kelt exploration

FIRST QUARTER REPORT

AS AT AND FOR THE THREE MONTHS ENDED

MARCH 31, 2017

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FINANCIAL AND OPERATIONAL HIGHLIGHTS

(CA$ thousands, except as otherwise indicated)	Three months ended March 31 **2017**	2016	%
FINANCIAL			
Revenue, before royalties and financial instruments	**60,225**	40,398	49
Adjusted funds from operations [1]	**26,823**	5,951	351
Basic ($/ common share) [1]	**0.15**	0.04	275
Diluted ($/ common share) [1]	**0.15**	0.04	275
Loss and comprehensive loss	**(2,267)**	(25,918)	-91
Basic ($/ common share)	**(0.01)**	(0.15)	-93
Diluted ($/ common share)	**(0.01)**	(0.15)	-93
Total capital expenditures, net of dispositions	**(35,364)**	23,405	-251
Total assets	**1,193,644**	1,268,268	-6
Bank debt, net of working capital [1]	**75,765**	230,290	-67
Convertible debentures	**71,810**	-	-
Shareholders' equity	**842,351**	822,229	2
Weighted average shares outstanding (000s)			
Basic	**175,715**	168,824	4
Diluted	**176,782**	168,869	5
OPERATIONS			
Average daily production			
Oil (bbls/d)	**5,797**	5,873	-1
NGLs (bbls/d)	**2,358**	2,740	-14
Gas (mcf/d)	**72,295**	88,093	-18
Combined (BOE/d)	**20,204**	23,295	-13
Production per million common shares (BOE/d) [1]	**115**	138	-17
Average realized prices, before financial instruments			
Oil ($/bbl)	**60.21**	34.01	77
NGLs ($/bbl)	**27.79**	14.24	95
Gas ($/mcf)	**3.52**	2.33	51
Operating netbacks ($/BOE) [1]			
Petroleum and natural gas revenue	**33.12**	19.06	74
Realized gain on financial instruments	**0.01**	-	-
Average realized price, after financial instruments	**33.13**	19.06	74
Royalties	**(3.64)**	(1.35)	170
Production expense	**(9.61)**	(10.24)	-6
Transportation expense	**(3.25)**	(2.71)	20
Operating netback [1]	**16.63**	4.76	249
Undeveloped land			
Gross acres	**756,540**	642,122	18
Net acres	**636,637**	518,725	23

(1) Refer to advisories regarding non-GAAP financial measures and other key performance indicators.

MESSAGE TO SHAREHOLDERS

Kelt Exploration Ltd. ("Kelt" or the "Company") reports its financial and operating results to shareholders for the first quarter ended March 31, 2017.

Average production for the three months ended March 31, 2017 was 20,204 BOE per day, up 2% compared to average production of 19,762 BOE per day during the fourth quarter of 2016. Daily average production in the first quarter of 2017 was 13% lower than average production of 23,295 BOE per day in the first quarter of 2016. Production during the first quarter of 2017 reflects the disposition of the majority of its oil and gas assets at Karr which included approximately 1,300 BOE per day of production. The Karr disposition was completed on January 18, 2017. During the second half of 2016, Kelt only added 2.3 net wells of new production from its 2016 drilling program. However, the Company drilled five wells from an existing pad at Pouce Coupe in the fourth quarter of 2016, targeting the Montney D1 and D2 formations. These wells were completed in early 2017 and the results of initial production rates from these wells and two previous wells drilled from the same pad are included in the table below.

Kelt has recently moved to pad drilling as part of its future development plan for its vast corporate Montney acreage. The Company's first significant pad drilling program was carried out at Pouce Coupe, Alberta (pad located at 15-06-78-11W6) with the following results:

Well	Montney Formation	On-stream date	Horizontal lateral length (metres)	Number of fracture stages	Amount of proppant/ sand (tonnes)	Average sand per stage (tonnes)	Drill & complete cost ($ millions)	IP30 (BOE/d)	Oil & NGLs percent
02/08-18-078-11W6	D2	Dec-10-2015	2,170	46	2,300	50	$ 4.8	1,034	73%
00/08-18-078-11W6	D1	Sep-24-2016	2,202	37	1,450	39	$ 4.8	852	38%
04/07-18-078-11W6	D2	Mar-1-2017	2,170	46	2,300	50	$ 4.7	1,320	57%
02/06-18-078-11W6	D2	Mar-1-2017	2,187	46	3,115	67	$ 4.7	2,004	68%
05/07-18-078-11W6	D1	Mar-8-2017	2,168	46	3,120	68	$ 4.5	1,546	58%
00/01-09-078-11W6	D2	Mar-11-2017	3,244	46	2,370	52	$ 4.8	1,529	65%
03/07-18-078-11W6	D1	Mar-17-2017	2,164	45	2,250	50	$ 4.1	2,045	66%
Total 15-6 Pad			**16,305**	**312**	**16,905**	**54**	**$ 32.4**	**10,330**	**62%**

Kelt expects to realize significant improved capital efficiencies from pad drilling and expects to commence with a multi-well pad on its large Inga/Fireweed (British Columbia) Montney land acreage during the second half of 2017.

The Company is expecting production in the second quarter of 2017 to average approximately 22,700 to 23,000 BOE per day. Included in this forecast are the following planned outages that will negatively affect production during the second quarter of 2017:

(1) TCPL has published expected outages on the NGTL pipeline system upstream of the James River receipt area in June for approximately two weeks. Kelt has budgeted 85% of firm service capability during this period;

(2) Enbridge (Spectra) has published expected outages in BC at the McMahon Gas Plant which is expected to be down for plant turnaround operations for three weeks from June 5th to 26th. As a result of compression downtime on the Westcoast Energy pipeline system during the McMahon plant outage, Kelt expects partial outages at the West Stoddart Gas Plant where the majority of the Company's gas is processed; and

(3) Wet weather conditions experienced in April during spring break-up at Pouce Coupe and Progress has limited the Company from producing at its full capability during the month.

Commodity prices continued to improve from 2016 levels and have shown significant gains in the first quarter of 2017 compared to the first quarter of 2016. Kelt's realized average oil price during the first quarter of 2017 was $60.21 per barrel, up 77% from $34.01 per barrel in the first quarter of 2016. The realized average NGLs price during the first quarter of 2017 was $27.79 per barrel, up 95% from $14.24 per barrel in the corresponding quarter of 2016. Kelt's realized average gas price for the first quarter of 2017 was $3.52 per MCF, up 51% from $2.33 per MCF in the first quarter of the previous year.

For the three months ended March 31, 2017, revenue was $60.2 million and adjusted funds from operations was $26.8 million ($0.15 per share, diluted), compared to $40.4 million and $6.0 million ($0.04 per share, diluted) respectively, in the first quarter of 2016. At March 31, 2017, bank debt, net of working capital was $75.8 million, down 67% from $230.3 million at March 31, 2016.

Capital expenditures incurred during the three months ended March 31, 2017, prior to dispositions, were $67.6 million. The Company spent $49.5 million (73%) on drilling and completion operations, $15.6 million (23%) on facilities, pipelines and equipment and $2.5 million (4%) on land and seismic. In addition, during the first quarter of 2017, Kelt completed the disposition of the majority of its oil and gas assets at Karr for cash proceeds of $103.0 million, improving the Company's financial flexibility significantly.

Kelt continues to focus on long-term value creation by accumulating significant undeveloped land acreage on resource style plays, with a primary focus on Triassic Montney oil and liquids-rich gas plays. As at March 31, 2017, Kelt's net working interest land holdings were 847,275 acres (1,324 sections) of which 417,386 net acres (652 sections) include Montney rights. This ranks Kelt in the top five for Montney land ownership amongst publicly traded oil and gas companies.

At Oak/Flatrock, British Columbia, where the Company owns 132,610 acres (207 sections) of lands with Montney rights, the Company has drilled and completed its first exploratory horizontal well located at 02/06-02-086-18W6. The well was completed using the ball drop completion method for hydraulic fracturing. The horizontal lateral of the well was approximately 2,500 metres and the well was completed using slick-water comprising 46 fracture stages. After flowing the frac-water back on a seven day clean-up, the Oak well tested gas and free condensate, with a final rate of 3.4 MMCF per day and approximately 74 barrels per day of 42˚ API field condensate. The well was shut-in after recovering approximately 19% of load frac water. The gas rate and casing pressure continued to build through the flow-back, with final flowing casing pressure recorded at 7,476 kPa. The gas composition at Oak is similar to the Company's gas at Inga where plant liquid recoveries are approximately 55 barrels per MMCF of raw gas. The Oak well currently remains shut-in due to wet spring break-up weather conditions. The Company plans to tie the well into nearby third-party infrastructure and expects to bring the well on production in late Q2 or early Q3 2017. The well will be produced at restricted rates limited by the third-party compression currently available. Kelt expects to follow-up with a second well at Oak to be drilled after spring break-up in 2017.

The Company also has 50,080 acres (78 sections) of lands with Montney rights at Pipestone/Wembley, Alberta where Kelt expects to drill its first horizontal exploratory well during the second quarter of 2017.

The Company's Board of Directors has agreed to increase the 2017 capital expenditure budget by $28.0 million. Kelt has changed its previously reported production and financial guidance for 2017 to reflect the increased capital spending. Oil and gas price forecasts for 2017 have been reduced from previous estimates. The table below summarizes Kelt's revised guidance for 2017:

	2017 Forecast	Previous Forecast	Change
Capital expenditures, net of dispositions ($ millions)	**70.0**	42.0	67%
Average Production (BOE/d)	**23,500**	23,000	2%
WTI crude oil price (US$/bbl)	**51.00**	52.00	- 2%
AECO natural gas price ($/GJ)	**2.70**	2.95	- 8%
Adjusted funds from operations ($ millions)	**130.0**	128.0	2%
$ per common share, diluted	**0.73**	0.73	0%
Bank debt, net of working capital, at year-end ($ millions)	**78.0**	52.0	50%
Net bank debt to trailing annual adjusted funds from operations ratio	**0.6 x**	0.4 x	

The Company is well positioned financially to execute its capital program during the remainder of 2017 and expects to enter 2018 with strong operational momentum.

Management looks forward to updating shareholders with 2017 second quarter results on or about August 9, 2017.

On behalf of the Board of Directors,

[signed]

David J. Wilson
President and Chief Executive Officer
May 9, 2017

MANAGEMENT'S DISCUSSION & ANALYSIS

INTRODUCTION

Kelt Exploration Ltd. ("Kelt" or the "Company") is an oil and gas company based in Calgary, Alberta, focused on the exploration, development and production of crude oil and natural gas resources, primarily in northwestern Alberta and northeastern British Columbia. Kelt's land holdings are located in two core areas, namely: (a) Grande Prairie (including Pouce Coupe, Progress and La Glace), Alberta; and (b) Fort St. John (including Inga, Fireweed and Stoddart), British Columbia. The Company's common shares and 5% convertible debentures are listed on the Toronto Stock Exchange ("TSX") under the symbol "KEL" and "KEL.DB", respectively. The head office of Kelt is located at Suite 300, 311 - 6th Avenue S.W., Calgary, Alberta T2P 3H2.

The Company was incorporated under the *Business Corporations Act* (Alberta) on October 11, 2012 and was inactive until February 26, 2013. On April 16, 2015, the Company completed the acquisition of Artek Exploration Ltd. ("Artek") by acquiring all of the issued and outstanding common shares of Artek pursuant to a statutory plan of arrangement under the *Business Corporations Act* (Alberta) (the "Artek Acquisition"). Pursuant to the arrangement, Artek common shares were delisted from the TSX and Artek became a wholly-owned subsidiary of Kelt. Immediately following the Artek Acquisition, Articles of Amendment were filed to change the name of Artek to Kelt Exploration (LNG) Ltd. ("Kelt LNG"). Kelt has transferred all of its British Columbia ("BC") assets to Kelt LNG and at the same time, Kelt LNG has transferred all of its Alberta assets to Kelt. Kelt LNG operates in BC as a wholly-owned subsidiary of Kelt, headquartered in Calgary, Alberta.

Additional information relating to Kelt can be found on SEDAR at www.sedar.com.

This Management's Discussion and Analysis ("MD&A") is dated May 9, 2017 and should be read in conjunction with the Company's unaudited condensed consolidated interim financial statements and related notes as at and for the three months ended March 31, 2017 and its audited consolidated annual financial statements and MD&A as at and for the year ended December 31, 2016. The accompanying financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") as set out in the *CPA Canada Handbook - Accounting* ("CPA Handbook"). The CPA Handbook incorporates International Financial Reporting Standards ("IFRS") and publicly accountable enterprises, including Kelt, are required to apply such standards. The Company's Board of Directors approved and authorized the condensed consolidated interim financial statements for issue on May 9, 2017.

ADVISORY REGARDING FORWARD-LOOKING STATEMENTS

This MD&A contains forward-looking statements and forward-looking information within the meaning of applicable securities laws. The use of any of the words "expect", "anticipate", "continue", "estimate", "objective", "ongoing", "may", "will", "project", "should", "believe", "plans", "intends" and similar expressions are intended to identify forward-looking information or statements. In particular, this MD&A contains forward-looking statements pertaining to the following: Kelt's intention to incur sufficient qualifying expenditures to fully satisfy its flow-through share commitments; the Company's ability to continue accumulating land at a low-cost in its core operating areas and potentially monetize non-core assets; and the Company's expected future financial position and operating results, as well as the amount and timing of future development capital expenditures. Statements relating to "reserves" or "resources" are deemed to be forward looking statements, as they involve the implied assessment, based on certain estimates and assumptions, that the reserves described exist in the quantities predicted or estimated and that the reserves can be profitably produced in the future. Actual reserves may be greater than or less than the estimates provided herein.

Although Kelt believes that the expectations and assumptions on which the forward-looking statements are based are reasonable, undue reliance should not be placed on the forward-looking statements because Kelt cannot give any assurance that they will prove to be correct. Since forward-looking statements address future events and conditions, by their very nature they involve inherent risks and uncertainties. Actual results could differ materially from those currently anticipated due to a number of factors and risks. These include, but are not limited to, the risks associated with the oil and gas industry in general (e.g., operational risks in development, exploration and production; delays or changes in plans with respect to exploration or development projects or capital expenditures; the uncertainty of reserve estimates; the uncertainty of estimates and projections relating to production, costs and expenses; failure to obtain necessary regulatory approvals for planned operations; health, safety and environmental risks; uncertainties resulting from potential delays or changes in plans with respect to exploration or development projects or capital expenditures; volatility of commodity prices, currency exchange rate fluctuations; imprecision of reserve estimates; and competition from other explorers) as well as general economic conditions, stock market volatility; and the ability to access sufficient capital. We caution that the foregoing list of risks and uncertainties is not exhaustive.

In addition, the reader is cautioned that historical results are not necessarily indicative of future performance. The forward-looking statements contained herein are made as of the date hereof and the Company does not intend, and does not assume any obligation, to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise unless expressly required by applicable securities laws.

Certain information set out herein may be considered as "financial outlook" within the meaning of applicable securities laws. The purpose of this financial outlook is to provide readers with disclosure regarding Kelt's reasonable expectations as to the anticipated results of its proposed business activities for the periods indicated. Readers are cautioned that the financial outlook may not be appropriate for other purposes.

GROWTH STRATEGY

The business plan of Kelt is to create sustainable and profitable growth as a participant in the oil and gas industry in Canada. Kelt implements a full cycle exploration program, resulting in exploration and development drilling based on opportunities generated internally. From time to time, Kelt may complement its exploration and development drilling program by acquiring strategic oil and gas properties in order to further enhance its opportunity base.

Kelt is opportunity driven and is confident that it can grow its production base by building on its current inventory of development projects and by adding new exploration prospects. Kelt will endeavor to maintain a high quality product stream that on a historical basis receives a superior price with reasonably low production and transportation costs. In addition, the Company will focus its exploration efforts in areas of multi-zone hydrocarbon potential, primarily in northwestern Alberta and northeastern British Columbia. Kelt will continue to seek optimization of its asset base by building on its core properties and monetizing non-core assets.

RESULTS OF OPERATIONS

On January 18, 2017, Kelt completed the disposition of the majority of its oil and gas assets in the Karr area of Alberta (the "Karr Property Disposition") for cash proceeds of $103.0 million after closing adjustments. At the time of the disposition, the assets were producing approximately 1,300 BOE per day (50% oil and NGLs). The Company's operating results for the quarter ended March 31, 2017 include production and operating income from the assets disposed for the 17 day period prior to closing on January 18, 2017. Additional information regarding the Karr Property Disposition is provided under the heading of *"Capital Expenditures"* in this MD&A.

- Production averaged 20,204 BOE per day during the first quarter of 2017, up 2% from 19,762 BOE per day in the fourth quarter of 2016 and down 13% from 23,295 BOE per day during the first quarter of 2016.
- Revenue for the quarter ended March 31, 2017 was $60.2 million, up 49% from the same quarter of 2016 on the recovery of commodity prices. The Company's combined realized price averaged $33.12 per BOE during the first quarter of 2017 compared to $19.06 per BOE in the first quarter of 2016.
- During the first three months of 2017, corporate royalty rates averaged 11.0% of revenue, production and transportation expenses (combined) were $12.86 per BOE, interest expense was $0.98 per BOE and G&A expense was $0.91 per BOE. In the same three month period of 2016, royalties averaged 7.1% of revenue, production and transportation expenses (combined) were $12.95 per BOE, interest expense was $1.05 per BOE and G&A expense was $0.89 per BOE.
- Due to management's continued efforts to maintain a low cost structure, the increase in revenue (after royalties and financial instruments), had a direct impact on operating netbacks and funds from operations. Kelt's operating netback was $16.63 per BOE for the quarter ended March 31, 2017, 3.5 times more than the netback of $4.76 per BOE during the quarter ended March 31, 2016. Kelt's operating netback is also up 10% from $15.08 per BOE in the fourth quarter of 2016 primarily due to continued upward momentum in oil and NGLs prices.
- The Company generated adjusted funds from operations of $26.8 million ($0.15 per common share, diluted)

during the three months ended March 31, 2017, up 351% from $6.0 million ($0.04 per common share, diluted) in the first quarter of 2016 and up 16% from $23.1 million ($0.13 per common share, diluted) during the fourth quarter of 2016.

- Capital expenditures before proceeds from the Karr Property Disposition were $67.6 million during the first three months of 2017, of which $49.5 million was incurred for drilling and completion operations, including the completion of Kelt's five-well Montney pad in its core area at Pouce Coupe, Alberta. The Company also spent $2.5 million on land and seismic and $15.6 million on infrastructure.
- Kelt's bank debt, net of working capital was $75.8 million at March 31, 2017, down 45% from $138.0 million at December 31, 2016 and down 67% from $230.3 million at March 31, 2016.
- Proceeds of the Karr Property Disposition have been used initially to reduce indebtedness under the Company's Credit Facility (defined herein), on which Kelt had drawn $39.3 million as of March 31, 2017. The syndicate of lenders confirmed that the authorized borrowing amount available under the Credit Facility remained unchanged at $185.0 million following the Karr Property Disposition and have amended the Credit Facility to extend the revolving period to April 28, 2018. Kelt is well positioned to execute on its 2017 capital expenditure program and has sufficient financial flexibility to take advantage of opportunities as they arise.

PRODUCTION AND REVENUE

	Three months ended March 31		
(CA$ thousands, except as otherwise indicated)	**2017**	2016	%
Average daily production:			
Oil (bbls/d)	**5,797**	5,873	-1
NGLs (bbls/d)	**2,358**	2,740	-14
Gas (mcf/d)	**72,295**	88,093	-18
Combined (BOE/d)	**20,204**	23,295	-13
Average realized prices, before financial instruments:			
Oil ($/bbl)	**60.21**	34.01	77
NGLs ($/bbl)	**27.79**	14.24	95
Gas ($/mcf)	**3.52**	2.33	51
Combined ($/BOE)	**33.12**	19.06	74
Revenue, before royalties and financial instruments:			
Oil	**31,407**	18,175	73
NGLs	**5,898**	3,551	66
Gas	**22,920**	18,672	23
Revenue, before royalties and financial instruments	**60,225**	40,398	49

Production averaged 20,204 BOE per day during the first quarter of 2017, down 13% compared the first quarter of 2016 in which Kelt reported its highest inception-to-date quarterly average production of 23,295 BOE per day. Capital expenditures in 2016 were 80% lower than in 2015 and as a result, normal production declines and asset sales more than offset new production added from Kelt's successful drilling program during 2016. The Company's corporate average production decreased following closing of the Karr Property Disposition on January 18, 2017. Average production during the comparative quarter of 2016 included approximately 1,800 BOE per day of production from the assets disposed at Karr, which were producing approximately 1,300 BOE per day (50% oil and NGLs) at the time of the disposition.

Average production for the quarter ended March 31, 2017 is 2% higher than average production of 19,762 BOE per day during the quarter ended December 31, 2016. The Company has reported prolific initial results from wells recently drilled in its core areas at Pouce Coupe, Alberta, and at Fireweed, BC. New production added as these wells were tested or brought on stream during the first quarter of 2017 more than offset the impact of the Karr Property Disposition and also contributed to the significant increase in oil production. Average oil production during the first three months of 2017 increased by 22% (more than 1,000 barrels per day) compared to average oil production in the fourth quarter of 2016. Oil and NGLs production represented 40% of corporate average production during the first quarter of 2017 compared to 37% on average during 2016.

Revenue for the first quarter of 2017 was $60.2 million, up 49% from the first quarter of 2016, despite production volumes being 13% lower over the same period. Realized commodity prices have recovered significantly compared to the historical lows of the first quarter of 2016 and the Company's combined average sales price was up 74% to $33.12 per BOE during the first quarter of 2017. Kelt's average realized price is also up 8% compared to $30.66 per BOE during the fourth quarter of 2016 as a result of continued improvement of oil and NGLs prices in conjunction with higher oil production. Oil and NGLs sales represented 62% of total revenue during the three months ended March 31, 2017 compared to 54% of total revenue on average during 2016.

OIL OPERATIONS

References to "oil" in this discussion includes crude oil and field condensate (see "Other Measurements" for additional references).

	Three months ended March 31		
(CA$ thousands, except as otherwise indicated)	**2017**	2016	%
Oil production (bbls per day)	**5,797**	5,873	-1
Oil revenue, before royalties and financial instruments	**31,407**	18,175	73
Average realized oil prices ($/bbl):			
Before financial instruments	**60.21**	34.01	77
Realized gain (loss) on financial instruments	**-**	-	-
After financial instruments	**60.21**	34.01	77
Average realized price, percentage of CLS	**93%**	83%	12
Benchmark oil prices:			
WTI Cushing Oklahoma (US$/bbl) (1)	**51.90**	33.45	55
WTI Cushing Oklahoma (CA$/bbl) (2)	**68.66**	45.84	50
Canadian Light Sweet ("CLS") ($/bbl) (1)	**64.74**	41.22	57
CLS % of CA$WTI	**94%**	90%	5
Average exchange rate (CA$/US$) (1)	**1.3233**	1.3723	-4

(1) Source: Sproule Associates Limited.

(2) Source: Sproule Associates Limited, Canadian dollar equivalent price WTI price ("CA$WTI") is calculated based on monthly average US$WTI price and the monthly average CA$/US$ exchange rate.

Oil revenues increased by 73% in the first quarter of 2017 despite oil production volumes being relatively unchanged compared to the first quarter of 2016. Kelt realized an average price for its oil sales of $60.21 per barrel during the three months ended March 31, 2017, up from $34.01 per barrel during the comparative period of 2016. The 77% increase in the Company's average realized oil price reflects the recovery of global crude oil prices as well as improvements to Kelt's internal oil price realization relative to benchmark prices.

The Company's realized oil price is discounted to benchmark oil prices as the base price paid by purchasers is adjusted for quality and is net of all applicable fees and deductions, including pipeline tariffs or location differentials. These tariffs and differentials vary depending on the delivery point, but do not fluctuate with oil prices. Pipeline tariffs are classified as transportation expenses when the Company has firm commitments or contractual arrangements on the pipeline.

The average discount of Kelt's realized oil price relative to the CLS reference price was $4.53 per barrel (7% of CLS) during the first quarter of 2017, compared to a discount of $7.21 per barrel (17% of CLS) in the first quarter of 2016. The decrease in Kelt's oil price discount reflects a combination of improved contract pricing and fewer deductions, partly attributable to lower pipeline tariffs. Refer to further discussion under the heading of *"Transportation Expenses"*.

NGL OPERATIONS

References to “NGLs” in this discussion includes pentanes (C5 and C5+), butane (C4), propane (C3) and ethane (C2) (see “Other Measurements” for additional references).

	Three months ended March 31		
(CA$ thousands, except as otherwise indicated)	**2017**	2016	%
NGLs production (bbls per day)	**2,358**	2,740	-14
NGLs production (bbls per mmcf of natural gas sales)	**33**	31	6
NGLs revenue, before royalties and financial instruments	**5,898**	3,551	66
Average realized NGLs price ($/bbl):			
Before financial instruments	**27.79**	14.24	95
Realized gain (loss) on financial instruments	**(0.03)**	-	-
After financial instruments	**27.76**	14.24	95
Average realized price, percentage of CA$WTI (1)	**40%**	31%	29
Benchmark NGLs prices (2) ($/bbl):			
Edmonton Pentane	**71.35**	45.34	57
% of CA$WTI	**104%**	99%	5
Edmonton Butane	**44.54**	29.34	52
% of CA$WTI	**65%**	64%	1
Edmonton Propane	**28.88**	7.14	304
% of CA$WTI	**42%**	16%	163
Edmonton Ethane	**7.45**	5.08	47
% of CA$WTI	**11%**	11%	-

(1) Average realized NGLs price, before financial instruments, divided by the Canadian dollar equivalent WTI reference price for the period.

(2) Source: Sproule Associates Limited.

NGLs revenue increased by 66% compared to the same quarter of 2016 on the recovery crude oil prices and continued strengthening of NGLs prices. Although total NGLs production was down 14% as a result of lower natural gas production during the first quarter of 2017, Kelt’s corporate average NGLs barrels recovered per million cubic feet of natural gas increased to 33 bbls/mmcf, up 6% from 31 bbls/mmcf in the first quarter of 2016. NGL sales volumes were weighted 24% pentanes, 26% butane, 31% propane and 19% ethane during the quarter ended March 31, 2017. In the comparative quarter of 2016, NGL sales volumes were weighted 27% pentanes, 27% butane, 29% propane and 17% ethane.

The Company realized an average price for its NGL sales of $27.79 per barrel during the quarter ended March 31, 2017, up 20% from Kelt’s realized price of $23.11 per barrel during the fourth quarter ended December 31, 2016 and up 95% from $14.24 per barrel during the quarter ended March 31, 2016. Propane prices were at record lows and sometimes negative starting mid-2015 and through the first half of 2016. Since then, Western Canadian propane inventories have fallen to a more normal range and exports have increased, resulting in the recovery of propane prices starting in the fourth quarter of 2016 and peaking in January 2017. The Company also benefited from premium pentane prices during the first quarter of 2017, which contributed to the increase in Kelt’s average realized NGLs price as a percentage of WTI.

In January 2017, Kelt entered into a financial derivative contract to lock-in the stronger propane price and reduce the Company’s downside price risk on a notional 500 barrels per day of propane for the period from February 1, 2017 to December 31, 2017. Refer to additional information under the heading of *“Derivative Financial Instruments”*.

GAS OPERATIONS

References to "gas" in this discussion includes natural gas and sulphur (see "Other Measurements" for additional references).

	Three months ended March 31		
(CA$ thousands, except as otherwise indicated)	**2017**	2016	%
Gas production (MCF per day)	**72,295**	88,093	-18
Gas revenue, before royalties and financial instruments	**22,920**	18,672	23
Average realized gas price ($/MCF):			
Before financial instruments	**3.52**	2.33	51
Realized gain (loss) on financial instruments	**-**	-	-
After financial instruments	**3.52**	2.33	51
Kelt average premium (discount) to AECO 5A (1)	**31%**	27%	15
Benchmark gas prices:			
NYMEX Henry Hub (US$/MMBtu) (2)	**3.25**	2.05	59
AECO 5A (CA$/GJ) (3)	**2.55**	1.74	47
Spectra Station 2 Day Ahead Index (CA$/GJ) (4)	**2.36**	1.33	78
Average discount to AECO 5A (CA$/GJ)	**-8%**	-24%	-67
Sumas/Huntingdon ("Sumas") (CA$/MMBtu) (5)	**4.42**	-	-
Average premium to Station 2 (CA$/MMBtu)	**76%**	-	-
Platts Chicago City-Gate (CA$/MMBtu) (6)	**3.94**	2.82	40
Average premium to AECO 5A (CA$/MMBtu)	**46%**	54%	-15

(1) Kelt's average realized price (before financial instruments) relative to AECO 5A (CA$/MMBtu) assumes 1 MMBtu = 1 MCF.

(2) Source: Canadian Gas Price Reporter (Henry Hub 3-Day Average Close).

(3) Source: Canadian Gas Price Reporter (NGX AB-NIT Same Day Index 5A).

(4) Source: Canadian Gas Price Reporter (NGX Spectra Station #2 Day Ahead Index).

(5) Source: Canadian Gas Price Reporter (Sumas/Huntingdon (US$/MMBtu). The Canadian dollar equivalent Sumas price is calculated based on monthly average US$ price and the monthly average CA$/US$ exchange rate. The Sumas price is not provided for the comparative period as Kelt's contract was not in effective until November 2016.

(6) Source: Platts Chicago City-Gate (US$/MMBtu) per Tidal Energy Marketing Inc. The Canadian dollar equivalent Chicago City-Gate price is calculated based on monthly average US$ price and the monthly average CA$/US$ exchange rate.

The Company realized an average gas sales price of $3.52 per MCF during the quarter ended March 31, 2017, up 51% from $2.33 per MCF during the quarter ended March 31, 2016. Over the corresponding periods, the AECO 5A gas reference price averaged $2.55 per GJ and $1.74 per GJ, respectively. Kelt receives a premium to the AECO 5A gas price due to the higher heat content of its gas production as well as various gas marketing arrangements that the Company has in place to diversify and gain exposure to alternative markets.

The increase in Kelt's average premium to AECO 5A from 27% to 31% reflects a new contract that came into effect November 1, 2016, whereby the Company's BC gas production processed at the Spectra McMahon facility that was previously sold at discounted Station 2 prices, now receives Sumas pricing less a fixed differential. In January 2017, Sumas peaked at $6.15 per MMBtu or 2.3 times the Station 2 price of $2.66 per MMBtu. On average for the quarter ended March 31, 2017, Sumas was a 76% premium to Station 2 (64% premium to AECO 5A).

The Company currently receives Chicago City-Gate pricing on 25% to 30% of its gas sales volumes. The Canadian dollar equivalent Chicago City-Gate price averaged $3.94 per MMBtu during the first quarter of 2017, a premium of 46% above the equivalent AECO 5A price per MMBtu. The average premium is up from 28% during the fourth quarter of 2016, but lower than the average premium of 54% during the first quarter of 2016. The impact of the higher realized gas price on Kelt's funds from operations is partially offset by higher tolls on the Alliance pipeline, which are included in transportation expenses.

ROYALTIES

(CA$ thousands, except as otherwise indicated)	Three months ended March 31 2017	2016	%
Royalties, before Crown Cost Allowances:			
Oil	**4,669**	2,372	97
NGLs	**1,241**	673	84
Gas	**2,112**	1,414	49
Total, before Crown Cost Allowances	**8,022**	4,460	80
Crown Cost Allowances (1)	**(1,399)**	(1,601)	-13
Royalties	**6,623**	2,859	132
Royalties, before Crown Cost Allowances:			
Oil (% of oil revenue)	**14.9%**	13.1%	14
NGLs (% of NGLs revenue)	**21.1%**	19.0%	11
Gas (% of gas revenue)	**9.2%**	7.6%	22
Total, before Crown Cost Allowances (% of total revenue)	**13.3%**	11.0%	21
Crown Cost Allowances (% of total revenue)	**-2.3%**	-3.9%	-41
Royalties (% of total revenue)	**11.0%**	7.1%	55

(1) "Crown Cost Allowances" include Alberta Crown Gas Cost Allowance ("GCA") and BC Producer Cost of Service ("PCOS").

Kelt's corporate average royalty rate was 11.0% during the first quarter of 2017, up from 7.1% during the same quarter of 2016, primarily due to the significant increase in commodity prices as well as the higher proportion of oil and NGLs production.

Oil royalties averaged 14.9% of oil revenue for the quarter ended March 31, 2017, up from 13.1% in the comparative quarter due to higher oil prices, partly offset by lower royalties on new production that qualifies for various royalty incentives.

NGL royalties averaged 21.1% of NGLs revenue during the first quarter of 2017 compared to 19.0% in the first quarter of 2016. NGLs royalty rates do not fluctuate with NGLs prices, but are reduced by certain drilling incentive credits. In addition, Kelt's corporate average NGLs royalty rate is impacted by the relative weighting of NGLs royalties in BC and Alberta. During the first three months of 2017, a higher proportion of NGLs royalties were paid (or payable) in Alberta.

Gas royalties (before Crown Cost Allowances) averaged 9.2% during the first quarter of 2017, up from 7.6% of the same quarter of 2016 due to higher gas prices.

Crown royalties are reduced by Crown Cost Allowances including BC Producer Cost of Service ("PCOS") and Alberta Gas Cost Allowance ("GCA") credits which do not fluctuate with gas prices. The Company has estimated total GCA and PCOS credits of $1.4 million for the first quarter of 2017, down compared to $1.6 million estimated during the comparative quarter. There are numerous factors that impact the amount of PCOS and GCA, however, the decrease in total estimated Crown Cost Allowances is primarily due to the Karr Property Disposition.

PRODUCTION EXPENSES

	Three months ended March 31		
(CA$ thousands, unless otherwise indicated)	**2017**	2016	%
Production expense	**17,466**	21,712	-20
$ per BOE	**9.61**	10.24	-6

The Company incurred total production expenses of $17.5 million during the first three months of 2017, down 20% from the comparative quarter due to lower production as well as the Company's ongoing operational cost saving initiatives. In addition, with the Company's geographically concentrated asset base, Kelt is able to add new production at a lower incremental cost, reducing average production expenses per BOE.

The Company performed various maintenance operations and production optimization workovers during the first quarter of 2017 resulting in production expenses of $9.61 per BOE, up compared to Kelt's 2016 average production expense of $9.29 per BOE.

TRANSPORTATION EXPENSES

	Three months ended March 31		
(CA$ thousands, unless otherwise indicated)	**2017**	2016	%
Transportation expense (1)	**5,909**	5,739	3
$ per BOE	**3.25**	2.71	20

(1) Pipeline tariffs are classified as transportation expenses when the Company has firm commitments or contractual arrangements on the pipeline. Pipeline tariffs may also be incurred indirectly by way of deduction from the base price paid by the purchasers of the Company's oil, NGLs and gas sales. In the latter case, and in the absence of a firm contractual obligation on the pipeline, the pipeline tariffs are presented as a reduction of revenue rather than as transportation expense.

Transportation expenses averaged $3.25 per BOE for the first quarter of 2017 compared to $3.12 per BOE during the fourth quarter of 2016 and $2.71 per BOE in the first quarter 2016. The increase is due to the higher oil weighting of Kelt's average production as well as gas transportation commitments pursuant to which Kelt has secured additional firm pipeline capacity.

Oil transportation expenses averaged $2.52 per barrel during the quarter ended March 31, 2017 compared to $1.73 per barrel in the same quarter of 2016. Kelt incurred higher trucking costs during the quarter on new oil production that is not yet pipeline connected as well as a general increase in trucking rates. In addition, although Kelt's BC oil production is pipeline connected, at certain times the Company may truck BC volumes to terminals in Alberta. Kelt incurs higher transportation expense on these trucked volumes, but the impact on operating netbacks is relatively neutral as Kelt reports a higher realized oil price due to significantly lower pipeline tariffs, equivalent to approximately $5 per barrel (see footnote 1 regarding the presentation of pipeline tariffs).

FINANCING EXPENSES

(CA$ thousands, unless otherwise indicated)	Three months ended March 31		
	2017	2016	%
Interest and fees on bank debt	**673**	2,236	-70
Interest on convertible debentures	**1,110**	-	-
Total interest expense	**1,783**	2,236	-20
Accretion of convertible debentures	**832**	-	-
Accretion of decommissioning obligations	**721**	759	-5
Total financing expense	**3,336**	2,995	11
Interest expense per BOE (1)	**0.98**	1.05	-7
Average principal amount outstanding during period:			
Bank debt	**39,897**	196,266	-80
Convertible debentures	**90,000**	-	-
Average total principal amount of debt outstanding	**129,897**	196,266	-34

(1) Interest expense used in the calculation of "Interest expense per BOE" includes interest and fees on bank debt and accrued cash interest on convertible debentures.

The Company's total interest expense paid or payable in cash of $1.8 million ($0.98 per BOE) for the quarter ended March 31, 2017 is down 20% from the comparative period due to the significant decrease in average total debt outstanding following completion of the Karr Property Disposition, and on improved commodity prices.

On May 3, 2016, Kelt reduced borrowings under its revolving bank credit facility using the net proceeds of the offering of $90.0 million principal amount of convertible unsecured subordinated debentures (the "Debentures"). The Debentures mature on May 31, 2021 and bear interest at 5.0% per annum, payable semi-annually on May 31st and November 30th. Financing expense for the quarter ended March 31, 2017 includes $1.1 million of accrued cash interest and $0.8 million of non-cash accretion expense. The Debentures are convertible onto common shares of the Company at a conversion price of $5.50 per share. Based on the closing price of Kelt common shares on the TSX of $6.68 per share on March 31, 2017, the Debentures are "in-the-money".

The Company has a revolving committed term credit facility (the "Credit Facility") with a syndicate of financial institutions. Amounts drawn under the Credit Facility are primarily in the form of bankers' acceptances ("BAs"). BA stamping fees fluctuate based on a pricing grid and range from 2.0% to 3.5%, depending upon the Company's quarter-end debt to cash flow ratio of between less than one and one tenth times to greater than three times. The Company's debt to cash flow ratio has improved significantly and Kelt realized a 125 basis point decrease in the applicable margin under the Credit Facility compared to the first quarter of 2016. The impact of lower interest and stamping fees is partly offset by higher standby charges on the undrawn portion of the Credit Facility.

Additional information regarding the Credit Facility and Debentures is provided under the heading of *"Capital Resources and Liquidity"*.

GENERAL AND ADMINISTRATIVE ("G&A") EXPENSES

The following table summarizes significant components of the Company's G&A expenses:

	Three months ended March 31		
(CA$ thousands, unless otherwise indicated)	**2017**	2016	%
Salaries and benefits	**2,016**	1,627	24
Other G&A expenses	**1,038**	1,162	-11
Gross G&A expenses	**3,054**	2,789	10
Overhead recoveries	**(1,408)**	(902)	56
G&A expense, net of recoveries	**1,646**	1,887	-13
Gross G&A ($ per BOE)	**1.68**	1.32	27
Net G&A ($ per BOE)	**0.91**	0.89	2

Kelt continues to incur below industry average G&A expenses as a result of management's continued efforts to maintain a low cost structure. G&A expense of $0.91 per BOE for the first quarter of 2017 is in line with Kelt's average G&A expense reported for the year ended December 31, 2016.

G&A expenses are reported net of overhead recoveries, however, Kelt does not capitalize any direct G&A expenses. Kelt earned higher overhead recoveries in the current quarter, primarily due to the significant increase in capital expenditures (before proceeds from dispositions).

SHARE BASED COMPENSATION ("SBC")

	Three months ended March 31		
(CA$ thousands, unless otherwise indicated)	**2017**	2016	%
Stock options	**896**	865	4
Restricted share units ("RSUs")	**354**	528	-33
Total SBC expense	**1,250**	1,393	-10
$ per BOE	**0.69**	0.66	5

Share based compensation is expensed using graded amortization over the three year vesting period. The 10% decrease in total SBC expense reflects management's efforts to provide long term incentives to employees while minimizing the dilutive impact to shareholders. As at March 31, 2017, stock options and RSUs outstanding represent 5% of total shares outstanding (5% of total shares outstanding at December 31, 2016).

EXPLORATION AND EVALUATION ("E&E") EXPENSES

	Three months ended March 31		
(CA$ thousands, unless otherwise indicated)	**2017**	2016	%
Expired mineral leases	**63**	629	-90
$ per BOE	**0.03**	0.30	-90

The Company expensed $0.1 million of costs related to the expiry of non-core land holdings during the quarter ended March 31, 2017. The majority of the mineral leases expired during 2016 were acquired through corporate acquisitions.

DEPLETION AND DEPRECIATION

	Three months ended March 31		
(CA$ thousands, unless otherwise indicated)	**2017**	2016	%
Depletion of D&P assets	**27,025**	40,717	-34
Depreciation of corporate assets	**202**	213	-5
Total depletion and depreciation	**27,227**	40,930	-33
Depletion and depreciation ($/BOE)	**14.97**	19.31	-22

The Company calculates depletion of development and production ("D&P") assets based on production relative to total proved reserves, for each depletion unit. Depletion expense of $27.0 million for the first three months of 2017 is down by 34% or $13.7 million from the comparative period, of which, approximately $4.3 million is attributed to the Karr Property Disposition. In addition, while the decrease in depletion is partly due to lower production volumes in the current quarter, the significant decrease of depletion expense per BOE reflects the Company's improving capital efficiencies. In particular, Kelt has added proved reserves at lower than historical finding and development capital costs.

GAIN (LOSS) ON SALE OF ASSETS

	Three months ended March 31		
(CA$ thousands, unless otherwise indicated)	**2017**	2016	%
Gain (loss) on sale of assets	**(21)**	2,134	-101%

On January 18, 2017, Kelt completed the Karr Property disposition for proceeds of $103.0 million after estimated closing adjustments. The assets and associated decommissioning obligations disposed were classified as held for sale as at December 31, 2016. Kelt reported an impairment reversal of $32.2 million during the fourth quarter ended December 31, 2016, based on the increase in fair value of the Karr property evidenced by the cash purchase price.

On March 31, 2016, the Company disposed of certain non-core assets located at Boundary Lake in northwestern Alberta, for gross proceeds of $1.1 million and reported a gain of $2.1 million.

Refer to additional information in respect of property dispositions under the heading of *"Capital Expenditures"*.

DERIVATIVE FINANCIAL INSTRUMENTS

The Company may, from time to time, enter into fixed price contracts and derivative financial instruments with respect to commodity prices, currency exchange and interest rates in order to secure a certain amount of cash flow to protect a desired level of capital spending. Fair value accounting for derivative financial instruments may cause significant fluctuations in the reported amounts of derivative financial instrument assets and liabilities and the resultant magnitude of unrealized gains and losses.

	Three months ended March 31		
(CA$ thousands, unless otherwise indicated)	**2017**	2016	%
Realized gain (loss)	**25**	(14)	-279
Unrealized gain	**237**	123	93
Gain on derivative financial instruments	**262**	109	140
$ per BOE	**0.23**	0.05	360

Interest rate risk management contracts

The Company is exposed to interest rate risk to the extent that changes in market interest rates will impact the Company's Credit Facility which is subject to a floating interest rate. Based on average bank debt outstanding of $39.9 million during the first quarter of 2017, an increase (decrease) in the market rate of interest by 25 basis points would have increased (decreased) interest expense by $0.1 million. During the previous year ended December 31, 2016, Kelt had an interest rate swap fixing CDOR at 0.925% on a notional amount of $100 million until June 30, 2017. In January 2017, in conjunction with the Karr Property Disposition and resulting reduction in bank debt, the interest rate swap was unwound and terminated for proceeds of $10 thousand.

Commodity price risk management contracts

As at March 31, 2017, the following commodity price risk management contracts are outstanding:

Contract Type	Notional Volume	Reference Prices	Fixed Contract Price	Remaining Term	Fair value Asset (Liability)
Financial Swap Natural Gas	10,000 MMBtu/d	SoCAL Border Avg. NYMEX Henry Hub	SoCAL Border Avg. plus US$0.055 per MMBtu	April to October 2017	**(624)**(1)
Financial Swap Propane	500 bbls/d	OPIS-Conway propane WTI Cushing Oklahoma	50% of US$WTI	April to December 2017	**237**(2)

(1) The fair value is sensitive to changes in natural gas reference prices. If the Southern California Border Average ("SoCAL Border Avg.") - NYMEX basis differential increased (decreased) by $0.10/MMBtu, the fair market value of the contract would decrease (increase) by approximately $0.3 million.

(2) The fair value is sensitive to changes in propane reference prices. If the OPIS-Conway propane price increased (decreased) by 5% relative to the fixed contract price, the fair market value of the contract would decrease (increase) by approximately $0.2 million.

Foreign exchange risk management contracts

As at March 31, 2017, the following foreign exchange risk management contract was outstanding:

Contract Type	Notional Amount per month	Fixed Contract Price	Remaining Term	Fair value Asset (Liability)
FX swap(1)	US$1,000,000	CA$/US$ 1.3300	April to December 2017	**25**(2)

(1) The FX swap outstanding at March 31, 2017 resulted from an FX swaption contract which was exercised by the counterparty on December 30, 2016. Kelt received a cash premium of $0.255 million at the time of entering into the contract on July 11, 2016.

(2) The fair value of the contract is sensitive to changes in the exchange rate. If the CA$/US$ exchange rate increased (decreased) by $0.05, the fair market value of the contract would decrease (increase) by approximately $0.5 million.

In November 2016, Kelt received a cash premium of $0.205 million for entering into a forward foreign exchange swaption contract whereby the counterparty had the right, if exercised on March 31, 2017, to enter a series of forward foreign exchange transactions fixing the exchange rate on a notional US$1.0 million per month at CA$/US$ 1.3600 from April 2017 to March 2018. The swaption was not exercised on March 31, 2017 and Kelt has no further obligations under the contract.

INCOME TAXES

	Three months ended March 31		
(CA$ thousands, unless otherwise indicated)	**2017**	2016	%
Deferred income tax recovery	**(627)**	(9,585)	-93
Loss before taxes	**(2,894)**	(35,503)	-92
Effective tax recovery rate	**22%**	27%	-20

The consolidated combined federal and provincial statutory tax rate averaged 26.2% and 26.6% during the three months ended March 31, 2017 and 2016, respectively.

A detailed analysis of the provision for deferred income taxes is included in note 12 of the interim financial statements, which includes a reconciliation of the difference between the deferred income tax recovery reported relative to expected recovery based on the statutory tax rate. The lower rate of tax recovery during the current quarter is due to qualifying expenditures incurred and renounced in respect of flow-through shares.

On November 2, 2016, the Company issued 1.0 million FTS in respect of Canadian development expenses for gross proceeds of $7.1 million. The FTS were issued at a price of $7.10 per FTS, resulting in a premium of $0.9 million or $0.88 per FTS. As at December 31, 2016, Kelt had incurred $5.8 million of qualifying expenditures and the remaining commitment of $1.3 million was incurred during the first quarter of 2017. The qualifying expenditures have been renounced to subscribers with an effective date of March 31, 2017.

Kelt was not required to pay income taxes in the current or prior year as the Company had sufficient income tax deductions available to shelter taxable income. The Company's consolidated tax pools are estimated to be approximately $912.5 million as of March 31, 2017, down 6% from $975.4 million at December 31, 2016. Proceeds from the Karr Property Disposition of $100.0 million, before closing adjustments, reduced Kelt's COGPE and UCC tax pools by $80 million and $20 million, respectively.

(CA$ thousands, unless otherwise indicated)	Rate	**2017**	2016	% change
Canadian oil and gas property expenses (COGPE)	10%	**162,958**	248,468	-34%
Canadian development expenses (CDE)	30%	**190,320**	154,830	23%
Canadian exploration expenses (CEE)	100%	**94,877**	94,597	0%
Undepreciated capital cost[(1)] (UCC)	25%	**162,537**	177,487	-8%
Share and debt issue costs (SIC/DIC)	5 years	**12,087**	13,795	-12%
Non-capital losses[(2)] (NCL)	100%	**289,699**	286,219	1%
Estimated tax deductions available, end of year		**912,478**	975,396	-6%

(1) The majority of the Company's undepreciated capital cost deductions relate to Class 41 assets, which are deductible at a rate of 25% per year.

(2) The Company's non-capital losses expire in years 2023 to 2036.

ADJUSTED FUNDS FROM OPERATIONS

Three months ended March 31	**2017**		2016		% change	
(CA$ thousands, unless otherwise indicated)	**Amount**	**$/BOE**	Amount	$/BOE	Amount	$/BOE
Petroleum and natural gas revenue	**60,225**	**33.12**	40,398	19.06	49	74
Realized gain on financial instruments [(1)]	**15**	**0.01**	-	-	-	-
Royalties	**(6,623)**	**(3.64)**	(2,859)	(1.35)	132	170
Revenue, after royalties and financial instruments	**53,617**	**29.49**	37,539	17,71	43	67
Production expense	**(17,466)**	**(9.61)**	(21,712)	(10.24)	-20	-6
Transportation expense	**(5,909)**	**(3.25)**	(5,739)	(2.71)	3	20
Operating income [(2)]	**30,242**	**16.63**	10,088	4.76	200	249
Financing expense [(3)]	**(1,783)**	**(0.98)**	(2,236)	(1.05)	-20	-7
G&A expense	**(1,646)**	**(0.91)**	(1,887)	(0.89)	-13	2
Realized gain (loss) on financial instruments [(4)]	**10**	**0.01**	(14)	(0.01)	-171	-200
Adjusted funds from operations [(5)]	**26,823**	**14.75**	5,951	2.81	351	425
Basic ($ per common share) [(6)]	**0.15**		0.04		275	
Diluted ($ per common share) [(6)]	**0.15**		0.04		275	
Common shares outstanding (000s):						
Basic, weighted average	**175,715**		168,824		4	
Diluted, weighted average	**176,782**		168,869		5	

(1) Includes realized gains (losses) on commodity price and foreign exchange derivatives. Excludes realized gains (losses) on interest rate swaps.

(2) "Operating income" is a non-GAAP financial measure which is calculated by deducting royalties, production expenses and transportation expenses from petroleum and natural gas revenue, after realized gains or losses on associated financial instruments.

(3) Excludes non-cash accretion of decommissioning obligations and convertible debentures.

(4) Includes realized gains (losses) on interest rate swaps.

(5) "Adjusted funds from operations" is a non-GAAP financial measure which is calculated as cash provided by operating activities before changes in non-cash operating working capital, and adding back (if applicable): transaction costs, provisions for potential credit losses, and settlement of decommissioning obligations.

(6) Adjusted funds from operations per common share is calculated on a consistent basis with profit (loss) per common share, using basic and diluted weighted average common shares as determined in accordance with GAAP.

The Company generated adjusted funds from operations of $26.8 million ($0.15 per common share, diluted) during the three months ended March 31, 2017, up 351% from $6.0 million ($0.04 per common share, diluted) in the first quarter of 2016 and up 16% from $23.1 million ($0.13 per common share, diluted) during the fourth quarter of 2016.

The increase in adjusted funds from operations is primarily attributed to the 49% increase in revenues driven by significant improvement in realized oil and gas prices, which more than offset lower production volumes during the first quarter of 2017. With the combined level of production expenses being relatively flat quarter-over-quarter, the increase in revenue (after royalties and financial instruments) contributed directly to the Company's operating netback, which averaged $16.63 per BOE during the quarter ended March 31, 2017. Similarly, the Company's low financing and G&A expenses result in the majority of operating income generated in the field contributing directly to Kelt's net funds from operations.

LOSS AND COMPREHENSIVE LOSS

	Three months ended March 31		
(CA$ thousands, unless otherwise indicated)	**2017**	2016	%
Loss and comprehensive loss	**(2,267)**	(25,918)	-91
Wtd avg. shares outstanding, basic (000s)	**175,715**	168,824	4
Wtd avg. shares outstanding, diluted (000s) (1)(2)	**175,715**	168,824	4
$ per common share, basic	**(0.01)**	(0.15)	-93
$ per common share, diluted (1)(2)	**(0.01)**	(0.15)	-93
$ per BOE	**(1.25)**	(12.23)	-90

(1) The Company uses the treasury stock method to determine the dilutive effect of stock options and RSUs. Under this method, only "in-the-money" dilutive instruments impact the calculation of diluted profit per common share. In computing the diluted loss per common share for the three months ended March 31, 2017 and 2016, the Company excluded the effect of stock options and RSUs as they were anti-dilutive. Therefore, the diluted weighted average is equal to the basic weighted average shares outstanding in those periods.

(2) The common shares potentially issuable on conversion of the Debentures are excluded from the calculation of diluted weighted average shares outstanding as they were anti-dilutive for the quarter ended March 31, 2017.

Kelt reported a loss of $2.3 million ($0.01 per common share, diluted) for the three months ended March 31, 2017, compared to a loss of $25.9 million ($0.15 per common share, diluted) in the same three month period of 2016. The decrease in loss is primarily due to the $20.2 million increase in operating income and decrease in depletion expense of $13.7 million, partly offset by the corresponding reduction in the deferred income tax recovery.

INVESTING ACTIVITIES

CAPITAL EXPENDITURES

Kelt is committed to future growth through its strategy to implement a full-cycle exploration and development program. In addition, Kelt has completed strategic acquisitions of oil and gas properties where it believes further exploitation, development and exploration opportunities exist. Kelt will continue to seek optimization of its asset base by building on its core properties and monetizing non-core assets.

The Company's total capital expenditures, including acquisitions and dispositions ("A&D"), are summarized in the following table:

	Three months ended March 31		
(CA$ thousands, unless otherwise indicated)	**2017**	2016	%
Capital expenditures:			
Lease acquisition and retention	**2,212**	740	199
Geological and geophysical	**280**	-	-
Drilling and completion of wells	**49,493**	13,331	271
Facilities, pipeline and well equipment	**15,517**	10,473	48
Corporate assets	**110**	8	1275
Capital expenditures, before A&D	**67,612**	24,552	175
Property acquisitions	**-**	37	-100
Property dispositions	**(102,976)**	(1,184)	8597
Total capital expenditures, net of dispositions	**(35,364)**	23,405	-251

Karr Property Disposition

On January 18, 2017, Kelt completed the disposition of the majority of its oil and gas assets in the Karr area of Alberta (the "Karr Property Disposition"). The disposition had an effective date of January 1, 2017. Kelt received gross cash proceeds, prior to adjustments at closing and following the waiver of certain preferential rights, in the amount of $100.0 million. Net proceeds have been used, initially, to reduce indebtedness under the Company's Credit Facility. The syndicate of lenders confirmed that the authorized borrowing amount available under the Credit Facility remained unchanged at $185.0 million.

The assets and associated decommissioning obligations disposed pursuant to the Karr Property Disposition were classified as held for sale as at December 31, 2016. Immediately prior to the initial classification as held for sale, the net carrying amount of PP&E was $68.9 million, including accumulated impairment of $46.2 million recognized during the year ended December 31, 2015. As at December 31, 2016, the impairment loss was partially reversed by $32.2 million based on the estimated fair value of consideration in excess of the carrying amount.

Estimates as of: *(CA$ thousands)*	**March 31 2017**	December 31 2016	Change in Estimates
Gross purchase price	100,000	100,000	-
Estimated closing adjustments (1)	2,976	2,926	50
Fair value of consideration (1)	**102,976**	**102,926**	**50**
Exploration and evaluation assets	4,377	4,377	-
Property, plant and equipment, net (2)	101,152	101,081	71
Assets held for sale and disposed	105,529	105,458	71
Decommissioning obligations held for sale and disposed(3)	(2,532)	(2,532)	-
Net assets held for sale and disposed	**102,997**	**102,926**	**71**

(1) At the time of preparation of the interim financial statements, closing adjustments are estimated to be approximately $3.0 million and include estimates for certain capital expenditures and operating income between the effective and closing date of the disposition. The total amount of

adjustments will not be known until completion of the final statement of adjustments and as a result, the fair value of consideration may differ from this estimate.

(2) Cost of $163.2 million, net of accumulated depletion and depreciation of $48.1 million and accumulated impairment of $14.0 million (net of impairment reversal).

(3) The carrying amount of the decommissioning obligations held for sale was estimated based on a risk-free rate of 2.3% and an inflation rate of 2.0% as at December 31, 2016. The undiscounted cash flows required to settle the obligations were estimated to be approximately $2.7 million.

Key Attributes of the Karr Property Disposition:

- At December 31, 2016, as evaluated by Sproule, proved reserves were 7.7 million BOE ($71.3 million of FDC required to develop proved reserves) and proved plus probable reserves were 13.5 million BOE ($105.3 million of FDC required to develop proved plus probable reserves) of which 26% were oil, 21% were NGLs and 53% were gas;
- Average production for December 2016 was approximately 1,300 BOE per day (34% oil, 16% NGLs and 50% gas);
- Land holdings include 16,480 gross acres (25.7 sections) and 16,400 net acres (25.6 sections) of which 9,920 gross acres (15.5 sections) and 9,840 net acres (15.4 sections) included Montney rights. Approximately 79% of net land holdings were classified as undeveloped by Kelt; and
- Tangible equipment includes a 100% interest in the Kelt Karr 10-21-65-3W6 oil battery and a 2.26% interest in the CNRL Karr 10-10-65-2W6 gas plant.

Kelt retained certain non-operated interests at Karr with current production of approximately 120 BOE per day and a 1.0% interest in the CNRL Karr 10-10-65-2W6 gas plant. The Company may endeavour to divest of these minor interests in the future.

Property Acquisitions and Dispositions – Year ended December 31, 2016

On March 31, 2016, the Company disposed of certain non-core assets located at Boundary Lake in northwestern Alberta, for cash consideration of $1.2 million, after closing adjustments, and reported a gain of $2.0 million. The carrying amount of decommissioning obligations disposed was $2.4 million, which exceeded the $1.4 million combined carrying amount of the E&E and D&P assets. At the time of disposition, production from the assets was approximately 16 BOE per day.

On April 28, 2016, the Company closed an acquisition of oil and gas assets in its core area at Progress, Alberta, for cash consideration of $18.5 million, after closing adjustments. The acquisition included approximately 600 BOE per day of production (60% light oil), 4,135 net acres of land, and infrastructure that is an integral part of Kelt's existing light oil play at Progress.

On September 21, 2016, Kelt completed a disposition of certain non-producing assets located at Karr, Alberta, for cash consideration of $5.0 million and recognized a gain of $2.6 million. The assets disposed primarily consisted of undeveloped land with a carrying amount of $2.5 million and decommissioning obligations of $0.1 million.

On October 7, 2016, Kelt completed the disposition of certain non-core assets located at Stoddart, BC, for proceeds of one dollar, before closing adjustments. Kelt discharged liabilities for future abandonment and site restoration of approximately $9.2 million ($9.6 million undiscounted) as a result of the disposition. At the time of the disposition, production from the assets was approximately 11 BOE per day as the majority of wells were inactive and did not have reserves assigned.

CAPITAL RESOURCES AND LIQUIDITY

Kelt's capital management objective is to maintain a flexible capital structure and sufficient liquidity to allow the Company to execute on its capital investment program and strategic growth plan. The Company strives to actively manage its capital structure in response to changes in economic conditions and the risk characteristics of its underlying oil and natural gas assets. As at March 31, 2017, Kelt's capital structure was comprised of shareholders' capital, convertible debentures, bank debt and working capital.

The Company monitors its capital structure and short-term financing requirements using a net bank debt to trailing adjusted funds from operations ratio, which is a non-GAAP financial measure. Kelt targets a net bank debt to trailing adjusted funds from operations ratio of less than 2.0 times.

	March 31, 2017	December 31, 2016
Bank debt	**39,258**	111,693
Working capital deficiency	**36,507**	26,349
Bank debt, net of working capital (1	**75,765**	138,042
Trailing annualized adjusted funds from operations (2)(3)	**102,004**	92,400
Net bank debt to trailing adjusted funds from operations ratio (1)	**0.7**	1.5

(1) "Net bank debt" is equal to "Bank debt, net of working capital" determined in accordance with GAAP.

(2) Adjusted funds from operations is a non-GAAP financial measure which is calculated as cash provided by operating activities before changes in non-cash operating working capital, and adding back (if applicable): transaction costs, provisions for potential credit losses, and settlement of decommissioning obligations.

(3) Trailing adjusted funds from operations is annualized based on the most recent quarter's adjusted funds from operations.

The Company has reduced its net bank debt to trailing adjusted funds from operations ratio to 0.7 times as at March 31, 2017 from 1.5 times at December 31, 2016. The Karr Property Disposition was completed on January 18, 2017 for cash proceeds of $103.0 million. The proceeds have been used initially to reduce bank indebtedness under the Credit facility and were used, along with $25.9 million of cash provided by operating activities, to fund exploration and development capital expenditures of $67.6 million during the first quarter of 2017. Future capital expenditures are expected to be funded through a combination of cash flow from operations and bank debt, supplemented with new equity or debt offerings if required.

The capital intensive nature of Kelt's operations may create a working capital deficiency position during periods with high levels of capital investment. However, during such periods, the Company maintains sufficient unused bank credit lines to satisfy such working capital deficiencies. As at March 31, 2017, the Company's working capital deficit of $36.5 million combined with outstanding bank debt of $39.3 million, represented 41% of the authorized borrowing amount available under the Credit Facility of $185.0 million (down from 75% of the authorized borrowing amount at December 31, 2016).

CREDIT FACILITY

The Company has a revolving committed term credit facility ("the Credit Facility") with a syndicate of financial institutions. As at March 31, 2017, the authorized borrowing amount available under the Credit Facility was $185.0 million. The Credit Facility is available for a revolving period of 364 days, maturing on April 29, 2017, and may be extended annually at Kelt's option and subject to lender approval, with a 364 day term-out period if not renewed. The Credit Facility is subject to semi-annual borrowing base reviews, occurring approximately in April and October of each year. In the event that the lenders reduced the borrowing base below the amount drawn at the time of the redetermination, the Company would have 60 days to eliminate any borrowing base shortfall by repaying the amount drawn in excess of the re-determined borrowing base or by providing additional security or other consideration satisfactory to the lenders. Repayments of principal are not required provided that the borrowings under the facility do not exceed the authorized borrowing amount and the Company is in compliance with all covenants, representations and warranties.

Subsequent to the quarter ended March 31, 2017, the Company and its lenders completed the semi-annual review and amended the Credit Facility to extend the current revolving period to April 28, 2018, with a term-out to April 28, 2019 if not renewed. The authorized borrowing amount is unchanged at $185.0 million.

There are no financial covenants under the Credit Facility and Kelt is in compliance with all other covenants. Covenants include industry standard positive and negative covenants including reporting requirements, permitted indebtedness, permitted dispositions (to a maximum in each calendar year which are in the aggregate not more than 5% of the borrowing base then in effect), permitted risk management activities (as more particularly described in note 13 of the interim financial statements), permitted encumbrances and other standard business operating covenants. Security is provided for by a first fixed and floating charge debenture over all assets in the amount of $800.0 million and general assignment of book debts.

CONVERTIBLE DEBENTURES

On May 3, 2016, the Company issued $90.0 million principal amount of convertible unsecured subordinated debentures (the "Debentures") for net proceeds of $86.4 million. The Debentures mature on May 31, 2021 (the "Maturity Date") and bear interest at 5.0% per annum payable semi-annually on May 31st and November 30th, commencing November 30, 2016. At the holder's option, the Debentures may be converted into common shares of the Company at any time prior to the close of business on the earlier of the business day immediately preceding (i) the Maturity Date, (ii) if called for redemption, the date fixed for redemption by the Company, or (iii) if called for repurchase in the event of a change of control, the payment date, at a conversion price of $5.50 per share (the "Conversion Price"), being a conversion rate of approximately 181.8182 common shares per $1,000 principal amount of Debentures, subject to adjustment in certain circumstances. The Debentures are "in-the-money" based on the closing price of Kelt common shares on the TSX of $6.68 as at March 31, 2017. To date, there have been no conversions the $90.0 million principal amount is outstanding.

The Debentures are redeemable by the Company after May 31, 2019 and prior to May 31, 2020, in whole or in part, from time to time, on not more than 60 days and not less than 40 days prior notice at a redemption price equal to their principal amount plus accrued and unpaid interest, if any, up to but excluding the date set for redemption, provided that the volume weighted average trading price of the common shares on the TSX for the 20 consecutive trading days ending five trading days (the "Current Market Price") prior to the date on which notice of redemption is provided is at least 125% of the Conversion Price. On or after May 31, 2020 and prior to the Maturity Date, the Debentures may be redeemed by the Company, in whole or in part, from time to time, on not more than 60 days and not less than 40 days prior notice at a redemption price equal to their principal amount plus accrued and unpaid interest, if any, up to but excluding the date set for redemption.

The Company may, at its option, elect to satisfy its obligation to repay all or any portion of the principal amount of the Debentures upon redemption or due at maturity, by issuing common shares instead of cash (subject to the receipt of any required regulatory approvals and provided that no event of default has occurred). The number of common shares to be issued would be obtained by dividing the principal amount of the Debentures by 95% of the Current Market Price on the date fixed for redemption or maturity, as applicable.

The Debentures trade on the TSX under the symbol "KEL.DB". As at March 31, 2017, the fair value of the Debentures was $130.5 million based on the closing market price of $145.00 per Debenture on March 30, 2017, being the date the Debentures last traded in the first quarter, unchanged from the fair value of $130.5 million at December 31, 2016.

SHARE INFORMATION

The Company is authorized to issue an unlimited number of common shares and an unlimited number of preferred shares. As at March 31, 2017 there were 175.8 million common shares issued and outstanding (as at May 9, 2017, there are 175.8 million common shares outstanding). There are no preferred shares issued or outstanding.

The Company's common shares trade on the TSX under the symbol "KEL". During the first three months of 2017, 60.6 million common shares traded on the TSX at a weighted average price of $6.46 per common share, up from the volume weighted average trading price of $4.93 per common share during the year ended December 31, 2016.

As at March 31, 2017, officers, directors, and employees have been granted options to purchase 8.3 million common shares of the Company at an average exercise price of $6.59 per common share. In addition, there are 0.6 million RSUs outstanding. Options and RSUs outstanding at March 31, 2017 represented 5.1% of total common shares issued and outstanding. Additional information regarding the Company's stock options and RSUs is included in note 11 of the interim financial statements.

CONTRACTUAL OBLIGATIONS

As of March 31, 2017, the Company is committed to future payments under the following agreements:

(CA$ thousands)	2017	2018	2019	2020	2021	Thereafter
Operating lease - office buildings	1,036	577	108	18	-	-
Operating lease - vehicles	269	273	161	17	-	-
Flow-through shares (1)	2,500	-	-	-	-	-
Firm processing commitments	5,507	3,881	-	-	-	-
Firm transportation commitments (2)	12,737	7,820	5,372	2,594	1,964	8,377
Total annual commitments	**22,049**	**12,551**	**5,641**	**2,629**	**1,964**	**8,377**

(1) On August 23, 2016, the Company raised gross proceeds of $2.5 million by issuing 0.385 million FTS at a price of $6.50 per FTS, resulting in a premium of $0.6 million or $1.66 per FTS. The premium is deferred at March 31, 2017 and the Company expects satisfy its commitment by incurring eligible Canadian exploration expenses prior to December 31, 2017.

(2) A portion of Kelt's commitments on the Alliance pipeline are denominated in US dollars. The volumes committed vary over the term of the contracts, which are effective until October 31, 2017, however, the maximum US denominated commitment in a given month does not exceed US$0.31 million. Amounts are translated to Canadian dollars at the spot rate on March 31, 2017 of CA$/US$1.3310.

The Company has firm commitments for oil and gas transportation on major pipelines in Alberta and British Columbia. For periods subsequent to 2021, Kelt has an annual commitment of $1.2 million for gas transportation until March 31, 2026 and an annual commitment of $0.6 million for oil transportation until June 30, 2027.

Payments under the office building operating leases relate to the Company's head office in Calgary, Alberta, and field offices in Grande Prairie, Alberta and Fort St. John, British Columbia. The leases expire on April 30, 2018, February 28, 2020, and November 30, 2018, respectively, if not extended.

RELATED PARTY TRANSACTIONS

A director of the Company is also a partner at a law firm which Kelt has engaged to provide legal services. During the three months ended March 31, 2017, the Company incurred $0.1 million (2016 – $0.1 million) in legal fees and disbursements, of which $0.1 million is payable at March 31, 2017 ($0.1 million at December 31, 2016). The Company expects to continue using the services of this law firm from time to time.

OFF-BALANCE SHEET TRANSACTIONS

The Company did not engage in any off-balance sheet transactions during the periods ended March 31, 2017 and 2016.

SUMMARY OF QUARTERLY RESULTS

The following tables summarize the Company's financial and operating results over the past eight quarters:

(CA$ thousands, except as otherwise indicated)	**Q1 2017**	Q4 2016	Q3 2016	Q2 2016
Revenue, before royalties and financial instruments	**60,225**	55,737	47,760	40,718
Adjusted funds from operations	**26,823**	23,100	17,658	11,671
Per share – basic ($/common share)	**0.15**	0.13	0.10	0.07
Per share – diluted ($/common share)	**0.15**	0.13	0.10	0.07
Profit (loss) and comprehensive income (loss)	**(2,267)**	11,856	(15,299)	(20,413)
Per share – basic ($/common share)	**(0.01)**	0.07	(0.09)	(0.12)
Per share – diluted ($/common share)	**(0.01)**	0.07	(0.09)	(0.12)
Total capital expenditures, net of dispositions	**35,364**	36,339	12,616	25,908
Total assets	**1,193,644**	1,255,958	1,232,147	1,260,245
Bank debt	**39,258**	111,693	122,024	126,993
Working capital deficiency	**36,507**	26,349	10,447	12,087
Convertible debentures	**71,810**	70,978	70,134	69,320
Shareholders' equity	**842,351**	843,301	823,887	835,241
Average daily production (BOE/d)	**20,204**	19,762	20,542	20,208
Average realized price, after financial instruments ($/BOE)	**33.13**	30.53	25.47	22.13
Operating netback ($/BOE)	**16.63**	15.08	11.73	8.72
Netback as a percentage of revenue	**50%**	49%	46%	39%

	Q1 2016	Q4 2015	Q3 2015	Q2 2015
Revenue, before royalties and financial instruments	40,398	42,797	45,015	52,131
Adjusted funds from operations	5,951	11,172	16,601	14,701
Per share – basic ($/common share)	0.04	0.07	0.10	0.10
Per share – diluted ($/common share)	0.04	0.07	0.10	0.09
Profit (loss) and comprehensive income (loss)	(25,918)	(92,987)	(21,557)	(9,971)
Per share – basic ($/common share)	(0.15)	(0.55)	(0.13)	(0.06)
Per share – diluted ($/common share))	(0.15)	(0.55)	(0.13)	(0.06)
Total capital expenditures, net of dispositions	23,405	42,487	33,389	343,697
Total assets	1,268,268	1,279,475	1,363,348	1,365,445
Bank debt	214,360	177,570	147,801	224,221
Working capital deficiency	15,930	35,389	34,729	27,031
Convertible debentures	-	-	-	-
Shareholders' equity	822,229	846,754	937,658	870,083
Average daily production (BOE/d)	23,295	20,086	18,695	19,473
Average realized price, after financial instruments ($/BOE)	19.06	22.01	25.71	29.57
Operating netback ($/BOE)	4.76	8.05	11.52	10.23
Netback as a percentage of revenue	25%	37%	45%	35%

Since commencing active operations on February 26, 2013 with initial production of approximately 3,500 BOE per day, Kelt achieved corporate record average production of 23,295 BOE per day during the first quarter of 2016. Average production was lower in subsequent quarters of 2016 and in the first quarter of 2017 due to normal declines in conjunction with much lower capital expenditures compared to 2015, as well as significant production downtime resulting from third-partly pipeline restrictions and plant/facility outages.

In the second half of 2014, global crude oil prices began a precipitous decline that subsequently resulted in massive cutbacks in capital spending on energy projects worldwide. After averaging US$93.00 per barrel in 2014, WTI oil prices averaged US$48.80 per barrel in 2015 and bottomed with a low average price of US$33.45 per barrel during the first quarter of 2016. In November 2016, OPEC and certain non-OPEC countries agreed to cut oil production supplies, resulting in a recovery of oil prices. The impact is seen starting in the fourth quarter of 2016 and in the first quarter of 2017, the Company reported its highest average realized price and operating netback in the past eight consecutive quarters. Adjusted funds from operations of $26.8 million ($0.15 per common share, diluted) for the quarter ended March 31, 2017 was also at its highest level over this period. The improvement in operating netbacks and adjusted funds from operations was also achieved as a result of the Company's ongoing operational cost saving initiatives

In addition to cash provided by operating activities, the Company's capital expenditures (net of proceeds from dispositions) were funded primarily through equity financings, supplemented by bank debt and the issuance of $90 million principal amount of 5% convertible debentures on May 3, 2016.

Refer to the *"Results of Operations"* section of this MD&A for further discussion. Additional information relating to Kelt, including the Company's MD&A for previous quarters, is filed on SEDAR and can be viewed at www.sedar.com.

NON-GAAP FINANCIAL MEASURES AND OTHER KEY PERFORMANCE INDICATORS

This MD&A contains certain financial measures, as described below, which do not have standardized meanings prescribed by GAAP. In addition, this MD&A contains other key performance indicators ("KPI"), financial and non-financial, that do not have standardized meanings under the applicable securities legislation. As these non-GAAP financial measures and KPI are commonly used in the oil and gas industry, the Company believes that their inclusion is useful to investors. The reader is cautioned that these amounts may not be directly comparable to measures for other companies where similar terminology is used.

Non-GAAP financial measures

"Operating income" is calculated by deducting royalties, production expenses and transportation expenses from petroleum and natural gas revenue, after realized gains or losses on associated financial instruments. The Company refers to operating income expressed per unit of production as an "Operating netback". "Adjusted funds from operations" is calculated as cash provided by operating activities before changes in non-cash operating working capital, and adding back (if applicable): transaction costs associated with acquisitions and dispositions, provisions for potential credit losses, and settlement of decommissioning obligations. Adjusted funds from operations per common share is calculated on a consistent basis with profit (loss) per common share, using basic and diluted weighted average common shares as determined in accordance with GAAP. Adjusted funds from operations and operating income or netbacks are used by Kelt as key measures of performance and are not intended to represent operating profits nor should they be viewed as an alternative to cash provided by operating activities, profit or other measures of financial performance calculated in accordance with GAAP.

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

	Three months ended March 31		
(CA$ thousands, except as otherwise indicated)	**2017**	2016	%
Cash provided by (used in) operating activities	**25,890**	(127)	-
Change in non-cash working capital	**272**	6,078	96
Funds from operations	**26,162**	5,951	340
Settlement of decommissioning obligations	**661**	-	-
Adjusted funds from operations	**26,823**	5,951	351

The following table demonstrates the calculation of operating income derived from the individual financial statement line items in accordance with GAAP:

	Three months ended March 31		
(CA$ thousands, except as otherwise indicated)	**2017**	2016	%
Petroleum and natural gas revenue	**60,225**	40,398	49
Realized gain on financial instruments (1)	**15**	-	-
Royalties	**(6,623)**	(2,859)	132
Production expenses	**(17,466)**	(21,712)	-20
Transportation expenses	**(5,909)**	(5,739)	3
Operating income	**30,242**	10,088	200
Production (mBOE)	**1,818**	2,120	-14
Operating netback ($/BOE)	**16.63**	4.76	249

(1) Excludes realized gains/losses on interest rate swaps

Throughout this MD&A, the term “net bank debt” is used synonymously with, and is equal to, “bank debt, net of working capital”. “Net bank debt” is calculated by adding the working capital deficiency to bank debt. The working capital deficiency is equal to total current assets net of total current liabilities. The Company uses a “net bank debt to trailing adjusted funds from operations ratio” as a benchmark on which management monitors the Company’s capital structure and short-term financing requirements. Management believes that this ratio, which is a non-GAAP financial measure, provides investors with information to understand the Company’s liquidity risk. The “net bank debt to trailing adjusted funds from operations ratio” is also indicative of the “debt to cash flow” calculation used to determine the applicable margin for a quarter under the Company’s Credit Facility agreement (though the calculation may not always be a precise match, it is representative).

Other KPI

“Production per common share” is calculated by dividing total production by the basic weighted average number of common shares outstanding, as determined in accordance with GAAP.

OTHER MEASUREMENTS

All dollar amounts are referenced in thousands of Canadian dollars, except when noted otherwise. This MD&A contains various references to the abbreviation BOE which means barrels of oil equivalent. Where amounts are expressed on a BOE basis, natural gas volumes have been converted to oil equivalence at six thousand cubic feet per barrel and sulphur volumes have been converted to oil equivalence at 0.6 long tons per barrel. The term BOE may be misleading, particularly if used in isolation. A BOE conversion ratio of six thousand cubic feet per barrel is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead and is significantly different than the value ratio based on the current price of crude oil and natural gas. This conversion factor is an industry accepted norm and is not based on either energy content or current prices. Such abbreviation may be misleading, particularly if used in isolation. References to “oil” in this MD&A include crude oil and field condensate. References to “natural gas liquids” or “NGLs” include pentane, butane, propane, and ethane. References to “liquids” include field condensate and NGLs. References to “gas” in this discussion include natural gas and sulphur.

CHANGES IN ACCOUNTING POLICIES

As of January 1, 2017, the Company adopted all of the requirements of IFRS 9 *Financial Instruments*, as amended in July 2014 (“IFRS 9”).

IFRS 9 uses a single approach to determine whether a financial asset is classified and measured at amortized cost or fair value, replacing the multiple rules in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments and the contractual cash flow characteristics of the financial assets. Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward in IFRS 9, and IFRS 9 has introduced a single expected credit loss impairment model, which is based on changes in credit quality since initial recognition. The adoption of the expected credit loss impairment model did not have a significant impact on the Company, however there are additional required disclosures which have been included in note 13 to the interim financial statements as at March 31, 2017.

The early adoption of IFRS 9 has been applied retrospectively and did not result in a change in the carrying value of any of Kelt's financial instruments on the transition date.

SIGNIFICANT JUDGMENTS AND ESTIMATES

The timely preparation of the financial statements requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amount of assets, liabilities, income and expenses. Actual results may differ materially from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are reviewed and for any future years affected. The significant judgments, estimates and assumptions made by management in the interim financial statements are outlined in note 2 of the December 31, 2016 annual financial statements. There have been no significant changes in the Company's judgments and estimates applied during the interim period ended March 31, 2017 relative to those described in the most recent annual financial statements as at and for the year ended December 31, 2016.

DISCLOSURE CONTROLS AND PROCEDURES

The Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO") have designed, or caused to be designed under their supervision, disclosure controls and procedures as defined in National Instrument 52-109 of the Canadian Securities Administrators, to provide reasonable assurance that: (i) material information relating to the Company is made known to the CEO and the CFO by others, particularly during the period in which the annual and interim filings are being prepared; and (ii) information required to be disclosed by the Company in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time periods specified in securities legislation.

INTERNAL CONTROLS OVER FINANCIAL REPORTING

The CEO and the CFO have designed, or caused to be designed under their supervision, internal controls over financial reporting as defined in National Instrument 52-109 of the Canadian Securities Administrators, in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS.

There were no changes to the Company's internal controls over financial reporting during the interim period from January 1, 2017 to March 31, 2017 that have materially affected, or are reasonably likely to materially affect the Company's internal controls over financial reporting.

Due to its inherent limitations, internal controls over financial reporting may not prevent or detect misstatements. In addition, projections of any evaluation relating to the effectiveness in future periods are subject to the risk that controls may become inadequate as a result of changes in conditions, or that the degree of compliance with policies and procedures may deteriorate.

CURRENT ECONOMIC ENVIRONMENT AND BUSINESS RISKS

The business of exploration, development, production and acquisition of oil and gas reserves involves a number of uncertainties. As a result, the Company is exposed to certain business risks inherent in the oil and gas industry which may impact the Company's operations or financial results. In the current business environment, Kelt continues to focus on maintaining a strong balance sheet, giving the Company the ability to take advantage of opportunities as they arise. The Company's capital expenditure program is also flexible, with the ability to defer expenditures into the future if the current economic environment deteriorates. A comprehensive discussion of business risks, as well as economic and industry factors affecting the Company is included in Kelt's annual MD&A for the year ended December 31, 2016, dated March 7, 2017. Additional information is included in Kelt's Annual Information Form dated March 10, 2017 which can be found at www.sedar.com.

BUSINESS OUTLOOK

ADVISORY REGARDING FORWARD-LOOKING STATEMENTS

Certain information with respect to Kelt contained herein, including management's assessment of future plans and operations, contains forward-looking statements. These forward-looking statements are based on assumptions and are subject to numerous risks and uncertainties, certain of which are beyond Kelt's control, including the impact of general economic conditions, industry conditions, volatility of commodity prices, currency exchange rate fluctuations, imprecision of reserve estimates, environmental risks, competition from other explorers, stock market volatility and ability to access sufficient capital. As a result, Kelt's actual results, performance or achievement could differ materially from those expressed in, or implied by, these forward-looking statements and, accordingly, no assurance can be given that any events anticipated by the forward-looking statements will transpire or occur. In addition, the reader is cautioned that historical results are not necessarily indicative of future performance.

OUTLOOK AND GUIDANCE

Kelt continues to be optimistic about the long-term outlook for oil and gas commodity prices. During the energy industry downturn throughout 2015 and 2016, Kelt took advantage of its strong financial position and executed on its strategy of long-term value creation by accumulating significant undeveloped land acreage on resource style plays, with a primary focus on Triassic Montney oil and liquids-rich gas plays. The cost to acquire land at Crown sales in the Company's core operating areas dropped significantly and service related costs to drill and complete wells also declined substantially. In order to capitalize on opportunities in the current energy business environment, Kelt was active at Crown land sales and has transitioned to development pad drilling in order to take advantage of lower oilfield related service costs.

Kelt's Board of Directors has approved the Company's increased 2017 capital expenditure budget of $173.0 million (previously $144.6 million), of which approximately 75% is expected to be incurred on drilling and completing wells. Approximately 40% of the total budget was incurred in the first quarter of 2017. A portion of the capital budget will be used for facilities, whereby Kelt expects to increase both compression and pipeline gathering capacity in its core producing areas to accommodate production additions. After giving effect to the Karr Property Disposition which closed on January 18, 2017 for proceeds of $103.0 million, net capital spending in 2017 is expected to be approximately $70.0 million (previously $42.0 million).

Kelt expects to drill 31 gross (23.1 net) wells in 2017, however, the Company expects to complete 37 gross (29.1 net) wells in 2017, as there are 6 gross (6.0 net) drilled but un-completed wells from 2016.

The table below outlines Kelt's revised forecasted financial and operating guidance for 2017, as well as the change from the Company's previous guidance. Kelt has changed its previously reported production and financial guidance for 2017 to reflect the increased capital spending and commodity price forecasts for 2017 have been reduced from previous estimates.

Forecast for year ended December 31, 2017 *(CA$ millions, except as otherwise indicated)*	**Current Guidance**	Previous Guidance	Change %
Average Production			
Oil (bbls/d)	**7,400**	6,700	10%
NGLs (bbls/d)	**2,550**	2,500	2%
Gas (mmcf/d)	**81,300**	82,800	-2%
Combined (BOE/d)	**23,500**	23,000	2%
Production per million common shares (BOE/d) (1)	**134**	131	2%
Forecasted Average Commodity Prices			
WTI crude oil price (US$/bbl)	**51.00**	52.00	-2%
Canadian Light Sweet ($/bbl)	**64.17**	65.24	-2%
NYMEX natural gas price (US$/MMBtu)	**3.10**	3.05	2%

AECO natural gas price ($/GJ)	**2.70**	2.95	-8%
Forecasted Average Exchange Rate (US$/CA$)	**0.748**	0.749	0%
Capital Expenditures			
Drilling & completions	**129.0**	104.6	23%
Facilities, pipeline & well equipment	**35.0**	32.0	9%
Land & seismic (net of dispositions)	**(94.0)**	(94.6)	1%
Total capital expenditures, net of dispositions	**70.0**	42.0	67%
Adjusted funds from operations (1)	**130.0**	128.0	2%
Per common share, diluted (1)	**0.73**	0.73	0%
Bank debt, net of working capital, at year-end (1)(2)	**78.0**	52.0	50%
Net bank debt to trailing annual adjusted funds from operations ratio (1)	**0.6 x**	0.4 x	50%
Weighted average common shares outstanding (millions)	**175.8**	175.7	0%
Common shares issued and outstanding (millions)	**175.8**	175.7	0%

(1) Refer to advisories regarding non-GAAP financial measures and other key performance indicators.

(2) In addition to bank debt, the Company has $90.0 million principal amount of convertible debentures outstanding with a coupon of 5% per annum, maturing May 31, 2021.

The Company is forecasting WTI crude oil prices to average US$51.00 per barrel in 2017, up 18% from the average price of US$43.32 per barrel in 2016. AECO natural gas prices are forecasted to average $2.70 per GJ in 2017, up 32% from the average price of $2.05 per GJ in 2016.

Forecast average production of 23,500 BOE per day in 2017 represents a 12% increase from 2016 average production of 20,947 BOE per day and is estimated to be weighted 42% to oil and NGLs and 58% to gas (previous guidance of 23,000 BOE per day was expected to be weighted 40% to oil and NGLs and 60% to gas). However, based on the Company's revised forecasted commodity prices for 2017, 76% of forecasted operating income in 2017 is expected to be generated from oil and NGLs versus 24% from gas (previously 69% oil/NGLs and 31% gas). Kelt exited 2016 with approximately 20,000 BOE per day of production. Pad drilling production additions in 2017 from Inga/Fireweed in BC are anticipated to occur in the later part of 2017 and therefore are not fully reflected in the average production forecast for 2017. However, the Company expects 2017 exit production to be approximately 26,000 BOE per day, 30% higher than 2016 exit production.

After giving effect to the aforementioned revised capital expenditure budget, production estimates, commodity price assumptions, and estimated expenses: adjusted funds from operations for 2017 is forecasted to be approximately $130.0 million or $0.73 per share, diluted (previously $128.0 million and $0.73 per share, diluted); Kelt estimates that the Company's bank debt, net of working capital, will be approximately $78.0 million as at December 31, 2017 (previously $52.0 million); royalties are expected to average 12.1% of revenue in 2017 (previously 11.2%); during 2017, combined production and transportation expense is estimated to be $11.94 per BOE (previously $11.59 per BOE); G&A expense is estimated to be $0.93 per BOE (previously $0.91 per BOE); and interest expense is forecasted at $0.81 per BOE (previously $0.83 per BOE).

Changes in forecasted commodity prices and variances in production estimates can have a significant impact on estimated adjusted funds from operations and profit. Please refer to the advisories regarding forward-looking statements and to the cautionary statement below.

The information set out herein is "financial outlook" within the meaning of applicable securities laws. The purpose of this financial outlook is to provide readers with disclosure regarding Kelt's reasonable expectations as to the anticipated results of its proposed business activities for 2017. Readers are cautioned that this financial outlook may not be appropriate for other purposes.

ADDITIONAL INFORMATION

Additional information relating to Kelt, including the Company's Annual Information Form ("AIF") dated March 10, 2017 is filed on SEDAR and can be viewed on their website at www.sedar.com. Copies of the AIF can also be obtained by contacting Sadiq H. Lalani, Vice President and Chief Financial Officer at Kelt Exploration Ltd., Suite 300, 311 Sixth Avenue SW, Calgary, Alberta, Canada, T2P 3H2. Further information relating to Kelt is also available on its website at www.keltexploration.com.

On behalf of the Board of Directors,

[signed]

David J. Wilson
President and Chief Executive Officer
May 9, 2017

KELT EXPLORATION LTD.
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
[UNAUDITED]

(CA$ thousands)	[Notes]	**March 31, 2017**	December 31, 2016
ASSETS			
Current assets			
Cash and cash equivalents		**304**	560
Accounts receivable and accrued revenue	[13]	**31,098**	30,406
Prepaid expenses and deposits		**1,379**	1,191
Derivative financial instruments	[13]	**262**	-
Total current assets		**33,043**	32,157
Assets held for sale	[5]	**-**	105,458
Exploration and evaluation assets	[6]	**121,317**	120,166
Property, plant and equipment	[7]	**1,039,284**	998,177
Total assets		**1,193,644**	1,255,958
LIABILITIES			
Current liabilities			
Accounts payable and accrued liabilities		**67,125**	55,659
Derivative financial instruments	[13]	**624**	599
Deferred premium on flow-through shares	[11]	**638**	798
Decommissioning obligations	[10]	**1,163**	1,450
Total current liabilities		**69,550**	58,506
Decommissioning obligations held for sale	[5]	**-**	2,532
Bank debt	[8]	**39,258**	111,693
Convertible debentures	[9]	**71,810**	70,978
Decommissioning obligations	[10]	**128,951**	126,597
Deferred income tax liability	[12]	**41,724**	42,351
Total liabilities		**351,293**	412,657
SHAREHOLDERS' EQUITY			
Shareholders' capital	[11]	**1,056,915**	1,055,959
Reserve from common control transaction		**(57,668)**	(57,668)
Equity component of convertible debentures	[9]	**12,856**	12,856
Contributed surplus		**17,815**	17,454
Retained earnings (deficit)		**(187,567)**	(185,300)
Total shareholders' equity		**842,351**	843,301
Total liabilities and shareholders' equity		**1,193,644**	1,255,958
Commitments	[15]		

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

On behalf of the Board of Directors:

[signed]
David J. Wilson, Director

[signed]
Neil G. Sinclair, Director

KELT EXPLORATION LTD.
CONSOLIDATED STATEMENT OF PROFIT (LOSS) AND COMPREHENSIVE INCOME (LOSS)
[UNAUDITED]

		Three months ended March 31	
(CA$ thousands, except per share amounts)	[Notes]	**2017**	2016
Revenue			
Petroleum and natural gas revenue		**60,225**	40,398
Royalties		**(6,623)**	(2,859)
		53,602	37,539
Expenses			
Production		**17,466**	21,712
Transportation		**5,909**	5,739
Financing	[14]	**3,336**	2,995
General and administrative		**1,646**	1,887
Share based compensation	[11]	**1,250**	1,393
Exploration and evaluation	[6]	**63**	629
Depletion and depreciation	[7]	**27,227**	40,930
		56,897	75,285
Loss before other items and taxes		**(3,295)**	(37,746)
Gain on derivative financial instruments	[13]	**262**	109
Premium on flow-through shares	[11]	**160**	-
Gain (loss) on sale of assets	[5]	**(21)**	2,134
Loss before taxes		**(2,894)**	(35,503)
Deferred income tax recovery	[12]	**(627)**	(9,585)
Loss and comprehensive loss		**(2,267)**	(25,918)
Loss per common share			
Basic	[11]	**(0.01)**	(0.15)
Diluted	[11]	**(0.01)**	(0.15)

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

KELT EXPLORATION LTD.
CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY
[UNAUDITED]

(CA$ thousands)	[Notes]	Shareholders' capital Number of Shares (000s)	Shareholders' capital Amount ($ thousands)	Reserve	Convertible debentures – equity portion	Contributed surplus	Retained earnings (deficit)	Total shareholders' equity
Balance at December 31, 2016		175,672	1,055,959	(57,668)	12,856	17,454	(185,300)	843,301
Loss and comprehensive loss		-	-	-	-	-	(2,267)	(2,267)
Exercise of stock options	[11]	16	86	-	-	(19)	-	67
Vesting of restricted share units	[11]	105	870	-	-	(870)	-	-
Share based compensation	[11]	-	-	-	-	1,250	-	1,250
Balance at March 31, 2017		**175,793**	**1,056,915**	**(57,668)**	**12,856**	**17,815**	**(187,567)**	**842,351**

Balance at December 31, 2015		168,668	1,022,115	(57,668)	-	17,833	(135,526)	846,754
Loss and comprehensive loss		-	-	-	-		(25,918)	(25,918)
Vesting of restricted share units	[11]	750	5,043	-	-	(5,043)	-	-
Share based compensation	[11]	-	-	-	-	1,393	-	1,393
Balance at March 31, 2016		169,418	1,027,158	(57,668)	-	14,183	(161,444)	822,229

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

KELT EXPLORATION LTD.
CONSOLIDATED STATEMENT OF CASH FLOWS
[UNAUDITED]

		Three months ended March 31	
(CA$ thousands)	[Notes]	**2017**	2016
Operating activities			
Loss and comprehensive loss		**(2,267)**	(25,918)
Items not affecting cash:			
Accretion of convertible debentures	[9,14]	**832**	-
Accretion of decommissioning obligations	[10,14]	**721**	759
Share based compensation		**1,250**	1,393
Exploration and evaluation		**63**	629
Depletion and depreciation		**27,227**	40,930
Unrealized gain on derivative financial instruments	[13]	**(237)**	(123)
Premium on flow-through shares		**(160)**	-
Loss (gain) on sale of assets		**21**	(2,134)
Deferred income tax recovery		**(627)**	(9,585)
Settlement of decommissioning obligations	[10]	**(661)**	-
Change in non-cash operating working capital	[16]	**(272)**	(6,078)
Cash provided by (used in) operating activities		**25,890**	(127)
Financing activities			
Increase (decrease) in bank debt		**(72,435)**	36,790
Proceeds on exercise of stock options	[11]	**67**	-
Cash (used in) provided by financing activities		**(72,368)**	36,790
Investing activities			
Exploration and evaluation assets		**(16,989)**	(12,921)
Property, plant and equipment		**(50,623)**	(11,631)
Property acquisitions	[4]	**-**	(37)
Property dispositions	[5]	**102,976**	1,184
Change in non-cash investing working capital	[16]	**10,858**	(13,831)
Cash provided by (used in) investing activities		**46,222**	(37,236)
Net change in cash and cash equivalents		**(256)**	(573)
Cash and cash equivalents, beginning of period		**560**	870
Cash and cash equivalents, end of period		**304**	297

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

KELT EXPLORATION LTD.
NOTES TO THE CONSOLIDATED CONDENSED INTERIM FINANCIAL STATEMENTS
AS AT AND FOR THE THREE MONTHS ENDED MARCH 31, 2017
[UNAUDITED]

(All tabular amounts in thousands of Canadian dollars, except as otherwise indicated)

1. DESCRIPTION OF THE BUSINESS

Kelt Exploration Ltd. ("Kelt" or the "Company") is an oil and gas company based in Calgary, Alberta, focused on the exploration, development and production of crude oil and natural gas resources, primarily in northwestern Alberta and northeastern British Columbia. The Company was incorporated under the *Business Corporations Act* (Alberta) on October 11, 2012 and was inactive until February 26, 2013. Kelt's land holdings are located in two core areas, namely: (a) Grande Prairie (including Pouce Coupe, Progress and La Glace), Alberta; and (b) Fort St. John (including Inga, Fireweed and Stoddart), British Columbia. The Company's common shares and 5% convertible debentures are listed on the Toronto Stock Exchange ("TSX") under the symbol "KEL" and "KEL.DB", respectively.

On April 16, 2015, the Company completed the acquisition of Artek Exploration Ltd. ("Artek") by acquiring all of the issued and outstanding common shares of Artek pursuant to a statutory plan of arrangement under the *Business Corporations Act* (Alberta) (the "Artek Acquisition"). Pursuant to the arrangement, Artek common shares were delisted from the TSX and Artek became a wholly-owned subsidiary of Kelt. Immediately following the Artek Acquisition, Articles of Amendment were filed to change the name of Artek to Kelt Exploration (LNG) Ltd. ("Kelt LNG"). Kelt has transferred all of its British Columbia ("BC") assets to Kelt LNG and at the same time, Kelt LNG has transferred all of its Alberta assets to Kelt. Kelt LNG operates in BC as a wholly-owned subsidiary of Kelt.

The head office of Kelt and Kelt LNG is located at Suite 300, 311 - 6th Avenue S.W., Calgary, Alberta T2P 3H2. Additional information relating to Kelt can be found on SEDAR at www.sedar.com.

2. BASIS OF PRESENTATION

The Company's Board of Directors approved and authorized these consolidated condensed interim financial statements for issue on May 9, 2017.

a) Statement of compliance

The Company prepares its financial statements in accordance with Canadian generally accepted accounting principles ("GAAP") as set out in the *CPA Canada Handbook - Accounting*. These condensed consolidated interim financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB"), applicable to the preparation of interim financial statements, including IAS 34 *Interim Financial Reporting*. Certain disclosures included in the notes to the annual financial statements have been condensed in the following note disclosures or have been disclosed on an annual basis only. Accordingly, these condensed consolidated interim financial statements should be read in conjunction with the audited consolidated annual financial statements as at and for the year ended December 31, 2016.

b) Basis of measurement

All references to dollar amounts in these financial statements and related notes are thousands of Canadian dollars, unless otherwise indicated.

The financial statements have been prepared on a historical cost basis, except for certain financial instruments which are recorded at fair value. The methods used to measure fair values are described in note 13 of these financial statements.

c) Significant judgments and estimates

The timely preparation of the financial statements requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amount of assets, liabilities, income and expenses. Actual results may differ materially from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are reviewed and for any future years affected. Significant judgments, estimates and assumptions made by management in these financial statements are outlined in note 2 of the December 31, 2016 consolidated annual financial statements. There have been no significant changes in the Company's judgments and estimates applied during the interim period ended March 31, 2017 relative to those described in the most recent annual financial statements as at and for the year ended December 31, 2016.

3. SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies applied by the Company are described in note 3 of the December 31, 2016 consolidated annual financial statements. Except as outlined below, these condensed consolidated interim financial statements at March 31, 2017 have been prepared following the same accounting policies and methods of computation as the most recent consolidated annual financial statements as at and for the year ended December 31, 2016.

Income tax expense for an interim period is based on an estimated average annual effective income tax rate.

The IASB has issued accounting standards that are not yet effective, including: IFRS 15 *Revenue from Contracts with Customers and* IFRS 16 *Leases*. Details of the foregoing are outlined in note 3 of the December 31, 2016 consolidated annual financial statements. There have been no changes as of the date of these condensed interim financial statements. The evaluation of all potential measurement and disclosure impacts is ongoing.

Changes in Accounting Policies

As of January 1, 2017, the Company adopted all of the requirements of IFRS 9 *Financial Instruments*, as amended in July 2014 ("IFRS 9").

IFRS 9 uses a single approach to determine whether a financial asset is classified and measured at amortized cost or fair value, replacing the multiple rules in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments and the contractual cash flow characteristics of the financial assets. Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward in IFRS 9, and IFRS 9 has introduced a single expected credit loss impairment model, which is based on changes in credit quality since initial recognition. The adoption of the expected credit loss impairment model did not have a significant impact on the financial statements of the Company, however there are additional required disclosures which have been included in note 13.

The early adoption of IFRS 9 has been applied retrospectively and did not result in a change in the carrying value of any of Kelt's financial instruments on the transition date.

4. PROPERTY ACQUISITIONS

The following table summarizes the fair value of net assets acquired pursuant to property acquisitions during the year ended December 31, 2016. There were no property acquisitions completed during the first quarter ended March 31, 2017.

	March 31, 2017	December 31, 2016
Exploration and evaluation assets	-	252
Property, plant and equipment	-	18,538
Decommissioning obligations	-	(278)
Fair value of net assets acquired	-	18,512
Cash consideration, after closing adjustments	-	18,512

On April 28, 2016, the Company acquired oil and gas assets in its core area at Progress, Alberta, for cash consideration of $18.0 million, before closing adjustments. The purchase price was adjusted for the results of operations between the effective date of January 1, 2016 and closing of the acquisition. The transaction was accounted for as a business combination whereby the net assets acquired and the liabilities assumed were recorded at fair value on the acquisition date, which was determined to be equal to the cash consideration paid of $18.5 million after closing adjustments.

5. PROPERTY DISPOSITIONS

Karr Property Disposition

On January 18, 2017, Kelt completed the disposition of the majority of its oil and gas assets located in the Karr area of Alberta, for cash consideration of $100.0 million before adjustments. The disposition (hereinafter referenced as the "Karr Property Disposition") had an effective date of January 1, 2017. Net proceeds have been used, initially, to reduce indebtedness under the Company's Credit Facility. The syndicate of lenders confirmed that the authorized borrowing amount available under the Credit Facility remained unchanged at $185.0 million.

The assets and associated decommissioning obligations disposed pursuant to the Karr Property Disposition were classified as held for sale as at December 31, 2016. Immediately prior to the initial classification as held for sale, the net carrying amount of PP&E was $68.9 million, including accumulated impairment of $46.2 million recognized during the year ended December 31, 2015. As at December 31, 2016, the impairment loss was partially reversed by $32.2 million based on the estimated fair value of consideration in excess of the carrying amount.

Estimates as of: *(CA$ thousands)*	**March 31 2017**	December 31 2016	Change in Estimates
Gross purchase price	100,000	100,000	-
Estimated closing adjustments (1)	2,976	2,926	50
Fair value of consideration (1)	**102,976**	**102,926**	**50**
Exploration and evaluation assets	4,377	4,377	-
Property, plant and equipment, net (2)	101,152	101,081	71
Assets held for sale and disposed	105,529	105,458	71
Decommissioning obligations held for sale and disposed (3)	(2,532)	(2,532)	-
Net assets held for sale and disposed	**102,997**	**102,926**	**71**

(1) At the time of preparation of the interim financial statements, closing adjustments are estimated to be approximately $3.0 million and include estimates for certain capital expenditures and operating income between the effective and closing date of the disposition. The total amount of adjustments will not be known until completion of the final statement of adjustments and as a result, the fair value of consideration may differ from this estimate.

(2) Cost of $163.2 million, net of accumulated depletion and depreciation of $48.1 million and accumulated impairment of $14.0 million (net of impairment reversal).

(3) The carrying amount of the decommissioning obligations held for sale was estimated based on a risk-free rate of 2.3% and an inflation rate of 2.0% as at December 31, 2016. The undiscounted cash flows required to settle the obligations were estimated to be approximately $2.7 million.

During the previous year ended December 31, 2016, Kelt completed dispositions of certain non-core assets for cash proceeds of $5.9 million, after closing adjustment and costs of disposal.

The table below summarizes the aggregate proceeds received and carrying values of the assets and associated decommissioning obligations disposed during the first three months of 2017 and year ended December 31, 2016, as well as the resulting net gain (loss) on sale in each period:

	March 31, 2017	December 31, 2016
Exploration and evaluation assets	**4,377**	2,575
Property, plant and equipment	**101,152**	6,257
Decommissioning obligations	**(2,532)**	(11,687)
Carrying value of net assets (liabilities) disposed	**102,997**	(2,855)
Cash proceeds, after closing adjustments (1)	**102,976**	5,891
Gain (loss) on sale of assets (1)	**(21)**	8,746

(1) The amounts reported in the table above were estimated based on information available at the time of preparation of these interim financial statements. In particular, closing adjustments were estimated based on an interim statement of adjustments. The actual gain or loss on the Karr Property Disposition ultimately recognized by the Company upon determination of final closing adjustments may differ from these estimates.

6. EXPLORATION AND EVALUATION ASSETS

Exploration and evaluation ("E&E") assets consist of the Company's undeveloped land, geological and geophysical assets, and exploratory drilling costs for projects in which the technical feasibility or commercial viability has yet to be determined. At the time sufficient information becomes available to determine whether the project is technically feasible or commercially viable, which is generally the point at which proved reserves are discovered, the costs are either transferred to property, plant, and equipment ("PP&E") or charged to exploration and evaluation expense.

The following table reconciles movements of exploration and evaluation assets:

	March 31, 2017	December 31, 2016
Balance, beginning of period	**120,166**	124,305
Additions	**16,989**	35,575
Property acquisitions [note 4]	**-**	252
Reclassification (to) from held for sale [note 5]	**4,377**	(4,377)
Property dispositions [note 5]	**(4,377)**	(2,575)
Transfers to property, plant and equipment	**(15,775)**	(28,754)
Expired mineral leases	**(63)**	(4,260)
Balance, end of period	**121,317**	120,166

The Company reviews its E&E assets for indicators of potential impairment each reporting period and prior to transferring E&E costs to PP&E. Except for costs associated with the expiry of mineral leases which are recognized as exploration and evaluation expense in the period incurred, the Company concluded that there are no indicators of potential impairment of its E&E assets at March 31, 2017.

7. PROPERTY, PLANT AND EQUIPMENT

Net carrying value	March 31, 2017	December 31, 2016
Development and production ("D&P") assets	**1,038,845**	997,646
Corporate assets	**439**	531
Total net carrying value of property, plant and equipment	**1,039,284**	998,177

The following table reconciles movements of property, plant and equipment ("PP&E") during the period:

Property, plant and equipment, at cost	D&P Assets	Corporate Assets	Total PP&E
Balance at December 31, 2015	1,458,222	1,838	1,460,060
Additions	49,436	636	50,072
Property acquisitions [note 4]	18,538	-	18,538
Reclassification (to) from held for sale [note 5]	(163,166)	-	(163,166)
Property dispositions [note 5]	(11,520)	-	(11,520)
Decommissioning costs	(2,848)	-	(2,848)
Transfers from E&E	28,754	-	28,754
Balance at December 31, 2016	**1,377,416**	**2,474**	**1,379,890**
Additions	**50,513**	**110**	**50,623**
Reclassification (to) from held for sale [note 5]	**163,166**	**-**	**163,166**
Property dispositions [note 5]	**(163,237)**	**-**	**(163,237)**
Decommissioning costs	**2,007**	**-**	**2,007**
Transfers from E&E	**15,775**	**-**	**15,775**
Balance at March 31, 2017	**1,445,640**	**2,584**	**1,448,224**

Accumulated depletion, depreciation and impairment	D&P Assets	Corporate Assets	Total PP&E
Balance at December 31, 2015	334,042	1,113	335,155
Depletion and depreciation expense	139,217	830	140,047
Impairments, net of impairment reversals	(26,141)	-	(26,141)
Reclassification (to) from held for sale [note 5]	(62,085)	-	(62,085)
Property dispositions [note 5]	(5,263)	-	(5,263)
Balance at December 31, 2016	**379,770**	**1,943**	**381,713**
Depletion and depreciation expense	**27,025**	**202**	**27,227**
Reclassification (to) from held for sale [note 5]	**62,085**	**-**	**62,085**
Property dispositions [note 5]	**(62,085)**	**-**	**(62,085)**
Balance at March 31, 2017	**406,795**	**2,145**	**408,940**

There were no borrowing costs capitalized in the current or prior year, as the Company did not have any qualifying assets. Future capital costs required to develop proved reserves in the amount of $541.0 million (December 31, 2016 – $588.5 million) are included in the depletion calculation for development and production assets.

8. BANK DEBT

	March 31, 2017	December 31, 2016
Bank loan	9,600	82,100
Bankers' acceptances	30,000	30,000
Unamortized financing fees (1)	(342)	(407)
Bank debt	39,258	111,693

(1) Includes $0.1 million of prepaid interest and stamping fees on bankers' acceptances as at March 31, 2017 ($0.1 million as at December 31, 2016).

The Company has a revolving committed term credit facility ("the Credit Facility") with a syndicate of financial institutions. As at March 31, 2017, the authorized borrowing amount available under the Credit Facility was $185.0 million. The Credit Facility is available for a revolving period of 364 days, maturing on April 29, 2017, and may be extended annually at Kelt's option and subject to lender approval, with a 364 day term-out period if not renewed. The Credit Facility is subject to semi-annual borrowing base reviews, occurring approximately in April and October of each year. In the event that the lenders reduced the borrowing base below the amount drawn at the time of the redetermination, the Company would have 60 days to eliminate any borrowing base shortfall by repaying the amount drawn in excess of the re-determined borrowing base or by providing additional security or other consideration satisfactory to the lenders. Repayments of principal are not required provided that the borrowings under the facility do not exceed the authorized borrowing amount and the Company is in compliance with all covenants, representations and warranties.

Subsequent to the quarter ended March 31, 2017, the Company and its lenders completed the semi-annual review and amended the Credit Facility to extend the current revolving period to April 28, 2018, with a term-out to April 28, 2019 if not renewed. The authorized borrowing amount is unchanged at $185.0 million.

There are no financial covenants under the Credit Facility and Kelt is in compliance with all other covenants. Covenants include industry standard positive and negative covenants including reporting requirements, permitted indebtedness, permitted dispositions (to a maximum in each calendar year which are in the aggregate not more than 5% of the borrowing base then in effect), permitted risk management activities (as more particularly described in note 13), permitted encumbrances and other standard business operating covenants. Security is provided for by a first fixed and floating charge debenture over all assets in the amount of $800.0 million and general assignment of book debts.

Interest is payable monthly for borrowings through direct advances. Interest rates fluctuate based on a pricing grid and range from bank prime plus 1.0% to bank prime plus 2.5%, depending upon the Company's then current debt to cash flow ratio of between less than one and one tenth times to greater than three times. Under the Credit Facility, borrowings through the use of bankers' acceptances are also available. Stamping fees fluctuate based on a pricing grid and range from 2.0% to 3.5%, depending upon the Company's then current debt to cash flow ratio of between less than one and one tenth times to greater than three times.

9. CONVERTIBLE DEBENTURES

	Number of convertible debentures	Liability component ($ thousands)	Equity Component ($ thousands)
Balance at December 31, 2015	-	-	-
Issuance of convertible debentures	90,000	71,665	18,335
Issue costs	-	(2,832)	(725)
Deferred income tax liability	-	-	(4,754)
Accretion of discount	-	2,145	-
Balance at December 31, 2016	**90,000**	**70,978**	**12,856**
Accretion of discount	**-**	**832**	**-**
Balance at March 31, 2017	**90,000**	**71,810**	**12,856**

On May 3, 2016, the Company issued $90.0 million principal amount of convertible unsecured subordinated debentures for net proceeds of $86.4 million. The Debentures mature on May 31, 2021 (the "Maturity Date") and bear interest at 5.0% per annum payable semi-annually on May 31st and November 30th, commencing November 30, 2016. At the holder's option, the Debentures may be converted into common shares of the Company at any time prior to the close of business on the earlier of the business day immediately preceding (i) the Maturity Date, (ii) if called for redemption, the date fixed for redemption by the Company, or (iii) if called for repurchase in the event of a change of control, the payment date, at a conversion price of $5.50 per share (the "Conversion Price"), being a conversion rate of approximately 181.8182 common shares per $1,000 principal amount of Debentures, subject to adjustment in certain events.

The Debentures are redeemable by the Company after May 31, 2019 and prior to May 31, 2020, in whole or in part, from time to time, on not more than 60 days and not less than 40 days prior notice at a redemption price equal to their principal amount plus accrued and unpaid interest, if any, up to but excluding the date set for redemption, provided that the volume weighted average trading price of the common shares on the TSX for the 20 consecutive trading days ending five trading days (the "Current Market Price") prior to the date on which notice of redemption is provided is at least 125% of the Conversion Price. On or after May 31, 2020 and prior to the Maturity Date, the Debentures may be redeemed by the Company, in whole or in part, from time to time, on not more than 60 days and not less than 40 days prior notice at a redemption price equal to their principal amount plus accrued and unpaid interest, if any, up to but excluding the date set for redemption.

The Company may, at its option, elect to satisfy its obligation to repay all or any portion of the principal amount of the Debentures upon redemption or due at maturity, by issuing common shares instead of cash (subject to the receipt of any required regulatory approvals and provided that no event of default has occurred). The number of common shares to be issued would be obtained by dividing the principal amount of the Debentures by 95% of the Current Market Price on the date fixed for redemption or maturity, as applicable.

The liability component of the Debentures was recognized initially at the fair value of a similar liability that does not have an equity conversion option, which was calculated based on a market interest rate of 10.5%. The difference between the $90.0 million principal amount of the Debentures and the fair value of the liability component was recognized in shareholders' equity, net of deferred income taxes. Total transaction costs directly attributable to the offering of $3.6 million were allocated to the liability and equity components of the Debentures proportionately.

Accretion of the liability component and accrued interest payable on the Debentures are included in financing expenses in the Consolidated Statement of Profit (Loss) and Comprehensive Income (Loss) (note 14). At March 31, 2017, the fair value of the Debentures was $130.5 million (note 13).

10. DECOMMISSIONING OBLIGATIONS

Decommissioning obligations arise as a result of the Company's net ownership interests in petroleum and natural gas assets including well sites, processing facilities and infrastructure. The following table provides a reconciliation of the carrying amount of the obligation associated with the retirement of oil and gas properties:

	March 31, 2017	December 31, 2016
Balance, beginning of period	**128,047**	142,801
Obligations incurred	**1,620**	1,233
Obligations acquired [note 4]	**-**	278
Reclassification (to) from held for sale [note 5]	**2,532**	(2,532)
Obligations disposed [note 5]	**(2,532)**	(11,687)
Obligations settled	**(661)**	(782)
Changes in discount rate	**-**	(8,502)
Revisions to estimates	**387**	4,421
Accretion expense	**721**	2,817
Balance, end of period	**130,114**	128,047
Decommissioning obligations – current	**1,163**	1,450
Decommissioning obligations – non-current	**128,951**	126,597

As at March 31, 2017, the key assumptions on which the carrying amount of the decommissioning obligations is based include a risk-free rate of 2.3% (December 31, 2016 – 2.3%) and an inflation rate of 2.0% (December 31, 2016 – 2.0%).

The underlying cost estimates are derived from a combination of published industry benchmarks as well as site specific information. As at March 31, 2017, the undiscounted amount of the estimated cash flows required to settle the obligation is $144.5 million (December 31, 2016 – $145.8 million), and is expected to be incurred over the next 50 years.

Accretion of the decommissioning obligation due to the passage of time is presented within financing expenses in the Consolidated Statement of Profit (Loss) and Comprehensive Income (Loss) (note 14).

11. SHARE CAPITAL

Authorized

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

Issued and outstanding

The following table summarizes the change in common shares issued and outstanding. There are no preferred shares issued or outstanding as of March 31, 2017 (December 31, 2016 – nil).

	Number of Shares (000s)	Amount ($ thousands)
Balance at December 31, 2015	168,668	1,022,115
Issued for cash through common share offerings	6,085	31,690
Deferred premium on flow-through shares	-	(4,103)
Issued for cash on exercise of stock options	67	293
Transfer from contributed surplus on exercise of stock options	-	91
Released upon vesting of restricted share units	852	6,153
Share issue costs, net of deferred taxes ($103)	-	(280)
Balance at December 31, 2016	**175,672**	**1,055,959**
Issued for cash on exercise of stock options	**16**	**67**
Transfer from contributed surplus on exercise of stock options	**-**	**19**
Released upon vesting of restricted share units	**105**	**870**
Balance at March 31, 2017	**175,793**	**1,056,915**

Private placements of flow-through common shares

The table below summarizes flow-through common shares (“FTS”) issued pursuant to private placements during the year ended December 31, 2016, the cumulative amount of qualifying expenditures incurred and the Company’s outstanding commitments to incur eligible expenditures as at the end of the current reporting period.

(CA$ thousands, except as otherwise indicated)					Eligible Expenditures (1)			Expenditure Period End / Effective date of Renunciation
						As at March 31, 2017		
Closing Dates	# of FTS	Price per FTS	Gross Proceeds	Deferred Premium	Type	**Incurred**	**Remaining**	
April 7, 2016	4.7 million	$4.70	22,090	2,585	CDE	**22,090**(2)	**-**	December 31, 2016 December 31, 2016
August 23, 2016	0.385 million	$6.50	2,500	638	CEE	**-**	**2,500**	December 31, 2017 December 31, 2016
November 2, 2016	1.0 million	$7.10	7,100	880	CDE	**7,100**(3)	**-**	March 31, 2017 March 31, 2017

(1) Pursuant to the provisions of the *Income Tax Act* (Canada), the Company shall incur eligible Canadian development expenses (“CDE”) or Canadian exploration expenses (“CEE”) as required under the respective subscription agreements.

(2) The full commitment of $22.1 million of qualifying expenditures were incurred by Kelt as of December 31, 2016.

(3) Of the total commitment of $7.1 million, Kelt incurred $5.8 million during the fourth quarter of 2016 and $1.3 million during the first quarter of 2017.

Stock options

Kelt has an Incentive Stock Option Plan (the "Option Plan") that provides for granting of stock options to directors, officers, employees and certain consultants. The stock options granted pursuant to the Option Plan are to be settled through the issuance of new common shares of the Company and have a maximum term of five years to expiry. The vesting schedule is determined at the discretion of the Company's Compensation Committee of the Board of Directors; stock options typically vest in equal tranches over a three year period. Each stock option granted permits the holder to purchase one common share of the Company at the stated exercise price. The exercise price is determined based on the volume weighted average trading price on the TSX over three trading days immediately prior to the date of grant.

The following table summarizes the change in stock options outstanding:

	Number of Options (000s)	Average Exercise Price ($/share)
Balance at December 31, 2015	6,690	7.40
Granted	2,533	4.71
Exercised (1)	(67)	4.38
Forfeited	(780)	7.85
Balance at December 31, 2016	**8,376**	**6.57**
Granted	**30**	**7.08**
Exercised (1)	**(16)**	**4.10**
Forfeited	**(80)**	**4.93**
Balance at March 31, 2017	**8,310**	**6.59**

(1) The weighted average share price on the date stock options were exercised during the period ended March 31, 2017 was $6.97 per common share ($5.25 per common share on average during the year ended December 31, 2016).

The total fair value of each option granted is estimated on the date of grant using the Black-Scholes option pricing model with weighted average assumptions as follows:

	Three months ended March 31	
	2017	2016
Risk free interest rate	**0.8%**	0.7%
Expected life (years)	**3.0**	3.7
Expected volatility (1)	**56.1%**	50.8%
Expected dividend yield	**0.0%**	0.0%
Expected forfeiture rate	**3.8%**	0.8%
Fair value of options granted during the year ($/share)	**2.64**	1.48

(1) The expected volatility for options granted is estimated based on Kelt's historical volatility over the expected life.

The following table summarizes information regarding stock options outstanding at March 31, 2017:

Range of exercise prices per common share	Number of options outstanding (000s)	Weighted average remaining term (years)	Weighted average exercise price for options outstanding ($/share)	Number of options exercisable (000s)	Weighted average exercise price for options exercisable ($/share)
$0.00 to $5.00	3,661	4.0	4.51	637	4.32
$5.01 to $10.00	3,595	1.9	6.95	2,866	6.97
$10.01 to $15.00	994	2.0	12.39	915	12.36
$15.01 to $20.00	60	2.2	15.40	40	15.40
Total	**8,310**	**2.8**	**6.59**	**4,458**	**7.78**

Restricted share units

Kelt has a Restricted Share Unit Plan (the “RSU Plan”) that provides for granting of RSUs to officers, employees and certain consultants. The RSUs granted under the RSU Plan are to be settled through the issuance of new common shares upon vesting. The vesting schedule is determined at the discretion of the Company’s Compensation Committee of the Board of Directors; RSUs typically vest in two equal tranches with the first half vesting after two years and the second half after three years. On the vesting date, one common share is released from treasury for each RSU.

The following table summarizes the change in RSUs outstanding:

	Number of RSUs (000s)
Balance at December 31, 2015	1,204
Granted	439
Released upon vesting	(852)
Forfeited	(71)
Balance at December 31, 2016	**720**
Granted	**6**
Released upon vesting	**(105)**
Forfeited	**(19)**
Balance at March 31, 2017	**602**

Share based compensation expense

The total fair value associated with stock options and RSUs is recognized over the service period using graded vesting, resulting in share based compensation expense as follows:

	Three months ended March 31	
	2017	2016
Stock options	**896**	865
Restricted share units	**354**	528
Total share based compensation expense	**1,250**	1,393

Per share amounts

The table below summarizes the weighted average number of common shares outstanding used in the calculation of basic and diluted profit (loss) per common share:

	Three months ended March 31	
(000s of common shares)	**2017**	2016
Weighted average common shares outstanding, basic	**175,715**	168,824
Effect of stock options and RSUs	**1,067**	45
Effect of convertible debentures	**-**	-
Weighted average common shares outstanding, diluted	**176,782**	168,869

The Company uses the treasury stock method to determine the dilutive effect of stock options and RSUs. Under this method, only “in-the-money” dilutive instruments impact the calculation of diluted profit per common share. Accordingly, in computing the diluted loss per common share for the periods ended March 31, 2017 and 2016, the Company excluded the effect of stock options and RSUs as they were anti-dilutive. The common shares potentially issuable on conversion of the Debentures are also excluded as they were determined to be anti-dilutive for the quarter ended March 31, 2017.

12. INCOME TAXES

Kelt was not required to pay income taxes in the current or prior year as the Company had sufficient income tax deductions available to shelter taxable income. Tax deductions available as of March 31, 2017 are estimated to be approximately $912.5 million (December 31, 2016 – $975.4 million).

The following table reconciles income taxes calculated at the weighted average Canadian statutory rate with the actual provision for deferred income taxes per the Consolidated Statement of Profit (Loss) and Comprehensive Income (Loss):

	Three months ended March 31	
	2017	2016
Loss before income taxes	**(2,894)**	(35,503)
Canadian statutory tax rate	**26.2%**	26.6%
Expected income tax recovery	**(758)**	(9,444)
Increase (decrease) resulting from:		
Non-deductible expenses (1)	**339**	378
Recognition of unrecognized deferred tax asset	**(514)**	(514)
Qualifying expenditures on flow-through shares	**349**	-
Premium on flow-through shares	**(43)**	-
True-up of tax pools	**-**	(5)
Deferred income tax recovery	**(627)**	(9,585)

(1) Non-deductible expenses primarily include share based compensation.

The Canadian statutory tax rate per the rate reconciliation above represents the weighted average combined federal and provincial corporate tax rate. The federal corporate tax rate is 15.0% and the provincial tax rate is 11.0% in British Columbia and 12.0% in Alberta.

The movement in deferred income tax assets and liabilities, without taking into consideration the offsetting balances within the same tax jurisdiction are as follows:

Deferred income tax asset (liability)	Balance at December 31, 2016	Recognized in profit and CI(1)	Recognized in balance sheet	**Balance at March 31, 2017**
Derivative financial instruments	162	(64)	-	**98**
PP&E and E&E	(144,335)	(1,080)	-	**(145,415)**
Decommissioning obligations	34,144	550	-	**34,694**
Convertible debentures	(4,368)	177	-	**(4,191)**
Share and debt issue costs	2,847	(383)	-	**2,464**
Reserve from common control transaction	(7,113)	514	-	**(6,599)**
Non-capital losses(2)	76,312	913	-	**77,225**
	(42,351)	627	-	**(41,724)**

(1) Comprehensive income has been abbreviated as "CI".

(2) The Company's non-capital losses expire in years 2023 to 2036.

The amount and timing of reversals of temporary differences will be dependent upon a number of factors, including the nature and timing of future capital expenditures and the Company's future operating results.

13. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Financial instruments of the Company include cash and cash equivalents, accounts receivable and accrued revenue, deposits, accounts payable and accrued liabilities, derivative financial instruments, convertible debentures, and bank debt. The Company is exposed to financial risks arising from its financial assets and liabilities that include credit and liquidity risk in addition to the market risks associated with commodity prices, and interest and foreign exchange rates. Profit (loss), cash flows and the fair value of financial assets and liabilities may fluctuate due to movement in market prices or as a result of the Company's exposure to credit and liquidity risks.

The Company uses derivative financial instruments from time to time in order to manage market risks. The objective of market risk management is to manage and control market risk exposures within acceptable limits, while maximizing long-term returns. All such transactions are conducted in accordance with the Company's established risk management policies that permit management to enter into commodity price agreements, provided that:

i) the contracts are not entered into for speculative purposes;
ii) the total notional quantity hedged, at the time of entering into the contract, does not exceed 65% of average daily production; and
iii) the contracted term does not exceed 36 months.

Commodity price risk management contracts

Inherent to the business of producing oil and gas, the Company's cash provided by operating activities is subject to commodity price risk. Commodity price risk is the risk that future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices are impacted by world economic events that dictate the levels of supply and demand as well as the currency exchange rate relationship between the Canadian and U.S. dollar.

As at March 31, 2017, the following commodity price risk management contracts are outstanding:

Contract Type	Notional Volume	Reference Prices	Fixed Contract Price	Remaining Term	Fair value Asset (Liability)
Financial Swap Natural Gas	10,000 MMBtu/d	SoCAL Border Avg. NYMEX Henry Hub	SoCAL Border Avg. plus US$0.055 per MMBtu	April to October 2017	**(624)**(1)
Financial Swap Propane	500 bbls/d	OPIS-Conway propane WTI Cushing Oklahoma	50% of US$WTI	April to December 2017	**237**(2)

(1) The fair value is sensitive to changes in natural gas reference prices. If the Southern California Border Average ("SoCAL Border Avg.") - NYMEX basis differential increased (decreased) by $0.10/MMBtu, the fair market value of the contract would decrease (increase) by approximately $0.3 million.

(2) The fair value is sensitive to changes in propane reference prices. If the OPIS-Conway propane price increased (decreased) by 5% relative to the fixed contract price, the fair market value of the contract would decrease (increase) by approximately $0.2 million.

Interest rate risk management contracts

The Company is exposed to interest rate risk to the extent that changes in market interest rates will impact the Company's Credit Facility which is subject to a floating interest rate. Based on average bank debt outstanding of $39.9 million during the first quarter of 2017, an increase (decrease) in the market rate of interest by 25 basis points would have increased (decreased) interest expense by $0.1 million. During the previous year ended December 31, 2016, Kelt had an interest rate swap fixing CDOR at 0.925% on a notional amount of $100 million until June 30, 2017. In January 2017, in conjunction with the Karr Property Disposition (note 5) and resulting reduction in bank debt, the interest rate swap was unwound and terminated for proceeds of $10 thousand.

Foreign exchange risk management contracts

Kelt is exposed to fluctuations of the Canadian to U.S. dollar exchange rate given realized pricing is directly influenced by U.S. dollar denominated benchmark pricing. In addition, the Company entered in a natural gas marketing arrangement effective November 1, 2016 through October 31, 2017, whereby Kelt receives revenue on the firm contract volume of 4,739 MMBtu per day in U.S. dollars. The Company also has commitments for firm gas transportation service under contracts denominated in U.S. dollars as outlined in note 15. Exposure to foreign exchange rates is mitigating by entering U.S. dollar denominated commodity price or foreign exchange derivative financial instruments.

As at March 31, 2017, the following foreign exchange risk management contract was outstanding:

Contract Type	Notional Amount per month	Fixed Contract Price	Remaining Term	Fair value Asset (Liability)
FX swap[1]	US$1,000,000	CA$/US$ 1.3300	April to December 2017	**25**[2]

(1) The FX swap outstanding at March 31, 2017 resulted from an FX swaption contract which was exercised by the counterparty on December 30, 2016. Kelt received a cash premium of $0.255 million at the time of entering into the contract on July 11, 2016.

(2) The fair value of the contract is sensitive to changes in the exchange rate. If the CA$/US$ exchange rate increased (decreased) by $0.05, the fair market value of the contract would decrease (increase) by approximately $0.5 million.

In November 2016, Kelt received a cash premium of $0.205 million for entering into a forward foreign exchange swaption contract whereby the counterparty had the right, if exercised on March 31, 2017, to enter a series of forward foreign exchange transactions fixing the exchange rate on a notional US$1.0 million per month at CA$/US$ 1.3600 from April 2017 to March 2018. The swaption was not exercised on March 31, 2017 and Kelt has no further obligations under the contract.

Gains and losses on risk management contracts

The table below summarizes realized and unrealized gains (losses) on risk management contracts:

	Three months ended March 31	
	2017	2016
Realized gain (loss)	**25**	(14)
Unrealized gain	**237**	123
Gain on derivative financial instruments	**262**	109

Fair value measurements

The Company classifies fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The Company maximizes the use of observable inputs when preparing calculations of fair value, where possible. The fair value hierarchy has the following levels:

- Level 1 - Values are based on unadjusted quoted prices available in active markets for identical assets or liabilities as of the reporting date.
- Level 2 - Values are based on inputs, including quoted forward prices for commodities, time value and volatility factors, which can be substantially observed or corroborated in the marketplace. Prices in Level 2 are either directly or indirectly observable as of the reporting date.
- Level 3 - Values are based on prices or valuation techniques that are not based on observable market data.

Assessment of the significance of a particular input to the fair value measurement requires judgment and may affect the placement within the fair value hierarchy.

The fair value of cash and cash equivalents, accounts receivable and accrued revenue, deposits, accounts payable and accrued liabilities approximate their carrying value due to the short term to maturity of these instruments. Bank debt bears interest at a floating market rate and accordingly the fair market value of bank debt approximates the carrying amount. The fair value of the convertible debentures is estimated using quoted market prices on the TSX as of the Consolidated Statement of Financial Position date.

The fair value of financial assets and liabilities, excluding working capital, is attributable to the following fair value hierarchy levels at March 31, 2017:

	Carrying Value ("CV")			Fair Value		
	Gross	Netting(1)	Net CV	Level 1	Level 2	Level 3
Financial assets						
Derivative financial instruments	262	-	-	-	262	-
Financial liabilities						
Derivative financial instruments	624	-	-	-	624	-
Convertible debentures (2)	71,810	-	-	130,500	-	-

(1) Financial assets and liabilities are only offset if the Company has the current legal right to offset and intends to settle on a net basis or settle the asset and liability simultaneously. Kelt offsets derivative contracts assets and liabilities when the counterparty, commodity, currency and timing of settlement are the same. As at March 31, 2017, there are no offsetting derivative financial contracts.

(2) The fair value of the convertible debentures is based on the closing market price of $145.00 per Debenture as at March 30, 2017, being the date the debentures last traded on the TSX, and represents the market value of the entire instrument.

Credit Risk

As at March 31, 2017, the carrying amount of cash and cash equivalents, accounts receivable and accrued revenue, deposits, and derivative financial instrument assets represent the Company's maximum credit exposure. Cash and cash equivalents are held on deposit with a Canadian chartered bank. The Company's credit risk exposure arises primarily from receivables from oil and gas marketers and joint venture partners.

The Company applies the simplified approach to providing for expected credit losses prescribed by IFRS 9, which permits the use of the lifetime expected loss provision for all trade receivables. The Company uses a combination of historical and forward looking information to determine the appropriate loss allowance provision.

During the quarter ended March 31, 2017, sales to three oil and gas marketers each individually represented more than 10% of total revenue. Sales to these marketers account for approximately 38%, 22%, and 13%, of total revenue, respectively. During the comparative quarter ended March 31, 2016, sales to three oil and gas marketers accounted for approximately 37%, 25%, and 15% of total revenue, respectively. Kelt has secured parental guarantees (with terms ranging from two to five years) or letters of credit covering approximately 85% of its monthly credit exposure from oil and gas marketers, calculated based on average sales by purchaser for the first quarter of 2017.

Credit risk from joint venture receivables is mitigated by obtaining partner approval of significant capital expenditures prior to expenditure and in certain circumstances may require cash deposits in advance of incurring financial obligations on behalf of joint venture partners. The Company has the ability to withhold production from joint venture partners in the event of non-payment or may be able to register security on the assets of joint venture partners.

The oil and gas industry has a pre-arranged monthly clearing day for payment of revenues from all buyers of oil and natural gas; this occurs on the 25th day following the month of sale. As a result, the Company's production revenues are current. All other accounts receivable are generally contractually due within 30 days.

The ageing of the Company's accounts receivable is summarized in the following table:

Accounts receivable and accrued revenue	Current	30-60 days	60-90 days	Over 90 days	Total
Balance at March 31, 2017	**29,544**	**83**	**163**	**1,308**	**31,098**
Balance at December 31, 2016	28,657	539	253	957	30,406

The balance of accounts receivable outstanding for more than 90 days relates primarily to receivables from the Company's joint venture partners. Due to the current business environment and low commodity prices, many oil and gas companies, including some of Kelt's partners, continue to face significant financial challenges. Management has reviewed past due accounts receivable balances as at March 31, 2017 and expects the accounts to be collectible, except for approximately $0.8 million of accounts receivable which are provided for in the allowance for doubtful accounts (December 31, 2016 – $0.8 million).

Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they are due. The Company's financial liabilities include accounts payable, derivative financial instruments, bank debt and convertible debentures. The Company manages liquidity risk through prudent use of bank debt and an actively managed production and capital expenditure budgeting process. In addition, risk management contracts such as derivative financial instruments may be used from time to time. As discussed further under the *Capital Management* section to follow, Kelt targets a relatively low debt to trailing adjusted funds from operations ratio. To manage this, the Board of Directors approves an annual capital expenditure budget, which is regularly monitored and updated as necessary in response to changing capital requirements. The Company utilizes a control system with respect to authorizations for expenditures on both operated and non-operated projects to further manage capital expenditures.

The capital intensive nature of Kelt's operations may create a working capital deficiency position during periods with high levels of capital investment. However, during such periods, the Company maintains sufficient unused bank credit lines to satisfy such working capital deficiencies. As at March 31, 2017, the Company's working capital deficit of $36.5 million combined with outstanding bank debt of $39.3 million, represented 41% of the authorized borrowing amount available under the Credit Facility of $185.0 million (down from 75% at December 31, 2016). The Credit Facility is available for a revolving period of 364 days, maturing on April 29, 2017, and may be extended annually at Kelt's option and subject to lender approval, with a 364 day term-out period if not renewed. Subsequent to the quarter ended March 31, 2017, the Company and its lenders amended the Credit Facility to extend the current revolving period to April 28, 2018, with a term-out to April 28, 2019 if not renewed.

The table below outlines a contractual maturity analysis for Kelt's financial liabilities as at March 31, 2017:

	Within 1 Year	1 to 5 Years	More than 5 Years	**Total**
Accounts payable and accrued liabilities	67,125	-	-	**67,125**
Derivative financial instrument liability	624	-	-	**624**
Bank debt and estimated interest(1)	1,492	39,364	-	**40,856**
Convertible debentures(2)	4,500	105,744	-	**110,244**
Total	**73,741**	**145,108**	**-**	**218,849**

(1) Estimated interest for future periods related to the Credit Facility was calculated using the weighted average interest rate of 3.8% for the quarter ended March 31, 2017, applied to the principal balance outstanding as at that date. For purposes of this analysis, principal repayment of the Company's revolving Credit Facility is assumed to occur on April 27, 2018. However, subsequent to March 31, 2017, the Company and its lenders amended the Credit Facility to extend the revolving period by 364 days and Term Maturity Date to April 28, 2019.

(2) The contractual maturity analysis includes semi-annual cash interest payments at the fixed coupon rate of 5.0%, assuming that the $90.0 million principal amount of the Debentures is outstanding for the full term to maturity on May 31, 2021, provided that: the equity conversion option is not first exercised by the holder; and that the Company does not elect to settle its financial obligation by issuing common shares instead of cash at redemption or maturity. Refer to additional information regarding the Debentures in note 9.

Capital Management

The Company's capital structure is comprised of shareholders' capital, convertible debentures, bank debt and working capital. Kelt's objectives when managing its capital structure is to maintain financial flexibility in order to meet financial obligations, as well as to finance future growth through capital expenditures relating to exploration, development and acquisition activities.

The Company monitors its capital structure and short-term financing requirements using a net bank debt to trailing adjusted funds from operations ratio, which is a non-GAAP financial measure.

	March 31, 2017	December 31, 2016
Bank debt	**39,258**	111,693
Working capital deficiency	**36,507**	26,349
Bank debt, net of working capital (1)	**75,765**	138,042
Trailing annualized adjusted funds from operations (2)(3)	**102,004**	92,400
Net bank debt to trailing adjusted funds from operations ratio (1)	**0.7**	1.5

(1) "Net bank debt" is equal to "Bank debt, net of working capital" determined in accordance with GAAP.

(2) Adjusted funds from operations is a non-GAAP financial measure which is calculated as cash provided by operating activities before changes in non-cash operating working capital, and adding back (if applicable): transaction costs, provisions for potential credit losses, and settlement of decommissioning obligations.

(3) Trailing adjusted funds from operations is annualized based on the most recent quarter's adjusted funds from operations.

Kelt targets a net bank debt to trailing adjusted funds from operations ratio of less than 2.0 times. The Company manages its capital structure and makes adjustments according to market conditions in order to maintain flexibility to achieve its objectives stated above. To adjust its capital structure, the Company may increase or decrease capital expenditures, issue new shares, issue new debt or repay existing debt.

The Company has reduced its net bank debt to trailing adjusted funds from operations ratio to 0.7 times as at March 31, 2017 from 1.5 times at December 31, 2016. The Karr Property Disposition was completed on January 18, 2017 for cash proceeds of $103.0 million (note 5). The proceeds have been used initially to reduce bank indebtedness under the Credit facility and were used, along with $25.9 million of cash provided by operating activities, to fund exploration and development capital expenditures during the first quarter of 2017.

As more particularly described in note 8, Kelt is subject to certain non-financial covenants under the Credit Facility agreement. As at March 31, 2017, the Company is in compliance with all covenants. The Company is not subject to any other externally imposed capital requirements.

14. FINANCING EXPENSES

The following table summarizes significant components of the Company's financing expenses:

		Three months ended March 31	
		2017	2016
Interest on bank debt	[note 8]	**673**	2,236
Interest on convertible debentures	[note 9]	**1,110**	-
Accretion of convertible debentures	[note 9]	**832**	-
Accretion of decommissioning obligations	[note 10]	**721**	759
Financing expense		**3,336**	2,995

15. COMMITMENTS

As of March 31, 2017, the Company is committed to future payments under the following agreements:

(CA$ thousands)	2017	2018	2019	2020	2021	Thereafter
Operating lease - office buildings	1,036	577	108	18	-	-
Operating lease - vehicles	269	273	161	17	-	-
Flow-through shares	2,500	-	-	-	-	-
Firm processing commitments	5,507	3,881	-	-	-	-
Firm transportation commitments (1)	12,737	7,820	5,372	2,594	1,964	8,377
Total annual commitments	**22,049**	**12,551**	**5,641**	**2,629**	**1,964**	**8,377**

(1) A portion of Kelt's commitments on the Alliance pipeline are denominated in US dollars. The volumes committed vary over the term of the contracts, which are effective until October 31, 2017, however, the maximum US denominated commitment in a given month does not exceed US$0.31 million. Amounts are translated to Canadian dollars at the spot rate on March 31, 2017 of CA$/US$1.3310.

The Company has firm commitments for oil and gas transportation on major pipelines in Alberta and British Columbia. For periods subsequent to 2021, Kelt has an annual commitment of $1.2 million for gas transportation until March 31, 2026 and an annual commitment of $0.6 million for oil transportation until June 30, 2027.

Payments under the office building operating leases relate to the Company's head office in Calgary, Alberta, and field offices in Grande Prairie, Alberta and Fort St. John, British Columbia. The leases expire on April 30, 2018, February 28, 2020, and November 30, 2018, respectively, if not extended.

16. SUPPLEMENTAL CASH FLOW INFORMATION

	Three months ended March 31	
Changes in non-cash working capital	**2017**	2016
Accounts receivable and accrued revenue	**(692)**	3,685
Prepaid expenses and deposits	**(188)**	169
Accounts payable and accrued liabilities	**11,466**	(23,763)
Change in non-cash working capital	**10,586**	(19,909)
Relating to:		
Operating activities	**(272)**	(6,078)
Investing activities	**10,858**	(13,831)
Change in non-cash working capital	**10,586**	(19,909)

During the reporting period, the Company made the following cash outlays in respect of interest and taxes:

	Three months ended March 31	
Cash outlays in respect of interest and taxes	**2017**	2016
Interest and standby fees on bank debt	**643**	2,685
Interest on convertible debentures (1)	**-**	-
Taxes (2)	**-**	-

(1) Interest on the Debentures is payable semi-annually on May 31st and November 30th (note 9).

(2) Kelt was not required to pay cash income taxes as the Company had sufficient income tax deductions available to shelter taxable income (note 12).

17. RELATED PARTY TRANSACTIONS

A director of the Company is also a partner at a law firm which Kelt has engaged to provide legal services. During the three months ended March 31, 2017, the Company incurred $0.1 million (2016 – $0.1 million) in legal fees and disbursements, of which $0.1 million is payable at March 31, 2017 ($0.1 million at December 31, 2016). The Company expects to continue using the services of this law firm from time to time.

ABBREVIATIONS

bbls	barrels
mbbls	thousand barrels
bbls/d	barrels per day
BOE	barrels of oil equivalent
mBOE	thousand barrels of oil equivalent
BOE/d	barrels of oil equivalent per day
mcf	thousand cubic feet
mmcf	million cubic feet
bcf	billion cubic feet
mmcf/d	million cubic feet per day
MMBtu	million British Thermal Units
GJ	gigajoules
LT	long tonnes
AECO-C	Alberta Energy Company "C" Meter Station of the Nova Pipeline System
WTI	West Texas Intermediate
NYMEX	New York Mercantile Exchange
CREC	Alliance Pipeline Canadian receipt location
Station 2	Spectra Energy receipt location
NGX	Natural Gas Exchange Inc. (Canada)
API	American Petroleum Institute
MD&A	Management's Discussion and Analysis
Q1	First quarter ended March 31st
Q2	Second quarter ended June 30th
Q3	Third quarter ended September 30th
Q4	Fourth quarter ended December 31st
YTD	Year to date
BT	Before income taxes
AT	After income taxes
1P	Proved reserves
2P	Proved plus probable reserves
FD&A	Finding, development and acquisition costs
CGU	Cash generating unit
FVLCD	Fair value less costs of disposal

CONVERSION OF UNITS

Imperial = Metric

1 acre = 0.4 hectares

2.5 acres = 1 hectare

1 bbl = 0.159 cubic metres

6.29 bbls = 1 cubic metre

1 foot = 0.3048 metres

3.281 feet = 1 metre

1 mcf = 28.2 cubic metres

0.035 mcf = 1 cubic metre

1 mile = 1.61 kilometres

0.62 miles = 1 kilometre

1 MMBtu = 1.054 GJ

0.949 MMBtu = 1 GJ

Natural gas is equated to oil on the basis of 6 mcf = 1 BOE

Sulphur is equated to gas on the basis of 1LT = 10 mcf (1 BOE = 0.6 LT)

CORPORATE INFORMATION

BOARD OF DIRECTORS

Robert J. Dales [2, 3, 4, 6]
President, Valhalla Ventures Inc.

William C. Guinan [1, 5]
Partner, Borden Ladner Gervais LLP

Eldon A. McIntyre [2, 3, 4, 6]
President, Jarrod Oils Ltd.

Neil G. Sinclair [2, 3, 4, 5, 6]
President, Sinson Investments Ltd.

David J. Wilson [5]
President & Chief Executive Officer
Kelt Exploration Ltd.

1 chairman of the board
2 member of the audit committee
3 member of the reserves committee
4 member of the compensation committee
5 member of the health, safety and environment committee
6 member of the nominating committee

OFFICERS

David J. Wilson
President & Chief Executive Officer

Sadiq H. Lalani
Vice President & Chief Financial Officer

Douglas J. Errico
Vice President, Land

Alan G. Franks
Vice President, Production

Bruce D. Gigg
Vice President, Engineering

Ashley D. Hohm
Vice President, Finance

Douglas O. MacArthur
Vice President, Operations

Patrick W.G. Miles
Vice President, Exploration

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BANKERS

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Calgary, Alberta T2P 3H2

AUDITORS

PricewaterhouseCoopers LLP
Suite 3100, 111 Fifth Avenue S.W.
Calgary, Alberta T2P 5L3

EVALUATION ENGINEERS

Sproule Associates Limited
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Calgary, Alberta T2P 3N3

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Convertible Debentures "KEL.DB"

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