# THIRD QUARTER INTERIM REPORT

For the three and nine months ended September 30, 2017

## Performance Data

| | Three Months Ended September 30, | | | Nine Months Ended September 30, | | |
|---|---|---|---|---|---|---|
| | **2017** | 2016 | Change | **2017** | 2016 | Change |
| (CDN 000s, except per share data) | **($)** | ($) | (%) | **($)** | ($) | (%) |
| Revenue | **64,576** | 38,633 | 67 | **179,417** | 111,619 | 61 |
| Income (loss) | **8,813** | (7,117) | — | **22,861** | (29,296) | — |
| Per share – basic | **0.10** | (0.08) | — | **0.27** | (0.35) | — |
| Per share – diluted | **0.10** | (0.08) | — | **0.27** | (0.35) | — |
| EBITDA (1) | **25,493** | 8,347 | 205 | **70,012** | 5,763 | 1,115 |
| As a % of revenue | **39.5** | 21.6 | 18 | **39.0** | 5.2 | 34 |
| Adjusted EBITDA (1) | **26,158** | 8,487 | 208 | **70,427** | 15,780 | 346 |
| As a % of revenue | **40.5** | 22.0 | 19 | **39.3** | 14.1 | 25 |
| Funds flow from operations | **19,896** | 9,130 | 118 | **59,765** | 11,491 | 420 |
| Per share – basic | **0.23** | 0.11 | 109 | **0.71** | 0.14 | 407 |
| Per share – diluted | **0.23** | 0.11 | 109 | **0.70** | 0.14 | 400 |
| Cash from operating activities | **15,128** | 4,653 | 225 | **69,160** | 18,977 | 264 |
| Free cash flow (1) | **11,002** | 4,404 | 150 | **59,141** | 6,084 | 872 |
| Capital expenditures | **5,371** | 1,377 | 290 | **11,604** | 12,886 | (10) |
| Working capital | **190,518** | 191,785 | (1) | **190,518** | 191,785 | (1) |
| Total assets | **398,926** | 438,671 | (9) | **398,926** | 438,671 | (9) |
| Total long-term debt | **—** | — | — | **—** | — | — |
| Cash dividends declared | **0.17** | 0.17 | — | **0.51** | 0.51 | — |
| Shares outstanding end of period (#000's) | **84,916** | 84,367 | 1 | **84,916** | 84,367 | 1 |

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

### Q3 2017 vs Q3 2016

The Company generated consolidated revenue of $64.6 million in the third quarter of 2017, an increase of 67% from the same period in 2016. A stable oil price environment and continued optimism has led to increased drilling activity in Canada and the US market. Revenue in the third quarter of 2017, when compared to 2016, was negatively impacted by a stronger Canadian dollar relative to the US dollar. Revenue from the International business unit was unchanged from the third quarter of 2016.

Consolidated adjusted EBITDA increased to $26.2 million in the third quarter, up from $8.5 million in the third quarter of 2016. Significant increases in operating profit in all of the Company's key markets led to the rebound in this key measure.

The Company recorded net income of $8.8 million ($0.10 per share) in the third quarter of 2017, compared to a net loss of $7.1 million ($0.08 per share) recorded in the same period in 2016. The increase in Canadian and US revenue, combined with cost reduction programs previously implemented and a significant decline in depreciation expense from prior year levels, led to the increase in income from 2016. These factors were partially offset by a strengthening Canadian dollar relative to the US dollar.

# President’s Message

We are pleased with Pason’s third quarter results. Pason generated revenue of $64.6 million in the quarter, an increase of 16% from the second quarter and 67% from the prior year quarter. The main drivers of revenue growth were increased drilling activity in the North American land market and market share gains in the United States, both sequentially and year-over-year. Revenue growth in the quarter was negatively impacted by a stronger Canadian dollar relative to the US dollar. Revenue from the International business unit was flat, with improvements in Australia and the Andean region offset by a decrease in activity in Argentina.

Adjusted EBITDA was $26.2 million for the quarter, an increase of 35% from the second quarter and 208% from the prior year quarter. Adjusted EBITDA as a percentage of revenue was 41%, up from 35% in the second quarter. The drivers of this improvement were the significant increase in revenue with high incremental margins and cost reduction programs that were executed during the downturn.

Pason recorded net income of $8.8 million ($0.10 per share) compared to $6.9 million ($0.08 per share) in the second quarter and a loss of $7.1 million ($0.08 per share) in the prior year quarter. In addition to the factors outlined above, a significant decline in depreciation expense led to the increase in income. Free cash flow for the quarter was $11.0 million. At September 30, 2017, our working capital position stood at $191 million, including cash of $159 million. There is no debt on our balance sheet. We are maintaining our quarterly dividend at $0.17 share.

Our customers across the United States and Canada have learned to operate in a "lower for longer" commodity price environment. Operators remain highly focused on the cost and efficiency of drilling operations. Big data analytics remains a high priority for many E&P companies. There is a strong belief that the oil and gas industry has a lot of catching up to do in this area compared to most other industries. In the context of “factory drilling” there is significant value to be unlocked by correlating drilling and completions practices with the lifetime production of a well or a field. In addition, many drilling contractors are looking to differentiate their service offering from their competitors’ through technology.

In response to the evolving needs of our customers, we have increased our investment in R&D and IT with further growth planned going into 2018. In addition to continuously enhancing the functionality and performance of existing products, our development efforts are focused on being a key enabler of big data analytics strategies and of drilling optimization and automation efforts.

Many of our products directly improve the efficiency, effectiveness and safety of drilling operations and wellbore quality. Examples of this include our ePVT Adaptive Alarms, AC AutoDriller, abbl Directional Advisor® and the deployment of the advanced Exxon Drilling Advisory System®. We are building on our acquisition of Verdazo Analytics to provide customers with a holistic platform to analyze drilling, completions, production, financial and operational data. The deployment of an enhanced Pason Live web service to our cloud-based offering benefits office-based users of Pason data.

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 approximately $20 million in capital expenditures in 2017. Our highly capable and flexible IT and communications platform can host new Pason and third party software at the rig site and in the cloud.

The reduction in oil inventories in the third quarter highlights that the oil market is now in balance. As a result, we have recently seen upward movement in oil prices. Comments from several key OPEC countries, as well as from Russia, suggest that a reduction of the existing production cuts beyond the current agreement is a possibility. Further upward movement in oil prices and subsequent growth in global E&P investment are possible in the medium term. This would further stimulate drilling activity worldwide. Pason’s market positions are very strong. 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 (currently over 800). We are uniquely positioned to participate in the industry's growth.

Marcel Kessler
President and Chief Executive Officer
November 7, 2017

# Management's Discussion and Analysis

The following discussion and analysis has been prepared by management as of November 7, 2017, 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 Corporation 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 it's 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, | | |
|---|---|---|---|---|---|---|
| | **2017** | 2016 | Change | **2017** | 2016 | Change |
| (000s) | **($)** | ($) | (%) | **($)** | ($) | (%) |
| **Revenue** | | | | | | |
| Electronic Drilling Recorder | **29,547** | 16,200 | 82 | **82,350** | 46,817 | 76 |
| Pit Volume Totalizer/ePVT | **9,394** | 5,011 | 87 | **25,693** | 14,832 | 73 |
| Communications | **6,565** | 3,799 | 73 | **18,414** | 10,388 | 77 |
| Software | **5,343** | 2,665 | 100 | **15,246** | 7,587 | 101 |
| AutoDriller | **3,838** | 2,259 | 70 | **10,688** | 6,542 | 63 |
| Gas Analyzer | **4,936** | 2,804 | 76 | **13,227** | 8,281 | 60 |
| Other | **4,953** | 5,895 | (16) | **13,799** | 17,172 | (20) |
| **Total revenue** | **64,576** | 38,633 | 67 | **179,417** | 111,619 | 61 |

Electronic Drilling Recorder (EDR) and Pit Volume Totalizer (PVT) rental day performance for Canada and the United States is reported below:

**Canada**

| | Three Months Ended September 30, | | | Nine Months Ended September 30, | | |
|---|---|---|---|---|---|---|
| | **2017** | 2016 | Change | **2017** | 2016 | Change |
| | # | # | (%) | # | # | (%) |
| EDR rental days | **16,900** | 10,500 | 61 | **49,900** | 29,900 | 67 |
| PVT rental days | **15,500** | 9,600 | 61 | **46,100** | 27,600 | 67 |

**United States**

| | Three Months Ended September 30, | | | Nine Months Ended September 30, | | |
|---|---|---|---|---|---|---|
| | **2017** | 2016 | Change | **2017** | 2016 | Change |
| | # | # | (%) | # | # | (%) |
| EDR rental days | **49,500** | 23,800 | 108 | **128,500** | 67,400 | 91 |
| PVT rental days | **38,200** | 18,100 | 111 | **100,800** | 51,500 | 96 |

The Pason 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 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.

Total revenue increased 67% and 61% for the three and nine months ending September 2017, over the same period in 2016. This increase is attributable to an increase in drilling activity in the Company's Canadian, US, and certain International markets. The third quarter 2017 results were negatively impacted from a stronger Canadian dollar relative to the US dollar.

Industry activity in the US market increased 102% in the third quarter of 2017 compared to the corresponding period in 2016 (80% on a year-to-date basis), while third quarter Canadian rig activity increased 76% (87% on a year-to-date basis). Canadian EDR days, which includes some non-oil and gas-related activity, increased

61% in the third quarter of 2017 from 2016 levels (67% on a year-to-date basis), while US EDR days increased by 108% from the third quarter of 2016 (91% on a year-to-date basis).

For the first nine months of 2017, the Pason EDR was installed on 56% of the land rigs in the US compared to 53% during the same time period in 2016.

For the nine months ended September 30, 2017, the Pason EDR was installed on 89% of the land rigs in the Canadian market; for the same time period in 2016 the number of EDR days exceeded the number of reported industry days. 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.

Relative to the corresponding period in 2016, the Canadian market saw an increase in pricing pressure in 2017. This pricing pressure has stabilized during 2017.

The revenue generated from the Company's other wellsite instrumentation products tracked the percentage increase in drilling activity. The notable exceptions were:

- increased product adoption of EDR peripherals, including workstations and Pason Rig Display
- increased ePVT adoption rates in the US
- increased AutoDriller rentals in both Canada and the US due to the significant increase in drilling activity which led to more mechanical rigs being deployed in 2017 compared to 2016
- decreased revenue of service rig recorders in Latin America due to the drop in drilling activity which impacted other revenue

Included in the software category is revenue from the Company's data analytics subsidiary, Verdazo.

Other revenue is down due to the sale of the net operating assets of 3PS, Inc. (3PS) effective January 1, 2017.

For the third quarter of 2017, the Company saw an increase in activity in its Australian and Andean operating areas, compared to the corresponding period in 2016. In Argentina, the rig count was lower compared to 2016 levels.

# Discussion of Operations

## United States Operations

| | Three Months Ended September 30, | | | Nine Months Ended September 30, | | |
|---|---|---|---|---|---|---|
| | **2017** | 2016 | Change | **2017** | 2016 | Change |
| (000s) | **($)** | ($) | (%) | **($)** | ($) | (%) |
| **Revenue** | | | | | | |
| Electronic Drilling Recorder | **20,458** | 10,041 | 104 | **55,982** | 28,111 | 99 |
| Pit Volume Totalizer/ePVT | **6,335** | 2,902 | 118 | **16,532** | 8,252 | 100 |
| Communications | **3,454** | 1,831 | 89 | **9,426** | 4,548 | 107 |
| Software | **3,268** | 1,829 | 79 | **9,067** | 4,924 | 84 |
| AutoDriller | **2,057** | 955 | 115 | **5,281** | 2,537 | 108 |
| Gas Analyzer | **2,525** | 1,428 | 77 | **6,568** | 4,103 | 60 |
| Other | **2,581** | 3,332 | (23) | **6,983** | 9,860 | (29) |
| **Total revenue** | **40,678** | 22,318 | 82 | **109,839** | 62,335 | 76 |
| **Operating costs** | **17,130** | 12,653 | 35 | **47,642** | 38,647 | 23 |
| **Depreciation and amortization** | **4,151** | 5,243 | (21) | **13,322** | 17,479 | (24) |
| **Segment operating profit** | **19,397** | 4,422 | 339 | **48,875** | 6,209 | 687 |

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | **2017** | 2016 | **2017** | 2016 |
| | **$** | $ | **$** | $ |
| Revenue per EDR day - USD | **647** | 652 | **648** | 632 |
| Revenue per EDR day - CAD | **809** | 851 | **847** | 836 |

US land-based drilling continued its sequential increase quarter over quarter. Although the majority of the absolute rig count gains were seen in the Permian, the Haynesville and the Bakken regions participated in the increase.

US segment revenue increased by 82% in the third quarter of 2017 over the 2016 comparable period. For the first nine months, revenue increased 76% compared to the prior year. Included in the prior year results was revenue (included in other revenue) from 3PS, the net operating assets of which were sold effective January 1, 2017. Removing 3PS revenue from the comparative figures, revenue increased by 98% in the third quarter of 2017 compared to 2016 (106% increase when measured in USD). The value of the Canadian dollar relative to the US dollar had a negative impact on revenue when measured in Canadian dollars in the third quarter of 2017. For the first nine months of 2017, and removing 3PS, revenue increased by 93% (96% when measured in USD).

Industry activity in the US market during the third quarter of 2017 increased 102% from the prior year, and 80% for the first nine months. US market share was 58% for the third quarter of 2017 compared to 56% during the same period of 2016, primarily driven by market share growth in key US regions combined with changes in the mix of active customers.

EDR rental days increased by 108% for the quarter ended September 30, 2017, over the same time period in 2016, while revenue per EDR day in the third quarter of 2017 decreased to US$647, a decrease of US $5 over the same period in 2016.

Revenue per EDR day for the first nine months of 2017 was US$648, up US$16 from the same period in 2016.

Operating costs increased by 35% in the 2017 third quarter relative to the same period in the prior year. When measured in USD, and removing 3PS costs, operating costs increased by 65%, with the increase attributable to the hiring of additional field staff and higher repair costs to support the increase in activity.

Depreciation expense for the third quarter of 2017 decreased 21% over 2016 amounts due to the reduction in the capital program since 2014.

Segment profit increased by $15.0 million in the third quarter of 2017 compared to the corresponding period in 2016.

# Canadian Operations

| | Three Months Ended September 30, | | | Nine Months Ended September 30, | | |
|---|---|---|---|---|---|---|
| | **2017** | 2016 | Change | **2017** | 2016 | Change |
| (000s) | **($)** | ($) | (%) | **($)** | ($) | (%) |
| **Revenue** | | | | | | |
| Electronic Drilling Recorder | **6,689** | 4,030 | 66 | **18,894** | 11,717 | 61 |
| Pit Volume Totalizer/ePVT | **2,486** | 1,734 | 43 | **7,465** | 5,093 | 47 |
| Communications | **2,872** | 1,676 | 71 | **8,213** | 4,864 | 69 |
| Software | **1,945** | 778 | 150 | **5,879** | 2,474 | 138 |
| AutoDriller | **1,378** | 796 | 73 | **4,036** | 2,201 | 83 |
| Gas Analyzer | **2,099** | 1,111 | 89 | **5,760** | 3,261 | 77 |
| Other | **851** | 630 | 35 | **2,539** | 1,970 | 29 |
| **Total revenue** | **18,320** | 10,755 | 70 | **52,786** | 31,580 | 67 |
| **Operating costs** | **6,473** | 3,817 | 70 | **17,826** | 13,136 | 36 |
| **Depreciation and amortization** | **6,053** | 6,203 | (2) | **17,632** | 20,116 | (12) |
| **Segment operating profit (loss)** | **5,794** | 735 | 688 | **17,328** | (1,672) | — |

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | **2017** | 2016 | **2017** | 2016 |
| | **$** | $ | **$** | $ |
| Revenue per EDR day- CAD | **1,041** | 1,011 | **1,010** | 1,039 |

The third quarter Canadian rig activity showed significant year-over-year improvement, although activity was range bound for much of the quarter.

Canadian segment revenue increased by 70% for the quarter ended September 30, 2017 compared to the same period in 2016. This increase is the result of a 76% increase in the number of drilling industry days in the third quarter compared to 2016 levels. Included in the software category for 2017 is revenue earned by Verdazo.

EDR rental days increased 61% in the third quarter of 2017 compared to 2016 (67% for the first nine months of 2017).

Revenue per EDR day increased by $30 to $1,041 during the third quarter of 2017 compared to 2016. Revenue per EDR day for the nine months ended September 30, 2017 was $1,010, down $29 from the same period in 2016, driven in most part by customer mix, and the ongoing effects of pricing concessions made in prior periods.

Operating costs increased by 70% in the third quarter of 2017 relative to the same period in 2016 (36% on a year-to-date basis), with repair costs and direct field costs increasing due to higher activity, combined with the inclusion of Verdazo operating costs.

Depreciation and amortization expense decreased by approximately 2% for the three months ended September 30, 2017. The 2017 amounts include the amortization of investment tax credits received in the third quarter of 2017, offset by the amortization of intangibles that were recognized on the acquisition of Verdazo.

The third quarter 2017 operating profit of $5.8 million is an improvement of $5.1 million from the prior year. Segment operating profit for the first nine months of 2017 is $17.3 million compared to a loss of $1.7 million in the prior year.

## International Operations

| | Three Months Ended September 30, | | | Nine Months Ended September 30, | | |
|---|---|---|---|---|---|---|
| | **2017** | 2016 | Change | **2017** | 2016 | Change |
| (000s) | **($)** | ($) | (%) | **($)** | ($) | (%) |
| **Revenue** | | | | | | |
| Electronic Drilling Recorder | **2,400** | 2,129 | 13 | **7,474** | 6,989 | 7 |
| Pit Volume Totalizer/ePVT | **573** | 375 | 53 | **1,696** | 1,487 | 14 |
| Communications | **239** | 292 | (18) | **775** | 976 | (21) |
| Software | **130** | 58 | 124 | **300** | 189 | 59 |
| AutoDriller | **403** | 508 | (21) | **1,371** | 1,804 | (24) |
| Gas Analyzer | **312** | 265 | 18 | **899** | 917 | (2) |
| Other | **1,521** | 1,933 | (21) | **4,277** | 5,342 | (20) |
| **Total revenue** | **5,578** | 5,560 | — | **16,792** | 17,704 | (5) |
| **Operating costs** | **4,317** | 4,362 | (1) | **13,282** | 14,081 | (6) |
| **Depreciation and amortization** | **980** | 3,483 | (72) | **3,026** | 7,274 | (58) |
| **Segment operating profit (loss)** | **281** | (2,285) | — | **484** | (3,651) | — |

The international rig count was up in several of the Company's international markets, most notably Australia and portions of the Andean region in South America. These increases were offset by a decrease in activity in Argentina. As a result, revenue in the International operations segment was flat in the third quarter of 2017 compared to the same period in 2016. For the nine months of 2017, revenue decreased by 5% from prior years levels as a result of lower activity in the Company's Argentina market.

Operating costs decreased by 1% in the third quarter relative to the same period in the prior year as previous year cost reductions were offset by higher field costs in certain regions.

Depreciation expense decreased by approximately 72% for the three months ended September 30, 2017. In the third quarter of 2016 a $1.4 million charge was recorded to recognize obsolete inventory. This charge was included in depreciation expense.

The segment operating profit was $0.3 million for the third quarter of 2017, an improvement from the $2.3 million loss recorded in the corresponding period in 2016. The year-to-date profit was $0.5 million compared to a loss of $3.7 million in the prior year.

# Corporate Expenses

| | Three Months Ended September 30, | | | Nine Months Ended September 30, | | |
|---|---|---|---|---|---|---|
| | **2017** | 2016 | Change | **2017** | 2016 | Change |
| (000s) | **($)** | ($) | (%) | **($)** | ($) | (%) |
| **Other expenses** | | | | | | |
| Research and development | **6,945** | 5,358 | 30 | **19,083** | 17,615 | 8 |
| Corporate services | **3,553** | 3,956 | (10) | **11,157** | 12,360 | (10) |
| Stock-based compensation | **3,145** | 1,457 | 116 | **8,869** | 4,657 | 90 |
| Other | | | | | | |
| Restructuring costs | **—** | — | — | **—** | 10,861 | — |
| Foreign exchange loss (gain) | **113** | 96 | 18 | **(353)** | (2,227) | 84 |
| Other | **552** | 44 | 1,155 | **768** | 1,383 | (44) |
| **Total corporate expenses** | **14,308** | 10,911 | 31 | **39,524** | 44,649 | (11) |

In the first quarter of 2016, the Company initiated additional cost reduction initiatives to address the prolonged downturn in oil and gas drilling activity. As a result, the Company recorded a restructuring charge of $10.9 million in the first quarter of 2016.

## Q3 2017 vs Q2 2017

Consolidated revenue was $64.6 million in the third quarter of 2017 compared to $55.8 million in the second quarter of 2017, an increase of $8.8 million, or 16%. The second quarter is usually the Company's weakest due to the spring break-up in Canada. US activity levels increased from second quarter 2017 levels, which were partially offset by the strengthening of the Canadian dollar versus the US dollar. The Canadian segment earned revenue of $18.3 million in the third quarter of 2017 compared to $10.5 million in the second quarter of 2017, an increase of $7.8 million. Revenue in the US market increased by $1.5 million, from $39.2 million in the second quarter of 2017 to $40.7 million in the third quarter of 2017, as both industry activity and the Company's market share increased. The International segment realized a revenue decrease of $0.5 million.

The Company recorded a net profit in the third quarter of 2017 of $8.8 million ($0.10 per share) compared to a profit of $6.9 million ($0.08 per share) in the second quarter of 2017. Included in the third quarter results is an increase in the Company's research and development expenses over the second quarter of $0.7 million and a foreign exchange loss reported of $0.1 million versus a foreign exchange gain of $0.7 million recorded in the second quarter of 2017.

Sequentially, EBITDA increased from $21.1 million in the second quarter of 2017 to $25.5 million in the third quarter of 2017. Adjusted EBITDA, which adjusts for foreign exchange and certain non-recurring charges, increased from $19.4 million in the second quarter of 2017 to $26.2 million in the third quarter of 2017. Funds flow from operations increased from $18.8 million in the second quarter of 2017 to $19.9 million in the third quarter of 2017.

# Summary of Quarterly Results

| Three Months Ended | Dec 31, 2015 | Mar 31, 2016 | Jun 30, 2016 | Sept 30, 2016 | Dec 31, 2016 | Mar 31, 2017 | Jun 30, 2017 | **Sept 30, 2017** |
|---|---|---|---|---|---|---|---|---|
| (000s, except per share data) | ($) | ($) | ($) | ($) | ($) | ($) | ($) | ($) |
| **Revenue** | 59,838 | 45,813 | 27,173 | 38,633 | 48,827 | 59,049 | 55,792 | **64,576** |
| **(Loss) income** | (841) | (10,860) | (11,319) | (7,117) | (11,325) | 7,153 | 6,895 | **8,813** |
| Per share – basic | (0.01) | (0.13) | (0.13) | (0.08) | (0.13) | 0.08 | 0.08 | **0.10** |
| Per share – diluted | (0.01) | (0.13) | (0.13) | (0.08) | (0.13) | 0.08 | 0.08 | **0.10** |
| **EBITDA** (1) | 20,736 | (353) | (2,231) | 8,347 | (2,291) | 23,469 | 21,050 | **25,493** |
| **Adjusted EBITDA** (1) | 20,128 | 8,763 | (1,470) | 8,487 | 15,225 | 24,908 | 19,361 | **26,158** |
| **Funds flow from (used in) operations** | 17,933 | 3,335 | (974) | 9,130 | 15,324 | 21,074 | 18,795 | **19,896** |
| Per share – basic | 0.21 | 0.04 | (0.01) | 0.11 | 0.18 | 0.25 | 0.22 | **0.23** |
| Per share – diluted | 0.21 | 0.04 | (0.01) | 0.11 | 0.18 | 0.25 | 0.22 | **0.23** |
| **Cash from operating activities** | 10,911 | 11,331 | 2,993 | 4,653 | 665 | 29,831 | 24,201 | **15,128** |
| **Free cash flow** (1) | 3,878 | 4,141 | (2,461) | 4,404 | (153) | 28,511 | 19,628 | **11,002** |

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

### Reconcile income (loss) to EBITDA

| Three Months Ended | Dec 31, 2015 | Mar 31, 2016 | Jun 30, 2016 | Sept 30, 2016 | Dec 31, 2016 | Mar 31, 2017 | Jun 30, 2017 | **Sept 30, 2017** |
|---|---|---|---|---|---|---|---|---|
| (000s) | ($) | ($) | ($) | ($) | ($) | ($) | ($) | **($)** |
| (Loss) income | (841) | (10,860) | (11,319) | (7,117) | (11,325) | 7,153 | 6,895 | **8,813** |
| Add: | | | | | | | | |
| Taxes | (1,027) | (6,817) | (6,728) | (922) | (3,019) | 1,796 | 155 | **2,351** |
| Depreciation and amortization | 19,802 | 16,362 | 13,578 | 14,929 | 10,515 | 11,973 | 10,823 | **11,184** |
| Stock-based compensation | 2,802 | 962 | 2,238 | 1,457 | 1,538 | 2,547 | 3,177 | **3,145** |
| **EBITDA** (1) | 20,736 | (353) | (2,231) | 8,347 | (2,291) | 23,469 | 21,050 | **25,493** |

### Reconcile EBITDA to Adjusted EBITDA

| Three Months Ended | Dec 31, 2015 | Mar 31, 2016 | Jun 30, 2016 | Sept 30, 2016 | Dec 31, 2016 | Mar 31, 2017 | Jun 30, 2017 | **Sept 30, 2017** |
|---|---|---|---|---|---|---|---|---|
| (000s) | ($) | ($) | ($) | ($) | ($) | ($) | ($) | **($)** |
| EBITDA | 20,736 | (353) | (2,231) | 8,347 | (2,291) | 23,469 | 21,050 | **25,493** |
| Add: | | | | | | | | |
| Impairment charges | — | — | — | — | 17,474 | — | — | **—** |
| Restructuring costs | 1,024 | 10,861 | — | — | — | — | — | **—** |
| Foreign exchange | (1,549) | (2,719) | 396 | 96 | 284 | 223 | (689) | **113** |
| Other | (83) | 974 | 365 | 44 | (242) | 1,216 | (1,000) | **552** |
| **Adjusted EBITDA** (1) | 20,128 | 8,763 | (1,470) | 8,487 | 15,225 | 24,908 | 19,361 | **26,158** |

### Reconcile cash from operating activities to free cash flow

| Three Months Ended | Dec 31, 2015 | Mar 31, 2016 | Jun 30, 2016 | Sep 30, 2016 | Dec 31, 2016 | Mar 31, 2017 | Jun 30, 2017 | **Sep 30, 2017** |
|---|---|---|---|---|---|---|---|---|
| (000s) | ($) | ($) | ($) | ($) | ($) | ($) | ($) | **($)** |
| Cash from operating activities | 10,911 | 11,331 | 2,993 | 4,653 | 665 | 29,831 | 24,201 | **15,128** |
| Less: | | | | | | | | |
| Additions to property, plant and equipment (net of proceeds and working capital) | (7,060) | (5,493) | (4,437) | 410 | (1,827) | (1,027) | (3,913) | **(3,881)** |
| Deferred development costs | 27 | (1,697) | (1,017) | (659) | 1,009 | (293) | (660) | **(245)** |
| **Free cash flow** (1) | 3,878 | 4,141 | (2,461) | 4,404 | (153) | 28,511 | 19,628 | **11,002** |

Though the Company has seen a deterioration in its operating results due to the decline in drilling activity, Pason's quarterly financial results still 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,** | **2017** | 2016 | Change |
|---|---|---|---|
| (000s) | **($)** | ($) | (%) |
| Cash and cash equivalents | **159,437** | 154,598 | 3 |
| Working capital | **190,518** | 191,785 | (1) |
| Funds flow from operations (1) | **59,765** | 11,491 | 420 |
| Capital expenditures (1) | **11,604** | 12,886 | (10) |
| As a % of funds flow (1) (2) | **19.4%** | 112.1% | (83) |

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

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

Effective December 31, 2016, the Company purchased all of the existing and outstanding shares of Verdazo Analytics, Inc. (Verdazo). In January 2017, the Company paid $4.8 million of the cash portion owing.

During 2016, the Company initiated a review of its investment in 3PS, Inc. (3PS). In the fourth quarter of 2016, a final agreement was entered into for the sale of the net operating assets of 3PS, effective January 1, 2017. Cash of $7.1 million was received in the first quarter of 2017.

In addition, during 2017 the Company received a tax refund of $6.7 million relating to the refiling of prior years' tax returns.

# Contractual Obligations

| | Less than 1 year | 1–3 years | Thereafter | Total |
|---|---|---|---|---|
| (000s) | ($) | ($) | ($) | ($) |
| Operating leases and other contracts | 13,197 | 7,904 | 5,727 | 26,828 |

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, 2017, 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, 2017, no amount had been drawn on the facility.

# Disclosure of Outstanding Share and Options Data

As at September 30, 2017, there were 84.9 million common shares and 4.2 million options issued and outstanding.

# SEDAR

Additional information relating to the Company can be accessed on the Company's website at www.pason.com and on the Canadian Securities Administrators' System for Electronic Document Analysis and Retrieval (SEDAR) at 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. See note 2 to the Condensed Consolidated Interim Financial Statements for additional information.

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 85% of the Company's revenues are generated in Canada and the US, which limits exposure to risks and uncertainties in foreign countries.

## 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. During the year ended December 31, 2016, 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**(1)(4)(6)(7)
President
Bragg Creek Financial
Consultants Ltd.
Calgary, Alberta

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

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

**Judi Hess**(2)(4)(5)
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**
President and General Manager – United States

**Bryce McLean**
General Manager, 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

**Melinda Ando**
General Counsel & Corporate Secretary

## Corporate Head Office

Pason Systems Inc.
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Calgary, Alberta
T2H 1K4
T: 403-301-3400
F: 403-301-3499
InvestorRelations@pason.com
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 to Canadian residents are considered to be “eligible” dividends.