Q1 2017

Condensed Consolidated Financial Statements

CHINOOK energy inc

Chinook Energy Inc. | 1000, 517 – 10th Avenue S.W. Calgary, Alberta T2R 0A8 TSX:CKE

Condensed Consolidated Statements of Financial Position

(unaudited)

(in thousands of Canadian dollars)	**March 31 2017**	December 31 2016
Assets		
Current		
Cash	**$ 21,622**	$ 14,821
Accounts receivable	**7,800**	6,658
Restricted cash (note 9)	**1,308**	1,308
Prepaids & deposits	**4,441**	3,569
Fair value of commodity price contracts (note 4)	**1,133**	-
Assets held for sale (note 7)	**-**	7,148
	36,304	33,504
Development & production assets (note 5)	**99,299**	92,959
Exploration & evaluation assets (note 6)	**13,062**	13,512
	$ 148,665	$ 139,975
Liabilities & Equity		
Current		
Accounts payable, accrued liabilities & other	**$ 9,549**	$ 11,218
Fair value of commodity price contract (note 4)	**-**	154
Decommissioning obligations (note 8)	**1,200**	1,300
Liabilities held for sale (note 7)	**-**	236
	10,749	12,908
Decommissioning obligations (note 8)	**27,943**	27,767
Shareholders' Equity		
Share capital	**784,105**	784,105
Contributed surplus	**20,010**	19,759
Deficit	**(694,142)**	(704,564)
	109,973	99,300
	$ 148,665	$ 139,975

See accompanying notes to the condensed consolidated financial statements.

Condensed Consolidated Statements of Operations and Comprehensive Income (Loss)

(unaudited)

Three months ended March 31	2017	2016
(in thousands of Canadian dollars, except per share amounts)		
Petroleum & natural gas revenues	$ 6,775	$ 7,761
Royalty recovery (expense)	63	(517)
Petroleum & natural gas revenues, net of royalties	6,838	7,244
Processing & gathering revenues	260	860
Petroleum, natural gas & other revenues, net of royalties	7,098	8,104
Realized gain on commodity price contract	436	-
Unrealized gain on commodity price contracts	1,287	-
Gain on commodity price contracts	1,723	-
Total revenues, net of royalties and commodity price contracts	8,821	8,104
Production & operating	3,824	8,778
General & administrative	1,612	1,890
Severance costs	373	-
Exploration & evaluation	92	496
Depletion, depreciation & amortization (notes 5 & 6)	2,933	7,146
(Gain) loss on dispositions of properties (note 7)	(10,926)	855
Share-based compensation	251	680
Bad debt expense	-	79
Foreign exchange losses & other	155	390
Total expenses, net of gains and losses on dispositions of properties, excluding finance expenses	(1,686)	20,314
Income (loss) before finance expenses	10,507	(12,210)
Interest & financing (income) charges	(84)	13
Accretion of decomissioning obligations (note 8)	169	552
Finance expenses	85	565
Net & comprehensive income (loss)	$ 10,422	$ (12,775)
Net income (loss) per share - basic and diluted (note 10)	$ 0.05	$ (0.06)

See accompanying notes to the condensed consolidated financial statements.

Condensed Consolidated Statements of Changes in Shareholders' Equity

(unaudited)

(in thousands of Canadian dollars, except common shares)	Common Shares (thousands)	Share Capital	Contributed Surplus	Deficit	Shareholders' Equity
Balance as at December 31, 2016	**216,443**	**$ 784,105**	**$ 19,759**	**$ (704,564)**	**$ 99,300**
Share-based compensation	-	-	251	-	251
Net income	-	-	-	10,422	10,422
Balance as at March 31, 2017	**216,443**	**$ 784,105**	**$ 20,010**	**$ (694,142)**	**$ 109,973**
Balance as at December 31, 2015	**215,349**	**$ 782,705**	**$ 18,916**	**$ (600,406)**	**$ 201,215**
Settlement of restricted share awards	1	3	(3)	-	-
Share-based compensation	-	-	680	-	680
Net loss	-	-	-	(12,775)	(12,775)
Balance as at March 31, 2016	**215,350**	**$ 782,708**	**$ 19,593**	**$ (613,181)**	**$ 189,120**

See accompanying notes to the condensed consolidated financial statements.

Condensed Consolidated Statements of Cash Flows

(unaudited)

Three months ended March 31	2017	2016
(in thousands of Canadian dollars)		
Operating Activities		
Net income (loss)	**$ 10,422**	$ (12,775)
Add (deduct):		
Depletion, depreciation & amortization (notes 5 & 6)	**2,933**	7,146
(Gain) loss on dispositions of properties (note 7)	**(10,926)**	855
Unrealized gain on commodity price contracts	**(1,287)**	-
Share-based compensation	**251**	680
Accretion of decomissioning obligations (note 8)	**169**	552
Bad debt expense	**-**	79
Foreign exchange losses & other	**9**	77
Decommissioning obligation expenditures (note 8)	**(93)**	(3,165)
Change in operating non-cash working capital (note 10)	**(2,923)**	2,216
Cash outflow from operating activities	**(1,445)**	(4,335)
Investing Activities		
Proceeds on property dispositions (note 7)	**17,838**	299
Development & exploration expenditures (note 5)	**(8,823)**	(3,026)
Change in investing non-cash working capital (note 10)	**(760)**	(6,367)
Cash flow (outflow) from investing activities	**8,255**	(9,094)
Change in cash, during the period	**6,810**	(13,429)
Cash, beginning of period	**14,821**	37,947
Cash, foreign currency loss	**(9)**	(133)
Cash, end of period	**$ 21,622**	$ 24,385

Other supplementary information (note 10)

See accompanying notes to the condensed consolidated financial statements.

Notes to the Condensed Consolidated Financial Statements

(unaudited)

For the three months ended March 31, 2017 and 2016

Tabular amounts in thousands of Canadian dollars, except as noted

1. Reporting Entity

Chinook Energy Inc. is a Calgary-based petroleum and natural gas production company focused on development and exploration opportunities in western Canada.

These unaudited condensed consolidated financial statements for the three months ended March 31, 2017 and 2016 (these “Financial Statements”) include the accounts of Chinook Energy Inc. and two directly held wholly-owned subsidiaries (collectively, including all subsidiaries, “Chinook” or the “Company”): 1542991 Alberta Ltd. and Storm Ventures International (BVI) Limited).

All intercompany balances and transactions have been eliminated.

2. Basis of Presentation

These Financial Statements have been prepared following the same accounting policies as summarized in note 3 in the audited consolidated financial statements of Chinook for the years ended December 31, 2016 and 2015 (the “Audited Financial Statements”). They do not include all of the required disclosures for annual consolidated financial statements and therefore should be read in conjunction with the Audited Financial Statements and the notes thereto.

These Financial Statements have been prepared by management in accordance with International Accounting Standard 34 ‘Interim Financial Reporting’ using accounting principles consistent with International Financial Reporting Standards issued by the International Accounting Standards Board.

These Financial Statements were approved and authorized for issuance by Chinook’s Board of Directors on May 9, 2017.

3. New Accounting Standards and Amendments

In July 2014, the IASB issued IFRS 9 “Financial Instruments” to replace IAS 39, “Financial Instruments Recognition and Measurement”. The new standard replaces the current multiple classification and measurement models for financial instruments with a single model that has only two classifications categories: amortized cost and fair value. Due to the fact that all of Chinook’s financial instruments are carried at amortized cost or fair value, this standard is not expected to have a significant effect on Chinook’s financial statement disclosure. Chinook does not currently apply, nor does it intend to apply, hedge accounting to its financial instrument commodity price contracts on adoption of IFRS 9.

In May 2014 the IASB issued IFRS 15 “Revenue from Contracts with Customers” to replace International Accounting Standard (‘IAS”) 18, Revenue, IAS 11 “Construction Contracts”, and related interpretations. The 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 recognized. New estimates and judgmental thresholds have been introduced, which affect the amount and/or timing of revenue recognized. Chinook is currently in the process of assessing underlying revenue contracts with customers to determine the impact, if any, that the adoption of IFRS 15 will have on its financial statements.

As of January 1, 2018, Chinook will be required to adopt the above two standards.

In January 2016, the IASB issued IFRS 16 “Leases”. The standard requires entities to recognize lease assets and lease obligations on the statements of financial position. For lessees, there will be a single lease accounting model for all leases. There will no longer be a classification test between finance and operating leases. The lessee will recognize a Right of Use (“ROU”) asset and a lease liability, and the lease will be treated as an asset on a financed basis. There will be an optional exemption from the above for short term leases and leases of low value assets, defined at 12 months or less and an option for portfolio accounting on leases that have similar criteria.

From the lessor's perspective, there will still be a dual lease accounting model, that follows the criteria set out in IAS 17. As of January 1, 2019, Chinook will be required to adopt this standard. Chinook is currently assessing all major leases including firm commitment contracts, which are expensed as operating leases for reclassification to the statement of financial position.

4. Fair Value of Commodity Price Contracts

As at March 31, 2017, Chinook had the following commodity price contracts:

Financial AECO Natural Gas Contracts					
Remaining Contractual Term	**Average Notional Volumes (GJ/d)**	**Company's Received Price**	**Indexed Price**		**Fair Value**
April 1, 2017 to December 31, 2017	7,500	$3.205/GJ	AECO	$	1,238
April 1, 2017 to October 31, 2017	4,000	$2.50/GJ	AECO		(105)
				$	1,133

At March 31, 2017, the natural gas price contracts had a combined fair value asset of $1.1 million as reported through the line item fair value of commodity price contracts in current assets on the condensed consolidated statements of financial position. The fair value of each contract was determined through the difference in the referenced benchmark forward price as compared to the contract's strike price multiplied by the notional volumes during the remaining contractual term. As at December 31, 2016, Chinook had one outstanding commodity price contract with a fair value liability of $0.2 million as reported through the line item fair value of commodity price contract as a current liability on the condensed consolidated statements of financial position.

5. Development and Production Assets ("D&P Assets")

The following table reconciles Chinook's D&P Assets for the three months ended March 31, 2017:

Cost of Assets		**2017**
Balance, beginning of period	**$**	**237,868**
Capital expenditures		**8,823**
Balance, end of period	**$**	**246,691**
Accumulated Depletion & Depreciation		
Balance, beginning of period	**$**	**(144,909)**
Depletion & depreciation		**(2,483)**
Balance, end of period	**$**	**(147,392)**
Net book values		
Balance as at December 31, 2016	**$**	**92,959**
Balance as at March 31, 2017	**$**	**99,299**

Capitalized general and administrative expenses

Chinook capitalized $0.2 million and $0.3 million of direct general and administrative costs related to its development activity during the three months ended March 31, 2017 and 2016, respectively.

6. Exploration & Evaluation Assets (“E&E Assets)

The following table reconciles Chinook’s E&E Assets for the three months ended March 31, 2017:

Cost of Assets		**2017**
Balance, beginning and end of period	**$**	**30,947**
Accumulated Amortization		
Balance, beginning of period	**$**	**(17,435)**
Amortization		**(450)**
Balance, end of period	**$**	**(17,885)**
Net book values		
Balance as at December 31, 2016	**$**	**13,512**
Balance as at March 31, 2017	**$**	**13,062**

7. Property dispositions

During the three months ended March 31, 2017, Chinook completed the sale of certain of its petroleum and natural gas properties including undeveloped lands located in the Knopcik/Pipestone and East Gold Creek areas of northwestern Alberta for net proceeds of $17.8 million after customary adjustments. At December 31, 2016, these properties were classified as held for sale. This classification included carrying values of $7.1 million for both developed and undeveloped properties less $0.2 million for associated decommissioning obligations. Combined, the net carrying amounts of these sold properties and undeveloped lands was less than the sales proceeds resulting in a gain of $10.9 million for the three months ended March 31, 2017. During the three months ended March 31, 2016, Chinook completed the sale of petroleum and natural gas properties for net proceeds of $0.3 million resulting in a loss of $0.9 million.

8. Decommissioning Obligations

The following table reconciles Chinook’s decommissioning obligations for the three months ended March 31, 2017:

		2017
Balance as at December 31, 2016	**$**	**29,067**
Decommissioning obligation expenditures		**(93)**
Accretion expense		**169**
Balance as at March 31, 2017	**$**	**29,143**

As reported on the condensed consolidated statements of financial position, Chinook’s decommissioning obligations balance consists of:

		2017
Current portion	**$**	**1,200**
Long-term portion		**27,943**
Decommissioning obligations	**$**	**29,143**

9. Long-Term Debt

During the three months ended March 31, 2017, Chinook’s previous credit facility agreement was terminated and Chinook negotiated and secured an $8.0 million demand credit facility (the “Demand Credit Facility”) with a Canadian chartered bank. Borrowings under the Demand Credit Facility are currently limited to $2 million until Chinook receives confirmation that the three Birley/Umbach wells completed and brought on-stream during the first quarter are producing to the lender’s satisfaction. At any time, the lender can request repayment of all outstanding drawn amounts resulting in any future borrowings being classified as a currently liability. The Demand Credit Facility’s availability is subject to annual reviews with the first review scheduled for June 1, 2017. Changes in the availability in the Demand Credit Facility are possible, from one review to the next, with draws in excess of availability becoming immediately payable. Borrowings incur interest at the prime rate plus an applicable margin and are collateralized by floating charges and security interests over all of Chinook's present and future properties and other assets. As at March 31, 2017, Chinook has not made any draws on the Demand Credit Facility.

The Demand Credit Facility has a financial covenant requiring that the adjusted working capital be 1:1 at each reporting period. For the purposes of this covenant, adjusted working capital is defined as working capital excluding both current commodity price contracts and debt. In addition, the Demand Credit Facility includes operating and financial restrictions on Chinook that include restrictions on paying dividends or repurchasing or making of other distributions with respect to Chinook's securities.

As at the end of any fiscal quarter, if Chinook has any net debt or Demand Credit Facility draws, within 60 days of the end of any such quarter, the terms of the Demand Credit Facility also require that Chinook must enter into commodity price contracts covering no less than 30% of its forecasted twelve month combined production volumes.

As at March 31, 2017, Chinook is in compliance with the above financial covenant and other requirements.

During the year ended December 31, 2016, Chinook voluntarily reduced its previous reserve-based credit facility from $50.0 million to $nil, as a result of the transfer of a significant portion of its assets to Craft Oil Inc. As a result of this voluntary reduction, as at March 31, 2017 and December 31, 2016, Chinook had guaranteed a total of $1.3 million in outstanding letters of credit through depositing an equivalent amount in cash with its lender.

10. Other Supplementary Information

Changes in non-cash working capital

Three months ended March 31	**2017**	2016
Cash provided by (used for):		
Accounts receivable	**$ (1,142)**	$ 984
Prepaids & deposits	**(872)**	(158)
Accounts payable, accrued liabilities & other	**(1,669)**	(4,977)
	$ (3,683)	$ (4,151)
Cash provided by (used for):		
Operating activities	**$ (2,923)**	$ 2,216
Investing activities	**(760)**	(6,367)
	$ (3,683)	$ (4,151)

Cash interest and financing fees paid

Three months ended March 31	**2017**	2016
Cash interest & financing fees paid	**$ 8**	$ 116

Per share amounts

Three months ended March 31	**2017**	2016
Weighted average shares outstanding - basic (thousands)	**216,443**	215,349
Dilutive impact of restricted and performance awards (thousands)	**457**	-
Weighted average shares outstanding - diluted (thousands)	**216,900**	215,349
Net income (loss)	**$ 10,422**	$ (12,775)
Net income (loss) per share - basic & diluted ($/share):	**$ 0.05**	$ (0.06)

For the three months ended March 31, 2017, Chinook's outstanding restricted and performance awards (the "Awards") were dilutive because the weighted average number of outstanding Awards exceeded the deemed repurchased shares calculated from unamortized share-based compensation. For the three months ended March 31, 2016, because Chinook reported a net loss, the effect of share options and Awards would have been anti-dilutive resulting in them being excluded in the calculation of diluted weighted average shares outstanding.