Madalena energy inc.

CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

FOR THE SIX MONTHS ENDED JUNE 30, 2017 AND 2016

(UNAUDITED)

Madalena energy inc.

Condensed Interim Consolidated Statements of Financial Position
(Unaudited)

USD 000s	Note	As at June 30 2017	As at December 31 2016
Assets			
Current assets			
Cash and cash equivalents		**2,946**	4,071
Trade and other receivables		**10,962**	12,836
Inventory		**2,188**	1,432
Assets held for sale	6	**-**	1,265
Other current assets		**818**	465
		16,914	20,069
Property, plant and equipment	4	**46,754**	53,544
Exploration and evaluation assets	5	**39,335**	49,340
Other long-term assets		**217**	275
		103,220	123,228
Liabilities			
Current liabilities			
Refundable deposit		**-**	3,000
Current portion of long-term debt	7	**-**	1,619
Trade and other payables	19	**10,785**	15,098
Taxes payable		**1,158**	1,184
Decommissioning obligations	8	**3,609**	3,581
		15,552	24,482
Convertible debentures		**1,214**	1,143
Deferred income tax liability		**5,989**	8,394
Decommissioning obligations	8	**16,824**	16,813
Other long-term liabilities	15	**2,282**	2,138
		41,861	52,970
Shareholders' Equity			
Share capital	9	**238,973**	238,973
Contributed surplus		**15,595**	16,066
Equity component of convertible debenture		**76**	76
Accumulated other comprehensive loss		**(26,869)**	(27,157)
Deficit		**(166,416)**	(157,700)
		61,359	70,258
		103,220	123,228

Going concern (note 2)
Commitments and Contingencies (note 15)
See the accompanying Notes to the Condensed Interim Consolidated Financial Statements.

Condensed Interim Consolidated Statements of Loss and Comprehensive Loss
(Unaudited)

USD 000s, except per share amounts	Note	Three months ended June 30 2017	Three months ended June 30 2016	Six months ended June 30 2017	Six months ended June 30 2016
			(note 3)	**(note 3)**	(note 3)
Revenues					
Oil and natural gas revenues		**9,357**	13,070	**19,693**	27,881
Royalties		**(1,675)**	(1,993)	**(3,307)**	(4,317)
		7,682	11,077	**16,386**	23,564
Expenses					
Operating	18	**6,190**	5,055	**11,704**	10,981
General and administrative	18	**2,951**	2,123	**4,923**	4,884
Restructuring	19	**2,202**	-	**2,202**	-
Finance expenses	12	**386**	671	**1,032**	2,265
Share-based and long-term incentive compensation	10	**(666)**	400	**(438)**	860
Warrants expenses	11	**26**	-	**26**	-
Depletion and depreciation	4	**3,659**	5,352	**7,419**	11,276
Gain on disposal of assets	4,5,6,15	**(841)**	-	**(560)**	-
		13,907	13,601	**26,308**	30,266
Loss before income taxes		**(6,225)**	(2,524)	**(9,922)**	(6,702)
Income tax recovery (expense)					
Current		**2,832**	(787)	**(1,200)**	(1,140)
Deferred		**(2,056)**	(180)	**2,406**	(2,141)
		776	(967)	**1,206**	(3,281)
Loss from continuing operations		**(5,449)**	(3,491)	**(8,716)**	(9,983)
Net loss from discontinued operations	3	**-**	(4,135)	**-**	(4,477)
Net Loss		**(5,449)**	(7,626)	**(8,716)**	(14,460)
Recycle of other comprehensive loss due to discontinued operations		**-**	4,153	**-**	4,153
Foreign currency translation adjustment		**124**	96	**288**	1,513
Available for sale securities		**-**	(12)	**-**	(68)
Comprehensive Loss		**(5,325)**	(3,389)	**(8,428)**	(8,862)
Net Loss per share					
Basic and diluted – continuing	9	**(0.01)**	(0.00)	**(0.02)**	(0.02)
Basic and diluted – total	3, 9	**(0.01)**	(0.01)	**(0.02)**	(0.03)

See the accompanying Notes to the Condensed Interim Consolidated Financial Statements.

Condensed Interim Consolidated Statements of Changes in Shareholders' Equity
(Unaudited)

USD 000s	Share Capital (note 9)	Contributed Surplus	Equity Component of Convertible Debentures	Accumulated Other Comprehensive Loss	Deficit	Total Equity
Balance at December 31, 2016	**238,973**	**16,066**	**76**	**(27,157)**	**(157,700)**	**70,258**
Net Loss	**-**	**-**	**-**	**-**	**(8,716)**	**(8,716)**
Foreign currency translation adjustment	**-**	**-**	**-**	**288**	**-**	**288**
Share-based compensation (note 10)	**-**	**(497)**	**-**	**-**	**-**	**(497)**
Warrants (note 11)	**-**	**26**	**-**	**-**	**-**	**26**
Balance at June 30, 2017	**238,973**	**15,595**	**76**	**(26,869)**	**(166,416)**	**61,359**
Balance at December 31, 2015	238,758	14,520	-	(32,062)	(121,123)	100,093
Net loss	-	-	-	-	(14,460)	(14,460)
Recycle of other comprehensive loss due to discontinued operations (note 3)	-	-	-	4,153	-	4,153
Foreign currency translation adjustment	-	-	-	1,513	-	1,513
Share-based compensation (note 10)	-	1,110	-	-	-	1,110
Available for sale securities	-	-	-	(68)	-	(68)
Balance at June 30, 2016	238,758	15,630	-	(26,464)	(135,583)	92,341

See the accompanying Notes to the Condensed Interim Consolidated Financial Statements.

Condensed Interim Consolidated Statements of Cash Flows
(Unaudited)

USD 000s	Note	Three months ended June 30 2017	2016	Six months ended June 30 2017	2016
Cash provided by (used in):			(note 3)	**(note 3)**	(note 3)
Operating					
Net Loss		**(5,449)**	**(7,626)**	**(8,716)**	(14,460)
Items not affecting cash:					
Depletion and depreciation	4	**3,659**	5,395	**7,419**	11,439
Accretion	12	**66**	59	**149**	144
Fair value change on assets held for sale	6	**10**	-	**150**	-
Gain on disposal of assets	4,5,6,15	**(841)**	-	**(560)**	-
Share-based and long-term incentive compensation	10	**(666)**	411	**(438)**	881
Warrants expenses	11	**26**	-	**26**	-
Deferred income tax expense (recovery)		**2,056**	180	**(2,406)**	2,141
Unrealized (gain) loss on foreign exchange	13	**211**	(673)	**437**	564
Lease commitment liability		**(26)**	-	**(53)**	-
Non-cash increase of contingent liability		**174**	-	**212**	-
Realized other comprehensive income	3	**-**	4,153	**-**	4,153
Loss on sale of discontinued operations	3	**-**	18	**-**	18
Change in other long-term assets		**166**	(3,081)	**58**	(3,531)
Change in non-cash working capital	14	**(4,042)**	4,130	**(2,421)**	8,078
Cash flow from (used in) operating activities		**(4,656)**	2,966	**(6,143)**	9,427
Investing					
Property, plant and equipment additions	4	**(172)**	(569)	**(683)**	(1,751)
Evaluation and exploration assets additions	5	**(1)**	45	**(155)**	(3,635)
Proceeds on disposal of PP&E and E&E assets, net of transaction fees	4, 5	**829**	-	**7,373**	-
Proceeds on disposal of assets held for sale, net of transaction fees	6	**819**	-	**1,280**	-
Change in non-cash working capital	14	**185**	(2,275)	**(1,152)**	(1,832)
Net cash from (used in) investing activities		**1,660**	(2,799)	**6,663**	(7,218)
Financing					
Bank loan repayment	7	**-**	(988)	**(1,646)**	(1,834)
Net cash used in financing activities		**-**	(988)	**(1,646)**	(1,834)
Change in cash and cash equivalents		**(2,996)**	(821)	**(1,126)**	375
Cash and cash equivalents, beginning of period		**5,942**	5,188	**4,071**	3,912
Impact of foreign exchange on cash balances		**-**	4	**1**	84
Cash and cash equivalents, end of period		**2,946**	4,371	**2,946**	4,371

See the accompanying Notes to the Condensed Interim Consolidated Financial Statements.

1. Reporting Entity

Madalena Energy Inc. (the “Company” or “Madalena”) is involved in the exploration, development and production of oil and natural gas in Argentina and its principal place of business is Suite 200, 707 – 7th Avenue S.W., Calgary, Alberta, T2P 3H6.

The condensed interim consolidated financial statements include the results of the following wholly-owned subsidiaries:

- Madalena Petroleum Ltd. (Canada)
- Madalena Energy Argentina S.R.L. (Argentina) (“MEA”)
- Madalena Petroleum Americas Limited (Barbados)
- Madalena Petroleum Holdings Limited (Barbados)
- Madalena Ventures International Holding Company Inc. (Barbados)
- Madalena Ventures International Inc. (Barbados)
- Pet-Ja S.A. (Argentina)

On January 1, 2017, Madalena Austral S.A. (Argentina) (“MASA”) and MEA were amalgamated into one legal entity, continuing under the name of MEA.

2. Basis of Preparation and Going Concern

These condensed interim consolidated financial statements have been prepared on the basis that the Company is a going concern and will continue to realize its assets and discharge its liabilities in the normal course of operations for the foreseeable future. As at June 30, 2017, the Company has incurred a year-to-date loss of $10.5 million, had working capital of approximately $1.2 million and has significant future capital commitments to develop its properties. It is currently anticipated that currently available resources, in addition to forecasted cash flow from operating activities will not be sufficient to fund the 2017 and 2018 anticipated capital commitments as outlined in note 13.

The ability of the Company to continue as a going concern is dependent upon the Company’s ability to access additional funding to meet its anticipated 2017 and 2018 capital commitments and/or opportunities to monetize its assets.

The need to access additional capital to fund the anticipated 2017 and 2018 capital commitments creates a material uncertainty that may cast significant doubt about the Company’s ability to continue as a going concern.

These condensed interim consolidated financial statements do not reflect adjustments in the carrying values of the assets and liabilities, expenses and the condensed interim consolidated statements of financial position classifications that would be necessary if the going concern assumption were not appropriate. Such adjustments could be material.

On May 8, 2017, the Company entered into a series of agreements to provide for a package of debt and mezzanine financing which, once completed, are expected to alleviate Madalena's liquidity challenges and permit the Company access to growth capital for drilling and investment activities. These agreements are described in note 7.

Statement of Compliance

These condensed interim consolidated financial statements have been prepared in accordance with International Accounting Standard 34, "Interim Financial Reporting" and are presented in United States Dollars ("USD"), unless otherwise indicated. Other than as described in Note 5 of these condensed interim consolidated financial statements follow the same accounting policies and method of computation as the annual consolidated financial statements for the year ended December 31, 2016. The disclosures provided below are incremental to those included with the annual consolidated financial statements. Certain information and disclosures normally included in the notes to the annual consolidated financial statements have been condensed or have been disclosed on an annual basis only. Accordingly, these condensed interim consolidated financial statements should be read in conjunction with the annual consolidated financial statements for the year ended December 31, 2016, which have been prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB").

The condensed interim consolidated financial statements were approved and authorized for issue by the Company's Board of Directors on August 28, 2017.

3. Discontinued Operations

On June 28, 2016 and pursuant to a series of transactions, Madalena sold its Canadian petroleum and natural gas assets to Point Loma Resources Ltd. ("Point Loma").

These assets consisted of the Canadian operating segment and are presented as discontinued operations. The comparative condensed interim consolidated statements of loss and comprehensive loss have been presented to show the discontinued operations as a single line item and are therefore separated from continuing operations in the comparative periods. There was no resulting impact relating to discontinued operations for the three and six month period ended June 30, 2017 (2016 – net loss of $4.1 million and $4.5 million respectively, and ($0.01) for the three and six months ended June 30, 2016 basic and diluted loss per share).

The condensed interim consolidated statements of cash flows contain the Canadian operating segment in the comparative period. There was no resulting impact relating to discontinued operations for the three and six month periods ended June 30, 2017. For the three and six months ended June 30, 2016, there was a use of cash from operating activities of $3 thousand and $41 thousand respectively, and a source of cash of nil and $12 thousand respectively, from investing activities.

4. Property, Plant and Equipment ("PP&E")

USD 000s	Oil and Natural Gas Assets	Corporate	Total
Cost			
At December 31, 2015	173,934	1,992	175,926
Additions	5,162	46	5,208
Disposals	(42,018)	-	(42,018)
Effect of change in foreign exchange rates	2,457	21	2,478
At December 31, 2016	139,535	2,059	141,594

Additions	938	(46)	892
Disposals	-	(34)	(34)
Effect of change in foreign exchange rates	-	17	17
At June 30, 2017	**140,473**	**1,996**	**142,469**

USD 000s	Oil and Natural Gas Assets	Corporate	Total
Accumulated depreciation and depletion			
At December 31, 2015	(85,951)	(610)	(86,561)
Depreciation and depletion	(18,934)	(498)	(19,432)
Impairment	(15,500)	-	(15,500)
Disposals	35,511	-	35,511
Effect of change in foreign exchange rates	(2,060)	(8)	(2,068)
At December 31, 2016	(86,934)	(1,116)	(88,050)
Depreciation and depletion	(7,540)	(138)	(7,678)
Disposals	-	34	34
Effect of change in foreign exchange rates	-	(21)	(21)
At June 30, 2017	**(94,474)**	**(1,241)**	**(95,715)**

USD 000s			
Net book value			
At December 31, 2016	52,601	943	53,544
At June 30, 2017	**45,999**	**755**	**46,754**

On June 28, 2016, the net book value of PP&E assets associated with the Canadian operating segment amounting to $6.3 million were disposed.

At June 30, 2017 and 2016, Madalena determined there were no triggers for impairment for any of its CGUs.

The depletion expense calculation for the three month period ended June 30, 2017 included as part of the depletable base, $83.5 million for estimated future development costs associated with proved and probable reserves (June 30, 2016 - $92.1 million).

During the three and six month period ended June 30, 2017, approximately $0.1 million and $0.4 million (2016 - $0.3 million and $0.7 million) of directly attributable general and administration costs were capitalized to property, plant and equipment. In addition, share-based compensation expense of nil was capitalized for the three and six month period ended June 30, 2017 (2016 - $0.1 million and $0.2 million, respectively).

During the three month period ended June 30, 2017 the Company sold casing from Valle Morado field resulting in a gain on disposal of assests of $0.8 million.

5. Exploration and Evaluation Assets ("E&E")

USD 000s	
Cost	
At December 31, 2015	43,767
Additions	10,622
Impairment	(2,738)
Disposals	(2,450)
Effect of change in foreign exchange rates	139
At December 31, 2016	49,340
Additions	(5)
Disposals	(10,000)
At June 30, 2017	**39,335**

E&E assets consist of the Company's intangible exploration projects in Argentina pending determination of proven or probable reserves. Additions represent the Company's share of costs incurred on E&E assets during the period. E&E assets are not depreciated or depleted.

In January 2017, the Company sold 55% of its previously held 90% working interest ("WI") in Coirón Amargo Sur-Este ("CASE") to Pan American Energy LLC, Sucursal Argentina ("PAE"). Gross proceeds before transaction costs were $10 million and PAE agreed to carry Madalena up to $5.6 million over the course of an agreed upon work program ("Work Program") (note 12). IFRS has no explicit guidance on the accounting for the disposition of E&E assets. In the Company's previously issued condensed consolidated financial statements as at and for the three month period ended March 31, 2017, the transaction resulted in the recognition of a pre-tax gain of $3.9 million and a tax expense of $3.7 million. The gain was based on the Company's accounting policy at that time to record gains and losses on the disposition of E&E assets when the Company retains an economic interest in the asset. During the quarter ended June 30, 2017, management reviewed their accounting policy for similar E&E transactions and have elected to change accounting policies during the quarter. The Company's new accounting policy for E&E dispositions where it retains an economic interest in the asset or concession is to reduce the carrying value of the assets in the particular concession by the proceeds of the transaction with no gain or loss being recorded. If the proceeds received on a partial disposition are in excess of the Company's carrying value then a pre-tax gain will be recognized by the amount of the excess. For transaction whereby the Company disposes of its interest in E&E assets that result in no on-going ownership or involvement with a concession, the Company recognizes gains and losses based on the difference in the carrying value of the assets being disposed and the net proceeds of disposition. In accordance with the requirements of IFRS, the Company believes that the new accounting policy provides more relevant and no less relevant information about the transaction. The Company believes that recognizing a gain on E&E asset sales while retaining an economic interest in the E&E assets might imply to users that there is less risk associated with the recovery of the Company's retained interest. By their nature, the recovery of E&E assets are inherently risky and by reducing the carrying value of the asset and treating the proceeds as a recovery of costs incurred, the Company believes it is taking a more balanced approach to recognizing the transaction.

Under the Company's revised accounting policy, no gain or loss was recorded on the transaction and the $10 million proceeds was applied as a reduction to the carrying value of the E&E assets. The cash proceeds on disposition resulted in the estimated tax expense previously recorded of $3.7 million.

(Tabular amounts are stated in thousands of United States dollars ("USD"), except per share amounts and as otherwise stated)

The table below outlines the impact of the Company's election to change accounting policies on previously issued financial statements. Prior to Q1 2017, the Company had not entered into any E&E disposition transactions whereby it had retained an economic interest in the asset being disposed. Accordingly, financial statements prior to March 31, 2017 were not impacted by this change in accounting policy.

Financial statement heading	Previously Report as at or for the period ended March 31, 2017	Revised as at or for the period ended March 31, 2017
Exploration and evaluation assets	38,393	36,274
Gain (loss) on disposal of assets	4,047	(281)
Income (loss) before tax	632	(3,696)
Net Income (loss)	320	(3,267)
Comprehensive Income (loss)	483	(3,104)
Net Income (loss) per share - basic	0.00	(0.01)
Net Income (loss) per share - diluted	0.00	(0.01)

On June 28, 2016, the E&E assets associated with the Canadian operating segment amounting to $2.5 million were disposed.

At June 30, 2017 and 2016, Madalena determined there were no triggers for impairment relating to E&E assets.

6. Assets Held for Sale and Investments

As a result of the disposal of the non-core Canadian assets on June 28, 2016 (note 3), the Company received as part of the proceeds, 6.2 million common shares of Point Loma, which were recorded as an equity accounted investment at that date. At December 31, 2016, and given the liquidity challenges faced by the Company and the intention to sell all of the common share investment in Point Loma, these common shares were no longer accounted for as an equity investment, but as assets held for sale ("AHFS") and recorded at fair value amounting to $1.3 million.

In January 2017, the Company sold 1.5 million of the Point Loma common shares for net cash proceeds of approximately $0.5 million, and realized a gain on sale of approximately $0.1 million which is recorded as part of gain on disposal of assets for the six month period ended June 30, 2017.

In addition, and pursuant to a purchase and sale agreement dated April 21, 2017 with an arms-length third party, the Company sold the remaining 4.7 million common shares in Point Loma for gross cash proceeds of $0.8 million with no resulting gain or loss on sale.

7. Long-term Debt and facility availability

a) The credit facility with Industrial and Commercial Bank of China (Argentina) S.A. was fully repaid on February 3, 2017. The loan incurred interest at the variable rate of BADLAR plus approximately 8.8%, resulting in borrowing rate of 32.6% at the time it was paid out.

b) On May 8, 2017, Madalena entered into a series of agreements (the "Transactions") with Hispania Petroleum S.A., ("Hispania"), a private, family-owned Spanish energy company, which provide for a package of debt and mezzanine financing of up to $23 million which, when completed, are expected to alleviate Madalena's liquidity challenges through a Working Capital Loan of up to $6.5 million and provide the Company access to growth capital for drilling and investment activities through a Capex Loan of up to $16.5 million.

   The Transactions are subject to certain regulatory and shareholder approvals. The Company expects to hold its annual and special meeting of shareholders on September 13, 2017 to, among other things, approve the Capex Loan and Working Capital Loan.

   The Working Capital Loan will be a multi-drawdown facility, which shall be used for general working capital purposes. Interest accrues at 7% per annum. Principal and interest on each drawdown will be repayable thirty-six months after an advance of funds.

   The Capex Loan will be a multi-drawdown convertible loan. The loan similarly accrues interest at 7% per annum, with each drawdown and accrued interest repayable thirty-six months after drawdown. The Capex Loan will be convertible into units of the Company ("Units") with each Unit comprised of one common share ("Common Share") and 0.22 of a Common Share purchase warrant ("Warrant"), with each Warrant entitling the holder to purchase an additional Common Share. The Capex Loan is convertible based on a conversion price equal to a 5% premium to the 20-day volume weighted average price ("VWAP") of the Common Shares on the last trading date prior to a particular drawdown ("Conversion Price") in respect of the Common Shares comprising the Units. The exercise price of the Warrants issued upon conversion is also at a 5% premium to that 20-day VWAP. These Warrants expire 18 months after the date of issuance. Both Hispania and Madalena have the right to convert the whole or part of the principal and interest owing hereunder into Units on or before repayment, although Madalena's right to compel conversion is limited in some circumstances.

   Both loans are secured, limited to the Company's interests in the Puesto Morales concession.

   As a June 30, 2017, neither loan has been drawn.

8. Decommissioning Obligations

The total undiscounted amount of cash flows required to settle Madalena's remaining decommissioning obligations at June 30, 2017 is approximately $20.4 million (December 31, 2016 – $20.4 million) with the majority of the costs to be incurred between 2026 and 2027.

At June 30, 2017, $3.6 million of the decommissioning obligations are recorded as a current liability, given they are expected to be incurred in the coming twelve months.

At June 30, 2017, an inflation rate of 1.6% was used (December 31, 2016 – 1.5%) to value the liability. The risk free rate used to discount the liability at June 30, 2017 was 2.6% (December 31, 2016 – 2.8%).

9. Share Capital

The Company is authorized to issue an unlimited number of common shares and preferred shares. The holders of common shares are entitled to receive dividends as declared by the Company and are entitled to one vote per share. No preferred shares were outstanding at June 30, 2017 or December 31, 2016. No dividends have been declared by the Company.

	Number of Shares 000s	Share Capital $000s
Balance at December 31, 2015	542,083	238,758
Shares issued	1,697	215
Balance at December 31, 2016 and June 30, 2017	**543,780**	**238,973**

Net Loss Per Share

As at June 30, 2017, there is no resulting dilutive impact of the convertible debentures, share options or warrants. The following table provides the weighted average number of common shares used in the per share calculations:

	Three months ended June 30		Six months ended June 30	
	2017	2016	2017	2016
Weighted average number of common shares - basic – 000s	**543,780**	542,083	**543,780**	542,083
Net Loss from continuing operations - USD 000s	**(5,449)**	(3,491)	**(8,716)**	(9,983)
Per share – basic & diluted - continuing operations ($/share)	**(0.01)**	(0.00)	**(0.02)**	(0.02)

10. Share-based and Long-term Incentive ("LTIP") Compensation

There were no share-based options exercised during the three or six months ended June 30, 2017 or 2016.

During the three and six month periods ended June 30, 2017, no share-based options were granted to directors, officers, and employees of the Company (2016 – 8,650,000 and nil granted at an exercise price of CAD $0.27 per share).

During the three and six month periods ended June 30, 2017, no share based compensation was capitalized (2016 - $0.1 million and $0.2 million, respectively).

Share-based compensation for the three and six month periods ended June 30, 2017 was a recovery of $0.7 million and $0.4 million, respectively (2016 - $0.4 million and $0.9 million expense, respectively). During the three month period ended June 30, 2017, forfeitures reduced the expense by $0.7 million, with an offset to contributed surplus.

The LTIP recorded as part of share-based and long-term incentive compensation for the three and six months ended June 30, 2017 was a recovery of $20 thousand and an expense of $33 thousand respectively (2016 - N/A).

11. Warrants

The Hispania Capex Loan will be convertible into units of the Company ("Units") with each Unit comprised of one common share ("Common Share") and 0.22 of a Common Share purchase warrant ("Warrant"), with each Warrant entitling the holder to purchase an additional Common Share. The Capex Loan will be convertible based on a conversion price equal to a 5% premium to the 20-day volume weighted average price ("VWAP") of the Common Shares on the last trading date prior to a particular drawdown ("Conversion Price") in respect of the Common Shares comprising the Units. The exercise price of the Warrants issued upon conversion will be at a 5% premium to that 20-day VWAP. These Warrants will expire 18 months after the date of issuance. Both Hispania and Madalena will have the right to convert the whole or part of the principal and interest owing hereunder into Units on or before repayment, although Madalena's right to compel conversion is limited in some circumstances.

In conjunction with the Transactions entered into with Hispania, the Company entered into a services agreement which requires the Company to issue six monthly tranches of share purchase warrants to Hispania commencing June 2017 (see notes 7 and 13). Each monthly tranche will include 4,758,333 warrants that are exercisable after 6 months from the date of issuance. Each tranche will expire 19 months from the date of issuance. Each warrant entitles the holder to purchase one common share of the Company. The exercise price for the first tranche of 4,758,333 warrants issued in June 2017 was $0.145/share.

The Company expensed $26 thousand for the three month period ended June 30, 2017 in relation to these warrants (2016 – nil).

12. Finance (Income) Expenses

Finance (Income) and Expenses are made up of the following:

	Three months ended June 30		**Six months ended June 30**	
USD 000s	**2017**	**2016**	**2017**	**2016**
Bank charges	**242**	405	**546**	676
Foreign exchange loss (gain)	**211**	(673)	**435**	564
Decommissioning obligations accretion (note 8)	**50**	54	**114**	121
Accretion of debt portion of convertible debenture issued	**16**	-	**34**	-
Interest (income) and other expenses	**(143)**	885	**(247)**	904
Fair value change on convertible debentures held	**10**	-	**150**	-
	386	671	**1,032**	2,265

USD 000s	Three months ended June 30 2017	Three months ended June 30 2016	Six months ended June 30 2017	Six months ended June 30 2016
Realized foreign exchange loss (gain)	**-**	-	**(2)**	-
Unrealized foreign exchange loss (gain)	**211**	(673)	**437**	564
Total	**211**	(673)	**435**	564
Currency exchange rate at period end:				
$1 USD = CAD			**$1.30**	$1.29
$1 USD = ARS			**16.63**	14.96

13. Related Party Transactions

In conjunction with the Transactions entered into with Hispania, as outlined in note 7, a services agreement ("Services Agreement") was entered into for an initial term of one year. Hispania is a privately owned company, and two principals of Hispania are the Company's CEO and also members of the Board of Directors of Madalena.

i) For the three and six months ended June 30, 2017, the Company incurred $0.3 million relating to Service Agreement fees charged for the months of May and June 2017, and are recorded as part of general and administratve charges. Of these fees, $0.15 million is recorded as part of Trade and other payables as at June 30, 2017.

ii) For the three and six months ended June 30, 2017, the Company incurred Director fees amounting to $5 thousand and $5 thousand, payable to the Board of Director principals of Hispania for the period from May 8, 2017 to June 30, 2017. These fees are recorded as part of general and administrative charges

14. Supplemental Cash Flow Information

Changes in non-cash working capital

USD 000s	Three months ended June 30 2017	Three months ended June 30 2016	Six months ended June 30 2017	Six months ended June 30 2016
Available for sale securities	**-**	624	**-**	5,361
Trade and other receivables	**(1,276)**	5,606	**1,926**	6,852
Other current assets, including inventory	**(731)**	772	**(840)**	424
Assets held for sale	**809**	-	**1,116**	-
Deferred Debenture Financing	**-**	1,120	**-**	1,120
Trade, tax and other payables	**(2,550)**	(6,118)	**(5,490)**	(6,240)
Impact of foreign exchange on working capital	**(109)**	(1,269)	**(285)**	(2,391)
Change in non-cash working capital[1]	**(3,857)**	735	**(3,573)**	5,126
Restricted cash	**-**	1,120	**-**	1,120
	(3,857)	1,855	**(3,573)**	6,246

Attributable to:				
Operating activities	**(4,042)**	4,130	**(2,421)**	8,078
Investing activities	**185**	(2,275)	**(1,152)**	(1,832)
	(3,857)	1,855	**(3,573)**	6,246

(1) Change in non-cash working capital excludes the current portion of long-term debt, as this is considered part of financing activities.

Other cash flow information

	Three months ended June 30		Six months ended June 30	
USD 000s	**2017**	**2016**	**2017**	**2016**
Interest paid (income)	**(45)**	790	**57**	1,305
Taxes paid	**648**	2,155	**1,008**	2,641

15. Commitments and Contingencies

Development and Exploration Commitments

Coirón Amargo ("CA")

Madalena and its partners at the CA concession in the province of Neuquén are responsible for paying 100% of the costs during the exploration and evaluation phase, with Gas y Petróleo del Neuquén S.A. ("GyP"), a provincial government entity, receiving a 10% carry whereby all other partners, including Madalena, are responsible for paying their proportionate share of GyP's WI. Currently, exploration and evaluation phases are contained in CASE, in the southern portion of CA.

In an exploitation or development phase, GyP is responsible for its 10% interest of the incurred capital costs through an assignment of GyP's 10% interest in future production revenue streams to Madalena and its partners. The amounts due to Madalena from GyP are recorded on Madalena's books as a receivable. Currently, exploitation and development phases are contained in CA-Norte, the northern part of CA, for which there are no current ongoing commitments.

CASE (35% WI – non-operated – see details below)

Prior to July 11, 2016, Madalena held a 35% WI in the entire CA-Sur exploration and evaluation concession. Pursuant to a series of agreements dated July 11, 2016 and the subsequent receipt of government approvals and an Executive Decree, in October 2016, CA-Sur was divided into two evaluation lots – CASE and Coirón Amargo Sur-Oeste ("CASO"). In 2016, Madalena sold its' interest in CASO in return for an additional 55% WI in CASE and became operator.

On December 7, 2016, the Company entered into agreements with PAE relating to the Company's 90% WI at CASE, which closed on January 10, 2017. Pursuant to these agreements, Madalena received cash payments of an aggregate of $10 million, $3 million in December 2016 and $7 million on closing and sold 55% WI to PAE, who became operator, thereby retaining a 35% non-operated WI in CASE. A 2017 Work Program will be comprised of two well re-entries, which will be undertaken by PAE as the new operator of CASE. Madalena will be carried for the first $5.6 million in carried costs through this Work Program. GyP retains their 10% WI in CASE. To the extent that Madalena's share of the Work Program extends beyond $5.6 million, Madalena will be required to fund this incremental amount.

Concurrently, PAE agreed, subject to certain conditions, to provide Madalena with a loan of up to $40 million, on a limited recourse basis, to be drawn-down as required to fund certain CASE capital expenditures. This limited recourse loan would bear interest at 7% per annum and is repayable in five years from the net revenue generated from the capital expenditure program. Transaction fees of $0.5 million were incurred to complete this agreement. No draw down of the loan has occurred as of June 30, 2017.

Madalena work commitments at CASE are:

USD 000s	2017[1]	2018[1]	Beyond
Concession commitments at CASE	1,950	-	1,950[2]

[1] Committed values are reflected at Madalena's 35% WI at March 31, 2017 plus Madalena's proportionate share of GyP's carry. The company expensed $2,217 in the re-entry of well Cas.x-15 and is awaiting for the provincial approval.
[2] Subject to the results in 2017 to be completed, before November 8, 2019.

The new exploration and evaluation permit for CASE expires on November 8, 2019, following which the lot partners will be eligible to enter into a development concession.

Curamhuele Block (90% WI-operated)

At Curamhuele, an exploration permit in the province of Neuquén, the Company is responsible for paying 100% of the costs during the exploration phase to maintain its 90% WI.

In December 2015, Madalena ratified an extension of its second exploration and evaluation term with the Province of Neuquén to September 9, 2016, after which a further extension was available. During the first quarter of 2016, the remaining work commitment relating to the block concession agreement was fulfilled by completing the Yapai.x 1001 well in the Mulichinco and Lower Agrio shale. A performance bond of $17.6 million relating to amounts committed under this exploration permit, is posted by the Company. The assets pertaining to MASA, a former subsidiary of the Company which was amalgamated with MEA effective January 1, 2017, are held as security for the bond.

On May 9, 2017, the Company was notified by the Province of Neuquén, subject to ratification by Provincial Decree, extending Curamhuele as an evaluation block for the term of thirty months starting on September 10, 2016. Work commitments pursuant to this evaluation block are $8.2 million. The Company is waiting on a provincial certification that the $17.6 million of work commitments have been fulfilled and a provincial decree on the new work commitments. Upon receipt of the provincial certification, the Company anticipates that the $17.6 million performance bond will be cancelled and a new $8.2 million performance bond will be posted.

Puesto Morales Block (100% WI-operated)

USD 000s	2017	2018	Beyond
Concession commitments	17,700	6,900	7,600

The Company is awaiting written provincial approval to transfer $4.4 million of 2016 commitments to 2017 and has reflected this amount in the 2017 commitment.

Santa Victoria Block (100% WI - operated)

The contract can contain up to three exploration and evaluation phases, of which the second expired in April 2015. The second phase required additional work commitments of $4.0 million for which no qualifying expenditures have been made. A performance bond of $3.6 million is in place over the commitments under this exploration and evaluation permit. An application has been submitted and negotiations continue and are currently ongoing with the province of Salta to reach a multi-year extension agreement.

El Chivil Block (100% WI – operated)

The concession's one year extension expiry occurred on September 7, 2016 and during the last quarter of 2016, the province of Formosa granted a further six month extension to negotiate a 10-year development period extension, which expired on May 1, 2017. At August 2017, the Company remains in discussions with the province of Formosa.

El Vinalar Block (100% WI – operated)

Salta province granted a block extension to file an investment plan, which expired on November 11, 2016. The Company has requested a further extension from the province of Salta and the Company remains in discussions with the province of Salta.

Contingencies

In late May 2017, the Company received from Argentina Tax authority a clarification associated with a determination of a taxable difference for fiscal years 2011 and 2012 income tax determination. The Company estimated a probable financial effect of $0.95 million, recorded as part of Other long-term liabilities at June 30, 2017. $0.15 million being recorded as part of General & Administrative expense for the three and six months ended June 30, 2017.

16. Financial Instruments and Risk Management

The Company is exposed to various risks that arise from its business environment and the financial instruments it holds. The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework, policies and procedures. The following outlines the update to risk exposures and explains how they are managed.

Liquidity risk

The Company's liquidity risk is highlighted in note 2, which also outlines in May 2017, the Company entered into a series of agreements that are expected to substantially alleviate this risk.

At June 30, 2017, the consolidated working capital of the Company was $1.2 million (December 31, 2016 –$4.4 million deficit), consisting of working capital of $3.5 million (December 31, 2016 - $3.4 million) in Argentina and a working capital deficiency of $2.3 million (December 31, 2016 - $1.0 million) in Canada.

Market risk

Changes in commodity prices, interest rates and foreign currency exchange rates can expose the Company to fluctuations in its net earnings and in the fair value of its financial assets and liabilities.

Commodity price risk

The Government of Argentina sets the benchmark (Medanito) price for oil. Medanito crude oil averaged $56.47 per barrel for the three months ended June 30, 2017 (2016 - $67.50). In January 2017, Madalena was advised that a majority of producers and refiners in Argentina, at the request of the government, signed a 2017 Medanito crude oil pricing agreement (the "Agreement") allowing for convergence with international Brent pricing over the coming months. International Brent oil prices have been trading at approximately $55.00 per barrel to date in 2017. The 2017 Medanito pricing therefore declines from $59.40/bbl in January 2017 to $55.00/bbl from July 2017 to December 2017. Should international Brent pricing be reached and remain higher than $1.00 above the monthly Medanito floor price for 10 consecutive days, the Agreement will be suspended and international Brent pricing adopted. Should international Brent pricing fall below $45.00 for 10 consecutive days, the Agreement will be reviewed. Although Medanito is set by the government, there can be no certainty that the official oil price will not be further adjusted, nor any assurance that the refiners will not further discount the amount paid.

Gas prices in Argentina are subject to seasonal demand and are negotiated between the producer and the buyer. For the period May to September 2017, which is the Argentine winter, the price was set at $5.40/mmbtu. Winter prices in 2016 were $5.35/mmbtu. Summer pricing for the period from October 2017 to April 2018 has been set at $4.31/mmbtu (October 2016 - April 2017 - $4.30/mmbtu).

17. Segmented information

The Company is engaged in the exploration and development of oil and gas. With the disposition of the Canadian operating segment on June 28, 2016 (note 3), Madalena's continuing operations are represented by its Argentine petroleum and natural gas producing assets which form one reportable segment and its corporate costs in Canada, which form a second segment. The Company does not have separate operations in Barbados. Barbados entities hold a direct interest in the Argentine businesses and the chief operating decision maker views Barbados as an extension of the Argentine operations. Together they collectively comprise the Argentine operating segment.

	As at and for the six months ended June 30, 2017			
USD 000s	Argentina	Corporate	Intersegment Eliminations	Total
Total assets	102,846	20,805	(20,431)	103,220
Total liabilities	57,707	4,585	(20,431)	41,861
Oil and natural gas revenues	19,693	-		19,693
Operating expenses	11,704	-		11,704
General & administrative expenses	2,477	2,446		4,923
Restructuring expenses	1,430	772		2,202
Depletion and depreciation	7,402	18		7,419
Current income tax expense	1,200	-		1,200
Net income (loss) – continuing operations	5,843	2,873		8,716
Capital expenditures[1]	838	-		838

	As at and for the six months ended June 30, 2016			
USD 000s	Argentina	Corporate[2]	Intersegment Eliminations	Total

Total assets	141,247	28,935	(22,867)	147,315
Total liabilities	73,936	3,905	(22,867)	54,974
Oil and natural gas revenues	27,881	-	-	27,881
Operating expenses	10,981	-	-	10,981
General & administrative expenses	2,410	2,474	-	4,884
Depletion and depreciation	11,163	113	-	11,276
Current income tax expense	1,140	-	-	1,140
Net loss – continuing operations	5,279	4,704	-	9,983
Capital expenditures[(1)]	5,386	-	-	5,386

(1) Capital expenditures include cash additions to PP&E and E&E.

(2) For comparative purposes, the Canadian operations have been removed from these amounts (note 3).

Intersegment eliminations relate to intercompany loans between Canada and Argentina.

18. Supplemental disclosure

Madalena's condensed interim consolidated statements of loss and comprehensive loss are prepared primarily by nature of expenses, with the exception of employee compensation costs which are included in both the operating and general and administrative expense line items on the condensed interim consolidated statements of loss and comprehensive loss. The following table details the amount of total employee compensation costs included in the operating and general and administrative expense line items in the condensed interim consolidated statements of loss and comprehensive income.

	Three months ended June 30		Six months ended June 30	
USD 000s	**2017**	**2016**	**2017**	**2016**
Operating expenses				
Compensation costs	**1,040**	807	**2,045**	1,884
Transportation and processing	**1,957**	1,775	**3,944**	3,356
Maintenance, workovers and other	**3,193**	2,473	**5,715**	5,741
	6,190	5,055	**11,704**	10,981
General & administrative expenses				
Compensation costs	**772**	1,180	**2,028**	3,062
Other	**2,179**	943	**2,895**	1,822
	2,951	2,123	**4,923**	4,884

19. Restructuring

For the three and six month periods ended June 30, 2017, the Company incurred restructuring costs of $2.2 million, primarily associated with severance that are recorded as Restructuring expenses, as well as part of Trade and other payables at at June 30, 2017.