



PrairieSky Royalty Ltd.

## Management's Discussion and Analysis

(Prepared in accordance with IFRS)

For the period ended June 30, 2014

(Prepared in Canadian Dollars)

## Management's Discussion and Analysis

*This Management's Discussion and Analysis ("MD&A") for PrairieSky Royalty Ltd. ("PrairieSky" or the "Company") should be read with the unaudited Interim Condensed Financial Statements for the period ended June 30, 2014 ("Interim Condensed Financial Statements") and its audited financial statements as at December 31, 2013 and for the period from incorporation on November 27, 2013 to December 31, 2013. This MD&A was prepared and is dated July 21, 2014.*

*The Interim Condensed Financial Statements and comparative information have been prepared in Canadian dollars and in accordance with International Accounting Standard ("IAS") 34, "Interim Financial Reporting" issued by the International Accounting Standards Board ("IASB"). PrairieSky receives royalty income on production; as such, the production volumes are equivalent on a gross and net basis.*

*Certain measures in this document do not have any standardized meaning as prescribed by International Financial Reporting Standards ("IFRS") and, therefore, are considered non-GAAP measures. Non-GAAP measures are commonly used in the oil and gas industry and by PrairieSky to provide potential investors with additional information regarding the Company's liquidity and its ability to generate funds to finance its operations. Non-GAAP measures include Operating Cash Flow, and Netback, Funds from Operations, Net Earnings and Comprehensive Income Adjusted per share basic and diluted, Funds from Operations Adjusted per Share basic and diluted. Further information can be found in the Non-GAAP Measures section of this MD&A, including a reconciliation of Cash from Operating Activities to Funds from Operations; a reconciliation of Net Earnings and Comprehensive Income Adjusted Per Share basic and diluted and Funds from Operations Adjusted Per Share basic and diluted.*

*The following volumetric measures may be abbreviated throughout this MD&A: barrel ("bbl") per day ("bbls/d"); barrel of oil equivalent ("BOE") per day ("BOE/d"); thousand cubic feet ("Mcf"); million cubic feet ("MMcf") per day ("MMcf/d"). Barrel of oil equivalent ("BOE") is an industry measurement to summarize the amount of energy equivalent found in a barrel of crude. See the discussion on energy conversions in the Advisory section of this document for explanation.*

**Readers should also read the Advisory section located at the end of this document, which provides information on Forward-Looking Statements, Natural Gas, Oil and Natural Gas Liquids ("NGL") conversions and currency and references to PrairieSky.**

## BUSINESS OVERVIEW

PrairieSky is a corporation focused on encouraging third parties to actively develop the Royalty Properties (as defined herein), while strategically seeking additional petroleum and natural gas assets that provide PrairieSky with medium-term to long-term value enhancement potential. The Company does not directly conduct operations to explore for, develop or produce petroleum or natural gas, rather, third party development of the Royalty Properties provides the Company with royalty revenues as petroleum and natural gas are produced from such properties.

The Company was incorporated under the *Business Corporations Act (Alberta)* under the name 1786071 Alberta Ltd. on November 27, 2013. On April 11, 2014, the Company filed articles of amendment to change its name to "PrairieSky Royalty Ltd.". The Company had no significant operating activity from the date of incorporation until May 27, 2014, when it acquired a royalty business (the "Acquisition") from Encana Corporation ("Encana"), which assets are comprised of: (i) fee simple mineral title in lands prospective for petroleum, natural gas and certain other mine and mineral rights located predominantly in central and southern Alberta (the "Fee Lands"); (ii) lessor interests in and to leases that are currently issued in respect of certain Fee Lands ("Lessor Interests"); (iii) royalty interests, including overriding royalty interests, gross overriding royalty interests and production payments ("GORR Interests") on lands located predominantly in Alberta ("GORR Lands"); (iv) an irrevocable, perpetual licence to certain proprietary seismic data of Encana; and (v) certain other related assets as set forth in the Purchase and Sale Agreement between the Company and Encana (collectively, the "Acquired Business"). In this MD&A the Fee Lands, the Lessor Interests and the GORR Lands are collectively referred to as the "Royalty Properties".

On May 29, 2014, PrairieSky completed an initial public offering ("IPO") whereby Encana sold 52,000,000 common shares and the Company's common shares were listed and posted for trading on the Toronto Stock Exchange ("TSX"). On June 3, 2014, the Company announced that in connection with the IPO the over-allotment option granted to the underwriters to purchase up to an additional 7,800,000 common shares from Encana at the offering price had been exercised in full. Following completion of the IPO and exercise of the over-allotment option, Encana owns 70,200,000 common shares, representing 54% of the issued and outstanding common shares of the Company.

PrairieSky's asset base includes a geologically and geographically diverse portfolio of Fee Lands predominately located in Alberta that encompasses approximately 5.2 million acres with petroleum and/or natural gas rights and an additional 1.1 million acres with coal rights.

PrairieSky's operations include royalty income earned through crude oil, NGLs and natural gas produced on the Company's Royalty Properties. The Company's royalty revenues are derived from the Lessor Interests from the Fee Lands that are leased out by the Company and upon which lessees pay lessor royalties and GORR Interests on GORR Lands leased by third parties.

The Company's costs are primarily freehold mineral taxes and administrative expenses. Costs typically related to upstream drilling, equipment, production and asset retirement obligations are not incurred by the Company; instead, these costs are incurred by the third parties who conduct activities on the Royalty Properties.

Management's discussion and analysis for this reporting period focuses on the commencement of operations on May 27, 2014 to the period ending June 30, 2014.

## PRAIRIESKY'S STRATEGIC OBJECTIVES

The Company's objective is to generate significant cash flow and growth for shareholders through indirect oil and gas investment at a relatively low risk and low cost to the Company. The Company seeks to achieve this objective by (i) focusing on organic growth of the royalty revenue from the Fee Lands; (ii) proactively monitoring and managing the portfolio of Royalty Properties to ensure third party adherence to lease terms and contractual provisions (including offset well obligations); and (iii) selectively pursuing strategic business development opportunities that are relatively low risk to the Company and accretive to shareholders. The Company intends to pay out the majority of the cash flow as dividends to shareholders over time.

## RESULTS OVERVIEW

### HIGHLIGHTS

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On May 27, 2014, the Company commenced active operations following the completion of the Acquisition; prior to this date, the Company did not have significant assets, liabilities, or operations.

During the period from May 27, 2014 to June 30, 2014, PrairieSky reported:

- Funds from Operations of \$31,038 thousand and Net Earnings of \$23,907 thousand.
- Average crude oil production volumes of 6,931 bbls/d, average NGL production volumes of 1,582 bbls/d and average natural gas production volumes of 42.9 MMcf/d.
- Average realized crude oil prices of \$98.50 per bbl. Average realized NGL prices of \$63.55 per bbl and average realized natural gas prices of \$4.51 per Mcf.
- Cash and cash equivalents of \$27,160 thousand.
- Working capital of \$57,535 thousand.

## FINANCIAL RESULTS AND QUARTERLY PRICES

(\$ thousands, unless otherwise noted)	For the period from May 27, 2014 to June 30, 2014
Net Earnings and Comprehensive Income	\$ 23,907
Per Share – basic <sup>(2)</sup>	1.01
Per Share – diluted <sup>(2)</sup>	1.00
Adjusted Per Share – basic <sup>(1)</sup>	0.18
Adjusted Per Share – diluted <sup>(1)</sup>	0.18
Funds from Operations <sup>(1)</sup>	31,038
Per Share – basic <sup>(2)</sup>	1.31
Per Share – diluted <sup>(2)</sup>	1.30
Adjusted Per Share – basic <sup>(1)</sup>	0.24
Adjusted Per Share – diluted <sup>(1)</sup>	0.24
Revenues	37,222
Dividends <sup>(3)</sup>	13,754
Per Share	0.1058
<b>Production Volumes</b>	
Natural Gas (MMcf/d)	42.9
Crude Oil (bbls/d)	6,931
NGL (bbls/d)	1,582
Total Crude Oil & NGL (bbls/d)	8,513
Total (BOE/d) <sup>(4)</sup>	15,664
<b>Realized Pricing</b>	
Natural Gas (\$/Mcf)	\$ 4.51
Crude Oil (\$/bbl)	98.50
NGL (\$/bbl)	63.55
Total Crude Oil and NGL(\$/bbl)	92.00
Total (\$/BOE) <sup>(4)</sup>	\$ 62.35
<b>Natural Gas Price Benchmarks</b>	
AECO (\$/Mcf)	\$ 4.68
<b>Oil Price Benchmarks</b>	
West Texas Intermediate (WTI) (US\$/bbl)	102.98
Edmonton Light Sweet (\$/bbl)	104.53

(1) A Non-GAAP measure, which is defined under the Non-GAAP Measures section in our MD&A.

(2) Net Earnings and Comprehensive Income and Funds from Operations per common share are calculated using the weighted average number of PrairieSky common shares outstanding from January 1st to June 30, 2014 giving effect to stock options.

(3) A dividend of \$0.1058 per Common Share was declared on June 18, 2014. The dividend was paid on July 15, 2014 to shareholders of record as at June 30, 2014.

(4) See "Conversions of Natural Gas to BOE".

Petroleum royalty structures are typically linked directly to production volumes and price by their nature. Therefore the Company's net earnings can be significantly impacted by fluctuations in commodity prices and production volumes. Production volumes can be influenced by various factors, including the extent of exploration and development by the third party lessees on the Fee Lands, the timing and amount of capital expenditures, and the expertise and financial resources of third party lessees. Commodity pricing is influenced by market supply and demand as well as other factors such as weather, quality of product and access to market. The Company is able to mitigate these risks to the extent that multiple third party lessees farm into the Fee Lands and that production for natural gas, crude oil, and NGLs is diversified.

In the period from May 27, 2014 to June 30, 2014, the Company realized a combined average price from natural gas, crude oil and NGL's of \$62.35 per BOE.

## For the period May 27, 2014 to June 30, 2014

- Funds from Operations were \$31,038 thousand and Operating Cash Flow was \$30,382 thousand.
- Average realized crude oil and NGL prices were \$98.50 per bbl and \$63.55 per bbl, respectively.
- Average crude oil and NGL production volumes were 6,931 bbls/d and 1,582 bbls/d, respectively.
- Average realized natural gas prices were \$4.51 per Mcf during the period and average natural gas production volumes were 42.9 MMcf/d.
- Current income tax was \$4,137 thousand.
- Depletion, Depreciation, and Amortization (“DD&A”) was \$3,748 thousand.
- Administrative expense was \$2,664 thousand.
- Freehold mineral taxes expense were \$1,136 thousand.
- Net Earnings were \$23,907 thousand.

## Seasonality of Results

Natural gas pricing within the North American market is typically impacted by seasonality and weather conditions. Natural gas is a seasonal fuel with demand generally being higher during the winter and summer and lower in the spring and fall. Crude oil prices are generally determined by global supply and demand factors and these variances do not have seasonal predictability. Production conditions on the Fee Lands are susceptible to diverse weather patterns experienced in Alberta and can impact operations. Natural gas and NGL pricing is also impacted by industrial demand and North American natural gas inventories. As such, PrairieSky’s royalty revenue will be directly impacted as third party lessees experience these conditions.

## PRODUCTION

### PRODUCTION VOLUMES

	For the period from May 27, 2014 to June 30, 2014
(average daily)	
Natural Gas (MMcf/d)	42.9
Crude Oil (bbls/d)	6,931
NGL (bbls/d)	1,582
Total Crude Oil and NGL (bbls/d)	8,513
Total Production (BOE/d)	15,664

Production volumes for the Company are set out in the table above. Accruals are based on historical production information. Actual production receipts from these wells are obtained from lessees and subsequently matched to government reporting databases. The nature of royalty interests can result in delays in production receipts and any such delays combined with the Company’s compliance program may result in reported royalty volumes that includes adjustments from prior periods. These factors may result in fluctuations in reported production volumes.

The Company currently has approximately 24,000 active leases, comprised of approximately 19,000 leases to third parties and approximately 5,000 leases to Encana, allowing for existing and ongoing petroleum and natural gas drilling and development. Over 300 lessees are actively engaged in producing petroleum and natural gas on the Fee Lands. PrairieSky’s crude oil, NGLs and natural gas production volumes are primarily marketed with lessees’ production.

## For the period May 27, 2014 to June 30, 2014

Royalty revenues of \$34,182 thousand were received from approximately 17,000 producing wells. Average crude oil production volumes were 6,931 bbls/d, average NGL production volumes were 1,582 bbls/d and average natural gas production volumes were 42.9 MMcf/d.

Production volumes are impacted by prior period production adjustments, third party development activities and natural declines. Although no prior period information is presented, the Company's compliance program continues to ensure receipt of revenues and production volumes from operating activities on the Royalty Properties prior to completion of the IPO.

## FINANCIAL RESULTS

### REVENUES

<b>Revenues by Product</b> (\$ thousands)	<b>For the period from May 27, 2014 to June 30, 2014</b>
Crude Oil	\$ 23,894
Natural Gas	6,768
NGL	3,520
	34,182
Other Revenues	3,040
<b>Total Revenues</b>	<b>\$ 37,222</b>

<b>Revenues by Royalty Classification</b> (\$ thousands)	<b>For the period from May 27, 2014 to June 30, 2014</b>
Fee Lands	\$ 33,578
GORR Interests	604
	34,182
Other Revenues	3,040
<b>Total Revenues</b>	<b>\$ 37,222</b>

<b>Finance Items</b> (\$ thousands)	<b>For the period from May 27, 2014 to June 30, 2014</b>
Finance Income	\$ (66)
Finance Expense	152
<b>Net Finance Items</b>	<b>\$ 86</b>

The Company's operations include royalty revenues earned from crude oil, NGL and natural gas produced on the Fee Lands and the GORR Lands. Royalty rates vary from approximately 1% to 40%. The average royalty rate for the period May 27, 2014 to June 30, 2014 was approximately 7%. In the period from May 27, 2014 to June 30, 2014, revenues from the Lessor Interests were \$33,578 thousand 98% of total royalty revenues and GORR Interests were \$604 thousand or 2% of total royalty revenues.

Other revenues include lease rental income from leases that are currently issued in respect of certain Fee Lands and revenues from sulphur.

As the Company receives royalties from third party lessees, production is not hedged, and the Company does not currently intend to enter into any commodity price hedges.

Net Finance Items consist primarily of Acquisition closing transactions, banking and Credit Facility set-up and maintenance fees, and interest earned since the commencement of operations.

## OPERATING RESULTS

	For the period from May 27, 2014 to June 30, 2014	
	Operating Cash Flow <sup>(1)</sup> (\$ thousands)	Total Netback <sup>(1)</sup> (\$/BOE)
Revenues <sup>(2)</sup>	\$ 34,182	\$ 62.35
Administrative Expenses	2,664	4.86
Freehold Mineral Taxes	1,136	2.07
Operating Cash Flow / Netback	\$ 30,382	\$ 55.42

	For the period from May 27, 2014 to June 30, 2014
Production Volumes (BOE/d)	15,664

(1) Non-GAAP measure. See "Non-GAAP Measures" in this MD&A.

(2) Excludes the impact of Other Revenues.

PrairieSky does not incur royalty expense on production from the Fee Lands. As the royalty owner, the Company receives the royalty as revenues from third party lessees.

Costs incurred by the Company are primarily freehold mineral taxes and lease administration expenses. Lease administration expenses include such items as land title management, contract administration, technical evaluation, negotiations and compliance costs to secure both mineral rights and ensure accurate royalty revenue payments. Costs and associated risks typical of oil and gas upstream development such as drilling, production equipment and land restoration are not incurred by PrairieSky. These costs are the responsibility of the third party lessee farming into the Royalty Properties.

### For the period May 27, 2014 to June 30, 2014

Operating Cash Flow was \$30,382 thousand and was impacted by:

- Average total realized price of \$62.35 per BOE on production;
- Average total production volumes of 15,664 BOE/d;
- Production revenue of \$34,182 thousand; and
- Freehold mineral of of \$1,136 thousand.

## ADMINISTRATIVE

(\$ thousands)	For the period from May 27, 2014 to June 30, 2014
Salaries and Benefits	\$ 1,087
Share-Based Compensation	1,216
Office Expense	271
Public Company Expense	73
Information Technology and Other	17
Total Administrative Expense	\$ 2,664

Of the total share-based compensation for the period ended June 30, 2014, the Company expensed \$868 thousand related to the Company's Deferred Share Unit ("DSU") plan. All Directors elected to receive their compensation as DSUs. The remaining \$348 thousand share-based compensation expense relates to the Company's other employee share-based plans. The share-based cash settled plans' expenses were determined based on the difference between the IPO price and the closing share price at June 30, 2014. For further explanation refer to Note 16 of the Interim Condensed Financial Statements.

## DEPLETION, DEPRECIATION AND AMORTIZATION (“DD&A”)

(\$ thousands)	For the period from May 27, 2014 to June 30, 2014
Depreciation, Depletion and Amortization	\$ 3,748

The Company calculates DD&A relative to total proved and probable reserves. DD&A was calculated based on production for the period from May 27, 2014 to June 30, 2014 following completion of the Acquisition.

On May 27, 2014 the Company began depleting crude oil, NGL and natural gas properties using the unit-of-production method over proved plus probable reserves on a prospective basis. For the period May 27, 2014 to June 30, 2014 the Company recorded \$928 thousand lower depletion expense than it would have using proved reserves. Based on the reserves at the date of the change in estimate, the effect reduced depletion by \$1.64 per BOE.

## INCOME TAX

(\$ thousands)	For the period from May 27, 2014 to June 30, 2014
Current Tax Expense	\$ 4,137
Deferred Tax Expense	1,544
Income Tax Expense	\$ 5,681

The Company's interim income tax expense is determined using the estimated annual effective income tax rate applied to year-to-date net earnings before tax.

For this reporting period the Company's effective tax rate was approximately 19.2%. The effective tax rate in any period is a function of total income tax to the amount of net earnings before income tax for the period. The Company's effective tax rate differs from the Canadian statutory tax rate of 25% primarily as a result of the reversal of the initial difference between the carrying value of net assets transferred and the tax pools acquired on May 27, 2014 for which no deferred tax asset was recognized and partially offset by non-deductible employee-related expenses.

Under the terms of the Acquired Business, the Company acquired tax pools of approximately \$500 million relating to the Royalty Properties. Under IFRS, deferred income tax liabilities and assets are not recognized for temporary differences arising on the initial recognition of an asset or liability in a transaction which is not a business combination and, at the time of transaction, affects neither accounting net earnings nor taxable earnings. For further explanation refer to Note 8 of the Interim Condensed Financial Statements.

Tax interpretations, regulations and legislation in the jurisdictions in which the Company operates are subject to change. Management believes that the provision for taxes for the Company is adequate.

## COMMON CONTROL TRANSACTION

(\$ thousands)	As at May 27, 2014
Exploration and Evaluation Assets	\$ 6,809
Property, Plant and Equipment, net	181,248
Other Assets	16,451
Goodwill	57,734
Net Working Capital	37,722
Carrying Value of Net Assets Acquired:	\$ 299,964

The Company commenced active operations on May 27, 2014 following the completion of the Acquisition from Encana to the Company. The Company was a wholly owned subsidiary and controlled by Encana prior to closing the IPO, and immediately subsequent to closing was controlled by Encana. Consequently, the entity was under common control at the time of the Acquisition. The Acquisition has been accounted

for using the predecessor values from the date of transaction method, whereby the Acquired Business is transferred to the Company based on the historical carrying value carved out of Encana. The table above summarizes the carrying value of the net assets transferred as of May 27, 2014.

The difference between the common share consideration of \$555,698 thousand and the carry value of the Acquired Business of \$299,964 thousand is recognized as a Reserve from Common Control in Shareholders' equity, as follows:

(\$ thousands)	
Common Shares	\$ 555,698
Carrying Value of Net Assets Transferred	(299,964)
Reserve from Common Control	\$ 255,734

The amounts reported above are management's estimates using information available at the time of preparation of the financial statements. In accordance with the terms of the Purchase and Sale Agreement ("PSA"), the transaction is subject to closing adjustments which will be settled within 180 days of closing of the Acquisition. Any closing adjustments will result in an adjustment to the carrying amounts of assets and liabilities reported above.

## LIQUIDITY AND CAPITAL RESOURCES

(\$ thousands)	For the period from May 27, 2014 to June 30, 2014
Net Cash From (Used In)	
Operating Activities	\$ 26,886
Investing Activities	459
Financing Activities	(245)
Increase (Decrease) in Cash and Cash Equivalents	27,100
Cash and Cash Equivalents, End of Period	\$ 27,160

### OPERATING ACTIVITIES

Net cash from operating activities for the period from May 27, 2014 to June 30, 2014 was \$26,886 thousand. For the period May 27, 2014 to June 30, 2014, the net change in other assets and liabilities was an increase of \$284 thousand and the net change in non-cash working capital was a decrease of \$3,938 thousand.

The Company had working capital of \$57,535 thousand as at June 30, 2014. Accounts receivable and accrued revenues consist primarily of trade receivable and accrued revenues related to lease and royalty payments from third parties. Accounts payable and accrued liabilities consist primarily of freehold mineral tax, share-based compensation and salary related accruals.

### INVESTING ACTIVITIES

Net cash from investing activities for the period from May 27, 2014 to June 30, 2014 was \$459 thousand, representing proceeds from lease issuance bonuses related to leases issued for certain Fee Lands in exchange for a royalty payment on production from the related properties.

### FINANCING ACTIVITIES

#### Credit Facility

PrairieSky has in place an unsecured \$75 million extendible revolving credit facility (the "Revolving Facility"), with a permitted increase to \$125 million, (subject to certain conditions) and an unsecured \$25 million extendible operating credit facility (the "Operating Facility"), and together with the Revolving Facility, constitutes the "Credit Facility". The Credit Facility has a three-year term and, subject to certain

requirements, may be extendible annually. The Credit Facility is fully revolving up to maturity and may be extended or accelerated pursuant to the Credit Facility's terms and conditions. Maintenance costs for the period were \$27 thousand.

### Common Shares

On incorporation, the Company issued 100 common shares to Encana at a subscription price and stated capital of \$100 per common share. In connection with an internal reorganization involving the Company and Encana that was completed effective December 13, 2013, the Company issued an additional 25,000,000 common shares with a nominal stated capital to Encana for non-cash consideration, and subsequently paid certain cash dividends and dividends in-kind to Encana.

### Share Consolidation

On January 31, 2014, the Company amended its articles to effect a consolidation of its common shares, pursuant to which one new common share was issued for every 4,166.6833 outstanding common shares.

### Initial Public Offering

On May 22, 2014, a final prospectus was filed qualifying the distribution of 52,000,000 common shares which were sold by Encana pursuant to the terms of an underwriting agreement dated May 22, 2014 at a price of \$28.00 per common share which closed on May 29, 2014. On June 3, 2014, the underwriters exercised the over-allotment option resulting in an additional 7,800,000 common shares being sold by Encana at a price of \$28.00 per common share. The Company did not receive any proceeds from the IPO nor was it responsible for any fees or expenses of the IPO.

On May 29, 2014, the Company and Encana entered into, among other agreements: (i) a Governance Agreement, which will govern the various aspects of their relationship; and (ii) an Investor Liquidity Agreement, which will provide Encana or its transferee the ability to require the Company, among other things, to file future prospectuses in respect of the distribution of all or a portion of the common shares held by Encana or its transferee.

### Acquisition of Royalty Business

On May 22, 2014, the Company and Encana entered into the PSA for the acquisition of the Acquired Business from Encana, pursuant to which Encana received 129,994,000 common shares as consideration. Under the PSA, the legal stated capital maintained by the Company for the common shares issued to Encana was \$555,698 thousand. As part of the Acquisition, the Company and Encana entered into: (i) a Seismic Licence Agreement for which Encana granted the Seismic Licence to the Company; and (ii) Lease Issuance and Administration Agreements pursuant to which the Company issued leases to document Encana's retention of a working interest in respect of the Encana Development Properties purchased in the Acquisition and pursuant to which, the Company receives royalties from Encana.

Upon completion of the Acquisition, the Company and Encana entered into a Transition Services Agreement ("TSA") pursuant to which Encana will provide certain day-to-day administrative services required by the Company until December 31, 2014, subject to earlier termination in certain circumstances.

### Dividends

On June 18, 2014, the Board declared a dividend of \$0.1058 per common share payable on July 15, 2014 to common shareholders of record as of June 30, 2014.

## Capital Structure

The Company's objective when managing its capital structure is to maintain financial flexibility in order to distribute to shareholders cash after consideration of the Company's financial requirements for its operations and fund growth opportunities.

The Company's capital structure is comprised of shareholders' equity and working capital. The Company's capital structure is managed by taking into account operating activities, dividends paid to shareholders, taxes, available credit facility, share issuance costs and other factors. The Company's operating results and capital structure is impacted by the level of development activity by third parties on the Royalty Properties and the resultant royalty revenues, level of costs incurred by the Company and commodity prices.

Management of the Company's capital structure is managed through its financial and operating forecast process. The forecast of the Company's future cash flows is based on estimates of production, crude oil, natural gas and NGL prices, freehold mineral tax expense, general and administrative expense and other investing and financing activities. The forecast is regularly updated based on changes in commodity prices, production expectations and other factors that in the Company's view would impact cash flow.

## COMMITMENTS AND CONTINGENCIES

### CONTRACTUAL COMMITMENTS

(\$ thousands) (undiscounted)	Expected Future Payments					Total
	2014	2015	2016	2017	Thereafter	
Information Technology	\$ 173	\$ 101	\$ 3	\$ -	\$ -	\$ 277
Office Lease	391	821	287	-	-	1,499
Commitments	\$ 564	\$ 922	\$ 290	\$ -	\$ -	\$ 1,776

The table above outlines the Company's contractual obligations at June 30, 2014.

### CONTINGENCIES

In the normal course of operations, the Company may become party to litigation. There are no known claims that the Company has determined are subject to accrual or disclosure.

### TRANSACTIONS WITH RELATED PARTIES

Concurrently with completion of the Acquisition and before closing of the IPO, the Company and Encana entered into a number of agreements: (i) Lease Issuance and Administration Agreements pursuant to which the Company will issue leases to document Encana's retention of a working interest in respect of certain Fee Lands purchased in the Acquisition and pursuant to which, the Company will receive royalties from Encana; (ii) TSA pursuant to which Encana will provide or arrange for the provision of certain day-to-day administrative services required by the Company, until December 31, 2014, subject to earlier termination in certain circumstances. These transactions were in the normal course of operations and were measured at the exchange amount.

The Company has the following related party transactions with Encana:

	For the period from May 27, 2014 to June 30, 2014
Royalties and lease rentals revenues	\$ 6,082
Office lease rental	102
Services under transition services agreement	8
	\$ 5,972

Amount recognized on the Statement of Earnings include:

Revenues	\$	6,082
Administrative		110
	\$	5,972

Amounts recognized on the Balance Sheet include:

	As at June 30, 2014	As at December 31, 2013
Accounts receivable and accrued revenues	\$ 926	\$ -
Prepaid expense	70	-
Dividend payable	(7,427)	-
	\$ (6,431)	\$ -

Certain Directors of the Company are common Directors with those of Encana.

## RISK MANAGEMENT

The Royalty Properties expose the Company to some of the same industry risks and conditions faced by all oil and gas companies. The most significant are those that directly impact production volumes and commodity pricing and include the following:

### OPERATING RISK

- Fluctuations in commodity prices and quality differentials as a result of weather patterns, world and North American market forces or shifts in the balance between supply and demand for crude oil, NGLs and natural gas;
- Access to pipelines or other transportation methods for bringing crude oil, NGLs and natural gas to market;
- Variations in currency exchange rates relative to commodity prices;
- Imprecision of reserve estimates and uncertainty of depletion and recoverability of reserves. The reserves will deplete over time through continued production and the Company, industry partners and royalty payors may not be able to replace these reserves on an economic basis;
- Industry activity levels and intense competition for land, goods and services, and qualified personnel;
- Stock market volatility and the ability to access sufficient capital from internal and external sources;
- Risk associated with volatility in global financial markets;
- Risk associated with the Credit Facility, including compliance with the agents and related covenants;
- Operational or marketing risks resulting in delivery interruptions, delays or unanticipated production declines;
- Changes in government regulations, taxation, and royalties; and
- Safety and environmental risks.

The Company employs the following strategies to mitigate these risks, including:

- Not undertaking any direct development or operational activities associated with production;
- An auditing program to collect royalties on production from the Royalty Properties in accordance with the terms of the various leases and agreements;

- Maintaining a focus on controlling costs to maximize profitability;
- A conservative approach to debt as demonstrated in the absence of any current debt issuance or use of the Credit Facility; and
- An active contract management strategy to ensure appropriate allocation of risk and adherence to all terms and conditions by counterparties.

## FINANCIAL RISKS

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The Company is exposed to financial risks arising from its financial liabilities. Financial risks include market risk (commodity prices and interest rates), credit risk and liquidity risks.

### Commodity Price Risk

Commodity price risk is the risk the Company will encounter fluctuations in the fair value of future cash flows with changes in commodity prices. Commodity prices for crude oil, NGL and natural gas are influenced by macroeconomic events that dictate the levels of supply and demand.

### Interest Rate Risk

Interest rate risk arises from changes in market interest rates that may affect the fair value or future cash flows from the Company's financial assets or liabilities. The Company may partially mitigate its exposure to interest rate changes by holding a mix of both fixed and floating rate debt.

### Credit Risk

Credit risk arises from the potential that the Company may incur a loss if a counterparty to a financial instrument fails to meet its obligation in accordance with agreed terms. The Company's diversified revenue stream limits the size of any one property or industry operator with respect to total receivables.

The Company maintains an auditing program to ensure that royalties are paid correctly on production from the Royalty Properties in accordance with the prices obtained by the royalty payor and that unwarranted or excessive deductions are not being taken.

A substantial portion of the Company's accounts receivable are from leases and other agreements with oil and gas industry operators and are subject to normal industry credit risks.

As at June 30, 2014, the Company had no counterparties whose accounts receivable individually accounted for more than 10% of the total accounts receivable balance. The maximum credit risk exposure associated with accounts receivable and accrued revenues is the total carrying value. For the period presented, the Company does not have an allowance for doubtful accounts nor provide for any doubtful accounts as there is negligible history of default.

### Liquidity Risk

Liquidity risk arises from the inability to meet general funding needs, in part due to accounts receivable from lessees typically being settled in the following months, and to manage the assets, liabilities, and capital structure of the Company. Liquidity risk is the risk that the Company will encounter difficulties in meeting a demand to fund its financial liabilities as they come due. The Company has access to funding alternatives through the Credit Facility. Liquidity risk is managed by maintaining sufficient liquid financial resources to fund obligations as they come due.

The Company's sources of liquidity include cash and cash equivalents, working capital funds and operating and revolving credit facilities. The primary use of funds are dividends, freehold mineral taxes, administrative expenses and cash taxes.

## ENVIRONMENTAL REGULATION AND RISK

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The oil and gas industry is subject to environmental regulations pursuant to provincial and federal legislation. Such legislation provides for restrictions and prohibitions on the release or emission of various substances produced in association with certain oil and gas industry operations. In addition, such legislation requires that well and facility sites be abandoned and reclaimed to the satisfaction of regulatory authorities. Liability for abandonment and reclamation costs on the Royalty Properties rests with the third party lessees.

Compliance with such legislation can require significant expenditures and a breach of such requirements may result in suspension or revocation of necessary licenses and authorizations, civil liability for pollution damage, and the imposition of material fines and penalties. It is reasonably likely that the trend towards stricter standards in environmental legislation and regulation will continue. Given the evolving nature of the debate related to climate change and the control of greenhouse gases and resulting requirements, it is not possible to predict the impact of those requirements on our operations and financial condition.

## ACCOUNTING POLICIES AND ESTIMATES

### CRITICAL ACCOUNTING ESTIMATES

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Management is required to make judgments, assumptions and estimates through the application of the Company's accounting policies and practices, which have a significant impact on the financial results. A summary of PrairieSky's significant accounting policies can be found in Note 3 to the Interim Condensed Financial Statements for the period May 27, 2014 to June 30, 2014. The following discussion outlines the accounting policies and practices involving the use of estimates that are critical to determining PrairieSky's financial results.

#### Reserve Estimates, Depletion and Impairments

Reserve estimates can have a significant impact on net earnings, as they are a key input to DD&A calculations and impairment tests. Costs accumulated within each area are depleted using the unit-of-production method based on proved and probable reserves using estimated future prices and costs. Costs subject to depletion include estimated future costs to be incurred in developing proved and probable reserves. A downward revision in reserves estimates could result in the recognition of a higher DD&A charge to net earnings.

PrairieSky's Property, Plant and Equipment relating to crude oil, NGLs and natural gas plus other mineral rights and exploration and evaluation costs, are aggregated into cash generating units ("CGUs") based on their ability to generate largely independent cash flows. If the carrying value of the CGU exceeds the recoverable amount, the CGU is written down with an impairment recognized in net earnings. The recoverable amount of the CGU is the greater of its fair value less costs of disposal and its value in use. Fair value less costs of disposal may be determined using after-tax discounted future net cash flows of proved and probable reserves using forecast prices and costs. Value in use is determined by estimating the present value of the future net cash flows expected to be derived from continued use of the CGU. A downward revision in reserves estimates could result in the recognition of impairments charged to net earnings. Upon assessment of the Royalty Properties, the Company has one CGU.

Reversals of impairments are recognized when there has been a subsequent increase in the recoverable amount. In this event, the carrying amount of the asset or CGU is increased to its revised recoverable amount with an impairment reversal recognized in net earnings.

All of PrairieSky's oil and gas reserves and resources are evaluated and reported on by independent qualified reserves evaluators ("IQRE"). The estimation of reserves is a subjective process. Forecasts are based on engineering data, projected future rates of production, estimated commodity price forecasts and future costs, all of which are subject to numerous uncertainties and various interpretations. Accordingly the impact of changes in reserves estimates on the Company's financial statements could be material.

## Oil and Gas Revenue Accruals and Royalty Interests

PrairieSky follows the accrual method of accounting, making estimates in the financial and operating results. This may include estimates of revenues, royalties, production and other expenses and capital items related to the period being reported, for which actual results have not yet been received. These accrual estimates are expected to be revised, based on the receipt of actual results. The Company has no operational control over the Fee Lands, as a result, the Company uses lessee information which is matched to government reporting databases and historical receipts to estimate revenue accruals.

## Share-Based Compensation

The Company's share-based compensation plans include an Incentive Stock Option Plan, Restricted Share Unit ("RSU") Plan, Performance Share Unit ("PSU") Plan, and a Deferred Share Unit ("DSU") Plan. Obligations for payments of cash or common shares under the Company's long term incentive plans are accrued over the vesting period using fair values. Judgments include which valuation model is most appropriate for the grant of the award to estimate its fair value. Estimates and assumptions are then used in the valuation model to determine the fair value.

For equity-settled compensation plans, including stock options, fair values are determined at the grant date and are recognized over the vesting period as compensation costs with a corresponding credit to Shareholder's Equity. The Company uses the Black-Scholes option pricing model which requires that management make assumptions for the expected life of the option, the anticipated volatility of the share price over the life of the option, the risk-free interest rate for the life of the option, and the number of options that will ultimately vest. The assumptions used by the Company are discussed in Note 16 to the Interim Condensed Financial Statements.

For cash-settled compensation plans, fair values are determined at each reporting date and periodic changes are recognized as compensation costs with a corresponding change in liabilities. The fair value of RSUs at grant date are estimated based on the volume weighted average trading price on the TSX of five trading days prior to one business day prior to the date of grant, except for the initial grant which was based on the IPO price. Judgment is also required to estimate the number of restricted share units that will ultimately vest.

PSUs, RSUs and DSUs are accounted for as liability instruments and are remeasured at fair value based on the market value of the Company's common shares at each reporting date.

## Goodwill

Upon acquisition, goodwill is attributed to the applicable CGU that is expected to benefit from the business combination's synergies. This represents the lowest level that goodwill is monitored for internal management purposes. Subsequent measurement of goodwill is at cost less any accumulated impairments.

Goodwill is assessed for impairment at least annually. If the goodwill carrying amount for the CGU exceeds the recoverable amount of the CGU, the associated goodwill is written down with an impairment recognized in net earnings. The recoverable amounts are determined annually based on the greater of fair value less costs of disposal or value in use. Fair value less costs of disposal is derived by estimating the discounted after-tax future net cash flows for the CGU. Discounted future net cash flows are based on forecast commodity prices and costs over the expected economic life of the proved and probable reserves and discounted using market-based rates. Value in use is determined by estimating the present value of the future net cash flows expected to be derived from the continued use of the CGU. Goodwill impairments are not reversed.

The Company's reserves are evaluated annually by our IQRE. The cash flows used in determining the receivable amount are based on information contained in the IQRE reports and management's assumptions provided therein.

## Income Taxes

Income tax is recognized in net earnings except to the extent that it relates to items recognized directly in Shareholders' Equity, in which case the income tax is recognized directly in Shareholders' Equity. Current income taxes are measured at the amount expected to be recoverable from or payable to the taxation authorities based on the income tax rates enacted or substantively enacted at the end of the reporting period.

The Company follows the liability method of accounting for income taxes. Under this method, deferred income taxes are recorded for the effect of any temporary difference between the accounting and income tax basis of an asset or liability.

Deferred income tax is calculated using the enacted or substantively enacted income tax rates expected to apply when the assets are realized or liabilities are settled. The effect of a change in the enacted or substantively enacted tax rates is recognized in net earnings or in Shareholders' Equity depending on the item to which the adjustment relates.

Deferred income tax liabilities and assets are not recognized for temporary differences arising on:

- the initial recognition of goodwill; or
- the initial recognition of an asset or liability in a transaction which is not a business combination and, at the time of the transaction, affects neither accounting net earnings nor taxable earnings.

Deferred income tax assets are recognized to the extent future recovery is probable. Deferred income tax assets are reduced to the extent that it is no longer probable that sufficient taxable earnings will be available to allow all or part of the asset to be recovered.

Related to the Acquisition under common control, the Company qualifies for the initial recognition exemption under IAS 12 "Income Taxes" and a deferred tax asset will not be recognized related to the excess of the tax pools acquired relative to the carrying value of the net assets transferred. The unrecognized deferred income tax asset is being amortized based on the net tax pool and DD&A claims calculated for the period.

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

## RECENT ACCOUNTING PRONOUNCEMENTS

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### New Pronouncements Adopted

On January 1, 2014, the Company adopted the following accounting standards updates issued by the International Accounting Standards Board ("IASB"), which have not had a material impact on the Interim Condensed Financial Statements:

- IAS 32, "Financial Instruments: Presentation" was amended to clarify requirements for offsetting financial instruments in the balance sheet. The amendment requires that the right to offset must be available on the current date and cannot be contingent on a future event. The standard has been applied retrospectively.
- International Financial Reporting Interpretations Committee 21, "Levies" provides guidance for accounting for levies that fall under the scope of IAS 37, Provisions, Contingent Liabilities and Contingent Assets. The interpretation requires that obligations arising from levies imposed through

legislation by governments are recognized when the triggering event or activity specified in the legislation occurs. The standard has been applied retrospectively.

### **New Standards Issued Not Yet Adopted**

On December 16, 2011, the IASB issued IFRS 9, “Financial Instruments”, which replaces IAS 39, “Financial Instruments: Recognition and Measurement”. The new standard replaces the current multiple classification and measurement models for financial assets and liabilities with a single model that has only two classification categories: amortized cost and fair value. The classification and measurement requirements will be applied retrospectively upon adoption of the standard. In November 2013, IFRS 9 and IFRS 7 “Financial Instruments: Disclosures”, were amended to include a new hedge accounting model that better reflects risk management activities in the financial statements of entities that elect to apply hedge accounting. This amendment to IFRS 9 also removes the previous mandatory effective date of January 1, 2015. The new effective date of IFRS 9 will be determined when the impairment phase of the project is completed. These new standards and amendments are not expected to have a material impact on the Company’s Financial Statements.

On May 12, 2014, the IASB issued “Clarification of Acceptable Methods of Depreciation and Amortization” which amends IAS 16 “Property, Plant and Equipment” and IAS 38 “Intangible Assets”. The amendments to IAS 16 clarify that use of revenue-based methods to calculate the depreciation of property, plant and equipment is not appropriate as revenue also includes factors other than the consumption of the economic benefits derived from the asset. The amendments to IAS 38 state that revenue is not an appropriate basis for amortization of intangible assets, except in limited circumstances. These amendments will apply prospectively, effective January 1, 2016 and early application is permitted. The amendment is not expected to have a material impact on the Company’s Financial Statements.

On May 28, 2014, the IASB issued IFRS 15, “Revenue from Contracts with Customers” which is the result of the joint project with Financial Accounting Standards Board. The new standard replaces the two main recognition standards IAS 18, “Revenue” and IAS 11, “Construction Contracts”. The new standard provides a five step model framework as a core principal upon which an entity recognizes revenue and becomes effective January 1, 2017. The Company is currently assessing the potential impact of the standard on the Company’s Financial Statements.

### **CHANGE IN ACCOUNTING ESTIMATE**

On May 27, 2014, the Company began depleting crude oil, NGL, and natural gas properties using the unit-of-production method over their proved plus probable reserves on a prospective basis. The previous policy was to deplete using the unit-of production method over the proved reserves. The change in estimate was made as proved plus probable reserves better reflects the estimated remaining service life of the related assets. For the period from May 27, 2014 to June 30, 2014 the Company recorded \$928 thousand lower depletion expense than it would have recorded using proved reserves. Based on the reserves at the date of change in estimate, the effect reduced depletion by \$1.64 per BOE. It is not practical for the Company to estimate the effect on depletion expense for future periods.

### **NON-GAAP MEASURES**

Certain measures in this document do not have any standardized meaning as prescribed by IFRS and therefore, are considered non-GAAP measures. These measures may not be comparable to similar measures presented by other issuers. These measures are commonly used in the oil and gas industry and by the Company to provide potential investors with additional information regarding the Company’s liquidity and its ability to generate funds to finance its operations. Non-GAAP measures include Operating Cash Flow, Netback, Funds from Operations, Net Earnings and Comprehensive Income Adjusted Per Share basic and diluted, Funds from Operations Adjusted Per Share basic and diluted. Management’s use of these measures is discussed further below.

“Operating Cash Flow” represents the cash margin for product sold. Operating Cash Flow is calculated as revenues, less freehold mineral taxes and administrative expenses. Operating Cash Flow provides a consistent measure of the cash generating performance for product sold to assess the comparability of the underlying performance between years.

“Netback” represents the cash margin for product sold on a BOE basis. Netback is calculated using Operating Cash Flow, excluding other revenues, on a per BOE basis. Netback is used to assess the ability to provide cash generating performance per unit of product sold. Netback measures are commonly used in the oil and gas industry to assess performance comparability. Refer to Operating Results table in this MD&A document for a summary of the reporting period’s netback summary.

## FUNDS FROM OPERATIONS

Funds from operations is used to evaluate the ability of the Company to generate cash from operations, as PrairieSky intends to distribute the majority of its cash flow on an ongoing basis to shareholders as dividends. Such a measure provides a useful tool of the Company’s operations on an ongoing basis by eliminating certain non-cash charges. Funds from Operations is defined as cash from operating activities including net change in non-cash working capital, lease issuance bonuses, capital expenditures and financing costs. Below is a reconciliation of funds from operations to cash from (used in) operating activities, which is the most comparable IFRS measure.

<i>(\$ thousands)</i>	<b>For the period from May 27, 2014 to June 30, 2014</b>
Cash From (Used in) Operating Activities	\$ 26,886
(Add back) deduct:	
Net Change in Non-cash Working Capital	(3,938)
Lease Issuance Bonus	(459)
Capital Expenditures	-
Financing Costs	245
<b>Funds From Operations</b>	<b>\$ 31,038</b>

## ADJUSTED PER SHARE CALCULATIONS – BASIC AND DILUTED

Adjusted Per Share calculations provide a better measure of the Company’s performance given the fact that the Company was in existence since January 1, 2014, but only commenced operations on May 27, 2014. Adjusted Basic Shares outstanding reflect the shares issued and outstanding as at June 30, 2014 which were 130,000,000 and Adjusted Diluted Shares outstanding reflect the impact of stock options. Below is a computation of Net Earnings Adjusted Per Share basic; Net Earnings Adjusted Per Share diluted; Funds from Operations Adjusted Per Share basic; Funds from Operations Adjusted Per Share diluted. Calculation of Earnings Per Share is disclosed in Note 15 of the Interim Condensed Financial Statements.

### Adjusted Net Earnings and Comprehensive Income Per Share

The following table presents the computation of Net Earnings per adjusted common share:

	<b>For the period from May 27, 2014 to June 30, 2014</b>
Net Earnings	\$ 23,907
Number of common shares:	
Common shares outstanding – basic	130,000
Effect of dilutive securities	124
Common shares outstanding – diluted	130,124
Adjusted Net Earnings per Common Share	
Basic <sup>(1)</sup>	\$ 0.18
Diluted <sup>(2)</sup>	\$ 0.18

(1) Adjusted Net Earnings per common share is calculated using the number of PrairieSky common shares outstanding as at June 30, 2014.

(2) Adjusted Net Earnings per common share is calculated using the number of PrairieSky common shares outstanding as at June 30, 2014, giving effect to stock options.

## Adjusted Funds from Operations Per Share

The following table presents the computation of Funds from Operations per adjusted common share:

	<b>For the period from May 27, 2014 to June 30, 2014</b>
Funds from Operations	\$ 31,038
Number of common shares:	
Common shares outstanding – basic	130,000
Effect of dilutive securities	124
Common shares outstanding – diluted	130,124
Adjusted Funds from Operations per Common Share	
Basic <sup>(1)</sup>	\$ 0.24
Diluted <sup>(2)</sup>	\$ 0.24

(1) Adjusted Funds from Operations per common share is calculated using the number of PrairieSky common shares outstanding as at June 30, 2014.

(2) Adjusted Funds from Operations per common share is calculated using the number of PrairieSky common shares outstanding as at June 30, 2014, giving effect to stock options.

### FORWARD-LOOKING STATEMENTS

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This document includes certain statements regarding PrairieSky's future plans and operations as at July 21, 2014, and contains forward-looking statements that we believe allow readers to better understand our business and prospects. Forward-looking statements contained in this MD&A include our expectations with respect to the following:

- commodity prices including supply and demand factors relating to crude oil, natural gas and natural gas liquids;
- expected future commitments and payments related thereto;
- the potential impact of the final statement of adjustments to be performed in accordance with the PSA with Encana;
- PrairieSky's business and growth strategy and anticipated sources of future income;
- industry drilling, development and licensing activity on our Royalty Properties, our exposure in emerging opportunities, and the potential impact of thereof on production and reserves;
- possible revisions to accrued estimates based on receipt of actual results;
- expected impacts of accounting standards, including those announced but not yet adopted;
- the expectation that there will be no operating costs, capital costs, environmental liabilities, or abandonment and reclamation obligations associated with development of the Royalty Properties;
- estimated general and administrative expenses;
- average production and contribution from the Royalty Properties; and
- amounts and rates of income taxes and timing of payment thereof.

By their nature, forward-looking statements are subject to numerous risks and uncertainties, some of which are beyond our control, including the impact of general economic conditions, industry conditions, volatility of commodity prices, lack of pipeline capacity, currency fluctuations, imprecision of reserve estimates, royalties, environmental risks, taxation, regulation, changes in tax or other legislation, competition from other industry participants, the lack of availability of qualified personnel or management, stock market volatility, and our ability to access sufficient capital from internal and external sources. In addition, PrairieSky is subject to numerous risks and uncertainties in relation to Encana, which owns a majority of PrairieSky's common shares. These risks and uncertainties include risks relating to Encana's shareholdings, the provision of certain transitional services by Encana, the potential for conflicts of interest and disputes to arise with Encana, limited ability to recover indemnification from Encana under the PSA, and other certain agreements, and future changes in the relationship with Encana. The foregoing and other risks are described in more detail in PrairieSky's final prospectus dated May 22, 2014 and in this MD&A under the heading "Risk Management".

With respect to forward-looking statements contained in this MD&A, we have made assumptions regarding, among other things, Encana's level of ownership of common shares; the ability of the lessees and working interest owners on the Royalty Properties to maintain or increase production and reserves from these properties; the ability and willingness of the lessees and working interest owners on the Royalty Properties to comply with, and PrairieSky to enforce, lease terms and contractual provisions, as applicable, in order to receive payments; the ability of the lessees or working interest owners on the Royalty Properties to operate in a safe, efficient and effective manner; the timely receipt of any required regulatory approvals by lessees or working interest owners on the Royalty Properties; the willingness and financial capability of the lessees and working interest owners to continue to develop and invest additional capital in the Royalty Properties; the ability of the lessees and working interest owners on the Royalty Properties to obtain financing on acceptable terms to fund capital expenditures; field production rates, decline rates and the well

performance and characteristics of the Royalty Properties; the ability to replace and increase crude oil, natural gas and NGL reserves and production associated with the Royalty Properties through acquisitions and third party development; the timing, cost and ability of third parties to access, maintain or expand necessary facilities and/or secure adequate product transportation and storage; the ability of the operators of the properties in which PrairieSky has a royalty interest in, to successfully market their respective petroleum and natural gas products or, for royalty payments taken-in-kind by PrairieSky, if any, the ability of PrairieSky or a third party marketer to successfully market PrairieSky's in-kind petroleum and natural gas products; surface rights access being granted to third parties on PrairieSky's properties; the benefits of the seismic data anticipated to be used by PrairieSky and sub-licensed to lessees on the PrairieSky's properties; the level of costs and expenses to be incurred by PrairieSky, including with respect to interest, general and administrative expenses and income tax expenses; the ability of PrairieSky to obtain and retain qualified staff and services in a timely and cost efficient manner; the absence of any material litigation or claims against PrairieSky; the general stability of the economic and political environment and the regulatory framework regarding royalties, taxes and environmental matters in the jurisdictions in which PrairieSky has an interest in oil and natural gas properties; and future crude oil, natural gas and NGL prices and currency, exchange and interest rates.

Readers and investors are cautioned that the assumptions used in the preparation of such forward looking information and statements, although considered reasonable at the time of preparation, may prove to be imprecise and, as such, undue reliance should not be placed on forward-looking statements. Our actual results, performance, or achievement could differ materially from those expressed in, or implied by, these forward-looking statements. We can give no assurance that any of the events anticipated will transpire or occur, or if any of them do, what benefits we will derive from them. Statements relating to "reserves" are deemed to be forward-looking statements as they involve the implied assessment, based on certain estimates and assumptions that the reserves described can be profitably produced in the future. Readers are cautioned that the foregoing lists of factors are not exhaustive.

**Any forward-looking statement is made only as of the date of this MD&A, and PrairieSky undertakes no obligation to update or revise any forward-looking statement or statements to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events, except as required by applicable securities laws. New factors emerge from time to time, and it is not possible for PrairieSky to predict all of these factors or to assess in advance the impact of each such factor on PrairieSky's business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward looking statements.**

**The forward-looking information contained in this document is expressly qualified by this cautionary statement.**

You are further cautioned that the preparation of financial statements in accordance with IFRS requires management to make certain judgments and estimates that affect the reported amounts of assets, liabilities, revenues, and expenses. These estimates may change, having either a positive or negative effect on net income, as further information becomes available and as the economic environment changes.

#### **CONVERSIONS OF NATURAL GAS TO BOE**

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To provide a single unit of production for analytical purposes, natural gas production and reserves volumes are converted mathematically to equivalent barrels of oil (BOE). We use the industry-accepted standard conversion of six thousand cubic feet of natural gas to one barrel of oil (6 Mcf = 1 bbl). The 6:1 BOE ratio is based on an energy equivalency conversion method primarily applicable at the burner tip. It does not represent a value equivalency at the wellhead and is not based on either energy content or current prices. While the BOE ratio is useful for comparative measures and observing trends, it does not accurately reflect individual product values and might be misleading, particularly if used in isolation. As well, given that the value ratio, based on the current price of crude oil to natural gas, is significantly different from the 6:1 energy equivalency ratio, using a 6:1 conversion ratio may be misleading as an indication of value.

## CURRENCY AND REFERENCES TO PRAIRIESKY

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All information included in this document, and the Interim Condensed Financial Statements is shown on a Canadian dollar basis. All proceeds from divestitures are provided on a before-tax basis.

For convenience, references in this document to the “Company”, “we”, “us”, “our”, and “its” may, where applicable, refer only to PrairieSky.

## ADDITIONAL INFORMATION

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Additional information about PrairieSky, including PrairieSky’s interim MD&A and unaudited Interim Condensed Financial Statements and notes thereto, and PrairieSky’s final prospectus dated May 22, 2014, is available on SEDAR at [www.sedar.com](http://www.sedar.com) or PrairieSky’s website at [www.prairiesky.com](http://www.prairiesky.com).