STEP energy services

TSX STEP

Condensed Consolidated Interim

# Financial Statements

AS AT AND FOR THE THREE MONTHS ENDED MARCH 31, 2019

# STEP ENERGY SERVICES LTD.

## CONDENSED CONSOLIDATED INTERIM STATEMENTS OF FINANCIAL POSITION

| As at<br>Unaudited (in thousands of Canadian dollars) | Notes | | March 31, 2019 | | December 31, 2018 |
|---|---|---|---|---|---|
| ASSETS | | | | | |
| Current Assets | | | | | |
| Cash and cash equivalents | | $ | 7,040 | $ | 364 |
| Trade and other receivables | 11 | | 133,804 | | 124,553 |
| Inventory | 2 | | 29,062 | | 32,646 |
| Prepaid expenses and deposits | | | 5,784 | | 6,691 |
| Foreign exchange forward contracts | | | - | | 44 |
| | | | 175,690 | | 164,298 |
| Property and equipment | 3 | | 586,137 | | 600,142 |
| Intangible assets | 4 | | 30,722 | | 33,202 |
| Goodwill | 4 | | 88,347 | | 90,266 |
| | | $ | 880,896 | $ | 887,908 |
| | | | | | |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | | | | |
| Current Liabilities | | | | | |
| Trade and other payables | 11 | $ | 87,433 | $ | 84,079 |
| Income tax payable | | | 1,835 | | 4,572 |
| Current portion of lease obligations | 1,6 | | 8,635 | | 8,489 |
| | | | 97,903 | | 97,140 |
| Deferred tax liabilities | | | 47,040 | | 51,713 |
| Lease obligations | 1,6 | | 13,247 | | 8,010 |
| Loans and borrowings | 5 | | 252,471 | | 252,441 |
| | | | 410,661 | | 409,304 |
| Shareholders' equity | | | | | |
| Share capital | 7 | | 426,769 | | 426,494 |
| Contributed surplus | | | 30,352 | | 29,447 |
| Accumulated other comprehensive income | | | 13,877 | | 22,670 |
| Deficit | | | (763) | | (7) |
| | | | 470,235 | | 478,604 |
| | | $ | 880,896 | $ | 887,908 |

See accompanying notes to the condensed consolidated interim financial statements

See Note 6 – Commitments

# STEP ENERGY SERVICES LTD.

## CONDENSED CONSOLIDATED INTERIM STATEMENTS OF NET (LOSS) INCOME AND OTHER COMPREHENSIVE (LOSS) INCOME

| For the three months ended March 31,<br>Unaudited (in thousands of Canadian dollars, except per share amounts) | Notes | | 2019 | | 2018 |
|---|---|---|---|---|---|
| Revenue | | $ | 176,469 | $ | 187,593 |
| Cost of sales | | | 167,339 | | 149,958 |
| Gross profit | | | 9,130 | | 37,635 |
| Selling, general and administrative expenses | | | 8,843 | | 7,940 |
| Results from operating activities | | | 287 | | 29,695 |
| Finance costs | 10 | | 3,253 | | 145 |
| Foreign exchange (gain) loss | | | (1,265) | | 135 |
| Gain on disposal of property and equipment | | | (672) | | (117) |
| Transaction costs | | | - | | 1,153 |
| Amortization of intangible assets | 4 | | 1,774 | | 10 |
| Loss on foreign exchange forward contracts | 11 | | 383 | | 1,771 |
| Net (loss) income before income tax | | | (3,186) | | 26,598 |
| Income tax expense (recovery) | | | | | |
| Current | | | 1,283 | | 6,642 |
| Deferred | | | (3,867) | | 1,540 |
| | | | (2,584) | | 8,182 |
| Net (loss) income | | | (602) | | 18,416 |
| Other comprehensive (loss) income | | | | | |
| Foreign currency translation (loss) gain | | | (8,793) | | 1,387 |
| Total comprehensive (loss) income | | $ | (9,395) | $ | 19,803 |
| Earnings (loss) per share: | | | | | |
| Basic | 9 | $ | (0.01) | $ | 0.30 |
| Diluted | 9 | $ | (0.01) | $ | 0.29 |

See accompanying notes to the condensed consolidated interim financial statements

STEP ENERGY SERVICES LTD.

## CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CHANGES IN EQUITY

| Unaudited (in thousands of Canadian dollars) | Notes | Share capital | Contributed surplus | Accumulated other comprehensive (loss) income | Retained earnings / (deficit) | Total |
|---|---|---|---|---|---|---|
| Balance at January 1, 2018 | | $ 369,436 | 24,664 | (2,357) | 39,297 | 431,040 |
| Net income for the period | | - | - | - | 18,416 | 18,416 |
| Foreign currency translation gain | | - | - | 1,387 | - | 1,387 |
| Share-based compensation | 8 | - | 1,742 | - | - | 1,742 |
| Exercise of equity instruments | 7 | 1,107 | (1,107) | - | - | - |
| Balance at March 31, 2018 | | 370,543 | $ 25,299 | $ (970) | $ 57,713 | $ 452,585 |
| | | | | | | |
| Balance at January 1, 2019 | | 426,494 | $ 29,447 | $ 22,670 | $ (7) | $ 478,604 |
| Impact of change in accounting policy | 1 | - | - | - | (154) | (154) |
| Net loss for the period | | - | - | - | (602) | (602) |
| Foreign currency translation (loss) | | - | - | (8,793) | - | (8,793) |
| Share-based compensation | 8 | - | 1,180 | - | - | 1,180 |
| Exercise of equity instruments | 7 | 275 | (275) | - | - | - |
| **Balance at March 31, 2019** | | **$ 426,769** | **$ 30,352** | **$ 13,877** | **$ (763)** | **$ 470,235** |

See accompanying notes to the condensed consolidated interim financial statements

## STEP ENERGY SERVICES LTD.

### CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CASH FLOWS

| For the three months ended March 31,<br>Unaudited (in thousands of Canadian dollars) | Notes | | 2019 | | 2018 |
|---|---|---|---|---|---|
| Operating activities: | | | | | |
| Net (loss) income | | $ | (602) | $ | 18,416 |
| Adjusted for the following: | | | | | |
| Depreciation and amortization | 3,4 | | 26,841 | | 10,320 |
| Share-based compensation | 8 | | 1,263 | | 1,776 |
| Unrealized foreign exchange (gain) loss | | | (1,562) | | 31 |
| Gain on disposal of property and equipment | | | (672) | | (117) |
| Loss on foreign exchange forward contracts | 11 | | 383 | | 1,771 |
| Finance costs | 10 | | 3,253 | | 145 |
| Income tax expense (recovery) | | | (2,584) | | 1,540 |
| Cash finance costs paid | | | (5,315) | | (92) |
| Income taxes paid | | | (4,014) | | (5,897) |
| Changes in non-cash working capital from operating activities | | | (225) | | (1,297) |
| Net cash provided by operating activities | | | 16,766 | | 26,596 |
| Investing activities: | | | | | |
| Purchase of property and equipment | 3 | | (10,347) | | (22,800) |
| Proceeds on disposal of property and equipment | | | 679 | | 208 |
| Changes in non-cash working capital from investing activities | | | (276) | | 2,527 |
| Net cash used in investing activities | | | (9,944) | | (20,065) |
| Financing activities: | | | | | |
| Issuance (repayment) of loans and borrowings | 5 | | 1,799 | | - |
| Repayment of lease obligations | | | (1,752) | | (1,065) |
| Settlement of foreign currency hedge | | | (338) | | - |
| Changes in non-cash working capital from financing activities | | | - | | (2,071) |
| Net cash used in financing activities | | | (291) | | (3,136) |
| Impact of exchange rate changes on cash | | | 145 | | 42 |
| Increase in cash and cash equivalents | | | 6,676 | | 3,347 |
| Cash and cash equivalents, beginning of period | | | 364 | | 36,859 |
| Cash and cash equivalents, end of period | | $ | 7,040 | $ | 40,296 |

See accompanying notes to the condensed consolidated interim financial statements

# STEP ENERGY SERVICES LTD.

## Notes to the condensed consolidated interim financial statements

(unaudited)

As at and for the three months ended March 31, 2019 and 2018.

Tabular amounts expressed in thousands of Canadian dollars, except where otherwise noted.

## NOTE 1 – NATURE OF BUSINESS AND BASIS OF PREPARATION

STEP Energy Services Ltd. (the "Company", "STEP Energy Services" or "STEP") is a publically traded company domiciled in Canada was incorporated under the laws of the Province of Alberta on March 25, 2011 and is listed under the symbol "STEP" on the Toronto Stock Exchange. The registered office of the Company is 4300, 888 - 3rd Street SW, Calgary, Alberta T2P 5C5. STEP provides specialized coiled tubing and associated pumping and fracturing equipment to service the oil and gas industry in Canada and the United States ("U.S."). The Company purchased 100% of the issued and outstanding capital stock of Tucker Energy Services Holdings, Inc. ("Tucker") effective April 2, 2018.

### Statement of Compliance

These condensed consolidated interim financial statements are prepared in accordance with International Accounting Standard 34, Interim Financial Reporting. These condensed consolidated interim financial statements do not include all the information and disclosures required in the annual financial statements, and should be read in conjunction with the Company's annual consolidated financial statements as at and for the year ended December 31, 2018.

Certain comparative figures have been reclassified to conform to the financial statement presentation adopted for the current period. Due to the maturation of the business and the acquisition of Tucker, STEP reassessed its operating segments. The realignment of operating segments assigned the separate disclosure of Corporate costs in addition to the Canadian Operations and U.S. Operations reportable segments (see Note 13). The Company also reclassified specified cost of sales and selling, general, and administrative costs.

These condensed consolidated interim financial statements were approved by the Board of Directors on May 7, 2019.

### Seasonality of operations

The Company's Canadian business is seasonal in nature with the periods of greatest activity being in the first, third and fourth quarters, and the least activity tending to be in the second quarter because of spring break-up. Spring break-up typically occurs between March and June. The Company's operating activities can also be affected by extended periods of adverse weather which can result in restrictions to the movement of heavy equipment. Activity in the southern and mid-continental United States is generally not as influenced by seasonal conditions.

### Critical accounting estimates and judgments

The preparation of these condensed consolidated interim financial statements requires management to make certain estimates and judgments concerning the reported amount of revenue and expenses and the carrying values of assets and liabilities. These estimates are based on historical experience and management's judgment. The estimation of anticipated future events involves uncertainty and therefore the estimates used by management in the preparation of the condensed consolidated interim financial statements may change as events unfold, additional knowledge is acquired or the environment in which the Company operates changes. The significant judgments made by management in applying the Company's accounting policies and the key sources of estimation uncertainty were the same as those that applied to the consolidated financial statements as at and for the year ended December 31, 2018.

## Changes in significant accounting policies

Except as described below, the same accounting policies and methods of computation were followed in preparation of these condensed consolidated interim financial statements as were followed in the preparation of the Company's annual consolidated financial statements for the year ended December 31, 2018.

*IFRS 16: Leases*
IFRS 16 is effective as of January 1, 2019. IFRS 16 replaces existing lease guidance including IAS 17, Leases and related interpretations. Upon identification of a lease contract, IFRS 16 requires the recognition of a right-of-use asset and lease liability. The Company has applied the standard using the modified retrospective approach in which the cumulative impact of initial application is recognized as an adjustment to the opening balance of retained earnings with no restatement of prior period information, subject to elected practical expedients.

At inception of a contract, the Company assesses whether a contract is, or contains a lease. A contract is, or contains a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. In order to perform this assessment, the Company determines whether: i.) The Company has the right to obtain substantially all of the economic benefits from use of the asset through the period use; and ii.) The Company has the right to direct the use of the identified asset.

The term of the lease is determined as the non-cancellable period of a lease and periods in which there is reasonable certainty the Company will exercise an option to extend or cancel a lease. The Company considers all relevant facts and circumstances that would create an economic incentive to extend or terminate a lease.

At the commencement date of a lease, the Company measures lease liabilities at the present value of remaining lease payments, discounted using the interest rate implicit in a lease, if that rate can be readily determined. If that rate cannot be readily determined, the Company uses its incremental borrowing rate. Prospectively, the carrying amount of lease liabilities is increased by interest, offset by lease payments made. The initial cost of right-of-use assets is measured as the value of the lease liability, adjusted for any lease incentives received and initial direct costs. Right-of-use assets are depreciated over the shorter of the lease term or the useful life of the asset and recognized as cost less any accumulated depreciation and any accumulated impairment losses. Right-of-use assets are presented within Property and Equipment (see Note 3). The Company primarily leases light duty vehicles, office buildings, service centers, and copiers. Recognition exemptions permitted include short term leases or leases for which the underlying asset is of low value. If a contract meets these criteria the Company expenses the payments in the consolidated statements of net (loss) income and other comprehensive (loss) income.

Upon adoption, previously recognized operating commitments disclosed in the annual consolidated financial statements for the year ended December 31, 2018 meeting IFRS 16 recognition criteria were measured at the present value of remaining future lease payments using the Company's incremental January 1, 2019 borrowing rate. The Company applied the following practical expedients on initial adoption of IFRS 16 for previously recognized operating commitments: account for leases with a remaining lease term of less than twelve months as at January 1, 2019 as short-term leases; account for lease payments as an expense for which the underlying asset is of low dollar value; and use hindsight in applying the new standard for lease terms where the contract contains options to extend or terminate the lease. There were no significant changes in the accounting for previously recognized finance lease obligations. The impact of adoption of IFRS 16 was a $7.2 million increase to lease liabilities, a $0.1 million decrease to accrued payables, a $6.9 million increase to property and equipment, and a $0.2 million decrease to retained earnings as at January 1, 2019 using an average incremental borrowing rate of 5.1%.

Reconciliation to Operating Lease Commitments

| | | January 1, 2019 |
|---|---|---|
| Operating leases capitalized included in commitments as at December 31, 2018 | $ | 6,848 |
| Estimate of lease extensions | | 1,098 |
| Discount | | (674) |
| Additional lease liability recognized due to adoption of IFRS 16 on January 1, 2019 | $ | 7,272 |

## NOTE 2 – INVENTORY

| As at | March 31, 2019 | December 31, 2018 |
|---|---|---|
| Coiled tubing | $ 6,658 | $ 6,412 |
| Sand and chemicals | 8,620 | 10,835 |
| Spare equipment/parts | 13,784 | 15,399 |
| Total Inventory | $ 29,062 | $ 32,646 |

During the three months ended March 31, 2019, the Company incurred a write-down of $0.1 million (March 31, 2018 - $0.6 million).

## NOTE 3 – PROPERTY AND EQUIPMENT

| | Land and buildings | Vehicles | Field equipment | Office equipment | Total |
|---|---|---|---|---|---|
| Cost: | | | | | |
| Balance at January 1, 2018 | $ 23,623 | $ 16,065 | $ 372,019 | $ 5,833 | $ 417,540 |
| Acquisition through business combination | 10,823 | 7,802 | 192,108 | - | 210,733 |
| Additions | 2,681 | 9,627 | 110,565 | 2,154 | 125,027 |
| Disposals | - | (5,361) | (2,136) | - | (7,497) |
| Effect of exchange rate changes | 692 | 884 | 16,814 | 42 | 18,432 |
| Balance at December 31, 2018 | 37,819 | 29,017 | 689,370 | 8,029 | 764,235 |
| Additions | 7,903 | 1,305 | 9,361 | 243 | 18,812 |
| Disposals | - | (3,691) | (170) | - | (3,861) |
| Effect of exchange rate changes | (222) | (281) | (6,410) | (15) | (6,928) |
| **Balance at March 31, 2019** | **$ 45,500** | **$ 26,350** | **$ 692,151** | **$ 8,257** | **$ 772,258** |
| | | | | | |
| Accumulated depreciation: | | | | | |
| Balance at January 1, 2018 | $ 2,498 | $ 4,464 | $ 70,087 | $ 4,113 | $ 81,162 |
| Depreciation | 1,455 | 7,926 | 73,372 | 1,287 | 84,040 |
| Disposals | - | (3,179) | (317) | - | (3,496) |
| Effect of exchange rate changes | 28 | 243 | 2,109 | 7 | 2,387 |
| Balance at December 31, 2018 | 3,981 | 9,454 | 145,251 | 5,407 | 164,093 |
| Depreciation | 956 | 2,246 | 21,545 | 320 | 25,067 |
| Disposals | - | (1,885) | (163) | - | (2,048) |
| Effect of exchange rate changes | (12) | (95) | (879) | (5) | (991) |
| **Balance at March 31, 2019** | **$ 4,925** | **$ 9,720** | **$ 165,754** | **$ 5,722** | **$ 186,121** |
| Carrying amounts: | | | | | |
| As at January 1, 2018 | $ 21,125 | $ 11,601 | $ 301,932 | $ 1,720 | $ 336,378 |
| As at December 31, 2018 | $ 33,838 | $ 19,563 | $ 544,119 | $ 2,622 | $ 600,142 |
| **As at March 31, 2019** | **$ 40,575** | **$ 16,630** | **$ 526,397** | **$ 2,535** | **$ 586,137** |

Included in field equipment at March 31, 2019 were assets under construction of $42.1 million (December 31, 2018 - $41.4 million). Assets under construction are not depreciated until they are substantially complete and available for use.

## Right-of-Use Assets

In addition to the previously recorded light duty vehicles, the Company added lease contracts for office buildings, service centers, and copiers as a result of the implementation of IFRS 16 (Note 1). The net carrying amount of the right-of-use assets measured under lease contracts included in property and equipment is as follows:

| As at March 31, 2019 | Land and buildings | Vehicles | Office equipment | Total |
|---|---|---|---|---|
| Cost: | $ 7,911 | $ 24,473 | $ 243 | $ 32,627 |
| Less: Accumulated depreciation | (548) | (8,967) | (3) | (9,518) |
| **Carrying amount** | **$ 7,363** | **$ 15,506** | **$ 240** | **$ 23,109** |

Depreciation expense on right-of-use assets recognized for the three months ending March 31, 2019 was $2.8 million.

## NOTE 4 – INTANGIBLE ASSETS AND GOODWILL

| | Intangibles | Goodwill |
|---|---|---|
| Cost: | | |
| Balance at January 1, 2018 | $ 3,543 | $ - |
| Acquisition through business combination | 35,626 | 129,599 |
| Impairment of Goodwill | - | (46,000) |
| Effect of exchange rate changes | 2,020 | 6,667 |
| Balance at December 31, 2018 | 41,189 | 90,266 |
| Effect of exchange rate changes | (800) | (1,919) |
| **Balance at March 31, 2019** | **$ 40,389** | **$ 88,347** |
| Accumulated depreciation: | | |
| Balance at January 1, 2018 | $ 3,184 | $ - |
| Amortization | 4,605 | - |
| Effect of exchange rate changes | 198 | - |
| Balance at December 31, 2018 | 7,987 | - |
| Amortization | 1,774 | - |
| Effect of exchange rate changes | (94) | - |
| **Balance at March 31, 2019** | **$ 9,667** | **$ -** |
| Carrying amounts: | | |
| As at January 1, 2018 | $ 359 | $ - |
| As at December 31, 2018 | $ 33,202 | $ 90,266 |
| **As at March 31, 2019** | **$ 30,722** | **$ 88,347** |

## NOTE 5 – LOANS AND BORROWINGS

On March 5, 2019 the Company amended its syndicated borrowing agreement. The Company's agreement is comprised of operating facilities (one Canadian and one U.S.) and a revolving facility (together the "Amended Credit Facilities"). The Amended Credit Facilities mature on April 2, 2021 and include a Canadian $330.0 million revolving credit facility, a Canadian $10.0 million operating facility and a U.S. $7.5 million operating facility. The maturity date of the Amended Credit Facilities may be extended for a period of up to 3 years with syndicate approval. The Amended Credit Facilities include a general security agreement providing a security interest over all present and after acquired personal property of the Company and all of its subsidiaries including mortgages on certain properties. An equity cure is available for the purposes of determining compliance with the Funded Debt to Adjusted bank EBITDA ratio. The equity cure is available for use up to two times, in non-consecutive quarters. Each use of the equity cure is limited to $25 million from the issuance of equity securities and must be utilized to repay borrowings under the Credit Facilities. Under the Amended Credit Facilities, any current and future leases that would have been accounted for as an operating lease at December 31, 2018 will continue to be recognized as operating leases for purposes of calculating financial covenants.

The Amended Credit Facilities includes certain financial and non-financial covenants, including:

1) Funded debt to Adjusted bank EBITDA ratio refers to the ratio of total outstanding interest-bearing debt including lease obligations and letters of credit less cash and cash equivalents held with approved financial institutions to earnings before interest, share-based compensation, non-recurring gains and losses on the sale of property and equipment, unrealized foreign exchange gains and losses, taxes, depreciation, amortization, impairment, unrealized foreign exchange forward contract (gain) loss and transaction costs ("Adjusted bank EBITDA") of the Company for the twelve preceding months. Also, realized foreign exchange (gain) loss is excluded from Adjusted bank EBITDA. These are differences from the Company's non-IFRS measure "Adjusted EBITDA". The Company is required to meet the following funded debt to adjusted bank EBITDA ratios:

| Quarters Ended | Required Funded debt to Adjusted bank EBITDA ratio |
|---|---|
| March 31, 2019 | 3.50:1 or less |
| June 30, 2019 | 4.00:1 or less |
| September 30, 2019 and December 31, 2019 | 4.50:1 or less |
| March 31, 2020 | 4.00:1 or less |
| June 30, 2020 | 3.50:1 or less |
| September 30, 2020 and thereafter | 3.00:1 or less |

At March 31, 2019, the Funded debt to Adjusted bank EBITDA ratio was 2.64:1.00.

2) Interest coverage ratio refers to the ratio of Adjusted bank EBITDA to interest expense for the preceding twelve months. Interest expense includes interest charges, capitalized interest, interest on lease obligations, fees payable in respect of letters of credit and letters of guarantee, and discounts incurred and fees payable in respect of bankers' acceptance advances. Interest on lease obligations for current and future leases which would have been accounted for as an operating lease at December 31, 2018 is not included in interest expense for purposes of calculating financial covenants. This ratio is not to fall below 3.00:1 or less.

   At March 31, 2019, the Interest Coverage Ratio was 6.92:1.00.

Interest is payable monthly, at the bank's prime lending rate plus 50 basis points to 300 basis points depending on certain financial ratios of the Company. The effective borrowing rate for loans and borrowings for the first quarter of 2019 was approximately 4.28%. At March 31, 2019, the full amount of the facility was available to be drawn on the Amended Credit Facilities of which there was $255.4 million outstanding and the Company was in compliance with all covenants.

## NOTE 6 – LEASE OBLIGATIONS

The Company has lease contracts for light duty vehicles, office buildings, service centers, and copiers. The maturity date of these contracts range from April 2019 to February 2026 with interest rates ranging from 2.26% to 10.67%. Lease payments made by the Company are blended interest and principal payments. Lease obligations recognized in 2018 included light duty vehicles which were recognized prior to the adoption of IFRS 16. The Company's lease obligations are payable as follows:

| As at, | | March 31, 2019 | | December 31, 2018 |
|---|---|---|---|---|
| Future minimum lease payments | $ | **23,654** | $ | 17,546 |
| Discount | | **(1,772)** | | (1,047) |
| Present value of minimum lease payments | $ | **21,882** | $ | 16,499 |
| Presented as: | | | | |
| Current portion of lease obligations | $ | **8,635** | $ | 8,489 |
| Lease obligations | $ | **13,247** | $ | 8,010 |

### Commitments

The following table summarizes the Company's estimated commitments as at March 31, 2019 for the following five years and thereafter:

| | | 2019 | | 2020 | | 2021 | | 2022 | | 2023 | | Thereafter | | Total |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Operating portion of lease obligations(1) | $ | 847 | $ | 1,429 | $ | 1,416 | $ | 1,256 | $ | 1,243 | $ | 412 | $ | 6,603 |
| Short term and low value lease obligations(1) | | 1,530 | | - | | - | | - | | - | | - | | 1,530 |
| Total commitments | $ | 2,377 | $ | 1,429 | $ | 1,416 | $ | 1,256 | $ | 1,243 | $ | 412 | $ | 8,133 |

(1) Includes U.S. obligations at a forecast exchange rate of 1 USD = 1.337 CAD.

The operating portion of lease obligations relate to leases of certain shop and office space with lease terms of between 1 years and 7 years. The total expense recognized in the current period for short term and low value lease obligations was $0.7 million. As at March 31, 2019, the Company has $6.2 million (December 31, 2018 - $8.2 million) of commitments related to capital expenditures. This commitment is expected to be incurred in fiscal 2019.

## NOTE 7 – SHAREHOLDERS' EQUITY AND ACCUMULATED OTHER COMPREHENSIVE INCOME

### Share capital

The Company is authorized to issue an unlimited number of common shares. The shares have no par value. All issued shares are fully paid.

| | Shares # | | Amount |
|---|---|---|---|
| Balance at January 1, 2018 | 60,309,738 | $ | 369,436 |
| Issued – public offering – April 2, 2018 | 6,055,000 | | 56,312 |
| Issued – exercise of share-based instruments | 317,581 | | 2,841 |
| Share issue costs (net of deferred tax) | - | | (2,095) |
| Balance at December 31, 2018 | 66,682,319 | | 426,494 |
| Issued – exercise of share-based instruments | 20,067 | | 275 |
| **Balance at March 31, 2019** | **66,702,386** | **$** | **426,769** |

On April 2, 2018, the Company closed an equity financing raising gross proceeds of $56.3 million by issuing 6,055,000 subscription receipts for $9.30 each. The proceeds of the offering were used to partially fund the acquisition. Total costs related to the equity offering were $2.9 million less $0.8 million deferred tax. These were classified as a reduction of share capital.

## NOTE 8 – SHARE-BASED COMPENSATION

### Equity settled share-based instruments

| | New stock options | Restricted share units | Performance share units | Prior stock options | Performance warrants | Total |
|---|---|---|---|---|---|---|
| Balance at January 1, 2018 | - | 223,467 | 208,079 | 4,074,849 | 8,758,680 | 13,265,075 |
| Granted | 201,987 | 659,736 | 318,819 | - | - | 1,180,542 |
| Added via performance factor | - | - | 19,777 | - | - | 19,777 |
| Exercised | - | (71,574) | (13,886) | (247,324) | (317,932) | (650,716) |
| Forfeited/Expired | - | (41,055) | (27,473) | (77,797) | (279,960) | (426,285) |
| **Outstanding at December 31, 2018** | **201,987** | **770,574** | **505,316** | **3,749,728** | **8,160,788** | **13,388,393** |
| Exercisable at December 31, 2018 | - | - | - | 3,023,691 | 5,246,838 | 8,270,529 |

| | New stock options | Restricted share units | Performance share units | Prior stock options | Performance warrants | Total |
|---|---|---|---|---|---|---|
| Balance at January 1, 2019 | 201,987 | 770,574 | 505,316 | 3,749,728 | 8,160,788 | 13,388,393 |
| Granted | - | - | - | - | - | - |
| Revised via performance factor | - | - | (13,128) | - | - | (13,128) |
| Exercised | - | (19,313) | (9,034) | - | - | (28,347) |
| Forfeited/Expired | - | (43,581) | - | (134,302) | (436,120) | (614,003) |
| **Outstanding at March 31, 2019** | **201,987** | **707,680** | **483,154** | **3,615,426** | **7,724,668** | **12,732,915** |
| Exercisable at March 31, 2019 | - | - | - | 2,990,716 | 5,117,518 | 8,108,234 |

### Cash settled share-based instruments

The Company has a cash-settled deferred share unit plan for its directors. The fair value of the liability and the corresponding expense is charged to net income in the period.

| | March 31, 2019 | December 31, 2018 |
|---|---|---|
| Outstanding units at beginning of period | **137,634** | 47,742 |
| Granted | **32,910** | 89,891 |
| **Outstanding units at end of period** | **170,544** | 137,634 |
| Exercisable at end of period | **170,544** | 137,634 |

### Share-based compensation expense

The composition of share-based compensation expense incurred was:

| Three months ended March 31, | 2019 | 2018 |
|---|---|---|
| New stock options | $ **89** | $ - |
| Prior stock options | **(3)** | 497 |
| Performance warrants | **(25)** | 535 |
| Deferred share units (cash settled) | **83** | 35 |
| Performance share units | **459** | 369 |
| Restricted share units | **660** | 340 |
| Total share-based compensation expense | $ **1,263** | $ 1,776 |

## NOTE 9 – PER SHARE COMPUTATIONS

| Three months ended March 31, | 2019 | 2018 |
|---|---|---|
| Weighted average number of shares outstanding - basic | 66,683,211 | 60,420,318 |
| Dilutive impact of stock based compensation instruments | - | 2,071,880 |
| Weighted average number of shares outstanding - diluted | 66,683,211 | 62,492,198 |

For the three months ended March 31, 2019, 3.6 million prior stock options, 7.7 million performance warrants and 0.2 million new options were excluded from the diluted weighted average number of shares calculation as their effect would have been anti-dilutive (March 31, 2018: 0.1 million stock options and 5.9 million performance warrants).

## NOTE 10 – FINANCE COSTS

| Three months ended March 31, | | 2019 | | 2018 |
|---|---|---|---|---|
| Interest on loans and borrowings | $ | 2,667 | $ | 78 |
| Interest on lease obligations | | 245 | | 126 |
| Interest income | | (14) | | (128) |
| Deferred financing charges | | 270 | | 53 |
| Other | | 85 | | 16 |
| Total finance costs | $ | 3,253 | $ | 145 |

## NOTE 11 – FINANCIAL INSTRUMENTS

### Accounting classifications and fair values

Cash and cash equivalents, trade and other receivables, trade and other payables, income tax payable, lease obligations and loans and borrowings are initially recognized at fair value and subsequently measured at amortized cost. The carrying value of cash and cash equivalents, trade and other receivables, trade and other payables and income tax payable, approximate their fair value due to the relatively short periods to maturity of the instruments. Loans and borrowings utilize floating rates and therefore fair market value approximates carrying value. The Company classifies its financial instruments measured at fair value according to the following hierarchy based on the amount of observable inputs used to value the instrument. Assessment of the significance of a particular input to the fair value measurement requires judgment and may affect the placement within the fair value hierarchy.

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

Foreign exchange forward contracts are classified and measured at fair value through profit or loss. Changes in fair value are recognized as they arise and are determined using quoted forward exchange rates at the reporting date (level 2). During the first quarter of 2019, there were no transfers between levels in the fair value hierarchy.

### Credit risk

The Company's aged trade and accounts receivable are as follows:

| As at, | March 31, 2019 | December 31, 2018 |
|---|---|---|
| Current (0 to 30 days from invoice date) | $ 100,614 | $ 66,844 |
| 31 - 60 days | 27,481 | 45,406 |
| 61 - 90 days | 3,625 | 8,708 |
| 91+ days | 2,403 | 3,782 |
| Receivables from trade clients | 134,123 | 124,740 |
| Other amounts | 2,406 | 2,588 |
| Allowance for doubtful accounts | (2,725) | (2,775) |
| Total trade and other receivables | $ 133,804 | $ 124,553 |

The Company's objective is to minimize credit losses. The Company's objectives, processes and policies for managing credit risk have not changed from the prior year.

### Liquidity risk

Liquidity risk is the risk that the Company will be unable to fulfill its obligations on a timely basis or at a reasonable cost. The Company's objective in managing liquidity risk is to maintain sufficient available resources to meet its liquidity requirements at any point. The Company achieves this by managing its capital spending and maintaining sufficient funds for anticipated short-term spending in cash and cash equivalent account.

The expected timing of cash outflows relating to financial liabilities on the statement of financial position as at March 31, 2019 are:

| | 2019 | 2020 | 2021 | 2022 | Thereafter | Total |
|---|---|---|---|---|---|---|
| Lease obligations[1] | $ 7,863 | $ 8,087 | $ 4,649 | $ 1,507 | $ 1,548 | $ 23,654 |
| Trade and other payables | 87,433 | - | - | - | - | 87,433 |
| Income tax payable | 1,835 | - | - | - | - | 1,835 |
| Loans and borrowings [2] | 8,236 | 10,961 | 258,165 | - | - | 277,362 |
| | $ 105,367 | $ 19,048 | $ 262,814 | $ 1,507 | $ 1,548 | $ 390,284 |

(1) Includes interest portion of lease obligations.
(2) Includes interest calculated based on principle and rate outstanding at March 31, 2019, both amounts are variable in nature.

The Company anticipates that its existing capital resources, including the credit facilities and cash flows from operations, will be adequate to satisfy its liquidity requirements over the next 12 months. Reductions in the Company's clients' cash flow or difficulty in their ability to source debt or equity could negatively impact the Company's assessment of liquidity risk.

### Market risk

During the first quarter of 2019, the Company settled forward exchange forward contracts outstanding at December 31, 2018, resulting in a realized loss of $0.3 million. The goal of these instruments was to limit exposure to U.S. dollar fluctuations.

## NOTE 12 - CONTINGENCIES AND PROVISIONS

### Litigation

Periodically, the Company may become involved in, named as a party to, or be the subject of various legal proceedings which are usually related to normal operational or labor issues. The results of such legal proceedings or related matters cannot be determined with certainty. The Company's assessment of the likely outcome of such matters is based on input from internal examination of the facts of the case and advice from external legal advisors, which is based on their judgment of a number of factors including the applicable legal framework and precedents, relevant financial and operational information, and other evidence and facts specific to the matter as known at the time of the assessment.

In January 2017, Calfrac Well Services Ltd. ("Calfrac") filed a statement of claim in the Judicial District of Calgary in the Court of Queen's Bench against the Company and an employee of the Company seeking $10.0 million in damages among other relief. Calfrac alleges that the employee, who is a former employee of Calfrac, misappropriated certain competitively sensitive materials from Calfrac. Calfrac further alleges that STEP benefited or made use of such materials, resulting in damages to Calfrac. STEP is presently investigating the claim and at this time intends to contest allegations made in the claim. While management does not believe that this action will have a material adverse effect on the business or financial condition of the Company, no assurance can be given as to the final outcome of this or any other legal proceeding. If this claim, or any claims to which the Company may be subject in the future, were to be concluded in a manner adverse to the Company or if the Company elects to settle one or more of such claims, it could have a material adverse effect on its business, financial condition, results of operations and cash flows.

## NOTE 13 – OPERATING SEGMENTS

Effective January 1, 2019, the Company reorganized the composition of its reportable segments due to the maturation of the business and acquisition of Tucker. The realignment of operating segments created the separate disclosure of Corporate costs in addition to Canadian Operations and U.S. Operations segments. The Company has restated prior period information to align with the new composition of operating segments.

The Company's services are conducted by the Canadian Operations and the U.S. Operations segments. The results of each operating segment are summarized below. Transactions between the segments are recorded at fair value and have been eliminated upon consolidation.

### Segmented operating results and activity

| Three months ended March 31, 2019 | Canadian Operations | U.S. Operations | Corporate | Total |
|---|---|---|---|---|
| Revenue | | | | |
| Fracturing | $ 82,352 | $ 40,234 | $ - | $ 122,586 |
| Coiled tubing | 25,874 | 28,009 | - | 53,883 |
| Total Revenue | 108,226 | 68,243 | - | 176,469 |
| Expenses | | | | |
| Cost of sales | 95,191 | 71,520 | 628 | 167,339 |
| Selling, general and administrative | 2,296 | 2,149 | 4,398 | 8,843 |
| Results from operating activities | 10,739 | (5,426) | (5,026) | 287 |
| Finance Costs | - | - | 3,253 | 3,253 |
| Foreign exchange (gain) loss | (1,264) | (1) | - | (1,265) |
| Gain on disposal of property and equipment | (603) | (69) | - | (672) |
| Amortization of intangible assets | 9 | 1,765 | - | 1,774 |
| Loss on foreign exchange forward contracts | - | - | 383 | 383 |
| Net (loss) income before income tax | 12,597 | (7,121) | (8,662) | (3,186) |
| | | | | |
| Capital expenditures [1] | $ 11,605 | $ 7,207 | $ - | $ 18,812 |
| Total assets as at March 31, 2019 | $ 425,994 | $ 452,536 | $ 2,366 | $ 880,896 |
| Total liabilities as at March 31, 2019 | $ 328,128 | $ 82,533 | $ - | $ 410,661 |

| Three months ended March 31, 2018 | | Canadian Operations | | U.S. Operations | | Corporate | | Total |
|---|---|---|---|---|---|---|---|---|
| Revenue | | | | | | | | |
| Fracturing | $ | 127,606 | $ | - | $ | - | $ | 127,606 |
| Coiled tubing | | 37,524 | | 22,463 | | - | | 59,987 |
| Total Revenue | | 165,130 | | 22,463 | | - | | 187,593 |
| Expenses | | | | | | | | |
| Cost of sales | | 133,918 | | 15,461 | | 579 | | 149,958 |
| Selling, general and administrative | | 3,914 | | 837 | | 3,189 | | 7,940 |
| Results from operating activities | | 27,298 | | 6,165 | | (3,768) | | 29,695 |
| Finance Costs | | - | | - | | 145 | | 145 |
| Foreign exchange (gain) loss | | 135 | | - | | - | | 135 |
| Gain on disposal of property and equipment | | (181) | | 64 | | - | | (117) |
| Transaction costs | | - | | - | | 1,153 | | 1,153 |
| Amortization of intangible assets | | 10 | | - | | - | | 10 |
| Loss on foreign exchange forward contracts | | - | | - | | 1,771 | | 1,771 |
| Net (loss) income before income tax | | 27,334 | | 6,101 | | (6,837) | | 26,598 |
| | | | | | | | | |
| Capital expenditures (1) | $ | 16,342 | $ | 8,255 | $ | - | $ | 24,597 |
| Total assets as at December 31, 2018 | $ | 416,191 | $ | 469,167 | $ | 2,550 | $ | 887,908 |
| Total liabilities as at December 31, 2018 | $ | 329,383 | $ | 79,921 | $ | - | $ | 409,304 |

(1) Capital expenditures include non-cash expenditures from the addition of leased right-of-use assets.

# CORPORATE INFORMATION

## Management

Regan Davis
President & Chief Executive Officer

Michael Kelly
Executive Vice President & Chief Financial Officer

Steve Glanville
Vice President Operations & Chief Operating Officer

Mike Burvill
President US Operations

Rory Thompson
President Canadian Operations

Brock Duhon
Vice President Coiled Tubing and Open Hole Wireline Services – U.S.

Lori McLeod-Hill
Vice President Finance

## Directors

Douglas Freel (1) – Chairman

Evelyn Angelle (1)

Regan Davis (3)

Jeremy Gackle (1) (2)

Donna Garbutt (3)

James Harbilas (1) (2)

Jason Skehar (2)(3)

## Corporate office

Bow Valley Square II
#1200, 205 – 5 Ave SW
Calgary, Alberta T2P 2V7

## Registered office

4300, 888 – 3rd Street SW
Calgary, Alberta T2P 5C5

## Website

www.stepenergyservices.com

## Trustee and transfer agent

TSX Trust Company
Calgary, Alberta and Toronto, Ontario

## Bank

ATB Corporate Financial Services

## Auditors

KPMG LLP
Chartered Professional Accountants
Calgary, Alberta

## Legal Counsel

Stikeman Elliott LLP

## Stock Symbol

"STEP"
Toronto Stock Exchange

Member of:
1. Audit Committee
2. Compensation and Corporate Governance Committee
3. Health and Safety Committee