



# THIRD QUARTER INTERIM REPORT

For the three and nine months ended September 30, 2018

## Performance Data

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2018	2017 (Restated)	Change	2018	2017 (Restated)	Change
(CDN 000s, except per share data)	(\$)	(\$)	(%)	(\$)	(\$)	(%)
Revenue	<b>82,344</b>	64,576	28	<b>224,428</b>	179,417	25
Net Income <sup>(1)</sup>	<b>24,386</b>	7,404	229	<b>42,224</b>	20,176	109
Per share – basic <sup>(1)</sup>	<b>0.29</b>	0.08	228	<b>0.50</b>	0.24	106
Per share – diluted <sup>(1)</sup>	<b>0.28</b>	0.08	227	<b>0.49</b>	0.24	105
EBITDA <sup>(2)</sup>	<b>44,633</b>	25,493	75	<b>100,467</b>	70,012	43
As a % of revenue	<b>54.2</b>	39.5	1,470 bps	<b>44.8</b>	39.0	574 bps
Adjusted EBITDA <sup>(2)</sup>	<b>42,473</b>	26,158	62	<b>106,684</b>	70,427	51
As a % of revenue	<b>51.6</b>	40.5	1,107 bps	<b>47.5</b>	39.3	828 bps
Funds flow from operations	<b>36,039</b>	19,896	81	<b>97,833</b>	59,765	64
Per share – basic	<b>0.42</b>	0.23	80	<b>1.15</b>	0.71	63
Per share – diluted	<b>0.42</b>	0.23	80	<b>1.14</b>	0.70	62
Cash from operating activities	<b>31,809</b>	15,128	110	<b>83,770</b>	69,160	21
Free cash flow <sup>(2)</sup>	<b>26,880</b>	11,002	144	<b>68,919</b>	59,141	17
Capital expenditures	<b>4,858</b>	5,371	(10)	<b>15,426</b>	11,604	33
Working capital	<b>234,771</b>	190,518	23	<b>234,771</b>	190,518	23
Total assets	<b>429,684</b>	398,926	8	<b>429,684</b>	398,926	8
Total long-term debt	—	—	—	—	—	—
Cash dividends declared	<b>0.18</b>	0.17	6	<b>0.52</b>	0.51	2
Shares outstanding end of period (#000's)	<b>85,431</b>	84,916	1	<b>85,431</b>	84,916	1

(1) As disclosed in Note 2 to the consolidated financial statements, in 2017 the Company identified an immaterial non-cash re-classification error with respect to a component of its deferred income tax expense associated with accounting for the deferred tax on its net investment in foreign operations related to an inter-company financing. The reclassification is between the deferred tax provision in the statement of operations and foreign currency translation reserve in equity. This adjustment has been corrected on a retrospective basis with all prior period comparative figures being restated.

(2) Non-IFRS financial measures are defined in the Management's Discussion and Analysis section.

### Q3 2018 vs Q3 2017

The Company generated consolidated revenue of \$82.3 million in the third quarter of 2018, an increase of 28% from the same period in 2017. In the US operations, industry activity increased by 12% while market share increased to 61% from 59%. In Canada, industry activity was comparable while market share decreased to 85% from 88%. The International business unit saw increases in activity in each of the Company's major markets. In the Argentinian business unit, the increase in activity was partially offset by the weakness in the Argentinian peso.

Consolidated adjusted EBITDA increased to \$42.5 million in the third quarter, an increase of 62% from the same period in 2017. For the nine-month period, consolidated adjusted EBITDA was \$106.7 million, an increase of 51% over the 2017 comparative period. Increases in revenue in all operating segments, combined with significant operating leverage, led to the improvement in this key measure.

The Company recorded net income of \$24.4 million (\$0.28 per share) in the third quarter of 2018, compared to net income of \$7.4 million (\$0.08 per share) recorded in the same period in 2017. Net income was positively impacted from the increased level of activity, increased market share in the US operations, and reduction in depreciation expense.

## President's Message

Pason achieved strong results in the third quarter of 2018 and our teams continue to perform very well in all geographies. We generated revenue of \$82.3 million in the period, an increase of 28% compared to the same quarter last year. The main drivers of revenue growth were increased drilling activity and market share gains in the United States, and higher activity levels in all of Pason's international markets.

Adjusted EBITDA was \$42.5 million for the quarter, an increase of 62%. Adjusted EBITDA as a percentage of revenue was 52% compared to 41% one year ago. The drivers of this improvement were the significant increase in revenue with high incremental margins. Pason recorded net income for the quarter of \$24.4 million (\$0.28 per share) compared to \$7.4 million (\$0.08 per share) in the prior year quarter.

Capital expenditures for the quarter were \$4.9 million and free cash flow was \$26.9 million. At September 30, 2018, our working capital position stood at \$235 million, including cash and short-term investments of \$184 million. There is no debt on our balance sheet. We are maintaining our quarterly dividend at \$0.18 share.

At the beginning of this year, we began reporting our revenue along five product categories to better reflect the changing nature of Pason's business as follows:

- **Drilling Data** contains all products and services associated with acquiring, displaying, storing, and delivering drilling data. Revenue in this segment increased 32% in the third quarter compared to the prior year period and accounted for 51% of our total revenue. The increase was driven by a 12% increase in total US land drilling activity and US market share gains from 59% to 61%. Drilling industry days and segment revenue in Canada were flat. Internationally, drilling activity increased in all major markets.
- **Mud Management & Safety** includes products such as the Pit Volume Totalizer (PVT), Gas Analyzer, Hazardous Gas Alarm, and the Electronic Choke Actuator. In the third quarter, Mud Management & Safety generated 27% of total revenue.
- **Communications** includes satellite and terrestrial Internet bandwidth, Wireless Rigsite, VoIP and Intercom services and accounted for 9% of total revenue. Revenue in this segment is showing lower growth because of the transition from satellite to terrestrial bandwidth with lower pricing and better user experience for customers.
- **Drilling Intelligence** bundles Pason's product offerings targeted at enabling our customers' drilling optimization and automation efforts. It contains products such as autodrillers, abbl Directional Advisor®, the ExxonMobil Drilling Advisory System® and Pivot, a pipe oscillation system for improving slide drilling. Drilling Intelligence is our highest growth segment as revenue increased 73% in the third quarter compared to the prior year and accounted for 9% of our total revenue. Our level of confidence in the successful commercialization of new drilling intelligence products continues to grow. There currently are over 150 drilling rig installations of new Drilling Intelligence software in North America.
- **Analytics & Other** includes our Verdazo Discovery Analytics product suite, various reports, and other revenue streams. This segment is not as directly correlated to drilling activity and accounted for 4% of revenue.

We have increased our investment in R&D and IT in the first nine months of 2018 compared to the previous year period with a focus on machine learning algorithms, particularly in Drilling Intelligence and Mud

Management & Safety. Our capital expenditures will be relatively modest going forward with a larger portion of development efforts focused on software and analytics. We intend to spend up to \$25 million in capital expenditures in 2018 and up to \$30 million in 2019. Our highly capable and flexible IT and communications platform can host additional new Pason and third-party software at the rigsite and in the Cloud.

From a macro perspective, the oil market continued to tighten in the third quarter. Despite continued strong production from the US and increasing output from OPEC countries, we had seen a further draw in global inventories and an increase in oil prices. The tightening supply and demand balance was driven by accelerating decline rates in the international production base and by the reduction in exports from Venezuela and Iran.

In the United States there are concerns for industry activity in the coming few quarters given take-away constraints across several basins, especially in the Permian in Texas and New Mexico. However, we have not yet seen any signs of a slowdown and we expect activity levels to plateau, rather than decline significantly. It is expected that the Permian takeaway constraints will be addressed in the next 12-18 months.

In Canada, we expect activity in the upcoming winter drilling season to be somewhat lower than last year. We continue to be concerned about the medium-term outlook for Canadian oil and gas as the ongoing crude oil and natural gas takeaway capacity issues, and price differentials, continue to create an environment of extreme caution for Canadian E&P companies.

In aggregate, we expect drilling activity in Pason's core markets to be largely flat in 2019 compared to 2018. Our market positions remain strong, and we expect to be able to deliver growth through higher product adoption going forward. We are the service provider of choice for many leading operators and drilling contractors with Pason equipment installed on over 65% of all active land drilling rigs in the Western Hemisphere. We continue to be very well-positioned to participate in the industry's recovery and growth.



Marcel Kessler  
President and Chief Executive Officer  
November 7, 2018

## Management's Discussion and Analysis

The following discussion and analysis has been prepared by management as of November 7, 2018, and is a review of the financial condition and results of operations of Pason Systems Inc. (Pason or the Company) based on International Financial Reporting Standards (IFRS) and should be read in conjunction with the consolidated financial statements and accompanying notes.

Certain information regarding the Company contained herein may constitute forward-looking statements under applicable securities laws. Such statements are subject to known or unknown risks and uncertainties that may cause actual results to differ materially from those anticipated or implied in the forward-looking statements.

All financial measures presented in this report are expressed in Canadian dollars unless otherwise indicated.

### Additional IFRS Measures

In its interim condensed consolidated financial statements, the Company uses certain additional IFRS measures. Management believes these measures provide useful supplemental information to readers.

#### Funds flow from operations

Management believes that funds flow from operations, as reported in the Consolidated Statements of Cash Flows, is a useful additional measure as it represents the cash generated during the period, regardless of the timing of collection of receivables and payment of payables. Funds flow from operations represents the cash flow from continuing operations, excluding non-cash items. Funds flow from operations is defined as net income adjusted for depreciation and amortization expense, non-cash, stock-based compensation expense, deferred taxes, and other non-cash items impacting operations.

#### Cash from operating activities

Cash from operating activities is defined as funds flow from operations adjusted for changes in working capital items.

### Non-IFRS Financial Measures

These definitions are not recognized measures under IFRS, and accordingly, may not be comparable to measures used by other companies. These Non-IFRS measures provide readers with additional information regarding the Company's ability to generate funds to finance its operations, fund its research and development and capital expenditure program, and pay dividends.

#### Revenue per EDR day

Revenue per EDR day is defined as the daily revenue generated from all products that the Company has on rent on a drilling rig that has the Company's base EDR installed. This metric provides a key measure on the Company's ability to increase production adoption and evaluate product pricing.

#### EBITDA

EBITDA is defined as net income before interest expense, income taxes, stock-based compensation expense, depreciation and amortization expense, and gains on disposal of investments.

## **Adjusted EBITDA**

Adjusted EBITDA is defined as EBITDA, adjusted for foreign exchange, impairment of property, plant, and equipment, restructuring costs, and other items which the Company does not consider to be in the normal course of continuing operations.

Management believes that EBITDA and Adjusted EBITDA are useful supplemental measures as they provide an indication of the results generated by the Company's principal business activities prior to the consideration of how these results are taxed in multiple jurisdictions, how the results are impacted by foreign exchange or how the results are impacted by the Company's accounting policies for equity-based compensation plans.

## **Free cash flow**

Free cash flow is defined as cash from operating activities plus proceeds on disposal of property, plant, and equipment, less capital expenditures (including changes to non-cash working capital associated with capital expenditures), and deferred development costs. This metric provides a key measure on the Company's ability to generate cash from its principal business activities after funding the capital expenditure program, and provides an indication of the amount of cash available to finance, among other items, the Company's dividend and other investment opportunities.

## Overall Performance

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2018	2017	Change	2018	2017	Change
(000s)	(\$)	(\$)	(%)	(\$)	(\$)	(%)
<b>Revenue</b>						
Drilling Data	<b>42,090</b>	31,889	32	<b>114,805</b>	88,974	29
Mud Management and Safety	<b>22,299</b>	19,288	16	<b>62,863</b>	53,225	18
Communications	<b>7,504</b>	6,567	14	<b>21,413</b>	18,440	16
Drilling Intelligence	<b>7,111</b>	4,099	73	<b>16,066</b>	11,313	42
Analytics and Other	<b>3,340</b>	2,733	22	<b>9,281</b>	7,465	24
<b>Total revenue</b>	<b>82,344</b>	64,576	28	<b>224,428</b>	179,417	25

The Pason Electronic Drilling Recorder (EDR) remains the Company's primary product. The EDR provides a complete system of drilling data acquisition, data networking, and drilling management tools and reports at both the wellsite and at customer offices. The EDR is the base product from which all other wellsite instrumentation products are linked. By linking these products, a number of otherwise redundant elements such as data processing, display, storage, and networking are eliminated. This ensures greater reliability and a more robust system of instrumentation for the customer.

EDR rental day performance for Canada and the United States is reported below:

	Pason Electronic Drilling Recorder (EDR) Rental Days					
	Three Months Ended September 30,			Nine Months Ended September 30,		
	2018	2017	Change	2018	2017	Change
	#	#	(%)	#	#	(%)
Canada	<b>16,100</b>	16,900	(5)	<b>45,500</b>	49,900	(9)
United States	<b>57,500</b>	49,500	16	<b>164,700</b>	128,500	28

Total revenue increased 28% and 25% for the three and nine months ending September 2018, over the same period in 2017. This increase is attributable to an increase in revenue per EDR day in all three operating segments combined with an increase in the activity in the US operating segment.

Industry activity in the US market increased 12% in the third quarter of 2018 compared to the corresponding period in 2017, while third quarter Canadian industry activity was consistent in the third quarter of 2018 compared to the corresponding period in 2017. US EDR days increased by 16% in the third quarter of 2018 compared to the corresponding period in 2017, while third quarter Canadian EDR days, which includes non-oil and gas-related activity, decreased 5% from 2017 levels.

In the third quarter of 2018, the Pason EDR was installed on 61% of the land rigs in the US market compared to 59% during the same time period of 2017.

In the third quarter of 2018, the Pason EDR was installed on 85% of the land rigs in the Canadian market compared to 88% during the same period of 2017. For the purposes of market share, the Company uses the number of EDR days billed and oil and gas drilling days as reported by accepted industry sources.

Revenue generated from the Company's other wellsite instrumentation products was largely driven by the increase in drilling activity in the US market combined with increases in the adoption of certain EDR peripherals, most notably the alarms and sensors, and an increase in revenue from the Company's drilling intelligence products.

For the third quarter of 2018, the Company saw an increase in activity in all major regions of the International operating segment with the largest increases in Australia and Argentina.

# Discussion of Operations

## United States Operations

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2018	2017	Change	2018	2017	Change
(000s)	(\$)	(\$)	(%)	(\$)	(\$)	(%)
<b>Revenue</b>						
Drilling Data	29,640	20,888	42	80,311	56,630	42
Mud Management and Safety	15,274	12,763	20	43,153	34,352	26
Communications	4,099	3,458	19	11,997	9,443	27
Drilling Intelligence	3,774	2,266	67	8,827	5,723	54
Analytics and Other	1,382	1,303	6	4,267	3,691	16
<b>Total revenue</b>	<b>54,169</b>	<b>40,678</b>	<b>33</b>	<b>148,555</b>	<b>109,839</b>	<b>35</b>
<b>Rental services and local administration</b>	<b>18,317</b>	<b>17,130</b>	<b>7</b>	<b>52,657</b>	<b>47,642</b>	<b>11</b>
<b>Depreciation and amortization</b>	<b>4,200</b>	<b>4,151</b>	<b>1</b>	<b>12,128</b>	<b>13,322</b>	<b>(9)</b>
<b>Segment gross profit</b>	<b>31,652</b>	<b>19,397</b>	<b>63</b>	<b>83,770</b>	<b>48,875</b>	<b>71</b>

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
	\$	\$	\$	\$
Revenue per EDR day - USD	716	647	694	648
Revenue per EDR day - CAD	936	809	893	847

Revenue from the US operations increased by 33% in the third quarter of 2018 over the 2017 comparable period (28% when measured in USD). For the first nine months of 2018, revenue increased 35% compared to the prior period (37% when measured in USD).

Industry activity in the US market increased by 12% in the third quarter of 2018 over the 2017 comparable period. For the first nine months of 2018, industry activity increased by 19% compared to the prior period. US market share was 61% for the third quarter of 2018 compared to 59% during the same period of 2017. For the first nine months of 2018, US market share was 61% compared to 57% during the same period of 2017. The increase in market share is driven by market share growth in key US regions combined with changes in the mix of active customers.

EDR rental days increased by 16% in the third quarter of 2018 over the 2017 comparable period. Revenue per EDR day increased to US\$716 in the third quarter of 2018, an increase of US\$69 over the same period in 2017. The increase in revenue per EDR day was driven by higher adoption of certain peripheral products and selective price increases on certain products.

Revenue per EDR day for the first nine months of 2018 was US\$694, an increase of US\$46 from the same period of 2017.

Rental services and local administration increased by 7% in the third quarter of 2018 over the 2017 comparative period (6% when measured in USD). For the first nine months of 2018, rental services and local administration increased 11% over the 2017 comparative period (15% when measured in USD). The increase in operating costs is attributable higher field staff levels and higher direct costs to support additional activity.

Depreciation expense increased by 1% in the third quarter of 2018 over the 2017 comparative period. For the first nine months of 2018, depreciation expense decreased 9% over the 2017 comparative period.

Segment gross profit increased by \$12.3 million or 63% in the third quarter of 2018 over the 2017 comparative period. For the first nine months of 2018, segment gross profit was \$83.8 million. This represents an increase of 71% over the 2017 comparative period.

## Canadian Operations

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2018	2017	Change	2018	2017	Change
(000s)	(\$)	(\$)	(%)	(\$)	(\$)	(%)
<b>Revenue</b>						
Drilling Data	7,804	7,763	1	21,904	22,365	(2)
Mud Management and Safety	5,333	5,366	(1)	14,956	15,475	(3)
Communications	3,028	2,869	6	8,303	8,222	1
Drilling Intelligence	2,869	1,414	103	6,104	4,192	46
Analytics and Other	981	908	8	2,837	2,532	12
<b>Total revenue</b>	<b>20,015</b>	<b>18,320</b>	<b>9</b>	<b>54,104</b>	<b>52,786</b>	<b>2</b>
<b>Rental services and local administration</b>	<b>6,046</b>	<b>6,473</b>	<b>(7)</b>	<b>19,510</b>	<b>17,826</b>	<b>9</b>
<b>Depreciation and amortization</b>	<b>3,900</b>	<b>6,053</b>	<b>(36)</b>	<b>12,508</b>	<b>17,632</b>	<b>(29)</b>
<b>Segment gross profit</b>	<b>10,069</b>	<b>5,794</b>	<b>74</b>	<b>22,086</b>	<b>17,328</b>	<b>27</b>

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
	\$	\$	\$	\$
Revenue per EDR day - CAD	1,191	1,041	1,133	1,010

Canadian drilling activity in the third quarter of 2018 was flat relative to the same period in 2017. The level of activity during the quarter was affected by weather-related issues during September. For the first nine months of 2018, drilling activity decreased by 6% compared to the same period in 2017. Rig activity reflected the challenging industry outlook and takeaway capacity issues in the WCSB.

Canadian segment revenue increased by 9% in the third quarter of 2018 over the 2017 comparative period. For the first nine months of 2018, revenue increased by 2% compared to the prior period.

Canadian market share was 85% for the third quarter of 2018 compared to 88% during the same period of 2017. For the first nine months of 2018, Canadian market share was 86% compared to 89% during the same period of 2017.

EDR rental days decreased 5% in the third quarter of 2018 compared to 2017. On a year-to-date basis EDR rental days decreased 9% over 2017 levels. Revenue per EDR day increased by \$150 to \$1,191 during the third quarter of 2018 compared to 2017. For the first nine months of 2018, revenue per EDR day increased by \$123 to \$1,133. The increase is driven by higher adoption of certain EDR peripherals and the successful introduction of drilling intelligence products.

Rental services and local administration decreased by 7% in the third quarter of 2018 relative to the same period in 2017. For the first nine months of 2018, rental services and local administration increased 9%

compared to the same period in 2017. The increase is due to repair costs and other direct field costs incurred primarily in the first two quarters of 2018.

Depreciation and amortization expense decreased by 36% in the third quarter of 2018 over the 2017 comparative period. The decrease is a result of lower capital programs since 2014 and a drop in amortization expense of previously deferred research and development costs as fewer project costs are being capitalized for accounting purposes.

Segment gross profit for the third quarter of 2018 increased 74% to \$10.1 million in the third quarter of 2018 compared to \$5.8 million in segment gross profit in the 2017 comparative period.

## International Operations

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2018	2017	Change	2018	2017	Change
(000s)	(\$)	(\$)	(%)	(\$)	(\$)	(%)
<b>Revenue</b>						
Drilling Data	4,646	3,238	43	12,590	9,979	26
Mud Management and Safety	1,692	1,159	46	4,754	3,398	40
Communications	377	240	57	1,113	775	44
Drilling Intelligence	468	419	12	1,135	1,398	(19)
Analytics and Other	977	522	87	2,177	1,242	75
<b>Total revenue</b>	<b>8,160</b>	<b>5,578</b>	<b>46</b>	<b>21,769</b>	<b>16,792</b>	<b>30</b>
<b>Rental services and local administration</b>	<b>4,434</b>	<b>4,317</b>	<b>3</b>	<b>13,882</b>	<b>13,282</b>	<b>5</b>
<b>Depreciation and amortization</b>	<b>804</b>	<b>980</b>	<b>(18)</b>	<b>2,663</b>	<b>3,026</b>	<b>(12)</b>
<b>Segment gross profit</b>	<b>2,922</b>	<b>281</b>	<b>940</b>	<b>5,224</b>	<b>484</b>	<b>979</b>

Drilling activity increased in the Company's major international markets, although the majority of the absolute gains were seen in Australia, Argentina, and the Andean region. The increase in activity in Argentina was offset by a weaker Argentinian peso compared to the prior year.

Revenue in the International segment increased by 46% in the third quarter of 2018 compared to the same period in 2017. For the first nine months of 2018, revenue increased by 30% compared to the prior period.

Rental services and local administration expenses increased by 3% in the third quarter of 2018 compared to the same period in 2017. For the first nine months of 2018, rental services and local administration expense increased by 5% compared to the prior period.

Depreciation expense decreased by 18% in the third quarter of 2018 compared to the same period in 2017.

Segment gross profit was \$2.9 million for the third quarter of 2018, an improvement from the \$0.3 million profit recorded in the corresponding period in 2017. For the first nine months of 2018, segment gross profit was \$5.2 million compared to \$0.5 million in 2017.

## Corporate Expenses

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2018	2017	Change	2018	2017	Change
(000s)	(\$)	(\$)	(%)	(\$)	(\$)	(%)
<b>Other expenses</b>						
Research and development	6,711	6,945	(3)	19,687	19,083	3
Corporate services	4,363	3,553	23	12,008	11,157	8
Stock-based compensation	2,589	3,145	(18)	8,978	8,869	1
Other						
Foreign exchange (gain) loss	(1,516)	113	—	6,675	(353)	—
Other	(644)	552	—	(458)	768	—
<b>Total corporate expenses</b>	<b>11,503</b>	<b>14,308</b>	<b>(20)</b>	<b>46,890</b>	<b>39,524</b>	<b>19</b>

Corporate service expenses increased in the third quarter of 2018 over the 2017 comparative period due to one time costs combined with certain expenses being recognized in different periods in 2018 as compared to 2017.

### Q3 2018 vs Q2 2018

Consolidated revenue was \$82.3 million in the third quarter of 2018 compared to \$68.3 million in the second quarter of 2018, an increase of \$14.0 million or 21%. The second quarter of the year is typically the weakest for the Company due to the seasonality of Canadian drilling activity. US and international activity levels continued to increase and this partially offset the anticipated drop in Canadian activity.

Revenue in the US segment was \$54.2 million in the third quarter of 2018 compared to \$50.3 million in the second quarter of 2018, an increase of \$3.9 million or 8% as industry activity, market share and revenue per EDR day all increased. The Canadian segment earned revenue of \$20.0 million in the third quarter of 2018 compared to \$10.7 million in the second quarter of 2018, an increase of \$9.4 million or 88%. The International segment earned revenue of \$8.2 million in the third quarter of 2018 compared to \$7.3 million in the second quarter of 2018, an increase of \$0.8 million or 11%.

Adjusted EBITDA, which adjusts EBITDA for foreign exchange and certain non-recurring charges, was \$42.5 million in the third quarter of 2018 compared to \$29.5 million in the second quarter of 2018. Funds flow from operations was \$36.0 million in the third quarter of 2018 compared to \$27.8 million in the second quarter of 2018.

The Company recorded net income in the third quarter of 2018 of \$24.4 million (\$0.28 per share) compared to a profit of \$5.5 million (\$0.06 per share) in the second quarter of 2018. The Company recorded an unrealized foreign exchange gain in the third quarter of 2018 compared to a significant unrealized foreign exchange loss in the second quarter of 2018.

## Summary of Quarterly Results

Three Months Ended	Dec 31, 2016	Mar 31, 2017	Jun 30, 2017	Sept 30, 2017	Dec 31, 2017	Mar 31, 2018	Jun 30, 2018	Sept 30, 2018
(000s, except per share data)	(\$)	(\$)	(\$)	(\$)	(\$)	(\$)	(\$)	(\$)
<b>Revenue</b>	48,827	59,049	55,792	64,576	66,226	73,813	68,271	<b>82,344</b>
<b>(Loss) income restated <sup>(1)</sup></b>	(10,446)	6,804	5,968	7,404	5,014	12,359	5,479	<b>24,386</b>
Per share – basic restated <sup>(1)</sup>	(0.12)	0.08	0.07	0.08	0.06	0.15	0.06	<b>0.29</b>
Per share – diluted restated <sup>(1)</sup>	(0.12)	0.08	0.07	0.08	0.06	0.14	0.06	<b>0.28</b>
<b>EBITDA <sup>(2)</sup></b>	(2,291)	23,469	21,050	25,493	26,651	32,220	23,614	<b>44,633</b>
<b>Adjusted EBITDA <sup>(2)</sup></b>	15,225	24,908	19,361	26,158	27,797	34,753	29,458	<b>42,473</b>
<b>Funds flow from operations</b>	15,324	21,074	18,795	19,896	27,356	33,958	27,836	<b>36,039</b>
Per share – basic	0.18	0.25	0.22	0.23	0.32	0.40	0.33	<b>0.42</b>
Per share – diluted	0.18	0.25	0.22	0.23	0.32	0.40	0.32	<b>0.42</b>
<b>Cash from operating activities</b>	665	29,831	24,201	15,128	16,637	24,344	27,617	<b>31,809</b>
<b>Free cash flow <sup>(2)</sup></b>	(153)	28,511	19,628	11,002	6,690	18,906	23,133	<b>26,880</b>

(1) As disclosed in Note 2 to the consolidated financial statements, in 2017 the Company identified an immaterial non-cash re-classification error with respect to a component of its deferred income tax expense associated with accounting for the deferred tax on its net investment in foreign operations related to an inter-company financing. The reclassification is between the deferred tax provision in the statement of operations and foreign currency translation reserve in equity. This adjustment has been corrected on a retrospective basis with all prior period comparative figures being restated. Refer to table below on the impact of the restatement on prior period figures.

(2) Non-IFRS financial measures are defined in the Management's Discussion and Analysis section.

### Restatement of Prior Period Error (refer to Note 2 to the consolidated financial statements)

Three Months Ended	Dec 31, 2016	Mar 31, 2017	Jun 30, 2017	Sept 30, 2017
(000s)	(\$)	(\$)	(\$)	(\$)
<b>Previously reported (Loss) income</b>	(11,325)	7,153	6,895	8,813
Per share – basic	(0.13)	0.08	0.08	0.10
Per share – diluted	(0.13)	0.08	0.08	0.10
(Decrease) increase in tax provision	(879)	349	927	1,409
<b>Restated (Loss) income</b>	(10,446)	6,804	5,968	7,404
Per share – basic	(0.12)	0.08	0.07	0.08
Per share – diluted	(0.12)	0.08	0.07	0.08

## Reconcile (loss) income to EBITDA

Three Months Ended	Dec 31, 2016	Mar 31, 2017	Jun 30, 2017	Sept 30, 2017	Dec 31, 2017	Mar 31, 2018	Jun 30, 2018	Sept 30, 2018
(000s)	(\$)	(\$)	(\$)	(\$)	(\$)	(\$)	(\$)	(\$)
(Loss) income restated <sup>(1)</sup>	(10,446)	6,804	5,968	7,404	5,014	12,359	5,479	<b>24,386</b>
Add:								
Taxes restated <sup>(1)</sup>	(3,898)	2,145	1,082	3,760	7,043	8,152	5,060	<b>8,754</b>
Depreciation and amortization	10,515	11,973	10,823	11,184	11,701	9,175	9,220	<b>8,904</b>
Stock-based compensation	1,538	2,547	3,177	3,145	2,893	2,534	3,855	<b>2,589</b>
<b>EBITDA <sup>(2)</sup></b>	<b>(2,291)</b>	<b>23,469</b>	<b>21,050</b>	<b>25,493</b>	<b>26,651</b>	<b>32,220</b>	<b>23,614</b>	<b>44,633</b>

## Reconcile EBITDA to Adjusted EBITDA

Three Months Ended	Dec 31, 2016	Mar 31, 2017	Jun 30, 2017	Sept 30, 2017	Dec 31, 2017	Mar 31, 2018	Jun 30, 2018	Sept 30, 2018
(000s)	(\$)	(\$)	(\$)	(\$)	(\$)	(\$)	(\$)	(\$)
EBITDA	(2,291)	23,469	21,050	25,493	26,651	32,220	23,614	<b>44,633</b>
Add:								
Impairment charges	17,474	—	—	—	—	—	—	—
Foreign exchange	284	223	(689)	113	1,459	2,404	5,787	<b>(1,516)</b>
Other	(242)	1,216	(1,000)	552	(313)	129	57	<b>(644)</b>
<b>Adjusted EBITDA <sup>(2)</sup></b>	<b>15,225</b>	<b>24,908</b>	<b>19,361</b>	<b>26,158</b>	<b>27,797</b>	<b>34,753</b>	<b>29,458</b>	<b>42,473</b>

## Reconcile cash from operating activities to free cash flow

Three Months Ended	Dec 31, 2016	Mar 31, 2017	Jun 30, 2017	Sept 30, 2017	Dec 31, 2017	Mar 31, 2018	Jun 30, 2018	Sept 30, 2018
(000s)	(\$)	(\$)	(\$)	(\$)	(\$)	(\$)	(\$)	(\$)
Cash from operating activities	665	29,831	24,201	15,128	16,637	24,344	27,617	<b>31,809</b>
Less:								
Net additions to property, plant and equipment	(1,827)	(1,027)	(3,913)	(3,881)	(8,749)	(4,452)	(3,227)	<b>(3,890)</b>
Deferred development costs	1,009	(293)	(660)	(245)	(1,198)	(986)	(1,257)	<b>(1,039)</b>
<b>Free cash flow <sup>(2)</sup></b>	<b>(153)</b>	<b>28,511</b>	<b>19,628</b>	<b>11,002</b>	<b>6,690</b>	<b>18,906</b>	<b>23,133</b>	<b>26,880</b>

Pason's quarterly financial results vary quarter to quarter due in part to the seasonality of the oil and gas service industry in Canada, which is somewhat offset by the less seasonal nature of US and International operations. The first quarter is generally the strongest quarter for the Company due to strong activity in Canada, where location access is best during the winter. The second quarter is typically the slowest due to spring break-up in Canada, when many areas are not accessible due to ground conditions, and, therefore, do not permit the movement of heavy equipment. Activity generally increases in the third quarter, depending on the year, as ground conditions have often improved and location access becomes available; however, a rainy summer can have a significant adverse effect on drilling activity. By the fourth quarter, often the Company's second strongest quarter, access to most areas in Canada becomes available when the ground freezes. Consequently, the performance of the Company may not be comparable quarter to consecutive quarter, but should be considered on the basis of results for the whole year, or by comparing results in a quarter with results in the same quarter for the previous year.

## Liquidity and Capital Resources

As at September 30,	2018	2017	Change
(000s)	(\$)	(\$)	(%)
Cash and cash equivalents	119,762	159,437	(25)
Short-term investments	64,725	—	—
Working capital	234,771	190,518	23
Funds flow from operations <sup>(1)</sup>	97,833	59,766	64
Capital expenditures <sup>(1)</sup>	15,426	11,604	33
As a % of funds flow <sup>(1)(2)</sup>	15.8%	19.4%	(365) bps

(1) Figures are for the Nine months ended September 30.

(2) Calculated by dividing capital expenditures by funds flow from operations.

During the second quarter of 2018, the Company invested in a USD \$50.0 million term deposit bearing an interest rate of 2.30% maturing in November 2018.

## Contractual Obligations

	Less than 1 year	1–3 years	Thereafter	Total
(000s)	(\$)	(\$)	(\$)	(\$)
Operating leases and other contracts	6,874	10,371	4,836	22,081

Contractual obligations relate primarily to minimum future lease payments required primarily for telecommunication charges and operating leases for certain facilities and vehicles.

At September 30, 2018, the Company had no capital lease obligations, and other than the operating leases detailed above, and the onerous lease obligation recorded, has no off-balance sheet arrangements.

The Company has available a \$5.0 million demand revolving credit facility. At September 30, 2018, no amount had been drawn on the facility.

## Disclosure of Outstanding Share and Options Data

As at September 30, 2018, there were 85.4 million common shares and 5.1 million options issued and outstanding.

## SEDAR

Additional information relating to the Company can be accessed on the Company's website at [www.pason.com](http://www.pason.com) and on the Canadian Securities Administrators' System for Electronic Document Analysis and Retrieval (SEDAR) at [www.sedar.com](http://www.sedar.com).

## Critical Accounting Estimates

The preparation of the consolidated financial statements requires that certain estimates and judgments be made with respect to the reported amounts of revenue and expenses and the carrying value of assets and liabilities. These estimates are based on historical experience and management's judgments, and as a result, the estimates used by management involve uncertainty and may change as additional experience is acquired.

### Depreciation and Amortization

The accounting estimate that has the greatest impact on the Company's financial statements is depreciation and amortization. Depreciation of the Company's capital assets includes estimates of useful lives. These estimates may change with experience over time so that actual results could differ significantly from these estimates.

### Carrying Value of Assets

The carrying amounts of the Company's non-financial assets, other than deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. Judgments and assessments are made to determine whether an event has occurred that indicates a possible impairment. If any such indication exists, then the asset's recoverable amount is estimated. For goodwill and intangible assets that have indefinite useful lives or that are not yet available for use, the recoverable amount is estimated each year.

### Stock-Based Payments

The fair value of stock-based payments is calculated using a Black-Scholes option pricing model. There are a number of estimates used in the calculation, such as the future forfeiture rate, expected option life, and the future price volatility of the underlying security, which can vary from actual future events. The factors applied in the calculation are management's best estimates based on historical information and future forecasts.

### Income Taxes

The calculation of deferred income taxes is based on a number of assumptions, including estimating the future periods in which temporary differences, tax losses, and other tax credits will reverse. Tax interpretations, regulations, and legislation in the various jurisdictions in which the Company and its subsidiaries operate are subject to change.

The estimation of deferred tax assets and liabilities includes uncertainty with respect to the reversal of temporary differences.

Deferred tax assets are recognized for the carry-forward of unused tax losses and unused tax credits when it is probable that taxable income will be available to utilize unused tax losses and unused tax credits. This requires estimation of future taxable income and usage of tax loss carry-forwards for a considerable period into the future. Income tax expense in future periods may be affected to the extent actual taxable income is not sufficient or available to use the temporary differences giving rise to the deferred tax asset.

## Risk and Uncertainties

Pason has implemented a risk management framework that helps the Company manage the reality that future events, decisions, or actions may cause undesirable effects. The framework takes a value-based approach to identifying, prioritizing, communicating, mitigating, and monitoring risks, and aligns this with the organization's appetite for risk considering our culture, strategy, and objectives.

Although a framework can help the Company to manage its risks, the Company's performance is subject to a variety of risks and uncertainties. Although the risks described below are the risks that we believe are material, there may also be risks of which we are currently unaware, or that we currently regard as immaterial based upon the information available to us. Interested parties should be aware that the occurrence of the events described in these risk factors could have a material adverse effect on our business, operating results, and financial condition.

### Operating Risks

Pason derives the majority of its revenue from the rental of instrumentation and data services to oil and gas companies and drilling contractors in Canada, the US, Australia, and Latin America. The demand for our products is directly related to land-based or offshore drilling activity funded by energy companies' capital expenditure programs. A substantial or extended decline in energy prices or diversion of funds to large capital programs could adversely affect capital available for drilling activities, directly impacting Pason's revenue.

### Commodity Prices

Prices for crude oil and natural gas fluctuate in response to a number of factors beyond Pason's control. The factors that affect prices include, but are not limited to, the following: the actions of the Organization of Petroleum Exporting Countries, world economic conditions, government regulation, political stability in the Middle East and elsewhere, the foreign supply of crude oil, the price of foreign imports, the availability of alternate fuel sources, and weather conditions. Any of these can reduce the amount of drilling activity.

### Seasonality

Drilling activity in Canada is seasonal due to weather that limits access to leases in the spring and summer, making the first and last quarters of each year the peak level of demand for Pason's services due to the higher level of drilling activity. The length of the drilling season can be shortened due to warmer winter weather or rainy seasons. Pason can offset some of this risk, although not eliminate it, through continued growth in the US and internationally, where activity is less seasonal.

### Proprietary Rights

Pason relies on innovative technologies and products to protect its competitive position in the market. To protect Pason's intellectual property, the Company employs trademarks, patents, employment agreements, and other measures to protect trade secrets and confidentiality of information. Pason also believes that due to the rapid pace of technological change in the industry, technical expertise, knowledge, and innovative skill, combined with an ability to rapidly develop, produce, enhance, and market products, also provides protection in maintaining a competitive position.

## **Litigation**

The Company is involved in various claims and litigation arising in the normal course of business. While the outcome of these matters is uncertain and there can be no assurance that such matters will be resolved in Pason's favour, the Company does not currently believe that the outcome of any pending or threatened proceedings related to these or other matters, or the amounts which the Company may be required to pay by reason thereof, would individually or in the aggregate have a material adverse impact on its day-to-day business operations.

## **Credit Risk**

Pason is exposed to credit risk to the extent that its customers, operating primarily in the oil and natural gas industry, may experience financial difficulty and be unable to meet their obligations. However, Pason has a large number of customers on both the Operator and Contractor side, which minimizes exposure to any single customer.

## **Availability of Qualified Personnel**

Due to the specialized and technical nature of Pason's business, Pason is highly dependent on attracting and retaining qualified or key personnel. There is competition for qualified personnel in the areas where Pason operates, and there can be no assurance that qualified personnel can be attracted or retained to meet the growth needs of the business. To mitigate this risk, Pason has a Human Resources department within each significant business unit to support that function.

## **Alternative Energies**

There continues to be extensive discussion at all levels of government worldwide and by the public concerning the burning of fossil fuels and the impact this may have on the global environment. Environmental legislation is evolving in a manner expected to result in stricter standards and enforcement, larger fines and liability, which could lead to potentially increased capital expenditures and operating costs. Implementation of strategies for reducing greenhouse gases could have a material impact on the nature of operations of the Company. Given the evolving nature of the debate related to climate change and the control of greenhouse gases and the possible resulting requirements, it is not possible to predict either the nature of those requirements or the impact on the Company.

## **International Operations**

Assets outside of Canada and the US may be adversely affected by changes in governmental policy, social instability, or other political or economic developments beyond the Company's control, including expropriation of property, exchange rate fluctuations, and restrictions on repatriation of cash. The Company has mitigated these risks where practical and considered warranted. Approximately 90% of the Company's revenues are generated in Canada and the US, which limits exposure to risks and uncertainties in foreign countries. The Company's Argentinian subsidiary is operating in a highly inflationary economy and its operating results are being impacted by a weakening Argentina peso relative to the Canadian dollar.

## Foreign Exchange Exposure

The Company operates internationally and is primarily exposed to exchange risk relative to the US dollar. The Canadian operations are exposed to currency risk on US denominated financial assets and liabilities with fluctuations in the rate recognized as foreign exchange gains or losses in the Consolidated Statements of Operations. The Company's self-sustaining foreign subsidiaries expose the Company to exchange rate risk on the translation of their financial assets and liabilities to Canadian dollars for consolidation purposes.

Adjustments arising when translating the foreign subsidiaries into Canadian dollars are reflected in the Consolidated Statements of Operations and Other Comprehensive Income as unrealized foreign currency translation adjustments. The Company has not hedged either one of these risks.

The Company does not employ any financial instruments to manage risk or hedge its activities. The vast majority of the Company's activities are conducted in Canada and the US, where local revenue is earned against local expenses and the Company is therefore naturally hedged.

## Major Customers

Pason has a large customer base, consisting of both Operators and Contractors, and does not rely on any single customer for a significant portion of its revenue. No single customer accounted for more than 10% of the consolidated revenues of the Company. The loss of one or more customers, or a reduction in the amount of business Pason does with any of its customers, if not offset by obtaining new customers or increasing the amount of business it does with existing customers, could have a detrimental impact on Pason's revenue.

## Key Personnel

Pason's success depends to a significant extent on the contributions of a number of its officers and key employees. The Company does not carry "key person" insurance on any of its key employees. As such, the loss of services of one or more of these key employees could have a material adverse effect on Pason's business, operating results, or financial condition.

## Dividends

The decision to pay dividends and the amount paid is at the discretion of Pason's board of directors, which regularly reviews the Company's financial position, operating results, and industry outlook. Pason's ability to pay dividends is dependent on the Company's ability to generate cash flow in excess of its operating and investment needs and the Company's financial position.

## Taxation

Pason and its subsidiaries are subject to income and other forms of taxation in the various jurisdictions in which they operate. Pason attempts to structure its operations in a tax efficient manner in light of prevailing tax regimes. Any adverse change to existing taxation measures, policies or regulations, or the introduction of new taxation measures, policies or regulations in any of the jurisdictions in which Pason operates could have a negative impact on Pason's business, operating results, or financial condition.

The management of Pason believes that the provision for income taxes is adequate and in accordance with both generally accepted accounting principles and appropriate regulations. However, the tax filing positions of the Company are subject to review and audit by tax authorities who may challenge and succeed in management's interpretation of the applicable tax legislation.

## Information Security

Pason's business operations use an extensive network of communications and computer hardware and software systems. In addition, Pason's equipment captures, transmits, and stores significant quantities of drilling data on behalf of its customers. The Company takes measures to protect the security and integrity of its information systems and data, however, there is a risk that these measures may not fully protect against a potential security breach, which could have a negative impact on the Company's ability to operate or its reputation with existing and potential customers.

# Corporate Information

## Directors

**James D. Hill**  
Chairman of the Board  
Pason Systems Inc.  
Calgary, Alberta

**James B. Howe**<sup>(1)(4)(6)(7)</sup>  
President  
Bragg Creek Financial  
Consultants Ltd.  
Calgary, Alberta

**Marcel Kessler**  
President & CEO  
Pason Systems Inc.  
Calgary, Alberta

**T. Jay Collins**<sup>(2)(3)(6)</sup>  
Director  
Oceaneering International Inc.  
Houston, Texas

**Judi Hess**<sup>(2)(4)(5)</sup>  
CEO & Director  
Copperleaf Technologies Inc.  
Vancouver, British Columbia

(1) Audit Committee Chairman

(2) Audit Committee Member

(3) HR and Compensation Committee  
Chairman

(4) HR and Compensation Committee  
Member

(5) Corporate Governance and Nominations  
Committee Chairman

(6) Corporate Governance and Nomination  
Committee Member

(7) Lead Director

## Officers & Key Personnel

**Marcel Kessler**  
President  
& Chief Executive Officer

**Jon Faber**  
Chief Financial Officer

**David Elliott**  
Vice President, Finance

**Timur Kuru**  
Vice President, Operations – United  
States

**Bryce McLean**  
Vice President, Operations – Canada

**Russell Smith**  
Vice President, Operations –  
International & Offshore

**Ryan Van Beurden**  
Vice President, Rig-site Research &  
Development

**Lars Olesen**  
Vice President, Product Management

**Kevin Boston**  
Vice President, Business Development

**Kevin Lo**  
Vice President, New Ventures

## Corporate Head Office

Pason Systems Inc.  
6130 Third Street SE  
Calgary, Alberta  
T2H 1K4  
T: 403-301-3400  
F: 403-301-3499  
InvestorRelations@pason.com  
[www.pason.com](http://www.pason.com)

## Auditors

**Deloitte LLP**  
Calgary, Alberta

## Banker

**Royal Bank of Canada**  
Calgary, Alberta

## Registrar and Transfer Agent

**Computershare Trust Company of  
Canada**  
Calgary, Alberta

## Stock Trading

**Toronto Stock Exchange**  
Trading Symbol: PSI.TO

## Eligible Dividend Designation

Pursuant to the Canadian Income Tax  
Act, dividends paid by the Company