# Tethys Petroleum Limited

Condensed Consolidated Interim Financial Statements
(Unaudited)
**June 30, 2019**

**NOTICE OF NO AUDITOR REVIEW
OF CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS**

Under National Instrument 51-102, Part 4.3 (3) (a), if an auditor has not performed a review of the financial statements, they must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor. The accompanying condensed consolidated interim financial statements of Tethys Petroleum Limited have been prepared by and are the responsibility of the Company's management and approved by the Board of Directors of the Company. The Company's independent auditor has not performed a review of these condensed consolidated interim financial statements.

## Contents

## Responsibility Statement of the Directors in Respect of the Condensed Consolidated Interim Financial Statements

We confirm on behalf of the Board that to the best of our knowledge, these condensed consolidated interim financial statements have been prepared in accordance with IAS 34 Interim Financial Reporting.

We draw attention to the section entitled “Going Concern” in Note 1 to the condensed consolidated interim financial statements which describes the material uncertainties relating to the Company’s adoption of the going concern basis in preparing the condensed consolidated interim financial Statements for the period ended June 30, 2019.

For and on behalf of the Board

**W. Wells**
Chairman
August 14, 2019

**A. Ogunsemi**
Director
August 14, 2019

# Tethys Petroleum Limited

Condensed Consolidated Interim Statements of Financial Position (unaudited)

(in thousands of US dollars)

| | | As at | |
|---|---|---|---|
| | **Note** | **June 30, 2019** | **December 31, 2018** |
| **Non-current assets** | | | |
| Intangible assets | | 29,275 | 29,423 |
| Property, plant and equipment | | 69,950 | 71,183 |
| Restricted cash | | 3 | 3 |
| Trade and other receivables | | 1,437 | 1,423 |
| | | **100,665** | **102,032** |
| **Current assets** | | | |
| Cash and cash equivalents | | 4,002 | 3,460 |
| Trade and other receivables | | 5,406 | 2,932 |
| Inventories | | 594 | 307 |
| Restricted cash | | - | 1 |
| | | **10,002** | **6,700** |
| **Total assets** | | **110,667** | **108,732** |
| **Non-current liabilities** | | | |
| Financial liabilities - borrowings | | - | 5,281 |
| Deferred tax | | 8,377 | 8,214 |
| Provisions | | 1,617 | 1,402 |
| | | **9,994** | **14,897** |
| **Current liabilities** | | | |
| Financial liabilities - borrowings | | 36,850 | 28,604 |
| Current taxation | | 604 | 604 |
| Trade and other payables | | 7,755 | 8,370 |
| | | **45,209** | **37,578** |
| **Total liabilities** | | **55,203** | **52,475** |
| **Equity** | | | |
| Share capital | | 6,832 | 6,832 |
| Share premium | | 360,769 | 360,769 |
| Other reserves | | 45,556 | 45,556 |
| Accumulated deficit | | (357,693) | (356,900) |
| **Total equity** | | **55,464** | **56,257** |
| **Total equity and liabilities** | | **110,667** | **108,732** |
| Going concern | 1 | | |

The notes on pages 6 to 9 form part of these condensed consolidated interim financial statements. The condensed consolidated interim financial statements were approved by the Board on August 14, 2019 and were signed on its behalf.

| | |
|---|---|
| **W. Wells** | **A. Ogunsemi** |
| Chairman | Director |
| August 14, 2019 | August 14, 2019 |

# Tethys Petroleum Limited

Condensed Consolidated Interim Statements of Comprehensive Income (Loss) (unaudited)

(in thousands of US dollars except per share information)

| | | Three months ended June 30 | | Six months ended June 30 | |
|---|---|---|---|---|---|
| | **Note** | **2019** | **2018** | **2019** | **2018** |
| Sales and other revenues | 3 | 3,570 | 2,017 | 8,227 | 3,933 |
| Production expenses | | (966) | (1,135) | (1,704) | (2,180) |
| Depreciation, depletion and amortisation | | (1,290) | (1,454) | (2,541) | (4,169) |
| Administrative expenses | | (772) | (912) | (1,388) | (1,899) |
| Share based payments | | - | (16) | - | (33) |
| Other gains | | - | - | 193 | - |
| Foreign exchange (loss)/gain | | (31) | 559 | (239) | 293 |
| Finance costs | | (1,615) | (1,378) | (3,175) | (2,991) |
| | | (4,674) | (4,336) | (8,854) | (10,979) |
| **Loss before tax from continuing operations** | | **(1,104)** | **(2,319)** | **(627)** | **(7,046)** |
| Taxation | | (429) | 425 | (166) | 816 |
| **Loss from continuing operations and total comprehensive loss** | | **(1,533)** | **(1,894)** | **(793)** | **(6,230)** |
| **Loss per share attributable to shareholders:** | | | | | |
| Basic - from continuing operations (USD) | 4 | (0.02) | (0.04) | (0.01) | (0.12) |
| Diluted - from continuing operations (USD) | 4 | (0.01) | (0.04) | (0.01) | (0.12) |

No dividends were paid or are declared for the period (2018: none).

The notes on pages 6 to 9 form part of these condensed consolidated interim financial statements.

# Tethys Petroleum Limited

Condensed Consolidated Interim Statements of Changes in Equity (unaudited)

(in thousands of US dollars)

| | Attributable to shareholders | | | | | |
|---|---|---|---|---|---|---|
| | **Share capital** | **Share premium** | **Accumulated deficit** | **Other reserves** | **Non-controlling interest** | **Total equity** |
| **At January 1, 2018** | **5,081** | **358,444** | **(357,357)** | **43,856** | **(2,082)** | **47,942** |
| Comprehensive loss for the period | - | - | (6,230) | - | - | |
| **Transactions with shareholders** | | | | | | |
| Share-based payments | - | - | - | 33 | - | |
| Total transactions with shareholders | - | - | - | 33 | - | |
| **At June 30, 2018** | **5,081** | **358,444** | **(363,587)** | **43,889** | **(2,082)** | **41,745** |
| **At January 1, 2019** | **6,832** | **360,769** | **(356,900)** | **45,556** | **-** | **56,257** |
| Comprehensive income for the period | - | - | (793) | - | - | (793) |
| **At June 30, 2019** | **6,832** | **360,769** | **(357,693)** | **45,556** | **-** | **55,464** |

Other reserves include reserves arising on the issuance of options, warrants and compound instruments and are denoted together as “other reserves” on the consolidated statement of financial position. These reserves are non-distributable.

The notes on pages 6 to 9 form part of these condensed consolidated interim financial statements.

# Tethys Petroleum Limited

Condensed Consolidated Interim Statements of Cash Flows (unaudited)

(in thousands of US dollars)

| | Three months ended June 30 | | Six months ended June 30 | |
|---|---|---|---|---|
| | **2019** | **2018** | **2019** | **2018** |
| **Cash flow from operating activities** | | | | |
| Loss before tax from continuing operations | (1,104) | (2,319) | (627) | (7,046) |
| Adjustments for: | | | | |
| Share based payments | - | 16 | - | 33 |
| Net finance cost | 1,615 | 1,378 | 3,175 | 2,991 |
| Depreciation, depletion and amortisation | 1,290 | 1,454 | 2,541 | 4,169 |
| Other gains and losses | - | - | (193) | - |
| Net unrealised foreign exchange gain | - | (45) | - | - |
| Net change in working capital | 1,518 | 45 | (2,515) | 441 |
| **Cash generated from operating activities** | **3,319** | **529** | **2,381** | **588** |
| Corporation tax paid | (2) | - | (2) | - |
| **Net cash generated from operating activities** | **3,317** | **529** | **2,379** | **588** |
| Cash flow from investing activities: | | | | |
| Proceeds from assets held for sale | - | 3,498 | - | 3,498 |
| Expenditure on exploration and evaluation assets | (4) | (13) | (6) | (301) |
| Expenditure on property, plant and equipment | (854) | (352) | (1,308) | (861) |
| Movement in restricted cash | - | 1 | 1 | 2 |
| Movement in advances to construction contractors | - | 3 | - | 2 |
| Movement in value added tax receivable | 5 | 262 | (1) | 170 |
| Net change in working capital | (859) | (139) | (904) | 402 |
| **Net cash (used in)/from investing activities** | **(1,712)** | **3,260** | **(2,218)** | **2,912** |
| Cash flow from financing activities: | | | | |
| Repayment of borrowings | - | (2,864) | - | (2,864) |
| Interest paid on borrowings | - | (284) | - | (284) |
| **Net cash used in financing activities** | **-** | **(3,148)** | **-** | **(3,148)** |
| Effects of exchange rate changes on cash and cash equivalents | 18 | (203) | 381 | 38 |
| **Net increase in cash and cash equivalents** | **1,623** | **438** | **542** | **390** |
| Cash and cash equivalents at beginning of the period | 2,379 | 29 | 3,460 | 77 |
| **Cash and cash equivalents at end of the period** | **4,002** | **467** | **4,002** | **467** |

The notes on pages 6 to 9 form part of these condensed consolidated interim financial statements.

## 1 General information and going concern

Tethys Petroleum Limited is incorporated in the Cayman Islands and the address of the Company's registered office is 190 Elgin Avenue, George Town, Grand Cayman, KY1-9005, Cayman Islands. Tethys is an oil and gas company operating within the Republic of Kazakhstan. Tethys' principal activity is the acquisition of and exploration and development of crude oil and natural gas fields.

The Company has its primary listing on the NEX Board of the Toronto Venture Exchange. The Company is also listed on the Kazakhstan Stock Exchange ("KASE").

*Going concern*

The Management and the Board has considered the Company's current activities, funding position and projected funding requirements for the period of at least twelve months from the date of approval of the condensed consolidated interim financial statements in determining the ability of the Company to adopt the going concern basis in preparing the condensed consolidated interim financial statements for the six months ended June 30, 2019. The Company reported a loss of $0.8 million for the six months ended June 30, 2019 (2018 full year: $4.5 million) and an accumulated deficit as at that date of $357.7 million (December 31, 2018: $356.9 million) and negative working capital of $35.2 million (December 31, 2018: negative $30.9 million). In addition, the Company reported cash flow from operating activities of $2.4 million for the six months ended June 30, 2019 (2018 full year: $1.0 million).

Due to the facts and circumstances described below, there are material uncertainties that cast significant doubt on the Company's ability to continue as a going concern.

The Company currently does not have sufficient funding to fund its obligations for the next twelve months should all lenders call in their debts at once. The Company is currently in default on loan obligations as disclosed further in note 15 of the 2018 consolidated financial statements and has various commitments and contingencies as disclosed in note 21 of the 2018 consolidated financial statements. The Company has been in discussions and negotiations with the related counterparties to restructure the repayments that are currently due. In order to continue as a going concern, the Company will need to agree adequate terms with counterparties to restructure repayments. There is material uncertainty about the outcome of these negotiations which casts significant doubt on the Company's ability to continue as a going concern.

In order to support the Company's short term liquidity position and improve the Company's financial situation, we will need to:

- Complete the proposed change of control transaction with Jaka Partners FZC;
- Maintain the improved oil and gas pricing received since September 2018 and work to improve prices further during 2019;
- Ensure continuity of gas production operations and optimise production volumes by completing the upgrade of the gas compression facility;

- Retain exploration & production contracts by fulfilling work program obligations including successfully drilling new oil wells in the Akkulka and Kul-bas contract areas; and

- Formalise repayment terms for overdue debts to lenders.

In September and October 2018, the Company announced it had raised funds of approximately $4.1 million from the issuance of shares to a new investor. Some of these proceeds have been used to upgrade gas compressor facilities and to tie in previously drilled gas wells to increase production and cash flow.

On March 19, 2019 the Company announced that it had signed a definitive agreement with the same investor for the acquisition of control of the Company at a significant premium to the trading price of the Company's shares before the proposed transaction was first announced in December 2018. The proposed transaction is subject to a number of approvals which are outside the Company's control although, if completed, it is anticipated that the new investor will provide the Company with the financial support required to continue to operate as a going concern. There is material uncertainty as to whether the proposed transaction will be completed and result in additional funding being made available to the Company. This casts significant doubt on the ability of the Company to continue as a going concern.

The Company's ability to continue as a going concern is dependent upon its ability to secure and deliver the above-described additional funding required to meet capital expenditure programs including its contractual obligations, its ability to renew and maintain access to debt facilities, equity issuances, manage risks associated with oil & gas prices and potential Tenge devaluation and ability to generate positive cash flows from operations. These financial statements do not reflect the adjustments to the carrying values of assets and liabilities and the reported revenues, expenses and balance sheet classifications that would be necessary if the Company was unable to realise its assets and settle its liabilities as a going concern in the normal course of operations. Such adjustments could be material.

## 2 Basis of preparation and accounting policies

The condensed consolidated interim financial statements of the Company are prepared on a going concern basis under the historical cost convention except as modified by the revaluation of financial assets and financial liabilities at fair value through profit and loss and are in accordance with International Financial Reporting Standards ("IFRSs") issued by the IASB and IFRIC interpretations issued by the IFRS Interpretations Committee and effective or issued and early adopted as at the time of preparing these condensed consolidated interim financial statements.

These unaudited condensed consolidated interim financial statements have been prepared in accordance with International Accounting Standard 34 "Interim Financial Reporting" as applicable to interim financial reporting and do not include all the information and disclosures required in the annual financial statements and should be read in conjunction with the annual consolidated financial statements reported for the year ended December 31, 2018.

The condensed consolidated interim financial statements are presented in United States Dollars ("$").

(in thousands of US dollars)

*New accounting policies*

There were no new and revised standards adopted by the Company during the six months ended June 30, 2019 that had an impact on the condensed consolidated interim financial statements.

*Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Company*

There are no significant new or amended standards that have been early adopted by the Company.

## 3 Segmental Reporting

*Geographical segments*

Management has determined the operating segments based on the reports reviewed by the Board of Directors that are used to make strategic decisions. Reports provided to the Board of Directors with respect to segment information are measured in a manner consistent with that of the condensed consolidated interim financial statements. The assets and liabilities are allocated based on the operations of the segment and for assets, the physical location of the asset.

The Board of Directors consider the business from predominantly a geographical perspective and the Company currently operates in two geographical markets: Kazakhstan and Rest of World (or Corporate).

In Kazakhstan, the Company is producing oil and gas from the Kyzyloi and Akkulka fields and is undertaking exploration and evaluation activity in the Kul-bas field. The Company also operates a corporate segment which provides loan funding for development activities in Kazakhstan.

The following is an analysis of the Company's revenue, results and assets by reportable segment for the six months ended June 30, 2019:

| | Kazakhstan | Corporate | Total | Eliminations | Group |
|---|---|---|---|---|---|
| Gas sales | 7,647 | - | 7,647 | - | 7,647 |
| Oil sales | 580 | - | 580 | - | 580 |
| **Segment revenue and other income** | **8,227** | **-** | **8,227** | **-** | **8,227** |
| **Loss before taxation** | 2,755 | (3,382) | (627) | - | (627) |
| Taxation | (166) | - | (166) | - | (166) |
| **Loss for the period** | **(2,589)** | **(3,382)** | **(793)** | **-** | **(793)** |
| Total assets | 110,313 | 109,384 | 219,697 | (109,030) | 110,667 |
| Total liabilities | 126,551 | 37,682 | 164,233 | (109,030) | 55,203 |
| Expenditure on exploration & evaluation assets, property, plant and equipment | 1,314 | - | 1,314 | - | 1,314 |
| Depreciation, depletion & amortization | 2,541 | - | 2,541 | - | 2,541 |

The following is an analysis of the Company's revenue, results and assets by reportable segment for the six months ended June 30, 2018:

| | Kazakhstan | Corporate | Total | Eliminations | Group |
|---|---|---|---|---|---|
| Gas sales | 2,587 | - | 2,587 | - | 2,587 |
| Oil sales | 1,335 | - | 1,335 | - | 1,335 |
| Other income | 11 | - | 11 | - | 11 |
| Other operating income | - | 54 | 54 | (54) | - |
| **Segment revenue and other income** | **3,933** | **54** | **3,987** | **(54)** | **3,933** |
| **Loss before taxation** | (3,178) | (3,868) | (7,046) | - | (7,046) |
| Taxation | 829 | (13) | 816 | - | 816 |
| **Loss for the period** | **(2,349)** | **(3,881)** | **(6,230)** | **-** | **(6,230)** |
| Total assets | 102,598 | 115,133 | 217,731 | (104,109) | 113,622 |
| Total liabilities | 127,903 | 48,083 | 175,986 | (104,109) | 71,877 |
| Expenditure on exploration & evaluation assets, property, plant and equipment | 1,162 | - | 1,162 | - | 1,162 |
| Depreciation, depletion & amortization | 4,139 | 30 | 4,169 | - | 4,169 |

## 4 Loss per share

| | | Three months ended June 30 | | Six months ended June 30 | |
|---|---|---|---|---|---|
| **Continuing operations** | **Units** | **2019** | **2018** | **2019** | **2018** |
| Loss for the purpose of basic and diluted loss attributable to ordinary shareholders | $'000 | (1,533) | (1,894) | (793) | (6,230) |
| Weighted average shares - basic | 000s | 68,324 | 50,814 | 68,324 | 50,814 |
| Loss per share - basic | $ | (0.02) | (0.04) | (0.01) | (0.12) |
| Weighted average shares - diluted | 000s | 102,471 | 50,814 | 102,471 | 50,814 |
| Loss per share - diluted | $ | (0.01) | (0.04) | (0.01) | (0.12) |

Basic loss per share is calculated by dividing the loss attributable to shareholders of the Company by the weighted average number of ordinary shares in issue during the year. Diluted per share information is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares.

# Tethys Petroleum Limited

Management's Discussion and Analysis
for the period ended June 30, 2019

## Contents

The following Management's Discussion and Analysis ("MD&A") is dated August 14, 2019 and should be read in conjunction with the Company's unaudited condensed consolidated interim financial statements and related notes for the period ended June 30, 2019 as well as the audited consolidated financial statements and the MD&A for the year ended December 31, 2018. The accompanying unaudited condensed consolidated interim financial statements of the Company have been prepared by management and approved by the Company's Audit Committee and Board of Directors. The 2018 annual audited consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board. The unaudited condensed consolidated interim financial statements have been prepared in accordance with International Accounting Standard 34 "Interim Financial Reporting". Additional information relating to the Company can be found on the SEDAR website at *www.sedar.com* and the Company's website at *www.tethys-group.com*.

Readers should also read the "Forward-Looking Statements" legal advisory wording contained at the end of this MD&A.

## Nature of Business

Tethys Petroleum Limited and its subsidiaries (collectively "Tethys" or "the Company") is an oil and gas company operating within the Republic of Kazakhstan. Tethys' principal activity is the exploration and development of crude oil and natural gas fields. The address of the Company's registered office is 190 Elgin Avenue, George Town, Grand Cayman, KY1-9005, Cayman Islands. The domicile of Tethys is the Cayman Islands where it is incorporated.

The Company has its primary listing on the NEX Board of the Toronto Venture Exchange. The Company is also listed on the Kazakhstan Stock Exchange ("KASE").

## Financial highlights

**(All references to $ are United States dollars unless otherwise noted and tabular amounts are in thousands, unless otherwise stated)**

| | Quarter ended June 30 | | | Six months ended June 30 | | |
|---|---|---|---|---|---|---|
| | 2019 | 2018 | Change | 2019 | 2018 | Change |
| Oil and gas sales and other revenues | 3,570 | 2,017 | 77% | 8,227 | 3,933 | 109% |
| Loss for the period from continuing operations | (1,533) | (1,894) | (19%) | (793) | (6,230) | (87%) |
| Loss (USD) per share from continuing operations - basic | (0.02) | (0.04) | (50%) | (0.01) | (0.12) | (92%) |
| Adjusted EBITDA[1] | 1,801 | 529 | 240% | 5,089 | 147 | 3362% |

| | As at June 30 | | |
|---|---|---|---|
| | 2019 | 2018 | Change |
| Total assets | 110,667 | 113,622 | (3%) |
| Cash & cash equivalents | 4,002 | 467 | 757% |
| Short & long term borrowings | 36,850 | 32,103 | 15% |
| Total non-current liabilities | 9,994 | 14,359 | (30%) |
| Net debt[1] | 32,848 | 31,636 | 4% |
| Number of ordinary shares outstanding | 68,324,430 | 50,813,609 | 34% |

Note 1 Adjusted EBITDA and net debt are non-GAAP Measures, refer to page 18 for details.

### Second quarter 2019 versus second quarter 2018

- Oil and gas sales and other revenues increased by 77% to USD3.6 million from USD2.0 million due to significantly higher gas revenues. Gas revenues increased from USD1.3 to USD3.5 million due to 10% higher production and a 137% increase in price. Oil revenues reduced from USD0.7 million to USD0.1 million due to production ceasing in March 2019;
- The loss for the quarter was USD1.5 million compared to a loss of USD1.9 million in the second quarter of 2018. The loss was lower due to the higher gas revenue and lower production and administrative expenses in the current quarter although oil revenue was lower and finance costs were higher. The prior year quarter also included a larger foreign exchange gain and deferred tax credit;
- Adjusted EBITDA was USD1.8 million compared with USD0.5 million as a result of the higher gross margin from gas sales and lower production and general & administrative expenses offset by a loss from oil operations as a result of the cessation of oil production.

### Period to date

- Oil and gas sales and other revenues increased by 109% to USD8.2 million from USD3.9 million due to significantly higher gas revenues. Gas revenues increased from USD2.6 to USD7.6 million due to 15% higher production and a 157% increase in price. Oil revenues reduced from USD1.3 million to USD0.6 million due to production ceasing in March 2019;
- The loss for six months was USD0.8 million compared to a loss of USD6.2 million in the same period in 2018. The loss was lower due to the higher gas revenue and lower DD&A, production and administrative expenses in the current period although oil revenue was lower and finance costs were higher. The prior year period also included a larger foreign exchange gain and deferred tax credit;

## Financial highlights

- Adjusted EBITDA was USD5.1 million compared with USD0.1 million as a result of the higher gross margin from gas sales and lower production and general & administrative expenses offset by a loss from oil operations as a result of the cessation of oil production.

## Operational Highlights

| | Units | Quarter ended June 30 2019 | 2018 | Change | Six months ended June 30 2019 | 2018 | Change |
|---|---|---|---|---|---|---|---|
| **Kazakhstan** | | | | | | | |
| Oil | bopd | - | 614 | (100%) | 75 | 746 | (90%) |
| Gas | boe/d | 2,227 | 2,021 | 10% | 2,243 | 1,954 | 15% |
| **Total** | boe/d | **2,227** | **2,635** | **(15%)** | **2,318** | **2,700** | **(14%)** |
| ***Oil*** | | | | | | | |
| Net production | Bbls | - | 55,831 | (100%) | 13,496 | 135,048 | (90%) |
| Net revenue | USD'000 | 98 | 680 | (86%) | 580 | 1,335 | (57%) |
| Production costs | USD'000 | 614 | 653 | (6%) | 991 | 1,374 | (28%) |
| **Gross margin** | USD'000 | **(516)** | **27** | **(2011%)** | **(411)** | **(39)** | **954%** |
| Oil price net | $/bbl | 34.08 | 11.85 | 188% | 33.94 | 10.09 | 236% |
| Cost | $/bbl | n/a | 11.70 | n/a | 73.43 | 10.17 | 622% |
| **Gross margin** | $/bbl | **n/a** | **0.15** | **n/a** | **(39.49)** | **(0.08)** | **49263%** |
| ***Gas*** | | | | | | | |
| Gross production | Mcm | 34,437 | 31,257 | 10% | 68,985 | 60,086 | 15% |
| Gas revenue net | $'000 | 3,473 | 1,335 | 160% | 7,647 | 2,587 | 196% |
| Production costs | $'000 | 352 | 471 | (25%) | 713 | 795 | (10%) |
| **Gross margin** | $'000 | **3,121** | **864** | **261%** | **6,934** | **1,792** | **286%** |
| Sales price net | $/Mcm | 102.55 | 43.36 | 137% | 112.54 | 43.76 | 157% |
| Cost | $/Mcm | 10.22 | 15.07 | (32%) | 10.34 | 13.23 | (22%) |
| **Gross margin** | $/Mcm | **92.33** | **28.29** | **226%** | **102.20** | **30.53** | **235%** |

## Oil

- Oil production ceased in March 2019 as the AKD-01 well stopped producing at economic levels and there was no production in Q2 2019. Production averaged 75 bopd for the six months to June 2019 compared with 746 bopd for the same period in 2018 reflecting a steady decline in production after an ESP was installed in May 2017 to maximise production over the well's remaining life;
- Oil production costs, which are mainly personnel costs, continued to be incurred in Q2 as the Company seeks to re-establish production from other wells. Production costs were $0.6 million for the quarter compared with $0.7 million in Q2 2018 and $1.0 million for the six months compared with $1.4 million for the same period in 2018, a reduction of 28%;
- Some sales from inventory were made in April 2019 at $34.08/bbl compared with an average of $11.85/bbl in Q2 2018 and for the six months they averaged $33.94/bbl compared with $10.09/bbl in 2018, an increase of 236% reflecting improved market pricing and the end of a fixed price contract.

## Gas

- Gas production for the quarter averaged 2,227 boe/d compared with 2,021 boe/d in Q2 2018, a 10% increase. For the six months gas production averaged 2,243 boe/d compared with 1,954 boe/d for the same period in 2018, an increase of 15%. The increases are due to new wells coming onto production and upgrading of gas compression facilities;
- Gas production cost per Mcm in the current quarter decreased to $10.22 from $15.07 in Q2 2018. For the six months the cost per Mcm reduced to $10.34 from $13.23.The reductions are due to due to lower overall production costs and the higher level of production;
- Gas was sold at a net average price equivalent to $102.55 per Mcm for the quarter compared with $43.36 in Q2 2018. For the six months the average sales price was $112.54 compared with

$43.76 in 2018. The increases reflect a significantly improved price from September 1, 2018 and a further price increase from January 1, 2019.

## Operational Review

### Outlook

The information provided under this heading is considered as forward looking information; as such please refer to page 21 – "*Forward Looking Statements*" of this MD&A.

The Company's objective is to become a leading oil and gas exploration and production Company in Central Asia, by exercising capital discipline, by generating cash flow from existing discoveries and by maturing large exploration prospects within our highly-attractive frontier acreage. The Company currently produces natural gas in Kazakhstan. The Company also produced oil in Kazakhstan until March 2019 and intends to recommence production if future drilling and workover activities are successful.

The Company's long-term ambition is to achieve a significant role in the production and delivery of hydrocarbons from the Central Asian region to local and global markets, especially to the Chinese market. In common with many oil and gas companies, in implementing its strategies, the Company regularly considers farm-out/farm-in and joint venture opportunities and new projects which provide synergy with the Company's activities. Meanwhile, the specific focus of management in the short term is to:

- Complete the change of control transaction with Jaka Partners FZC, as more particularly described on page 7;
- Maintain the improved oil and gas pricing received since September 2018 and work to improve prices further;
- Ensure continuity of gas production operations and optimise production volumes;
- Retain exploration & production contracts by fulfilling work program obligations including successfully drilling new oil wells in the Akkulka and Kul-bas contract areas; and
- Formalise repayment terms for overdue debts to lenders.

## Significant events and transactions for the six months ended June 30, 2019

- *Definitive Agreement for Acquisition of Control*

On March 29, 2019 the Company announced that it had signed a binding arrangement agreement (the "Definitive Agreement") with respect to a potential acquisition by Jaka Partners FSC (“Acquiror”) of Tethys’ outstanding ordinary shares ("Ordinary Shares") it does not already own pursuant to a scheme of arrangement under the Companies Law (2018 Revision) of the Cayman Islands (the "Companies Law"), and applicable Canadian securities laws. Such proposed acquisition is referred to hereafter as the "Proposed Transaction".

*1. Proposed Transaction Structure*

The Proposed Transaction will be carried out by way of a scheme of arrangement under the Companies Law, and effected pursuant to the Definitive Agreement, the terms and conditions of which are summarised below.

*2. Consideration*

Acquiror proposes to acquire up to 70% of the Ordinary Shares that it does not already own and to offer shareholders the opportunity to exchange up to 30% of the Ordinary Shares that the Acquiror does not already own for preferred shares ("Preferred Shares") on a one-for-one basis. Each shareholder who approved the Proposed Transaction could elect to:

(a) receive cash consideration of $0.60 per ordinary share in exchange for up to 70% of its Ordinary Shares and to also receive Preferred Shares in exchange for up to 30% of its Ordinary Shares;

(b) receive cash consideration of $0.60 per ordinary share exchange for up to 70% of its Ordinary Shares and retain the remaining Ordinary Shares;

(c) receive Preferred Shares in exchange for up to 30% of its Ordinary Shares and retain the remaining Ordinary Shares; or

(d) retain all of its Ordinary Shares.

Shareholders who did not make any election by the June 28, 2019 election deadline were deemed to have elected to retain all of their Ordinary Shares.

In total, holders of 5,857,462 Ordinary Shares elected to receive cash consideration and holders of 11,493,899 Ordinary Shares elected to receive Preferred Shares. Based on the current number of outstanding Ordinary Shares Acquiror would own approximately 33% of the resulting number of Ordinary Shares.

The Preferred Shares shall be non-voting and non-convertible, and shall be automatically redeemed by Tethys on the date that is three (3) years from the closing of the Proposed Transaction at a redemption price of $1.80 per Preferred Share (the "Redemption Amount"). To the extent that Tethys is unable to fund all or part of the payment of the Redemption Amount, Tethys will have an option to require Acquiror to provide funding for such payment by purchasing new ordinary shares in Tethys under a share purchase warrant or similar security (the "Warrant"). Pursuant to the Definitive Agreement, Acquiror’s obligations under the Warrant will be guaranteed by an affiliated company of Jaka, Inform Systems LLP.

Convertible securities (including options, warrants and convertible debt) shall remain outstanding post-closing and any such securities that are exercised or converted into Ordinary Shares prior to the record date of the special meeting shall entitle the holder to vote at such meeting.

The consideration offered per Ordinary Share of $0.60 per share and $1.80 per Preferred Shares represents premiums of approximately 320% and 960%, respectively to the Cdn$0.25 price of the Ordinary Shares on the NEX on December 19, 2018, the date before the Proposed Transaction was first announced.

*3. Stock Market Listing*

Upon completion of the Proposed Transaction, Tethys will seek to maintain a listing of its Ordinary Shares on the NEX, or other recognised securities exchange, and apply for a listing of the Preferred Shares. Listing will be subject to satisfaction of the rules of the NEX or other applicable exchange.

*4. Management and the Board*

As part of the Proposed Transaction, Acquiror will propose new directors as replacements for Mr. Mattias Sjoborg and Mr. William P. Wells. Acquiror shall ensure that following the completion of the Proposed Transaction, Tethys' board of directors, which would consist of at least three (3) members and will comply with all Canadian securities laws, including the rules of the NEX, applicable to public companies. In addition, upon completion of the Proposed Transaction, Mr. Sjoborg will resign from his position as Chief Executive Officer of Tethys. Annuity and Life Reassurance Ltd ("Annuity"), a company controlled by Mr. Wells, shall have a right to appoint a board observer and the right to inspect Tethys' corporate books, records and premises, for a period of three (3) years following the closing of the Proposed Transaction.

*5. Definitive Agreement*

The Definitive Agreement includes conditions precedent, representations and warranties, "fiduciary outs", covenants and provisions dealing with the mechanics of completing the Proposed Transaction.

The Definitive Agreement also contains certain minority protections such as restricting Tethys from issuing shares in excess of 18,000,000 shares and not pledging, selling, encumbering or disposing any of Tethys' assets for an agreed period of time.

The Definitive Agreement also contains a proposed settlement agreement which, subject to shareholder approval, Tethys will seek to enter into with Olisol Petroleum Ltd, Olisol Investments Ltd, Eurasia Gas Group LLP, DSFK Special Finance Company LLP and certain of their principals.

*6. Approval of the Proposed Transaction*

The Proposed Transaction has received the required approval of the NEX board of the TSX Venture Exchange (the "NEX"), shareholders at a special meeting convened for the purpose on June 28, 2019 and the Grand Court of the Cayman Islands on July 16, 2019. The approval of the Ministry of Energy of the Republic of Kazakhstan will also be required. It is anticipated that the Proposed Transaction will be completed around the end of August 2019.

Since becoming a Shareholder, the Acquiror has assisted the Company in addressing legacy issues and improving its business in a number of ways including, but not limited to, contributing to cost optimisation initiatives and assisting the Company with negotiating a new gas sale contract, resulting in a significantly higher gas price received by the Company for the gas it produces. Completing the Proposed Transaction will better align the Acquiror's interests with the Company's. The Company anticipates that following the effective Date, the Acquiror will increase the level of its contribution and the financial resources it makes available to the Company's business.

- *Drilling Plans for Klymene Prospect*

On June 25, 2019 the Company announced plans to drill the KBD-02 ("Klymene") prospect commencing mid-July 2019. This well is planned to be drilled to a depth of around 2,500 metres and is expected to take between 3 and 4 months to drill.

In 2014, the Company announced that it had commissioned an updated Oil Resource Report prepared by Gustavson Associates of the United States in accordance with the reporting requirements of NI 51-101 adopted by Canadian securities regulatory authorities. The report estimated gross Unrisked Mean Prospective Recoverable Oil Resources for the Klymene prospect totaling some 422 million barrels of oil.

The Klymene prospect is located in the Kul-Bas Exploration and Production Contract to the west of the Company's producing assets in the Akkulka Exploration Contract. The prospect was identified from 2D seismic and indicates a four-way closure with bright spots at two of three prospective stratigraphic levels within the Cretaceous and Jurassic sequence, both of which are productive in the Company's Doris oilfield some 60 km to the east.

- *Annual General and Special Meeting*

On June 28, 2019 the Company held its 2019 Annual General and Special Meeting and all resolutions were passed on a poll at the meeting including approval of the scheme of arrangement.

## Significant events and transactions subsequent to the period end

At the date of this MD&A there were no matters to report.

## Results of Operations and Operational Review - Kazakhstan

### Oil production – Akkulka Contract

| | 2019 | | | | | 2018 | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Gross fluid | | Net | Net production | | Gross fluid | | Net | Net production | |
| | m³ | barrels | barrels | days | bopd | m³ | barrels | barrels | days | bopd |
| Q1 | 29,462 | 185,312 | 13,496 | 90 | 150 | 52,034 | 327,285 | 79,217 | 90 | 880 |
| Q2 | - | - | - | 91 | - | 47,420 | 298,261 | 55,831 | 91 | 614 |
| **Total** | **29,462** | **185,312** | **13,496** | **181** | **75** | **99,454** | **625,546** | **135,048** | **181** | **746** |

*Oil operations update*

The Company ceased producing oil from the AKD01 well in March 2019 and there was no oil production in the quarter (Q2 2018: 614 bopd). The well had been producing with an ESP since May 2017 and thereafter production declined steadily and the water content reached 93% until production was no longer economic.

## **Operational Review** - continued

The Company reviewed its five year development in late 2018 following contract extensions through to March 2022 and the priority is to conduct the works required to fulfil the work programs and maintain the licence. Subject to funding, these works will include the drilling of three new deep wells AKD12, 13 and 14.

The Company recently worked over the nearby AKD03 well and whilst oil was confirmed present the water content was approximately 96%. Further works, including perforation of a different interval, are underway to decide if it will be possible to produce oil from this well.

Historically, the Company has produced oil under a pilot production license which requires all production to be sold domestically. Depending on the success of AKD12, 13 and 14 it may be possible to apply for a full commercial production licence in future if production reaches commercial levels and the necessary infrastructure is put in place such as a gas utilisation facility for associated gas and transportation. A commercial production licence would enable a percentage (possibly around 75%) of oil to be exported and higher prices to be realised.

### *Joint Venture – Aral Oil Terminal ("AOT")*

The Company has a 50% interest in the AOT which was previously used to tranship oil produced by the Company after it was trucked to the AOT by the Company's oil buyer. The Company is considering its options with regard to the future of its interest in the terminal.

## **Gas production – Kyzyloi and Akkulka Contracts**

| | 2019 | | | | 2018 | | | |
|---|---|---|---|---|---|---|---|---|
| | **Mcm** | **Mcf** | **Mcm/d** | **Boe/d** | **Mcm** | **Mcf** | **Mcm/d** | **Boe/d** |
| **Kyzyloi** | | | | | | | | |
| Q1 | 22,942 | 810,068 | 255 | 1,500 | 13,512 | 477,103 | 150 | 884 |
| Q2 | 24,247 | 856,167 | 266 | 1,568 | 17,057 | 602,295 | 187 | 1,103 |
| **Total** | **47,189** | **1,666,235** | **261** | **1,534** | **30,569** | **1,079,398** | **169** | **994** |
| **Akkulka** | | | | | | | | |
| Q1 | 11,606 | 409,812 | 129 | 759 | 15,317 | 540,827 | 170 | 1,001 |
| Q2 | 10,190 | 359,816 | 112 | 659 | 14,200 | 501,397 | 156 | 918 |
| **Total** | **21,796** | **769,628** | **120** | **709** | **29,517** | **1,042,224** | **163** | **960** |
| **Grand total** | **68,985** | **2,435,863** | **381** | **2,243** | **60,086** | **2,121,622** | **332** | **1,954** |

### *Gas operations update*

Gas production for the quarter increased by 10% to 378 Mcm per day compared with Q2 2018 reflecting the natural decline in production from existing wells offset by the increase in production from the connection of new wells as well as improvements to the gas compression facility.

During the period, the Company produced dry gas from a total of 16 wells at a depth of approximately 480-600m below surface, comprising ten producing wells in the Kyzyloi field and six in the Akkulka field.

The completed Bozoi-Shymkent-China gas pipeline means that Tethys now has two potential gas export routes that provide alternatives to sell its gas; the route taking gas to the more populous south eastern part of Kazakhstan and, ultimately to China, and the Bukhara-Urals trunk line that transports gas from Central Asia into Russia. Export to China, if this can be achieved, would allow the Company to realise a higher net sales price. The Company believes that the long-term price for gas will rise in the region, in particular dry gas exported via pipeline from Central Asia and that Chinese demand will increase over the medium to long term, especially with the substitution in China of a greater percentage of energy use from gas instead of coal.

On January 11, 2018 the Company announced that it had completed drilling seven new shallow gas wells out of the previously announced eight well program. All seven wells were tested successfully for gas at a depth of between 470 and 550 meters. In addition to the new wells drilled, one existing well was successfully worked over.

By January 1, 2018 five wells, comprising one existing well and four new wells, had been tied in to the Company's existing pipelines and added to production. The other new wells, which were furthest from the Company's existing pipelines, were connected in December 2018 and January 2019 resulting in average production of over 400 Mcm per day in February 2019.

There has been a longstanding need for repairs and parts replacement of parts at the compressor station to increase capacity. There are five compressors at the compressor station of which three are operating 24 hours a day at any one time. An offsite overhaul of Engine No. 3 was completed in Q1 2019. In addition, eight new cylinders were installed in January 2019 and a further four new cylinders in late March 2019. Together these works will ensure improved overall efficiency of gas production and continuity of operations should issues arise with one of the compressors.

*Exploration - update*

The KBD02 ("Klymene") prospect is planned to be drilled to a total depth of 2,500 metres targeting a large structure in the south west of the Kul-Bas block, and will target three horizons in the Lower Cretaceous and Upper Jurassic. The Klymene prospect has the potential to be an order of magnitude bigger than the Doris oil discovery and surrounding prospects in the Akkulka contract area which has produced over 4 million barrels of oil (the geographical area of the prospect is up to ten times the areal extent of the Doris oil field). It appears to have good four-way structural closure and positive amplitude effects which may be indicative of enhanced porosity on the seismic acquired and interpreted.

The extension of the appraisal period for the Kul-blas block for two years to November 11, 2019 includes an obligation to drill and test Klymene and on June 25, 2019 the Company announced plans to drill the prospect commencing mid-July 2019 which is expected to take between 3 and 4 months.

## Financial Review

### Summary of Quarterly Results

| | Q2, 2019 | Q1, 2019 | Q4, 2018 | Q3, 2018 | Q2, 2018 | Q1, 2018 | Q4, 2017 | Q3, 2017 |
|---|---|---|---|---|---|---|---|---|
| Oil & gas sales and other revenues | 3,570 | 4,656 | 3,895 | 2,511 | 2,017 | 1,916 | 2,070 | 2,593 |
| (Loss)/profit for the period | (1,533) | 743 | 11,074 | (324) | (1,894) | (4,333) | (36,302) | (2,879) |
| (Loss)/earnings ($) per share | (0.02) | 0.01 | 0.18 | (0.01) | (0.04) | (0.09) | (0.70) | (0.06) |
| Adjusted EBITDA[1] | 1,801 | 3,289 | 2,945 | 1,734 | 529 | (382) | (2,216) | 1,735 |
| Capital expenditure | 858 | 455 | 2,759 | 93 | 365 | 797 | 3,705 | 465 |
| Total assets | 110,667 | 110,817 | 108,732 | 112,251 | 113,622 | 115,679 | 116,923 | 149,076 |
| Cash & cash equivalents | 4,002 | 2,379 | 3,460 | 2,800 | 467 | 29 | 77 | 186 |
| Short & long term borrowings | 36,850 | 35,341 | 33,885 | 32,851 | 32,103 | 33,829 | 31,588 | 32,520 |
| Total non-current liabilities | 9,994 | 9,450 | 14,897 | 14,247 | 14,359 | 14,784 | 13,737 | 18,051 |
| Net debt[1] | 32,848 | 32,962 | 30,425 | 30,051 | 31,636 | 33,800 | 31,511 | 32,334 |
| Number of common shares outstanding | 68,324,430 | 68,324,430 | 68,324,430 | 63,517,013 | 50,813,609 | 50,813,609 | 50,813,609 | 50,813,609 |

Note 1 Adjusted EBITDA and net debt are non-GAAP Measures, refer to page 15 for details.

### Loss for the period

| | Quarter ended June 30 | | | Six months ended June 30 | | |
|---|---|---|---|---|---|---|
| | 2019 | 2018 | Change | 2019 | 2018 | Change |
| Sales and other revenue | 3,570 | 2,017 | 77% | 8,227 | 3,933 | 109% |
| Production expenses | (966) | (1,135) | (15%) | (1,704) | (2,180) | (22%) |
| Depreciation, depletion & amortization | (1,290) | (1,454) | (11%) | (2,541) | (4,169) | (39%) |
| Administrative expenses | (772) | (912) | (15%) | (1,388) | (1,899) | (27%) |
| Share based payments | - | (16) | (100%) | - | (33) | (100%) |
| Other gains | - | - | - | 193 | - | - |
| Foreign exchange (loss)/gain | (31) | 559 | (106%) | (239) | 293 | (182%) |
| Finance costs | (1,615) | (1,378) | 17% | (3,175) | (2,991) | 6% |
| | (4,674) | (4,336) | 8% | (8,854) | (10,979) | (19%) |
| **Loss before taxation from continuing operations** | **(1,104)** | **(2,319)** | **(52%)** | **(627)** | **(7,046)** | **(91%)** |
| Taxation | (429) | 425 | (201%) | (166) | 816 | (120%) |
| **Loss for the period** | **(1,533)** | **(1,894)** | **(19%)** | **(793)** | **(6,230)** | **(87%)** |

Loss after tax for the quarter was $1.5 million compared with $1.9 million in Q2 2018 and for the six months was $0.8 million compared with $6.2 million, the principal variances being:

- Higher gas revenues from higher production and significantly improved pricing, offset by lower oil revenue due to lower production from the AKD01 well which ceased producing in March 2019;
- Lower production expenses from lower oil production volumes and cost cutting;
- Lower administrative expenses from cost cutting;

- Lower depreciation, depletion and amortization charges following due to the lower oil production;

- A foreign exchange loss in 2019 compared with a gain in 2018, mainly from movements in the KZT:USD exchange rate;

- Higher finance costs due to accumulating loan interest and no loan payments being made, except for rig loans which were repaid in full in May 2018; and

- Deferred tax charge in 2019 periods compared with a deferred tax credit in 2018 due to accounting versus taxation timing differences.

Further variances between the two periods are summarized below together with a discussion of significant variances between the two periods.

## Sales & other revenue

| | Quarter ended June 30 | | | Six months ended June 30 | | |
|---|---|---|---|---|---|---|
| | **2019** | **2018** | **Change** | **2019** | **2018** | **Change** |
| Kazakhstan - Oil | 98 | 680 | (86%) | 580 | 1,335 | (57%) |
| Kazakhstan - Gas | 3,472 | 1,335 | 160% | 7,647 | 2,587 | 196% |
| Kazakhstan - Other | - | 2 | (100%) | - | 11 | (100%) |
| **Total** | **3,570** | **2,017** | **77%** | **8,227** | **3,933** | **109%** |

## Kazakhstan – Oil revenue and price

| | Gross sales bbls | Gross sales $000 | Realised price at wellhead $/bbl | VAT $000 | Net sales revenue $000 | Net price $/bbl |
|---|---|---|---|---|---|---|
| **2019** | | | | | | |
| Q1 | 14,213 | 540 | 37.99 | 58 | 482 | 33.91 |
| Q2 | 2,876 | 109 | 37.90 | 11 | 98 | 34.08 |
| **Total** | **17,089** | **649** | **37.98** | **69** | **580** | **33.94** |
| **2018** | | | | | | |
| Q1 | 74,850 | 734 | 9.80 | 79 | 655 | 8.75 |
| Q2 | 57,389 | 762 | 13.28 | 82 | 680 | 11.85 |
| **Total** | **132,239** | **1,496** | **11.31** | **161** | **1,335** | **10.09** |

- Under the pilot production licence oil can only be sold in the domestic Kazakhstan market and is priced in local currency, the Tenge;
- Sale price is determined at the wellhead where the oil is sold and therefore the Company incurred no transportation or marketing costs;
- Current quarter revenue benefited from a higher realised price of $34.08/bbl (Q2 2018: $11.85/bbl) and for the six months $33.94/bbl (H1 2018: $10.09/bbl) but this was more than offset by lower production sold. An ESP was installed in the AKD01 well in May 2017 and production has declined significantly since that time as the well reached the end of its producing life and ceased producing in March 2019, although there were some sales in April from inventory.

## **Financial Review -** continued

### Kazakhstan - Gas revenue and price

- Gas revenues were 160% higher for the quarter and 196% higher for the six months due to higher production, which was up by 10% and 15% respectively, following new wells coming online and a significantly higher gas price from September 1, 2018;
- Gas production for the quarter was sold at a Tenge price of KZT 43,701 per 1,000 cubic metres, including 12% VAT compared with KZT 16,000 per 1,000 cubic metres in Q2 2018, representing an increase of 273% in local currency terms. For the six months the average Tenge price was KZT 47,793 per 1,000 cubic metres, including 12% VAT compared with KZT 16,000 per 1,000 cubic metres for the same period in 2018, representing an increase of 299% in local currency terms. A higher gas price was received in the first quarter of 2019 compared with the second quarter due to seasonal factors;
- Gas contracts are subject to exchange rate risk – refer to page 20 – "*Sensitivities*".

### Production expenses

| | | **Quarter ended June 30** | | | **Six months ended June 30** | | |
|---|---|---|---|---|---|---|---|
| | **Units** | **2019** | **2018** | **Change** | **2019** | **2018** | **Change** |
| **Kazakhstan** | | | | | | | |
| Oil production | $000's | 614 | 653 | (6%) | 991 | 1,374 | (28%) |
| Gas production | $000's | 352 | 471 | (25%) | 713 | 795 | (10%) |
| Other | $000's | - | 11 | (100%) | - | 11 | (100%) |
| **Total** | $000's | **966** | **1,135** | **(15%)** | **1,704** | **2,180** | **(22%)** |
| ***Oil*** | | | | | | | |
| Net production | bbls | - | 55,831 | (100%) | 13,496 | 135,048 | (90%) |
| Cost | $/bbl | n/a | 11.70 | n/a | 73.43 | 10.17 | 622% |
| ***Gas*** | | | | | | | |
| Production | boe | 203,326 | 183,960 | 11% | 406,003 | 353,626 | 15% |
| Cost | $/boe | 1.73 | 2.56 | (32%) | 1.76 | 2.25 | (22%) |
| Weighted average cost per boe | $/boe | 4.75 | 4.73 | 0% | 4.06 | 4.44 | (9%) |

### Kazakhstan – oil production

Oil production costs, which are mainly personnel costs, continued to be incurred in Q2 as the Company seeks to re-establish production from other wells following production from the AKD01 well ceasing in March. Production costs were $0.6 million for the quarter compared with $0.7 million in Q2 2018 and $1.0 million for the six months compared with $1.4 million for the same period in 2018, a reduction of 28% and reflecting an element of variable costs.

### Kazakhstan – gas production

Gas production costs decreased in the current quarter by 25% and 10% for the six months due to a weakening of the Kazakhstan Tenge and also cost efficiencies, although gas production, generally more so than the oil, has a significant fixed cost element which includes compressor supplies denominated in US dollars and consequently, as production declines, the production cost per Mcm (or boe) generally increases.

## Financial Review - continued

### Depreciation, depletion and amortization ("DD&A")

DD&A for the quarter was $1.3 million (Q2 2018: $1.5 million) and for the six months $2.5 million (H1 2018: $4.2 million) mainly relating to the Kazakh producing assets. The decrease in DD&A expense mainly reflects lower oil production volumes, partly offset by higher gas production and a reassessment of oil and gas reserves at December 31, 2018.

### Administrative expenses

| | Quarter ended June 30 | | | Six months ended June 30 | | |
|---|---|---|---|---|---|---|
| | **2019** | **2018** | **Change** | **2019** | **2018** | **Change** |
| Staff | 316 | 629 | (50%) | 548 | 1,236 | (56%) |
| Non-executive director fees | 48 | 52 | (8%) | 100 | 114 | (12%) |
| Professional fees | 165 | 102 | 62% | 345 | 308 | 12% |
| Other administrative expenses | 243 | 129 | 88% | 395 | 241 | 64% |
| **Total** | **772** | **912** | **(15%)** | **1,388** | **1,899** | **(27%)** |
| G&A expenses per boe ($) | 3.80 | 3.80 | 0% | 3.31 | 3.89 | (15%) |

- Staff costs decreased significantly in the quarter and for the six months as a result of personnel and salary reductions;
- Professional fees were higher due to legal fees associated with the scheme of arrangement described on page 7; and
- Other administrative expenses were higher due to higher socio economic contributions in Kazakhstan and regulatory compliance costs. In addition, the prior year amounts were lower than normal due to reversals of accruals for vehicles costs.

### Share based payments

Share based payments were nil in 2019 as no option awards have been made since March 2016 and the cost of vested options was fully recognised by the end of 2018.

### Other gains

Other gains includes the gain arising on deconsolidating the liabilities of a subsidiary which was dissolved.

### Foreign exchange loss - net

Foreign exchange gains and losses arise from the revaluation of monetary assets and liabilities denominated in currencies other than the reporting currency and the receipt or settlement of foreign currency denominated amounts at a different amount than the originally recorded transaction amount. These have mainly arisen in Kazakhstan and in 2018 from the revaluation of the GBP denominated rig loans.

### Finance costs - net

Finance costs comprise interest expense net of interest income and are higher due to accumulating interest on loans where no repayments of principal or interest have been made in either period, apart from the rig loans which were fully repaid in April 2018.

## Financial Review - continued

### Taxation

The deferred tax credit was lower and arises mainly due to property, plant & equipment timing differences for accounting and tax purposes.

## Liquidity and Capital Resources

The Company reported a loss of $0.8 million for the six months ended June 30, 2019 (2018 full year: $4.5 million) and an accumulated deficit as at that date of $357.7 million (December 31, 2018: $356.9 million) and negative working capital of $35.2 million (December 31, 2018: negative $30.9 million). In addition, the Company reported negative cash flow from operating activities of $2.4 million for the six months ended June 30, 2019 (2018 full year: positive $1.0 million).

The Company currently does not have sufficient funding to fund its obligations for the next twelve months should all lenders call in their debts at once. The Company is currently in default on loan obligations as disclosed further in note 15 of the 2018 consolidated financial statements and has various commitments and contingencies as disclosed in note 21 of the 2018 consolidated financial statements. The Company has been in discussions and negotiations with the related counterparties to restructure the repayments that are currently due. In order to continue as a going concern, the Company will need to agree adequate terms with counterparties to restructure repayments. There is material uncertainty about the outcome of these negotiations which casts significant doubt on the Company's ability to continue as a going concern.

In order to support the Company's short term liquidity position and improve the Company's financial situation, we will need to:

- Complete the proposed change of control transaction with Jaka Partners FZC;
- Maintain the improved oil and gas pricing received since September 2018 and work to improve prices further during 2019;
- Ensure continuity of gas production operations and optimise production volumes by completing the upgrade of the gas compression facility;
- Retain exploration & production contracts by fulfilling work program obligations including successfully drilling new oil wells in the Akkulka and Kul-bas contract areas; and
- Formalise repayment terms for overdue debts to lenders.

In September and October 2018, the Company announced it had raised funds of approximately $4.1m from the issuance of shares to a new investor. Some of these proceeds have been used to upgrade gas compressor facilities and to tie in previously drilled gas wells to increase production and cash flow.

On March 19, 2019 the Company announced that it had signed a definitive agreement with the same investor for the acquisition of control the Company at a significant premium to the trading price of the Company's shares before the proposed transaction was first announced in December 2018. The proposed transaction is subject to a number of approvals, which are outside the Company's control although, if completed, it is anticipated that the new investor will provide the Company with the financial support required to continue to operate as a going concern. There is material uncertainty as to whether the definitive agreement will be approved and result in additional funding being made available to the Company.

## Financial Review - continued

### Financing and Going Concern

Details of the Company's financing and going concern assessment are provided in note 1 of the condensed consolidated interim financial statements.

### Cash Flow

| | Quarter ended June 30 | | | Six months ended June 30 | | |
|---|---|---|---|---|---|---|
| | 2019 | 2018 | Change | 2019 | 2018 | Change |
| **Net cash from operating activities** | **3,317** | **529** | **527%** | **2,379** | **588** | **305%** |
| Proceeds from assets held for sale | - | 3,498 | (100%) | - | 3,498 | (100%) |
| Capital expenditure | (858) | (365) | 135% | (1,314) | (1,162) | 13% |
| Net changes in working capital | (859) | (139) | 518% | (904) | 402 | (325%) |
| Other investing cash flows | 5 | 266 | (98%) | - | 174 | (100%) |
| **Net cash (used in)/from investing activities** | **(1,712)** | **3,260** | **(153%)** | **(2,218)** | **2,912** | **(176%)** |
| Loan principal and interest payments | - | (3,148) | (100%) | - | (3,148) | (100%) |
| **Net cash used in financing activities** | **-** | **(3,148)** | **(100%)** | **-** | **(3,148)** | **(100%)** |
| Effect of exchange rates | 18 | (203) | (109%) | 381 | 38 | 903% |
| **Net increase in cash** | **1,623** | **438** | **271%** | **542** | **390** | **39%** |
| Cash & cash equivalents at beginning of period | 2,379 | 29 | 8103% | 3,460 | 77 | 4394% |
| **Cash & cash equivalents at end of period** | **4,002** | **467** | **757%** | **4,002** | **467** | **757%** |

### Operating activities

Net cash from operating activities in the current quarter and six months was higher due to higher receipts for gas sales receivables and lower payments to suppliers from cost reductions.

### Investing activities

Capital expenditure comprised payments for the tie-in of gas wells, the re-entry of the AKD03 oil well and seismic acquisition and in the prior year related to the shallow gas well drilling program.

### Financing activities

There were no cash flows from financing activities in either period.

## Accounting policies, changes to accounting standards and critical estimates

The Company's significant accounting policies and discussion of changes to accounting standards are disclosed in note 2 of the June 30, 2019 condensed consolidated interim financial statements. Refer to note 4 of the 2018 consolidated financial statements for full details of the Company's accounting policies and information on the Company's significant judgments and assumptions and critical estimates.

## Off-Balance Sheet Arrangements

The Company has no off-balance sheet arrangements.

## **Financial Review -** continued

## Non-GAAP Measures

### *Adjusted EBITDA*

Adjusted EBITDA is defined as "Profit or loss before Interest, Tax, Depreciation, Amortization, Impairment, Fair value gains or losses and Share Based Payments" and is calculated on the results of continuing operations. It provides an indication of the results generated by the Company's principal business activities prior to how these activities are financed, assets are depreciated and amortized, or how results are taxed in various jurisdictions.

The reconciliation of loss before taxation to Adjusted EBITDA to for the period is as follows:

| | Quarter ended June 30 | | | Six months ended June 30 | | |
|---|---|---|---|---|---|---|
| | **2019** | **2018** | **Change** | **2019** | **2018** | **Change** |
| Loss before taxation | (1,104) | (2,319) | (52%) | (627) | (7,046) | (91%) |
| Depreciation, depletion and amortization | 1,290 | 1,454 | (11%) | 2,541 | 4,169 | (39%) |
| Share based payments | - | 16 | (100%) | - | 33 | (100%) |
| Finance costs - net | 1,615 | 1,378 | 17% | 3,175 | 2,991 | 6% |
| **Adjusted EBITDA** | **1,801** | **529** | **240%** | **5,089** | **147** | **3362%** |

### *Net debt*

Net debt is calculated as total borrowings (which includes current and non-current borrowings) less cash and cash equivalents. Total capital is calculated as equity plus net debt. All figures are as stated in the statements of financial position for the respective reporting periods.

| | As at June 30 | | |
|---|---|---|---|
| | **2019** | **2018** | **Change** |
| Total financial liabilities - borrowings | 36,850 | 32,103 | 15% |
| Less: cash and cash equivalents | (4,002) | (467) | 757% |
| **Net debt** | **32,848** | **31,636** | **4%** |
| Total equity | 55,913 | 41,745 | 34% |
| **Total capital** | **88,761** | **73,381** | **21%** |

Refer to the section above *"Liquidity and capital resources"* for a description of the Company's plans to reduce net debt.

Adjusted EBITDA and Net debt shown in this MD&A do not have any standardised meaning as prescribed under IFRS and, therefore, are considered non-GAAP measures. These measures have been described and presented to provide shareholders and potential investors with additional information regarding the Company's financial results. These measures may not be comparable to similar measures presented by other entities.

## Stockholder Equity

As at June 30, 2019 the Company had authorised share capital of 145,000,000 (2018: 145,000,000) ordinary shares of which 68,324,430 (June 30, 2018: 50,813,609) had been issued and 50,000,000 (June 30, 2018: 50,000,000) preference shares of which none had yet been issued. The preference shares have the rights as set out in the Memorandum and Articles of Association of the Company.

The number of ordinary shares issued and outstanding at the date of this MD&A was 68,324,430 and the number of preference shares issued and outstanding was nil.

## Financial Review - continued

As at June 30, 2019, a total of 4,037,432 (June 30, 2018: 4,037,432) ordinary shares were reserved under the Company's Long Term Stock Incentive Plan. The number of options outstanding as at June 30, 2019 was 1,362,188 (June 30, 2018: 1,371,187) all of which were exercisable (June 30, 2018: 945,458) and the number of warrants outstanding is 14,422,500 (June 30, 2018: 19,230,000) all of which were exercisable. Loan facilities are in place which were convertible into a total of up to 18,361,606 (June 30, 2018: 18,361,606) ordinary shares.

On November 28, 2018 the Company completed a 10 for 1 share consolidation and all figures shown above are on a post-consolidation basis.

## Dividends

There were no dividends paid or declared in the period.

## Transactions with Related Parties

There were no transactions with related parties requiring disclosure.

## Commitments and contingencies

Details of the Company's commitments and contingencies including litigation, claims and assessments, work programme commitments and operating leases are provided in note 21 of the 2018 consolidated financial statements.

A summary of the Company's contractual obligations for each of the next five years and thereafter is shown in the table below:

| | **Total** | **Payments due by period** | | | |
|---|---|---|---|---|---|
| **Contractual obligations** | | **Less than 1 year** | **1 – 3 years** | **4 – 5 years** | **After 5 years** |
| Borrowings | 36,850 | 36,850 | - | - | - |
| Kazakhstan work programme commitments | 63,193 | 17,746 | 22,031 | 5,588 | 17,828 |
| Trade and other payables | 7,754 | 7,754 | - | - | - |
| Provisions | 1,617 | 117 | 372 | - | 1,128 |
| **Total contractual obligations** | **109,414** | **62,467** | **22,403** | **5,588** | **18,956** |

## Risks, uncertainties and other information

Risk management is carried out by senior management, in particular the Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO") as well as the Board of Directors. The Company has identified its principal risks for 2019 to include:

(1) Liquidity and going concern;

(2) Retention and extension of existing licences;

(3) Production volumes and pricing – both oil and gas; and

(4) Political, fiscal, litigation and related risks.

## Financial Risk Management

The Company's activities expose it to a variety of financial risks including: market risk, credit risk, liquidity risk, interest rate, commodity price and foreign exchange risk. Details of the Company's exposure to these risks and how this is managed is given in note 3 to the consolidated financial statements for the year ended December 31, 2018. The Company's overall risk management program focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Company's financial performance.

The Board of Directors of the Company has overall responsibility for the Company's management of risk, including the identification and analysis of risks faced by the Company and the consideration of controls that monitor changes in risk and minimise risk wherever possible.

## Sensitivities

The price of gas sales from gas produced from both the Kyzyloi and Akkulka gas fields under gas sales contracts denominated in Tenge is sensitive to a fluctuation in exchange rates. A 20% devaluation of the Tenge, from KZT380 to the $ to KZT456 for example, would result in a net price reduction of $22.74 per Mcm. Based on a sales volume of 110,000 Mcm per annum, this would result in a reduction of $2.5 million in gas revenues.

The price of oil sales is sensitive to movements in the market price. On a production level of 250 bopd, a movement of $1 per barrel on the price received by the Company would result in a plus or minus movement in oil sales revenue of $0.1 million per annum.

## Critical Accounting Policies and Estimates

The annual and condensed consolidated interim financial statements of the Company are prepared in accordance with IFRS and IFRIC Interpretations issued by the IFRS Interpretations Committee, refer to 2018 Consolidated Financial Statements - note 2 *Summary of Significant Accounting Policies* and Note 4 – *Critical Judgements and Accounting Estimates* – for further details.

## Derivative Financial Instruments

The Company has not recognised any derivative financial instruments.

## Significant equity investees

Details of significant equity investees are discussed in note 19 of the consolidated financial statements for the year ended December 31, 2018.

## Forward-looking statements

In the interest of providing Tethys' shareholders and potential investors with information regarding the Company and its subsidiaries, including management's assessment of the Company's and its subsidiaries' future plans and operations, certain statements contained in this MD&A constitute forward-looking statements or information (collectively referred to herein as "forward-looking statements") within the meaning of the "safe harbour" provisions of applicable securities legislation. Forward-looking statements are typically identified by words such as "anticipate", "believe", "expect", "plan", "intend", "forecast", "target", "project" or similar words suggesting future outcomes or statements regarding an outlook.

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 risks, uncertainties and assumptions include, among other things: the significant uncertainty over the Company's ability to generate sufficient cash flow from operations to meet its current and future obligations and continue as a going concern; risks of exploration and production licenses, contracts and permits being cancelled due to non-fulfilment of contractual commitments or not being renewed when they expire; the Company will not be successful in negotiating binding terms for the export of oil and gas at prices significantly higher than prices currently realised; volatility of and assumptions regarding oil and gas prices; fluctuations in currency and interest rates; ability to successfully complete proposed debt or equity financings or restructuring; product supply and demand; market competition; ability to realise current market oil and gas prices; risks inherent in the Company's and its subsidiaries' marketing operations, including credit risks; imprecision of reserve estimates and estimates of recoverable quantities of oil and natural gas and other sources not currently classified as proved; the Company's and its subsidiaries' ability to replace and expand oil and gas reserves; unexpected cost increases or technical difficulties in constructing pipeline or other facilities; unexpected delays in its drilling operations; unexpected difficulties in transporting oil or natural gas; risks associated with technology; the timing and the costs of well and pipeline construction; the Company's and its subsidiaries' ability to secure adequate product transportation; changes in royalty, tax, environmental and other laws or regulations or the interpretations of such laws or regulations; political and economic conditions in the countries in which the Company and its subsidiaries operate; the risk associated with the uncertainties, inconsistencies and contradictions in local laws and their interpretation and application in local jurisdictions in which the Company operates; the risk of international war, hostilities and terrorist threats, civil insurrection and instability affecting countries in which the Company and its subsidiaries operate; risks associated with existing and potential future lawsuits and regulatory actions made against the Company and its subsidiaries; and other risks and uncertainties described from time to time in the reports and filings made with securities regulatory authorities by Tethys.

**Forward-looking statements** - continued

With regard to forward looking information contained in this MD&A, the Company has made assumptions regarding, amongst other things, the continued existence and operation of existing pipelines; the proposed increase in the selling price for the delivery of gas to China; future prices for oil and natural gas; future currency and exchange rates; the Company's ability to generate sufficient cash flow from operations and access to capital markets to meet its future obligations and ability to continue as a going concern; the regulatory framework representing mineral extraction taxes, royalties, taxes and environmental matters in the countries in which the Company conducts its business, gas production levels; and the Company's ability to obtain qualified staff and equipment in a timely and cost effective manner to meet the Company's demands. Statements relating to "reserves" or "resources" or "resource potential" 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 exist in the quantities predicted or estimated, and can be profitably produced in the future. Although Tethys 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, Tethys 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.

## Glossary

| | |
|---|---|
| **AKD** | Akkulka Deep |
| **AOT** | Aral Oil Terminal LLP |
| **Bbls** | Barrels of oil |
| **boe/d** | Barrel of oil equivalent per day |
| **bopd** | Barrels of oil per day |
| **CEO** | Chief Executive Officer |
| **CFO** | Chief Financial Officer |
| **EBITDA** | Earnings before interest, taxes, depreciation and amortisation |
| **EOR** | Enhanced oil recovery |
| **ESP** | Electrical submersible pump |
| **GAAP** | Generally accepted accounting principles |
| **H1** | Six month period commencing January 1 and ending 30 June |
| **H2** | Six month period commencing July 1 and ending 31 December |
| **IFRS** | International Financial Reporting Standards |
| **KASE** | Kazakhstan Stock Exchange |
| **KZT** | Kazakhstani Tenge |
| **m3** | Cubic metre |
| **Mcf** | Thousand cubic feet |
| **Mcf/d** | Thousand cubic feet per day |
| **Mcm** | Thousand cubic metres |
| **Mcm/d** | Thousand cubic metres per day |
| **MD&A** | Management's Discussion & Analysis |
| **NPV** | Net present value |
| **NEX** | NEX Board of the TSX Venture Exchange |
| **Olisol** | Olisol Investments Limited and Olisol Petroleum Limited |
| **Q1** | Three month period commencing January 1 and ending 31 March |
| **Q2** | Three month period commencing April 1 and ending 30 June |
| **Q3** | Three month period commencing July 1 and ending 30 September |
| **Q4** | Three month period commencing October 1 and ending 31 December |
| **sq.km** | Square kilometre |
| **TAG** | Tethys Aral Gas LLP |
| **$** | United States Dollar |
| **TSX** | Toronto Stock Exchange |
| **TSXV** | TSX Venture Exchange |
| **$/bbl** | $ per barrel |
| **$/Mcm** | $ per thousand cubic metre |
| **VAT** | Value added tax |
| **YTD** | Year to date cumulative |