Condensed Consolidated Interim Statements of Financial Position

Stated in thousands of dollars

(Unaudited)

As at	March 31, 2021	December 31, 2020
Assets		
Current Assets		
Accounts receivable	**$ 30,240**	$ 29,796
Prepaid expenses and deposits	**5,921**	5,253
	36,161	35,049
Petroleum and natural gas properties (note 4)	**563,709**	672,915
	$ 599,870	$ 707,964
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	**$ 56,354**	$ 51,265
Fair value of financial contracts (note 6)	**41,989**	18,883
Bank debt (note 7)	**170,650**	260,908
Current portion of lease and other obligations (note 14)	**8,751**	8,796
Current portion of decommissioning obligations (note 9)	**6,000**	4,000
	283,744	343,852
Fair value of financial contracts (note 6)	**2,766**	3,778
Term debt (note 7)	**40,649**	32,718
Convertible debentures (note 8)	**71,842**	71,181
Decommissioning obligations (note 9)	**246,393**	290,655
Long term lease and other obligations (note 14)	**29,274**	31,996
Shareholders' equity		
Share capital	**1,482,249**	1,482,249
Equity component of convertible debentures (note 8)	**6,266**	6,266
Contributed surplus	**53,521**	52,118
Deficit	**(1,616,834)**	(1,606,849)
	(74,798)	(66,216)
Commitments (note 13)		
Subsequent event (note 15)		
	$ 599,870	$ 707,964

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

Condensed Consolidated Interim Statements of Loss and Comprehensive Loss

Stated in thousands of dollars, except per share amounts

(Unaudited)

	Three Months Ended March 31, 2021	2020
Petroleum and natural gas revenue (note 11)	$ **80,694**	$ 63,706
Processing income (note 11)	**1,089**	1,720
Royalties	**(8,477)**	(8,505)
Realized gain (loss) on financial contracts	**(16,822)**	13,509
Unrealized gain (loss) on financial contracts (note 6)	**(23,500)**	31,187
	32,984	101,617
Expenses		
Operating	**28,083**	28,199
Transportation	**1,539**	3,046
General and administrative	**2,957**	3,416
Transaction costs	**1,700**	98
Stock-based compensation (note 10)	**932**	1,120
Depletion and depreciation (note 4)	**21,631**	36,113
Impairment (note 5)	**—**	590,628
Finance expense	**9,074**	13,232
Gain on disposal of petroleum and natural gas properties (note 4)	**(22,294)**	—
Other costs (income) (note 12)	**(653)**	31
	42,969	675,883
Loss before income taxes	**(9,985)**	(574,266)
Deferred income tax expense	**—**	40,961
Net loss and comprehensive loss for the period	$ **(9,985)**	$ (615,227)
Loss per share (note 10)		
Basic	$ **(0.03)**	$ (1.85)
Diluted	$ **(0.03)**	$ (1.85)

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

Condensed Consolidated Interim Statements of Changes in Shareholders' Equity

Stated in thousands of dollars, except share amounts

(Unaudited)

	Number of common shares	Share capital	Convertible debentures - equity portion	Contributed surplus	Deficit	Total equity
Balance at December 31, 2019	326,330,027	$ 1,466,506	$ 6,266	$ 52,224	$ (853,689)	$ 671,307
Net loss for the period	—	—	—	—	(615,227)	(615,227)
Share issue costs, net of tax of $23	—	(64)	—	—	—	(64)
Flow-through shares issued	8,738,889	10,268	—	—	—	10,268
Premium on flow-through shares	—	(1,442)	—	—	—	(1,442)
Stock-based compensation	—	—	—	1,877	—	1,877
Dividends	—	—	—	—	(5,863)	(5,863)
Balance at March 31, 2020	335,068,916	$ 1,475,268	$ 6,266	$ 54,101	$ (1,474,779)	$ 60,856
Balance at December 31, 2020	339,784,739	$ 1,482,249	$ 6,266	$ 52,118	$ (1,606,849)	$ (66,216)
Net loss for the period	—	—	—	—	(9,985)	(9,985)
Stock-based compensation	—	—	—	1,403	—	1,403
Balance at March 31, 2021	**339,784,739**	**$ 1,482,249**	**$ 6,266**	**$ 53,521**	**$ (1,616,834)**	**$ (74,798)**

(1) RSA and PSA defined as restricted share and performance share awards

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

Condensed Consolidated Interim Statements of Cash Flows

Stated in thousands of dollars

(Unaudited)

	Three Months Ended March 31, 2021	2020
Cash provided by (used in)		
Operating		
Net loss	**$ (9,985)**	$ (615,227)
Gain on disposal of petroleum and natural gas properties	**(22,294)**	—
Unrealized loss (gain) on financial contracts	**23,500**	(31,187)
Finance expense	**9,074**	13,232
Interest expense	**(8,148)**	(5,741)
Depletion and depreciation	**21,631**	36,113
Impairment	**—**	590,628
Decommissioning expenditures	**(1,481)**	(1,540)
Other costs (income)	**(653)**	31
Stock-based compensation	**932**	1,120
Deferred income tax expense	**—**	40,961
Change in non-cash working capital	**2,974**	14,748
Cash flow from operating activities	**15,550**	43,138
Financing		
Bank debt	**(90,258)**	(10,600)
Term debt	**7,500**	—
Dividends paid	**—**	(8,304)
Issuance of flow-through shares	**—**	10,268
Payments on lease obligations	**(2,139)**	(1,967)
Share issue costs	**—**	(87)
Cash flow used in financing activities	**(84,897)**	(10,690)
Investing		
Petroleum and natural gas properties	**(31,898)**	(32,504)
Disposition of petroleum and natural gas properties	**102,591**	—
Change in non-cash working capital	**(1,346)**	56
Cash flow from (used in) investing activities	**69,347**	(32,448)
Change in cash	**—**	—
Cash, beginning of the period	**—**	—
Cash, end of the period	**$ —**	$ —

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Tabular amounts are in thousands of dollars, except share and per share data

1. REPORTING ENTITY

Surge Energy Inc.'s (the "Corporation" or "Surge") business consists of the exploration, development and production of oil and gas from properties in western Canada. The address of Surge's registered office is 2100, 635-8th Avenue SW, Calgary, Alberta, Canada, T2P 3M3. The consolidated financial statements include the accounts of the Corporation and its wholly-owned subsidiaries.

2. BASIS OF PREPARATION

Statement of compliance

These condensed consolidated interim financial statements have been prepared in accordance with International Accounting Standard 34, "Interim Financial Reporting" and using the accounting policies outlined by the Corporation in its annual consolidated financial statements for the year ended December 31, 2020. These condensed consolidated interim financial statements do not include all of the information required for full annual financial statements. These condensed consolidated interim financial statements should be read in conjunction with the annual financial statements for the year ended December 31, 2020.

For matters relating to the COVID-19 pandemic, refer to Note 2 "Basis of preparation" in the consolidated financial statements as at December 31, 2020.

The condensed consolidated interim financial statements were authorized for issuance by the Board of Directors on May 14, 2021.

3. SIGNIFICANT ACCOUNTING POLICIES

These condensed consolidated interim financial statements at March 31, 2021 have been prepared following the same accounting policies as the consolidated financial statements as at December 31, 2020.

4. PETROLEUM AND NATURAL GAS PROPERTIES

Petroleum and Natural Gas Properties

		Total
Balance at December 31, 2019	$	2,729,660
Acquisitions		—
Dispositions		(56,219)
Additions		52,773
Right of use assets		2,209
Change in decommissioning obligations		30,901
Capitalized stock-based compensation		1,170
Transfer to Assets held for sale		—
Balance at December 31, 2020	$	2,760,494
Dispositions		(369,488)
Additions		31,898
Right of use assets		(269)
Change in decommissioning obligations		(28,381)
Capitalized stock-based compensation		471
Balance at March 31, 2021	**$**	**2,394,725**

		Total
Accumulated depletion and depreciation		
Balance at December 31, 2019	$	(1,393,815)
Depletion and depreciation expense		(105,042)
Impairment		(628,053)
Dispositions		39,331
Balance at December 31, 2020	$	(2,087,579)
Depletion and depreciation expense		(21,631)
Dispositions		278,194
Balance at March 31, 2021	**$**	**(1,831,016)**

		Total
Carrying amounts		
At December 31, 2020	$	672,915
At March 31, 2021	**$**	**563,709**

The calculation of depletion and depreciation expense for the period ended March 31, 2021 included an estimated $817.1 million (December 31, 2020 - $839.4 million) for future development costs associated with proved plus probable reserves and deducted $57.9 million (December 31, 2020 - $59.6 million) for the estimated salvage value of production equipment and facilities.

2021 Dispositions

During the period ended March 31, 2021, the Corporation disposed of certain assets in Southeast Alberta and Northeast Alberta for cash proceeds of $102.6 million. The assets had a carrying value of $93.4 million and an associated decommissioning liability of $13.1 million, resulting in a gain on disposal of $22.3 million.

5. IMPAIRMENT

	Three Months Ended March 31, 2021	2020
Impairment of petroleum and natural gas properties	—	590,628

For the period ended March 31, 2021, the Corporation determined there were no indicators of impairment in any of the cash generating units and no indications that impairment losses recognized in prior periods are to be reversed.

Under IFRS, deferred income tax assets may only be recognized to the extent that it is probable that future taxable profits will be available against which the unused tax losses and deductible temporary differences can be utilized. Accordingly, the Corporation has not recognized a total deferred income tax asset of approximately $205.4 million as at March 31, 2021.

2020 Impairment

Refer to Note 6 "Impairment" in the consolidated financial statements as at December 31, 2020.

6. RISK MANAGEMENT

At March 31, 2021, the following risk management contracts were outstanding with an asset fair market value of nil and a liability fair market value of $44.8 million (December 31, 2020 – asset of nil and liability of $22.7 million):

West Texas Intermediate Crude Oil Derivative Contracts (WTI)

	Swaps		Collars			Three-way Collar			
Period	Volumes (bbls/d)	Average Price (CAD/bbl)	Volumes (bbls/d)	Average Bought Put (CAD/bbl)	Average Sold Call (CAD/bbl)	Volumes (bbls/d)	Average Sold Put (CAD/bbl)	Average Bought Put (CAD/bbl)	Average Sold Call (CAD/bbl)
Qtr. 2 2021	6,167	$53.32	950	$53.53	$60.41	500	$38.96	$49.02	$64.10
Qtr. 3 2021	4,684	$55.02	1,700	$53.59	$61.55	250	$43.99	$54.04	$64.10
Qtr. 4 2021	4,534	$55.33	1,450	$53.34	$61.64	250	$43.99	$54.04	$64.10
Qtr. 1 2022	1,000	$59.11	2,000	$55.00	$69.23	500	$60.33	$72.89	$90.49

Western Canadian Select Derivative Contracts (WCS)

	Swaps	
Period	Volumes (bbls/d)	Average Price (CAD/bbl)
Qtr. 2 2021	6,000	$(17.56)
Qtr. 3 2021	5,000	$(17.34)
Qtr. 4 2021	2,500	$(16.32)
Qtr. 1 2022	1,000	$(15.35)
Qtr. 2 2022	1,000	$(15.35)

Mixed Sweet Blend Derivative Contracts (MSW)

	Swaps	
Period	Volumes (bbls/d)	Average Price (CAD/bbl)
Qtr. 2 2021	2,000	$(6.78)
Qtr. 3 2021	2,250	$(6.64)
Qtr. 4 2021	1,500	$(6.62)

Natural Gas Derivative Contracts

	Chicago Swaps		Chicago Collars			AECO Swaps	
Period	Volumes (MMBtu/d)	Average Price (CAD/MMBtu)	Volumes (MMBtu/d)	Average Bought Put (CAD/MMBtu)	Average Sold Call (CAD/MMBtu)	Volumes (GJ/d)	Average Price (CAD/GJ)
Qtr. 2 2021	3,000	$3.17	3,000	$2.70	$3.64	4,000	$2.40
Qtr. 3 2021	3,000	$3.17	3,000	$2.70	$3.64	2,000	$2.12
Qtr. 4 2021	1,011	$3.17	1,011	$2.70	$3.64	3,326	$2.40
Qtr. 1 2022						2,000	$2.83

Interest Rate Derivative Contracts

Type	Term	Notional Amount (CAD$)	Surge Receives	Surge Pays	Fixed Rate SGY Pays
Fixed-to-Floating Rate Swap	Feb 2018 - Feb 2023	$100,000,000	Floating Rate	Fixed Rate	Semi-Annual Step Up 1. Beginning at 1.786% 2. Ending at 2.714% 3. Averaging 2.479%
Fixed-to-Floating Rate Swap	Jul 2019 - Jun 2024	$50,000,000	Floating Rate	Fixed Rate	1.7850%

The following table summarizes the sensitivity of the fair value of the Corporation’s market risk management positions to fluctuations in natural gas prices, crude oil prices and interest rates. All such fluctuations were evaluated independently, with all other variables held constant. Fluctuations in the following on the respective derivative contracts would have had the following impact on the net earnings:

Net earnings impact for the period ended March 31, 2021	Increase	Decrease
Crude Oil - Change of +/- $1.00	(3,102)	3,102
Natural Gas - Change of +/- $0.10	(174)	174
Interest rate - Change of +/- 100 points	1,125	(1,125)

7. DEBT

Bank Debt

As at March 31, 2021, the Corporation had a total commitment of $215.0 million, being the aggregate of a committed revolving term facility of $120.0 million, a committed non-revolving term facility of $75.0 million, and an operating loan facility of $20.0 million, with a syndicate of banks. As at March 31, 2021, the Corporation had $95.7 million drawn on its committed revolving term facility and $75.0 million drawn on its committed non-revolving term facility. The revolving term commitment will continue to revolve until the next scheduled borrowing base redetermination date on or before November 30, 2021. If a borrowing base redetermination has not occurred prior to October 1, 2021, the total commitment will be reduced from $215.0 million to $205.0 million. On completion of the flow-through share financing discussed in Note 15 "Subsequent Event", the maturity date of the total commitment has been extended to July 1, 2022. As the available lending limits of the facilities are based on the syndicate's interpretation of the Corporation's reserves, commodity prices and decommissioning obligations, there can be no assurance that the amount of the available facilities will not decrease at the next scheduled review. In the current pricing environment, there is an increased risk that the lenders may decrease the amount available under the credit facilities and the decreases could be material. Interest rates vary depending on the ratio of Senior Debt to EBITDA (as defined in the lending agreement). As at March 31, 2021, the Corporation had an effective interest rate of prime plus 3.50 percent on the revolving term/operating loan facility (December 31, 2020 – prime plus 3.50 percent) and an effective interest rate of prime plus 6.50 percent on the non-revolving term facility (December 31, 2020 - prime plus 6.50 percent).

The facilities are secured by a general assignment of book debts, debentures of $1.5 billion with a floating charge over all assets of the Corporation with a negative pledge and undertaking to provide fixed charges on the major producing petroleum and natural gas properties at the request of the bank.

Term Debt

As at March 31, 2021, the Corporation had a term loan of $40 million plus capitalized interest with Business Development Bank of Canada, for a four year, non-revolving second lien term facility, maturing on November 17, 2024. Interest on the outstanding term loan will accrue and be added to the principal amount (capitalized) in the first year. Interest on the outstanding term loan will be due and payable monthly by the Corporation thereafter. Interest on borrowings are summarized as follows:

i. for the period between November 17, 2020 and the first anniversary date, at a per annum rate equal to 5.0 percent;

ii. thereafter until the second anniversary date, at a per annum rate equal to the greater of: the senior interest rate plus 1.0 percent; and 6.0 percent;

iii. thereafter until the third anniversary date, at a per annum rate equal to the greater of: the senior interest rate plus 2.0 percent; and 7.0 percent;

iv. thereafter, at a per annum rate equal to the greater of: the senior interest rate plus 3.0 percent; and 8.0 percent.

As at March 31, 2021, the Corporation had an effective interest rate of 5.0 percent on the non-revolving term facility (December 31, 2020 - 5.0 percent).

As at March 31, 2021, the Corporation was compliant with all restrictions in its first and second lien credit agreements.

8. CONVERTIBLE DEBENTURES

Convertible Debentures

	Number of convertible debentures	Liability Component	Equity Component
Balance at December 31, 2019	79,000	68,699	6,266
Accretion of discount	—	2,482	—
Balance at December 31, 2020	79,000	71,181	6,266
Accretion of discount	—	661	—
Balance at March 31, 2021	**79,000**	**71,842**	**6,266**

The fair value of the convertible debentures at March 31, 2021 was $68.1 million using quoted market prices on the TSX (level 1 fair value).

9. DECOMMISSIONING OBLIGATIONS

The Corporation’s decommissioning obligations result from net ownership interests in petroleum and natural gas assets including well sites, gathering systems and processing facilities. The Corporation estimates the total uninflated and undiscounted amount of cash flows required to settle its decommissioning obligations is approximately $265.0 million (December 31, 2020 – $279.7 million). These payments are expected to be made over the next 20 years with the majority of costs to be incurred between 2021 and 2041. A risk free rate of 1.97 percent (December 31, 2020 – 1.00 percent) and an inflation rate of 1.69 percent (December 31, 2020 – 1.28 percent) was used to calculate the decommissioning obligations.

A reconciliation of the decommissioning obligations is provided below:

	March 31, 2021	December 31, 2020
Balance, beginning of period	**$ 294,655**	$ 275,339
Liabilities related to dispositions	**(13,158)**	(5,757)
Change in estimate [1]	**(29,482)**	28,809
Liabilities incurred	**1,101**	2,092
Accretion expense	**1,240**	3,425
Site rehabilitation program grant	**(482)**	(4,948)
Decommissioning expenditures	**(1,481)**	(4,305)
Balance, end of period	**$ 252,393**	$ 294,655
Expected to be incurred within one year	**$ 6,000**	$ 4,000
Expected to be incurred beyond one year	**$ 246,393**	$ 290,655

[1]The change in estimate was primarily the result of the change in discount and inflation rates.

During the period ended March 31, 2021, approximately $0.5 million was granted to Surge through the Alberta Site Rehabilitation Program ("SRP") to pay service companies to complete abandonment and reclamation work.

10. SHARE CAPITAL

(a) Flow-through Share Issuance

In November 2019, the Corporation issued 2.1 million flow-through shares related to Canadian exploration expenditures at a price of $1.18 per share for total gross proceeds of $2.5 million. The implied premium on the flow-through shares of $0.17 per share or $0.4 million was recorded as a flow-through share liability. As at March 31, 2021, the Corporation had incurred $0.1 million of the qualifying exploration expenditures, with the remaining commitment to be spent in 2021 based on an extension to flow through share commitments issued by the Federal Government in December of 2020.

(b) Restricted and Performance Share Award Incentive Plan

The Corporation has a Stock Incentive Plan which authorizes the Board of Directors to grant restricted share awards ("RSAs") and performance share awards ("PSAs") to directors, officers, employees and certain consultants of Surge.

Subject to the terms and conditions of the plan, each RSA entitles the holder to an award value to be typically paid as to one-third on each of the first, second and third anniversaries from the date of grant. Each PSA entitles the holder to an award value to be typically paid on the third anniversary of the date of grant. For the purpose of calculating share-based compensation, the fair value of each award is determined at the grant date using the closing price of the common shares. A weighted average forfeiture rate of nil (March 31, 2020 - 8%) for PSAs and nil (March 31, 2020 - 6%) for RSAs was used to value all awards granted for the period ended March 31, 2021. The weighted average fair value of awards granted for the period ended March 31, 2021 is nil (March 31, 2020 - $0.21) per PSA granted and nil (March 31, 2020 - $0.21) per RSA. In the case of PSAs, the award value is adjusted for a payout multiplier which can range from 0.0 to 2.0 and is dependent on the performance of the Corporation relative to pre-defined corporate performance measures for a particular period. On the vesting dates, the Corporation has the option of settling the award value in cash or common shares of the Corporation. For purposes of stock-based compensation a payout multiple of 1.0 was assumed for the PSAs granted during the period.

The total number of shares reserved for issuance under the stock incentive plan cannot exceed 5 percent of the issued and outstanding shares of the Corporation.

The number of restricted and performance share awards outstanding are as follows:

	Number of restricted share awards	Number of performance share awards
Balance at December 31, 2020	9,987,634	11,927,348
Forfeited	(237,708)	(87,968)
Balance at March 31, 2021	**9,749,926**	**11,839,380**

(c) Stock-based compensation

A reconciliation of the stock-based compensation expense is provided below:

	Three Months Ended March 31,	
	2021	2020
Stock-based compensation on PSAs and RSAs	**1,403**	1,877
Capitalized stock-based compensation	**(471)**	(757)
Total stock-based compensation expense	**$ 932**	$ 1,120

(d) Per share amounts

The following table summarizes the shares used in calculating loss per share:

	Three Months Ended March 31, 2021	2020
Weighted average number of shares - basic and diluted	**339,784,739**	332,187,964

In computing diluted per share amounts at March 31, 2021, all RSAs and PSAs were excluded from the calculation as their effect was anti-dilutive. The common shares potentially issuable on the conversion of the convertible debentures were also excluded as they were determined to be anti-dilutive.

11. REVENUE

The following table presents the Corporation's petroleum and natural gas revenues disaggregated by revenue source:

	Three Months Ended March 31, 2021	2020
Oil	**$ 69,956**	$ 61,211
Natural gas liquids	**1,948**	1,063
Natural gas	**8,790**	1,432
Total petroleum and natural gas revenue	**$ 80,694**	$ 63,706
Processing	**1,089**	1,720
Total petroleum, natural gas and processing revenue	**$ 81,783**	$ 65,426

Surge's revenue was generated entirely in the provinces of Alberta and Saskatchewan. The majority of revenue resulted from sales whereby the transaction price was based on the index prices. Of total petroleum and natural gas revenue, three customers represented combined sales of $59.6 million for the period ended March 31, 2021 (March 31, 2020 - $54.6 million).

12. OTHER COSTS (INCOME)

The following table presents the Corporation's Other costs (income):

	Three Months Ended March 31, 2021	2020
Bad debt provision (recoveries)	**$ (171)**	31
Site rehabilitation program grant income	**(482)**	—
Total other costs (income)	**$ (653)**	$ 31

13. COMMITMENTS

Future minimum payments relating to variable office rent payments and firm transport commitments at March 31, 2021 are as follows:

	March 31, 2021	December 31, 2020
Less than 1 year	**$ 8,032**	$ 9,861
1 - 3 years	**6,646**	7,081
3 - 5 years	**4,703**	4,842
5+ years	**2,596**	3,109
Total commitments	**$ 21,977**	$ 24,893

During the year ended December 31, 2019, the Corporation disposed of a 1.7 percent gross overriding royalty ("GORR") on total revenue from the Corporation's Southwest Saskatchewan, Southeast Alberta and North Central Alberta assets. The Corporation has a drilling commitment on the GORR lands that must be fulfilled by April 30, 2022. In the event that the Corporation fails to fulfill the drilling commitment, the GORR shall increase from 1.7 percent to 2.7 percent.

14. LEASES

The Corporation has recognized the following lease and other obligations:

	Total
Lease obligations at December 31, 2019	$ 46,684
Additions	2,209
Interest expense	3,325
Payments	(11,426)
Lease and other obligations at December 31, 2020	$ 40,792
Dispositions	(629)
Interest expense	776
Payments	(2,914)
Lease and other obligations at March 31, 2021	**$ 38,025**
Current portion	**8,751**
Long term portion	**29,274**

During the period ended March 31, 2021, the Corporation cancelled the term of certain existing leases resulting in the derecognition of $0.3 million right-of-use assets and $0.6 million lease obligations.

15. SUBSEQUENT EVENT

Subsequent to March 31, 2021, the Corporation issued 39.0 million flow-through shares related to Canadian development expenditures at a price of $0.59 per share for total gross proceeds of $23.0 million. The qualifying development expenditures are required to be spent by December 31, 2021.