ORCA EXPLORATION GROUP INC.

MANAGEMENT'S DISCUSSION & ANALYSIS

Financial and Operating Highlights

(Expressed in US$'000 unless indicated otherwise)	THREE MONTHS ENDED/ AS AT 31 MARCH 2016	2015
OPERATING		
Daily average gas delivered and sold *(MMcfd)*		
Protected Gas	**36.8**	39.0
Additional Gas	**46.3**	49.1
Industrial	**10.7**	10.3
Power	**35.6**	38.8
Total gas production	**83.1**	88.1
Average price *(US$/mcf)*		
Industrial	**8.15**	7.54
Power	**3.55**	3.49
Total	**4.61**	4.34
Operating netback *(US$/mcf)*	**3.08**	1.86
FINANCIAL		
Revenue	**15,810**	9,720
Funds flow from operating activities [(1)]	**9,853**	3,712
per share - basic and diluted *(US$)*	**0.28**	0.11
Net cash flows from operating activities	**(1,154)**	7,375
per share - basic and diluted *(US$)*	**(0.03)**	0.21
Net loss	**(5,638)**	(1,677)
per share - basic and diluted *(US$)*	**(0.16)**	(0.05)
Working capital	**56,340**	34,870
Cash	**72,300**	62,640
Capital expenditures	**13,997**	1,139
Long-term loan	**58,350**	–
Outstanding shares *('000)*		
Class A	**1,751**	1,751
Class B	**33,106**	33,164
Total shares outstanding	**34,857**	34,915
Options	**–**	400
Weighted average diluted Class A and Class B shares	**34,857**	35,315

[(1)] *See MD&A – Non-GAAP Measures.*

Q1 2016 Operating Highlights

- Revenue for the quarter increased 63% to US$15.8 million from US$9.7 million in Q1 2015. The increase is primarily a consequence of the Company being entitled to a greater allocation of net revenue due to the workover of three offshore wells and the drilling of a new offshore well. The offshore workover and development programme commenced in the third quarter of 2015 and was completed in the first quarter of 2016. The expenditures substantially increased the pool of recoverable cost, entitling the Company to 75% of net revenue as Cost Gas in the quarter with the corresponding reduction in Profit Gas reducing the Profit Gas attributable to TPDC by 61%. The 6% fall in the volumes of Additional Gas sold in the quarter to 46.3 MMcfd from 49.1 MMcfd in Q1 2015 having been substantially offset by a 6% rise in the weighted average sale price to US$4.61/Mcf from US$4.34/Mcf in Q1 2015.
- Funds flow from operating activities increased by 165% to US$9.9 million or US$0.28 per share basic and diluted (Q1 2015: US$3.7 million or US$0.11 per share basic and diluted), primarily as a result of the 63% increase in revenue.
- A net loss of US$5.6 million or US$0.16 per share was recorded for the quarter compared to a net loss of US$1.7 million or US$0.05 per share in Q1 2015. The loss in the quarter was primarily the result of a US$8.0 million provision against the receivable from TANESCO. The increase in the provision together with the US$2.8 million charge for stock based compensation offset the increase in revenue for the quarter. The increase in the level of stock based compensation being the combination of an increase in the share price to CDN$4.14 per share from CDN$2.75 as at 31 December 2015 and the granting of new Restrictive Stock Units to non-executive directors.
- TANESCO payments for the quarter continued to be irregular. During the quarter, the Company received a total of US$3.6 million (Q4 2015: US$4.5 million) from TANESCO against sales invoices totaling US$10.9 million (Q4 2015: US$11.7 million). Management has reviewed the current position with TANESCO and feels that the current policy to reclassify all amounts receivable from TANESCO in excess of 60 days, and in arrears, as a long-term receivable is still appropriate. For Q1 2016, the Company has classified an additional US$8.0 million, the arrears in excess of 60 days, as a long-term receivable and has recorded a full provision against this. The current total provision is US$69.9 million (Q4 2015: US$61.9 million). As at the date of this report the total receivable is US$77.3 million.
- Working capital as at 31 March 2016 increased by 62% to US$56.3 million from US$34.9 million in Q1 2015. The increase is primarily a result of the increase in long-term debt of US$58.4 million offset by capital expenditures primarily related to the recently completed Offshore Programme.
- Total capital expenditures for the quarter were US$14.0 million compared to US$1.1 million in Q1 2015. The capital expenditure in the quarter was incurred on the successful completion of the new offshore well SS-12 that was spud in December 2015.
- On 29 October 2015, the Company and the International Finance Corporation ("IFC") completed a debt financing agreement to borrow up to US$60 million. The financing is a subordinated, income participating loan with flexible repayment terms and a maximum tenure of approximately 10 years. The Company has drawn the US$60 million Loan facility in full, with an initial drawdown of US$20 million on 14 December 2015 followed by an additional draw down of US$40 million on 9 February 2016. The Offshore Programme was completed on 11 February 2016. The loan is stated on the balance sheet net of associated capitalized set up costs which will be amortised over the life of the loan.

Management's Discussion & Analysis

THIS MD&A OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED 31 MARCH 2016 SHOULD BE READ IN CONJUNCTION WITH THE AUDITED CONSOLIDATED FINANCIAL STATEMENTS AND NOTES TOGETHER WITH THE MD&A FOR THE YEAR ENDED 31 DECEMBER 2015. THIS MD&A IS BASED ON THE INFORMATION AVAILABLE ON 19 MAY 2016.

FORWARD LOOKING STATEMENTS

This management's discussion and analysis ("MD&A") contains forward-looking statements or information (collectively, "forward-looking statements") within the meaning of applicable securities legislation. More particularly, this MD&A contains, without limitation, forward-looking statements pertaining to the following: the Company's expectations regarding supply and demand of natural gas; anticipated power sector revenues; potential impact of TPDC future back-in rights on the economic terms of the Production Sharing Agreement ("PSA"); the commissioning of the second gas processing facility on Songo Song Island which is part of the National Natural Gas Infrastructure Project ("NNGIP") which includes the construction and commissioning of two gas processing facilities, a 505 kilometer pipeline supplying gas from the Mtwara Region of Tanzania to Dar es Salaam and a 28 kilometer pipeline supplying gas from Songo Songo Island to the mainland NNGIP; ability to meet all conditions under the International Finance Corporation ("IFC") financing agreement signed on 29 October 2015; the Company's estimated spending for the planned Development Programme for 2016 and 2017, which includes construction of the production platform for well SS-12, tie-in of well SS-12 to the production facilities and implementation of a refrigeration unit to enable production into the NNGIP; the potential impact of the Petroleum Act, 2015 ("Act") on the Company's business in Tanzania; the Company's belief that the parties to the unsigned Amended and Restated Gas Agreement ("ARGA") will continue to conduct themselves in accordance with the ARGA until the new Gas Sales Agreement ("GSA") is signed; the Company's expectation that, despite the Re-Rating Agreement of the gas processing plant owned by Songas Limited ("Songas") having expired, the Songas gas processing plant will not be de-rated and the risk that Songas and the Company will not agree on appropriate terms and sign the GSA in a timely manner; the Company's expectation that it can expand and maintain the deliverability of gas volumes in excess of the existing Songas infrastructure; the Company's expectation that the SS-4 well may need to be suspended in the future; the forward-looking statements under "Contractual Obligations and Committed Capital Investment"; the Company's expectation that it will not have a shortfall during the term of the Protected Gas delivery obligation to July 2024; and the Company's expectations in respect of its appeal on the decision of the Tax Revenue Appeals Tribunal and other statements under "Contingencies – Taxation". In addition, statements relating to "reserves" are by their nature forward-looking statements, as they involve the implied assessment, based on certain estimates and assumptions that the reserves described can be profitably produced in the future. The recovery and reserve estimates of the Company's reserves provided herein are estimates only and there is no guarantee that the estimated reserves will be recovered. As a consequence, actual results may differ materially from those anticipated in the forward-looking statements. Although management believes that the expectations reflected in the forward-looking statements are reasonable, it cannot guarantee future results, levels of activity, performance or achievement since such expectations are inherently subject to significant business, economic, operational, competitive, political and social uncertainties and contingencies.

These forward-looking statements involve substantial known and unknown risks and uncertainties, certain of which are beyond the Company's control, and many factors could cause the Company's actual results to differ materially from those expressed or implied in any forward-looking statements made by the Company, including, but not limited to: failure to receive payments from the Tanzanian Electrical Supply Company ("TANESCO"); risk on timing for the NNGIP to be fully commissioned; risk that the Tanzanian Production Development Corporation ("TPDC"), the Ministry of Energy and Minerals ("MEM") and the Company are unable to agree on commercial terms for future incremental gas sales and consequently the Company cannot expand the Songo Songo development beyond the existing Songas infrastructure and supply gas to the NNGIP; risk that additional gas volumes available to the NNGIP from third parties will replace all or a portion of the volumes currently nominated by TANESCO under the Portfolio Gas Sales Agreement ("PGSA") until additional gas-fired power generation is brought on-stream to consume all of the Company's available gas production; risk that the Development Programme is not completed as planned and the actual cost to complete the Development Programme exceeds the Company's estimates; risk that the remaining well workovers under the Development Programme are unsuccessful or determined to be infeasible; risk that the contingencies related to the development work for the full field development plan for Songo Songo are not satisfied; potential negative effect on the Company's rights under the PSA and other agreements relating to its business in Tanzania as a result of the recently approved Act, as well as the risk that such legislation will create additional costs and time connected with the Company's business in Tanzania; risk that, without extending or replacing the Re-Rating Agreement, the gas processing plant may be de-rated back to its original capacity, resulting in a material reduction in the Company's sales volumes of Additional Gas; risk that the Company will not fully recover Songas' share of capital expenditures associated with the workovers of wells SS-5 and SS-9; risk that the Company will be required to pay additional taxes and penalties; the impact of general economic conditions in the areas in which the Company operates; civil unrest; industry conditions; changes in laws and regulations including the adoption of new environmental laws and regulations and changes in how they are interpreted and enforced; increased competition; the lack of availability of qualified personnel or management; fluctuations in commodity prices, foreign exchange or interest rates; stock market volatility; competition for, among other things, capital, drilling equipment and skilled personnel; failure to obtain required equipment for drilling; delays in drilling plans; failure to obtain expected results from drilling of wells; effect of changes to the PSA on the Company; changes in laws; imprecision in reserve estimates; the production and growth potential of the Company's assets; obtaining required approvals of regulatory authorities; risks associated with negotiating with foreign governments; inability to satisfy debt obligations and conditions; failure to successfully negotiate agreements; and risk that the Company will not be able to fulfil its contractual obligations. In addition there are risks and uncertainties associated with oil and gas operations, therefore the Company's actual results, performance or achievement could differ materially from those expressed in, or implied by, these forward-looking statements and, accordingly, no assurances can be given that any of the events anticipated by these forward-looking statements will transpire or occur, or if any of them do so, what benefits the Company will derive therefrom. Readers are cautioned that the foregoing list of factors is not exhaustive.

Such forward-looking statements are based on certain assumptions made by the Company in light of its experience and perception of historical trends, current conditions and expected future developments, as well as other factors the Company believes are appropriate in the circumstances, including, but not limited to, that the NNGIP is completed; the TPDC, the MEM and the Company are able to agree on commercial terms for future incremental gas sales and the Company can expand Songo Songo development beyond the existing Songas infrastructure and supply gas to the NNGIP; the Development Programme will be completed within the timing anticipated; the actual costs to complete the Development Programme are in line with estimates; that there will continue to be no restrictions on the movement of cash from Mauritius or Tanzania; that the Company will have sufficient cash flow, debt or equity sources or other financial resources required to fund its capital and operating expenditures and requirements as needed; that the Company will have adequate funding to continue operations; that the Company will successfully negotiate agreements; receipt of required regulatory approvals; the ability of the Company to increase production at a consistent rate; infrastructure capacity; commodity prices will not further deteriorate significantly; the ability of the Company to obtain equipment and services in a timely manner to carry out exploration, development and exploitation activities; future capital expenditures; availability of skilled labour; timing and amount of capital expenditures; uninterrupted access to infrastructure; the impact of increasing competition; conditions in general economic and financial markets; effects of regulation by governmental agencies; that the Company's appeal of various tax assessments will be successful; that the enactment of the Act in Tanzania will not impair the Company's rights under the PSA to develop and market natural gas in Tanzania; current or, where applicable, proposed industry conditions, laws and regulations will continue in effect or as anticipated as described herein; and other matters.

The forward-looking statements contained in this MD&A are made as of the date hereof and the Company undertakes no obligation to update publicly or revise any forward-looking statements or information, whether as a result of new information, future events or otherwise, unless so required by applicable securities laws.

NON-GAAP MEASURES

THE COMPANY EVALUATES ITS PERFORMANCE USING A NUMBER OF NON-GAAP (GENERALLY ACCEPTED ACCOUNTING PRINCIPLES) MEASURES. THESE NON-GAAP MEASURES ARE NOT STANDARDISED AND THEREFORE MAY NOT BE COMPARABLE TO SIMILAR MEASUREMENTS OF OTHER ENTITIES.

- FUNDS FLOW FROM OPERATING ACTIVITIES IS A TERM THAT REPRESENTS CASH FLOW FROM OPERATIONS BEFORE WORKING CAPITAL CHANGES. IT IS A KEY MEASURE AS IT DEMONSTRATES THE COMPANY'S ABILITY TO GENERATE CASH NECESSARY TO ACHIEVE GROWTH THROUGH CAPITAL INVESTMENTS.
- OPERATING NETBACKS REPRESENT THE PROFIT MARGIN ASSOCIATED WITH THE PRODUCTION AND SALE OF ADDITIONAL GAS AND IS CALCULATED AS REVENUES LESS PROCESSING AND TRANSPORTATION TARIFFS, GOVERNMENT PARASTATAL'S REVENUE SHARE, OPERATING AND DISTRIBUTION COSTS FOR ONE THOUSAND STANDARD CUBIC FEET OF ADDITIONAL GAS. THIS IS A KEY MEASURE AS IT DEMONSTRATES THE PROFIT GENERATED FROM EACH UNIT OF PRODUCTION, AND IS WIDELY USED BY THE INVESTMENT COMMUNITY.
- FUNDS FLOW FROM OPERATING ACTIVITIES PER SHARE IS CALCUALATED ON THE BASIS OF THE FUNDS FLOW FROM OPERATING ACTIVITIES DIVIDED BY THE WEIGHTED AVERAGE NUMBER OF SHARES.
- CASH FLOW FROM OPERATING ACTIVITIES PER SHARE IS CALCULATED AS CASH FLOW FROM OPERATIONS DIVIDED BY THE WEIGHTED AVERAGE NUMBER OF SHARES.

ADDITIONAL INFORMATION REGARDING ORCA EXPLORATION IS AVAILABLE UNDER THE COMPANY'S PROFILE ON SEDAR AT www.sedar.com.

NATURE OF OPERATIONS

The Company's principal operating asset is its interest in a PSA with TPDC and the Government of Tanzania in the United Republic of Tanzania. This PSA covers the exploration, development, production and marketing of certain gas from the Songo Songo Block offshore Tanzania.

The PSA defines gas from the Songo Songo field as "Protected Gas" and "Additional Gas". The "Protected Gas" is owned by TPDC and is sold under a 20-year agreement (until July 2024) to Songas ("Gas Agreement"). Songas is the owner of the infrastructure that enables the gas to be processed and delivered to Dar es Salaam, which includes a gas processing plant on Songo Songo Island.

Songas utilizes the Protected Gas as feedstock for its gas turbine electricity generators for onward sale to customers. The Company receives no revenue for the Protected Gas delivered to Songas and operates the field and gas processing plant on a 'no gain no loss' basis.

Under the PSA, the Company has the right to produce and market all gas in the Songo Songo Block in excess of the Protected Gas requirements ("Additional Gas").

TANESCO is a parastatal organization which is wholly-owned by the Government of Tanzania, with oversight by the Ministry of Energy and Minerals ("MEM"). TANESCO is responsible for the generation, transmission and distribution of electricity throughout Tanzania. Natural gas has become an integral component of TANESCO's power generation fuel mix as a more reliable source of supply over seasonal hydro power and a more cost effective alternative to liquid fuels. The Company currently supplies gas directly to TANESCO by way of the PGSA and indirectly through the supply of Protected Gas and Additional Gas to Songas which in turn generates and sells power to TANESCO. The state utility is the Company's largest customer and the gas supplied by the Company to TANESCO today fires approximately 45% of the electrical power generated in Tanzania.

In addition to gas supplied to Songas and TANESCO for the generation of power, the Company has developed and supplies an industrial gas market in the Dar es Salaam area consisting of some 38 industrial customers.

Consolidation

The companies which are 100% owned that are being consolidated are:

COMPANY	INCORPORATED
Orca Exploration Group Inc.	British Virgin Islands
Orca Exploration Italy Inc.	British Virgin Islands
Orca Exploration Italy Onshore Inc.	British Virgin Islands
PAE PanAfrican Energy Corporation	Mauritius
PanAfrican Energy Tanzania Limited ("PAET")	Jersey
Orca Exploration UK Services Limited	United Kingdom

BUSINESS RISKS

See "Business Risks" in MD&A for the year-ended 31 December 2015 for a complete discussion of business risks of the Company.

Financing

The ability of the Company to meet its financing obligations or to arrange financing in the future will if necessary depend in part upon the prevailing capital market conditions as well as the business performance of the Company. There can be no assurance that the Company would be successful in its efforts to meet its current commitments or arrange additional financing on terms satisfactory to the Company. If additional financing is raised by the issuance of shares from treasury of the Company, control of the Company may change and shareholders may suffer additional dilution.

From time to time the Company may enter into transactions to acquire assets or the shares of other companies. These transactions may be financed partially or wholly with debt, which may temporarily increase the Company's debt levels above industry standards.

Collectability of receivables

The Company evaluates the collectability of its receivables on the basis of payment history, frequency and predictability, as well as Management's assessment of the customer's willingness and ability to pay. Both Songas and the Company have been impacted by TANESCO's inability to pay.

At 31 March 2016, TANESCO owed the Company US77.2 million excluding interest (of which arrears were US$69.9 million) compared to US$69.7 million (including arrears of US$61.9 million) as at 31 December 2015. During the quarter, the Company received a total of US$3.6 million (Q4 2015: US$4.5 million) from TANESCO against sales invoices totaling US$10.9 million (Q4 2015: US$11.7 million). Current TANESCO receivables as at 31 March 2016 amounted to US$7.3 million (Q4 2015 US$7.8 million). Since the quarter end, TANESCO has paid the Company US$2.5 million, and as at the date of this report the total TANESCO receivable is US$77.3 million (of which US$69.9 million has been provided for). The amounts owed do not include interest billed to TANESCO.

Amounts collected with respect to the long-term receivable in the future will be reflected in earnings when payment is received. Notwithstanding this provision, the Company and TANESCO continue to operate in accordance with the terms of the PGSA whereby natural gas continues to be delivered by the Company and TANESCO is invoiced pursuant to the terms of the PGSA. This provision against the TANESCO net long-term receivable will not prejudice the Company's rights to payment in full or its ability to pursue collection in accordance with the terms of the agreement with TANESCO.

In December 2015, TANESCO agreed to a payment plan with the Company and TPDC to make ongoing payments for current deliveries and begin paying down arrears in March 2016 ("Payment Plan"). During Q1, TANESCO defaulted on the Payment Plan and, pursuant to the terms of the PGSA, on 25 April 2016 the Company and TPDC issued a joint notice informing TANESCO that if TANESCO failed to pay the arrears as against the Payment Plan within ten days, then the supply of gas would be suspended. In response to this notice, TANESCO, TPDC and Government of Tanzania representatives have engaged with the Company with the goal of resolving the TANESCO non-payment issues and to avoid suspension of deliveries. Based on discussions held on 17 May 2016, the Company and TPDC have agreed to continue to supply gas provided sufficient regular payments are made to cover current deliveries and discussions continue with TANESCO and Government of Tanzania officials on how to resolve the arrears. The Company has reserved the right to implement the suspension should either of the previously mentioned conditions not be met.

As at 31 March 2016, Songas owed the Company US$20.7 million (Q4 2015: US$19.0 million), whilst the Company owed Songas US$2.5 million (Q4 2015: US$2.6 million); there was no contractual right to offset these amounts. Amounts due to Songas primarily relate to pipeline tariff charges of US$0.9 million (Q4 2015: US$1.1 million), whereas the amounts due to the Company are mainly for capital expenditures of US$11.8 million (Q4 2014: US$11.2 million), sales of gas of US$1.9 million (Q4 2015: US$2.2 million) and for the operation of the gas plant of US$7.0 million (Q4 2015: US$5.6 million). The operation of the gas plant is conducted at cost and the charges are billed to Songas on a flow through basis on a "no profit, no loss" basis.

As at 31 March 2016 the net amount owed by Songas to the Company was US$18.2 million (Q4 2015: US$16.4 million). The deterioration in the outstanding balances is a consequence of the increase in the operatorship balance and the Songas share of well workover costs. The Company considers the doubtful debt provision of US$9.8 million is at an appropriate level recognizing the pending settlement of the remaining overdue operatorship charges and the Songas share of the well workover costs. Any significant amounts not agreed to will be pursued through the mechanisms provided in the agreements with Songas.

The "Tax Recoverable" figure carried on the balance sheet arises from the revenue sharing mechanism within the PSA which entitles the Company to recover from TPDC, by way of a deduction from TPDC's Profit Gas share, an amount "the adjustment factor" equal to the actual income taxes payable by the Company. Recovery, by offset against TPDC's share of revenue is dependent on payment of income taxes relating to prior period adjustment factors as they are assessed.

Access to Songas processing and transportation

Whilst the Company operates the Songo Songo gas processing plant, Songas is the owner of plant and pipeline system which transports natural gas from Songo Songo to Dar es Salaam. The Company's ability to deliver gas to its customers in Dar es Salaam is dependent upon it having access to the Songas infrastructure. Although there are agreements with Songas to allow the Company to process and transport gas, there is no assurance that these rights could not be challenged or curtailed by Songas. The inability to access Songas plant and processing facilities would materially impair the Company's ability to realise revenue from natural gas sales.

As a result of the Songo Songo gas plant re-rating that occurred in 2011 pursuant to the Re-Rating Agreement, the capacity of the Songas gas processing plant was increased to a maximum of 110 MMcfd (restricted to 102 MMcfd because of pipeline and pressure requirements). The Re-Rating Agreement expired in 2013 and no new agreement is currently in place. Without the Re-Rating Agreement, the gas plant capacity may be de-rated to 70 MMcfd (the capacity originally agreed to), which would result in a material reduction in the Company's sales volumes of Additional Gas.

The Petroleum Act, 2016

In July 2015 the Tanzania Parliament passed The Petroleum Act, 2015, which was passed into law by Presidential decree on 4 August 2015. The Act repeals earlier legislation, provides a regulatory framework over mid-stream and downstream gas activity and as well consolidates and puts in place a single, effective and comprehensive legal framework for regulating the oil and gas industry in the country. The Act also provides for the creation of an upstream regulator, the Petroleum Upstream Regulatory Authority ("PURA"). The mid and downstream petroleum as well as gas activities are proposed to be regulated by the current authority, the Energy and Water Utilities Regulatory Authority ("EWURA").

The Act also confers upon on TPDC, the status of the National Oil Company, mandated with the task of managing the country's commercial interest in the petroleum operations as well as mid and downstream natural gas activities. The Act vests TPDC with exclusive rights in the entire petroleum upstream value chain and the natural gas mid and downstream value chain. However, the exclusive rights of the National Oil Company do not extend to mid and downstream petroleum supply operations.

The Act does provide grandfathering provisions upholding the rights of the Company under the PSA as it was signed prior to passing of the Act. However, it is still unclear how the provisions of the Act will be interpreted and implemented regarding upstream and downstream activities.

Amended and Restated Gas Agreement

Terms of the original Gas Agreement were modified by the ARGA which was initialed by all parties but not signed. The ARGA provides clarification of the Protected Gas volumes and removes all terms dealing with the security of the Protected Gas and contract terms dealing with the consequences of any insufficiency are dealt with in a new Insufficiency Agreement ("IA"). The IA specifies terms under which Songas may demand cash security in order to keep it whole in the event of a Protected Gas insufficiency. Should the IA be signed, it will govern the basis for determining security. Under the provisional terms of the IA, when it is calculated that funding is required, the Company is required to fund an escrow account at a rate of US$2.00/MMbtu on all Industrial Additional Gas sales out of its and TPDC's share of revenue, and TANESCO is required to contribute the same amount on Additional Gas sales to the Power sector. The funds provide security for Songas in the event of an insufficiency of Protected Gas. The Company is actively monitoring the reservoir and, supported by the report of its independent engineers, does not anticipate that a liability will occur in this respect. As at the date of this report, the ARGA has only been initialed. Although the ARGA is unsigned, the parties have and continue to conduct themselves, in certain respects, as though the ARGA is in effect. Management does not foresee at this time a material risk with the conduct of the Company's business with an unsigned ARGA.

Additional Gas

The Company has the right under the terms of the PSA to market volumes of Additional Gas subject to satisfying the requirements to deliver Protected Gas to Songas.

There is a risk that Songas could interfere in the Company's ability to produce, transport and sell volumes of Additional Gas if the Company's obligations to Songas under the Gas Agreement are not met. In particular, Songas has the right in specific circumstances to request reasonable security on all Additional Gas sales.

With the passing of the Act TPDC was given significant rights over upstream and downstream operations in the country and is the sole aggregator of natural gas in the country. The Act recognises the rights of the Company pursuant to the PSA. Some clauses in the Act conflict with the Company's rights under the PSA to directly market Additional Gas and there is a risk that this prior right will not continue to be recognised and that the Company's ability to maximize revenue on Additional Gas sales may be impaired by the requirement to sell gas to TPDC as aggregator.

CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The preparation of the Company's unaudited condensed consolidated interim financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the period. Actual results could differ materially from these estimates. In preparing these unaudited condensed consolidated interim financial statements, the significant judgements made by the management in applying the Company's accounting policies and the key sources of estimation uncertainty were the same as those applied to the consolidated financial statements as at and for the year ended 31 December 2015. See "Critical Accounting Estimates and Judgements" in the MDA for the year ended 31 December 2015 for a complete discussion.

Collectability of receivables

Management reviews the accounts receivable aging and payment history on a weekly basis. Accounts which are in excess of 60-days in arrears are identified as potential doubtful accounts. When sustained arrears performance is exhibited over a quarter, together with an assessment by management of the customer's willingness and ability to pay, an account is deemed "doubtful" and a provision against that account is made for the reporting period based on an assessment of that amount of arrears which are unlikely to be paid in the immediate future.

TANESCO is, and has been, experiencing financial difficulties since 2011. These have been caused by a combination of dependence on high cost liquid fuel power generation following droughts in Tanzania, a government mandate to provide additional power stations and inadequate consumer tariffs to cover operational costs.

Prior to 2016 the Company had reached an understanding with TANESCO that it would only continue to supply gas if TANESCO remained reasonably current with payments for current gas deliveries. Excess payments received over and above the current balances would be applied to the arrears balance. TANESCO payments have continued to be irregular but were sufficient to cover current gas deliveries until the third quarter of 2015, since that time the level of payments received has not been sufficient to cover current gas deliveries. During the quarter, the Company received a total of US$3.6 million (Q4 2015: US$4.5 million) from TANESCO against sales totaling US$10.9 million (Q4 2015: US$11.7 million).

Management has reviewed the current position with TANESCO and feels that the current policy to reclassify all amounts receivable from TANESCO in excess of 60 days, and in arrears, as a long-term receivable is still appropriate. This decision takes into consideration the results of discussions and meetings since issuing the joint notice to suspend gas supply on 25 April 2016, the payments made by TANESCO since 31 March 2016 to cover current deliveries and the commitment of representatives of the Government of Tanzania to participate in meaningful discussions to resolve the TANESCO arrears.

Results for the three months ended 31 March 2016

SUMMARY

During the quarter ended 31 March 2016 the Company successfully completed the drilling of well SS-12. This completed all work-over and drilling activities planned under the Offshore Programme. Based on preliminary evaluation, the Company anticipates that production capabilities will increase by approximately 35 MMcfd once the SS-12 production platform is completed and the well is tied into the NNGIP infrastructure. Total capital expenditures during the quarter were US$14.0 million (Q1 2015: US$1.1 million).

The Company's gross sales revenue for the quarter increased by 1% to US$19.4 million (Q1 2015: US$19.2 million). However, the Company's operating revenue increased 47% to US$14.1 million in the first quarter of 2016 (Q1 2015: US$9.6 million). The increase is primarily a result of the capital expenditures from the recently completed Offshore Programme increasing the pool of recoverable costs which entitled the Company to a greater share of net revenue and a corresponding reduction in Profit Gas attributable to TPDC.

The Company's net loss for the quarter was US$5.7 million (Q1 2015: 1.7 million) primarily as a result of the increase in the provision on the TANESCO long-term receivable of US$8.0 million (Q1 2015: $nil). Payments from TANESCO continue to be irregular and not sufficient to cover current period gas deliveries.

The Company finished the quarter in a stable financial position with US$56.4 million of working capital (31 December 2015: US$32.5 million). This reflects the final drawdown of US$40 million on the IFC financing facility bringing total long-term debt at 31 March 2016 to US$58.4 (31 December 2015: US$18.6 million).

OPERATING VOLUMES

The total volume of Protected Gas and Additional Gas delivered and sold for the quarter ended 31 March 2016 was 7,558 MMcf (Q1 2015: 7,931 MMcf) or 83.1 MMcfd (Q1 2015: 88.1 MMcfd), net of approximately 0.3 MMcfd (Q1 2015: 0.1 MMcfd) consumed locally for fuel gas.

The Additional Gas sales volumes for the quarter year were 4,213 MMcf (Q1 2015: 4,419 MMcf) or average daily volumes of 46.3 MMcfd (Q1 2015: 49.1 MMcfd). This represents a decrease in average daily volumes of 5% over the prior year quarter.

The decrease in Additional Gas volumes year over year is primarily the result of unscheduled maintenance at the Ubungo power generation plants during March. This directly impacts the level of Additional Gas volumes as the Songas Additional Gas volumes are 19.5% of the total Ubungo plants consumption.

The Company's sales volumes were split between the Industrial and Power sectors as detailed in the table below:

	THREE MONTHS ENDED 31 MARCH	
	2016	2015
Gross sales volume *(MMcf)*		
Industrial sector	**972**	925
Power sector	**3,241**	3,494
Total volumes	**4,213**	4,419
Gross average daily sales volume *(MMcfd)*		
Industrial sector	**10.7**	10.3
Power sector	**35.6**	38.8
Total daily sales volume	**46.3**	49.1

Industrial sector

Industrial sales volume increased by 5% to 972 MMcf (10.7 MMcfd) from 925 MMcf (10.3 MMcfd) in the prior year quarter. The increase is primarily the result of increased consumptions by an edible oil company and a cement company during the first two months of 2016.

Power sector

Power sector sales volumes decreased by 7% to 3,241 MMcf (35.6 MMcfd), compared to 3,494 MMcf (38.8 MMcfd) in the prior year quarter. The decrease in production is primarily a result of maintenance shut downs at Songas power generation plants.

SONGO SONGO DELIVERABILITY

As at 31 March 2016, the Company had a field productive capacity of approximately 155 MMcfd, with the expansion of production volumes limited to 102 MMcfd by the available Songas infrastructure. The increase in field productive capacity was due to successful workovers on wells SS-5, SS-7 and SS-9 completed during the second half of 2015. Well SS-3 is currently suspended; it is the Company's intention to undertake workovers on SS-3 and SS-4 wells in the future. During the quarter, the Company completed drilling well SS-12 adding a further 35 MMcfd to the field productive capacity. The SS-12 well cannot be produced until the construction of a platform and flowline to tie the well into the NNGIP infrastructure.

COMMODITY PRICES

The commodity prices achieved in the different sectors during the quarter are shown in the table below:

	THREE MONTHS ENDED 31 MARCH	
US$/mcf	**2016**	2015
Average sales price		
Industrial sector [(1)]	**8.15**	7.54
Power sector	**3.55**	3.49
Weighted average price	**4.61**	4.34

Industrial sector

The average gas price achieved during the quarter was US$8.15/mcf an increase of 8% from US$7.54/mcf in Q1 2015. This is a consequence of several factors: (i) the impact of the annual contractual increase in the floor price, which protects the Company from further decline in the world energy markets: (ii) a change in the sales mix with an increase in the level of sales to the customers at the lower discount rate and (iii) a step change in the gas prices to a cement company with effect from January 2016.

Power sector

The average gas price achieved during the quarter was US$3.55/mcf an increase of 2% from US$3.49/mcf in Q1 2015. The increase is a result of the annual indexation rise of 2% each July under contractual arrangements.

OPERATING REVENUE

Under the terms of the PSA, the Company is responsible for invoicing, collecting and allocating the revenue from Additional Gas sales.

The Company is able to recover all costs incurred on the exploration, development and operations of the project up to a maximum of 75% of the Net Revenue ("Cost Gas") prior to the distribution of Profit Gas. Any costs not recovered in any period are carried forward for recovery out of future revenues. Once the Cost Gas has been recovered, TPDC is able to recover any pre-approved marketing costs.

The Additional Gas sales volumes for the quarter and Q1 2015 were below 50 MMcfd and, as a consequence, the Company was only entitled to a 40% share of Profit Gas revenue for the year as opposed to a 55% share (net of Cost Gas recoveries from revenue). See "Principal Terms of the Tanzanian PSA and Related Agreements."

The Company was allocated a total of 75% of Net Revenue in the quarter (Q1 2015: 33%): The increase in the allocation of net revenue is a consequence of the Company being at maximum costs recovery following the Offshore Programme which was completed in the current quarter.

	THREE MONTHS ENDED 31 MARCH	
US$'000	**2016**	2015
Gross sales revenue	**19,437**	19,178
Gross tariff for processing plant and pipeline infrastructure	**(2,856)**	(3,161)
Gross revenue after tariff ("net revenues")	**16,581**	16,017
Analysed as to:		
Company Cost Gas	**12,436**	5,332
Company Profit Gas	**1,658**	4,274
Company operating revenue	**14,094**	9,606
TPDC share of revenue	**2,487**	6,411
	16,581	16,017

The Company's total revenues for the quarter ended 31 March 2016 amounted to US$15.8 million, after adjusting the Company's operating revenues of US$14.1 million by:

i) adding US$2 million for income tax for the quarter. The Company is liable for income tax in Tanzania, but the income tax is recoverable out of TPDC's Profit Gas when the tax is payable. To account for this, revenue is adjusted to include the current income tax charge grossed up at 30%; and,

ii) subtracting US$0.3 million for deferred Additional Profits Tax charged in the quarter, this tax is considered a royalty and is presented as a reduction in revenue.

Revenue presented on the Condensed Consolidated Interim Financial Statements

Statement of Comprehensive Loss may be reconciled to the operating revenue as follows:

	THREE MONTHS ENDED 31 MARCH	
US$'000	**2016**	2015
Industrial sector	**7,925**	6,971
Power sector	**11,512**	12,207
Gross sales revenue	**19,437**	19,178
Processing and transportation tariff	**(2,856)**	(3,161)
Net revenue	**16,581**	16,017
TPDC share of revenue	**(2,487)**	(6,411)
Company operating revenue	**14,094**	9,606
Additional Profits Tax charge	**(308)**	(885)
Current income tax adjustment	**2,024**	999
Revenue	**15,810**	9,720

The Company's gross sales revenue increased 1% to US$19.4 million (Q1 2015: US$19.2 million) resulting from a combination of a 6% increase in the weighted average sales price and a 5% reduction in sales volumes.

The Company's operating revenue increased 47% to US$14.1 million in the first quarter of 2016 compared with US$9.6 million in Q1 2015. The increase is primarily due to the capital expenditures related to the recently completed Offshore Programme. The capital development program commenced in the third quarter of 2015 and was completed in the first quarter of 2016. The expenditures substantially increased the pool of recoverable costs. This entitled the Company to 75% of net revenue as Cost Gas in the quarter and the corresponding reduction in Profit Gas also reduced the Profit Gas attributable to TPDC by 61%.

A reduction of US$0.6 million or 65% in the APT charge for the year is a result of the fall in the effective rate from 20.7% to 18.6% compounded by a fall of 61% in the Company's share of Profit Gas to US$1.7 million (Q1 2015: US$4.3 million) on which it is based. The drop in Profit Gas is a direct result of capital expenditure increasing Cost Gas.

PROCESSING AND TRANSPORTATION TARIFF

The Company effectively pays a tariff of US$0.30/mcf for sales between 70 MMcfd and 90 MMcfd and US$0.40/mcf for volumes above 90 MMcfd in addition to the regulated tariff of US$0.59/mcf payable to Songas. The charge for the quarter was US$2.9 million (Q1 2015: US$3.2 million). The reduction in the tariff for the quarter is the result of lower volumes during the respective periods.

PRODUCTION AND DISTRIBUTION EXPENSES

Well maintenance costs are allocated between Protected Gas and Additional Gas in proportion to their respective sales during the period. The total cost of maintenance for the quarter was US$0.2 million (Q1 2015: US$0.2 million). Amounts allocated for Additional Gas for the quarter were US$0.1 million (Q1 2015: US$0.1 million).

Other field and operating costs include an apportionment of the annual PSA licence costs, regulatory fees, insurance, some costs associated with the evaluation of the reserves, and the cost of personnel which are not recoverable from Songas.

Distribution costs represent the direct cost of maintaining the ring main distribution pipeline and pressure reduction station (security, insurance and personnel). Ring main distribution costs were US$0.7 million for the quarter (Q1 2015: US$0.5 million). The production and distribution costs are detailed in the table below:

	THREE MONTHS ENDED 31 MARCH	
US$'000	**2016**	2015
Share of well maintenance	**128**	100
Other field and operating costs	**308**	763
	436	863
Ringmain distribution costs	**684**	493
Production and distribution expenses	**1,120**	1,356

OPERATING NETBACKS

The netback per mcf before general and administrative costs, overhead, tax and APT is detailed in the table below:

US$/mcf	THREE MONTHS ENDED 31 MARCH 2016	2015
Gas price – Industrial	**8.15**	7.54
Gas price – Power	**3.55**	3.49
Weighted average price for gas	**4.61**	4.34
Tariff	**(0.68)**	(0.72)
TPDC share of revenue	**(0.59)**	(1.45)
Net selling price	**3.34**	2.17
Well maintenance and other operating costs	**(0.10)**	(0.20)
Ring main distribution costs	**(0.16)**	(0.11)
Operating netback	**3.08**	1.86

The operating netback increased by 66% from US$1.86/mcf in Q1 2015 to US$3.08/mcf in Q1 2016. The primary reason for the increase was the 61% decrease in TPDC share of revenue as a consequence of an increase in the Cost Gas recovered, mainly as a result of the workover and drilling programme. In addition, there was a 6% increase in the weighted average sales from US$4.34/mcf in Q1 2015 to US$4.61/mcf in Q1 2016. The overall production and distribution cost averaged US$0.26/mcf compared to US$0.31 in Q1 2015. The decrease was primarily a result of the reduced level of required maintenance activities as a result of the successful workovers completed in Q4 2015 as part of the Offshore Programme.

GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses are detailed in the table below:

US$'000	THREE MONTHS ENDED 31 MARCH 2016	2015
Employee and related costs	**1,949**	1,484
Stock based compensation	**2,858**	1,129
Office costs	**692**	723
Marketing and business development costs	**82**	11
Reporting, regulatory and corporate	**465**	750
General and administrative expenses	**6,046**	4,097

General and administrative expenses include the costs of running the natural gas distribution business in Tanzania which is recoverable as Cost Gas and is relatively fixed in nature. Excluding stock based compensation, general and administrative expenses averaged US$1.06 million (Q1 2015: US$0.99 million) per month during the quarter.

STOCK-BASED COMPENSATION

The breakdown of the costs incurred in relation to stock based compensation is detailed in the table below:

	THREE MONTHS ENDED 31 MARCH	
US$'000	**2016**	2015
Stock appreciation rights ("SARs")	**2,097**	763
Restricted stock units ("RSUs")	**761**	366
Stock-based compensation	**2,858**	1,129

No stock options were outstanding as at 31 March 2016 or 31 December 2015. No options were granted during the quarter (Q1 2015: nil).

As at 31 March 2016 a total of 3,040,000 SARs were outstanding compared to 3,100,000 as at 31 December 2015 with a total of 60,000 SARS with an exercise price of CDN$2.30 having been exercised during the quarter. A total of 239,361 RSUs were granted during the quarter and remain outstanding at 31 March 2016 (Q4 2015: nil). The newly granted RSUs vested on the date of grant have an exercise price of CDN$ nil and have a five year term.

As SARs and RSUs are settled in cash, they are re-valued at each reporting date using the Black-Scholes option pricing model with the resulting liability being recognised in trade and other payables. In the valuation of stock appreciation rights and restricted stock units at the reporting date, the following assumptions have been made: a risk free rate of interest of 1.5%; stock volatility of 51.4% to 54.1; 0% dividend yield; 5% forfeiture; and a closing price of CDN$4.14 per Class B share.

As at 31 March 2016, a total accrued liability of US$4.4 million (Q4 2015: US$1.6 million) has been recognised in relation to SARS and RSUs. The Company recognised a charge of US$2.9 million (Q1 2015: US$1.1 million) for the quarter.

NET FINANCE EXPENSE

The movement in net finance expense is detailed in the table below:

	THREE MONTHS ENDED 31 MARCH	
US$'000	**2016**	2015
Finance income	**49**	4
Interest expense	**(1,005)**	–
Net foreign exchange loss	**(28)**	(1,831)
Provision for doubtful accounts	**(7,986)**	–
Finance expense	**(9,019)**	(1,831)
Net finance expense	**(8,970)**	(1,827)

During the quarter, the Company billed TANESCO US$0.9 million (Q1 2015: US$0.7 million) of interest for late payments. The interest income is not recorded in the financial statements because it does not meet the revenue recognition criteria with respect to assurance of collectability. The Company is pursuing collection and amounts will be recognised in earnings when collected. The US$ 8.0 million (Q1 2015: US$ nil) current provision for doubtful accounts relates to overdue TANESCO receivables.

The total amount of interest paid in the quarter was US$0.2 million (Q1 2015: US$ nil). The interest relates to the long term loan with the IFC and is payable quarterly in arrears.

The foreign exchange loss reflects the impact of movements in the value of the Tanzanian shilling against the US dollar during the period on outstanding customer/supplier balances and bank accounts in Tanzanian shillings.

TANESCO

At 31 March 2016, TANESCO owed the Company US77.2 million excluding interest (of which arrears were US$69.9 million) compared to US$69.7 million (including arrears of US$61.9 million) as at 31 December 2015. During the quarter, the Company received a total of US$3.6 million (Q4 2015: US$4.5 million) from TANESCO against sales invoices totaling US$10.9 million (Q4 2015: US$11.7 million). Current TANESCO receivables as at 31 March 2016 amounted to US$7.3 million (Q4 2015 US$7.8 million). Since the quarter end, TANESCO has paid the Company US$2.5 million, and as at the date of this report the total TANESCO receivable is US$77.3 million (of which US$69.9 million has been provided for). The amounts owed do not include interest billed to TANESCO.

Management concluded that the continued recognition of TANESCO revenue is appropriate. In arriving at this conclusion management has taken account of:

- Recent discussions with the World Bank, the IMF and IFC during which the Company found strong support for funding to be directed at TANESCO, supported by a recent announcement from the IMF stating the need to address TANESCO debt.
- TANESCO, according to the World Bank, is now making a small profit. With the seasonal increase in available hydro power and new gas to power facilities coming on line later this year, the need for expensive liquid fuel will significantly reduce.
- Most recently, TPDC has co-signed with the Company a commitment from TANESCO establishing a payment plan going forward. This plan was agreed between the Company and TANESCO at the beginning of December 2015, and countersigned by TPDC in January 2016. TANESCO has fallen behind the agreed schedule of payments, but with TPDC signing the agreement and supporting the Company, the Company has a much stronger legal position to pursue collection of arrears.
- The joint notice to suspend gas supplies issued on 25 April 2016 took into account the payment commitments made by TANESCO in December 2015 and the fact that the commitments were not being met. Based on discussions held on 17 May 2016, the Company and TPDC have agreed to continue to supply gas provided sufficient regular payments are made to cover current deliveries and discussions continue with TANESCO and Government of Tanzania representatives on how to resolve the arrears.

TAXATION

Income Tax

Under the terms of the PSA with TPDC and the Government of Tanzania, the Company is liable for income tax in Tanzania at the corporate tax rate of 30%. However, the PSA provides a mechanism by which income tax payable is recovered from TPDC by reducing TPDC's share of Profit Gas and increasing the allocation to the Company. This is reflected in the accounts by increasing the Company's share of revenue by an amount equivalent to income taxes payable.

As at 31 March 2016, there were temporary differences between the carrying value of the assets and liabilities for financial reporting purposes and the amounts used for taxation purposes under the Income Tax Act 2004. Applying the 30% Tanzanian tax rate, the Company has recognised a deferred tax liability of US$10.2 million (Q4 2015: US$9.3 million). During the quarter there was a deferred tax charge of US$0.9 million compared with a recovery of US$0.7 million in Q1 2015. The deferred tax has no impact on cash flow until it becomes a current income tax, at which point the tax is paid and recovered from TPDC's share of Profit Gas.

Additional Profits Tax

Under the terms of the PSA, in the event that all costs have been recovered with an annual return of 25% plus the percentage change in the United States Industrial Goods Producer Price Index ("PPI"), an Additional Profits Tax is payable.

The timing and the effective rate of APT depends on the realised value of Profit Gas which in turns depends of the level of expenditure. The Company provides for APT by forecasting annually the total APT payable as a proportion of the forecast Profit Gas over the term of the PSA. The forecast takes into account the timing of future development capital spending.

The Company provides for deferred APT by forecasting the total APT payable as a proportion of the forecast Profit Gas over the term of the PSA. The effective APT rate of 18.6% (Q1 2015: 20.7%) has been applied to Profit Gas of US$1.7 million (Q1 2015: US$4.3 million). Accordingly, US$0.3 million (Q1 2015: US$0.9 million) has been netted off revenue for the three months ended 31 March 2016.

DEPLETION AND DEPRECIATION

Natural gas properties are depleted using the unit of production method based on the production for the period as a percentage of the total future production from the Songo Songo proven reserves. As at 31 December 2015 the proven reserves estimated to have been produced over the term of the PSA licence, as evaluated by the independent reservoir engineers, McDaniel & Associates Consultants Ltd., were 368 Bcf (2014: 450 Bcf). A depletion expense of US$2.4 million has been recorded for the quarter (Q1 2015: US$3.2 million); the reduction compared to Q1 2015 is the result of 23% decrease in the average depletion rate to US$0.56/mcf (Q1 2015: US$0.73/mcf). The decrease in the depletion rate is the consequence of the successful completion of the Offshore Programme at a lower level of expenditure than planned which in turn reduced expected future development costs from what had been originally forecast at the end of 2014.

Non-natural gas properties are depreciated as follows:

Leasehold improvements:	Over remaining life of the lease
Computer equipment:	3 years
Vehicles:	3 years
Fixtures and fittings:	3 years

CARRYING AMOUNT OF ASSETS

Capitalised costs are periodically assessed to determine whether it is likely that such costs will be recovered in the future. To the extent that these capitalised costs are unlikely to be recovered in the future, they are impaired and recorded in earnings.

FUNDS FLOW FROM OPERATING ACTIVITIES

Funds flow from operating activities before working capital changes was US$9.9 million for the quarter (Q1 2015: US$3.7 million) and is detailed in the table below:

	THREE MONTHS ENDED 31 MARCH	
US$'000	**2016**	2015
Funds flow from operating activities	**9,853**	3,712
Working capital adjustments (1)	**(11,007)**	3,663
Net cash flows (used in) from operating activities	**(1,154)**	7,375
Net cash used in investing activities	**(19,062)**	(1,139)
Net cash from financing activities	**38,746**	–
Increase in cash	**18,530**	6,236
Effect of change in foreign exchange on cash	**(27)**	(1,655)
Net increase in cash	**18,503**	4,581

(1) See Condensed Consolidated Interim Statement of Cash Flows

The increase in funds flow from operating activities before working capital changes is primarily the consequence of the 47% increase in the Company operating revenue to US$14.1 million in the first quarter of 2016 compared with US$9.6 million in Q1 2015. The increase is primarily due to the capital expenditure related to the Offshore Programme. The Offshore Programme commenced in the third quarter of 2015 and was completed in the first quarter of 2016. The expenditures substantially increased the pool of recoverable costs. This entitled the Company to 75% of net revenue as Cost Gas in the quarter and the corresponding reduction in Profit Gas also reduced the Profit Gas attributable to TPDC by 61%. The use of cash flow from operating activities of US$1.2 million (Q1 2015: US$7.4 million positive net cash flow) was a result of the increase in trade and other receivables, primarily related to TANESCO.

CAPITAL EXPENDITURES

During the quarter the Company incurred US$14.0 million (Q1 2015: US$1.1 million) in capital expenditures relating to the drilling of well SS-12, improvement of Songo Songo infrastructure, and purchase of other equipment. The 2016 capital expenditures are net of recharges of US$0.5 million to Songas for its share of costs on wells SS-5 and SS-9 following the completion of the Offshore Programme.

	THREE MONTHS ENDED 31 MARCH	
US$'000	**2016**	2015
Geological and geophysical and well drilling	**13,639**	984
Pipelines and infrastructure	**356**	155
Other equipment	**2**	–
	13,997	1,139

WORKING CAPITAL

Working capital as at 31 March 2016 was US$56.3 million (31 December 2015: US$32.5 million) and is detailed in the table below:

	AS AT			
US$'000		**31 MARCH 2016**		31 DECEMBER 2015
Cash		**72,300**		53,797
Trade and other receivables		**25,799**		25,391
TANESCO	7,313		7,831	
Songas	1,933		2,178	
Industrial customers	6,104		6,894	
Songas gas plant operations	6,994		5,631	
Songas well workover programme	11,745		11,209	
Other receivables	1,666		1,604	
Provision for doubtful accounts	(9,956)		(9,956)	
Tax recoverable		**4,656**		4,519
Prepayments		**983**		1,118
		103,738		84,825
Trade and other payables		**44,546**		49,531
TPDC	28,523		28,208	
Songas	939		1,071	
Other trade payables	5,786		11,234	
Deferred income	667		667	
Accrued liabilities	8,631		8,351	
Tax payable		**2,852**		2,773
Working capital (1)		**56,340**		32,521

Notes:

(1) Working capital as at 31 March 2016 includes a TANESCO receivable (excluding interest) of US$7.3 million (31 December 2015: US$7.8 million). Management has recorded a provision for doubtful accounts against the long-term receivables in excess of 60 days totaling US$69.9 million (31 December 2015: US$61.9 million). The total of long and short-term TANESCO receivables, including interest, as at 31 March 2016 was US$85.2 million. The financial statements do not recognise the interest receivable from TANESCO as it does not meet IAS 18 income recognition criteria. The Company is however actively pursuing the collection of all the receivables and the interest that has been charged to TANESCO.

Working capital as at 31 March 2016 increased by 73% over 31 December 2015, primarily as a result of having drawn down the balance of the loan from the IFC and the reclassification of a further US$8.0 million of TANESCO receivables as long-term. Other significant points are:

- There are no restrictions on the movement of cash from Mauritius or Tanzania, and currently the majority of cash is outside of Tanzania. As at the date of this report, approximately 80% of the Company's cash was held outside of Tanzania.
- Since the quarter end the Company has received US$2.5 million from TANESCO and US$4.2 million from Songas.
- Of the US$6.1 million relating to other trade debtors US$4.7 million had been received as at the date of this report.

The balance of US$28.2 million payable to TPDC represents the remaining balance of its share of revenue as at 31 March 2016.

LONG TERM LOAN

On 29 October 2015, the Company entered into an agreement with the IFC, a member of the World Bank Group, to provide financing of up to US$60 million for the Company's operating subsidiary, PAET.

The term of the Loan is 10-years, with no required repayment of principal for the first seven years, followed by a three-year amortization period. The Company may voluntarily prepay all or part of the Loan but must simultaneously pay any accrued base interest costs related to the principal amount being prepaid. If any portion of the Loan is prepaid prior to the fourth anniversary of the first drawdown, the Company would be required to pay the accrued base interest as if the prepaid portion of the Loan had remained outstanding for the full four years. The Loan is an unsecured subordinated obligation of PAET and is guaranteed by the Company to a maximum of US$30 million. The guarantee may only be called upon by IFC at maturity in 2025 and, subject to IFC and receipt of all required regulatory approvals, the Company may issue shares in fulfillment of all or part of the guarantee obligation in 2025.

Base interest on the Loan is payable quarterly at 10% per annum on a 'pay-if-you-can-basis' using a formula to calculate the net cash available for such payments as at any given interest payment date. In addition, an annual variable participatory interest equating to 7% of the cash flow of PAET net of capital expenditures is payable in respect of any given year, commencing with 2016. Such participatory interest survives the repayment and/or maturity of the Loan until 15 October 2026. No provision has been made for the three months ended 31 March 2016 as the projection of current cash flow less capital expenditures for 2016 is a negative amount. Dividends and distributions from PAET to the Company are restricted at any time that amounts of unpaid interest, principal or participating interest are outstanding.

The Company has drawn the US$60 million Loan facility in full, with an initial drawdown of US$20 million on 14 December 2015 followed by an additional draw down of US$40 million on 9 February 2016. The Offshore Programme was completed on 11 February 2016.

SHAREHOLDERS' EQUITY AND OUTSTANDING SHARE DATA

There were 34,856,432 shares outstanding as at 31 March 2016 as detailed in the table below:

	AS AT	
Number of shares ('000)	**31 MARCH 2016**	31 DECEMBER 2015
Shares outstanding		
Class A shares	**1,751**	1,751
Class B shares	**33,106**	33,106
Class A and Class B shares outstanding	**34,857**	34,857
Convertible securities		
Options	**–**	–
Fully diluted Class A and Class B shares	**34,857**	34,857
Weighted average		
Class A and Class B shares	**34,857**	34,887
Convertible securities		
Options	**–**	–
Weighted average diluted Class A and Class B shares	**34,857**	34,887

As at the date of this report, there were a total of 1,750,517 Class A common voting shares ("Class A shares") and 33,105,915 Class B subordinated voting shares ("Class B shares") outstanding.

RELATED PARTY TRANSACTIONS

One of the non-executive Directors is a partner at a law firm that provides legal advice to the Company and its subsidiaries. During the quarter, the Company incurred US$0.05 million (Q1 2015: US$0.05 million) to this firm for services provided. The transactions with this related party were made at the exchange amount.

One Officer, acting as an Executive Vice-President, provided services to the Company through a consulting agreement with a personnel services company. During the quarter, the Company incurred US$0.01 million (Q1 2015: US$0.1 million) to this firm for services provided.

As at 31 March 2016 the Company has a total of US$0.05 million (Q1 2015: US$ nil) recorded in trade and other payables in relation to the related parties.

CONTRACTUAL OBLIGATIONS AND COMMITTED CAPITAL INVESTMENT

Protected Gas

Under the terms of the original Gas Agreement for the Songo Songo project ("Gas Agreement"), in the event that there is a shortfall/insufficiency in Protected Gas as a consequence of the sale of Additional Gas, the Company is liable to pay the difference between the price of Protected Gas (US$0.55/MMbtu escalated) and the price of an alternative feedstock multiplied by the volumes of Protected Gas up to a maximum of the volume of Additional Gas sold (148.3 Bcf as at 31 March 2016). The Company did not have a shortfall during the reporting period and does not anticipate a shortfall arising during the term of the Protected Gas delivery obligation to July 2024.

Re-Rating Agreement

In 2011, the Company signed a re-rating agreement with TANESCO and Songas (the "Re-Rating Agreement") to increase the gas processing capacity to a maximum of 110 MMcfd (the pipeline and pressure requirements at the Ubungo power plant restrict the infrastructure capacity to a maximum of 102 MMcfd). Under the terms of the Re-Rating Agreement, the Company effectively pays an additional tariff of US$0.30/mcf for sales between 70 MMcfd and 90 MMcfd and US$0.40/mcf for volumes above 90 MMcfd in addition to the tariff of US$0.59/ mcf payable to Songas as set by the energy regulator, EWURA. The Re-Rating agreement expired in 2013. Since 2013 production has continued within the higher rated limit and, given the Government's interest in pursuing further development and increasing gas production, the Company expects this to continue. However, there are no assurances that this will occur.

Under the terms of this agreement, the Company agreed to indemnify Songas for damage to its facilities caused by the re-rating, up to a maximum of US$15 million, but only to the extent that this was not already covered by indemnities from TANESCO's or Songas' insurance policies.

Capital Commitments

Italy

The Company has an agreement to farm in on the Central Adriatic B.R268.RG Permit offshore Italy. The farm-in commits the Company to fund 30% of the Elsa-2 appraisal well up to a maximum of US$11.5 million to earn a 15% working interest in the permit. Thereafter, the Company will fund all future costs relating to the well and the permit in proportion to its participating interest. The Company has also agreed to pay fifteen per cent (15%) of the back costs in relation to the well up to a maximum of US$0.5 million. Changes in Italian environmental legislation in late 2015 have resulted in the development of this permit being postponed indefinitely. As at the date of this report, the Company has no further capital commitments in Italy.

Tanzania

There are no contractual commitments for exploration or development drilling or other field development either in the PSA or otherwise agreed which would give rise to significant capital expenditure at Songo Songo. Any significant additional capital expenditure in Tanzania is discretionary.

Given the completion of the Offshore component of Phase I of the Development Programme in February 2016, which has restored field deliverability and provides sufficient natural gas production to fill the Songas plant and pipeline to capacity for the greater portion of the remaining life of the production licence, the Company does not expect to commit to further significant capital expenditures until: (i) agreeing commercial terms with TPDC for the supply of gas to the NNGIP regarding the sale of incremental gas volumes from Songo Songo; and/or (ii) TANESCO arrears have been substantially reduced, guaranteed or other arrangements for payment made which are satisfactory to the Company; and/or (iii) the establishment of payment guarantees with the World Bank or other multi-lateral lending agencies to secure future receipts under any new sales contracts with Government entities.

When conditions are deemed appropriate and there is justification to further improve the reliability/capacity of field deliverability, the Company may contemplate undertaking the remaining part or all of the Phase I Development Programme. The additional costs are estimated to be approximately US$30 million. There is no assurance that financing will be available and on acceptable commercial terms to complete Phase I.

CONTINGENCIES

Petroleum Act, 2015

During the third quarter of 2015, The Petroleum Act, 2015 was passed into law. The Act repeals earlier legislation, provides a regulatory framework over upstream, mid-stream and downstream gas activity, and consolidates and puts in place a comprehensive legal framework for regulating the oil and gas industry in the country. The Act also provides for the creation of an upstream regulator, the Petroleum Upstream Regulatory (PURA). The mid and downstream oil and gas activities are proposed to be regulated by the current authority, the Energy and Water Utilities Regulatory Authority (EWURA). The bill also confers upon on TPDC, the status of the National Oil Company, mandated with the task of managing the country's commercial interest in petroleum operations as well as mid and downstream natural gas activities. The bill vests TPDC with exclusive rights in the entire petroleum upstream value chain and the natural gas mid and downstream value chain. However, the exclusive rights of TPDC do not extend to mid and downstream petroleum supply operations. The Company is uncertain regarding the potential impact on its business in Tanzania. The Act does provide grandfathering provisions upholding the rights of the Company under their PSA as it was signed prior to passing of the Act. However, it is still unclear how the provisions of the Act will be interpreted and implemented regarding upstream and downstream activities.

Cost recovery

TPDC conducted an audit of the historic Cost Pool and in 2011 disputed approximately US$34 million of costs that had been recovered from the Cost Pool from 2002 through to 2009. In 2014 TPDC and the Company agreed to remove approximately US$1.0 million from the Cost Pool and TPDC agreed that US$9.4 million was no longer in dispute. There have been no further developments during 2015 or the first quarter of 2016. Under the dispute mechanism outlined in the PSA, TPDC are to appoint an independent specialist to assist the parties in reaching agreement on costs that are still subject to dispute. At the time of writing this report no such specialist has been appointed. If the matter is not resolved to the Company's satisfaction, the Company intends to proceed to arbitration via the International Centre for Settlement of Investment Disputes ("ICSID") pursuant to the terms of the PSA.

Taxation

		Tax dispute	**Disputed amount US$' million**		
Area	**Period**	**Reason for dispute**	**Principal**	**Interest**	**Total**
PAYE	2008-10	Pay-As-You-Earn ("PAYE") withholding tax on taxable income of employees on grossed up equivalent of staff salaries, which are contractually stated as net.	0.3	-	0.3(1)
WHT	2005-10	WHT on services by non-resident persons performed outside of Tanzania.	1.1	0.7	1.8(2)
Income Tax	2008-13	Deductibility of capital expenditures and expenses (2009), additional income tax (2008, 2010, 2011), and foreign exchange rate application (2013).	5.2	1.3	6.5(3)
VAT	2008-10	Output VAT on imported services and SSI Operatorship services.	2.7	2.9	5.6(4)
			9.3	4.9	14.2

(1) During 2015, PAET appealed the Tax Revenue Appeals Board ("TRAB") ruling that PAET is liable to pay PAYE on grossed up equivalent of staff salaries. PAET is awaiting appeal date to be set up with the Tax Revenue Appeals Tribunal ("TRAT");

(2) 2005-2009 (US$1.7 million): During 2015, TRAT ruled in favor of PAET. TRA filed a notice of appeal with the Court of Appeal and subsequent to the end of Q1 2016, the Court of Appeal ruled in favor of PAET.

2010 (US$0.1 million): TRAB was awaiting the ruling on the (2005-2009) case before making a decision on this dispute. Given the favorable ruling by the Court of Appeal, the Company expects a favorable decision.

(3) (a) 2009 (US$1.8 million): During the year, TRAB has ruled against PAET with respect to the deductibility of capital expenditures and expenses. PAET appealed to TRAT and is awaiting hearing date to be scheduled;

(b) 2008, 2010-2011 (US$4.5 million): During the year, PAET filed objections against TRA assessments with respect to additional tax and is awaiting a response;

(c) 2013 (US$ 0.2 million): During the year, PAET filed objections to TRA assessment with respect to foreign exchange rate application and is awaiting a response.

(4) In 2014, PAET filed an objection to TRA's claims and is awaiting a response.

Management, with the advice from its legal counsel, has reviewed the Company's position on the above objections and appeals and has concluded that no provision is required with regard to the above matters.

NEW ACCOUNTING POLICIES

On May 28 2014, the IASB issued IFRS 15, "Revenue from Contracts with Customers," which replaces IAS 18 "Revenue," IAS 11 "Construction Contracts," and related interpretations. The new standard is effective for annual periods beginning on or after January 1, 2017, with early adoption permitted. The Company intends to adopt IFRS 15 on the finalized adoption date and is currently evaluating the impact of adopting the standard on its consolidated financial statements.

On July 24, 2014, the IASB issued the complete IFRS 9, "Financial Instruments" to replace IAS 39, "Financial Instruments: Recognition and Measurement". IFRS 9 is effective for years beginning on or after January 1, 2018 and must be applied retrospectively with some exemptions. Early adoption is permitted if IFRS 9 is adopted in its entirety at the beginning of a fiscal period. The Company is currently evaluating the impact of adopting IFRS 9 on its consolidated financial statements.

On January 13, 2016, the IASB issued IFRS 16, "Leases", which replaces IAS 17 "Leases". The new standard introduces a single recognition and measurement model for leases, which would require the recognition of assets and liabilities for most leases with a term of more than twelve months. The new standard is effective for annual periods beginning on or after January 1, 2019. Early adoption is permitted for entities that apply IFRS 15 "Revenue from Contracts with Customers" at or before the initial adoption date of January 1, 2018. The Corporation intends to adopt IFRS 16 in its financial statements for the annual period beginning on January 1, 2019. The extent of the impact of the adoption of the standard has not yet been determined.

Financial instrument classification and measurement

The Company classifies the fair value of financial instruments according to the following hierarchy based on the amount of observable inputs used to value the instrument:

Level 1 – Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions occur in sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2 – Pricing inputs are other than quoted prices in active markets included in Level 1. Prices in Level 2 are either directly or indirectly observable as of the reporting date. Level 2 valuations are based on inputs, including expected interest rate, share prices, and volatility factors, which can be substantially observed or corroborated in the marketplace.

Level 3 – Valuation in this level are those with inputs for the asset or liabilities that are not based on observable market data.

SUMMARY QUARTERLY RESULTS OUTSTANDING

The following is a summary of the results for the Company for the last eight quarters:

	2016	2015				2014		
Figures in US$'000 except where otherwise stated	Q1	Q4	Q3	Q2	Q1	Q4	Q3	Q2
Financials						restated	restated	restated
Revenue	**15,810**	15,872	15,943	12,553	9,720	9,645	14,631	18,854
Net (loss) income	**(5,638)**	(6,468)	6,112	3,566	(1,677)	(46,381)	4	6,137
Earnings (loss) per share - basic and diluted *(US$)*	**(0.16)**	(0.19)	0.18	(1.30)	(0.05)	(1.32)	–	0.17
Funds flow from operating activities	**9,853**	8,508	9,462	4,889	3,712	8,733	6,641	11,651
Funds flow per share - basic and diluted *(US$)*	**0.28**	0.24	0.27	0.14	0.11	0.25	0.19	0.33
Cash flows from (used in) operating activities	**(1,154)**	5,450	(2,693)	(2,844)	7,375	(2,235)	24,077	7,255
Cash flows per share - basic and diluted *(US$)*	**(0.03)**	0.16	(0.09)	(0.08)	0.21	(0.06)	0.69	0.21
Operating netback *(US$/mcf)*	**3.08**	3.03	2.65	2.68	1.86	1.69	2.12	2.92
Working capital	**56,340**	32,521	39,660	38,067	34,870	34,148	42,001	30,399
Long-term loan	**58,350**	18,599	–	–	–	–	–	–
Shareholders' equity	**72,482**	78,154	84,476	78,480	74,944	76,635	123,004	123,019
Capital expenditures								
Geological and geophysical and well drilling	**13,639**	23,099	7,578	4,135	984	522	273	9
Pipeline and infrastructure	**356**	1,382	547	275	155	193	12	(270)
Other equipment	**2**	59	150	47	–	3	39	48
Operating								
Additional Gas sold – industrial *(MMcf)*	**972**	1,089	1,137	1,015	925	1,084	1,304	1,046
Additional Gas sold – power *(MMcf)*	**3,241**	3,483	3,127	3,041	3,494	3,377	3,935	3,503
Average price per mcf – industrial *(US$)*	**8.15**	7.62	7.67	7.45	7.54	8.24	8.85	9.27
Average price per mcf – power *(US$)*	**3.55**	3.56	3.62	3.47	3.49	3.49	3.6	3.65

PRIOR EIGHT QUARTERS

The Company's revenue for the last two years has fluctuated between quarters due to several factors including seasonal issues such as the availability of hydro power, scheduled and unscheduled maintenance by customers resulting in reduced demand, declining well production capacity, a drop in world HFO prices and increased competition for supply of gas within Tanzania.

The drop in sales in Q4 2014 saw the Company's share of Profit Gas drop from 55% to 40% (see "Principal Terms of the Tanzanian PSA and Related Agreements") as the volumes of Additional Gas sold were below 50 MMcfd, where it has remained for the last five quarters. The increase in revenue from Q2 2015 is directly related to the capital expenditure programme which has permitted the Company to take a significantly increased share of revenue as Cost Gas, with the underlying sales volumes remaining fairly static from Q2 2015 to Q1 2016.

Changes in net income over the last two years have been dominated by TANESCO. In Q4 2014 the Company recorded a US$52.2 million doubtful debts provision against TANESCO arrears. In Q4 2015 and Q1 2016 additional doubtful debt provisions of US$9.8 million and US$8.0 million respectively were provided against increased TANESCO arrears. Other significant factors affecting the results were:

- The collapse of the Tanzanian Shilling led to a Q4 2014 exchange loss of US$4.8 million and a further loss of US$1.8 million in Q1 2015.
- In Q3 2014 the Company took a charge of US$4.2 million for stock based compensation, with a total charge of US$3.5 million for the year.
- In Q4 2014 the Company wrote off US$5.1 million relating to site survey costs for an exploration well which it no longer plans to drill.
- In Q1 2016 the Company took a charge of US$2.8 million for stock based compensation as a consequence of the share price closing as CDN$4.14 compared to CDN$2,75 at the end of Q4 2015 together with the issuance of new Restrictive Stock Units.

Changes in cash flow from (used in) operations between quarters were primarily a result of when TANESCO receivables were collected. In Q3 2014, large payments were received as a result of World Bank funds received by the Government of Tanzania to assist in settling TANESCO arrears and TANESCO making several additional payments towards arrears.

The decrease in working capital from Q3 2015 to Q4 2015 was a consequence of the increase in creditors associated with the workover and drilling programme together with the additional bad debt provision against TANESCO, both of which were offset by the initial draw down of US$18.6 million from the IFC (net of expenses). The second draw down from the IFC of US$40 million in Q1 2016 has offset the decrease in working capital associated with the completion of the workover and drilling programme from Q4 2015 to Q1 2016.

Capital expenditure for the last four quarters Q2 2015 to Q1 2016 has amounted to US$51.3 million compared to US$2.0 million from Q2 2014 to Q1 2015. The 2015 workover and drilling programme commenced in Q3 2015 with some preliminary expenditure in Q2 2015 and was completed in Q1 2016.

The level of Industrial volumes decreased by 3% in the four quarters ending Q1 2016 to an average of 1,053 MMcf from an average of 1,090 MMcf for the four quarters ending Q1 2015. The decline is mainly a consequence of unscheduled maintenance work by a number of customers. Overall for the past eight quarters, the level of industrial sales has remained static.

The level of Power volumes decreased by 10% in the four quarters ending Q1 2016 to an average of 3,223 MMcf from an average of 3,572 MMcf for the four quarters ending Q1 2015, the decline is mainly the consequence of the decision by TANESCO not to renew a contract with an emergency power plant and the increased competition for supply of gas within Tanzania.