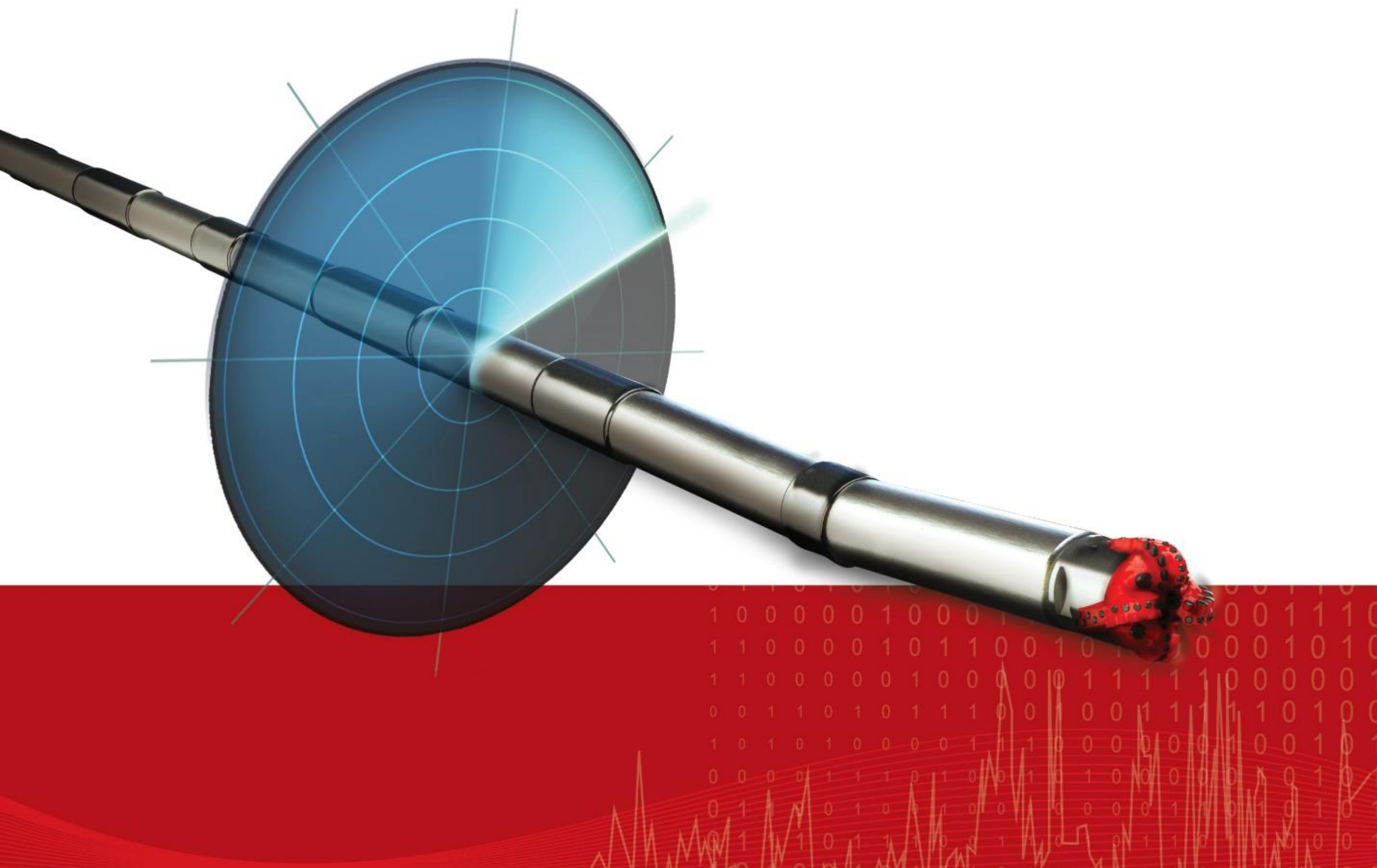
2018 ANNUAL REPORT

BETTER PERFORMANCE EVERY DAY

CATHEDRAL



FIVE YEAR FINANCIAL HISTORY

Dollars in 000's except per share amounts

	2018	2017	2016	2015 [5]	2014 [5]
Revenues [4]	**$ 160,827**	$ 147,095	$ 80,866	$ 106,243	$ 208,655
Adjusted gross margin % [1] [4]	**11%**	18%	22%	18%	21%
Total Adjusted EBITDAS [1]	**$ 12,060**	$ 18,674	$ 5,840	$ 7,699	$ 38,487
Diluted per share	**$ 0.24**	$ 0.39	$ 0.16	$ 0.21	$ 1.06
Cash flow - operations	**$ 3,732**	$ 2,952	$ 4,140	$ 25,931	$ 36,941
Gain on disposal / (Write-down of) investment in associate and related assets	**$ -**	$ -	$ 10,865	$ -	$ 177
Write-downs of goodwill, equipment and inventory	**$ (1,474)**	$ (8,584)	$ (277)	$ (12,773)	$ -
Earnings (loss) before income taxes	**$ (6,139)**	$ (382)	$ (722)	$ (24,894)	$ 8,112
Basic and diluted per share	**$ (0.12)**	$ (0.01)	$ (0.02)	$ (0.69)	$ 0.22
Write-down of deferred taxes related to CRA settlement	**$ -**	$ -	$ -	$ (10,346)	$ -
Derecognition of deferred tax asset	**$ (13,059)**	$ -	$ -	$ -	$ -
Net earnings (loss)	**$ (17,061)**	$ 87	$ (5,779)	$ (35,342)	$ 10,283
Basic and diluted per share	**$ (0.35)**	$ -	$ (0.16)	$ (0.97)	$ 0.28
Cash dividends declared per share [2]	**$ -**	$ -	$ -	$ 0.1200	$ 0.3300
Equipment additions [3]	**$ 17,391**	$ 11,322	$ 899	$ 6,908	$ 30,763
Net equipment additions [1]	**$ 4,514**	$ 2,371	$ (4,387)	$ (4,210)	$ 25,213
Weighted average shares outstanding					
Basic (000s)	**49,445**	47,381	36,295	36,295	36,244
Diluted (000s)	**49,586**	47,577	36,295	36,295	36,255
Working capital	**$ 30,599**	$ 31,016	$ 39,324	$ 13,550	$ 38,135
Total assets	**$ 121,770**	$ 121,630	$ 136,017	$ 155,610	$ 230,534
Loans and borrowings excluding current portion	**$ 7,000**	$ 46	$ 26,322	$ 30,477	$ 56,142
Shareholders' equity	**$ 89,143**	$ 101,391	$ 90,772	$ 96,607	$ 128,368

(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 2014 to 2017 exclude Discontinued Operations.

(5) 2014 and 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 9, 2019 at our Head Office 6030 – 3 Street SE, Calgary, Alberta.

REPORT TO SHAREHOLDERS

2018 was a challenging year for Cathedral from an operations execution perspective. Although revenues grew 9% from $147 million in 2017 to $160 million, in 2018 our EBITDAS declined from $18.7 million to $12.1 million. The EBITDAS decline was due to increased repair and rental expenses along with operational issues that led to non-recurring margin compression in 2018 Q2.

In 2018 Q1, we implemented a number of cost saving measures which started to positively impact results in late Q2. These included better controls on rental expenses, trucking and continued focus on labour costs and efficiencies. Over the year, we also implemented engineering improvements to our equipment to improve durability and performance in order to mitigate equipment repair and refurbishment costs in future quarters.

Our financial results for 2018 Q3 were greatly improved compared to the first half of the year with EBITDAS of $6.2 million which included a favorable impact from gain on lost-in-hole equipment. Compared to 2018 Q3, 2018 Q4 results were impacted by lower lost-in-hole gains and also SG&A increases due largely to one-time events, however, our Q4 adjusted gross margin was consistent at 15% versus 16% in Q3. 2018 Q4 contained some one-time expenses in cost of sales as well. Although we have been able to achieve price increases from our customers over the past two years, our labour and supplier related costs, particularly in the U.S., have also increased over the same period. We continue to look for opportunities to further optimize our operational expenses.

In late 2018, we elected to close our Washington, Pennsylvania (PA) district office and shop. The closure coincided with the need to commit to a new lease in the face of the type of drilling and lower activity levels in the Northeast U.S. (Utica and Marcellus basins) compared to other regions Cathedral operates, in such as the Permian. Cathedral intends to remain active in the U.S. Northeast (NE) market; however, both motors and Measurement-While-Drilling ("MWD") equipment for the area is now being provisioned from our Oklahoma City (OKC), Oklahoma facility. Since closing the PA facility, the consolidation of NE U.S. operations into OKC has been successful. We have maintained client service levels while reducing overhead costs. We are also benefiting from deploying the PA equipment to other more active Cathedral U.S. locations.

2018 again saw us significantly increasing our new equipment capital expenditures. The objectives with our capital program are to achieve higher drilling performance, reduce operating costs and grow our job capacity. Over the past two years, we have spent $29 million in new equipment including the replacement of equipment lost-in-hole. When customers lose equipment downhole, it is typically replaced with the most current generation of equipment which often results in an incremental upgrade to the overall equipment fleet. Substantially all our equipment additions are targeted at the U.S. market where we believe we have stronger growth opportunities.

The main focus of our capital expenditure program to the end of 2018 has been on drilling motors as they currently provide the biggest performance differentiator in the market. In 2018, we introduced 3 new versions of our very successful CLAW™ motor series. These motors included our CLAW™ 250 (7 1/4") and 400 (7") power sections which deliver specific performance characteristics targeted at drilling programs in higher mud flow, deeper drilling environments. 92 of these motors were added to our fleet in 2018. In addition, we added 12 of our CLAW™ 650 (5 5/8") motor which is targeted specifically for 6-3/4" holes sizes in rotary steerable application rentals. These rental motors are deployed in both the U.S. and Canada. We also continued to invest in MWD equipment adding additional EMc2 downhole generators and making significant upgrades to our MWD fleet.

On the technology development front, we achieved a number of accomplishments in 2018. We continue to be on track to introduce our next generation FUSION™ Dual Telemetry (DT) (MWD) tool in 2019. The proposed tool design will incorporate improvements over Cathedral's existing FUSION™ DT platform and compared to competitive products. In 2018, we finalized the mechanical design of the new DT tool and deployed the first prototypes for field testing by year end. Electronics design changes were made to improve reliability, performance and enable operation in higher temperature environments in addition to allowing the future MWD tool strings to be shorter than previous generation systems. Reducing the overall MWD tool length reduces its overall mass which mitigates shock and vibration impacts along with reducing equipment capital costs and facilitating off-site tool assembly and transport to site. Improvements were also made to the Cathedral's MWD surface detection equipment to improve detection capabilities along with being able to use one version of the equipment across Cathedral's MWD equipment fleet for both EM and pulse detection. Finally, we introduced an upgraded FUSION RP (Rotary Pulse) system to incorporate a higher torque capability. This capability further resists plugging of the tool and also improves its transmission speed and pulse signal amplitude to improve surface detection.

In 2018 Q1, Cathedral was approved for financial contribution from the Government of Canada under its Industrial Research Assistance Program (IRAP) in connection with Cathedral's next generation DT MWD project. The IRAP grant reimburses Cathedral for certain technology development costs and has allowed Cathedral to hire additional technical resources and expand the DT project scope. The IRAP grant was initially approved at $300,000 over 2 years but was expanded to $500,000 in late 2018.

In 2018 Q3, we rolled out the first set of Cathedral Linear Pulser (LP) tools as an add-on to our FUSION MWD platform. This technology will be our main MWD pulse telemetry platform going forward and will reduce our deployment and repair costs as we are currently dependent on third party suppliers with our capacity constrained existing linear pulse telemetry platform. Since introducing the LP tool, Cathedral has been able to make additional performance improvements to the tool specifically related to improving transmission speed and pulse detection capabilities.

In late 2018, Cathedral finalized the design and developed commercial prototypes of a drill bit RPM sensor which will be incorporated into the bearing section of Cathedral's motors. This sensor logs drill bit RPM and the motor usage time. The downhole information provided by this sensor when coupled with analysis by Cathedral's Drilling Engineering Group will provide another means to help Cathedral's customers improve their drilling performance. The additional downhole information will also contribute to further development of Cathedral's motor technology.

Fiscal management is a continuing focus of Cathedral's leadership team and our balance sheet continues to remain strong. In 2018, we ended the year $6.9 million in cash and $7.2 million drawn on our credit facility.

The business environment for oil field services in general continues to be tough, however, we believe we are making good progress. We continue to focus on strategic initiatives and making changes to our business to position us favorably over the long-term. Based on our leading-edge technology and executing our Better Performance Every Day mantra we are confident about our future prospects.

We thank our employees for their continued dedication and hard work and our customers, vendors and business partners for their support as we all navigate through a very dynamic business environment. 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 7, 2019

MANAGEMENT'S DISCUSSION & ANALYSIS

This Management's Discussion and Analysis ("MD&A") for the year ended December 31, 2018 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, 2018, as well as the Company's 2018 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 7, 2019.

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

		2018		2017		2016
Revenues	**$**	**160,827**	$	147,095	$	80,866
Adjusted gross margin % [(1)]		**11%**		18%		22%
Adjusted EBITDAS from continuing operations [(1)]	**$**	**12,060**	$	18,796	$	7,459
Diluted per share	**$**	**0.24**	$	0.40	$	0.21
As % of revenues		**7%**		13%		9%
Total Adjusted EBITDAS [(1)]	**$**	**12,060**	$	18,674	$	5,840
Diluted per share	**$**	**0.24**	$	0.39	$	0.16
Cash flow - operations	**$**	**3,732**	$	2,952	$	4,140
Write-downs of goodwill, equipment and inventory	**$**	**(1,474)**	$	(8,584)	$	(277)
Gain on disposal on investment in associate and related assets	**$**	**-**	$	-	$	10,865
Provision for settlements	**$**	**-**	$	-	$	(4,217)
Loss before income taxes	**$**	**(6,139)**	$	(382)	$	(722)
Basic per share	**$**	**(0.12)**	$	(0.01)	$	(0.02)
Derecognition of deferred tax asset	**$**	**(13,059)**	$	-	$	-
Net earnings (loss) from continuing operations	**$**	**(17,061)**	$	229	$	2,617
Basic and diluted per share	**$**	**(0.35)**	$	-	$	0.07
Net earnings (loss)	**$**	**(17,061)**	$	87	$	(5,779)
Basic and diluted per share	**$**	**(0.35)**	$	-	$	(0.16)
Property and equipment additions [(2)]	**$**	**17,391**	$	11,322	$	899
Net equipment additions [(1)]	**$**	**4,514**	$	2,371	$	(4,387)
Weighted average shares outstanding						
Basic (000s)		**49,445**		47,381		36,295
Diluted (000s)		**49,586**		47,577		36,295
Working capital	**$**	**30,599**	$	31,016	$	39,324
Total assets	**$**	**121,770**	$	121,630	$	136,017
Loans and borrowings excluding current portion	**$**	**7,000**	$	46	$	26,322
Shareholders' equity	**$**	**89,143**	$	101,391	$	90,772

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

(2) Equipment additions exclude non-cash additions

FISCAL 2018 KEY TAKEAWAYS

Revenues increased by $13,732 or 9% from $147,095 in 2017 to $160,827 in 2018;

Adjusted gross margin decreased from 18% to 11% due to increased equipment repairs and field labour costs particularly impacting the first half of the year. Adjusted gross margin percentage improved in the second half of the year;

Total Adjusted EBITDAS decreased $6,614, or 35% to $12,060 in 2018 as a result of reduced adjusted gross margin, one-time operational issues resulting in unpaid work and additional SG&A expenses occurring in Q4;

In 2018 Q4, Cathedral derecognized $13,059 of deferred tax assets due to a recent history of tax losses within Cathedral's Canadian entity;

The primary focus of Cathedral's $17,400 capital expenditures in 2018 was adding high performance Claw™ drilling motors to Cathedral's fleet to facilitate future growth in the U.S. market; and

Additional investment in technology development in 2018 resulted in deployment of new products, progress being made on Cathedral's next generation Dual Telemetry Measurement-While-Drilling ("MWD") tool and performance and reliability enhancements being incorporated into Cathedral's existing MWD equipment fleet.

OUTLOOK

In 2018, the U.S. rig count continued to grow from 929 rigs at the end of 2017 to 1,083 active rigs at the end of 2018 for an average rig count of 1,032 during the year (source: Baker Hughes Rig Count data). In 2018, the U.S. rig count growth was largely driven by West Texas Intermediate ("WTI") oil price increases from the USD $60 bbl range at the beginning of 2018 to the USD $75 bbl range by mid-year. However, starting in October 2018 there was a sharp decrease in WTI pricing into the $50 bbl range by the end of the year. This oil price drop resulted in many energy companies reviewing their drilling budgets for 2019 with the result that there has been a modest drop in the U.S. rig count in early 2019. Another factor which may impact U.S. rig activity in 2019 is takeaway capacity issues in the Permian. These are expected to be resolved in late 2019 and early 2020. Investors are also messaging to energy companies that they need to live within their cash flow.

All the above considerations have industry analysts prognosticating there could be a drop in the U.S. average rig count in 2019 by up to 10%. This rig count drop may impact Cathedral's activity levels in 2019 however, the impact is uncertain when it comes down to individual customer situations and Cathedral's operations and sales performance in this environment. The U.S. market is our primary focus and our intention is to continue to grow our market share. We believe that our recent equipment additions and upgrades position us well to achieve this.

Following curtailment in 2018 Q4, the Canadian operating environment has seen volatility in the early months of 2019. Coinciding with the WTI price drop in late 2018, the Canadian industry was further impacted by high oil price differentials resulting from oil take-away capacity from Canada being constrained. At the end of 2018, many Canadian energy companies were reviewing their drilling budgets with a view to reduce them in 2019. Since the end of 2018 pricing for Canadian oil has improved, however, drilling activity levels in Canada remain very uncertain at least in the first half of 2019. Analysts anticipate Canadian drilling activity levels will be down year-over-year 8% to 39% - with the wide range highlighting the degree of uncertainty.

Although the outlook for Canada looks challenging in the short-term, the expectation is that things will improve into 2020 based on additional take-away capacity coming on line. The Canadian industry also stands to get a boost in the early 2020s based on Liquefied Natural Gas ("LNG") export capacity coming on stream mid-decade. Our strategy in Canada is to maintain the optionality on future industry growth through focusing on serving stronger customers in areas we have advantages in, maintaining a focused and lean cost structure and again leveraging our differentiated technology advantages in the Canadian market.

There continues to be movement in the industry to combine or consolidate operations in order to achieve enhanced profitability through greater size and scale. In order to leverage our existing strong balance sheet, to improve equipment utilization and to better leverage our proprietary technologies our strategy includes looking at opportunities for growth through market share additions and accretive combination with other entities.

After a large capital spend over the last two years we can now shift to a more modest capital program as we deploy the new equipment. Our primary capital expenditure focus to the end of 2018 was on our motor fleet. In early 2019, we are expecting to field test two new patented motor designs – "Double Bend" and "Double Pad". Both motor designs are based upon substantially the same principles and are expected to significantly reduce drag, stick slip and rotary torque as well as extending the length of laterals that can be drilled with a conventional bottom hole assembly ("BHA") as compared to using a rotary steerable system. We have had discussions with a number of U.S. operators that are interested in testing this new technology. We also expect to add a mud lube version of our nDurance™ bearing section into our motor fleet. Introducing a mud lube bearing assembly, in addition to our sealed bearing design, is aimed at facilitating better motor performance in areas of high downhole temperature and with higher mud flow and pressure situations.

In 2019, our focus is primarily on building out our new MWD technology. Our 2019 net capital budget is targeted at approximately $4,000 and $1,700 of intangible additions related to technology developments. Subject to operating results and industry outlook, equipment lost-in-hole will be replaced and funded from the proceeds received.

Although we expect the first half of 2019 to be very fluid based on changing market conditions, we are in a strong position and ready to seize opportunities.

RESULTS OF OPERATIONS - 2018 COMPARED TO 2017

Overview

The Company completed 2018 with revenues of $160,827 compared to 2017 revenues of $147,095 a 9% increase. 81% of 2018 revenues were derived from the U.S. compared to 78% of revenue in 2017. 2018 Adjusted EBITDAS from continuing operations was $12,060 ($0.24 per share diluted) which represents a $(6,614) or 35% decrease from $18,796 ($0.40 per share diluted) in 2017. In 2018, the Company's net loss was $(17,061) ($(0.35) per share) compared to net earnings of $87 ($nil per share) in 2017. 2018 net earnings includes write-downs of $14,533 (2017 - $8,584).

Revenues		2018		2017
Canada	$	31,123	$	32,315
United States		129,704		114,780
Total	$	160,827	$	147,095

Revenues 2018 revenues were $160,827, which represented a $13,732 increase or 9% from 2017 revenues of $147,095.

Canadian revenues (excluding motor rental revenues) increased to $28,495 in 2018 from $27,644 in 2017; a 3% increase. This increase was the result of: i) a 9% decrease in activity days to 3,541 in 2018 from 3,890 in 2017; and ii) a 13% increase in the average day rate to $8,047 in 2018 from $7,106 in 2017.

The average active land rig count in Canada declined 9% in 2018 compared to 2017 (source: Baker Hughes). The decrease in the Company's activity days of 9% was in line with the industry decrease. The slight increases in day rates was due to general increases in customer pricing.

U.S. revenues (excluding motor rental revenues) increased to $128,206 in 2018 from $114,012 in 2017; a 12% increase. This increase was the result of: i) a 6% increase in activity days to 10,382 in 2018 from 9,782 in 2017; and ii) a 6% increase in the average day rate to $12,349 in 2018 from $11,655 in 2017 (when converted to Canadian dollars).

The average active land rig count for the U.S. was up 20% in 2018 compared to 2017 (source: Baker Hughes). The Company experienced a 6% increase in activity days relative to the industry resulting in a decrease in market share over this period. This market share decrease was largely due to equipment availability constraints starting in 2017 that extended into 2018. The Company's investment in new equipment as well as client changes in the timing and scope of their drilling programs resulted in an improvement in market share in 2018 H2. Day rates in USD increased to $9,515 USD in 2018 from $8,981 USD in 2017; a 6% increase. The increase in day rates was primarily due to customer price increases.

Motor rentals in Canada declined while U.S. rentals increased. Combined rental revenues declined to $4,126 in 2018 compared to $5,439 in 2017 primarily as a result of reduced motor rentals from Canadian customers in 2018 Q3 and Q4 and particularly one customer pausing their Canadian drilling program. U.S. rental increases are attributable to the new CLAW™ 250 and 400 motors.

Gross margin and adjusted gross margin Gross margin for 2018 was 3% compared to 11% in 2017. Adjusted gross margin (see Non-GAAP Measurements) for 2018 was $18,391 or 11% compared to $26,677 or 18% for 2017.

Adjusted gross margin, as a percentage of revenue, decreased due to higher equipment repairs, higher field labour and related benefits and burdens and specific one-time credits related to performance issues with certain U.S. clients in Q2. Adjusted gross margin were also adversely impacted by specialty equipment rentals in Q2 that were billed through to clients with a lower mark-up than typical margins. The impact of these rentals and the performance credits on U.S. work caused 1% of the decrease in adjusted gross margin.

The remaining decrease in adjusted gross margin was primarily from increased equipment repairs in 2018 H1 and higher field labour expenses in H2. Repairs increased in part due to a more demanding drilling environment and to a lesser extent upgrades being made to the Company's existing equipment fleet. Field labour cost increased as a result of industry wage pressures to retain staff. Lastly, there was an increase in the fixed component of cost of sales that were 2% higher on a percentage of revenue basis in 2018 compared to 2017. This increase was mostly attributable to office and shop payroll and other labour related costs. 2018 H2 adjusted gross margin improved compared to 2018 H1.

Depreciation allocated to cost of sales decreased to $12,719 in 2018 from $11,043 in 2017. Depreciation included in cost of sales as a percentage of revenue was 8% for 2018 and 2017. Effective October 1, 2018, the Company adjusted the estimated useful life of its directional drilling equipment to 5 to 8 years from 15.5 to 20 years used previously. This increased depreciation in 2018 Q4 by $2,566.

Selling, general and administrative expenses ("SG&A") SG&A expenses were $15,696 in 2018; an increase of $2,264 compared with $13,432 in 2017. As a percentage of revenue, SG&A was 10% in 2018 and 9% in 2017. SG&A increased primarily due to wage increases, including the reinstatement of previous wage rollbacks, severance, increased U.S. health benefits and to a lesser extent, staff additions. Staffing costs included in SG&A include executive, sales, accounting, human resources, payroll, safety and related support staff. Additionally, SGA increased due to provision for uncollectible trade receivables in 2018 Q4.

Technology group expenses Technology group expenses are related to new product development and supporting and upgrading existing technology. Technology group expenses consist of salaries and related benefits and burdens as well as shop supplies. Technology group activities spent on new product development are capitalized as intangible assets. Total technology group expenses were $3,424 in 2018; an increase of $1,158 compared with $2,266 in 2017. In 2018, $943 of technology group expenses related to new product development were capitalized as intangible assets (2017 - $nil). Technology group expenses not related to new product development were $2,481 in 2018; an increase of $215 compared with $2,266 in 2017. Technology group expenses increased primarily due to wage increases, including the reinstatement of previous wage rollbacks and new staff additions.

Gain on disposal of equipment During 2018, the Company had a gain on disposal of equipment of $10,623 compared to $7,236 in 2017. 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. In 2018, the Company received proceeds from clients on lost-in-hole recoveries of $12,877 (2017 - $9,203).

Finance costs Finance costs consist of interest expenses on operating loans, loans and borrowings and bank charges of $443 for 2018 compared to $684 for 2017. The decrease in finance costs relate to primarily to lower average debt levels in 2018.

Foreign exchange loss The Company had a foreign exchange loss of $(2,160) in 2018 compared to a gain of $1,783 in 2017 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 2018 foreign currency gains are unrealized losses of $2,260 (2017 – gain of $1,903) related to intercompany balances.

Write-down of inventory The Company made a provision related to slow moving and obsolete inventory used to service equipment of $1,474 (2017 - $151). The impacted inventory was used to service older revisions to tools that are obsolete as well as tools that have had lower demand since the industry down-turn. The tools with lower demand are primarily legacy non-proprietary motors that are being used less and less each year.

Write-downs 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, 2018 or December 31, 2017. However, in 2017 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 in connection with international operations which were subsequently discontinued. 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 motors in the current drilling environment as their performance capabilities are lower than the Company's proprietary motors. As a consequence, the Company conducted a review and wrote-off the remaining net book value for any non-proprietary motors that were no longer expected to be utilized. There was also an impairment of $146 related to a technology development project in 2017.

Income tax For 2018, the Company had an income tax expense of $10,922 compared to a recovery of $611 in 2017. In 2018 Q4, Cathedral derecognized $13,059 of deferred tax assets due to a recent history of tax losses within Cathedral's Canadian entity. Cathedral has approximately

$37,700 of unrecognized tax attributes and approximately $5,100 of investment tax credits that can be used to offset future Canadian taxes.

Excluding adjustments to prior years' tax provisions and the derecognition of deferred tax assets, the effective tax rate was 26% for 2018 and 57% for 2017. The 2017 provision includes reduction to U.S. deferred income tax asset due to reduction in U.S. rates from recent tax reform. 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 and proceeds from equipment lost-in-hole. In addition, the Company has the ability to fund liquidity requirements through its credit facility and the issuance of debt and/or equity. Cash flow from continuing operations in 2018 decreased to $970 from $11,169 in 2017. This decrease was primarily due to decreased net earnings. For the year ended December 31, 2018, the Company had cash flow from operating activities of $3,732 (2017 - $2,952). The increase in funds from operating activities is due to the change in non-cash operating working capital from a use of cash of $8,948 in 2017 to a source of cash of $4,044 in 2018 offset by $1,282 in income taxes paid in 2018 compared to income taxes refunded of $866 in 2017.

Working capital At December 31, 2018 the Company had working capital of $30,599 (2017 - $31,016).

Credit facility During December 2017, the Company signed a credit facility (the "Facility") with a new lending syndicate. The Facility consists of a $5 million operating facility and a $15 million extendible revolving credit facility. The facility was renewed on November 8, 2018 under the same terms as the original facility and now expires December 31, 2020. The Facility is secured by a general security agreement over all present and future personal property. The Facility provides a definition of 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 compared 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.

Compliance with Facility covenants

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

At December 31, 2018, the Company had drawn $7,000 of its revolving credit facility, $188 of its operating facility and had $6,875 in cash. At December 31, 2018, the Company had consolidated funded debt of $1,595 which includes five outstanding letters of credit ("LOC") which are included in the funded debt calculation. For the trailing twelve months ended December 31, 2018, Credit Agreement EBITDA was $14,314.

The calculation of the financial covenants under the Facility as at December 31, 2018 is as follows:

Covenant	Actual Ratio	Required Ratio
Consolidated funded debt to consolidated Credit Agreement EBITDA ratio	0.1:1	3.0:1 (maximum)
Consolidated interest coverage ratio	32.3:1	2.5:1 (minimum)

Contractual obligations 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, 2018.

The Company has issued the following five LOC:

- two 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 securing the Company's corporate credit cards in the amounts of $75 CAD and $175 USD.

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

	Total	2019	2020	2021	2022	2023	Thereafter
Equipment purchase obligations	$ 409	$ 409	$ -	$ -	$ -	$ -	$ -
Secured revolving term loan	7,000	-	-	7,000	-	-	-
Operating lease obligations	29,117	3,508	3,505	3,528	3,565	3,602	11,409
Provision for settlement	491	164	164	163			
Finance lease obligations	91	91	-	-	-	-	-
Total	$ 37,108	$ 4,172	$ 3,669	$ 10,691	$ 3,565	$ 3,602	$ 11,409

As at December 31, 2018, the Company's commitment to purchase equipment is approximately $409. Cathedral anticipates expending these funds in 2019 Q1.

Share capital At March 7, 2019, the Company has 49,468,117 common shares and 3,670,334 options outstanding with a weighted average exercise price of $1.20.

In 2018, the Company issued 1,040,500 stock options to staff and directors with an average exercise price of $0.92 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:

		2018		2017
Short-term employment benefits (1)	$	2,379	$	1,546
Share-based compensation		341		159
Total expense recognized as share-based compensation	$	2,720	$	1,705

(1) Including severance payments

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 (2017 - nil), and no outstanding balances exist as at period end (2017 - nil).

OFF-BALANCE SHEET ARRANGEMENTS

As at December 31, 2018, the Company has entered into $29,218 of commitments under operating leases for premises and issued standby LOC as detailed above under contractual obligations. 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.

2018 CAPITAL PROGRAM

During the year ended December 31, 2018 the Company invested $17,391 (2017 - $11,322) in equipment and $1,226 (2017 - $474) in new technology development primarily related to MWD systems.

The following table details the current period's net equipment additions:

		Year ended December 31, 2018
Equipment additions:		
Motors and related equipment	$	10,147
MWD and related equipment		6,387
Other		857
Total cash additions		17,391
Less: proceeds on disposal of equipment (excluding capital lease settlements)		(12,877)
Net equipment additions (1)	$	4,514

(1) See "NON-GAAP MEASUREMENTS"

2019 CAPITAL PROGRAM

Cathedral's 2019 capital budget approved by the Board of Directors in December 2018 was for net equipment additions of approximately $4,000 and $1,700 of intangible additions related to technology development. Subject to operating results and industry outlook, equipment lost-in-hole will be replaced and funded from the proceeds received.

RESULTS OF OPERATIONS – THREE MONTHS ENDED DECEMBER 31

Revenues and operating expenses

		2018 Q4		2017 Q4		$ Change	% Change
Revenues	$	43,127	$	38,402	$	4,725	12%
Cost of sales		(42,177)		(34,741)		(7,436)	21%
Gross margin - $	$	950	$	3,661	$	(2,711)	-74%
Gross margin - %		2%		10%		-8%	
Adjusted gross margin $ (1)	$	6,310	$	6,602	$	(292)	-4%
Adjusted gross margin % (1)		15%		17%		-2%	

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

Revenues		2018 Q4		2017 Q4
Canada	$	8,146	$	7,749
United States		34,981		30,653
Total	$	43,127	$	38,402

Revenues 2018 Q4 revenues were $43,127, which represented an increase of $4,725 or 12% from 2017 Q4 revenues of $38,402.

Canadian revenues (excluding motor rental revenues) increased to $7,705 in 2018 Q4 from $6,216 in 2017 Q4; a 24% increase. This increase was the result of: i) a 12% increase in activity days to 912 in 2018 Q4 from 814 in 2017 Q4 and ii) an 11% increase in the average day rate to $8,449 in 2018 Q4 from $7,637 in 2017 Q4.

The average active land rig count in Canada was down 13% in 2018 Q4 compared to 2017 Q4 (source: Baker Hughes). Cathedral's activity levels relative to the industry were impacted by the scope of its customer drilling programs and their geographical focus relative to the overall industry. The increase in day rates was due to general increases in customer pricing.

U.S. revenues (excluding motor rental revenues) increased to $34,573 in 2018 Q4 from $30,561 in 2017 Q4; a 13% increase. This increase was the result of: i) a 9% increase in activity days to 2,677 in 2018 Q4 from 2,453 in 2017 Q4; and ii) a 4% increase the average day rate to $12,915 in 2018 Q4 from $12,459 in 2017 Q4 (when converted to Canadian dollars).

The average active land rig count for the U.S. was up 17% in 2018 Q4 compared to 2017 Q4 (source: Baker Hughes). The Company experienced a 13% increase in activity days resulting in a slight decrease in market share compared to 2017 Q4. Day rates in USD decreased slightly to $9,760 USD in 2018 Q4 from $9,799 USD in 2017 Q4; a change of less than 1%.

Motor rentals in Canada declined while U.S. rentals increased. Combined rental revenues declined to $849 in 2018 compared to $1,624 in 2017 primarily as a result of reduced motor rentals from Canadian customers in 2018 Q4 resulting from a pause in their Canadian drilling programs. U.S. rental increases are attributable to new CLAW™ 250 and 400 motors.

Gross margin and adjusted gross margin Gross margin for 2018 Q4 was 2% compared to 10% in 2017 Q4. Adjusted gross margin (see Non-GAAP Measurements) for 2018 Q4 was $6,310 or 15% compared to $6,602 or 17% for 2017 Q4.

Adjusted gross margin, as a percentage of revenue, decreased due to higher field labour and related expenses and an increase in the fixed component of cost of sales, offset by a decrease in repairs. The field labour increased due to industry pressures to retain staff. The increase in the fixed component of cost of sales was mostly attributable to increased office and shop payroll and other labour related costs.

Depreciation allocated to cost of sales increased to $5,304 in 2018 Q4 from $2,915 in 2017 Q4 due to changes in estimate of useful life made effective October 1, 2018. This increased depreciation in 2018 Q4 by $2,566. Depreciation included in cost of sales as a percentage of revenue was 12% for 2018 Q4 and 8% in 2017 Q4.

Selling, general and administrative expenses ("SG&A") SG&A expenses were $4,705 in 2018 Q4; an increase of $2,169 compared with $2,536 in 2017 Q4. As a percentage of revenue, SG&A was 11% in 2018 Q4 compared to 7% in 2017 Q4. SG&A increased primarily due to U.S. state sales taxes on intercompany equipment rentals as 2017 Q4 had an adjustment related to amounts accrued previously in 2017. Cathedral's Canadian entity owns all Cathedral's downhole drilling equipment and rents it to the U.S. entity and is subject to state sales tax on these amounts. Additionally, there was an increase in wages in 2018 Q4 for severance costs that are not expected to recur.

Technology group expenses Technology group expenses are related to new product development and supporting and upgrading existing technology. Technology group expenses consist of salaries and related benefits and burdens as well as shop supplies. Technology group activities spent on new product development are capitalized as intangible assets. Total technology group expenses were $954 in 2018 Q4; an increase of $327 compared with $627 in 2017. There was capitalization of $214 of technology group expenses related to new product development as intangible assets (2017 - $nil). Technology group expenses not related to new product development were $740 in 2018; an increase of $113 compared with $627 in 2017. Technology group expenses increased primarily due to wage increases, including the reinstatement of previous wage rollbacks and new staff additions.

Gain on disposal of equipment During 2018 Q4, the Company had a gain on disposal of equipment of $1,789 compared to $2,038 in 2017 Q4. These gains mainly relate to equipment lost-in-hole. Proceeds from clients on lost-in-hole equipment are based on amounts specified in service agreements and, in most cases; these proceeds exceed the net book value of the equipment and result in a gain. The timing of lost-in-hole recoveries is not in the control of the Company and therefore can fluctuate significantly from quarter-to-quarter. In 2018 Q4, the Company received proceeds on lost-in-hole recoveries from clients of $2,201 (2017 Q4 - $2,535).

Finance costs Finance costs consist of interest expenses on operating loans, loans and borrowings and bank charges of $181 for 2018 Q4 versus $157 for 2017 Q4.

Foreign exchange The Company had a foreign exchange loss of $(1,745) in 2018 Q4 compared to $(193) in 2017 Q4 due to the fluctuations of the Canadian dollar relative to the U.S. dollar. The Company's foreign operations are denominated in USD and therefore, upon consolidation, gains and losses due to fluctuations in the foreign currency exchange rates are recorded as other comprehensive income on the balance sheet as a component of equity. However, gains and losses in the Canadian entity on U.S. denominated intercompany balances continue to be recognized in the statement of comprehensive income (loss). Included in the 2018 Q4 foreign currency loss are unrealized losses of $(1,814) (2017 Q4 - $(113)) related to intercompany balances.

Write-down of inventory The Company made a provision related to slow moving and obsolete inventory used to service equipment of $1,474 (2017 - $151). The impacted inventory was used to service older revisions to tools that are obsolete as well as tools that have had lower demand since the industry down-turn. The tools with lower demand are primarily legacy non-proprietary motors that are being used less and less each year.

Write-downs 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, 2018 or December 31, 2017. However, in 2017 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 in connection with international operations which were subsequently discontinued. 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 motors in the current drilling environment as their performance capabilities are lower than the Company's proprietary motors. As a consequence, the Company conducted a review and wrote-off the remaining net book value for any non-proprietary motors that were no longer expected to be utilized. There was also an impairment of $146 related to a technology development project in 2017.

Income tax For 2018 Q4, the Company had an income tax expense of $11,752 compared to an income tax recovery of $1,908 in 2017 Q4. In 2018 Q4, Cathedral derecognized $13,059 of deferred tax assets due to a recent history of tax losses within Cathedral's Canadian entity. Cathedral has approximately $37,700 of unrecognized tax attributes and approximately $5,100 of investment tax credits that can be used to offset future Canadian taxes.

Excluding adjustments to prior years' tax provisions and the derecognition of deferred tax assets, the effective tax rate was 18% (2017 -24%). The effective tax rate for 2018 Q4 is impacted by one legal entity having pre-tax income and the other having pre-tax losses. Income tax expense is booked based upon expected annualized effective rates based upon the statutory rates of 27% for Canada and 23% for the U.S.

SUMMARY OF QUARTERLY RESULTS

Three month periods ended	Dec 2018	Sep 2018	Jun 2018	Mar 2018	Dec 2017	Sep 2017	Jun 2017	Mar 2017
Revenues	$ 43,127	$ 42,570	$ 34,973	$ 40,157	$ 38,402	$ 36,015	$ 34,355	$ 38,323
Total Adjusted EBITDAS [(1)]	$ 3,412	$ 6,190	$ (985)	$ 3,443	$ 5,606	$ 3,909	$ 2,363	$ 6,796
Total Adjusted EBITDAS [(1)] per share - diluted	$ 0.07	$ 0.13	$ (0.02)	$ 0.07	$ 0.11	$ 0.08	$ 0.05	$ 0.09
Net earnings (loss)	$ (17,858)	$ 3,001	$ (2,498)	$ 294	$ (4,490)	$ 1,810	$ 186	$ 2,581
Net earnings (loss) per share - basic and diluted	$ (0.36)	$ 0.06	$ (0.05)	$ 0.01	$ (0.09)	$ 0.04	$ -	$ 0.06

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

A portion of the Company's operations is 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 western Canada.

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 to make 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 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 intangibles 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 25 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 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, 2019 and have not been applied in preparing the Consolidated Financial Statements for the year ended December 31, 2018. The standards applicable to the Company are as follows and will be adopted on their respective effective dates:

(i) 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.

IFRS 16 comes into effect on January 1, 2019. The Company is in the process of finalizing the impact on the financial statements. The Company's assessment indicates that many of the operating lease arrangements will meet the definition of a lease under IFRS 16 and thus be recognized in the statement of financial position as a right-of-use asset with a corresponding liability. The most significant impact of this will be for the lease of premises. The Company does not expect other items to have a significant impact.

The Company has chosen to utilize the modified retrospective approach in application of the standard. This will result in the recognition of a lease liability and a corresponding recognition of a right-of-use asset. The Company has chosen to recognize the right-of-use asset on January 1, 2019 at a value equal to the related liability of the lease. The Company will also use the exemption for any capital leases recognized prior to January 1, 2019 and to only apply IFRS 16 to contracts that were previously identified as leases. As such, the Company will not apply the standard to any contracts not previously identified as containing a lease.

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. Exemptions exist for short-term leases where the term is 12 months or less and for leases of low value items. As well, the classification of cash flows will be impacted as the current presentation of operating lease payments as operating cash flows will be split into financing (principal portion) and operating (interest portion) cash flows under IFRS 16.

Additional disclosures will also be required under IFRS 16. Cathedral plans to apply IFRS 16 initially on January 1, 2019 and estimates that the right-of-use asset and lease liability will be approximately $24 million. The Company continues to assess the impact of adopting IFRS 16 on deferred tax balances.

(ii) Uncertainty over Income Tax Treatments

IFRS Interpretations Committee ("IFRIC") issued IFRIC 23 Uncertainty over Income Tax Treatments ("IFRIC 23") which clarifies the accounting for uncertainties in income taxes. The interpretation requires the entity to use the most likely amount or the expected value of the tax treatment if it concludes that it is not probable that a particular tax treatment will be accepted. It requires an entity to assume that a taxation authority with the right to examine any amounts reported to it will examine those amounts and will have full knowledge of all relevant information when doing so.

IFRIC 23 is effective for annual reporting periods beginning on or after January 1, 2019. Earlier application is permitted. The requirements are applied by recognizing the cumulative effect of initially applying them in retained earnings, or in other appropriate components of equity, at the start of the reporting period in which an entity first applies them, without adjusting comparative information. Full retrospective application is permitted, if an entity can do so without using hindsight. The Company does not expect this standard to have any impact on its 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 Interim 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, 2018. 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, 2018.

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, 2018 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, 2018 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 is introducing 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.

Commodity price volatility may impact E&P companies' willingness to commit to capital spending, which in turn may have a significant adverse effect the rig count and thus on the Corporation's activity levels, 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 Cathedral 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 and 2018 Cathedral faced cost increases in many areas of its business. 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 and cash flow. In Canada and the U.S. Permian Basin area, takeaway capacity issues have recently impacted local oil pricing and net backs with the result that drilling activity levels in these areas have been negatively impacted.

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. See "Dividend Policy" herein.

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 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 this AIF, 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 $20 million credit facility with a syndicate of lenders consisting of Alberta Treasury Branches and Export Development Canada consisting of a revolving facility of $15 million and a $5 million operating facility with a maturity date of December 31, 2020. 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 Corporation could temporarily breach the covenants included in its credit facility. If the Corporation does temporarily breach these covenants, the credit facility 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 financial results and other factors including the payment of a dividend and prevailing financial market factors and investor interest in the Company or the industry the Company operates in. The market price of the Common Shares may also be impacted by other factors including the net asset value of Cathedral's 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 result 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, 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, certain tools, equipment or technology developed by Cathedral may 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 and economic considerations, 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 some of its equipment becoming technically obsolete or creating market obsolescence based on lower demand which has resulted in write-downs of certain equipment and associated parts inventory. 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 and omissions 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 its 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 of equipment and vehicle travel by staff 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, but not necessarily fully eliminate 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 appropriate insurance coverage is in place and 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 and 2018 Cathedral experienced higher than previous levels of equipment damages and equipment lost-in-hole than previous years and the pre-industry downturn levels which in part was due to changes in customer drilling practices.

Business continuity, disaster recovery and crisis management An 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 In the future, 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.

Weather and Seasonality A 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. Canadian operating activities generally increase in the fall and peak in the winter months from December until late March, depending on 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, however, U.S. operations can also be impacted by weather related issues. In general, activity levels in North America can be impacted year round by weather conditions and temperatures, including major weather events such as summer and winter storms and hurricanes which can create additional unpredictability in operational results.

Foreign Currency Exchange Rates Cathedral derives a significant portion of its revenues from the U.S. which are denominated in the local currency. This causes a 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 U.S. dollars. 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.

Business Transaction Risks Cathedral expects to continue to selectively seek mergers, acquisitions and other types of business transactions in connection with its growth strategy. Cathedral's ability to consummate and to integrate effectively any future mergers, acquisitions or other business transactions on terms that are favorable to it may be limited by the number of attractive transaction targets, internal demands on Cathedral's resources, internal management capabilities and to the extent necessary, Cathedral's ability to obtain financing on satisfactory terms for larger transactions, if at all. Business transactions 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 2018, approximately 15% of the Company's revenue was attributable to sales transactions with a single customer. 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. 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 several 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: continue to be on track to introduce our next generation FUSION™ Dual Telemetry (DT) MWD tool in 2019; the proposed tool design will incorporate a number of improvements over Cathedral's existing FUSION™ DT platform and compared to competitive products; continue to focus on strategic initiatives and making changes to our business to position us well over the long-term; based on our leading- edge technology and executing our Better Performance Every Day mantra we are confident about our future prospects; takeaway capacity issues in the Permian are expected to be resolved in late 2019 and early 2020; industry analysts prognosticating there could be a drop in the U.S. average rig count in 2019 by up to 10%; this rig count drop may impact Cathedral's activity levels in 2019 however, the impact is uncertain when it comes down to individual customer situations and Cathedral's operations and sales performance in this environment; believe that our recent equipment additions and upgrades position us well to grow our market share; analysts anticipate Canadian drilling activity levels will be down year-over-year 8% to 39%; expectation is that things will improve into 2020 based on additional take-away capacity coming on line; the Canadian industry also stands to get a boost the early 2020s based on LNG export capacity coming on stream mid-decade; strategy in Canada is to maintain optionality on future industry growth through focusing on serving stronger customers in areas we have advantages in, maintaining a focused and lean cost structure and again leveraging our differentiated technology advantages in the Canadian market; in 2019 our capital spending focus is primarily on building out our new MWD technology; 2019 net Capital Budget is targeted at approximately $4,000 and $1,700 of intangible additions related to technology developments; subject to operating results and industry outlook, equipment lost-in-hole will be replaced and funded from the proceeds received; in early 2019 we are expecting to field test two new patented motor designs – "Double Bend" and "Double Pad" Both motor designs are based upon substantially the same principles and are expected to significantly reduce drag, stick slip and rotary torque as well as extending the length of laterals that can be drilled with a conventional bottom hole assembly ("BHA") as compared to using a rotary steerable system; U.S. operators that are interested in testing this new technology; expect to add a mud lube version of it nDurance™ bearing section into our motor fleet; mud lube bearing assembly in addition to our sealed bearing design is aimed at facilitating better motor performance in areas of high downhole temperature and with higher mud flow and pressure situations; we are in a strong position and ready to seize opportunities; projected capital expenditures and commitments and the financing thereof; and Cathedral expects to comply with all covenants during 2019.

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 business;
- impact of economic and social trends;
- oil and natural gas commodity prices and production levels;
- capital expenditure programs and other expenditures by Cathedral and its customers;
- the ability of Cathedral to retain and hire qualified personnel;
- the ability of Cathedral to obtain parts, consumables, equipment, technology, and supplies in a timely manner to carry out its activities;
- the ability of Cathedral to maintain good working relationships with key suppliers;
- the ability of Cathedral to retain customers, market its services successfully to existing and new customers and reliance on major customers;
- risks associated with technology development and intellectual property rights;
- obsolesce of Cathedral's equipment and/or technology
- the ability of Cathedral to maintain safety performance;
- the ability of Cathedral to obtain adequate and timely financing on acceptable terms;
- the ability of Cathedral to comply with the terms and conditions of its credit facility;
- the ability to obtain sufficient insurance coverage to mitigate operational risks;
- currency exchange and interest rates;
- risks associated with future foreign operations
- risks associated with acquisitions, dispositions and business development efforts;
- environmental risks;
- risks related to legal proceedings;
- business risks resulting from weather, disasters and related to information technology
- changes under governmental regulatory regimes and tax, environmental and other laws in Canada and the United States ("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 finance costs, unrealized foreign exchange on intercompany balances, taxes, depreciation, non-recurring costs (including severance), 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) "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 30	
	2018	2017	2018	2017
Gross margin	$ 950	$ 3,661	$ 5,492	$ 15,565
Add non-cash items included in cost of sales:				
Depreciation	5,304	2,915	12,719	11,043
Share-based compensation	56	26	180	69
Adjusted gross margin	$ 6,310	$ 6,602	$ 18,391	$ 26,677
Adjusted gross margin %	15%	17%	11%	18%

Total Adjusted EBITDAS

	Three months ended December 31		Year ended December 30	
	2018	2017	2018	2017
Earnings (loss) before income taxes	$ (6,106)	$ (6,398)	$ (6,139)	$ (382)
Add:				
Depreciation included in cost of sales	5,304	2,915	12,719	11,043
Depreciation included in selling, general and administrative expenses	71	29	202	104
Share-based compensation included in cost of sales	56	26	180	69
Share-based compensation included in selling, general and administrative expenses	151	67	454	206
Finance costs	181	157	443	684
Subtotal	(343)	(3,204)	7,859	11,724
Unrealized foreign exchange (gain) loss on intercompany balances	1,814	113	2,260	(1,903)
Write-down of equipment	-	8,433	-	8,433
Write-down of inventory	1,474	151	1,474	151
Non-recurring expenses	467	113	467	391
Adjusted EBITDAS from continuing operations	3,412	5,606	12,060	18,796
Adjusted EBITDAS from discontinued operations	-	-	-	(122)
Total Adjusted EBITDAS	$ 3,412	$ 5,606	$ 12,060	$ 18,674

MANAGEMENT'S REPORT

The consolidated financial statements have been prepared by the management in accordance with International Financial Reporting Standards ("IFRS") 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. Additionally, management prepares the Management's Discussion and Analysis ("MD&A"). The MD&A is based on the Company's financial results prepared in accordance with IFRS. The MD&A compares the audited financial results for the years ended December 31, 2018 and December 31, 2017.

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, which is comprised of three independent directors who are not employees of the Company, 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, Chief Executive Officer and Interim Chief Financial Officer

INDEPENDENT AUDITORS' REPORT

To the Shareholders of Cathedral Energy Service Ltd.:

Opinion

We have audited the consolidated financial statements of Cathedral Energy Services Ltd. (the "Company"), which comprise:

- the consolidated statements of financial position as at December 31, 2018 and December 31, 2017;
- the consolidated statements of comprehensive loss for the years then ended;
- the consolidated statements of changes in shareholders' equity for the years then ended;
- the consolidated statements of cash flows for the years then ended;
- and notes to the consolidated financial statements, including a summary of significant accounting policies.

Hereinafter referred to as the "financial statements".

In our opinion, the accompanying financial statements present fairly, in all material respects, the consolidated financial position of the Company as at December 31, 2018 and December 31, 2017, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards ("IFRS").

Basis for Opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the "*Auditors' Responsibilities for the Audit of the Financial Statements*" section of our auditors' report.

We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial statements in Canada and we have fulfilled our other ethical responsibilities in accordance with these requirements.

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

Other Information

Management is responsible for the other information. Other information comprises:

- the information included in Management's Discussion and Analysis to be filed with the relevant Canadian Securities Commissions.
- the information, other than the financial statements and the auditor's report thereon, included in a document likely to be entitled "2018 Annual Report".

Our opinion on the financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

We obtained the Management's Discussion and Analysis to be filed with the relevant Canadian Securities Commissions as at the date of this auditors' report. If, based on the work we have performed on this other information, we conclude that there is a material misstatement of this other information, we are required to report that fact in the auditors' report. We have nothing to report in this regard.

Information, other than the financial statements and the auditors' report thereon, included in a document likely to be entitled "2018 Annual Report" is expected to be made available to us after the date of this auditors' report. If, based on the work we will perform on this other information, we conclude that there is a material misstatement of this other information, we are required to report that fact to those charged with governance.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

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

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit.

We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion.

  The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit 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 Company's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represents the underlying transactions and events in a manner that achieves fair presentation.

- Communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

- Provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

The engagement partner on the audit resulting in this auditors' report is Jason Stuart Brown.

Signed: *"KPMG LLP"*

Chartered Professional Accountants

Calgary, Canada
March 11, 2019

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

December 31, 2018 and 2017

Dollars in '000s

		December 31 2018		December 31 2017
Assets				
Current assets:				
Cash (note 5)	$	6,875	$	2,683
Restricted cash equivalents (note 5)		-		1,514
Trade receivables (note 6)		35,583		33,885
Current taxes recoverable		-		86
Prepaid expenses		1,691		1,460
Inventories (note 7)		11,750		11,128
Total current assets		55,899		50,756
Equipment (note 8)		61,068		58,383
Intangible assets (note 9)		2,827		1,953
Deferred tax assets (note 11)		1,976		10,538
Total non-current assets		65,871		70,874
Total assets	$	121,770	$	121,630
Liabilities and Shareholders' Equity				
Current liabilities:				
Operating loan (note 12)	$	188	$	1,233
Trade and other payables (note 13)		23,868		17,926
Current taxes payable		991		-
Loans and borrowings (note 14)		89		233
Liability for settlements, current		164		348
Total current liabilities		25,300		19,740
Loans and borrowings (note 14)		7,000		46
Liability for settlements, long-term		327		453
Total non-current liabilities		7,327		499
Total liabilities		32,627		20,239
Shareholders' equity:				
Share capital (note 15)		88,155		88,059
Contributed surplus		10,410		9,801
Accumulated other comprehensive income		12,252		8,144
Deficit		(21,674)		(4,613)
Total shareholders' equity		89,143		101,391
Total liabilities and shareholders' equity	$	121,770	$	121,630

See accompanying notes to consolidated financial statements.

Approved by the Directors:

Signed: *"P. Scott MacFarlane"*

P. Scott MacFarlane

Director

Signed: *"Rod Maxwell"*

Rod Maxwell

Director

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

Years ended December 31, 2018 and 2017

Dollars in '000s except per share amounts

		2018		2017
Revenues (note 20)	$	160,827	$	147,095
Cost of sales (notes 7 and 17):				
Direct costs		(142,436)		(120,418)
Depreciation		(12,719)		(11,043)
Share-based compensation		(180)		(69)
Total cost of sales		(155,335)		(131,530)
Gross margin		5,492		15,565
Selling, general and administrative expenses (note 17):				
Direct costs		(15,040)		(13,122)
Depreciation		(202)		(104)
Share-based compensation		(454)		(206)
Total selling, general and administrative expenses		(15,696)		(13,432)
		(10,204)		2,133
Technology group expenses (note 17)		(2,481)		(2,266)
Gain on disposal of equipment		10,623		7,236
Earnings (loss) from operating activities		(2,062)		7,103
Finance costs (note 18)		(443)		(684)
Foreign exchange gain (loss) (note 18)		(2,160)		1,783
Asset impairment (note 8)		-		(8,433)
Write-down of inventory (note 7)		(1,474)		(151)
Loss before income taxes		(6,139)		(382)
Income tax recovery (expense) (note 11):				
Current		(2,297)		(405)
Deferred		4,434		1,016
Derecognition of deferred tax asset		(13,059)		-
Total income tax recovery (expense)		(10,922)		611
Net earnings (loss) from continuing operations		(17,061)		229
Net loss from discontinued operations (note 10)		-		(142)
Net earnings (loss)		(17,061)		87
Other comprehensive income (loss):				
Foreign currency translation differences for foreign operations		4,108		(3,227)
Total comprehensive loss	$	(12,953)	$	(3,140)
Net earnings from continuing operations per share				
Basic and diluted	$	(0.34)	$	-
Net loss from discontinued operations per share				
Basic	$	-	$	-
Net earnings (loss) per share				
Basic and diluted	$	(0.34)	$	-

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

Years ended December 31, 2018 and 2017

Dollars in '000s except per share amounts

	Share capital	Contributed surplus	Accumulated other comprehensive income	Deficit	Total shareholders' equity
Balance at December 31, 2016	**$ 74,481**	**$ 9,620**	**$ 11,371**	**$ (4,700)**	**$ 90,772**
Total comprehensive income (loss) for year ended December 31, 2017	-	-	(3,227)	87	(3,140)
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**
Total comprehensive income (loss) for year ended December 31, 2018	-	-	4,108	(17,061)	(12,953)
Issue of shares upon exercise of options	96	(25)	-	-	71
Share-based compensation	-	634	-	-	634
Total contributions by and distributions to shareholders	96	609	-	-	705
Balance at December 31, 2018	**$ 88,155**	**$ 10,410**	**$ 12,252**	**$ (21,674)**	**$ 89,143**

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended December 31, 2018 and 2017

Dollars in ‘000s except per share amounts

		2018		2017
Cash provided by (used in):				
Operating activities:				
Net earnings from continuing operations	$	(17,061)	$	229
Items not involving cash				
Depreciation		12,921		11,147
Share-based compensation		634		275
Income tax (recovery) expense		10,922		(611)
Gain on disposal of equipment		(10,623)		(7,236)
Finance costs		443		684
Unrealized foreign exchange (gain) loss on intercompany balances		2,260		(1,903)
Asset impairment		-		8,433
Write-down of inventory		1,474		151
Cash flow - continuing operations		970		11,169
Cash flow - discontinued operations (note 10)		-		(135)
Changes in non-cash operating working capital (note 19)		4,044		(8,948)
Income taxes refunded (paid)		(1,282)		866
Cash flow - operating activities		3,732		2,952
Investing activities:				
Equipment additions		(17,391)		(11,322)
Intangible asset additions		(1,226)		(474)
Proceeds on disposal of equipment		12,877		9,203
Proceeds on disposal of discontinued operations		-		17,252
Changes in non-cash investing working capital		(562)		1,925
Cash flow - investing activities		(6,302)		16,584
Financing activities:				
Change in operating loan		(1,045)		(872)
Repayments on loans and borrowings		(205)		(26,420)
Proceeds on share issuance from bought deal public offering and insider private placement		-		13,131
Proceeds on share issuance from exercise of share options		71		354
Payment on settlements		(316)		(2,607)
Restricted cash		1,514		(1,514)
Interest paid		(443)		(687)
Advances of loans and borrowings		7,000		-
Cash flow - financing activities		6,576		(18,615)
Effect of exchange rate on changes on cash		186		(136)
Change in cash and cash equivalents		4,192		785
Cash, beginning of year		2,683		1,898
Cash, end of year	$	6,875	$	2,683

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, 2018 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.

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 7, 2019.

(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 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, 2018, 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 impacted by estimates for usage, technology changes, customer requirements and other factors. 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.

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 25 "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 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 25.

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

(i) Financial assets

Initial recognition and measurement

Financial assets within the scope of IFRS 9 are classified as financial assets at amortized cost, fair value through profit or loss or fair value through other comprehensive income, as appropriate. The Company determines the classification of its financial assets at initial recognition, based on trade date. All financial assets are recognized initially at fair value. The Company’s financial assets include cash and cash equivalents, and trade receivables. All financial assets are measured at amortized cost.

Subsequent measurement

Financial assets at fair value through profit or loss

The Company has no financial assets at fair value through profit or loss.

Impairment of financial assets

The Company assesses at each reporting date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the debtor is experiencing significant financial difficulty and where observable data indicate that there is a measurable decrease in the estimated future cash flows.

Financial assets carried at amortized cost

For financial assets carried at amortized cost, the Company applies the simplified approach to measuring expected credit losses which uses a lifetime expected loss allowance for all trade receivables. Trade receivables are written off when there is no reasonable expectation of recovery.

(ii) Financial liabilities

Initial recognition and measurement

Financial liabilities within the scope of IFRS 9 are classified as financial liabilities at fair value through profit or loss or at amortized cost. The Company determines the classification of its financial liabilities at initial recognition. All financial liabilities are recognized initially at fair value and in the case of other financial liabilities, plus directly attributable transaction costs. The Company's financial liabilities include operating loan, trade and other payables, loans and borrowings and provision for settlement. All financial liabilities are measured at amortized cost.

Subsequent measurement

After initial recognition, interest bearing loans and borrowings are subsequently measured at amortized cost using the effective interest rate ("EIR") method. Gains and losses are recognized in the consolidated statements of earnings when the liabilities are derecognized as well as through the EIR method amortization process. The EIR amortization is included in interest expense in the consolidated statements of earnings.

Derecognition and modification

A financial liability is derecognized when the obligation under the liability is discharged, cancelled or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognized in the consolidated statements of earnings.

(iii) Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount reported in the consolidated statements of financial position if there is a currently enforceable legal right to offset the recognized amounts and there is an intention to settle on a net basis, or to realize the assets and settle the liabilities simultaneously.

(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	5 to 8	25 to 37.5%	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 year and adjusted if appropriate.

Effective October 1, 2018 the estimated useful life of the following equipment were revised to take into account accelerated technological advancements in directional drilling equipment:

Equipment type	**Prior estimated useful life**	**Revised estimated useful life**
Directional drilling equipment	15.5 to 20 years	5 to 8 years

These changes in estimates have been accounted for prospectively beginning October 1, 2018. This increased depreciation in 2018 Q4 by $2,566. It is estimated that the revised estimated useful life will increase 2019 depreciation by approximately $7,500.

(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.

Trade receivables are recognized and carried at original invoice amount less an allowance for any amounts estimated to be uncollectible. The Company calculates an expected credit loss based on historical experience of bad debts and specific provisions created when there is objective evidence that the collection of the full amount of a receivable is no longer probable under the terms of the original invoice. The amount of this allowance represents management's best estimate of expected credit losses. Trade receivables are derecognized when they are assessed as uncollectible.

(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

The Company provides directional drilling services. Revenue is recognized when a customer obtains control of the good or services. Determining the timing of the transfer of control (at a point in time or over time) requires judgement. Revenue for these services are recognized over time based on drilling days. Invoices are generated at the end of the job and are due based on the Master Service Agreement with client or Cathedral's signed Terms and Conditions, generally 30 or 60 days. 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 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. However, as the Company's Canadian entity has a history of recent tax losses, the Company only recognizes deferred tax assets to the extent that there is convincing other evidence that sufficient taxable income will be available to realize the tax pools.

(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 accounting standards

(i) Revenue

The Company has adopted IFRS 15 *Revenue from Contracts with Customers* ("IFRS 15") and IFRS 9 *Financial Instruments ("IFRS 9")* at January 1, 2018. The adoption of these standards did not have a material effect on the Company's financial statements.

Under IFRS 15, revenue is recognized when a customer obtains control of the good or services. Determining the timing of the transfer of control (at a point in time or over time) requires judgement.

The Company provides directional drilling services. Revenue for these services are recognized over time based on drilling days. Invoices are generated at the end of the job and are due based on the Master Service Agreement with client or Cathedral's signed Terms and Conditions, generally 30 or 60 days.

(ii) Financial instruments

Under IFRS 9, financial assets and liabilities are classified and measured at amortized cost, fair value through other comprehensive income or fair value through profit and loss. The classification of financial assets and liabilities is generally based on the business model in which the asset or liability is managed and its contractual cash flow characteristics. Financial assets held within a business model whose objective is to collect contractual cash flows and whose contractual terms give rise to cash flows on specified dates that are solely payments of principal and interest on the principal amount outstanding are measured at amortized cost. After their initial fair value measurement, trade receivable, trade and other payables, operating loan, provision for settlement and loans and borrowings are classified and measured at amortized cost using the effective interest rate method. Upon initial recognition of a non-derivative financial asset, a loss allowance is recorded for expected credit losses (ECL). Loss allowances for trade receivables are measured based on lifetime ECL, based on historical loss information adjusted for current economic and credit conditions.

Under the previous standard, cash, restricted cash equivalents and trade receivable were classified as loans and receivables and operating loan, trade and other payables, provision for settlement and loans and borrowings were classified as other financial liabilities. These are now all classified as amortized cost. There were no changes to the carrying amount recognized in financial statements for any of these items.

(p) 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, 2019 and have not been applied in preparing the Consolidated Financial Statements for the year ended December 31, 2018. The standards applicable to the Company are as follows and will be adopted on their respective effective dates:

(i) 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.

IFRS 16 comes into effect on January 1, 2019. The Company is in the process of finalizing the impact on the financial statements. The Company's assessment indicates that many of the operating lease arrangements will meet the definition of a lease under IFRS 16 and thus be recognized in the statement of financial position as a right-of-use asset with a corresponding liability. The most significant impact of this will be for the lease of premises. The Company does not expect other items to have a significant impact.

The Company has chosen to utilize the modified retrospective approach in application of the standard. This will result in the recognition of a lease liability and a corresponding recognition of a right-of-use asset. The Company has chosen to recognize the right-of-use asset on January 1, 2019 at a value equal to the related liability of the lease. The Company will also use the exemption for any capital leases recognized prior to January 1, 2019 and to only apply IFRS 16 to contracts that were previously identified as leases. As such, the Company will not apply the standard to any contracts not previously identified as containing a lease.

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. Exemptions exist for short-term leases where the term is 12 months or less and for leases of low value items. As well, the classification of cash flows will be impacted as the current presentation of operating lease payments as operating cash flows will be split into financing (principal portion) and operating (interest portion) cash flows under IFRS 16.

Additional disclosures will also be required under IFRS 16. Cathedral plans to apply IFRS 16 initially on January 1, 2019 and estimates that the right-of-use asset and lease liability will be approximately $24 million. The Company continues to assess the impact of adopting IFRS 16 on deferred tax balances.

(ii) Uncertainty over Income Tax Treatments

IFRS Interpretations Committee ("IFRIC") issued IFRIC 23 Uncertainty over Income Tax Treatments ("IFRIC 23") which clarifies the accounting for uncertainties in income taxes. The interpretation requires the entity to use the most likely amount or the expected value of the tax treatment if it concludes that it is not probable that a particular tax treatment will be accepted. It requires an entity to assume that a taxation authority with the right to examine any amounts reported to it will examine those amounts and will have full knowledge of all relevant information when doing so.

IFRIC 23 is effective for annual reporting periods beginning on or after January 1, 2019. Earlier application is permitted. The requirements are applied by recognizing the cumulative effect of initially applying them in retained earnings, or in other appropriate components of equity, at the start of the reporting period in which an entity first applies them, without adjusting comparative information. Full retrospective application is permitted, if an entity can do so without using hindsight. The Company does not expect this standard to have any impact on its 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 consists 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 as at December 31, 2017 consisted of GICs that were 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 25.

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 25.

7. Inventories

All of the Company's inventories are composed of raw materials and consumables. There are no finished goods inventories. For the year ended December 31, 2018, raw materials and consumables recognized as cost of sales were $45,295 (2017 - $34,198). At December 31, 2018, a review of expected demand for inventory balances to be used in equipment repairs was conducted. In 2018, a write-down of $1,474 (2017 - $151) on inventory was recognized.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

8. Equipment

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

Cost	Balance December 31 2017	Additions	Write-off fully amortized	Disposals	Effects of movements in exchange rates	Balance December 31 2018
Directional Drilling equipment	$ 126,555	$ 18,906	$ -	$ (6,846)	$ 236	$ 138,851
Office and computer equipment	8,356	153	-	(27)	151	8,633
Automotive equipment under capital lease	1,296	-	-	(147)	91	1,240
Automotive equipment	1,213	-	-	(63)	88	1,238
Leasehold improvements	1,072	71	(592)	-	(2)	549
Total	$ 138,492	$ 19,130	$ (592)	$ (7,083)	$ 564	$ 150,511

Accumulated depreciation	Balance December 31 2017	Additions	Write-off fully amortized	Disposals	Effects of movements in exchange rates	Balance December 31 2018
Directional Drilling equipment	$ 69,539	$ 12,125	$ -	$ (2,906)	$ 157	$ 78,915
Office and computer equipment	7,580	308	-	(24)	143	8,007
Automotive equipment under capital lease	1,000	28	-	(116)	75	987
Automotive equipment	970	73	-	(45)	75	1,073
Leasehold improvements	1,020	28	(592)	-	5	461
Total	$ 80,109	$ 12,562	$ (592)	$ (3,091)	$ 455	$ 89,443

Net book values	2018	2017
Directional Drilling equipment	$ 59,936	$ 57,016
Office and computer equipment	626	776
Automotive equipment under capital lease	253	296
Automotive equipment	165	243
Leasehold improvements	88	52
Total	$ 61,068	$ 58,383

Leased automotive equipment

The Company leases equipment under a number of finance lease agreements. The leased equipment secures the related lease obligations (see note 14). During 2018, there were non-cash fixed asset additions of $nil (2017 - $45) related to finance lease arrangements.

Review for impairment and direct write-offs

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

The Company determined an impairment test for the directional drilling CGU was not required as at December 31, 2018 or 2017. However, in 2017, the Company determined that certain equipment should be directly written off as a result of low utilization in the amount of $8,287. The assets written down included non-proprietary drilling motors and certain non-proprietary MWD systems. The Company has experienced lower demand for certain non-proprietary equipment.

9. Intangible assets

The Company's intangible assets consist of materials and wages related to equipment development and improvement. The Company reviews the accumulated costs at least quarterly. The 2018 internally developed additions contain $943 of technology group wages related to new product development (2017 - $nil).

In 2018 the Company recognized an impairment of $nil on in progress intangibles (2017 - $146).

	2018	2017
Cost		
Balance at January 1	$ 2,993	$ 2,665
Internally developed additions	1,226	474
Write-down	-	(146)
Balance at end of year	$ 4,219	$ 2,993
Accumulated amortization		
Balance at January 1	$ 1,040	$ 687
Amortization for year	352	353
Balance at end of year	$ 1,392	$ 1,040
Net carrying value at end of year	$ 2,827	$ 1,953

10. 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 related operations have been presented as discontinued operations for 2017. The sale closed in January 2017.

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.

	2018	2017
Revenues	$ -	$ 361
Cost of sales:		
Direct costs	-	(430)
Depreciation	-	(21)
Total cost of sales	-	(451)
Gross margin	-	(90)
Selling, general and administrative expenses:		
Direct costs	-	(66)
Share-based compensation	-	3
Total selling, general and administrative expenses	-	(63)
	-	(153)
Gain (loss) on disposal of property and equipment	-	14
Finance costs	-	(3)
Net loss from discontinued operations	$ -	$ (142)

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

	2018	2017
Cash provided by (used in):		
Operating activities:		
Total loss from discontinued operations	$ -	$ (142)
Items not involving cash		
Depreciation	-	21
Share-based compensation	-	(3)
(Gain) loss on disposal of property and equipment	-	(14)
Finance costs	-	3
Cash flow from (used in) discontinuing operations	$ -	$ (135)

11. Deferred tax assets and income tax expense

In 2018 Q4, Cathedral derecognized $13,059 of deferred tax assets due to a recent history of tax losses within Cathedral's Canadian entity.

Recognized deferred tax assets and liabilities

Deferred tax assets are attributable to the following:

	2018	2017
Equipment	$ (7,512)	$ (8,009)
Non-capital loss carry forwards	6,320	9,302
Accrued expenses deductible in future years	1,726	-
Scientific research and development expenditures	-	4,786
Investment tax credits	-	3,323
Inventory valuation allowance	1,128	749
Intangible assets	193	207
Provision for settlement	121	180
Total	$ 1,976	$ 10,538

Un-recognized deferred tax assets and liabilities:

There are un-recognized deferred tax assets (liabilities) of $15,281 (2017 - $657) related to the following Canadian tax attributes:

	2018 Gross amount	Tax effect	2017 Gross amount	Tax effect
Non-capital loss carry forwards	$ 17,003	$ 4,591	$ -	$ -
Scientific research and development expenditures	17,531	4,733	-	-
Investment tax credits	n/a	5,116	-	-
Net capital loss carry forwards	3,116	841	2,432	657
Total	$ 37,650	$ 15,281	$ 2,432	$ 657

Deferred tax assets have not been recognized in respect of the deductible temporary differences at December 31, 2018 due to a recent history of taxable losses in Canada. The non-capital losses have expiries ranging from 2035 to 2038 and investment tax credits have expiries from 2026 to 2037. The remaining tax attributes do not expire.

Movement in temporary differences during the year

	Balance December 31 2016	Recognized in profit	Recognized in OCI	Balance December 31 2017
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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

	Balance December 31 2017	Recognized in profit	Recognized in OCI	Balance December 31 2018
Equipment	$ (8,009)	$ 497	$ -	$ (7,512)
Non-capital loss carry forwards	9,302	(2,982)	-	6,320
Accrued expenses deductible in future years	-	1,726	-	1,726
Scientific research and development expenditures	4,786	(4,786)	-	-
Investment tax credits	3,323	(3,323)	-	-
Inventory valuation allowance	749	379	-	1,128
Intangible assets	207	(14)	-	193
Provision for settlement	180	(59)	-	121
Total	$ 10,538	$ (8,562)	$ -	$ 1,976

The income taxes are based upon the estimated annual effective rates of 27% (2017 – 27%) for Canadian entities and 22.5% (2017 – 36% for current tax and 22.5% for deferred taxes) for U.S. entities. The income tax expense for the period is comprised as follows:

	2018	2017
Current tax (expense) recovery:		
Current period	$ (2,538)	$ (327)
Adjustment to prior period provisions	241	(78)
Total current tax expense	(2,297)	(405)
Deferred tax (expense) recovery:		
Origination and reversal of temporary differences	4,111	546
Adjustment to prior period provisions	323	470
Total deferred tax recovery	4,434	1,016
Derecognition of deferred tax asset	(13,059)	-
Income tax recovery (expense)	$ (10,922)	$ 611

Income tax expense for 2018 and 2017 differs from the amount that would be expected by applying the expected statutory income tax rates for the following reasons:

	2018	2017
Expected statutory tax rate	27%	27%
Loss before income tax	$ (6,139)	$ (382)
Effective tax rate applied to loss before income tax	$ 1,658	$ 103
Derecognition of deferred tax asset	(13,059)	-
Adjustment to deferred taxes for change in effective tax rates	(8)	(371)
Income taxed in jurisdictions with different tax rates	(225)	74
Non-deductible expenses	(243)	(147)
Adjustment to prior year tax provisions	564	393
Non-taxable portion of gain on disposal of property and equipment	387	522
Other	4	37
Total tax recovery (expense)	$ (10,922)	$ 611

12. Operating loans

	2018	2017
Canadian dollar operating loan	$ 188	$ 1,233
U.S. dollar operating loan	-	-
Total	$ 188	$ 1,233

The Company has a $5,000 operating facility (2017 - $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

	2018	2017
Trade payables	$ 14,597	$ 12,661
Accrued payables	9,271	5,265
Total	$ 23,868	$ 17,926

The Company's exposure to currency and liquidity risk related to trade and other payables is disclosed in note 25.

14. Loans and borrowings

		2018		2017
Current liabilities:				
Current portion of finance lease liabilities	$	89	$	233
Non-current liabilities:				
Finance lease liabilities	$	-	$	46
Secured revolving term loan		7,000		-
Total	$	7,000	$	46

During 2018, there were advances of $7,000 and repayments of $nil on the Company's secured revolving term loan.

Terms and debt repayment schedule

During December 2017, the Company signed a credit facility (the "Facility") with a new lending syndicate. The Facility consists of a $5 million operating facility and a $15 million extendible revolving credit facility. The facility was renewed on November 8, 2018 under the same terms as the original facility and now expires December 31, 2020. The Facility is secured by a general security agreement over all present and future personal property. The Facility provides a definition of 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 compared 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.

Compliance with Facility covenants

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

At December 31, 2018, the Company had drawn $7,000 of its revolving credit facility, $188 of its operating facility and had $6,875 in cash. At December 31, 2018, the Company had consolidated funded debt of $1,595 which includes five outstanding letters of credit ("LOC") which are included in the funded debt calculation. For the trailing twelve months ended December 31, 2018, Credit Agreement EBITDA was $14,314.

The calculation of the financial covenants under the Facility as at December 31, 2018 is as follows:

Covenant	Actual Ratio	Required Ratio
Consolidated funded debt to consolidated Credit Agreement EBITDA ratio	0.1:1	3.0:1 (maximum)
Consolidated interest coverage ratio	32.3:1	2.5:1 (minimum)

Finance lease liabilities

Finance lease liabilities bear interest at rates between 6.0% and 6.7% with maturities in 2019 and are payable as follows:

	2018						2017					
		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	$	91		(2)	$	89	$	209		(1)	$	208
Between one and four years		-		-		-		72		(1)		71
Total	$	91	$	(2)	$	89	$	281	$	(2)	$	279

These amounts are secured by the automotive equipment under capital lease which has a net book value of $253 (2017 - $640).

15. Share capital

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

Common shares issued:

	2018			2017		
	Number		Amount	Number		Amount
Issued, beginning of period	49,383,951	$	88,059	36,295,380	$	74,481
Issued on bought deal and private placement	-		-	12,616,071		13,131
Issued on exercise of options	84,166		96	472,500		447
Issued, end of period	49,468,117	$	88,155	49,383,951	$	88,059

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.

84,166 common shares (2017 - 472,500) were issued as a result of the exercise of vested options. Options were exercised at an average strike price of $0.85 per option (2017 - $0.75). 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 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 earlier 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, 2018 and 2017, and changes during the years then ended is presented below:

	2018 Number	2018 Weighted average exercise price	2017 Number	2017 Weighted average exercise price
Outstanding, beginning of year	2,947,000	$ 1.85	1,350,500	$ 1.85
Granted	1,040,500	0.92	2,197,750	1.08
Expired or forfeited	(233,000)	3.08	(128,750)	2.20
Exercised	(84,166)	0.85	(472,500)	0.75
Outstanding, end of year	3,670,334	$ 1.20	2,947,000	$ 1.85
Exercisable, end of year	1,607,665	$ 1.46	593,319	$ 2.50

The range of exercise prices for the options outstanding at December 31, 2018 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	1,027,834	$ 0.92	2.67	3,334	$ 0.43
$1.01 to $2.00	2,088,500	1.08	1.38	1,050,331	1.11
$2.01 to $3.00	554,000	2.13	0.20	554,000	2.13
$0.43 to $2.13 total	3,670,334	$ 1.20	1.56	1,607,665	$ 1.46

During the year ended December 31, 2018, the Company has recorded share-based compensation expense of $634 (2017 - $275) related to the share option plan.

During the year ended December 31, 2018, the Company granted 1,040,500 share options. The following table sets out the assumptions used in applying the Black-Scholes model for the options issued as well as the resulting fair value:

	2018
Number of options issued	1,040,500
Exercise price	$ 0.92
Fair value per option (weighted average)	$ 0.48
Expected annual dividend per share	$ -
Risk-free interest rate (weighted average)	2.0%
Expected share price volatility (weighted average)	79.8%
Forfeiture rate per annum	10.0%

16. Earnings (loss) per share

Basic earnings per share

The calculation of basic earnings per share at December 31, 2018 was based on the net earnings (loss) attributable to common shareholders of $(17,061) (2017 –$87) and a weighted average number of common shares outstanding of 49,445,205 (2017 – 47,380,723), calculated as follows:

Weighted average number of ordinary shares

	2018	2017
Issued January 1	49,383,951	36,295,380
Effect of shares issued during the year	61,254	11,085,343
Weighted average number of common shares	49,445,205	47,380,723

Diluted earnings per share

The calculation of diluted earnings per share at December 31, 2018 was based on the net earnings (loss) attributable to common shareholders of $(17,061) (2017 –$87) and a weighted average number of common shares outstanding of 49,546,567 (2017 – 47,577,298), calculated as follows

Weighted average number of common shares (diluted)

	2018	2017
Weighted average number of common shares (basic)	49,445,205	47,380,723
Effect of share options on issue	101,362	196,575
Weighted average number of common shares (diluted)	49,546,567	47,577,298

At December 31, 2018, 1,598,500 options (2017 – 2,863,000) 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.

17. Nature of expenses

The nature of expenses can be specified as follows:

	Cost of sales	Selling, general & administrative	Technology	Total
Year ended December 31, 2018				
Depreciation and amortization	$ (12,719)	$ (202)	$ -	$ (12,921)
Share-based compensation	(180)	(454)	-	(634)
Staffing costs, excluding share-based compensation	(57,927)	(9,203)	(2,341)	(67,130)
Repairs and maintenance	(45,292)	-	-	(45,292)
Other expenses	(39,217)	(5,837)	(140)	(45,054)
Total	$ (155,335)	$ (15,696)	$ (2,481)	$ (171,031)
Year ended December 31, 2017				
Depreciation and amortization	$ (11,043)	$ (104)	$ -	$ (11,147)
Share-based compensation	(69)	(206)	-	(275)
Staffing costs, excluding share-based compensation	(48,862)	(7,683)	(2,204)	(56,545)
Repairs and maintenance	(36,983)	-	-	(36,983)
Other expenses	(34,573)	(7,705)	(62)	(42,278)
Total	$ (131,530)	$ (15,698)	$ (2,266)	$ (147,228)

18. Foreign exchange gain (loss) and finance costs

	2018	2017
Foreign exchange gain (loss):		
Realized foreign exchange gain (loss)	$ 100	$ (120)
Unrealized foreign exchange gain (loss) on intercompany balances	(2,260)	1,903
Foreign exchange gain (loss)	$ (2,160)	$ 1,783
Finance costs		
Interest on revolving term loan	$ (182)	$ (150)
Interest on operating loan	(75)	(49)
Standby fees	(46)	(151)
Interest on finance lease liabilities	(4)	(15)
Other interest	(136)	(319)
Finance costs	$ (443)	$ (684)

19. Changes in non-cash working capital

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

	2018	2017
Trade receivables	$ (927)	$ (7,640)
Inventories	(1,507)	(3,243)
Prepaid expenses and deposits	(231)	151
Trade and other payables	4,583	5,089
Impact of foreign exchange rate differences	1,564	(1,380)
Total changes in non-cash working capital	3,482	(7,023)
Changes in investing non-cash working capital	(562)	1,925
Changes in operating non-cash working capital	$ 4,044	$ (8,948)

20. Operating segments

The Company and its wholly owned subsidiary are engaged in the business of providing directional drilling services to oil and natural gas companies in western Canada and 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.

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, 2018	Year ended December 31, 2017	December 31, 2018	December 31, 2017
Canada	$ 31,123	$ 32,315	$ 52,814	$ 47,941
United States	129,704	114,780	26,116	22,933
Total	$ 160,827	$ 147,095	$ 78,930	$ 70,874

Major customer

In 2018 revenues from a customer of the Company represented approximately 15% (2017 –20%) of the Company's total revenues.

21. Commitments

In the normal course of business, the Company incurs contractual obligations. As at December 31, 2018, the Company's commitment to purchase equipment is approximately $409. Cathedral anticipates expending these funds in 2019 Q1.

The Company has issued the following five LOC:

- two 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 securing the Company's corporate credit cards in the amounts of $75 CAD and $175 USD.

22. 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 January 2019 to March 2030. Certain leases have set annual increases. The total future minimum lease payments are as follows:

2019	$3,508
2020	3,505
2021	3,528
2022	3,565
2023	3,602
Thereafter	11,409

During the year ended December 31, 2018, an amount of $4,219 was recognized as an expense in profit or loss in respect of operating leases (2017 - $3,671).

23. 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 15).

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:

	2018	2017
Short-term employment benefits (1)	$ 2,379	$ 1,546
Share-based compensation	341	159
Total expense recognized as share-based compensation	$ 2,720	$ 1,705

(1) Including severance payments

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 (2017 - nil), and no outstanding balances exist as at period end (2017 - nil).

24. Comparative figures

Certain comparative figures have been reclassified to conform to current year presentation.

25. 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 15% of the Company's receivables are attributable to sales transactions with a single customer (2017 - 20%).

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

		2018		2017
Trade receivables	$	35,583	$	33,885

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

Carrying amount

		2018		2017
Canada	$	7,851	$	7,896
United States		27,732		25,989
Total	$	35,583	$	33,885

The Company's most significant customer accounts for $3,953 of the trade receivables carrying amount at December 31, 2018 (2017 - $5,151).

Impairment losses

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

	2018				2017			
		Gross		Impairment		Gross		Impairment
Not past due	$	31,864	$	(232)	$	29,178	$	(58)
Past due 61-90 days		2,491		-		2,922		-
Past due over 91 days		1,612		(152)		1,899		(56)
Total	$	35,967	$	(384)	$	33,999	$	(114)

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

		2018		2,017
Balance, beginning of year	$	58	$	433
Current year provisions		326		-
Reversals of losses previously recognized		-		(375)
Balance, end of year	$	384	$	58

At December 31, 2018 an impairment loss of $89 (2017 - $64) 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, 2018		Carrying amount		Contractual cash flow		Under 6 months		6-12 months		1-2 years		2-5 years		Thereafter
Demand bank loans	$	188	$	188	$	188	$	-	$	-	$	-	$	-
Secured revolving term loan		7,000		7,000		-		-		7,000		-		-
Finance lease liabilities		89		91		51		40		-		-		-
Trade and other payables		22,508		22,508		22,508		-		-		-		-
Provision for settlement		491		491		82		82		327		-		-
	$	30,276	$	30,278	$	22,829	$	122	$	7,327	$	-	$	-

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		2018		2017
Cash	$	4,795	$	2,805
Trade receivables		20,336		25,990
Trade payables		(12,070)		(9,807)
Finance lease liabilities		(19)		(193)
Provision for settlement		(360)		(637)
Total	$	12,682	$	18,158

The following significant exchange rates applied during the year:

		Average rate				Reporting date spot rate		
		2018		2017		December 31, 2018		December 31, 2017
USD $1 to CAD	$	1.30	$	1.30	$	1.36	$	1.26

Sensitivity analysis

A 10% strengthening of CAD against USD at December 31, 2018 would decrease equity and other comprehensive income by $1,573 (2017 - $2,075). The analysis assumes that all other variables, in particular interest rates remain constant. The analysis is performed on the same basis for 2017, albeit that the reasonably possible foreign exchange rate variances were different.

A weakening of CAD at December 31, 2018 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, 2017	
	Fixed rate carrying value	Variable rate carrying value	Fixed rate carrying value	Variable rate carrying value
Financial liabilities	$ 89	$ 7,188	$ 279	$ 1,233

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 $72 (2017 - $12) per annum based upon the balance of financial institution indebtedness and long-term debt with a floating interest rate outstanding as at December 31, 2018.

Fair values of financial instruments

The Company has designated its trade and other payables as other financial liabilities carried at amortized cost. Trade 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 Company has no financial instruments that are recorded at fair values.

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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