
Management Discussion of Financial Results Q1 2017

White Owl Energy Services Inc. (“White Owl” or the “Company”) is a private company and therefore is not required to prepare and file Management Discussion and Analysis (“MD&A”) in accordance with National Instrument 51-102 – Continuous Disclosure Obligations, which requires public companies to prepare MD&A in accordance with Form 51-102F1 of National Instrument 51-102 or Items 303 of Regulation S-K or Regulation S-B under applicable United States securities laws. **Therefore, this discussion may not include all the information that might otherwise be required or expected thereunder. The following discussion of financial results does not constitute MD&A for the purposes of Canadian or United States securities laws or any other laws.** This discussion called the Management Discussion of Financial Results (“MDFR”) is being provided to help shareholders, lenders and other stakeholders meet their needs for additional information beyond what is provided in the financial statements and notes.

This MDFR is based on information available to June 12, 2017 and should be read in conjunction with White Owl’s unaudited condensed consolidated financial statements for the three months ended March 31, 2017 (“consolidated financial statements and audited consolidated financial statements for the year ended December 31, 2016. The financial statements and comparative information have been prepared in accordance with International Financial Reporting Standards (“IFRS”).

All amounts are in Canadian dollars unless otherwise noted.

CORPORATE OVERVIEW

White Owl is an oilfield service company involved in the collection, processing and disposal of oilfield waste in North Dakota. White Owl operates an expanding network of produced water and flow back disposal facilities providing services to some of the largest independent oil and gas operators on the continent. These strong customer relationships combined with new facilities opportunities, are allowing White Owl to handle an increasing volume of oilfield fluids for its North Dakota customers.

A description of the Company’s key business segments follows.

Produced Water and Waste Water Disposal

The Company provides produced water and “frac” water disposal services through a network of four operating Class 2 salt water disposal (“SWD”) wells and one suspended SWD well which is being re-permitted for Class 1 disposal. The Company also has seven new facility locations in North Dakota at varying stages of development and is contemplating expanding into other shale basins in the future. The operating Class 2 SWD wells and facilities are situated at Ross, New Town, Watford, and Tioga and the development locations in North Dakota are at Alexander (Class 1), Epping, Clarke’s Creek, Johnson’s Corner, Banks, Killdeer Hills, and Van Hook.

Oilfield Waste Processing

Liquid waste is generated as a result of drilling, completions and production-related activities. White Owl has planned to develop two oilfield treatment plants to process these streams, one at Johnson’s Corner (permitted) and one at Tioga (in permitting). These plants will separate fluids into three components: recoverable oil, waste water and residual solids. Recovered oil will be sold while separated solids will be processed and transported to third party landfills in North Dakota. It is the Company’s intention to eventually provide oilfield waste processing and disposal services across the entire Bakken development in North Dakota.

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Class 1 Non-Hazardous Waste Water Disposal

In the fall of 2017, the Company expects to receive a permit for the processing and disposal of Class 1 non-hazardous waste water at the Alexander location and to have the site commissioned. Class 1 fluids are regulated by the Department of Health in the State of North Dakota with oversight by the US Environmental Protection Agency. A variety of industries including midstream oil and gas, landfills and mines produce Class 1 non-hazardous waste water which must be disposed of at a Class 1 non-hazardous waste water facility. There are currently no commercial Class 1 non-hazardous waste water facilities in North Dakota.

Operational Philosophy

Within its markets, the Company differentiates itself by:

- Operating with the highest levels of responsible environmental, health and safety stewardship;
- Providing a high level of customer service including a focus on expedited truck unload times;
- Operation, design and construction of facilities that provide efficient and safe separation of fluids;
- Acquiring and integrating strategically-located SWD plants into its expanding network; and,
- Vertically integrating into complementary, value-add, and higher margin services.

OPERATIONAL AND FINANCIAL HIGHLIGHTS

A continuation of low activity levels, increased competition, low price levels, and weather conditions had a negative impact on all four of the Company's operating facilities during the first quarter of 2017, although White Owl was still able to attain a 31% operating margin. The quarter did see oil prices stabilizing above US\$50 per barrel and rig counts in North Dakota climbing to 50 rigs which stabilized the sector, but not enough to provide meaningful growth for the Company. White Owl continued to develop its inventory of organic projects and make facility expansions and improvements ensuring the Company will be well positioned when the sector turns around.

Financial and operating results

	Three months ended March 31,	
(\$000's except for volumes)	2017	2016
Volumes received (barrels)	2,775,655	2,555,898
Oilfield waste disposal services revenue	2,434	2,293
Operating expenses	(1,689)	(1,334)
Operating income⁽¹⁾	745	959
General and administrative	(463)	(357)
EBITDA ⁽¹⁾	282	602
Other income and expenses		
Depreciation and amortization	(349)	(344)
Finance (costs) income	(250)	(492)
Share-based payments	(87)	(78)
Foreign exchange (losses) gains	4	(31)
Gain on debt extension	-	269
Loss on disposal of assets	-	(44)
Net loss	(400)	(118)

⁽¹⁾ Refer to "Non-GAAP Measures" for additional information.

The operational and financial highlights for the first quarter of 2017 are as follows:

- Earnings before interest, taxes, depreciation and amortization ("EBITDA") in first quarter totaled \$282,000, a decrease of \$320,000 or 53% from the first quarter of 2016. The decrease in EBITDA has largely resulted from

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an increase in operational costs due to weather conditions that caused operational issues and five times the budgeted snow removal costs, scheduled pump maintenance, and accruing for annual tank clean outs that were not budgeted in prior years. Overall White Owl is seeing higher operating costs from facilities that were acquired due to their engineering design or lack thereof. First quarter 2017 general and administrative (“G&A”) expense was higher year over year mostly due to higher business development costs on new projects.

- First quarter revenues were up 6% year over year with volumes up 9%, oil sales relatively unchanged, and overall operating margin was 31%.

Revenue and operating income by facility

(\$000's)	Three months ended March 31,	
	2017	2016
Oilfield waste disposal services revenue		
New Town	1,008	983
Watford	860	809
Ross	284	428
Alexander	-	73
Tioga JV	282	-
	2,434	2,293
Operating income ⁽¹⁾		
New Town	270	444
Watford	315	386
Ross	18	163
Alexander	(9)	(34)
Tioga JV	151	-
	745	959

⁽¹⁾ Refer to “Non-GAAP Measures” for additional information.

Operating income for the three months ended March 31, 2017 at the New Town facility was 39% lower than the same period the prior year due to weather conditions causing high maintenance costs, two-year scheduled pump maintenance costs, and annual tank clean out costs now being accrued at \$16,500 per month. The decrease in operating income was partially offset by a 7% increase in oil sales over the same periods. Disposal volumes were relatively unchanged for Q1 2017 year over year. Revenues, operating income, disposal volumes, and oil sales were all relatively unchanged from the fourth quarter of 2016.

Operating income for the three months ended March 31, 2017 at the Watford facility was 18% lower than the prior year for the same period due to weather conditions, maintenance costs, two-year scheduled pump maintenance costs, and annual tank clean out costs now being accrued at \$13,200 per month. A one-time cost of \$26,500 was incurred over the period to remove solar panels for the tank sensors and replace with standard electrical operation. The decrease in operating income was partially offset by a 22% increase in disposal volumes. Revenues, operating income, disposal volumes, and oil sales were all relatively unchanged from the fourth quarter of 2016.

Operating income for the three months ended March 31, 2017 at the Ross facility was 89% lower than the prior year for the same period due to weather conditions causing higher maintenance costs, general site repairs and annual tank clean out costs now being accrued at \$6,600 per month. Maintenance costs of \$25,250 were incurred over the period; \$8,200 for site lease maintenance, \$12,950 for general equipment maintenance, and \$4,100 to replace the interface panel for the truck unload system. The 90% decrease in operating income for the first quarter of 2017 compared to 2016 was equally impacted by decreased revenues, volumes and oil sales. The Ross facility remains in an area where there is not much drilling and completions activity. Revenues, operating income, disposal volumes, and oil sales were all relatively unchanged from the fourth quarter of 2016.

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Operations at the Alexander facility continue to be suspended. Alexander continues to incur costs of approximately \$9,000 per month for insurance, taxes, and royalty obligations. The facility is now actively being re-permitted for Class 1 disposal at a cost of approximately \$100,000 with approval expected in the fourth quarter of 2017. Total cost to reopen the facility for Class 1 is approximately \$600,000.

Operating income for the three months ended March 31, 2017 at the Tioga facility for White Owl's 32% interest was \$151,371 which consists of \$138,431 of operating income from the facility and \$12,940 of overhead income to the Company as compensation for its role as operator in the Tioga Joint Venture. Revenues, operating income, disposal volumes, and oil sales were all relatively unchanged from the fourth quarter of 2016.

G&A expenses

(\$000's)	Three months ended March 31,	
	2017	2016
Salaries and management	240	232
Professional fees	65	37
Travel and related expenses	41	42
General office expenses	49	38
Third party consulting fees	68	8
	463	357

G&A expenses in the three months ended March 31, 2017 were higher than the comparable period in the prior year due to higher third-party consulting fees related to business development on new projects.

Depreciation and amortization

Depreciation and amortization for the three months ended March 31, 2017 was \$349,000 compared to \$344,000 for the same period in 2016.

Finance costs

(\$000's)	Three months ended December 31,	
	2017	2016
Interest on term loan	228	235
Interest on long-term debt	3	26
Cost of share repurchase obligation settlement	-	139
Accretion of long-term debt	-	31
Accretion of share repurchase obligations	-	55
Accretion of asset retirement obligations	8	6
Interest, bank charges and other	11	-
	250	492

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Foreign exchange losses (gains)

The Company recorded foreign exchange gains of \$4,000 during the three months ended March 31, 2017 compared to foreign exchange losses of \$31,000 for the same period in 2016. The gains and losses primarily relate to the impact of changes in exchange rates on US dollar cash balances and short-term intercompany loans. The average exchange rate for the three months ended March 31, 2017 was 1.32 USD/CDN compared to 1.37 USD/CDN during the same period in 2016.

Share-based payments

During the three months ended March 31, 2017, the Company recorded share-based payments of \$87,000 compared to \$78,000 for the same period in 2016. Share-based payments relate to the cost of stock options issued to management, employees and directors of the Company.

SUMMARY OF QUARTERLY RESULTS

	2017	2016				2015		
(\$000's)	Q1	Q4	Q3	Q2	Q1	Q4	Q3	Q2
Revenue	2,434	2,594	2,436	2,693	2,293	2,815	2,859	2,651
EBITDA	282	210	683	947	602	898	565	703
Net Income (loss)	(400)	(867)	620	306	(118)	(10,937)	(199)	(169)

⁽¹⁾ Refer to “Non-GAAP Measures” for additional information.

EBITDA in the first quarter of 2017 was lower than the first quarter of 2016. This decrease in EBITDA was largely due to significant increases in operating costs that were due to weather conditions and scheduled bi-annual pump maintenance.

LIQUIDITY AND CAPITAL RESOURCES

Liquidity risk is the risk that the Company will not be able to meet financial obligations at the point at which they are due. The Company manages its liquidity risk through cash and debt management combined with equity financing when available. Management’s assessment of the Company’s liquidity reflects estimates, assumptions and judgments relating to current market conditions. The Company has funded its operations, acquisitions and capital program with a combination of equity, bank debt and vendor take-back notes. To manage its liquidity and capital resources, the Company ensures that adequate sources of capital are available to fund capital investments, while ensuring that sufficient operating cash flow is available to sustain and grow the operating business.

As at March 31, 2017, the Company had negative working capital of \$11,988,000 an accumulated deficit of \$13,382,000 and a net loss for the three months ended March 31, 2017 of \$400,000. These factors indicate the existence of material uncertainties which may cast significant doubt about the Company’s ability to continue as a going concern. The ability of the Company to continue as a going concern and realize the carrying value of its assets and discharge its liabilities when due is dependent on achieving future profitable operations. There is no certainty that the Company will achieve profitable operations in the future due to factors such as commodity prices, industry activity levels in the regions in which the Company operates, changes by competitors, successfully raising capital for acquisition and development opportunities and successful implementation of the Company’s business plan. The consolidated financial statements do not include any adjustments to the amounts and classifications of assets and liabilities, and reported revenues and expenses, that might be necessary should the Company be unable to continue as a going concern, and therefore, be required to realize its assets and discharge its liabilities other than in the normal course of business and at carrying amounts different from those reflected in the accompanying consolidated financial statements. Any such adjustments could be material.

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Cash provided by operations

	Three months ended March 31,	
(\$000's)	2017	2016
Cash provided by operating activities	94	725
Change in non-cash working capital	(54)	(524)
Cash provided by operations	40	201

Cash provided by operating activities before changes in working capital in the first quarter of 2017 was lower than the same period in the prior year due to higher operating costs at all facilities. These costs were mostly non-recurring annual maintenance items and an annual accrual of tank cleaning costs.

Investing activities

	Three months ended March 31,	
(\$000's)	2017	2016
Capital expenditures	742	1,374

The following major capital projects were completed during the three months ended March 31, 2017:

- At New Town, customer demand required an upgrade to the transformer at a cost of approximately \$121,900, and costs of approximately \$22,300 were required to upgrade the offload pad.
- \$500,000 was deposited towards the first payment on the Clairmont acquisition. At March 31, 2017, this amount is recorded in the consolidated financial statements under deposits and prepaid expenses.
- At Killdeer, downhole work and abandonment costs were approximately \$337,270.
- A pressure washer was acquired to be used at all facilities at a cost of approximately \$17,400

Financing activities

Share Capital

(000's)	Common shares	Preferred shares	Total
Balance, December 31, 2016	40,633	26,469	67,102
Shares issued	286	-	286
Balance, March 31, 2017	40,919	26,469	67,388

At March 31, 2017, there were 4,000,000 (December 31, 2016 – 4,000,000) common shares held in escrow.

In January 2017, the Company issued 285,714 common shares at \$0.35 per common share for total proceeds of \$100,000.

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Share Options

There were 4,069,000 share options outstanding as of March 31, 2017, with a weighted average exercise price of \$0.43 per share.

Term Loan and Operating Loan

The term loan is a non-revolving, reducing demand facility at an annual interest rate of US prime plus 1.75%. Principal payments of \$133,880 (US\$100,000) were made during the three months ended March 31, 2017 (2016 - \$117,444 (US\$82,573)). The Company is required to make monthly interest payments as well as total principal payments of US\$100,000 each quarter until June 30, 2017. The Company is required to make two additional payments of principal and interest if the debt service coverage ratio is greater than 1.5 to 1 as calculated on March 31, 2017 and June 30, 2017. These additional payments would be equal to the Company's excess earnings before interest, depreciation, taxes and amortization for the three months ended March 31, 2017 and June 30, 2017, respectively. At March 31, 2017, the Company's debt service ratio is less than 1.5 to 1 and no additional payment will be required. The remaining balance at June 30, 2017 will be repaid over a seven-and-a-half-year amortization period. Blended monthly principal and interest payments of approximately US\$156,575 will start on July 31, 2017 if the US prime rate remains unchanged from current rates. The loan is subject to annual review with the next review scheduled for June 2017.

The Company also has an operating line of US\$1,000,000 which remains substantially undrawn except for outstanding letters of credit of \$53,862, and \$18,340 for credit cards. There are no other amounts drawn on the operating line at March 31, 2017 (December 31, 2016 – nil).

Under the loan agreement for the term and operating loans, the Company is required to maintain a minimum Debt Service Coverage Ratio of 1.25 to 1. The Debt Service Coverage Ratio is calculated as follows:

$$\text{Debt Service Coverage Ratio} = \frac{\text{Earnings before interest, depreciation, taxes and amortization}}{\text{Debt service obligations}}$$

The Debt Service Coverage Ratio at March 31, 2017 was 1.35 (December 31, 2016 – 1.55). The ratio is calculated based on the trailing four quarters at March 31, 2017.

OUTLOOK

During the first quarter of the year, we experienced an improvement in market conditions with oil averaging around US\$50 per barrel and the rig count exceeding 50 rigs for most of the quarter. However, this improvement in market conditions did not translate into improved operating performance due to the effect of poor weather and the resulting higher operating costs. The winter in North Dakota was one of the coldest and windiest experienced over the past few years and had an adverse impact on the operations of most producers and service companies. During April and May, however, we have seen a significant improvement in operating performance with monthly volumes closer to the historical averages and we are starting to see the anticipated increase in flow back and production water volumes.

In Western Canada, the focus of producers and service companies is on the Montney play in northwest Alberta and northeast B.C. Producers are regaining confidence in the sector and are allocating capital to drill and complete long horizontal Montney wells. During the first quarter of 2017, White Owl was presented with an opportunity to acquire an oil pipeline-connected processing and disposal facility in the Sexsmith area and in March signed a Letter of Intent to acquire an oil processing, blending and water disposal facility from an area producer. The acquisition is anticipated to close in June. This is a significant development for White Owl which creates an opportunity to generate a new revenue and cash flow stream from a new market. The Company is executing an agreement with a large international crude oil marketer to deliver crude oil blending and treating volumes to the facility and to provide capital for plant expansions.

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NON-GAAP MEASURES

Operating income and EBITDA are not recognized measures under IFRS. Management believes that operating income is a useful measure of financial performance, cost control and operating efficiency. Management believes that in addition to net income, EBITDA is a useful supplemental measure of financial performance as it provides an indication of results generated by the Company's principal business activities prior to consideration of non-cash charges. Operating income and EBITDA are commonly accepted measures in the industry which is useful for knowledgeable investors for comparison purposes. Operating income is calculated as revenue from oilfield waste disposal services less operating expenses. EBITDA is calculated as operating income less G&A expenses. White Owl's determination of operating income and EBITDA may not be comparable to that reported by other companies.

FORWARD-LOOKING INFORMATION

This discussion contains forward-looking information, which is disclosure regarding possible events, conditions or financial performance that is based on assumptions about future courses of action and economic conditions. Such forward-looking information may be identified by words such as "anticipate", "will", "intend", "could", "should", "may", "might", "expect", "forecast", "plan", "potential", "project", "assume", "contemplate", "believe", "budget", "shall", "continue", "milestone", "target", "vision", and similar terms or the negative thereof or other comparable terminology.

The forward-looking information in this discussion is subject to significant risks and uncertainties and is based on a number of material factors and assumptions which may prove to be incorrect, including, but not limited to, the following: corporate strategy; general market conditions; the oil and natural gas industry; activity levels in the oil and gas sector, including market fundamentals, drilling levels, commodity prices for oil and natural gas; demand for the Company's services; operational performance; expansion strategy; debt service; capital expenditures; completion of facilities; the impact of new facilities on the Company's financial and operational performance; future capital needs; and access to capital through equity market and debt markets.

The forward-looking information relies on material assumptions and known and unknown risks and uncertainties, certainty of which are beyond the Company's control. Such risks and uncertainties include, without limitation, the impact of general economic conditions in the United States, Canada and globally; industry conditions; the Company's ability to increase its market share; volatility of commodity prices; delays resulting from an inability to obtain regulatory approvals; an inability to access sufficient capital from internal and external sources; changes in laws and regulations and changes in how they are interpreted and enforced; environmental risks; increased competition; and the lack of qualified personnel or management. Readers are cautioned that the foregoing list of factors and risks are not exhaustive. The Company's actual results, performance or achievements could differ materially from those expressed in, or implied by, the forward-looking information and, accordingly, no assurances can be given that any of the events anticipated by the Forward-Looking Statements will transpire or occur. Although the Company has attempted to identify important risks and factors that could cause actual actions, events or results to differ materially from those described, there may be other factors and risks that cause actions, events or results not anticipated, estimated or intended. Accordingly, readers should not place any undue reliance on the forward-looking information, as such information may not be appropriate for other purposes.

website at www.whiteowl-services.com