NORTH 40
RESOURCES LTD.

September 20, 2023

PRESIDENT'S MESSAGE

North 40 Resources Ltd. Is pleased to report its operating and financial results for the three and six months ended June 30, 2023.

Highlights for this period include:

- Realized Q2 2023 average quarterly production of 6,331 boe/day (66% oil and liquids), which represents a 70% increase over the same period in 2022 and a record high production rate for the company. Current production is approximately 6,800 boe/day (70% liquids).
- Generated funds flow from operations of $17.0 million in the quarter.
- Invested $18.7 million in capital spending in the quarter that included three wells at Wayne, facilities construction, and acquisition of land and seismic at Sheerness.
- Approved an increase in capital spending for 2023 from $75 million to $85 million.
- Maintained strong LMR rating by virtue of our greenfield approach which was 19.76 at September 2nd.
- Above industry average on compliance. No lost time work incidents in the field.

Wayne

During the quarter, North 40 drilled three horizontal oil wells at Wayne that were brought on production in July 2023. The wells have had strong production results with current production of the three wells combined of over 1,500 boe/day (80% oil and liquids). We see several additional drilling locations in this area that have been de-risked and anticipate further drilling activity in the area in 2024.

Drumheller

In August, a horizontal development well was brought onstream in Drumheller that is currently being pumped at rates in excess of 340 boe/day (75% oil and liquids). Our Drumheller 08-36-026-18W4 disposal well was also drilled in Q3, and the water disposal scheme will become operational later this month. The 8-36 facility will dispose of produced water from Drumheller, Wayne and other North 40 properties and is anticipated to realize annual savings estimated at $1 million. Numerous other drilling locations are being acquired. Base production from existing North 40 Banff wells will be increased from well optimizations / workovers to resolve wax / pumping issues.

Sheerness

In the 2nd quarter of 2023, North 40 acquired 105,000 acres or 163 sections of Crown land on the Sheerness prospect. This purchase was paid for by a third party in return for a GORR. This prospect is characterized by thick, aerially extensive Mannville channel sands containing light oil and/or liquids rich natural gas.

Our first exploration well at Sheerness was brought onstream in August and is currently flowing at approximately 400 boe/d (75% oil and liquids) with the production rate significantly restricted by solution gas handling capacity. Sheerness represents a material new play for North 40 and we expect to test two Basal Quartz prospects with the drilling of two exploration wells in the 4th quarter.

Budget Increase

Our capital budget was increased from $75 mm to $85 mm at the September 20, 2023, Board meeting. Our capital program is expected to mainly be funded from cash flow. The company has drilled 12 wells so far this year (including one disposal well) and anticipate four more wells to be drilled in the balance of the year, including two at Sheerness and two at Tide Lake.

We anticipate average production of 6,300 boe/day for 2023 and after-tax cash flow of $76 million based on an average of $80 WTI for the second half of the year.

North 40 is pleased to announce that Calvin House has joined our North 40 team in the role of VP Land & Business Development. Calvin has over 30 years of industry experience and is an excellent addition to our team.

As always, we appreciate and thank you for your support. Please feel free to contact myself or Kim Schoenroth with any questions or comments you may have.

Sincerely,

NORTH 40 RESOURCES LTD.

Don W Robson
President & CEO

NORTH 40
RESOURCES LTD.

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following analysis was prepared as at September 20, 2023, and should be read in conjunction with North 40 Resources Ltd.'s ("North 40" or "the Company") condensed financial statements and notes thereto for the three and six months ended June 30, 2023 and 2022 ("Interim Financial Statements") and the Company's audited financial statements and notes thereto for the years ended December 31, 2022, and December 31, 2021, which have been prepared in accordance with International Financial Reporting Standards ("IFRS" or "GAAP").

Basis of Presentation *– The reporting and the measurement currency is the Canadian dollar. For the purposes of calculating unit costs, natural gas is converted to a barrel of oil equivalent ("boe") using six thousand cubic feet of natural gas equal to one barrel of oil unless otherwise stated.*

Forward-Looking Statements *– Certain information set forth in this document, including management's assessment of North 40's future plans for capital expenditures and expectations for production rates, prices and operating results, contains forward-looking statements. By their nature, forward-looking statements are subject to numerous risks and uncertainties, some of which are beyond North 40's control, including the impact of general economic conditions, industry conditions, volatility of commodity prices, currency fluctuations, imprecision of reserve estimates, environmental risks, competition from other industry participants, the lack of availability of qualified personnel or management, stock market volatility and ability to access sufficient capital from internal and external sources. Readers are cautioned that the assumptions used in the preparation of such information, although considered reasonable at the time of preparation, may prove to be imprecise and, as such, undue reliance should not be placed on forward-looking statements. North 40's actual results, performance or achievement could differ materially from those expressed in, or implied by, these forward-looking statements.*

Non-IFRS Measurements *– Within Management's Discussion and Analysis, references are made to terms commonly used in the oil and gas industry. This document contains "funds flow from operations" which is a non-IFRS financial measure. This document also contains the terms "operating netback", "working capital surplus (deficiency)", and capital expenditures which are non-IFRS financial measures. These non-IFRS terms do not have any standardized meaning prescribed by IFRS and therefore it may not be comparable with the calculation of similar measures for other entities.*

Funds flow from operations

Management uses funds flow from operations to evaluate performance. Funds flow from operations as presented is not intended to represent operating cash flow or operating profits for the period nor should it be viewed as an alternative to cash flow from operating activities. Funds flow from operations per share is calculated based on the weighted average number of shares outstanding consistent with the calculation of net income or loss per share. Total boe is calculated by multiplying the daily production by the number of days in the period.

The following table reconciles funds flow from operations to cash provided by (used in) operating activities, which is the most directly comparable measure calculated in accordance with IFRS.

	Three months ended June 30		*Six months ended June 30*	
(millions)	*2023*	*2022*	*2023*	*2022*
Cash provided by operating activities	*$15.7*	*$17.0*	*$27.6*	*$29.3*
Plus: Net change in non-cash working capital	*1.3*	*(0.5)*	*5.1*	*(1.0)*
Funds flow from operations	*$17.0*	*$16.5*	*$32.7*	*$28.3*

Operating netback

Management uses operating netbacks as a profitability measure relative to current commodity prices. Operating netback is calculated as the average sales price of all its commodities less royalties, operating and transportation expenses. There are no IFRS measures that are reasonably comparable to operating netbacks.

Working capital surplus (deficiency)

Working capital surplus (deficiency) is the total of current assets less current liabilities. This measure is used to assess efficiency, liquidity and general financial strength of the Company.

Capital Expenditures

Capital expenditures are the sum of exploration and evaluation and property and equipment expenditures disclosed in the Statements fo Cash Flow.

	Three months ended June 30		Six months ended June 30	
(thousands, except per unit amounts and where indicated)	2023	2022	2023	2022
FINANCIAL				
Petroleum and natural gas revenue	$33,839	$30,675	$64,507	$53,605
Funds flow from operations *(1)*	$16,989	$16,467	$32,745	$28,293
Per share – basic	$0.22	$0.22	$0.43	$0.38
Per share – diluted	$0.21	$0.20	$0.41	$0.35
Net income	$4,572	$10,222	$9,883	$16,389
Per share – basic	$0.06	$0.14	$0.13	$0.22
Per share – diluted	$0.06	$0.13	$0.12	$0.20
Capital expenditures (2)	$18,656	$18,850	$46,464	$29,732
Working capital surplus (deficiency) *(3)* at end of period	($6,644)	$12,141	($6,644)	$12,141
Common shares outstanding at end of period	76,624	75,340	76,624	75,340
OPERATING				
Sales volumes				
Oil and liquids (bbls/day)	4,203	2,155	3,875	2,088
Natural gas (mcf/day)	12,767	9,363	13,334	9,741
Total (boe/day) (4)	6,331	3,715	6,098	3,711
% Oil and liquids	66	58	64	56
Commodity prices realized (before pipeline tariffs)				
Oil and liquids ($/bbl)	84.41	126.40	85.45	115.68
Natural gas ($/mcf)	2.72	7.91	3.18	6.54
Total ($/boe)	61.53	93.24	61.26	82.25
Operating netback ($/boe) (5)	32.91	56.99	32.94	49.15
Funds flow from operations netback ($/boe) *(1)*	29.49	48.71	29.67	42.12
Net wells drilled	3.0	5.0	9.0	9.0
Net acres of land at end of period	307,909	221,777	307,909	221,777

(1) Funds flow from operations and funds flow from operations netback does not have a standardized meaning prescribed by IFRS. See Non-IFRS Measurements section of the MD&A.
(2) Capital expenditures does not have a standardized meaning prescribed by IFRS. See Non-IFRS Measurements section of the MD&A.
(3) Working capital surplus (deficiency) does not have a standardized measure prescribed by IFRS. See Non-IFRS Measurements section of the MD&A. Working capital deficiency at June 30, 2023, includes $6.9 million in cash ($21.7 million at June 30, 2022, and $19.1 million at December 31, 2022).
(4) Boe conversion is 6:1
(5) Operating netback does not have a standardized meaning prescribed by IFRS. See Non-IFRS Measurements section of the MD&A.

PRODUCTION

	Three months ended June 30		Six months ended June 30	
	2023	2022	2023	2022
Oil (bbls per day)	3,882	1,955	3,565	1,880
Liquids (bbls per day)	321	200	310	208
Natural gas (mcf per day)	12,767	9,363	13,334	9,741
BOE per day	6,331	3,715	6,098	3,711

Production in Q2 2023 averaged 6,331 boe per day (66% oil and liquids) which is a 70% increase from Q2 2022 average of 3,715 boe per day (58% oil and liquids). Production for the first six months of 2023 averaged 6,098 boe per day (64% oil and liquids) compared to 3,711 boe per day (56% oil and liquids) in the same period of 2022. Production increases are primarily due to the 2022 and Q1 2023 drilling program.

Oil and liquids production increased 95% to 4,203 bbls per day in Q2 2023 from 2,155 bbls per day in Q2 2022 and increased 86% to 3,875 bbls per day in the first six months of 2023 from 2,088 bbls per day in the comparable 2022 period. The three Wayne wells drilled in Q1 2023 contributed significantly to this increase as well as production from the 2022 drilling program.

Natural gas production increased 36% and 37% in the quarter and six months ended June 30, 2023, respectively compared to the same periods in 2022. A Drumheller natural gas well brought on production later in the first quarter of 2023 as well as associated natural gas production from the other wells drilled in 2023 contributed significantly to the increase. The

Company shut in non-associated natural gas production (excluding the Drumheller natural gas well drilled in 2023 which is being evaluated) on April 1, 2023, due to low natural gas price realizations.

None of the three wells drilled in Q2 2023 were on production in the quarter.

OPERATING NETBACK

	Three months ended June 30		Six months ended June 30	
($ per BOE)	2023	2022	2023	2022
Revenue [1]	$58.73	$90.74	$58.45	$79.81
Royalties	(12.55)	(22.57)	(12.90)	(19.30)
Operating expenses	(10.39)	(9.39)	(10.14)	(9.66)
Transportation expenses	(2.88)	(1.79)	(2.47)	(1.70)
Operating netback [2]	$32.91	$56.99	$32.94	$49.15

(1) Includes pipeline tariff amount of $2.80 and $2.81 per boe for the three and six months ended June 30, 2023, and $2.50 and $2.44 per boe in the comparable periods of 2022 respectively.
(2) Operating netback does not have a standardized meaning prescribed by IFRS. See Non-IFRS Measurements section of the MD&A.

For the three and six months ended June 30, 2023, the operating netback was lower than the same periods in 2023 primarily due to lower commodity prices and higher operating and transportation expenses partially offset by lower royalties.

COMMODITY PRICES

	Three months ended June 30		Six months ended June 30	
($ per bbl)	2023	2022	2023	2022
WTI (US$/bbl)	$73.78	$108.41	$74.95	$101.35
MSW benchmark price [1]	$95.19	$137.76	$97.26	$126.75
WCS benchmark price [2]	$78.76	$122.04	$74.04	$111.48
Realized crude oil price	$87.15	$130.81	$87.95	$120.26

(1) Mixed sweet blend (MSW) is the benchmark conventionally produced light sweet crude for Western Canada. It is often referenced as Edmonton Par Crude.
(2) Western Canadian Select (WCS) is a Hardisty based blend of conventional and oil sands production. WCS is a heavy sour blend of crude oil.

North 40's realized crude oil price reflects 27° API and differentials are typically close to the average of the MSW and WCS benchmark differentials.

North 40's realized crude oil price (before pipeline tariffs) in Q2 2023 was $87.15 per barrel which is 33% lower than the Q2 2022 price of $130.81 per barrel. WTI benchmark prices decreased 32% from $108.41 per barrel in Q2 2022 to $73.78 per barrel in Q2 2023 contributing to most of the decrease in North 40's realized price. Wider Canadian stream differentials also contributed to the lower realized price in Q2 2023 which was partially offset by a weaker Canadian dollar.

North 40's realized oil price decreased 27% in the first half of 2023 to $87.95 per barrel from $120.26 per barrel realized in the first half of 2022 due to the same factors stated above.

Benchmark WTI prices softened due to recessionary concerns resulting from central bankers continuing to increase interest rates to slow inflation, lower than expected demand from China and a number of regional US banking failures.

	Three months ended June 30		Six months ended June 30	
($ per mcf)	2023	2022	2023	2022
AECO Daily (5A) index	$2.45	$7.24	$2.83	$5.99
Realized natural gas price	$2.72	$7.91	$3.18	$6.54

North 40's natural gas production is sold at the AECO daily 5A index and realizes a slightly better price than the index due to its higher-than-standard heat content. North 40's realized price decreased 66% to $2.72 per mcf in Q2 2023 from $7.91 per mcf in Q2 2022 and decreased 51% to $3.18 per mcf for the first six months of 2023 from $6.54 per mcf in the same period of 2022.

Both Nymex And AECO natural gas prices have moved materially lower due to warmer weather and an increase in Canadian and US supply causing higher storage levels.

REVENUE

	Three months ended June 30		Six months ended June 30	
($ thousands)	2023	2022	2023	2022
Oil and liquids	$31,012	$24,256	$57,592	$42,691
Natural gas	2,827	6,419	6,915	10,914
Petroleum and natural gas revenue	$33,839	$30,675	$64,507	$53,605
% Oil and liquids	92	79	89	80

Note: Petroleum and natural gas revenue presented in the Statements of Income and Comprehensive Income is net of pipeline tariffs.

Revenue in Q2 2023 increased to $33.8 million from $30.7 million in Q2 2022. Most of the increase resulted from higher crude oil production volumes. Increased natural gas and liquids production volumes also contributed to the revenue increase which was partially offset by lower price realizations for all commodities.

Revenue for the six months ended June 30 increased by 20% from $53.6 million in Q2 2022 to $64.5 million in Q2 2023 for the same reasons as the Q2 increase.

Oil and liquids revenue represents 92% of total revenue in Q2 2023 and increased 28%, from $24.3 million in Q2 2022 to $31.0 million in Q2 2023. Crude oil realizations were 33% lower and oil production volumes were 99% higher in Q2 2023 compared to the same quarter last year.

Natural gas revenue decreased 56% in Q2 2023 from $6.4 million in Q2 2022 to $2.8 million in Q2 2023. The decrease is due to a 66% decrease in price realizations partially offset by a 36% increase in production volume in Q2 2023 compared to the same period in Q2 2022.

Oil pipeline tariffs of $1.3 million and $2.3 million are included in revenue for the second quarter and the first six months of 2023 respectively. This compares to $0.5 million and $1.0 million in the same periods of 2022. The custody transfer to the purchaser is at the point the oil is offloaded at the terminal. Gas pipeline tariffs of $0.3 million and $0.8 million are also included in revenue for the three months and six months ended June 30, 2023, respectively. This compares to $0.3 million and $0.6 million in the same periods of 2022. The custody transfer to the purchaser is at the point the natural gas enters the receipt meter.

ROYALTIES

	Three months ended June 30		Six months ended June 30	
(thousands, except per unit amounts)	2023	2022	2023	2022
Royalties	$7,231	$7,631	$14,236	$12,961
Per BOE	$12.55	$22.57	$12.90	$19.30
% of Revenue	21%	25%	22%	24%

Royalties will fluctuate with commodity prices and production rates and are determined primarily by the terms of the mineral rights owner agreements and the Alberta provincial government royalty regime.

Royalties on a boe basis decreased to $12.55 per boe and $7.2 million in the second quarter of 2023 compared to $22.57 per boe and $7.6 million in the second quarter of 2022 commensurate with lower realized commodity prices partially offset by higher production volumes.

Royalties as a percentage of revenue were 21% and 25% in the second quarters of 2023 and 2022 respectively. Royalties as a percentage of revenue decreased to 22% for the first six months of 2023 compared to 24% for the first six months of 2022.

The majority of the Company's royalties are freehold royalties and freehold mineral tax (which is included in royalties for financial reporting purposes).

OPERATING AND TRANSPORTATION

	Three months ended June 30		Six months ended June 30	
(thousands, except per unit amounts)	2023	2022	2023	2022
Operating expenses	$5,986	$3,173	$11,193	$6,491
Per BOE	$10.39	$9.39	$10.14	$9.66
Transportation expenses	$1,660	$605	$2,730	$1,139
Per BOE	$2.88	$1.79	$2.47	$1.70

Operating expenses averaged $10.39 and $10.14 per boe for the second quarter and the first six months of 2023, respectively compared to $9.39 and $9.66 per boe in the second quarter and first six months of 2022. Main contributors to the increase were well servicing costs, water handling costs, and the impact of inflationary pressures most prevalent with labor services, chemicals and fuel.

Transportation costs, which are clean oil trucking expenses, averaged $2.88 and $2.47 per boe in the second quarter and the first six months of 2023, respectively compared to $1.79 and $1.70 per boe in the second quarter and first half of 2022, respectively. The cost is incurred on oil production only and therefore decreases in the natural gas production weighting will increase the per boe cost. Natural gas production represented 34% of total production in Q2 2023 and 42% in Q2 2022.

North 40's crude oil production may be sold in different sales streams in Alberta which may vary month to month depending on the netback at those different streams. As a result, there will be fluctuations in crude oil differentials and transportation costs as the Company seeks out the highest netback opportunity.

GENERAL AND ADMINISTRATIVE

	Three months ended June 30		Six months ended June 30	
(thousands, except per unit amounts)	2023	2022	2023	2022
Gross G&A	$740	$670	$1,614	$1,355
Capitalized G&A	(43)	(42)	(88)	(87)
Net G&A	$697	$628	$1,526	$1,268
Per BOE	$1.21	$1.86	$1.38	$1.89

Net general and administrative ("G&A") expenses were $0.7 million and $1.5 million for the second quarter and first half of 2023 respectively compared to $0.6 million and $1.3 million in the comparable periods of 2022. There were higher costs for professional and contractor services as well as computer software costs in 2023 compared to 2022. On a boe basis, net G&A was $1.21 and $1.38 per boe in Q2 and first half of 2023 respectively compared to $1.86 and $1.89 per boe in same periods of 2022. The decrease in the per boe amount is due to higher production volumes.

The most significant costs in the first half of 2023 can be attributed to employee salaries and benefits as well as professional and contractor services.

Capitalized G&A relates to a portion of the Company's engineering compensation.

SHARE-BASED COMPENSATION

	Three months ended June 30		Six months ended June 30	
(thousands, except per unit amounts)	2023	2022	2023	2022
Share-based compensation	$734	$38	$804	$78
Capitalized share-based compensation	(92)	(3)	(96)	(7)
	$642	$35	$708	$71
Per BOE	$1.11	$0.10	$0.64	$0.11

Share-based compensation expense is related to the issuance of Class B and C shares and the grants of options on Class B and C shares to directors, officers, employees, and consultants.

In June 2023, the Board of Directors extended the expiry of certain Class B and Class C shares and options to September 2026 from September 2023. The term extension is a modification under IFRS and requires an update to the calculation of share-based compensation expense.

Incremental value of $0.6 million was determined for the vested Class B shares and options. This incremental value is recognized immediately and $0.5 million has been expensed and $0.1 million has been capitalized in the second quarter.

Incremental value of $1.1 million was determined for the Class C shares and options and will be recognized over the estimated remaining expected term of 1.8 years for the Class C shares and options. The Company recognized $25,803 as share based compensation expense and capitalized $1,590 in the second quarter.

Detailed information regarding the Class B and Class C shares and options have been disclosed in Note 10 of the financial statements.

DEPLETION AND DEPRECIATION

	Three months ended June 30		Six months ended June 30	
(thousands, except per unit amounts)	2023	2022	2023	2022
Depletion and depreciation	$11,003	$5,397	$20,630	$10,178
Per BOE	$19.10	$15.96	$18.69	$15.15

The Company recognized depletion and depreciation expense ("D&D") of $11.0 million ($19.10 per boe) and $20.6 million ($18.69 per boe) for the quarter and six months ended June 30, 2023, respectively compared to $5.4 million ($15.96 per boe) and $10.2 million ($15.15 per BOE) in the same periods of 2022. The D&D expense was based on an internal evaluation of proved and probable reserves and an internal estimate of future development costs.

D&D expense increased in Q2 2023 and the first six months of 2023 compared to the same periods in 2022 largely due to higher production volume as well as a higher rate. Higher estimates for future development costs, due to additional capital and inflation, are the main contributors to the increase in the per unit D&D expense in 2023.

The D&D expense recognized was comprised primarily of depletion expense with minor amounts relating to depreciation of office assets. In Q2 2022, included in depletion and depreciation, is an impairment charge of $0.2 million related to equipment failure at a Drumheller North oil battery. In addition, other income of $0.2 million was recognized in the Q2 2022 for estimated expected insurance proceeds for the damaged equipment.

D&D per boe will differ from period to period depending on the amount and type of capital spending, the number of reserves added, and production volume. The Company uses total proved plus probable reserves as its depletion base in the calculation of depletion.

EXPLORATION EXPENSE

North 40 recognized exploration expense of $0.1 million ($0.24 per boe) in Q2 2023 and $0.2 million ($0.21 per boe) in the first half of 2023. This compares to $0.1 million ($0.19 per boe) in Q2 2022 and $0.3 million ($0.45 per boe) in the first half of 2022. Exploration expense relates to undeveloped land expiries.

FINANCE EXPENSE

	Three months ended June 30		Six months ended June 30	
(thousands)	2023	2022	2023	2022
Accretion of decommissioning obligations	$55	$43	$107	$80
Banking fees	85	29	108	45
Interest on lease liabilities	5	7	10	15
Total	$145	$79	$225	$140
Per BOE	$0.25	$0.23	$0.20	$0.21

Finance expense relates to accretion on decommissioning obligations, banking fees and interest on lease liabilities. Banking fees include standby fees and fees associated with the annual bank facility review. Accretion of decommissioning obligations and interest on lease liabilities are non-cash charges. The increase in accretion of decommissioning obligations is mostly due to the increase in interest rates.

North 40 increased its bank credit facility to $25 million from $8.5 million in late 2022. The increase in banking fees in 2023 is largely due to fees related to this increase as well as higher standby fees.

INCOME TAXES

North 40 recognized current income tax expense of $1.3 million in Q2 2023 and $2.3 million for the first half of the year compared to $2.4 million and $3.6 million in the comparable periods of 2022 respectively.

Deferred income taxes arise from differences between the accounting and tax basis of assets and liabilities. The estimate of deferred taxes is based on the current tax status of the Company, enacted legislation, and management's best estimates of future events.

For the three and six months ended June 30, 2023, a deferred income tax expense of $0.6 million and $1.2 million, respectively, was recognized compared to a deferred income tax expense of $0.7 million and $1.3 million for the comparable periods in 2022.

The following tax pool balances are estimated at June 30, 2023:

(thousands)	Maximum Annual Deduction	June 30 2023	June 30 2022
Canadian oil and gas property expense (COGPE)	10%	15,239	$15,333
Canadian development expense (CDE)	30%	50,350	39,490
Undepreciated capital cost (UCC)	25%	38,316	20,560
		$103,905	$75,383

NET INCOME AND COMPREHENSIVE INCOME

	Three months ended June 30		Six months ended June 30	
(thousands)	2023	2022	2023	2022
Net income and comprehensive income	$4,572	$10,222	$9,883	$16,389
Per share - basic	$0.06	$0.14	$0.13	$0.22
Per share - diluted	$0.06	$0.13	$0.12	$0.20

The decrease in net income for the three and six months ended June 30, 2023, as compared to the same periods in 2022 is primarily due to increases in operating and transportation costs, share-based compensation expense, and depletion and depreciation partially offset by an increase in revenue, lower royalties and current and deferred income taxes.

CAPITAL EXPENDITURES

Capital expenditures by type and by property for the three and six months ended June 30, 2023, and 2022 were as follows:

	Three months ended June 30		Six months ended June 30	
(thousands)	2023	2022	2023	2022
Land and lease rentals [(1)]	$528	$2,327	$769	$2,612
Seismic and geological	1,738	116	1,889	120
Drilling and completion	7,343	9,121	23,527	17,817
Equipping and tie-ins	4,037	7,245	13,081	9,096
Facilities	4,875	-	7,017	-
Office and other	135	41	181	87
Total capital expenditures	$18,656	$18,850	$46,464	$29,732

(1) Net of land fund reimbursements.

	Three months ended June 30		Six months ended June 30	
(thousands)	2023	2022	2023	2022
Wayne (formerly Drumheller North)	$12,764	$7,772	$25,379	$14,003
Drumheller	2,193	7,672	9,687	12,104
Sheerness	1,880	-	1,880	-
Matziwin	493	2,398	5,555	2,515
Princess	679	739	2,428	782
Other	647	269	1,535	328
Total capital expenditures	$18,656	$18,850	$46,464	$29,732

Wells drilled by property were as follows:

	Three months ended June 30		Six months ended June 30	
	2023	2022	2023	2022
Wayne (formerly Drumheller North)	3	2	6	4
Drumheller [(1)]	-	2	1	4
Wintering Hills [(1)]	-	1	-	1
Matziwin South [(2)]	-	-	1	-
Princess	-	-	1	-
Total	3	5	9	9

(1) Included in Drumheller area
(2) Included in Matziwin area

Capital expenditures in Q2 2023 were $18.5 million. Capital activity included the drilling of three wells at Wayne (formerly Drumheller North), leasing of land and purchase of 3D seismic data at Sheerness, continued construction and start up of the Wayne oil battery, continued construction of the water disposal facility at Drumheller and well workovers. Capital was also expended on equipment purchases for future locations and equipping and tie-in projects.

For the first six months of 2023 capital expenditures were $46.3 million which included the drilling of nine wells. The majority of the capital was spent at Wayne where six wells were drilled and an oil battery was constructed. The battery became operational in Q2. Activity at Drumheller included the drilling of one well and construction of water disposal facilities which will become operational later in the year. Other activities include acquisition of land leases and purchase of 3D seismic data at Sheerness (a new North 40 area), one well at each of Matziwin South and Princess, workover and recompletion operations, and equipment purchases for future locations.

Capital expenditures in the second quarter of 2022 were $18.8 million. Capital activity included the drilling of five wells with three of those wells completed in the quarter, recompletion of three acquired wellbores (two at Princess and one at Matziwin South) and the extension of freehold leases at Matziwin South. None of the wells drilled in the second quarter were brought on production in the quarter.

For the first six months of 2022 capital expenditures were $29.6 million which included the drilling of nine wells. The majority of capital has been expended in the Wayne (formerly Drumheller North) and Drumheller area with four wells drilled at each of Wayne and Drumheller and one well at Wintering Hills. Capital was also expended to upgrade existing surface facilities to meet new regulatory standards with new wells being added to existing leases.

North 40's land holdings per area were as follows:

(acres)	June 30 2023	December 31, 2022	June 30 2022
Wayne (formerly Drumheller North)	15,630	17,702	15,170
Drumheller	57,175	80,390	79,363
Sheerness	118,527	7,912	7,912
Matziwin	54,902	78,579	79,020
Princess	18,858	18,700	18,700
Tide Lake	10,444	10,444	10,444
Other	32,372	10,851	11,168
Total	307,909	224,578	221,777

The increase in land holdings at June 30, 2023, compared to the same time last year is primarily due to the acquisition of leases at Sheerness partially offset by undeveloped land expiries at Drumheller and Matziwin.

The land holdings consist of 65% crown and 35% freehold leases at June 30, 2023. Working interest in North 40's land holdings is 100 percent.

DECOMMISSIONING OBLIGATIONS

Decommissioning obligations are based on estimated costs and timing to abandon and reclaim ownership interests in oil and natural gas assets. North 40 has recognized a provision for decommissioning obligations of $7.0 million at June 30, 2023 ($6.3 million at December 31, 2022).

Estimated abandonment and reclamation costs are based on the directives issued by the Alberta Energy Regulator and management's experience. The decommissioning obligation is measured using the estimated present value of costs to abandon and reclaim all ownership interests. A risk-free rate of 3.21% (3.29% at December 31, 2022) and an inflation rate of 2.20% (2.20% at December 31, 2022) were used to calculate the best estimate of the decommissioning obligation. The increase in the decommissioning obligation at June 30, 2023, compared to December 31, 2022, is primarily due to new liabilities recognized for wells drilled.

LIQUIDITY AND CAPITAL RESOURCES

At June 30, 2023, the Company had no drawn debt and a working capital deficiency of $6.6 million comprised of $6.9 million in cash and a working capital deficit of $13.5 million. All activities to date have been funded with proceeds from the Company's initial equity financing, cash flow from operations, land fund reimbursements and interest income on cash balances.

At June 30, 2023, the Company had a $25.0 million revolving demand operating facility with a Canadian chartered bank. The facility bears interest based on the prime rate or banker's acceptance rates plus a margin. Interest rates applicable to draws and standby fees are based on a pricing margin grid and will change as a result of the ratio of net debt to cash flow as calculated in accordance with the credit facility agreement. Standby fees on undrawn amounts are currently 0.25%. The Company has a letter of credit outstanding for $0.5 million at June 30, 2023 that reduces the amount otherwise available to be drawn on the operating facility.

The facility includes a financial covenant that requires the working capital, adjusted for unrealized hedging, the current portion of debt, and the undrawn availability under the facility, to not be less than 1.0 at each fiscal quarter end. The Company was in compliance with this covenant at June 30, 2023. The facility also includes a covenant that the Company maintain a liability management rating (LMR) established by each applicable energy regulator of not less than 2. The Company's LMR at June 30, 2023 is 18.7. Advances under the facility are secured by a first floating charge debenture and borrowings under the facility may be made by way of prime loans and banker's acceptances. The credit facility is subject to periodic review at the lenders' discretion. A review was completed May 31, 2023 with no changes to the amount and terms of the credit facility. The next review date has been set for November 30, 2023.

The Company has entered into a Royalty Acquisition Agreement (the "agreement") with an arm's length party (the "party") whereby the party will fund certain crown land purchases incurred by the Company in exchange for a royalty on future production from those crown lands. The term of the agreement is to October 31, 2024. The agreement includes a funding limit of $14 million, which may be increased at the sole discretion of the party. At June 30, 2023, there is $4.0 million remaining on the funding limit.

SELECTED QUARTERLY INFORMATION

Three Months Ended	Jun 30 2023	Mar 31 2023	Dec 31 2022	Sept 30 2022	Jun 30 2022	Mar 31 2022	Dec 31 2021	Sep 30 2021
FINANCIAL								
Petroleum and natural gas revenue	$33,839	$30,668	$34,029	$28,699	$30,675	$22,930	$22,927	$18,861
Funds flow from operations [(1)]	$16,989	$15,755	$18,206	$15,011	$16,467	$11,826	$13,497	$10,984
Per share – basic	$0.22	$0.21	$0.24	$0.20	$0.22	$0.16	$0.18	$0.15
Per share – diluted	$0.21	$0.20	$0.23	$0.18	$0.20	$0.15	$0.17	$0.14
Net income	$4,572	$5,311	$7,677	$6,291	$10,222	$6,166	$6,190	$5,032
Per share – basic	$0.06	$0.07	$0.10	$0.08	$0.14	$0.08	$0.08	$0.07
Per share – diluted	$0.06	$0.07	$0.10	$0.08	$0.13	$0.08	$0.08	$0.07
Capital expenditures [(2)]	$18,656	$27,808	$17,852	$20,385	$18,850	$10,882	$6,530	$13,986
Working capital surplus (deficiency) at end of period [(3)]	($6,644)	($4,946)	$7,139	$6,737	$12,141	$14,401	$13,486	$6,545
Common shares outstanding end of period	76,624	76,624	76,624	76,624	75,340	75,250	75,250	75,250
OPERATING								
Sales volumes								
Oil and liquids (bbls/day)	4,203	3,544	3,391	2,656	2,155	2,020	2,554	2,454
Natural gas (mcf/day)	12,767	13,907	10,693	9,897	9,363	10,122	8,731	6,460
Total (boe/day) [(4)]	6,331	5,862	5,174	4,306	3,715	3,707	4,009	3,531
% Oil and liquids	66	60	66	62	58	54	64	70
Commodity prices realized (before pipeline tariffs)								
Oil and liquids ($/bbl)	84.41	86.71	96.05	104.34	126.40	104.13	83.71	76.21
Natural gas ($/mcf)	2.72	3.60	5.42	4.59	7.91	5.26	5.11	4.07
Total ($/boe)	61.53	60.96	74.17	74.91	93.24	71.10	64.46	60.42
Operating netback [(5)] ($/boe)	32.91	32.96	42.56	41.97	56.99	41.20	39.66	35.26
Funds flow from operations netback ($/boe) [(1)]	29.49	29.86	38.25	37.89	48.71	35.45	36.60	33.81
Net wells drilled	3.0	6.0	3.0	5.0	5.0	4.0	-	7.0
Net acres of land at end of period	307,909	191,849	224,578	221,828	221,777	235,266	256,346	254,682

(1) Funds flow from operations and funds flow from operations netback does not have a standardized meaning prescribed by IFRS. See Non-IFRS Measurements section of the MD&A.
(2) Capital expenditures does not have a standardized meaning prescribed by IFRS. See Non-IFRS Measurements section of the MD&A.
(3) Working capital surplus (deficiency) does not have a standardized measure prescribed by IFRS. See Non-IFRS Measurements section of the MD&A.
(4) Boe conversion is 6:1.
(5) Operating netback does not have a standardized meaning prescribed by IFRS. See Non-IFRS Measurements section of the MD&A

Significant factors and trends that have impacted the Company's results during the above periods include:

- Organic growth in production volume from the Company's drilling program.
- In early 2020, crude oil prices experienced a rapid and sudden decline as the COVID-19 global pandemic began to negatively impact crude oil demand and a dispute amongst major oil producing nations resulted in additional crude oil supply. Crude oil prices began a gradual increase mid-year supported by coordinated production cuts by OPEC and OPEC+, voluntary production curtailments by producers and reduced drilling activity. In 2021, global demand, notably in large economies such as the United States and China, was increasing in response to continued recovery from the COVID-19 pandemic, vaccination programs and significant adherence to production cuts by OPEC and OPEC+. This was partially offset by new waves of COVID-19 and the spread of variant cases.
- The volatility in commodity prices and the resultant effect on revenue, funds flow from operations, and net income.
- Current income tax expense was first recognized in Q1 2022.

NORTH 40

RESOURCES LTD.

Quarterly Condensed Interim Financial Statements
June 30, 2023

North 40 Resources Ltd.
Statements of Financial Position

As at	June 30 2023	December 31 2022
($ thousands)		
ASSETS		
Current Assets		
Cash	6,878	19,066
Accounts receivable	10,021	10,853
Prepaids and deposits	1,166	691
Total Current Assets	18,065	30,610
Exploration and evaluation assets (Note 4)	22,982	23,318
Property and equipment (Note 5)	153,218	126,595
Total Assets	**194,265**	**180,523**
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities		
Accounts payable and accrued liabilities	24,039	18,923
Current income taxes (Note 7)	670	4,548
Total Current Liabilities	24,709	23,471
Lease liabilities (Note 9)	184	248
Decommissioning obligations (Note 8)	6,966	6,273
Deferred income taxes	14,984	13,796
Total Liabilities	46,843	43,788
Shareholders' Equity		
Share capital (Note 10)	76,245	76,245
Contributed surplus	4,146	3,342
Retained earnings	67,031	57,148
Total Shareholders' Equity	147,422	136,735
Total Liabilities and Shareholders' Equity	**194,265**	**180,523**

The accompanying notes are an integral part of these Financial Statements.

North 40 Resources Ltd.

Statements of Net Income and Comprehensive Income

(unaudited)	Three months ended June 30		Six months ended June 30	
	2023	**2022**	**2023**	**2022**
($ thousands except per share amounts)				
Revenue				
Petroleum and natural gas revenue (Note 11)	33,839	30,675	64,507	53,605
Less: Royalties	7,231	7,631	14,236	12,961
	26,608	23,044	50,271	40,644
Interest income	104	58	331	85
Other income	-	166	-	166
	26,712	23,268	50,602	40,895
Expenses				
Operating	5,986	3,173	11,193	6,491
Transportation	1,660	605	2,730	1,139
General and administrative	697	628	1,526	1,268
Share-based compensation (Note 10)	642	35	708	71
Depletion and depreciation (Note 5)	11,003	5,397	20,630	10,178
Exploration expense (Note 4)	138	63	229	300
Finance expense	145	79	225	140
Total expenses	20,271	9,980	37,241	19,587
Income before taxes	6,441	13,288	13,361	21,308
Current income tax expense	1,290	2,359	2,290	3,644
Deferred income tax expense	579	707	1,188	1,275
Net Income and Comprehensive Income	**4,572**	**10,222**	**9,883**	**16,389**
Net Income per share (Note 12)				
Basic	$0.06	$0.14	$0.13	$0.22
Diluted	$0.06	$0.13	$0.12	$0.20

The accompanying notes are an integral part of these Financial Statements.

North 40 Resources Ltd.
Statements of Changes in Equity
(unaudited)

($ thousands)	Share Capital	Contributed Surplus	Retained Earnings	Total Equity
Balance as at December 31, 2021	**75,416**	**3,832**	**26,283**	**105,531**
Net income	-	-	16,389	16,389
Issue of share capital	153	-	-	153
Share based compensation (Note 10)	-	78	-	78
Balance as at June 30, 2022	**75,589**	**3,910**	**42,672**	**122,151**
Balance as at December 31, 2022	**76,245**	**3,342**	**57,148**	**136,735**
Net income	-	-	9,883	9,883
Share-based compensation (Note 10)	-	804	-	804
Balance as at June 30, 2023	**76,245**	**4,146**	**67,031**	**147,422**

The accompanying notes are an integral part of these Financial Statements.

North 40 Resources Ltd.
Statements of Cash Flow

(unaudited)	Three months ended June 30		Six months ended June 30	
	2023	**2022**	**2023**	**2022**
($ thousands)				
Cash provided by (used in):				
Operating activities				
Net income for the year	4,572	10,222	9,883	16,389
Adjusted for:				
Depletion and depreciation (Note 5)	11,003	5,397	20,630	10,178
Exploration expense (Note 4)	138	63	229	300
Accretion expense (Note 8)	55	43	107	80
Share-based compensation (Note 10)	642	35	708	71
Deferred income tax expense	579	707	1,188	1,275
	16,989	16,467	32,745	28,293
Net change in non-cash working capital (Note 13)	(1,310)	524	(5,127)	1,000
	15,679	16,991	27,618	29,293
Financing activities				
Issue of share capital (Note 10)	-	153	-	153
Repayment of lease liabilities (Note 9)	(30)	(30)	(62)	(57)
	(30)	123	(62)	96
Investing activities				
Exploration and evaluation expenditures (Note 4)	(2,584)	(3,361)	(2,928)	(3,532)
Property and equipment expenditures (Note 5)	(16,072)	(15,489)	(43,536)	(26,200)
Net change in non-cash working capital (Note 13)	1,965	4,258	6,720	8,142
	(16,691)	(14,592)	(39,744)	(21,590)
Change in cash and cash equivalents	(1,042)	2,522	(12,188)	7,799
Cash and cash equivalents, beginning of period	7,920	19,229	19,066	13,952
Cash and cash equivalents, end of period	**6,878**	**21,751**	**6,878**	**21,751**
Cash income tax paid	900	-	6,168	-

The accompanying notes are an integral part of these Financial Statements.

North 40 Resources Ltd.
Notes to the Financial Statements

June 30, 2023, and 2022 *(all tabular amounts in thousands of Canadian $, except per share amounts or as otherwise indicated)*

1. CORPORATE INFORMATION

North 40 Resources Ltd. (the "Company" or "North 40"), is a privately held oil and gas exploration and development company incorporated in the province of Alberta, Canada on October 16, 2007. The Company was not active until April 2016. The address of the principal place of business is 400, 215 – 9th Avenue SW, Calgary, Alberta, Canada T2P 1K3.

The Company explores, acquires, develops, and produces oil and natural gas reserves in the Western Canadian Sedimentary Basin.

2. BASIS OF PRESENTATION

(a) Statement of Compliance

These condensed financial statements have been prepared by management in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB").

These financial statements have been prepared using the accounting policies and methods as described in Note 3 below.

These financial statements were approved and authorized for issuance by the Board of Directors on September 20, 2023.

3. SIGNIFICANT ACCOUNTING POLICIES

All accounting policies followed in preparation of these financial statements are consistent with those of the previous financial year. The Company's significant accounting policies are disclosed in Note 3 of the financial statements for the year ended December 31, 2022.

4. EXPLORATION AND EVALUATION ASSETS

($)	June 30 2023	December 31 2022
Balance, beginning of period	23,318	21,422
Additions	2,928	8,905
Exploration expense	(229)	(523)
Transferred to property and equipment	(3,035)	(6,486)
Balance, end of period	22,982	23,318

Exploration and evaluation ("E&E") assets consist of the Company's undeveloped land, geological and geophysical assets and exploration drilling projects in which technical feasibility or commercial viability has yet to be determined. Costs primarily relate to undeveloped land.

Exploration expense relate primarily to undeveloped land expiries.

5. PROPERTY AND EQUIPMENT

($)	June 30 2023	December 31 2022
Property and equipment, at cost	254,352	207,099
Accumulated depletion and depreciation	(101,134)	(80,504)
Net book value, end of period	153,218	126,595
Reconciliations of movements during the period:		
Cost, beginning of period	207,099	142,002
Accumulated depletion and depreciation, beginning of period	(80,504)	(55,459)
Net book value, beginning of period	126,595	86,543
Additions	43,632	59,001
Transferred from exploration and evaluation assets	3,035	6,486
Changes in decommissioning obligations (Note 8)	586	(390)
Depletion and depreciation	(20,630)	(25,045)
Net book value, end of period	153,218	126,595

Included in the calculation of depletion was an estimate for future development costs of $70.8 million at June 30, 2023 ($85.0 million at December 31, 2022). An estimated future salvage value of $6.0 million was excluded from the calculation of depletion at June 30, 2023 ($5.5 million at December 31, 2022).

Included in the June 30, 2023, property and equipment balance is the right-of-use asset of $0.2 million ($0.2 million at December 31, 2022).

Included in additions is capitalized general and administrative expenses of $0.2 million ($0.3 million at December 31, 2022).

At June 30, 2023, there were no indicators of impairment identified and an impairment test was not performed.

6. CREDIT FACILITY

At June 30, 2023, the Company had a $25.0 million revolving demand operating facility with a Canadian chartered bank. The facility bears interest based on the prime rate or banker's acceptance rates plus a margin. Interest rates applicable to draws and standby fees are based on a pricing margin grid and will change as a result of the ratio of net debt to cash flow as calculated in accordance with the credit facility agreement. Standby fees on undrawn amounts are currently 0.25%. The Company has a letter of credit outstanding for $0.5 million at June 30, 2023 that reduces the amount otherwise available to be drawn on the operating facility.

The facility includes a financial covenant that requires the working capital, adjusted for unrealized hedging, the current portion of debt, and the undrawn availability under the facility, to not be less than 1.0 at each fiscal quarter end. The Company was in compliance with this covenant at June 30, 2023. The facility also includes a covenant that the Company maintain a liability management rating (LMR) established by each applicable energy regulator of not less than 2. The Company's LMR at June 30, 2023 is 18.7. Advances under the facility are secured by a first floating charge debenture and borrowings under the facility may be made by way of prime loans and banker's acceptances. The credit facility is subject to periodic review at the lenders' discretion. A review was completed May 31, 2023 with no changes to the amount and terms of the credit facility. The next review date has been set for November 30, 2023.

7. CURRENT INCOME TAXES

($)	**June 30 2023**	**December 31 2022**
Balance, beginning of period	4,548	-
Current income tax expense	2,290	4,548
Payments [1]	(6,168)	-
Balance, end of period	670	4,548

[1] *Includes instalments.*

8. DECOMMISSIONING OBLIGATIONS

The Company's decommissioning obligations result from its responsibility to abandon and reclaim its net ownership interests in oil and natural gas assets including well sites, gathering systems and facilities. The Company estimates the total uninflated undiscounted amount of cash flows required to settle its decommissioning obligations is approximately $8.1 million ($7.4 million at December 31, 2022). A risk-free rate of 3.21% and an inflation rate of 2.20% were used to calculate the best estimate of the decommissioning obligations compared to 3.29% and 2.20% respectively which were the rates used at December 31, 2022.

A reconciliation of the decommissioning obligations is provided below.

($)	**June 30 2023**	**December 31 2022**
Balance, beginning of period	6,273	6,486
Liabilities incurred	557	1,398
Change in estimates	29	(1,788)
Accretion expense	107	177
Balance, end of period	6,966	6,273

9. LEASE LIABILITIES

The Company incurs lease payments related to office facilities. For the six months ended June 30, 2023, finance expense of $9,900 ($15,294 for the six months ended June 30, 2022) and repayment of lease liabilities of $57,840 ($57,840 for the six months ended June 30, 2022) were recognized for a total cash outflow of $73,134 ($73,134 for the six months ended June 30, 2022). Lease obligations contractually expire in January 2025.

10. SHARE CAPITAL

Authorized

Unlimited number of common voting shares (“common shares”) without nominal or par value
Unlimited number of Class B common non-voting shares (“Class B”) without nominal or par value
Unlimited number of Class C common non-voting shares (“Class C”) without nominal or par value

Issued and Outstanding		**June 30 2023**		**December 31 2022**
	Number *(thousands)*	**Consideration**	**Number** *(thousands)*	**Consideration**
Common Shares				
Balance, beginning of period	76,624	$76,093	75,250	$75,228
Issued for cash	-	-	90	153
Issued on conversion of Class B’s and C’s	-	-	1,284	712
Balance, end of period	76,624	$76,093	76,624	$76,093
Class B Common Non-Voting Shares				
Balance, beginning of period	4,870	$49	6,370	$64
Converted to common shares	-	-	(1,500)	($15)
Balance, end of period	4,870	$49	4,870	$49
Class C Common Non-Voting Shares				
Balance, beginning of period	10,380	$103	12,480	$124
Converted to common shares	-	-	(1,050)	(11)
Forfeited	-	-	(1,050)	(10)
Balance, end of period	10,380	$103	10,380	$103
Total		$76,245		$76,245

Common Shares

Common shares are subject to the provisions and terms contained in Schedule A of the Company’s Articles of Incorporation and to the provisions and terms of the respective share subscription agreements among the Company and its shareholders.

Class B Shares and Options on Class B Shares

Class B shares and options on Class B shares have been reserved for issue to directors, officers, employees, and consultants of the Company. The aggregate number of Class B shares and options issued may not exceed 10% of the issued and outstanding common shares of the Company

Class B shares are convertible to common shares of the Company until expiry in September 2026 at an exercise price of $1.00 per share. One third of the Class B shares purchased and options granted will vest equally on each of the second, third and fourth anniversary of the issue date. At June 30, 2023, 5,483,500 Class B shares and options were vested (6,802,583 at June 30, 2022).

The number and weighted average exercise price of the options on Class B shares are as follows:

	Number of Options	**Weighted Average Exercise Price**
Balance, January 1, 2022	932,750	$0.61
Granted	619,250	0.81
Exercised	(37,500)	(0.77)
Forfeited	(112,500)	(0.51)
Balance, December 31, 2022	1,402,000	$0.70
Granted	100,000	1.00
Forfeited	(70,000)	(0.61)
Balance, June 30, 2023	1,432,000	$0.73

In 2022, 1,500,000 Class B shares and 37,500 options on Class B shares were converted into common shares through a cashless exercise.

The fair market value of each Class B share issued and option granted was estimated on the date of issue using the Black-Scholes pricing model and the following weighted average assumptions in the calculations:

Weighted average risk-free interest rate (%)	1.21
Expected life (years)	3.1- 4.0
Estimated volatility of underlying common shares (%)	50
Share Price ($)	1.20
Estimated forfeiture rate (%)	nil

The Company recognized share-based compensation expense of $460,956 and $506,264 related to the Class B shares and options for the three and six months ended June 30, 2023 ($25,646 and $49,970 for the three and six months ended June 30, 2022) and capitalized $88,930 and $91,607 ($2,008 and $4,038 for the quarter and six months ended June 30, 2022).

In June 2023, the Board of Directors extended the expiry of certain Class B shares and options to September 2026 from September 2023. The term extension is a modification under IFRS and requires an update to the calculation of share-based compensation expense. The incremental value of $0.6 million was determined for the vested Class B shares and options. This incremental value is recognized immediately and $0.5 million has been expensed and $0.1 million has been capitalized in the second quarter.

The incremental value is the difference in value immediately before the modification (term extension) and immediately after the modification. The following assumptions were used in the calculations:

	Before Modification	**After Modification**
Weighted average risk-free interest rate (%)	4.83	4.55
Expected life (years)	0.3	1.8
Estimated volatility of underlying common shares (%)	60	60
Share Price ($)	1.99	1.99
Estimated forfeiture rate (%)	nil	nil

Class C Shares and Options on Class C Shares

Class C shares and options on Class C shares have been reserved for issue to directors, officers, employees, and consultants of the Company. The aggregate number of Class C shares and options issued may not exceed 20% of the issued and outstanding common shares of the Company.

Class C shares are convertible to common shares of the Company if a liquidity event occurs before September 2026 at certain minimum price thresholds per share. A liquidity event includes the sale of all or substantially all of the common shares of the Company or assets for consideration that includes cash and/or securities, the liquidation of the Company, or any listing of the Company on a recognized exchange. The Class C shares were issued with various minimum price vesting and exercise price thresholds.

A summary of the number of Class C shares (assuming exercise of options on Class C shares) that vest and are convertible upon achieving price thresholds and at various exercise prices is as follows:

Number of Class C Shares Convertible	**Liquidity Event Price Per Fully Diluted Share**	**Conversion Price Per Share**
2,175,667	$1.50	$1.00
2,175,667	$2.00	$1.15
2,175,667	$2.25	$1.30
2,175,667	$2.50	$1.45
2,175,667	$2.75	$1.60
2,175,667	$3.00	$1.75

In June 2023, the Board of Directors eliminated the terms to increase both the liquidity event price and the conversion price by eight percent compounded annually beginning in June 2023 until the date the Company enters into a definitive agreement for the completion of a liquidity event.

The number and weighted average exercise price of the options on Class C shares are as follows:

	Number of Options	Weighted Average Exercise Price
Balance, January 1, 2022	1,695,500	$0.61
Granted	1,268,500	0.80
Exercised	(157,500)	(0.43)
Forfeited	(262,500)	(0.66)
Balance, December 31, 2022	2,544,000	$0.71
Granted	200,000	1.00
Forfeited	(70,000)	(0.62)
Balance, June 30, 2023	2,161,500	$0.74

In 2022, 1,050,000 Class C shares and 157,500 options on Class C shares were converted into common shares through a cashless exercise.

The fair market value of each Class C share issued and option granted was estimated on the date of issue using the Black-Scholes pricing model and the following assumptions in the calculations:

Weighted average risk-free interest rate (%)	1.11
Expected life (years)	3.8
Estimated volatility of underlying common shares (%)	50
Share Price ($)	1.20
Estimated forfeiture rate (%)	nil

In addition, the Company assumed the probability of a liquidity event within the term to be 25% and the probability of achieving the price thresholds disclosed in the table above to be 95%, 90%, 90%, 85%, 85% and 80%, respectively.

The Company recognized share-based compensation expense of $35,723 and $56,548 related to the Class C non-voting shares for the three and six months ended June 30, 2023 ($10,963 and $21,171 for the three and six months ended June 30, 2022) and capitalized $3,175 and $4,743 ($1,187 and $2,388 for the three and six months ended June 30, 2022).

In June 2023, the Board of Directors extended the expiry of certain Class C shares and options to September 2026. The term extension is a modification under IFRS and requires an update to the share-based compensation expense. The incremental value of $1.1 million was determined and will be recognized over the estimated remaining expected term of 1.8 years for the Class C shares and options. The Company recognized $25,803 as share based compensation expense and capitalized $1,590 in the second quarter.

The incremental value is the difference in value immediately before the modification (term extension) and immediately after the modification. The following assumptions were used in the calculations:

	Before Modification	After Modification
Weighted average risk-free interest rate (%)	4.83	4.55
Expected life (years)	0.3	1.8
Estimated volatility of underlying common shares (%)	60	60
Share Price ($)	1.99	1.99
Estimated forfeiture rate (%)	nil	nil

11. REVENUES

The Company produces crude oil, natural gas, and natural gas liquids from its assets in Alberta. The Company sells its production pursuant to variable-price physical delivery contracts. The transaction price for variable-price contracts is based on a benchmark commodity price, adjusted for quality, location and/or other factors whereby each component of the pricing component is fixed or variable, depending on the contract terms. Under the contracts, the Company is required to deliver fixed or variable quantities of crude oil, natural gas, and natural gas liquids to the contract counterparty.

Petroleum and natural gas revenue is recognized when control is transferred from North 40 to its customers which is typically when the product enters the terminal or pipeline. Revenue is measured based on the consideration specified in a contract with the customer and the volumes delivered. North 40's revenue was generated in Alberta and sold to customers in the oil and natural gas business subject to normal credit terms and under customary industry sale and payment terms at monthly market prices. Contract terms are one year or less. Crude oil and natural gas revenues are collected on or about the 25th day of the month following production.

($)	Three months ended June 30 2023	2022	Six months ended June 30 2023	2022
Crude oil revenues	29,514	22,745	54,410	39,895
Natural gas revenues	2,827	6,419	6,915	10,914
Natural gas liquids revenues	1,498	1,511	3,182	2,796
Total	33,839	30,675	64,507	53,605

12. NET INCOME PER SHARE

	Three months ended June 30 2023	2022	Six months ended June 30 2022	2022
Net Income per share				
Basic	$0.06	$0.14	$0.13	$0.22
Diluted	$0.06	$0.13	$0.12	$0.20
Weighted average shares outstanding				
Basic	76,624	75,264	76,624	75,257
Diluted	80,152	80,688	80,585	80,601

13. SUPPLEMENTAL CASH FLOW INFORMATION

Changes in non-cash working capital is comprised of the following:

($)	June 30 2023	June 30 2022
Source / (use) of cash:		
Accounts receivable	832	(2,656)
Prepaid expenses and deposits	(475)	(376)
Accounts payable and accrued liabilities	5,114	8,529
Current income taxes	(3,878)	3,644
Change in non-cash working capital	1,595	9,142
Related to:		
Operating activities	(5,127)	1,000
Investing activities	6,720	8,142

14. COMMITMENTS

The Company has an office lease commitment of $146,000 per year for 2023 to 2024, and $12,000 in 2025.

The Company has a four-year natural gas transportation commitment with an estimated annual cost of $200,000 to begin in August 2023.

15. CAPITAL RISK MANAGEMENT

The Company’s objectives when managing capital are to deploy capital to provide an appropriate return on shareholder investment and to maintain financial flexibility to execute on strategic opportunities and meet financial obligations. The Company manages its capital structure and makes adjustments in response to changes in economic conditions and the risk characteristics of its underlying oil and natural gas assets.

The Company has entered into a Royalty Acquisition Agreement (the “agreement”) with an arm’s length party (the “party”) whereby the party will fund certain crown land purchases incurred by the Company in exchange for a royalty on future production from those crown lands. The term of the agreement is to October 31, 2024. The agreement includes a funding limit of $14 million, which may be increased at the sole discretion of the party. At June 30, 2023, there is $4.0 million remaining on the funding limit.

The Company considers its capital structure to include shareholder’s equity, the bank credit facility and working capital. In order to maintain or adjust the capital structure, the Company may from time-to-time issue new shares, draw on the bank credit facility and/or adjust its capital spending.

16. FINANCIAL RISK MANAGEMENT

Credit risk

The Company may be exposed to certain losses in the event that counterparties fail to meet their obligations in accordance with agreed terms. The Company mitigates this risk by entering into transactions with highly rated major financial institutions and by routinely assessing the financial strength of its customers.

At June 30, 2023, and December 31, 2022, financial assets on the statement of financial position are comprised of cash and cash equivalents and trade and other receivables and the maximum credit risk associated with these financial instruments is the total carrying amount of these financial assets.

Cash equivalents include short-term deposits placed with financial institutions with strong investment grade ratings.

Accounts receivable for crude oil and natural gas sales are collected on or about the 25th day of the month following production. At June 30, 2023, 97% of the accounts receivable amount relates to production revenue (97% at December 31, 2022).

Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they are due. The Company's approach to managing liquidity is to ensure that it will have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions. The Company utilizes authorizations for expenditures on both operated and non-operated projects to manage capital expenditures.

The Company's financial liabilities on the statement of financial position consist of trade and other payables.

The Company expects to satisfy obligations under trade and other payables in less than one year.

The Company has a $25.0 million revolving demand operating facility with a Canadian chartered bank which could be accessed if required.

Market risk

Market risk is comprised of currency risk, interest rate risk and commodity price risks which consist primarily of fluctuations in petroleum and natural gas prices. The valuation of the financial assets and liabilities on the statement of financial position as at June 30, 2023, and December 31, 2022, has not been significantly impacted by changes in currency rates. Currency rates influence petroleum and natural gas prices; however, this influence on commodity prices and the resulting impact on financial assets and liabilities cannot be accurately quantified.

Interest rate risk

The Company is exposed to interest rate risk to the extent that changes in market interest rates will impact any bank interest earned/indebtedness that has a floating interest rate, potentially affecting future cash flows. As a means to mitigating exposure to interest rate risk, the Company has the ability to enter into interest rate swap agreements.

Commodity price risk

The Company may be exposed to commodity price risk arising from the effect that fluctuations of future commodity prices may have on the fair value or future cash flows of financial assets and liabilities.

Corporate Information

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Vice President Finance and Chief Financial Officer

Gerald Aleman
Vice President, Production

Calvin House
Vice President, Land and Business Development

Preston Kraft
Vice President, Operations

Steven Metzger
Vice President, Exploration

Lonny Tetley
Corporate Secretary

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