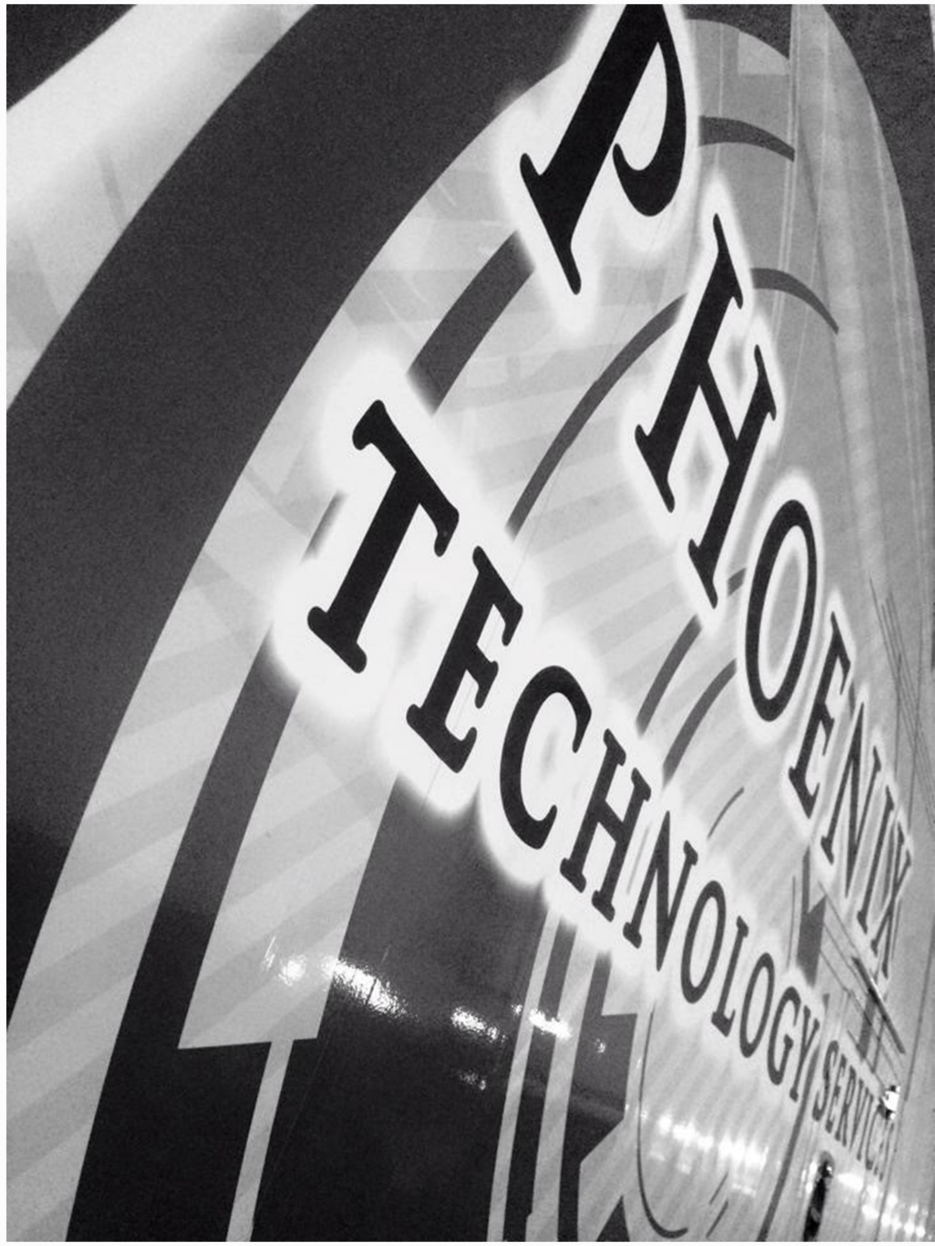
PHX
ENERGY SERVICES CORP.

Q2 2022



Quarterly Report

PHX Energy Services Corp.

Second Quarter Report for the three and six-month periods ended June 30, 2022 and 2021

The following Management's Discussion and Analysis ("MD&A") of the financial condition, results of operations, and cash flow of PHX Energy Services Corp. ("PHX Energy" or the "Corporation") should be read in conjunction with the Corporation's 2021 annual report, including the MD&A, and audited consolidated financial statements and the accompanying notes contained therein as well as other sections contained within the Corporation's 2021 annual report, and the Corporation's 2022 unaudited interim second quarter report, including the unaudited condensed consolidated interim financial statements and the accompanying notes contained therein as well as other sections contained within the Corporation's 2022 second quarter report. Readers can also obtain additional information on the Corporation including its Information Circular and Annual Information Form ("AIF") filed on SEDAR at www.sedar.com. This MD&A has been prepared taking into consideration information available up to and including August 9, 2022.

PHX Energy's Interim Financial Report for the three and six-month periods ended June 30, 2022 and 2021 has been prepared in accordance with International Financial Reporting Standards ("IFRS"). The MD&A and Interim Financial Report was reviewed by PHX Energy's Audit Committee and approved by PHX Energy's Board of Directors (the "Board") on August 9, 2022.

This MD&A contains Forward-Looking Information and Non-GAAP Financial Measures. Please refer to the "Cautionary Statement Regarding Forward-Looking Information and Statements" section below. Please refer to the "Non-GAAP Measures" section of this MD&A for applicable definitions and reconciliations.

Second Quarter Highlights

- The Corporation's adjusted EBITDA[(1)] from continuing operations increased to $25.1 million, 20 percent of consolidated revenue[(1)] This is the highest second quarter adjusted EBITDA in the Corporation's history.
- Earnings from continuing operations of $12.8 million is also the best second quarter result in the Corporation's history.
- Consolidated revenue of $126.2 million is the highest second quarter revenue on record, an increase of 67 percent over the comparative 2021-quarter.
- For the second consecutive quarter, PHX Energy's US division generated its highest quarterly revenue in the Corporation's history. US revenue was $105.4 million in the second quarter of 2022, representing 83 percent of consolidated revenue.
- The Corporation divested its Russian subsidiary, Phoenix TSR LLC ("Phoenix TSR"), resulting in full withdrawal from Russia.
- A quarterly dividend of $0.075 per common share was paid on July 15, 2022, which is triple the dividend per share declared in the second quarter of 2021. In light of continued strong financial performance, PHX

[(1)] Non-GAAP measure that does not have any standardized meaning under IFRS and therefore may not be comparable to similar measures presented by other entities. Refer to Non-GAAP Measures section of this MD&A.

Energy's Board has approved a further increase to the quarterly dividend to $0.10 per share effective for the dividend payable to shareholders of record at the close of business on September 30, 2022.

- The Corporation maintained a strong financial position, with working capital[(1)] of $75.7 million and credit facility capacity in excess of $60 million.
- PHX Energy intends to protect and preserve its balance sheet strength, capitalize on unique growth strategies and continue to reward its shareholders.

(Stated in thousands of dollars except per share amounts, percentages and shares outstanding)

	Three-month periods ended June 30,			Six-month periods ended June 30,		
	2022	2021	% Change	**2022**	2021	% Change
Operating Results – Continuing Operations	***(unaudited)***	*(unaudited)*		***(unaudited)***	*(unaudited)*	
Revenue	**126,238**	75,765	67	**235,568**	144,312	63
Earnings	**12,818**	4,447	188	**10,504**	9,781	7
Earnings per share – diluted	**0.25**	0.08	213	**0.21**	0.19	11
Adjusted EBITDA [(1)]	**25,084**	14,154	77	**31,528**	28,645	10
Adjusted EBITDA per share – diluted [(1)]	**0.49**	0.27	81	**0.63**	0.56	13
Adjusted EBITDA as a percentage of revenue [(1)]	**20%**	19%		**13%**	20%	
Cash Flow – Continuing Operations						
Cash flows from operating activities	**11,449**	8,845	29	**7,740**	10,374	(25)
Funds from operations [(1)]	**21,822**	12,299	77	**24,703**	24,102	2
Funds from operations per share – diluted [(1)]	**0.43**	0.24	79	**0.49**	0.47	4
Dividends paid per share	**0.075**	0.025	200	**0.125**	0.050	150
Dividends paid	**3,791**	1,260	201	**6,273**	2,525	148
Capital expenditures	**15,214**	10,519	45	**33,420**	17,408	92
Free cash flow [(1)]	**19,163**	11,007	74	**20,737**	22,996	(10)
Financial Position (unaudited)				**Jun 30, '22**	Dec 31, '21	
Working capital [(1)]				**75,678**	57,872	31
Net debt [(1)]				**2,137**	(24,829)	n.m.
Shareholders' equity				**146,467**	134,432	9
Common shares outstanding				**50,378,074**	47,978,662	5

n.m. – not meaningful

[(1)] Non-GAAP measure that does not have any standardized meaning under IFRS and therefore may not be comparable to similar measures presented by other entities. Refer to Non-GAAP Measures section of this MD&A.

Non-GAAP Measures

Throughout this MD&A, PHX Energy uses certain measures to analyze operational and financial performance that do not have standardized meanings prescribed under Canadian generally accepted accounting principles ("GAAP"). These non-GAAP measures include adjusted EBITDA, adjusted EBITDA per share, adjusted EBITDA as a percentage of revenue, gross profit as a percentage of revenue excluding depreciation and amortization and government grants, selling, general and administrative ("SG&A") costs excluding share-based compensation as a percentage of revenue, funds from operations, funds from operations per share, free cash flow, net debt, and working capital. Management believes that these measures provide supplemental financial information that is useful in the evaluation of the Corporation's operations and are commonly used by other oil and natural gas service companies. Investors should be cautioned, however, that these measures should not be construed as alternatives to measures determined in accordance with GAAP as an indicator of PHX Energy's performance. The Corporation's method of calculating these measures may differ from that of other organizations, and accordingly, such measures may not be comparable. Please refer to the "Non-GAAP Measures" section following the Outstanding Corporation Share Data section of this MD&A for applicable definitions, rationale for use, method of calculation and reconciliations where applicable.

Outlook

We are proud of the records achieved in the second quarter of 2022 and believe these results can be attributed to the execution of our strategies to focus on the best markets in the world, providing premium technologies, employing the industry's top professionals, and using our financial strength to mitigate supply chain challenges and create a competitive advantage.

- Although there is some caution related to a possible recession, we believe the rig count will continue to grow and commodity prices will remain favourable as inventories are depleted due to the capital restraints of producers since 2014. As such premium equipment will remain in high demand as Operators will not settle for mediocre drilling performance.
- This will bode well for our operations which will be equipped with additional job capacity from the large 2022 capital expenditures program. In the second quarter our fleet operated near or at maximum capacity, and this constrained activity growth, however, this was partially offset by the ability to improve day rates.
- We will continue to receive equipment deliveries through the second half of the year and into 2023, and have built up our inventory to service this equipment in a market where this premium technology will be scarce.
- We have created a competitive advantage where we can continue to grow, potentially see further pricing increases, and further strengthen our financial position for additional shareholder rewards.

- In the current economic environment, there are challenges that us and the entire sector are facing including supply chain constraints such as long lead times for materials for repair, inflationary cost and labour shortages. We remain diligent in trying to proactively mitigate these through our resources in supply chain and training.
- The solutions to mitigate these challenges, particularly related to labour, will likely take time and may impact our costs, however this will not be unique to our operations and the technology supply demand imbalance should create the opportunity to protect operating margins.
- We anticipate that in 2023 capital expenditures will largely be directed towards maintenance capital, creating additional financial strength, strong profitability and substantial free cash flow, which we expect to continue to return to shareholders, hopefully at an even greater percentage in the upcoming quarters.
- We are committed to shareholder returns as shown by our quarterly dividend increasing from $0.025 per share to the newly announced $0.10 per share since its re-commencement in December 2020. Our ability to increase dividends while growing our operations demonstrates the strength of our sector-leading balance sheet, which we are diligent in protecting.
- If we are correct in our forecast for a robust industry environment, we will remain steadfast in our commitment to creating shareholder value and continue to explore additional opportunities to benefit shareholders which could include, future quarterly dividend increases, special dividends, and continued NCIB purchases.

We are in an enviable position with one of the largest fleets of industry leading technology that has proven its ability to deliver the drilling performance that Operators expect. We believe there will be further increases to the North American rig count creating more opportunities for greater activity and we will be equipped to meet this demand. With the robust commodity prices forecasted to continue, we anticipate our financial and operating results will strengthen in future quarters sustaining our balance sheet strength. This position coupled with our unfairly low valuation in the stock market will drive our continued desire to reward shareholders leveraging the strong free cash flow forecasted.

Michael Buker, President
August 9, 2022

Financial Results

In the quarter PHX Energy achieved the highest second quarter revenue in the Corporation's history and the US division again achieved all-time record quarterly revenue, having also done so in the first quarter of the year. PHX Energy's consolidated revenue from continuing operations grew by 67 percent to $126.2 million from $75.8 million in the comparative 2021-quarter. PHX Energy's proactive supply chain strategy allowed the Corporation to capitalize on the robust commodity prices as parts and equipment ordered in late 2021 were delivered and deployed in the second quarter. The greater capacity in the Corporation's fleet of high-performance technologies along with strong demand from oil and gas producers drove increases to both consolidated operating activity and average revenue per day across all segments.

The Corporation's consolidated activity levels increased by 40 percent to 6,486 operating days in the 2022-quarter relative to 4,639 operating days in the 2021-quarter. Average revenue per day excluding US motor rentals improved by 21 percent from $15,526 in the 2021-quarter to $18,782 in the 2022-quarter. The increase in activity coupled with the improvement in average revenue per day were the main drivers of the 77 percent improvement in adjusted EBITDA which was the highest for a second quarter in PHX Energy's history. In the quarter adjusted EBITDA was $25.1 million, 20 percent of revenue, compared to $14.2 million, 19 percent of revenue, reported in the second of quarter of 2021. For the three-month period ended June 30, 2022, the Corporation achieved earnings from continuing operations of $12.8 million compared to $4.4 million in the 2021-period. This level of earnings is also the best second quarter earnings in the Corporation's history. Included in the 2021-quarter's adjusted EBITDA and earnings from continuing operations is $4.5 million of government grants. Excluding the impact of government grants, adjusted EBITDA improved by 159 percent in the 2022-quarter.

For the three-month period ended June 30, 2022, PHX Energy's strong momentum in the US continued, and for the second quarter in a row, the US division attained its highest quarterly revenue in the history of the Corporation. US revenue increased by 61 percent to $105.4 million from $65.5 million in the corresponding 2021-quarter. Stronger drilling activity partially contributed to this record level of revenue with the US segment's operating days growing by 33 percent in the 2022-quarter to 4,707 operating days from 3,549 days in the 2021-quarter. The Corporation increased activity in the US by expanding the capacity of its high performance technology fleets, specifically Velocity Real Time-Time Systems ("Velocity"), PowerDrive Orbit Rotary Steerable Systems ("RSS"), and Atlas High Performance ("Atlas") Motors. The US division's revenue represented 83 percent of the Corporation's consolidated revenue from continuing operations for the period (2021 – 86 percent).

The Canadian industry's activity levels in the second quarter of 2022 improved substantially over the same quarter of 2021 and PHX Energy's Canadian division recorded 1,688 operating days in the 2022-quarter, a 55 percent increase from the 1,090 operating days realized in the comparable 2021-period. The increase in the Canadian segment's drilling activity quarter-over-quarter was consistent with the Canadian market's activity where the average quarterly rig count increased 57 percent from 72 in the 2021-period to 113 in the 2022-period (Source: Baker Hughes). The recovery in activity greatly contributed to the improvement in the Canadian segment's revenue which almost doubled to $19.7 million in the three-month period ended June 30, 2022 from $10.3 million in the 2021-period.

As at June 30, 2022, the Corporation continued to maintain a strong balance sheet with a net debt [1] of only $2.1 million and available credit facilities in excess of $60 million. As at June 30, 2022, the Corporation's working capital was $75.7 million.

Dividends

In light of the continued strong performance and financial results, the Board has approved an increase to the Corporation's quarterly dividend to $0.10 per common share from $0.075 per common share, commencing with the dividend payable October 15, 2022 to shareholders of record at the close of business on September 30, 2022. This is the third dividend increase since its re-instatement in December 2020.

On June 15, 2022, PHX Energy declared a cash dividend of $0.075 per common share payable to shareholders of record at the close of business on June 30, 2022. An aggregate of $3.8 million was paid on July 15, 2022.

Capital Spending

In the second quarter of 2022, the Corporation spent $15.2 million on capital expenditures, which is $4.7 million greater than the expenditures of $10.5 million in the 2021-quarter. Capital expenditures for the 2022-quarter were primarily directed towards Atlas motors, Velocity systems, and RSS. Of the total capital expenditures in the 2022-quarter, $10 million was spent on growing the Corporation's fleet of drilling equipment and the remaining $5.2 million was spent on maintenance of the current fleet of drilling and other equipment. The Corporation funded capital spending primarily using its cash and cash equivalents held at March 31, 2022 and drawings on its Canadian credit facilities.

As at June 30, 2022, the Corporation has commitments to purchase drilling and other equipment for $47.2 million. Majority of the purchases are expected to be delivered throughout the second half of the 2022-year, with the remaining anticipated in the first quarter of 2023. Commitments include $13.6 million for Velocity systems, $26.7 million for performance drilling motors primarily relating to Atlas, and $6.9 million for RSS and other machinery and equipment. As previously announced, the Board approved to increase the 2022 capital expenditure program to $85 million to allow the Corporation to proactively order materials and equipment to expand its fleet for activity in late 2022 and into 2023. Given the current supply chain environment, lead times and costs are increasing and the Corporation's ability to place advanced orders is continuing to create a competitive advantage.

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The Corporation currently possesses approximately 554 Atlas motors, comprised of various configurations including its 5.13", 5.25", 5.76", 6.63", 7.12", 7.25", 8" and 9" Atlas motors, 105 Velocity systems, and 42 PowerDrive Orbit RSS, the largest independent fleet in North America.

Divesture of Russian Subsidiary

On June 30, 2022, PHX Energy divested Phoenix TSR LLC and exited Russia. The divestiture resulted in a loss on disposition of $3.5 million and the recognition of $10.6 million in foreign exchange losses resulting from accumulated currency translation adjustments. Pursuant to the disposition of Phoenix TSR, the Corporation has terminated all presence in Russia.

Shares Held in Trust

For the three-month period ended June 30, 2022, the Corporation equity settled a portion of its outstanding Retention Awards ("RA") under its Retention Award Plan (the "RAP"). Pursuant to the RA settlement, 168,390 common shares were issued in the second quarter of the 2022-year to settle $1.1 million in RAP liabilities. The Corporation, through an independent trustee, continues to acquire common shares on the open market from time-to-time for the potential settlement of future share-based compensation obligations. For the three-month period ended June 30, 2022, the trustee purchased 240,700 common shares for a total cost of $1.5 million. As at June 30, 2022, 245,830 common shares are held in trust for purposes of the RAP.

Normal Course Issuer Bid

During the third quarter of 2021, the TSX approved the renewal of PHX Energy's Normal Course Issuer Bid ("NCIB") to purchase for cancellation, from time-to-time, up to a maximum of 3,679,797 common shares, representing 10 percent of the Corporation's public float of common shares outstanding as at August 6, 2021. The NCIB commenced on August 16, 2021 and will terminate on August 15, 2022 or such earlier time as the NCIB is completed or terminated by PHX Energy. Purchases of common shares are to be made on the open market through the facilities of the TSX and through alternative trading systems. The price which PHX Energy is to pay for any common shares purchased is to be at the prevailing market price on the TSX or alternate trading systems at the time of such purchase. Pursuant to the current NCIB, an aggregate of 1,499,900 common shares were purchased by the Corporation and cancelled as at December 31, 2021. For the three-month period ending June 30, 2022, the Corporation did not repurchase shares through its current NCIB.

The Corporation intends to make an application to the TSX for renewal of its NCIB for a further one year term. The anticipated renewal of the NCIB remains subject to the review and approval of the TSX.

PHX Energy continues to use NCIBs as an additional tool to enhance total long-term shareholder returns in conjunction with management's disciplined capital allocation strategy.

Responding to COVID-19

In the 2022-quarter, government responses to COVID-19 continued to have a material impact on businesses worldwide. Despite easing of restrictions by most governments which led to improved industry and economic conditions in the period, the situation remains dynamic and the ultimate duration and magnitude of the impact on the economy and the financial effect on the Corporation is not known at this time. Supply chain challenges continue to create shortages and inflation related to the products and services required within the energy sector, including within the Corporation's supply chain. PHX Energy has been proactive with efforts to lessen the supply chain disruptions' impact on its operations. Specifically, as a result of these efforts, which included maintaining higher minimum safety stock levels and taking advantage of bulk discounts, inventory levels have increased by 29 percent from $36.7 million at the end of 2021 to $47.5 million at June 30, 2022.

PHX Energy has and will continue to preserve a solid financial position and retain financial flexibility through substantial liquidity on its credit facilities. As at June 30, 2022, the Corporation has working capital of $75.7 million and approximately CAD $45 million and USD $15 million available from its credit facilities. Additional information regarding the risks, uncertainties and impact on the Corporation's business can be found throughout this MD&A, including under the headings "Capital Spending", "Operating Costs and Expenses", "Segmented Information", and "Outlook".

About PHX Energy Services Corp.

PHX Energy is a growth oriented, public oil and natural gas services company. The Corporation, through its directional drilling subsidiary entities provides horizontal and directional drilling services to oil and natural gas exploration and development companies principally in Canada and the US. In connection with the services it provides, PHX Energy engineers, develops and manufactures leading-edge technologies. In recent years, PHX Energy has developed various new technologies that have positioned the Corporation as a technology leader in the horizontal and directional drilling services sector.

PHX Energy's Canadian directional drilling operations are conducted through Phoenix Technology Services LP. The Corporation maintains its corporate head office, research and development, Canadian sales, service and operational centers in Calgary, Alberta. In addition, PHX Energy has a facility in Estevan, Saskatchewan. PHX Energy's US operations, conducted through the Corporation's wholly-owned subsidiary, Phoenix Technology Services USA Inc. ("Phoenix USA"), is headquartered in Houston, Texas. Phoenix USA has sales and service facilities in Houston, Texas; Casper, Wyoming; Midland, Texas; and Oklahoma City, Oklahoma. Internationally, PHX Energy has sales offices and service facilities in Albania, and administrative offices in Nicosia, Cyprus and Luxembourg City, Luxembourg. The Corporation also operates in the Middle East regions through an arrangement with National Energy Services Reunited Corp.

The common shares of PHX Energy trade on the Toronto Stock Exchange under the symbol PHX.

Results of Operations

Three and Six-Month Periods Ended June 30, 2022

Revenue

(Stated in thousands of dollars)

	Three-month periods ended June 30,			Six-month periods ended June 30,		
	2022	2021	% Change	**2022**	2021	% Change
Revenue	**126,238**	75,765	67	**235,568**	144,312	63

For the three-month period ended June 30, 2022, the Corporation generated consolidated revenue of $126.2 million as compared to $75.8 million in the 2021-quarter, an increase of 67 percent driven by higher revenue per day and operating days across all PHX Energy's segments. The average consolidated revenue per day, excluding the motor rental division in the US, in the 2022-quarter rose by 21 percent to $18,782 relative to $15,526 in the corresponding 2021-quarter. The higher revenue per day was mainly driven by increased capacity in the Corporation's fleet of high performance technologies, pricing increases rolled out to help curtail inflationary costs, and the strengthening of the US dollar relative to the 2021-quarter. Consolidated operating days increased by 40 percent from 4,639 days in the 2021-quarter to 6,486 days in the 2022-quarter. Strong activity in the US and Canadian operations plus resumption of operations in Albania helped bolster operating days relative to the comparative 2021-quarter. For the three-month period ended June 30, 2022, US revenue represented 83 percent of consolidated revenue (2021 – 86 percent).

During the second quarter of 2022, the Western Texas Intermediate ("WTI") crude oil price was 58 percent higher than in the 2021-quarter averaging USD $104/bbl (2021-quarter – USD $66/bbl) and the Western Canadian Select ("WCS") oil prices also showed a 78 percent increase averaging USD $96/bbl (2021-quarter – USD $54/bbl). As a result of strong commodity prices both the US and Canadian industry's activity improved quarter-over-quarter to an average of 713 rigs (2021-quarter – 450 rigs) operating per day in the US and an average of 113 rigs (2021-quarter – 72 rigs) in Canada. Throughout North America the vast majority of wells continued to be horizontal and directional representing 98 percent of all wells drilled in Canada and 96 percent of the average number of rigs operating per day in the US (Sources: Daily Oil Bulletin and Baker Hughes).

For the six-month period ended June 30, 2022, the Corporation realized consolidated revenue of $235.6 million, a 63 percent increase, compared to the $144.3 million in the same 2021-period. The improvement in revenue for the 2022 six-month period was primarily a result of strong activity levels, high performance technology offerings, and the strengthening of the US dollar in the 2022-period relative to 2021. For the 2022-period, the average consolidated revenue per day, excluding the motor rental division in the US, was $17,086 as compared to $14,618 in the 2021-period, an increase of 17 percent. In the six-month period ended June 30, 2022, there were 13,281 operating days recorded which rose by 40 percent relative to 9,487 days in the corresponding 2021-period.

Operating Costs and Expenses

(Stated in thousands of dollars except percentages)

	Three-month periods ended June 30,			Six-month periods ended June 30,		
	2022	2021	% Change	**2022**	2021	% Change
Direct costs	**100,520**	59,437	69	**192,466**	113,953	69
Depreciation & amortization drilling and other equipment (included in direct costs)	**7,823**	6,277	25	**15,099**	12,509	21
Depreciation & amortization right-of-use asset (included in direct costs)	**849**	825	3	**1,685**	1,661	1
Gross profit as a percentage of revenue excluding depreciation & amortization and government grants[(1)]	**27%**	26%		**25%**	26%	

Direct costs are comprised of field and shop expenses and include depreciation and amortization on the Corporation's equipment and right-of-use assets. For the three-month period ended June 30, 2022, direct costs increased by 69 percent to $100.5 million from $59.4 million in the 2021-quarter. Higher direct costs are mainly attributable to increased activity across all divisions plus continued inflationary pressures increasing direct labour, equipment repair costs, and equipment rentals. In addition, no government grants were recognized in direct costs in the 2022-quarter whereas in the second quarter of 2021 the Corporation recognized $3.5 million in government grants.

The Corporation's depreciation and amortization on drilling and other equipment for the three-month period ended June 30, 2022, increased by 25 percent from $6.3 million to $7.8 million as capital expenditures progressively increased in the 2021-year and 2022-period.

In the three and six-month periods of 2022, gross profit as a percent of revenue excluding depreciation and amortization and government grants were 27 percent and 25 percent, respectively, compared to 26 percent for both periods in 2021. The decrease in year-to-date gross profitability in 2022 relative to the corresponding 2021-period is mainly due to the effect of inflationary pressures; however, gross profit as a percent of revenue excluding depreciation and amortization and government grants improved in the second quarter of 2022 as management's response to inflation began to take effect. In addressing

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inflation, management continues to take a proactive approach by leveraging volume purchases, quick pay discounts, and other strategies to soften the impact of rising material and service costs.

(Stated in thousands of dollars except percentages)

	Three-month periods ended June 30,			Six-month periods ended June 30,		
	2022	2021	% Change	**2022**	2021	% Change
Selling, general and administrative ("SG&A") costs	**11,836**	10,629	11	**33,947**	19,612	73
Cash-settled share-based compensation (included in SG&A costs)	**715**	3,924	(82)	**12,452**	6,568	90
Equity-settled share-based compensation (included in SG&A costs)	**(75)**	150	n.m.	**260**	218	19
SG&A costs excluding share-based compensation as a percentage of revenue (1)	**9%**	9%		**9%**	9%	

n.m. – not meaningful

For the three-month period ended June 30, 2022, the Corporation's SG&A costs increased by 11 percent to $11.8 million as compared to $10.6 million in the 2021-period, which was primarily due to higher personnel-related costs incurred to support the increase in drilling activity. No government grants were recognized in SG&A in the second quarter of 2022 (2021 - $1 million). Included in SG&A costs are share-based compensation expenses totaling $0.6 million in the 2022-quarter compared to $4.1 million in the 2021-quarter. Excluding share-based compensation, SG&A costs as a percentage of revenue for the three-month period ended June 30, 2022 remained steady with the 2021-period at 9 percent.

Share-based compensation mainly relates to retention awards which are measured at fair value and the decrease in the 2022-quarter was primarily due to decreases in the Corporation's share price.

(Stated in thousands of dollars)

	Three-month periods ended June 30,			Six-month periods ended June 30,		
	2022	2021	% Change	**2022**	2021	% Change
Research & development expense	**873**	624	40	**1,630**	1,185	38

Research and development ("R&D") expenditures for the three and six-month periods ended June 30, 2022 were $0.9 million (2021 - $0.6 million) and $1.6 million (2021 - $1.2 million), respectively. The higher R&D expenditures in both 2022 periods is primarily due to the increase of personnel related costs and a greater number of initiatives in the R&D department. PHX Energy's R&D focus continues to be on developing new technologies, improving the reliability of equipment, and reducing costs to operations.

(Stated in thousands of dollars)

(1) Non-GAAP measure that does not have any standardized meaning under IFRS and therefore may not be comparable to similar measures presented by other entities. Refer to Non-GAAP Measures section of this MD&A.

	Three-month periods ended June 30,			Six-month periods ended June 30,		
	2022	2021	% Change	**2022**	2021	% Change
Finance expense	**262**	94	179	**374**	265	41
Finance expense lease liability	**501**	534	(6)	**1,008**	1,083	(7)

Finance expense mainly relates to interest charges on the Corporation's long-term and short-term bank facilities. For the three and six-month periods ended June 30, 2022, finance charges increased to $0.3 million (2021 - $0.1 million) and $0.4 million (2021 - $0.3 million), respectively, due to higher drawings on the credit facilities as the Corporation secures equipment and material to facilitate growth.

Finance expense lease liability relates to interest expenses incurred on lease liabilities and decreased by 6 percent and 7 percent in the three and six-month periods as the Corporation's long-term leases wind down and are renewed with more favorable terms.

(Stated in thousands of dollars)

	Three-month periods ended June 30,		Six-month periods ended June 30,	
	2022	2021	**2022**	2021
Net gain on disposition of drilling equipment	**(3,060)**	(1,483)	**(6,642)**	(4,302)
Foreign exchange losses	**64**	61	**76**	61
Recovery of bad debts	**-**	(265)	**-**	(265)
Other	**(512)**	-	**(512)**	-
Other income	**(3,508)**	(1,687)	**(7,078)**	(4,506)

For the three and six-month periods ended June 30, 2022, the Corporation recognized other income of $3.5 million and $7.1 million, respectively (2021 - $1.7 million and $4.5 million, respectively). In both periods, the improvement was mainly driven by increases in net gain on disposition of drilling equipment and recognition into income of a held deposit.

Net gain on disposition of drilling equipment is comprised of gains on disposition of drilling equipment and proceeds from insurance programs. The recognized gain is net of losses, which typically result from asset retirements that were made before the end of the equipment's useful life and self-insured downhole equipment losses. In the 2022-quarter, more instances of downhole equipment losses occurred as compared to the 2021-quarter, resulting in higher net gain on disposition of drilling equipment.

(Stated in thousands of dollars except percentages)

	Three-month periods ended June 30,		Six-month periods ended June 30,	
	2022	2021	**2022**	2021
Provision for income taxes	**2,934**	1,687	**2,717**	2,939
Effective tax rates	**19%**	28%	**21%**	23%

For the three and six-month periods ended June 30, 2022, the Corporation reported income tax provisions of $2.9 million (2021 - $1.7 million) and $2.7 million (2021 - $2.9 million), respectively. Higher provision in the 2022-quarter was mainly a result of improved taxable profits in the US jurisdictions.

Segmented Information

The Corporation reports three operating segments on a geographical basis throughout the Canadian provinces of Alberta, Saskatchewan, British Columbia, and Manitoba; throughout the Gulf Coast, Northeast and Rocky Mountain regions of the US; and internationally mainly in Albania.

Canada

(Stated in thousands of dollars)

	Three-month periods ended June 30,			Six-month periods ended June 30,		
	2022	2021	% Change	**2022**	2021	% Change
Revenue	**19,704**	10,250	92	**46,843**	25,697	82
Reportable segment profit (loss) before tax[(1)]	**(16)**	224	n.m.	**3,450**	2,549	35

(1) Includes adjustments to intercompany transactions.
n.m. – not meaningful

For the three and six-month periods ended June 30, 2022, PHX Energy's Canadian revenue was $19.7 million and $46.8 million, respectively, in comparison to revenue of $10.3 million and $25.7 million in the same 2021-periods. Despite spring break-up when activity levels are typically lower as compared to the other quarters of the year, the Corporation exceeded 1,600 operating days in the 2022-quarter which was only achieved twice prior in the Corporation's history.

For the three and six-month periods ended June 30, 2022, operating days improved 55 percent in both periods to 1,688 days and 4,418 days, respectively, compared to 1,090 days and 2,855 days, respectively, in the comparable 2021-periods. In comparison industry horizontal and directional drilling activity, as measured by drilling days, increased 62 percent to 10,407 days in the second quarter of 2022 and 44 percent to 26,840 in the first half of the 2022-year (Source: Daily Oil Bulletin).

Despite higher volume of active rigs operating in 2022, the Canadian market remained highly competitive. However, the Canadian division was successful in maintaining its market share and well-diversified client base. During the 2022-quarter, PHX Energy was active in the Duvernay, Montney, Glauconite, Frobisher, Cardium, Viking, Bakken, Torquay, Colony, Clearwater, and Scallion basins.

In the second quarter of 2022, the Canadian operations' reportable segment profit before tax decreased to a loss of $16 thousand from a reportable segment profit before tax of $0.2 million in the 2021-quarter. For the 2022 six-month period, the division's reportable segment profit before tax increased to $3.5 million from $2.5 million in the comparable 2021-period. No government grants were received in the 2022-year. Excluding the impact from government grants, PHX Energy's Canadian segment profitability improved in both 2022-periods from reportable segment loss before tax of $1.6 million and $0.9 million, respectively, for the three and six-month periods ended June 30, 2021.

United States

(Stated in thousands of dollars)

	Three-month periods ended June 30,			Six-month periods ended June 30,		
	2022	2021	% Change	**2022**	2021	% Change
Revenue	**105,367**	65,515	61	**187,162**	118,615	58
Reportable segment income before tax[(1)]	**16,885**	11,272	50	**23,331**	18,494	26

[(1)] Includes adjustments to intercompany transactions.

For the three-month period ended June 30, 2022, the US division achieved the highest quarterly divisional revenue in the Corporation's history. US revenue in the 2022-quarter improved by 61 percent to $105.4 million as compared to $65.5 million in the corresponding 2021-quarter. Drilling activity increased by 33 percent in the 2022-quarter to 4,707 days compared to 3,549 days in the same 2021-quarter. In comparison, the US industry horizontal and directional rig count increased by 59 percent quarter-over-quarter with an average of 687 active horizontal and directional rigs per day in 2022 compared to an average of 432 active horizontal and directional rigs per day in the 2021-quarter (Source: Baker Hughes). During the quarter PHX Energy's fleet was operating at full capacity and was impacted by supply chain challenges. However, despite the limitations on drilling activity, the Corporation's improvement in revenue demonstrates the continuing high demand for the Corporation's high-performance technologies, superior operational performance of personnel and equipment, and targeted marketing efforts. For the three-month period ended June 30, 2022, revenue per day, excluding the Corporation's US motor rental division, rose to $21,442 compared to $17,403 in the corresponding 2021-quarter. The 23 percent increase to revenue per day is attributable to demand for the Corporation's high-performance technologies and strengthening of the US dollar. The US-denominated average revenue per day increased by 18 percent quarter-over-quarter from USD $14,173 to USD $16,795.

For the three-month period ended June 30, 2022, PHX Energy's US operations realized reportable segment profit before tax of $16.9 million, a 50 percent increase from $11.3 million in the same 2021-period. Included in the 2021-quarter reportable segment profit before tax was $2.7 million in government grants. Excluding government grants, reportable segment income almost doubled in the 2022-quarter compared to the 2021-period. The significant improvement in divisional profit is primarily attributable to improved activity levels and effective inflation-mitigating strategies deployed by management.

Horizontal and directional drilling continues to represent the majority of rigs running on a daily basis during the second quarter of 2022. For the three-month period ended June 30, 2022, the Corporation's US division was active in the Permian, Eagle Ford, SCOOP/STACK, Marcellus, Bakken, and Niobrara basins.

Consistent with the second quarter of 2022, for the six-month period ended June 30, 2022, the Corporation capitalized on high performance technologies and generated higher operational days and higher revenue per day. Drilling activity for the six-month period ended June 30, 2022, increased 32 percent to 8,753 days as compared to 6,633 days in the same 2021-period. In comparison, US industry activity, as measured by the average number of horizontal and directional rigs running on a daily basis, improved to 650 rigs in the first half of 2022 as compared to an average of 403 rigs in the comparable 2021-period (Source: Baker Hughes). For the six-month period ended June 30, 2022, average revenue per day, excluding the Corporation's motor rental division, was $20,396, which is 20 percent higher than the $17,035 reported in the 2021-period. For the six-month period ended June 30, 2022, the US-denominated revenue per day increased to USD $16,034, 17 percent higher, compared to USD $13,685 achieved in the comparable 2021-period.

For the six-month period ended June 30, 2022, a reportable segment income before tax of $23.3 million was realized as compared to $18.5 million in the corresponding 2021-period. Excluding government grants, reportable segment income before tax in the first half of the 2022-year improved by 74 percent from the $13.4 million realized in the comparable 2021-period. Higher profitability in the period is mainly attributed to the rise in activity levels and revenue per day.

International – Continuing Operations

(Stated in thousands of dollars)

	Three-month periods ended June 30,			Six-month periods ended June 30,		
	2022	2021	% Change	**2022**	2021	% Change
Revenue	**1,167**	-	n.m.	**1,563**	-	n.m.
Reportable segment profit (loss) before tax	**523**	(471)	n.m.	**361**	(798)	n.m.

n.m. – not meaningful

The Corporation's International segment revenue is mainly comprised of revenue from Albania. For the three and six-month periods ended June 30, 2022, International revenue increased to $1.2 million and $1.6 million, respectively, as compared to nil in the 2021-periods as Albania operations were paused at that time and resumed late in the first quarter of 2022 with one rig. With the resumption of activity in the first half of 2022, the International segment realized reportable segment profits of $0.5 million and $0.4 million for the three and six-month periods (2021 – loss of $0.5 million and loss of $0.8 million, respectively.)

Discontinued Operations – Russia

On June 30, 2022, the Corporation disposed of the Russian division operating under the entity, Phoenix TSR. Accordingly, for the three and six-month periods ended June 30, 2022, the Russian operations and loss on disposition have been presented as discontinued operations.

The results of the sold Phoenix TSR operations are as follows:

(Stated in thousands of dollars)

	Three-month periods ended June 30,		Six-month period ended June 30,	
	2022	2021	**2022**	2021
Revenue	**4,648**	2,073	**7,443**	3,632
Expenses	**(3,072)**	(2,141)	**(5,781)**	(4,170)
	1,576	(68)	**1,662**	(538)
Reclassification of foreign currency translation loss on disposition of Phoenix TSR	**(10,561)**	-	**(10,561)**	-
Loss on disposition of Phoenix TSR	**(3,496)**	-	**(3,496)**	-
Impairment and other write-offs		-	**(1,967)**	-
Loss from discontinued operations	**(12,481)**	(68)	**(14,362)**	(538)
Income tax from discontinued operations	**(169)**	-	**(196)**	1
Loss from discontinued operations, net of taxes	**(12,650)**	(68)	**(14,558)**	(537)

Summary of Quarterly Results – Continuing Operations

(Stated in thousands of dollars except per share amounts)

	Jun-22	Mar-22	Dec-21	Sept-21	Jun-21	Mar-21	Dec-20	Sept-20
Revenue	**126,238**	109,331	104,357	93,338	75,765	68,547	54,805	37,044
Earnings (loss)	**12,818**	(2,315)	9,403	4,206	4,447	5,334	2,028	(1,544)
Earnings (loss) per share – basic	**0.25**	(0.04)	0.19	0.09	0.08	0.11	0.04	(0.03)
Earnings (loss) per share – diluted	**0.25**	(0.04)	0.18	0.08	0.08	0.11	0.04	(0.03)
Dividends paid	**3,791**	2,482	2,505	1,260	1,260	1,266	-	-
Cash and cash equivalents	**17,971**	11,284	24,829	24,917	21,026	23,468	25,746	18,889
Loans and borrowings	**20,108**	3,749	-	-	-	-	-	-

Liquidity

(Stated in thousands of dollars)

	Three-month periods ended June 30,		Six-month periods ended June 30,	
	2022	2021	**2022**	2021
Funds from operations (1)	**21,822**	12,298	**24,703**	24,102

	Jun. 31, '22	Dec. 31, '21
Working capital (1)	**75,678**	57,872

In the second quarter and first half of 2022, mainly due to greater activity in the US segment and increased profitability, the Corporation generated higher funds from operations of $21.8 million (2021 - $12.3 million) and $24.7 million (2021 - $24.1 million), respectively.

As at June 30, 2022, the Corporation had working capital of $75.7 million, which is $17.8 million higher than the $57.9 million reported at December 31, 2021. The increase to working capital at June 30, 2022 was primarily due to higher trade and other receivables resulting from the increase in operating activity and higher inventory on hand resulting from strategies implemented to address supply chain challenges.

Cash Flow and Dividends

In December 2020, PHX Energy reinstated a quarterly dividend program. The Board will continually review the dividend program and take into consideration, without limitation, the Corporation's financial performance, forecasted activity levels and the industry outlook. The actual amount of future quarterly dividends, if any, remains subject to the approval of and declaration by the Board. The Board reviews the Corporation's dividend policy in conjunction with their review of quarterly financial and operating results. The Corporation's ability to maintain the current level of dividends to its shareholders is dependent upon the realization of cash flow from operations, among other considerations, and if the Corporation does not meet its budgeted cash flow from operations, dividends to shareholders may be reduced or suspended entirely.

In light of the continued strong performance and financial results, the Board has approved an increase to the Corporation's quarterly dividend to $0.10 per common share from $0.075 per common share, commencing with the dividend payable October 15, 2022 to shareholders of record at the close of business on September 30, 2022. This is the third dividend increase since its re-instatement in December 2020.

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(1) Non-GAAP measure that does not have any standardized meaning under IFRS and therefore may not be comparable to similar measures presented by other entities. Refer to Non-GAAP Measures section of this MD&A.

On June 15, 2022, PHX Energy declared a cash dividend of $0.075 per common share and an aggregate of $3.8 million was paid on July 15, 2022.

Investing Activities

PHX Energy used net cash in investing activities of $14.5 million in the second quarter of 2022 compared to $5.4 million in the 2021-quarter. In the second quarter of 2022, the Corporation received proceeds of $3.9 million (2021 - $2.7 million) from the disposition of drilling equipment, primarily related to the involuntary disposal of drilling equipment in well bores. Additionally, the Corporation spent $15.2 million on capital expenditures in the second quarter of 2022 (2021 - $10.5 million). These expenditures included:

- $7.5 million downhole performance drilling motors,
- $7.4 million in MWD systems and spare components and RSS; and
- $0.3 million in machinery and equipment and other assets.

The capital expenditure program undertaken in the period was primarily financed from cash and cash equivalents and the credit facilities. Of the total capital expenditures in the 2022-quarter, $10 million was used to grow the Corporation's fleet of drilling equipment and the remaining $5.2 million was used to maintain the current fleet of drilling and other equipment.

During the three-month period ended June 30, 2022, the Corporation acquired intangible assets in the amount of $0.2 million (2021 - $nil).

The change in non-cash working capital balances of $2.9 million (use of cash) for the three-month period ended June 30, 2022, relates to the net change in the Corporation's trade payables that are associated with the acquisition of capital assets. This compares to a $2.4 million (source of cash) for the three-month period ended June 30, 2021.

Financing Activities

For the three-month period ended June 30, 2022, net cash from financing activities was $10.4 million as compared to $5.4 million used in financing activities in the same 2021-period. In the 2022-period:

- 240,700 common shares were purchased by an independent trustee in the open market for $1.5 million to be held in trust for the potential future settlement of restricted awards granted under the Corporation's RAP;
- dividends of $3.8 million were paid to shareholders;
- payments of $0.9 million were made towards lease liability;
- 83,333 common shares were issued from treasury for proceeds of $0.2 million upon the exercise of share options; and
- $16.4 million net in drawings were taken against the operating and syndicated facilities.

Capital Resources

As of June 30, 2022, the Corporation had CAD $20.1 million drawn on its Canadian credit facilities, nothing drawn on its US operating facility, and a cash balance of $18 million. As at June 30, 2022, the Corporation had approximately CAD $45 million and USD $15 million available to be drawn from its credit facilities. The credit facilities are secured by substantially all of the Corporation's assets.

As at June 30, 2022, the Corporation was in compliance with all its financial covenants.

Cash Requirements for Capital Expenditures

Historically, the Corporation has financed its capital expenditures and acquisitions through cash flows from operating activities, debt and equity. On April 14, 2022, the Corporation announced an increase to its 2022 capital expenditure program from $47.7 million to $85 million. The increase is primarily dedicated to growing the Velocity, RSS and Atlas fleets to meet increased demand anticipated in late 2022 and 2023.

These planned expenditures are expected to be financed from cash flow from operations, cash and cash equivalents, and / or the Corporation's unused credit facilities, if necessary. However, if a sustained period of market uncertainty and financial market volatility persists, the Corporation's activity levels, cash flows and access to credit may be negatively impacted, and the expenditure level would be reduced accordingly where possible. Conversely, if future growth opportunities present themselves, the Corporation would look at expanding this planned capital expenditure amount.

As at June 30, 2022, the Corporation has commitments to purchase drilling and other equipment for $47.2 million. Majority of the delivery is expected to occur within the second half of 2022 with the remainder expected to be delivered in the first quarter of 2023.

Off-Balance Sheet Arrangements

The Corporation had no material off-balance sheet arrangements as at June 30, 2022 and 2021.

Proposed Transactions

The Corporation regularly reviews and evaluates possible strategic material business or asset acquisitions or capital asset divestitures in the normal course of its operations.

Critical Accounting Estimates and Judgments

The consolidated interim financial statements have been prepared in accordance with IAS 34 Interim Financial Reporting. The Corporation's significant accounting policies are described in its annual audited consolidated financial statements for the year ended December 31, 2021.

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

In preparing the condensed consolidated interim financial statements, the significant judgments made by management in applying the Corporation's accounting policies and the key sources of estimation uncertainty have not changed significantly since December 31, 2021.

Changes in Accounting Policies

The condensed consolidated interim financial statements have been prepared utilizing the same accounting policies and methods as the consolidated financial statements of the Corporation for the year ended December 31, 2021, unless specified.

Business Risk Factors

The business risk factors applicable to the Corporation have not materially changed since December 31, 2021. Refer to the "Business Risk Factors" section of the MD&A in PHX Energy's 2021 annual report as well as in the Corporation's most recent Annual Information Form filed on SEDAR at www.sedar.com.

Corporate Governance

This MD&A has been prepared by the management of PHX Energy and it has been reviewed and approved by the Audit Committee and the Board of the Corporation. Additional information relating to the Corporation's Corporate Governance can be found in the Corporation's AIF and in its Information Circular in respect of its annual meeting of Shareholders, each of which are annually filed on SEDAR at www.sedar.com.

Disclosure Controls and Procedures

The Corporation's Chief Executive Officer and Chief Financial Officer (the "Certifying Officers") have designed, or caused to be designed under their supervision, disclosure controls and procedures ("DC&P"), as defined in National Instrument 52-109 Certification of Disclosure in Issuers' Annual and Interim Filings ("NI 52-109"), to provide reasonable assurance that information required to be disclosed by the Corporation in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time periods specified in the securities legislation and include controls and procedures designed to ensure that information required to be so disclosed is accumulated and communicated to the Corporation's management, including the Certifying Officers, as appropriate to allow timely decisions regarding required disclosure.

Internal Controls Over Financial Reporting

The Corporation's Certifying Officers have designed, or caused to be designed under their supervision, internal controls over financial reporting ("ICFR"), as defined in NI 52-109, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles applicable to the Corporation. ICFR includes those policies and procedures that (i) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Corporation; (ii) are designed to provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP, and that receipts and expenditures of the Corporation are being made only in accordance with authorizations of management and directors of the Corporation; and (iii) are designed to provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Corporation's assets that could have a material effect on the annual financial statements or interim financial reports.

The control framework used to design and evaluate the Corporation's ICFR is "Internal Control - Integrated Framework (2013)" published by The Committee of Sponsoring Organizations of the Treadway Commission (COSO).

There were no changes in the Corporation's ICFR that occurred during the period beginning on April 1, 2022 and ended on June 30, 2022 that have materially affected, or are reasonably likely to materially affect, the Corporation's ICFR.

While the Certifying Officers believe that the Corporation's ICFR provide a reasonable level of assurance and are effective, they do not expect that the ICFR will prevent all errors and fraud. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

Outstanding Corporation Share Data

(In thousands of shares)	**As at August 9, 2022**
Common shares outstanding, excluding shares held in trust	50,378,074
Common shares held in trust [(1)]	245,830
Total common shares outstanding	50,623,904
Dilutive securities:	
Options	1,416,667
Corporation shares – diluted	52,040,571

[(1)] Common Shares held in trust by an independent trustee for the potential future settlement of awards granted to eligible participant's under the Corporation's Retention Award Plan

Non-GAAP Measures

Adjusted EBITDA

Adjusted EBITDA, defined as earnings before finance expense, finance expense lease liability, income taxes, depreciation and amortization, impairment losses on drilling and other equipment and goodwill and other write-offs, equity-settled share-based payments, severance payouts relating to the Corporation's restructuring cost, and unrealized foreign exchange gains or losses, does not have a standardized meaning and is not a financial measure that is recognized under GAAP. However, Management believes that adjusted EBITDA provides supplemental information to net earnings that is useful in evaluating the results of the Corporation's principal business activities before considering certain charges, how it was financed and how it was taxed in various countries. Investors should be cautioned, however, that adjusted EBITDA should not be construed as an alternative measure to net earnings determined in accordance with GAAP. PHX Energy's method of calculating adjusted EBITDA may differ from that of other organizations and, accordingly, its adjusted EBITDA may not be comparable to that of other companies.

The following is a reconciliation of net earnings to adjusted EBITDA:

(Stated in thousands of dollars)

	Three-month periods ended June 30,		Six-month periods ended June 30,	
	2022	2021	**2022**	2021
Net earnings from continuing operations:	**12,818**	4,447	**10,504**	9,781
Add:				
Depreciation and amortization drilling and other equipment	**7,823**	6,277	**15,099**	12,509
Depreciation and amortization right-of-use asset	**849**	825	**1,685**	1,661
Provision for income taxes	**2,934**	1,687	**2,717**	2,939
Finance expense	**262**	94	**374**	265
Finance expense lease liability	**501**	534	**1,008**	1,083
Equity-settled share-based payments	**(75)**	150	**260**	218
Unrealized foreign exchange (gain) loss	**(28)**	140	**(119)**	189
Adjusted EBITDA	**25,084**	14,154	**31,528**	28,645

Adjusted EBITDA per share - diluted is calculated using the treasury stock method whereby deemed proceeds on the exercise of the share options are used to reacquire common shares at an average share price. The calculation of adjusted EBITDA per share - dilutive is based on the adjusted EBITDA as reported in the table above divided by the diluted number of shares outstanding.

Adjusted EBITDA as a percentage of revenue is calculated by dividing the adjusted EBITDA as reported in the table above by revenue as stated on the Consolidated Statements of Comprehensive Income (Loss).

Funds from Operations

Funds from operations is defined as cash flows generated from operating activities before changes in non-cash working capital, interest paid, and income taxes paid. This non-GAAP measure does not have a standardized meaning and is not a financial measure recognized under GAAP. Management uses funds from operations as an indication of the Corporation's ability to generate funds from its operations before considering changes in working capital balances and interest and taxes paid. Investors should be cautioned, however, that this financial measure should not be construed as an alternative measure to cash flows from operating activities determined in accordance with GAAP. PHX Energy's method of calculating funds from operations may differ from that of other organizations and, accordingly, it may not be comparable to that of other companies.

The following is a reconciliation of cash flows from operating activities to funds from operations:

(Stated in thousands of dollars)

	Three-month periods ended June 30,		Six-month periods ended June 30,	
	2022	2021	**2022**	2021
Cash flows from operating activities	**11,449**	8,845	**7,740**	10,374
Add (deduct):				
Changes in non-cash working capital	**10,261**	3,399	**17,004**	13,601
Interest paid	**127**	47	**178**	107
Income taxes paid (received)	**(15)**	8	**(219)**	20
Funds from operations	**21,822**	12,299	**24,703**	24,102

Funds from operations per share - diluted is calculated using the treasury stock method whereby deemed proceeds on the exercise of the share options are used to reacquire common shares at an average share price. The calculation of funds from operations per share - diluted is based on the funds from operations as reported in the table above divided by the diluted number of shares outstanding.

Free Cash Flow

Free cash flow is defined as funds from operations (as defined above) less maintenance capital expenditures and cash payment on leases and increased by proceeds on disposition. This non-GAAP measure does not have a standardized meaning and is not a financial measure recognized under GAAP. Management uses free cash flow as an indication of the Corporation's ability to generate funds from its operations to support operations and maintain the Corporation's drilling and other equipment. This performance measure is useful to investors for assessing the Corporation's operating and financial performance, leverage and liquidity. Investors should be cautioned, however, that this financial measure should not be construed as an alternative measure to cash flows from operating activities determined in accordance with GAAP. PHX Energy's method of calculating free cash flow may differ from that of other organizations and, accordingly, it may not be comparable to that of other companies.

The following is a reconciliation of cash flows from operating activities to free cash flow:

(Stated in thousands of dollars)

	Three-month periods ended June 30,		Six-month periods ended June 30,	
	2022	2021	**2022**	2021
Cash flows from operating activities	**11,449**	8,845	**7,740**	10,374
Add (deduct):				
Changes in non-cash working capital	**10,261**	3,399	**17,004**	13,601
Interest paid	**127**	47	**178**	107
Income taxes paid (received)	**(15)**	8	**(219)**	20
Maintenance capital expenditures	**(5,168)**	(2,684)	**(10,406)**	(4,943)
Proceeds on disposition	**3,883**	2,741	**9,180**	6,526
Cash payment on leases	**(1,374)**	(1,349)	**(2,740)**	(2,689)
Free cash flow	**19,163**	11,007	**20,737**	22,996

Working Capital

Working capital is defined as the Corporation's current assets less its current liabilities and is used to assess the Corporation's short-term liquidity. This non-GAAP measure does not have a standardized meaning and is not a financial measure recognized under GAAP. Management uses working capital to provide insight as to the Corporation's ability to meet obligations as at the reporting date. PHX Energy's method of calculating working capital may differ from that of other organizations and, accordingly, it may not be comparable to that of other companies.

The following is a reconciliation of current assets and current liabilities to working capital:

(Stated in thousands of dollars)

		As at:
	June 30, 2022	December 31, 2021
Current assets	**166,559**	141,159
Deduct:		
Current liabilities	**(90,881)**	(83,287)
Working capital	**75,678**	57,872

Net Debt

Net debt is defined as the Corporation's loans and borrowings less cash and cash equivalents. This non-GAAP measure does not have a standardized meaning and is not a financial measure recognized under GAAP. Management uses net debt to provide insight as to the Corporation's ability to meet obligations as at the reporting date. PHX Energy's method of calculating net debt may differ from that of other organizations and, accordingly, it may not be comparable to that of other companies.

The following is a reconciliation of loans and borrowings and cash and cash equivalents to net debt:

(Stated in thousands of dollars)

	As at:	
	June 30, 2022	December 31, 2021
Loans and borrowings	**20,108**	-
Deduct:		
Cash and cash equivalents	**(17,971)**	(24,829)
Net debt	**2,137**	(24,829)

Gross Profit as a Percentage of Revenue Excluding Depreciation & Amortization and Government Grants

Gross profit as a percentage of revenue excluding depreciation & amortization and government grants is defined as the Corporation's gross profit excluding depreciation and amortization and government grants divided by revenue and is used to assess operational profitability. This non-GAAP measure does not have a standardized meaning and is not a financial measure recognized under GAAP. PHX Energy's method of calculating gross profit as a percentage of revenue may differ from that of other organizations and, accordingly, it may not be comparable to that of other companies.

The following is a reconciliation of revenue, direct costs, depreciation and amortization, government grants and gross profit to gross profit as a percentage of revenue excluding depreciation and amortization and government grants:

(Stated in thousands of dollars)

	Three-month periods ended June 30,		Six-month periods ended June 30,	
	2022	2021	**2022**	2021
Revenue	**126,237**	75,765	**235,568**	144,312
Direct costs	**100,520**	59,437	**192,466**	113,953
Gross profit	**25,717**	16,328	**43,102**	30,359
Depreciation & amortization drilling and other equipment (included in direct costs)	**7,823**	6,277	**15,099**	12,509
Depreciation & amortization right-of-use asset (included in direct costs)	**849**	825	**1,685**	1,661
Government grants (included in direct costs)	**-**	(3,543)	**-**	(6,637)
	34,389	19,887	**59,886**	37,892
Gross profit as a percentage of revenue excluding depreciation & amortization and government grants	**27%**	26%	**25%**	26%

SG&A Costs Excluding Share-Based Compensation as a Percentage of Revenue

SG&A costs excluding share-based compensation as a percentage of revenue is defined as the Corporation's SG&A costs excluding share-based compensation divided by revenue and is used to assess the impact of administrative costs excluding the effect of share price volatility. This non-GAAP measure does not have a standardized meaning and is not a financial measure recognized under GAAP. PHX Energy's method of calculating SG&A costs excluding share-based compensation as a percentage of revenue may differ from that of other organizations and, accordingly, it may not be comparable to that of other companies.

The following is a reconciliation of SG&A costs, share-based compensation, and revenue to SG&A costs excluding share-based compensation as a percentage of revenue:

(Stated in thousands of dollars)

	Three-month periods ended June 30,		Six-month periods ended June 30,	
	2022	2021	**2022**	2021
SG&A Costs	**11,836**	10,629	**33,947**	19,612
Deduct:				
Share-based compensation (included in SG&A)	**640**	4,074	**12,712**	6,786
	11,196	6,555	**21,235**	12,826
Revenue	**126,238**	75,765	**235,568**	144,312
SG&A costs excluding share-based compensation as a percentage of revenue	**9%**	9%	**9%**	9%

SG&A costs excluding share-based compensation and government grants as a percentage of revenue is defined as the Corporation's SG&A costs excluding share-based compensation and government grants as quantified in the respective periods divided by revenue.

Definitions

When the Corporation refers to operating days throughout this document, it is referring to the billable days on which PHX Energy is providing services to the client at the rig site. Average operating revenue per day is calculated by dividing revenue by the number of operating days. Average consolidated revenue per day is calculated by dividing consolidated revenue by the consolidated number of operating days.

Cautionary Statement Regarding Forward-Looking Information and Statements

This MD&A contains certain forward-looking information and statements within the meaning of applicable securities laws. The use of "expect", "anticipate", "continue", "estimate", "objective", "ongoing", "may", "will", "project", "could", "should", "can", "believe", "plans", "intends", "strategy" and similar expressions are intended to identify forward-looking information or statements.

The forward-looking information and statements included in this MD&A are not guarantees of future performance and should not be unduly relied upon. These statements and information involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking statements and information. The Corporation believes the expectations reflected in such forward-looking statements and information are reasonable, but no assurance can be given that these expectations will prove to be correct. Such forward-looking statements and information included in this MD&A should not be unduly relied upon. These forward-looking statements and information speak only as of the date of this MD&A.

In particular, forward-looking information and statements contained in this MD&A include, without limitation:

- PHX Energy intends to protect and preserve its balance sheet strength, capitalize on unique growth strategies and continue to reward its shareholders;
- Anticipated continuation of the Corporation’s quarterly dividend program and the amounts of dividends;
- The projected capital expenditures budget for 2022 of $85 million, and how the budget will be allocated and funded and the competitive advantage that will be created by advanced orders in a challenging supply chain environment;
- Equipment on order as at June 30, 2022 is expected to be delivered throughout second half of 2022 and in the first quarter of 2023;
- The anticipated increased demand for the Corporation’s services and high-performance technologies in North America;
- The Corporation intends to make an application to the TSX for renewal of its NCIB for a further one year term. The anticipated renewal of the NCIB remains subject to the review and approval of the TSX;
- The potential for further impact of COVID-19 on the Corporation’s operations, results and the Corporation’s planned responses thereto;
- The anticipated impact of global supply chain disruptions on the Corporation’s operations, results, and the Corporation’s planned responses thereto;
- Planned expenditures are expected to be financed primarily by funds from operations. However, if a sustained period of market and commodity price uncertainty and financial market volatility persists in 2022, the Corporation’s activity

levels, cash flows and access to credit may be negatively impacted, in which event the proceeds from borrowing may be required to fund operations, and the expenditure level would be reduced accordingly; and

- The potential future settlement of restricted and performance awards in common shares that were purchased by an independent trustee in the open market for such purposes and the expectation that the majority of future settlements will be settled in common shares.

The above are stated under the headings: "Second Quarter Highlights", "Financial Results", "Liquidity", and "Cash Requirements for Capital Expenditures". In addition, all information contained under the headings "Responding to COVID-19", "Critical Accounting Estimates and Judgements", "Business Risk Factors" and "Outlook" sections of this MD&A may contains forward-looking statements.

In addition to other material factors, expectations and assumptions which may be identified in this MD&A and other continuous disclosure documents of the Corporation referenced herein, assumptions have been made in respect of such forward-looking statements and information regarding, among other things: the Corporation will continue to conduct its operations in a manner consistent with past operations; the general continuance of current industry conditions; anticipated financial performance, business prospects, impact of competition, strategies, the general stability of the economic and political environment in which the Corporation operates; the continuing impact of COVID-19 and the Russian-Ukrainian war on the global economy, specifically trade, manufacturing, supply chain and energy consumption, among other things and the resulting impact on the Corporation's operations and future results which remain uncertain, exchange and interest rates including the potential for further interest rate hikes by global central banks and the impact on financing charges and foreign exchange and the anticipated global economic response to concerted interest rate hikes; the continuance of existing (and in certain circumstances, the implementation of proposed) tax, royalty and regulatory regimes; the sufficiency of budgeted capital expenditures in carrying out planned activities; the availability and cost of labour and services and the adequacy of cash flow; debt and ability to obtain financing on acceptable terms to fund its planned expenditures, which are subject to change based on commodity prices; market conditions and future oil and natural gas prices; and potential timing delays. Although management considers these material factors, expectations, and assumptions to be reasonable based on information currently available to it, no assurance can be given that they will prove to be correct.

Readers are cautioned that the foregoing lists of factors are not exhaustive. Additional information on these and other factors that could affect the Corporation's operations and financial results are included in reports on file with the Canadian Securities Regulatory Authorities and may be accessed through the SEDAR website (www.sedar.com) or at the Corporation's website. The forward-looking statements and information contained in this MD&A are expressly qualified by this cautionary statement. The Corporation does not undertake any obligation to publicly update or revise any forward-looking statements or information, whether as a result of new information, future events or otherwise, except as may be required by applicable securities laws.

Condensed Consolidated Statements of Financial Position

(unaudited)

	June 30, 2022	December 31, 2021 *(Adjusted - Note 8f)*
ASSETS		
Current assets:		
Cash and cash equivalents	**$ 17,971,334**	$ 24,828,830
Trade and other receivables	**96,152,034**	76,478,093
Inventories	**47,492,571**	36,691,141
Prepaid expenses	**4,587,966**	2,814,272
Current tax assets	**354,756**	346,554
Total current assets	**166,558,661**	141,158,890
Non-current assets:		
Drilling and other long-term assets (Note 6)	**93,597,375**	76,363,001
Right-of-use asset	**24,822,151**	25,708,177
Intangible assets	**15,833,846**	16,137,024
Investments	**3,000,500**	3,000,500
Deferred tax assets	**311,589**	126,133
Total non-current assets	**137,565,461**	121,334,835
Total assets	**$ 304,124,122**	$ 262,493,725
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Trade and other payables	**$ 84,313,427**	$ 77,571,887
Lease liability	**2,770,862**	3,232,503
Dividends payable (Note 8d)	**3,796,793**	2,482,060
Total current liabilities	**90,881,082**	83,286,450
Non-current liabilities:		
Lease liability	**32,214,382**	32,638,819
Loans and borrowings (Note 7)	**20,107,992**	-
Deferred tax liability	**12,669,815**	9,346,426
Other (Note 8f)	**1,783,812**	2,789,786
Total non-current liabilities	**66,776,001**	44,775,031
Equity:		
Share capital (Note 8a)	**248,949,605**	235,463,414
Contributed surplus	**7,117,440**	9,462,091
Deficit	**(133,214,072)**	(121,721,790)
Accumulated other comprehensive income	**23,614,066**	11,228,529
Total equity	**146,467,039**	134,432,244
Total liabilities and equity	**$ 304,124,122**	$ 262,493,725

See accompanying notes to unaudited condensed consolidated interim financial statements.

Condensed Consolidated Statements of Comprehensive Income (Loss)

(unaudited)

	Three-month periods ended June 30,		Six-month periods ended June 30,	
	2022	2021	**2022**	2021
Revenue	**$ 126,237,557**	$ 75,765,208	**$ 235,568,256**	$ 144,311,945
Direct costs	**100,520,480**	59,436,713	**192,466,162**	113,952,764
Gross profit	**25,717,077**	16,328,495	**43,102,094**	30,359,181
Expenses:				
Selling, general and administrative expenses	**11,836,064**	10,629,415	**33,947,420**	19,611,825
Research and development expenses	**873,207**	624,447	**1,629,766**	1,184,548
Finance expense	**262,188**	94,007	**373,984**	265,232
Finance expense lease liability	**501,385**	534,208	**1,008,401**	1,082,682
Other income (Note 9)	**(3,508,490)**	(1,686,926)	**(7,077,881)**	(4,505,598)
	9,964,354	10,195,151	**29,881,690**	17,638,689
Earnings from continuing operations before income taxes	**15,752,723**	6,133,344	**13,220,404**	12,720,492
Provision for (recovery of) income taxes				
Current	**(13,775)**	11,619	**(229,272)**	20,453
Deferred	**2,948,037**	1,675,191	**2,946,091**	2,918,648
	2,934,262	1,686,810	**2,716,819**	2,939,101
Earnings from continuing operations	**12,818,461**	4,446,534	**10,503,585**	9,781,391
Discontinued operations				
Net loss from discontinued operations, net of taxes (Note 4)	**(12,649,964)**	(67,656)	**(14,558,032)**	(537,493)
Net earnings (loss)	**168,497**	4,378,878	**(4,054,447)**	9,243,898
Other comprehensive income (loss)				
Foreign currency translation	**4,144,053**	(987,617)	**1,824,583**	(2,168,988)
Total comprehensive income (loss) for the period	**$ 4,312,550**	$ 3,391,261	**$ (2,229,864)**	$ 7,074,910
Earnings (loss) per share – basic and diluted				
Continuing operations	**$ 0.25**	$ 0.08	**$ 0.21**	$ 0.19
Discontinued operations	**$ (0.25)**	$ -	**$ (0.29)**	$ (0.01)
Net earnings (loss)	**$ -**	$ 0.08	**$ (0.08)**	$ 0.18

See accompanying notes to unaudited condensed consolidated interim financial statements.

Condensed Consolidated Statements of Changes in Equity

(unaudited)

Six-month period ended June 30, 2022	Share Capital Number	Share Capital Amount ($)	Contributed Surplus	Accumulated Other Comprehensive Income	Retained Earnings	Total Equity
Balance, December 31, 2021	**47,978,662**	**$ 235,463,414**	**$ 9,462,091**	**$ 11,228,529**	**$ (121,721,790)**	**$ 134,432,244**
Issuance of share capital on exercise of options	**982,705**	**1,811,853**	**-**	**-**	**-**	**1,811,853**
Issuance of share capital from trust on settlement of retention awards	**1,972,007**	**12,569,679**	**-**	**-**	**-**	**12,569,679**
Common shares purchased and held in trust	**(555,300)**	**(3,500,000)**	**-**	**-**	**-**	**(3,500,000)**
Share-based payments	**-**	**-**	**260,008**	**-**	**-**	**260,008**
Fair value of options exercised	**-**	**2,604,659**	**(2,604,659)**	**-**	**-**	**-**
Net loss	**-**	**-**	**-**	**-**	**(4,054,447)**	**(4,054,447)**
Foreign currency translation, net of tax	**-**	**-**	**-**	**1,824,583**	**-**	**1,824,583**
Reclassification of foreign currency translation loss on disposition (Note 4)	**-**	**-**	**-**	**10,560,954**	**-**	**10,560,954**
Dividends	**-**	**-**	**-**	**-**	**(7,437,835)**	**(7,437,835)**
Balance, June 30, 2022	**50,378,074**	**$ 248,949,605**	**$ 7,117,440**	**$ 23,614,066**	**$ (133,214,072)**	**$ 146,467,039**

Six-month period ended June 30, 2021	Share Capital Number	Share Capital Amount ($)	Contributed Surplus	Accumulated Other Comprehensive Income	Retained Earnings	Total Equity
Balance, December 31, 2020	50,625,920	$ 247,543,263	$ 10,131,786	$ 11,296,987	$ (136,939,398)	$ 132,032,638
Issuance of share capital on exercise of options	225,267	395,271	-	-	-	395,271
Common shares repurchased and cancelled	(460,888)	(1,204,133)	-	-	-	(1,204,133)
Common shares purchased and held in trust	(786,539)	(3,316,171)	-	-	-	(3,316,171)
Share-based payments	-	-	218,318	-	-	218,318
Fair value of options exercised	-	231,614	(231,614)	-	-	-
Net earnings	-	-	-	-	9,243,898	9,243,898
Foreign currency translation, net of tax	-	-	-	(2,168,988)	-	(2,168,988)
Dividends	-	-	-	-	(2,519,515)	(2,519,515)
Balance, June 30, 2021	49,603,760	$ 243,649,844	$ 10,118,490	$ 9,127,999	$ (130,215,015)	$ 132,681,318

See accompanying notes to unaudited condensed consolidated interim financial statements.

Condensed Consolidated Statements of Cash Flows

(unaudited)

	Three-month periods ended June 30,		Six-month periods ended June 30,	
	2022	2021	**2022**	2021
Cash flows from operating activities:				
Earnings from continuing operations	**$ 12,818,461**	$ 4,446,534	**$ 10,503,585**	$ 9,781,391
Adjustments for:				
Depreciation and amortization	**7,822,953**	6,277,011	**15,099,473**	12,509,160
Depreciation and amortization right-of-use asset	**848,681**	825,454	**1,684,727**	1,661,353
Provision for income taxes	**2,934,262**	1,686,810	**2,716,819**	2,939,101
Unrealized foreign exchange loss (gain)	**(27,999)**	140,177	**(118,526)**	188,816
Gain on disposition of drilling equipment	**(3,059,873)**	(1,483,034)	**(6,641,623)**	(4,302,196)
Equity-settled share-based payments	**(74,706)**	149,817	**260,008**	218,318
Finance expense	**262,188**	94,007	**373,984**	265,232
Recovery of bad debts	**-**	(264,623)	**-**	(264,623)
Provision for inventory obsolescence	**297,639**	426,538	**824,656**	1,105,881
Interest paid	**(127,248)**	(47,463)	**(178,171)**	(106,836)
Income taxes received (paid)	**14,880**	(8,097)	**219,130**	(20,316)
Change in non-cash working capital	**(10,259,827)**	(3,398,566)	**(17,003,987)**	(13,601,474)
Continuing operations	**11,449,411**	8,844,565	**7,740,075**	10,373,807
Discontinued operations (Note 4)	**(520,334)**	(472,558)	**(1,254,859)**	(590,149)
Net cash from operating activities	**10,929,077**	8,372,007	**6,485,216**	9,783,658
Cash flows from investing activities:				
Proceeds on disposition of drilling equipment	**3,883,133**	2,740,941	**9,179,549**	6,525,814
Acquisition of drilling and other equipment	**(15,213,688)**	(10,518,640)	**(33,419,918)**	(17,408,157)
Acquisition of intangible assets	**(206,930)**	-	**(618,205)**	-
Change in non-cash working capital	**(2,924,122)**	2,411,228	**710,890**	4,715,729
Continuing operations	**(14,461,607)**	(5,366,471)	**(24,147,684)**	(6,166,614)
Discontinued operations (Note 4)	**(316,392)**	13,406	**(68,068)**	13,855
Net cash used in investing activities	**(14,777,999)**	(5,353,065)	**(24,215,752)**	(6,152,759)
Cash flows from financing activities:				
Proceeds from loans and borrowings	**16,359,192**	-	**20,107,992**	-
Proceeds from issuance of share capital	**169,666**	-	**1,811,853**	395,271
Dividends paid to shareholders	**(3,790,543)**	(1,259,757)	**(6,272,603)**	(2,525,405)
Purchase of shares held in trust	**(1,500,000)**	(3,316,171)	**(3,500,000)**	(3,316,171)
Payments of lease liability	**(872,923)**	(814,514)	**(1,731,911)**	(1,605,880)
Repurchase of shares under the NCIB	**-**	-	**-**	(1,204,133)
Continuing operations	**10,365,392**	(5,390,442)	**10,415,331**	(8,256,318)
Discontinued operations	**-**	-	**-**	-
Net cash from (used in) financing activities	**10,365,392**	(5,390,442)	**10,415,331**	(8,256,318)
Net increase (decrease) in cash and cash equivalents	**6,516,470**	(2,371,500)	**(7,315,205)**	(4,625,419)
Cash and cash equivalents, beginning of period	**11,283,545**	23,468,419	**24,828,830**	25,745,911
Effect of movements in exchange rates on cash held	**171,319**	(70,872)	**457,709**	(94,445)
Cash and cash equivalents, end of period	**$ 17,971,334**	$ 21,026,047	**$ 17,971,334**	$ 21,026,047

See accompanying notes to unaudited condensed consolidated interim financial statements.

Notes to the Condensed Consolidated Financial Statements

For the three and six-month periods ended June 30, 2022 and 2021

In Canadian dollars (unaudited)

1. Reporting Entity

PHX Energy Services Corp. ("PHX Energy" or the "Corporation") is a publicly-traded Corporation listed on the Toronto Stock Exchange ("TSX") under the symbol "PHX". The Corporation's registered office is at Suite 1600, 215 – 9th Avenue SW Calgary, Alberta, Canada.

The Corporation, through its subsidiaries, provides horizontal and directional drilling services to oil and natural gas exploration and development companies in Canada, United States, Albania, and the Middle East regions. The Middle East region operates through an arrangement with National Energy Services Reunited Corp. The Corporation also develops and manufactures technologies that are made available for internal operational use.

The condensed consolidated interim financial statements include the accounts of the Corporation and its wholly owned subsidiaries. The Corporation has presented its operations in Russia as a discontinued operation (see Note 4).

2. Basis of Preparation

a) Statement of Compliance

These condensed consolidated interim financial statements have been prepared in accordance with IAS 34 Interim Financial Reporting. The condensed consolidated interim financial statements do not include all of the information required for full annual financial statements and should be read in conjunction with the consolidated financial statements of the Corporation as at and for the year ended December 31, 2021.

These condensed consolidated interim financial statements were authorized by the Board of Directors on August 9, 2022.

b) Basis of Measurement

The condensed consolidated interim financial statements have been prepared on a going concern basis using the historical cost basis except for liabilities for cash-settled share-based payment arrangements and investments, which are measured at fair value. Liabilities for cash-settled share-based payment arrangements are included in trade and other payables in the statement of financial position.

c) Functional and Presentation Currency

These condensed consolidated interim financial statements are presented in Canadian dollars ("CAD"), which is the Corporation's functional currency.

d) Use of Estimates and Judgments

The preparation of the condensed consolidated interim financial statements in conformity with International Financial Reporting Standards ("IFRS") requires Management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

In preparing these condensed consolidated interim financial statements, the significant judgments made by Management in applying the Corporation's accounting policies and the key sources of estimation uncertainty have not changed significantly since December 31, 2021.

3. Significant Accounting Policies

These condensed consolidated interim financial statements have been prepared utilizing the same accounting policies and methods as the consolidated financial statements of the Corporation for the year ended December 31, 2021, unless specified.

4. Discontinued Operations

a) Impairment and Other Write-Offs of Russian Assets

In the first quarter of 2022, the Corporation determined the Russian operations to be in its own cash-generating unit ("CGU") due to a divergence in its overall risk profile from the rest of the International CGU. Concurrently, PHX Energy recognized:

- Impairment loss of approximately $0.4 million on drilling and other equipment owned by the Russian operations, Phoenix TSR LLC ("Phoenix TSR");
- Write-offs of $0.6 million related to inventories owned by the Russian operations; and,
- Expected credit losses of $1 million related to certain trade receivables owned by Phoenix TSR.

b) Discontinued Operations and Loss on Disposition

On June 30, 2022, the Corporation completed the sale of its Russian division. The transaction involved the sale of all shares of Phoenix TSR, a legally wholly-owned subsidiary of PHX Energy that held the entire Russian drilling operations. The operations were previously classified under the Russia operating segment for reporting purposes.

	June 30, 2022
Consideration on sale of Phoenix TSR, satisfied in cash	**$ 404**
Less net assets of Phoenix TSR comprised of working capital:	**(3,496,576)**
Loss on disposition of Phoenix TSR	**$ (3,496,172)**

The divested Russian division met the criteria for discontinued operations in the second quarter of 2022.

The results of the divested Phoenix TSR operations are as follows:

	Three-month period ended June 30,		Six-month period ended June 30,	
	2022	2021	**2022**	2021
Revenue	**$ 4,647,656**	$ 2,072,857	**$ 7,443,368**	$ 3,631,911
Expenses	**(3,071,762)**	2,140,513	**(5,781,276)**	4,170,483
	1,575,894	(67,656)	**1,662,092**	(538,572)
Reclassification of foreign currency translation loss on disposition of Phoenix TSR	**(10,560,954)**	-	**(10,560,954)**	-
Loss on disposition of Phoenix TSR	**(3,496,172)**	-	**(3,496,172)**	-
Impairment and other write-offs	**-**	-	**(1,966,848)**	-
Loss from discontinued operations	**(12,481,232)**	(67,656)	**(14,361,882)**	(538,572)
Income tax from discontinued operations	**168,732**	-	**196,150**	(1,079)
Loss from discontinued operations, net of taxes	**$ (12,649,964)**	$ (67,656)	**$ (14,558,032)**	$ (537,493)

Reconciliation of net loss from discontinued operations, net of taxes to cash used in discontinued operations is as follows:

	Three-month period ended June 30,		Six-month period ended June 30,	
	2022	2021	**2022**	2021
Net loss from discontinued operations, net of taxes	**$ (12,649,964)**	$ (67,656)	**$ (14,558,032)**	$ (537,493)
Addback (deduct):				
Depreciation and amortization	**-**	-	**136,024**	-
Provision for income taxes	**168,732**	-	**196,150**	(1,079)
Unrealized foreign exchange (gain) loss	**(83,816)**	1,755	**(56,497)**	7,576
Interest and taxes received (paid), net	**(3,110)**	(3,172)	**(3,316)**	3,778
Loss (gain) on disposition of drilling equipment	**316,392**	(5,273)	**68,068**	(5,722)
Finance expense	**2,004**	3,154	**3,316**	(3,915)
Reclassification of foreign currency translation loss on disposition of Phoenix TSR	**10,560,954**	-	**10,560,954**	-
Impairment and other write-offs	**-**	-	**1,966,848**	-
Loss on disposition of Phoenix TSR	**3,496,172**	-	**3,496,172**	-
Change in non-cash working capital	**(2,327,698)**	(401,366)	**(3,064,546)**	(53,294)
Cash used in operating activities	**$ (520,334)**	$ (472,558)	**$ (1,254,859)**	$ (590,149)

Cash from (used in) investing activities of discontinued operations are due to proceeds from disposition and a reversal of previously accrued proceeds.

5. Operating Segments

The Corporation provides directional and horizontal oil and natural gas well drilling services. PHX Energy's reportable segments have been aligned as follows:

Information about reportable segments

(Stated in thousands of dollars)

	Canada		United States		International		Total	
Three-month periods ended June 30,	**2022**	2021	**2022**	2021	**2022**	2021	**2022**	2021
Total Revenue	**19,704**	10,250	**105,367**	65,515	**1,167**	-	**126,238**	75,765
Reportable segment profit (loss) before income taxes	**(16)**	224	**16,885**	11,272	**523**	(471)	**17,392**	11,025

(Stated in thousands of dollars)

	Canada		United States		International		Total	
Six-month periods ended June 30,	**2022**	2021	**2022**	2021	**2022**	2021	**2022**	2021
Total Revenue	**46,843**	25,697	**187,162**	118,615	**1,563**	-	**235,568**	144,312
Reportable segment profit (loss) before income taxes	**3,450**	2,549	**23,331**	18,494	**361**	(798)	**27,142**	20,245

(Stated in thousands of dollars)

	Canada		United States[1]		International		Total	
As at June 30,	**2022**	2021	**2022**	2021	**2022**	2021	**2022**	2021
Drilling and other equipment	**18,216**	13,030	**74,856**	57,608	**525**	426	**93,597**	71,064

[1] June 30, 2022 includes USD $1.5 million of drilling and other equipment physically located in the Middle East region as part of a technology arrangement (2021 – USD $2 million).

Reconciliation of reportable segment profit and other material items

(Stated in thousands of dollars)

	Three-month periods ended June 30,		Six-month periods ended June 30,	
	2022	2021	**2022**	2021
Reportable segment income before income taxes	**17,392**	11,025	**27,142**	20,245
Corporate:				
Selling, general and administrative expenses	**3,511**	5,327	**17,988**	9,498
Research and development expenses	**873**	624	**1,630**	1,185
Finance expense	**262**	94	**374**	265
Finance expense lease liability	**501**	534	**1,008**	1,083
Other income	**(3,508)**	(1,687)	**(7,078)**	(4,506)
Earnings from continuing operations before income taxes	**15,753**	6,133	**13,220**	12,720

6. Drilling and Other Equipment

a) Acquisitions and Disposals

During the six-month period ended June 30, 2022, the Corporation acquired assets with a cost of $33.4 million (2021 - $17.4 million).

Assets with a carrying amount of $2.5 million (2021 - $2.2 million) were disposed of as a result of tools lost down hole and scrapped assets, resulting in a net gain on disposition of $6.6 million (2021 - $4.3 million), which is included in other income in the condensed consolidated statement of comprehensive income (loss).

b) Capital Commitments

As at June 30, 2022, the Corporation has commitments to purchase drilling and other equipment for $47.2 million with delivery expected to occur throughout the 2022 year and into early 2023.

7. Loans and Borrowings

(Stated in thousands of dollars)

	Currency	Amount of Facility	Date of Maturity	**Currency**	**Carrying Amount at June 30, 2022**	Currency	Carrying Amount at December 31, 2021
Operating Facility	CAD	15,000	December 12, 2023	CAD	**9,108**	CAD	-
Syndicated Facility	CAD	50,000	December 12, 2023	CAD	**11,000**	CAD	-
US Operating Facility	USD	15,000	December 12, 2023	USD	**-**	USD	-

Under the syndicated loan agreement, the Corporation is required to maintain certain financial covenants. As at June 30, 2022 the Corporation was in compliance with all of its financial covenants as follows:

Ratio	Covenant	**June 30, 2022**
Debt to covenant EBITDA	< 3.0x	**0.36**
Interest coverage ratio	> 3.0x	**90.80**

The facilities bear interest based primarily on the Corporation's debt to earnings before interest, taxes, depreciation and amortization ("EBITDA") ratio, as defined in the credit agreement. Interest on the operating facility is at the bank's prime rate plus 0.5 percent. Interest on the syndicated facility is at the Secured Overnight Financing Rate ("SOFR") plus 1.5 percent.

As at June 30, 2022 the Corporation has approximately CAD $45 million and USD $15 million available to be drawn from its credit facilities. The credit facilities are secured by substantially all of the Corporation's assets.

8. Share Capital

a) Authorized and Issued Shares

The Corporation is authorized to issue an unlimited number of shares.

	Number		Amount
Balance as at January 1, 2021	50,625,920	$	247,543,263
Common shares repurchased and cancelled	(1,960,788)		(7,979,601)
Common shares repurchased and held in trust	(1,662,537)		(7,500,000)
Issued shares pursuant to share option plan	976,067		3,399,752
Balance as at December 31, 2021	47,978,662	$	235,463,414
Common shares repurchased and held in trust	**(555,300)**		**(3,500,000)**
Issued shares pursuant to retention awards plan	**1,972,007**		**12,569,679**
Issued shares pursuant to share option plan	**982,705**		**4,416,512**
Balance as at June 30, 2022	**50,378,074**	**$**	**248,949,605**

b) Share Option Program (Equity-Settled)

PHX Energy has a share option program that entitles key management personnel and other employees to purchase common shares in the Corporation. Grants under the plan vest as to one-third 6 months from the grant date, one-third 18 months from grant date and one-third 30 months from grant date. In accordance with these programs, options are exercisable using the five-day weighted-average trading price of the common shares ending immediately prior to the date of grant, or in the case of a US option holder, the trading price of the common shares ending immediately prior to the date of grant. The options have a term of five years.

Summary of option grants in 2022

Number		Exercise Price	Expiration Date		Fair Value
150,000	$	6.08	March 4, 2027	$	1.91
100,000		6.16	March 4, 2027		1.89
250,000					

The Corporation values all of its share options using the Black-Scholes model. The Corporation's determination of fair value of options on the date of grant is affected by the Corporation's share price as well as assumptions regarding a number of variables. For the options granted during 2022 these variables include, but are not limited to, the Corporation's expected share price volatility over the term of the options of 54 percent, forfeiture rate of nil, dividend yield of 4.89 percent and a risk-free interest rate of 1.4 percent. The amounts computed according to the Black-

Scholes model method may not be indicative of the actual values realized upon the exercise of these options by the holders.

During the six-month period ended June 30, 2022, a total of 1,047,800 options granted in 2017 were net equity-settled through the issuance of 342,972 common shares. Total compensation expense related to stock options recognized for the three and six-month periods ended June 30, 2022 were $0.1 million recovery and $0.3 million, respectively (2021 - $0.1 million and $0.2 million, respectively).

A summary of the status of the plan as at June 30, is presented below:

	June 30, 2022		December 31, 2021	
	Options	**Weighted-Average Exercise Price**	Options	Weighted-Average Exercise Price
Outstanding, beginning of period	**2,854,200**	**$ 3.15**	3,345,267	$ 3.01
Granted	**250,000**	**6.11**	500,000	2.70
Exercised	**(1,687,533)**	**3.60**	(976,067)	2.40
Forfeited / cancelled	**-**	**-**	(15,000)	4.15
Outstanding, end of period	**1,416,667**	**3.14**	2,854,200	3.15
Options exercisable, end of period	**749,997**	**2.45**	2,437,530	3.25

The range of exercise prices for options outstanding at June 30, 2022 are as follows:

Options Outstanding			Options Exercisable	
Number	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price	Number	Weighted-Average Exercise Price
50,000	0.69 yrs	1.95	50,000	1.95
150,000	0.69 yrs	2.00	150,000	2.00
66,667	2.68 yrs	2.09	33,333	2.09
150,000	2.68 yrs	2.19	99,999	2.19
200,000	3.68 yrs	2.64	66,666	2.64
300,000	3.68 yrs	2.74	99,999	2.74
200,000	1.69 yrs	2.81	200,000	2.81
50,000	1.69 yrs	2.83	50,000	2.83
150,000	4.68 yrs	6.08	-	6.08
100,000	4.68 yrs	6.16	-	6.16
1,416,667	2.93 yrs	$ 3.14	749,997	$ 2.45

c) Retention Award Plan

The retention award plan has two types of awards: Restricted Awards (“RAs”) and Performance Awards (“PAs”) and results in eligible participants receiving cash or common shares in relation to the value of a specified number of underlying notional retention awards. If common shares are used to settle awards, an additional multiplier to the award value of 1.25 times is applied. Common shares acquired in the open market are held in trust for the potential settlement of RA and PA award values and are netted out of share capital, including the cumulative purchase cost, until they are distributed for future settlements. For the six-month period ended June 30, 2022, the trustee purchased 555,300 common shares (2021 – 786,539) for a total cost of $3.5 million (2021 - $3.3 million) and released 1,972,007 common shares (2021 – nil) to settle retention award obligations of $12.6 million (2021 - $nil). As at June 30, 2022, the Corporation held 245,830 common shares in trust (2021 – 786,539). The Corporation continues to account for its retention award plan as cash-settled share-based compensation.

RAs vest evenly over a period of three-years. Upon vesting and subsequent exercise, the holder is entitled to receive a cash payment or common shares based on the fair value of the underlying shares determined using the five-day weighted-average trading price of the shares ending immediately prior to the exercise date plus accrued re-invested dividends.

PAs vesting and subsequent exercise is similar to RAs, except a payout multiplier is applied to the final payout. The payout multiplier is linked solely to total shareholder return on the Corporation’s common shares relative to returns on securities of members of the Corporation’s peer comparison group over the applicable vesting period and can range from a payout of zero percent to 200 percent. For the six-month period ended June 30, 2022, 750,000 PAs were granted (2021 – 750,000), 774,152 PAs settled at a weighted average payout multiplier of 200 percent (2021 – 757,184), no PAs were forfeited (2021 - nil), and as at June 30, 2022, 1,538,504 PAs were outstanding (2021 – 1,507,184).

The Corporation recorded a total of $12.5 million compensation expense relating to these plans for the six-month period ended June 30, 2022 (2021 – $6.5 million). The expense is included in selling, general and administrative expense and has a corresponding liability in trade and other payables for the current portion and other liabilities for the long-term portion. There were 3,425,196 RAs and PAs outstanding as at June 30, 2022 (2021 – 3,356,736).

A summary of the status of the plan as at June 30, 2022 is presented below:

	June 30, 2022	December 31, 2021
RAs and PAs outstanding, beginning of period	**3,267,579**	3,487,297
Granted	**1,609,299**	1,666,514
Settled	**(1,451,682)**	(1,808,415)
Forfeited / cancelled	**-**	(77,817)
RAs and PAs outstanding, end of period	**3,425,196**	3,267,579

d) Dividends

On June 15, 2022, the Corporation declared a dividend of $0.075 per share or $3.8 million payable on July 15, 2022.

e) Normal Course Issuer Bid

During the third quarter of 2021, the TSX approved the renewal of PHX Energy's Normal Course Issuer Bid ("NCIB") to purchase for cancellation, from time-to-time, up to a maximum of 3,679,797 common shares, representing 10 percent of the Corporation's public float of Common Shares as at August 6, 2021. The NCIB commenced on August 16, 2021 and will terminate on August 15, 2022. Purchases of common shares are to be made on the open market through the facilities of the TSX and through alternative trading systems. The price which PHX Energy is to pay for any common shares purchased is to be at the prevailing market price on the TSX or alternate trading systems at the time of such purchase. Pursuant to the current NCIB, 1,499,900 common shares were purchased by the Corporation and cancelled as at December 31, 2021. For the six-month period ending June 30, 2022, the Corporation did not repurchase shares through its current NCIB.

The Corporation's previous NCIB commenced on August 14, 2020 and terminated on August 13, 2021. Pursuant to the previous NCIB, 3,131,388 common shares were repurchased and cancelled by the Corporation of which 460,888 were repurchased and cancelled in 2021.

f) Prior Period Adjustment

The Corporation identified that the classification of the cash-settled liability awards between current and long-term liabilities was not correct as at December 31, 2021. As a result, the Corporation adjusted the December 31, 2021 statement of financial position to reclassify $2.8 million of liabilities from current (trade and other payables) to long-term (other non-current liabilities).

9. Other Income

(Stated in thousands of dollars)

	Three-month periods ended June 30,		Six-month periods ended June 30,	
	2022	2021	**2022**	2021
Net gain on disposition of drilling equipment	**(3,060)**	(1,483)	**(6,642)**	(4,302)
Foreign exchange losses	**64**	61	**76**	61
Recovery of bad debts	**-**	(265)	**-**	(265)
Other	**(512)**	-	**(512)**	-
Other income	**(3,508)**	(1,687)	**(7,078)**	(4,506)

10. Fair Values of Financial Instruments

The Corporation has designated its trade and other payables, dividends payable, and loans and borrowings as non-derivative financial liabilities carried at amortized cost. Cash and cash equivalents and trade and other receivables are designated as non-derivative financial assets measured at amortized cost. The Corporation's carrying values of these items approximate their fair value due to the relatively short periods to maturity of the instruments.

Equity investments in a company are designated as non-derivative financial assets measured at Fair Value Through Other Comprehensive Income ("FVOCI") as the investment is not held-for-trading and fair value changes are not reflective of the Corporation's operations. The investment asset is carried at fair value on the Consolidated Statement of Financial Position. Fair value is considered level 3 under the fair value hierarchy and requires management to assess information available, which may include private placements, available financial statement information and other available market data.

Corporate Information

Board of Directors

John Hooks

Randolph (“Randy”) M. Charron

Myron Tétreault

Karen David-Green

Lawrence Hibbard

Roger Thomas

Terry Freeman

Officers

John Hooks
CEO

Michael Buker
President

Cameron Ritchie
Sr. Vice President Finance and CFO
Corporate Secretary

Craig Brown
Sr. Vice President Engineering and Technology

Jeffery Shafer
Sr. Vice President Sales and Marketing

Legal Counsel

Burnet, Duckworth & Palmer LLP
Calgary, Alberta

Auditors

KPMG LLP
Calgary, Alberta

Bankers

HSBC Bank Canada
Calgary, Alberta

Transfer Agent

Odyssey Trust Company
Calgary, Alberta