



Condensed Interim Consolidated Financial Statements

Nine Month Period Ended

September 30, 2019

(Unaudited)

(Expressed in Canadian Dollars)

NOTICE TO READER

The accompanying unaudited condensed interim consolidated financial statements have been prepared by and are the responsibility of the management.

The Company's independent auditor has not performed a review of these financial statements in accordance with the standards for a review of interim financial statements by an entity's auditor.

HILLCREST PETROLEUM LTD.**Condensed Interim Consolidated Statements of Financial Position**

(Expressed in Canadian dollars)

(Unaudited)

	September 30,	December 31,
	2019	2018
	(\$)	(\$)
ASSETS		
Current assets		
Cash	27,063	21,348
Receivables	361,316	38,505
Prepaid expenses	103,878	90,689
Total current assets	492,257	150,542
Non-current assets		
Exploration and evaluation assets (Note 4)	-	964,881
Property and equipment (Note 5)	741,882	-
TOTAL ASSETS	1,234,139	1,115,423
LIABILITIES		
Current liabilities		
Accounts payable and accrued liabilities (Note 6)	2,314,258	1,452,044
Loans (Notes 7 and 8)	974,827	1,012,241
Embedded derivative liability (Note 7)	52,500	52,500
Current portion of decommissioning liability (Note 11)	23,458	34,564
Total current liabilities	3,365,043	2,551,349
Convertible debentures (Note 9)	706,092	690,646
Other liability (Note 9)	116,000	116,000
Decommissioning liability (Note 11)	436,819	429,920
TOTAL LIABILITIES	4,623,954	3,787,915
SHAREHOLDERS' DEFICIENCY		
Share capital (Note 12)	7,812,201	7,681,347
Contributed surplus (Note 12)	1,351,661	1,350,917
Reserves (Note 12)	249,463	167,473
Deficit	(12,803,140)	(11,872,229)
	(3,389,815)	(2,672,492)
TOTAL LIABILITIES & SHAREHOLDERS' DEFICIENCY	1,234,139	1,115,423

Nature of operations and going concern (Note 1)**Commitments (Note 13)****Subsequent events (Note 18)**

On behalf of the Board of Directors:

"Michael Krzus"
Director

"Thomas Milne"
Director

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

HILLCREST PETROLEUM LTD.**Condensed Interim Consolidated Statements of Loss and Comprehensive Loss**

(Expressed in Canadian dollars)

(Unaudited)

	Three Month Period Ended September 30, 2019	Three Month Period Ended September 30, 2018	Nine Month Period Ended September 30, 2019	Nine Month Period Ended September 30, 2018
	(\$)	(\$)	(\$)	(\$)
Revenue				
Oil sales	377,620	10,759	716,828	55,995
Royalties	(104,930)	(4,155)	(188,522)	(4,372)
	272,690	6,604	528,306	51,623
Expenses				
Operating costs	252,936	20,831	458,679	111,271
Consulting fees (Note 10)	98,222	9,485	285,294	110,335
Depletion and depreciation (Note 5)	85,300	-	159,131	-
Office and general	98,090	134,351	331,267	446,283
Share-based payments (Note 12)	-	3,223	744	44,821
	534,548	167,890	1,235,115	712,710
Loss from operations	(261,858)	(161,286)	(706,809)	(661,087)
Change in fair value of loan conversion liability (Note 7)	-	32,700	-	64,500
Financing expenses (Notes 7 and 8)	(62,545)	(55,288)	(226,375)	(207,507)
Impairment of oil and gas properties (Note 5)	-	-	-	(202,525)
Foreign exchange gain	(251)	1,054	2,273	(626)
Net loss for the period	(324,654)	(182,820)	(930,911)	(1,007,245)
Item that may be subsequently reclassified to net loss				
Exchange differences on translating foreign operations	3	17	(10)	273
Comprehensive loss for the period	(324,651)	(182,803)	(930,921)	(1,006,972)
Basic and diluted loss per share	(0.00)	(0.00)	(0.01)	(0.01)
Weighted average common shares outstanding:				
Basic	91,217,270	87,293,226	89,366,486	84,227,589
Diluted	91,217,270	87,293,226	89,366,486	84,227,589

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

HILLCREST PETROLEUM LTD.

Condensed Interim Consolidated Statements of Changes in Shareholders' Deficiency

(Expressed in Canadian dollars)

(Unaudited)

	Share Capital		Reserves				Shareholders' Deficiency
	Number of Shares	Amount	Contributed Surplus	Warrants	Foreign Currency Translation	Deficit	
		(\$)	(\$)	(\$)	(\$)	(\$)	(\$)
Balance at December 31, 2017	74,876,226	7,029,436	1,345,420	47,550	123,081	(10,005,694)	(1,460,207)
Proceeds from private placement	9,992,000	499,600	-	-	-	-	499,600
Exercise of stock options	725,000	84,559	(41,059)	-	-	-	43,500
Shares issued to settle debts	1,700,000	85,000	-	-	-	-	85,000
Vesting of stock options	-	-	44,821	-	-	-	44,821
Comprehensive loss for the period	-	-	-	-	273	(1,007,245)	(1,006,972)
Balance at September 30, 2018	87,293,226	7,698,595	1,349,182	47,550	123,354	(11,012,939)	(1,794,258)
Share issuance costs	-	(17,248)	-	-	-	-	(17,248)
Vesting of stock options	-	-	1,735	-	-	-	1,735
Comprehensive loss for the period	-	-	-	-	(3,431)	(859,290)	(862,721)
Balance at December 31, 2018	87,293,226	7,681,347	1,350,917	47,550	119,923	(11,872,229)	(2,672,492)
Proceeds from private placement	4,300,000	137,000	-	78,000	-	-	215,000
Share issuance costs	-	(6,146)	-	4,000	-	-	(2,146)
Vesting of stock options	-	-	744	-	-	-	744
Comprehensive loss for the period	-	-	-	-	(10)	(930,911)	(930,921)
Balance at September 30, 2019	91,593,226	7,812,201	1,351,661	129,550	119,913	(12,803,140)	(3,389,815)

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

HILLCREST PETROLEUM LTD.**Condensed Interim Consolidated Statements of Cash Flows**

(Expressed in Canadian dollars)

(Unaudited)

	Nine Month Period Ended September 30, 2019	Nine Month Period Ended September 30, 2018
	(\$)	(\$)
Net loss for the period	(930,911)	(1,007,245)
Adjusted for items not involving cash:		
Accretion expense	34,751	42,197
Accrued interest expense	37,743	28,452
Change in fair value of loan conversion liability	-	(64,500)
Depletion and depreciation	159,131	-
Impairment of oil and gas properties	-	202,525
Share-based payments	744	44,821
Unrealized foreign exchange loss	-	261
Changes in non-cash working capital:		
Prepaid expenses	(109,298)	106,625
Receivables	(322,812)	12,947
Accounts payable and accrued liabilities	958,099	271,593
Cash flows used in operating activities	(172,553)	(362,324)
Proceeds from disposal of oil and gas properties	170,000	-
Exploration and evaluation expenditures	(106,132)	(114,163)
Cash flows provided by investing activities	63,868	(114,163)
Proceeds from private placement	195,000	445,600
Proceeds from convertible debentures	55,000	-
Proceeds from exercise of stock options	-	35,000
Share subscriptions received in advance	15,000	-
Share issuance costs	(2,146)	-
Proceeds from loans	-	37,000
Repayment of loans	(148,444)	(98,049)
Cash flows provided by financing activities	114,410	419,551
Change in cash	5,725	(56,936)
Effect of exchange rate changes on cash denominated in a foreign currency	(10)	12
Cash, beginning of the period	21,348	59,186
Cash, end of the period	27,063	2,262

Supplemental cash flow information (Note 17)

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

Hillcrest Petroleum Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
Nine Month Period Ended September 30, 2019
(Unaudited - Expressed in Canadian dollars)

1. NATURE OF OPERATIONS AND GOING CONCERN

Hillcrest Petroleum Ltd. (the "Company") was incorporated on May 2, 2006 under the Business Corporations Act of British Columbia, and is in the business of acquiring, exploring and developing exploration interests in oil and gas projects located in North America. The Company's registered office is suite 1300 - 1030 West Georgia Street, Vancouver, BC, V6E 2Y3. The Company's shares are listed for trading on the TSX Venture Exchange ("TSXV") under the symbol "HRH" and on the OTC pink sheets under the symbol "HLRTF".

The Company is subject to several categories of risk associated with the exploration and development of oil and gas resources. Oil and gas exploration and production is a speculative business, and involves a high degree of risk. Among the factors that have a direct bearing on the Company's prospects are uncertainties inherent in estimating oil and gas reserves, future hydrocarbon production, and cash flows, particularly with respect to wells that have not been fully tested and with wells having limited production histories; access to additional capital; changes in the price of oil and gas; availability and cost of services and equipment; and the presence of competitors with greater financial resources and capacity.

These consolidated financial statements have been prepared on the basis of a going concern, which contemplates the realization of assets and the discharge of liabilities in the normal course of business for the foreseeable future. The Company recorded a net loss of \$929,877 (2018 - \$1,007,245), an accumulated deficit of \$12,802,106 (December 31, 2018 - \$11,872,229) and had a working capital deficiency of \$2,873,413 (December 31, 2018 - \$2,400,807) as at and for the nine month period ended September 30, 2019. The Company is currently in default on certain loans, but continues to accrue interest in accordance with the terms of the agreements (Note 7). The Company's ability to meet its obligations as they fall due and to continue to operate as a going concern is dependent on the continued financial support of its creditors and its shareholders and ultimately, the attainment of profitable operations. There is no certainty that the Company will continue to produce revenue due to the inherent production risks associated with the oil and natural gas industry. In the past, the Company has relied on sales of equity securities, debt instruments and asset sales to meet its cash requirements. There can be no assurance that funding from this or other sources will be sufficient in the future to satisfy operational requirements and cash commitments. Even if the Company is able to obtain new financing, it may not be on commercially reasonable terms or terms that are acceptable to it. Failure to obtain such financing on a timely basis could cause the Company to reduce or terminate its operations.

Due to the conditions and events as noted above, there is material uncertainty casting significant doubt on the Company's ability to continue as a going concern. These consolidated financial statements do not include any adjustments to the recoverability and classification of recorded asset amounts and classification of liabilities that might be necessary should the Company be unable to continue as a going concern. These adjustments could be material.

2. BASIS OF PREPARATION

(a) Statement of Compliance

The Company prepares its consolidated financial statements in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board.

These consolidated financial statements were approved by the Audit Committee and the Board of Directors of the Company on November 29, 2019.

Hillcrest Petroleum Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
Nine Month Period Ended September 30, 2019
(Unaudited - Expressed in Canadian dollars)

2. BASIS OF PREPARATION (continued)

(b) Statement of Compliance

The consolidated financial statements have been prepared on a historical cost basis, with the exception of the embedded derivatives in the Ballakilley loan and the Convertible debentures which are recognised at fair value (Notes 7 and 9), using the accrual basis of accounting, except for cash flow information.

(c) Basis of Consolidation

These consolidated financial statements include the accounts of the parent company, Hillcrest Petroleum Ltd., and its wholly-owned subsidiaries. Intercompany balances and transactions, and any unrealized income and expenses arising from intercompany transactions, are eliminated in preparing the consolidated financial statements.

Name of Subsidiary	Jurisdiction of Incorporation	Principal Activity
Hillcrest Exploration Ltd. ("HEL")	USA	Oil and Gas exploration
1084580 BC Ltd.	Canada	Oil and Gas exploration
2044573 Alberta Ltd.	Canada	Oil and Gas exploration
102031850 Saskatchewan Ltd.	Canada	Oil and Gas exploration
Hillcrest Resources (Arizona) Ltd. ("HARL")	USA	Dormant

(d) Functional and Presentation Currency

These consolidated financial statements are presented in Canadian dollars. The functional currency of the parent, 1084580 BC Ltd., 2044573 Alberta Ltd., 102031850 Saskatchewan Ltd. and HARL is the Canadian dollar. The functional currency of HEL is the United States dollar.

(e) Use of Estimates and Judgements

The preparation of these consolidated financial statements requires management to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and reported amounts of expenses during the period. Actual results could differ from these estimates.

These consolidated financial statements include estimates which, by their nature, are uncertain. The impacts of such estimates are pervasive throughout the consolidated financial statements, and may require accounting adjustments based on future occurrences. Revisions to accounting estimates are recognized in the period in which the estimate is revised and future periods if the revision affects both current and future periods. These estimates are based on historical experience, current and future economic conditions and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Significant assumptions about the future and other sources of estimation uncertainty that management has made at the reporting date that could result in a material adjustment to the carrying amounts of assets and liabilities, in the event that actual results differ from assumptions made, relate to, but are not limited to, the following:

Hillcrest Petroleum Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
Nine Month Period Ended September 30, 2019
(Unaudited - Expressed in Canadian dollars)

2. BASIS OF PREPARATION (continued)

(e) Use of Estimates and Judgements (continued)

Depletion and Depreciation

The amounts recorded for depletion and depreciation of oil and natural gas properties and the amounts used in impairment testing are based on independent estimates of proved and probable reserves, well production rates, realized and forecast oil and natural gas prices, future development costs and other relevant assumptions. By their nature, these estimates are subject to measurement uncertainty. Accordingly, the impact on the consolidated financial statements for future periods may be material.

Decommissioning provisions

Restoration costs will be incurred by the Company at the end of the operating life of the Company's oil properties. The Company estimates abandonment and reclamation costs based on a combination of publicly available industry benchmarks and internal site specific information. For producing wells and facilities, the expected timing of settlement is estimated based on the period to abandonment for each field, as per an independent report. The ultimate restoration liability is uncertain and can vary in response to many factors including changes to relevant legal requirements, the emergence of new restoration techniques, experience at other production sites, or changes in the risk-free discount rate. The expected timing and amount of expenditure can also change in response to changes in reserves or changes in laws and regulations or their interpretation. As a result, there could be significant adjustments to the provisions established which would affect future financial results.

Income taxes

The calculation of income taxes requires judgment in applying tax laws and regulations, estimating the timing of the reversals of temporary differences, and estimating the reliability of deferred tax assets. These estimates impact current and deferred income tax assets and liabilities, and current and deferred income tax expense (recovery).

Significant judgements that management has made at the end of the reporting period are as follows:

Carrying value and the recoverability of exploration and evaluation assets

Management has determined that exploration, evaluation and related costs incurred which were capitalized may have future economic benefits and may be economically recoverable. Management uses several criteria in its assessments of economic recoverability and probability of future economic benefits including geologic and other technical information, history of conversion of mineral deposits with similar characteristics to its own properties to proven and probable mineral reserves, scoping and feasibility studies, accessible facilities and existing permits.

Fair value of stock options and other share-based payments

Management assesses the fair value of stock options and other share-based payments granted in accordance with the accounting policy stated in Note 3 to the consolidated financial statements. The fair value of the options granted is measured using the Black-Scholes model, taking into account the terms and conditions upon which the options are granted. Changes in assumptions concerning volatilities, interest rates and expected life could have significant impact on the fair valuation attributed to the Company's stock options.

Going concern

In order to assess whether it is appropriate for the Company to be reported as a going concern, the Directors apply judgement, having undertaken appropriate inquiries and having considered the business activities and the Company's principal risks. Management estimates future cash flows, including the timing of future capital expenditures and equity funding.

Hillcrest Petroleum Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
Nine Month Period Ended September 30, 2019
(Unaudited - Expressed in Canadian dollars)

2. BASIS OF PREPARATION (continued)

(e) Use of Estimates and Judgements (continued)

Fair value of embedded derivatives and other liability

Management assesses its financial instruments in order to identify whether or not non-derivative instruments might contain an embedded derivative component. If such a derivative component is identified, then it must be separated from the non-derivative host contract and recorded at fair value. The fair value of the embedded derivative is measured using the Black-Scholes model, taking into account the terms and conditions upon which the derivative is granted. Changes in assumptions concerning volatilities, interest rates and expected life could have significant impact on the fair valuation attributed to the embedded derivative. Fair value of the other liability is measured using a market-based approach.

Carrying value and the recoverability of property and equipment

The Company reviews its equipment for indicators of impairment whenever there is a change in events or circumstances that indicate an asset may be impaired and at each reporting period. Reviews are undertaken to evaluate the carrying value of the property and equipment considering, among other factors: the carrying value of each type of asset and the changes in circumstances that affect the carrying value of the Company's property and equipment. If such indication exists, a formal estimate of recoverable amount is performed and an impairment loss is recognized to the extent that the carrying amount exceeds the recoverable amount. The recoverable amount of an asset or a CGU is the greater of its value in use ("VIU") and its fair value less costs to dispose ("FVLCD"). The FVLCD is the amount obtainable from the sale of an asset or CGU in an arm's length transaction between knowledgeable, and willing parties, less the costs of disposal or in the case of lack of comparable transactions, based upon discounted cash after tax cash flow. VIU is determined by estimating the pre-tax present value of the future net cash flows expected to be derived from the continued use of the asset or CGU.

Determination of cash generating units

Management must make judgements as to which oil and gas properties can be aggregated into a cash generating unit ("CGU"). The Company's oil and gas assets are aggregated into CGUs for the purpose of calculating impairment and depletion. Factors considered by management include, but are not limited to, the product produced (i.e. oil versus gas), the common infrastructure shared by individual properties, proximity of properties to each other, and planned development activities.

3. Significant Accounting Policies

These condensed interim consolidated financial statements, including comparatives, have been prepared in accordance with International Accounts Standards ("IAS") 34, "Condensed Interim Financial Reporting" using accounting policies consistent with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and Interpretations issued by the International Financial Reporting Interpretations Committee ("IFRIC"). The accounting policies applied in these condensed interim financial statements are consistent with those stated in the Company's most recent annual audited financial statements, except for any new standards and amendments adopted (Note 3). Accordingly, these condensed interim financial statements should be read in conjunction with the Company's annual financial statements for the year ended December 31, 2018.

Hillcrest Petroleum Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
Nine Month Period Ended September 30, 2019
(Unaudited - Expressed in Canadian dollars)

New Standards, Amendments and Interpretations to Existing Standards Not Yet Effective

The following standard was adopted on January 1, 2019:

IFRS 16, Leases

This new standard replaces the existing leasing guidance in IAS 17, Leases.

IFRS 16 distinguishes between leases and service contracts on the basis of whether the customer controls the asset being leased. For those contracts determined to meet the definition of a lease, IFRS 16 requires a lessee to recognize on the balance sheet a lease asset along with the associated lease liability which reflects future lease payments, similar to current finance lease accounting. There are limited exceptions for leases with a term of less than 12 months or leases of assets which have a very low value. As a result of the adoption of IFRS 16, operating leases which were previously only recognized on the consolidated statement of income (loss) will be recognized on the consolidated statement of financial position.

The adoption of this standard did not have a material impact on the Company's financial statements.

4. EXPLORATION AND EVALUATION ASSETS

	Flaxcombe	West Hazel	Total
	(\$)	(\$)	(\$)
Balance at January 1, 2018	38,264	-	38,264
Additions	114,163	595,181	709,344
ARO	50,098	369,700	419,798
Reclassification	(202,525)	-	(202,525)
Balance at December 31, 2018	-	964,881	964,881
Additions	-	106,132	106,132
Disposals	-	(170,000)	(170,000)
Reclassification	-	(901,013)	(901,013)
Balance at September 30, 2019	-	-	-

Flaxcombe Project, Saskatchewan

On December 14, 2017, the Company entered into a farm-in agreement with Westcore Energy Ltd. ("Westcore") to workover two previously shut-in oil wells (16-13 and 7-13) in the Flaxcombe area of southwestern Saskatchewan. The Company was required to incur 100% of the workover costs in exchange for a 50% working interest in the wells. In accordance with an approved budget, the Company incurred \$152,427 to complete the workovers. Both wells were completed and reactivated in the first quarter of 2018, and as a result were reclassified to property and equipment.

West Hazel Project, Saskatchewan

On October 4, 2017, the Company entered into a joint venture agreement with Charterhouse Co. ("Charterhouse"), a private Alberta corporation, to workover four previously shut-in oil wells in southeastern Saskatchewan. The Company was required to incur 100% of the workover costs in exchange for a 75% working interest in the wells before recovery of all reactivation costs incurred ("Payout") and a 50% working interest after Payout.

Hillcrest Petroleum Ltd.

Notes to the Condensed Interim Consolidated Financial Statements

Nine Month Period Ended September 30, 2019

(Unaudited - Expressed in Canadian dollars)

4. EXPLORATION AND EVALUATION ASSETS (continued)

If after the work program obligations have been completed for the West Hazel project (the "WH Property"), but prior to Payout for the WH Property, average total daily oil production from the WH Property over any calendar month, is less than 200 barrels per day and the Company's working interest revenue from the WH Property is insufficient to cover the minimum financing costs related to that work program, then the Company may, at its sole discretion, retain net Charterhouse's working interest revenue from the WH Property sufficient to meet the minimum financing cost for that month. Any retained Charterhouse revenue would be credited in Payout account calculations.

In February 2019, the Company sold 16.67% of its interest in the West Hazel project in exchange for cash proceeds of \$170,000. In addition, the Company completed the reactivation of three wells, and as a result the West Hazel project costs were reclassified to property and equipment.

5. PROPERTY AND EQUIPMENT

	Computers	Oil and Gas Interests	Total
	(\$)	(\$)	(\$)
Cost			
At January 1, 2018	16,028	1,713,407	1,729,435
Additions	-	202,525	202,525
At December 31, 2018	16,028	1,915,932	1,931,960
Additions	-	901,013	901,013
At September 30, 2019	16,028	2,816,945	2,832,973
Accumulated depletion and depreciation			
At January 1, 2018	16,028	1,221,864	1,237,892
Depletion and depreciation for the year	-	-	-
At December 31, 2018	16,028	1,221,864	1,237,892
Additions	-	159,131	73,831
At September 30, 2019	16,028	1,380,995	1,311,723
Impairment			
At January 1, 2018	-	491,543	491,543
Additions	-	202,525	202,525
At December 31, 2018 and September 30, 2019	-	694,068	694,068
Carrying amounts:			
At December 31, 2018	-	-	-
At September 30, 2019	-	741,882	827,182

Hillcrest Petroleum Ltd.

Notes to the Condensed Interim Consolidated Financial Statements

Nine Month Period Ended September 30, 2019

(Unaudited - Expressed in Canadian dollars)

5. PROPERTY AND EQUIPMENT (continued)

West Hazel, Saskatchewan

In February 2019, three wells under the West Hazel farm-in agreement were reactivated, and as a result the Company reclassified the associated costs from exploration and evaluation assets to property and equipment on the consolidated statement of financial position.

Flaxcombe, Saskatchewan

In January 2018, Well 16-13 and Well 07-13 under the Westcore farm-in agreement were reactivated, and as a result the Company reclassified the associated costs from exploration and evaluation assets to property and equipment on the consolidated statement of financial position.

Impairment

During the nine month period ended September 30, 2019, the Company reviewed the carrying value of its oil and gas interests and determined there were no indicators of impairment with respect to the performance and operating costs of the West Hazel wells.

6. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	September 30, 2019	December 31, 2018
	(\$)	(\$)
Trade payables	1,568,506	900,553
Related party payables (Note 10)	513,718	318,478
Accrued liabilities	232,034	233,013
	<u>2,314,258</u>	<u>1,452,044</u>

7. SECURED LOANS

ASI Loan

As at September 30, 2019, the Company has \$138,550 (December 31, 2018 - \$138,550) outstanding on a senior secured loan facility that bears interest at a rate of 20% per annum and is currently payable on demand. As part of the consideration for the loan facility, the lenders and the arranging agent receive an aggregate 10% overriding royalty interest in the Company's proceeds from all oil, gas and other hydrocarbons produced from any new wells developed on the Company's Hartburg Properties using any portion of the proceeds from the loan. The Company has fully impaired these Hartburg assets and they are no longer producing (refer to Note 5).

During the nine month period ended September 30, 2019, the Company repaid \$Nil (2018 - \$Nil) in loan principal and incurred \$20,726 (2018 - \$20,726) in interest expense.

Hillcrest Petroleum Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
Nine Month Period Ended September 30, 2019
(Unaudited - Expressed in Canadian dollars)

7. SECURED LOANS (continued)

Ballakilley Loan

On June 15, 2017, the Company borrowed \$140,950 under a convertible loan agreement (the "Ballakilley Loan") bearing interest at 20% per annum, payable semi-annually, and maturing on May 31, 2019. The Ballakilley Loan is convertible into common shares of the Company at a price of \$0.05 per share, due to the Company's 2018 private placement. The conversion price is subject to a reduction if the Company completed a private placement or issues options or warrants at a lower price, at the option of the lender. The cash received under the Ballakilley Loan has been allocated between the fair value of the loan liability and the value of the loan conversion feature which is considered an embedded derivative. The value ascribed to the loan liability as at the loan date was \$35,650, and the residual amount has been allocated to the loan conversion feature.

During the nine month period ended September 30, 2019, the Company incurred \$59,869 (2018 - \$56,505) in interest expense, including \$36,820 (2018 - \$35,362) in accretion of the loan liability. At September 30, 2019 a total of \$193,598 (December 31, 2018 - \$170,550) in loan principal and accrued interest remained outstanding. Additionally, the loan conversion feature has been revalued to \$52,500 (December 31, 2018 - \$52,500), and the Company has recorded a gain of \$Nil (2018 - \$Nil) on the consolidated statement of income (loss) for the nine month period ended September 30, 2019.

The loan is in default but the Company continues to accrue interest in accordance with the agreement.

Project Financing

In February 2017, the Company entered into an arrangement with a third party to provide potential debt financing of up to \$2,500,000. The Company incurred standby charges at a rate of 7% per annum for the availability of this potential debt financing for the acquisition and development of oil projects located in Canada. Upon making a draw down under the facility additional fees would be incurred resulting in an effective borrowing rate of 20% per annum. The Company did not borrow any funds, but has incurred standby charges totalling \$Nil (2018 - \$67,027) during the nine month period ended September 30, 2019. The arrangement is still currently in place but there are no funds currently incurring standby charges as at September 30, 2019.

8. UNSECURED LOANS

Bridge Loan

On August 10, 2016, the Company borrowed \$300,000 under a loan agreement (the "Bridge Loan") bearing interest at 1% per month, compounded monthly, and maturing on August 9, 2017. The Company also issued 1,500,000 common shares with a value of \$75,000 as payment of arrangement fees and syndication fees incurred in connection with the Bridge Loan. The cash received under the Bridge Loan has been allocated between the fair value of the loan liability and the value of the 1,500,000 common shares. The value ascribed to the common shares as at the loan date was \$75,000, and the residual amount has been allocated to the loan liability.

During the nine month period ended September 30, 2019, the Company incurred \$33,446 (2018 - \$28,452) in interest expense and paid \$Nil (2018 - \$36,000) in accrued interest through the issuance of 720,000 common shares. At September 30, 2019 a total of \$391,473 (December 31, 2018 - \$358,027) in loan principal and accrued interest remained outstanding.

The loan is in default but the Company continues to accrue interest in accordance with the agreement.

1055328 BC Ltd. Loan

On October 6, 2017, the Company borrowed \$63,000 under an unsecured loan that bears 12% interest per annum and is repayable on or before October 6, 2018. On June 6, 2018, the Company borrowed an additional \$37,000 under the same terms.

During the nine month period ended September 30, 2019, the Company incurred \$8,975 (2018 - \$8,794) in interest expense. At September 30, 2019, a total of \$120,847 (December 31, 2018 - \$111,871) in loan principal and accrued interest remained outstanding.

The loan is in default but the Company continues to accrue interest in accordance with the agreement.

Hillcrest Petroleum Ltd.

Notes to the Condensed Interim Consolidated Financial Statements
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8. UNSECURED LOANS (continued)

Credit Line

On December 10, 2015, the Company obtained access to an unsecured line of credit bearing interest at an annual rate calculated semi-annually which is equal to the lending rate of the Canadian Imperial Bank of Commerce ("CIBC"). The credit line had an initial term of 30 months, and it has a maximum capacity of \$400,000 that requires monthly repayments equal to the lesser of i) \$15,000 and ii) the aggregate principal and interest outstanding. In addition, the Company issued 1,000,000 common shares as consideration to the lender. The Company borrowed \$390,000 under the credit line, and the cash received has been allocated between the fair value of the loan liability and the fair value of the 1,000,000 common shares. The fair value of the common shares as at the loan date was \$30,000, and the residual amount has been allocated to the loan liability.

During the nine month period ended September 30, 2019, the Company incurred \$7,947 (2018 - \$15,712) in interest expense, including \$Nil (2018 - \$5,452) in accretion of the loan liability. At September 30, 2019, a total of \$138,750 (December 31, 2018 - \$266,478) in loan principal and accrued interest remained outstanding.

9. CONVERTIBLE DEBENTURES

Through a series of advances between November 2018 and February 2019, the Company borrowed a total of \$750,000 under convertible debenture agreements (the "Convertible Debentures") bearing interest at 15% per annum, payable quarterly, and maturing two years from the date of advance. A total of \$600,000 of the Convertible Debentures were issued to the CEO of the Company.

The Convertible Debentures are secured by the West Hazel property and are convertible into common shares of the Company at a price equal to market price of the common shares of the Company in the first twelve months or the greater of \$0.10 and market price thereafter. In addition, should the West Hazel property be sold prior to the first anniversary of the advance date of the Convertible Debentures, then the Company will pay an amount equal to one full year of interest, the loan principal and 15% of any profit realized on the sale above the original reactivation costs. Should the West Hazel property be sold subsequent to the first anniversary of the advance date and prior to maturity of the Convertible Debentures, then the Company will pay an amount equal to the loan principal and 15% of any profit realized on the sale above the original reactivation costs.

The cash received under the Convertible Debentures has been allocated between the fair value of the loan liability and the conversion feature. The value ascribed to the loan liability, net of transaction costs of \$5,731, as at the loan date was \$744,269, and the conversion feature was determined to have no value. In addition, the 20% retained profit interest which was attached to the Convertible Debentures and takes effect upon full loan repayment, and is applicable only to specific zones of the four original reactivation wells, was determined to have a fair value of \$116,000 which was recorded as financing expense during the year ended December 31, 2018.

During the nine month period ended September 30, 2019, the Company settled \$200,000 (2018 - \$Nil) of the Debentures through the issuance of 400,000 common shares and incurred \$83,295 (2018 - \$Nil) in interest and accretion expense. At September 30, 2019 a total of \$712,962 (December 31, 2018 - \$690,646) in loan principal and accrued interest remained outstanding.

Hillcrest Petroleum Ltd.

Notes to the Condensed Interim Consolidated Financial Statements

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10. RELATED PARTY TRANSACTIONS

The following summarizes the Company's related party transactions during the nine month periods ended September 30, 2019 and 2018. Key management personnel included the Chief Executive Officer ("CEO"), Chief Financial Officer ("CFO"), and directors and officers and companies controlled or significantly influenced by them:

Key management compensation

	<u>2019</u>	<u>2018</u>
	(\$)	(\$)
Salary and consulting fees paid or accrued to directors, officers or corporations controlled by directors and officers of the Company	287,965	67,500
Share-based payments paid to certain directors and officers of the Company in connection with the extension of the expiry date of share purchase warrants	-	35,400
	<u>287,965</u>	<u>102,900</u>

- a) As at September 30, 2019, a total of \$513,718 (December 31, 2018 - \$318,478) was included in accounts payable and accrued liabilities owing to the directors and officers or corporations controlled by directors and officers of the Company for unpaid consulting fees and reimbursable expenses. These liabilities are non-interest bearing and payable on demand.
- b) As at September 30, 2019, a total of \$579,284 (December 31, 2018 - \$600,000) was included in convertible debentures owing to the CEO. A total of \$25,000 (December 31, 2018 - \$57,353) has been paid in advance for future interest payments and is recorded as prepaids on the consolidated statement of financial position. (Refer to Note 9)
- c) As at September 30, 2019, a total of \$50,104 (December 31, 2018 - \$45,055) was included in loans owing to the Chairman of the Company.

11. DECOMMISSIONING LIABILITY

The decommissioning liability relates to the expected present value of costs of plugging and abandoning the oil properties held by Hillcrest. The provision for decommissioning is estimated after taking account of inflation, years to abandonment and an appropriate discount rate. As at September 30, 2019, the oil properties had estimated abandonment dates between 2019 and 2028.

Actual decommissioning costs will ultimately depend upon future market prices for the decommissioning work required, which will reflect market conditions at the relevant time. Furthermore, the timing of decommissioning is likely to depend on when the fields cease to produce at economically viable rates. This in turn will depend upon future oil prices, which are inherently uncertain.

Hillcrest Petroleum Ltd.

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11. DECOMMISSIONING LIABILITY (continued)

The movement in the provision for the decommissioning liability was as follows:

	Hartburg, Texas	West Hazel, Saskatchewan	Flaxcombe, Saskatchewan	Total
	(\$)	(\$)		(\$)
Balance, January 1, 2018	42,844	-	-	42,844
Accretion	850	-	992	1,842
Additions	-	369,700	50,098	419,798
Balance, December 31, 2018	43,694	369,700	51,090	464,484
Accretion	650	5,490	759	6,899
Disposal	(11,106)	-	-	(11,106)
Balance, September 30, 2019	33,238	375,190	51,849	460,277
Current portion	23,458	-	-	23,458
Non-current portion	9,780	375,190	51,849	436,819
	33,238	375,190	51,849	460,277

The total undiscounted amount of estimated cash flows required to settle the provision for decommissioning liability for the Hartburg Project is \$34,189 (December 31, 2018 - \$46,358) as at September 30, 2019. The provision has been estimated using a risk-free discount rate of 1.93% (December 31, 2018 - 1.93%) and an inflation rate of 2.00% (December 31, 2018 - 2.00%).

The total undiscounted amount of estimated cash flows required to settle the provision for decommissioning liability for the Flaxcombe Project is \$60,950 (December 31, 2018 - \$60,950) at September 30, 2019. The provision has been estimated using a risk-free discount rate of 1.93% (December 31, 2018 - 1.93%) and an inflation rate of 2.00% (December 31, 2018 - 2.00%).

The total undiscounted amount of estimated cash flows required to settle the provision for decommissioning liability for the West Hazel Project is \$415,854 (December 31, 2018 - \$415,854) at September 30, 2019. The provision has been estimated using a risk-free discount rate of 1.93% (December 31, 2018 - 1.93%) and an inflation rate of 2.00% (December 31, 2018 - 2.00%).

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12. SHARE CAPITAL

Authorized

Unlimited number of common shares without par value

Issued and outstanding

Nine Month Period Ended September 30, 2019

- a) The Company completed a non-brokered private placement wherein it issued an aggregate of 3,900,000 units at \$0.05 per unit for gross proceeds of \$195,000. Each unit is comprised of a common share and one half of a common share purchase warrant. Each whole warrant entitles the holder to acquire an additional common share at \$0.10 for two years from the date of closing of the placement. The Company used the residual method to determine the value of the warrants issued as part of the private placement. It was determined that the warrants issued as part of the private placement had a value of \$78,000. The Company incurred \$6,146 in share issuance costs in connection with this private placement.
- b) The Company issued 400,000 common shares in connection with the conversion of a portion of the outstanding Convertible Debentures at \$0.05 per share.

Year Ended December 31, 2018

- a) The Company issued 1,700,000 common shares to settle \$85,000 in outstanding debts.
- b) The Company completed a non-brokered private placement in two tranches wherein it issued an aggregate of 9,992,000 units at \$0.05 per unit for gross proceeds of \$499,600. Each unit is comprised of a common share and one half of a common share purchase warrant. Each whole warrant entitles the holder to acquire an additional common share at \$0.10 for two years from the date of closing of the placement. The Company used the residual method to determine the value of the warrants issued as part of the private placement. It was determined that the warrants issued as part of the private placement do not have any value. The Company incurred \$17,248 in share issuance costs in connection with this private placement.
- c) The Company issued 725,000 common shares due to the exercise of stock options at \$0.06 per share for gross proceeds of \$43,500. The fair value of the options was determined to be \$41,059, and accordingly the amount has been transferred from contributed surplus to share capital.

Share Purchase Warrants

Nine Month Period Ended September 30, 2019

- a) The Company issued 1,950,000 share purchase warrants in connection with a non-brokered private placement completed on May 10, 2019. Each warrant entitles the holder to acquire a common share of the Company at \$0.10 until May 10, 2021. The Company also issued 272,000 finder's warrants under the same terms in connection with the financing. The finder's warrants were determined to have a value of \$4,000 and this was recorded as a share issuance cost.
- b) A total of 4,450,000 share purchase warrants exercisable at \$0.08 per share expired during the period.

Hillcrest Petroleum Ltd.

Notes to the Condensed Interim Consolidated Financial Statements

Nine Month Period Ended September 30, 2019

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12. SHARE CAPITAL (continued)

Year Ended December 31, 2018

- c) The Company issued 4,396,000 share purchase warrants in connection with the first tranche of a non-brokered private placement. Each warrant entitles the holder to acquire a common share of the Company at \$0.10 until February 27, 2020.
- d) The Company issued 600,000 share purchase warrants in connection with the second tranche a non-brokered private placement. Each warrant entitles the holder to acquire a common share of the Company at \$0.10 until March 23, 2020.

The continuity of the Company's share purchase warrants is as follows:

	Number of Warrants	Weighted Average Exercise Price (\$)
Balance, January 1, 2018	11,897,429	0.08
Issued	4,996,000	0.10
Expired	(3,650,000)	0.08
Balance, December 31, 2018	13,243,429	0.09
Issued	2,222,000	0.10
Expired	(7,247,429)	0.09
Balance, September 30, 2019	8,218,000	0.10

The following table summarizes the share purchase warrants outstanding as at September 30, 2019:

Number of Warrants	Weighted Average Exercise Price (\$)	Expiry Date	Weighted Average Remaining Contractual Life (yrs)
2,222,000	0.10	May 10, 2021	1.61
500,000	0.07	August 17, 2020	0.88
500,000	0.10	August 17, 2020	0.88
600,000	0.10	March 23, 2020	0.48
4,396,000	0.10	February 27, 2020	0.41
8,218,000	0.10		0.80

Hillcrest Petroleum Ltd.

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12. SHARE CAPITAL (continued)

Stock Options

Effective November 4, 2010, the Company adopted a stock option plan to grant stock options to its directors, officers, employees and consultants. In accordance with the policies of the TSXV, the aggregate number of securities reserved for issuance under the plan, at any point in time, will be 10% of the number of common shares of the Company issued and outstanding at the time the option is granted, less any common share reserved for issuance under share options granted under share compensation arrangements other than the plan. The exercise price of option grants will be determined by the Board of Directors, but will not be less than the closing market price of the common shares on the Exchange at the time of grant. All unexercised options granted under the plan will expire no later than five years from the date of grant.

The Company granted an aggregate of 950,000 stock options during the year ended December 31, 2018. The options vest over different time periods, and the Company expensed \$41,598 as share-based compensation. The Company expensed an additional \$744 during the nine month period ended September 30, 2019 in connection with the 2018 option grants.

The options granted were valued using the Black-Scholes option pricing model under the following weighted average assumptions:

	2018
Risk-free interest rate	2.11%
Expected life of options	3.7 yrs
Volatility	149%
Expected Dividend yield	Nil
Forfeiture rate	Nil
Weighted average fair value	\$0.05

The continuity of the Company's stock options is as follows:

	Number of Options	Weighted Average Exercise Price (\$)
Balance, January 1, 2018	6,400,000	0.07
Issued	950,000	0.06
Exercised	(725,000)	0.06
Expired	(1,700,000)	0.06
Balance, December 31, 2018	4,925,000	0.07
Expired	(275,000)	0.07
Balance, September 30, 2019	4,650,000	0.07

Hillcrest Petroleum Ltd.

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12. SHARE CAPITAL (continued)

The following table summarizes the stock options outstanding and exercisable as at September 30, 2019:

Number of Options Outstanding	Number of Options Exercisable	Weighted Average Exercise Price (\$)	Expiry Date	Weighted Average Remaining Contractual Life (yrs)
300,000	75,000	0.06	April 3, 2021	1.51
3,700,000	3,700,000	0.07	February 21, 2022	2.40
300,000	300,000	0.06	May 1, 2022	2.59
350,000	350,000	0.065	June 13, 2022	2.70
4,650,000	4,650,000	0.07		2.38

13. COMMITMENTS

- a) The Company entered into an office rental agreement in Vancouver, British Columbia with a term of 36 months, terminating on June 15, 2020. The remaining base rent payable under the lease is \$17,570 up until the lease expires. In addition to the base rent of \$2,067, the Company's share of operating costs is estimated at approximately \$1,598 per month.
- b) HEL entered into an office rental agreement with a term of 72 months, terminating on February 28, 2023. The landlord issued a notice of termination to the Company effective January 31, 2019 and has sent a demand for payment of \$43,961 (US\$32,245) representing unpaid rental charges under the rental agreement. The Company has recognized the full liability as at September 30, 2019.

14. GEOGRAPHICAL SEGMENTED INFORMATION

The Company is engaged in one business activity, being the acquisition, exploration, development and production of oil reserves in Canada and the United States. For the nine month periods ended September 30, 2019 and 2018, all revenues were derived from operations in Canada and all non-current assets were located in Canada.

15. CAPITAL MANAGEMENT

The Company manages its capital structure and makes adjustments to it, based on the funds available to the Company, in order to support the acquisition, exploration and development of oil and gas properties. The Board of Directors does not establish quantitative return on capital criteria for management, but rather relies on the expertise of the Company's management to sustain future development of the business.

The Company is primarily dependent on external financing to fund its activities. In order to carry out the planned exploration and development and pay for administrative costs, the Company will spend its existing working capital and raise additional funds as needed using best efforts. The Company will continue to assess new properties and seek to acquire an interest in additional properties if it feels there is sufficient economic potential and if it has adequate available or committed financial resources to complete such acquisitions.

Management reviews its capital management approach on an ongoing basis and believes that this approach, given the size of the Company, is reasonable.

There were no changes in the Company's approach to capital management during the period ended September 30, 2019. The Company is not subject to externally imposed capital requirements.

Hillcrest Petroleum Ltd.

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16. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Financial Risk Management

The Company's financial instruments that are measured at fair value on a recurring basis in periods subsequent to initial recognition and the fair value hierarchy used to measure them are presented in the table below. The Company classifies its other financial assets and other financial liabilities measured at fair value using a fair value hierarchy that reflects the significance of the inputs used in making the measurements.

The fair value hierarchy has the following levels:

- Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3: Inputs for the asset or liability that is not based on observable market data (unobservable inputs).

The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Company's financial instruments consist of cash, receivables, accounts payable and accrued liabilities, loans and convertible debentures.

The fair value of cash, receivables and accounts payable and accrued liabilities approximate their book values because of the short-term nature of these instruments. The carrying amounts of the loans approximate fair value as the applicable interest rates, which were negotiated between the Company and arm's length third parties, are similar to market interest rates which would be available to the Company at the balance sheet date. The fair value of the convertible debentures has been determined after deducting transaction costs and allocating the portion of the proceeds applicable to the retained profit interest.

Financial Instrument Risk Exposure

The Company is exposed in varying degrees to a variety of financial instrument related risks. The Board approves and monitors the risk management processes.

Credit risk

The Company's credit risk is primarily attributable to cash and accounts receivable. The Company's maximum exposure to credit risk at the end of the reporting period is the carrying value of these assets. Substantially all of the Company's customers are in the oil industry and are subject to normal industry credit risks. The remaining customers are related to the recovery of shared office rent. The Company has minimal collection risk related to these receivables and expects to collect the outstanding receivables in the normal course of operations. At September 30, 2019, the maximum credit exposure is the carrying amount of Receivables of \$361,316 (December 31, 2018 - \$38,505).

The Company has no significant concentration of credit risk arising from operations. Cash is held with reputable financial institutions, from which management believes the risk of loss to be remote.

Market risk

Market risk is the risk of loss that may arise from changes in market factors such as interest rates, foreign exchange rates, and commodity and equity prices. The Company's primary commodity is heavy oil which is closely tied to the price of Western Canadian Select.

Interest rate risk

The Company is exposed to interest rate risk. The Company has an unsecured loan associated with a CIBC line of credit which has a variable interest rate, recalculated quarterly. A 1% change in market interest rates would result in an increase/decrease of \$1,244 on the Company's net loss.

Hillcrest Petroleum Ltd.

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16. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (continued)

Liquidity risk

The Company's approach to managing liquidity risk is to ensure that it will have sufficient liquid capital to meet its current liabilities as they come due. At September 30, 2019, the Company had a working capital deficiency of \$2,872,786 (December 31, 2018 - \$2,400,807). The Company finances its operations through a combination of cash, loans, equity and convertible debentures. The Company's ability to continue as a going concern is dependent upon the ongoing support from its lenders and its ability to fund the repayment of its debt by generating positive cash flows from operations, securing funding from additional debt, equity financing, disposing of assets or making other arrangements. Refer to Note 1 for further discussion.

The Company's financial liabilities had contractual maturities as follows:

	September 30, 2019	December 31, 2018
	(\$)	(\$)
Less than 1 year	3,457,585	2,616,800
Between 1 – 2 years	706,092	594,686
Between 2 – 5 years	-	-
	<u>4,163,677</u>	<u>3,211,486</u>

Foreign currency risk

Foreign currency exchange rate risk is the risk that the fair value of financial instruments or future cash flows will fluctuate as a result of changes in foreign exchange rates. The Company operates in Canada and the United States. All of the Company's oil sales are denominated in Canadian dollars. As a result, the Company has minimal exposure to foreign exchange risk.

17. SUPPLEMENTAL CASH FLOW INFORMATION

	September 30, 2019	September 30, 2018
	(\$)	(\$)
Non-cash investing and financing activities:		
Recognition of the estimated asset retirement obligation for the Flaxcombe property	-	50,098
Common shares issued to settle outstanding liabilities	-	85,000
Common shares issued on conversion of convertible debentures	20,000	-
Exploration and evaluation assets reclassified to property and equipment	-	152,427
Interest paid during the period	27,998	35,262
Income taxes paid during the period	-	-

18. SUBSEQUENT EVENTS

Subsequent to September 30, 2019, the Company:

- a) repriced a total of 4,190,600 existing share purchase warrants down to \$0.05 per share
- b) repriced a total of 4,650,000 existing stock options down to \$0.05 per share.