2023 Q2 INTERIM REPORT

FINANCIAL HIGHLIGHTS

Canadian dollars in 000's except for otherwise noted

	Three months ended June 30, 2023	Three months ended June 30, 2022	Six months ended June 30, 2023	Six months ended June 30, 2022
Revenues	$ 115,058	$ 27,652	$ 242,723	$ 62,037
Gross margin %	14%	2%	14%	10%
Adjusted gross margin % (1)	23%	19%	22%	24%
Adjusted EBITDAS (1)	$ 18,222	$ 2,836	$ 33,409	$ 9,749
Adjusted EBITDAS margin % (1)	16%	10%	14%	16%
Cash flow - operating activities	$ 11,232	$ 4,511	$ 35,148	$ 2,753
Free cash flow (deficit) (1)	$ 4,984	$ (12,008)	$ 4,285	$ (9,197)
Net income (loss)	$ 2,416	$ (2,824)	$ 3,210	$ (581)
Per share - basic and diluted	$ 0.01	$ (0.02)	$ 0.01	$ (0.01)
Weighted average shares outstanding:				
Basic (000s)	238,394	129,200	231,516	110,353
Diluted (000s)	240,653	131,898	238,563	112,969

As at	June 30, 2023	December 31, 2022
Working capital, excluding current portion of loans and borrowings	$ 62,048	$ 60,447
Total assets	$ 344,491	$ 353,990
Loans and borrowings	$ 60,080	$ 80,535
Shareholders' equity	$ 169,914	$ 153,897

(1) Refer to the "Non-GAAP Measures" section in this MD&A.

MANAGEMENT'S DISCUSSION & ANALYSIS

Cathedral Energy Services Ltd. (the "Company" or "Cathedral") is a publicly traded company listed on the Toronto Stock Exchange ("TSX") under the symbol "CET". The Company is primarily involved and engaged in the business of providing directional drilling services to oil and natural gas companies in Western Canada and the United States ("U.S.").

This Management's Discussion & Analysis ("MD&A") for the three and six months ended June 30, 2023 is dated August 10, 2023 and should be read in conjunction with the Company's unaudited condensed consolidated financial statements for the three and six months ended June 30, 2023, the Company's MD&A and audited consolidated financial statements for the year ended December 31, 2022, and Annual Information Form for the year ended December 31, 2022 dated April 14, 2023. These documents are filed on SEDAR+ (www.sedarplus.ca) and appear on the Company's website (www.cathedralenergyservices.com). Canadian dollar amounts are in '000's except for otherwise noted.

Cathedral uses certain performance measures throughout this MD&A that are not defined under International Financial Reporting Standards ("IFRS"). See the 'Non-GAAP Measures' section in this MD&A.

2023 Q2 KEY TAKEAWAYS

The Company achieved the following 2023 Q2 results and highlights:

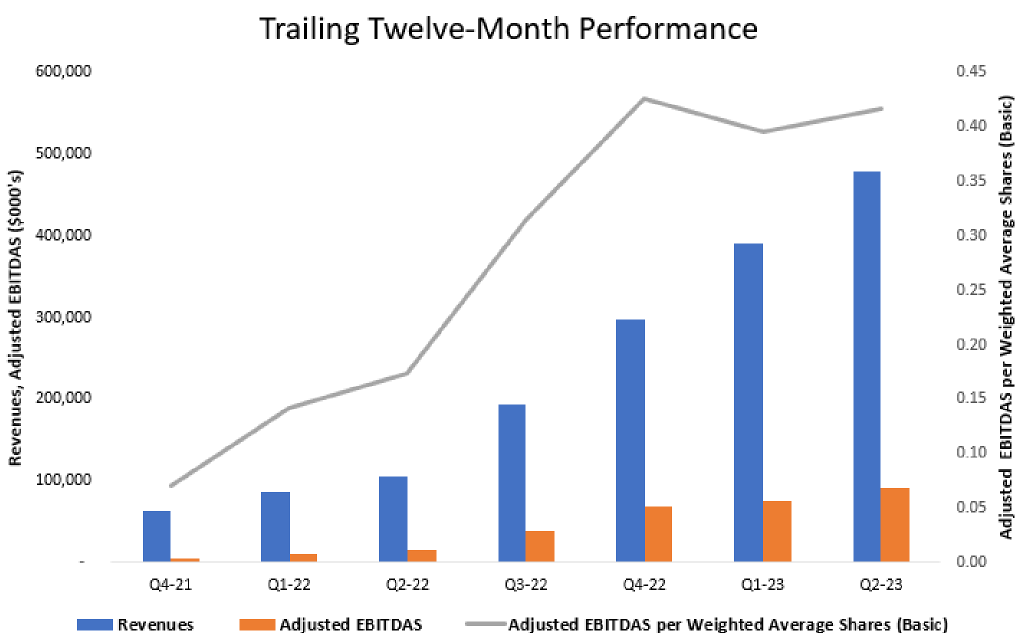
- Revenue of $115,058 in 2023 Q2 is the highest for any second quarter in the Company's history and represents an increase of 316%, compared to $27,652 in 2022 Q2.

- Adjusted EBITDAS of $18,222 in 2023 Q2 is also a new record for any second quarter in the Company's history and represents an increase of 543%, compared to $2,836 in 2022 Q2.
- Net income of $2,416, compared to a net loss of $2,824 in 2022 Q2.
- Despite the seasonally slower second quarter in Canada, the Company generated free cash flow of $4,984, a testament to size and scale and a business model with lower capital intensity.
- Canadian directional drilling market share averaged 20.1% in 2023 Q2, an increase from 15.4% in 2022 Q2.
- U.S. directional drilling market share averaged 8.7% in 2023 Q2.
- Loans and borrowings less cash of $39,957 as at June 30, 2023, compared to $69,360 as at December 31, 2022.
- The Company received $16,012 in total cumulative proceeds related to the April 2022 bought deal offering warrants, which accounted for 99.7% of eligible warrants. The Company also received warrants proceeds of $138 and $1,200 relating to the February 2021 private placement warrants and the Precision Drilling acquisition, respectively, as of the date of this MD&A.
- Cathedral paid off the $13,000 balance owed on its Syndicated Operating Facility.
- Subsequent to June 30, 2023, the Company acquired Rime Downhole Technologies, LLC ("Rime"), a privately-held, Texas-based, engineering business that specializes in building products for the downhole measurement-while-drilling ("MWD") industry in exchange for approximately USD $41,000 (refer to the subsequent event section of this MD&A).
- The Company retains a great deal of flexibility in regards to its capital budget with the ability to increase or decrease expenditures in response to changing market conditions, including commodity prices which generally drive activity levels. The Company is maintaining its 2023 net capital budget of $36,000.

PRESIDENT'S MESSAGE

Comments from President & CEO Tom Connors:

"Record revenue of $115,058 and Adjusted EBITDAS of $18,222 for any second quarter in corporate history demonstrates continued and deliberate progress on the execution of our size and scale strategy. In fact, since we embarked on our plan we have delivered consistent growth in Adjusted EBITDAS on a weighted average shares outstanding basis when comparing the trailing twelve-month performance at each quarter end from the beginning of 2021.



"With approximately 70% of our revenue on an annualized basis generated in the U.S., the transformative growth in our U.S. business offset the seasonal lows in Canada and bolstered Adjusted EBITDAS, cash flow and net income in a quarter, which is typically challenging. Our increased scale in previous quarters and more consistent performance driven by our U.S. business in the second quarter have contributed to stronger overall performance, which has allowed us to reduce our borrowings substantially from July 2022. Although our debt levels did increase moderately with the recent Rime acquisition, we have continued confidence in activity levels and corresponding cash flows in order to maintain a strong level of liquidity in the business. With a focus on disciplined capital deployment, Cathedral will continue to reduce its leverage profile over the coming quarters, while also having the financial flexibility to allocate funds to share repurchases, depending on market conditions.

"Despite the recent challenging market conditions in the U.S., we achieved a job count in the mid-60's in the second quarter up from the high-40's in late Q1. While the higher job count comes with a higher mix of conventional work, bringing average day rates lower, it is a testament to the performance capabilities of our U.S. team and technology that enabled growth in demand from our customers for our services. We expect the U.S. rig count will bottom sometime in 2023 Q3 and are encouraged by our strong job count on approximately 60 active rigs that continues into the third quarter. We expect the job count to remain steady or slightly improved through the remainder of the year. With the higher job count comes full asset utilization, and in the short-term we anticipate a higher level of equipment rentals to meet demand as we wait on deliveries from our capital program.

“In Canada, the expansion of our business and market share led to a significantly more active second quarter than last year with 64% year-over-year Q2 revenue growth. Our customers remain disciplined with most committed to maintaining capital programs for 2023. Industry rig counts have ticked lower than the same period in 2022, but are expected to remain somewhat consistent to slightly improved in the back half of the year. We anticipate improved margins and consistent market share in the third quarter as the benefits from our repair program earlier in the year flow through to a lower need for rentals.

With MWD components active on an estimated 40% of U.S. land rigs, our recent acquisition of Rime will provide a pipeline of technology that has wide market acceptance and adoption. We have a tremendous opportunity to deploy industry recognized technology to minimize rentals in Altitude and significantly expand margins as we build out our own proprietary MWD platform beginning in 2023 and into 2024. We are also excited about the expanded capacity to further differentiate ourselves in the market with industry leading technology now and into the future,” concluded Mr. Connors.

NON-GAAP MEASURES

Cathedral uses certain performance measures throughout this MD&A that are not defined under IFRS or Generally Accepted Accounting Principles (“GAAP”). These non-GAAP measures do not have a standardized meaning and may differ from that of other organizations, and accordingly, may not be comparable.

These measures include the Adjusted gross margin, Adjusted gross margin %, Adjusted EBITDAS, Adjusted EBITDAS margin %, Adjusted EBITDAS per diluted share and Free cash flow. Management believes these measures provide supplemental financial information that is useful in the evaluation of Cathedral’s operations. They are commonly used by other oilfield service companies. Investors should be cautioned, however, that these measures should not be construed as alternatives to IFRS measures as an indicator of Cathedral’s performance.

These non-GAAP measures are defined as follows:

i) **"Adjusted gross margin"** - calculated as gross margin before non-cash costs (depreciation, amortization and share-based compensation); is considered a primary indicator of operating performance (see tabular calculation);

ii) **"Adjusted gross margin %"** - calculated as Adjusted gross margin divided by revenues; is considered a primary indicator of operating performance (see tabular calculation);

iii) **"Adjusted EBITDAS"** - calculated as net income before finance costs, unrealized foreign exchange on intercompany balances, income tax expense, depreciation, amortization, non-recurring costs (including acquisition and restructuring costs), write-down of inventory and share-based compensation; provides supplemental information to earnings that is useful in evaluating the results and financing of the Company’s business activities before considering certain charges (see tabular calculation);

iv) **"Adjusted EBITDAS margin %"** - calculated as Adjusted EBITDAS divided by revenues; provides supplemental information to earnings that is useful in evaluating the results and financing of the Company’s business activities before considering certain charges as a percentage of revenues (see tabular calculation);

v) **"Adjusted EBITDAS per diluted share"** - calculated as Adjusted EBITDAS divided by the diluted weighted average shares outstanding; provides supplemental information to earnings that is useful in evaluating the results and financing of the Company’s business activities before considering certain charges on a per diluted share basis; and

vi) **"Free cash flow" -** calculated as cash flow provided by (used in) operating activities prior to: i) changes in non-cash working capital, ii) income taxes paid (refunded) and iii) non-recurring costs less: i) property, plant and equipment additions, excluding assets acquired in business combinations, ii) required repayments on loans and borrowings, and iii) cash lease payments, offset by proceeds from dispositions of property, plant and equipment. Management uses this measure as an indication of the Company's ability to generate funds from its operations to support future capital expenditures, additional debt repayment or other initiatives (see tabular calculation).

The following tables provide reconciliations from the IFRS measures to non-GAAP measures included in this MD&A.

Adjusted gross margin

	Three months ended June 30,		Six months ended June 30,	
	2023	2022	2023	2022
Gross margin	$ 16,338	$ 500	$ 33,402	$ 6,029
Add non-cash items included in cost of sales:				
Inventory write-down	—	—	378	—
Depreciation and amortization	10,115	4,622	19,340	8,911
Share-based compensation	96	49	240	92
Adjusted gross margin	$ 26,549	$ 5,171	$ 53,360	$ 15,032
Adjusted gross margin %	23%	19%	22%	24%

Adjusted EBITDAS

	Three months ended June 30, 2023	Three months ended June 30, 2022	Six months ended June 30, 2023	Six months ended June 30, 2022
Net income (loss)	$ 2,416	$ (2,824)	$ 3,210	$ (581)
Add (deduct):				
Income tax expense (recovery)	2,176	(756)	2,583	(756)
Depreciation and amortization included in cost of sales	10,115	4,622	19,340	8,911
Depreciation and amortization included in selling, general and administrative expenses	1,499	124	3,008	248
Share-based compensation included in cost of sales	96	49	240	92
Share-based compensation included in selling, general and administrative expenses	674	83	1,449	174
Finance costs - loans and borrowings	1,486	295	3,216	524
Finance costs - lease liabilities	205	195	419	384
	18,667	1,788	33,465	8,996
Unrealized foreign exchange gain on intercompany balances	(910)	758	(899)	463
Inventory write-down and non-recurring expenses	465	290	843	290
Adjusted EBITDAS	$ 18,222	$ 2,836	$ 33,409	$ 9,749
Adjusted EBITDAS margin %	16%	10%	14%	16%

Free cash flow

	Three months ended June 30, 2023	Three months ended June 30, 2022	Six months ended June 30, 2023	Six months ended June 30, 2022
Cash flow provided by operating activities	$ 11,232	$ 4,511	$ 35,148	$ 2,753
Add (deduct):				
Income tax refund (paid)	817	(20)	648	(28)
Changes in non-cash operating working capital	1,617	(3,243)	(9,987)	4,614
Non-recurring expenses	465	290	465	290
Proceeds on disposal of property, plant and equipment	4,208	3,091	9,780	4,324
Less:				
Property, plant and equipment additions(1)	(8,714)	(6,218)	(22,465)	(9,522)
Required repayments on loans and borrowings(2)	(3,727)	(9,686)	(7,455)	(10,292)
Repayments of lease liabilities, net of finance costs	(914)	(733)	(1,849)	(1,336)
Free cash flow (deficit)	$ 4,984	$ (12,008)	$ 4,285	$ (9,197)

(1) Property, plant and equipment additions exclude non-cash additions and assets acquired in business combinations.
(2) Required repayments on loans and borrowings in accordance with the credit facility agreement. Excludes discretionary debt repayments.

2022 ACQUISITIONS

In 2022, the Company executed five strategic acquisitions as detailed below:

- U.S.- based company, Altitude Energy Partners, LLC ("Altitude") in July 2022 for total consideration of $124,112, comprised of a cash payment of $87,245 and a common share issuance of $36,867, with the purchase price allocated primarily to working capital, property, plant and equipment, intangible assets and goodwill;
- U.S.- based operations, Discovery Downhole Services ("Discovery") in February 2022 for total consideration of $20,892, comprised of a cash payment of $18,160 and a common share issuance of $2,732, with the purchase price allocated primarily to inventory and property, plant and equipment;
- LEXA Drilling Technologies Inc. ("Lexa") in June 2022 for total consideration of $1,761 in exchange for intangible assets;
- Compass Directional Services ("Compass") in June 2022 for total consideration of $8,315, comprised of a cash payment of $4,000 and a common share issuance of $4,315, with the purchase price allocated primarily to inventory and property, plant and equipment; and

- the Canadian directional drilling business of Ensign Energy Services ("Ensign") in October 2022 for total common share consideration of $5,965 with the purchase price allocated primarily to inventory and property, plant and equipment.

In addition to the assets acquired as described above, there were certain other minor working capital, right-of-use assets and lease liabilities, and deferred tax liabilities recognized as part of the purchase price allocations.

RESULTS OF OPERATIONS

	Three months ended June 30,		Six months ended June 30,	
	2023	2022	2023	2022
Revenues				
Canada	$ 21,515	$ 13,091	$ 66,858	$ 38,490
United States	93,543	14,561	175,865	23,547
Total revenues	115,058	27,652	242,723	62,037
Cost of sales:				
Direct costs	(88,509)	(22,481)	(189,741)	(47,005)
Depreciation and amortization	(10,115)	(4,622)	(19,340)	(8,911)
Share-based compensation	(96)	(49)	(240)	(92)
Cost of sales	(98,720)	(27,152)	(209,321)	(56,008)
Gross margin	$ 16,338	$ 500	$ 33,402	$ 6,029
Gross margin %	14%	2%	14%	10%
Adjusted gross margin % [1]	23%	19%	22%	24%

[1] Refer to the "Non-GAAP Measures" section in this MD&A.

Consolidated

The Company recognized $115,058 of revenues in 2023 Q2, an increase of $87,406 or 316%, compared to $27,652 in 2022 Q2. The Company recognized $242,723 of revenues in the six months ended June 30, 2023, an increase of $180,686 or 291%, compared to $62,037 for the same period in 2022.

The Company recognized $98,720 of cost of sales in 2023 Q2, an increase of $71,568 or 264%, compared to $27,152 in 2022 Q2. The Company recognized $209,321 of cost of sales in the six months ended June 30, 2023, an increase of $153,313 or 274%, compared to $56,008 for the same period in 2022.

The Gross margin % increased to 14% both in 2023 Q2 and the six months ended June 30, 2023, compared to 2% and 10% for the same periods in 2022, respectively.

The Adjusted gross margin % increased to 23% in 2023 Q2, compared to 19% in 2022 Q2. The Adjusted gross margin % decreased to 22% in the six months ended June 30, 2023, compared to 24% for the same period in 2022.

Depreciation and amortization expense allocated to cost of sales increased to $10,115 and $19,340 in 2023 Q2 and the six months ended June 30, 2023, compared to $4,622 and $8,911 in the same periods in 2022, respectively, due to property, plant and equipment additions, including those related to the 2022 acquisitions.

Depreciation and amortization expense included in cost of sales as a percentage of revenue was 9% and 8% for 2023 Q2 and the six months ended June 30, 2023, compared to 17% and 14% for the same periods in 2022, respectively.

Canadian segment

Revenues

Canadian revenues were $21,515 in 2023 Q2, an increase of $8,424 or 64%, compared to $13,091 in 2022 Q2, mainly due to acquisitions completed in 2022, including Compass and Ensign. The Company realized: i) a 33% increase in activity days to 1,662 days in 2023 Q2, compared to 1,246 days in 2022 Q2, and ii) a 23% increase in the average day rate to $12,945 per day in 2023 Q2, compared to $10,507 per day in 2022 Q2.

Canadian revenues were $66,858 in the six months ended June 30, 2023, an increase of $28,368 or 74%, compared to $38,490 for the same period in 2022, mainly due to acquisitions completed in 2022, including Compass and Ensign. The Company realized: i) a 36% increase in activity days to 5,321 days in the six months ended June 30, 2023, compared to 3,916 days the same period in 2022, and ii) a 28% increase in the average day rate to $12,565 per day in the six months ended June 30, 2023, compared to $9,829 per day for the same period in 2022.

Based on publicly disclosed Canadian drilling activity, Cathedral's Canadian market share in 2023 Q2 and the six months ended June 30, 2023 was 20.1% and 23.4%, compared to 15.4% and 18.2% for the same periods in 2022, respectively.

Direct costs

Canadian direct costs included in cost of sales were $16,422 in 2023 Q2, an increase of $4,735 or 41%, compared to $11,687 in 2022 Q2. The increase is mainly due to higher costs related to the 2022 acquisitions. As a percentage of revenues, direct costs decreased to 76% in 2023 Q2 from 89% in 2022 Q2, mainly due to lower repair and maintenance, third-party rental costs and fixed costs as a percentage of revenues.

Canadian direct costs included in cost of sales were $51,151 in the six months ended June 30, 2023, an increase of $20,935 or 69%, compared to $30,216 for the same period in 2022. The increase is mainly due to higher costs related to the 2022 acquisitions. As a percentage of revenues, direct costs decreased slightly to 77% in the six months ended June 30, 2023 from 79% for the same period in 2022.

United States segment

Revenues

U.S. revenues were $93,543 in 2023 Q2, an increase of $78,982 or 542%, compared to $14,561 in 2022 Q2, mainly as a result of the acquisitions completed in 2022, including Discovery and Altitude. The Company realized a 862% increase in activity days to 3,963 days in 2023 Q2, compared to 412 days in 2022 Q2. The average day rate decreased to $23,604 per day in 2023 Q2, compared to $35,343 per day in 2022 Q2, mainly as a result of the Altitude acquisition and a change in job mix.

U.S. revenues were $175,865 in the six months ended June 30, 2023, an increase of $152,318 or 647%, compared to $23,547 for the same period in 2022, mainly as a result of the acquisitions completed in 2022, including Discovery and Altitude. The Company realized a 841% increase in activity days to 7,280 days in the six months ended June 30, 2023, compared to 774 days for the same period in 2022. The average day rate decreased to $24,157 per day in the six months ended June 30, 2023, compared to $30,422 per day for the same period in 2022, mainly as a result of the Altitude acquisition and a change in job mix.

Based on publicly disclosed U.S. drilling rig activity, Cathedral's U.S. market share for 2023 Q2 and the six months ended June 30, 2023 was 8.7% and 7.7%, respectively, compared to under 1% for the same periods in 2022.

Direct costs

U.S. direct costs included in cost of sales were $72,087 in 2023 Q2, an increase of $61,293 or 568%, compared to $10,794 in 2022 Q2. The increase is mainly due to higher costs related to the 2022 acquisitions, including Discovery and Altitude. As a percentage of revenues, direct costs also increased to 77% in 2023 Q2 from 74% in 2022 Q2, mainly due to higher labour, third-party equipment rental and other minor costs, offset by lower fixed costs as a percentage of revenues.

U.S. direct costs included in cost of sales were $138,590 in the six months ended June 30, 2023, an increase of $121,801 or 725%, compared to $16,789 for the same period in 2022. The increase is mainly due to higher costs related to the 2022 acquisitions, including Discovery and Altitude. As a percentage of revenues, direct costs also increased to 79% in the six months ended June 30, 2023, compared to 71% in the same period in 2022, mainly due to higher labour and third-party equipment rental costs.

Selling, general and administrative ("SG&A") expenses

	Three months ended June 30, 2023	2022	Six months ended June 30, 2023	2022
Selling, general and administrative expenses:				
Direct costs	$ 12,004	$ 3,287	$ 26,090	$ 6,853
Depreciation and amortization	1,499	124	3,008	248
Share-based compensation	674	83	1,449	174
Selling, general and administrative expenses	$ 14,177	$ 3,494	$ 30,547	$ 7,275

The Company recognized SG&A expenses of $14,177 in 2023 Q2, an increase of $10,683, compared to $3,494 in 2022 Q2. The increase is mainly due to the 2022 acquisitions. SG&A expenses as a percentage of revenues were 12% in 2023 Q2 and 2022 Q2.

The Company recognized SG&A expenses of $30,547 in the six months ended June 30, 2023, an increase of $23,272, compared to $7,275 for the same period in 2022. The increase is mainly due to the 2022 acquisitions and discretionary short-term incentive program payments, which were approved and recognized in 2023, compared to no discretionary incentive payments recognized in 2022. As a percentage of revenues, SG&A expenses were slightly higher at 13% in the six months ended June 30, 2023, compared to 12% for the same period in 2022, mainly due to the discretionary short-term incentive program payments.

Depreciation and amortization recognized in SG&A were $1,499 and $3,008 in 2023 Q2 and the six months ended June 30, 2023, compared to $124 and $248 for the same periods in 2022, respectively.

Stock-based compensation recognized in SG&A were $674 and $1,449 in 2023 Q2 and the six months ended June 30, 2023, compared to $83 and $174 for the same periods in 2022, respectively.

Technology group expenses

The Company recognized technology group expenses of $458 and $1,010 in 2023 Q2 and the six months ended June 30, 2023, compared to $231 and $450 for the same periods in 2022, respectively. Technology group expenses are salaries, benefits and shop supply costs related to new product development and technology.

Gain on disposal of equipment

The Company recognized a gain on disposal of equipment of $4,091 and $7,135 in 2023 Q2 and six months ended June 30, 2023, compared to $1,298 and $2,120 for the same periods in 2022, respectively, mainly related to equipment lost-in-hole. Proceeds on lost-in-hole equipment are based on service agreements held with clients. The Company received proceeds on disposal of equipment of $4,208 and $9,780 in 2023 Q2 and the six months ended June 30, 2023, compared to $3,091 and $4,324 for the same periods in 2022, respectively.

Finance costs

Finance costs were $1,486 in 2023 Q2, an increase of $1,191, compared to $295 in 2022 Q2. Finance costs were $3,216 in the six months ended June 30, 2023, an increase of $2,692, compared to $524 for the same period in 2022.

The higher costs are mainly due to the Company's increased debt levels from $9,170 as at June 30, 2022 to $60,080 as at June 30, 2023, coupled with an increase in interest rates in 2023 relative to 2022. The increased debt was in relation to the 2022 acquisitions (refer to the 'Liquidity and Capital Resources' section of this MD&A for more details).

In addition, the Company had $205 and $419 of finance costs in 2023 Q2 and the six months ended June 30, 2023 related to lease liabilities, compared to $195 and $384 for the same periods in 2022, respectively.

Foreign exchange

The Company recognized a foreign exchange gain of $954 in 2023 Q2, compared to a foreign exchange loss of $873 in 2022 Q2. The Company recognized a foreign exchange gain of $913 in the six months ended June 30, 2023, compared to a foreign exchange loss of $563 for the same period in 2022. The impact of foreign exchange is due to fluctuations of the Canadian dollar relative to the U.S. dollar related to foreign currency transactions recognized in net income.

The Company recognized a foreign currency translation loss on foreign operations of $3,826 in 2023 Q2, compared to a gain of $983 in 2022 Q2. The Company recognized a foreign currency translation loss on foreign operations of $4,251 in the six months ended June 30, 2023, compared to a gain of $627 for the same period in 2022. The Company’s foreign operations are denominated in USD and differences due to fluctuations in the foreign currency exchange rates are recorded in other comprehensive income.

Income tax

Income tax expense was $2,176 and $2,583 in 2023 Q2 and the six months ended June 30, 2023, respectively, compared to an income tax recovery of $756 for the same periods in 2022. Income tax expense is booked based upon expected annualized rates using the statutory rates of 23% for Canada and the U.S.

The Company’s effective income tax rate is higher than expected at approximately 45% due to its Canadian entity incurring losses for income tax purposes in the period, the tax benefit of which has not been recognized.

LIQUIDITY AND CAPITAL RESOURCES

Annually, the Company’s principal source of liquidity is cash generated from operations and its proceeds from equipment lost-in-hole. In addition, the Company has the ability to fund liquidity requirements through its syndicated credit facility and the issuance of additional debt and/or equity, if available.

In order to facilitate the management of its liquidity, the Company prepares an annual budget, which is updated as necessary depending on varying factors, including changes in capital structure, execution of the Company’s business plan and general industry conditions. The annual budget is approved by the Board of Directors and updated forecasts are prepared as the fiscal year progresses with changes reviewed by the Board of Directors.

Cash flow provided by operating activities was $11,232 and $35,148 in 2023 Q2 and the six months ended June 30, 2023, compared to $4,511 and $2,753 for the same periods in 2022, respectively. Cathedral intends to use the free cash flow generated in the remainder of 2023 to continue to pay down debt while remaining opportunistic in making strategic and accretive acquisitions.

During the six months ended June 30, 2023, 17,731,888 of the April 2022 bought deal offering warrants and 575,000 of the February 2021 private placement warrants were exercised at $0.85 per warrant and $0.24 per warrant totaling $15,072 and $138 in gross cash proceeds, respectively. On April 26, 2023, the remaining 55,462 of the April 2022 bought deal offering warrants expired.

As at June 30, 2023, the 2,000,000 warrants related to the Precision Drilling acquisition were outstanding. Subsequent to June 30, 2023, the warrants were exercised at $0.60 per warrant for gross cash proceeds of $1,200.

At June 30, 2023, the Company had working capital, excluding current portion of loans and borrowings of $62,048 (December 31, 2022 - $60,447).

Syndicated credit facility

During the six months ended June 30, 2023, the Company repaid its balance owing on the Syndicated Operating Facility of $13,000. In addition, the Company made contractual repayments totaling $7,400 related to its Syndicated Term Facility reducing the carrying value to $59,200 as at June 30, 2023. As at June 30, 2023, the $10,000 Revolving Operating Facility remained undrawn. In addition, the Company continues to hold a Highly Affected Sectors Credit Availability Program (“HASCAP”) loan.

At June 30, 2023, the Company was in compliance with its financial covenants, which were as follows:

- Consolidated Funded Debt to Consolidated Credit Agreement EBITDA ratio shall not exceed 2.5.0:1; and
- Consolidated Fixed Charge Coverage ratio shall not be less than 1.25:1

Subsequent to June 30, 2023, the Company entered into a three-year term credit facility (the “Credit Facility”), replacing its existing credit facility with its syndicate of lenders led by ATB Financial (“ATB”) related to the acquisition of Rime. The Credit Facility provides an approximate $137,000 principal amount comprised of: i) a $59,200 Syndicated Term Facility (replacing the existing Syndicated Term Facility), ii) a new USD $21,000 term loan, repayable in equal quarterly installments over a five-year amortization period, iii) a $35,000 Syndicated Operating Facility (previously $15,000), and iv) a $15,000 Revolving Operating Facility (previously $10,000). The Credit Facility was utilized to replace and repay Cathedral’s existing credit facility. The interest rate and financial covenants were unchanged under the new Credit Facility.

Contractual obligations and contingencies

As at June 30, 2023, the Company’s commitment to purchase property, plant and equipment was approximately $8,003. Cathedral anticipates expending these funds in 2023 Q3 and Q4, subject to supply chain delays.

The Company also holds six letters of credit totaling $1,895 related to rent payments, corporate credit cards and a utilities deposit.

The Company is involved in various legal claims associated with the normal course of operations. The Company believes that any liabilities that may arise pertaining to such matters would not have a material impact on its financial position.

Subsequent event

On July 11, 2023, Cathedral, through a wholly-owned subsidiary, acquired Rime, a privately-held, Texas-based, engineering business that specializes in building products for the downhole measurement-while-drilling (“MWD”) industry (the “Rime acquisition”) in exchange for approximately USD $41,000 comprised of: (a) the payment of USD $21,000 in cash; and (b) the issuance of USD $20,000 of subordinated exchangeable promissory notes (“EP Notes”) that are exchangeable into a maximum of 24,570,000 common shares in the capital of Cathedral (“EP Shares”) at a deemed price of CAD $1.10 per common share.

The EP Notes have a three-year term and accrue interest payable quarterly at a rate of 5% per annum. Any time prior to expiry of the EP Notes, if the 20-day volume weighted average trading price of the common shares of Cathedral (“Common Shares”) equals or exceeds CAD $1.10 per Common Share, Cathedral may cause the exchange of the EP Notes for Common Shares. Cathedral and the holders of the EP Notes may agree to an earlier exchange of the EP Notes into Common Shares. In addition to the statutory hold periods applicable to the EP Shares under Canadian and U.S. securities laws, the parties agreed to contractual restrictions on resale of any EP Shares as follows: 33% of the EP Shares are restricted until July 11, 2024; a further 33% of the EP Shares are restricted until July 11, 2025; and a further 34% of the EP Shares are restricted until July 11, 2026, subject to certain exceptions contained in the terms governing the EP Notes.

Share capital

As at August 10, 2023, the Company has 245,200,173 common shares, no warrants, 19,169,300 stock options and EP Notes that are exchangeable into a maximum of 24,570,000 common shares outstanding.

Change of Transfer Agent

Effective July 11, 2023, Cathedral has replaced Computershare Trust Company, as the registrar and transfer agent of the Company’s common shares, with Odyssey Trust Company. Shareholders do not need to take any action with respect to the change in registrar and transfer agent services. All inquiries and correspondence related to shareholder records, transfers of shares, lost certificates and changes of address should now be directed to Odyssey Trust Company, through their offices in Calgary, Vancouver and Toronto: https://odysseytrust.com/.

CAPITAL EXPENDITURES

The following table details the property, plant and equipment additions:

	Three months ended June 30,		Six months ended June 30,	
	2023	2022	2023	2022
Motors and related equipment	$ 5,231	$ 1,346	$ 12,647	$ 2,825
MWD and related equipment	885	4,866	5,408	6,671
Shop and automotive equipment	973	—	1,750	—
Other	1,100	6	2,638	26
Capital expenditures	$ 8,189	$ 6,218	$ 22,443	$ 9,522

The additions of $8,189 and $22,443 (2022 - $6,218 and $9,522) were partially funded by proceeds on disposal of equipment of $4,208 and $9,780 (2022 - $3,091 and 4,324) in 2023 Q2 and the six months ended June 30, 2023, respectively.

The Company's 2023 net capital program has been maintained at $36,000, excluding any potential acquisitions. The net capital program is targeted at growing Cathedral’s high-performance mud motor and MWD in both Canada and the U.S. Cathedral intends to fund its 2023 capital plan from cash flow provided by operating activities, along with proceeds on equipment lost-in-hole.

OUTLOOK

Despite recent volatility in oil and gas prices, the outlook for oilfield services remains constructive. OPEC's continued vigilance around managing a solid floor price for oil in the mid-$60 per barrel has paid off in a summer West Texas Intermediate ("WTI") rally back to approximately $80 per barrel. Commodity markets are now discounting an economic soft landing in the global central bank fight against inflation. There are other factors driving the recovery in oil prices, including an intra-year plateauing of Permian oil production, stalled Russian oil export levels, the end of oil sales from the U.S. Strategic Petroleum Reserve, as well as generally strong oil demand forecasts from numerous agencies, such as the IEA and the EIA. U.S. natural gas prices have also moved higher in 2023 Q3 from second quarter levels, although the lack of additional North American LNG takeaway capacity until later 2024 may be a barrier to a larger near-term price recovery.

A survey of forecasts from seven Canadian-based investment banks shows an expectation for a bottoming of the U.S. land rig count sometime in 2023 Q3 or early 2023 Q4 with a slow ramp up through all four quarters of 2024 (Source: ATB Capital Markets, BMO Capital Markets, National Bank Financial, Peters & Co, Stifel, Raymond James Canada, TD Securities). Specifically, the consensus average U.S. land rig count is forecast to decline to 661 active rigs in 2023 Q3 from 699 in 2023 Q2 (5% drop) before recovering to 670 in 2023 Q4 (1% recovery). The forecast average U.S. land rig count for 2023 is currently 693, down only 2% year-over-year, on average. Although it is early, the forecast average among these seven investment banks is for a modest uptick in 2024 – to an average of approximately 700 active rigs. Looking to 2024 and beyond, to incentivize increased development, oil and natural gas prices need to stabilize at current or higher levels, while natural gas takeaway capacity needs to be added from the Haynesville and Permian to supply the plethora of LNG projects now under development. Once this infrastructure is in place, the call on oilfield service companies with a well-scaled U.S. operating footprint is likely to be considerable. Cathedral believes it is well on the way to establishing such an operating footprint in the U.S.

In Western Canada, the seven analysts predict that the average rig count will be modestly stronger year-over-year in 2023 and 2024 (9% and 4%, respectively), mostly due to the ramping in field spending, related to supplying the first natural gas into LNG Canada for 2025. Although the U.S. has been a much stronger growth market over the last decade, due primarily to field spending in the Permian, looking out to 2024, Canada appears to offer more near-term growth visibility. Canadian exploration and production ("E&P") companies are generating healthy levels of free cash flow and have improved their balance sheets dramatically. Improved E&P balance sheets are less exposed to oil and gas price volatility, which may lead to a moderation in the amplitude of the drilling cycles going forward. Cathedral expects to maintain a strong market share in Canada through the rest of 2023 and is equally optimistic on 2024 activity, given the ongoing ramp in LNG-related spending.

CONTROLS AND PROCEDURES

The Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO") are responsible for designing disclosure controls and procedures ("DC&P") and internal controls over financial reporting ("ICFR") as defined in National Instrument 52-109 Certification of Disclosure in Issuer's Annual and Interim Filings ("52-109"), 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.

Cathedral's DC&P have been designed to provide reasonable assurance that material information relating to Cathedral is made known to the CEO and the CFO by others and that information required to be disclosed by Cathedral in its annual filings, interim filings or other reports filed or submitted by Cathedral under securities legislation is recorded, processed, summarized and reported within the time periods specified in applicable securities legislation. Because of their inherent limitations, DC&P and ICFR may not prevent or detect all misstatements, errors or fraud. Control systems, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control systems are met.

No material change in the Company's DC&P and its ICFR were identified during the three months ended June 30, 2023 that have materially affected, or are reasonably likely to materially affect the Company's ICFR.

Cathedral has limited the scope of design of DC&P and ICFR to exclude controls, policies and procedures of Altitude Energy Partners, LLC which was acquired on July 13, 2022, the financial performance of which is included in the unaudited condensed consolidated financial statements for the three months ended June 30, 2023. The scope limitation is in accordance with section 3.3(1)(b) of NI 52-109 which allows an issuer to limit its design of DC&P and ICFR to exclude controls, policies and procedures of a business that the issuer acquired not more than 365 days before the end of the fiscal period.

The tables below presents the summary of financial information of Altitude:

	Three months ended June 30, 2023	Six months ended June 30, 2023
Revenues	$ 86,759	$ 161,729
Net income	6,322	7,527

		As at June 30, 2023
Current assets	$	94,824
Non-current assets		125,024
Current liabilities		68,692
Non-current liabilities		13,479
Capital purchase commitments		6,649

RISK FACTORS

Risk factors associated with the Company are included in the Company's Annual Information Form for the year ended December 31, 2022 dated April 14, 2023, which is available on SEDAR+ at www.sedarplus.ca and on the Company's website (www.cathedralenergyservices.com). Those risk factors remain in effect as at June 30, 2023.

GOVERNANCE

The Audit Committee of the Board of Directors has reviewed this MD&A and the related unaudited condensed consolidated financial statements and recommended they be approved to the Board of Directors. Following a review by the Board of Directors, the MD&A and the unaudited condensed consolidated financial statements for the three and six months ended June 30, 2023 were approved on August 10, 2023.

NEW AND FUTURE ACCOUNTING POLICIES

There were no new or amended standards issued during the three and six months ended June 30, 2023 that are expected to have a significant impact on the Company's financial statements.

SUMMARY OF QUARTERLY RESULTS

Three months ended	Jun 2023	Mar 2023	Dec 2022	Sep 2022	Jun 2022	Mar 2022	Dec 2021	Sep 2021
Revenues	$ 115,058	$ 127,665	$ 128,518	$ 107,846	$ 27,652	$ 34,385	$ 23,710	$ 20,127
Adjusted EBITDAS [(1)]	$ 18,222	$ 15,187	$ 30,284	$ 28,065	$ 2,865	$ 6,944	$ 1,273	$ 5,170
Adjusted EBITDAS [(1)] per share - diluted	$ 0.08	$ 0.06	$ 0.13	$ 0.14	$ 0.02	$ 0.07	$ 0.02	$ 0.07
Net income (loss)	$ 2,416	$ 794	$ 10,270	$ 8,658	$ (2,824)	$ 2,243	$ (1,097)	$ 403
Net income (loss) per share - diluted	$ 0.01	$ —	$ 0.05	$ 0.04	$ (0.02)	$ 0.02	$ (0.01)	$ 0.01

(1) Refer to the "Non-GAAP Measures" section in this MD&A

A portion of the Company's operations are carried on in Western Canada where activity levels in the oilfield services industry are subject to a degree of seasonality. Operating activities in Western Canada are generally lower during "spring breakup" which normally commences in mid to late-March and continues through to May. Operating activities generally peak in the winter months from December until mid to late-March. Additionally, volatility in the weather and temperatures not only during this period, but year-round, can create additional unpredictability in operational results. Activity levels in the oil and natural gas basins in the U.S. are not subject to the same level of seasonality that occurs in the Western Canada region.

FORWARD LOOKING STATEMENTS

This MD&A contains certain forward-looking statements and forward-looking information (collectively referred to herein as "forward-looking statements") within the meaning of applicable Canadian securities laws. All statements other than statements of present or historical fact are forward-looking statements. Forward-looking statements are often, but not always, identified by the use of words such as "anticipate", "achieve", "believe", "plan", "intend", "objective", "continuous", "ongoing", "estimate", "outlook", "expect", "may", "will", "project", "should" or similar words suggesting future outcomes. In particular, this MD&A contains forward-looking statements relating to, among other things:

- Future commitments;
- The 2023 capital program and financing of the program;
- The Company retains a great deal of flexibility in regards to its capital budget with the ability to increase or decrease expenditures in response to changing market conditions, including commodity prices which generally drive activity levels;
- We have continued confidence in activity levels and corresponding cash flows to maintain a strong level of liquidity in the business;
- With a focus on disciplined capital deployment, Cathedral will continue to reduce its leverage profile over the coming quarters, while also having the financial flexibility to allocate funds to share repurchases, depending on market conditions;
- We expect the U.S. rig count will bottom sometime in 2023 Q3 and are encouraged by our strong job count on approximately 60 active rigs that continues into the third quarter;
- We expect the job count to remain steady or slightly improved through the remainder of the year;
- With the higher job count comes full asset utilization, and in the short-term we anticipate a higher level of equipment rentals to meet demand as we wait on deliveries from our capital program;

- Our customers remain disciplined with most committed to maintaining capital programs for 2023;
- Industry rig counts have ticked lower than the same period in 2022, but are expected to remain somewhat consistent to slightly improved in the back half of the year;
- We anticipate improved margins and consistent market share in the third quarter as the benefits from our repair program earlier in the year flow through to a lower need for rentals;
- With MWD components active on an estimated 40% of U.S. land rigs, our recent acquisition of Rime will provide a pipeline of technology that has wide market acceptance and adoption;
- We have a tremendous opportunity to deploy industry recognized technology to minimize rentals in Altitude and significantly expand margins as we build out our own proprietary MWD platform beginning in 2023 and into 2024;
- We are also excited about the expanded capacity to further differentiate ourselves in the market with industry leading technology now and into the future;
- Despite recent volatility in oil and gas prices, the outlook for oilfield services remains constructive;
- U.S. natural gas prices have also moved higher in 2023 Q3 from second quarter levels, although the lack of additional North American LNG takeaway capacity until later 2024 may be a barrier to a larger near-term price recovery;
- A survey of forecasts from seven Canadian-based investment banks shows an expectation for a bottoming of the U.S. land rig count sometime in 2023 Q3 or early 2023 Q4 with a slow ramp up through all four quarters of 2024;
- Specifically, the consensus average U.S. land rig count is forecast to decline to 661 active rigs in 2023 Q3 from 699 in 2023 Q2 (5% drop) before recovering to 670 in 2023 Q4 (1% recovery);
- The forecast average U.S. land rig count for 2023 is currently 693, down only 2% year over year, on average;
- Although it is early, the forecast average among these seven investment banks is for a modest uptick in 2024 – to an average of approximately 700 active rigs;
- Looking to 2024 and beyond, oil and natural gas prices need to stabilize at current or higher levels, while natural gas takeaway capacity needs to be added from the Haynesville and Permian, to supply the plethora of LNG projects now under development. Once this infrastructure is in place, the call on oilfield service companies with a well-scaled U.S. operating footprint is likely to be considerable. Cathedral believes it is well on the way to establishing such an operating footprint in the U.S;
- In Western Canada, the seven analysts predict that the average rig count will be modestly stronger year-over-year in 2023 and 2024 (9% and 4%, respectively), mostly due to the ramping in field spending, related to supplying the first natural gas into LNG Canada for 2025;
- Although the U.S. has been a much stronger growth market over the last decade, due primarily to field spending in the Permian, looking out to 2024, Canada appears to offer more near-term growth visibility;
- Improved E&P balance sheets are less exposed to oil and gas price volatility, which may lead to a moderation in the amplitude of the drilling cycles going forward;
- Cathedral expects to maintain a strong market share in Canada through the rest of 2023 and is equally optimistic on 2024 activity, given the ongoing ramp in LNG-related spending.

The Company believes the expectations reflected in such forward-looking statements are reasonable as of the date hereof but no assurance can be given that these expectations will prove to be correct and such forward-looking statements should not be unduly relied upon.

Various material factors and assumptions are typically applied in drawing conclusions or making the forecasts or projections set out in forward-looking statements. Those material factors and assumptions are based on information currently available to the Company, including information obtained from third-party industry analysts and other third-party sources. In some instances, material assumptions and material factors are presented elsewhere in this MD&A in connection with the forward-looking statements. You are cautioned that the following list of material factors and assumptions is not exhaustive. Specific material factors and assumptions include, but are not limited to:

- the performance of Cathedral's business;
- impact of economic and social trends;
- oil and natural gas commodity prices and production levels;
- capital expenditure programs and other expenditures by Cathedral and its customers;
- the ability of Cathedral to retain and hire qualified personnel;
- the ability of Cathedral to obtain parts, consumables, equipment, technology, and supplies in a timely manner to carry out its activities;
- the ability of Cathedral to maintain good working relationships with key suppliers;
- the ability of Cathedral to retain customers, market its services successfully to existing and new customers and reliance on major customers;
- risks associated with technology development and intellectual property rights;
- obsolescence of Cathedral’s equipment and/or technology;
- the ability of Cathedral to maintain safety performance;
- the ability of Cathedral to obtain adequate and timely financing on acceptable terms;
- the ability of Cathedral to comply with the terms and conditions of its credit facility;
- the ability to obtain sufficient insurance coverage to mitigate operational risks;
- currency exchange and interest rates;
- risks associated with future foreign operations;
- the ability of Cathedral to integrate its transactions and the benefits of any acquisitions, dispositions and business development efforts;

- environmental risks;
- business risks resulting from weather, disasters and related to information technology;
- changes under governmental regulatory regimes and tax, environmental, climate and other laws in Canada and the U.S.; and
- competitive risks.

Forward-looking statements are not a guarantee of future performance and involve a number of risks and uncertainties some of which are described herein. Such forward-looking statements necessarily involve known and unknown risks and uncertainties, which may cause the Company's actual performance and financial results in future periods to differ materially from any projections of future performance or results expressed or implied by such forward-looking statements. These risks and uncertainties include, but are not limited to, the risks identified in this MD&A and in the Company's Annual Information Form under the heading "Risk Factors". Any forward-looking statements are made as of the date hereof and, except as required by law, the Company assumes no obligation to publicly update or revise such statements to reflect new information, subsequent or otherwise.

All forward-looking statements contained in this MD&A are expressly qualified by this cautionary statement. Further information about the factors affecting forward-looking statements is available in the Company's current Annual Information Form that has been filed with Canadian provincial securities commissions and is available on www.sedarplus.ca and the Company's website (www.cathedralenergyservices.com)

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at June 30, 2023 and December 31, 2022
Canadian dollars in ‘000s
(unaudited)

As at	June 30, 2023	December 31, 2022
Assets		
Current assets:		
Cash	$ 20,123	$ 11,175
Trade receivables	93,487	113,477
Prepaid expenses	2,652	4,529
Inventories	35,282	26,195
Total current assets	151,544	155,376
Property, plant and equipment (note 4)	109,435	108,530
Intangible assets (note 5)	34,855	38,511
Right-of-use assets (note 6)	10,169	12,178
Goodwill (note 5)	38,488	39,395
Total non-current assets	192,947	198,614
Total assets	$ 344,491	$ 353,990
Liabilities and Shareholders' Equity		
Current liabilities:		
Trade and other payables	$ 85,467	$ 90,389
Current taxes payable	807	909
Loans and borrowings, current (note 7)	15,680	15,735
Lease liabilities, current (note 6)	3,222	3,631
Total current liabilities	105,176	110,664
Loans and borrowings, long-term (note 7)	44,400	64,800
Lease liabilities, long-term (note 6)	12,851	14,249
Deferred tax liability	12,150	10,380
Total non-current liabilities	69,401	89,429
Total liabilities	174,577	200,093
Shareholders' equity:		
Share capital (note 8)	198,923	180,484
Treasury shares	(709)	(959)
Contributed surplus	14,223	15,854
Accumulated other comprehensive income	13,138	17,389
Deficit	(55,661)	(58,871)
Total shareholders' equity	169,914	153,897
Total liabilities and shareholders' equity	$ 344,491	$ 353,990

Subsequent events (note 12)

See accompanying notes to the unaudited condensed consolidated financial statements.

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (LOSS)

Three and six months ended June 30, 2023 and 2022
Canadian dollars in '000s except per share amounts
(unaudited)

	Three months ended June 30, 2023	Three months ended June 30, 2022	Six months ended June 30, 2023	Six months ended June 30, 2022
Revenues (note 10)	$ 115,058	$ 27,652	$ 242,723	$ 62,037
Cost of sales:				
Direct costs	(88,509)	(22,481)	(189,741)	(47,005)
Depreciation and amortization	(10,115)	(4,622)	(19,340)	(8,911)
Share-based compensation	(96)	(49)	(240)	(92)
Total cost of sales	(98,720)	(27,152)	(209,321)	(56,008)
Gross margin	16,338	500	33,402	6,029
Selling, general and administrative expenses:				
Direct costs	(12,004)	(3,287)	(26,090)	(6,853)
Depreciation and amortization	(1,499)	(124)	(3,008)	(248)
Share-based compensation	(674)	(83)	(1,449)	(174)
Total selling, general and administrative expenses	(14,177)	(3,494)	(30,547)	(7,275)
Technology group expenses	(458)	(231)	(1,010)	(450)
Gain on disposal of property, plant and equipment	4,091	1,298	7,135	2,120
Income (loss) from operating activities	5,794	(1,927)	8,980	424
Finance costs - loans and borrowings	(1,486)	(295)	(3,216)	(524)
Finance costs - lease liabilities	(205)	(195)	(419)	(384)
Foreign exchange (loss) gain	954	(873)	913	(563)
Acquisition and restructuring costs	(465)	(290)	(465)	(290)
Income (loss) before income taxes	4,592	(3,580)	5,793	(1,337)
Income tax (expense) recovery:				
Current	(525)	—	(561)	—
Deferred	(1,651)	756	(2,022)	756
Total income tax (expense) recovery	(2,176)	756	(2,583)	756
Net income (loss)	2,416	(2,824)	3,210	(581)
Other comprehensive income (loss)				
Foreign currency translation differences on foreign operations	(3,826)	983	(4,251)	627
Total comprehensive income (loss)	**$ (1,410)**	**$ (1,841)**	**$ (1,041)**	**$ 46**
Net income (loss) per share - basic and diluted (note 9)	$ 0.01	$ (0.02)	$ 0.01	$ (0.01)

See accompanying notes to unaudited condensed consolidated financial statements.

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

Six months ended June 30, 2023 and 2022
Canadian dollars in '000s
(unaudited)

	Share capital	Treasury shares	Contributed surplus	Accumulated other comprehensive income	Non-controlling interest	Deficit	Total shareholders' equity
Balance, December 31, 2021	$ 98,918	$ —	$ 11,793	$ 9,011	$ —	$ (77,218)	$ 42,504
Comprehensive (loss) income for the period	—	—	—	627	—	(581)	46
Issued pursuant to private placements, net of share issue costs	27,983	—	3,074	—	—	—	31,057
Consideration for business combination, net of share issue costs	8,038	—	—	—	—	—	8,038
Non-controlling interest	—	—	—	—	177	—	177
Treasury shares issued for business combination	959	(959)	—	—	—	—	—
Issued pursuant to stock option exercises	148	—	(46)	—	—	—	102
Share-based compensation	—	—	266	—	—	—	266
Balance, June 30, 2022	$ 136,046	$ (959)	$ 15,087	$ 9,638	$ 177	$ (77,799)	$ 82,190

	Share capital	Treasury shares	Contributed surplus	Accumulated other comprehensive income	Deficit	Total shareholders' equity
Balance, December 31, 2022	$ 180,484	$ (959)	$ 15,854	$ 17,389	$ (58,871)	$ 153,897
Comprehensive (loss) income for the period	—	—	—	(4,251)	3,210	(1,041)
Contributed surplus on vesting of treasury shares	—	250	(250)	—	—	—
Issued pursuant to warrant exercises	18,186	—	(2,976)	—	—	15,210
Issued pursuant to stock option exercises	253	—	(94)	—	—	159
Share-based compensation	—	—	1,689	—	—	1,689
Balance, June 30, 2023	$ 198,923	$ (709)	$ 14,223	$ 13,138	$ (55,661)	$ 169,914

See accompanying notes to unaudited condensed consolidated financial statements.

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

Three and six months ended June 30, 2023 and 2022
Canadian dollars in '000s
(unaudited)

	Three months ended June 30, 2023	Three months ended June 30, 2022	Six months ended June 30, 2023	Six months ended June 30, 2022
Cash provided by (used in):				
Operating activities:				
Net income (loss)	$ 2,416	$ (2,824)	$ 3,210	$ (581)
Non-cash adjustments:				
Income tax expense (recovery)	2,176	(756)	2,583	(756)
Depreciation and amortization	11,614	4,746	22,348	9,159
Share-based compensation	770	132	1,689	266
Gain on disposal of property, plant and equipment	(4,091)	(1,298)	(7,135)	(2,120)
Write-down of inventory included in cost of sales	—	—	378	—
Finance costs - loans and borrowings	1,486	295	3,216	524
Finance costs - lease liabilities	205	195	419	384
Income tax (paid) refund	(817)	20	(648)	28
Unrealized foreign exchange (gain) loss on intercompany balances	(910)	758	(899)	463
	12,849	1,268	25,161	7,367
Changes in non-cash operating working capital	(1,617)	3,243	9,987	(4,614)
Cash flow - operating activities	11,232	4,511	35,148	2,753
Investing activities:				
Cash paid on acquisition (note 3)	—	(3,930)	—	(22,090)
Property, plant and equipment additions	(8,714)	(6,218)	(22,465)	(9,522)
Intangible asset additions (note 5)	(22)	—	(144)	—
Proceeds on disposal of property, plant and equipment	4,208	3,091	9,780	4,324
Changes in non-cash investing working capital	174	1,046	(1,755)	841
Cash flow - investing activities	(4,354)	(6,011)	(14,584)	(26,447)
Financing activities:				
Advances of loans and borrowings	—	—	—	19,859
Repayments on loans and borrowings	(16,727)	(10,779)	(20,455)	(16,723)
Payments on lease liabilities, net of finance costs	(914)	(733)	(1,849)	(1,336)
Interest paid	(1,691)	(490)	(3,635)	(908)
Proceeds on common share issuances	14,479	24,686	15,367	31,160
Cash flow - financing activities	(4,853)	12,684	(10,572)	32,052
Effect of exchange rate on changes on cash	(990)	87	(1,044)	56
Change in cash	1,035	11,271	8,948	8,414
Cash, beginning of period	19,088	41	11,175	2,898
Cash, end of period	$ 20,123	$ 11,312	$ 20,123	$ 11,312

See accompanying notes to unaudited condensed consolidated financial statements.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Reporting entity

Cathedral Energy Services Ltd. ("LTD") is a company domiciled in Canada. LTD, along with the below noted subsidiaries, together are referred to as the "Company" or "Cathedral". The Company is a publicly traded company listed on the Toronto Stock Exchange ("TSX") under the symbol "CET". The unaudited condensed consolidated financial statements of the Company as at and for the three and six months ended June 30, 2023 are comprised of LTD and the following 100% owned subsidiaries:

- Cathedral Energy Services Inc. ("INC");
- 2438155 Alberta Ltd.;
- LEXA Drilling Technologies Inc. ("LEXA");
- CET Flight Holdco, Inc. ("Flight");
- Altitude Energy Holdco, LLC ("AEH"); and
- Altitude Energy Partners, LLC ("Altitude").

The Company is primarily involved and engaged in the business of providing directional drilling services to oil and natural gas companies in Western Canada and the United States ("U.S.").

LTD has a functional currency of Canadian dollars while INC, Flight, AEH and Altitude are incorporated in the U.S. and their functional currency is United States dollars ("USD").

2. Basis of preparation

These unaudited condensed consolidated financial statements have been prepared in accordance with International Accounting Standard 34, *Interim Financial Reporting* ("IAS 34") using accounting policies consistent with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). Accordingly, certain information and note disclosures normally included in the annual financial statements, prepared in accordance with IFRS, have been omitted or condensed.

These unaudited condensed consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements for the year ended December 31, 2022.

Certain figures in the comparative period have been reclassified for comparability with the current period presentation.

These unaudited condensed consolidated financial statements were prepared using accounting policies and methods of their application consistent with those used in the preparation of the Company's consolidated audited annual financial statements for the year ended December 31, 2022.

The unaudited condensed consolidated financial statements were authorized for issue by the Board of Directors on August 10, 2023.

These unaudited condensed consolidated financial statements for the three and six months ended June 30, 2023 are presented in Canadian dollars ("CAD"), which is the Company's functional currency. All financial information presented in dollars has been rounded to the nearest thousands, except for share and per share amounts.

Use of estimates and judgements

The preparation of the unaudited condensed consolidated financial statements requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected. The significant judgements made by management in applying the Company's accounting policies and the information used in assessing uncertainty have not changed significantly since December 31, 2022.

Significant estimates and judgements used in the preparation of these unaudited condensed consolidated financial statements remained unchanged from those disclosed in the Company's consolidated audited annual financial statements for the year ended December 31, 2022.

Future Accounting Pronouncements

There were no new or amended standards issued during the three and six months ended June 30, 2023 that are expected to have a significant impact on the Company's financial statements.

3. 2022 Acquisitions

On February 10, 2022, the Company acquired the operating assets of Discovery Downhole Services ("Discovery"). The acquisition included the operating assets and non-executive personnel of Discovery's U.S.- based, high-performance mud motor technology rental business. Cathedral paid $18,160 in cash consideration and issued 5,254,112 common shares valued at $0.52 per common share for total consideration of $20,892. In addition to a four-month statutory hold period on the common shares, the parties have agreed to contractual restrictions on resale as follows:

25% were restricted until February 10, 2023; a further 25% are restricted until August 10, 2023; and a further 50% are restricted until February 10, 2024, subject to certain exceptions. The Company expensed $31 in transaction costs related to the acquisition.

On June 17, 2022, the Company purchased 90.98% of LEXA Drilling Technologies Inc. ("LEXA"), a Calgary-based, downhole technology company for equity consideration in Cathedral. On July 19, 2022, the Company purchased the remaining 9.02% shares of LEXA. In total 1,772,727 common shares were issued, valued at $0.63 per common share for total consideration of $1,117. In addition, the Company recognized settlement of a technology license from a pre-existing relationship for consideration of $644.

On June 22, 2022, the Company acquired the operating assets of Compass Directional Services Ltd. ("Compass"). Cathedral paid $4,000 in cash consideration and issued 6,253,475 common shares valued at $0.69 per common share for total consideration of $8,315. Of the total share consideration, 1,389,664 common shares are subject to contractual restrictions vesting over four years. As such, these common shares are classified as treasury shares and a set portion vest each year on the anniversary of the acquisition. The compensation expense related to these treasury shares will be recognized over the vesting period.

4. Property, Plant and Equipment

Cost	Directional drilling equipment	Shop and automotive equipment	Other	Total
Balance, December 31, 2022	$ 164,816	$ 9,265	$ 2,213	$ 176,294
Additions	18,124	1,692	2,627	22,443
Disposals	(4,184)	(449)	—	(4,633)
Other comprehensive income	(1,280)	(143)	(82)	(1,505)
Balance, June 30, 2023	$ 177,476	$ 10,365	$ 4,758	$ 192,599

Accumulated depreciation	Directional drilling equipment	Shop and automotive equipment	Other	Total
Balance, December 31, 2022	$ 64,373	$ 2,794	$ 597	$ 67,764
Depreciation	16,671	735	277	17,683
Disposals	(1,765)	(222)	—	(1,987)
Other comprehensive income	(260)	(29)	(7)	(296)
Balance, June 30, 2023	$ 79,019	$ 3,278	$ 867	$ 83,164

Net book value	Directional drilling equipment	Shop and automotive equipment	Other	Total
Balance, December 31, 2022	$ 100,443	$ 6,471	$ 1,616	$ 108,530
Balance, June 30, 2023	$ 98,457	$ 7,087	$ 3,891	$ 109,435

5. Intangibles and goodwill

Cost	Customer Relationships	Brand Name	Non-Compete Agreements	RSS Licenses	Technology	Total	Goodwill
Balance, December 31, 2022	$ 22,500	$ 7,048	$ 779	$ 8,419	$ 5,386	$ 44,132	$ 39,395
Additions	—	—	—	—	144	144	—
Other comprehensive income	(518)	(162)	(18)	(194)	—	(892)	(907)
Balance, June 30, 2023	$ 21,982	$ 6,886	$ 761	$ 8,225	$ 5,530	$ 43,384	$ 38,488

Accumulated amortization	Customer Relationships	Brand Name	Non-Compete Agreements	RSS Licenses	Technology	Total	Goodwill
Balance, December 31, 2022	$ 1,743	$ 219	$ 72	$ 464	$ 3,123	$ 5,621	$ —
Amortization	1,864	234	77	523	314	3,012	—
Other comprehensive income	(72)	(9)	(3)	(20)	—	(104)	—
Balance, June 30, 2023	$ 3,535	$ 444	$ 146	$ 967	$ 3,437	$ 8,529	$ —

Net book value		Customer Relationships		Brand Name		Non-Compete Agreements		RSS Licenses		Technology		Total		Goodwill
Balance, December 31, 2022	$	20,757	$	6,829	$	707	$	7,955	$	2,263	$	38,511	$	39,395
Balance, June 30, 2023	$	18,447	$	6,442	$	615	$	7,258	$	2,093	$	34,855	$	38,488
Remaining amortization in years		4.9		13.9		3.9		6.9		3.9				n/a

6. Right-of-use assets and lease liabilities

Right-of-use assets

Balance, December 31, 2022	$	12,178
Additions		247
Derecognition		(44)
Depreciation		(1,653)
Impact of leasehold incentives		(495)
Other comprehensive income		(64)
Balance, June 30, 2023	$	10,169

Lease liabilities

Balance, December 31, 2022	$	17,880
Additions		247
Derecognition		(44)
Interest		419
Payments		(2,307)
Other comprehensive income		(122)
Balance, June 30, 2023		16,073
Less: lease liabilities, current		(3,222)
Lease liabilities, long-term	$	12,851

7. Loans and borrowings

As of		June 30, 2023		December 31, 2022
Syndicated Operating Facility	$	—	$	13,000
Syndicated Term Facility		59,200		66,600
HASCAP loan		880		935
Total loans and borrowings		60,080		80,535
Less: HASCAP loan, current		(880)		(935)
Less: Syndicated Term Facility, current		(14,800)		(14,800)
Loans and borrowings, current		(15,680)		(15,735)
Loans and borrowings, long-term	$	44,400	$	64,800

During the six months ended June 30, 2023, the Company repaid its balance owing on the Syndicated Operating Facility of $13,000. In addition, the Company made contractual repayments totaling $7,400 related to its Syndicated Term Facility reducing the carrying value to $59,200 as at June 30, 2023. As at June 30, 2023, a $10,000 Revolving Operating Facility remained undrawn. In addition, the Company continues to hold a Highly Affected Sectors Credit Availability Program ("HASCAP") loan.

At June 30, 2023, the Company was in compliance with its financial covenants, which were as follows:

- Consolidated Funded Debt to Consolidated Credit Agreement EBITDA ratio shall not exceed 2.5.0:1; and
- Consolidated Fixed Charge Coverage ratio shall not be less than 1.25:1

8. Share capital

An unlimited number of common shares and preferred shares (issuable in series) are authorized.

	Number (000s)		Amount
Balance, December 31, 2022	224,124	$	180,484
Issued on exercise of warrants	18,307		15,210
Contributed surplus on warrants exercised	—		2,976
Issued on exercise of stock options	769		159
Contributed surplus on options exercised	—		94
Balance, June 30, 2023	243,200	$	198,923

Stock options

A summary of the Company's outstanding stock options as at June 30, 2023 is as follows:

	Number (000s)		Weighted average exercise price
Balance, December 31, 2022	20,672	$	0.61
Granted	1,925	$	0.94
Exercised	(769)		0.21
Expired or forfeited	(2,658)		0.59
Balance, June 30, 2023	19,170		0.66
Exercisable, June 30, 2023	2,818	$	0.39

During the six months ended June 30, 2023, the Company granted 1,825,000 and 100,000 stock options to certain officers and employees at exercise prices of $0.95 per stock option and $0.84 per stock option, respectively. These stock options are set to expire on April 26, 2026 and May 9, 2026, respectively. The stock options will vest in one-third tranches twelve months, eighteen months and twenty-four months from the grant date, respectively.

The range of exercise prices for the options outstanding as at June 30, 2023 is as follows:

	Outstanding				Exercisable			
Exercise price range	Number (000s)	Weighted average remaining life (years)		Weighted average exercise price	Number (000s)	Weighted average remaining life (years)		Weighted average exercise price
$0.12 to $0.25	383	0.29	$	0.12	383	0.29	$	0.12
$0.26 to $0.50	3,062	1.04	$	0.44	2,308	1.00	$	0.42
$0.51 to $0.87	13,475	2.12	$	0.67	127	1.71	$	0.77
$0.87 to $1.18	2,250	2.76	$	0.99	—	—	$	—
Total	19,170	1.98	$	0.66	2,818	0.94	$	0.39

Warrants

A summary of the Company's warrants granted related to acquisitions and private placements as at June 30, 2023 is as follows:

	Number (000s)		Weighted average exercise price
Balance, December 31, 2022	20,362	$	0.81
Exercise of warrants	(18,307)		(0.83)
Expiry of warrants	(55)		(0.85)
Balance, June 30, 2023	2,000	$	0.60

During the six months ended June 30, 2023, 17,731,888 of the April 2022 bought deal offering warrants and 575,000 of the February 2021 private placement warrants were exercised at $0.85 per warrant and $0.24 per warrant totaling $15,072 and $138 in gross cash proceeds, respectively. On April 26, 2023, the remaining 55,462 of the April 2022 bought deal offering warrants expired.

As at June 30, 2023, the 2,000,000 warrants related to the Precision Drilling acquisition were outstanding. Subsequent to June 30, 2023, the warrants were exercised at $0.60 per warrant for gross cash proceeds of $1,200.

9. Net income (loss) per share

	Three months ended June 30, 2023	Three months ended June 30, 2022	Six months ended June 30, 2023	Six months ended June 30, 2022
Net income (loss)	$ 2,416	$ (2,824)	$ 3,210	$ (581)
Outstanding shares, beginning of the period	225,278	100,319	224,124	80,200
Effect of share capital issued during the period	13,116	28,881	7,392	30,153
Weighted average common shares (basic)	238,394	129,200	231,516	110,353
Effect of outstanding stock options and warrants	2,259	2,698	7,047	2,616
Weighted average common shares (diluted)	240,653	131,898	238,563	112,969
Net income (loss) per share - basic and diluted	$ 0.01	$ (0.02)	$ 0.01	$ (0.01)

During the three and six months ended June 30, 2023, 15,724,566 and 4,050,766 stock options and warrants, respectively (2022 – 3,286,600 and 3,286,600) were excluded from the diluted weighted average number of common shares calculation as their effect was anti-dilutive.

10. Operating segments

The Company has two operating segments based on its geographic operating locations of Canada and U.S. and a non-operating segment, for joint corporate costs ("Corporate services"). The Company determines its reportable segments based on internal information regularly reviewed by management to allocate resources and assess performance. The Corporate services segment is comprised of costs which are managed on a group basis and are not allocated to the operating segments. The Corporate services segment primarily consists of general and administrative expenses, foreign exchange gains (losses), interest expenses and acquisition and reorganization costs.

	Three months ended June 30, 2023				Three months ended June 30, 2022			
	Canada	U.S.	Corporate services	Total	Canada	U.S.	Corporate services	Total
Revenues	$ 21,515	$ 93,543	$ —	$ 115,058	$ 13,091	$ 14,561	$ —	$ 27,652
Income (loss) before income taxes	$ (1,015)	$ 10,131	$ (4,524)	$ 4,592	$ (3,667)	$ 2,820	$ (2,733)	$ (3,580)

	Six months ended June 30, 2023				Six months ended June 30, 2022			
	Canada	U.S.	Corporate services	Total	Canada	U.S.	Corporate services	Total
Revenues	$ 66,858	$ 175,865	$ —	$ 242,723	$ 38,490	$ 23,547	$ —	$ 62,037
Income (loss) before income taxes	$ 3,202	$ 13,547	$ (10,956)	$ 5,793	$ (1,834)	$ 4,387	$ (3,890)	$ (1,337)

	As at June 30, 2023				As at December 31, 2022			
	Canada	U.S.	Corporate services	Total	Canada	U.S.	Corporate services	Total
Total non-current assets	$ 56,158	$ 127,029	$ 9,760	$ 192,947	$ 58,575	$ 129,190	$ 10,849	$ 198,614
Property, plant and equipment	$ 56,158	$ 53,055	$ 222	$ 109,435	$ 58,575	$ 49,704	$ 251	$ 108,530

There are no material differences in the basis of accounting or the measurement of income, assets and liabilities between the Company and reported segment information. Revenues and expenses are attributed to geographical areas based on the location in which the services are rendered. The segment presentation of assets is based on legal owner of the assets which bears the related depreciation and amortization expenses.

Seasonality of operations

A portion of the Company's operations are carried on in Western Canada where activity levels in the oilfield services industry are subject to a degree of seasonality. Operating activities in Western Canada are generally lower during "spring breakup" which normally commences in mid to late-March and continues through to May. Operating activities generally peak in the winter months from December until mid to late-March. Additionally, volatility in the weather and temperatures not only during this period, but year-round, can create additional unpredictability in operational results. Activity levels in the oil and natural gas basins in the U.S. are not subject to the same level of seasonality that occurs in the Western Canada region.

11. Contractual obligations and contingencies

As at June 30, 2023, the Company's commitment to purchase property, plant and equipment is approximately $8,003. Cathedral anticipates expending these funds in 2023 Q3 and Q4 subject to supply chain delays.

The Company is involved in various legal claims associated with the normal course of operations. The Company believes that any liabilities that may arise pertaining to such matters would not have a material impact on its financial position.

The Company also holds six letters of credit totaling $1,895 related to rent payments, corporate credit cards and a utilities deposit.

12. Subsequent events

On July 11, 2023, Cathedral, through a wholly-owned subsidiary, acquired Rime Downhole Technologies, LLC ("Rime"), a privately-held, Texas-based, engineering business that specializes in building products for the downhole measurement-while-drilling ("MWD") industry (the "Rime acquisition") in exchange for approximately USD $41,000 comprised of: (a) the payment of USD $21,000 in cash; and (b) the issuance of USD $20,000 of subordinated exchangeable promissory notes ("EP Notes") that are exchangeable into a maximum of 24,570,000 common shares in the capital of Cathedral ("EP Shares") at a deemed price of CAD $1.10 per common share.

The EP Notes have a three-year term and accrue interest payable quarterly at a rate of 5% per annum. Any time prior to expiry of the EP Notes, if the 20-day volume weighted average trading price of the common shares of Cathedral ("Common Shares") equals or exceeds CAD $1.10 per Common Share, Cathedral may cause the exchange of the EP Notes for Common Shares. Cathedral and the holders of the EP Notes may agree to an earlier exchange of the EP Notes into Common Shares. In addition to the statutory hold periods applicable to the EP Shares under Canadian and U.S. securities laws, the parties agreed to contractual restrictions on resale of any EP Shares as follows: 33% of the EP Shares are restricted until July 11, 2024; a further 33% of the EP Shares are restricted until July 11, 2025; and a further 34% of the EP Shares are restricted until July 11, 2026, subject to certain exceptions contained in the terms governing the EP Notes.

In connection with the Rime acquisition, the Company entered into a three-year term credit facility (the "Credit Facility"), replacing its existing credit facility with its syndicate of lenders led by ATB Financial ("ATB"). The Credit Facility provides an approximate $137,000 principal amount comprised of: i) a $59,000 Syndicated Term Facility (replacing the existing Syndicated Term Facility), ii) a new USD $21,000 term loan, repayable in equal quarterly installments over a five-year amortization period, iii) a $35,000 Syndicated Operating Facility (previously $15,000), and iv) a $15,000 Revolving Operating Facility (previously $10,000). The Credit Facility was utilized to replace and repay Cathedral's existing credit facility. The interest rate and financial covenants remained unchanged from the existing credit facility.