



Condensed Interim Consolidated Financial Statements

Nine Month Period Ended

September 30, 2018

(Unaudited)

(Expressed in Canadian Dollars)

NOTICE TO READER

The accompanying unaudited condensed interim consolidated financial statements have been prepared by and are the responsibility of the management.

The Company's independent auditor has not performed a review of these financial statements in accordance with the standards for a review of interim financial statements by an entity's auditor.

HILLCREST PETROLEUM LTD.**Condensed Interim Consolidated Statements of Financial Position**

(Expressed in Canadian dollars)

(Unaudited)

	September 30, 2018	December 31, 2017
	(\$)	(\$)
ASSETS		
Current assets		
Cash	2,262	59,186
Receivables	11,226	15,674
Prepaid expenses	33,436	137,953
Total current assets	46,924	212,813
Non-current assets		
Exploration and evaluation assets (Note 4)	-	38,264
TOTAL ASSETS	46,924	251,077
LIABILITIES		
Current liabilities		
Accounts payable and accrued liabilities (Note 6)	728,272	505,166
Current portion of loans (Notes 7 and 8)	763,945	829,533
Current portion of decommissioning liability (Note 8)	34,396	33,893
Total current liabilities	1,526,613	1,368,592
Loans (Notes 7 and 8)	245,441	260,041
Embedded derivative liability (Note 7)	9,200	73,700
Decommissioning liability (Note 10)	59,928	8,951
TOTAL LIABILITIES	1,841,182	1,711,284
SHAREHOLDERS' DEFICIENCY		
Share capital (Note 11)	7,698,595	7,029,436
Contributed surplus (Note 11)	1,349,182	1,345,420
Reserves (Note 11)	170,904	170,631
Deficit	(11,012,939)	(10,005,694)
	(1,794,258)	(1,460,207)
TOTAL LIABILITIES & SHAREHOLDERS' DEFICIENCY	46,924	251,077

Nature of operations and going concern (Note 1)**Commitments (Note 12)**

On behalf of the Board of Directors:

"Don Currie"
Director

"Thomas Milne"
Director

HILLCREST PETROLEUM LTD.**Condensed Interim Consolidated Statements of Income (Loss) and Comprehensive Income (Loss)**

(Expressed in Canadian dollars)

(Unaudited)

	Three Month Period Ended September 30, 2018	Three Month Period Ended September 30, 2017	Nine Month Period Ended September 30, 2018	Nine Month Period Ended September 30, 2017
	(\$)	(\$)	(\$)	(\$)
Revenue, net of royalties	6,387	-	51,623	36,299
Expenses				
Operating costs	20,831	7,207	111,271	49,035
Consulting fees (Note 9)	9,485	82,058	110,335	194,807
Depletion and depreciation (Note 5)	-	-	-	3,588
Office and general	134,351	217,550	446,283	488,673
Share-based payments (Note 11)	3,223	-	44,821	231,400
Workover costs	-	-	-	59,303
	167,890	306,815	712,710	1,026,806
Loss from operations	(161,503)	(306,815)	(661,087)	(990,507)
Change in fair value of loan conversion liability (Note 7)	32,700	-	64,500	-
Financing expenses	(55,288)	(111,136)	(207,507)	(247,813)
Gain on disposal of oil and gas properties (Note 5)	-	-	-	56,728
Gain on loss of control of HGOM (Note 17)	-	-	-	6,847,550
Impairment of oil and gas properties (Note 5)	-	-	(202,525)	-
Foreign exchange gain	1,054	2,802	(626)	13,205
Net income (loss) for the period	(183,037)	(415,149)	(1,007,245)	5,679,163
Item that may be subsequently reclassified to net loss				
Exchange differences on translating foreign operations	17	(5,140)	273	186,611
Comprehensive income (loss) for the period	(183,020)	(420,289)	(1,006,972)	5,865,774
Basic and diluted income (loss) per share	(0.00)	(0.01)	(0.01)	0.08
Weighted average common shares outstanding:				
Basic	87,293,226	74,103,891	84,227,589	70,162,899
Diluted	87,293,226	74,103,891	84,227,589	70,162,899

The accompanying notes are an integral part of these condensed interim consolidated financial statements

HILLCREST PETROLEUM LTD.**Condensed Interim Consolidated Statements of Changes in Shareholders' Deficiency**

(Expressed in Canadian dollars)

(Unaudited)

	Share Capital		Reserves				Shareholders' Deficiency
	Number of Shares	Amount	Contributed Surplus	Warrants	Foreign Currency Translation	Deficit	
		(\$)	(\$)	(\$)	(\$)	(\$)	(\$)
Balance at December 31, 2016	60,095,655	6,178,384	980,454	76,000	1,272,392	(15,290,227)	(6,782,997)
Proceeds from private placement	14,494,857	836,640	-	-	-	-	836,640
Share issuance costs	-	(5,588)	-	-	-	-	(5,588)
Vesting of stock options	-	-	231,400	-	-	-	231,400
Loss of control of subsidiary	-	-	-	-	(1,340,577)	-	(1,340,577)
Net income and comprehensive income for the period	-	-	-	-	186,611	5,679,163	5,865,774
Balance at September 30, 2017	74,590,512	7,009,436	1,211,854	76,000	118,426	(9,611,064)	(1,195,348)
Shares for services	285,714	20,000	-	-	-	-	20,000
Vesting of stock options	-	-	57,566	-	-	-	57,566
Loss of control of subsidiary	-	-	-	-	(1,327)	-	(1,327)
Transfer expired warrants to contributed surplus	-	-	76,000	(76,000)	-	-	-
Warrants issued for services	-	-	-	47,550	-	-	47,550
Net income and comprehensive income for the period	-	-	-	-	5,982	(394,630)	(388,648)
Balance at December 31, 2017	74,876,226	7,029,436	1,345,420	47,550	123,081	(10,005,694)	(1,460,207)
Proceeds from private placement	9,992,000	499,600	-	-	-	-	499,600
Exercise of stock options	725,000	84,559	(41,059)	-	-	-	43,500
Shares issued to settle debts	1,700,000	85,000	-	-	-	-	85,000
Vesting of stock options	-	-	44,821	-	-	-	44,821
Net income and comprehensive income for the period	-	-	-	-	273	(1,007,245)	(1,006,972)
Balance at September 30, 2018	87,293,226	7,698,595	1,349,182	47,550	123,354	(11,012,939)	(1,794,258)

The accompanying notes are an integral part of these condensed interim consolidated financial statements

HILLCREST PETROLEUM LTD.**Condensed Interim Consolidated Statements of Cash Flows**

(Expressed in Canadian dollars)

(Unaudited)

	Nine Month Period Ended September 30, 2018	Nine Month Period Ended September 30, 2017
	(\$)	(\$)
Net income (loss) for the period	(1,007,245)	5,679,163
Adjusted for items not involving cash:		
Accretion expense	42,197	65,096
Accrued interest expense	28,452	36,411
Change in fair value of loan conversion liability	(64,500)	-
Depletion and depreciation	-	3,588
Impairment of oil and gas properties	202,525	-
Gain on loss of control of HGOM	-	(6,847,550)
Gain on disposal of oil and gas properties	-	(56,728)
Share-based payments	44,821	231,400
Unrealized foreign exchange loss	261	(8,908)
Changes in non-cash working capital:		
Accounts receivable	12,947	27,160
Prepaid expenses	106,625	31,184
GST receivable	-	(2,085)
Accounts payable and accrued liabilities	271,593	(253,811)
Cash flows used in operating activities	(362,324)	(1,095,080)
Proceeds from disposal of oil and gas properties	-	309,873
Exploration and evaluation expenditures	(114,163)	-
Cash disposed of due to loss of control of HGOM	-	(111,763)
Cash flows provided by investing activities	(114,163)	198,110
Proceeds from private placement	445,600	771,640
Proceeds from exercise of stock options	35,000	-
Share subscriptions received in advance	-	14,000
Share issuance costs	-	(5,589)
Proceeds from loans	37,000	260,950
Repayment of loans	(98,049)	(247,657)
Cash flows provided by financing activities	419,551	793,344
Change in cash	(56,936)	(103,626)
Effect of exchange rate changes on cash denominated in a foreign currency	12	(16)
Cash, beginning of the period	59,186	184,940
Cash, end of the period	2,262	81,298
Supplemental cash flow information (Note 16)		

The accompanying notes are an integral part of these condensed interim consolidated financial statements

Hillcrest Petroleum Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
Nine Month Period Ended September 30, 2018
(Unaudited - Expressed in Canadian dollars)

1. NATURE OF OPERATIONS AND GOING CONCERN

Hillcrest Petroleum Ltd. (the "Company") was incorporated on May 2, 2006 under the Business Corporations Act of British Columbia, and is in the business of acquiring, exploring and developing exploration interests in oil and gas projects located in North America. The Company's registered office is suite 1300 - 1030 West Georgia Street, Vancouver, BC, V6E 2Y3. The Company's shares are listed for trading on the TSX Venture Exchange ("TSXV") under the symbol "HRH" and on the OTCQB Exchange under the symbol "HLRTF".

The Company is subject to several categories of risk associated with the exploration and development of oil and gas resources. Oil and gas exploration and production is a speculative business, and involves a high degree of risk. Among the factors that have a direct bearing on the Company's prospects are uncertainties inherent in estimating oil and gas reserves, future hydrocarbon production, and cash flows, particularly with respect to wells that have not been fully tested and with wells having limited production histories; access to additional capital; changes in the price of oil and gas; availability and cost of services and equipment; and the presence of competitors with greater financial resources and capacity.

These condensed interim consolidated financial statements have been prepared on the basis of a going concern, which contemplates the realization of assets and the discharge of liabilities in the normal course of business for the foreseeable future. The Company recorded a net loss for the nine month period ended September 30, 2018 of \$1,007,245 and had a working capital deficiency of \$1,479,689 as at September 30, 2018. The Company's ability to meet its obligations as they fall due and to continue to operate as a going concern is dependent on the continued financial support of its creditors and its shareholders and ultimately, the attainment of profitable operations. There is no certainty that the Company will continue to produce revenue due to the inherent production risks associated with the oil and natural gas industry. In the past, the Company has relied on sales of equity securities, debt instruments and asset sales to meet its cash requirements. There can be no assurance that funding from this or other sources will be sufficient in the future to satisfy operational requirements and cash commitments. Even if the Company is able to obtain new financing, it may not be on commercially reasonable terms or terms that are acceptable to it. Failure to obtain such financing on a timely basis could cause the Company to reduce or terminate its operations.

Due to the conditions and events as noted above, there is material uncertainty casting significant doubt on the Company's ability to continue as a going concern. These condensed interim consolidated financial statements do not include any adjustments to the recoverability and classification of recorded asset amounts and classification of liabilities that might be necessary should the Company be unable to continue as a going concern. These adjustments could be material.

2. BASIS OF PREPARATION

Statement of Compliance

These condensed interim financial statements, including comparatives, have been prepared in accordance with IAS 34, Interim Financial Reporting, as issued by the International Accounting Standards Board ("IASB") and the interpretations of the IFRS Interpretations committee. They do not include all disclosures required by International Financial Reporting Standards ("IFRS") for annual financial statements, and therefore should be read in conjunction with the Company's audited financial statements for the year ended May 31, 2018, prepared in accordance with IFRS as issued by the IASB

These condensed interim consolidated financial statements were approved by the Board of Directors of the Company on November 29, 2018.

Hillcrest Petroleum Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
Nine Month Period Ended September 30, 2018
(Unaudited - Expressed in Canadian dollars)

2. BASIS OF PREPARATION (continued)

Basis of Measurement

The condensed interim consolidated financial statements have been prepared on a historical cost basis, using the accrual basis of accounting, except for cash flow information and certain financial liabilities that are measured at fair value.

Basis of Consolidation

These condensed interim consolidated financial statements include the accounts of the parent company, Hillcrest Petroleum Ltd., and its wholly-owned subsidiaries. Intercompany balances and transactions, and any unrealized income and expenses arising from intercompany transactions, are eliminated in preparing the condensed interim consolidated financial statements.

<u>Name of Subsidiary</u>	<u>Jurisdiction of Incorporation</u>	<u>Principal Activity</u>
Hillcrest Exploration Ltd. ("HEL")	USA	Oil and Gas exploration
1084580 BC Ltd.	Canada	Oil and Gas exploration
2044573 Alberta Ltd.	Canada	Oil and Gas exploration
102031850 Saskatchewan Ltd.	Canada	Oil and Gas exploration
Hillcrest Resources (Arizona) Ltd. ("HARL")	USA	Dormant

Functional and Presentation Currency

These condensed interim consolidated financial statements are presented in Canadian dollars. The functional currency of the parent, 1084580 BC Ltd., 2044573 Alberta Ltd., 102031850 Saskatchewan Ltd. and HARL is the Canadian dollar. The functional currency of HEL is the United States dollar.

Use of Estimates and Judgements

The preparation of these condensed interim consolidated financial statements requires management to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and reported amounts of expenses during the period. Actual results could differ from these estimates.

These condensed interim consolidated financial statements include estimates which, by their nature, are uncertain. The impacts of such estimates are pervasive throughout the consolidated financial statements, and may require accounting adjustments based on future occurrences. Revisions to accounting estimates are recognized in the period in which the estimate is revised and future periods if the revision affects both current and future periods. These estimates are based on historical experience, current and future economic conditions and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Significant assumptions about the future and other sources of estimation uncertainty that management has made at the reporting date that could result in a material adjustment to the carrying amounts of assets and liabilities, in the event that actual results differ from assumptions made, relate to, but are not limited to, the following:

Hillcrest Petroleum Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
Nine Month Period Ended September 30, 2018
(Unaudited - Expressed in Canadian dollars)

2. BASIS OF PREPARATION (continued)

Use of Estimates and Judgements (continued)

Depletion and Depreciation

The amounts recorded for depletion and depreciation of oil and natural gas properties and the amounts used in impairment testing are based on independent estimates of proved and probable reserves, well production rates, realized and forecast oil and natural gas prices, future development costs and other relevant assumptions. By their nature, these estimates are subject to measurement uncertainty. Accordingly, the impact on the consolidated financial statements for future periods may be material.

Decommissioning provisions

Restoration costs will be incurred by the Company at the end of the operating life of the Company's oil properties. The Company estimates abandonment and reclamation costs based on a combination of publicly available industry benchmarks and internal site specific information. For producing wells and facilities, the expected timing of settlement is estimated based on the period to abandonment for each field, as per an independent report. The ultimate restoration liability is uncertain and can vary in response to many factors including changes to relevant legal requirements, the emergence of new restoration techniques, experience at other production sites, or changes in the risk-free discount rate. The expected timing and amount of expenditure can also change in response to changes in reserves or changes in laws and regulations or their interpretation. As a result, there could be significant adjustments to the provisions established which would affect future financial results.

Income taxes

The calculation of income taxes requires judgment in applying tax laws and regulations, estimating the timing of the reversals of temporary differences, and estimating the reliability of deferred tax assets. These estimates impact current and deferred income tax assets and liabilities, and current and deferred income tax expense (recovery).

Significant judgements that management has made at the end of the reporting period are as follows:

Determination of functional currency

The functional currency of each entity is the currency of the primary economic environment in which that entity operates. The Company has determined the functional currency of the parent company, 1084580 BC Ltd., 2044573 Alberta Ltd., 102031850 Saskatchewan Ltd. and Hillcrest Resources (Arizona) Ltd. to be the Canadian dollar, and that of the remaining subsidiaries be the United States dollar. Determination of the functional currency involves certain judgments to determine the primary economic environment. The functional currency may change if there is a change in events and conditions which determine the primary economic environment.

Carrying value and the recoverability of exploration and evaluation assets

Management has determined that exploration, evaluation and related costs incurred which were capitalized may have future economic benefits and may be economically recoverable. Management uses several criteria in its assessments of economic recoverability and probability of future economic benefits including geologic and other technical information, history of conversion of mineral deposits with similar characteristics to its own properties to proven and probable mineral reserves, scoping and feasibility studies, accessible facilities and existing permits.

Hillcrest Petroleum Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
Nine Month Period Ended September 30, 2018
(Unaudited - Expressed in Canadian dollars)

2. BASIS OF PREPARATION (continued)

Use of Estimates and Judgements (continued)

Fair value of stock options and other share-based payments

Management assesses the fair value of stock options and other share-based payments granted in accordance with the accounting policy stated in Note 3 to the consolidated financial statements. The fair value of the options granted is measured using the Black-Scholes model, taking into account the terms and conditions upon which the options are granted. Changes in assumptions concerning volatilities, interest rates and expected life could have significant impact on the fair valuation attributed to the Company's stock options.

Fair value of embedded derivatives

Management assesses its financial instruments in order to identify whether or not non-derivative instruments might contain an embedded derivative component. If such a derivative component is identified, then it must be separated from the non-derivative host contract and recorded at fair value. The fair value of the embedded derivative is measured using the Black-Scholes model, taking into account the terms and conditions upon which the derivative is granted. Changes in assumptions concerning volatilities, interest rates and expected life could have significant impact on the fair valuation attributed to the embedded derivative.

Carrying value and the recoverability of property and equipment

The Company reviews its equipment for indicators of impairment whenever there is a change in events or circumstances that indicate an asset may be impaired and at each reporting period. Reviews are undertaken to evaluate the carrying value of the property and equipment considering, among other factors: the carrying value of each type of asset and the changes in circumstances that affect the carrying value of the Company's property and equipment. If such indication exists, a formal estimate of recoverable amount is performed and an impairment loss is recognized to the extent that the carrying amount exceeds the recoverable amount. The determination of recoverable amount is based on fair value estimation.

Determination of cash generating units

Management must make judgements as to which oil and gas properties can be aggregated into a cash generating unit ("CGU"). The Company's oil and gas assets are aggregated into CGUs for the purpose of calculating impairment and depletion. Factors considered by management include, but are not limited to, the product produced (i.e. oil versus gas), the common infrastructure shared by individual properties, proximity of properties to each other, and planned development activities.

Hillcrest Petroleum Ltd.

Notes to the Condensed Interim Consolidated Financial Statements

Nine Month Period Ended September 30, 2018

(Unaudited - Expressed in Canadian dollars)

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

These condensed interim consolidated financial statements have been prepared using the same accounting policies as those used in the Company's annual financial statements at December 31, 2017, with the exception of the newly adopted standards noted below.

During the nine month period ended September 30, 2018, the Company adopted the following accounting standards:

IFRS 9, Financial instruments

This new standard replaces International Accounting Standards ("IAS") 39, Financial Instruments: Recognition and Measurement. IFRS 9 addresses the classification, measurement and de-recognition of financial assets and financial liabilities, introduces a new impairment model for financial assets and new rules for hedge accounting.

IFRS 9 requires financial assets to be classified into one of three measurement categories on initial recognition: FVTPL, fair value through OCI and amortized cost. Measurement and classification of financial assets is dependent on the entity's business model for managing financial assets and the contractual cash flow characteristics of the financial asset. The new standard retains most of the existing requirements for financial liabilities.

IFRS 9 introduces a new impairment model for financial assets. This new model may result in the earlier recognition of credit losses as it requires the Company to account for expected credit losses from the time the financial instruments are first recognized.

IFRS 15, Revenue from Contracts with Customers

This new standard is based on the principle that revenue should be recognized to depict the transfer of goods or services to customers at an amount that the entity expects it will be entitled to in exchange for those goods.

IFRS 15 introduces a new five step model for the recognition of revenue based on when control of a good or service transfers to a customer. The notion of control replaces the existing notion of risks and rewards and could result in changes in the timing of revenue recognition for certain contracts

The adoption of these standards did not have a material impact on the Company's financial statements.

4. EXPLORATION AND EVALUATION ASSETS

	<u>Flaxcombe</u>
	(\$)
Balance at January 1, 2017	-
Additions	<u>38,264</u>
Balance at December 31, 2017	38,264
Additions	114,163
Reclassification (Note 5)	<u>152,427</u>
Balance at September 30, 2018	<u>-</u>

On December 14, 2017, the Company entered into a farm-in agreement with Westcore Energy Ltd. ("Westcore") to workover two previously shut-in oil wells (16-13 and 7-13) in the Flaxcombe area of southwestern Saskatchewan. The Company was required to incur 100% of the workover costs in exchange for a 50% working interest in the wells. In accordance with an approved budget, the Company advanced \$135,000 to complete the workovers. Both wells were completed and reactivated in the first quarter of 2018, and as a result have been reclassified to property and equipment.

Hillcrest Petroleum Ltd.

Notes to the Condensed Interim Consolidated Financial Statements

Nine Month Period Ended September 30, 2018

(Unaudited - Expressed in Canadian dollars)

5. PROPERTY AND EQUIPMENT

	Computers	Oil and Gas Interests	Total
	(\$)	(\$)	(\$)
Cost			
At January 1, 2017	27,293	3,269,335	3,296,628
Disposals	(10,886)	(1,555,928)	(1,566,814)
Foreign exchange movement	(379)	-	(379)
At December 31, 2017	16,028	1,713,407	1,729,435
Additions	-	202,525	202,525
At September 30, 2018	16,028	1,915,932	1,931,960
Accumulated depletion and depreciation			
At January 1, 2017	23,800	2,346,005	2,369,805
Depletion and depreciation for the year		3,588	3,588
Disposals	(7,510)	(1,127,729)	(1,135,239)
Foreign exchange movement	(262)	-	(262)
At December 31, 2017 and September 30, 2018	16,028	1,221,864	1,237,892
Impairment			
At January 1, 2017	-	654,293	654,293
Disposals	-	(162,750)	(162,750)
At December 31, 2017	-	491,543	491,543
Additions	-	202,525	202,525
At September 30, 2018	-	694,068	694,068
Carrying amounts:			
At December 31, 2017	-	-	-
At September 30, 2018	-	-	-

Flaxcombe, Saskatchewan

In January 2018, Well 16-13 and Well 07-13 under the Westcore farm-in agreement were reactivated, and as a result the Company has reclassified the associated costs from exploration and evaluation assets to property and equipment on the condensed interim consolidated statement of financial position.

Hillcrest Petroleum Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
Nine Month Period Ended September 30, 2018
(Unaudited - Expressed in Canadian dollars)

5. PROPERTY AND EQUIPMENT (continued)

Hartburg Project, Texas

As at September 30, 2018, the Company has the following working interests:

<u>Well</u>	<u>Working Interest</u>
Donner #4	48.0%
Brown #1	90.0%

During the year ended December 31, 2017, the Company sold its interest in the Donner #1 well for a cash payment of \$309,873 and the release of liability for any future asset retirement obligations estimated at \$12,305 on a discounted basis. As a result, the Company recorded a gain on disposal of \$56,728.

As at December 31, 2017, all of the remaining wells are shut-in, and the underlying lease agreements with the land owners has terminated. The Company is currently evaluating the status of the well bores and any future plans.

Gulf of Mexico Properties

During the year ended December 31, 2017, the Company completed the Chapter 7 liquidation of its wholly-owned subsidiary HGOM in the U.S. Court for the Southern District of Texas. This has resulted in the disposal of the remaining non-operated assets located shallow offshore waters of the Gulf of Mexico. (Note 18)

Impairment

As at September 30, 2018, the Company reviewed the carrying value of its oil and gas interests and determined there were indicators of impairment with respect to the Flaxcombe wells. As a result, the Company has recorded an impairment charge of \$202,525 on the condensed interim consolidated statement of income (loss) and comprehensive income (loss).

The recoverable amount for the CGUs were based on their fair value less costs of disposal ("FVLCD"). To determine the FVLCD, the Company considered the current operational status and the profitability during the period.

6. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	<u>September 30, 2018</u>	<u>December 31, 2017</u>
	<u>(\$)</u>	<u>(\$)</u>
Trade payables	566,932	411,652
Related party payables	7,875	238
Accrued liabilities	153,465	93,276
	<u>728,272</u>	<u>505,166</u>

7. SECURED LOANS

ASI Loan

As at September 30, 2018, the Company has \$138,550 (December 31, 2017 - \$138,550) outstanding on a senior secured loan facility that bears interest at a rate of 20% per annum and is currently payable on demand. As part of the consideration for the loan facility, the lenders and the arranging agent receive an aggregate 10% overriding royalty interest in the Company's proceeds from all oil, gas and other hydrocarbons produced from any new wells developed on the Company's Hartburg Properties using any portion of the proceeds from the loan.

Hillcrest Petroleum Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
Nine Month Period Ended September 30, 2018
(Unaudited - Expressed in Canadian dollars)

7. SECURED LOANS (continued)

During the nine month period ended September 30, 2018, the Company repaid \$Nil (2017 - \$120,950) in loan principal and incurred \$20,726 (2017 - \$29,204) in interest expense.

Bridge Loan

On August 10, 2016, the Company borrowed \$300,000 under a secured loan agreement (the "Bridge Loan") bearing interest at 1% per month, compounded monthly, and maturing on August 9, 2017. The Bridge Loan is secured by the Company's interest in the Pettit Project leases. The Company also issued 1,500,000 common shares with a value of \$75,000 as payment of arrangement fees and syndication fees incurred in connection with the Bridge Loan. The cash received under the Bridge Loan has been allocated between the fair value of the loan liability and the value of the 1,500,000 common shares. The value ascribed to the common shares as at the loan date was \$75,000, and the residual amount has been allocated to the loan liability.

During the nine month period ended September 30, 2018, the Company incurred \$28,452 (2017 - \$76,396) in interest expense, including \$Nil (2017 - \$47,944) in accretion of the loan liability, and paid \$36,000 (2017 - \$Nil) in accrued interest through the issuance of 720,000 common shares. At September 30, 2018 a total of \$345,395 (December 31, 2017 - \$352,943) in loan principal and accrued interest remained outstanding.

Ballakilley Loan

On June 15, 2017, the Company borrowed \$140,950 under a convertible loan agreement (the "Ballakilley Loan") bearing interest at 20% per annum, payable semi-annually, and maturing on May 31, 2019. The Ballakilley Loan is convertible into common shares of the Company at a price of \$0.07 per share, subject to a reduction if the Company completed a private placement or issues options or warrants at a lower price, at the option of the lender. The cash received under the Ballakilley Loan has been allocated between the fair value of the loan liability and the value of the loan conversion feature which is considered an embedded derivative. The value ascribed to the loan liability as at the loan date was \$35,650, and the residual amount has been allocated to the loan conversion feature.

During the nine month period ended September 30, 2018, the Company incurred \$56,505 (2017 - \$15,207) in interest expense, including \$35,362 (2017 - \$7,326) in accretion of the loan liability. At September 30, 2018 a total of \$162,093 (December 31, 2017 - \$155,878) in loan principal and accrued interest remained outstanding. Additionally, the loan conversion feature has been revalued to \$9,200, and the Company has recorded a gain of \$64,500 on the condensed interim consolidated statement of income (loss).

Project Financing

In February 2017, the Company entered into an arrangement with a third party to provide potential debt financing of up to \$2,500,000. The Company incurred standby charges at a rate of 7% per annum for the availability of this potential debt financing for the acquisition and development of oil projects located in Canada. The Company has not yet borrowed any funds, but has incurred standby charges totalling \$67,027 (2017 - \$103,868) during the nine month period ended September 30, 2018. The actual borrowing terms are to be negotiated if and when funds are borrowed. As at September 30, 2018, the funds available have been reduced to \$600,000.

1055328 BC Ltd. Loan

On October 6, 2017, the Company borrowed \$63,000 under an unsecured loan that bears 12% interest per annum and is repayable on or before October 6, 2018. On June 6, 2018, the Company borrowed an additional \$37,000 under the same terms.

During the nine month period ended September 30, 2018, the Company incurred \$8,794 (2017 - \$Nil) in interest expense. At September 30, 2018, a total of \$108,794 (December 31, 2017 - \$64,039) in loan principal and accrued interest remained outstanding.

Hillcrest Petroleum Ltd.

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8. UNSECURED LOANS

Credit Line

On December 10, 2015, the Company obtained access to an unsecured line of credit bearing interest at an annual rate calculated semi-annually which is equal to the lending rate of the Canadian Imperial Bank of Commerce ("CIBC"). The credit line has a term of 30 months, and it has a maximum capacity of \$400,000 that requires monthly repayments equal to the lesser of i) \$15,000 and ii) the aggregate principal and interest outstanding. In addition, the Company issued 1,000,000 common shares as consideration to the lender. The Company borrowed \$390,000 under the credit line, and the cash received has been allocated between the fair value of the loan liability and the fair value of the 1,000,000 common shares. The fair value of the common shares as at the loan date was \$30,000, and the residual amount has been allocated to the loan liability.

During the nine month period ended September 30, 2018, the Company borrowed \$200,000 (2017 - \$120,000) and incurred \$15,712 (2017 - \$17,993) in interest expense, including \$5,452 (2017 - \$9,026) in accretion of the loan liability. At September 30, 2018, a total of \$337,978 (December 31, 2017 - \$233,393) in loan principal and accrued interest remained outstanding.

Yesnik Loan

On December 21, 2017, the Company entered into an unsecured loan with the spouse of the CEO of the Company wherein the Company borrowed \$200,000 which is to be repaid over a period of five years. The loan bears interest at rate of 12% per annum in addition to 8% per annum in administrative and oversight charges calculated based on outstanding principal. The loan requires quarterly payments over which are comprised of outstanding interest, administrative and oversight charges and \$10,000 of principal.

During the nine month period ended September 30, 2018, the Company repaid the loan in full and incurred \$9,863 (2017 - \$Nil) in interest expense. At September 30, 2018, a total of \$Nil (December 31, 2017 - \$200,000) in loan principal remained outstanding.

9. RELATED PARTY TRANSACTIONS

The following summarizes the Company's related party transactions during the nine month periods ended September 30, 2018 and 2017. Key management personnel included the Chief Executive Officer ("CEO"), Chief Financial Officer ("CFO"), and directors and officers and companies controlled or significantly influenced by them:

Key management compensation

	<u>2018</u>	<u>2017</u>
	(\$)	(\$)
Salary and consulting fees paid or accrued to directors, officers or corporations controlled by directors and officers of the Company	67,500	93,330
Share-based payments paid to certain directors and officers of the Company in connection with the extension of the expiry date of share purchase warrants	35,400	141,411
	<u>102,900</u>	<u>234,741</u>

- a) As at September 30, 2018, a total of \$7,875 (December 31, 2017 - \$Nil) was included in accounts payable and accrued liabilities owing to a corporation controlled by an officer of the Company for unpaid consulting fees. These liabilities are non-interest bearing and payable on demand.
- b) As at September 30, 2018, a total of \$Nil (December 31, 2017 - \$200,000) was included in loans payable owing to the spouse of the CEO. (Refer to Note 8)

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10. DECOMMISSIONING LIABILITY

The decommissioning liability relates to the expected present value of costs of plugging and abandoning the oil and gas held by Hillcrest. The provision for decommissioning is estimated after taking account of inflation, years to abandonment and an appropriate discount rate. As at September 30, 2018, the oil and gas properties had estimated abandonment dates between 2018 and 2025.

Actual decommissioning costs will ultimately depend upon future market prices for the decommissioning work required, which will reflect market conditions at the relevant time. Furthermore, the timing of decommissioning is likely to depend on when the fields cease to produce at economically viable rates. This in turn will depend upon future oil and gas prices, which are inherently uncertain.

The movement in the provision for the decommissioning liability was as follows:

	Hartburg, Texas	Gulf of Mexico Properties	Flaxcombe, Saskatchewan	Total
	(\$)	(\$)		(\$)
Balance, January 1, 2017	68,118	2,698,925	-	2,767,043
Financing expense	1,066	-	-	1,066
Change in estimate	(4,112)	-	-	(4,112)
Disposal	(22,228)	(2,608,160)	-	(2,630,388)
Foreign exchange movement	-	(90,765)	-	(90,765)
Balance, December 31, 2017	42,844	-	-	42,844
Accretion	638	-	744	1,382
Additions	-	-	50,098	50,098
Balance, September 30, 2018	43,482	-	50,842	94,324
Current portion	34,396	-	-	34,396
Non-current portion	9,086	-	50,842	59,928
	43,482	-	50,842	94,324

The total undiscounted amount of estimated cash flows required to settle the provision for decommissioning liability for the Hartburg Project is \$46,358 (December 31, 2017 - \$45,132) as at September 30, 2018. The provision has been estimated using a risk-free discount rate of 1.98% (December 31, 2017 - 1.98%) and an inflation rate of 2.00% (December 31, 2017 - 2.00%).

The total undiscounted amount of estimated cash flows required to settle the provision for decommissioning liability for the Flaxcombe Project is \$60,950 (December 31, 2017 - \$Nil) as at September 30, 2018. The provision has been estimated using a risk-free discount rate of 1.98% (December 31, 2017 - 1.98%) and an inflation rate of 2.00% (December 31, 2017 - 2.00%).

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11. SHARE CAPITAL

Authorized

Unlimited number of common shares without par value

Issued and outstanding

Nine Month Period Ended September 30, 2018

- a) The Company issued 1,700,000 common shares to settle \$85,000 in outstanding debts.
- b) The Company completed a non-brokered private placement in two tranches wherein it issued an aggregate of 9,992,000 units at \$0.05 per unit for gross proceeds of \$499,600. Each unit is comprised of a common share and one half of a common share purchase warrant. Each whole warrant entitles the holder to acquire an additional common share at \$0.10 for two years from the date of closing of the placement.
- c) The Company issued 725,000 common shares due to the exercise of stock options at \$0.06 per share for gross proceeds of \$43,500. The fair value of the options was determined to be \$41,059, and accordingly the amount has been transferred from contributed surplus to share capital.

Year Ended December 31, 2017

- a) The Company completed the second tranche of a non-brokered private placement wherein it issued 8,900,000 units at a price of \$0.05 per unit for gross proceeds of \$445,000. Each unit consisted of one common share in the capital of the Company plus one half of one common share purchase warrant. Each whole warrant of this second tranche offering will entitle the holder to purchase one additional share at a price of \$0.08 until January 18, 2019. The Company paid cash costs of \$5,199 in connection with the closing of the second tranche.
- b) The Company completed a non-brokered private placement in two tranches wherein it issued an aggregate of 5,594,857 units at \$0.07 per unit for gross proceeds of \$391,640. Each unit is comprised of a common share and one half of a common share purchase warrant. Each whole warrant entitles the holder to acquire an additional common share at \$0.10 for a period of two years from the date of closing. The Company paid cash costs of \$389 in connection with the closing of the placement.
- c) The Company issued 285,714 common shares valued at \$20,000 as consideration for consulting services.

Share Purchase Warrants

Nine Month Period Ended September 30, 2018

- a) The Company issued 4,396,000 share purchase warrants in connection with the first tranche of a non-brokered private placement. Each warrant entitles the holder to acquire a common share of the Company at \$0.10 until February 27, 2020.
- b) The Company issued 600,000 share purchase warrants in connection with the second tranche a non-brokered private placement. Each warrant entitles the holder to acquire a common share of the Company at \$0.10 until March 23, 2020.

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11. SHARE CAPITAL (continued)

Year Ended December 31, 2017

- a) The Company issued 4,450,000 share purchase warrants in connection with a non-brokered private placement. Each warrant entitles the holder to acquire a common share of the Company at \$0.08 until January 19, 2019.
- b) The Company issued 1,997,429 share purchase warrants in connection with the first tranche of a non-brokered private placement of units. Each warrant entitles the holder to acquire a common share of the Company at \$0.10 until July 7, 2019.
- c) The Company issued 800,000 share purchase warrants in connection with the second tranche of a non-brokered private placement of units. Each warrant entitles the holder to acquire a common share of the Company at \$0.10 until July 14, 2019.
- d) The Company issued 1,000,000 warrants as partial compensation for services. A total of 500,000 warrants are exercisable at \$0.07 per share and the remainder are exercisable at \$0.10 per share. Each warrant entitles the holder to acquire a common share of the Company until August 17, 2020.

The continuity of the Company's share purchase warrants is as follows:

	Number of Warrants	Weighted Average Exercise Price (\$)
Balance, January 1, 2017	8,962,500	0.08
Issued	8,247,429	0.09
Expired	(5,312,500)	0.08
Balance, December 31, 2017	11,897,429	0.08
Issued	4,996,000	0.10
Balance, September 30, 2018	16,893,429	0.09

The following table summarizes the share purchase warrants outstanding as at September 30, 2018:

Number of Warrants	Weighted Average Exercise Price (\$)	Expiry Date	Weighted Average Remaining Contractual Life (yrs)
500,000	0.07	August 17, 2020	1.88
500,000	0.10	August 17, 2020	1.88
600,000	0.10	March 23, 2020	1.48
4,396,000	0.10	February 27, 2020	1.41
800,000	0.10	July 14, 2019	0.79
1,997,429	0.10	July 7, 2019	0.77
4,450,000	0.08	January 18, 2019	0.30
3,650,000	0.08	December 8, 2018	0.19
16,893,429	0.09		0.78

Hillcrest Petroleum Ltd.

Notes to the Condensed Interim Consolidated Financial Statements

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11. SHARE CAPITAL (continued)

Stock Options

Effective November 4, 2010, the Company adopted a stock option plan to grant stock options to its directors, officers, employees and consultants. In accordance with the policies of the TSXV, the aggregate number of securities reserved for issuance under the plan, at any point in time, will be 10% of the number of common shares of the Company issued and outstanding at the time the option is granted, less any common share reserved for issuance under share options granted under share compensation arrangements other than the plan. The exercise price of option grants will be determined by the Board of Directors, but will not be less than the closing market price of the common shares on the Exchange at the time of grant. All unexercised options granted under the plan will expire no later than five years from the date of grant.

The Company granted an aggregate of 950,000 stock options during the nine month period ended September 30, 2018. The options vest on different terms, and the Company expensed \$41,598 as share-based compensation.

On February 21, 2017, the Company granted 4,500,000 stock options with a fair value of \$231,400. The options were fully vested on the grant date, and the Company expensed \$231,400 as share-based compensation.

The options granted were valued using the Black-Scholes option pricing model under the following weighted average assumptions:

	2018	2017
Risk-free interest rate	2.11%	1.16%
Expected life of options	3.7 yrs	5 yrs
Volatility	149%	98%
Expected Dividend yield	Nil	Nil
Forfeiture rate	Nil	Nil
Weighted average fair value	\$0.05	\$0.05

The continuity of the Company's stock options is as follows:

	Number of Options	Weighted Average Exercise Price (\$)
Balance, January 1, 2017	1,900,000	0.06
Issued	4,500,000	0.07
Balance, December 31, 2017	6,400,000	0.07
Issued	950,000	0.06
Exercised	(725,000)	0.06
Expired	(1,700,000)	0.06
Balance, September 30, 2018	4,925,000	0.07

Hillcrest Petroleum Ltd.

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11. SHARE CAPITAL (continued)

The following table summarizes the stock options outstanding and exercisable as at September 30, 2018:

Number of Options Outstanding	Number of Options Exercisable	Weighted Average Exercise Price	Expiry Date	Weighted Average Remaining Contractual Life
		(\$)		(yrs)
300,000	75,000	0.06	April 3, 2021	2.51
3,975,000	3,975,000	0.07	February 21, 2022	3.40
300,000	300,000	0.06	May 1, 2022	3.59
350,000	350,000	0.065	June 13, 2022	3.70
4,925,000	4,700,000	0.07		2.89

12. COMMITMENTS

- The Company entered into an office rental agreement in Vancouver, British Columbia with a term of 36 months, terminating on June 15, 2020. The remaining base rent payable under the lease is \$42,374 up until the lease expires. In addition to the base rent of \$2,067, the Company's share of operating costs is estimated at approximately \$1,608 per month.
- HEL entered into an office rental agreement with a term of 72 months, terminating on February 28, 2023. The remaining base rent payable under the lease is US\$125,500 up until the lease expires. In addition to the base rent, the Company's share of operating costs is estimated at approximately US\$1,568 per month.

13. GEOGRAPHICAL SEGMENTED INFORMATION

The Company is engaged in one business activity, being the acquisition, exploration, development and production of oil and gas reserves in Canada and the United States. For the nine month period ended September 30, 2018, all revenues were derived from operations in Canada (2017 - the United States of America).

14. CAPITAL MANAGEMENT

The Company manages its capital structure and makes adjustments to it, based on the funds available to the Company, in order to support the acquisition, exploration and development of oil and gas properties. The Board of Directors does not establish quantitative return on capital criteria for management, but rather relies on the expertise of the Company's management to sustain future development of the business.

The Company is primarily dependent on external financing to fund its activities. In order to carry out the planned exploration and development and pay for administrative costs, the Company will spend its existing working capital and raise additional funds as needed using best efforts. The Company will continue to assess new properties and seek to acquire an interest in additional properties if it feels there is sufficient economic potential and if it has adequate available or committed financial resources to complete such acquisitions.

Management reviews its capital management approach on an ongoing basis and believes that this approach, given the size of the Company, is reasonable.

There were no changes in the Company's approach to capital management during the nine month period ended September 30, 2018. The Company is not subject to externally imposed capital requirements.

Hillcrest Petroleum Ltd.

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15. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Financial Risk Management

The Company's financial instruments that are measured at fair value on a recurring basis in periods subsequent to initial recognition and the fair value hierarchy used to measure them are presented in the table below. The Company classifies its other financial assets and other financial liabilities measured at fair value using a fair value hierarchy that reflects the significance of the inputs used in making the measurements.

The fair value hierarchy has the following levels:

- Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3: Inputs for the asset or liability that is not based on observable market data (unobservable inputs).

The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Company's financial instruments consist of cash, receivables, accounts payable and accrued liabilities and loans.

The fair value of cash, receivables and accounts payable and accrued liabilities approximate their book values because of the short-term nature of these instruments. The carrying amounts of the loans approximate fair value as the applicable interest rates, which were negotiated between the Company and arm's length third parties, are similar to market interest rates which would be available to the Company at the balance sheet date.

Financial Instrument Risk Exposure

The Company is exposed in varying degrees to a variety of financial instrument related risks. The Board approves and monitors the risk management processes.

Credit risk

The Company's credit risk is primarily attributable to cash and accounts receivable. The Company's maximum exposure to credit risk at the end of the reporting period is the carrying value of these assets. Substantially all of the Company's customers are in the oil and natural gas industry and are subject to normal industry credit risks. The remaining customers are related to the recovery of shared office rent and share subscription proceeds. The Company has minimal collection risk related to these receivables and expects to collect the outstanding receivables in the normal course of operations. At September 30, 2018, the maximum credit exposure is the carrying amount of receivable of \$11,226 (December 31, 2017 - \$15,674).

The Company has no significant concentration of credit risk arising from operations. Cash is held with reputable financial institutions, from which management believes the risk of loss to be remote.

Market risk

Market risk is the risk of loss that may arise from changes in market factors such as interest rates, foreign exchange rates, and commodity and equity prices.

Interest rate risk

The Company is exposed to interest rate risk. The Company has an unsecured loan associated with a CIBC line of credit which has a variable interest rate, recalculated quarterly.

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15. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (continued)

Liquidity risk

The Company's approach to managing liquidity risk is to ensure that it will have sufficient liquid capital to meet its current liabilities as they come due. At September 30, 2018, the Company had a working capital deficiency of \$1,477,580 (December 31, 2017 - \$1,155,779), refer to note 1 for further discussion.

The Company's financial liabilities had contractual maturities as follows:

	September 30, 2018	December 31, 2017
	(\$)	(\$)
Less than 1 year	1,520,108	1,334,699
Between 1 – 2 years	224,641	213,741
Between 2 – 5 years	-	120,000
	1,744,749	1,668,440

Foreign currency risk

Foreign currency exchange rate risk is the risk that the fair value of financial instruments or future cash flows will fluctuate as a result of changes in foreign exchange rates. The Company operates in Canada and the United States. All of the Company's oil sales are denominated in Canadian dollars. As a result, the Company has minimal exposure to foreign exchange risk.

16. SUPPLEMENTAL CASH FLOW INFORMATION

	September 30, 2018	September 30, 2017
	(\$)	(\$)
Non-cash investing and financing activities:		
Recognition of the estimated asset retirement obligation for the Flaxcombe project	50,098	-
Common shares issued to settle outstanding liabilities	85,000	-
Exploration and evaluation assets reclassified to property and equipment	152,427	-
Interest paid during the period	35,262	37,271
Income taxes paid during the period	-	-

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17. LOSS OF CONTROL OF HGOM

On February 3, 2017, the Company placed its wholly-owned subsidiary HGOM into a Chapter 7 liquidation in the U.S. Court for the Southern District of Texas. Consequently, the Company has lost control over all of the assets and liabilities of HGOM. In accordance with the guidance of IFRS 10, Consolidated Financial Statements, the Company derecognized the carrying value of the assets and liabilities of HGOM on the effective date.

	Amount
	(\$)
Cash	(111,764)
Restricted cash	(1,979,709)
Equipment	(3,376)
Accounts payable	4,993,662
Asset retirement obligations	<u>2,608,160</u>
	5,506,973
Reclassification of foreign currency balances	<u>1,340,577</u>
Gain on loss of control of HGOM	<u><u>6,847,550</u></u>