kelt exploration

THIRD QUARTER REPORT

AS AT AND FOR THE THREE AND NINE MONTHS ENDED

SEPTEMBER 30, 2018

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FINANCIAL AND OPERATIONAL HIGHLIGHTS	Three months ended September 30			Nine months ended September 30		
(CA$ thousands, except as otherwise indicated)	**2018**	2017	%	**2018**	2017	%
FINANCIAL						
Petroleum and natural gas revenue, before royalties	**100,219**	56,422	78	**288,927**	176,719	63
Cash provided by operating activities	**29,881**	24,394	22	**122,727**	78,764	56
Adjusted funds from operations (1)	**46,876**	22,957	104	**139,699**	75,113	86
Basic ($/ common share) (1)	**0.25**	0.13	92	**0.77**	0.43	79
Diluted ($/ common share) (1)	**0.25**	0.13	92	**0.76**	0.42	81
Profit (loss) and comprehensive income (loss)	**3,632**	(10,653)	134	**5,311**	(17,789)	130
Basic ($/ common share)	**0.02**	(0.06)	133	**0.03**	(0.10)	130
Diluted ($/ common share)	**0.02**	(0.06)	133	**0.03**	(0.10)	130
Total capital expenditures, net of dispositions	**68,427**	75,933	-10	**215,166**	72,199	198
Total assets	**1,378,114**	1,227,962	12	**1,378,114**	1,227,962	12
Net debt (1)	**176,046**	134,759	31	**176,046**	134,759	31
Convertible debentures	**77,350**	73,584	5	**77,350**	73,584	5
Shareholders' equity	**889,274**	830,344	7	**889,274**	830,344	7
Weighted average shares outstanding (000s)						
Basic	**183,919**	176,013	4	**182,262**	175,875	4
Diluted	**186,449**	177,206	5	**184,319**	177,204	4
OPERATIONS						
Average daily production						
Oil (bbls/d)	**7,519**	6,881	9	**8,101**	6,206	31
NGLs (bbls/d)	**2,821**	2,714	4	**2,984**	2,348	27
Gas (mcf/d)	**95,186**	77,489	23	**92,078**	75,524	22
Combined (BOE/d)	**26,204**	22,510	16	**26,431**	21,141	25
Production per million common shares (BOE/d)(1)	**142**	128	11	**145**	120	21
Average realized prices, before financial instruments(1)						
Oil ($/bbl)	**80.62**	53.22	51	**76.29**	56.51	35
NGLs ($/bbl)	**41.20**	24.34	69	**36.39**	26.79	36
Gas ($/mcf)	**2.81**	2.33	21	**2.86**	3.09	-7
Operating netbacks ($/BOE) (1)						
Petroleum and natural gas revenue	**41.57**	27.24	53	**40.04**	30.62	31
Cost of purchases	**(3.83)**	-	-	**(2.61)**	-	-
Average realized price, before financial instruments(1)	**37.74**	27.24	39	**37.43**	30.62	22
Realized loss on financial instruments	**-**	0.02	-100	**-**	(0.06)	-100
Average realized price, after financial instruments(1)	**37.74**	27.26	38	**37.43**	30.56	22
Royalties	**(3.75)**	(2.46)	52	**(3.49)**	(2.84)	23
Production expense	**(9.31)**	(9.19)	1	**(9.30)**	(9.67)	-4
Transportation expense	**(3.75)**	(2.75)	36	**(3.66)**	(3.14)	17
Operating netback (1)	**20.93**	12.86	63	**20.98**	14.91	41
Undeveloped land						
Gross acres	**750,609**	775,485	-3	**750,609**	775,485	-3
Net acres	**634,982**	657,175	-3	**634,982**	657,175	-3

(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 third quarter ended September 30, 2018.

Average production for the three months ended September 30, 2018 was 26,204 BOE per day, up 16% compared to average production of 22,510 BOE per day during the third quarter of 2017. Quarter-over-quarter, daily average production in the third quarter of 2018 was flat compared to average production of 26,120 BOE per day in the second quarter of 2018. Flat quarter-over-quarter production was primarily the result of a re-allocation of capital expenditures as previously announced by the Company in its press release dated September 4, 2018. Production for the three months ended September 30, 2018 was weighted 39% oil and NGLs and 61% gas. However, operating income was weighted 88% oil and NGLs and 12% gas.

Kelt's realized average oil price during the third quarter of 2018 was $80.62 per barrel, up 51% from $53.22 per barrel in the third quarter of 2017. The realized average NGLs price during the third quarter of 2018 was $41.20 per barrel, up 69% from $24.34 per barrel in the same quarter of 2017. Kelt's realized average gas price for the third quarter of 2018 was $2.81 per Mcf, up 21% from $2.33 per Mcf in the corresponding quarter of the previous year. Kelt benefits with premium natural gas price realizations compared to AECO as a result of its gas market diversification portfolio and high heat content gas. During the third quarter of 2018, the Company's realized average gas price was 138% higher than the average AECO 5A price of $1.18 per MMBtu.

To date, in the fourth quarter of 2018, the light oil differential from WTI to Edmonton CLS has widened significantly due to downstream refinery maintenance and insufficient pipeline egress from western Canada which is expected to negatively impact oil revenue for the Company during the fourth quarter of 2018. The Company expects to partially mitigate lower oil prices in the fourth quarter with significantly higher gas prices in its gas market portfolio. Kelt has entered into financial contracts as follows:

- fixed the price of Sumas natural gas at a price of US$5.97 per MMBtu on 7,500 MMBtu per day for the five month period from November 1, 2018 to March 31, 2019;
- fixed the Canadian Dollar exchange rate at $1.3050 per US Dollar on US$1.0 million per month for the twelve month period from January 1, 2019 to December 31, 2019;
- fixed the NYMEX to Dawn natural gas basis differential at negative US$0.0975 per MMBtu on 10,000 MMBtu per day for the twelve month period from January 1, 2019 to December 31, 2019; and
- fixed the NYMEX to Chicago natural gas basis differential at negative US$0.14 per MMBtu on 10,000 MMBtu per day for the ten month period from January 1, 2019 to October 31, 2019.

After considering existing contracts to deliver physical gas at Station 2, adjusting for heat value and after deducting the fixed financial basis contracted and current transportation costs, Kelt is expected to realize approximately $7.00 per Mcf for its B.C. gas delivered at Station 2 pursuant to the aforementioned fixed price Sumas contract of US$5.97/MMBtu for the period from November 1, 2018 to March 31, 2019.

For the three months ended September 30, 2018, revenue was $100.2 million and adjusted funds from operations was $46.9 million ($0.25 per share, diluted), compared to $56.4 million and $23.0 million ($0.13 per share, diluted) respectively, in the third quarter of 2017. Net capital expenditures incurred during the three months ended September 30, 2018 were $68.4 million. During the third quarter of 2018, the Company spent $29.6 million on drill and complete operations, $39.7 million on facilities, pipelines and equipment and $0.8 million on land and seismic. Despite large expenditures in recent years on land accumulation, exploration drilling and facilities, Kelt reported net earnings of $3.6 million for the quarter. This capital investment is expected to translate into future earnings growth as the Company moves into a full development drilling program.

Ongoing discussions relating to potential tariffs or an access surtax on steel products imported into Canada may result in significantly higher steel costs, if implemented. Kelt has been pro-active in this respect and has pre-acquired approximately $4.9 million of casing, tubing, rods and line pipe and intends to acquire up to an aggregate of $12.0 million by year-end. These steel products will be held in inventory in 2018 and are expected to be used in 2019 as part of the Company's budgeted operations. The incremental $12.0 million for steel products is included in the Company's estimated total net capital expenditure budget of $287.0 million for 2018.

At September 30, 2018, bank debt, net of working capital was $176.0 million, utilizing 70% of the authorized borrowing amount available under the Company's credit facility of $250.0 million.

2018 OUTLOOK

As a result of lower production than originally forecasted during the third quarter, primarily due to the re-allocation of capital expenditures, Kelt has reduced its annual 2018 average production estimate to be within a range of 27,000 to 28,000 BOE per day (previously 28,000 to 29,000 BOE per day). The expected range for production in 2018 would represent an increase between 22% and 27% from average production in 2017 of 22,130 BOE per day. Estimated production for 2018 is expected to be weighted approximately 42% oil and NGLs and 58% gas. The table below summarizes Kelt's revised financial guidance for 2018:

	New 2018 Forecast	Previous 2018 Forecast	Change
Commodity Prices:			
WTI Crude Oil (USD/bbl)	67.50	67.50	N/C
WTI to Edmonton CLS Basis Discount (CAD/bbl)	16.27	7.43	+ 119%
CLS Crude Oil (CAD/bbl)	70.94	79.59	− 11%
NYMEX Natural Gas (USD/MMBtu)	2.95	2.90	+ 2%
DAWN Gas Daily Index (USD/MMBtu)	3.00	2.85	+ 5%
CHICAGO City Gate Gas Daily Index (USD/MMBtu)	2.92	2.80	+ 4%
MALIN Gas Monthly Index (USD/MMBtu)	2.43	2.35	+ 3%
SUMAS Gas Monthly Index (USD/MMBtu)	2.85	2.15	+ 33%
AECO 5A Gas Daily Index (USD/MMBtu)	1.28	1.40	− 9%
Station 2 Gas NGX Daily Index (USD/MMBtu)	1.13	1.15	− 2%
Exchange Rate (USD/CAD)	0.774	0.776	N/C
Capital expenditures, net of dispositions ($ MM)	287.0	275.0	+ 4%
Funds from operations ("FFO") ($ MM)	193.0	210.0	− 8%
Per common share, diluted ($)	1.04	1.14	− 9%
Bank debt, net of working capital, at year-end ($ MM)	195.0	168.0	+ 16%
Net bank debt to trailing FFO ratio	1.0 x	0.8 x	+ 25%

Note: N/C – no change.

Kelt's 2018 capital expenditure program includes approximately $60.0 million of drilling and completion expenditures for wells that are not included in the 2018 production estimates as these wells are expected to be brought on-stream in 2019:

(a) 5 Montney wells at Wembley/Pipestone – drilled and completed in 2018 and expected to be brought on-stream in the second half of 2019 after construction of a proposed deep cut natural gas processing plant is completed; and
(b) 11 Montney wells at Inga/Fireweed – drilled in 2018, to be completed in 2019, and expected to be brought on-stream starting in the first half of 2019.

2019 GUIDANCE

The Company's Board of Directors has approved an initial capital expenditure budget of $270.0 million for 2019. Kelt expects to drill 34 gross (33.0 net) wells in 2019 and expects to complete 36 gross (35.0 net) wells in 2019. The Company expects to have 11 gross (11.0 net) wells drilled but un-completed ("DUC") in 2018 and 8 gross (8.0 net) wells drilled but un-completed in 2019. The 2019 capital expenditures are expected to be allocated as follows: $201.0 million for drilling and completing wells, $60.0 million for facilities, pipeline and equipment and $9.0 million for land and seismic.

Preparation of the 2019 budget includes the following forecasted commodity price assumptions (with estimated forecasted 2018 commodity prices shown for comparative purposes):

	2019 Forecast	2018 Forecast	Change
Commodity Prices:			
WTI Crude Oil (USD/bbl)	67.50	67.50	N/C
WTI to Edmonton CLS Basis Discount (CAD/bbl) (1)	19.43	16.27	+ 19%
CLS Crude Oil (CAD/bbl)	66.97	70.94	− 6%
NYMEX Natural Gas (USD/MMBtu)	3.00	2.95	+ 2%
DAWN Gas Daily Index (USD/MMBtu)	2.90	3.00	− 3%
CHICAGO City Gate Gas Daily Index (USD/MMBtu)	2.85	2.92	− 2%
MALIN Gas Monthly Index (USD/MMBtu)	2.45	2.43	+ 1%
SUMAS Gas Monthly Index (USD/MMBtu)	2.90	2.85	+ 2%
AECO 5A Gas Daily Index (USD/MMBtu)	1.60	1.28	+ 25%
Station 2 Gas NGX Daily Index (USD/MMBtu)	1.30	1.13	+ 15%
Exchange Rate (USD/CAD)	0.781	0.774	+ 1%

(1) Actual and estimated quarterly light oil differentials are as follows: Q119 $30.00 (Q118 $9.52), Q219 $23.00 (Q218 $10.05), Q319 $15.00 (Q318 $15.42), Q419 $10.00 (Q418 $30.00).

Kelt has prepared its 2019 financial guidance based on a capital expenditure budget of $270.0 million and the aforementioned forecasted commodity prices that result in the following:

- Estimated average production of 33,500 to 34,500 BOE per day, an increase of approximately 24% from estimated 2018 production levels;
- Production mix is expected to be weighted 47% to oil & NGLs and 53% to gas;
- Operating income is expected to be derived 85% from oil & NGLs and 15% from gas;
- Estimated funds from operations of $240.0 million ($1.23 per share, diluted); and
- Estimated bank debt, net of working capital as at December 31, 2019 of $225.0 million (0.9x forecasted 2019 funds from operations).

OPERATIONS UPDATE

Wembley/Pipestone area

Kelt previously reported that it has entered into agreements to process its gas from the Wembley/Pipestone area to Tidewater Midstream and Infrastructure Ltd.'s ("Tidewater") proposed newly constructed deep-cut gas processing plant. In October 2018, Tidewater reported that it had received approval from the Alberta Energy Regulator ("AER") to construct and operate the Pipestone Montney sour deep-cut gas processing complex targeting an in-service date of mid-2019. Kelt expects to bring production on-stream from eight to ten Montney wells at the time of start-up of the Tidewater gas plant.

Inga/Fireweed area

Kelt has commenced drilling operations at its first 24-well multi-layer Montney cube pad at Inga located at 05-09-088-23W6 ("Inga 5-9 Pad"). The Company expects to complete the drilling of all 24 wells by the fourth quarter of 2019. Wells will be completed and put on-stream six wells at a time with the first six wells expected to start producing in April 2019. Kelt recently received approval from the British Columbia Oil & Gas Commission ("BCOGC") to construct a pipeline from the Inga 5-9 pad to the Company's Inga gas facility located at 02-10-088-23W6 ("Inga 2-10 Facility").

At Fireweed, where the Company drilled five Montney wells at a pad located at B-33-I/94-A-12 ("Fireweed B-33-I Pad") in the summer of 2018, Kelt has now received approval from the BCOGC to construct a pipeline (first segment) from the Inga 2-10 Facility to a pad located at 02-23-088-23W6 ("2-23 Pad"). The approval from the BCOGC to construct the pipeline (second segment) from the 2-23 Pad to the Fireweed B-33-I Pad is expected prior to year-end. The Company expects to complete these five wells prior to spring break-up in 2019 and put the wells on production by the summer of 2019.

Oak/Flatrock area

At Oak, the second delineation well drilled in the area was tied into a third party facility in early November 2018. During the initial start-up of the well located at 02/13-13-087-18W6, the third-party operated facility had difficulty handling the fluid slugs from the well resulting in sporadic production volumes. Despite the irregular run times, it appears that the well is in an oilier part of the reservoir than the initial Oak well located at 02/06-02-086-18W6/02.

During the last twenty four hours, on November 7th and 8th, the well produced average volumes of approximately 592 barrels per day of oil and 1.0 MMcf per day of raw gas. The well is expected to be constrained to existing compression limits at the third party facility of approximately 2.0 MMcf per day. Kelt is pleased with the results from the first two Montney wells drilled at Oak and expects to drill an additional four to six delineation wells in the area during 2019.

<u>Pouce Coupe/Progress area</u>

At Pouce Coupe, Kelt has completed all five wells from its most recent drilling pad and is currently bringing these wells on-stream. Four of the wells were drilled in the Lower-Middle Montney (D1) and Middle Montney (D2) zones, similar to previously drilled development wells in the area. Initial flow rates are very encouraging and appear to be at similar rates to the previous adjacent five-well pad that was brought on stream back in the first quarter of 2017. The fifth well was drilled in the Upper-Middle Montney (D4), a zone that has not previously been tested in the Pouce Coupe area. This well, which is located at 03/05-18-078-11W6 was drilled with a horizontal lateral of approximately 2,112 metres and was completed using the ball drop hydraulic fracturing method with 2,561 tonnes of proppant. Frac fluid was pumped at an average rate of 10.8 cubic metres per minute. After flowing the frac fluid back on an 11-day clean-up, the well, over the last 7 days produced average sales volumes of approximately 842 BOE per day (58% oil/NGLs and 42% gas). Kelt is pleased with the initial results from this well and will monitor the well for a longer term production profile, as this could unlock a significant amount of additional drilling inventory on the Company's lands in the area.

The Company is pleased with its operational results to date in 2018 and is well positioned financially to execute its capital program during the remainder of the year and into 2019. Kelt expects to exit 2018 with a net bank debt/funds from operations ratio of 1.0 times, reducing to 0.9 times by the end of 2019.

Management looks forward to updating shareholders with 2018 third quarter results on or about November 9, 2018.

On behalf of the Board of Directors,

[signed]

David J. Wilson
President and Chief Executive Officer
May 9, 2018

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 ("BC"). The Company was incorporated under the *Business Corporations Act* (Alberta) on October 11, 2012. Kelt's land holdings are located in two core areas, namely: (a) Grande Prairie, Alberta (including Pouce Coupe, Progress, La Glace and Wembley), held directly by Kelt; and (b) Fort St. John, BC (including Inga, Fireweed, Stoddart and Oak), held by the Company's wholly-owned subsidiary, Kelt Exploration (LNG) Ltd. ("Kelt LNG"). The head office of the Company is located at Suite 300, 311 - 6th Avenue S.W., Calgary, Alberta T2P 3H2. 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.

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

This Management's Discussion and Analysis ("MD&A") is dated November 9, 2018 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 and nine months ended September 30, 2018 and its audited consolidated annual financial statements and MD&A as at and for the year ended December 31, 2017. 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 consolidated annual financial statements for issue on November 8, 2018.

ADVISORY REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report and 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", "potentially" and similar expressions are intended to identify forward-looking information or statements. In particular, this Quarterly Report and MD&A contains forward-looking statements pertaining to the following: Kelt's expected price realizations and future commodity prices; the cost and timing of future capital expenditures and expected results; the Company's ability to continue accumulating land at a low-cost in its core operating areas and potentially monetize non-core assets; the expected timing of wells drilled and well completions, facility expenditures and production additions from capital expenditures; and the Company's expected future financial position and operating results. 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].

Any references in this Quarterly Report to initial production rates are useful in confirming the presence of hydrocarbons; however, such rates are not determinative of the rates at which such wells will continue production and decline thereafter and are not necessarily indicative of long-term performance or ultimate recovery. While encouraging, readers are cautioned not to place reliance on such rates in calculating the aggregate production for the Company. Such rates are based on field estimates and may be based on limited data available at this time.

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, 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; 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 to further enhance its opportunity base.

Kelt is opportunity driven and is confident that it can grow its production by both developing its current inventory of 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

- Production averaged 26,204 BOE per day (39% oil/NGLs) compared to 26,120 BOE per day (42% oil/NGLs) in the second quarter of 2018, and up 16% from 22,510 BOE per day (43% oil/NGLs) in the third quarter of 2017.
- Total revenue for the three months ended September 30, 2018 was $100.2 million, up 78% from $56.4 million in the same quarter of 2017. Kelt’s average realized price before financial instruments of $37.74 per BOE during the third quarter of 2018 was 39% higher than the average realized price before financial instruments of $27.24 per BOE realized in the third quarter of 2017, reflecting the increase in Kelt’s corporate average oil production weighting, as well as the increase in the benchmark oil and NGLs prices.
- During the three months ended September 30, 2018, production expenses of $9.31 per BOE was slightly higher than production expenses of $9.19 per BOE in 2017. For the nine months ended September 30, 2018 production expenses of $9.30 improved by 4% from $9.67 per BOE in 2017.
- During the three months ended September 30, 2018, corporate royalty rates averaged 10%, transportation expenses were $3.75 per BOE, interest expense was $1.04 per BOE and G&A expense was $0.87 per BOE. In the comparative quarter of 2017, corporate royalty rates averaged 9%, transportation expenses were $2.75 per BOE, interest expense was $0.98 per BOE and G&A expense was $0.79 per BOE.
- Kelt’s operating netback was $20.93 per BOE for the quarter ended September 30, 2018, down 3% from $21.57 per BOE during the quarter ended June 30, 2018 and up 63% from $12.86 per BOE during the quarter ended September 30, 2017. The increase in operating netback was primarily driven by Kelt’s higher combined average realized price.
- Adjusted funds from operations of $46.9 million ($0.25 per share, diluted) during the third quarter of 2018 decreased 0.4% from $47.1 million ($0.25 per share, diluted) in the second quarter of 2018 and increased 104% from $23.0 million ($0.13 per share, diluted) during the third quarter of 2017.

- Capital expenditures incurred during the three months ended September 30, 2018 were $70.1 million. The Company spent $29.6 million on drill and complete operations, $39.7 million on equipment, facilities and pipelines and $0.8 million on land and seismic. The spend in facilities included $16.4 million on the on-going construction of a natural gas facilities in BC.
- As at September 30, 2018, Kelt's net working interest land holdings were 858,157 acres (1,341 sections) of which 634,982 net acres (992 sections) are undeveloped. Kelt is focused 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.
- The Company maintained a strong balance sheet with net debt of $176.0 million at September 30, 2018 (0.9 times trailing adjusted funds from operations).
- The Company has $89.9 million principal amount of convertible debentures outstanding with a conversion price of $5.50 per share and maturity date of May 31, 2021, if not converted or redeemed prior to maturity. As at September 30, 2018, the convertible debentures are "in-the-money" based on the closing price of Kelt common shares on the TSX of $8.41 on the last trading day of the quarter.

Kelt is well positioned to execute on its 2018 capital expenditure program and has sufficient financial flexibility to take advantage of opportunities as they arise.

PRODUCTION

	Three months ended September 30			Nine months ended September 30		
(CA$ thousands, except as otherwise indicated)	**2018**	2017	%	**2018**	2017	%
Average daily production:						
Oil (bbls/d)	**7,519**	6,881	9	**8,101**	6,206	31
NGLs (bbls/d)	**2,821**	2,714	4	**2,984**	2,348	27
Gas (mcf/d)	**95,186**	77,489	23	**92,078**	75,524	22
Combined (BOE/d)	**26,204**	22,510	16	**26,431**	21,141	25

Average production for the three months ended September 30, 2018 was 26,204 BOE per day, up 16% compared to average production of 22,510 BOE per day during the third quarter of 2017, and up slightly compared to the average production of 26,120 BOE per day during the second quarter of 2018. Average oil production during the third quarter of 2018 increased by 9% compared to average oil production in the third quarter of 2017. Oil and NGLs production represented 39% of corporate average production during the third quarter of 2018 compared to 43% during the third quarter of 2017.

Kelt's average production reported for the first nine months of 2018 of 26,431 BOE per day is 25% higher than the comparative period in 2017. Average oil production during the nine months ending September 30, 2018 increased by 31% compared to average oil production for the first nine months of 2017. Oil and NGLs production represented 42% of corporate average production during the first nine months of 2018 compared to 40% during the comparable period on 2017.

The increase in production in 2018 from the comparable periods in 2017 was driven by strong results from the Company's active development drilling program in its core areas in Alberta and BC targeting multiple zones of its oil and condensate rich Montney acreage. The production increase in 2018 was partially offset due to a delay in the completion of a five-well pad drilled at Fireweed BC during the second and third quarter of 2018. These completions were delayed due to a "pause" implemented by the BC Oil and Gas Commission while it negotiates interim measures for applications that fall within sensitive areas of the Blueberry River First Nations. The Company expects to complete and bring these wells on production in 2019.

REVENUE

All references to revenue in this discussion are before royalties. Petroleum and natural gas revenue (before royalties) as reported in the Consolidated Statement of Profit (Loss) and Comprehensive Income (Loss) has been abbreviated as "total revenue". "Kelt Revenue" includes total revenue, net of the cost of the third party volumes purchased and is before royalties – refer to additional information under the heading of "Non-GAAP Financial Measures and Other Key Performance Indicators".

	Three months ended September 30			Nine months ended September 30		
(CA$ thousands, except as otherwise indicated)	**2018**	2017	%	**2018**	2017	%
Revenue, before royalties and financial instruments:						
Oil	**55,754**	33,694	65	**168,394**	95,747	76
NGLs	**10,691**	6,077	76	**29,651**	17,174	73
Gas	**24,063**	16,651	45	**71,303**	63,798	12
Revenue, before marketing	**90,508**	56,422	60	**269,348**	176,719	52
Marketing revenue (2)	**9,711**	-	-	**19,579**	-	-
Total revenue (1)	**100,219**	56,422	78	**288,927**	176,719	63
Cost of purchases (3)	**(9,230)**	-	-	**(18,846)**	-	-
Kelt Revenue (4)	**90,989**	56,422	61	**270,081**	176,719	53
Average realized prices (5)						
Oil ($/bbl)	**80.62**	53.22	51	**76.29**	56.51	35
NGLs ($/bbl)	**41.20**	24.34	69	**36.39**	26.79	36
Gas ($/mcf)	**2.81**	2.33	21	**2.86**	3.09	-7
Combined ($/BOE)	**37.74**	27.24	39	**37.43**	30.62	22

(1) Petroleum and natural gas revenue (before royalties) as reported in the consolidated financial statements is abbreviated as "total revenue".

(2) Sales of third party volumes related to the Company's oil blending operations and natural gas activities.

(3) Cost of third party volumes purchased for use and resale in the Company's oil blending operations and natural gas activities.

(4) "Kelt Revenue" is a non-GAAP measure and includes petroleum and natural gas revenue (before royalties), net of the cost of the third party volumes purchased.

(5) Average realized prices are calculated based on Kelt Revenue (4) and reflect Kelt's realized commodity prices plus the net benefit of oil blending and natural gas marketing activities (2)(3). Refer to additional information under the heading of *"Non-GAAP Financial Measures and Other Key Performance Indicators"*.

Revenue for the third quarter of 2018 was $90.5 million, up 60% from $56.4 million from the third quarter of 2017. Revenue for the nine months ending September 30, 2018 was $269.3 million, up 52% from the comparable period in 2017. The increase in revenue was driven by a combination of higher production volumes and higher combined average realized prices. Average realized prices increased 39% to $37.74 per BOE in the third quarter of 2018 and increased 22% to 37.43 per BOE in the nine months ending September 30, 2018 versus the comparable periods in 2017. The increase in Kelt's average realized oil and NGLs price was primarily due to higher benchmark commodity prices. Kelt's average realized natural gas price increased 21% in the third quarter of 2018 versus a decline of 19% in AECO 5A benchmark pricing. The increase in Kelt's average realized natural gas price was primarily due to the various gas marketing arrangements that the Company entered into in November 2017 to diversity and gain exposure to alternative markets.

OIL REVENUE

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

	Three months ended September 30			Nine months ended September 30		
(CA$ thousands, except as otherwise indicated)	**2018**	2017	%	**2018**	2017	%
Oil production (average bbls per day)	**7,519**	6,881	9	**8,101**	6,206	31
Oil revenue, before marketing	**55,754**	33,694	65	**168,394**	95,747	76
Marketing revenue, net of cost of purchases (1)	**20**	-	-	**337**	-	-
Kelt Oil Revenue	**55,774**	33,694	66	**168,731**	95,747	76
Average realized oil prices ($/bbl) (2)(3)	**80.62**	53.22	51	**76.29**	56.51	35
Average realized price, percentage of CLS	**107%**	93%		**102%**	93%	
Benchmark oil prices:						
WTI Cushing Oklahoma (US$/bbl) (5)	**69.46**	48.20	44	**66.74**	49.47	35
WTI Cushing Oklahoma (CA$/bbl) (5)	**90.79**	60.38	50	**86.06**	64.66	33
Canadian Light Sweet ("CLS") ($/bbl) (4)	**75.64**	57.15	32	**74.52**	60.57	23
CLS % of CA$WTI	**83%**	95%	-12	**87%**	94%	-8
Average exchange rate (CA$/US$) (4)	**1.3070**	1.2529	4	**1.2883**	1.3055	-1

(1) Net marketing revenue related to the purchase and resale of third party volumes used in the Company's oil blending operations.

(2) Calculated based on Kelt Oil Revenue and reflects Kelt's realized oil price plus the net benefit of the Company's oil blending operations.

(3) 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. Refer to further discussion under the heading of *"Transportation Expenses"*.

(4) Source: Sproule Associates Limited.

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

Kelt realized an average oil price of $80.62 per barrel during the three months ended September 30, 2018, up from $53.22 per barrel during the comparative period of 2017. Kelt realized an average oil price of $76.29 per barrel during the nine months ended September 30, 2018, up from $56.51 per barrel during the comparative period of 2017.

Global benchmark crude oil prices have strengthened significantly in 2018 due to global oil demand growth exceeding global supply growth, along with an overall increase in geopolitical risks. During the three months ended September 30, 2018, WTI averaged US$69.46 (CA$90.79) per barrel, up 44% from US$48.20 (CA$60.38) per barrel in the third quarter of 2017 and up 2% compared to US$67.88 (CA$87.86) in the in the second quarter of 2018. During the nine months ended September 30, 2018, WTI averaged US$66.74 (CA$86.06) per barrel, up 35% from US$49.47 (CA$64.66) per barrel in the nine months ending September 30, 2017.

For the three months ending September 30, 2018 the impact of a stronger US denominated WTI oil price was further impacted by the depreciation of the Canadian dollar which increased the equivalent price realized by Kelt in Canadian dollars. For the nine months months ending September 30, 2018 the impact of a stronger US denominated WTI oil price was partially offset by the appreciation of the Canadian dollar.

NGL REVENUE

References to "NGLs" in this discussion includes pentanes (C5 and C5+), butane (C4), propane (C3) and ethane (C2) (see "Other Measurements" for additional references). All references to "NGLs revenue" are before NGLs royalties.

	Three months ended September 30			Nine months ended September 30		
(CA$ thousands, except as otherwise indicated)	**2018**	2017	%	**2018**	2017	%
NGLs production (average bbls per day)	**2,821**	2,714	4	**2,984**	2,348	27
NGLs barrels per mmcf of natural gas sales	**30**	35	-14	**32**	31	3
NGLs revenue	**10,691**	6,077	76	**29,651**	17,174	73
Average realized NGLs price ($/bbl):						
Before financial instruments	**41.20**	24.34	69	**36.39**	26.79	36
Realized gain (loss) on financial instruments	**-**	(1.49)	-100	**-**	(0.64)	-100
After financial instruments	**41.20**	22.85	80	**36.39**	26.15	39
Average realized price, percentage of CA$WTI (1)	**45%**	40%		**42%**	41%	
Benchmark NGLs prices (2) ($/bbl):						
Edmonton Pentane	**86.04**	61.42	40	**84.26**	65.04	30
% of CA$WTI	**95%**	102%	-7	**98%**	101%	-3
Edmonton Butane	**31.73**	39.90	-20	**40.43**	41.04	-1
% of CA$WTI	**35%**	66%	-47	**47%**	63%	-25
Edmonton Propane	**26.17**	26.66	-2	**27.95**	24.89	12
% of CA$WTI	**29%**	44%	-34	**32%**	38%	-16
Edmonton Ethane	**3.56**	4.47	-20	**4.19**	6.55	-36
% of CA$WTI	**4%**	7%	-43	**5%**	10%	-50

(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.

Kelt's NGLs revenue increased by 76% in the third quarter of 2018, and increased by 73% in the nine months ending September 30, 2018 compared to the same periods in 2017. The increase in revenues resulted from a combination of both higher NGLs production, and higher benchmark WTI prices.

The Company's NGLs production increased by 4% in the third quarter of 2018, and 27% in the nine months ending September 30, 2018 as compared to the same periods in 2017. The increase in production in 2018 was driven by strong results from the Company's active development drilling program in its oil and condensate rich Montney acreage.

Kelt realized an average price before financial instruments for its NGL sales of $41.20 per barrel (45% of CA$WTI) during the third quarter of 2018, up from $24.34 per barrel (40% of CA$WTI) during the third quarter of 2017. Kelt realized an average price before financial instruments for its NGL sales of $36.39 per barrel (42% of CA$WTI) during the nine months ending September 30 2018, up from $26.79 per barrel (41% of CA$WTI) during the comparable period in 2017. The increase in NGLs prices was driven primarily by the increase in benchmark WTI crude oil prices.

GAS REVENUE

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

(CA$ thousands, except as otherwise indicated)	Three months ended September 30 **2018**	2017	%	Nine months ended September 30 **2018**	2017	%
Gas production (MCF per day)	**95,186**	77,489	23	**92,078**	75,524	22
Gas revenue, before marketing	**24,063**	16,651	45	**71,303**	63,798	12
Marketing revenue, net of cost of purchases (10)	**460**	-	-	**395**	-	-
Kelt Gas Revenue	**24,523**	16,651	47	**71,698**	63,798	12
Average realized gas price ($/MCF)						
Before financial instruments	**2.81**	2.33	21	**2.86**	3.09	-7
Realized gain (loss) on financial instruments	**-**	0.06	-100	**-**	-	-
After financial instruments	**2.81**	2.39	21	**2.86**	3.09	-7
Kelt average premium to AECO 5A (1)	**138%**	61%		**93%**	34%	
Benchmark gas prices:						
NYMEX Henry Hub (US$/MMBtu) (2)	**2.87**	2.97	-3	**2.87**	3.12	-8
Average exchange rate (CA$/US$) (3)	**1.3069**	1.2524	4	**1.2876**	1.3066	-1
NYMEX Henry Hub (CA$/MMBtu) (2)	**3.76**	3.72	1	**3.69**	4.08	-10
AECO 5A (CA$/MMBtu) (4)	**1.18**	1.45	-19	**1.48**	2.31	-36
Chicago-City Gate (CA$/MMBtu) (5)	**3.64**	3.54	3	**3.60**	3.80	-5
Dawn (CA$/MMBtu) (6)	**3.81**	3.64	5	**3.73**	4.02	-7
Malin (CA$/MMBtu) (7)	**3.12**	3.38	-8	**2.94**	3.74	-21
Sumas (CA$/MMBtu) (8)	**2.62**	3.05	-14	**2.62**	3.60	-27
Station 2 (CA$/MMBtu) (9)	**1.31**	0.88	49	**1.44**	1.89	-24

(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" (US$/MMBtu). The Canadian dollar equivalent NYMEX price is calculated based on the monthly average US$ price and the monthly average CA$/US$ exchange rate (3).

(3) Source: Bank of Canada

(4) Source: Canadian Gas Price Reporter "NGX AB-NIT Same Day Index 5A" (CA$/GJ) converted to CA$/MMBtu.

(5) Source: Platts "Alliance, into Interstates" Daily Midpoint Average (US$/MMBtu). The Canadian dollar equivalent Chicago-City Gate price is calculated based on the monthly average US$ price and the monthly average CA$/US$ exchange rate (3).

(6) Source: Canadian Gas Price Reporter "NGX Union-Dawn Spot Day Ahead Index" (CA$/GJ) converted to CA$/MMBtu.

(7) Source: Platts "P&G Malin" Monthly Bidweek Spot Gas Price (US$/MMBtu). The Canadian dollar equivalent Malin price is calculated based on the monthly average US$ price and the monthly average CA$/US$ exchange rate (3).

(8) Source: Platts "Northwest, Canadian Border (Sumas)" Monthly Bidweek Spot Gas Price (US$/MMBtu). The Canadian dollar equivalent Sumas price is calculated based on the monthly average US$ price and the monthly average CA$/US$ exchange rate (3).

(9) Source: Canadian Gas Price Reporter "NGX Spectra Station #2 Day Ahead Index" (CA$/GJ) converted to CA$/MMBtu.

(10) Net marketing revenue related to the purchase and resale of third party volumes.

With AECO 5A gas reference prices maintaining historical lows throughout the third quarter of 2018, Kelt's gas marketing diversification strategy introduced in November 2017 continued to pay off significant dividends in 2018 with Kelt's average premium to AECO 5A reaching 138% in the third quarter of 2018 and 93% year to date in 2018, versus 61% and 34% for the comparable periods in 2017. During 2017, gas sales under AECO based contracts represented 60-65% of the Company's total gas production and Kelt received Chicago-City Gate pricing on approximately 25-30% of its gas production. With the commencement of the new marketing contracts effective November 1, 2017, approximately 20-30% of the Company's gas sales are sold under AECO based contracts, with the remaining production sold under the Company's Dawn, Malin, Chicago-City and Sumas based contracts. The impact of the higher realized gas price on Kelt's funds from operations is partially offset by higher transportation tolls which are included in transportation expenses.

Natural gas revenue before marketing increased 47% to $24.1 million in the third quarter of 2018 and increased 12% to $71.3 million in the nine months ending September 30, 2018 versus the comparable periods in 2017. Revenues increased primarily due to an increase in production versus the comparable periods in 2017.

ROYALTIES

	Three months ended September 30			Nine months ended September 30		
(CA$ thousands, except as otherwise indicated)	**2018**	2017	%	**2018**	2017	%
Royalties	**9,051**	5,107	77	**25,159**	16,372	54
Average royalty rate (1)	**10.0%**	9.0%	10	**9.3%**	9.3%	-
$ per BOE	**3.75**	2.47	52	**3.49**	2.84	23

(1) Average royalty rate is calculated based on total royalties as a percentage of "Revenue, before marketing" which excludes revenue related to the sale of third party production volumes used in oil blending operations (see table under the heading of *"Revenue"*).

Kelt's average royalty rate was 10.0% during the third quarter of 2018, compared to 9.0% during the third quarter of 2017. Kelt's average royalty rate was 9.3% during both the nine months ending September 30, 2018 and September 30, 2017. The increase in the third quarter of 2018 compared to 2017 was primarily due to high productivity oil and condensate wells which have maximized the favorable treatments under Alberta and BC royalty frameworks.

PRODUCTION EXPENSES

	Three months ended September 30			Nine months ended September 30		
(CA$ thousands, unless otherwise indicated)	**2018**	2017	%	**2018**	2017	%
Production expense	**22,443**	19,025	18	**67,118**	55,816	20
$ per BOE	**9.31**	9.19	1	**9.30**	9.67	-4

The Company incurred total production expenses of $22.4 million during the third quarter of 2018, up 18% from the third quarter of 2017. The increase in total production expenses in the third quarter of 2018 compared to the third quarter of 2017 reflects the 16% increase in corporate average production. Production expenses averaged $9.31 per BOE during the third quarter of 2018, compared to $9.19 per BOE in the same period in 2017.

The Company incurred total production expenses of $67.1 million during the first nine months of 2018, up 20% from $55.8 million during the nine months ending September 30, 2017. Production expenses averaged $9.30 per BOE during the nine months ending September 2018, compared to $9.67 per BOE in the same period in 2017. The reduction of production expenses per BOE in 2018 was primarily the result of bringing on new production with lower average production costs.

TRANSPORTATION EXPENSES

	Three months ended September 30			Nine months ended September 30		
(CA$ thousands, unless otherwise indicated)	**2018**	2017	%	**2018**	2017	%
Transportation expense (1)	**9,036**	5,691	59	**26,383**	18,129	46
$ per BOE	**3.75**	2.75	36	**3.66**	3.14	17

(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 $3.75 per BOE during the third quarter of 2018, an increase of 36% from $2.75 per BOE in the third quarter of 2017. Transportation expenses averaged $3.66 per BOE during the nine months ending September 30, 2018, an increase of 17% from $3.14 per BOE in the nine months ending September 30, 2017. The increase in average per unit transportation expenses compared to 2017 was due to higher pipeline tolls under the various marketing arrangements that the Company entered into in the fourth quarter of 2017 in order to diversify its gas sales markets.

FINANCING EXPENSES

	Three months ended September 30			Nine months ended September 30		
(CA$ thousands, unless otherwise indicated)	**2018**	2017	%	**2018**	2017	%
Interest and fees on bank debt	**1,375**	904	52	**3,786**	2,297	65
Interest on convertible debentures	**1,133**	1,134	-	**3,364**	3,366	-
Total interest expense	**2,508**	2,038	23	**7,150**	5,663	26
Accretion of convertible debentures	**1,002**	899	11	**2,909**	2,606	12
Accretion of decommissioning obligations	**792**	743	7	**2,347**	2,207	6
Total financing expense	**4,302**	3,680	17	**12,406**	10,476	18
Interest expense per BOE (1)	**1.04**	0.98	6	**0.99**	0.98	1
Average principal amount outstanding during period:						
Bank debt	**127,446**	83,243	53	**118,127**	59,708	98
Convertible debentures	**89,910**	90,000	-	**89,989**	90,000	-
Average interest rates:						
Bank debt (2)	**4.3**	4.3	-	**4.3**	5.1	-16
Convertible debentures	**5.0**	5.0	-	**5.0**	5.0	-

(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.

(2) Average interest rate inclusive of fees on bank debt.

The Company's total interest expense paid or payable in cash of $2.5 million ($1.04 per BOE) for the third quarter of 2018 increased 23% from the comparative quarter and increased 26% for the nine months ending September 30, 2018 compared to the nine months ending September 30, 2017. The increase in interest expense was due to the increase in average total debt.

GENERAL AND ADMINISTRATIVE ("G&A") EXPENSES

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

	Three months ended September 30			Nine months ended September 30		
(CA$ thousands, unless otherwise indicated)	**2018**	2017	%	**2018**	2017	%
Salaries and benefits	**2,371**	2,090	13	**7,047**	6,180	14
Other G&A expenses	**1,119**	971	15	**3,235**	2,997	8
Gross G&A expenses	**3,490**	3,061	14	**10,282**	9,177	12
Overhead recoveries	**(1,383)**	(1,416)	-2	**(4,366)**	(3,881)	12
G&A expense, net of recoveries	**2,107**	1,645	28	**5,916**	5,296	12
Gross G&A ($ per BOE)	**1.45**	1.48	-2	**1.42**	1.59	-11
Net G&A ($ per BOE)	**0.87**	0.79	10	**0.82**	0.92	-11

Kelt continues to incur below industry average G&A expenses as a result of management's continued efforts to maintain a low cost structure. Net G&A of $0.87 per BOE during the third quarter of 2018 increased 10% compared the third quarter of 2017, however decreased 11% for the nine months ending September 30, 2018 compared to the nine months ending September 30, 2017.

Total overhead recoveries for the third quarter of 2018 are comparable to the third quarter of 2017. Year-to-date overhead recoveries in 2018 are higher than in 2017 in conjunction with an increase in capital expenditures in 2018.

SHARE BASED COMPENSATION ("SBC")

	Three months ended September 30			Nine months ended September 30		
(CA$ thousands, unless otherwise indicated)	**2018**	2017	%	**2018**	2017	%
Stock options	**902**	931	-3	**3,022**	2,687	12
Restricted share units ("RSUs")	**514**	393	31	**1,342**	1,186	13
Total SBC expense	**1,416**	1,324	7	**4,364**	3,873	13
$ per BOE	**0.59**	0.64	-8	**0.60**	0.67	-10

Share based compensation is expensed using graded amortization over the three year vesting period. The increase in SBC expense during the quarter ended September 30, 2018 and during the nine months ending September 30, 2018 versus the comparable periods in 2017 is a result of higher restricted share units being granted, and a higher average fair value of new stock options and RSU's granted, partially offset by a decrease in the number of new stock options granted in 2018.

As at September 30, 2018, stock options and RSUs outstanding represent 5.0% of total shares outstanding (December 31, 2017 – 6%).

EXPLORATION AND EVALUATION ("E&E") EXPENSES

	Three months ended September 30			Nine months ended September 30		
(CA$ thousands, unless otherwise indicated)	**2018**	2017	%	**2018**	2017	%
Expired mineral leases	**1,398**	460	204	**3,495**	987	254
$ per BOE	**0.58**	0.22	164	**0.48**	0.17	182

The Company expensed $1.4 million of costs related to the expiry of non-core land holdings during the quarter ended September 30, 2018 and $3.5 million in the nine months ending September 30, 2018, compared to lease expiries of $0.5 million and 1.0 million expensed in the comparative period.

DEPLETION, DEPRECIATION AND IMPAIRMENT

	Three months ended September 30			Nine months ended September 30		
(CA$ thousands, unless otherwise indicated)	**2018**	2017	%	**2018**	2017	%
Depletion of D&P assets	**35,564**	33,504	6	**108,571**	90,800	20
Depreciation of corporate assets	**190**	277	-31	**507**	748	-32
Depletion and depreciation	**35,754**	33,781	6	**109,078**	91,548	19
Impairment	**-**	-	-	**3,000**	-	-
Total depletion, depreciation and impairment	**35,754**	33,781	6	**112,078**	91,548	22
Depletion and depreciation ($/BOE)	**14.83**	16.31	-9	**15.12**	15.86	-5
Impairment ($/BOE)	**-**	-	-	**0.42**	-	-

The Company calculates depletion of development and production ("D&P") assets based on production relative to total proved reserves for each depletion unit. Depletion and depreciation of $35.8 million for the quarter ended September 30, 2018 increased by 6% from comparable period in 2017, with the increase attributed to a 16% increase in average production partially offset by an increase in proved reserves.

Depletion and depreciation of $109.1 million for the nine months ended September 30, 2018 increased by 19% from comparable period in 2017, with the increase attributed to a 25% increase in average production partially offset by an increase in proved reserves.

On July 31, 2018, the Company completed the disposition of the Leduc-Woodbend Cash Generating Unit ("CGU") for $2.6 million after closing adjustments. The Leduc-Woodbend CGU had a carrying value of $2.6 million, resulting in a gain on sale of $0.05 million. In the second quarter of 2018, the Leduc-Woodbend CGU was impaired by $3.0 million based on the sale in the third quarter of 2018.

There is no indication of impairment for the Company's CGUs as at September 30, 2018.

GAIN (LOSS) ON SALE OF ASSETS

	Three months ended September 30			Nine months ended September 30		
(CA$ thousands, unless otherwise indicated)	**2018**	2017	%	**2018**	2017	%
Gain on sale of assets	**38**	23	65	**197**	1,586	-88

On January 18, 2017, Kelt completed the Karr Property Disposition for proceeds of $103.1 million after closing adjustments. Closing of the Karr Property Disposition had a minimal impact on the gain on sale of assets reported in 2017 because the assets and associated decommissioning obligations disposed were classified as held for sale 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.

DERIVATIVE FINANCIAL INSTRUMENTS

The Company may enter into fixed price contracts and derivative financial instruments for 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.

For the nine months ending September 30, 2018, the Company did not enter into, or have any outstanding risk management contracts. The table below summarizes realized and unrealized gains (losses) on risk management contracts:

	Three months ended September 30			Nine months ended September 30		
(CA$ thousands, unless otherwise indicated)	**2018**	2017	%	**2018**	2017	%
Realized gain (loss)	**-**	41	-100	**-**	(330)	-100
Unrealized gain (loss)	**-**	(548)	-100	**-**	(127)	-100
Gain (loss) on derivative financial instruments	**-**	(507)	-100	**-**	(457)	-100
$ per BOE	**-**	(0.24)	-100	**-**	(0.08)	-100

Commodity price risk

Commodity price risk is the price uncertainty to the Company's financial performance upon fluctuations in the prices of commodities that are out of the control of the Company. Commodity prices are primarily driven by market forces that dictate the levels of supply and demand as well as the currency exchange rate relationship between the Canadian and U.S. dollar.

Subsequent to September 30, 2018 the Company entered into the following commodity risk management contracts:

Contract Type	Notional Volume	Reference Prices	Fixed Contract Price	Term
Financial Swap Natural Gas	10,000 MMBtu/d	NYMEX to Chicago Citygate Basis Differential	NYMEX Henry Hub less USD$0.14 per MMBtu	January 2019 to October 2019
Financial Swap Natural Gas	10,000 MMBtu/d	NYMEX to Union Dawn Basis Differential	NYMEX Henry Hub less USD$0.0975 per MMBtu	January 2019 to December 2019
Financial Swap Natural Gas	7,500 MMBtu/d	Sumas	USD$5.97 per MMBTU	November 2018 to March 2019

Interest rate risk

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 $118.1 million during the first nine months of 2018, an increase (decrease) in the market rate of interest by 25 basis points would have increased (decreased) annualized interest expense by $0.3 million.

Foreign exchange risk

Kelt is exposed to fluctuations of the Canadian to U.S. dollar exchange rate as benchmark oil and natural gas prices are denominated in U.S. dollars and the Company has both sales and transportation contracts in U.S. dollars.

Subsequent to September 30, 2018 the Company entered into the following foreign exchange risk management contract:

Contract Type	Notional Amount per month	Fixed Contract Price	Term
FX swap	US$1,000,000	CA$/US$ 1.3050	January 2019 to December 2019

PREMIUM ON FLOW-THROUGH SHARES

	Three months ended September 30			Nine months ended September 30		
(CA$ thousands, unless otherwise indicated)	**2018**	2017	%	**2018**	2017	%
Premium on flow-through shares	**1,376**	-	-	**4,141**	798	419

Management has utilized the Company's strong tax position to raise capital by issuing common shares on a "flow-through" basis which are typically issued at a premium to the market price of the Company's common shares. The premium received by the Company in excess of the fair value of its common shares at the time of the offering, is initially deferred and subsequently recognized in income as the premium is earned by incurring qualifying capital expenditures.

In April 2018, the Company completed non-brokered private placements of 2.7 million common shares for aggregate gross proceeds of $24.8 million, of which: 2.3 million common shares were issued on a "flow-through" basis in respect of Canadian Development Expenses at a price of $8.85 per share for gross proceeds of $20.8 million (the "2018 CDE Private Placement"); and 0.4 million common shares were issued on a "flow-through" basis in respect of Canadian Exploration Expenses at a price of $9.75 per share for gross proceeds of $4.0 million (the "2018 CEE Private Placement"). After estimated expenses related to the private placements, net proceeds to Kelt were approximately $24.0 million and resulted in a total premium $3.1 million relative to the fair value of Kelt's common shares at the respective dates of announcement of each tranche of the private placement. Pursuant to the provisions in the *Income Tax Act* (Canada), Kelt will incur eligible Canadian Development Expenses and Canadian Exploration Expenses prior to December 31, 2018. As at September 30, 2018, the Company fully satisfied all obligations related to 2018 CDE Private Placement and 2018 CEE Private Placement. The deferred premium of $3.1 million was recognized in income as expenditures during the nine months ending September 30, 2018, with $1.4 million being recognized in income during the third quarter of 2018.

In October 2017, the Company completed non-brokered private placements of 2.6 million flow-through common shares for aggregate gross proceeds of $20.6 million, of which: 2.0 million flow-through shares were issued in respect of Canadian development expenses at a price of $7.75 per share for gross proceeds of $15.6 million (the "2017 CDE Private Placement"); and 0.6 million flow-through shares were issued in respect of Canadian exploration expenses at a price of $8.75 per share for gross proceeds of $5.0 million (the "2017 CEE Private Placement"). After estimated expenses related to the private placements, net proceeds to Kelt were approximately $20.3 million and resulted in a total premium $2.6 million relative to the fair value of Kelt's common shares at the respective dates of announcement of each tranche of the private placement.

As at December 31, 2017, the Company fully satisfied all obligations related to 2017 CDE Private Placement and renounced the qualifying expenditures to the subscribers with an effective date of December 31, 2017. The deferred premium of $1.5 million ($0.75 per share) was recognized in income as expenditures were incurred during the fourth of 2017.

As at March 31, 2018, the Company fully satisfied all obligations related to 2017 CEE Private Placement and renounced the qualifying expenditures to the subscribers with an effective date of December 31, 2018. The deferred premium of $1.0 million ($1.82 per share) was recognized in income as expenditures were incurred during the first quarter of 2018.

INCOME TAXES

	Three months ended September 30			Nine months ended September 30		
(CA$ thousands, unless otherwise indicated)	**2018**	2017	%	**2018**	2017	%
Deferred income tax expense (recovery)	**4,295**	(4,122)	-204	**13,532**	(6,062)	-323
Profit (Loss) before taxes	**7,927**	(14,775)	-154	**18,843**	(23,851)	-179
Effective tax recovery rate	**54.2%**	27.9%	94	**71.8%**	25.4%	183

Kelt's consolidated combined federal and provincial statutory tax rate averaged 27.0% and 26.8% during the three months ended September 30, 2018 and 2017, respectively and averaged 27.0% and 26.7% during the nine months ended September 30, 2018 and 2017, respectively.

The increase in Kelt's effective tax rate in the third quarter of 2018 was primarily due to $5.4 million of qualifying expenditures incurred and renounced in respect of the Company's CDE flow-through share commitments, and $4.0 million of qualifying expenditures incurred and renounced in respect of the Company's CEE flow-through share commitments. For the nine months ended September 30, 2018 Kelt incurred $29.8 million of qualifying expenditures which have been renounced to subscribers of the flow-through private placements.

Kelt does not expect to pay income taxes in the current as the Company had sufficient income tax deductions available to shelter taxable income. The Company's consolidated tax pools are estimated to be approximately $1,025 million as of September 30, 2018 as summarized in the table below.

(CA$ thousands, unless otherwise indicated)	Rate	**September 30 2018**	December 31 2017	% change
Canadian oil and gas property expenses (COGPE)	10%	**138,179**	146,010	-5
Canadian development expenses (CDE)	30%	**224,206**	195,362	15
Canadian exploration expenses (CEE)	100%	**84,625**	102,708	-18
Undepreciated capital cost (1) (UCC)	25%	**234,025**	187,426	25
Share and debt issue costs	5 years	**5,063**	7,340	-31
Non-capital losses (2) (NCL)	100%	**339,031**	338,978	-
Estimated tax deductions available, end of period		**1,025,129**	977,824	5

(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 2038.

CASH PROVIDED BY OPERATING ACTIVITIES

The Company's cash provided by operating activities increased by 22% to $29.9 million in the third quarter of 2018 compared to $24.4 million in the comparable quarter of 2017. Year-to-date in 2018, cash provided by operating activities increased 56% to $122.7 million compared to $78.8 million in the same nine month period of 2017.

The following table reconciles cash provided by operating activities reported in accordance with GAAP to adjusted funds from operations, which is a non-GAAP financial measure used by Kelt as a key measures of performance:

	Three months ended September 30			Nine months ended September 30		
(CA$ thousands, unless otherwise indicated)	**2018**	2017	%	**2018**	2017	%
Cash provided by operating activities	**29,881**	24,394	22	**122,727**	78,764	56
Change in non-cash working capital	**16,871**	(1,638)	-1130	**16,085**	(4,679)	-444
Funds from operations	**46,752**	22,756	105	**138,812**	74,085	87
Settlement of decommissioning obligations	**124**	201	-38	**887**	1,028	-14
Adjusted funds from operations	**46,876**	22,957	104	**139,699**	75,113	86

For the three months ended September 30, 2018, and nine months ending September 30, 2018 cash provided by operating activities is lower than the Company's funds from operations due to a decrease in the non-cash working capital deficit. Specifically, the balance of accounts payable and accrued liabilities as at September 30, 2018 compared to the prior periods was reduced as the Company paid its suppliers for its on-going drilling program.

ADJUSTED FUNDS FROM OPERATIONS

Adjusted funds from operations and operating income or netbacks ($ per BOE) are non-GAAP measures 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. Management feels that adjusted funds from operations and operating income or netbacks provides useful information to the Company's stakeholders as it provides the ability to better analyze performance with information that is commonly used by other crude oil and natural gas producers. The following table provides a continuity of income and expenses included in the Company's calculation of operating income and adjusted funds from operations generated during the three and nine month periods ended September 30, 2018 and 2017.

THREE MONTHS ENDED SEPTEMBER 30TH	**2018**		2017		% change	
(CA$ thousands, unless otherwise indicated)	**Amount**	**$/BOE**	Amount	$/BOE	Amount	$/BOE
Petroleum and natural gas revenue	**100,219**	**41.57**	56,422	27.24	78	53
Cost of purchases	**(9,230)**	**(3.83)**	-	-	-	-
Realized loss on financial instruments (1)	**-**	**-**	41	0.02	-100	-100
Royalties	**(9,051)**	**(3.75)**	(5,107)	(2.46)	77	52
Revenue, after royalties and financial instruments	**81,938**	**33.99**	51,356	24.80	60	37
Production expense	**(22,443)**	**(9.31)**	(19,025)	(9.19)	18	1
Transportation expense	**(9,036)**	**(3.75)**	(5,691)	(2.75)	59	36
Operating income (2)	**50,459**	**20.93**	26,640	12.86	89	63
Financing expense (3)	**(2,508)**	**(1.04)**	(2,038)	(0.98)	23	6
G&A expense	**(2,107)**	**(0.87)**	(1,645)	(0.79)	28	10
Other income	**1,115**	**0.46**	-	-	-	-
Realized gain (loss) on foreign exchange	**(83)**	**(0.04)**	-	-	-	-
Adjusted funds from operations (4)	**46,876**	**19.44**	22,957	11.09	104	75
Basic ($ per common share) (5)	**0.25**		0.13		92	
Diluted ($ per common share) (5)	**0.25**		0.13		92	
Common shares outstanding (000s):						
Basic, weighted average	**183,919**		176,013		4	
Diluted, weighted average	**186,449**		177,206		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) "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.

(5) 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.

NINE MONTHS ENDED SEPTEMBER 30TH	2018		2017		% change	
(CA$ thousands, unless otherwise indicated)	**Amount**	**$/BOE**	Amount	$/BOE	Amount	$/BOE
Petroleum and natural gas revenue	**288,927**	**40.04**	176,719	30.62	63	31
Cost of purchases	**(18,846)**	**(2.61)**	-	-	-	-
Realized gain (loss) on financial instruments (1)	**-**	**-**	(340)	(0.06)	-100	-100
Royalties	**(25,159)**	**(3.49)**	(16,372)	(2.84)	54	23
Revenue, after royalties and financial instruments	**244,922**	**33.94**	160,007	27.72	53	22
Production expense	**(67,118)**	**(9.30)**	(55,816)	(9.67)	20	-4
Transportation expense	**(26,383)**	**(3.66)**	(18,129)	(3.14)	46	17
Operating income (2)	**151,421**	**20.98**	86,062	14.91	76	41
Financing expense (3)	**(7,150)**	**(0.99)**	(5,663)	(0.98)	26	1
G&A expense	**(5,916)**	**(0.82)**	(5,296)	(0.91)	12	-11
Other income	**1,115**	**0.15**	-	-	-	-
Realized gain (loss) on foreign exchange	**229**	**0.04**	-	-	-	-
Realized gain (loss) on financial instruments (4)	**-**	**-**	10	-	-100	-
Adjusted funds from operations (5)	**139,699**	**19.36**	75,113	13.01	86	49
Basic ($ per common share) (6)	**0.77**		0.43		79	
Diluted ($ per common share) (6)	**0.76**		0.42		81	
Common shares outstanding (000s):						
Basic, weighted average	**182,262**		175,875		4	
Diluted, weighted average	**184,319**		177,204		4	

(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.

During the three months ended September 30, 2018, adjusted funds from operations of $46.9 million ($0.25 per share, diluted) increased by 104% from $23.0 million ($0.13 per share, diluted) during the third quarter ended September 30, 2017. The increase in adjusted funds from operations is primarily attributed to the increase in Kelt’s revenues (after royalties and financial instruments) which are up 60% to $81.9 million compared to $51.4 million in the third quarter of 2017. The increase is driven primarily by a 16% increase in average production, and a 50% increase in the benchmark WTI (CA$/bbl) oil price.

During the nine months ended September 30, 2018, adjusted funds from operations of $139.7 million ($0.76 per share, diluted) increased by 86% from $75.1 million ($0.42 per share, diluted) during the nine months ended September 30, 2017. The increase in adjusted funds from operations is primarily attributed to the increase in Kelt’s revenues (after royalties and financial instruments) which are up 53% to $244.9 million compared to $160.0 million in the nine months ending September 30, 2017. The increase is driven primarily by a 25% increase in average production, and a 33% increase in the benchmark WTI (CA$/bbl) oil price which mitigated the impact of lower gas prices in the third quarter of 2018. On a BOE basis, adjusted funds from operations per BOE increased 49% from the nine months ended September 30, 2017.

PROFIT (LOSS) AND COMPREHENSIVE INCOME (LOSS)

	Three months ended September 30			Nine months ended September 30		
(CA$ thousands, unless otherwise indicated)	**2018**	2017	%	**2018**	2017	%
Profit (loss) and comprehensive income (loss)	**3,632**	(10,653)	-134	**5,311**	(17,789)	-130
Wtd avg. shares outstanding, basic (000s)	**183,919**	176,013	4	**182,262**	175,875	4
Wtd avg. shares outstanding, diluted (000s) (1)(2)	**186,449**	176,013	6	**184,319**	175,875	5
$ per common share, basic	**0.02**	(0.06)	-133	**0.03**	(0.10)	-130
$ per common share, diluted (1)(2)	**0.02**	(0.06)	-133	**0.03**	(0.10)	-130
$ per BOE	**1.51**	(5.14)	-133	**0.74**	(3.08)	-130

(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 third quarter ended September 30, 2017 the Company excluded the effect of stock options and RSUs as they were anti-dilutive. In computing the diluted loss per common share for the third quarter ended September 30, 2018 the dilutive impact of the effect of stock options and RSUs did not result in a change in the $ per common share.

(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 to the loss reported for all periods outstanding.

Kelt reported a profit of $3.6 million for the three months ended September 30, 2018, compared to a loss of $10.7 million ($0.06 per common share, diluted) in the same three month period of 2017. The decrease in the loss is primarily due to an increase of $23.9 million in adjusted funds from operations, partially offset by an increase in depletion expense of $2.0 million and an increase in the deferred income tax expense of $8.4 million.

Kelt reported a profit of $5.3 million for the nine months ended September 30, 2018, compared to a loss of $17.8 million ($0.10 per common share, diluted) in the same period of 2017. The decrease in the loss is primarily due to an increase of $64.3 million in adjusted funds from operations, partially offset by an increase in depletion expense of $20.5 million and an increase in the deferred income tax expense of $19.6 million.

INVESTING ACTIVITIES

CAPITAL EXPENDITURES

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

	Three months ended September 30			Nine months ended September 30		
(CA$ thousands, unless otherwise indicated)	**2018**	2017	%	**2018**	2017	%
Capital expenditures:						
Lease acquisition and retention	**572**	3,994	-86	**4,143**	7,396	-44
Geological and geophysical	**242**	1,641	-85	**299**	1,921	-84
Drilling and completion of wells	**29,603**	45,686	-35	**123,916**	114,778	8
Facilities, pipeline and well equipment	**39,066**	24,530	59	**86,092**	53,607	61
Corporate assets	**623**	37	1584	**752**	769	-2
Capital expenditures, before A&D	**70,106**	75,888	-8	**215,202**	178,471	21
Property acquisitions	**922**	67	1276	**2,849**	67	4152
Property dispositions	**(2,601)**	(22)	11723	**(2,885)**	(106,339)	-97
Total capital expenditures, net of dispositions	**68,427**	75,933	-10	**215,166**	72,199	198

Drilling and completion expenditures incurred during the three month period ended September 30, 2018, and during the nine months ending September 30, 2018 were focused on Montney wells in the Company's core Alberta and BC areas. Kelt drilled nine net wells during the quarter, four at Fireweed/Inga in BC, four at Pouce Coupe in Alberta and one at La Glace in Alberta. In the fourth quarter of 2018, Kelt anticipates it will bring on production its five-well pad drilled at Pouce Coupe, its one well drilled La Glace and two wells drilled at Fireweed/Inga.

In 2017 the Company purchased a major infrastructure package for $12.5 million. The infrastructure package includes a total of 100 mmcf per day of natural gas compression and dehydration and related facilities. In addition to re-building the original facility, the Company is constructing large diameter gas and emulsion pipelines as well as a large diameter water line which will enable Kelt to reuse frac water as well as access additional water from two large water ponds being constructed at the Kelt Inga Facility. This infrastructure will allow Kelt to continue with its multi-well pad development at Inga, in a cost effective manner that is expected to lower future production expenses, and is expected to be completed in the fourth quarter of 2018. During the third quarter of 2018 and the nine months ending September 30, 2018 Kelt incurred $16.4 million and $34.7 million of costs, respectively, related to the re-building and construction of this facility.

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”) for proceeds of $103.1 million after closing adjustments.

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 September 30, 2018, 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 debt to trailing adjusted funds from operations ratio, which is a non-GAAP financial measure. Kelt targets a net debt to trailing adjusted funds from operations ratio of less than 2.0 times.

The capital intensive nature of Kelt’s operations may result in increases to bank debt or working capital deficiency during periods with high levels of capital investment. For the nine months ended 2018 the Company’s capital expenditures of $215.2 million were in excess of the Company’s funds from operations of $139.4 million and net proceeds from the flow-through private placement of $24.1 million. As a result, Kelt’s net debt increased to $176.0 million at September 30, 2018 from $136.7 million at December 31, 2017. However, the company’s funds from operations improved with increased production and higher commodity prices resulting in a decrease in net debt to trailing adjusted funds from operations ratio to 0.9 times as at September 30, 2018 from 1.0 times as at December 31, 2017.

	September 30, 2018	December 31, 2017
Bank debt	**135,054**	91,465
Working capital deficiency	**40,992**	45,264
Net debt (1)	**176,046**	136,729
Trailing annualized adjusted funds from operations (2)(3)	**187,506**	131,592
Net debt to trailing adjusted funds from operations ratio (1)	**0.9**	1.0

(1) “Net 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 maintains sufficient unused bank credit lines to satisfy such working capital deficiencies. As at September 30, 2018, the Company’s working capital deficit of $41.0 million combined with outstanding bank debt of $135.1 million, represented 70% of the authorized borrowing amount available under the credit facility of $250.0 million.

Future capital expenditures are expected to be funded through a combination of cash flow from operations and bank debt, and may be supplemented by new equity or debt offerings.

CREDIT FACILITY

The Company has a revolving committed term credit facility ("the Credit Facility") with a syndicate of financial institutions. On April 18, 2018 the facility was amended and the revolving period was extended to April 28, 2019 with a 364 day term-out period if not renewed. The authorized borrowing amount available under the Credit Facility was increased to $215 million from $185 million which includes an accordion feature giving the Company the right, with the consent of the lenders, to increase the commitments under the facility to $250 million with the existing lending syndicate or by adding additional lenders. The pricing grid range was amended to bank prime plus 0.5% to bank prime plus 2.5% (from 1.0% to 2.5% previously), and the stamping fee range was changed to 1.5% to 3.5% (from 2.0% to 3.5% previously) depending upon the Company's then current debt to cash flow ratio of between less than one half times to greater than three times.

Subsequent to the quarter ended September 30, 2018, the Company and its lenders completed the semi-annual bank compliance review and amended the Credit Facility to increase the lenders commitments to $250.0 million.

There are no financial covenants under the Credit Facility and Kelt is in compliance with all other covenants. The Credit Facility is subject to semi-annual borrowing base reviews, occurring approximately in April and October of each year.

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. 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 trade on the TSX under the symbol "KEL.DB". As at September 30, 2018, the Debentures are "in-the-money" based on the closing price of Kelt common shares on the TSX of $8.41, on the last trading day in the quarter. As at September 30, 2018, the fair value of the Debentures was $145.8 million based on the closing market price of $162.0 per Debenture, being the price at which the Debentures last traded in the third quarter. The fair value was $135.0 million at December 31, 2017. To date, $0.09 million of the face value has been converted to $0.02 million shares. As at September 30, 2018, $89.9 million of the 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, 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 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 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.

The Company may 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.

SHARE INFORMATION

The Company is authorized to issue an unlimited number of common shares and an unlimited number of preferred shares. As at September 30, 2018 there were 184.0 million common shares issued and outstanding. There are no preferred shares issued or outstanding.

The Company's common shares trade on the TSX under the symbol "KEL". During the third quarter of 2018, 47.2 million common shares traded on the TSX at a weighted average price of $8.86 per common share.

As at September 30, 2018, officers, directors, and employees have been granted options to purchase 7.9 million common shares of the Company at an average exercise price of $6.67 per common share. In addition, there are 1.1 million RSUs outstanding. Options and RSUs outstanding at September 30, 2018 represented 5% of total common shares issued and outstanding. Additional information regarding the Company's stock options and RSUs is included in note 10 of the interim financial statements.

COMMITMENTS AND CONTRACTUAL OBLIGATIONS

As of September 30, 2018, the Company is committed to future payments under the following agreements:

(CA$ thousands)	2018	2019	2020	2021	2022	Thereafter
Operating lease - office buildings	44	967	1,035	1,056	1,077	376
Operating lease - vehicles	99	322	173	41	-	-
Firm processing commitments	2,394	7,860	1,566	1,605	1,365	-
Firm transportation commitments (1)	8,235	33,677	27,163	23,009	22,508	180,533
Total annual commitments	10,772	42,826	29,937	25,711	24,950	180,909

(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 contract, which is effective until October 31, 2020, respectively. Amounts are translated to Canadian dollars at the spot rate on September 30, 2018 of CA$/US$1.2945.

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, 2023, February 28, 2020, and July 31, 2023, respectively, if not extended.

In July 2018, the Company entered into a letter of intent for firm processing of 75 mmcf per day of raw gas under a 10 year proposed take or pay arrangement. In August 2018, a firm take or pay processing agreement was entered into allowing Kelt an option to increase the firm processing up to an additional 95 mmcf/d and the option to extend the term up to 20 years. The take or pay arrangement is conditional upon the commissioning and construction of a processing facility which is currently expected to be on-stream in the fourth quarter of 2019. As the commissioning and construction of the facility has not yet been finalized, it has not been included in the commitment table above.

Kelt has also entered into a proposed firm processing agreement for 30 mmcf per day of raw gas under a five year proposed take or pay arrangement. This agreement is subject to obtaining regulatory approvals and the construction of a processing facility which is not expected to be fully on-stream the second half of 2019. Subsequent to September 30, 2018, the operator of the processing facility obtained approvals from the Alberta Energy regulator for the construction and operation of the facility. As the commissioning and construction of the facility has not yet been finalized, it has not been included in the commitment table above.

During the third quarter of 2018 firm transportation commitments increased by $165 million over the entire commitment term from the second quarter of 2018. The increase in commitments is primarily due to take or pay commitments on the North Montney Mainline which is expected to be in-service in the second half of 2019.

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 nine months ended September 30, 2018, the Company incurred $0.4 million (2017 – $0.2 million) in legal fees and disbursements. 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 September 30, 2018 and 2017.

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)	**Q3 2018**	Q2 2018	Q1 2018	Q4 2017
Petroleum and natural gas revenue, before royalties	100,219	98,715	89,993	80,838
Cash provided by operating activities	29,881	39,183	53,663	36,458
Adjusted funds from operations (1)	46,876	47,099	45,724	32,898
Per share – basic ($/common share) (1)	0.25	0.26	0.25	0.18
Per share – diluted ($/common share) (1)	0.25	0.25	0.25	0.18
Profit (loss) and comprehensive income (loss)	3,246	1,702	(23)	(5,389)
Per share – basic ($/common share)	0.02	0.01	-	(0.03)
Per share – diluted ($/common share)	0.02	0.01	-	(0.03)
Total capital expenditures, net of dispositions	68,427	54,702	92,037	55,778
Total assets	1,378,114	1,346,701	1,337,688	1,276,567
Net debt (1)	176,046	157,058	173,587	136,729
Convertible debentures	77,350	76,348	75,443	74,517
Shareholders' equity	889,275	882,916	857,019	845,701
Average daily production (BOE/d)	26,204	26,120	26,978	25,063
Average realized price ($/BOE) (1)(2)	37.74	38.51	36.07	33.42
Operating netback ($/BOE) (1)	20.93	21.57	20.47	16.18
Operating netback % of average realized price (2)	55%	56%	57%	48%

	Q3 2017	Q2 2017	Q1 2017	Q4 2016
Petroleum and natural gas revenue, before royalties	56,422	60,072	60,225	55,737
Cash provided (used in) by operating activities	24,394	28,480	25,890	21,919
Adjusted funds from operations (1)	22,957	25,333	26,823	23,100
Per share – basic ($/common share) (1)	0.13	0.14	0.15	0.13
Per share – diluted ($/common share) (1)	0.13	0.14	0.15	0.13
Profit (loss) and comprehensive income (loss)	(10,653)	(4,869)	(2,267)	11,856
Per share – basic ($/common share)	(0.06)	(0.03)	(0.01)	0.07
Per share – diluted ($/common share)	(0.06)	(0.03)	(0.01)	0.07
Total capital expenditures, net of dispositions	75,933	31,630	(35,364)	36,339
Total assets	1,227,962	1,203,174	1,193,644	1,255,958
Net debt (1)	134,759	80,618	75,765	138,042
Convertible debentures	73,584	72,685	71,810	70,978
Shareholders' equity	830,344	839,485	842,351	843,301
Average daily production (BOE/d)	22,510	20,684	20,204	19,762
Average realized price ($/BOE) (1)(2)	27.26	31.70	33.13	30.53
Operating netback ($/BOE) (1)	12.86	15.49	16.63	15.08
Operating netback as a % of average realized price (2)	47%	49%	50%	49%

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

(2) In this table, average realized prices are after financial instruments.

In the five years since commencing active operations in 2013, Kelt has grown production from approximately 3,500 BOE per day to over 26,000 BOE per day. Production has increased significantly in 2017 and 2018 as the Company executed on an active and successful Montney drilling program.

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. The positive momentum for global crude oil prices commenced in November 2016 when OPEC and certain non-OPEC countries agreed to cut oil production, which led to a slow balancing of global oil demand and supply. In addition to a balancing of global oil supply and demand, heighted geopolitical risks, combined with a risk of future oil demand growth outpacing supply growth have resulted in oil prices in WTI reaching its highest level in the past twelve consecutive quarters, averaging US$69.46 per barrel.

The recovery of oil prices and the increase in the Company's average oil production weighting, taken together with higher average production, drove the significant increase in revenues, cash provided by operating activities, and operating netbacks during the third quarter of 2018.

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, net of the cost of purchases and 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 table included under the heading of *"Cash Provided by Operating Activities"* in this MD&A reconciles cash provided by operating activities to adjusted funds from operations and the table included under the heading of "*Adjusted Funds From Operations*" in this MD&A demonstrates the calculation of operating income derived from the individual financial statement line items in accordance with GAAP.

Throughout this MD&A, reference is made to "total revenue", "Kelt Revenue" and "average realized prices". "Total revenue" refers to petroleum and natural gas revenue (before royalties) as reported in the consolidated financial statements in accordance with GAAP, and is before realized gains or losses on financial instruments. "Kelt Revenue" is a non-GAAP measure and is calculated by deducting the cost of purchases from petroleum and natural gas revenue (before royalties). "Average realized prices" are calculated based on "Kelt Revenue" divided by production and reflect the Company's realized selling prices plus the net benefit of oil blending/marketing activities, which commenced during the fourth quarter of 2017. In addition to using its own production, the Company may purchase butane and crude oil from third parties for use in its blending operations, with the objective of selling the blended oil product at a premium. Marketing revenue from the sale of third party volumes is included in total petroleum and natural gas revenue as reported in the Consolidated Statement of Profit (Loss) and Comprehensive Income (Loss) in accordance with GAAP. Given the Company's per unit operating statistics disclosed throughout this MD&A are calculated based on Kelt's production volumes, management believes that disclosing its average realized prices based on Kelt Revenue is more appropriate and useful, because the cost of third party volumes purchased to generate the incremental marketing revenue has been deducted.

"Average realized prices" referenced throughout this MD&A are before financial instruments, except as otherwise indicated as being after financial instruments.

The term "net debt" is used synonymously with, and is equal to, "bank debt, net of working capital". "Net 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 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 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

Revenue

Kelt adopted IFRS 15 *Revenue* from contracts with customers with a date of initial application of January 1, 2018. IFRS 15 will replace IAS 18 *Revenue*, IAS 11 *Construction Contracts*, and other related interpretations. Kelt used the modified retrospective approach to adopt the new standard, electing to use a practical expedient to apply the standard retrospectively only to contracts that were not completed contracts on January 1, 2017. There was no change or adjustment to the Company's consolidated Financial Statements as a result of the adoption of IFRS 15. However IFRS 15 contains additional disclosure requirements which are detailed in note 12 of the interim financial statements.

Kelt recognizes revenue at a point in time when control of the product has been transferred to the customer and performance obligations have been satisfied. This is generally met when the customer obtains legal title to the product and physical delivery at a delivery point has taken place. Revenue is measured based on the consideration specified in the contracts the Company has with its customers.

Kelt evaluates its arrangements with 3rd parties and partners to determine if a principal or agent relationship exists. In making this evaluation, management considers if it maintains control of the product, which is indicated by the

Company having the primary responsibility for the delivery of the product, having the ability to establish prices or having inventory risk. If an agency relationship exists, then the revenue is recognized on a net-basis, only reflecting the fee, if any, realized by the party from the transaction.

Royalty income is recognized as it accrues in accordance with the terms of the overriding royalty agreements.

Investments in Securities

Investments in securities are classified as fair value through profit or loss. Investments in the securities of private entities are carried at fair value, which is estimated using values based on equity issuances and other indications of value from time-to-time (level three fair value hierarchy estimates).

ACCOUNTING STANDARDS ISSUED BUT NOT YET EFFECTIVE

IFRS 16 *Leases,* is intended to replace IAS 17 and will bring fundamental changes for all companies, including Kelt, who lease assets. The new standard is effective for annual reporting periods beginning on or after January 1, 2019, with early application permitted. The most significant financial reporting impacts of the changes include: all leases will be on the balance sheet of lessees, except those that meet the limited exception criteria; the measurement and presentation of expenses will be impacted and replaced by the recording of depreciation and financing expenses; the amount of profit (loss) recognized in a period will likely change as the timing of expenses is accelerated when applying the new standard which uses a finance lease model compared to a straight line operating lease expense; and key ratios may be impacted with the introduction of lease assets and liabilities on the balance sheet and changes to the timing of expenses. Management is currently in the implementation phase of IFRS 16, with the impact on the Company's consolidated financial statements still being assessed; however the additional leases being brought on the balance sheet will likely be material.

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, 2017 annual financial statements. There have been no significant changes in the Company's judgments and estimates applied during the interim period ended September 30, 2018 relative to those described in the most recent annual financial statements as at and for the year ended December 31, 2017.

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 July

1, 2018 to September 30, 2018 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.

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. A 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, 2017, dated March 6, 2018. Additional information is included in Kelt's Annual Information Form dated March 7, 2018 which can be found at www.sedar.com

BUSINESS OUTLOOK

CURRENT ECONOMIC ENVIRONMENT

The current economic environment in the energy industry remains volatile despite WTI reaching a three year high in the third quarter of 2018. Bottlenecks in the Canadian crude oil pipeline network have resulted in oversupply in the Canadian market and a significant widening of the Canadian light and heavy crude differentials as compared to US benchmark prices. There are a number of factors that are expected to narrow price discounts over time including an increase in crude delivered by rail, the restarting of Midwest refineries currently offline for seasonal maintenance and new pipeline capacity.

Natural gas infrastructure and capacity constraints have continued to impact realized natural gas prices in domestic western Canadian markets relative to other North American markets. Kelt has taken measures to diversify its gas sales markets in order to mitigate the effect of low prices in Alberta and British Columbia. U.S. natural gas storage continues to be well below the five-year average however, the price impact has been muted due to the significant natural gas supply growth in 2018.

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 rapidly. Kelt continues to be optimistic about the long-term outlook for oil and gas commodity prices.

OUTLOOK AND GUIDANCE

2018 OUTLOOK

As of the date of this MD&A, management has updated its guidance from August 9, 2018 to incorporate revised commodity price assumptions and third quarter results.

The Company has updated its forecasted 2018 commodity prices and currency assumptions. The Company's assumption for WTI US$/bbl remains the same; however, Canadian oil differentials have widened significantly and fourth quarter Canadian light sweet differentials are forecasted to be $30/bbl. As a result, forecasted annual average Canadian Light Sweet prices have decreased by 11 percent to $70.94/bbl. NYMEX natural gas prices have increased by 2% while AECO natural gas prices declined by 8%. Based the revised production forecast and commodity price assumptions, 2018 funds from operations is expected to be $193 million or $1.04 per common share, diluted compared to previous guidance of $210 million or $1.14 per common share, diluted.

The 2018 capital expenditure budget has increased by 4% to $287 million. The Company expects that recently enacted tariffs and import quotas will result in higher steel prices and the 2018 budget includes an additional $12 million for pipeline acquired in advance for 2019 capital projects. The Company's drilling program will continue to be directed primarily towards Montney development and related facilities, pipelines and infrastructure. Forecasted drilling and completion capital has been revised upwards by 5% as 4.6 net wells have been added to the 2018 drilling program.

2018 average production is now expected to average between 27,000 BOE/d and 28,000 BOE/d after taking into account planned completion activities and onstream dates for new wells. At the end of 2018 the Company expects to have 16 horizontal wells drilled that it expects add to production in 2019 providing momentum for future growth.

(CA$ millions, except as otherwise indicated)	**Revised 2018 Budget**	**2018 Budget (August 2018)**	**% Change**
Average Production			
Oil and NGLs (bbls/d)	**11,500 – 12,400**	**12,500 – 13,300**	**-7% to -8%**
Gas (mmcf/d)	**90.0 – 97.0**	**92.0 – 95.0**	**-2% to +2%**
Combined (BOE/d)	**27,000 - 28,000**	**28,000 - 29,000**	**-3% to -4%**
Production per million common shares (BOE/d)	**148 – 153**	**153 – 159**	**-3% to -4%**
Forecasted Average Commodity Prices			
WTI oil price (US$/bbl)	**67.50**	**67.50**	**-**
Canadian Light Sweet ($/bbl)	**70.94**	**79.59**	**-11%**
NYMEX natural gas price (US$/MMBTU)	**2.95**	**2.90**	**2%**
AECO natural gas price ($/GJ)	**1.57**	**1.71**	**-8%**
Average Exchange Rate (US$/CA$)	**0.774**	**0.776**	**-**
Capital Expenditures			
Drilling & completions	**178.5**	**170.0**	**5%**
Facilities, pipeline & well equipment	**110.0**	**95.0**	**16%**
Land, seismic & property acquisitions	**10.0**	**12.5**	**-20%**
Property dispositions	**(11.5)**	**(2.5)**	**360%**
Net Capital Expenditures	**287.0**	**275.0**	**4%**
Funds from operations	**193.0**	**210.0**	**-8%**
Per common share, diluted	**1.04**	**1.14**	**-9%**
Bank debt, net of working capital, at year-end (1)	**195.0**	**168.0**	**16%**
Net bank debt to trailing annual funds from operations ratio	**1.0 x**	**0.8 x**	**25%**
Weighted average common shares outstanding (millions)	**182.7**	**182.6**	**-**
Common shares issued and outstanding (millions)	**184.0**	**183.8**	**-**

2019 GUIDANCE

The Company's Board of Directors has approved a 2019 capital expenditure budget of $270 million. Kelt expects to drill 34.0 gross (33.0 net) wells and complete 36.0 gross (35.0 net) wells. All of the Company's 2019 drilling is expected to target the Montney with 20.0 net wells planned at Inga/Fireweed, 7.0 net wells at Wembley, 4.0 net wells at Oak and 1 net well at each of Stoddart and Progress. Kelt expects to have 8 net wells drilled but un-completed and not on production at the end of 2019. Facility expenditures are expected to decrease by 45% in 2019 to $60.0 million as there is no major facility expenditures planned for 2019.

Forecasted average production for 2019 is estimated to be between 33,500 BOE/d to 34,500 BOE/d, representing an increase of 23% - 24% from 2018. It is estimated that production will be weighted approximately 47% to oil and NGLs and 53% to natural gas.

WTI crude oil prices are forecasted to average US$67.50 in 2019. Canadian oil differentials are expected to remain wide in 2019 and the Company has forecasted a discount of $30/bbl in the first quarter of 2019 and gradually improving to average $19.43/bbl for the year. As a result, Canadian Light Sweet is forecasted to average $66.97/bbl. Natural gas prices are forecast to average $1.94 CAD/GJ for AECO and $3.00 USD/mmbtu for NYMEX. After taking in account its marketing arrangements, Kelt expects to realize a natural gas price of $3.28/mcf in 2019 which is a premium to AECO of 60%.

The Company is forecasting 2019 funds from operations of $240.0 million of $1.23 per common share, diluted, an increase of 24% and 18%, respectively. Bank debt net of working capital is estimated to be $225 million at December 31, 2019 representing a Net Bank Debt to Funds Flow from Operations ratio of 0.9X. The Company has assumed that the outstanding convertible debentures of $89.9 million will be converted in June 2019, resulting in an increase of 16.3 million common shares.

The table below outlines the Company's forecast assumptions and financial and operating results for 2019 with a comparison to 2018:

(CA$ millions, except as otherwise indicated)	**2019 Budget**	**Revised 2018 Budget**	**% Change**
Average Production			
Oil and NGLs (bbls/d)	**15,500 – 16,400**	**11,500 – 12,400**	**32% - 35%**
Gas (mmcf/d)	**105.0 – 112.0**	**90.0 – 97.0**	**15% - 17%**
Combined (BOE/d)	**33,500 – 34,500**	**27,000 - 28,000**	**23% - 24%**
Production per million common shares (BOE/d)	**172 - 177**	**148 – 153**	**16%**
Forecasted Average Commodity Prices			
WTI oil price (US$/bbl)	**67.50**	**67.50**	**-**
Canadian Light Sweet ($/bbl)	**66.97**	**70.94**	**-6%**
NYMEX natural gas price (US$/MMBTU)	**3.00**	**2.95**	**2%**
AECO natural gas price ($/GJ)	**1.94**	**1.57**	**24%**
Average Exchange Rate (US$/CA$)	**0.781**	**0.774**	**1%**
Capital Expenditures			
Drilling & completions	**201.0**	**178.5**	**13%**
Facilities, pipeline & well equipment	**60.0**	**110.0**	**-45%**
Land, seismic & property acquisitions	**9.0**	**10.0**	**-10%**
Property dispositions	**-**	**(11.5)**	**-100%**
Net Capital Expenditures	**270.0**	**287.0**	**-6%**

(CA$ millions, except as otherwise indicated)	**2019 Budget**	**Revised 2018 Budget**	**% Change**
Funds from operations	**240.0**	**193.0**	**24%**
Per common share, diluted	**1.23**	**1.04**	**18%**
Bank debt, net of working capital, at year-end (1)	**225.0**	**195.0**	**15%**
Net bank debt to trailing annual funds from operations ratio	**0.9 x**	**1.0 x**	**-10%**
Weighted average common shares outstanding (millions)	**194.9**	**182.7**	**7**
Common shares issued and outstanding (millions) (1)	**200.5**	**184.0**	**9**
2019 Funds Flow from Operations Sensitivities:			
Oil/NGLs price minus 10%	**(28.5)**		
Natural gas price minus 10%	**(13.8)**		
CAD/USD minus $0.05	**(15.6)**		

(1) The Company has assumed that the outstanding convertible debentures of $89.9 million will be converted in June 2019, resulting in the issuance of 16.3 million common shares.

ADVISORY REGARDING FORWARD-LOOKING STATEMENTS

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 the calendar year 2018. Readers are cautioned that this financial outlook may not be appropriate for other purposes.

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. 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.

ADDITIONAL INFORMATION

Additional information relating to Kelt, including the Company's Annual Information Form ("AIF") dated March 7, 2018 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.

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

(CA$ thousands)	[Notes]	**September 30, 2018**	December 31, 2017
ASSETS			
Current assets			
Cash and cash equivalents		**1,088**	3,695
Accounts receivable and accrued revenue	[11]	**39,193**	39,446
Prepaid expenses and deposits		**3,289**	2,005
Total current assets		**43,570**	45,146
Investment in securities	[11]	**1,000**	-
Exploration and evaluation assets	[5]	**128,273**	123,349
Property, plant and equipment	[6]	**1,205,271**	1,108,072
Total assets		**1,378,114**	1,276,567
LIABILITIES			
Current liabilities			
Accounts payable and accrued liabilities		**83,248**	87,783
Deferred premium on flow-through shares	[10]	**-**	1,042
Decommissioning obligations	[9]	**1,314**	1,585
Total current liabilities		**84,562**	90,410
Bank debt	[7]	**135,054**	91,465
Convertible debentures	[8]	**77,350**	74,517
Decommissioning obligations	[9]	**139,407**	135,343
Deferred income tax liability		**52,466**	39,131
Total liabilities		**488,839**	430,866
SHAREHOLDERS' EQUITY			
Shareholders' capital	[10]	**1,119,162**	1,078,773
Reserve from common control transaction		**(57,668)**	(57,668)
Equity component of convertible debentures	[8]	**12,843**	12,856
Contributed surplus		**18,105**	20,218
Retained earnings (deficit)		**(203,167)**	(208,478)
Total shareholders' equity		**889,275**	845,701
Total liabilities and shareholders' equity		**1,378,114**	1,276,567
Commitments	[14]		

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 September 30		Nine months ended September 30	
(CA$ thousands, except per share amounts)	[Notes]	**2018**	2017	**2018**	2017
Revenue					
Petroleum and natural gas revenue	[12]	**100,219**	56,422	**288,927**	176,719
Royalties		**(9,051)**	(5,107)	**(25,159)**	(16,372)
		91,168	51,315	**263,768**	160,347
Expenses					
Production		**22,443**	19,025	**67,118**	55,816
Transportation		**9,036**	5,691	**26,383**	18,129
Cost of purchases		**9,230**	-	**18,846**	-
Financing	[13]	**4,302**	3,680	**12,406**	10,476
General and administrative		**2,107**	1,645	**5,916**	5,296
Share based compensation	[10]	**1,416**	1,324	**4,364**	3,873
Exploration and evaluation	[5]	**1,398**	460	**3,495**	987
Depletion, depreciation and impairment	[6]	**35,754**	33,781	**112,078**	91,548
		85,686	65,606	**250,606**	186,125
(Loss) on derivative financial instruments	[11]	**-**	(507)	**-**	(457)
Foreign exchange gain (loss)		**(84)**	-	**228**	-
Premium on flow-through shares	[10]	**1,376**	-	**4,141**	798
Gain on sale of assets	[4]	**38**	23	**197**	1,586
Other income		**1,115**	-	**1,115**	-
Profit (loss) before taxes		**7,927**	(14,775)	**18,843**	(23,851)
Deferred income tax recovery (expense)		**(4,295)**	4,122	**(13,532)**	6,062
Profit (loss) and comprehensive income (loss)		**3,632**	(10,653)	**5,311**	(17,789)
Profit (loss) per common share					
Basic	[10]	**0.02**	(0.06)	**0.03**	(0.10)
Diluted	[10]	**0.02**	(0.06)	**0.03**	(0.10)

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]

		Shareholders' capital						
(CA$ thousands)	[Notes]	Number of Shares (000s)	Amount ($ thousands)	Reserve	Convertible debentures – equity portion	Contributed surplus	Retained earnings (deficit)	Total shareholders' equity
Balance at December 31, 2017		178,858	1,078,773	(57,668)	12,856	20,218	(208,478)	845,701
Profit and comprehensive income		-	-	-	-	-	5,311	5,311
Common shares issued, net of costs:								
Private placements	[10]	2,758	24,776	-	-	-	-	24,776
Premium on flow-through shares	[10]	-	(3,099)	-	-	-	-	(3,099)
Share issue costs, net of tax	[10]	-	(541)	-	-	-	-	(541)
Conversion of convertible debentures	[8]	16	89		(13)			76
Exercise of stock options	[10]	2,081	17,694	-	-	(5,007)	-	12,687
Vesting of restricted share units	[10]	268	1,470	-	-	(1,470)	-	-
Share based compensation	[10]	-	-	-	-	4,364	-	4,364
Balance at September 30, 2018		**183,981**	**1,119,162**	**(57,668)**	**12,843**	**18,105**	**(203,167)**	**889,275**

Balance at December 31, 2016		175,672	1,055,959	(57,668)	12,856	17,454	(185,300)	843,301
Loss and comprehensive loss		-	-	-	-	-	(17,789)	(17,789)
Exercise of stock options	[10]	195	1,272	-	-	(313)	-	959
Vesting of restricted share units	[10]	181	1,712	-	-	(1,712)	-	-
Share based compensation	[10]	-	-	-	-	3,873	-	3,873
Balance at September 30, 2017		176,048	1,058,943	(57,668)	12,856	19,302	(203,089)	830,344

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

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

(CA$ thousands)	[Notes]	Three months ended September 30 **2018**	Three months ended September 30 2017	Nine months ended September 30 **2018**	Nine months ended September 30 2017
Operating activities					
Profit (loss) and comprehensive income (loss)		**3,632**	(10,653)	**5,311**	(17,789)
Items not affecting cash:					
Accretion of convertible debentures	[8,13]	**1,002**	899	**2,909**	2,606
Accretion of decommissioning obligations	[9,13]	**792**	743	**2,347**	2,207
Share based compensation		**1,416**	1,324	**4,364**	3,873
Exploration and evaluation		**1,398**	460	**3,495**	987
Depletion, depreciation and impairment		**35,754**	33,781	**112,078**	91,548
Unrealized gain on derivative financial instruments	[11]	**-**	548	**-**	127
Unrealized gain on foreign exchange		**1**	-	**1**	-
Premium on flow-through shares		**(1,376)**	-	**(4,141)**	(798)
Gain on sale of assets		**(38)**	(23)	**(197)**	(1,586)
Deferred income tax expense (recovery)		**4,295**	(4,122)	**13,532**	(6,062)
Settlement of decommissioning obligations	[9]	**(124)**	(201)	**(887)**	(1,028)
Change in non-cash operating working capital	[15]	**(16,871)**	1,638	**(16,085)**	4,679
Cash provided by operating activities		**29,881**	24,394	**122,727**	78,764
Financing activities					
Increase (decrease) in bank debt		**28,061**	28,398	**43,589**	(18,720)
Issue of common shares, net of costs	[10]	**-**	-	**24,038**	-
Proceeds on exercise of stock options	[10]	**1,312**	188	**12,687**	959
Cash (used in) provided by financing activities		**29,373**	28,586	**80,314**	(17,761)
Investing activities					
Exploration and evaluation assets		**(3,113)**	(12,996)	**(43,215)**	(39,243)
Property, plant and equipment		**(66,993)**	(62,892)	**(171,987)**	(139,228)
Property acquisitions		**(922)**	(67)	**(2,849)**	(67)
Property dispositions	[4]	**2,601**	22	**2,885**	106,339
Investment in securities	[11]	**-**	-	**(1,000)**	-
Change in non-cash investing working capital	[15]	**10,233**	23,614	**10,519**	11,896
Cash provided by (used in) investing activities		**(58,194)**	(52,319)	**(205,647)**	(60,303)
Foreign exchange on cash and cash equivalents		**(1)**	-	**(1)**	-
Net change in cash and cash equivalents		**1,059**	661	**(2,607)**	700
Cash and cash equivalents, beginning of period		**29**	599	**3,695**	560
Cash and cash equivalents, end of period		**1,088**	1,260	**1,088**	1,260

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

(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. Kelt's land holdings are located in two core areas, namely: (a) Grande Prairie (including Pouce Coupe, Wembley, Progress and La Glace), Alberta; and (b) Fort St. John (including Inga, Fireweed, Stoddart and Oak), British Columbia. The Company's British Columbia assets are operated by Kelt Exploration (LNG) Ltd.), a wholly owned subsidiary of Kelt. 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 and Kelt LNG is located at Suite 300, 311 - 6th Avenue S.W., Calgary, Alberta T2P 3H2.

2. BASIS OF PRESENTATION

The Company's Board of Directors approved and authorized these consolidated condensed interim financial statements for issue on November 8, 2018.

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, 2017.

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 11 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, 2017 consolidated annual financial statements. There have been no significant changes in the Company's judgments and estimates applied during the interim period ended September 30, 2018 relative to those described in the most recent annual financial statements as at and for the year ended December 31, 2017.

3. SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies applied by the Company are described in note 3 of the December 31, 2017 consolidated annual financial statements. Except as outlined below, these condensed consolidated interim financial statements at September 30, 2018 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, 2017.

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

New Accounting Policies

Revenue

Kelt adopted IFRS 15 *Revenue* from contracts with customers with a date of initial application of January 1, 2018 as detailed in note 12. IFRS 15 will replace IAS 18 *Revenue*, IAS 11 *Construction Contracts*, and other related interpretations. Kelt used the modified retrospective approach to adopt the new standard, electing to use a practical expedient to apply the standard retrospectively only to contracts that were not completed on January 1, 2017. There was no change or adjustment to the Company's consolidated financial statements as a result of the adoption of IFRS 15. However IFRS 15 contains additional disclosure requirements which are detailed in note 12.

Kelt recognizes revenue at a point in time when control of the product has been transferred to the customer and performance obligations have been satisfied. This is generally met when the customer obtains legal title to the product and physical delivery at a delivery point has taken place. Revenue is measured based on the consideration specified in the contracts the Company has with its customers.

Kelt evaluates its arrangements with 3rd parties and partners to determine if a principal or agent relationship exists. In making this evaluation, management considers if it maintains control of the product, which is indicated by the Company having the primary responsibility for the delivery of the product, having the ability to establish prices or having inventory risk. If an agency relationship exists, then the revenue is recognized on a net-basis, only reflecting the fee, if any, realized by the party from the transaction.

Royalty income is recognized as it accrues in accordance with the terms of the overriding royalty agreements.

Investments in Securities

Investments in securities are classified as fair value through profit or loss. Investments in the securities of private entities are carried at fair value, which is estimated using values based on equity issuances and other indications of value from time-to-time (level three fair value hierarchy estimates).

Major maintenance expenditures

The costs of major maintenance associated with turnaround activities that benefit future years of operations are capitalized and depreciated over the period to the next major maintenance turnaround. All other maintenance costs are expensed as incurred.

Accounting standards issued but not yet effective

IFRS 16 *Leases,* is intended to replace IAS 17 and will bring fundamental changes for all companies, including Kelt, who lease assets. The new standard is effective for annual reporting periods beginning on or after January 1, 2019, with early application permitted. The most significant financial reporting impacts of the changes include: all leases will be on the balance sheet of lessees, except those that meet the limited exception criteria; the measurement and presentation of expenses will be impacted and replaced by the recording of depreciation and financing expenses; the amount of profit (loss) recognized in a period will likely change as the timing of expenses is accelerated when applying the new standard which uses a finance lease model compared to a straight line operating lease expense; and key ratios may be impacted with the introduction of lease assets and liabilities on the balance sheet and changes to the timing of expenses. Management is currently in the implementation phase of IFRS 16, with the impact on the Company's consolidated financial statements still being assessed; however the additional leases being brought on the balance sheet will likely be material.

4. PROPERTY DISPOSITIONS

The table below summarizes the aggregate proceeds received and carrying values of the assets and associated decommissioning obligations disposed during the nine months ended September 30, 2018 and year ended December 31, 2017, as well as the resulting net gain (loss) on sale in each period:

	September 30, 2018	December 31, 2017
Exploration and evaluation assets	**42**	7,310
Property, plant and equipment	**4,506**	102,985
Decommissioning obligations	**(1,860)**	(4,408)
Carrying value of net assets (liabilities) disposed	**2,688**	105,887
Cash proceeds, after closing adjustments (1)	**2,885**	116,323
Gain (loss) on sale of assets (1)	**197**	10,436

(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.

On July 31, 2018, the Company completed the disposition of the Leduc-Woodbend Cash Generating Unit ("CGU") for $2.6 million after closing adjustments. The Leduc-Woodbend CGU had a carrying value of $2.6 million, resulting in a gain on sale of $0.05 million.

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 with an effective date of January 1, 2017.

During the year ended December 31, 2017, Kelt completed dispositions of certain non-core assets for cash proceeds of $13.3 million, after closing adjustments. The assets and associated decommissioning obligations disposed had a net carrying value of approximately $2.8 million resulting in a gain on sale of $10.5 million (after estimated closing adjustments).

5. 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:

	September 30, 2018	December 31, 2017
Balance, beginning of period	**123,349**	120,166
Additions	**43,215**	42,627
Property acquisitions	**2,976**	531
Reclassification (to) from held for sale [note 4]	**-**	4,377
Property dispositions [note 4]	**(42)**	(7,310)
Transfers to property, plant and equipment	**(37,730)**	(35,731)
Expired mineral leases	**(3,495)**	(1,311)
Balance, end of period	**128,273**	123,349

The Company concluded that there are no indicators of potential impairment of its E&E assets at September 30, 2018.

6. PROPERTY, PLANT AND EQUIPMENT

Net carrying value	September 30, 2018	December 31, 2017
Development and production ("D&P") assets	**1,204,669**	1,107,715
Corporate assets	**602**	357
Total net carrying value of property, plant and equipment	**1,205,271**	1,108,072

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, 2016	1,377,416	2,474	1,379,890
Additions	200,349	793	201,142
Reclassification (to) from held for sale [note 4]	163,166	-	163,166
Property dispositions [note 4]	(172,821)	-	(172,821)
Decommissioning costs	9,288	-	9,288
Transfers from E&E	35,731	-	35,731
Balance at December 31, 2017	**1,613,129**	**3,267**	**1,616,396**
Additions	**171,235**	**752**	**171,987**
Property acquisitions	**485**	-	**485**
Property dispositions [note 4]	**(25,217)**	**-**	**(25,217)**
Decommissioning costs	**3,581**	**-**	**3,581**
Transfers from E&E	**37,730**	**-**	**37,730**
Balance at September 30, 2018	**1,800,943**	**4,019**	**1,804,962**

Accumulated depletion, depreciation and impairment	D&P Assets	Corporate Assets	Total PP&E
Balance at December 31, 2016	379,770	1,943	381,713
Depletion and depreciation expense	126,531	967	127,498
Impairments, net of impairment reversals	6,864	-	6,864
Reclassification (to) from held for sale [note 4]	62,085	-	62,085
Property dispositions [note 4]	(69,836)	-	(69,836)
Balance at December 31, 2017	**505,414**	**2,910**	**508,324**
Depletion and depreciation expense	**108,571**	**507**	**109,078**
Dispositions	**(20,711)**	**-**	**(20,711)**
Impairments	**3,000**	**-**	**3,000**
Balance at September 30, 2018	**596,274**	**3,417**	**599,691**

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 $692.0 million (December 31, 2017 – $776.0 million) are included in the depletion calculation for development and production assets. At September 30, 2018, the balance of assets under construction not subject to depreciation or depletion was $52.2 million (December 31, 2017 – $13.5 million) and relate to the construction of a gas processing facility.

On July 31, 2018, the Company completed the disposition of the Leduc-Woodbend Cash Generating Unit ("CGU"), a non-core oil weighted property for $2.6 million after closing adjustments. The Leduc-Woodbend CGU had a net carrying value of $2.6 million (costs of $25.1 million, accumulated depletion, depreciation and impairment of $20.7 million, and abandonment obligations of $1.8 million), resulting in a gain on sale of $0.05 million. In the second quarter of 2018, the Leduc-Woodbend CGU was impaired by $3.0 million based on the sale in the third quarter of 2018.

7. BANK DEBT

	September 30, 2018	December 31, 2017
Bank loan	**1,100**	17,000
Bankers' acceptances	**135,000**	75,000
Prepaid interest and unamortized financing fees	**(1,046)**	(535)
Bank debt	**135,054**	91,465

The Company has a revolving committed term credit facility ("the Credit Facility") with a syndicate of financial institutions. On April 18, 2018 the facility was amended and the revolving period was extended to April 28, 2019. The authorized borrowing amount available under the Credit Facility was increased to $215.0 million from $185.0 million which includes an accordion feature giving the Company the right, with the consent of the lenders, to increase the commitments under the facility to $250 million with the existing lending syndicate or by adding additional lenders. The pricing grid range was amended to bank prime plus 0.5% to bank prime plus 2.5% (from 1.0% to 2.5% previously), and the stamping fee range was changed to 1.5% to 3.5% (from 2.0% to 3.5% previously) depending upon the Company's then current debt to cash flow ratio of between less than one half times to greater than three times.

The Credit Facility 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.

There are no financial covenants under the Credit Facility and Kelt is in compliance with all other covenants.

Subsequent to the quarter ended September 30, 2018, the Company and its lenders completed the semi-annual bank compliance review and amended the Credit Facility to increase the lenders commitments to $250.0 million.

8. CONVERTIBLE DEBENTURES

	Number of convertible debentures	Liability component ($ thousands)	Equity Component ($ thousands)
Balance at December 31, 2016	90,000	70,978	12,856
Accretion of discount	-	3,539	-
Balance at December 31, 2017	**90,000**	**74,517**	**12,856**
Conversion of convertible debentures to equity	**(90)**	**(76)**	**(13)**
Accretion of discount	**-**	**2,909**	**-**
Balance at September 30, 2018	**89,910**	**77,350**	**12,843**

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. 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").

The Debentures are redeemable by the Company after May 31, 2019 and prior to May 31, 2020, in whole or in part, 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 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 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.

The Company may 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.

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 13). At September 30, 2018, the fair value of the Debentures was $145.8 million (note 11).

9. 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:

	September 30, 2018	December 31, 2017
Balance, beginning of period	**136,928**	128,047
Obligations incurred	**7,506**	6,624
Obligations acquired	**612**	-
Reclassification (to) from held for sale [note 4]	**-**	2,532
Obligations disposed [note 4]	**(1,860)**	(4,408)
Obligations settled	**(887)**	(1,512)
Changes in discount rate	**(4,819)**	2,221
Revisions to estimates	**894**	443
Accretion expense	**2,347**	2,981
Balance, end of period	**140,721**	136,928
Decommissioning obligations – current	**1,314**	1,585
Decommissioning obligations – non-current	**139,407**	135,343
Key Assumptions		
Risk free rate	**2.41%**	2.26%
Inflation rate	**2.0%**	2.0%

The underlying cost estimates are derived from a combination of published industry benchmarks as well as site specific information. As at September 30, 2018, the undiscounted amount of the estimated cash flows required to settle the obligation is $156.6 million (December 31, 2017 – $148.3 million), and is expected to be incurred over the next 50 years. Based on an inflation rate of 2.0%, the undiscounted amount of the estimated future cash flows required to settle the obligation is $300.3 million at September 30, 2018 (December 31, 2017 – $282.0 million). The inflated future cost estimates are discounted based on a risk-free rate to determine the carrying amounts presented in the table above.

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 13).

10. 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 September 30, 2018 (December 31, 2017 – nil).

	Number of Shares (000s)	Amount ($ thousands)
Balance at December 31, 2016	175,672	1,055,959
Issued for cash through common share offerings	2,585	20,605
Deferred premium on flow-through shares	-	(2,553)
Issued for cash on exercise of stock options	415	2,299
Transfer from contributed surplus on exercise of stock options	-	935
Released upon vesting of restricted share units	186	1,740
Share issue costs, net of deferred taxes ($103)	-	(212)
Balance at December 31, 2017	**178,858**	**1,078,773**
Issued for cash through common share offerings	**2,758**	**24,776**
Deferred premium on flow-through shares	**-**	**(3,099)**
Conversion of convertible debentures to common shares	**16**	**76**
Transfer from equity component of convertible debentures on conversion of convertible debentures to common shares	**-**	**13**
Issued for cash on exercise of stock options	**2,081**	**12,687**
Transfer from contributed surplus on exercise of stock options	**-**	**5,007**
Released upon vesting of restricted share units	**268**	**1,470**
Share issue costs, net of deferred taxes ($199)	**-**	**(541)**
Balance at September 30, 2018	**183,981**	**1,119,162**

Private placements of flow-through common shares

The table below summarizes flow-through common shares ("FTS") issued pursuant to private placements during the nine months ended September 30, 2018 and the year ended December 31, 2017, and 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
Closing Dates	# of FTS	Price per FTS	Gross Proceeds	Deferred Premium	Type	**As at September 30, 2018** Incurred	Remaining	
October 11, 2017	**1.263 million**	**$7.75**	**9,785**	**896**	**CDE**	**9,785**	**-**	**December 31, 2017** **December 31, 2017**
October 27, 2017	**0.75 million**	**$7.75**	**5,811**	**615**	**CDE**	**5,811**	**-**	**December 31, 2017** **December 31, 2017**
October 27, 2017	**0.572 million**	**$8.75**	**5,009**	**1,042**	**CEE**	**5,009**	**-**	**December 31, 2018** **December 31, 2017**
April 27, 2018, April 30, 2018	**2.348 million**	**$8.85**	**20,778**	**2,324**	**CDE**	**20,778**	**-**	**December 31, 2018** **December 31, 2018**
April 27, 2018, April 30, 2018	**0.410 million**	**$9.75**	**3,998**	**775**	**CEE**	**3,998**	**-**	**December 31, 2018** **December 31, 2018**

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

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, typically vest in equal tranches over a three year period and have a maximum term of five years to expiry.

The following table summarizes the change in stock options outstanding:

	Number of Options (000s)	Average Exercise Price ($/share)
Balance at December 31, 2016	8,376	6.57
Granted	2,347	6.25
Exercised (1)	(415)	5.54
Forfeited	(414)	7.03
Balance at December 31, 2017	**9,894**	**6.51**
Granted	**446**	**7.85**
Exercised (1)	**(2,081)**	**6.10**
Forfeited	**(247)**	**6.94**
Expired	**(158)**	**7.39**
Balance at September 30, 2018	**7,854**	**6.67**

(1) The weighted average share price on the date stock options were exercised during the period ended September 30, 2018 was $7.74 per common share ($6.96 per common share on average during the year ended December 31, 2017).

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:

	Nine months ended September 30	
	2018	2017
Risk free interest rate	**1.9%**	1.3%
Expected life (years)	**3.1**	3.5
Expected volatility [(1)]	**47.4%**	54.0%
Expected dividend yield	**0.0%**	0.0%
Expected forfeiture rate	**4.5%**	2.3%
Fair value of options granted during the year ($/share)	**2.70**	2.42

(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 September 30, 2018:

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	2,913	2.5	4.53	1,833	4.53
$5.01 to $10.00	4,008	3.0	6.85	1,990	7.10
$10.01 to $15.00	873	0.5	12.40	873	12.40
$15.01 to $20.00	60	0.7	15.40	60	15.40
Total	**7,854**	**2.5**	**6.67**	**4,756**	**7.19**

Restricted share units

Kelt has a restricted share unit plan that provides for granting of restricted share units ("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. RSUs typically vest in two equal tranches with the first half vesting after two years and the second half after three years.

The following table summarizes the change in RSUs outstanding:

	Number of RSUs (000s)
Balance at December 31, 2016	720
Granted	325
Released upon vesting	(186)
Forfeited	(66)
Balance at December 31, 2017	**793**
Granted	**607**
Released upon vesting	**(268)**
Forfeited	**(30)**
Balance at September 30, 2018	**1,102**

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 September 30		Nine months ended September 30	
	2018	2017	**2018**	2017
Stock options	**902**	931	**3,022**	2,687
Restricted share units	**514**	393	**1,342**	1,186
Total share based compensation expense	**1,416**	1,324	**4,364**	3,873

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 September 30		Nine months ended September 30	
(000s of common shares)	**2018**	2017	**2018**	2017
Weighted average common shares outstanding, basic	**183,919**	176,013	**182,262**	175,875
Effect of stock options and RSUs	**2,530**	1,193	**2,057**	1,329
Effect of convertible debentures	**-**	-	**-**	-
Weighted average common shares outstanding, diluted	**186,449**	177,206	**184,319**	177,204

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 profit or loss per common share for the periods ended September 30, 2018 and 2017, 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 September 30, 2018.

11. 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

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 September 30, 2018, there are no commodity price risk management contracts outstanding. Subsequent to September 30, 2018 the Company entered into the following contracts:

Contract Type	Notional Volume	Reference Prices	Fixed Contract Price	Term
Financial Swap Natural Gas	10,000 MMBtu/d	NYMEX to Chicago Citygate Basis Differential	NYMEX Henry Hub less USD$0.14 per MMBtu	January 2019 to October 2019
Financial Swap Natural Gas	10,000 MMBtu/d	NYMEX to Union Dawn Basis Differential	NYMEX Henry Hub less USD$0.0975 per MMBtu	January 2019 to December 2019
Financial Swap Natural Gas	7,500 MMBtu/d	Sumas	USD$5.97 per MMBTU	November 2018 to March 2019

Interest rate risk

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 $118.1 million during the first nine months of 2018, an increase (decrease) in the market rate of interest by 25 basis points would have increased (decreased) interest expense by $0.3 million.

As at September 30, 2018, there are no interest rate risk management contracts outstanding.

Foreign exchange risk

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 has natural gas marketing arrangements in place whereby Kelt receives revenue 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 14. The Company may enter into derivative contracts to mitigate the impact of foreign currency fluctuations. As at December 31, 2017, there were no foreign exchange risk management contracts outstanding.

On July 11, 2016, the Company entered into a foreign exchange swaption contract and received a cash premium of $0.255 million. The swaption was exercised by the counterparty resulting in a derivative contract that fixed the exchange rate at CA$/US$1.33 on a notional US$1.0 million per month over the initial contract term of January to December 2017. On July 26, 2017, the Company unwound the foreign exchange swap for cash proceeds of $0.4 million, extinguishing the contract for the remaining five month term from August to December 2017. Kelt realized a cumulative net cash gain of $0.7 million under this contract, including the cash premium earned at inception.

As at September 30, 2018, there are no foreign exchange risk management contracts outstanding. Subsequent to September 30, 2018 the Company entered into the following contract:

Contract Type	Notional Amount per month	Fixed Contract Price	Term
FX swap	US$1,000,000	CA$/US$ 1.3050	January 2019 to December 2019

Gains and losses on risk management contracts

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

	Three months ended September 30		Nine months ended September 30	
	2018	2017	**2018**	2017
Realized gain (loss)	**-**	41	**-**	(330)
Unrealized gain	**-**	(548)	**-**	(127)
Gain on derivative financial instruments	**-**	(507)	**-**	(457)

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 September 30, 2018:

	Carrying Value ("CV")			Fair Value		
	Gross	Netting(1)	Net CV	Level 1	Level 2	Level 3
Financial assets						
Investment in securities	1,000	-	-	-	-	1,000
Financial liabilities						
Convertible debentures (note 8)	77,350	-	-	145,782	-	-

(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 September 30, 2018, there are no outstanding or offsetting derivative financial contracts.

Kelt's investment in securities includes an investment in a private corporation entered into during the first quarter of 2018. The estimated fair value of the Company's investments in the shares of private companies is based on equity issuances and other indications of value from time-to-time (level three fair value hierarchy inputs).

The fair value of the convertible debentures of $145.8 million as at September 30, 2018, is based on the closing market price of $162.00 per Debenture, being the price at which the Debentures last traded on the third quarter ending September 30, 2018, and represents the market value of the entire instrument. As at December 31, 2017, the fair value was $135.0 million based on the closing market price of $150.00 per Debenture at the end of the year.

Credit Risk

As at September 30, 2018, the carrying amount of cash and cash equivalents, accounts receivable and accrued revenue, and deposits, 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 composition of the Company's accounts receivable is set out in the following table:

Accounts receivable and accrued revenue	**September 30, 2018**	December 31, 2017
Oil and gas marketers	**5,539**	30,996
Joint venture partners	**28,936**	3,654
GST input tax credits	**4,374**	4,419
Other	**344**	377
Accounts receivable and accrued revenue	**39,193**	39,446

During the nine months ended September 30, 2018, sales to two oil and gas marketers each individually represented more than 10% of total revenue. Sales to these marketers account for approximately 41% and 19% of total revenue, respectively. During the comparative period ended December 31, 2017, sales to three oil and gas marketers accounted for approximately 38%, 17%, and 11% of total revenue, respectively. Kelt's oil and gas marketers have either provided parental guarantees (with terms ranging from two to five years), provided letters of credit, or have been rated investment-grade by a reputable ratings agency for substantially all of the Company's monthly credit exposure.

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 30-90 days.

The balance of accounts receivable outstanding for more than 90 days relates primarily to receivables from the Company's joint venture partners. Credit risk related to 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 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. The aging of the Company's accounts receivable and the loss allowance provision is determined as follows:

Accounts receivable and accrued revenue	Current	30-60 days	60-90 days	Over 90 days	Total
Gross accounts receivable	34,701	2,197	505	2,456	39,859
Estimated credit loss rate	0.5%	3.6%	5.3%	15.7%	
Loss allowance provision	(176)	(78)	(27)	(385)	(666)
Balance at September 30, 2018	**34,525**	**2,119**	**478**	**2,071**	**39,193**
Balance at December 31, 2017	37,889	325	189	1,043	39,446

The allowance for doubtful accounts provision as at December 31, 2017 reconciles to the opening loss allowance provision as at January 1, 2017 in the following table:

	Amount ($ thousands)
Allowance for doubtful accounts at January 1, 2017	789
Direct write-off of amounts included in provision	(123)
Allowance for doubtful accounts at December 31, 2017	**666**
Provisions for potential credit losses through profit or loss	-
Loss allowance balance at September 30, 2018	**666**

During the nine months ended September 30, 2018, there were no losses recognized in the Company's Consolidated Statement of Profit (Loss) and Comprehensive Income in relation to impaired receivables (December 31, 2017 – nil).

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 September 30, 2018, the Company's working capital deficit of $41.0 million combined with outstanding bank debt of $135.1 million, represented 70% of the authorized borrowing amount available under the Credit Facility of $250.0 million (down from 74% at December 31, 2017). The Credit Facility is available for a revolving period of 364 days, maturing on April 28, 2019, and may be extended annually at Kelt's option and subject to lender approval, with a 364 day term-out period if not renewed.

On April 18, 2018 the facility was amended and the revolving period was extended to April 28, 2019. The authorized borrowing amount available under the Credit Facility was increased to $215.0 million from $185 million which includes an accordion feature allowing the Company the right, with the consent of the lenders, to increase the commitments under the facility to $250 million with the existing lending syndicate or by adding additional lenders. The pricing grid range was amended to bank prime plus 0.5% to bank prime plus 2.5% (from 1.0% to 2.5% previously), and the stamping fee range was changed to 1.5% to 3.5% (from 2.0% to 3.5% previously) depending upon the Company's then current debt to cash flow ratio of between less than one half times to greater than three times.

Subsequent to the quarter ended September 30, 2018, the Company and its lenders completed the semi-annual bank compliance review and amended the Credit Facility to increase the lenders commitments to $250.0 million.

The table below outlines a contractual maturity analysis for Kelt's financial liabilities as at September 30, 2018:

	Within 1 Year	1 to 5 Years	More than 5 Years	Total
Accounts payable and accrued liabilities	83,248	-	-	**83,248**
Bank debt and estimated interest(1)	4,997	135,054	-	**140,051**
Convertible debentures(2)	4,496	97,411	-	**101,907**
Total	**92,741**	**232,465**	**-**	**325,206**

(1) Estimated interest for future periods related to the Credit Facility was calculated using the weighted average interest rate of 3.7% for the quarter ended September 30, 2018, 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 28, 2019.

(2) The contractual maturity analysis includes semi-annual cash interest payments at the fixed coupon rate of 5.0%, assuming that the $89.9 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 8.

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 debt to trailing adjusted funds from operations ratio, which is a non-GAAP financial measure.

	September 30, 2018	December 31, 2017
Bank debt	**135,054**	91,465
Working capital deficiency	**40,992**	45,264
Net debt (1)	**176,046**	136,729
Trailing annualized adjusted funds from operations (2)(3)	**187,506**	131,592
Net debt to trailing adjusted funds from operations ratio (1)	**0.9**	1.0

(1) "Net 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 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 reduced its net debt to trailing adjusted funds from operations ratio to 0.9 times as at September 30, 2018 from 1.0 times at December 31, 2017.

As more particularly described in note 7, Kelt is subject to certain non-financial covenants under the Credit Facility agreement. As at September 30, 2018, the Company is in compliance with all covenants. The Company is not subject to any other externally imposed capital requirements.

12. REVENUE

Kelt sells its oil, natural gas, and NGLs production pursuant to variable price contracts. The transaction price for variable priced contracts is based on a benchmark commodity price, adjusted for quality, location or other factors, whereby each component of the pricing formula (apart from the benchmark commodity price) can be either fixed or variable, depending on the contract terms. Revenues are typically collected on the 25th day of the month following the prior month's production, with revenue being recorded once the product is delivered to a contractually agreed upon delivery point.

Kelt generates oil treating, gas processing, and other services income from fees charged to third parties provided at facilities where Kelt has an ownership interest. Kelt generates marketing revenue from the sales of third party volumes related to the Company's oil blending operations, with the production being sold under the same terms of the Company's variable oil price contracts discussed above.

In the first quarter of 2018, Kelt adopted IFRS 15 Revenue from contracts with customers as detailed in note 3, using modified retrospective approach. There was no change or adjustment to the Company's consolidated financial statements as a result of the adoption of IFRS 15.

The following table presents Kelt's production disaggregated by revenue source:

	Three months ended September 30		Nine months ended September 30	
(CA$ thousands, except as otherwise indicated)	**2018**	2017	**2018**	2017
Revenue, before royalties and financial instruments:				
Oil production	**54,886**	33,054	**166,000**	94,220
Oil treating and other	**868**	640	**2,394**	1,527
NGLs production	**10,691**	6,077	**29,651**	17,174
Gas production	**23,816**	15,496	**70,011**	61,075
Gas processing and other	**247**	1,155	**1,292**	2,723
Marketing revenue	**9,711**	-	**19,579**	-
Total revenue	**100,219**	56,422	**288,927**	176,719

Included in accounts receivable at September 30, 2018 is $5.5 million (December 31, 2017 - $31.0 million) of accrued oil and gas sales related to September 2018 production.

13. FINANCING EXPENSES

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

	Three months ended September 30		Nine months ended September 30	
	2018	2017	**2018**	2017
Interest on bank debt [note 7]	**1,375**	904	**3,786**	2,297
Interest on convertible debentures [note 8]	**1,133**	1,134	**3,364**	3,366
Accretion of convertible debentures [note 8]	**1,002**	899	**2,909**	2,606
Accretion of decommissioning obligations [note 9]	**792**	743	**2,347**	2,207
Financing expense	**4,302**	3,680	**12,406**	10,476

14. COMMITMENTS

As of September 30, 2018, the Company is committed to future payments under the following agreements:

(CA$ thousands)	2018	2019	2020	2021	2022	Thereafter
Operating lease - office buildings	44	967	1,035	1,056	1,077	376
Operating lease - vehicles	99	322	173	41	-	-
Firm processing commitments	2,394	7,860	1,566	1,605	1,365	-
Firm transportation commitments [(1)]	8,235	33,677	27,163	23,009	22,508	180,533
Total annual commitments	10,772	42,826	29,937	25,711	24,950	180,909

(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 contract, which is effective until October 31, 2020, respectively. Amounts are translated to Canadian dollars at the spot rate on September 30, 2018 of CA$/US$1.2945.

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, 2023, February 28, 2020, and July 31, 2023, respectively, if not extended.

In July 2018, the Company entered into a letter of intent for firm processing of 75 mmcf per day of raw gas under a 10 year proposed take or pay arrangement. In August 2018, a firm take or pay processing agreement was entered into allowing Kelt an option to increase the firm processing up to an additional 95 mmcf/d and the option to extend the term up to 20 years. The take or pay arrangement is conditional upon the commissioning and construction of a processing facility which is expected to be on-stream in the fourth quarter of 2019. As the commissioning and construction of the facility has not yet been finalized, it has not been included in the commitment table above.

Kelt has also entered into a proposed firm processing agreement for 30 mmcf per day of raw gas under a five year proposed take or pay arrangement. This agreement is also subject to obtaining regulatory approvals and the construction of a processing facility which is expected to be on-stream in the third quarter of 2019. Subsequent to September 30, 2018, the operator of the processing facility obtained approvals from the Alberta Energy regulator for the construction and operation of the facility. As the commissioning and construction of the facility has not yet been finalized, it has not been included in the commitment table above.

During the third quarter of 2018 firm transportation commitments increased by $165 million over the entire commitment term from the second quarter of 2018. The increase in commitments is primarily due to take or pay commitments on the North Montney Mainline which is expected to be in-service in the second half of 2019.

15. SUPPLEMENTAL CASH FLOW INFORMATION

	Three months ended September 30		Nine months ended September 30	
Changes in non-cash working capital	**2018**	2017	**2018**	2017
Accounts receivable and accrued revenue	**(4,327)**	3,220	**253**	5,449
Prepaid expenses and deposits	**(46)**	231	**(1,284)**	(1,167)
Accounts payable and accrued liabilities	**(2,265)**	21,801	**(4,535)**	12,293
Change in non-cash working capital	**(6,638)**	25,252	**(5,566)**	16,575
Relating to:				
Operating activities	**(16,871)**	1,638	**(16,085)**	4,679
Investing activities	**10,233**	23,614	**10,519**	11,896
Change in non-cash working capital	**(6,638)**	25,252	**(5,566)**	16,575

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

	Three months ended September 30		Nine months ended September 30	
Cash outlays in respect of interest and taxes	**2018**	2017	**2018**	2017
Interest and standby fees on bank debt	**1,425**	1,122	**4,348**	2,513
Interest on convertible debentures (1)	**-**	-	**2,244**	2,244
Taxes (2)	**-**	-	**-**	-

(1) Interest on the Debentures is payable semi-annually on May 31st and November 30th (note 8).

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

16. 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 nine months ended September 30, 2018, the Company incurred $0.4 million (2017 – $0.2 million) in legal fees and disbursements. 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
AECO	Alberta Energy Company "C" Meter Station of the NOVA Pipeline System
NIT	NOVA Inventory Transfer ("AB-NIT"), being the reference price at the AECO Hub
WTI	West Texas Intermediate
NYMEX	New York Mercantile Exchange
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

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)

IP120 = initial production from a well for the first 2,880 hours (120 days) based on operating / producing hours

CORPORATE INFORMATION

BOARD OF DIRECTORS

Robert J. Dales [2, 3, 4, 7]
President, Valhalla Ventures Inc.

Geri Greenall [2, 3, 6]
Vice President, Portfolio Manager & Chief Operating Officer of Kyklopes Capital Management Ltd.

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

Michael R. Shea [3, 4, 6]

Neil G. Sinclair [2, 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
7 lead director

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

David A. Gillis
Vice President, Finance

Douglas O. MacArthur
Vice President, Operations

Patrick W.G. Miles
Vice President, Exploration

Carol Van Brunschot
Vice President, Marketing

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Toronto Stock Exchange
Common shares “KEL”
Convertible Debentures “KEL.DB”

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