First Quarter Report
Three months ended March 31, 2014

Q1

cequence energy ltd

www.cequence-energy.com

HIGHLIGHTS

	Three months ended March 31,		
(000s except per share and per unit amounts)	**2014**	2013	% Change
Financial ($)			
Production revenue [1]	**41,095**	22,005	87
Comprehensive income (loss)	**512**	(5,439)	109
Per share, basic and diluted	**0.00**	(0.03)	100
Funds flow from operations [2]	**23,082**	10,652	117
Per share, basic and diluted	**0.11**	0.05	120
Production volumes			
Natural gas (Mcf/d)	**59,898**	46,306	29
Crude oil (bbls/d)	**992**	608	63
Natural gas liquids (bbls/d)	**638**	496	29
Total (boe/d)	**11,613**	8,822	32
Sales prices			
Natural gas, including realized hedges ($/Mcf)	**5.28**	3.51	50
Crude oil ($/bbl)	**101.65**	91.90	11
Natural gas liquids ($/bbl)	**62.08**	52.84	17
Total ($/boe)	**39.32**	27.72	42
Netback ($/boe)			
Price	**39.32**	27.72	42
Royalties	**(4.13)**	(2.63)	57
Transportation	**(1.52)**	(1.59)	(4)
Operating costs	**(7.40)**	(7.24)	2
Operating netback	**26.27**	16.26	62
General and administrative	**(2.34)**	(2.02)	16
Interest [5]	**(1.79)**	(0.48)	273
Cash netback	**22.14**	13.76	61
Capital expenditures ($)			
Capital expenditures	**58,547**	43,659	34
Net acquisitions (dispositions) [4]	**(3,229)**	18	n/a
Total capital expenditures	**55,318**	43,677	27
Net debt and working capital (deficiency) [3]	**(143,536)**	(78,365)	83
Weighted average shares outstanding			
Basic	**210,918**	200,610	5
Diluted	**212,964**	200,610	6

(1) Production revenue is presented gross of royalties and includes realized gains (loss) on commodity contracts.

(2) Funds flow from operations is calculated as cash flow from operating activities before adjustments for decommissioning liabilities expenditures and net changes in non-cash working capital.

(3) Net debt and working capital (deficiency) is calculated as cash and net working capital less commodity contract assets and liabilities, demand credit facilities, principal value of senior notes and excluding other liabilities.

(4) Represents the cash proceeds from the sale of assets and cash paid for the acquisition of assets, as applicable.

(5) Represents finance costs less amortization on transaction costs and accretion expense on senior notes and provisions.

Management's Discussion and Analysis

This Management's Discussion and Analysis ("MD&A") of the financial and operating results of Cequence Energy Ltd. ("Cequence" or the "Company") should be read in conjunction with the Company's unaudited condensed consolidated financial statements (the "consolidated financial statements") and related notes for the three months ended March 31, 2014 as well as with the audited consolidated financial statements (the "annual financial statements") and related notes for the years ended December 31, 2013 and 2012.

Additional information relating to the Company, including its MD&A for the prior year and the annual information form is available on SEDAR at www.sedar.com.

This MD&A is dated May 13, 2014.

Basis of Presentation

The consolidated financial statements and comparative information have been prepared in accordance with IAS 34, "Interim Financial Reporting" ("IAS 34"), as issued by the International Accounting Standards Board ("IASB"). The financial information presented reflects the consolidated financial statements of Cequence.

The reporting and the measurement currency is the Canadian dollar. For the purpose of calculating unit costs, natural gas is converted to a barrel of oil equivalent ("boe") using six thousand cubic feet of natural gas equal to one barrel of oil unless otherwise stated. The term barrel of oil equivalent (boe) may be misleading, particularly if used in isolation. A boe conversion ratio for gas of 6 Mcf:1 boe is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

For three months ended March 31, 2014, the ratio between the average price of West Texas Intermediate ("WTI") crude oil at Cushing and NYMEX natural gas was approximately 21:1 ("Value Ratio"). The Value Ratio is obtained using the first quarter 2014 WTI average price of $98.65 (US$/Bbl) for crude oil and the first quarter 2014 NYMEX average price of $4.72 (US$/MMbtu) for natural gas. This Value Ratio is significantly different from the energy equivalency ratio of 6:1 and using a 6:1 ratio would be misleading as an indication of value.

Unless otherwise stated and other than per unit items, all figures are presented in thousands.

Non-GAAP Measurements

Within the MD&A references are made to terms commonly used in the oil and gas industry, including operating netback, cash netback, net debt and working capital (deficiency) and funds flow from operations.

Operating and cash netback is not defined by IFRS in Canada and is referred to as a non-GAAP measure. Operating netback equals total revenue less royalties, operating costs and transportation costs. Cash netback equals the operating netback less general and administrative expenses and interest expense. Management utilizes these measures to analyze operating performance.

Net debt and working capital (deficiency) is a non-GAAP term that is calculated as cash and net working capital less commodity contract assets and liabilities, demand credit facilities, principal value of senior notes and excluding other liabilities. Cequence uses net debt and working capital deficiency as it provides an estimate of the Company's assets and obligations expected to be settled in cash.

Funds flow from operations is a non-GAAP term that represents cash flow from operating activities before adjustments for decommissioning liabilities expenditures and net changes in non-cash working capital. The Company evaluates its performance based on earnings and funds flow from operations. The Company considers funds flow from operations a key measure as it demonstrates the Company's ability to generate the cash flow necessary to fund future growth through capital investment and to repay debt. The Company's calculation of funds flow from operations may not be comparable to that reported by other companies. Funds flow from operations per share is calculated using the same weighted average number of shares outstanding used in the calculation of comprehensive income (loss) per share.

Non-GAAP financial measures do not have a standardized meaning prescribed by IFRS and are therefore unlikely to be comparable to similar measures presented by other issuers.

Description Of The Business

Cequence is actively engaged in the exploration for and the development of oil and natural gas reserves. Cequence's primary focus is the development of internally generated resource plays at Ansell and Simonette in the Alberta Deep Basin. The Company also has assets in Northeast British Columbia and the Peace River Arch of Alberta. The common shares of Cequence trade on the Toronto Stock Exchange under the symbol CQE.

Selected Financial Information

A reconciliation of cash flow from operating activities to funds flow from operations and other selected financial information is as follows:

	Three months ended March 31,		
$(000s)	**2014**	**2013**	**2012**
Cash flow from operating activities	**28,805**	15,110	8,443
Decommissioning liabilities expenditures	**208**	74	530
Net change in non-cash working capital	**(5,931)**	(4,532)	(2,218)
Funds flow from operations	**23,082**	10,652	6,755
Per share, basic and diluted ($)	**0.11**	0.05	0.04
Production revenue	**41,095**	22,005	19,864
Comprehensive income (loss)	**512**	(5,439)	(7,936)
Per share, basic and diluted ($)	**0.00**	(0.03)	(0.05)
Total assets	**641,577**	544,106	511,600
Demand credit facilities	**26,747**	41,033	53,139
Senior notes – principal	**60,000**	–	–

Cequence recorded comprehensive income of $512 for the three months ended March 31, 2014 compared to a loss of $5,439 in 2013. The increase is mainly due to increased production revenues due to higher production and pricing in 2014 compared to 2013. The increase in production revenue more than offset the increase in losses on derivative contracts, senior notes interest expense, deferred income tax expense and higher depletion expense due to increased volumes in 2014.

Funds flow from operations was $23,082 for the three months ended March 31, 2014 compared to $10,652 in 2013. The increase in funds flow from operations was attributable to increased production volumes and higher natural gas prices compared to the comparative period. Cequence realized an average natural gas price after hedging losses of $5.28 per mcf for the three months ended March 31, 2014 representing an 50 percent increase from the first quarter of 2013.

Results Of Operations

PRODUCTION

	Three months ended March 31,	
	2014	2013
Natural gas (Mcf/d)	**59,898**	46,306
Crude oil (bbls/d)	**992**	608
Natural gas liquids (bbls/d)	**638**	496
Total (boe/d)	**11,613**	8,822
Total production (boe)	**1,045,170**	793,966

Production for the three months ended March 31, 2014 averaged 11,613 boe/d compared to production of 8,822 boe/d in 2013. Production additions were largely from the Company's Simonette property. Average production from Simonette for the three months ended March 31, 2014 increased to 8,250 boe/d from 5,350 boe/d in the first quarter of 2013. Cequence is also actively drilling at Ansell and participated in 7 gross (3.4 net) wells in the past year of which only two wells produced in the first quarter due to facility restrictions. Cequence is constructing a facility at Ansell and production is expected to increase in the second quarter of 2014.

REVENUE

	Three months ended March 31,	
$(000s)	**2014**	2013
Revenue		
Natural gas	**33,655**	14,520
Realized gain (loss) on natural gas hedges	**(5,198)**	95
Total natural gas	**28,457**	14,615
Crude oil	**9,072**	5,032
Natural gas liquids	**3,566**	2,358
Total production revenue, gross of royalties	**41,095**	22,005
Average prices		
Natural gas ($/Mcf)	**6.24**	3.48
Realized natural gas hedge ($/Mcf)	**(0.96)**	0.03
Natural gas including hedge ($/Mcf)	**5.28**	3.51
Crude oil ($/bbl)	**101.65**	91.90
Natural gas liquids ($/bbl)	**62.08**	52.84
Average sales price before hedge ($/boe)	**44.29**	27.60
Average sales price including hedge ($/boe)	**39.32**	27.72
Benchmark pricing		
AECO-C spot (CDN$/Mcf)	**5.59**	3.20
WTI crude oil (US$/bbl)	**98.65**	94.30
Edmonton par price (CDN$/bbl)	**99.85**	88.55
US$/CDN$ exchange rate	**0.91**	0.99

Total production revenue, gross of royalties, was $41,095 in the first quarter of 2014 compared to $22,005 in 2013. The increase in revenue is attributable to the 42 percent increase in realized sales prices and 32 percent increase in production.

Canadian benchmark natural gas prices averaged $5.59 per mcf in 2014, up 75 percent from the same time period in 2013. AECO prices increased significantly in 2014 as inventory levels decreased in response to a cold North American winter. Cequence realized an increase in natural gas sales prices comparable to the increase in benchmark prices as it sells most of its natural gas on the AECO 5A daily index. Cequence realized an average natural gas price of $6.24 per mcf for the three months ended March 31, 2014 up 79 percent from the comparable period in 2013. Realized natural gas prices for the three months ended March 31, 2014 are above benchmark prices as much of the Company's natural gas sells at a premium to AECO due to the heat content of the gas.

Oil prices for the first quarter of 2014 were $101.65 per barrel, up 11 percent from the same time period in 2013. The Company reports wellhead condensate and crude oil together. Wellhead condensate sold at a premium to crude oil in the first quarter resulting in an average sales price greater than the benchmark Edmonton par price. Natural gas liquids prices for the three months ended March 31, 2014 were $62.08 per barrel, up 17 percent from the same time period in 2013. The increase in average realized natural gas liquids prices is due to increased benchmark natural gas liquids prices in 2014 compared to 2013.

COMMODITY PRICE MANAGEMENT

	Three months ended March 31,	
$(000s)	**2014**	2013
Realized gain (loss) on commodity contracts	**(5,198)**	95
Unrealized loss on commodity contracts	**(6,621)**	(3,328)
Total	**(11,819)**	(3,233)

Cequence has a commodity price risk management program which provides the Company flexibility to enter into derivative and physical commodity contracts to protect future cash flows for planned capital expenditures against an unpredictable commodity price environment. Management is authorized to establish hedges equal to approximately 50 percent of production net of estimated royalty payments. Historically, natural gas hedges have been executed on the AECO 5A index to match the Company's marketing arrangements.

For the remainder of 2014, Cequence has hedged approximately 50 percent (30,000 GJ/d) of its forecasted natural gas production volumes net of royalties at an average AECO 5A price of $3.45 per GJ or approximately $3.86 per mcf based on the heat content of the Company's natural gas.

For the first quarter of 2015, Cequence has 20,000 GJ/d hedged at an average price of $3.79 per GJ or $4.25 per mcf. For the remainder of 2015 Cequence has 10,000 GJ/d hedged at an average price of $3.73 per GJ or $4.17 per mcf.

The fair value of the commodity contracts outstanding at March 31, 2014 was a current liability of $9,470 and a non-current liability of $107 (December 31, 2013 - current liability of $2,880 and a non-current liability of $76).

ROYALTY EXPENSE

	Three months ended March 31,	
$(000s)	**2014**	2013
Crown	**2,385**	1,337
Freehold / Overriding	**1,933**	752
Total Royalties	**4,318**	2,089
Per unit of production ($/boe)	**4.13**	2.63
As a % of Revenue, Before Hedging Activity		
Crown	**5%**	6%
Freehold / Overriding	**4%**	4%
	9%	10%

Royalty expense for the three months ended March 31, 2014 was $4,318 or 9 percent of revenue compared to $2,089 or 10 percent of revenue in 2013. Crown royalties as a percentage of revenue in both 2014 and 2013 reflect low natural gas prices and royalty rates of 5 percent on initial production from new horizontal wells. Based on forecast commodity prices and production levels, Cequence expects royalties will average approximately 9 percent of production revenue in 2014.

TRANSPORTATION EXPENSE

	Three months ended March 31,	
$(000s)	**2014**	2013
Transportation ($)	**1,587**	1,259
Per unit of production ($/boe)	**1.52**	1.59

Transportation expense for the three months ended March 31, 2014 was $1.52 per boe and is consistent with the prior period.

OPERATING COSTS

	Three months ended March 31,	
$(000s)	**2014**	2013
Operating costs ($)	**7,731**	5,746
Per unit of production ($/boe)	**7.40**	7.24

For the three months ended March 31, 2014, operating costs were $7.40 per boe consistent with $7.24 per boe in the comparative period in 2013. Operating costs for the Simonette property are significantly lower than corporate operating costs due to facility ownership and the Company's marketing arrangements. For the three months ended March 31, 2014 Simonette operating costs were $5.59 per boe, compared to operating costs of $11.86 per boe in the Company's other properties. Simonette currently comprises 71 percent of corporate production and has been a focus of the Company's capital expenditures and production growth for the past three years. Cequence expects operating costs at Simonette to remain low as production volumes from the property increase. The Company expects 2014 corporate operating costs to average $6.85 per boe as production additions are expected to have low per unit operating costs.

OPERATING NETBACK

	Three months ended March 31,	
($/boe)	**2014**	2013
Production revenue [(1)]	**39.32**	27.72
Royalty expense	**(4.13)**	(2.63)
Transportation expense	**(1.52)**	(1.59)
Operating costs	**(7.40)**	(7.24)
Operating netback, $/boe	**26.27**	16.26
Operating netback, excluding realized hedges , $/boe	**31.25**	16.14

(1) Production revenue is presented gross of royalties and includes realized gain (loss) on commodity contracts.

Cequence's netback for the three months ended March 31, 2014 increased 62 percent to $26.27 per boe from $16.26 per boe in 2013. The increase in 2014 operating netbacks is mainly due to increased production revenue due to higher production volumes and commodity prices in 2014 compared to 2013.

GENERAL AND ADMINISTRATIVE EXPENSES

	Three months ended March 31,	
$(000s)	**2014**	2013
G&A expenses ($)	**2,451**	1,600
Per unit of production ($/boe)	**2.34**	2.02

General and administrative ("G&A") costs per boe for the three months ended March 31, 2014 increased to $2.34 per boe from $2.02 per boe in the prior year. The increase relates to higher compensation and legal expenses in the first quarter of 2014. Annual G&A expenses are expected to decrease on a year over year basis to approximately $1.50 - $2.00 per boe.

FINANCE COSTS

	Three months ended March 31,	
$(000s)	**2014**	2013
Interest expense on credit facilities	**544**	384
Interest expense on senior notes	**1,332**	–
Amortization of transaction costs	**77**	–
Accretion expense on senior notes	**60**	–
Accretion expense on provisions	**203**	198
Total finance costs	**2,216**	582
Per unit of production ($/boe)	**2.12**	0.73
Interest per unit of production ($/boe)	**1.79**	0.48

Finance costs for the three months ended March 31, 2014 were $2,216 compared to $582 for the comparative period in 2013. The increase is directly attributable to higher credit facility standby charges and commitment fees and increased interest expense on the senior notes which were issued by the Company on October 3, 2013.

OTHER EXPENSE (INCOME)

	Three months ended March 31,	
$(000s)	**2014**	2013
Gain on sale of property and equipment	**(2,061)**	–
Transaction costs	**–**	225
Other	**(30)**	(30)
Total other expense (income)	**(2,091)**	195

During the three months ended March 31, 2014, the Company completed the sales of certain oil and gas properties for total cash consideration of $5,634 (2013 - $nil), subject to final adjustments. The sales resulted in a gain recognized in comprehensive income (loss) of $2,061 (2013 - $nil).

DEPLETION, DEPRECIATION AND IMPAIRMENT

	Three months ended March 31,	
$(000s)	**2014**	2013
Depletion and depreciation expense	**12,442**	8,930
Impairment	**–**	–
Total depletion, depreciation and impairment	**12,442**	8,930
Per unit of production ($/boe)	**11.90**	11.25
Per unit of production, excluding impairment ($/boe)	**11.90**	11.25

Depletion and depreciation expense for the three months ended March 31, 2014 and 2013, was $12,442 ($11.90 per boe) and $8,930 ($11.25 per boe), respectively. Depletion and depreciation rates are similar to the comparable period in 2013. Cequence reviewed its CGUs for impairment indicators at March 31, 2014 and determined that there were none.

PROVISIONS

Decommissioning liabilities

Total decommissioning liabilities at March 31, 2014 were $27,227 compared to $26,643 at December 31, 2013. The following table summarizes the changes in decommissioning liabilities for the respective periods:

(000s)	**March 31, 2014**	December 31, 2013
Balance, beginning of period	**26,643**	32,564
Property acquisitions	**–**	285
Property dispositions	**(450)**	(1,729)
Accretion expense	**201**	819
Liabilities incurred	**544**	1,120
Abandonment costs incurred	**(208)**	(619)
Revisions in estimated cash flows	**(788)**	(973)
Revisions due to change in discount rates	**1,285**	(4,824)
Balance, end of period	**27,227**	26,643

Onerous contracts

As at March 31, 2014, the Company recognized a provision related to an onerous lease contract of $423 (December 31, 2013 - $502). The provision for onerous lease contract represents the present value of the future lease obligations that the Company is presently obligated to make under a non-cancellable onerous operating lease contract, less revenue expected to be earned on the lease, including estimated future sub-lease revenue.

SHARE BASED PAYMENTS

Stock Options

For the three months ended March 31, 2014, Cequence recorded $599 (2013 – $1,134) in share based payment expense related to stock options with a corresponding increase to contributed surplus.

	March 31, 2014		December 31, 2013	
	Number of Options (000s)	**Weighted Average Exercise Price $**	Number of Options (000s)	Weighted Average Exercise Price $
Outstanding, beginning of period	**18,617**	**2.15**	17,289	2.19
Granted	**20**	**1.70**	1,780	1.70
Forfeited	**–**	**–**	(444)	1.92
Exercised	**–**	**–**	(8)	1.35
Outstanding, end of period	**18,637**	**2.15**	18,617	2.15

Restricted Share Units

For the three months ended March 31, 2014, Cequence recorded $242 (2013 – nil) in share based payment expense related to restricted share units ("RSU") with a corresponding increase to share based payment liability.

Number of RSUs (000s)	**March 31, 2014**	December 31, 2013
Outstanding, beginning of period	**561**	–
Granted	**20**	561
Outstanding, end of period	**581**	561

COMMON SHARES OUTSTANDING

Cequence has an unlimited number of common voting shares and common non-voting shares with no par value.

Issued common voting shares (000s)	Number	Stated Value
Balance, December 31, 2012	200,610	$ 606,703
Common shares issued on property acquisition	10,300	17,510
Common shares issued on exercise of stock options	8	15
Share issue costs, net of taxes of ($35)	–	104
Balance, December 31, 2013 and March 31, 2014	**210,918**	**$ 624,332**

On April 15, 2013, the Company issued an aggregate of 10,300,000 Cequence common shares as partial consideration for the acquisition of oil and gas properties located in the Simonette area of Alberta. The common shares were distributed directly to the shareholders of a publicly listed Canadian company.

Issued warrants (000s)	Number	Stated Value
Balance, December 31, 2012	–	$ –
Granted on issuance of senior notes, net of tax of $183	3,000	1,339
Share issue costs, net of taxes of $13	–	(39)
Balance, December 31, 2013 and March 31, 2014	**3,000**	**$ 1,300**

On October 3, 2013, Cequence granted to the lender of the senior notes 3.0 million warrants at an exercise price of $2.03 to purchase common shares. The warrants will expire on October 3, 2020 and were issued with an exercise price of $2.03 which was based at a 30 percent premium to the 30 trading day volume weighted average trading price of the Cequence common shares on the TSX ending on the day immediately preceding the closing date.

As of the date of this MD&A, Cequence had the following securities outstanding: 210,988 common voting shares, 3,000,000 warrants to purchase common shares, 18,667 stock options and 581 RSUs.

CAPITAL EXPENDITURES

	Three months ended March 31,	
$(000s)	**2014**	2013
Property acquisitions [1]	**2,405**	18
Property dispositions [1]	**(5,634)**	–
Land	**278**	651
Geological & geophysical and capitalized overhead	**546**	455
Drilling, completions and workovers	**35,166**	30,542
Equipment, pipelines and facilities	**22,500**	11,956
Office furniture & equipment	**57**	55
Total capital expenditures	**55,318**	43,677

(1) Represent the cash proceeds from the sale of assets and cash paid for the acquisition of assets, as applicable.

Net capital expenditures for the three months ended March 31, 2014 increased to $55,318 from $43,677 in 2013. For the three months ended March 31, 2014, drilling, completion and workover expenditures totalled $35,166 which included the drilling of 7.0 gross (3.9 net) horizontal wells and the completion of 11.0 gross (7.1 net) horizontal wells. Of the wells drilled in the first quarter 4.0 gross (0.9 net) were Wilrich wells at Ansell, and 2.0 gross (2.0 net) Montney wells at Simonette and 1.0 gross (1.0 net) Wilrich well at Simonette.

Equipment and facility expenditures in the three months ended March 31, 2014 of $22,500 were mainly directed towards the construction of a gathering system and compression facility at Ansell and additional compression at Simonette. The Ansell facilities were completed in the second quarter and increased Cequence's production capacity at Ansell to 20 mmcf/d. At Simonette, Cequence compression was added to the main production facility in the field increasing its capacity to approximately 70 mmcf/d.

During the three months ended March 31, 2014, the Company completed the sales of certain oil and gas properties for total cash consideration of $5,634 (2013 - $nil), subject to final adjustments. The sales resulted in a gain recognized in comprehensive income (loss) of $2,061 (2013 - $nil).

Cequence has budgeted net capital expenditures of $120,000 for the year ended December 31, 2014 and is expected to be focused on the development of the Company's Simonette and Ansell assets. Capital expenditures for 2014 are expected to be funded from cash flow, proceeds from the senior notes and borrowing from the Company's senior credit facility. The Company continually monitors fluctuations in natural gas prices and may adjust budgeted discretionary capital spending based on the Company's hedge position and short to medium term natural gas prices.

Income Taxes

At March 31, 2014, a deferred income tax asset of $31,627 (December 31, 2013 - $36,094) has been recognized as the Company believes, based on estimated cash flows, its realization is probable. At March 31, 2014, Cequence has the following estimated tax pools:

Classification	Amount $(000s)
Canadian exploration expense	213,577
Non-capital losses	133,458
Undepreciated capital cost	138,001
Canadian oil and gas property expense	80,507
Canadian development expense	86,521
Scientific research and experimental development tax credit	22,704
Share issue costs	4,889
Investment tax credits	3,981
	683,638

The Company's non-capital losses expire in 2026 and thereafter. Based on the Company's expected cash flow and available tax pools, Cequence does not expect to be taxable for the next three years.

Liquidity and Capital Resources

Cequence's objectives are to maintain a flexible capital structure in order to meet its financial obligations and to execute its business plan throughout the commodity cycle. The Company's capital comprises shareholders' equity, demand credit facilities, senior notes and working capital. Cequence manages the capital structure and makes adjustments in light of economic conditions and the risk characteristics of the underlying assets.

In October 2013, Cequence closed an investment with CPPIB Credit Investments Inc., ("CII"), a wholly-owned subsidiary of Canada Pension Plan Investment Board ("CPPIB"), for an initial investment by CII of $60 million in unsecured five year senior notes with a further $60 million of notes available at a future date, subject to the approval of both CII and Cequence on terms to be confirmed at the time of issuance. In addition, Cequence granted CII 3.0 million warrants to purchase common shares. The investment has allowed Cequence to accelerate the development of its assets.

The Company monitors net debt to funds flow as one measure of the Company's ability to manage its debt levels under current operating conditions and meet current obligations as they come due. Management targets a debt to funds flow ratio of less than two times. As at March 31, 2014, the Company's net debt to annualized funds flow ratio was calculated as 1.6:1 (December 31, 2013 – 1.9:1) based on annualized first quarter results. In a typical year due to seasonality, capital expenditures increase in the winter months and are lower in the spring and early summer. As a result, the Company's accounts payable and accrued liabilities often peak at the end of the first quarter.

As disclosed in the annual financial statements, Cequence has periodically issued common shares and flow through common shares to fund a capital program that has been greater than the Company's cash flow. For the three months ended March 31, 2014, Cequence used funds flow from operations of $23,082, bank debt and proceeds from the issuance of the senior notes to finance its capital expenditures of $55,318.

The Company has two credit facilities with a syndicate of Canadian chartered banks. Credit facility A is a $110,000 (December 31, 2013 - $110,000) extendible revolving term credit facility by way of prime loans, U.S. Base Rate Loans, Banker's Acceptances and Libor Loans. Credit facility B is a $10,000 (December 31, 2013 - $10,000) operating facility by way of prime loans, U.S. Base Rate Loans, Banker's Acceptances and letters of credit. Prime loans and U.S. Base Rate Loans on these facilities bear interest at the bank prime rate or U.S. Base Rate, respectively, plus 1.0 percent to 2.5 percent on a sliding scale, depending on the Company's debt to adjusted EBITDA ratio (ranging from being less than or equal to 1.0:1.0 to greater than 2.5:1.0). Banker's Acceptances, Libor Loans and letters of credit on these facilities bear interest at the Banker's Acceptance rate, Libor rate or letter of credit rate, as applicable, plus 2.0 percent to 3.5 percent based on the same sliding scale as above. The credit facilities may be extended and revolve beyond the initial one-year period, if requested by the Company and accepted by the lenders. If the credit facilities do not continue to revolve, the facilities will convert to a 366-day non-revolving term loan facility.

Both credit facilities, and the amount available for draws under the facilities, are subject to periodic review by the bank and are secured by a general assignment of book debts and a $250,000 demand debenture with a first floating charge over all assets of the Company. As at March 31, 2014, the Company has drawn $26,747 under the extendible revolving term credit facility and $nil under the operating facility (December 31, 2013 – $22,763 and $nil for the revolving and operating facilities, respectively). The Company has covenants that require Consolidated Debt and Senior Debt to twelve month trailing earnings before interest, taxes and depletion and depreciation to be less than 4:0 to 1:0 and 3:0 to 1:0, respectively. Consolidated Debt is defined as the sum of the Company's period end balance of the credit facility and senior notes. Senior Debt is defined as the sum of Consolidated Debt less the period end balance of the senior notes. The Company was in compliance with the lender's covenants at March 31, 2014 and December 31, 2013. The effective annualized interest rate, including standby fees and commitment fees, for the three months ended March 31, 2014 was 6.44 percent (2013 – 4.16 percent). The next scheduled credit facility review is to take place on May 2014.

The oil and gas business can involve significant capital expenditures as assets are explored for and developed. In order to fund capital expenditures Cequence may adjust the capital structure through the issue of new common shares, new debt or replace existing debt, adjust capital expenditures and acquire or dispose of assets. Historically, a significant portion of the Company's capital expenditures have been discretionary and can be adjusted in response to fluctuation in commodity prices in order to manage the Company's debt levels. The Company has also hedged natural gas production to protect future cash flow.

Net Debt And Working Capital (Deficiency)

Net debt and working capital (deficiency) is calculated as cash and net working capital less commodity contract assets and liabilities, demand credit facilities, principal value of senior notes and excluding other liabilities, as follows:

$(000s)	**As at March 31, 2014**	As at December 31, 2013
Demand credit facilities	**(26,747)**	(22,763)
Senior notes – principal	**(60,000)**	(60,000)
Accounts payable and accrued liabilities	**(82,996)**	(51,692)
Accounts receivable	**22,782**	19,834
Deposits and prepaid expenses – current	**3,425**	3,188
Net debt and working capital (deficiency)	**(143,536)**	(111,433)

Contractual Obligations

	2014	2015	2016	2017	2018+	Total
Office leases	639	1,016	829	622	–	3,106
Pipeline transportation	1,325	1,609	–	–	–	2,934
Total	1,964	2,625	829	622	–	6,040

The pipeline transportation contract expires on November 30, 2015.

In 2011, the Company entered into a drilling service agreement whereby the Company made a deposit of $3,500 to obtain a right of first refusal on the use of two drilling rigs over the five years following the date that use of the rigs commences. The deposit is to be applied as the Company incurs costs related to the use of the drilling rigs and $1,949 has been drawn down at March 31, 2014. Cequence expects to reduce the deposit by $846 in the year ended March 31, 2014, which amount is included with deposits and prepaid expenses at March 31, 2014. The portion of the outstanding deposit expected to be drawn down in the period subsequent to March 31, 2015 of $705 is carried as a non-current asset at March 31, 2014.

Disclosure Controls and Internal Controls over Financial Reporting

The President and Chief Executive Officer and the Vice President, Finance and Chief Financial Officer are responsible for designing internal controls over financial reporting or causing them to be designed under their supervision in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS. The Company's President and Chief Executive Officer and Vice President, Finance and Chief Financial Officer have designed, or caused to be designed under their supervision, disclosure controls and procedures to provide reasonable assurance that information required to be disclosed by the Company in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time periods specified in the securities legislation and include controls and procedures designed to ensure that information required to be disclosed by an issuer in its annual filings, interim filings or other reports filed or submitted under securities legislation is accumulated and communicated to the Company's management, including its President and Chief Executive Officer and Vice President, Finance and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

The Committee of Sponsoring Organizations ("COSO") framework provides the basis for management's design of internal controls over financial reporting. Management and the Board work to mitigate the risk of a material misstatement in financial reporting; however, a control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met and it should not be expected that the disclosure and internal control procedures will prevent all errors or fraud.

As at March 31, 2014, the President and Chief Executive Officer and the Vice President, Finance and Chief Financial Officer have concluded, based on their evaluation of the design and operating effectiveness of the Company's disclosure controls and internal controls over financial reporting ("ICFR") that disclosure controls and ICFR are effective.

Quarterly Information

FINANCIAL

($ thousands except per share data)	2014 Q1	2013 Q4	2013 Q3	2013 Q2	2013 Q1	2012 Q4	2012 Q3	2012 Q2
Production revenue [1]	**41,095**	28,483	25,325	29,803	22,005	21,939	17,814	16,032
Royalties expense	**4,318**	1,769	2,305	2,452	2,089	1,546	992	118
Transportation expense	**1,587**	1,550	1,558	1,590	1,259	1,449	1,801	1,661
Operating costs	**7,731**	7,007	7,852	7,867	5,746	5,397	5,627	6,554
Comprehensive income (loss)	**512**	(827)	(517)	4,170	(5,439)	666	(3,824)	(6,579)
Per share – basic & diluted	**0.00**	(0.00)	(0.00)	0.02	(0.03)	(0.00)	(0.02)	(0.04)
Funds flow from operations [2]	**23,082**	14,855	10,973	14,831	10,652	11,603	10,803	4,563
Per share – basic & diluted	**0.11**	0.07	0.05	0.07	0.05	0.06	0.06	0.03
Capital expenditures, net	**58,547**	51,578	17,949	4,723	43,659	23,997	16,818	9,909
Net acquisitions (dispositions) [3]	**(3,229)**	(47)	(5)	(2,641)	18	644	20	(2,980)
Total capital expenditures	**55,318**	51,531	17,944	2,082	43,677	24,641	16,838	6,929

(1) Production revenue is presented gross of royalties and includes realized gain (loss) on commodity contracts.

(2) Funds flow from operations is calculated as cash flow from operating activities before adjustments for decommissioning liabilities expenditures, proceeds from the sale of commodity contracts and net changes in non-cash working capital.

(3) Represents the cash proceeds from the sale of assets and cash paid for the acquisition of assets, as applicable.

OPERATIONAL

	2014 Q1	2013 Q4	2013 Q3	2013 Q2	2013 Q1	2012 Q4	2012 Q3	2012 Q2
Production volumes								
Natural gas (Mcf/d)	**59,898**	53,433	52,848	58,153	46,306	47,125	46,641	45,042
Oil (bbls/d)	**992**	838	844	874	608	583	606	618
NGLs (bbls/d)	**638**	651	640	639	496	515	516	535
Total (boe/d)	**11,613**	10,394	10,292	11,205	8,822	8,951	8,895	8,660
Average selling price								
Natural gas ($/Mcf)	**5.28**	3.82	3.08	3.85	3.51	3.49	2.61	2.11
Oil ($/bbl)	**101.65**	87.37	97.42	90.56	91.90	86.78	83.38	79.92
NGLs ($/bbl)	**62.08**	49.54	47.26	38.23	52.84	45.83	41.89	59.54
Total ($/boe)	**39.32**	29.79	26.75	29.23	27.72	26.64	21.77	20.34
Operating netback ($/boe)								
Price	**39.32**	29.79	26.75	29.23	27.72	26.64	21.77	20.34
Royalties	**(4.13)**	(1.85)	(2.44)	(2.40)	(2.63)	(1.88)	(1.13)	(0.15)
Transportation	**(1.52)**	(1.62)	(1.65)	(1.56)	(1.59)	(1.76)	(2.20)	(2.11)
Operating costs	**(7.40)**	(7.33)	(8.29)	(7.71)	(7.24)	(6.55)	(6.88)	(8.32)
Operating netback	**26.27**	18.99	14.37	17.56	16.26	16.45	11.56	9.76

Funds flow from operations is impacted from quarter to quarter primarily due to changes in productions volumes, realized average selling prices, royalties, operating expenses, transportation costs and G&A expense. The Company's production volumes are 86 percent natural gas and fluctuations in natural gas prices have the greatest impact on the Company's revenue and funds flow from operations.

The Company's quarterly net comprehensive income (loss) is affected by fluctuations in non-cash charges, in particular, depletion, depreciation and impairment expense, accretion of decommissioning obligations, gains/losses on derivative financial instruments, share based payments and other expense (income). During the twelve months ended December 31, 2012, the Company recorded impairment expense of $26,894 compared to $2,164 in the comparable period in 2013. The 2012 impairments were incurred on the Company's Northeast British Columbia and Peace River Arch CGUs. Impairments recognized were mainly the result of declining benchmark natural gas prices and minimal capital expenditures being incurred in the Northeast British Columbia and Peace River Arch CGUs as substantially all of the Company's capital expenditures over the past two years have been allocated to the Deep Basin CGU. These impairments cause significant reductions and increased volatility in the Company's net comprehensive income (loss).

Please refer to the results of operations and other sections of this MD&A and the Company's previously issued MD&A for detailed discussions on variances between reporting periods and changes in prior periods.

Outlook Information

On October 3, 2013 Cequence provided the following guidance:

	2013 Actuals	2014 Guidance
Average production, BOE/d [1]	10,183	13,500 - 14,000
Average production per share [2]	49	65
Exit production, BOE/d	12,000	15,000
Funds flow from operations ($)[3]	$51 million	$85 million
Funds flow from operations per share	$0.25	$0.3
Capital expenditures ($)	$115 million	$120 million
Wells drilled	15(12)	16(14)
Operating costs ($ per boe)	$7.66	$6.85
Royalties (% revenue)	8	8
Crude – WTI (US$/bbl)	$98.01	$95.75
Natural gas – AECO (Cdn$/GJ)	$3.01	$3.50
December 31, net debt and working capital deficiency ($) [4]	$111 million	$145 million
Basic shares outstanding	208 million	211 million

(1) Average production estimates on a per BOE basis are comprised of 85% natural gas and 15% oil and natural gas liquids.

(2) Calculated as average production per million shares.

(3) Funds flow from operations is calculated as cash flow from operating activities before adjustments for decommissioning liabilities expenditures and net changes in non-cash working capital.

(4) Net debt and working capital (deficiency) is calculated as cash and net working capital less commodity contract assets and liabilities, demand credit facilities and the aggregate principal amount of the senior notes and excluding other liabilities.

Capital expenditures for 2014 are expected to be funded from funds flow from operations, available bank lines and proceeds from the 2013 issuance of senior notes. The Company closely monitors fluctuations in natural gas prices and will adjust the 2014 budget if facts and circumstances require.

Accounting Policies Adopted

On January 1, 2014, Cequence adopted the following standards and amendments, as issued by the IASB:

- IAS 36, "Impairment of Assets". The amendments reduce the circumstances in which the recoverable amount of CGUs is required to be disclosed and clarifies the disclosures required when an impairment loss has been recognized or reversed in the period. The adoption of this standard did not have a material impact on the Company's consolidated financial statements.
- IFRS Interpretations Committee ("IFRIC") 21 "Levies". IFRIC 21 clarifies that an entity recognizes a liability for a levy when the activity that triggers payment, as identified in the relevant legislation, occurs. The adoption of this standard did not have a material impact on the Company's consolidated financial statements.

Forward-looking Statements

Certain statements contained within this MD&A constitute forward-looking statements. These statements relate to future events or the Company's future performance. All statements other than statements of historical fact may be forward-looking statements. Forward-looking statements are often, but not always, identified by the use of words such as "seek", "anticipate", "budget", "plan", "continue", "estimate", "expect", "forecast", "may", "will", "project", "predict", "potential", "targeting", "intend", "could", "might", "should", "believe", and similar expressions. Forward-looking statements in this MD&A include, but are not limited to, statements with respect to: the potential impact of implementation of the Alberta Royalty Framework on Cequence's condition and projected 2014 capital investments; projections with respect to growth of natural gas production; the projected impact of land access and regulatory issues; projections relating to the volatility of crude oil and natural gas prices in 2014 and beyond and reasons therefore; the Company's projected capital investment levels for 2014 and the source of funding therefore; the effect of the Company's risk management program, including the impact of derivative financial instruments; the Company's defence of lawsuits; the impact of the climate change initiatives on operating costs; the impact of Western Canada pipeline constraints. Readers are cautioned not to place undue reliance on forward-looking statements, as there can be no assurance that the plans, intentions or expectations upon which they are based will occur.

By their nature, forward-looking statements involve numerous assumptions, known and unknown risks and uncertainties, both general and specific, that contribute to the possibility that the predictions, forecasts, projections and other forward-looking statements will not occur, which may cause the Company's actual performance and financial results in future periods to differ materially from any estimates or projections of future performance or results expressed or implied by such forward-looking statements. These assumptions, risks and uncertainties include, among other things: volatility of and assumptions regarding oil and natural gas prices; assumptions based upon Cequence's current guidance; fluctuations in currency and interest rates; product supply and demand; market competition; risks inherent in the Company's marketing operations, including credit risks; imprecision of reserves estimates and estimates of recoverable quantities of oil, natural gas and liquids from resource plays and other sources not currently classified as proved; the Company's ability to replace and expand oil and gas reserves; the Company's ability to generate sufficient cash flow from operations to meet its current and future obligations; the Company's ability to access external sources of debt and equity capital; the timing and cost of well and pipeline constructions; the Company's ability to secure adequate product transportation; changes in royalty, tax, environmental and other laws or regulations or the interpretations of such laws or regulations; risks associated with existing and potential future lawsuits and regulatory actions made against the Company; and other risks and uncertainties described from time to time in the reports and filings made with securities regulatory authorities by Cequence. Statements relating to "reserves" are deemed to be forward-looking statements, as they involve the implied assessment, based on certain estimates and assumptions that the resources and reserves described can be profitably produced in the future.

The forward looking statements contained herein concerning production, sales prices, operating expenses and capital spending are based on Cequence's 2014 capital program. The material assumptions supporting the 2014 capital program are provided in the table above under the heading "Outlook Information".

Financial outlook information contained in this MD&A about prospective results of operations, financial position or cash flows is based on assumptions about future events, including economic conditions and proposed courses of action, based on management's assessment of the relevant information currently available. The purpose of such financial outlook is to enrich this MD&A. Readers are cautioned that such financial outlook information contained in this MD&A should not be used for purposes other than for which it is disclosed herein.

Although Cequence believes that the expectations represented by such forward-looking statements are reasonable, there can be no assurance that such expectations will prove to be correct. Readers are cautioned that the foregoing list of important factors is not exhaustive. Furthermore, the forward-looking statements contained in this MD&A are made as of the date of this MD&A and, except as required by law, Cequence does not undertake any obligation to update publicly or to revise any of the included forward-looking statements, whether as a result of new information, future events or otherwise. The forward-looking statements contained in this MD&A are expressly qualified by this cautionary statement.

Consolidated Balance Sheets

(Unaudited) (Expressed in thousands of Canadian dollars)

	March 31, 2014	December 31, 2013
	$	$
ASSETS		
CURRENT		
Accounts receivable	**22,782**	19,834
Deposits and prepaid expenses	**3,425**	3,188
	26,207	23,022
Property and equipment (Note 3)	**583,038**	537,511
Deposits and prepaid expenses	**705**	1,047
Deferred income taxes	**31,627**	36,094
	641,577	597,674
LIABILITIES		
CURRENT		
Demand credit facilities (Note 4)	**26,747**	22,763
Accounts payable and accrued liabilities	**82,996**	51,692
Share based payment liability (Note 11)	**352**	111
Commodity contracts (Note 14)	**9,470**	2,880
Other liabilities (Note 9)	**318**	317
	119,883	77,763
Senior notes (Note 5)	**56,774**	56,637
Commodity contracts (Note 14)	**107**	76
Provisions (Note 9)	**27,332**	26,828
	204,096	161,304
CONTINGENCIES AND COMMITMENTS (Note 13)		
SHAREHOLDERS' EQUITY		
Share capital (Note 10)	**624,332**	624,332
Warrants (Note 10)	**1,300**	1,300
Contributed surplus	**26,784**	26,185
Deficit	**(214,935)**	(215,447)
	437,481	436,370
	641,577	597,674

APPROVED BY THE BOARD

[signed] "Donald Archibald"
Donald Archibald, Director

[signed] "Brian Felesky"
Brian Felesky, Director

Consolidated Statements of Comprehensive Income (Loss)

(Unaudited) (Expressed in thousands of Canadian dollars except per share amounts)

	Three months ended March 31,	
	2014	2013
	$	$
REVENUE		
Production revenue (Note 6)	**41,975**	19,821
Loss on derivative financial instruments (Note 14)	**(11,819)**	(3,233)
	30,156	16,558
EXPENSES		
Depletion and depreciation (Note 3)	**12,442**	8,930
General and administrative	**2,451**	1,600
Finance costs (Note 8)	**2,216**	582
Operating costs	**7,731**	5,746
Share based payment (Note 11)	**841**	1,134
Transportation	**1,587**	1,259
Other expense (income) (Note 7)	**(2,091)**	195
	25,177	19,446
INCOME (LOSS) BEFORE INCOME TAXES	**4,979**	(2,858)
INCOME TAXES	**4,467**	2,581
NET INCOME (LOSS) AND COMPREHENSIVE INCOME (LOSS)	**512**	(5,439)
Income (loss) per share, basic and diluted (Note 12)	**$ 0.00**	$ (0.03)

Consolidated Statements of Changes in Equity

(Unaudited) (Expressed in thousands of Canadian dollars)

	Three months ended March 31, 2014	2013
	$	$
SHARE CAPITAL		
Common Shares (Note 10)		
Balance, beginning of period	**624,332**	606,703
Share issue costs, net of tax of $nil (2013 – ($23))	**–**	64
Balance, end of period	**624,332**	606,767
Warrants (Note 10)		
Balance, beginning of period	**1,300**	–
Balance, end of period	**1,300**	–
CONTRIBUTED SURPLUS		
Balance, beginning of period	**26,185**	22,556
Share based payment expense (Note 11)	**599**	1,134
Balance, end of period	**26,784**	23,690
DEFICIT		
Balance, beginning of period	**(215,447)**	(212,834)
Comprehensive income (loss)	**512**	(5,439)
Balance, end of period	**(214,935)**	(218,273)
TOTAL EQUITY	**437,481**	412,184

Consolidated Statements of Cash Flows

(Unaudited) (Expressed in thousands of Canadian dollars)

	Three months ended March 31, 2014	2013
	$	$
CASH FLOWS RELATED TO THE FOLLOWING ACTIVITIES:		
OPERATING		
Net income (loss)	**512**	(5,439)
Adjustments for non-cash items:		
Depletion and depreciation	**12,442**	8,930
Finance costs related to provisions (Note 8)	**203**	198
Share based payment (Note 11)	**841**	1,134
Amortization of transaction costs on senior notes (Note 8)	**77**	–
Accretion on senior notes (Note 8)	**60**	–
Unrealized loss on derivative financial instruments (Note 14)	**6,621**	3,328
Costs related to onerous contracts (Note 9)	**(80)**	(80)
Gain on sale of assets (Note 3)	**(2,061)**	–
Deferred income tax expense (recovery)	**4,467**	2,581
Decommissioning liabilities expenditures (Note 9)	**(208)**	(74)
Net change in non-cash working capital (Note 15)	**5,931**	4,532
	28,805	15,110
INVESTING		
Property and equipment and exploration and evaluation assets expenditures (Note 3)	**(58,547)**	(43,659)
Property acquisitions (Note 3)	**(2,405)**	(18)
Proceeds from sale of assets (Note 3)	**5,634**	–
Net change in non-cash working capital (Note 15)	**22,631**	10,638
	(32,687)	(33,039)
FINANCING		
Proceeds from demand credit facilities (Note 4)	**3,984**	17,842
Share issue costs	**–**	87
Net change in non-cash working capital (Note 15)	**(102)**	–
	3,882	17,929
NET CHANGE IN CASH	**–**	–
CASH, BEGINNING OF PERIOD	**–**	–
CASH, END OF PERIOD	**–**	–
SUPPLEMENTARY INFORMATION		
Income taxes paid	**–**	–
Interest paid	**1,978**	388

Notes to the Condensed Consolidated Financial Statements

Three months ended March 31, 2014 and 2013
(All figures expressed in thousands except per share amounts unless otherwise noted)

1. Nature and Description of the Company

Cequence Energy Ltd. (the "Company" or "Cequence") is incorporated under the laws of Alberta with common shares that are widely held and listed on the Toronto Stock Exchange. Cequence is engaged in the acquisition, exploration and production of petroleum and natural gas reserves in Western Canada. The registered office of the Company is located at Suite 3100, 525 - 8th Ave. SW, Calgary, Alberta, T2P 1G1.

These interim condensed consolidated financial statements ("consolidated financial statements") include all assets, liabilities, revenues and expenses of Cequence and its wholly-owned subsidiary, 1175043 Alberta Ltd.

2. Significant Accounting Policies

STATEMENT OF COMPLIANCE AND AUTHORIZATION

These consolidated financial statements have been prepared in accordance with IAS 34, "Interim Financial Reporting" ("IAS 34"), as issued by the International Accounting Standards Board ("IASB"). Accordingly, certain information or footnote disclosure normally included in the annual consolidated financial statements prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the IASB, have been condensed or omitted.

These consolidated financial statements should be read in conjunction with the Company's consolidated financial statements for the year ended December 31, 2013.

The consolidated financial statements were authorized for issue by the Company's Board of Directors on May 13, 2014.

BASIS OF PRESENTATION

Except as noted below, the consolidated financial statements have been prepared using the same accounting policies and methods as those used in the consolidated financial statements for the year ended December 31, 2013. The consolidated financial statements have been presented in Canadian dollars, which is also the Company's functional currency, rounded to the nearest thousand, unless otherwise indicated.

ACCOUNTING PRONOUNCEMENTS

On January 1, 2014, Cequence adopted the following standards and amendments, as issued by the IASB:

- IAS 36, "Impairment of Assets". The amendments reduce the circumstances in which the recoverable amount of CGUs is required to be disclosed and clarifies the disclosures required when an impairment loss has been recognized or reversed in the period. The adoption of these amendments did not have a material impact on the Company's consolidated financial statements.

- IFRS Interpretations Committee ("IFRIC") 21 "Levies". IFRIC 21 clarifies that an entity recognizes a liability for a levy when the activity that triggers payment, as identified in the relevant legislation, occurs. The adoption of this standard did not have a material impact on the Company's consolidated financial statements.

3. Property and Equipment and Exploration and Evaluation Assets

	Property and Equipment	E&E Assets	Total
Cost:			
Balance at December 31, 2012	636,356	13,829	650,185
Additions	103,834	14,075	117,909
Transferred to property and equipment	27,904	(27,904)	–
Decommissioning obligation additions and change in estimates	(4,632)	–	(4,632)
Acquisitions	23,540	–	23,540
Disposals	(22,019)	–	(22,019)
Balance at December 31, 2013	764,983	–	764,983
Additions	**58,547**	**–**	**58,547**
Decommissioning obligation additions and change in estimates	**1,041**	**–**	**1,041**
Acquisitions	**2,405**	**–**	**2,405**
Disposals	**(19,941)**	**–**	**(19,941)**
Balance at March 31, 2014	**807,035**	**–**	**807,035**
Depletion, depreciation and impairment:			
Balance at December 31, 2012	(197,297)	–	(197,297)
Depletion and depreciation	(40,932)	–	(40,932)
Impairment loss	(2,164)	–	(2,164)
Disposals	12,921	–	12,921
Balance at December 31, 2013	(227,472)	–	(227,472)
Depletion and depreciation	**(12,442)**	**–**	**(12,442)**
Disposals	**15,917**	**–**	**15,917**
Balance at March 31, 2014	**(223,997)**	**–**	**(223,997)**
Carrying amounts:			
At December 31, 2013	537,511	–	537,511
At March 31, 2014	**583,038**	**–**	**583,038**

Costs subject to depletion include $780,307 of estimated future capital costs (December 31, 2013 – $785,249).

The Company's credit facilities are secured by a demand debenture with a first floating charge over all assets of the Company (see note 4).

IMPAIRMENT

The Company reviewed each CGU comprising its property and equipment at March 31, 2014 for indicators of impairment and determined that there were none.

SALE OF ASSETS

During the three months ended March 31, 2014, the Company completed the sales of certain oil and gas properties for total cash consideration of $5,634 (2013 - $nil), subject to final adjustments. The sales resulted in a gain recognized in comprehensive income (loss) of $2,061 (2013 - $nil).

4. Demand Credit Facilities

The Company has credit facilities totalling $120,000 with a syndicate of Canadian chartered banks. Credit facility A is a $110,000 (December 31, 2013 - $110,000) extendible revolving term credit facility by way of prime loans, U.S. Base Rate Loans, Banker's Acceptances and Libor Loans. Credit facility B is a $10,000 (December 31, 2013 - $10,000) operating facility by way of prime loans, U.S. Base Rate Loans, Banker's Acceptances and letters of credit. As at March 31, 2014, the Company has drawn $26,747 under the extendible revolving term credit facility and $nil under the operating facility (December 31, 2013 – $22,763 and $nil for the revolving and operating facilities, respectively). The Company has covenants that require Consolidated Debt and Senior Debt to twelve month trailing earnings before interest, taxes and depletion and depreciation to be less than 4:0 to 1:0 and 3:0 to 1:0, respectively. Consolidated Debt is defined as the sum of the Company's period end balance of the credit facility and senior notes. Senior Debt is defined as the sum of Consolidated Debt less the period end balance of the senior notes. The Company was in compliance with the lender's covenants at March 31, 2014. The next scheduled review is to take place in May 2014.

5. Senior Notes

	March 31, 2014	December 31, 2013
Senior notes	**58,477**	58,477
Less transaction costs	**(1,703)**	(1,840)
Total senior notes	**56,774**	56,637

On October 3, 2013, Cequence issued $60,000 of unsecured five year term notes ("senior notes") at par with a 9% coupon per annum for gross proceeds net of transaction costs of $57,974. The senior notes are unsecured and are subordinate to Cequence's credit facilities. The senior notes were issued pursuant to a trust indenture with a Canadian trust company, which provides for an additional $60,000 of unsecured senior notes at a future date, subject to approval of both the lender and the Company on terms to be confirmed at the time of issuance.

The senior notes are subject to the same financial covenants as the Company credit facilities as well as other non-financial covenants and restrictive covenants, including restrictions over asset sales, restricted payments and the incurrence of additional indebtedness. The Company was in compliance with the senior notes covenants at March 31, 2014 and December 31, 2013.

6. Production Revenue

	Three months ended March 31,	
	2014	2013
Sales of oil and natural gas	**46,293**	21,910
Royalties	**(4,318)**	(2,089)
Total production revenue	**41,975**	19,821

7. Other Expense (Income)

	Three months ended March 31,	
	2014	2013
Gain on sale of property and equipment	**(2,061)**	–
Transaction costs	**–**	225
Other	**(30)**	(30)
Total other expense (income)	**(2,091)**	195

8. Finance Costs

	Three months ended March 31,	
	2014	2013
Interest expense on demand credit facilities (including stand-by fees and commitment fees of $225 (2013 - $80))	**544**	384
Interest expense on senior notes	**1,332**	–
Amortization of transaction costs	**77**	–
Accretion expense on senior notes	**60**	–
Accretion expense on provisions	**203**	198
Total finance costs	**2,216**	582

9. Provisions

DECOMMISSIONING LIABILITIES

The following table summarizes the changes in decommissioning liabilities for the periods ending March 31, 2014 and December 31, 2013:

	2014	2013
Balance, beginning of period	**26,643**	32,564
Property acquisitions	**–**	285
Property dispositions (Note 3)	**(450)**	(1,729)
Accretion expense	**201**	819
Liabilities incurred	**544**	1,120
Abandonment costs incurred	**(208)**	(619)
Revisions in estimated cash flows	**(788)**	(973)
Revisions due to change in discount rates	**1,285**	(4,824)
Balance, end of period	**27,227**	26,643

The Company's decommissioning liabilities result from its ownership in oil and natural gas assets including well sites, facilities and gathering systems. The total estimated, undiscounted cash flows, inflated at 2 percent, required to settle the obligations are $54,968 (December 31, 2013 - $55,632). These cash flows have been discounted using a risk-free interest rate of 2.96 percent (December 31, 2013 – 3.20 percent) based on Government of Canada long-term benchmark bonds. The Company expects these obligations to be settled in approximately 1 to 50 years (December 31, 2013 – 1 to 50 years). As at March 31, 2014, no funds have been set aside to settle these liabilities.

ONEROUS CONTRACTS

As at March 31, 2014, the Company recognized a provision related to an onerous lease contract of $423 (December 31, 2013 - $502). Cequence expects to reduce the provision by $318 in the twelve months ended March 31, 2015, which amount is included with other liabilities in the consolidated balance sheet. The portion of the provision expected to be realized in the period subsequent to March 31, 2015 of $105 is carried with provisions as a non-current liability in the consolidated balance sheet as at March 31, 2014.

10. Share Capital

Cequence has an unlimited number of common voting shares and common non-voting shares with no par value authorized.

	Three months ended March 31, 2014		Year ended December 31, 2013	
Issued common voting shares	**Number**	**Stated Value**	Number	Stated Value
	(000s)	**$**	(000s)	$
Balance, beginning of period	**210,918**	**624,332**	200,610	606,703
Common shares	**–**	**–**	8	15
Common shares issued on property acquisition	**–**	**–**	10,300	17,510
	210,918	**624,332**	210,918	624,228
Share issue costs, net of taxes of ($nil) (2013 – ($35))	**–**	**–**	–	104
Balance, end of period	**210,918**	**624,332**	210,918	624,332
Warrants				
Balance, beginning of period	**3,000**	**1,300**	–	–
Granted on issuance of senior notes, net of tax of $nil (2013 – $183) (Note 5)	**–**	**–**	3,000	1,339
Transaction costs, net of tax of $nil (2013 – $13)	–	–	–	(39)
Balance, end of period	**3,000**	**1,300**	3,000	1,300

On October 3, 2013, the Company granted to the lender of the senior notes 3.0 million warrants at an exercise price of $2.03 to purchase Cequence common shares (see note 5).

11. Share Based Payment Plans

STOCK OPTIONS

The Company has a stock option plan for directors, officers, employees and consultants of the Company and its subsidiaries. The number of common shares granted with respect to options may not exceed a rolling maximum of 10 percent of the Company's outstanding common shares. Options typically vest over a three year period, expire five years from the date of grant and are settled by issuing shares of the Company.

A summary of the status of the Company's stock option plan and changes during the three months ended March 31, 2014 and the year ended December 31, 2013 is as follows:

		2014		2013
	Number of options	**Weighted average exercise price**	Number of options	Weighted Average exercise price
	(000s)	**$**	(000s)	$
Outstanding, beginning of period	**18,617**	**2.15**	17,289	2.19
Granted	**20**	**1.70**	1,780	1.70
Forfeited	**–**	**–**	(444)	1.92
Exercised	**–**	**–**	(8)	1.34
Outstanding, end of period	**18,637**	**2.15**	18,617	2.15

The following table summarizes information about stock options outstanding at March 31, 2014:

			Options outstanding		Options exercisable
Range of Exercise Price	Weighted average exercise price	Number of options outstanding	Weighed average contractual life remaining	Number of options	Weighed average exercise price
$	$	(000s)	(years)	(000s)	$
1.24 – 1.99	1.72	14,613	2.4	9,711	1.86
2.96 – 3.94	3.69	4,024	2.3	2,686	3.69
	2.15	18,637	2.4	12,397	2.26

During the three months ended March 31, 2014, $599 (2013 - $1,134) in share based payment expense related to equity-settled stock options has been recognized in comprehensive income (loss).

RESTRICTED SHARE UNITS

In 2013, the Company implemented an restricted share unit ("RSU") plan for directors, officers, employees and consultants of the Company and its subsidiaries. An RSU is a conditional grant to receive a Cequence common share, or the cash equivalent, as determined by the Company, upon vesting of the RSUs and in accordance with the terms of the RSU plan and grant agreement. The value of one RSU is notionally equivalent to one Cequence common share. RSUs vest over a three year period and management plans to settle the RSUs in cash on the respective vesting date.

A summary of the status of the Company's RSU plan and changes during the three months ended March 31, 2014 and the year ended December 31, 2013 is as follows:

Number of RSUs (000s)	**2014**	2013
Outstanding, beginning of period	**561**	–
Granted	**20**	561
Outstanding, end of period	**581**	561

During the three months ended March 31, 2014, the Company recognized $242 (2013 - $nil) in share based payment expense related to the cash-settled RSUs in comprehensive income (loss).

12. Income (Loss) Per Share

Income (loss) per share has been calculated based on the weighted average number of common shares outstanding during the year. The Company has excluded 11,987 stock options and 3,000 warrants in the calculation of diluted shares outstanding for the three months ended March 31, 2014 (2013 – 17,249 stock options) as their inclusion would be anti-dilutive. The following table reconciles the denominators used for the basic and diluted income (loss) per share calculations.

	Three months ended March 31,	
	2014	2013
Basic weighted average shares	**210,918**	200,610
Effect of dilutive instruments	**2,046**	–
Diluted weighted average shares	**212,964**	200,610

13. Contingencies and Commitments

	2014	2015	2016	2017	2018+	Total
Office leases	639	1,016	829	622	–	3,106
Pipeline transportation	1,325	1,609	–	–	–	2,934
Total	1,964	2,625	829	622	–	6,040

14. Financial Instruments and Risk Management

The Company's financial instruments, including derivative financial instruments, recognized in the consolidated balance sheets consist of accounts receivable, deposits, commodity contracts, demand credit facilities, senior notes and accounts payable and accrued liabilities.

The Company's accounts receivable, deposits, demand credit facilities and accounts payable and accrued liabilities approximate their carrying values due to their short terms to maturity and the floating interest rate on the Company's debt. The senior notes bear interest at rates available to Cequence and accordingly the fair value approximates the carrying value excluding deferred financing costs.

The Company's fair value hierarchy for those assets and liabilities measured at fair value comprises commodity contracts which are measured at level 2 under the Company's fair value hierarchy as of March 31, 2014. The fair value of commodity contracts is determined by discounting the remaining contracted petroleum and natural gas volumes by the difference between the contracted price and published forward price curves as at the balance sheet date.

The nature of these financial instruments and the Company's operations expose the Company to market risk, credit risk and liquidity risk. The Company manages its exposure to these risks by operating in a manner that minimizes these risks. Senior management employs risk management strategies and policies to ensure that any exposure to risk is in compliance with the Company's business objectives and risk tolerance levels. The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Board has established policies in setting risk limits and controls and monitors these risks in relation to market conditions.

COMMODITY PRICE RISK

The nature of the Company's operations results in exposure to fluctuations in commodity prices. Management continuously monitors commodity prices and initiates instruments to manage exposure to these risks when it deems appropriate. As a means of managing commodity price volatility, the Company enters into various derivative financial instrument agreements and physical contracts. The fair values of the derivative financial instruments are based on mark-to-market assessments and estimates of fair value and are recorded on the consolidated balance sheet as either an asset or liability with the change in fair value recognized in comprehensive income (loss).

The following information presents all outstanding positions by year for commodity derivative financial instruments contracts at March 31, 2014:

Term	Product	Type	Volume	Price	Basis
2014					
January 1, 2014 to September 30, 2014	Gas	Swap	2,500 gj/day	$3.51	AECO
January 1, 2014 to December 31, 2014	Gas	Swap	2,500 gj/day	$3.42	AECO
January 1, 2014 to December 31, 2014	Gas	Swap	2,500 gj/day	$3.53	AECO
January 1, 2014 to December 31, 2014	Gas	Swap	2,500 gj/day	$3.70	AECO
January 1, 2014 to December 31, 2014	Gas	Swap	2,500 gj/day	$3.47	AECO
January 1, 2014 to December 31, 2014	Gas	Swap	2,500 gj/day	$3.40	AECO
January 1, 2014 to December 31, 2014	Gas	Swap	2,500 gj/day	$3.45	AECO
January 1, 2014 to October 31, 2014	Gas	Swap	2,500 gj/day	$3.46	AECO
January 1, 2014 to December 31, 2014	Gas	Swap	2,500 gj/day	$3.15	AECO
January 1, 2014 to December 31, 2014	Gas	Swap	2,500 gj/day	$3.25	AECO
January 1, 2014 to December 31, 2014	Gas	Swap	2,500 gj/day	$3.41	AECO
January 1, 2014 to December 31, 2014	Gas	Swap	2,500 gj/day	$3.47	AECO
November 1, 2014 to December 31, 2014	Gas	Swap	2,500 gj/day	$3.70	AECO
November 1, 2014 to December 31, 2014	Gas	Swap	2,500 gj/day	$4.23	AECO
2015					
January 1, 2015 to March 31, 2015	Gas	Swap	2,500 gj/day	$3.70	AECO
January 1, 2015 to March 31, 2015	Gas	Swap	2,500 gj/day	$4.23	AECO
January 1, 2015 to March 31, 2015	Gas	Swap	5,000 gj/day	$3.76	AECO
January 1, 2015 to December 31, 2015	Gas	Swap	2,500 gj/day	$3.58	AECO
January 1, 2015 to December 31, 2015	Gas	Swap	5,000 gj/day	$3.69	AECO
January 1, 2015 to December 31, 2015	Gas	Swap	2,500 gj/day	$3.95	AECO

For the three months ended March 31, 2014, realized loss from commodity derivative contracts recognized in comprehensive income (loss) was $5,198 (2013 - $95 gain).

The fair value of the commodity contracts outstanding at March 31, 2014 was a current liability of $9,470 and non-current liability of $107 (December 31, 2013 – current liability $2,880 and non-current liability of $76).

For the three months ended March 31, 2014, the Company recorded an unrealized loss of $6,621 from derivative commodity contracts (2013 - $3,328).

As at March 31, 2014, an increase in gas price of $0.50/gj results in a decrease in the fair value of the commodity contracts of $6,353 ($4,765 after tax) and a commensurate increase to comprehensive income (loss).

CREDIT RISK

Credit risk is the risk of financial loss to the Company if a counterparty to a financial instrument fails to meet its contractual obligation. The Company is exposed to credit risk with respect to its accounts receivable and cash.

The majority of the Company's accounts receivable are due from joint venture partners in the oil and gas industry and from marketers of the Company's petroleum and natural gas production. The Company mitigates its credit risk by entering into contracts with established counterparties that have strong credit ratings and reviewing its exposure to individual counterparties on a regular basis.

As at March 31, 2014, the accounts receivable balance was $22,782 of which $1,628 was past due. The Company considers all amounts greater than 90 days past due. These past due accounts are considered to be collectible, except as provided in the allowance for doubtful accounts. When determining whether past due accounts are uncollectible, the Company factors in the past credit history of the counterparties. The following table provides an aging analysis of the Company's accounts receivables:

Current	30-60 days	60-90 days	90+days	Total
20,219	439	496	1,628	22,782

15. Changes in Non-Cash Working Capital

	Three months ended March 31,	
	2014	2013
Accounts receivable	**(2,948)**	1,247
Deposits and prepaid expenses	**104**	(60)
Accounts payable and accrued liabilities	**31,304**	13,983
Net change in non-cash working capital	**28,460**	15,170
Allocated to:		
Operating activities	**5,931**	4,532
Investing activities	**22,631**	10,638
Financing activities	**(102)**	–
	28,460	15,170

Corporate Information

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Howard Crone, P.Eng
Executive Vice President & COO

David Gillis, CA
Vice President, Finance & CFO

James R. Jackson, P.Eng, CFA
Vice President, Engineering

David P. Robinson
Vice President, Geology

Christopher C. Soby
Vice President, Land

Stephen R. Stretch
Vice President, Geophysics

Mike Stewart
Vice President, Operations

Erin Thorson, CMA
Controller

Directors

Don Archibald
Chairman

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