



**MANAGEMENT'S DISCUSSION AND ANALYSIS**

For the Nine Months Ended June 30, 2018

## **INTRODUCTION**

This Management's Discussion and Analysis ("MD&A") has been prepared by the management of Permex Petroleum Corporation ("Permex" or the "Company") as of August 28, 2018, and should be read in conjunction with the unaudited interim consolidated financial statements and related notes of the Company for the nine months ended June 30, 2018, and the audited consolidated financial statements of the Company together with the related notes thereto for the period from incorporation on April 24, 2017 to September 30, 2017. The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). All amounts are stated in Canadian dollars unless otherwise indicated.

Additional information related to the Company and its operations is available on SEDAR at [www.sedar.com](http://www.sedar.com) and on the Company web site at <http://permexpetroleum.com>.

## **FORWARD-LOOKING STATEMENTS**

This MD&A may contain "forward-looking statements" that reflect the Company's current expectations and projections about its future results. Forward-looking statements are statements that are not historical facts, and include, but are not limited to: estimates and their underlying assumptions; statements regarding plans, objectives and expectations with respect to future operations, capital raising initiatives, the impact of industry and macroeconomic factors on the Company's operations, and market opportunities; and statements regarding future performance.

Forward-looking statements used in this MD&A are subject to various risks, uncertainties and other factors, most of which are difficult to predict and are generally beyond the control of the Company. These risks, uncertainties and other factors may include, but are not limited to, those set forth under "*Risks and Uncertainties*" below.

Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this MD&A or as of the date otherwise specifically indicated herein. Due to risks, uncertainties and other factors, including the risks, uncertainties and other factors identified above and elsewhere in this MD&A, actual events may differ materially from current expectations. The Company disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by securities law.

## **COMPANY OVERVIEW**

Permex was incorporated on April 24, 2017 under the laws of British Columbia, Canada. The Company is primarily engaged in the acquisition, development and production of oil and gas properties in North America. The Company focuses on acquiring producing assets at a discount to market, increasing production and cash-flow through recompletion and re-entries, secondary recovery and low risk infill drilling and development. Currently, Permex owns and operates oil and gas properties located in Texas and New Mexico, USA.

On May 16, 2018, the Company completed its IPO of 8,135,500 common shares of the Company at a price of \$0.50 per share for aggregate gross proceeds of \$4,067,750. The Company's common shares commenced trading on the Canadian Securities Exchange (the "CSE") on May 17, 2018 under the symbol "OIL".

## **OIL AND GAS PROPERTIES**

### *West Henshaw Property and Oxy Yates Property – New Mexico*

The West Henshaw Property is located in Eddy County, New Mexico in the Delaware basin. Eddy County is in Southeast New Mexico. It is bounded by Chaves County to the north, Otero County to the east, Loving County,

Texas to the south, and Lea County to the west. Eddy County covers 4,198 square miles. The West Henshaw Property is 12 miles northeast of Loco Hills, New Mexico.

As at the date of this MD&A, Permex holds a 100% working interest in the West Henshaw Property, and a 72% net revenue interest.

The West Henshaw Property covers 1,880 acres held by production. There are nine producing wells and four saltwater disposal wells.

The Oxy Yates Property is located in Eddy County, approximately eight miles north of Carlsbad, New Mexico. Eddy County is in Southeast New Mexico. It is bounded by Chaves County to the north, Otero County to the east, Loving County, Texas to the south, and Lea County to the west. Eddy County covers 4,198 square miles. The asset is located in the Delaware Basin.

As at the date of this MD&A, Permex holds a 100% working interest in the Oxy Yates Property, and a 77% net revenue interest.

The Oxy Yates Property covers 680 acres held by production. There are eight producing wells and two shut-in wells. The Yates formation is located at an average depth of 1,200 feet and overlies the Seven River formation and underlies the Tansill formation.

On May 29, 2018, the Company announced that it has signed a farmout agreement with Blackspear Capital Corp to farm out the Oxy Yates property.

#### Pittcock North Property - Texas

The Pittcock North Property is situated in Stonewall County. Stonewall County is in Northwest Texas, in the central part of the North Central Plains. It is bounded on the north by King County, on the east by Haskell County, on the south by Fisher and Jones Counties, and on the west by Kent County. The county seat is approximately 60 miles north-northwest of Abilene. Stonewall County covers 926 square miles.

Permex holds a 100% working interest in the Pittcock North Property, and an 81.25% net revenue interest.

The Pittcock North Property covers 320 acres held by production. There are currently six producing wells, four shut-in wells, two saltwater disposal wells, and a water injection well.

#### Pittcock South Property - Texas

The Pittcock South Property is also in Stonewall County, Texas. Permex holds a 100% working interest in the lease, and a 71.90% net revenue interest.

The Pittcock South Property covers 498 acres in four tracts. There are currently eight producing wells, eleven shut-in wells and two saltwater disposal wells.

#### Peavy Property - Texas

The Peavy Property is located in Young County, Texas in the Permian basin. Young County is in North Central Texas. It is bounded by Archer County to the north, Jack County to the east, Stephens County to the south, and Throckmorton County to the west. Young County covers 931 square miles. The county seat is approximately 55 miles south of Wichita Falls and 65 miles northwest of Fort Worth.

Permex holds a 100% working interest in the Peavy Property, and a 70.48% net revenue interest.

The Peavy Property covers 160 acres held by production. There are currently nine producing wells, four shut-in wells, and one saltwater disposal well.

### McMurtry and Loving Properties - Texas

The McMurtry and Loving Properties are located on the boundary between Jack and Young Counties in Texas. The asset is situated on the north end of the Fort Worth Basin, on the east flank of the Bend Arch. Young County is bounded by Archer County to the north, Jack County to the east, Stephens County to the south and Throckmorton County to the west. Young County covers 931 square miles. Jack County is bounded by Archer, Clay, and Montague Counties to North, Young County to the west, Palo Pinto and Parker Counties to the south, and Wise County to the east. Jack County covers 920 square miles.

Permex holds 100% working interest in the McMurtry and Loving Properties, and a 75% net revenue interest.

The McMurtry lease covers 530 net acres in Young County and has three producing wells and two shut-in wells.

The Loving Estate lease, located in Jack County, contains 980 net acres and has two producing wells, six shut-in wells, and a water disposal well.

### Mary Bullard Property - Texas

The Mary Bullard Property is located in Stonewall County, about 5 ½ miles south west of Aspermont, Texas. The asset is situated on the Eastern Shelf of the Midland Basin. Stonewall County is in Northwest Texas, in the central part of the North Central Plains. It is bounded on the north by King County, on the east by Haskell County, on the south by Fisher and Jones Counties, and on the west by Kent County. The county seat is approximately 60 miles north-northwest of Abilene. Stonewall County covers 926 square miles.

Permex holds a 100% working interest in the Mary Bullard Property, and a 78.625% net revenue interest.

The Mary Bullard Property covers 241 acres held by production and is productive in the Clearfork formation at a depth of approximately 3,200 feet. There is currently one producing well, four shut-in wells, and two water injection wells.

### Windy Jones Property - Texas

The Windy Jones Property consists of forty acres and includes two injection wells and two suspended oil wells. The sole purpose of the Windy Jones Property is to provide waterflood to the offset wells being the Pittcock wells located east boundary of the Windy Jones Property.

Permex holds a 100% working interest in the Windy Jones Property, and a 78.9% net revenue interest.

### ODC San Andres Unit and W.J. "A" Taylor lease - Texas

On June 1, 2018, the Company entered into a purchase and sale agreement with Energy Properties 2000-1 LLC ("Energy Properties") to acquire a 41.4% working interest with a 34.7% net revenue interest in the ODC San Andres Unit and 48% working interest with a 41.51% net revenue interest W.J. "A" Taylor lease located in Gaines County, Texas, in consideration of US\$1,950,000. The Company paid an initial deposit of US\$195,000 upon signing of the agreement and the remaining balance subsequent to June 30, 2018 to complete the purchase.

The property is just under two contiguous sections for a total of 1,220 gross acres, all held by production with all rights and no depth restrictions in the Central Basin Platform of the Permian Basin. There are a total of 52 vertical wells of which 26 are producers, 21 are injection wells, 4 are shut in wells, and one is temporarily abandoned.

## DISCUSSION OF OPERATIONS

### Nine month period ended June 30, 2018

During the nine months ended June 30, 2018, the Company expended \$463,053 in acquisition costs and \$793,960 in development costs for a total of \$1,257,013. A breakdown of capital expenditures incurred during the nine months ended June 30, 2018 on each property is as follows:

	Acquisition costs	Development costs	Total
West Henshaw & Oxy Yates	\$ 210,333	\$ 149,593	\$ 359,926
Pittcock North	-	297,306	297,306
Pittcock South	-	77,407	77,407
Peavy	-	21,234	21,234
McMurtry & Loving	-	118,841	118,841
Mary Bullard	-	73,529	73,529
Windy Jones	-	56,050	56,050
ODC/Taylor	252,720	-	252,720
Total	\$ 463,053	\$ 793,960	\$ 1,257,013

During the nine months ended June 30, 2018, the Company reported a net loss of \$2,176,298. The Company generated total revenue of \$363,823 and incurred direct operating expenses of \$337,643 for a gross profit of \$26,180 or 7.2% during the nine month period.

The general operating expenses excluding share-based payment expenses for the nine months ended June 30, 2018 were \$1,274,590. Some of the significant expense items are summarized as follows:

- Accounting and audit of \$146,260 include audit, accounting, and tax compliance related costs.
- Consulting fees of \$129,838 relate mainly to general engineering, lease management and technical evaluation consulting work.
- Legal fees of \$142,752 relate mainly to legal services related to the IPO and prospectus filing and property acquisitions.
- Marketing and promotion of \$338,625 include costs of IPO road shows, investment conferences, media events and publications, and promotional materials.
- Salaries of \$158,425 include salary expenses for the Company's CEO and administrative personnel. The Company has an employment agreement with the CEO of the Company for monthly base salary of \$12,500.

Stock-based compensation expenses of \$958,552, a non-cash charge, are the estimated fair value of the stock options granted and vested during the period. The Company used the Black-Scholes option pricing model for the fair value calculation.

Decommissioning liabilities are the present value of management's estimate of future costs to be incurred to properly abandon and reclaim the properties held by the Company. Accretion expense is the increase in the decommissioning liability resulting from the passage of time. The accretion of decommissioning liabilities is \$17,703 for the nine months ended June 30, 2018.

### Three month period ended June 30, 2018

During the three months ended June 30, 2018, the Company reported a net loss of \$600,525. The Company generated total revenue of \$122,911 and incurred direct operating expenses of \$103,612 for a gross profit of \$19,299 or 15.7% during the second third quarter.

The general operating expenses excluding share-based payment expenses for the three months ended June 30, 2018 were \$535,966 and were mainly related to IPO and office administrative activities.

### **SUMMARY OF QUARTERLY RESULTS**

Quarterly information for periods prior to September 30, 2017 have not been presented as there is no requirement to present financial information for interim periods prior to the Company becoming a reporting issuer if the Company has not previously prepared financial statements for those periods. As a non-reporting issuer, the Company has not prepared any interim or quarterly financial statements since its inception on April 24, 2017.

The following is the selected unaudited financial information for the Company's two most recent quarters ending with the last quarter for the three months ended June 30, 2018.

	June 30, 2018	March 31, 2018	December 31, 2017
Oil and gas sales	\$ 122,911	\$ 128,379	\$ 112,533
Net income (loss)	\$ (600,525)	\$ (305,497)	\$ (1,270,276)
Net income (loss) – basic and diluted	\$ (0.02)	\$ (0.01)	\$ (0.05)

### **LIQUIDITY AND CAPITAL RESOURCES**

As at June 30, 2018, the Company had a cash balance of \$2,541,083, an increase of \$1,988,914 from the cash balance of \$552,169 on September 30, 2017. The Company spent \$863,266 in operating activities and \$918,297 on capital expenditures. The Company completed two private placements with gross proceeds of \$283,000 during the first quarter and an IPO with gross proceeds of \$4,067,750 in the third quarter.

The Company had working capital of \$2,316,345 as at June 30, 2018 compared to working capital of \$555,869 as at September 30, 2017. On July 3, 2018, the Company paid \$2,233,223 to complete the purchase of the ODC San Andres Unit and W.J. "A" Taylor lease located in Gaines County, Texas, pursuant to the purchase and sale agreement signed on June 1, 2018.

Management estimates that the general operating costs, excluding share-based payments expense, for the next 12 months will be approximately \$1,200,000. In addition, the Company expects to invest additional capital on its oil and gas project development. At present, the current working capital of the Company may not be sufficient to meet these anticipated operating and capital requirements. Management is currently evaluating various financing options including a loan facility and equity financing. The Company will continue to monitor the current economic and financial market conditions and evaluate their impact on the Company's liquidity and future prospects.

### Going Concern

The Company has incurred losses since inception and not yet achieved profitable operations. The Company's ability to continue as a going concern is dependent on its ability to obtain adequate financing on reasonable terms from lenders, shareholders and other investors and/or to commence profitable operations in the future. While the Company has been successful in securing financing to date, there can be no assurances that it will be able to do so in the future. The aforementioned factors indicate the existence of a material uncertainty which may cast significant doubt about the Company's ability to continue as a going concern. Management believes it will be able to raise

equity capital as required in the long term, but recognizes there will be risks involved that may be beyond their control. The annual and interim financial statements do not include any adjustments to the recoverability and classification of reduced asset amounts and classification of liabilities that might be necessary should the Company be unable to continue operations. These adjustments could be material. The Company is not subject to material externally-imposed capital constraints.

## OFF-BALANCE SHEET ARRANGEMENTS

The Company does not have any off-balance sheet arrangements.

## RELATED PARTY TRANSACTIONS

Key management personnel include directors (executive and non-executive) and officers of the Company. The compensation paid or payable to key management personnel during the nine month period ended June 30, 2018 is as follows:

Consulting fees	\$	22,500
Salaries		112,500
Share-based payments		700,873
<b>Total</b>	<b>\$</b>	<b>835,873</b>

On August 1, 2017, the Company entered into an employment agreement with the CEO of the Company for monthly base salary of \$12,500, with no specified term. The employment agreement may be terminated with twelve months' notice or a termination payment equal to twelve months of accrued base salary and a bonus equal to 20% of the annual salary.

As at June 30, 2018, a total of \$1,727 (September 30, 2017 - \$nil) is owing to the Company's CEO for expenses paid on behalf of the Company. The amount is unsecured, non-interest bearing, and repayable on demand.

As at June 30, 2018, a total of \$10,250 (September 30, 2017 - \$7,500) is owing to the Company's Chief Financial Officer ("CFO") for consulting services provided. The amount is unsecured, non-interest bearing, and repayable on demand.

## COMMITMENTS

### Office lease

The Company has entered into an office lease agreement for its office premises for a term ending August 31, 2018. On March 12, 2018, the Company renewed the lease for an additional five year term until August 31, 2023. The annual minimum lease commitments under the lease are as follows:

2018	\$	12,372
2019		49,487
2020		49,487
2021		49,581
2022		50,614
2023		46,396
	<b>\$</b>	<b>257,937</b>

## **Service agreements**

On June 18, 2018, the Company entered into a marketing consulting agreement for a six month term for a fee of \$40,000, payable in common shares of the Company upon next round of financing.

On July 1, 2018, the Company entered into an investor awareness agreement for a three month term for a fee of \$40,000, payable in common shares of the Company upon next round of financing.

On August 14, 2018, the Company entered into an online marketing agreement for a twelve month term for a fee of \$8,200, payable in common shares of the Company upon next round of financing.

On August 15, 2018, the Company entered into a business development consulting agreement for a six month term for a fee of \$50,000, payable in common shares of the Company upon next round of financing.

## **CRITICAL ACCOUNTING ESTIMATES**

The preparation of the Company's consolidated financial statements requires management to make estimates 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. The Company's management reviews these estimates and underlying assumptions on an ongoing basis, based on experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Revisions to estimates are adjusted for prospectively in the period in which the estimates are revised. Significant areas requiring the use of management estimates include:

### *Decommissioning obligations*

Decommissioning obligations require the use of management's best estimates of future decommissioning expenditures, expected timing of expenditures and future inflation rates.

### *Depreciation*

Equipment is amortized over the estimated useful life of the assets. Changes in the estimated useful lives or depreciation rate used could significantly increase or decrease the amount of depreciation recorded during the period and the carrying value of equipment.

### *Petroleum and natural gas interests*

Reserves resources are used in the unit-of-production calculation for depreciation and depletion and the impairment analysis, which affects net loss. There are numerous uncertainties inherent in estimating petroleum and natural gas ("P&NG") reserves. Estimating reserves is complex, requiring many judgments based on geological, geophysical, engineering and economic data. Changes in these judgments could have a material impact on the estimated reserves. These estimates may change, having either a negative or positive effect on net earnings as further information becomes available and as the economic environment changes.

### *Share-based payments*

The determination of the fair value of stock options and agent's warrants using stock pricing models, require the input of highly subjective assumptions, including the expected price volatility. Changes in the subjective input assumptions could materially affect the fair value estimate.

### *Going concern assumption*

The assessment of whether the going concern assumption is appropriate requires management to take into account all available information about the future, which is at least, but not limited to, twelve months from the end of the



reporting period. The Company is aware that material uncertainties related to events or conditions may cast significant doubt upon the Company's ability to continue as a going concern.

## **FINANCIAL INSTRUMENTS**

The Company classified its financial instruments as follows: cash, trade and other receivables, restricted cash and reclamation deposits as loans and receivables and measured at amortized cost; and trade and other payables and amounts due to related parties, as other financial liabilities and measured at amortized cost. Information on certain types of financial instruments is included elsewhere in these financial statements as follows: trade and other receivables (Note 6), restricted cash (Note 7), reclamation deposits (Note 9), trade and other payables (Note 10), and amounts due to related parties (Note 12).

The carrying amount of cash, trade and other receivables, restricted cash, reclamation deposits, trade and other payables and amounts due to related parties carried at amortized cost is a reasonable approximation of fair value due to the relatively short period to maturity of these financial instruments and/or the rate of interest being charged.

### **Financial risk management**

The Company's financial risks arising from its financial instruments are credit risk, liquidity risk, foreign currency exchange risk, interest rate risk and commodity price risk. The Company's exposures to these risks and the policies on how to mitigate these risks are set out below. Management monitors and manages these exposures to ensure appropriate measures are implemented on a timely basis and in an effective manner.

#### *Credit risk*

Credit risk is the risk of potential loss to the Company if the counter party to a financial instrument fails to meet its contractual obligations. The credit risk of the Company is associated with cash, trade and other receivables, amount due from related party, restricted cash and reclamation deposits. The credit risk with respect to its cash, restricted cash and reclamation deposits is minimal as they are held with high-credit quality financial institutions. The Company's GST recoverable is due from the Canadian Government. Management does not expect these counterparties to fail to meet their obligations. The Company does not anticipate any default of its trade receivables, as it transacts with creditworthy customers and management does not expect any losses from non-performance by these customers.

#### *Liquidity risk*

Liquidity risk is the risk that the Company will not meet its obligations associated with its financial liabilities as they fall due. The Company performs cash flow forecasting to ensure sufficient cash is available to fund its projects and operations. As at June 30, 2018, the Company has current assets of \$2,748,668 and current liabilities of \$432,323. The Company's financial liabilities include accrued expenses and trade and other payables which have contractual maturities of 30 days or are due on demand.

At present, the Company's operations do not generate positive cash flows. The Company's primary source of funding has been the issuance of equity securities through private placements and revenue from oil and gas production. Despite previous success in acquiring these financings, there is no guarantee of obtaining future financings.

#### *Foreign exchange rate risk*

Foreign currency exchange risk is the risk that fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Company's functional currency is the Canadian dollar and administrative expenditures are transacted in Canadian dollars. The Company funds its oil and gas operations in the United States by using United States dollars ("US dollars") converted from its Canadian bank accounts. At June 30,

2018, the Company had financial assets of \$2,757,936 and financial liabilities of \$243,489 denominated in United States dollars. A 10% strengthening of the US dollar would affect net loss by approximately \$250,000. The Company does not hedge its foreign exchange risk.

#### *Interest rate risk*

The Company is exposed to interest rate risk arising from cash held in Canadian financial institutions. The interest rate risk on cash is not considered significant due to its short-term nature and maturity. The exposure to interest rates for the Company is considered minimal. The Company has not used any financial instrument to hedge potential fluctuations in interest rates.

#### *Commodity price risk*

Commodity price risk is the risk that future cash flows will fluctuate as a result of changes in the price of oil and natural gas. Commodity prices are impacted by world economic events that affect supply and demand, which are generally beyond the Company's control. Changes in crude oil prices may significantly affect the Company's results of operations, cash generated from operating activities, capital spending and the Company's ability to meet its obligations. The Company manages this risk by constantly monitoring commodity prices and factoring them into operational decisions, such as contracting or expanding its capital expenditures program.

### **OUTSTANDING SHARE DATA**

The Company had the following common shares, stock options and warrants outstanding as at the date of this report:

Issued and Outstanding Common shares	35,973,748
Stock options	3,332,185
Warrants	650,840
	39,956,773

### **CHANGES IN ACCOUNTING POLICIES INCLUDING INITIAL ADOPTION**

There were no new standards effective for periods beginning on or after January 1, 2017 that had an impact on the Company's financial statements. A number of new standards and amendments to existing standards have been issued by the IASB that are mandatory for accounting periods beginning on or after January 1, 2018, or later periods. The Company has not applied these new standards in preparing these financial statements. The following pronouncements are considered by the Company to be the most significant of several pronouncements that may affect the financial statements in future periods.

- New standard IFRS 9 *Financial Instruments* ("IFRS 9") has been issued by the IASB to replace IAS 39 *Financial Instruments: Recognition and Measurement*. IFRS 9 has two measurement categories: amortized cost and fair value. The mandatory effective date of IFRS 9 is for annual periods beginning on or after January 1, 2018.
- New standard IFRS 15 *Revenue from Contracts with Customers* ("IFRS 15") has been issued by IASB to replace IAS 18 *Revenue* and IAS 11 *Construction Contracts*. This new standard sets out the requirements for recognizing and disclosing revenues that apply to all contracts with customers. The effective date of IFRS 15 is for annual periods beginning on or after January 1, 2018.
- New standard IFRS 16 *Leases* ("IFRS 16") has been issued by the IASB to replace IAS 17 *Leases*. This new standard sets out the requirements for recognizing and disclosing leases. The objective is to ensure that lessees and lessors provide relevant information that faithfully represents the transactions. The effective date of IFRS 16 is for annual periods beginning on or after January 1, 2019.

The Company is currently assessing the impact that these new standards will have on its financial statements and has not early adopted any of the new standards.

## **RISK AND UNCERTAINTIES**

### *Commodity price risk*

The prices we receive for our oil and natural gas production heavily influence our revenue, operating results, profitability, access to capital, future rate of growth and carrying value of our properties. Oil and natural gas are commodities, and, therefore, their prices are subject to wide fluctuations in response to relatively minor changes in supply and demand.

Historically, the commodities markets have been volatile, and these markets will likely continue to be volatile in the future. If the prices of oil and natural gas experience a substantial decline, our operations, financial condition and level of expenditures for the development of our oil and natural gas reserves may be materially and adversely affected. The prices we receive for our production, and the levels of our production, depend on numerous factors beyond our control and include the following:

- changes in global supply and demand for oil and natural gas;
- the actions of the Organization of Petroleum Exporting Countries, or OPEC;
- political conditions, including embargoes, in or affecting other oil-producing activity;
- the level of global oil and natural gas exploration and production activity;
- the level of global oil and natural gas inventories;
- weather conditions;
- technological advances affecting energy consumption; and
- the price and availability of alternative fuels.

Volatile oil and natural gas prices make it difficult to estimate the value of producing properties for acquisition and often cause disruption in the market for oil and natural gas producing properties, as buyers and sellers have difficulty agreeing on such value. Price volatility also makes it difficult to budget for and project the return on acquisitions and development and exploitation projects.

Our revenues, operating results, profitability and future rate of growth depend primarily upon the prices we receive for oil and, to a lesser extent, natural gas that we sell. Prices also affect the amount of cash flow available for capital expenditures and our ability to borrow money or raise additional capital. In addition, we may need to record asset carrying value write-downs if prices fall. A significant decline in the prices of natural gas or oil could adversely affect our financial position, financial results, cash flows, access to capital and ability to grow.

### *Reserve recovery risk*

There are numerous uncertainties inherent in estimating crude oil and natural gas reserves and their value. Reservoir engineering is a subjective process of estimating underground accumulations of crude oil and natural gas that cannot be measured in an exact manner. Because of the high degree of judgment involved, the accuracy of any reserve estimate is inherently imprecise, and a function of the quality of available data and the engineering and geological interpretation. Our reserves estimates are based on 12-month average prices, except where contractual arrangements exist; therefore, reserves quantities will change when actual prices increase or decrease. In addition, results of drilling, testing, and production may substantially change the reserve estimates for a given reservoir over time. The estimates of our proved reserves and estimated future net revenues also depend on a number of factors and assumptions that may vary considerably from actual results, including:

- historical production from the area compared with production from other areas;
- the effects of regulations by governmental agencies, including changes to severance and excise taxes;
- future operating costs and capital expenditures; and

- workover and remediation costs

For these reasons, estimates of the economically recoverable quantities of crude oil and natural gas attributable to any particular group of properties, classifications of those reserves and estimates of the future net cash flows expected from them prepared by different engineers or by the same engineers but at different times may vary substantially. Accordingly, reserves estimates may be subject to upward or downward adjustment, and actual production, revenue and expenditures with respect to our reserves likely will vary, possibly materially, from estimates.

Additionally, because some of our reserves estimates are calculated using volumetric analysis, those estimates are less reliable than the estimates based on a lengthy production history. Volumetric analysis involves estimating the volume of a reservoir based on the net feet of pay of the structure and an estimation of the area covered by the structure. In addition, realization or recognition of proved undeveloped reserves will depend on our development schedule and plans. A change in future development plans for proved undeveloped reserves could cause the discontinuation of the classification of these reserves as proved.

#### *Property acquisition risk*

Although we perform a review of properties that we acquire that we believe is consistent with industry practices, such reviews are inherently incomplete. It generally is not feasible to review in-depth every individual property involved in each acquisition. Ordinarily, we will focus our review efforts on the higher-value properties and will sample the remainder. However, even a detailed review of records and properties may not necessarily reveal existing or potential problems, nor will it permit us as a buyer to become sufficiently familiar with the properties to assess fully and accurately their deficiencies and potential. Inspections may not always be performed on every well, and environmental problems, such as groundwater contamination, are not necessarily observable even when an inspection is undertaken. Even when problems are identified, we often assume certain environmental and other risks and liabilities in connection with acquired properties. There are numerous uncertainties inherent in estimating quantities of proved oil and gas reserves and future production rates and costs with respect to acquired properties, and actual results may vary substantially from those assumed in the estimates. In addition, there can be no assurance that acquisitions will not have an adverse effect upon our operating results, particularly during the periods in which the operations of acquired businesses are being integrated into our ongoing operations.

#### *Weather and climate*

Demand for oil and gas are, to a degree, dependent on weather and climate, which impact the price we receive for the commodities we produce. In addition, our exploration and development activities and equipment can be adversely affected by severe weather, which may cause a loss of production from temporary cessation of activity or lost or damaged equipment. Our planning for normal climatic variation, insurance programs, and emergency recovery plans may inadequately mitigate the effects of such weather conditions, and not all such effects can be predicted, eliminated, or insured against.

#### *Environmental factors*

As an owner or lessee and operator of oil and gas properties, we are subject to various federal, state, local, and foreign country laws and regulations relating to discharge of materials into, and protection of, the environment. These laws and regulations may, among other things, impose liability on the lessee under an oil and gas lease for the cost of pollution clean-up and other remediation activities resulting from operations, subject the lessee to liability for pollution and other damages, limit or constrain operations in affected areas, and require suspension or cessation of operations in affected areas. Our efforts to limit our exposure to such liability and cost may prove inadequate and result in significant adverse effects to our results of operations. In addition, it is possible that the increasingly strict requirements imposed by environmental laws and enforcement policies could require us to make significant capital expenditures. Such capital expenditures could adversely impact our cash flows and our financial condition.

#### *Governmental risk*

Our US operations have been, and at times in the future may be, affected by political developments and by federal, state, and local laws and regulations such as restrictions on production, changes in taxes, royalties and other amounts payable to governments or governmental agencies, price or gathering rate controls, and environmental protection laws and regulations.

The U.S. federal and state income tax laws affecting oil and gas exploration, development, and extraction may be modified by administrative, legislative, or judicial interpretation at any time. Previous legislative proposals, if enacted into law, could make significant changes to such laws, including the elimination of certain key U.S. federal income tax incentives currently available to oil and gas exploration and production companies. These changes include, but are not limited to, (i) the repeal of the percentage depletion allowance for oil and gas properties, (ii) the elimination of current deductions for intangible drilling and development costs, and (iii) an extension of the amortization period for certain geological and geophysical expenditures. The passage or adoption of these changes, or similar changes, could eliminate or postpone certain tax deductions that are currently available with respect to oil and gas exploration and development. We are unable to predict whether any of these changes or other proposals will be enacted. Any such changes could adversely affect our business, financial condition, and results of operations.

#### *Market conditions*

The financial markets are subject to fluctuation and are vulnerable to unpredictable shocks. We have a significant development project inventory, which will require substantial future investment. We and/or our partners may need to seek financing in order to fund these or other future activities. Our future access to capital, as well as that of our partners and contractors, could be limited if the debt or equity markets are constrained. This could significantly delay development of our property interests.

#### *Liquidity and future financing risk*

The Company is in the early stages of business and has not generated revenue in excess of its expenses. The Company will likely operate at a loss until its business becomes established and the Company may require additional financing in order to fund future operations and expansion plans. The Company's ability to secure any required financing to sustain operations will depend in part upon prevailing capital market conditions and business success. There can be no assurance that the Company will be successful in its efforts to secure any additional financing or additional financing on terms satisfactory to management. If additional financing is raised by issuance of additional shares, control may change and shareholders may suffer dilution. If adequate funds are not available, or are not available on acceptable terms, the Company may be required to scale back its current business plan or cease operating.

#### *Going-Concern risk*

The Company's financial statements have been prepared on a going-concern basis under which an entity is considered to be able to realize its assets and satisfy its liabilities in the ordinary course of business. The Company's future operations are dependent upon the identification and successful completion of equity or debt financing and the achievement of profitable operations at an indeterminate time in the future. There can be no assurances that the Company will be successful in completing equity or debt financing or in achieving profitability. The financial statements do not give effect to any adjustments relating to the carrying values and classification of assets and liabilities that would be necessary should the Company be unable to continue as a going concern.

#### *Global Economy risk*

Economic slowdowns and volatility of global capital markets may from time to time make the raising of capital by equity or debt financing more difficult. The Company may be dependent upon capital markets to raise additional financing in the future while concurrently establishing a wider customer base. Access to financing may be negatively impacted by global economic downturns. As such, the Company is subject to liquidity risks in meeting its operating expenditure requirements and future development cost requirements in instances where adequate cash positions are unable to be maintained or appropriate financing is unavailable. These factors may impact the ability to raise equity or obtain loans and other credit facilities in the future and on terms favourable to the Company and its

management. If levels of volatility and slow market conditions persist, the Company's operations, the Company's ability to raise capital and the trading price of the Company's shares could be adversely impacted.

#### *Limited prior operating history*

The Company has limited operating history, business operations and assets. There is no assurance that it will be profitable or that its investment strategy will be successful. The Company's operations are subject to all of the risks inherent in the creation of new investment activity, including a limited prior operating history.

#### *Dilution*

Any sale of the Company's shares will result in dilution to existing holders of shares. The Company may issue additional shares without the consent from the shareholders of the Company.

#### *Loan facilities*

The interest expense and banking fees incurred in respect of any loan facility that may be secured by the Company may exceed the incremental capital gains and tax benefits generated by the incremental investment of the Company in any oil and gas properties. There can be no assurance that the borrowing strategy employed by the Company will enhance returns.

### **DISCLOSURE CONTROLS**

In connection with Exemption Orders issued by each of the securities commissions across Canada, the Chief Executive Officer and Chief Financial Officer of the Company will file a Venture Issuer Basic Certificate with respect to the financial information contained in the audited annual financial statements and respective accompanying Management's Discussion and Analysis.

In contrast to the certificates under National Instrument ("NI") 52-109 (Certification of disclosure in an Issuer's Annual and Interim Filings), the Venture Issuer Basic Certification does not include representations relating to the establishment and maintenance of disclosure controls and procedures and internal control over financial reporting as defined in NI 52-109.

### **APPROVAL**

The Board of Directors of Permex Petroleum Corporation has approved the contents of this management discussion and analysis on August 28, 2018.