



## Management's Discussion and Analysis

### Three and nine months ended September 30, 2015

Strategic Oil & Gas Ltd. ("Strategic" or the "Company") is a publicly-traded oil and gas exploration and production company, with operations focused on light oil development in northern Alberta. The following is management's discussion and analysis ("MD&A") of Strategic's consolidated operating and financial results for the three and nine months ended September 30, 2015, as well as information concerning the Company's future outlook based on currently available information. The MD&A was approved and authorized for issue by Strategic's board of directors on November 13, 2015. This MD&A should be read in conjunction with the Company's interim condensed consolidated financial statements for the three and nine months ended September 30, 2015 and 2014, together with the accompanying notes, which have been prepared in accordance with International Financial Reporting Standards ("IFRS").

#### FINANCIAL AND OPERATIONAL SUMMARY

	Three months ended September 30			Nine months ended September 30		
	2015	2014	% change	2015	2014	% change
<b>Financial (\$thousands, except per share amounts)</b>						
Oil and natural gas sales <sup>(1)</sup>	7,783	19,394	(60)	29,146	64,148	(55)
Funds from operations <sup>(2)</sup>	1,122	2,774	(60)	6,015	7,300	(18)
Per share basic & diluted <sup>(2)</sup>	-	0.01	-	0.01	0.02	(50)
Cash provided by (used in) operating activities	4,235	791	435	2,080	5,267	(61)
Per share basic & diluted	0.01	-	-	-	0.01	-
Net loss	(63,918)	213	-	(78,327)	(12,170)	544
Per share basic & diluted	(0.12)	-	-	(0.14)	(0.04)	288
Capital expenditures (excluding acquisitions)	1,401	24,871	(94)	9,475	76,864	(88)
Net acquisitions (dispositions)	-	-	-	-	(3,821)	-
Bank debt (comparative figure is as of December 31, 2014)	52,000	29,016	79	52,000	29,016	79
Net debt (comparative figure is as of December 31, 2014) <sup>(2)</sup>	53,791	48,399	11	53,791	48,399	11
<b>Operating</b>						
Average daily production						
Crude oil (bbl per day)	1,608	2,023	(21)	1,970	2,225	(11)
Natural gas (mcf per day)	3,028	7,264	(58)	3,873	6,491	(40)
Barrels of oil equivalent (boe per day)	2,113	3,234	(35)	2,615	3,307	(21)
Average prices						
Oil & NGL, before risk management (\$ per bbl)	46.72	88.51	(47)	48.34	91.64	(47)
Oil & NGL, including risk management (\$ per bbl)	52.90	78.27	(32)	56.20	79.95	(30)
Natural gas, before risk management (\$ per mcf)	3.13	4.37	(28)	2.98	4.79	(38)
Natural gas, including risk management (\$ per mcf)	3.12	4.34	(28)	2.98	4.53	(34)
Netback (\$ per boe) <sup>(2)</sup>						
Oil and natural gas sales <sup>(1)</sup>	40.04	65.18	(39)	40.82	71.06	(43)
Royalties	(6.04)	(14.76)	(59)	(4.47)	(15.64)	(71)
Operating expenses	(21.96)	(22.76)	(3)	(22.75)	(26.88)	(15)
Transportation expenses <sup>(1)</sup>	(0.70)	(2.55)	(72)	(1.14)	(3.40)	(67)
Operating Netback	11.34	25.11	(55)	12.46	25.14	(50)
<b>Common Shares (thousands)</b>						
Common shares outstanding, end of period	542,319	524,927	3	542,319	524,927	3
Weighted average common shares (basic)	542,319	362,719	50	542,319	328,858	65
Weighted average common shares (diluted)	542,319	362,719	50	542,319	328,858	65

<sup>(1)</sup> In 2015, revenues are presented net of pipeline tariffs on oil sales which occur after title to the product has passed to the customer. Prior period amounts for revenue and transportation have been reclassified to conform to the current period presentation

<sup>(2)</sup> Funds from operations, net debt and operating netback are non-IFRS measurements; see "Non-IFRS Measurements" in this MD&A.

## OPERATIONAL AND FINANCIAL SUMMARY

Strategic has continued to identify operational efficiencies and exercise capital discipline in this low commodity price environment. WTI oil prices for the current quarter decreased 52% compared to the same period in 2014, resulting in a 47% decrease in average sale prices.

- Funds from operations of \$1.1 million were 60% lower than the third quarter of 2014, as significantly lower commodity prices were partly offset by lower operating costs, royalty rates, transportation costs and a realized gain on risk management contracts of \$0.9 million. The net loss for the quarter was \$63.9 million or \$0.12 per common share, primarily due to an impairment charge of \$60.0 million related to a substantial reduction in current and forward oil prices.
- Strategic had a \$57.0 million credit facility at September 30, 2015, consisting of a \$40 million revolving operating loan and a \$17.0 million non-revolving facility that is reduced at a rate of \$0.5 million per month (\$16.0 million as of November 1, 2015). Subsequent to the reporting period, Strategic executed a term sheet with the lender to amend its credit facility. Upon amendment, the Company will continue to reduce the non-revolving facility by \$0.5 million per month and is required to repay additional amounts as follows:
  - \$9.5 million on or before February 1, 2016
  - The balance of the non-revolving facility on or before June 1, 2016

In conjunction with the term sheet, the Company is also required to raise \$40.0 million in capital subordinated to the lender on or before June 1, 2016, with a minimum of \$25.0 million raised prior to February 1, 2016, and drill 2 wells before March 31, 2016, primarily to retain certain undeveloped lands at Marlowe with prospective Muskeg rights.

- In order to provide short-term capital to fund the Company's working capital deficiency, credit facility repayments and initiate the land retention drilling program required by its lender, Strategic has obtained a \$10.0 million loan from an entity which is a significant shareholder in the Company and controlled by the Chairman of the Board of Directors. The loan bears interest at 1% per month up to March 31, 2016 and 1.5% per month thereafter and is repayable on the earlier of the closing of a raise of junior capital or June 30, 2016. The loan is convertible at the option of the holder into common shares of the Company at a conversion price which is the lesser of \$0.115 per common share or a price per common share that is the issue price of the common shares issued on any equity raise on or before March 1, 2016.
- Operating netbacks decreased 55 percent to \$11.34/boe for the three months ended September 30, 2015 from \$25.11/boe for the comparative period in 2014, as the 39% drop in oil & gas revenues per boe was partially mitigated by lower royalty rates, operating and transportation expenses. The Company has made significant strides in reducing costs at Marlowe to limit the effect of low oil prices and reduced production volumes on operating netbacks. At \$21.97/boe, unit operating costs for the third quarter are lower than the third quarter of 2014 (\$22.76/boe) and the second quarter of 2015 (\$25.21/boe) despite being spread over a smaller production volume. Operating costs at Marlowe were \$17.94/boe for the third quarter of 2015, leading to an operating netback of \$14.66/boe.
- Capital expenditures of \$1.4 million for the third quarter of 2015 reflected a 94% decrease from the third quarter of 2014.

- Average daily production totaled 2,113 boe/d for the three months ended September 30, 2015 compared to 2,480 boe/d for the second quarter of 2015 as 250 boe/d of Muskeg production was offline due to pump upgrades required and temporary regulatory production restrictions during the period. The regulatory restrictions were removed in October and the Company's current production is approximately 2,200 boe/d.

Strategic's Board of Directors has initiated a process to identify, examine and consider funding alternatives available to raise capital, manage the credit facility repayments and enhance shareholder value. Alternatives may include, but are not limited to, identification and negotiation with alternative debt providers, the raising of additional capital via private or public share placement, recapitalization, the sale of the Company, merger, joint venture or other business combination, the sale of all or a portion of the Company's assets, or any combination thereof. Management and the Board of Directors are committed to acting in the best interests of the Company and its stakeholders. RBC Capital Markets has been retained as financial advisor to assist the Company with this process.

It is the Company's current intention not to disclose developments with respect to the review process until the Board of Directors has approved a specific transaction or otherwise determines that disclosure is necessary or appropriate. The Company will provide quarterly financial and material operational updates. The Company cautions that there are no assurances or guarantees that the process will result in a transaction or, if a transaction is undertaken, the terms or timing of such a transaction.

### **Going Concern**

Strategic's interim condensed consolidated financial statements as at and for the three and nine months ended September 30, 2015 have been prepared using the going concern basis of presentation, which assumes that the Company will continue in operation for the foreseeable future and will be able to realize its assets and discharge its liabilities and commitments in the normal course of business. For the quarter ended September 30, 2015, the Company reported a net loss of \$63.9 million. At September 30, 2015, the Company had negative working capital of \$52.8 million and an accumulated deficit of \$279.3 million. The Company is required to repay \$16 million in bank debt prior to June 1, 2016 and will need to obtain financing to fund this repayment. Strategic's cash flows and compliance with debt covenants are highly dependent on realized oil prices. Sustained low commodity prices will significantly reduce the Company's cash flows, resulting in significant doubt upon the Company's ability to continue as a going concern.

The interim condensed consolidated financial statements do not reflect adjustments that would be necessary if the going concern basis was not appropriate. The appropriateness of the going concern basis is dependent upon, among other things, the ability to obtain debt or equity financing, a joint venture or a sale of assets in order to have sufficient funds to meet its obligations that enables the Company to continue as a going concern, the ability to generate sufficient cash from operations and future profitable operations.

## OUTLOOK

Strategic curtailed drilling activities in early 2015 and is maintaining capital discipline during the current low commodity price environment, but continues to believe in the potential profitability of its conventional Muskeg light oil resource at Marlowe. Strategic is focused on streamlining operations and is encouraged by continued strong netbacks at Marlowe in 2015 (\$14.66/boe for the third quarter and \$18.42/boe for the first nine months) despite low oil prices. Due to the high fixed-cost nature of the Marlowe asset, operating netbacks trend upwards with additional production volumes, and the Company has a substantial drilling inventory on its extensive land base in the area.

Strategic is evaluating alternatives to proactively manage the repayment of the non-revolving portion of its credit facility and obtain additional capital to recommence the Muskeg development, and has retained a financial advisor to assist with this process.

### About Strategic

Strategic is a junior oil and gas company committed to becoming a premier northern oil and gas operator by exploiting its light oil assets primarily in northern Alberta. The Company relies on its extensive subsurface and reservoir experience to develop its asset base and grow production and cash flows while managing risk. The Company maintains control over its resource base through high working interest ownership in wells, construction and operation of its own processing facilities and a significant undeveloped land and opportunity base. Strategic's primary operating area is at Marlowe, Alberta.

## RESULTS OF OPERATIONS

### Production

Average daily production volumes	Three months ended September 30		Nine months ended September 30	
	2015	2014	2015	2014
Oil & NGL (bbl/d)	1,608	2,023	1,970	2,225
Natural gas (mcf/d)	3,028	7,264	3,873	6,491
Total (boe/d)	2,113	3,234	2,615	3,307

Average daily oil & NGL production for the three and nine months ended September 30, 2015 decreased 21% and 11% respectively from the comparative periods in 2014, as a result of the shut-in of 180 bbl/d of oil production at Cameron Hills in February 2015, the sale of 40 bbl/d of NGL production in central Alberta in June 2014 and a lack of drilling activity in the current year to replace production declines at Marlowe.

Natural gas production volumes for the three and nine months ended September 30, 2015 decreased 58% and 40%, respectively from the comparative periods in 2014 primarily due to the shut-in of 3 MMcf/d natural gas volumes at Bistcho and Cameron Hills in February 2015, as well as a lack of drilling activity at Marlowe.

## Revenue

(\$thousands, except where noted)	Three months ended September 30		Nine months ended September 30	
	2015	2014	2015	2014
Sales				
Oil & NGL <sup>(1)</sup>	<b>6,911</b>	16,476	<b>25,998</b>	55,658
Natural gas	<b>872</b>	2,918	<b>3,148</b>	8,490
Oil and natural gas sales	<b>7,783</b>	19,394	<b>29,146</b>	64,148
Unrealized gain (loss) on risk management contracts	<b>860</b>	6,758	<b>(2,472)</b>	4,162
Realized gain (loss) on risk management contracts	<b>912</b>	(2,072)	<b>4,230</b>	(7,554)
	<b>9,555</b>	24,080	<b>30,904</b>	60,756
Average prices <sup>(2)</sup>				
Oil & NGL, before realized gain (loss) on risk management contracts (\$/bbl)	<b>46.72</b>	88.51	<b>48.34</b>	91.64
Oil & NGL, including realized gain (loss) on risk management contracts (\$/bbl)	<b>52.90</b>	78.27	<b>56.20</b>	79.95
Natural gas, before realized gain (loss) on risk management contracts (\$/mcf)	<b>3.13</b>	4.37	<b>2.98</b>	4.79
Natural gas, including realized gain (loss) on risk management contracts (\$/mcf)	<b>3.12</b>	4.34	<b>2.98</b>	4.53
Price per boe before realized gain (loss) on risk management contracts (\$/boe)	<b>40.04</b>	65.18	<b>40.82</b>	71.06
Reference prices				
Oil – WTI (\$US/bbl)	<b>46.43</b>	97.17	<b>51.00</b>	99.61
Natural gas – AECO Daily Index (\$/MMBtu)	<b>2.89</b>	4.00	<b>2.76</b>	4.78

<sup>(1)</sup> In 2015, revenues are presented net of pipeline tariffs on oil sales which occur after title to the product has passed to the customer. Prior period amounts for revenue and transportation have been reclassified to conform to the current period presentation.

<sup>(2)</sup> Average prices do not include unrealized losses on risk management contracts.

Average oil prices received are a function of the benchmark West Texas Intermediate (“WTI”) oil price, less foreign exchange, transportation and quality differentials to arrive at Canadian dollar price received at delivery points in northern Alberta. WTI oil prices weakened in the third quarter of 2015 relative to the second quarter, and remained well below 2014 prices as a result of the ongoing global imbalance between supply and demand for crude oil. Strategic’s average oil price for the third quarter of 2015 decreased by 47% from the corresponding period in 2014 due to a 52% decrease in WTI oil prices, partially mitigated by a higher CDN/US foreign exchange rate. Substantially all of the Company’s natural gas is sold at the AECO Daily Index price, adjusted for fuel charges. Strategic’s average natural gas prices for the third quarter of 2015 decreased by 28% from the corresponding period in 2014, in line with lower AECO Daily Index prices.

The Company’s oil and natural gas revenues decreased to \$7.8 million and \$29.1 million for the three and nine months ended September 30, 2015 from \$19.4 million and \$64.1 million for the respective comparative periods in 2014. The decrease was due to a substantial decline in commodity prices and lower production levels stemming from a lack of drilling and recompletion activities in 2015.

## Risk management contracts

The Company's net income and funds from operations are exposed to fluctuations in commodity prices, interest rates and foreign exchange rates. As part of its risk management program, Strategic may enter into financial commodity price management contracts for up to 60 percent of expected production levels, depending on current commodity prices, price volatility and the size and nature of the Company's capital spending programs.

Strategic's risk management program resulted in realized gains on oil and natural gas contracts of \$0.9 million or \$4.69/boe for the current quarter and \$4.2 million or \$5.88/boe for the first nine months of 2015 (three and nine months ended September 30, 2014 - \$2.1 million and \$7.6 million realized losses, respectively). A summary of Strategic's commodity price risk management contracts as at September 30, 2015 is as follows:

### Financial WTI crude oil contracts

Term		Contract Type	Volume (bbl/d)	Fixed (Cdn\$/bbl)	Price Index
01-Jul-2015	31-Dec-2015	Option <sup>(1)</sup>	250	\$90.00	WTI – NYMEX
01-Jul-2015	31-Dec-2015	Swap	500	USD \$61.65	WTI – NYMEX

<sup>(1)</sup> Counterparty has an option to convert into a swap at the fixed price indicated. The 250 bbl/d option expires monthly during the contract term.

### Financial AECO gas contracts

Term		Contract Type	Volume (GJ/d)	Fixed Price (\$/GJ)	Index
01-Apr-2015	31-Oct-2015	Swap	300	2.70	AECO Daily
01-Jun-2015	31-Oct-2015	Swap	200	2.70	AECO Daily

Unrealized gains and losses on risk management contracts are related to changes in the unrealized portion of the Company's risk management position, as well as fluctuations in the forward price curves for oil and natural gas. Strategic recorded an unrealized gain on risk management contracts of \$0.9 million and an unrealized loss of \$2.5 million for the three and nine months ended September 30, 2015 (gain of \$6.8 million and \$4.2 million for the three and nine months ended September 30, 2014, respectively). Strategic employs risk management contracts in order to mitigate commodity price volatility and protect cash flows. Although Strategic believes its risk management program provides an effective hedge against WTI and AECO price volatility for a portion of the Company's production volumes, the Company does not follow hedge accounting for these contracts. As a result, the contracts are marked to market at each reporting date, with the change in market value included in net income (loss) for the period.

## Royalties

(\$thousands, except where noted)	Three months ended September 30		Nine months ended September 30	
	2015	2014	2015	2014
Crown royalties	1,079	4,208	2,894	13,443
Freehold and overriding royalties	96	184	301	672
Total royalties	1,175	4,392	3,195	14,115
Per boe	6.04	14.76	4.47	15.64
Percentage of oil and natural gas sales	15.1%	22.6%	11.0%	22.0%

Royalty expense consists of royalties paid to provincial governments (including the effect of the Crown royalty initiative program), freehold land owners and overriding royalty owners. Royalty expense also includes the impact of gas cost allowance, which is the reduction of natural gas royalties payable to the Government of Alberta to recognize capital and operating expenditures incurred in the gathering and processing of its royalty share of production. Crown royalties on oil production are paid in product, which is taken in kind and marketed separately by the provincial government. Royalty rates in western Canada vary based on volume produced by individual wells, market oil prices and the area the production is derived from. Revenues from newly drilled wells benefit from a crown royalty reduction to five percent for the first year of production, up to a maximum of 500,000 Mcf of natural gas or 50,000 bbls of crude oil for a well up to 2,500 metres of total depth. The time frame and maximum production amounts are increased by six months and 100,000 Mcf or 10,000 bbls for each additional 500 metres of total depth. Strategic's wells are typically from 2,500 to 3,100 metres in total depth.

Royalties decreased to \$1.2 million and \$3.2 million for the three and nine months ended September 30, 2015 from \$4.4 million and \$14.1 million, respectively for the comparative periods in 2014 due to lower oil pricing used by the provincial government to calculate royalty rates, as well as reduced well productivity for older Keg River production at Marlowe and a higher portion of oil and natural gas sales derived from Muskeg wells drilled in the past 12-18 months, which benefit from the lower crown royalty rate. The royalty rate in the current period was higher than the 9.5% average rate for the first half of 2015 as certain high productivity Muskeg wells have reached maximum production levels and royalty rates for these wells increased from 5% to approximately 25-30%.

At current oil and gas prices, crown royalty rates on natural gas are 5-10%, compared to rates of 0-40% for Marlowe oil production, depending on well productivity and vintage.

### Operating and transportation costs

(\$thousands, except per boe amounts)	Three months ended September 30		Nine months ended September 30	
	2015	2014	2015	2014
Operating costs	4,269	6,772	16,245	24,271
Transportation costs <sup>(1)</sup>	137	759	813	3,072
	4,406	7,531	17,058	27,343
Per boe				
Operating	21.96	22.76	22.76	26.88
Transportation	0.70	2.55	1.14	2.87
	22.67	25.31	23.89	30.29

<sup>(1)</sup> In 2015, revenues are presented net of pipeline tariffs on oil sales which occur after title to the product has passed to the customer. Prior period amounts for revenue and transportation have been reclassified to conform to the current period presentation

Operating costs decreased to \$4.3 million or \$21.96/boe for the three months ended September 30, 2015 from \$6.8 million or \$22.76/boe for the third quarter of 2014, and to \$16.2 million or \$22.76/boe for the first nine months of 2015 from \$24.3 million or \$26.88/boe in 2014 as the Company made significant changes to its cost structure in 2015, including shutting in non-economic properties and reducing maintenance expenditures and field staff. The effect of these savings on unit operating costs was partially mitigated by the decline in production volumes caused by the shut-in of Bistcho/Cameron Hills and a lack of drilling activity in 2015.

Operating costs were \$1.4 million lower than the second quarter of 2015 due to reductions in workovers, labor costs, chemicals and property taxes, as well as a \$0.5 million prior period charge incurred in the previous quarter.

Unit transportation costs decreased from \$2.55/boe and \$2.87/boe for the three and nine months ended September 30, 2014 to \$0.70/boe and \$1.14/boe for the third quarter and first nine months of 2015 respectively, due to the elimination of oil sales by rail in January 2015 (and associated trucking costs) and the shut-in of production at Bistcho/Cameron Hills in February 2015.

## Netbacks

(\$/boe)	Three months ended September 30		Nine months ended September 30	
	2015	2014	2015	2014
Revenue <sup>(1)</sup>	<b>40.04</b>	65.18	<b>40.82</b>	71.06
Royalties	<b>(6.04)</b>	(14.76)	<b>(4.47)</b>	(15.64)
Operating costs	<b>(21.97)</b>	(22.76)	<b>(22.75)</b>	(26.88)
Transportation costs <sup>(1)</sup>	<b>(0.70)</b>	(2.55)	<b>(1.14)</b>	(3.40)
<b>Operating netback</b>	<b>11.33</b>	25.11	<b>12.46</b>	25.14

<sup>(1)</sup> In 2015, revenues are presented net of pipeline tariffs on oil sales which occur after title to the product has passed to the customer. Prior period amounts for revenue and transportation have been reclassified to conform to the current period presentation.

Strategic's operating netback decreased to \$11.33/boe and \$12.46/boe for the three and nine months ended September 30, 2015 from \$25.11/boe and \$25.14/boe respectively for the comparative periods in 2014, mostly due to the substantial drop in commodity prices. The third quarter decrease in commodity price of \$25.14/boe from the same period in 2014 was partially offset by lower royalties rate (\$8.72/boe) due to lower production and oil pricing, lower operating costs (\$0.79/boe), despite the fact the these costs were spread over smaller production volumes, as well as a reduction in transportation costs (\$1.85/boe) due to the elimination of rail transportation.

Strategic's focus area is Marlowe, which is 100% owned and operated by the Company. The Marlowe assets generated a netback of \$14.66/boe despite low commodity prices in the third quarter. The corporate netback is negatively affected by low netbacks at the Company's minor oil properties and fixed costs at Bistcho/Cameron Hills, which was shut in earlier in 2015 due to low commodity prices. The breakdown of Strategic's operating netback for the three months ended September 30, 2015 is as follows:

<b>Operating netback (\$/boe)</b>	Marlowe	Other	Total
Revenue	39.51	50.49	<b>40.04</b>
Royalties	(6.22)	(2.63)	<b>(6.04)</b>
Operating costs	(17.94)	(101.31)	<b>(21.97)</b>
Transportation costs	(0.69)	(0.94)	<b>(0.70)</b>
<b>Operating netback</b>	<b>14.66</b>	<b>(54.39)</b>	<b>11.33</b>

## General and administrative expense

(\$thousands, except per boe amounts)	Three months ended September 30		Nine months ended September 30	
	2015	2014	2015	2014
General and administrative expense	<b>1,258</b>	1,564	<b>5,091</b>	5,159
Per boe	<b>6.47</b>	5.26	<b>7.13</b>	5.72

General and administrative ("G&A") expense for the current quarter decreased to \$1.3 million from \$1.6 million for the third quarter of 2014 due to a lower staff count and reduced consulting and professional fees, partially offset by a reduction in overhead recoveries related to the shut-in of Bistcho/Cameron Hills in February 2015 and lower capitalized G&A. For the nine months ended September 30, 2015 G&A expense decreased to \$5.1 million from \$5.2 million for the comparative period in the prior year, despite lower overhead recoveries and a \$0.5 million charge for severance costs related to staff reductions in the first quarter of 2015.



## Finance expense

(\$thousands, except per boe amounts)	Three months ended September 30		Nine months ended September 30	
	2015	2014	2015	2014
Interest expense	734	1,061	2,017	2,677
Accretion expense	286	363	839	920
Total	1,020	1,424	2,856	3,597

Interest expense reduced to \$0.7 million in the third quarter of 2015 from \$1.1 million for the comparative quarter in 2014 due to lower bank debt balances. For the nine months ended September 30, 2015 interest expense decreased to \$2.0 million from \$2.7 million in 2014 due to a decrease in average bank debt, partially mitigated by higher interest rates on the non-revolving portion of the Company's credit facility.

Accretion expense is a reflection of an increase in Strategic's discounted decommissioning liability due to the passage of time. Accretion expense was slightly lower for the third quarter of 2015 compared to the same period in 2014 mostly attributable to lower discount rates.

## Stock based compensation

Stock based compensation is a non-cash charge which reflects the estimated value of stock options granted. The Company uses the fair value method of accounting for stock options granted to directors, officers, employees and consultants. The fair value of all stock options granted is recorded as a charge to net loss over the period from the grant date to the vesting date of the option. The fair value of common share options granted is estimated on the date of grant using the Black-Scholes options pricing model.

For the third quarter and first nine months of 2015 the Company incurred \$0.1 million and \$0.3 million in stock based compensation expense, a decrease from \$0.5 million and \$0.8 million for the corresponding periods in 2014. There have been no significant issuances of stock options in 2015 to date.

## Depletion, depreciation, amortization and exploration costs

(\$thousands, except per boe amounts)	Three months ended September 30		Nine months ended September 30	
	2015	2014	2015	2014
Depreciation, depletion and amortization ("DD&A")	5,088	8,555	19,177	25,671
Per boe	26.18	28.75	26.86	28.44

DD&A is computed individually for each producing area on a unit of production basis, using proved and probable reserves and including future development expenditures in the cost base subject to depletion. DD&A expense also includes amortization of undeveloped land costs. Major components, such as facilities and pipelines, are separated from oil and gas properties and depreciated on a straight-line basis over their estimated useful lives. DD&A expense decreased to \$5.1 million and \$19.2 million for the three and nine months ending September 30, 2015 from \$8.6 million and \$25.7 million, respectively for the 2014 periods as a result of lower production levels in 2015.

Exploration expense for the current period of \$0.4 million relates to E&E costs in the Bistcho/Cameron Hills cash generating unit (CGU), where there are currently no plans for future exploration.

## Impairment

The Company's exploration, development and production assets are aggregated into CGUs based on their ability to generate largely independent cash flows.

The December 31, 2014 reserve volumes and values were evaluated by the Company's independent reserve evaluators. At September 30, 2015 the decline in forward commodity prices compared to December 2014 was an indicator of potential impairment.

The recoverable value of each CGU was estimated as the fair value less cost to sell based on the net present value of before tax cash flows (discounted at 10%) from crude oil and natural gas proved plus probable reserves originally estimated by the Company's third party reserve evaluators, internally updated for production since December 31, 2014, plus an internal estimate of incremental drilling locations. The value of resources incremental to the reserve report was further supported by contingent resource studies compiled by independent reserve engineers and discounted at a rate of 15%.

In determining impairment, the Company considered various estimates, including: future pricing, timing of capital expenditures, impact of changes in cost structures. Forecast benchmark prices and exchange rates were as follows:

	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025+
WTI crude oil (US\$/bbl)	50.00	55.00	61.20	65.00	69.00	73.10	77.30	81.60	86.20	87.90	89.60
Edmonton CS (CAD\$/bbl)	60.68	67.40	73.40	78.10	80.90	86.00	91.10	96.40	102.00	104.00	106.00
AECO Gas Price (CAD\$/mcf)	2.90	3.35	3.65	3.85	4.00	4.25	4.45	4.70	5.00	5.10	5.20

It was determined that the carrying value of certain CGU's exceeded the recoverable value and a \$60.0 million (December 31, 2014 - \$114.0 million) impairment was recognized. The impairment specifically relates to Steen/Marlow CGU (\$54.4 million), Bistcho CGU (\$4.5 million) and other Canadian CGU (\$1.1 million). The impairment recorded reflects the Company's best estimates based on currently available information.

At December 31, 2015, in conjunction with the December reserve report from the independent reserve evaluators, the Company will review the aforementioned estimates to determine any future potential impairment or reversal.

### Funds from operations and net loss

(\$thousands, except per share amounts)	Three months ended September 30		Nine months ended September 30	
	2015	2014	2015	2014
Funds from operations	1,122	2,774	6,015	7,300
Per share – basic & diluted	-	0.01	0.01	0.02
Cash provided by (used in) operating activities	4,235	791	2,080	5,267
Net income (loss) for the period	(63,918)	213	(78,327)	(12,170)
Per share – basic & diluted	(0.12)	-	(0.14)	(0.04)

Funds from operations decreased to \$1.1 million in the three months ended September 30, 2015 from \$2.8 million for the same period in 2014 and to \$6.0 million for the current nine month period from \$7.3 million for the nine months ended September 30, 2014, primarily due to low oil prices. Strategic implemented a series of cost-cutting initiatives in early 2015 to reduce cash costs and mitigate the impact of commodity declining commodity prices. This included shutting in uneconomic assets, and trimming office and field staff as well as maintenance expenses. Funds from operations also benefited from realized risk management gains of \$0.9 million and \$4.2 million for the three and nine month periods in 2015 compared to risk management losses of \$2.1 million and \$7.6 million for the third quarter and first nine months of 2014, respectively.

Cash flow provided by operating activities totaled \$4.2 million for the current period compared to \$0.8 million for the third quarter of 2014, as the Company held significant oil inventories in 2014 due to the short term shut-down of a third party sales pipeline. Cash flow provided by (used in) operating activities dropped to \$2.1 million for the first nine months of 2015 compared to \$5.3 million for the same period in 2014 due to \$4.4 million in expenditures on decommissioning liabilities to date in 2015, primarily related to the remediation of a prior year pipeline spill at Marlowe.

Net loss increased to \$63.9 million (\$0.12 per basic and diluted common share) for the three months ended September 30, 2015 from net income of \$0.2 million for the comparative quarter in 2014 due to an impairment charge of \$60.0 million and lower funds from operations due to lower current and forward oil prices. Net loss for the first nine months of 2015 increased to \$78.3 million (\$0.14 per basic and diluted common share) from \$12.2 million (\$0.04 per basic and diluted common share) in 2014 as a result of impairment charges, reduced oil prices and a valuation allowance of \$1.1 million related to an insurance receivable.

### Capital expenditures

(\$thousands)	Three months ended September 30		Nine months ended September 30	
	2015	2014	2015	2014
Drilling, completions and equipping	970	18,823	8,567	42,321
Pipelines and facilities	380	5,910	702	31,969
	1,350	24,733	9,269	74,290
Proceeds on disposal	-	-	-	(3,821)
Total property, plant and equipment	1,350	24,733	9,269	70,469
Total exploration and evaluations	51	138	206	2,574
Total capital expenditures	1,401	24,871	9,475	73,043

Capital expenditures decreased significantly to \$1.4 million and \$9.5 million for the third quarter and first nine months of 2015, respectively from \$24.9 million and \$73.0 million for the comparative periods in 2014 as the decline in commodity prices restricted Strategic's cash flows and the borrowing base on the Company's credit facility. Current quarter expenditures were limited to minor well equipping and facilities costs.

In February 2015 Strategic had provided guidance of \$11 million in capital expenditures for the first six months of 2015. Actual capital expenditures were \$8.1 million as the Company elected to preserve capital rather than conduct recompletion and workover activities on certain low-productivity wells at Marlowe.

### Decommissioning Liabilities

Decommissioning liabilities decreased to \$53.6 million at September 30, 2015 from \$54.9 million at December 31, 2014 primarily due to \$4.4 million in decommissioning expenditures during the first nine months of 2015. Approximately \$3.1 million of the expenditures relate to remediation of a prior year pipeline spill at Marlowe. As the pipeline spill was claimed under the Company's insurance policy coverage, a receivable of \$2.6 million has been recorded on the balance sheet as at September 30, 2015 (December 31, 2014 - \$3.7 million) representing the cost of remediation work completed in the first quarter of 2015 and ongoing monitoring costs, that are virtually certain to be recovered, of which \$1.8 million is included in current assets and \$0.8 million in long-term receivables. A valuation allowance of current receivables in the amount of \$1.1 million was recorded in the second quarter of 2015 based on preliminary discussions with the Company's insurers. On November 3, 2015, a \$1.9 million interim payment was received from the insurer.

The Company estimates that an additional \$5.3 million in remediation costs will be incurred to fully restore the affected area to its original condition and has included this estimate in decommissioning liabilities. Whether costs incurred related to the remediation are reimbursed by the Company's insurer will depend on the language and interpretations of such in the Company's insurance policy, as well as the specific activities undertaken. The Company does not intend to complete the restoration project in the next 12 months. Any insurance receivables that are related to future remediation costs will be recorded as claims are submitted to and approved by the Company's insurer.

## SUMMARY OF QUARTERLY FINANCIAL DATA

The following table summarizes quarterly financial results:

Quarter ended (\$thousands, except where noted)	Sept 30, 2015	Jun 30, 2015	Mar 31, 2015	Dec 31, 2014
Oil and natural gas sales	7,783	10,942	10,422	18,790
Net income (loss)	(63,918)	(5,797)	(8,610)	(117,321)
Net income (loss) per share – basic & diluted	(0.12)	(0.01)	(0.02)	(0.22)
Average daily production (boed)	2,113	2,480	3,267	3,925
Average price (\$/boe)	40.04	48.49	35.45	52.04

Quarter ended (\$thousands, except where noted)	Sept 30, 2014	Jun 30, 2014	Mar 31, 2014	Dec 31, 2013
Oil and natural gas sales	19,394	23,384	21,370	15,377
Net income (loss)	213	(2,717)	(9,664)	(9,852)
Net income (loss) per share – basic & diluted	0.00	(0.01)	(0.04)	(0.04)
Average daily production (boed)	3,234	3,538	3,147	2,847
Average price (\$/boe)	65.18	72.61	73.82	58.72

Oil and natural gas sales are a function of average daily production levels, the oil/gas production mix and commodity prices and decreased significantly with reduced production levels and lower oil prices in the first and second quarters of 2015. Sales were highest in the first and second quarters of 2014 as average realized prices are over \$70/boe for those periods. Conversely, sales are lower in the first three quarters of 2015 due to reduced production volumes and low oil prices.

Net income (loss) varies with funds from operations, as well as non-cash expenses incurred such as unrealized losses and gains on risk management contracts, DD&A and impairment. Net losses are high in the fourth quarter of 2014 and third quarter of 2015 due to impairment charges of \$114.0 million and \$59.9 million, respectively. The Company realized net income of \$0.2 million for the three months ended September 30, 2014 due to a realized gain on risk management contracts of \$6.8 million. Maintaining positive net income on a consistent basis will depend on the Company's ability to increase production and reduce unit production costs and DD&A, as well as on an increase in commodity prices.

## LIQUIDITY AND CAPITAL RESOURCES

The Company considers its capital structure to include shareholders' equity and working capital, including bank debt. The objectives of the Company are to maintain a strong balance sheet affording the Company financial flexibility to achieve goals of continued growth and access to capital. In order to maintain or adjust the capital structure, the Company may issue new common shares, issue or repay debt, or adjust exploration and development capital expenditures. The Company monitors its capital structure based on net debt and adjusted working capital (deficiency), as calculated below:

(\$thousands)	September 30, 2015	December 31, 2014
Current assets (excluding risk management contracts)	7,312	11,439
Accounts payable and accruals	(8,728)	(26,815)
Current decommissioning liabilities	(375)	(4,007)
Adjusted working capital (deficiency)	(1,791)	(19,383)
Bank indebtedness	(52,000)	(29,016)
Net debt	(53,791)	(48,399)

Strategic had a \$57.0 million credit facility at September 30, 2015, consisting of a \$40 million revolving operating demand loan and a \$17.0 million non-revolving facility that is reduced at a rate of \$0.5 million per month (\$16.0

million as of November 1, 2015). Subsequent to the reporting period, Strategic executed a term sheet with the lender to amend its credit facility. Upon amendment, the Company will continue to reduce the non-revolving facility by \$0.5 million per month and is required to repay additional amounts as follows:

- \$9.5 million on or before February 1, 2016
- the balance of the non-revolving facility on or before June 1, 2016

The Company is also required to raise \$40.0 million in capital subordinated to the lender on or before June 1, 2016, with a minimum of \$25.0 million raised prior to February 1, 2016, and drill 2 wells before March 31, 2016, primarily to retain certain undeveloped lands.

Amounts outstanding under the amended revolving facility are repayable on demand, and bear interest at a rate of 3.0% over the bank's prime lending rate. Amounts due under the non-revolving facility bear interest at a rate of 2.0% above the interest rates on the revolving facility. The Facility is secured by a general security agreement including a floating charge on all property, plant and equipment. The Facility contains a financial covenant that requires the Company to maintain an adjusted working capital ratio of not less than 1:1, but for the purpose of the calculation the unused portion of the Facility is included in current assets and, the current portion of debt and risk management liabilities are both excluded from current liabilities. As of September 30, 2015 the adjusted working capital ratio was 0.84:1. In conjunction with the executed term sheet, the working capital covenant under the credit facility is not applicable until February 1, 2016, but will be tested monthly thereafter. In addition to \$52.0 million drawn on the facility at September 30, 2015, the Company has \$4.7 million letters of credit outstanding with third parties which reduce the amount of funds available under the facility.

Bank debt outstanding increased from \$29.0 million at December 31, 2014 to \$52.0 million at September 30, 2015 due to use of the credit facility to pay invoices related to the winter capital program, decommissioning expenditures and ongoing operations. Net debt increased to \$53.8 million at September 30, 2015 from \$48.4 million at December 31, 2014 as capital expenditures and decommissioning costs exceeded funds from operations for the period.

The Company had a working capital deficiency at September 30, 2015 and December 31, 2014 as capital spending has exceeded cash flows from operations for 2014 and the first nine months of 2015. In addition, invoices related to capital spending and operating costs are typically paid on 60 to 90 day terms, whereas receivables related to oil and gas production are collected after 25 days, per normal industry terms.

In future periods, compliance with the working capital covenant and increasing production volumes and funds from operations through the recommencement of the Muskeg development program at Marlowe will be dependent on sourcing additional financing, a joint venture or a sale of assets.

In order to provide short-term capital to fund the Company's working capital deficiency, credit facility repayments and initiate the land retention drilling program required by its lender, Strategic has obtained a \$10.0 million loan from an entity which is a significant shareholder in the Company and controlled by the Chairman of the Board of Directors. The loan bears interest at 1% per month up to March 31, 2016 and 1.5% per month thereafter and is repayable on the earlier of the closing of a raise of junior capital or June 30, 2016. The loan is convertible at the option of the holder into common shares of the Company at a conversion price which is the lesser of \$0.115 per common share or a price per common share that is the issue price of the common shares issued on any equity raise on or before March 1, 2016.

## SHARE CAPITAL

	Three months ended		Nine months ended	
	September 30		September 30	
	2015	2014	2015	2014
Weighted average common shares outstanding (thousands)				
Basic	542,319	362,719	542,319	328,858
Diluted	542,319	362,719	542,319	328,858

  

	September 30, 2015	December 31, 2014
Outstanding securities (thousands)		
Common shares	542,319	542,319
Stock options	11,390	15,313

During the first nine months of 2015, 3.5 million stock options were cancelled and 0.5 million stock options expired. No common shares have been issued or cancelled in 2015.

As of November 13, 2015 there were 542,318,629 common shares outstanding and 11,365,000 stock options outstanding.

## TRANSACTIONS WITH RELATED PARTIES

For the nine months ended September 30, 2015, legal fees in the amount of \$0.15 million (September 30, 2014 - \$0.27 million) were incurred with a legal firm of which a director is a partner, and these amounts are included as general and administrative expenses. Software rental of \$0.15 million (September 30, 2014 - \$0.15 million) were charged by a company controlled by an officer. Trade and other receivables at September 30, 2015 include \$0.02 million (December 31, 2014 - \$nil) receivable from related parties. Accounts payable and accrued liabilities at September 30, 2015 include \$0.17 million (December 31, 2014 - \$0.09 million) due to related parties. The above transactions were conducted in the normal course of operations and were recorded at exchange amounts which were agreed upon between the Company and the related parties.

## COMMITMENTS

The Company has lease agreements for office space, office equipment and natural gas transportation resulting in the following commitments:

Year	Office (\$000)	Gas transportation (\$000)
2015	\$ 64	\$ 113
2016	65	453
2017	-	453
2018	-	199
2019	-	89
2020 and thereafter	-	95
	\$ 129	\$ 1,402

## ADVISORIES

### Basis of presentation

This discussion and analysis of Strategic's oil and natural gas production and related performance measures is presented on a working-interest, before royalty basis. For the purpose of calculating unit information, the Company's production and reserves are reported in barrels of oil equivalent ("boe"). Boe may be misleading, particularly if used in isolation. A boe conversion ratio for natural gas of 6 Mcf: 1 boe has been used, which is

based on an energy equivalency conversion method primarily applicable at the burner tip and does not necessarily represent a value equivalency at the wellhead. As the value ratio between natural gas and crude oil based on the current prices of natural gas and crude oil is significantly different from the energy equivalency of 6:1, utilizing a conversion on a 6:1 basis may be misleading as an indication of value.

Management 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 consolidated financial statements and revenues and expenses during the reporting period. Management reviews these estimates, including those related to accruals, environmental and decommissioning liabilities, income taxes, and the determination of proved and probable reserves on an ongoing basis. Changes in facts and circumstances may result in revised estimates and actual results may differ from these estimates.

### Non-IFRS measurements

The Company utilizes the following terms for measurement within the MD&A that do not have a standardized meaning or definition as prescribed by IFRS and therefore may not be comparable with the calculation of similar measures by other entities.

“Funds from operations” is a term used to evaluate operating performance and assess leverage. The Company considers funds from operations an important measure of its ability to generate funds necessary to finance operating activities, capital expenditures and debt repayments if any. Funds from operations are calculated based on cash flow from operating activities before changes in non-cash working capital and decommissioning expenditures. Funds from operations as presented is not intended to represent cash flow from operating activities, net earnings, or other measures of financial performance calculated in accordance with IFRS.

The following table reconciles funds from operations to cash provided by operating activities:

(\$thousands)	Three months ended September 30		Nine months ended September 30	
	2015	2014	2015	2014
Cash provided by operating activities	4,235	791	2,080	5,267
Expenditures on decommissioning liabilities	(79)	446	4,425	1,747
Changes in non-cash working capital	(3,034)	1,537	(490)	286
Funds from operations	1,122	2,774	6,015	7,300

“Operating Netback” is used to evaluate operating performance of crude oil and natural gas assets. The term netback is calculated as oil and gas sales revenue excluding realized and unrealized gains and losses on risk management contracts, less royalties, and production costs. There is no IFRS measurement that would be directly comparable to operating netbacks.

“Adjusted net working capital (deficiency)” and “net debt” are used to assess capital requirements and leverage, as well as evaluate funds available on the Company’s credit facility. Adjusted net working capital (deficiency) is calculated as current assets less current liabilities, excluding bank debt, deferred price premium on flow through shares and any assets or liabilities related to risk management contracts. Net debt is calculated as bank debt plus adjusted net working capital deficiency, or less adjusted net working capital. A reconciliation of adjusted net working capital and net debt to working capital deficiency is as follows:

(\$thousands)	September 30, 2015	December 31, 2014
Current assets	8,300	14,899
Current liabilities	(61,103)	(59,838)
Working capital deficiency	(52,803)	(44,939)
Add back: risk management contract liability (asset)	(988)	(3,460)
Net debt	(53,791)	(48,399)
Bank debt	52,000	29,016
Adjusted net working capital (deficiency)	(1,791)	(19,383)

## **FUTURE ACCOUNTING PRONOUNCEMENTS**

In May 2014, the IASB issued IFRS 15 “Revenue from Contracts with Customers,” which replaces IAS 18 “Revenue,” IAS 11 “Construction Contracts,” and related interpretations. The standard is required to be adopted either retrospectively or using a modified transition approach for fiscal years beginning on or after January 1, 2018, with earlier adoption permitted. The Company is currently evaluation the impact of this standard on its financial statements.

In July 2014, the IASB completed the final elements of IFRS 9 “Financial instruments.” The standard supersedes earlier versions of IFRS 9 and completes the IASB’s project to replace IAS 39 “Financial Instruments: Recognition and Measurement.” 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. The standard will come into effect for annual periods beginning on or after January 1, 2018, with earlier adoption permitted. The Company is currently evaluating the impact of this standard on its financial statements.

## **CRITICAL ACCOUNTING ESTIMATES**

This MD&A is based on Strategic’s interim condensed consolidated financial statements, which have been prepared in accordance with IFRS. A summary of the Company’s significant accounting policies is contained in *Note 3* to the Company’s consolidated financial statements for the year ended December 31, 2014. These accounting policies are subject to estimates and key judgments about future events, many of which are beyond the Company’s control. Actual results may differ from these estimates and the differences may be significant. A discussion of specific estimates employed in the preparation of the Company’s interim condensed consolidated financial statements is included in Strategic’s MD&A for the year ended December 31, 2014.

## **BUSINESS RISKS**

There are numerous risks facing participants in the oil and gas industry. Some of the risks are common to all businesses while others are specific to a sector. While Strategic realizes that these risks cannot be eliminated, it is committed to monitoring and mitigating these risks.

### **Substantial capital requirements and liquidity**

The Company anticipates that it will make substantial capital expenditures for the acquisition, exploration, development and production of oil and natural gas reserves in the future. If the Company’s future revenues or reserves decline, the Company’s ability to expend the capital necessary to undertake or complete future drilling programs may be limited. There can be no assurance that debt or equity financing or cash generated by operations will be available or sufficient to meet these requirements or for other corporate purposes or, if debt or equity financing is available, that it will be on terms acceptable to the Company. Moreover, future activities may require Strategic to alter its capitalization significantly, and potentially increase the Company’s debt levels above industry standards. Strategic’s credit facility is in the form of a demand loan, which must be renewed periodically and may be reduced at the option of the lender. The credit facility is also being reduced at a rate of \$0.5 million per month. The inability of the Company to access sufficient capital for its operations could have a material adverse effect on the Company’s financial condition, results of operations or prospects.

Based on expected cash flows over the next 12 months management has determined that the Company will need to pursue additional financing in order to complete capital activities and to fund liabilities as they come due. Strategic’s Board of Directors has initiated a process to identify, examine and consider strategic and financial alternatives available to raise capital, manage the facility repayments and enhance shareholder value. Alternatives may include, but are not limited to, identification and negotiation with alternative debt providers, the raising of



additional capital via private or public share placement, recapitalization, the sale of the Company, merger, joint venture or other business combination, the sale of all or a portion of the Company's assets, or any combination thereof. In the event that adequate funds from these initiatives are not available, the Company may be required to scale back or eliminate certain projects.

### **Oil and natural gas prices and marketing**

The Company's revenues are dependent upon prevailing prices for oil and natural gas. Oil and natural gas prices can be extremely volatile and are affected by the actions of domestic and international markets, foreign governments, international cartels and the Canadian federal and provincial governments. Petroleum prices have fallen precipitously over the last 9 months due to global oversupply, caused primarily by growth in North American oil production and lack of a voluntary production curtailment by the Organization of Petroleum Exporting Countries ("OPEC"). In addition, the marketability of the production depends upon the availability and capacity of gathering systems and pipelines, the effect of federal and provincial regulation (including tax and royalty regimes) on such production and general economic conditions. All of these factors are beyond the control of the Company. Any decline in oil or natural gas prices could have a material adverse effect on the Company's operations, financial condition, proved reserves and the level of expenditures undertaken for the development of its oil and natural gas reserves.

The Company may manage the risk associated with changes in commodity prices and foreign exchange rates by, from time to time, entering into crude oil or natural gas price hedges and forward foreign exchange contracts. To the extent that the Company engages in risk management activities related to commodity prices and foreign exchange rates, it will be subject to credit risks associated with counterparties with which it contracts. The Company may be required to make cash payments to its counterparties in respect of these contracts, and therefore net income and cash flows will be affected by fluctuations in the value of these forward contracts, and the effect could be significant. In addition, a ceiling price on a risk management contract would restrict the Company from obtaining the full benefit of any commodity price appreciation.

### **Environmental concerns**

The operation of oil and natural gas wells and pipelines involves a number of natural hazards that may result in blowouts, environmental damage or other unexpected or dangerous conditions resulting in liability to the Company and possibly liability to fourth parties. The oil and natural gas industry is subject to extensive environmental regulation that provides for restrictions and prohibitions on releases or emissions of various substances produced in association with certain oil and natural gas industry operations, and such regulations may be expanded to include regulation of, among other things, emissions of carbon dioxide. In addition, legislation requires that well and facility sites are abandoned and reclaimed to the satisfaction of provincial authorities. A breach of such legislation may result in fines or the issuance of clean-up orders. The Company carries insurance to mitigate the cost of remediating damage from environmental incidents, but there can be no assurance that the insurance will cover all types of incidents or that remediation costs will not exceed the limit of the insurance carried. In addition, the Company will make reasonable provisions for well abandonment, facility decommissioning and site remediation where appropriate; however there can be no assurance that such provisions will be sufficient to satisfy all such obligations. In addition, decommissioning expenditures that are planned for the first 12 months after the reporting date are classified as current liabilities on the balance sheet and affect the Company's net debt levels and debt covenant calculations.

Other business risks affecting Strategic's operations are substantially unchanged from those presented in the Company's MD&A for the year ended December 31, 2014.

## **FORWARD-LOOKING STATEMENTS**

This report includes certain information, with management's assessment of Strategic's future plans and operations, and contains forward-looking statements which may include some or all of the following: (i) forecasted capital expenditures and plans; (ii) exploration, drilling and development plans, (iii) prospects and drilling inventory and locations; (iv) anticipated production rates; (v) expected royalty rate; (vi) anticipated production and service costs; (vii) the Company's financial strength; (viii) incremental development opportunities; (ix) reserve life index; (x) total shareholder return; (xi) growth prospects; (xii) asset disposition plans; (xiii) sources of funding, which are provided to allow investors to better understand Strategic's business. By their nature, forward-looking statements are subject to numerous risks and uncertainties; some of which are beyond Strategic's control, including the impact of general economic conditions, industry conditions, operations risks, volatility of commodity prices, currency fluctuations, imprecision of reserve estimates, environmental risks, changes in environmental tax and royalty legislation, competition from other industry participants, the lack of availability of qualified personnel or management, stock market volatility and ability to access sufficient capital from internal and external sources, and other risks and uncertainties described under the heading 'Risk Factors' and elsewhere in the Company's Annual Information Form for the year ended December 31, 2014 and other documents filed with Canadian provincial securities authorities, available to the public at [www.sedar.com](http://www.sedar.com). Readers are cautioned that the assumptions used in the preparation of such information, although considered reasonable at the time of preparation, may prove to be imprecise and, as such, undue reliance should not be placed on forward-looking statements. The principal assumptions Strategic has made includes security of land interests; drilling cost stability; royalty rate stability; oil and gas prices to remain in their current range; finance and debt markets continuing to be receptive to financing the Company and industry standard rates of geologic and operational success. Strategic's actual results, performance or achievement could differ materially from those expressed in, or implied by, these forward-looking statements or if any of them do so, what benefits that Strategic will derive there from. Strategic disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law.

Further information with respect to the Company can be found on its website at [www.sogoil.com](http://www.sogoil.com) and on the SEDAR website: [www.sedar.com](http://www.sedar.com).



## **Interim Condensed Consolidated Financial Statements**

**For the three and nine months ended September 30, 2015 and 2014**

# Strategic Oil & Gas Ltd.

Interim condensed consolidated balance sheets (unaudited)

(\$000)	Note	September 30, 2015	December 31, 2014
<b>Assets</b>			
Current Assets:			
Cash and cash equivalents		\$ 2,368	\$ 360
Trade and other receivables		4,781	10,807
Inventory		163	272
Risk management contracts	14	988	3,460
		<b>8,300</b>	14,899
Long-term receivable	4	800	800
Property, plant, and equipment, net	6	144,402	209,999
Exploration and evaluation assets	5	11,639	13,903
<b>Total Assets</b>		<b>\$ 165,141</b>	<b>\$ 239,601</b>
<b>Liabilities</b>			
Current Liabilities:			
Accounts payable and accrued liabilities		\$ 8,728	\$ 26,815
Bank indebtedness	7	52,000	29,016
Decommissioning liabilities	8	375	4,007
		<b>\$ 61,103</b>	<b>\$ 59,838</b>
Long term Liabilities:			
Decommissioning liabilities	8	53,178	50,904
<b>Total Liabilities</b>		<b>\$ 114,281</b>	<b>\$ 110,742</b>
<b>Shareholders' Equity</b>			
Share capital	9	319,678	319,678
Contributed surplus		10,515	10,187
Deficit		(279,333)	(201,006)
		<b>\$ 50,860</b>	<b>\$ 128,859</b>
<b>Total Liabilities and Shareholders' Equity</b>		<b>\$ 165,141</b>	<b>\$ 239,601</b>

See accompanying notes to the Interim Condensed Consolidated Financial Statements

# Strategic Oil & Gas Ltd.

Interim condensed consolidated statements of net income (loss) and comprehensive income (loss) (unaudited)

(\$000, except per share amounts)	Note	Three months ended September 30,		Nine months ended September 30,	
		2015	2014	2015	2014
<b>Revenue</b>					
Petroleum and natural gas sales		\$ 7,783	\$ 19,394	\$ 29,146	\$ 64,148
Royalties		(1,175)	(4,392)	(3,195)	(14,115)
<b>Revenues, net of royalties</b>		<b>6,608</b>	<b>15,002</b>	<b>25,951</b>	<b>50,033</b>
Unrealized gain (loss) on risk management contracts	14	860	6,758	(2,472)	4,162
Net realized gain (loss) on risk management contracts	14	912	(2,072)	4,230	(7,554)
		\$ 8,380	\$ 19,688	\$ 27,709	\$ 46,641
<b>Expenses</b>					
Operating		\$ 4,269	\$ 6,772	\$ 16,245	\$ 24,271
Transportation		137	759	813	3,072
General and administrative		1,258	1,564	5,091	5,159
Finance costs	11	1,020	1,424	2,856	3,597
Stock-based compensation		100	487	328	782
Depletion, depreciation and amortization		5,088	8,555	19,177	25,671
Valuation allowance	4	-	-	1,100	-
Exploration	5	426	-	426	-
Impairment	6	60,000	-	60,000	-
Gain on disposal of property, plant and equipment		-	-	-	(2,304)
		\$ 72,298	\$ 19,561	\$ 106,036	\$ 60,248
<b>Operating income (loss) before taxes</b>		\$ (63,918)	\$ 127	\$ (78,327)	\$ (13,607)
Deferred tax recovery		-	86	-	1,437
<b>Net income (loss) and comprehensive income (loss) for the period</b>		\$ (63,918)	\$ 213	\$ (78,327)	\$ (12,170)
<b>Net income (loss) per weighted average share</b>					
Basic	9(c)	\$ (0.12)	\$ 0.00	\$ (0.14)	\$ (0.04)
Diluted	9(c)	\$ (0.12)	\$ 0.00	\$ (0.14)	\$ (0.04)

See accompanying notes to the Interim Condensed Consolidated Financial Statements.

# Strategic Oil & Gas Ltd.

Interim condensed consolidated statements of changes in shareholders' equity (unaudited)

(\$000)	Share Capital	Contributed Surplus	Deficit	Total equity
<b>Balance January 1, 2015</b>	\$ 319,678	\$ 10,187	\$ (201,006)	\$ 128,859
Stock based compensation	-	328	-	328
Net loss	-	-	(78,327)	(78,327)
<b>Balance September 30, 2015</b>	\$ 319,678	\$ 10,515	\$ (279,333)	\$ 50,860

(\$000)	Share Capital	Contributed Surplus	Deficit	Total Equity
<b>Balance January 1, 2014</b>	\$ 197,970	\$ 9,227	\$ (71,516)	\$ 135,681
Issue of shares	115,716	-	-	115,716
Share issue costs	(765)	-	-	(765)
Stock options exercised	205	(66)	-	139
Stock based compensation	-	782	-	782
Net loss	-	-	(12,170)	(12,170)
<b>Balance September 30, 2014</b>	\$ 313,126	\$ 9,943	\$ (83,686)	\$ 239,383

See accompanying notes to the Interim Condensed Consolidated Financial Statements.

# Strategic Oil & Gas Ltd.

Interim condensed consolidated statements of cash flow (unaudited)

(\$000)	Note	Three months ended September 30,		Nine months ended September 30,	
		2015	2014	2015	2014
<b>Operating activities:</b>					
Net income (loss) for the period		\$ (63,918)	\$ 213	\$ (78,327)	\$ (12,170)
Non-cash items:					
Depletion, depreciation, and amortization		5,088	8,555	19,177	25,671
Accretion of decommissioning liabilities		286	363	839	920
Stock-based compensation		100	487	328	782
Unrealized loss (gain) on risk management contracts		(860)	(6,758)	2,472	(4,162)
Valuation allowance		-	-	1,100	-
Exploration expense		426	-	426	-
Impairment	6	60,000	-	60,000	-
Deferred tax recovery		-	(86)	-	(1,437)
Gain on disposal of property, plant and equipment		-	-	-	(2,304)
<b>Funds from operations</b>		<b>\$ 1,122</b>	<b>\$ 2,774</b>	<b>\$ 6,015</b>	<b>\$ 7,300</b>
Expenditures on decommissioning liabilities		79	(446)	(4,425)	(1,747)
Change in non-cash working capital	12	3,034	(1,537)	490	(286)
<b>Cash provided by operating activities</b>		<b>\$ 4,235</b>	<b>\$ 791</b>	<b>\$ 2,080</b>	<b>\$ 5,267</b>
<b>Financing activities:</b>					
Issue of common shares, net of share issue costs		\$ -	\$ 19,708	\$ -	\$ 69,006
Increase in bank loan		500	-	22,984	-
Decrease in bank loan		-	(21,351)	-	(10,126)
Issue of promissory notes		-	10,930	-	10,930
Exercise of options		-	-	-	139
<b>Cash provided by financing activities</b>		<b>\$ 500</b>	<b>\$ 9,287</b>	<b>\$ 22,984</b>	<b>\$ 69,949</b>
<b>Investing activities:</b>					
Expenditures – property, plant and equipment		\$ (1,350)	\$ (24,733)	\$ (9,269)	\$ (74,290)
Expenditures – exploration and evaluation assets		(51)	(138)	(206)	(2,574)
Proceeds on disposal of property, plant and equipment		-	-	-	3,821
Changes in non-cash working capital	12	(1,845)	8,740	(13,581)	(1,759)
<b>Cash used in investing activities</b>		<b>\$ (3,246)</b>	<b>\$ (16,131)</b>	<b>\$ (23,056)</b>	<b>\$ (74,802)</b>
<b>Increase (Decrease) in cash and cash equivalents during the period</b>		<b>\$ 1,489</b>	<b>\$ (6,053)</b>	<b>\$ 2,008</b>	<b>\$ 414</b>
<b>Cash and cash equivalents, beginning of the period</b>		<b>879</b>	<b>6,693</b>	<b>360</b>	<b>226</b>
<b>Cash and cash equivalents, end of the period</b>		<b>\$ 2,368</b>	<b>\$ 640</b>	<b>\$ 2,368</b>	<b>\$ 640</b>

See accompanying notes to the Interim Condensed Consolidated Financial Statements.

# Strategic Oil & Gas Ltd.

Notes to the interim condensed consolidated financial statements (unaudited)  
September 30, 2015 and 2014

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## 1. Corporate information

Strategic Oil & Gas Ltd. (“Strategic”) is a company registered and domiciled in Alberta. Strategic is a publicly traded Company whose shares are listed on the TSX Venture Exchange. Strategic, together with its subsidiaries, (collectively referred to as the “Company”), is engaged in the exploration for and development of petroleum and natural gas reserves in Western Canada with insignificant operations in the Western United States. The Company is headquartered in Canada at Suite 1100, 645 – 7th Avenue SW, Calgary, Alberta.

## 2. Basis of presentation

### a) Going concern

These interim condensed consolidated financial statements have been prepared using the going concern basis of presentation, which assumes that the Company will continue in operation for the foreseeable future and will be able to realize its assets and discharge its liabilities and commitments in the normal course of business. For the quarter ended September 30, 2015, the Company reported a net loss of \$63.9million. At September 30, 2015, the Company had negative working capital of \$52.8 million and an accumulated deficit of \$279.3 million. Subsequent to the reporting period, the Company executed a term sheet with the lender to amend its credit facility, which terms are described in Note 7. Strategic’s cash flows and compliance with debt covenants are highly dependent on realized oil prices. Sustained low commodity prices will significantly reduce the Company’s cash flows, resulting in significant doubt upon the Company’s ability to continue as a going concern.

The interim condensed consolidated financial statements do not reflect adjustments that would be necessary if the going concern basis was not appropriate. The appropriateness of the going concern basis is dependent upon, among other things, the ability to obtain debt or equity financing, a joint venture or a sale of assets in order to have sufficient funds to meet its obligations.

### b) Statement of compliance

These interim condensed consolidated financial statements (the “financial statements”) have been prepared in accordance with International Accounting Standard (“IAS”) 34 “Interim Financial Reporting” using accounting policies consistent with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Boards (“IASB”). These financial statements are condensed as they do not include all of the information required by IFRS for annual financial statements and therefore should be read in conjunction with the Company’s annual consolidated financial statements for the year ended December 31, 2014.

These financial statements were authorized for issue by the Board of Directors on November 13, 2015.

### c) Basis of measurement

These financial statements are prepared using the same accounting policies and methods of computation as disclosed in the Company’s annual consolidated financial statements for the year ended December 31, 2014. There have been no changes in the application or use of estimates or judgments since December 31, 2014.



# Strategic Oil & Gas Ltd.

Notes to the interim condensed consolidated financial statements (unaudited)  
September 30, 2015 and 2014

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**d) Functional and presentation currency**

These financial statements are presented in Canadian dollars, the Company's functional currency.

**e) Comparative figures**

Certain comparative figures from prior periods have been reclassified to conform to the current year's presentation. For the three and nine months ended September 30, 2014, \$0.35 million and \$1.08 million, respectively of pipeline tariffs after the custody transfer point have been reclassified from transportation expense to petroleum and natural gas sales in the statement of loss and comprehensive loss.

### 3. Significant accounting policies

**a) Future accounting policy changes**

**Financial instruments**

- In July 2014, the IASB completed the final elements of IFRS 9 "Financial instruments." The standard supersedes earlier versions of IFRS 9 and completes the IASB's project to replace IAS 39 "Financial Instruments: Recognition and Measurement." 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. The standard will come into effect for annual periods beginning on or after January 1, 2018, with earlier adoption permitted. The Company is currently evaluating the impact of this standard on its financial statements.

**Revenue**

- In May 2014, the IASB issued IFRS 15 "Revenue from Contracts with Customers," which replaces IAS 18 "Revenue," IAS 11 "Construction Contracts," and related interpretations. The standard is required to be adopted either retrospectively or using a modified transition approach for fiscal years beginning on or after January 1, 2018, with earlier adoption permitted. The Company is currently evaluating the impact of this standard on its financial statements.

### 4. Insurance receivable

Included in decommissioning liabilities is an estimate of \$8.5 million for remediation of a prior year pipeline spill in the Marlowe area. As the pipeline spill was claimed under the Company's insurance policy coverage, a receivable of \$2.6 million has been recorded on the balance sheet as at September 30, 2015 (December 31, 2014 - \$3.7 million) representing the cost of remediation work completed in the first quarter of 2015 and ongoing monitoring costs, that are virtually certain to be recovered, of which \$1.8 million is included in current assets and \$0.8 million in long-term receivables. A valuation allowance of current receivables in the amount of \$1.1 million has been recorded based on preliminary discussions with the Company's insurers. On November 3, 2015, a \$1.9 million interim payment was received from the insurer.

# Strategic Oil & Gas Ltd.

Notes to the interim condensed consolidated financial statements (unaudited)  
September 30, 2015 and 2014

## 5. Exploration and evaluation (“E&E”) assets

(\$000)	September 30, 2015	December 31, 2014
Opening balance	\$ 13,903	\$ 14,695
E&E expenditures	206	2,905
E&E transfer to Property, plant and equipment	(511)	(702)
E&E expense	(426)	(399)
Amortization for the period	(1,534)	(2,596)
Closing balance	\$ 11,639	\$ 13,903

For the nine months ended September 30, 2015, the Company expensed \$0.4 million (year ended December 31, 2014 - \$0.4 million) related to seismic expenditures on land on which there are currently no plans for future exploration.

## 6. Property, plant, and equipment (“PPE”)

(\$000)	D&P assets		Office	Total
Carrying value before accumulated depletion and depreciation				
As at December 31, 2014	\$ 436,855	\$ 1,170	\$	\$ 438,025
Additions	9,269	-	-	9,269
E&E transfer	511	-	-	511
Change in decommissioning costs	2,228	-	-	2,228
<b>As at September 30, 2015</b>	<b>\$ 448,863</b>	<b>\$ 1,170</b>	<b>\$</b>	<b>\$ 450,033</b>

(\$000)	D&P assets		Office	Total
Accumulated depletion and depreciation (“D&D”)				
As at December 31, 2014	\$ 227,088	\$ 938	\$	\$ 228,026
D&D expensed	17,543	101	-	17,643
D&D capitalized to inventory	(39)	-	-	(39)
Impairment	60,000	-	-	60,000
<b>As at September 30, 2015</b>	<b>\$ 304,592</b>	<b>\$ 1,039</b>	<b>\$</b>	<b>\$ 305,631</b>

(\$000)	D&P assets		Office	Total
Net carrying value				
As at December 31, 2014	\$ 209,767	\$ 232	\$	\$ 209,999
<b>As at September 30, 2015</b>	<b>\$ 144,271</b>	<b>\$ 131</b>	<b>\$</b>	<b>\$ 144,402</b>

Substantially all of the Company’s development and production (“D&P”) assets are located within Canada. The cost of PPE includes amounts in respect to the provision for decommissioning obligations. For the nine month period ended September 30, 2015, \$0.91 million of direct general and administrative expenses were capitalized to PPE (\$1.46 million for the nine month period ended September 30, 2014).

Future capital costs of \$121.5 million (September 30, 2014 - \$127.0 million) have been included in the depletable balance as at September 30, 2015. Major components account for \$61.9 million (September 30, 2014 - \$72.5 million) and are depreciated and tested for impairment separately.

# Strategic Oil & Gas Ltd.

Notes to the interim condensed consolidated financial statements (unaudited)  
September 30, 2015 and 2014

## Impairment

The Company's exploration, development and production assets are aggregated into cash generating units ("CGUs") based on their ability to generate largely independent cash flows.

The December 31, 2014 reserve volumes and values were evaluated by the Company's independent reserve evaluators. At September 30, 2015 the decline in forward commodity prices compared to December 2014 was an indicator of potential impairment.

The recoverable values of the Company's CGUs were estimated as the fair value less cost to sell based on the net present value of before tax cash flows (discounted at 10%) from crude oil and natural gas proved plus probable reserves originally estimated by the Company's third party reserve evaluators, internally updated for production since December 31, 2014, plus an internal estimate of incremental drilling locations. The value of resources incremental to the reserve report was further supported by contingent resource studies compiled by independent reserve engineers and discounted at a rate of 15%.

In determining impairment, the Company considered various estimates, including future pricing, timing of capital expenditures, and impact of changes in cost structures. Forecast benchmark prices and exchange rates were as follows:

	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025+
WTI crude oil (US\$/bbl)	50.00	55.00	61.20	65.00	69.00	73.10	77.30	81.60	86.20	87.90	89.60
Edmonton CS (CAD\$/bbl)	60.68	67.40	73.40	78.10	80.90	86.00	91.10	96.40	102.00	104.00	106.00
AECO Gas Price (CAD\$/mcf)	2.90	3.35	3.65	3.85	4.00	4.25	4.45	4.70	5.00	5.10	5.20

It was determined that the carrying value of certain CGU's exceeded the recoverable value and a \$60.0 million (December 31, 2014 - \$114.0 million) impairment was recognized. The impairment specifically relates to Steen/Marlow CGU (\$54.4 million), Bistcho CGU (\$4.5 million) and other Canadian CGU (\$1.1). The impairment recorded reflects the Company's best estimates based on currently available information.

Three months ended September 30, 2015 (\$000)	Impairment Expense	Recoverable Amount
Steen/Marlow CGU	\$ 54,388	\$ 146,173
Bistcho CGU	4,558	7,503
Other Canadian CGU	1,054	600
<b>Total</b>	<b>\$ 60,000</b>	<b>\$ 154,276</b>

At December 31, 2015, in conjunction with the December reserve report from the independent reserve evaluators, the Company will review the aforementioned estimates to determine any future potential impairment or reversal.

# Strategic Oil & Gas Ltd.

Notes to the interim condensed consolidated financial statements (unaudited)  
September 30, 2015 and 2014

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## 7. Bank indebtedness

Strategic had a \$57.0 million credit facility at September 30, 2015, consisting of a \$40 million revolving operating loan and a \$17.0 million non-revolving facility that is reduced at a rate of \$0.5 million per month (\$16.0 million as of November 1, 2015). Subsequent to the reporting period, Strategic executed a term sheet with the lender to amend its credit facility. Upon amendment, the Company will continue to reduce the non-revolving facility by \$0.5 million per month and is required to repay additional amounts as follows:

- \$9.5 million on or before February 1, 2016
- the balance of the non-revolving facility on or before June 1, 2016

The Company is also required to raise \$40.0 million in capital subordinated to the lender on or before June 1, 2016, with a minimum of \$25.0 million raised prior to February 1, 2016, and drill 2 wells before March 31, 2016, primarily to retain certain undeveloped lands.

Amounts outstanding under the amended revolving facility are repayable on demand, and bear interest at a rate of 3.0% over the bank's prime lending rate. Amounts due under the non-revolving facility bear interest at a rate of 2.0% above the interest rates on the operating loan. The Facility is secured by a general security agreement including a floating charge on all property, plant and equipment. The Facility contains a financial covenant that requires the Company to maintain an adjusted working capital ratio of not less than 1:1, but for the purpose of the calculation the unused portion of the Facility is included in current assets and, the current portion of debt and risk management liabilities are both excluded from current liabilities. As of September 30, 2015 the adjusted working capital ratio was 0.84:1. In conjunction with the term sheet, the working capital covenant under the credit facility is not applicable until February 1, 2016, but will be tested monthly thereafter. In addition to \$52.0 million drawn on the facility at September 30, 2015, the Company has \$4.7 million letters of credit outstanding with third parties which reduce the amount of funds available under the facility.

## 8. Decommissioning liabilities

Total future decommissioning liabilities are estimated based on the Company's net working interest in all wells and facilities, the estimated costs to abandon and reclaim the wells, pipelines and facilities and the estimated timing of the costs to be incurred in future periods. These costs are expected to be incurred over a range up to 33 years, depending on the estimated reserve life. The undiscounted amount of the estimated costs at September 30, 2015 were \$91.9 million (December 31, 2014 - \$86.4 million). The estimated costs have been discounted at a risk free rate from 0.60% to 2.21% (December 31, 2014 - 1.01% to 2.33%) and an inflation rate of 2% (December 31, 2014 - 2%) was applied.

# Strategic Oil & Gas Ltd.

Notes to the interim condensed consolidated financial statements (unaudited)  
September 30, 2015 and 2014

The following table reconciles the changes to the Company's decommissioning liabilities:

(\$000)	Nine months ended September 30, 2015	Year ended December 31, 2014
Balance beginning of the period	\$ 54,911	\$ 35,932
Liabilities incurred during the period	126	1,349
Disposition of liabilities	-	(170)
Expenditures on existing liabilities	(4,425)	(1,745)
Change in estimated future cash flows	55	13,655
Change in discount rate	2,047	4,702
Accretion	839	1,188
Balance end of the period	\$ 53,553	\$ 54,911
Current	375	4,007
Long term	\$ 53,178	\$ 50,904

## 9. Share capital

### a) Authorized

The Company is authorized to issue an unlimited number of common shares without par value.

### b) Issued and outstanding

(\$000, except for share amounts)	Number of shares	Nine months ended September 30, 2015
Balance beginning and end of the period	542,318,629	\$ 319,678

There were no changes related to share capital for the three and nine months ended September 30, 2015.

### c) Weighted average shares

(000)	Three months ended September 30		Nine months ended September 30	
	2015	2014	2015	2014
Weighted average shares (basic)	542,319	362,719	542,319	328,858
Weighted average shares (diluted)	542,319	362,719	542,319	328,858

For the three and nine months ended September 30, 2015, the outstanding stock options were excluded from the dilution calculations as they were anti-dilutive.

## 10. Stock-based compensation

The outstanding number and weighted average exercise price of stock options are as follows:

	Number of options	Weighted average Exercise Price
Balance at December 31, 2014	15,313,334	\$ 0.79
Granted	25,000	0.15
Cancelled/Forfeited	(3,498,334)	0.89
Expired	(450,000)	0.65
Balance at September 30, 2015	11,390,000	\$ 0.76

# Strategic Oil & Gas Ltd.

Notes to the interim condensed consolidated financial statements (unaudited)  
September 30, 2015 and 2014

The following table sets out the outstanding and exercisable options as at September 30, 2015:

	Outstanding Options			Exercisable Options	
	Number of Options	Weighted Average Exercise Price	Weighted Average Life Years	Number of Options	Weighted Average Exercise Price
	5,430,000	\$ 0.42	3.93	3,593,319	\$ 0.42
	85,000	0.48	3.58	56,669	0.48
	110,000	0.61	1.87	106,667	0.61
	530,000	0.83	2.14	526,667	0.83
	765,000	0.90	1.40	765,000	0.90
	165,000	0.95	1.78	155,001	0.95
	765,000	1.10	0.27	765,000	1.10
	3,165,000	1.16	2.27	3,165,000	1.16
	375,000	1.30	2.35	375,000	1.30
	11,390,000	\$ 0.76	2.86	9,508,323	\$ 0.83

The fair value of options granted was estimated on the date of grant using a Black-Scholes option pricing model with the following weighted average inputs:

Assumptions	Nine months ended September 30	
	2015	2014
Risk free interest rate (%)	1.51	1.52
Expected life (years)	3.65	3.65
Expected volatility (%)	74.36	74.40
Forfeiture rate (%)	15.94	13.37
Weighted average fair value of options granted	0.07	0.18

## 11. Finance costs

(\$000)	Three months ended September 30		Nine months ended September 30	
	2015	2014	2015	2014
Interest expense	\$ 734	\$ 1,061	\$ 2,017	\$ 2,677
Accretion of decommissioning liabilities	286	363	839	920
	\$ 1,020	\$ 1,424	\$ 2,856	\$ 3,597

# Strategic Oil & Gas Ltd.

Notes to the interim condensed consolidated financial statements (unaudited)  
September 30, 2015 and 2014

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## 12. Supplemental cash flow information

(\$000)	Nine months ended September 30	
	2015	2014
Interest paid	\$ 2,017	\$ 2,677
Changes in non-cash working capital		
Valuation allowance of trade and other receivables	(1,100)	-
Trade and other receivables	6,026	705
Inventory	109	(1,238)
Accumulated depletion in inventory	(39)	764
Accounts payable and accrued liabilities	(18,087)	(2,276)
	\$ (13,091)	\$ (2,045)
Operating	490	(286)
Investing	(13,581)	(1,759)
	\$ (13,091)	\$ (2,045)

## 13. Transactions with related parties

For the nine months ended September 30, 2015, legal fees in the amount of \$0.15 million (September 30, 2014 - \$0.27 million) were incurred with a legal firm of which a director is a partner, and these amounts are included as general and administrative expenses. Software rental of \$0.15 million (September 30, 2014 - \$0.15 million) were charged by a company controlled by an officer. Trade and other receivables at September 30, 2015 include \$0.02 million (December 31, 2014 - \$nil) receivable from related parties. Accounts payable and accrued liabilities at September 30, 2015 include \$0.17 million (December 31, 2014 - \$0.09 million) due to related parties. The above transactions were conducted in the normal course of operations and were recorded at exchange amounts which were agreed upon between the Company and the related parties.

## 14. Financial instruments and financial risk management

The Company's financial instruments include cash and cash equivalents, trade and other receivables, long-term receivable, bank indebtedness, accounts payable and accrued liabilities, and risk management contracts. The carrying value of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities and bank indebtedness approximate their fair values due to their relatively short periods to maturity.

The Company is required to classify fair value measurements using a hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy is as follows:

- Level 1 - quoted prices in active markets for identical assets or liabilities;
- Level 2 - inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly; and
- Level 3 - inputs for the asset or liability that are not based on observable market data.

The fair value of risk management contracts is measured at level 2.

# Strategic Oil & Gas Ltd.

Notes to the interim condensed consolidated financial statements (unaudited)  
September 30, 2015 and 2014

The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to market conditions and the Company's activities. The Company has exposure to credit risk, liquidity risk and market risk as a result of its use of financial instruments. The following presents information about the Company's exposure to each of the above risks and the Company's objectives, policies and processes for measuring and managing commodity risks. Further quantitative disclosures are included throughout these financial statements.

## Commodity price risk

Commodity price risk is the risk that the fair value of assets or liabilities or future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices for petroleum and natural gas are impacted by world economic events that dictate the levels of supply and demand as well as the relationship between the Canadian and United States dollar. The Company may, in certain circumstances, enter into forward oil or natural gas sales contracts to mitigate commodity price risk.

At September 30, 2015, the following risk management contracts were outstanding with a mark-to-market asset value of \$0.99 million (September 30, 2014 – liability value of \$4.6 million).

## Financial WTI crude oil contracts

Term	Contract Type	Volume (bbl/d)	Fixed Price (Cdn\$/bbl)	Index	
01-Jul-2015	31-Dec-2015	Option <sup>(1)</sup>	250	\$90.00	WTI – NYMEX
01-Jul-2015	31-Dec-2015	Swap	500	USD \$61.65	WTI – NYMEX

<sup>(1)</sup> Counterparty has an option to convert into a swap at the fixed price indicated. The 250 bbl/d option expires monthly during the contract term.

## Financial AECO gas contracts

Term	Contract Type	Volume (GJ/d)	Fixed Price (\$/GJ)	Index	
01-Apr-2015	31-Oct-2015	Swap	300	2.70	AECO
01-Jun-2015	31-Oct-2015	Swap	200	2.70	AECO

The Company does not apply hedge accounting to these risk management contracts and they are recorded as fair value with changes in fair value included in the condensed consolidated statement of loss and comprehensive loss.

The following table summarizes the fair value as at September 30, 2015 and the change in fair value for the three and nine months ended September 30, 2015:

(\$000)	September 30, 2015	December 31, 2014
Risk management contracts, beginning of period	\$ 3,460	\$ (8,757)
Unrealized change in fair value	(2,472)	12,217
Risk management contracts, end of period	988	3,460
Gross assets, end of period	989	3,460
Gross liabilities, end of period	\$ (1)	\$ -



# Strategic Oil & Gas Ltd.

Notes to the interim condensed consolidated financial statements (unaudited)  
September 30, 2015 and 2014

## 15. Capital management

Strategic considers its capital structure to include shareholders' equity and working capital employed including bank indebtedness. The objectives of the Company are to maintain a strong balance sheet affording the Company financial flexibility to achieve goals of continued growth and access to capital. In order to maintain or adjust the capital structure, the Company may issue new common shares, issue new debt, or adjust exploration and development capital expenditures.

The Company monitors its capital program based on available funds, which is the combination of working capital (excluding risk management contracts) and remaining unused line of credit, as calculated below:

(\$000)	September 30, 2015	December 31, 2014
Credit facility (Note 7)	\$ 57,000	\$ 80,000
Amount drawn	(52,000)	(29,016)
Letters of credit	(4,689)	(4,385)
<b>Unutilized portion of debt facility</b>	<b>\$ 311</b>	<b>\$ 46,599</b>

## 16. Commitments and contingencies

- a) The Company has lease agreements for office space, office equipment and natural gas transportation resulting in the following commitments:

Year	Office	Gas transportation
2015	\$ 64	\$ 113
2016	65	453
2017	-	453
2018	-	199
2019	-	89
2020 and thereafter	-	95
	\$ 129	\$ 1,402

- b) By the nature of its oil and gas operations in Northern Alberta, the Company is subject to numerous safety and environmental regulations, with which non-compliance may result in adverse financial impact. The Company mitigates these risks through the adherence to formal safety and environmental policies, as well as industry standard insurance coverage. The Company is currently remediating an environmental spill in the Marlowe area. While the Company believes it has recorded its best estimate of the impact of these contingencies in these financial statements, and accrued its best estimate of amounts expected to be received under its insurance policy, the ultimate outcome of these matters is uncertain.

# Strategic Oil & Gas Ltd.

Notes to the interim condensed consolidated financial statements (unaudited)

September 30, 2015 and 2014

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## 17. Subsequent event

Subsequent to the reporting period, the Company obtained a \$10.0 million loan from an entity which is a significant shareholder in the Company and controlled by the Chairman of the Board of Directors, in order to fund the Company's working capital deficiency, credit facility repayments and initiate the land retention drilling program required by its lender. The loan bears interest at 1% per month up to March 31, 2016 and 1.5% per month thereafter and is repayable on the earlier of the closing of a raise of capital subordinated to the credit facility or June 30, 2016. The loan is convertible at the option of the holder into common shares of the Company at a conversion price which is the lesser of \$0.115 per common share or a price per common share that is the issue price of the common shares issued on any equity raise on or before March 1, 2016.