cuttings that need to be conveyed out of the wellbore in less time. The high mud flow capability of this motor will facilitate wellbore solids cleaning during the drilling operation and allow for faster rate of penetration. Cathedral successfully tested variations of this new motor in early 2018 and intends to manufacture additional motors as part of its 2018 capital expenditure program.

In 2017 Cathedral also developed a drilling motor for use with rotary steerable systems (RSS). Rotary steerable technology is an alternative to the bent motor steering technique used by Cathedral and the majority of our directional drilling competitors. RSS is more applicable in certain drilling environments particularly with extended reach wellbores (horizontal wellbores exceeding 2 times vertical depth). Based on field testing in 2017, Cathedral's RSS motor design was shown to provide reliability and performance advantages over competitive products. Cathedral intends to invest in developing further drilling motor capabilities for the RSS market in 2018. Cathedral is also working on a strategy to allow it to participate more fully in the extended reach wellbore market. Part of this strategy will be leveraging our existing MWD telemetry capabilities.

In 2018, Cathedral will also be further supplementing its MWD fleet with additional downhole generators. This technology enables Cathedral to offer a high power telemetry system to support longer runs and higher signal strength compared to conventional battery systems.

We are both optimistic and confident about our prospects going into 2018.

RESULTS OF OPERATIONS - 2017 COMPARED TO 2016

Overview

The Company completed 2017 with revenues of $147,095 compared to 2016 revenues of $80,866 an 82% increase. 78% of 2017 revenues were derived from the U.S. compared to 73% of revenue in 2016. 2017 Adjusted EBITDAS from continuing operations was $18,796 ($0.40 per share diluted) which represents an $11,337 or 152% increase from $7,459 ($0.21 per share diluted) in 2016. In 2017, the Company's net earnings was $87 ($nil per share) compared to net loss of $(5,779) ($0.16 loss per share) in 2016. The 2017 net earnings includes a write-down of equipment and intangibles of $8,584 (2016 - $277).

Revenues		2017		2016
Canada	$	32,315	$	22,220
United States		114,780		58,646
Total	$	147,095	$	80,866

Revenues 2017 revenues were $147,095, which represented a $66,229 increase or 82% from 2016 revenues of $ 80,866. Both Canada and U.S. operations had increases due to an improvement in overall drilling activity. In late 2016, due to a limited supply of the Company's proprietary motors, the Company made the decision to reduce the number of rental motors available in both Canada and the U.S. in favor of redirecting motors on jobs where both equipment and staff are deployed and the cash flow contribution is higher. As a consequence motor rental revenue in both Canada and the U.S. were less in 2017 compared to 2016.

Canadian revenues (excluding motor rental revenues) increased to $27,644 in 2017 from $16,164 in 2016; a 71% increase. This increase was the result of: i) a 59% increase in activity days to 3,890 in 2017 from 2,440 in 2016; and ii) a 7% increase in the average day rate to $7,106 in 2017 from $6,625 in 2016. Partially offsetting these increases was a decrease on the rental of motors to $4,671 from 2016 at $6,056.

The average active land rig count in Canada was up 59% in 2017 compared to 2016 (source: Baker Hughes). The increase in the Company's activity days of 59% was in line with the industry increase. The slight increases in day rates was due to the mix of work performed.

U.S. Directional Drilling revenues (excluding motor rental revenues) increase to $114,012 in 2017 from $55,452 in 2016; a 106% increase. This increase was the result of: i) a 90% increase in activity days to 9,782 in 2017 from 5,145 in 2016; and ii) a 8% increase in the average day rate to $11,655 in 2017 from $10,778 in 2016 (when converted to Canadian dollars). All U.S. operating areas saw increases in activity days. U.S. motor rental revenues for 2017 were $768 compared to $3,194 in 2016.

The average active land rig count for the U.S. was up 78% in 2017 compared to 2016 (source: Baker Hughes). The increase of U.S. activity days of 90% relative to the active rigs drilling was due to efforts of sales and marketing staff and performance on client jobs. The Company was able to increase its U.S. market share compared to 2016. Day rates in USD increased to $8,981 in 2017 from $8,124 in 2016; an 11% increase. U.S. day rates were up due to client price increases, the mix of work performed by the U.S. division, including providing footage drilling services to certain clients, which can result in higher relative day rates.

Gross margin and adjusted gross margin Gross margin for 2017 was 11% compared to 7% in 2016. Adjusted gross margin (see Non-GAAP Measurements) for 2017 was $26,677 or 18% compared to $17,875 or 22% for 2016.

Adjusted gross margin percentage decreased due to increases in field labour rates, equipment repairs and higher equipment rentals on a percentage of revenue basis. These increases were offset by a reduction in the fixed component of cost of sales that were 7% lower on a percentage of revenue basis in 2017 compared to 2016. The decrease in the fixed component of cost of sales as a percentage of revenue was mostly attributable to increase in revenues, however there were increases in costs largely related to salaries and other labour related costs.

Depreciation allocated to cost of sales decreased to $11,043 in 2017 from $12,358 in 2016. Depreciation included in cost of sales as a percentage of revenue was 8% for 2017 and 15% in 2016.

Selling, general and administrative expenses ("SG&A") SG&A expenses were $15,698 in 2017; an increase of $513 compared with $15,185 in 2016. As a percentage of revenue, SG&A was 11% in 2017 and 19% in 2016. SG&A increased primarily due to increases in sales commissions and U.S. sales tax charges on intercompany equipment rentals, net of a reduction in SG&A from the recovery of a bad debt.

Gain on disposal of equipment During 2017, the Company had a gain on disposal of equipment of $7,236 compared to $3,212 in 2016. These gains mainly relate to equipment lost-in-hole. Proceeds from clients on lost-in-hole equipment are based on amounts specified in client service agreements and generally consider the replacement cost of the equipment. In most cases, the lost-in-hole proceeds exceed the net book value of the equipment and result in a gain. The timing and amount of lost-in-hole recoveries is not in the control of the Company and therefore can fluctuate significantly from quarter-to-quarter.

Finance costs Finance costs consist of interest expenses on operating loans, loans and borrowings and bank charges of $684 for 2017 compared to $2,061 for 2016. The decrease in finance costs relate to primarily to repayments of loans in 2017 Q1.

Foreign exchange loss The Company had a foreign exchange gain of $1,783 in 2017 compared to $1,438 in 2016 due to the fluctuations of the Canadian dollar relative to the U.S. dollar. The Company's foreign operations are denominated in a currency other than the Canadian dollar and therefore, upon consolidation, gains and losses due to fluctuations in the foreign currency exchange rates are recorded in other comprehensive income ("OCI") on the balance sheet as a component of equity. However, gains and losses in the Canadian entity on U.S. denominated intercompany balances continue to be recognized in the statement of income. Included in the 2017 foreign currency gains are unrealized gains of $1,903 (2016 – $1,455) related to intercompany balances.

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

The Settlement Agreement covered claims from employed and contracted MWD and DD staff who participated in the settlement. Under the terms of the Settlement Agreement, the parties established an initial settlement fund of up to $3,400 USD. The final determination of the settlement fund amount was based on the number of claimants that participated in the settlement at the end of December 2016, which under the terms of the Settlement Agreement is confidential. The settlement fund payments will be paid quarterly by the Company over a three-year period with the final payment due on or before September 2019. The quarterly payments may be accelerated in the event Cathedral meets certain financial targets over the payment period and can be deferred if a scheduled payment would put Cathedral in violation of its credit facility covenants subject to not more than three payments being deferred. In 2017 the majority of the payments under the Settlement Agreement were made.

In 2017 Q1, the Company entered a settlement with one of its U.S. clients related to a down-hole drilling incident in December 2013. The terms of this settlement agreement are confidential and following an initial payment in 2017 Q1 involve a series of quarterly payments to occur until 2021. This liability was recorded at December 31, 2016.

In 2016 there were total expenses recognized of $4,217 related to the 2 settlements (2017 - $nil).

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

Write-down of equipment and intangibles The Company determined an impairment test for the directional drilling Cash Generating Unit (CGU) was not required as at December 31, 2017. However, the Company chose to write-off certain assets where utilization was very low due to low market demand in the amount of $8,287. The assets written down included non-proprietary drilling motors and certain non-proprietary MWD systems. The non-proprietary MWD systems had been purchased related to the disposed of international operations and were retained by the Company after the sale of DPI in 2016 Q1. This equipment was not used extensively in the Company's North American operations and was fully written-off. The Company has experienced lower demand for non-proprietary mud motors in the current drilling environment as their performance capabilities are lower than the Company's proprietary mud motors. The Company conducted a review and wrote-off the remaining net book value for any non-proprietary mud motors that were no longer expected to be utilized. There was also an impairment of $146 related to an intangible project.

Write-down of inventory The Company made a provision related to inventory used to service the non-proprietary mud motors of $151 (2016 - $277).

Net loss from discontinued operations In 2016 Q4, the Company made the decision to sell its F&PT assets and focus its attention and resources fully on the directional drilling business where it believes it has a strong competitive advantage and better future growth prospects. The proceeds from this sale were used to pay down debt. As such, operating results for the years ended December 31, 2017 and 2016 for the F&PT business have been included in the statements of income and retained earnings and cash flows as discontinued operations. For 2017, the net loss from discontinued operations was $142 compared to $4,089 for 2016.

Write-down of assets held for sale from discontinued operations, net of tax In 2016 the F&PT assets were written down by $5,900 to their net realizable value of approximately $17,241. This write-down of $5,900 was offset by a deferred tax recovery of $1,593.

Income tax For 2017, the Company had an income tax recovery of $611 compared to a recovery of $3,339 in 2016. Excluding the non-cash gain on disposal of foreign subsidiary, write-down of goodwill and adjustments to prior years' tax provisions, the effective tax rate was 57% for 2017 and 31% for 2016. The 2017 provision includes reduction to U.S. deferred income tax asset due to reduction in U.S. rates from recent tax reform. The impact of the U.S. tax reform was not material to the 2017 tax provision or deferred tax asset. Excluding this amount the effective rate for 2017 was 36%. Income tax expense is booked based upon expected annualized effective rates.

LIQUIDITY AND CAPITAL RESOURCES

Overview On an annualized basis, the Company's principal source of liquidity is cash generated from operations. In addition, the Company has the ability to fund liquidity requirements through its credit facility and the issuance of debt and/or equity. For the year ended December 31, 2017, the Company had cash flow from operating activities of $2,952 (2016 - $4,140). The decrease in funds from operating activities is due to the change in non-cash operating working capital from a source of cash of $1,570 in 2016 to a use of cash of $8,948 in 2017. Cash flow from continuing operations increased to $11,169 from $2,937 in 2016. This increase was primarily due to increased revenues and net earnings.

Working capital At December 31, 2017 the Company had working capital of $31,016 (2016 - $39,324) and a working capital ratio of 2.6 to 1 (2016 – 3.3 to 1). Included in the December 31, 2016 balance is $17,241 related to Assets held for sale. $17,200 of proceeds on this sale were used to repay the secured revolving term loan in January 2017. Excluding Assets held for sale, December 31, 2016 working capital was $22,083 and the 2017 working capital reflects an $8,933 increase from the adjusted 2016 value. The increase was mainly due to an increase in accounts receivable due to the overall increase in revenues in 2017 Q4 as well as increase in inventories a portion of which will be used for 2018 capital build.

Credit facility During December 2017, the Company signed a new credit facility (the "Facility") with a new lending syndicate. The Facility consists of a $5 million operating facility and $15 million extendible revolving credit facility and expires December 31, 2019. The Facility is secured by a general security agreement over all present and future personal property.

The financial covenants associated with the amended Facility are:

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

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

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

At December 31, 2017, the Company had cash balances in excess of outstanding letters of credit and capital lease obligations. As such its funded debt to Credit Agreement EBITDA ratio ("Funded debt ratio") was negative (i.e. net cash balance). As such, the Funded debt ratio has been met, but is not meaningful ("NM") for presentation. For the rolling twelve months ended December 31, 2017 Credit Agreement EBITDA was $20,374.

Ratio	Actual	Required
Consolidated funded debt to consolidated Credit Agreement EBITDA ratio	NM	3.0:1
Consolidated interest coverage ratio	29.8:1	2.5:1

The amount drawn under the Facility at December 31. 2017 was $1,233 due to a requirement that the Company pledge cash deposits as security for three outstanding letters of credit ("LOC") with the Company's former financial institution. These LOCs were replaced by the current financial institution in January 2018 resulting in the related restricted cash funds being returned to general accounts.

Contractual obligations In the normal course of business, the Company incurs contractual obligations and those obligations are disclosed below. As at December 31, 2017, the Company had a commitment to purchase equipment of approximately $3,317. Cathedral anticipates expending these funds 2018 Q1.

The Company has issued the following five LOC:

- two LOC securing rent payments on property leases and renew annually with the landlords. The first LOC is $700 CAD for the first ten years of the lease and then reduces to $500 for the last five years of the lease. The second LOC is currently for $542 USD and increases annually based upon annual changes in rent;
- $75 USD issued for U.S. workers compensation coverage; and
- two LOC securing the Company's corporate credit cards in the amounts of $100 CAD and $150 USD.

The following table outlines the anticipated payments related to purchase commitments subsequent to December 31, 2018:

	Total	2018	2019	2020	2021	2022	Thereafter
Purchase obligations	$ 3,317	$ 3,317	$ -	$ -	$ -	$ -	$ -
Secured revolving term loan	-	-	-	-	-	-	-
Operating lease obligations	32,581	3,537	3,119	2,924	2,907	2,960	17,134
Finance lease obligations	285	236	49	-	-	-	-
Total	$ 36,183	$ 7,090	$ 3,168	$ 2,924	$ 2,907	$ 2,960	$ 17,134

Share capital At March 8, 2018, the Company has 49,403,951 common shares and 2,927,000 options outstanding with a weighted average exercise price of $1.44.

In 2017, the Company issued 2,197,750 stock options to staff and directors with an average exercise price of $1.08 per option.

Related party transactions Cathedral has determined that the key management personnel of the Company consist of its executive officers and directors.

In addition to their salaries and director's fees, the Company also provides non-cash benefits to directors and executive officers including participation in the Company's share option program.

Certain executive officers have employment agreements. Upon resignation at the Company's request, they are entitled to termination benefits including: i) 1.5 to 2.0 times base salary; ii) 1.5 to 2.0 times average annual bonus over the past 3 years; and iii) health, dental, life insurance and disability coverage for 18 to 24 months.

Key management personnel (including directors) compensation comprised:

		2017		2016
Short-term employment benefits	$	1,546	$	1,850
Share-based compensation		120		99
Total expense recognized as share-based compensation	$	1,666	$	1,949

Key management personnel and director transactions

Directors and executive officers of the Company control approximately 6% of the common shares of the Company.

There have been no other transactions over the reporting period with key management personnel (2016 - nil), and no outstanding balances exist as at period end (2016 - nil).

OFF-BALANCE SHEET ARRANGEMENTS

As at December 31, 2017, the Company has entered into $32,581 of commitments under operating leases for premises and issued standby LOC in the amounts of $700 CAD and $617 USD (refer to notes 23 and 24 to the audited consolidated financial statements). The Company indemnifies its directors and officers, to the extent permitted by law, against any and all claims or losses (including amounts paid in settlement of claims) incurred as a result of their service to the Company. The maximum amount payable under these indemnities cannot be reasonably estimated. The Company expects that it would be covered by insurance for most, but not all, tort liabilities.

2017 CAPITAL PROGRAM

During the year ended December 31, 2017 Company invested $11,322 (2016 - $899) in equipment. The following table details the net equipment additions:

		December 31 2017		December 31 2016
Property and equipment additions:				
Growth capital [(1)]	$	4,049	$	324
Maintenance capital [(1)]		3,610		105
Replacement capital [(1)]		3,663		470
Total cash additions		11,322		899
Less: proceeds on disposal of equipment lost down-hole		(8,951)		(5,286)
Net property and equipment additions (disposals) [(1)]	$	2,371	$	(4,387)

(1) See "NON-GAAP MEASUREMENTS"

The replacement and maintenance capital amounts noted above is expenditures to replace items that have been lost-in-hole over the past two years and for equipment upgrades and replacements to improve the capacity of Cathedral's existing Measurement-While-Drilling ("MWD") and drilling motor fleet. Over the past 2 years, Cathedral deferred replacement and maintenance capital expenditures in the face of low equipment utilization and in order to pay down debt. Subject to operating results and industry outlook, equipment lost-in-hole will be replaced and funded from the proceeds received. As such, Cathedral's total capex in any year may exceed the budgeted net additions. At December 31, 2017, the Company had 107 active MWD kits (2016 – 126 total kits) and 741 drilling motors (2016 -746). During 2017, the Company changed how it tracks kits and is now tracking those that can be actively deployed. The 2016 amount is under the prior practice of reporting total kits as this new system was not in place at that time.

A capital budget of $10,000 plus re-investment of proceeds on disposition of property and equipment was approved by the Board of Directors for 2017. There is a carry forward of $7,629 to be expended in 2018.

2018 CAPITAL PROGRAM

Cathedral's 2018 capital budget approved by the Board of Directors in January 2018 was for new expenditures of $12,500 which includes approximately $2,500 of intangible additions related to technology developments. In addition to this amount, there is a carry forward from 2017 of $7,629 largely related to lost-in-hole equipment replacements that will be expended in 2018.

DIVIDENDS

The Board of Directors made the decision to suspend the payment of Cathedral's quarterly dividend in late 2015. The decision to suspend the dividend was made in order to preserve cash, to manage liquidity, invest selectively in capital asset additions and pursue operational initiatives to better position the Company for improved industry conditions. The Board of Directors will review dividend distributions from time to time considering current performance, historical and future trends in the business and the expected sustainability of those trends in addition to considering the growth and maintenance capital expenditures required to support the business and other factors impacting the business.

RESULTS OF OPERATIONS – THREE MONTHS ENDED DECEMBER 31

Revenues and operating expenses

	2017 Q4	2016 Q4	$ Change	% Change
Revenues	38,402	28,009	10,393	37%
Cost of sales	(34,741)	(24,454)	(10,287)	42%
Gross margin - $	3,661	3,555	106	3%
Gross margin - %	10%	13%	-3%	
Adjusted gross margin $ (1)	6,602	6,634	(32)	0%
Adjusted gross margin % (1)	17%	24%	-7%	

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

Revenues	2017	2016
Canada	$ 7,748	$ 7,428
United States	30,654	20,581
Total	$ 38,402	$ 28,009

Revenues 2017 Q4 revenues were $38,402, which represented an increase of $10,393 or 37% from 2016 Q4 revenues of $28,009. Both Canada and U.S. operations had increases due to increase in drilling activity.

Canadian revenues (excluding motor rental revenues) decreased to $6,216 in 2017 Q4 from $6,509 in 2016 Q4; a reduction of 5%. This decrease was the net result of: i) an 18% decrease in activity days to 814 in 2017 Q4 from 995 in 2016 Q4; net of ii) a 17% increase in the average day rate to $7,636 in 2017 Q4 from $6,542 in 2016 Q4. Offsetting this decline was an increase of $613 on the rental of motors. Motor rental revenues for 2017 Q4 were $1,532 (2016 Q4 - $919).

The average active land rig count for Canada was up 11% in 2017 Q4 compared to 2016 Q4. The reduction in days for Cathedral relative to the overall market was the result of clients who temporarily reduced their drilling programs in the quarter. In addition, throughout 2017, the Company made the decision to deploy equipment to the U.S. market where day rates are higher and there is more consistent client demand.

U.S. Directional Drilling revenues (excluding motor rental revenues) increased to $30,561 in 2017 Q4 from $20,032 in 2016 Q4; a 53% increase. This increase was the result of: i) an 29% increase in activity days to 2,453 in 2017 Q4 from 1,899 in 2016 Q4; and ii) an 18% increase in the average day rate to $12,459 in 2017 Q4 from $10,549 in 2016 Q4 (when converted to Canadian dollars). The average active land rig count for the U.S. was up 63% in 2017 Q4 compared to 2016 Q4. In the quarter, there were issues with having sufficient equipment available to service additional jobs and as such the Company's increase was not as great as the industry increase. Rates in USD increased to $9,798 in 2017 Q4 from $7,907 in 2016 Q4; a 24% increase. U.S. day rates were up due to price increases from clients and the mix of work performed by the U.S. division, including providing footage drilling services to certain clients, which can result in higher relative day rates. U.S. motor rental revenues for 2017 Q4 were $93 compared to $549 in 2016 Q4.

Gross margin and adjusted gross margin Gross margin for 2017 Q4 was 10% compared 13% in 2016 Q4. Adjusted gross margin (see Non-GAAP Measurements) for 2017 Q4 was $6,602 or 17% compared to $6,634 or 24% for 2016 Q4.

Adjusted gross margin percentage decreased due to increases in equipment repairs offset by lower field labour costs. This net increase was offset by a reduction in the fixed component of cost of sales that were 2% lower on a percentage of revenue basis in 2017 compared to 2016. The decrease in the fixed component of cost of sales as a percentage of revenue was mostly attributable to increase in revenues.

Depreciation allocated to cost of sales decreased to $2,915 in 2017 Q4 from $3,073 in 2016 Q4. Depreciation included in cost of sales as a percentage of revenue was 8% for 2017 Q4 and 11% in 2016 Q4.

Selling, general and administrative expenses ("SG&A") SG&A expenses were $3,163 in 2017 Q4; a decrease of $694 compared with $3,857 in 2016 Q4. As a percentage of revenue, SG&A was 8% in 2017 Q4 and 14% in 2016 Q4. The SG&A decrease was primarily due to decrease in U.S. sales tax charges on intercompany equipment rentals and reduction in insurance, net of increases in SG&A due to increases in staffing costs. Staffing costs included in SG&A include executive, sales, accounting, human resources, payroll, safety, technology support and related support staff.

Gain on disposal of equipment During 2017 Q4, the Company had a gain on disposal of equipment of $2,038 compared to $1,010 in 2016 Q4. These gains mainly relate to equipment lost-in-hole. Proceeds from clients on lost-in-hole equipment are based on amounts specified in client service agreements and generally consider the replacement cost of the equipment. In most cases, the lost-in-hole proceeds exceed the net book value of the equipment and result in a gain. The timing of lost-in-hole recoveries is not in the control of the Company and therefore can fluctuate significantly from quarter-to-quarter.

Finance costs Finance costs consist of interest expenses on operating loans, loans and borrowings and bank charges of $157 for 2017 Q4 compared to $679 for 2016 Q4. The decrease in finance costs relate to the reduction of loans within the Company's credit facility.

Foreign exchange loss The Company had a foreign exchange loss of $193 in 2017 Q4 compared to a loss of $701 in 2016 Q4 due to the fluctuations of the Canadian dollar relative to the U.S. dollar. The Company's foreign operations are denominated in a currency other than the Canadian dollar and therefore, upon consolidation, gains and losses due to fluctuations in the foreign currency exchange rates are recorded in OCI on the balance sheet as a component of equity. However, gains and losses in the Canadian entity on U.S. denominated intercompany balances continue to be recognized in the statement of comprehensive income (loss). Included in the 2017 Q4 foreign currency gains are unrealized loss of $113 (2016 Q4 – loss of $719) related to intercompany balances.

Provision for settlement During 2016 Q4, the participation rate related to the FLSA matter was finalized and during 2017 the majority of the payments under the Settlement Agreement were made. Additionally in 2017 Q1, the Company entered a settlement with one of its U.S. clients related to an alleged down-hole drilling incident in December 2013. This settlement was payable based on an initial payment in 2017 Q1 and the remainder in quarterly installments concluding in 2021.

In 2016 Q4, there was a net increase to the settlement provision of $421 (2017 Q4 - $nil).

Write-down of equipment and intangibles The Company determined an impairment test for the directional drilling CGU was not required as at December 31, 2017. However, the Company chose to write-off certain assets where utilization was very low due to low market demand in the amount of $8,287. The assets written down included non-proprietary drilling motors and certain non-proprietary MWD systems. The non-proprietary MWD systems had been purchased related to the disposed of international operations and were retained by the Company after the sale of DPI in 2016 Q1. This equipment was not used extensively in the Company's North American operations and was fully written-off. The Company has experienced lower demand for non-proprietary mud motors in the current drilling environment as their performance capabilities are lower than the Company's proprietary mud motors. The Company conducted a review and wrote-off the remaining net book value for any non-proprietary mud motors that were no longer expected to be utilized. There was also an impairment of $146 related to an intangible project.

Write-down of inventory The Company made a provision related to inventory used to service the non-proprietary mud motors of $151 (2016 - $nil).

Net loss from discontinued operations In 2016 Q4, the Company made the decision to sell its F&PT assets and focus its attention and resources fully on the directional drilling business where it believes it has a strong competitive advantage and better future growth prospects. The proceeds from this sale were used to pay down debt. For 2017 Q4, the net loss from discontinued operations was $nil compared to $896 for 2016 Q4.

Write-down of assets held for sale from discontinued operations, net of tax In 2016 Q4 the F&PT assets were written down by $5,900 to their net realizable value of approximately $17,241. This write-down of $5,900 was offset by a deferred tax recovery of $1,593

Income tax For 2017 Q4, the Company had an income tax recovery of $1,908 compared to $124 in 2016 Q4. Excluding adjustments to prior years' tax provisions, the effective tax rate was 24% for 2017 Q4 and 28% for 2016 Q4. The 2017 provision includes reduction to U.S. deferred income tax asset due to reduction in U.S. rates from recent tax reform. The impact of the U.S. tax reform was not material to the 2017 tax provision or deferred tax asset. Excluding this amount the effective rate for 2017 was 18%. Income tax expense is booked based upon expected annualized effective rates.

SUMMARY OF QUARTERLY RESULTS

Three month periods ended	Dec 2017	Sep 2017	Jun 2017	Mar 2017	Dec 2016	Sep 2016	Jun 2016	Mar 2016
Revenues	$ 38,402	$ 36,015	$ 34,355	$ 38,323	$ 28,009	$ 19,489	$ 14,624	$ 18,744
Total Adjusted EBITDAS (1)	$ 5,606	$ 3,909	$ 2,363	$ 6,796	$ 3,829	$ 2,173	$ (1,638)	$ 1,476
Total Adjusted EBITDAS (1) per share - diluted	$ 0.11	$ 0.06	$ 0.05	$ 0.09	$ 0.11	$ 0.06	$ (0.05)	$ 0.04
Net earnings (loss)	$ (4,490)	$ 1,810	$ 186	$ 2,581	$ (6,420)	$ (2,126)	$ (6,916)	$ 9,683
Net earnings (loss) per share - basic and diluted	$ (0.09)	$ 0.04	$ 0.00	$ 0.06	$ (0.18)	$ (0.06)	$ (0.19)	$ 0.27

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

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

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The Company's audited consolidated financial statements have been prepared in accordance with Generally Accepted Accounting Principles ("GAAP") and significant accounting policies utilized by the Company are described in note 3 to the Company's audited consolidated financial statements. Management believes the accounting principles selected are appropriate under the circumstances and the Audit Committee of the Company has approved the policies selected.

Under GAAP, the Company is required to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the audited consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. The estimates and assumptions utilized are based on experience and other information available to management at the time the estimate or assumption is made. The estimates and assumptions used by management are constantly evaluated for relevance under the circumstances and if circumstances on which the estimates or assumptions were based change, the impact is included in the results of operations for the period in which the change occurs. Management believes the estimates, judgments and assumptions involved in its financial reporting are reasonable.

The following accounting policies require management's more significant judgments and estimates in the preparation of the Company's audited consolidated financial statements, and as such, are considered critical.

Equipment The Company makes estimates about the residual value and expected useful life of equipment. These estimates are based on management's historical experience and industry norms. Expected useful life and depreciation rates are as disclosed in note 3 (d) (iii) to the audited consolidated financial statements.

Impairment of long-lived assets Goodwill was assessed for impairment when circumstances suggest that the carrying amount may exceed the recoverable amount for the asset or at least annually. Equipment and intangibles are assessed for impairment when circumstances suggest that the carrying amount may exceed the recoverable amount for the asset. These calculations require estimates and assumptions and are subject to change as new information becomes available. These estimates include number of years of cash flow available from the assets, growth rates, pre-tax discount rates as well as various estimates and assumptions used in the preparation of revenues and expenses used in the cash flow analysis. The assumptions used in the impairment test of equipment and goodwill are disclosed in notes 8 and 9 to the audited consolidated financial statements.

Trade accounts receivable Trade accounts receivable require estimates to be made regarding the financial stability of the Company's customers and the environment in which they operate in order to assess if accounts receivable balances will be received. Credit risks for outstanding accounts receivable are assessed regularly and an allowance for doubtful accounts is recorded based upon specific customer information and experience as well as for groups of similar assets. See note 26 to the audited consolidated financial statements "Credit risk" for further details.

Inventory Inventory is reviewed periodically in order to determine if there is obsolescence. This estimate is based upon historic data and management's estimates of future demand. See note 7 to the audited consolidated financial statements for discussion of the 2016 and write-downs of inventory.

Income taxes The Company uses the asset and liability method of accounting for future income taxes whereby deferred income tax assets and liabilities are determined based on temporary differences between the accounting basis and the tax basis of the assets and liabilities, and are measured using substantively enacted tax rates and laws expected to apply when these differences reverse. As a result, a projection of taxable income is required for those years, as well as an assumption of the ultimate recovery/settlement period for the temporary differences.

The business and operations of the Company are complex and the Company has executed a number of significant financings, reorganizations, acquisitions and other material transactions over the course of its history. The computation of income taxes payable as a result of these transactions involves many complex factors as well as the Company's interpretation of relevant tax legislation and regulations. The Company's management believes that the provision for income tax is adequate and in accordance with GAAP and applicable legislation and regulations. However, tax filing positions are subject to review by taxation authorities who may successfully challenge the Company's interpretation of the applicable tax legislation and regulations.

FUTURE ACCOUNTING POLICIES

A number of new accounting standards, amendments to accounting standards and interpretations are effective for annual periods beginning on or after January 1, 2018 and have not been applied in preparing the Consolidated Financial Statements for the year ended December 31, 2017. The standards applicable to the Company are as follows and will be adopted on their respective effective dates:

(i) Revenue Recognition

On May 28, 2015, the IASB issued IFRS 15, "Revenue From Contracts With Customers" ("IFRS 15") replacing International Accounting Standard 11, "Construction Contracts" ("IAS 11"), IAS 18, "Revenue" ("IAS 18"), and several revenue-related interpretations. IFRS 15 establishes a single revenue recognition framework that applies to contracts with customers. The standard requires an entity to recognize revenue to reflect the transfer of goods and services for the amount it expects to receive, when control is transferred to the purchaser in accordance with a five step model. Disclosure requirements have also been expanded.

The new standard is effective for annual periods beginning on or after January 1, 2018, with earlier adoption permitted. The standard may be applied retrospectively or using a modified retrospective approach. The Company has completed the review of the new standard and has concluded that there is no material impact to the timing of recognition or measurement of revenue under IFRS 15.

(ii) Financial Instruments

On July 24, 2015, the International Accounting Standards Board (IASB) issued the final version of IFRS 9, "Financial Instruments" ("IFRS 9") to replace IAS 39, "Financial Instruments: Recognition and Measurement" ("IAS 39").

IFRS 9 introduces a single approach to determine whether a financial asset is measured at amortized cost or fair value and replaces the multiple rules in IAS 39. The approach is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. For financial liabilities, IFRS 9 retains most of the IAS 39 requirements; however, where the fair value option is applied to financial liabilities, the change in fair value resulting from an entity's own credit risk is recorded in OCI rather than net earnings, unless this creates an accounting mismatch. In addition, a new expected credit loss model for calculating impairment on financial assets replaces the incurred loss impairment model used in IAS 39. The new model will result in more timely recognition of expected credit losses. IFRS 9 also includes a simplified hedge accounting model, aligning hedge accounting more closely with risk management. Cathedral does not currently apply hedge accounting and does not value any financial liabilities at fair value.

IFRS 9 is effective for years beginning on or after January 1, 2018. The Company does not expect the change in the impairment model or any of the other changes to have a material impact on the consolidated financial statements.

(iii) Leases

In January 2016, the IASB issued IFRS 16 Leases that provides a single lease accounting model for lessees, which require the recognition of most leases as finance leases on the balance sheet.

This will result in the recognition of a lease liability and a corresponding recognition of a leased asset called right-of-use asset. On the statement of net earnings and comprehensive income, lease expense will be recognized and will consist of two components, depreciation expense of the right-of-use asset and interest expense related to the lease liability. Finance lease exemptions exist for short-term leases where the term is 12 months or less and for leases of low value items.

IFRS 16 comes into effect on January 1, 2019. The Company is currently evaluating the impact of adopting IFRS 16 on the consolidated financial statements.

CONTROLS AND PROCEDURES

In order to ensure that information with regard to reports filed or submitted under securities legislation present fairly in all material respect the financial information of the Company, management including the Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") are responsible for establishing and maintaining disclosure controls and procedures, as well as internal controls over financial reporting based upon The Committee of Sponsoring Organizations of the Treadway Commission (2013 framework).

Disclosure controls and procedures The Company's disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed by the Company is reported within the time periods specified under securities laws, and include controls and procedures that are designed to ensure that information is communicated to management of the Company, including the CEO and CFO, to allow timely decisions regarding required disclosure. An evaluation of the effectiveness of the Company's disclosure controls and procedures (as defined in Multilateral Instrument 52-109, Certification of Disclosure in Issuers' Annual Financial and Interim Filings) was conducted as at December 31, 2017. Based on this evaluation, the CEO and CFO of Cathedral have concluded that the design and operation of the Company's disclosure controls and procedures were effective as at December 31, 2017.

Internal controls over financial reporting Management is responsible for establishing and maintaining adequate internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP. The CEO and CFO have designed or have caused such internal controls over financial reporting (as defined in Multilateral Instrument 52-109, Certification of Disclosure in Issuers' Annual Financial and Interim Filings) to be designed under their supervision to provide reasonable assurance regarding the reliability of financial reporting and preparation of the Company's financial statements for external purposes in accordance with GAAP. In addition, the CEO and CFO directed the assessment of the design and operating effectiveness of the Company's internal controls over financial reporting as at December 31, 2017 and based upon that assessment determined that the Company's internal controls over financial reporting were, in all material respects, appropriately designed and operating effectively.

Management of the Company believe that "cost effective" disclosure controls and procedures and internal controls over financial reporting, no matter how well conceived or implemented, can only provide reasonable assurance, and not absolute assurance, that the objective of controls and procedures are met. Because of inherent limitations, disclosure controls and procedures and internal control over financial reporting may not prevent errors or fraud.

There has been no change in the Company's internal controls over financial reporting during the year ended December 31, 2017 that has materially affected, or is reasonably likely to materially affect, the Company's internal controls over financial reporting.

RISK FACTORS

Crude Oil and Natural Gas Prices Demand for the services provided by Cathedral is directly impacted by the prices that Cathedral's customers receive for the crude oil and natural gas they produce. The prices received and the volumes produced have a direct correlation to the cash flow available to invest in drilling activity and other oilfield services. The markets for oil and natural gas are separate and distinct and are largely driven by supply and demand factors. Oil is a global commodity with a vast distribution network. As natural gas is most economically transported in its gaseous state via pipeline, its market is dependent on pipeline infrastructure and is subject to regional supply and demand factors. Recent developments in the transportation of liquefied natural gas ("LNG") in ocean going tanker ships could introduce more of an element of globalization to the natural gas market. Crude oil and natural gas prices are quite volatile, which accounts for much of the cyclical nature of the oilfield services business.

Prices for oil and natural gas are subject to large fluctuations in response to relatively minor changes in the supply of, and demand for, oil and natural gas, market uncertainty and a variety of additional factors beyond the control of Cathedral. These factors include economic conditions in the U.S. and Canada, the actions of the Organization of Petroleum Exporting Countries ("OPEC"), government regulation, political stability in the Middle East and elsewhere, the foreign supply of oil and natural gas, risks of supply disruption, the price of foreign imports, technological advances improving the efficiency of oil and natural gas extraction and production, and the availability of alternative fuel sources and other advances that reduce energy use efficiency impacting consumption. In addition to pricing determined based on worldwide or North American supply and demand factors, there are a number of regional factors that also influence pricing such as transportation capacity, oil and natural gas physical properties and local supply and demand. Petroleum prices are expected to remain volatile for the near future as a result of market uncertainties over the supply and the demand of these commodities related to the current state of the world economies, OPEC actions and credit availability and liquidity concerns in the energy industry.

During 2016 and 2017, the price of West Texas Intermediate Crude more than doubled from its February 2016 low of approximately USD $26/bbl to end the 2017 year at approximately USD $60/bbl. This price improvement positively impacted the Company's business; however, crude prices remain approximately 50% below the price of approximately USD $108/bbl achieved in June 2014. Commodity prices at the current levels may not be supportive of oil and natural gas development and exploration spending historically. Furthermore, there is considerable volatility with oil and natural gas prices. Commodity price volatility may impact E&P companies' willingness to commit to capital spending, which in turn may have a significant adverse effect on the Company's business and financial results.

World crude oil prices and North American natural gas prices, including LNG, are not subject to control by Cathedral. With that in mind, Cathedral attempts to partially manage this risk by way of maintaining cost structure that can be adjusted to reflect activity levels. A significant portion of Cathedral's fieldwork is performed by sub-contractors and staff paid on a day rate or hourly basis which allows us to operate with lower variable costs and fixed overhead costs in seasonally low activity periods as well as extended downturns in the oilfield services sector. In addition, Cathedral also strives to continuously improve its operational efficiencies and reduce the cost of the equipment it deploys. Notwithstanding the above, throughout 2017 Cathedral faced cost increases in many areas of its business which were in part related to industry activity level increases These included, but were are not limited to, supplier costs, employee and contractor wages, equipment costs, equipment and other rental costs, equipment and other repair costs, administrative and other business support costs. Although Cathedral continues to manage costs in order to maintain margins, Cathedral's revenues and profitability could be negatively impacted should such costs continue to rise faster than revenues.

Take Away Capacity for Cathedral's Customers Cathedral's customers rely on various transportation methods to deliver the produced oil and natural gas to the end market including: pipelines, truck and railway. If such take away capacity becomes full and incremental capacity is not added, the price and production of hydrocarbons may be adversely impacted resulting in lower oilfield service industry activity levels. This could have a material adverse effect on Cathedral's business operations, financial condition, results of operations, cash flow and the ability to pay dividends to shareholders.

Alternatives to and Changing Demand for Hydrocarbon Products Fuel conservation measures, alternative fuel requirements, electric automobiles, increasing consumer demand for alternatives to oil and natural gas, and technological advances in fuel economy, vehicle electrification and energy generation devices could reduce the demand for crude oil, natural gas and other hydrocarbons. The Company cannot predict the impact of changing demand for oil and natural gas products, and any major changes may have a material adverse effect on the Cathedral's business, financial condition, results of operations and cash flows.

Cash Dividends to Shareholders are Dependent on the Performance of Cathedral Cathedral's ability to make dividend payments to shareholders is dependent upon the operations and business of Cathedral. In November 2015, the Board made the decision to suspend the payment of the Company's quarterly dividend based the reductions in commodity prices and the resulting decline in industry activity levels in 2015 and uncertainties around expected activity levels in the future (see "Dividend Policy"). There is no assurance that dividends will be declared at all in the future and, if declared, there is no assurance regarding the amounts of cash that may be available from Cathedral's operations and business that could be available to fund such future dividends. The actual amount of any dividends will depend on a variety of factors, including without limitation, the current performance, historical and future trends in the business, the expected sustainability of those trends, enacted tax legislation which will affect future taxes payable as well as required long-term debt repayments, maintenance capital expenditures required to sustain performance, future growth capital expenditures, effect of acquisitions or dispositions on Cathedral's business, compliance with debt covenants and other factors that may be beyond the control of Cathedral or not anticipated by management of Cathedral.

Cathedral's dividend policy is subject to change at the discretion of its Board of Directors. In addition, Cathedral's credit facility covenants include certain restrictions on the payment of cash dividends without the consent of the lenders in certain circumstances.

Performance of Obligations The Company's success depends in large part on whether it fulfills its obligations with clients and maintains client satisfaction. If Cathedral fails to satisfactorily perform its obligations, makes errors in the provision of its services, or does not perform its services

to the expectations of its clients, its clients could terminate working relationships, including master service agreements, exposing Cathedral to loss of its professional reputation and risk of loss or reduced profits, or in some cases, the loss of a project and claims by customers for damages. Typically, Cathedral's master service agreements do not contain any guaranteed payments and are cancellable on 30 or less days' notice.

Access to Capital The credit facilities of Cathedral contain covenants that require it to meet certain financial tests and that restrict, among other things, the ability of Cathedral to incur additional debt, make significant acquisitions, dispose of assets or pay dividends in certain circumstances. To the extent the cash flow from operations is not adequate to fund Cathedral's cash requirements, external financing may be required. Lack of timely access to such additional financing, or which may not be on favorable terms, could limit the future growth of the business of Cathedral and, potentially have a material adverse effect on the amount of cash available for dividends. To the extent that external sources of capital, including public and private markets, become limited or unavailable, Cathedral's ability to make the necessary capital investments to maintain or expand its current business and to make necessary principal payments under its credit facility may be impaired.

Forward-looking Information May Prove Inaccurate Numerous statements containing forward-looking information are found in documents incorporated by reference herein and other documents forming part of Cathedral's public disclosure record. Such statements and information are subject to risks and uncertainties and involve certain assumptions, some, but not all, of which are discussed elsewhere in this document. The occurrence or non-occurrence, as the case may be, of any of the events described in such risks could cause actual results to differ materially from those expressed in the forward-looking information.

Interest Rates Cathedral's current credit facility bears interest at a floating interest rate and, therefore, to the extent Cathedral borrows under this facility, it is at risk of rising interest rates. Management continually monitors interest rates and would consider locking in the rate of its term debt.

Debt Service Cathedral has a committed extendible revolving credit facility with a syndicate of lenders consisting of Alberta Treasury Branches and Export Development Canada in the amount of $15 million (excluding the $5 million operating facility) with a maturity date of December 31, 2019. Although it is believed that the credit facility is sufficient, there can be no assurance that the amount will be adequate for the financial obligations of Cathedral. As well, if Cathedral requires additional financing such financing may not be available or, if available, may not be available on favorable terms. Cathedral's lenders have been provided with security over substantially all of the assets of Cathedral. There is no assurance that the existing credit facility will be extended beyond its maturity date.

In light of the current volatility in oil and natural gas prices and uncertainty regarding commodity price levels in the future there is a risk that the Company could temporarily breach the covenants included in its credit facility. If the Company does temporarily breach these covenants, the secured revolving term loan could become due and payable on demand.

Additional Shares If the Board of Cathedral decides to issue additional common shares, Preferred Shares or securities convertible into common shares, existing shareholders may suffer significant dilution.

Unpredictability and Volatility of Share Price The prices at which the common shares trade cannot be predicted. The market price of the common shares could be subject to significant fluctuations in response to variations in quarterly operating results and other factors. In addition, in the event a dividend is paid the annual dividend yield on the common shares as compared to the annual yield on other financial instruments may also influence the price of common shares in the public trading markets. An increase in prevailing interest rates will result in higher yield on other financial instruments, which could adversely affect the market price of the common shares. The market price of the common shares may also be impacted by other factors including the net asset value of our assets which will vary from time to time depending on factors beyond our control.

In addition, the securities markets have experienced significant market wide and sectorial price and volume fluctuations from time to time that often have been unrelated or disproportionate to the operating performance of particular issuers. Such fluctuations may adversely affect the market price of the common shares.

Income Tax Matters The business and operations of Cathedral are complex and Cathedral and its predecessors have executed a number of significant financings, reorganizations, acquisitions and other material transactions over the course of its history. The computation of income taxes payable as a result of these transactions involves many complex factors as well as Cathedral's interpretation of relevant tax legislation and regulations.

Cathedral's management believes that the provision for income tax is adequate and in accordance with generally accepted accounting principles and applicable legislation and regulations. However, tax filing positions are subject to review by taxation authorities who may successfully challenge Cathedral's interpretation of the applicable tax legislation and regulations. It is also possible that tax authorities may retroactively or prospectively amend tax legislation or its interpretation, which could affect Cathedral's current and future income taxes.

Key Personnel and Employee/Sub-contractor Relationships Shareholders must rely upon the ability, expertise, judgment, discretion, integrity and good faith of the management and employees of Cathedral. The success of Cathedral is dependent upon its personnel and key sub-contractors. The unexpected loss or departure of any of Cathedral's key officers, employees or sub-contractors could be detrimental to the future operations of Cathedral. Cathedral does not maintain key man insurance on any of its officers. The success of Cathedral's business will depend, in part, upon Cathedral's ability to attract and retain qualified personnel as they are needed. Additionally, the ability of Cathedral to expand its services is dependent upon its ability to attract additional qualified employees. During high levels of activity, attracting quality staff can be challenging due to competition for such services. As a consequence of the industry downturn experienced since mid-2014 resulting in workforce reductions, many former industry workers have left the industry either temporarily or permanently. As a consequence of this, attracting and retaining staff may be more challenging in the future than in the past. Cathedral provides its staff with a quality working environment, effective training, tools with current technology and competitive remuneration packages that allows it to attract and retain the quality of its workforce, whether in the field, shop or office. There can be no assurance that Cathedral will be able to engage the services of such personnel or retain its current personnel.

Competition The oil and natural gas service industry in which Cathedral and its operating entities conduct business is highly competitive. Cathedral competes with other more established companies which have greater financial, marketing and other resources and certain of which are large international oil and natural gas service companies which offer a wider array of oil and natural gas services to their clients than does Cathedral.

At any time there may be an excess of certain classes of oilfield service equipment in North America in relation to current levels of demand. The supply of equipment in the industry does not always correlate to the level of demand for that equipment. Periods of high demand often spur increased capital expenditures on oilfield service equipment, and those capital expenditures may result in equipment levels which exceed actual demand. In periods of low demand, there may be excess equipment available within the industry resulting in equipment obsolescence. Excess equipment supply in the industry could cause competitors to lower their rates and could lead to a decrease in rates in the oilfield services industry generally, which could have an adverse effect on revenues, cash flows and earnings in the industry and for the Company.

Access to Parts, Consumables and Technology and Relationships with Key Suppliers The ability of Cathedral to compete and expand will be dependent on Cathedral having access, at a reasonable cost, to equipment, parts and components for purchased equipment for the development and acquisition of new competitive technologies. An inability to access these items and delays in accessing these items could have a material adverse effect on Cathedral's business, financial condition, results of operations and cash flow. Cathedral's equipment may become obsolete or experience a decrease in demand due to competing products that are lower in cost, have enhanced performance capabilities or are determined by the market to be more preferable for environmental or other reasons. Although Cathedral has very good relationships with its key suppliers, there can

be no assurances that those sources of equipment, parts, components or relationships with key suppliers will be maintained. If these are not maintained, Cathedral's ability to compete may be impaired. If the relationships with key suppliers come to an end, the availability and cost of securing certain parts, components and equipment may be adversely affected.

Technology The success and ability of Cathedral to compete depends in part on the technologies that it brings to the market, and the ability of Cathedral to prevent others from copying such technologies. Cathedral currently relies on industry confidentiality practices ("trade secrets"), including entering into industry standard confidentiality agreements and in some cases patents (or patents pending) to protect its proprietary technology. Cathedral may have to engage in litigation in order to protect its intellectual property rights, including patents or patents pending, or to determine the validity or scope of the proprietary rights of itself or others. This kind of litigation can be time-consuming and expensive, regardless of whether or not Cathedral is successful.

Additionally, there can be no assurance that certain tools, equipment or technology developed by Cathedral may not be the subject of future patent infringement claims or other similar matters which could result in litigation, the requirement to pay licensing fees or other results that could have a material adverse effect on Cathedral's business, results of operations and financial condition.

The intellectual property rights of Cathedral may be invalidated, circumvented, challenged, infringed or required to be licensed to others. It cannot be assured that any steps Cathedral may take to protect its intellectual property rights and other rights to such proprietary technologies that are central to Cathedral's operations will prevent misappropriation or infringement.

Cathedral competes with other more established companies which have greater financial resources to develop new technologies. Competitors may also develop similar or substitute tools, equipment and technology to Cathedral's thereby adversely affecting Cathedral's competitive advantage and/or market share. There may also be changes in customer or market requirements which make Cathedral's technology obsolete or result in a lower demand for Cathedral's products and services. Certain competing technologies are beginning to enter Cathedral's market which may have a negative impact on Cathedral long term. RSS technology is becoming more cost-effective and can be used as a substitute for certain methods currently in place by Cathedral. As a result, there is the risk that a larger portion of Cathedral's customer base will move away from technology provided by Cathedral. Although Cathedral intends to adopt processes to provide similar services and develop competing technology, there is no guarantee that it will be successful and Cathedral is likely to face a number of challenges, including intellectual property matters, in order to implement new competing technology.

Potential Replacement or Reduced Use of Products and Services Certain of Cathedral's equipment or systems may become obsolete or experience a decrease in demand through the introduction of competing products that are lower in cost, exhibit enhanced performance characteristics or are determined by the market to be more preferable for environmental or other reasons. Cathedral is beginning to see a change in customer requirements, resulting in certain equipment becoming technically obsolete or creating market obsolescence based on lower demand which resulted in Cathedral writing-down certain equipment. In addition, the drilling industry is experiencing a trend towards automation, the impact of which on Cathedral's business is not yet known. Cathedral will need to keep current with the changing market for oil and natural gas services and technological and regulatory changes. If Cathedral fails to do so, this could have a material adverse effect on its business, financial condition, results of operations and cash flows.

Operating Risks and Insurance Cathedral has an insurance and risk management plan in place to protect its assets, operations and employees. However, Cathedral's oilfield services are subject to risks inherent in the oil and natural gas industry, such as equipment defects, equipment obsolesce, malfunctions, failures, natural disasters and errors by staff, some of which may not be covered by insurance. These risks could expose Cathedral to substantial liability for personal injury, loss of life, business interruption, property damage or destruction, pollution and other environmental damages. Cathedral attempts to obtain indemnification from our customers by contract for some of these risks in addition to having insurance coverage. These indemnification agreements may not adequately protect against liability from all of the consequences described above. In addition, Cathedral's operating activities includes a significant amount of transportation and therefore is subject to the inherent risks including potential liability which could result from, among other things, personal injury, loss of life or property damage derived from motor vehicle accidents. Cathedral carries insurance to provide protection in the event of destruction or damage to its property and equipment, subject to appropriate deductibles and the availability of coverage. Liability insurance is also maintained at prudent levels to limit exposure to unforeseen incidents. An annual review of insurance coverage is completed to assess the risk of loss and risk mitigation alternatives. It is anticipated that insurance coverage will be maintained in the future, but there can be no assurance that such insurance coverage will be available in the future on commercially reasonable terms or be available on terms as favorable as Cathedral's current arrangements. The occurrence of a significant event outside of the coverage of Cathedral's insurance policies could have a material adverse effect on the results of the Company. If there is an event that is not fully insured or indemnified against, or a customer or insurer does not meet its indemnification or insurance obligations, it could result in substantial losses.

Energy companies are demanding wells be drilled, cheaper, longer and faster than wells drilled prior to the industry downturn which has adversely impacted Cathedral's drilling equipment and may continue to do so. In 2017, Cathedral experienced higher than previous levels of equipment damages and equipment lost-in-hole which in part was due to changes in customer drilling practices.

Business continuity, disaster recovery and crisis management Inability to restore or replace critical capacity in a timely manner may impact business and operations. A serious event could have a material adverse effect on Cathedral's business, results of operations and financial condition. This risk is mitigated by the development of business continuity arrangements, including disaster recovery plans and back-up delivery systems, to minimize any business disruption in the event of a major disaster. Insurance coverage may minimize any losses in certain circumstances.

Risks of Foreign Operations Cathedral may conduct a portion of its business outside North America through a number of means including projects, joint ventures and partnerships and other business relationships. As such, Cathedral could be exposed to risks inherent in foreign operations including, but not limited to: loss of revenue, property and equipment as a result of expropriation and nationalization, war, civil and/or labour unrest, strikes, terrorist threats, civil insurrection and other political risks; fluctuations in foreign currency and exchange controls; increases in duties, taxes and governmental royalties and renegotiation of contracts with governmental entities; trade and other economic sanctions or other restrictions imposed by the Canadian government or other governments or organizations; as well as changes in laws and policies governing operations of foreign-based companies.

Carrying on business outside of Canada gives rise to the risk of dealing with business and political systems that are different than Cathedral is accustomed to in Canada.

Cathedral made the decision to terminate its pursuit of operations in Venezuela in 2014 which were provided through a joint venture with a wholly-owned subsidiary of PDVSA, the state-owned oil and natural gas corporation of the Bolivarian Republic of Venezuela. The joint venture company, Vencana, was owned 60% by the PDVSA wholly-owned subsidiary and 40% by Cathedral's wholly-owned subsidiary, DPI. On February 29, 2016, Cathedral announced it had closed the sale of its Venezuelan investment by way of selling its wholly-owned Barbados subsidiary, DPI. See AIF "General Development of the Business - Three Year History –2016".

Weather and Seasonality A significant portion of Cathedral's operations are carried on in western Canada where activity levels in the oilfield services industry are subject to a degree of seasonality. Operating activities in western Canada are generally lower during "spring breakup" which normally commences in March and continues through to May. Operating activities generally increase in the fall and peak in the winter months from

December until late March depending weather conditions.

Activity levels in the oil and natural gas basins in the U.S. are not subject to the seasonality to the same extent that it occurs in the western Canada region. In general, activity levels in North America can be impacted year round by weather conditions and temperatures, including major weather events such as winter storms and hurricanes which can create additional unpredictability in operational results.

Foreign Currency Exchange Rates Cathedral derives revenues from the U.S. which are denominated in the local currency. This causes a degree of foreign currency exchange rate risk which Cathedral attempts to mitigate by matching local purchases in the same currency. Furthermore, Cathedral's Canadian operations are subject to foreign currency exchange rate risk in that some purchases for parts, supplies and components in the manufacture of equipment are denominated in USD. Cathedral's foreign currency policy is to monitor foreign current risk exposure in its areas of operations and mitigate that risk where possible by matching foreign currency denominated expense with revenues denominated in foreign currencies. Cathedral strives to maintain limited amounts of cash and cash equivalents denominated in foreign currency on hand and attempts to further limit its exposure to foreign currency through collecting and paying foreign currency denominated balance in a timely fashion.

In addition, Cathedral is exposed to currency exchange risk on those of its assets denominated in USD. Since Cathedral presents its financial statements in Canadian dollars, any change in the value of the Canadian dollar relative to the USD during a given financial reporting period would result in a foreign currency loss or gain on the translation of its assets measured in other currencies into Canadian dollars. Consequently, Cathedral's reported earnings could fluctuate materially as a result of foreign exchange translation gains or losses. Other than natural hedges arising from the normal course of business in foreign jurisdictions, Cathedral does not currently have any hedging positions.

Acquisition Risks Cathedral expects to continue to selectively seek acquisitions in connection with its growth strategy. Cathedral's ability to consummate and to integrate effectively any future acquisitions on terms that are favorable to it may be limited by the number of attractive acquisition targets, internal demands on Cathedral's resources, and to the extent necessary, Cathedral's ability to obtain financing on satisfactory terms for larger acquisitions, if at all. Acquisitions may expose Cathedral to additional risks, including: difficulties in integrating administrative, financial reporting, operational and information systems and managing newly-acquired operations and improving their operating efficiency; difficulties in maintaining uniform standards, controls, procedures and policies through all of Cathedral's operations; entry into markets in which Cathedral has little or no direct prior experience; difficulties in retaining key employees of the acquired operations; disruptions to Cathedral's ongoing business; and diversion of management time and resources.

Business Development Risks In implementing its strategy, Cathedral may pursue new business or growth opportunities. There is no assurance that Cathedral will be successful in executing those opportunities. Cathedral may have difficulty executing the its strategy because of, among other things, increased competition, difficulty entering new markets or geographies, difficulties in introducing new products, the ability to attract qualified personnel, barriers to entry into geographic markets, and changes in regulatory requirements.

Credit Risk All of Cathedral's accounts receivables are with customers involved in the oil and natural gas industry, whose revenue may be impacted by fluctuations in commodity prices. Although collection of these receivables could be influenced by economic factors affecting this industry and thereby have a materially adverse effect on operations, management considers risk of significant loss to be minimal at this time. To mitigate this risk, Cathedral's customers are subject to an internal credit review along with ongoing monitoring of the amount and age of receivables balances outstanding.

Reliance on Major Customers Management of Cathedral believes it currently has a good mix of customers. In 2017, approximately 20% of the Company's revenue was attributable to sales transactions with a single customer. In 2016, approximately 13% of the Company's revenue was attributable to sales transactions with a single customer. In 2015, two different customers represented approximately 12% and 10% of the Company's revenue. While Cathedral believes that its relationship with existing customers is good, the loss of any one or more of these customers, or a significant reduction in business done with Cathedral by one or more of these customers, if not offset by sales to new or existing customers, could have a material adverse effect on Cathedral's business, results of operations and prospects and therefore on the ability to pay dividends to shareholders in the future. Mergers and acquisitions activity in the oil and natural gas exploration and production sector can impact demand for our services as customers focus on internal reorganization prior to committing funds to significant oilfield services. In addition, demand for Cathedral's services could be negatively affected in that upon completion, the merger and acquisitions customers may re-direct their work to Cathedral's competitors.

Environmental Risks Cathedral is subject to various environmental laws and regulations enacted in the jurisdictions in which it operates which govern the manufacture, processing, importation, transportation, handling and disposal of certain materials used in Cathedral's operations. Cathedral has established procedures to address compliance with current environmental laws and regulations and monitors its practices concerning the handling of environmentally hazardous materials. However, there can be no assurance that Cathedral's procedures will prevent environmental damage occurring from spills of materials handled by Cathedral or that such damage has not already occurred. On occasion, substantial liabilities to third parties may be incurred. Cathedral may have the benefit of insurance maintained by it or the operator; however Cathedral may become liable for damages against which it cannot adequately insure or against which it may elect not to insure because of high costs or other reasons.

There is growing concern about the apparent connection between the burning of fossil fuels and climate change. The issue of energy and the environment has created intense public debate in Canada, the U.S. and around the world in recent years that is likely to continue for the foreseeable future and could potentially have a significant impact on all aspects of the economy including the demand for hydrocarbons and resulting in lower demand for Cathedral's services. There can be no assurance that the provincial, state and local governments or the Federal Governments of Canada and U.S. and other jurisdictions in which Cathedral enters into to provide its services will not adopt new environmental regulations, rules or legislation or make modifications to existing regulations, rules or legislation which could increase costs paid by Cathedral's customers. An increase in environmental related costs could reduce Cathedral's customers' earnings and/or it could make capital expenditures by Cathedral's customers uneconomic.

Over the past two years both the Canadian Federal Government and the Government of Alberta have announced various programs related to climate change and have made certain commitments regarding regulating greenhouse gases ("GHG") and other air pollutants. These programs implement taxes on GHG emissions to be paid by the users of hydrocarbons and caps on emissions by producers of hydrocarbons such as oilsands and energy companies.

Cathedral is unable to predict the total impact of the potential and forthcoming regulations upon its business. As a user of hydrocarbons in its business for heating and vehicles, Cathedral is impacted on an operational cost basis. Cathedral's customers may face increases in operating costs in order to comply with legislation which could have the effect of curtailing exploration and development by oil and natural gas producers and that in turn, could adversely affect Cathedral's operations by reducing demand for its services.

Government Regulation The oil and natural gas industry in Canada and the U.S. is subject to federal, provincial, state and municipal legislation and regulation governing such matters as land tenure, commodity prices, production royalties, production rates, environmental protection controls, the exportation of crude oil, natural gas and other products, as well as other matters. The industry is also subject to regulation by governments in such matters, including laws and regulations relating to health and safety, the conduct of operations, the protection of the environment and the manufacture, management, transportation, storage and disposal of certain materials used in Cathedral's operations.

Government regulations may change from time to time in response to economic or political conditions. The exercise of discretion by governmental

authorities under existing regulations, the implementation of new regulations or the modification of existing regulations affecting the crude oil and natural gas industry could reduce demand for Cathedral's services or increase its costs, either of which could have a material adverse impact on Cathedral.

There can be no assurance that the provincial, state and local governments or the Federal Governments of Canada and U.S. and other jurisdictions in which Cathedral enters into to provide its services will not adopt a new royalty regime or modify the methodology of royalty calculation which could increase the royalties paid by Cathedral's customers. An increase in royalties could reduce Cathedral's customers' earnings and/or it could make capital expenditures by Cathedral's customers uneconomic. Although Cathedral is not a direct investor in the oil and natural gas market, it does affect Cathedral's customers' cash flow available to invest in drilling activity and other oilfield services.

Safety Performance Cathedral has programs in place to address compliance with current safety and regulatory standards. Cathedral has a corporate safety manager responsible for maintaining and developing policies and monitoring operations consistent with those policies. Poor safety performance could lead to lower demand for Cathedral's services. Standards for accident prevention in the oil and natural gas industry are governed by company safety policies and procedures, accepted industry safety practices, customer-specific safety requirements, and health and safety legislation. Safety is a key factor that customers consider when selecting an oilfield service company. A decline in Cathedral's safety performance could result in lower demand for services, and this could have a material adverse effect on revenues, cash flows and earnings. Cathedral is subject to various health and safety laws, rules, legislation and guidelines which can impose material liability, increase costs or lead to lower demand for services.

Conflict of Interest Certain directors and officers of Cathedral are also directors and/or officers of oil and natural gas exploration and/or production entities and conflicts of interest may arise between their duties as officers and directors of Cathedral and as officers and directors of such other companies. Such conflicts must be disclosed in accordance with, and are subject to such other procedures and remedies as apply under the ABCA.

Legal Proceedings Cathedral is involved in litigation from time to time. No assurance can be given as to the final outcome of any legal proceedings or that the ultimate resolution of any legal proceedings will not have a materially adverse effect on Cathedral.

Risks Associated with Information Technology Systems Cathedral is dependent upon information technology systems in the conduct of its operations. Any significant malfunction, breakdown, downtime, invasion, virus, cyber-attack, security breach, destruction or interruption of these systems due to equipment or software failures or by employees, others with access to Cathedral's systems, or unauthorized persons could negatively impact its operations. To the extent any breakdown, downtime, malfunction, invasion, cyber-attack or security breach results in disruption to Cathedral's operations, loss or disclosure of, or damage to, its data or confidential information, its reputation, business, results of operations and financial condition could be materially adversely affected. Cathedral's systems and insurance coverage for protecting against information technology or cyber security risks may not be sufficient. Although to date Cathedral has not experienced any material losses relating to information technology failures or cyber-attacks, it may suffer such losses in the future. Cathedral may be required to expend significant additional resources to continue to modify or enhance its protective measures, to investigate and remediate any information security vulnerabilities or to maintain its information technology systems in good repair.

GOVERNANCE

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

SUPPLEMENTARY INFORMATION

Additional information regarding the Company, including the Annual Information Form ("AIF"), is available on SEDAR at www.sedar.com.

FORWARD LOOKING STATEMENTS

This MD&A contains certain forward-looking statements and forward-looking information (collectively referred to herein as "forward-looking statements") within the meaning of applicable Canadian securities laws. All statements other than statements of present or historical fact are forward-looking statements. Forward-looking statements are often, but not always, identified by the use of words such as "anticipate", "achieve", "believe", "plan", "intend", "objective", "continuous", "ongoing", "estimate", "outlook", "expect", "may", "will", "project", "should" or similar words suggesting future outcomes. In particular, this MD&A contains forward-looking statements relating to, among other things: oil prices will continue to be volatile and North American rig counts will show flat to slow growth; our strategy is that any market share we gain in 2018 will be at the expense of competitors; U.S. market will continue to be our primary focus in 2018 and we will continue to favor this market in terms of resource and equipment allocation; intend to continue to develop our Canadian business where we see good prospects; launch of the new DT platform is anticipated to occur in 2019; intends to manufacture additional motors as part of its 2018 capital expenditure program; Cathedral intends to invest in developing further drilling motor capabilities for the RSS market in 2018; Cathedral will also be further supplementing its MWD fleet with additional downhole generators; optimistic and confident about our prospects going into 2018; projected capital expenditures and commitments and the financing thereof; and Cathedral expects to comply with all covenants during 2017.

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

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

- the performance of Cathedral's businesses, including current business and economic trends;
- oil and natural gas commodity prices and production levels;
- alternatives to and changing demand for hydrocarbon products;
- performance obligation to clients;
- capital expenditure programs and other expenditures by Cathedral and its customers;
- currency exchange and interest rates;
- the ability of Cathedral to service its debt;
- the ability of Cathedral to retain and hire qualified personnel;
- the ability of Cathedral to obtain parts, consumables, equipment, technology, and supplies in a timely manner to carry out its activities;
- the ability of Cathedral to maintain good working relationships with key suppliers;
- the ability of Cathedral to market its services successfully to existing and new customers and reliance on major customers;
- risks associated with technology development and intellectual property rights;

- the ability of Cathedral to maintain safety performance;
- the ability of Cathedral to obtain timely financing on acceptable terms;
- the ability to obtain sufficient insurance coverage to mitigate operational risks;
- risks associated with acquisitions and business development efforts;
- environmental risks;
- risks associated with information technology systems;
- changes under governmental regulatory regimes and tax, environmental and other laws in Canada and U.S.; and
- competitive risks.

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

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

NON-GAAP MEASUREMENTS

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

The specific measures being referred to include the following:

i) "Adjusted gross margin" - calculated as gross margin plus non-cash items (depreciation and share-based compensation); is considered a primary indicator of operating performance (see tabular calculation);

ii) "Adjusted gross margin %" - calculated as adjusted gross margin divided by revenues; is considered a primary indicator of operating performance (see tabular calculation);

iii) "Total Adjusted EBITDAS" - defined as earnings before share of income/loss from associate, write-down/recovery on investment in associate finance costs, unrealized foreign exchange on intercompany balances, unrealized foreign exchange due to hyper-inflation accounting, taxes, non-recurring gains and losses on disposal of equipment (see non-GAAP measurement), depreciation, write-down of goodwill, write-down of equipment, write-down of inventory and share-based compensation; is considered an indicator of the Company's ability to generate funds flow from operations prior to consideration of how activities are financed, how the results are taxed and measured and non-cash expenses (see tabular calculation). This measure includes both discontinued F&PT operations and continuing Directional Drilling operations;

iv) "Adjusted EBITDAS from discontinued operations" – Total Adjusted EBITDAS as calculated above from discontinued F&PT operations only;

v) "Adjusted EBITDAS from continuing operations" – Total Adjusted EBITDAS as calculated above for ongoing Directional Drilling as well as corporate administrative costs;

vi) "Growth equipment additions" or "Growth capital" – is capital spending which is intended to result in incremental revenues or decreased operating costs. Growth capital is considered to be a key measure as it represents the total expenditures on equipment expected to add incremental revenues and funds flow to the Company;

vii) "Maintenance equipment additions" or "Maintenance capital" – is capital spending incurred in order to refurbish or replace previously acquired equipment other than "replacement equipment additions" described below. Maintenance capital is a key component in understanding the sustainability of the Company's business as cash resources retained within Cathedral must be sufficient to meet maintenance capital needs to replenish the assets for future cash generation;

viii) "Replacement equipment additions" or "Replacement capital" – is capital spending incurred in order to replace equipment that is lost-in-hole. Cathedral recovers lost-in-hole costs including previously expensed depreciation on the related assets from customers. Such additions do not provide incremental revenues. The identification of replacement equipment additions is considered important as such additions are financed by way of proceeds on disposal of equipment (see discussion within the MD&A on "gain on disposal of equipment); and

ix) "Net equipment additions" – is equipment additions expenditures less proceeds from equipment lost down-hole. Cathedral uses net equipment additions to assess net cash flows related to the financing of Cathedral's equipment additions.

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

Adjusted gross margin

	Three months ended December 31		Year ended December 31	
	2017	2016	2017	2016
Gross margin	$ 3,661	$ 3,555	$ 15,565	$ 5,503
Add non-cash items included in cost of sales:				
Depreciation	2,915	3,073	11,043	12,358
Share-based compensation	26	6	69	14
Adjusted gross margin	$ 6,602	$ 6,634	$ 26,677	$ 17,875
Adjusted gross margin %	17%	24%	18%	22%

Total Adjusted EBITDAS

	Three months ended December 31		Year ended December 31	
	2017	2016	2017	2016
Earnings (loss) before income taxes	$ (6,398)	$ (1,093)	$ (382)	$ (722)
Add:				
Depreciation included in cost of sales	2,915	3,073	11,043	12,358
Depreciation included in selling, general and administrative expenses	29	34	104	134
Share-based compensation included in cost of sales	26	6	69	14
Share-based compensation included in selling, general and administrative expenses	67	19	206	130
Finance costs	157	679	684	2,061
Subtotal	(3,204)	2,718	11,724	13,975
Unrealized foreign exchange (gain) loss on intercompany balances	113	719	(1,903)	(1,455)
Write-down of equipment and intangibles	8,433	-	8,433	-
Write-down of inventory	151	-	151	277
Provision for settlement	-	421	-	4,217
Gain on disposal of foreign subsidiary	-	-	-	(10,865)
Non-recurring expenses	113	298	391	1,310
Adjusted EBITDAS from continuing operations	5,606	4,156	18,796	7,459
Adjusted EBITDAS from discontinued operations	-	(325)	(122)	(1,619)
Total Adjusted EBITDAS	$ 5,606	$ 3,831	$ 18,674	$ 5,840

MANAGEMENT'S REPORT

The consolidated financial statements have been prepared by the management in accordance with International Financial Reporting Standards which is the basis for Canadian generally accepted accounting principles and, where appropriate, reflect estimates based upon management's judgment. Financial information contained elsewhere in the annual report has been prepared on a consistent basis with that in the consolidated financial statements.

Management is also responsible for a system of internal controls which is designed to provide reasonable assurance that the Company's assets are safeguarded and accounting systems provide timely, accurate financial reports.

The Audit Committee of the Board of Directors has reviewed in detail the consolidated financial statements with management and the external auditor. The Board of Directors has approved the consolidated financial statements on the recommendation of the Audit Committee.

KPMG LLP, an independent firm of chartered professional accountants, have examined the Company's consolidated financial statements in accordance with Canadian generally accepted auditing standards and provided an independent professional opinion. The auditors have full and unrestricted access to the Audit Committee to discuss their audit and their related findings as to the integrity of the financial reporting process.

Signed: *"P. Scott MacFarlane"*

P. Scott MacFarlane

President and Chief Executive Officer

Signed: *"Michael F. Hill"*

Michael F. Hill

Chief Financial Officer

INDEPENDENT AUDITORS' REPORT

To the Shareholders of Cathedral Energy Services Ltd.

We have audited the accompanying consolidated financial statements of Cathedral Energy Services Ltd., which comprise the consolidated statements of financial position as at December 31, 2017 and December 31, 2016, the consolidated statements of comprehensive income (loss), changes in shareholders' equity and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of Cathedral Energy Services Ltd. as at December 31, 2017 and December 31, 2016, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards.

Signed: "KPMG LLP"

Chartered Professional Accountants

March 8, 2018

Calgary, Canada

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

December 31, 2017 and 2016

Dollars in '000s

		December 31 2017		December 31 2016
Assets				
Current assets:				
Cash (note 5)	$	2,683	$	1,898
Restricted cash equivalents (note 5)		1,514		-
Trade receivables (note 6)		33,885		26,245
Current taxes recoverable		86		1,336
Prepaid expenses		1,460		1,611
Inventories (note 7)		11,128		8,037
Assets held for sale (note 10)		-		17,241
Total current assets		50,756		56,368
Equipment (note 8)		58,383		68,158
Intangible assets (note 9)		1,953		1,978
Deferred tax assets (note 11)		10,538		9,513
Total non-current assets		70,874		79,649
Total assets	$	121,630	$	136,017
Liabilities and Shareholders' Equity				
Current liabilities:				
Operating loan (note 12)	$	1,233	$	2,105
Trade and other payables (note 13)		17,926		12,837
Loans and borrowings (note 14)		233		459
Provision for settlements, current (note 15)		348		1,643
Total current liabilities		19,740		17,044
Loans and borrowings (note 14)		46		26,322
Provision for settlements, long-term (note 15)		453		1,879
Total non-current liabilities		499		28,201
Total liabilities		20,239		45,245
Shareholders' equity:				
Share capital (note 16)		88,059		74,481
Contributed surplus		9,801		9,620
Accumulated other comprehensive income		8,144		11,371
Deficit		(4,613)		(4,700)
Total shareholders' equity		101,391		90,772
Total liabilities and shareholders' equity	$	121,630	$	136,017

See accompanying notes to consolidated financial statements.

Approved by the Directors:

Signed: "P. Scott MacFarlane"	*Signed: "Rod Maxwell"*
P. Scott MacFarlane	Rod Maxwell
Director	Director

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

Years ended December 31, 2017 and 2016

Dollars in '000s except per share amounts

	2017	2016
Revenues (note 22)	$ 147,095	$ 80,866
Cost of sales (notes 7 and 19):		
Direct costs	(120,418)	(62,991)
Depreciation	(11,043)	(12,358)
Share-based compensation	(69)	(14)
Total cost of sales	(131,530)	(75,363)
Gross margin	15,565	5,503
Selling, general and administrative expenses (note 19):		
Direct costs	(15,388)	(14,921)
Depreciation	(104)	(134)
Share-based compensation	(206)	(130)
Total selling, general and administrative expenses	(15,698)	(15,185)
	(133)	(9,682)
Gain on disposal of equipment (note 8)	7,236	3,212
Earnings (loss) from operating activities	7,103	(6,470)
Finance costs	(684)	(2,061)
Foreign exchange gain (loss)	1,783	1,438
Write-down of equipment and intangibles (note 8 and 9)	(8,433)	-
Write-down of inventory (note 7)	(151)	(277)
Provision for settlement (note 15)	-	(4,217)
Gain on disposal of foreign subsidiary (note 18)	-	10,865
Loss before income taxes	(382)	(722)
Income tax recovery (expense) (note 11):		
Current	(405)	(106)
Deferred	1,016	3,445
Total income tax recovery	611	3,339
Net earnings from continuing operations	229	2,617
Net loss from discontinued operations (note 10)	(142)	(4,089)
Write-down of assets held for sale from discontinued operations, net of tax (note 10)	-	(4,307)
Net earnings (loss)	87	(5,779)
Other comprehensive income (loss):		
Foreign currency translation differences for foreign operations	(3,227)	(1,554)
Foreign currency translation gain on disposal of foreign subsidiary	-	1,348
Total comprehensive loss	$ (3,140)	$ (5,985)
Net earnings from continuing operations per share		
Basic and diluted	$ -	$ 0.07
Net loss from discontinued operations per share		
Basic	$ -	$ (0.11)
Net earnings (loss) per share		
Basic and diluted	$ -	$ (0.16)

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

Years ended December 31, 2017 and 2016

Dollars in '000s except per share amounts

	Share capital	Contributed surplus	Accumulated other comprehensive income	Retained earnings (deficit)	Total shareholders' equity
Balance at December 31, 2015	**$ 74,481**	**$ 9,470**	**$ 11,577**	**$ 1,079**	**$ 96,607**
Total comprehensive loss for the year ended December 31, 2016	-	-	(206)	(5,779)	(5,985)
Transactions with shareholders, recorded directly in equity contributions by and distributions to shareholders for the year ended December 31, 2016:					
Share-based compensation	-	150	-	-	150
Total contributions by and distributions to shareholders	-	150	-	-	150
Balance at December 31, 2016	**$ 74,481**	**$ 9,620**	**$ 11,371**	**$ (4,700)**	**$ 90,772**
Total comprehensive income (loss) for the year December 31, 2017	-	-	(3,227)	87	(3,140)
Transactions with shareholders, recorded directly in equity contributions by and distributions to shareholders for the year ended December 31, 2017:					
Issue of shares from bought deal public offering and insider private placement	13,131				13,131
Issue of shares upon exercise of options	447	(91)			356
Share-based compensation	-	272	-	-	272
Total contributions by and distributions to shareholders	13,578	181	-	-	13,759
Balance at December 31, 2017	**$ 88,059**	**$ 9,801**	**$ 8,144**	**$ (4,613)**	**$ 101,391**

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended December 31, 2017 and 2016
Dollars in '000s except per share amounts

	2017	2016
Cash provided by (used in):		
Operating activities:		
Net earnings from continuing operations	$ 229	$ 2,617
Items not involving cash		
Depreciation	11,147	12,492
Share-based compensation	275	144
Income tax recovery	(611)	(3,339)
Gain on disposal of equipment	(7,236)	(3,212)
Finance costs	684	2,061
Unrealized foreign exchange gain on intercompany balances	(1,903)	(1,455)
Write-down of equipment and intangibles	8,433	-
Write-down of inventory	151	277
Provision for settlements	-	4,217
Gain on disposal of foreign subsidiary	-	(10,865)
Cash flow - continuing operations	11,169	2,937
Cash flow - discontinued operations (note 10)	(135)	(1,800)
Changes in non-cash operating working capital (note 21)	(8,948)	1,570
Income taxes refunded	866	1,433
Cash flow - operating activities	2,952	4,140
Investing activities:		
Equipment additions	(11,322)	(899)
Intangible asset additions	(474)	(160)
Proceeds on disposal of equipment	9,203	5,286
Proceeds on disposal of discontinued operations (note 10)	17,252	-
Changes in non-cash investing working capital (note 21)	1,925	(762)
Cash flow - investing activities	16,584	3,465
Financing activities:		
Change in operating loan	(872)	(388)
Repayments on loans and borrowings	(26,420)	(5,499)
Proceeds on share issuance from bought deal public offering and insider private placement	13,131	-
Proceeds on share issuance from exercise of share options	354	-
Payment on settlements	(2,607)	(851)
Change in restricted cash	(1,514)	-
Interest paid	(687)	(1,605)
Advances of loans and borrowings	-	1,250
Cash flow - financing activities	(18,615)	(7,093)
Effect of exchange rate on changes on cash	(136)	(40)
Change in cash and cash equivalents	785	472
Cash, beginning of year	1,898	1,426
Cash, end of year	$ 2,683	$ 1,898

See accompanying notes to consolidated financial statements.

1. Reporting entity

Cathedral Energy Services Ltd. (the "Company" or "Cathedral") is a company domiciled in Canada. The Company is a publicly traded company listed on the Toronto Stock Exchange under symbol "CET". The consolidated financial statements of the Company as at and for the year ended December 31, 2017 comprise the Company and its 100% owned subsidiary, Cathedral Energy Services Inc. ("INC"), (together referred to as "Cathedral"). INC is incorporated in the United States of America ("U.S.") and its functional currency is U.S. dollars ("USD").

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

During 2016 Q1, the Company disposed of its 100% interest in Directional Plus International Inc. ("DPI"). See note 18 for further details.

2. Basis of preparation

(a) Statement of compliance

The consolidated financial statements have been prepared in accordance with Canadian Generally Accepted Accounting Principles ("GAAP") which are defined as International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). The consolidated financial statements were authorized for issue by the Board of Directors on March 8, 2018.

(b) Basis of measurement

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

(c) Functional and presentation currency

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

(d) Use of estimates and judgments

The preparation of the consolidated financial statements in conformity with GAAP requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Areas that require management to make significant judgment and estimates in determining the amounts recognized in these consolidated financial statements include, but are not limited to the following:

Judgments

(i) Current and deferred income taxes

The Company must make determinations on whether to record amounts for various tax pools it has available for future use. In making this determination, the Company looks at its history and future expectations to determine what amounts, if any can be recognized. The Company also reviews all tax assessments to determine which assessments it concurs with and will record in its records and which assessments it disputes and which it expects to be changed. If the Company believes the assessment was incorrect, it does not make a provision for a liability in its accounts. As such the provisions for current and deferred income taxes are subject to measurement uncertainty.

(ii) Recognition of contingent liabilities

The determination if a contingent liability requires an accrual in the financial statements or only requires disclosure is an area that requires significant judgment. In making this determination, management reviews the specific details of the contingency and may seek professional help if the matter is of sufficient complexity. For items not recorded as contingent liabilities, there is also a determination required if the amount of claim would be material, as only material amounts are disclosed in financial statements. As at December 31, 2017, the Company had no material contingent liabilities.

Estimates

(i) Equipment

The Company makes estimates about the residual value and expected useful life of equipment. These estimates are based on management's historical experience and industry norms. Expected useful life and depreciation rates are as disclosed in note 3 (d) (iii).

(ii) Impairment of assets

Equipment and intangibles are assessed for impairment when circumstances suggest that the carrying amount may exceed the recoverable amount for the asset. These calculations require estimates and assumptions and are subject to change as new information becomes available. These estimates include number of years of cash flow available from the assets, growth rates, pre-tax discount rates as well as various estimates and assumptions used in the preparation of revenues and expenses used in the cash flow analysis. The assumptions used in the 2016 impairment tests of equipment are disclosed in note 8.

Trade accounts receivable require estimates to be made regarding the financial stability of the Company's customers and the environment in which they operate in order to assess if accounts receivable balances will be received. Credit risks for outstanding accounts receivable are assessed regularly and an allowance for doubtful accounts is recorded based upon specific customer information and experience as well as for groups of similar assets. See note 26 "Credit risk" for further details.

Inventory is reviewed periodically in order to determine if there is obsolescence. This estimate is based upon historic data and management's estimates of future demand. The estimates used in the 2016 write-downs of inventory are discussed in note 7.

(iii) Income taxes

The Company uses the asset and liability method of accounting for future income taxes whereby deferred income tax assets and liabilities are determined based on temporary differences between the accounting basis and the tax basis of the assets and liabilities, and are measured using substantively enacted tax rates and laws expected to apply when these differences reverse. As a result, a projection of taxable income is required for those years, as well as an assumption of the ultimate recovery/settlement period for the temporary differences.

The business and operations of the Company are complex and the Company has executed a number of significant financings, reorganizations, acquisitions and other material transactions over the course of its history. The computation of income taxes payable resulting from these transactions involves many complex factors as well as the Company's interpretation of relevant tax legislation and regulations. The Company's management believes that the provision for income tax is adequate and in accordance with GAAP and applicable legislation and regulations. However, tax-filing positions are subject to review by taxation authorities who may successfully challenge the Company's interpretation of the applicable tax legislation and regulations.

(iv) Liquidity

As part of its capital management process, the Company prepares a forecast / budget. Management and the board of directors use the forecast / budget to direct and monitor the strategy and ongoing operations and liquidity of the Company. Forecasts / budgets are subject to significant judgment and estimates relating to activity levels, future cash flows and the timing thereof and other factors which may or may not be within the control of the Company. See further discussions relating to liquidity in note 26.

3. Significant accounting policies

The accounting policies set out below have been applied consistently by the Company to all periods presented in these consolidated financial statements unless otherwise indicated.

(a) Basis of consolidation

Business combinations are accounted for using the acquisition method of accounting in which the identifiable assets acquired, liabilities assumed and any non-controlling interest are recognized and measured at their fair value at the date of acquisition. Any excess of the purchase price plus any non-controlling interest over the fair value of the net assets acquired is recognized as goodwill. Any deficiency of the purchase price over the fair value of the net assets acquired is credited to net earnings.

At acquisition, goodwill is allocated to each of the CGUs to which it relates. Subsequent measurement of goodwill is at cost less any accumulated impairment losses.

(i) Subsidiaries

Subsidiaries are entities controlled by Cathedral. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. The accounting policies of subsidiaries align with the policies adopted by Cathedral.

(ii) Transactions eliminated on consolidation

Intra-group balances and transactions, and any unrealized income, expenses, gains or losses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

(b) Foreign currency

(i) Foreign currency transactions

All transactions that are not denominated in an entity's functional currency are foreign currency transactions. These transactions are initially recorded in the functional currency by applying the appropriate daily rate which best approximates the actual rate of transaction.

CAD is the functional and presentation currency of the Company. The functional currency of Cathedral's subsidiary is listed in note 1.

Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. All differences are recognized in the consolidated statement of comprehensive income.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

(ii) Foreign operations

The assets and liabilities of foreign operations are translated to CAD at exchange rates at the reporting date. The income and expenses of foreign operations are translated to CAD at exchange rates at the dates of the transactions.

Foreign currency differences are recognized in other comprehensive income and have been recognized in accumulated other comprehensive income (‘AOCI’) in the cumulative translation. When a foreign operation is disposed of, the relevant amount in AOCI (in the cumulative translation account) is transferred to profit or loss as part of the profit or loss on disposal. On the partial disposal of a subsidiary that includes a foreign operation, the relevant proportion of such cumulative amount is reattributed to non-controlling interest. In any other partial disposal of a foreign operation, the relevant proportion is reclassified to profit or loss.

(c) Financial instruments

At December 31, 2017 and 2016, Cathedral has the following financial instruments: cash and cash equivalents, loans and receivables.

(i) Non-derivative financial assets

Cathedral initially recognizes trade and other receivables on the date that they originate. All other financial assets (including assets designated at fair value through profit or loss) are recognized initially on the trade date at which Cathedral becomes a party to the contractual provisions of the instrument.

Cathedral derecognizes a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by Cathedral is recognized as a separate asset or liability.

Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, Cathedral has a legal right to offset the amounts and intends either to settle on a net basis or to realize the asset and settle the liability simultaneously.

Cash and cash equivalents

Cash and cash equivalents comprise cash balances and guaranteed investment certificates ("GIC") with original maturities of six months or less.

Loans and receivables

Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are recognized initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition, loans and receivables are measured at amortized cost using the effective interest method, less any impairment losses.

(ii) Non-derivative financial liabilities

Cathedral initially recognizes debt securities issued on the date that they are originated. Cathedral derecognizes a financial liability when its contractual obligations are discharged or cancelled or expire.

Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, Cathedral has a legal right to offset the amounts and intends either to settle on a net basis or to realize the asset and settle the liability simultaneously.

Cathedral has the following non-derivative financial liabilities: loans and borrowings, operating loan and trade and other payables.

Such financial liabilities are recognized initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition, these financial liabilities are measured at amortized cost using the effective interest method.

(d) Equipment

(i) Recognition and measurement

Items of equipment are measured at cost less accumulated depreciation and accumulated impairment losses.

Cost includes expenditure that is directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the assets to a working condition for their intended use, the costs of dismantling and removing the items and restoring the site on which they are located, and borrowing costs on qualifying assets.

Purchased software that is integral to the functionality of the related equipment is capitalized as part of that equipment.

When parts of an item of equipment have different useful lives, they are accounted for as separate items (major components) of equipment.

Gains and losses on disposal of an item of equipment are determined by comparing the proceeds from disposal with the carrying amount of equipment, and are recognized net within other income in profit or loss.

(ii) Subsequent costs

The cost of replacing a part of an item of equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to Cathedral, and its cost can be measured reliably. The carrying amount of the replaced part is derecognized. The costs of the day-to-day servicing of equipment (repair and maintenance) are recognized in profit or loss as incurred.

(iii) Depreciation

Depreciation is calculated over the depreciable amount, which is the cost of an asset, or other amount substituted for cost, less its residual value.

Depreciation is recognized in profit or loss on either a straight-line or diminishing balance basis over the estimated useful lives of each part of an item of equipment. Leased assets are depreciated over the shorter of the lease term and their useful lives unless it is reasonably certain that Cathedral will obtain ownership by the end of the lease term. Land is not depreciated.

Items of equipment are depreciated from the date that they are installed and are available for use, or in respect of internally constructed assets, from the date that the asset is completed and available for use.

The estimated useful lives, depreciation rates and depreciation methods for the current and comparative periods are as follows:

	Estimated life in years	Depreciation rates	Depreciation method
Directional drilling equipment	15.5 to 20	13 to 20%	Declining balance
Flow back and production testing equipment	11.5 to 15.5	15 to 20%	Declining balance
Office and computer equipment	3.0 to 11.5	20 to 55%	Declining balance
Automotive equipment	8 to 11.5	20 to 30%	Declining balance
Automotive equipment under capital lease	3 to 4	20% or 33%	Straight-line
Leasehold improvements	5	20%	Straight-line

Depreciation methods, useful lives and residual values are reviewed at each financial year-end and adjusted if appropriate.

(e) Intangible assets

(i) Goodwill

Goodwill that arises upon the acquisition of subsidiaries is included in the financial statements. For measurement of goodwill at initial recognition, see note 3(a).

(ii) Internally generated intangible asset - Research and development

Expenditure on research activities, undertaken with the prospect of gaining new scientific or technical knowledge and understanding, is recognized in profit or loss as incurred.

Development activities involve a plan or design for the production of new or substantially improved products and processes. Development expenditure is capitalized only if development costs can be measured reliably, the product or process is technically and commercially feasible, future economic benefits are probable, and Cathedral intends to and has sufficient resources to complete development and to use or sell the asset. The expenditure capitalized includes the cost of materials, direct labour, overhead costs that are directly attributable to preparing the asset for its intended use, and borrowing costs on qualifying assets. Other development expenditure is recognized in profit or loss as incurred.

Capitalized development expenditure is measured at cost less accumulated amortization and accumulated impairment losses.

(iii) Subsequent expenditure

Subsequent expenditure is capitalized only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure, including expenditure on internally generated goodwill and brands, is recognized in profit or loss as incurred.

(iv) Amortization

Amortization is calculated on the cost of the asset less its residual value.

Amortization is recognized in profit or loss on a straight-line basis over the estimated useful lives of intangible assets, other than goodwill, from the date that they are available for use, since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. The estimated useful life for capitalized development costs is 5 years.

Amortization methods, useful lives and residual values are reviewed at each financial year-end and adjusted if appropriate.

(f) Leased assets

Leases in terms of which Cathedral assumes substantially all the risks and rewards of ownership are classified as finance leases. Upon initial recognition, the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset.

Other leases are operating leases and the leased assets are not recognized in Cathedral's statement of financial position.

(g) Inventories

Inventories are measured at the lower of cost and net realizable value. The cost of inventories is based on the average cost principle, and includes expenditure incurred in acquiring the inventories, production or conversion costs and other costs incurred in bringing them to their existing location and condition.

Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

(h) Impairment

(i) Financial assets (including receivables)

A financial asset other than those carried at fair value through profit or loss is assessed for indicators of impairment at each reporting date. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be reliably estimated.

Cathedral considers evidence of impairment for receivables at both a specific asset and collective level. All individually significant receivables are assessed for specific impairment. All individually significant receivables found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not identified. Receivables that are not individually significant are collectively assessed for impairment by grouping together receivables with similar risk characteristics.

In assessing collective impairment Cathedral uses historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgment as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical trends.

(ii) Non-financial assets

The carrying amounts of Cathedral's non-financial assets, other than inventories and deferred tax assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit", or "CGU"). For the purposes of goodwill impairment testing, goodwill acquired in a business combination is allocated to CGUs that are expected to benefit from the synergies of the combination. This allocation is subject to an operating segment ceiling test and reflects the lowest level at which that goodwill is monitored for internal reporting purposes.

Cathedral's corporate assets do not generate separate cash inflows. If there is an indication that a corporate asset may be impaired, then the recoverable amount is determined for the CGU to which the corporate asset belongs.

An impairment loss is recognized if the carrying amount of an asset or its CGU exceeds its estimated recoverable amount. Impairment losses are recognized in profit or loss. Impairment losses recognized in respect of CGUs are allocated first to reduce the carrying amount of any goodwill allocated to the units, and then to reduce the carrying amounts of the other assets in the unit (group of units) on a pro rata basis.

An impairment loss in respect of goodwill is not reversed. In respect of other assets, impairment losses recognized in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.

(i) Employee benefits

(i) Termination benefits

Termination benefits are recognized as an expense when Cathedral is committed demonstrably, without realistic possibility of withdrawal, to a formal detailed plan either to terminate employment before the normal retirement date, or to provide termination benefits because of an offer made to encourage voluntary redundancy. Termination benefits for voluntary redundancies are recognized as an expense if Cathedral has made an offer of voluntary redundancy, it is probable that the offer will be accepted, and the number of acceptances can be estimated reliably. If benefits are payable more than 12 months after the reporting period, then they are discounted to their present value.

(ii) Short-term employee benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

A liability is recognized for the amount expected to be paid under short-term cash bonus or profit-sharing plans if Cathedral has a present legal or constructive obligation to pay this amount because of past service provided by the employee, and the obligation can be estimated reliably.

(iii) Share-based payment transactions – equity settled

The grant date fair value of share-based payment awards granted to employees, directors and consultants is recognized as an employee expense, with a corresponding increase in equity, over the period that the employees unconditionally become entitled to the awards (vesting period). The amount recognized as an expense is adjusted to reflect the number of awards for which the related service and non-market vesting conditions are expected to be met, such that the amount ultimately recognized as an expense is based on the number of awards that do meet the related service and non-market performance conditions at the vesting date.

Share-based payment arrangements in which Cathedral receives goods or services as consideration for its own equity instruments are accounted for as equity-settled share-based payment transactions.

(j) Revenue

Revenue is recognized when there is persuasive evidence that an arrangement exists (usually when executed), the risks and rewards have been transferred to the buyer, the service has been provided, the rate is fixed, the associated costs can be estimated reliably, the collection of the amounts billed to the customer is considered probable and revenue can be measured reliably. Cathedral considers persuasive evidence to exist when a formal contract is signed or customer acceptance is obtained. Contract terms do not include a provision for significant post-service delivery obligations.

Cathedral's services are generally sold based upon service orders or contracts with customers that include fixed or determinable prices based upon daily, hourly or job rates.

(k) Lease payments

Payments made under operating leases are recognized in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognized as an integral part of the total lease expense, over the term of the lease.

Minimum lease payments made under finance leases are apportioned between the finance expense and the reduction of the outstanding liability. The finance expense is allocated to each period during the lease term to produce a constant periodic rate of interest on the remaining balance of the liability.

Determining whether an arrangement contains a lease

At inception of an arrangement, Cathedral determines whether such an arrangement is or contains a lease. A specific asset is the subject of a lease if fulfillment of the arrangement is dependent on the use of that specified asset. An arrangement conveys the right to use the asset if the arrangement conveys to Cathedral the right to control the use of the underlying asset.

At inception or upon reassessment of the arrangement, Cathedral separates payments and other consideration required by such an arrangement into those for the lease and those for other elements on the basis of their relative fair values. If Cathedral concludes for a finance lease that it is impracticable to separate the payments reliably, an asset and a liability are recognized at an amount equal to the fair value of the underlying asset. Subsequently the liability is reduced as payments are made and an imputed finance charge on the liability is recognized using Cathedral's incremental borrowing rate.

(l) Finance income and costs

Finance costs comprise interest expense on borrowings, bank charges and other interest and foreign exchange gains or losses. Borrowing costs that are not directly attributable to the acquisition, construction or production of a qualifying asset are recognized in profit or loss using the effective interest method.

Foreign currency gains and losses are reported on a net basis.

(m) Income tax

Income tax expense comprises current and deferred tax. Current tax and deferred tax are recognized in profit or loss except to the extent that it relates to a business combination, or items recognized directly in equity or in other comprehensive income.

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognized for the following temporary differences: the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss, and differences relating to investments in subsidiaries and jointly controlled entities to the extent that it is probable that they will not reverse in the foreseeable future. In addition, deferred tax is not recognized for taxable temporary differences arising on the initial recognition of goodwill. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

A deferred tax asset is recognized for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable income will be available against which they can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

(n) Earnings per share

Cathedral presents basic and diluted earnings per share ("EPS") data for its common shares. Basic EPS is calculated by dividing the profit or loss attributable to common shareholders of the Company by the weighted average number of common shares outstanding during the period. Diluted EPS is determined by adjusting the profit or loss attributable to common shareholders and the weighted average number of common shares outstanding, adjusted for own shares held, for the effects of all dilutive potential common shares, which comprise share options granted to employees, directors and consultants.

(o) New standards not yet adopted

A number of new accounting standards, amendments to accounting standards and interpretations are effective for annual periods beginning on or after January 1, 2018 and have not been applied in preparing the Consolidated Financial Statements for the year ended December 31, 2017. The standards applicable to the Company are as follows and will be adopted on their respective effective dates:

(i) Revenue Recognition

On May 28, 2015, the IASB issued IFRS 15, “Revenue From Contracts With Customers” (“IFRS 15”) replacing International Accounting Standard 11, “Construction Contracts” (“IAS 11”), IAS 18, “Revenue” (“IAS 18”), and several revenue-related interpretations. IFRS 15 establishes a single revenue recognition framework that applies to contracts with customers. The standard requires an entity to recognize revenue to reflect the transfer of goods and services for the amount it expects to receive, when control is transferred to the purchaser in accordance with a five step model. Disclosure requirements have also been expanded.

The new standard is effective for annual periods beginning on or after January 1, 2018, with earlier adoption permitted. The standard may be applied retrospectively or using a modified retrospective approach. The Company has completed the review of the new standard and has concluded that there is no material impact to the timing of recognition or measurement of revenue under IFRS 15.

(ii) Financial Instruments

On July 24, 2015, the IASB issued the final version of IFRS 9, “Financial Instruments” (“IFRS 9”) to replace IAS 39, “Financial Instruments: Recognition and Measurement” (“IAS 39”).

IFRS 9 introduces a single approach to determine whether a financial asset is measured at amortized cost or fair value and replaces the multiple rules in IAS 39. The approach is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. For financial liabilities, IFRS 9 retains most of the IAS 39 requirements; however, where the fair value option is applied to financial liabilities, the change in fair value resulting from an entity’s own credit risk is recorded in OCI rather than net earnings, unless this creates an accounting mismatch. In addition, a new expected credit loss model for calculating impairment on financial assets replaces the incurred loss impairment model used in IAS 39. The new model will result in more timely recognition of expected credit losses. IFRS 9 also includes a simplified hedge accounting model, aligning hedge accounting more closely with risk management. Cathedral does not currently apply hedge accounting and does not value any financial liabilities at fair value.

IFRS 9 is effective for years beginning on or after January 1, 2018. The Company does not expect the change in the impairment model or any of the other changes to have a material impact on the consolidated financial statements.

(iii) Leases

In January 2016, the IASB issued IFRS 16 Leases that provides a single lease accounting model for lessees, which require the recognition of most leases as finance leases on the balance sheet.

This will result in the recognition of a lease liability and a corresponding recognition of a leased asset called right-of-use asset. On the statement of net earnings and comprehensive income, lease expense will be recognized and will consist of two components, depreciation expense of the right-of-use asset and interest expense related to the lease liability. Finance lease exemptions exist for short-term leases where the term is 12 months or less and for leases of low value items.

IFRS 16 comes into effect on January 1, 2019. The Company is currently evaluating the impact of adopting IFRS 16 on the consolidated financial statements.

4. Determination of fair values

A number of Cathedral’s accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

(a) Equipment

The fair value of equipment recognized because of a business combination is based on market values. The market value of equipment is the estimated amount for which a property could be exchanged on the date of valuation between a willing buyer and a willing seller in an arm’s length transaction after proper marketing wherein the parties had each acted knowledgeably and willingly. The fair value of items of equipment is based on the market approach and cost approaches using quoted market prices for similar items when available and replacement cost when appropriate.

(b) Inventories

Inventories consist of operating supplies and parts to be used in repairing equipment. The fair value of inventories is determined based on the net realizable value of these items.

(c) Trade and other receivables

The fair value of trade and other receivables is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. This fair value is determined for disclosure purposes.

(d) Non-derivative financial liabilities

Fair value, which is determined for disclosure purposes, is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date. For finance leases, the market rate of interest is determined by reference to similar lease agreements.

(e) Share-based payment transactions

The fair value of the employee share options is measured using the Black-Scholes option-pricing model. Measurement inputs include the share price on measurement date, the exercise price of the instrument, the expected volatility (based on weighted average historic volatility adjusted for changes expected due to publicly available information), the weighted average expected life of the instruments (based on historical experience and general option holder behavior), the expected dividends, forfeiture rate per annum and the risk-free interest rate (based on government bonds). Service and non-market performance conditions are not taken into account in determining fair value.

5. Cash and restricted cash equivalents

The Company's cash consist of balances in accounts with financial institutions. This balance does not include any term deposits and temporary investments or overdrafts. The Company's restricted cash equivalents consist of GICs that have been pledged as security for three outstanding letters of credit ("LOC") with the Company's former financial institution. These LOC were replaced by the current financial institution in January 2018 and these funds were returned to general accounts.

The Company's exposure to interest rate risk and a sensitivity analysis for financial assets and liabilities is disclosed in note 26.

6. Trade receivables

All of the Company's amounts are trade receivables. This balance does not include any related party amounts or other loans and receivables. All amounts are current assets. The Company's exposure to credit and currency risks, and impairment losses related to trade and other receivables is disclosed in note 26.

7. Inventories

All of the Company's inventories are composed of raw materials, consumables and work-in-progress. There are no finished goods inventories. For the year ended December 31, 2017, raw materials and consumables recognized as cost of sales were $34,198 (2016 - $25,885). Annually, a review of expected demand for inventory balances to be used in equipment repairs was conducted. In 2017 a write-down of $151 (2016 - $277) on inventory was recognized.

8. Equipment

Cost	Balance December 31 2015	Additions	Disposals	Effects of movements in exchange rates	Balance December 31 2016
Directional Drilling equipment	$ 144,770	$ 591	$ (2,461)	$ (78)	$ 142,822
Flow back and production testing equipment	64,048	41	(64,023)	(66)	-
Automotive equipment	1,308	-	(98)	(34)	1,176
Office and computer equipment	8,439	41	(3)	(59)	8,418
Automotive equipment under capital lease	2,809	46	(517)	(77)	2,261
Leasehold improvements	1,441	226	(531)	(22)	1,114
Total	$ 222,815	$ 945	$ (67,633)	$ (336)	$ 155,791

Accumulated depreciation	Balance December 31 2015	Additions	Disposals	Effects of movements in exchange rates	Balance December 31 2016
Directional Drilling equipment	$ 66,562	$ 11,391	$ (1,142)	$ (43)	$ 76,768
Flow back and production testing equipment	36,748	3,773	(40,521)	-	-
Automotive equipment	945	104	(82)	(23)	944
Office and computer equipment	6,799	570	-	(47)	7,322
Automotive equipment under capital lease	1,668	363	(369)	(41)	1,621
Leasehold improvements	1,175	112	(293)	(16)	978
Total	$ 113,897	$ 16,313	$ (42,407)	$ (170)	$ 87,633

Cost		Balance December 31 2016		Additions		Write-downs		Disposals		Effects of movements in exchange rates		Balance December 31 2017
Directional Drilling equipment	$	142,822	$	14,870	$	(23,484)	$	(7,506)	$	(147)	$	126,555
Office and computer equipment		8,418		61				-		(123)		8,356
Automotive equipment under capital lease		2,261		97				(966)		(96)		1,296
Automotive equipment		1,176		105				-		(68)		1,213
Leasehold improvements		1,114		-				-		(42)		1,072
Total	$	155,791	$	15,133	$	(23,484)	$	(8,472)	$	(476)	$	138,492

Accumulated depreciation		Balance December 31 2016		Additions		Write-downs		Disposals		Effects of movements in exchange rates		Balance December 31 2017
Directional Drilling equipment	$	76,768	$	10,120	$	(15,197)	$	(2,041)	$	(111)	$	69,539
Office and computer equipment		7,322		368				-		(110)		7,580
Automotive equipment under capital lease		1,621		162				(708)		(75)		1,000
Automotive equipment		944		73				-		(47)		970
Leasehold improvements		978		81				-		(39)		1,020
Total	$	87,633	$	10,804	$	(15,197)	$	(2,749)	$	(382)	$	80,109

Net book values		2017		2016
Directional Drilling equipment	$	57,016	$	66,054
Office and computer equipment		776		1,096
Automotive equipment under capital lease		296		640
Automotive equipment		243		232
Leasehold improvements		52		136
Total	$	58,383	$	68,158

On December 16, 2016, the Company entered into a definitive agreement to sell the fixed assets of its flowback and production testing ("F&PT") CGU. As such, the net realizable value of the F&PT equipment was reclassified as assets held for sale on the consolidated balance sheet (see note 10).

Leased automotive equipment

The Company leases equipment under a number of finance lease agreements. The leased equipment secures lease obligations (see note 14). During 2017, there were non-cash fixed asset additions of $45 (2016 - $nil) related to finance lease arrangements.

Review for impairment

The Company reviews the carrying value of equipment and intangible assets at each reporting period where there are indicators of impairment.

The Company determined an impairment test for the directional drilling CGU was not required as at December 31, 2017. However, the Company chose to write-off certain assets where utilization was very low due to low market demand in the amount of $8,287. The assets written down included non-proprietary drilling motors and certain non-proprietary MWD systems. The non-proprietary MWD systems had been purchased related to the disposed of international operations and were retained by the Company after the sale of DPI in 2016 Q1. This equipment was not used extensively in the Company's North American operations and was fully written-off. The Company has experienced lower demand for non-proprietary mud motors in the current drilling environment as their performance capabilities are lower than the Company's proprietary mud motors. The Company conducted a review and wrote-off the remaining net book value for any non-proprietary mud motors that were no longer expected to be utilized.

The Company conducted a review for impairment of equipment as at December 31, 2016. The recoverable amount of each CGU was determined using the discounted cash flow model for value-in-use for each CGU. This was determined based on a detailed budget of revenues was prepared based upon revenue forecasted by heads of sales departments. The budget was prepared with consultation of senior operating managers and accounting staff based upon existing costs, historical information and anticipated cost reductions. The detailed budget was used to prepare a high level for the next two years. Variable costs were adjusted based on percentage of sales, while fixed costs were maintained at current levels, with increases to wages as the recovery progresses. Cash flow projections thereafter have been extrapolated based on a 5% per annum growth rate and incorporate a future 25% downturn in the 11th year of the forecast. The forecasted cash flows are based on management's best estimates of pricing, activity levels, costs to maintain equipment and a pre-tax discount rate of 14% per annum. A terminal value was used based on the annual growth rate for cash flows through the remainder of the segment's life. Based on these cash flows to determine value in use, there was no impairment of equipment or intangible assets at December 31, 2016.

9. Intangible assets

The Company's intangible assets consist of internally generated development costs related to its Directional Drilling division. The Company reviews

the accumulated costs at least quarterly. In 2017 the Company recognized an impairment of $146 on in progress intangibles (2016 - $nil).

		2017		2016
Cost				
Balance at January 1	$	2,665	$	2,505
Internally developed additions		474		160
Write-down		(146)		-
Balance at end of year	$	2,993	$	2,665
Accumulated amortization				
Balance at January 1	$	687	$	499
Amortization for year		353		188
Balance at end of year	$	1,040	$	687
Net carrying value at end of year	$	1,953	$	1,978

10. Assets held for sale and discontinued operations

On December 16, 2016, the Company entered into an agreement to sell the fixed assets of its F&PT CGU. As such, the net realizable value of the F&PT equipment has been reclassified as assets held for sale on the consolidated balance sheet and the related operations have been presented as discontinued operations for 2017 and 2016. The sale closed in January 2017, and as at December 31, 2016 the assets had been written down to their estimated net realizable value of $17,241.

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

		2017		2016
Revenues	$	361	$	6,305
Cost of sales:				
Direct costs		(430)		(6,318)
Depreciation		(21)		(4,010)
Share-based compensation		-		-
Total cost of sales		(451)		(10,328)
Gross margin		(90)		(4,023)
Selling, general and administrative expenses:				
Direct costs		(66)		(1,787)
Depreciation		-		(1)
Share-based compensation		3		(6)
Total selling, general and administrative expenses		(63)		(1,794)
		(153)		(5,817)
Gain (loss) on disposal of property and equipment		14		(48)
Finance costs		(3)		(18)
Loss before income taxes		(142)		(5,883)
Income tax recovery:				
Deferred		-		1,794
Total income tax recovery		-		1,794
Net loss from discontinued operations		(142)		(4,089)
Write-down of assets held for sale from discontinued operations, net of tax		-		(4,307)
Total loss from discontinued operations	$	(142)	$	(8,396)

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

		2017		2016
Cash provided by (used in):				
Operating activities:				
Total loss from discontinued operations	$	(142)	$	(8,396)
Items not involving cash				
Depreciation		21		4,011
Share-based compensation		(3)		6
Income tax recovery		-		(1,794)
(Gain) loss on disposal of property and equipment		(14)		48
Finance costs		3		18
Write-down of assets held for sale		-		4,307
Cash flow from (used in) discontinuing operations	$	(135)	$	(1,800)

11. Deferred tax assets and income tax expense

Recognized deferred tax assets and liabilities

Deferred tax assets are attributable to the following:

		2017		2016
Property and equipment	$	(8,009)	$	(10,402)
Non-capital loss carry forwards		9,302		9,547
Scientific research and development expenditures		4,786		4,876
Investment tax credits		3,323		3,247
Inventory valuation allowance		749		772
Intangible assets		207		223
Provision for settlement		180		1,250
Total	$	10,538	$	9,513

Movement in temporary differences during the year

		Balance December 31 2015		Recognized in profit		Recognized in OCI		Balance December 31 2016
Property and equipment	$	(11,493)	$	1,106	$	(15)	$	(10,402)
Non-capital loss carry forwards		5,686		3,861		-		9,547
Scientific research and development expenditures		4,776		100		-		4,876
Investment tax credits		2,339		908		-		3,247
Inventory valuation allowance		1,071		(299)		-		772
Intangible assets		231		(8)		-		223
Provision for settlement		-		1,250		-		1,250
Total	$	2,610	$	6,918	$	(15)	$	9,513

		Balance December 31 2016		Recognized in profit		Recognized in OCI		Balance December 31 2017
Property and equipment	$	(10,402)	$	2,384	$	9	$	(8,009)
Non-capital loss carry forwards		9,547		(245)		-		9,302
Scientific research and development expenditures		4,876		(90)		-		4,786
Investment tax credits		3,247		76		-		3,323
Inventory valuation allowance		772		(23)		-		749
Intangible assets		223		(16)		-		207
Provision for settlement		1,250		(1,070)		-		180
Total	$	9,513	$	1,016	$	9	$	10,538

The income taxes are based upon the estimated annual effective rates of 27% (2016 – 27%) for Canadian entities and 36% (2016 – 36%) for U.S. entities. Deferred taxes for U.S. entities were booked at new rate of 22.5%. The income tax expense for the period is comprised as follows:

		2017		2016
Current tax (expense) recovery:				
Current period	$	(327)	$	(161)
Adjustment to prior period provisions		(78)		55
Total current tax (expense) recovery		(405)		(106)
Deferred tax (expense) recovery:				
Origination and reversal of temporary differences		546		3,534
Adjustment to prior period provisions		470		(89)
Total deferred tax recovery		1,016		3,445
Income tax recovery	$	611	$	3,339

Income tax expense for 2017 and 2016 differs from the amount that would be expected by applying the expected statutory income tax rates for the following reasons:

		2017		2016
Expected statutory tax rate		27%		27%
Loss before income tax	$	(382)	$	(722)
Effective tax rate applied to loss before income tax	$	103	$	195
Adjustment to deferred taxes for change in effective tax rates		(371)		39
Income taxed in jurisdictions with different tax rates		74		(302)
Non-deductible expenses		(147)		3,251
Adjustment to prior year tax provisions		393		(34)
Non-taxable portion of gain on disposal of property and equipment		522		177
Other		37		13
Total tax recovery	$	611	$	3,339

12. Operating loans

		2017		2016
Canadian dollar operating loan	$	1,233	$	1,250
U.S. dollar operating loan		-		855
Total	$	1,233	$	2,105

The Company has a $5,000 operating facility (2016 - $5,000) with a major financial institution. The terms and conditions of this loan are as disclosed in note 14.

13. Trade and other payables

		2017		2016
Trade payables	$	12,661	$	9,325
Accrued payables		5,265		3,512
Total	$	17,926	$	12,837

The Company's exposure to currency and liquidity risk related to trade and other payables is disclosed in note 26.

14. Loans and borrowings

		2017		2016
Current liabilities:				
Current portion of finance lease liabilities	$	233	$	459
Non-current liabilities:				
Finance lease liabilities	$	46	$	72
Secured revolving term loan		-		26,250
Total	$	46	$	26,322

During 2017, there were advances of $nil and repayments of $26,250 on the Company's secured revolving term loan.

Terms and debt repayment schedule

During December 2017, the Company signed a new credit facility (the "Facility") with a new lending syndicate. The Facility consists of a $5 million operating facility and $15 million extendible revolving credit facility and expires December 31, 2019. The Facility is secured by a general security agreement over all present and future personal property. The Facility defines EBITDA ("Credit Agreement EBITDA") to be used in calculation of financial covenants.

The financial covenants associated with the amended Facility are:

Consolidated funded debt to consolidated Credit Agreement EBITDA ratio shall not exceed 3.0:1.00; and
Consolidated interest coverage ratio shall not be less than 2.5:1.00.

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

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

At December 31, 2017, the Company had cash balances in excess of outstanding letters of credit and capital lease obligations. As such its funded debt to Credit Agreement EBITDA ratio ("Funded debt ratio") was negative (i.e. net cash balance). As such, the Funded debt ratio has been met, but is not meaningful ("NM") for presentation. For the rolling twelve months ended December 31, 2017 Credit Agreement EBITDA was $20,374.

Ratio	Actual	Required
Consolidated funded debt to consolidated Credit Agreement EBITDA ratio	NM	3.0:1
Consolidated interest coverage ratio	29.8:1	2.5:1

Finance lease liabilities

Finance lease liabilities bear interest at rates between 5.6% and 6.7% with maturities from 2018 to 2019 and are payable as follows:

	2017			2016		
	Future minimum lease payments	Interest	Present value of minimum lease payments	Future minimum lease payments	Interest	Present value of minimum lease payments
Less than one year	$ 209	(1)	$ 208	$ 456	(5)	$ 451
Between one and four years	72	(1)	71	85	(5)	80
Total	$ 281	$ (2)	$ 279	$ 541	$ (10)	$ 531

These amounts are secured by the automotive equipment under capital lease which has a net book value of $640 (2016 - $1,141).

15. Provisions for settlement

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

The Settlement Agreement covered claims from employed and contracted MWD and DD staff who participated in the settlement. Under the terms of the Settlement Agreement, the parties established an initial settlement fund of up to $3,400 USD. The final determination of the settlement fund amount was based on the number of claimants that participated in the settlement at the end of December 2016, which under the terms of the Settlement Agreement is confidential. The settlement fund payments will be paid quarterly by the Company over a three-year period with the final payment due on or before September 2019. The quarterly payments may be accelerated in the event Cathedral meets certain financial targets over the payment period and can be deferred if a scheduled payment would put Cathedral in violation of its credit facility covenants subject to not more than three payments being deferred. In 2017 the majority of the payments under the Settlement Agreement were made.

In 2017 Q1, the Company entered a settlement with one of its U.S. clients related to a down-hole drilling incident in December 2013. The terms of this settlement agreement are confidential and following an initial payment in 2017 Q1 involve a series of quarterly payments to occur until 2021. During 2016 Q4, there was an increase the settlement provision of $421.

During 2017, payments of $2,607 (2016 - $851) were made under the Settlement Agreements.

16. Share capital

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

Common shares issued:

	2017		2016	
	Number	Amount	Number	Amount
Issued, beginning of period	36,295,380	$ 74,481	36,295,380	$ 74,481
Issued on bought deal and private placement	12,616,071	13,131	-	-
Issued on exercise of options	472,500	447	-	-
Issued, end of period	49,383,951	$ 88,059	36,295,380	$ 74,481

Issuance of common shares

11,500,000 shares were issued on February 15, 2017 on a bought deal basis (the "Bought Deal") and concurrent with the Bought Deal, 1,116,071 shares were issued to certain directors and officers on an insider private placement basis. Shares were issued at $1.12 per share. There were $999 in share issue costs that have been deducted against the gross proceeds of $14,130.

472,500 common shares were issued as a result of the exercise of vested options arising from grants to employees in 2015. Options were exercised at an average strike price of $0.75 per option. All issued shares are fully paid.

Dividends

Effective November 10, 2015 the Company suspended quarterly dividend payments.

Issuance of share options

The Company's share based compensation plan is a "rolling number" type option plan which provides that the number of authorized but unissued common shares that may be subject to options granted under the share option plan at any time can be up to 10% of the number of common shares outstanding from time to time.

Under the plan, the exercise price of each option at the date of issuance equals the volume adjusted weighted average trading value of of the Company's common shares for the five days prior to the grant, and has a maximum term till expiry of ten years. Options issued in 2015 Q4 and subsequent vest over a period of two years, options issued in 2015 Q3 and previously vest over three years from the date of grant as employees, directors or consultants render continuous service to the Company.

A summary of the status of the Company's equity based compensation plan as at December 31, 2017 and 2016, and changes during the years then ended is presented below:

		2017		2016
	Number	Weighted average exercise price	Number	Weighted average exercise price
Outstanding, beginning of year	1,350,500	$ 1.85	2,146,597	$ 3.18
Granted	2,197,750	1.08	30,000	0.43
Expired or forfeited	(128,750)	2.20	(826,097)	5.27
Exercised	(472,500)	0.75	-	-
Outstanding, end of year	2,947,000	$ 1.43	1,350,500	$ 1.85
Exercisable, end of year	593,319	$ 2.50	506,806	$ 2.27

The range of exercise prices for the options outstanding at December 31, 2017 is as follows:

	Total outstanding options			Exercisable	
Exercise price range	Number	Weighted average exercise price	Weighted average remaining life (in years)	Number	Weighted average exercise price
$0.43 to $1.00	84,000	$ 0.71	0.98	77,333	$ 0.74
$1.01 to $2.00	2,169,000	1.08	2.38	13,333	1.99
$2.01 to $3.00	574,000	2.13	1.20	382,653	2.13
$3.01 to $4.89	120,000	4.89	0.48	120,000	4.89
$0.43 to $4.89 total	2,947,000	$ 1.43	2.03	593,319	$ 2.50

During the year ended December 31, 2017, the Company has recorded share-based compensation expense of $275 (2016 - $144) related to the share option plan.

During the year ended December 31, 2017, the Company granted 2,197,750 share options. The following table sets out the assumptions used in applying the Black-Scholes option-pricing model for the options issued as well as the resulting fair value:

	2017 Q1	2017 Q3
Number of options issued	1,141,250	1,056,500
Exercise price	$ 1.13	$ 1.02
Fair value per option (weighted average)	$ 0.52	$ 0.48
Expected annual dividend per share	$ -	$ -
Risk-free interest rate (weighted average)	0.8%	1.2%
Expected share price volatility (weighted average)	101.9%	79.2%
Forfeiture rate per annum	10.0%	10.0%

17. Earnings (loss) per share

Basic earnings per share

The calculation of basic earnings per share at December 31, 2017 was based on the profit (loss) attributable to common shareholders of $229 being net earnings from continuing operations (2016 - $2,617) and net earnings of $87 (2016 – loss $5,779) and a weighted average number of common shares outstanding of 47,380,723 (2016 – 36,295,380), calculated as follows:

Weighted average number of ordinary shares

	2017	2016
Issued January 1	36,295,380	36,295,380
Effect of share options exercised	11,085,343	-
Weighted average number of common shares at end of year	47,380,723	36,295,380

Diluted earnings per share

The calculation of diluted earnings per share at December 31, 2017 was based on the profit attributable to common shareholders of $229 being net earnings from continuing operations (2016 - $2,617) and net earnings of $87 (2016 – not applicable as loss) and a weighted average number of common shares outstanding of 47,577,298 (2016 – 36,295,380), calculated as follows

Weighted average number of common shares (diluted)

	2017	2016
Weighted average number of common shares (basic)	47,380,723	36,295,380
Effect of share options on issue	196,575	-
Weighted average number of common shares (diluted) at end of year	47,577,298	36,295,380

At December 31, 2017, 2,863,000 options (2016 – 1,350,000) were excluded from the diluted weighted average number of common shares calculation as their effect would have been anti-dilutive. The average market value of the Company's common shares for purposes of calculating the dilutive effect of share options was based on quoted market prices for the period during which the options were outstanding.

18. Gain on disposal of foreign subsidiary

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

19. Nature of expenses

The nature of expenses can be specified as follows:

		Cost of sales		Selling, general and administrative		Total
Year ended December 31, 2017						
Depreciation	$	(11,043)	$	(104)	$	(11,147)
Share-based compensation		(69)		(206)		(275)
Staffing costs, excluding share-based compensation		(48,862)		(9,887)		(58,749)
Repairs and maintenance		(36,983)		-		(36,983)
Other expenses		(34,573)		(5,501)		(40,074)
Total	$	(131,530)	$	(15,698)	$	(147,228)
Year ended December 31, 2016						
Depreciation	$	(12,358)	$	(134)	$	(12,492)
Share-based compensation		(14)		(130)		(144)
Staffing costs, excluding share-based compensation		(28,795)		(9,991)		(38,786)
Repairs and maintenance		(17,207)		-		(17,207)
Other expenses		(16,989)		(4,930)		(21,919)
Total	$	(75,363)	$	(15,185)	$	(90,548)

20. Foreign exchange gain (loss) and finance costs

		2017		2016
Foreign exchange gain (loss):				
Realized foreign exchange loss	$	(120)	$	(17)
Unrealized foreign exchange gain on intercompany balances		1,903		1,455
Foreign exchange gain (loss)	$	1,783	$	1,438
Finance costs				
Interest on revolving term loan	$	(150)	$	(1,455)
Interest on operating loan		(49)		(114)
Standby fees		(151)		(141)
Interest on finance lease liabilities		(15)		(17)
Other interest		(319)		(334)
Finance costs	$	(684)	$	(2,061)

21. Changes in non-cash working capital

The components of changes in non-cash working capital are as follows:

		2017		2016
Trade receivables	$	(7,640)	$	(3,139)
Inventories		(3,243)		2,294
Prepaid expenses and deposits		151		(142)
Trade and other payables		5,089		1,823
Impact of foreign exchange rate differences		(1,380)		(28)
Total changes in non-cash working capital		(7,023)		808
Changes in investing non-cash working capital		1,925		(762)
Changes in operating non-cash working capital	$	(8,948)	$	1,570

22. Operating segments

The Company and its wholly owned subsidiaries are engaged in the business of providing directional drilling services to oil and natural gas companies in western Canada and selected basins in the U.S., and is viewed as a single operating segment by the chief operating decision maker of the Company for the purpose of resource allocation and assessing performance.

Directional drilling services are currently being provided in both Canada and the U.S. The amounts related to each geographic segment are as follows:

Geographical information

The Company conducts operations in the following geographic areas:

	Revenues		Non-current assets	
	Year ended December 31, 2017	Year ended December 31, 2016	December 31, 2017	December 31, 2016
Canada	$ 32,315	$ 22,220	$ 47,941	$ 45,741
United States	114,780	58,646	22,933	33,908
Total	$ 147,095	$ 80,866	$ 70,874	$ 79,649

Major customer

In 2017 revenues from a customer of the Company represented approximately 20% (2016 – two different customers represented approximately 22%) of the Company's total revenues.

23. Commitments

In the normal course of business, the Company incurs contractual obligations and those obligations are disclosed in the Company's annual financial statements for the year ended December 31, 2017. As at December 31, 2017, the Company's commitment to purchase equipment is approximately $3,317. Cathedral anticipates expending these funds in 2018 Q1.

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

- two LOC securing rent payments on property leases and renew annually with the landlords. The first LOC is $700 CAD for the first ten years of the lease and then reduces to $500 for the last five years of the lease. The second LOC is currently for $542 USD and increases annually based upon annual changes in rent;
- $75 USD issued for U.S. workers compensation coverage; and
- two LOC securing the Company's corporate credit cards in the amounts of $100 CAD and $150 USD.

24. Operating leases

Leases as lessee

The Company leases a number of offices, warehouse and operating facilities under operating leases. The leases typically run for a period of at least five years, with an option to renew the lease after that date. Leases incurred in relation to sale and leaseback transactions have longer lease terms. Current leases have expiries ranging from December 2018 to March 2030. Certain leases have set annual increases. The total future minimum lease payments are as follows:

2018	$3,537
2019	3,119
2020	2,924
2021	2,907
2022	2,960
Thereafter	17,134

Certain vehicle leases have been renewed on a month-to-month term at the expiration of the finance type lease. These leases have been classified as operating leases.

During the year ended December 31, 2017, an amount of $3,671 was recognized as an expense in profit or loss in respect of operating leases (2016 - $3,952).

25. Related parties

Key management personnel compensation

Cathedral has determined that the key management personnel of the Company consist of its executive officers and directors.

In addition to their salaries and director's fees, the Company also provides non-cash benefits to directors and executive officers including participation in the Company's share option program (see note 16).

Certain executive officers have employment agreements. Upon resignation at the Company's request, they are entitled to termination benefits including: i) 1.5 to 2.0 times base salary; ii) 1.5 to 2.0 times average annual bonus over the past 3 years; and iii) health, dental, life insurance and disability coverage for 18 to 24 months.

Key management personnel (including directors) compensation comprised:

	2017	2016
Short-term employment benefits	$ 1,546	$ 1,850
Share-based compensation	120	99
Total expense recognized as share-based compensation	$ 1,666	$ 1,949

Key management personnel and director transactions

Directors and executive officers of the Company control approximately 6% of the common shares of the Company.

There have been no other transactions over the reporting period with key management personnel (2016 - nil), and no outstanding balances exist as

at period end (2016 - nil).

26. Financial risk management and financial instruments

Overview

The Company has exposure to the following risks from its use of financial instruments:

- credit risk
- liquidity risk
- market risk

This note presents information about the Company's exposure to each of the above risks, the Company's objectives, policies and processes for measuring and managing risk, and the Company's management of capital.

Risk management framework

The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. 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 limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Company's activities.

Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's receivables from customers.

Trade and other receivables

The Company's exposure to credit risk is influenced mainly by the individual characteristics of each customer. However, management also considers the demographics of the Company's customer base, including the default risk of the industry and country in which customers operate, as these factors may have an influence on credit risk. Approximately 13% of the Company's receivables are attributable to sales transactions with a single customer. In 2016, two different customers were approximately 12% and 10% of the Company's receivables.

The Company has established a credit policy under which each new customer is analyzed individually for creditworthiness before the Company's standard payment and delivery terms and conditions are offered. The Company's review includes external ratings, when available. Customers that fail to meet the Company's benchmark creditworthiness generally are restricted to services on a prepayment basis only.

In monitoring customer credit risk, customers are grouped according to their credit characteristics, including whether they are an individual or legal entity, geographic location, industry, aging profile, maturity and existence of previous financial difficulties. Customers that are considered as "high risk" are closely monitored, and future sales may be made on a prepayment basis.

The Company does not require collateral in respect of trade and other receivables.

The Company establishes an allowance for impairment that represents its estimate of incurred losses in respect of trade and other receivables and investments. The main components of this allowance are a specific loss component that relates to individually significant exposures, and a collective loss component established for groups of similar assets in respect of losses that have been incurred but not yet identified. The collective loss allowance is determined based on historical data of payment statistics for similar financial assets.

Exposure to credit risk

The carrying amount of financial assets represents the maximum credit exposure. The maximum exposure to credit risk at the reporting date was.

Carrying amount

		2017		2016
Trade receivables	$	33,885	$	26,245

The maximum exposure to credit risk for trade and other receivables at the reporting date by geographic region was:

Carrying amount

		2017		2016
Canada	$	7,896	$	7,753
United States		25,989		18,492
Total	$	33,885	$	26,245

The Company's most significant customer accounts for $5,151 of the trade receivables carrying amount at December 31, 2017 (2016 - $6,168).

Impairment losses

The aging of trade and other receivables at the reporting date was:

	2017				2016			
		Gross		Impairment		Gross		Impairment
Not past due	$	29,178	$	(58)	$	22,680	$	-
Past due 61-90 days		2,922		-		3,176		-
Past due over 91 days		1,899		(56)		822		(433)
Total	$	33,999	$	(114)	$	26,678	$	(433)

The movement in the allowance for impairment in respect of trade and other receivables during the year was as follows:

		2017		2016
Balance, beginning of year	$	433	$	460
Reversals of losses previously recognized		(375)		(27)
Balance, end of year	$	58	$	433

At December 31, 2017 an impairment loss of $64 (2016 - $433) was recognized relating to customers that have been unable to make payments in accordance with normal terms and conditions, mainly due to economic circumstances. The Company believes that the unimpaired amounts that are past due are still collectible, based on historic payment behavior and an analysis of the underlying customers' ability to pay.

Based on historic default rates, the Company believes that, apart from the above, no impairment allowance is necessary in respect of trade receivables not past due.

Impairment losses

The allowance accounts in respect of trade and other receivables are used to record impairment losses unless the Company is satisfied that no recovery of the amount owing is possible; at that point the amounts are considered irrecoverable and are written off against the financial asset directly.

Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting the obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. The Company'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, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Company's reputation.

The following are the contractual maturities of financial liabilities, including estimated interest payments and excluding the impact of netting agreements based upon the secured revolving term loan being renewed on the same terms and not converted to a non-revolving term loan.

December 31, 2017		Carrying amount		Contractual cash flow		Under 6 months		6-12 months		1-2 years		2-5 years		Thereafter
Demand bank loans	$	1,233	$	1,233	$	1,233	$	-	$	-	$	-	$	-
Secured revolving term loan		-		-		-		-		-		-		-
Finance lease liabilities		279		285		222		14		49		-		-
Trade and other payables		17,926		17,926		17,926		-		-		-		-
	$	19,438	$	19,444	$	19,381	$	14	$	49	$	-	$	-

It is not expected that the cash flows included in the maturity analysis could occur significantly earlier, or at significantly different amounts.

Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices will affect the Company's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return.

Currency risk

The Company is exposed to currency risk on working capital and borrowings that are denominated in a currency other than the respective functional currencies of Company entities, primarily CAD, but USD. The currencies in which these transactions primarily are denominated are CAD and USD.

Generally, borrowings are denominated in currencies that match the cash flows generated by the underlying operations of the Company, primarily dollar. This provides a partial economic hedge without derivatives being entered into and therefore hedge accounting is not applied in these circumstances.

Cathedral's foreign currency policy is to monitor foreign current risk exposure in its areas of operations and mitigate that risk where possible by matching foreign currency denominated expense with revenues denominated in foreign currencies. Cathedral strives to maintain limited amounts of cash and cash equivalents denominated in foreign currency on hand and attempts to limit its exposure to foreign currency through collecting and paying foreign currency denominated balance in a timely fashion.

The Company's exposure to foreign currency risk related to USD denominated balances as follows:

USD		2017		2016
Cash and restricted cash	$	2,805	$	1,577
Trade receivables		25,990		13,772
Trade payables		(9,807)		(5,827)
Finance lease liabilities		(193)		(301)
Total	$	18,795	$	9,221

The following significant exchange rates applied during the year:

	Average rate				Reporting date spot rate			
		2017		2016		December 31, 2017		December 31, 2016
USD $1 to CAD	$	1.30	$	1.33	$	1.26	$	1.34

Sensitivity analysis

A 10% strengthening of CAD against USD at December 31 would decrease equity and other comprehensive income by $2,148 (2016 - $1,126). The analysis assumes that all other variables, in particular interest rates remain constant. The analysis is performed on the same basis for 2016, albeit that the reasonably possible foreign exchange rate variances were different.

A weakening of CAD at December 31 would have had the equal but opposite effect on USD amounts, on the basis that all other variables remain constant.

Interest rate risk

At the reporting date the interest rate profile of the Company's interest-bearing financial instruments was:

	December 31, 2017		December 31, 2016	
	Fixed rate carrying value	Variable rate carrying value	Fixed rate carrying value	Variable rate carrying value
Financial liabilities	$ 279	$ 1,233	$ 531	$ 28,355

Cash flow sensitivity analysis for variable rate instruments

A 1% increase in the Company's financial institution's lending rate would cause interest expense to increase by approximately $12 (2016 - $283) per annum based upon the balance of financial institution indebtedness and long-term debt with a floating interest rate outstanding as at December 31, 2017.

Fair values of financial instruments

The Company has designated its trade and other payables as other financial liabilities carried at amortized cost. Accounts receivable are designated as loans and receivables, measured at amortized cost. The Company's carrying values of these items approximate their fair value due to the relatively short periods to maturity of the instruments. Loans and borrowings have been designated as other financial liability, and are measured at amortized cost. The fair value of loans and borrowings included in the consolidated statement of financial position approximates carrying values as the indebtedness is subject to floating rates of interest.

The basis for determining fair values is disclosed in note 4.

Capital management

The Board of Directors' policy is to maintain a strong capital base to maintain investor, creditor and market confidence and to sustain future development of the business. Management and the Board of Directors monitor capital using loans and borrowings, including current portion to total capitalization and funded debt to earnings before interest, taxes, depreciation, amortization and share-based compensation ("Credit Agreement EBITDA") both of which are defined in the credit agreement.

The Board of Directors seeks to maintain a balance between the higher returns that might be possible with higher levels of borrowings and the advantages and security afforded by a sound capital position. In response to the overall decline in activity levels and profitability, the Company implemented a number of cost cutting initiatives to protect the Company's balance sheet.

The Company's loans and borrowings to total capitalization and Credit Agreement EBITDA ratios at the end of the reporting period are disclosed in note 14.

There were no changes in the Company's approach to capital management during the year.

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David Diachok, Vice President, Sales

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