

Condensed Interim Consolidated Financial Statements
(Unaudited)

ARSENAL ENERGY INC.

For the three months ended March 31, 2015 and 2014

Arsenal Energy Inc.

Condensed Interim Consolidated Statements of Financial Position
(Unaudited)

		March 31, 2015	December 31, 2014
	(thousands of \$Cdn)		
Assets			
Current assets:			
Cash	\$	4,167	\$ 2,573
Accounts receivable		6,449	10,553
Inventory		453	570
Risk management contracts (note 8)		300	11,946
Prepaid expenses and deposits		490	649
		11,859	26,291
Reclamation deposit		190	174
Exploration and evaluation assets		3,639	3,639
Property, plant and equipment (note 4)		214,883	206,320
	\$	230,571	\$ 236,424
Liabilities and Shareholders' Equity			
Current liabilities:			
Accounts payable and accrued liabilities	\$	13,872	\$ 16,700
Current tax payable		218	522
Current portion of decommissioning obligations (note 6)		750	750
Incentive compensation liability		397	1,571
Risk management contracts (note 8)		256	57
		15,493	19,600
Bank loan (note 5)		53,551	60,000
Flow-through share premium		1,139	1,628
Risk management contracts (note 8)		490	139
Decommissioning obligations (note 6)		45,377	43,979
Deferred taxes		21,550	20,386
		137,600	145,732
Shareholders' Equity:			
Common shares (note 7)		151,505	151,434
Contributed surplus		11,574	11,388
Accumulated other comprehensive income		6,206	3,182
Deficit		(76,314)	(75,312)
		92,971	90,692
	\$	230,571	\$ 236,424
Subsequent events (notes 4, 7)			
Segmented information (note 11)			

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

Arsenal Energy Inc.

Condensed Interim Consolidated Statements of Income (Loss) and Comprehensive Income

(Unaudited)

For the three months ended March 31,

(thousands of \$Cdn, except per share amounts)		2015	2014
Revenues			
Oil and natural gas	\$	13,866	\$ 27,606
Royalties		(3,569)	(5,421)
Net revenue		10,297	22,185
Realized gain (loss) on risk management contracts		13,128	(1,544)
Unrealized loss on risk management contracts		(12,196)	(1,441)
Net revenue after risk management		11,229	19,200
Expenses			
Operating and transportation		5,997	7,874
General and administrative		1,101	987
Exploration and evaluation		1,666	644
Interest and other financing		536	663
Depletion and depreciation		7,442	6,762
Accretion (note 6)		290	306
Share-based compensation		(988)	920
Foreign exchange gain		(3,220)	(1,142)
		12,824	17,014
Income (loss) before income tax		(1,595)	2,186
Provision for (recovery of) income taxes			
Current		53	171
Deferred		(1,182)	987
		(1,129)	1,158
Net income (loss)	\$	(466)	\$ 1,028
Other comprehensive income			
Translation gain on foreign operations		3,024	948
Comprehensive income	\$	2,558	\$ 1,976
Net income (loss) per share (note 7)			
Basic and diluted	\$	(0.03)	\$ 0.06

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Arsenal Energy Inc.

Condensed Interim Consolidated Statements of Changes in Shareholders' Equity

(Unaudited)

<i>(thousands)</i>	Number of Shares	Share capital	Contributed surplus	Accumulated other comprehensive income (loss)	Deficit	Total Shareholders' equity
Balance December 31, 2013	16,080	\$137,705	\$10,940	\$802	\$(96,575)	\$52,872
Net income for the period	-	-	-	-	1,028	1,028
Dividends	-	-	-	-	(965)	(965)
Issued on exercise of options	10	51	-	-	-	51
Translation gain on foreign operations	-	-	-	948	-	948
Balance March 31, 2014	16,090	\$137,756	\$10,940	\$1,750	\$(96,512)	\$53,934

<i>(thousands)</i>	Number of Shares	Share capital	Contributed surplus	Accumulated other comprehensive income (loss)	Deficit	Total Shareholders' equity
Balance December 31, 2014	17,877	\$151,434	\$11,388	\$3,182	\$(75,312)	\$90,692
Net loss for the period	-	-	-	-	(466)	(466)
Dividends	20	71	-	-	(536)	(465)
Share-based compensation	-	-	186	-	-	186
Translation gain on foreign operations	-	-	-	3,024	-	3,024
Balance March 31, 2015	17,897	\$151,505	\$11,574	\$6,206	\$(76,314)	\$92,971

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

Arsenal Energy Inc.

Condensed Interim Consolidated Statements of Cash flows

(Unaudited)

For the three months ended March 31,

<i>(thousands of \$Cdn)</i>	2015	2014
Operating Activities:		
Net income (loss) for the period	\$ (466)	\$ 1,028
Items not affecting cash:		
Unrealized loss on risk management contracts	12,196	1,441
Depletion and depreciation	7,442	6,762
Accretion of decommissioning obligations (note 6)	290	306
Deferred income taxes	(1,182)	987
Share-based compensation	(988)	920
Unrealized foreign exchange gain	(3,198)	(1,035)
Decommissioning obligations settled (note 6)	(87)	(234)
Net change in non-cash working capital (note 10)	3,102	(2,546)
	17,109	7,629
Financing Activities:		
Bank loan advances (repayments)	(6,449)	1,896
Dividends paid	(465)	(965)
Issue of shares on exercise of stock options	-	20
Net change in non-cash working capital items (note 10)	(134)	-
	(7,048)	951
Investing Activities:		
Property, plant and equipment	(6,671)	(11,913)
Exploration and evaluation assets	-	(276)
Acquisition of properties	-	(152)
Net change in non-cash working capital items (note 10)	(1,976)	5,665
	(8,647)	(6,676)
Foreign exchange gain on cash held in foreign currency	180	95
Change in cash during the period	1,594	1,999
Cash, beginning of period	2,573	1,219
Cash, end of period	\$ 4,167	\$ 3,218
The following are included in cash flow from operating activities:		
Interest paid in cash	505	630
Income taxes paid in cash	\$ 405	\$ 515

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

ARSENAL ENERGY INC

March 31, 2015

Notes to condensed interim consolidated financial statements (Unaudited) **(Tabular amounts in thousands except per share amounts)**

1. Reporting entity:

Arsenal Energy Inc. ("Arsenal" or the "Company") is an oil and gas exploration, development and production Company based in Calgary, Alberta, Canada. The Company conducts its operations in the Western Canadian Sedimentary basin in Canada and the Williston basin in the United States. The condensed interim consolidated financial statements of the Company as at March 31, 2015 comprise the Company and its wholly owned subsidiaries, Arsenal Energy USA Ltd. and Arsenal Energy Holdings Ltd.; which were incorporated in the USA and Canada respectively. Arsenal's principle place of business is located at Suite 1900, 639 – 5th Avenue SW, Calgary Alberta, Canada, T2P 0M9.

2. Basis of preparation:

(a) Statement of compliance:

These condensed interim consolidated financial statements have been prepared by management in accordance with International Financial Reporting Standards ("IFRS") and International Accounting Standard (IAS) 34 *Interim Financial Reporting* as issued by the International Accounting Standards Board ("IASB") and were prepared using accounting policies consistent with IFRS. These condensed interim consolidated financial statements have been prepared following the same accounting policies and methods of computation as the consolidated financial statements and notes for the year ended December 31, 2014 and should be read in conjunction with the audited consolidated financial statements and notes for the year ended December 31, 2014. In the opinion of management, these condensed interim consolidated financial statements contain all adjustments necessary to present fairly Arsenal's financial position as at March 31, 2015 and the results of its operations and its cash flow for the three months then ended.

The condensed interim consolidated financial statements were authorized for issue by the Board of Directors on May 4, 2015.

(b) Basis of measurement:

The condensed interim consolidated financial statements have been prepared on the historical cost basis except for the derivative financial instruments and short term incentive compensation liability.

(c) Functional and presentation currency:

These condensed interim consolidated financial statements are presented in Canadian dollars, which is the parent company's functional currency. Arsenal's subsidiary Arsenal Energy USA Ltd. has a U.S. dollar functional currency.

3. New accounting policies:

The International Accounting Standards Board has issued new standards and amendments to existing standards.

(a) IFRS 11 – Acquisitions of Interest in Joint Operations

(b) IFRS 15 – Revenue from Contracts and Customers

(c) IFRS 9 – Financial Instruments

These changes are not yet adopted by the Company and the effects on our consolidated financial statements are being assessed.

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4. Property, plant and equipment:

Cost or deemed cost	Total
Balance at December 31, 2013	\$ 255,778
Additions	52,187
Acquisitions	152
Transfer from exploration and evaluation assets	1,908
Divestitures	(259)
Capitalized general and administration	860
Decommissioning obligations acquired and incurred	646
Change in decommissioning obligations	7,601
Foreign currency translation	10,520
Balance at December 31, 2014	\$ 329,393
Additions	6,496
Capitalized general and administration	175
Decommissioning obligations incurred	550
Change in decommissioning obligations	17
Foreign currency translation	12,709
Balance at March 31, 2015	\$ 349,340
Accumulated depletion and depreciation	Total
Balance at December 31, 2013	\$ 89,116
Depletion and depreciation provision	31,003
Divestitures	(100)
Foreign currency translation	3,054
Balance at December 31, 2014	\$ 123,073
Depletion and depreciation provision	7,372
Foreign currency translation	4,012
Balance at March 31, 2015	\$ 134,457
NBV	Total
Balance, at December 31, 2014	206,320
Balance, at March 31, 2015	214,883

Subsequent to March 31, 2015 the Company closed deals for the disposition of a portion of the Blackstone exploration and evaluation assets for proceeds of \$500,000 and the disposition of a developed and producing property in the Provost area for proceeds of \$1.2 million.

5. Bank loan:

The credit facility is subject to a semi-annual borrowing base review or redetermination in the event of a material adverse effect. The \$90 million facility was reviewed at November 30, 2014 with no changes to the terms. The next review date is scheduled for completion on or before May 31, 2015 and due to the severe decline in crude prices since the last review date, is expected to be reduced from its current level.

At March 31, 2015, debt under the credit facility amounted to \$53.6 million (December 31, 2014 – \$60.0 million). There were no US dollar denominated borrowings under the credit facility. Interest on the \$80 million facility for Bankers' Acceptances ("BA") and LIBOR loans bear interest at the BA or LIBOR rate plus a margin ranging from 2.0% to 3.5% per annum. Interest on the \$10 million operating facility bears interest at the agent's prime interest rate plus an applicable margin ranging from 1.0% to 2.5% per annum. A standby fee ranging from 0.50% to 0.875% per annum is charged on the unutilized portion of the facility.

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The Company's credit facility has a financial covenant that, without the written consent of the lenders, would result in a breach of the agreement. The Company cannot permit the adjusted working capital ratio, including the unutilized portion of the facility and excluding the value of any risk management contracts, to fall to below 1:1. At March 31, 2015, the Company was in compliance with this covenant.

6. Decommissioning obligations:

	Three months ended March 31, 2015		Year ended December 31, 2014	
Beginning of period	\$	44,729	\$	36,321
Obligations settled		(87)		(1,987)
Obligations disposed		-		(36)
Obligations incurred		550		646
Change in estimates		17		7,601
Foreign currency translation		628		431
Accretion expense		290		1,753
End of period	\$	46,127	\$	44,729
Expected to be incurred within one year	\$	750	\$	750
Expected to be incurred beyond one year	\$	45,377	\$	43,979

7. Share capital:

At March 31, 2015, the Company was authorized to issue an unlimited number of common shares with the holders of common shares being entitled to one vote per share.

(a) Issued

	Three months ended March 31, 2015		Year ended December 31, 2014	
	Number of Shares	Share capital	Number of Shares	Share Capital
Balance, beginning of period	17,877	\$151,434	16,080	\$137,705
Issue of shares, net of costs and premium	-	-	1,712	12,843
Issued on exercise of options	-	-	101	877
Issued on share dividend	20	71	42	358
Repurchase of shares	-	-	(41)	(349)
Cancelled on expiration of exchange provision	-	-	(17)	-
Balance, end of period	17,897	\$151,505	17,877	\$151,434

Dividends

During the three months ended March 31, 2015, the Company declared a quarterly dividend of \$0.03 per share (\$0.12 annualized) that resulted in a cash dividend payment of \$465,325 and a share dividend valued at \$70,994 on February 27, 2015. As at March 31, 2015, there were no dividends payable to shareholders (December 31, 2014 - \$ nil).

At the Company's Board of Directors meeting on May 4, 2015, the Directors declared a quarterly dividend of \$0.02 per common share to shareholders of record on May 15, 2015 to be paid on May 29, 2015.

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(b) Share based payments

Share award incentive plan

There were no grants, vestings, cancellations or forfeitures of share awards during the quarter ended March 31, 2015. As at March 31, 2015 there were 241,200 share awards outstanding.

Share option plan

During the period there were no grants and no exercises. There were 82,967 options either cancelled or expired. As at March 31, 2015 there were 930,837 options outstanding with a weighted average strike price of \$6.51 and 723,551 options exercisable at a weighted average strike price of \$7.18.

(c) Loss per share

The following table shows the weighted average number of common and diluted shares.

	Three months ended March 31, 2015	Three months ended March 31, 2014
Weighted average shares outstanding:		
Basic	17,884	16,090
Diluted	17,884	16,119

In computing diluted income per share for the period ended March 31, 2015, 1,172,037 (2014- 1,033,107) options and share awards were excluded from the dilution calculations as they were anti-dilutive.

(d) Normal course issuer bid:

On March 27, 2014, the Company announced a normal course issuer bid ("NCIB") that commenced April 1, 2014 and ended March 31, 2015. To December 31, 2014, the Company had purchased and cancelled 40,900 common shares at a cost of \$296,164 or \$7.24 per share plus expenses. There were no shares purchased during 2015.

8. Risk management and financial instruments:

Foreign currency exchange rate risk

The Company had no foreign currency exchange contracts in place as at March 31, 2015.

Interest rate risk

The Company had the following interest rate risk management contract in place as at March 31, 2015.

Subject of Contract	Remaining Term	National Quantity	Reference	Strike Price	Option Traded	Fair Value
30 day BA rate	April 1, 2015- February 13, 2018	\$30,000,000	CAD – BA – CDOR	1.50%	Swap	(\$746)

Commodity price risk

The Company had the following commodity risk management contracts in place as at March 31, 2015.

(\$Cdn. unless otherwise noted)

Commodity Sold	Volume Sold	Remaining Term	Pricing	Fair Value
Oil	500 bbl per day	October 1, 2015 – December 31, 2015	\$60.80 USD per bbl	\$ 265
Oil	300 bbl per day	January 1, 2016 – March 31, 2016	\$57.90 USD per bbl	35
				\$ 300

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During January 2015, the Company terminated all oil risk management contracts outstanding at that time for cash proceeds of \$13.1 million.

9. Capital management:

The Company considers its capital structure to include working capital, the credit facility and shareholders' equity. The Company manages its capital base primarily on its net debt to annualized funds from operations ratio and its net debt to equity ratio. The Company continually monitors, through its annual budgeting and quarterly forecasting process, the risk reward profile of its exploration and development projects, its production profile and the economic indicators in the market including commodity prices, interest rates and foreign exchange rates. It then determines increases or decreases to its capital budget and what, if any, additional initiatives may need to be implemented.

Net debt as at March 31,	2015	2014
Working capital deficiency ¹	(3,678)	(3,297)
Bank loan	(53,551)	(70,997)
Net debt ⁵	(57,229)	(74,294)
Annualized funds from operations ^{2,3,4}	\$ 63,041	\$ 44,214
Net debt to annualized funds from operations ratio ⁶	0.91	1.68
Shareholders' equity	\$ 92,971	\$ 53,934
Net debt to equity	0.62	1.38

¹ Excludes the value of risk management contracts.

² Excludes exploration and evaluation expenses.

³ Based on the last quarter's funds from operations annualized.

⁴ Management uses funds from operations before changes in non-cash working capital ("funds flow"), funds flow per common share and annualized funds flow to analyze operating performance and leverage. Funds flow as presented does not have any standardized meaning prescribed by IFRS and therefore it may not be comparable to the calculation of similar measures for other entities. Funds flow as presented is not intended to represent operating cash flow or operating profits for the period nor should it be viewed as an alternative to cash flow provided by operating activities, net earnings or loss or other measures of financial performance calculated in accordance with IFRS.

⁵ Net debt is used by Management to analyze leverage. Net debt does not have any standardized meaning prescribed by IFRS and therefore these terms may not be comparable with the calculation of similar measures for other entities.

⁶ Net debt to annualized funds flow ratio is not comparable with the calculation of the Corporations ratios of twelve months trailing earnings before interest, taxes and depletions and depreciation to consolidated debt.

10. Supplemental cash flow information:

Three months ended March 31,	2015	2014
Change in non-cash working capital items:		
Accounts receivable	\$ 3,981	\$ (1,002)
Prepaid expenses and deposits	166	292
Inventory	93	(120)
Accounts payable and accrued liabilities	(3,248)	3,949
	992	3,119
Amounts relating to operating activities	3,102	(2,546)
Amounts relating to financing activities	(134)	-
Amounts relating to investing activities	(1,976)	5,665
	\$ 992	\$ 3,119

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11. Segmented information:

A portion of the Company's assets and revenues are earned in the United States and Canada, and are monitored as an identifiable reporting segment by management. Business risks and economic indicators are similar across both geographical regions.

March 31, 2015 (000's Cdn. \$)	Canada	U.S.	Total
Oil and gas revenue	7,443	6,423	13,866
Operating income ¹	817	3,483	4,300
Funds from operations ²	13,707	2,053	15,760
Income before income taxes	30	(1,625)	(1,595)
Income after income taxes	519	(985)	(466)
Exploration and evaluation assets	3,639	-	3,639
Property, plant and equipment	109,794	105,089	214,883
Property, plant and equipment expenditures	3,770	2,901	6,671
Exploration and evaluation expenditures	-	-	-

March 31, 2014 (000's Cdn. \$)	Canada	U.S.	Total
Oil and gas revenue	16,031	11,575	27,606
Operating income ¹	6,968	7,343	14,311
Funds from operations ²	6,137	4,916	11,053
Income (loss) before income taxes	398	1,788	2,186
Income (loss) after income taxes	436	592	1,028
Exploration and evaluation assets	9,919	-	9,919
Property, plant and equipment	95,672	79,233	174,905
Property, plant and equipment expenditures	3,696	8,369	12,065
Exploration and evaluation expenditures	276	-	276

(1) Defined as oil and gas revenues less royalties, operating costs and transportation. Operating income does not have any standardized meaning prescribed by IFRS and therefore this term may not be comparable with the calculation of for other entities.

(2) Defined as operating income less general and administrative expenses, interest and financing, plus or minus realized foreign exchange gains or losses expenses. Funds from operations does not have any standardized meaning prescribed by IFRS and therefore this terms may not be comparable with the calculation for other entities.