valeura energy inc.

# MANAGEMENT'S DISCUSSION AND ANALYSIS

For the three and six months ended June 30, 2018 and 2017

(tabular amounts in thousands of Canadian Dollars, except share, per share or per unit amounts)

The following Management's Discussion and Analysis ("MD&A") as provided by the management of Valeura Energy Inc. ("Valeura" or the "Company") is dated as of August 8, 2018 and should be read in conjunction with Valeura's unaudited condensed interim consolidated financial statements and related notes for the three and six month periods ended June 30, 2018 and 2017. Additional information relating to Valeura is available under Valeura's profile on www.sedar.com, including Valeura's Annual Information Form for the year ended December 31, 2017 ("2017 AIF"). The reporting currency is the Canadian Dollar (see the sections titled "Foreign Exchange" and "Currency Translation Adjustment" for discussion on Valeura's functional currencies).

**Basis of Presentation**

These unaudited condensed interim consolidated financial statements have been prepared in accordance with IAS 34 – Interim Financial Reporting of the International Financial Reporting Standards ("IFRS"). The unaudited condensed interim consolidated financial statements have been prepared in accordance with IFRS accounting policies and methods of computation as set forth in Valeura's 2017 audited consolidated financial statements, with the exception of certain disclosures that are normally required to be included in annual consolidated financial statements, which have been condensed or omitted in the interim statements. The unaudited condensed interim consolidated financial statements should be read in conjunction with Valeura's audited consolidated financial statements and MD&A for the year ended December 31, 2017.

The discussion and analysis of oil and natural gas production is presented on a working-interest, before royalty basis. For the purpose of calculating unit of production information, natural gas is converted to a barrel of oil equivalent ("boe") using six thousand cubic feet of natural gas equal to one barrel of oil. This conversion ratio of 6:1 is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. Readers are cautioned that boe as a unit of measure may be misleading, particularly if used in isolation.

The Company makes estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the revenues and expenses during the reporting period. Management reviews these estimates, including those related to accruals, reserves, environmental and decommissioning obligations and income taxes at each financial reporting period. Changes in facts and circumstances may result in revised estimates and actual results may differ from these estimates. Readers should be aware that historical results are not necessarily indicative of future performance.

valeura energy inc.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

For the three and six months ended June 30, 2018 and 2017

(tabular amounts in thousands of Canadian Dollars, except share, per share or per unit amounts)

## Highlights and Selected Financial Information

| | Three months ended | | Six months ended | |
|---|---|---|---|---|
| | **June 30, 2018** | June 30, 2017 | **June 30, 2018** | June 30, 2017 |
| **Financial** | | | | |
| Petroleum and natural gas sales | **$ 2,949** | $ 3,764 | **$ 6,418** | $ 6,852 |
| Net loss | **(1,404)** | (526) | **(3,839)** | (2,527) |
| Per share, basic and diluted | **(0.02)** | (0.01) | **(0.05)** | (0.04) |
| Adjusted funds flow (used) [1] | **461** | 959 | **1,006** | (1,924) |
| Per share, basic and diluted | **$ 0.01** | $ 0.01 | **$ 0.01** | $ (0.03) |
| **Production volumes** | | | | |
| Natural gas (Mcf/d) | **4,360** | 5,550 | **4,711** | 5,189 |
| Crude oil (bbl/d) | **9** | 9 | **12** | 6 |
| Total (boe/d) | **736** | 934 | **797** | 871 |
| **Sales prices** | | | | |
| Natural gas (per Mcf) | **$ 7.24** | $ 7.34 | **$ 7.31** | $ 7.21 |
| Crude oil (per bbl) | **95.77** | 68.39 | **87.59** | 69.64 |
| Total (per boe) | **44.06** | 44.28 | **44.50** | 43.46 |
| Exploration and development capital | **1,128** | 4,011 | **2,002** | 5,943 |
| Acquisitions | **-** | - | **-** | 21,450 |
| Dispositions | **-** | (3,973) | **-** | (26,288) |
| Working capital [2] | | | **60,296** | 8,618 |
| Cash | | | **$ 55,945** | $ 9,903 |
| Weighted average shares outstanding | | | | |
| Basic and diluted (thousands) [3] | **85,608** | 73,148 | **81,681** | 68,703 |

### Outstanding Share Data

| | **June 30, 2018** |
|---|---|
| Common shares | 86,136,988 |
| Stock options | 4,846,332 |
| Fully Diluted | 90,983,320 |

[1] Non-GAAP measure – see note regarding non-GAAP measures on page 18.

[2] Working capital is current assets less current liabilities.

[3] The weighted average number of common shares outstanding is not increased for outstanding stock options when the effect is anti-dilutive.

## The Company

Valeura is a Canada-based public company currently engaged in the exploration, development and production of oil and natural gas in the Thrace Basin of northwest Turkey. Valeura's shares are traded on the Toronto Stock Exchange ("TSX") under the trading symbol "VLE".

Valeura was established in 2010 to grow internationally through opportunistic acquisitions of producing assets with exploitation and exploration upside in selected countries in regions of interest, which included the Mediterranean Basin. The Company completed its first international transaction in Turkey during 2010 and since that time has executed a number of other transactions and won several new exploration licence awards in the country.

The asset and financing deals completed by the Company between Q4 2016 and Q1 2018 have transformed the Company by increasing the size of the asset base, giving Valeura operatorship of all key assets, and providing the financial capacity to explore and appraise the unconventional basin-centered gas accumulation ("BCGA") play. Additionally, the Company has secured Equinor (name changed from Statoil in May 2018) as a large, well-respected partner which provides further technical and financial capacity to explore and appraise the deep, unconventional potential of the lands.

As at June 30, 2018, the Company held an interest in 20 exploration licences and production leases in the Thrace Basin of Turkey comprising approximately 0.46 million gross acres (0.37 million net acres of shallow rights and 0.26 million net acres of deep rights). The Thrace Basin assets include an 81.5% working interest in the shallow rights and deep rights of 11 production leases referred to as the ("**South Thrace Lands**")**,** and an 81.5% (shallow rights) working interest, 31.5% (deep rights) working interest in 3 production leases and 1 exploration license, referred to as the ("**West Thrace Lands**") (together the "**TBNG JV**"), and a 100% (shallow rights) and a 50% (deep rights) working interest in the two Banarli exploration licenses (the "**Banarli Licences**"). On June 12, 2018 one exploration license on the West Thrace Lands was officially relinquished.

The Thrace Basin lands have shallow gas production and further development and exploration potential from both conventional reservoirs and tight gas reservoirs. All or some of the Banarli Licenses, West Thrace Lands and South Thrace Lands are also believed to have potential for an unconventional BCGA play in over-pressured formations below approximately 2,500m. Valeura has recently drilled, completed and flow-tested the Yamalik-1 gas-condensate discovery on the Banarli Licenses. This well successfully proved the BCGA thesis concept at this location.

The Company is focussed on growing its established business in Turkey, particularly its natural gas operations in the Thrace Basin which yields very high natural gas prices relative to North America. As a result of the success of the Yamalik-1 gas-condensate discovery, the primary focus of Valeura's business has transitioned to the delineation and commercial demonstration of the multi-TCF BCGA play. However, the Company still continues to optimize the established conventional shallow gas assets in the Thrace Basin.

## Operations

### Production Operations

The Company generates cash flow from sales of petroleum and natural gas production from its assets in the Thrace Basin of Turkey. Natural gas is currently produced from approximately 91 wells (gross). The gas, which is composed primarily of methane, is gathered, dehydrated and compressed in Company-operated facilities and distributed on a Company-operated sales line network directly to 55 light industry customers. Valeura is the operator of all of its production operations.

In Q2 2018 the Company drilled the Karanfiltepe-7 exploration well, which was a commitment well in its West Thrace Lands. The well was a gas discovery which was completed and brought on production in July. Additionally, in the quarter Valeura carried out a number of workover activities on the existing wells and commenced preparation for some abandonment and reclamation activities on a number of older well sites which are no longer producing.

**BCGA Play**

Valeura completed a number of transactions in 2016 and 2017 including the Banarli Farm-in, under which Equinor was given the option to acquire a 50% interest in the deep formations on the West Thrace Lands and the Banarli Licenses. The Equinor investment comprised a purchase cost of US$21 million, back costs of US$6 million and a work program carry of Valeura on two deep wells and new 3D seismic. The minimum gross cost of the work program carry was US$30 million.

The first well, Yamalik-1, has been drilled and tested and the 3D seismic data has been acquired and processed. Equinor will complete their earning obligation by drilling and testing the Inanli-1 well which is expected to spud around the end of Q3 2018. On completing the drilling and testing of Inanli-1, it is expected that Statoil's expenditures for their 50% working interest will be approximately US$100 million.

Valeura is operator of the deep exploration program in both Banarli and the West Thrace Lands during the earning phase of the Banarli Farm-in. Once Equinor has fully earned its 50% interest in Banarli, Equinor has the option to request operatorship of the deep program.

In Q2 2018 Valeura progressed planning, procurement and permitting for the BCGA appraisal program which will include further production testing and the tie-in of Yamalik-1 and the drilling and testing of three deep appraisal wells.

All of the planning and approvals were completed for further testing on Yamalik-1. Testing equipment was also mobilized from the US which will be available for Yamalik-1 and the three appraisal wells. A pipeline was built from the Yamalik-1 site to Valeura's existing gas gathering infrastructure. Testing and tie-in operations are expected in Q3 2018.

In preparation for the appraisal drilling program, Valeura focussed on work planning, well design, and procuring materials and services required for the campaign. During the second quarter of 2018, Valeura received the required government permits for nine potential well sites. The permits obtained include the site of the first well, Inanli-1, 6km to the NE of Yamalik-1 and the second well, Devepinar-1, which will be located in the West Thrace Lands.

## Political and Regulatory Environment

In late June Turkey held elections for the President and the parliament. The election was conducted without civil unrest, and the incumbent president was re-elected. The government is also moving ahead with constitutional changes supported by a referendum in 2017. While Turkey went through a period of political uncertainty in 2016 and 2017, it is expected that the 2018 election results will lead to increased stability going forward. Valeura's ability to conduct drilling and production operations in the Thrace Basin has never been adversely affected by political unrest in the country, and the Company has not encountered any unusual delays or security issues in its Thrace basin operations. The Company continues to maintain a professional working relationship with local authorities and regulators.

While there has been a continued devaluation on the Turkish Lira ("TL"), the government has continued to adjust the reference natural gas sales price to offset these currency effects.

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Management acknowledges that its ability to make reliable estimates can be complicated by political, economic and security situation events as and when they occur. Management has based its estimates with respect to the Company's operations on information available up to the date of this MD&A.

## Outlook

Valeura is fully focused on appraising and de-risking its BCGA discovered by the Yamalik-1 well. The objective of the 2018 and 2019 work program is to demonstrate that over-pressured gas is pervasive across Valeura's Thrace Basin lands and to show that commercial flow rates can be achieved. The key activities to support this objective are the tie-in and long-term testing of the Yamalik-1 well and a three well appraisal program.

The Company has sourced production test equipment appropriate for the flow back of the Yamalik-1 well post fracing. All required equipment has now arrived on the Yamalik-1 well site and operations have commenced. Assuming a successful test, the well will be immediately completed and tied in to Valeura's gas infrastructure, with production sold to Valeura's existing customers. The pipeline was completed and commissioned in advance of testing operations, so as to eliminate the need for gas flaring during the long-term test.

Inanli-1 is the first well in the appraisal drilling program and is planned to be drilled to a depth of 5,000m. The well location is 6 km northeast of Yamalik-1 and has been selected to target an area of the play interpreted to have more natural fracturing of the reservoir than Yamalik-1. All government permits have been received for the well location and construction of the well pad has commenced. KCA Deutag will provide a 2,000hp drilling rig for the three-well campaign and it is currently being mobilized to Turkey with expected arrival at the end of August. Other key long-lead items have been procured, with all equipment and services planned to be available for a spud of the well around the end of Q3 2018. Valeura is planning an extensive data acquisition program for the well, including more than 300m of core. The well is expected to take approximately 80 days to drill and case for testing. Results of the well are expected in the second half of Q4 2018. With success, Inanli-1 will be fraced and flow tested in Q1 2019. Equinor will fund the drilling and testing of Inanli-1 which will fulfill their earning obligations under the Banarli farm-in agreement.

Valeura and its partners have selected Devepinar-1 as the second well in the appraisal campaign. This well will be drilled approximately 18km west of Yamalik-1. The location was selected as a significant step out from the Yamalik and Inanli sites to prove that the BCGA play is pervasive across to the west margin of the basin. Government permits have been received for the well location. Seven additional well locations have been approved by the government as potential sites for the third well.

In the shallow, conventional gas production play, subsequent to the end of Q2, the Company completed the tie-in of the Karanfiltepe-7 well which was a gas discovery. The Company is also continuing with its plan of selective low-cost workovers throughout the conventional play, to slow the natural decline from the existing fields.

In all its activities, the Company remains committed to continuing its safe operations and ensuring that operational and administrative functions are conducted in the most cost-efficient way.

(tabular amounts in thousands of Canadian Dollars, except share, per share or per unit amounts)

## Results of Operations

| | Three months ended | | Six months ended | |
|---|---|---|---|---|
| | **June 30, 2018** | June 30, 2017 | **June 30, 2018** | June 30, 2017 |
| Petroleum and natural gas sales | **$ 2,949** | $ 3,764 | **$ 6,418** | $ 6,852 |
| Royalties | **(396)** | (527) | **(856)** | (926) |
| Production costs | **(1,045)** | (1,334) | **(2,094)** | (1,943) |
| Operating netback[4] | **1,508** | 1,903 | **3,468** | 3,983 |
| Other income | **496** | 376 | **861** | 711 |
| General and administrative expenses | **(1,406)** | (1,340) | **(2,741)** | (2,996) |
| Transaction costs | **-** | (48) | **(287)** | (966) |
| Realized foreign exchange loss | **(22)** | (187) | **(97)** | (1,791) |
| Current tax recovery (expense) | **(115)** | 255 | **(198)** | (865) |
| Adjusted funds flow (used)[5] | **461** | 959 | **1,006** | (1,924) |
| **Non-cash expenses** | | | | |
| Share-based compensation | **(374)** | (96) | **(550)** | (192) |
| Accretion on decommissioning liabilities | **(404)** | (523) | **(925)** | (805) |
| Unrealized foreign exchange gain (loss) | **287** | (79) | **147** | 571 |
| Depletion and depreciation | **(1,843)** | (2,265) | **(3,866)** | (4,163) |
| Deferred tax recovery | **469** | 1,478 | **349** | 3,986 |
| Net loss | **$ (1,404)** | $ (526) | **$ (3,839)** | $ (2,527) |

**Sales Volumes**

| | Three months ended | | Six months ended | |
|---|---|---|---|---|
| | **June 30, 2018** | June 30, 2017 | **June 30, 2018** | June 30, 2017 |
| Natural gas (Mcf/d) | **4,360** | 5,550 | **4,711** | 5,189 |
| Crude oil (bbl/d) | **9** | 9 | **12** | 6 |
| Total (boe/d) | **736** | 934 | **797** | 871 |

Sales volumes for the three and six months ended June 30, 2018 were 736 boe/d and 797 boe/d, respectively, compared to 934 boe/d and 871 boe/d for the same periods in 2017. Sales volumes decreased due to natural declines causing lower gross production on both the TBNG JV and Banarli Licences.

[4] Non-GAAP measure – see note regarding non-GAAP measures on page 18.
[5] Non-GAAP measure– see note regarding non-GAAP measures on page 18.

(tabular amounts in thousands of Canadian Dollars, except share, per share or per unit amounts)

**Pricing Information**

| | Three months ended | | Six months ended | |
|---|---|---|---|---|
| Average reference prices | **June 30, 2018** | June 30, 2017 | **June 30, 2018** | June 30, 2017 |
| Natural gas – BOTAS (per Mcf)[6] | **TL 24.73** | TL 19.84 | **TL 23.64** | TL 19.84 |
| Natural gas – BOTAS (per Mcf) | **$ 7.33** | $ 7.47 | **$ 7.48** | $ 7.29 |
| Average exchange rate (TL/CAD) | **3.376** | 2.655 | **3.161** | 2.720 |

| | Three months ended | | Six months ended | |
|---|---|---|---|---|
| Average realized prices | **June 30, 2018** | June 30, 2017 | **June 30, 2018** | June 30, 2017 |
| Natural gas (per Mcf) | **$ 7.24** | $ 7.34 | **$ 7.31** | $ 7.21 |
| Crude oil (per bbl) | **$ 95.77** | $ 68.39 | **$ 87.59** | $ 69.64 |

Natural gas prices under sales contracts for all production in the Thrace Basin are linked to the BOTAS benchmark price in TL. Tracking of the BOTAS price, converted to US$, suggests that the price trends similar to the EU natural gas price. This is not unexpected, as the gas sources are similar for both BOTAS and the EU. Natural gas prices remain relatively strong in Turkey compared to North America, despite the recent volatility and overall decrease in the value of the TL.

Natural gas sales from the TBNG JV lands are under direct sales contracts to industrial buyers and power generation companies in the area and each contract is at a negotiated discount to the BOTAS benchmark price. Natural gas from Banarli is being sold to the TBNG JV, net of a transportation and marketing fee. Valeura receives the majority of the benefits from this fee arrangement and the associated proceeds by virtue of its current 81.5% working interest in the TBNG JV facilities.

Effective January 1, 2018 and April 1, 2018, the BOTAS reference price was increased by 14% and 10% respectively. The Company's Q2 2018 average realized natural gas price in Turkey was $7.24 per Mcf which is consistent with Q2 2017 due primarily to the increases in the BOTAS benchmark in 2018 which was offset by the devaluation of the TL against the Canadian Dollar. The average realized natural gas price in Turkey for Q2 2018 of $7.24 per Mcf represents a 1.0% discount to the BOTAS benchmark price.

On August 1, 2018 the government announced a further increase in the BOTAS reference price. The price was increased 49.5% for power generation companies and 14.0% for Valeura's other industrial clients. This increase offsets recent loses in the TL currency value. While Valeura has recently been selling approximately a quarter of its gas for power generation, this split is not guaranteed going forward.

**Petroleum and Natural Gas Sales Revenues**

| | Three months ended | | Six months ended | |
|---|---|---|---|---|
| | **June 30, 2018** | June 30, 2017 | **June 30, 2018** | June 30, 2017 |
| Natural gas | **$ 2,872** | $ 3,710 | **$ 6,232** | $ 6,775 |
| Crude oil | **77** | 54 | **186** | 77 |
| Total revenues | **$ 2,949** | $ 3,764 | **$ 6,418** | $ 6,852 |

The composition of petroleum and natural gas sales revenues for the three and six months ended June 30, 2018 was approximately 97 percent natural gas and three percent crude oil. Revenues for the three and six months ended June 30, 2018 decreased in comparison to the same periods in 2017 due primarily to lower production volumes.

[6] BOTAS owns and operates the national crude oil and natural gas pipeline grids in Turkey and purchases the majority of Turkey's natural gas imports. BOTAS regularly posts prices and its Level-2 Wholesale Tariff benchmark is shown herein as a reference price. See the 2017 AIF for further discussion.

(tabular amounts in thousands of Canadian Dollars, except share, per share or per unit amounts)

**Royalties**

| | Three months ended | | Six months ended | |
|---|---|---|---|---|
| | **June 30, 2018** | June 30, 2017 | **June 30, 2018** | June 30, 2017 |
| Royalties | **$ 396** | $ 527 | **$ 856** | $ 926 |
| Percentage of revenue | **13.4%** | 14.0% | **13.3%** | 13.5% |

Royalties for the three and six months ended June 30, 2018 decreased in comparison to the same periods in 2017 as a result of lower petroleum and natural gas sales revenues. Revenues are subject to a 12.5% government royalty and an overriding royalty only on the TBNG JV lands of one percent.

**Production Costs**

| | Three months ended | | Six months ended | |
|---|---|---|---|---|
| | **June 30, 2018** | June 30, 2017 | **June 30, 2018** | June 30, 2017 |
| Production costs | **$ 1,045** | $ 1,334 | **$ 2,094** | $ 1,943 |
| $ per boe | **15.62** | 15.70 | **14.52** | 12.32 |

Production costs for Q2 2018 decreased in comparison to the same period in 2017 due primarily to higher costs in 2017 associated with integrating the TBNG Acquisition. Unit production costs remained consistent which is reflective of the level of fixed costs included in total operating costs and lower gross production from the TBNG JV and Banarli Licenses. Production costs for the six months ended June 30, 2018 increased in comparison to the same period in 2017 due primarily to Valeura increasing its ownership of the TBNG JV from 40% to 81.5% commencing in February 2017. The higher unit production costs are reflective of the level of fixed costs included in total operating costs and lower gross production from the TBNG JV and Banarli Licenses.

**Operating Netbacks (per boe)**

| | Three months ended | | Six months ended | |
|---|---|---|---|---|
| | **June 30, 2018** | June 30, 2017 | **June 30, 2018** | June 30, 2017 |
| Petroleum and natural gas sales | **$ 44.06** | $ 44.28 | **$ 44.50** | $ 43.46 |
| Royalties | **(5.91)** | (6.20) | **(5.93)** | (5.88) |
| Production costs | **(15.62)** | (15.70) | **(14.52)** | (12.32) |
| Operating netback | **$ 22.53** | $ 22.38 | **$ 24.05** | $ 25.26 |

Operating netbacks in Q2 2018 are consistent with 2017. The decrease in the realized price, due primarily to the devaluation of the TL, was offset by lower production costs. Operating netbacks for the six months ended June 30, 2018 decreased in comparison to the same period in 2017 due primarily to higher per unit productions costs offset by higher realized prices.

**General and Administrative Expenses**

| | Three months ended | | Six months ended | |
|---|---|---|---|---|
| | **June 30, 2018** | June 30, 2017 | **June 30, 2018** | June 30, 2017 |
| General and administrative expenses | **$ 1,991** | $ 1,850 | **$ 4,303** | $ 3,635 |
| Business development | **-** | 11 | **-** | 23 |
| Total | **1,991** | 1,861 | **4,303** | 3,658 |
| Recoveries | **(585)** | (521) | **(1,562)** | (662) |
| Total general and administrative expenses | **$ 1,406** | $ 1,340 | **$ 2,741** | $ 2,996 |

Total general and administrative expenses before recoveries for 2018 increased in comparison to the same periods in 2017 as a result of increased personnel related to the expansion of the business. The expansion is two-fold including operatorship of the shallow program on the TBNG JV lands and the deep drilling program on the BCGA which is currently in the earning phase. These operator roles require significantly increased responsibilities and, at the same time, enabled increased overhead recoveries which resulted in a decrease in total general and administrative expenses for the six months ended June 30, 2017 when compared to the same period in 2017.

(tabular amounts in thousands of Canadian Dollars, except share, per share or per unit amounts)

**Foreign Exchange**

Foreign exchange (realized and unrealized) for the three and six months ended June 30, 2018 was a gain of $0.3 million and $ 0.1 million, respectively, compared to a loss of $0.3 million and $1.2 million for the same periods in 2017.

The functional currency for the Company's Turkish operations is the TL. Foreign exchange gains and losses are the result of translation of accounts denominated in currencies other than the functional currencies of Valeura and its subsidiaries, and settling transactions denominated in currencies other than the functional currency of the entity.

The Company's petroleum and natural gas sales are conducted in Turkey and are denominated in TL. As such, the Company is exposed to any fluctuations in the TL to Canadian Dollar (CAD) and United States Dollar (USD) exchange rates. A decrease in the value of the TL against the Canadian or United States Dollars will result in a decrease in revenues, royalty expense and operating costs. Correspondingly, an increase in the value of the TL against the Canadian and United States Dollars will result in an increase in revenues, royalty expense and operating costs. Changes in the value of the TL against the Canadian and United States Dollars could also impact reserve values.

The recent negative volatility in the value of the TL may impair the ability of the Company to effectively manage foreign exchange exposure. Continued devaluation of the TL, without a corresponding increase in the natural gas reference price, will have a negative impact on adjusted funds flow and could affect the ability of the Company to fund its capital program in the future.

Changes to the TL/CAD exchange rate would have had the following impact on revenues, royalties and production costs for the three and six months ended June 30, 2018:

| +/- 1% change in realized TL/CAD exchange rate | Petroleum and natural gas revenues | Royalties | Production costs |
|---|---|---|---|
| Three months ended June 30, 2018 | $ 32 | $ 4 | $ 11 |
| Six months ended June 30, 2018 | $ 68 | $ 8 | $ 21 |

The Company's drilling and seismic operations and related contracts in Turkey are predominantly based in US Dollars. Material changes in the value of the US Dollar against the TL or Canadian Dollar will impact the Company's capital costs.

Changes to the TL/USD exchange rate, which are impacted by the TL/CAD exchange rate upon conversion to the Company's Canadian Dollar presentation currency, would have had the following impact on capital expenditures for the three and six months ended June 30, 2018:

| +/- 1% change in realized TL/USD exchange rate, upon conversion to presentation currency | Capital expenditures |
|---|---|
| Three months ended June 30, 2018 | $ 9 |
| Six months ended June 30, 2018 | $ 12 |

(tabular amounts in thousands of Canadian Dollars, except share, per share or per unit amounts)

To the extent that the Company engages in risk management activities related to foreign exchange rates, there is a credit risk associated with counterparties with which the Company may contract. Valeura continues to assess its exposure to all foreign currencies, including its exposure to the TL and any cost effective ways to mitigate such exposure.

**Other Income**

During the three and six months ended June 30, 2018, the Company recorded other income of $0.5 million and $0.9 million, respectively, compared to $0.4 million and $0.7 million for the same periods in 2017. Other income is comprised of third party processing and marketing income and interest income related to cash on hand. The majority of the increase can be attributed to higher average cash levels in 2018 in comparison to 2017.

**Adjusted Funds Flow**

Adjusted funds flow for the three and six months ended June 30, 2018 was $0.5 million and $1.0 million, respectively, compared to $1.0 million and an outflow of $1.9 million for the same periods in 2017. The decrease in adjusted funds flow in Q2 2018 was due to lower revenue offset by decreased production costs. The increase in adjusted funds flow for the six months ended June 30, 2018 was the absence of expenses related to the TBNG acquisition and Banarli Farm-in including transactions costs, income taxes and realized foreign exchange losses, which negatively impacted 2017 results

The following table reconciles Valeura's cash provided by operating activities to adjusted funds flow:

| | Three months ended | | Six months ended | |
|---|---|---|---|---|
| | **June 30, 2018** | June 30, 2017 | **June 30, 2018** | June 30, 2017 |
| Cash provided by (used in) operating activities | **$ (447)** | $ (1,128) | **$ (4,382)** | $ (687) |
| Decommissioning costs incurred | **17** | 11 | **42** | 14 |
| Change in non-cash working capital | **891** | 2,076 | **5,346** | (1,251) |
| Adjusted funds flow (used) | **$ 461** | $ 959 | **$ 1,006** | $ (1,924) |

## Non-cash Expenses:

**Share-based Compensation**

Share-based compensation is a non-cash expense associated with the stock options issued to directors, officers, employees and certain other service providers of the Company.

Share-based compensation expense for the three and six months ended June 30, 2018 was $0.4 million and $0.6 million, respectively, compared to $0.1 million and $0.2 million for the same periods in 2017. During the six months ended June 30, 2018, the Company granted 1,077,500 options at a weighted average exercise price of $4.62 per option.

**Accretion on Decommissioning Liabilities**

Accretion on decommissioning obligations for the three and six months ended June 30, 2018 was $0.4 million and $0.9 million, respectively, compared to $0.5 million and $0.8 million for the same periods in 2017. The decrease in Q2 2018 when compared to the same period in 2017 is due to revisions in estimates. The increase for the six months ended June 30, 2018 is in comparison to the same period in 2017 is due to the TBNG Acquisition and an increased percentage ownership in the TBNG JV wells and facilities and the associated impact on decommissioning obligations.

(tabular amounts in thousands of Canadian Dollars, except share, per share or per unit amounts)

### Depletion and Depreciation

Depletion and depreciation for the three and six months ended June 30, 2018 was $1.8 million and $3.9 million, respectively, compared to $2.3 million and $4.2 million for the same periods in 2017. Depletion is calculated on a unit-of-production basis utilizing proved plus probable reserves.

On a per unit basis, depletion and depreciation for the three and six months ended June 30, 2018 was $27.52/boe and $26.80/boe, respectively, compared to $26.65/boe and $26.41/boe for the same periods in 2017.

### Current Tax

Current tax for the three and six months ended June 30, 2018 was an expense of $0.1 million and $0.2 million, respectively, compared to a recovery of $0.3 million and an expense of $0.9 million for the same periods in 2017. The current tax represents taxes due related to normal operating activities in Turkey. The corporate tax rate in Turkey increased from 20% to 22% effective for tax years beginning on January 1, 2018 for the years 2018, 2019 and 2020.

### Deferred Tax

Deferred tax for the three and six months ended June 30, 2018 was a recovery of $0.5 million and $0.3 million, respectively, compared to a recovery of $1.5 million and $4.0 million for the same periods in 2017. Deferred tax relates to changes in the temporary difference between the net book value and the tax basis of the assets and liabilities in the Company's Turkish operations.

### Currency Translation Adjustments

Translation of all assets and liabilities from their respective functional currencies to the reporting currency are performed using the rates prevailing at the statement of financial position date. The differences arising upon translation from the functional currency to the reporting currency are recorded as currency translation adjustments in accumulated other comprehensive income or loss ("AOCI") and are held within AOCI until a disposal or partial disposal of a subsidiary. A disposal or partial disposal will then give rise to a realized foreign exchange gain or loss which is recorded in net earnings.

The currency translation adjustment for the three and six months ended June 30, 2018 was a loss of $5.3 million and $6.0 million, respectively, compared to a gain of $0.9 million and a loss of $0.7 million for the same periods in 2017 reflecting the fluctuation in the value of the TL compared to the Canadian dollar in the respective periods.

## Capital Expenditures

The following summarizes the Company's capital spending:

| | Three months ended | | Six months ended | |
|---|---|---|---|---|
| | **June 30, 2018** | June 30, 2017 | **June 30, 2018** | June 30, 2017 |
| Geological and geophysical | **$ (34)** | $ 273 | **$ 94** | $ 679 |
| Drilling & completions | **865** | 2,718 | **1,124** | 3,825 |
| Workovers & recompletions | **161** | 916 | **547** | 1,260 |
| Equipping, facilities & other | **136** | 104 | **237** | 179 |
| Total exploration and development capital program | **1,128** | 4,011 | **2,002** | 5,943 |
| Acquisitions | **-** | - | **-** | 21,450 |
| Dispositions | **-** | (3,973) | **-** | (26,288) |
| Total net capital | **$ 1,128** | $ 38 | **$ 2,002** | $ 1,105 |

(tabular amounts in thousands of Canadian Dollars, except share, per share or per unit amounts)

The Company's capital spending for Q2 2018 was $1.1 million, including $0.9 million for drilling and completions, $0.2 million for workovers and recompletions and $0.1 million of equipping, facilities and other.

During Q2 2018, the Company drilled one well, Karanfiltepe-7, on the TBNG JV lands (Valeura 81.5% working interest). Karanfiltepe-7 was drilled to a measured depth of 1,454 metres and is currently on production.

During the quarter, Valeura developed a definitive program to appraise the BCGA play and put in place major contracts and regulatory approvals. The first activity for Q3 2018 is the final completion and long term test of the Yamalik 1 well and the spud of the second commitment well, Inanli-1, under the Banarli Farm in. Equinor will fund the drilling, completion and testing of the second farm in well. For the remainder of 2018, the focus will be on the deep drilling program as described below.

**2018/2019 Planned Capital Program**

Valeura's 2018 and 2019 capital program will be almost entirely focused on the drilling and testing of wells to delineate and demonstrate commerciality of the unconventional BCGA play discovered by Yamalik-1 in 2017. Funds are also allocated for the tie-in of these wells to allow for production and sales of any discovered gas.

During Q2 2018, planning and procurement activities for the drilling of three deep wells and the completion, tie in and testing of Yamalik-1 continued. With more information regarding cost and timing, the plan for capital expenditures for 2018/2019 BCGA program is updated as follows, projects moved to 2020 are excluded from the table below:

| Operation | Net VLE Cost (in dollars) | Anticipated Timing |
|---|---|---|
| Yamalik-1 Completion and Tie-in to Production Facilities | $600,000 | Q3 2018 |
| Drill and Test Inanli-1 (Banarli) | $0 | Q4 2018 - Q1 2019 |
| Drill and Test Devepinar-1 (West Thrace) | $10,000,000 | Q4 2018 -Q2 2019 |
| Drill and Test Banarli #3 Deep Well | $15,900,000 | Q2 2019–Q3 2019 |
| Hayrabolu-10 Frac and Test | $1,600,000 | Q2 2019 |
| Facilities Capital and Tie-in for 4 wells | $3,200,000 | 2019 |
| G&G and studies on Banarli and West Thrace | $1,400,000 | 2018 - 2019 |
| Development and Early Production Planning | $3,900,000 | 2019 |
| **Total:** | **$36,600,000** | |

After further work on planning, procurement, cost estimates and project timing, the total 2018/19 BCGA capital program has been reduced to a total of $36.6 million from $55 million previously anticipated. Changes include the reduction in cost for: the Yamalik-1 completion and tie-in; the Hayrabolu-10 workover; and Devepinar-1 (previously West Thrace #1 Deep Well) and Banarli #3 Deep Well. Changes in timing include: moving Devepinar-1 from Q4 2018 to Q4 2018 through Q2 2019; moving the Hayrabolu-10 workover from Q4 2018 to Q2 2019; moving the Banarli #3 Deep Well from Q1 2019 to Q2/Q3 2019; and moving the facilities and capital tie in previously scheduled for Q4 2018 to 2019. It is expected that any early production wells and an anticipated 3D seismic program will move to 2020. Therefore capital previously allocated to a Pilot Production Well and 3D seismic has been removed from the 2018/2019 program and will be funded in 2020 from working capital available. The capital program planned for 2018 for the deep and shallow drilling is anticipated to be in the range of $5 million and $7 million. The table above primarily outlines the deep drilling program. Valeura has drilled one shallow well on the TBNG JV lands in Q2 2018, Karanfiltepe-7, which was strategically important as it represents a license retention well. The net cost of this well was $0.8 million. The Company will also continue with workovers and maintenance work to support production and maintain facilities in good working order.

(tabular amounts in thousands of Canadian Dollars, except share, per share or per unit amounts)

The Company maintains considerable flexibility in managing its capital budget for 2018 and 2019. As a result of the TBNG acquisition, the Company is now the operator of the TBNG JV, which provides a greater level of control of capital spending. The drilling and workover capital spending on the TBNG JV lands is focused on fulfilling drilling commitments and mitigating natural production declines. The Company will continue to utilize current working capital and adjusted funds flow to fund any capital spending on the TBNG JV lands. In addition to the TBNG JV lands, Valeura expects to maintain operatorship of the deep rights on the Banarli Lands and West Thrace Lands for 2018 and through the drilling, completion and testing of the 3 well appraisal program and will tightly manage all capital requirements and commitments.

## Liquidity, Financing and Capital Resources

| | Three months ended | | Six months ended | |
|---|---|---|---|---|
| | **June 30, 2018** | June 30, 2017 | **June 30, 2018** | June 30, 2017 |
| **Opening cash position** | **$ 56,899** | $ 5,760 | **$ 11,108** | $ 1,987 |
| **Inflow of funds** | | | | |
| Share issuance – net of share issuance costs | **6** | (2) | **55,408** | 10,108 |
| West Thrace Deep Rights sales | **-** | 3,973 | **-** | 18,841 |
| Equinor Farm-in proceeds | **-** | - | **-** | 7,447 |
| Adjusted funds flow[7] | **461** | 959 | **1,006** | - |
| Restricted Cash | **309** | - | **400** | - |
| Proceeds from stock option exercises | **1,816** | - | **1,816** | - |
| Changes in working capital and foreign exchange on cash[8] | **-** | 3,442 | **-** | 4,451 |
| | **2,592** | 8,372 | **58,630** | 40,847 |
| **Outflow of funds** | | | | |
| Capital expenditures[9] | **(1,128)** | (4,011) | **(2,002)** | (5,943) |
| Decommissioning costs incurred | **(17)** | (11) | **(42)** | (14) |
| TBNG Acquisition | **-** | - | **-** | (21,450) |
| Restricted cash | **-** | (207) | **-** | (3,600) |
| Changes in working capital and foreign exchange on cash[10] | **(2,401)** | - | **(11,749)** | - |
| Adjusted funds flow | **-** | - | **-** | (1,924) |
| | **(3,546)** | (4,229) | **(13,793)** | (32,931) |
| **Closing cash position** | **$ 55,945** | $ 9,903 | **$ 55,945** | $ 9,903 |

[7] Non-GAAP measure – see note regarding non-GAAP measures on page 18.

[8] Includes the following captions from the condensed interim consolidated statements of cash flows: changes in non-cash working capital from operating activities, changes in non-cash working capital from investing activities and foreign exchange gain (loss) on cash held in foreign currencies.

[9] Includes the following captions from the condensed interim consolidated statements of cash flows: exploration and evaluation expenditures and property and equipment expenditures.

[10] Includes the following captions from the condensed interim consolidated statements of cash flows: changes in non-cash working capital from operating activities, changes in non-cash working capital from investing activities and foreign exchange gain (loss) on cash held in foreign currencies.

**Capital Funding and Resources**

As at June 30, 2018, Valeura's working capital[11] balance was $60.3 million including cash of $56.0 million. Valeura's 2018 opening cash position was $11.1 million. The increase in the working capital/cash position in 2018 was due to the net proceeds of $55.4 million from the equity financing (net of share issuance costs) completed in Q1 2018 ("the 2018 Offerring") and $1.8 million of proceeds from stock option exercises. In the first 6 months of 2018, the Company utilized this opening cash balance plus adjusted funds flow to fund an exploration and development capital program of $2.0 million. The Company anticipates a working capital position at the end of 2018 in excess of $55 million, based on the capital spending program described above.

**Financial Capacity**

As at June 30, 2018 the Company's working capital[11] was $60.3 million.

On March 1, 2018 the Company closed the 2018 Offering, issuing common shares for net proceeds of approximately $55.4 million, after share issue costs. Valeura intends to use the net proceeds from the 2018 Offering to fund its 2018 and 2019 capital program (outlined above) and for general corporate purposes.

**Capital Management**

The Company's objective is to maintain a flexible capital structure which allows it to execute its growth strategy through expenditures on exploration and development activities while maintaining a strong financial position. The Company's capital structure includes working capital and shareholders' equity. Currently, total capital resources available include working capital and adjusted funds flow.

The successful future operations of the Company are dependent on the ability of the Company to secure sufficient funds through operations, bank financing, equity offerings or other sources and there are no assurances that such funding will be available when needed. Failure to obtain such funding on a timely basis could cause the Company to reduce capital spending and could lead to the loss of exploration licences due to failure to meet drilling deadlines and lower production volumes and associated revenues.

The Company's capital expenditures include expenditures in oil and gas activities which may or may not be successful. The Company makes adjustments to the capital structure in light of changes in economic conditions and the risk characteristics of the underlying petroleum and natural gas assets. In order to maintain or adjust the capital structure, the Company may, from time to time, issue shares, adjust its capital spending or issue debt instruments. The Company is not subject to any externally imposed capital requirements while it maintains operatorship over all the lands in the Thrace Basin. An exception to this statement could occur in 2019 if Equinor elects to complete Phase 3 under the Banarli Farm-in and thereby earns a 50% working interest in the deep rights at Banarli. At that point, Equinor may exercise its option under the Banarli Farm-in to take operatorship of the deep rights and propose a more significant drilling program. The Company has received net proceeds of $55.4 million in an equity offering as described in the Financial Capacity section above in order to meet commitments for a delineation well capital program. However, such a program could result in an even more significant capital commitment for which the Company will be required to further assess alternatives including the availability of equity and debt capital to fund the program.

**Credit Facilities**

The Company has a general credit facility in the amount of US$0.3 million with a Turkish bank for the purpose of obtaining letters of credit required by the Turkish government. As at June 30, 2018, the Company has issued letters of credit totaling US$0.04 million (December 31, 2017 – US$0.04 million). The general credit facility is not

[11] Working capital is current assets less current liabilities.

(tabular amounts in thousands of Canadian Dollars, except share, per share or per unit amounts)

secured by any of the Company's assets and interest rate terms have not been set as the purpose of this facility is for issuance of letters of credit only.

Effective June 22, 2018, the company has available an Account Performance Security Guarantee ("ASPG") from Export Development Canada ("EDC"). The ASPG, which was issued to National Bank of Canada ("NBC") allows the Company to use the ASPG as collateral for certain letters of credit issued by NBC. The facility is effective from May 16, 2018 to May 31, 2019 with a limit of US$ 2.5 million, and can be renewed on an annual basis. The Company intends to use letters of credit issued by NBC under the ASPG to replace restricted cash collateral. As of June 30, 2018, no letters of credit were issued under this facility.

## Selected Quarterly Information

| | Three months ended | | | |
|---|---|---|---|---|
| | **June 30, 2018** | **March 31, 2018** | **December 31, 2017** | **September 30, 2017** |
| Total daily production (boe/d) | 736 | 859 | 1,038 | 1,024 |
| Average wellhead price ($/boe) | $ 44.06 | $ 44.87 | $ 40.03 | $ 42.14 |
| Petroleum and natural gas sales | 2,949 | 3,469 | 3,824 | 3,970 |
| Adjusted funds flow (used) | 461 | 545 | (446) | 1,165 |
| Per share, basic and diluted | 0.01 | 0.01 | (0.01) | 0.02 |
| Net loss | (1,404) | (2,435) | (946) | (4,911) |
| Per share, basic and diluted | $ (0.02) | $ (0.03) | $ (0.01) | $ (0.07) |
| | **Three months ended** | | | |
| | **June 30, 2017** | **March 31, 2017** | **December 31, 2016** | **September 30, 2016** |
| Total daily production (boe/d) | 934 | 807 | 795 | 680 |
| Average wellhead price ($/boe) | $ 44.28 | $ 42.49 | $ 47.97 | $ 56.10 |
| Petroleum and natural gas sales | 3,764 | 3,088 | 3,508 | 3,510 |
| Adjusted funds flow (used) | 959 | (2,883) | 915 | 1,066 |
| Per share, basic and diluted | 0.01 | (0.04) | 0.02 | 0.02 |
| Net loss | (526) | (2,001) | (3,189) | (1,263) |
| Per share, basic and diluted | $ (0.01) | $ (0.03) | $ (0.06) | $ (0.02) |

Significant factors that have impacted the Company's results during the above periods include:

- Revenue is directly impacted by the Company's ability to mitigate natural production declines with production additions from an on-going capital expenditure program and acquisitions.
- Valeura has benefited from relatively high natural gas prices and netbacks in Turkey compared to North America, although the weakening of the TL since 2016 reduced wellhead price realizations compared to 2016.
- With its revenues in TL, capital expenditures primarily in United States Dollars and reporting currency in Canadian Dollars, Valeura has a high level of foreign exchange and currency translation exposure.

## Commitments

On August 1, 2016 the Company renegotiated its existing office space sublease in Calgary that was originally signed on June 15, 2015. The term of this sublease runs through January 30, 2019. The Company has the option to terminate the sublease agreement after 18 months. The remaining amount committed under this renegotiated sublease is approximately $0.2 million including an estimate for operating costs. At June 30, 2018 the remaining commitment of $0.2 million will be discharged in the following years: 2018 – $0.2 million, 2019 – $nominal.

## Critical Accounting Policies

### Use of Estimates and Judgments

The preparation of consolidated financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. The reader is referred to Valeura's December 31, 2017 audited consolidated financial statements and MD&A for a description of estimates and judgments.

### Changes in Significant Accounting Policies

IFRS 15 Revenue from Contracts with Customers

Valeura adopted the new standard on January 1, 2018 on a retrospective basis. The standard requires enhanced disclosure of revenue from contracts with customers as detailed in Note 8 of the interim financial statements, including categories that depict the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors. Valeura management reviewed its revenue streams and major contracts with customers and concluded that there were no material impacts on the Company's revenues or cash flows for the period as a result of adopting the new standard.

The new standard contains a single model that applies to contracts with customers and two approaches to recognizing revenue: at a point in time or over time. The model features a contract-based five-step analysis of transactions to determine whether, how much and when revenue is to be recognized. New estimates and judgmental thresholds have been introduced, which may affect the amount and timing of the revenue recognized. The new standard applies to contracts with customers and does not apply to insurance contracts, financial instruments or lease contracts.

Valeura's petroleum and natural gas revenues from the sale of natural gas and crude oil are based on the consideration specified in the contracts with customers. For natural gas, pricing is linked to BOTAS benchmark pricing, while crude oil pricing is linked to Brent benchmark pricing. Valeura recognizes revenue when it transfers control of the product to the customer, which is generally when legal title passes to the customer and collection is reasonably assured.

Valeura evaluates its arrangements with third parties and partners to determine if Valeura is acting as the principal or as the agent. Valeura is considered the principal in a transaction when it has primary responsibility for the transaction. If Valeura acts in the capacity of an agent rather than as a principal in a transaction, then the revenue is recognized on a net basis, only reflecting the fee, if any realized by Valeura from the transaction.

IFRS 9 Financial Instruments

IFRS 9, as amended, includes a principle-based approach for classification and measurement of financial assets, a single 'expected loss' impairment model and a substantially reformed approach to hedge accounting, which is more in line with risk management activities. IFRS 9 has been adopted on a retrospective basis by Valeura on January 1, 2018. IFRS 9 contains three principal classification categories for financial assets: measured at amortized cost, fair value through other comprehensive income ("FVOCI"), or fair value through profit or loss ("FVTPL").

Under IFRS 9, where the fair value option is applied to financial liabilities, any change in fair value resulting from an entity's own credit risks is recorded through other comprehensive income or loss rather than net income or loss. The classification of financial assets under IFRS 9 is generally based on the business model in which a financial asset is managed and its contractual cash flow characteristics.

A financial asset is subsequently measured at amortized cost if it meets both of the following conditions: a) the asset is held with a business model whose objective is to hold assets to collect contractual cash flows; and b) the contractual terms of the financial assets give rise to cash flows on specified dates that are solely payments of principal and interest on principal amounts outstanding.

Financial assets that meet criteria (b) above that are held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets is subsequently measured at FVOCI. All other financial assets and liabilities are subsequently measure at FVTPL. There was no change to the measurement categories of financial liabilities.

Accounts receivable, prepaid expenses and deposits, accounts payable and accrued liabilities continue to be measured at amortized cost and are now classified as "amortized cost".

**Recent Accounting Standards and Interpretations**

The International Accounting Standards Board ("IASB") released the following new standards:

In January 2016, the IASB issued IFRS 16 Leases, which replaces IAS 17 Leases. For lessees applying IFRS 16, a single recognition and measurement model for leases would apply, with required recognition of assets and liabilities for most leases. The standard will come into effect for annual periods beginning on or after January 1, 2019, with earlier adoption permitted. IFRS 16 will be applied by Valeura on January 1, 2019 and the Company is currently in the process of reviewing and analyzing contracts that fall into the scope of the new standard. The extent of the impact of the adoption of the standard has not yet been determined.

**Disclosure Controls and Procedures and Internal Controls over Financial Reporting**

The Company's Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") have designed, or caused to be designed under their supervision, disclosure controls and procedures to provide reasonable assurance that: material information relating to the Company is made known to the Company's CEO and CFO by others, particularly during the period in which the annual and interim filings are being prepared; and information required to be disclosed by the Company in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time period specified in securities legislation.

The Company's CEO and CFO have designed, or caused to be designed under their supervision, internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS. The Company is required to disclose herein any change in the Company's internal controls over financial reporting that occurred during the period beginning on April 1, 2018 and ending on June 30, 2018 that has materially affected, or is reasonably likely to materially affect, the Company's internal controls over financial reporting. No material changes in the Company's internal controls over financial reporting were identified during such period that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

It should be noted that a control system, including the Company's disclosure and internal controls and procedures, no matter how well conceived can provide only reasonable, but not absolute assurance that the objectives of the control system will be met and it should not be expected that the disclosure and internal controls and procedures will prevent all errors or fraud.

## Off Balance Sheet Arrangements

The Company had no off balance sheet arrangements outstanding as at June 30, 2018 other than those previously disclosed under the Commitments and Contractual Obligations section.

## Financial Instruments

Financial instruments of the Company include cash, accounts receivable, accounts payable and accrued liabilities. The carrying values of the financial instruments approximate their fair values due to their relatively short periods to maturity.

## Business Risks and Uncertainties

There are a number of risk factors that the Company faces as a participant in the international oil and gas industry which are inherently risky.

All risk factors have not materially changed from December 31, 2017. The reader is referred to Valeura's December 31, 2017 audited consolidated financial statements, MD&A and 2017 AIF for a description of these risks.

### Special Note Regarding Non-GAAP Measures

This MD&A includes references to financial measures commonly used in the oil and gas industry. The terms "operating netback" (petroleum and natural gas sales less royalties, production expenses and transportation costs), and "adjusted funds flow" (cash provided by operating activities before decommissioning costs incurred and changes in non-cash working capital) are non-GAAP measures and do not have standardized meanings prescribed by GAAP and are therefore unlikely to be comparable to similar measures used by other issuers. The Company uses these supplemental non-GAAP measures to assist readers in evaluating operating performance. The Company considers adjusted funds flow a key measure as it demonstrates the ability of the Company's continuing operations to generate the cash flow necessary to fund future growth through capital investments and considers operating netback an important measure as it demonstrates its profitability level relative to current commodity prices.

## Forward-looking Statements

Certain information included in this MD&A constitutes forward-looking information under applicable securities legislation. Such forward-looking information is for the purpose of explaining management's current expectations and plans relating to the future. Readers are cautioned that reliance on such information may not be appropriate for other purposes, such as making investment decisions. Forward-looking information typically contains statements with words such as "anticipate", "believe", "expect", "plan", "intend", "estimate", "propose", "project", "target" or similar words suggesting future outcomes or statements regarding an outlook. Forward-looking information in this MD&A includes, but is not limited to: the 2018 work program and budget; the timeliness and costs for the deep drilling program in 2018 and 2019; the potential for a 3D seismic program and early production wells in 2020; the identification and finalization of locations for the third well of the deep program; potential to tie-in and conduct a long term production test and achieve natural gas sales from the Yamalik-1 well; the anticipated working capital balance at the end of 2018; the timing of the commencement of the delineation drilling campaign, including the spud date for Inanli-1; the potential of a basin-centered gas play in the Thrace Basin; management's belief regarding the potential of the Company's deep basin-centred gas play and shallow gas business in the Thrace Basin; the Company's belief in the pervasiveness of over-pressured gas across the Company's Thrace Basin lands; the Company's commitment to safety and optimizing operational and administrative functions; the Company's business strategy and outlook, operational plans, and expected capital expenditures; and the availability of operating cash flow and the ability to finance development from existing cash and operating cash flow.

Forward-looking information is based on management's current expectations and assumptions regarding, among other things: political stability of the areas in which the Company is operating and completing transactions, and in particular the period of political change and uncertainty in Turkey in 2016 and 2017; continued safety of operations and ability to proceed in a timely manner; continued operations of and approvals forthcoming from the

Turkish government in a manner consistent with past conduct; future seismic and drilling activity on the expected timelines; the prospectivity of the TBNG JV lands and Banarli Licences, including the deep potential; the continued favourable pricing and operating netbacks in Turkey; future production rates and associated operating netbacks and cash flow; decline rates; future sources of funding; future economic conditions; future currency exchange rates; the ability to meet drilling deadlines and other requirements under licences and leases; and the Company's continued ability to obtain and retain qualified staff and equipment in a timely and cost efficient manner. In addition, the Company's work programs and budgets are in part based upon expected agreement among joint venture partners and associated exploration, development and marketing plans and anticipated costs and sales prices, which are subject to change based on, among other things, the actual results of drilling and related activity, availability of drilling, fracing and other specialized oilfield equipment and service providers, changes in partners' plans and unexpected delays and changes in market conditions. Although the Company believes the expectations and assumptions reflected in such forward-looking information are reasonable, they may prove to be incorrect.

Forward-looking information involves significant known and unknown risks and uncertainties. Exploration, appraisal, and development of oil and natural gas reserves are speculative activities and involve a significant degree of risk. A number of factors could cause actual results to differ materially from those anticipated by the Company including, but not limited to: the risks of currency fluctuations; changes in gas prices and netbacks in Turkey; uncertainty regarding the contemplated timelines for the Yamalik-1 tie-in program; completion of the Banarli Farm-in program and the basin-centered gas delineation drilling program; the risks of disruption to operations and access to worksites, threats to security and safety of personnel and potential property damage related to political issues, terrorist attacks, insurgencies or civil unrest in Turkey; political stability in Turkey, including potential changes in Turkey's constitution, political leaders or parties or a resurgence of a coup or other political turmoil; the uncertainty regarding government and other approvals; counterparty risk; potential changes in laws and regulations; risks associated with weather delays and natural disasters; the risk associated with international activity; and, the uncertainty regarding the ability to fulfill the drilling commitments on the West Thrace lands in 2019. See Valeura's 2017 AIF filed on SEDAR at www.sedar.com for a detailed discussion of the risk factors.

The forward-looking information contained in this MD&A is made as of the date hereof and the Company undertakes no obligation to update publicly or revise any forward-looking information, whether as a result of new information, future events or otherwise, unless required by applicable securities laws. The forward looking information contained in this MD&A is expressly qualified by this cautionary statement.