

**HEADWATER EXPLORATION INC.**  
**Interim Condensed Statements of Financial Position**  
(unaudited)

	September 30, 2024	December 31, 2023
<i>(Cdn\$ thousands)</i>	\$	\$
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and cash equivalents	136,591	146,052
Restricted cash	350	350
Accounts receivable (note 12)	72,936	46,744
Contribution receivable (note 6)	-	1,771
Financial derivative receivable (note 12)	921	3,758
Inventories	875	788
Prepays and deposits	1,325	1,461
<b>Total current assets</b>	<b>212,998</b>	<b>200,924</b>
Financial derivative receivable (note 12)	214	-
Exploration and evaluation assets (note 3)	23,653	17,930
Property, plant and equipment (note 4)	700,743	616,375
Other assets	1,012	1,106
<b>Total assets</b>	<b>938,620</b>	<b>836,335</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities (note 12)	96,453	73,715
Stock-based compensation payable (note 8)	3,594	2,431
Financial derivative liability (note 12)	1,120	79
Current portion of lease liability	6	34
Current income tax liability	11,786	22,397
Dividends payable (note 7)	23,767	23,658
Repayable contribution (note 6)	1,347	-
<b>Total current liabilities</b>	<b>138,073</b>	<b>122,314</b>
Financial derivative liability (note 12)	72	-
Stock-based compensation payable (note 8)	452	498
Lease liability	810	808
Decommissioning liability (note 5)	49,826	40,951
Repayable contribution (note 6)	10,713	11,405
Deferred income tax liability	54,188	49,861
<b>Total liabilities</b>	<b>254,134</b>	<b>225,837</b>
<b>Shareholders' Equity</b>		
Capital stock (note 7)	486,536	483,013
Contributed surplus	21,575	18,970
Retained earnings	176,375	108,515
<b>Total shareholders' equity</b>	<b>684,486</b>	<b>610,498</b>
<b>Total liabilities and shareholders' equity</b>	<b>938,620</b>	<b>836,335</b>

Subsequent events (note 13)

*See accompanying notes to the interim condensed financial statements*

Approved on behalf of the Board of Directors:

(signed) "Chandra Henry"  
Chandra Henry, CPA, CA  
Director

(signed) "Neil Roszell"  
Neil Roszell  
Executive Chairman

**HEADWATER EXPLORATION INC.**  
**Interim Condensed Statements of Income and**  
**Comprehensive Income**  
(unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2024	2023	2024	2023
<i>(Cdn\$ thousands, except per share data)</i>	\$	\$	\$	\$
<b>REVENUE</b>				
Sales (note 9)	158,382	149,632	456,697	372,808
Royalties	(29,438)	(26,721)	(80,935)	(61,770)
Revenue, net of royalties	128,944	122,911	375,762	311,038
Gains on financial derivatives (note 12)	737	2,199	1,951	10,858
	129,681	125,110	377,713	321,896
<b>EXPENSES</b>				
Blending and transportation	17,678	14,374	51,002	47,378
Production	13,949	12,211	39,418	33,625
General and administrative	2,656	2,496	7,960	6,886
Stock-based compensation	1,541	1,498	6,318	4,338
Depletion and depreciation	32,015	30,723	93,501	88,721
	67,839	61,302	198,199	180,948
Interest income and other expense (note 10)	766	795	2,782	3,149
Income before income taxes	62,608	64,603	182,296	144,097
Income taxes				
Current income tax expense	12,223	14,647	38,848	29,322
Deferred income tax expense	2,751	279	4,327	4,172
	14,974	14,926	43,175	33,494
<b>Net income and comprehensive income</b>	<b>47,634</b>	<b>49,677</b>	<b>139,121</b>	<b>110,603</b>
Net income per share (note 7)				
Basic	0.20	0.21	0.59	0.47
Diluted	0.20	0.21	0.58	0.47

*See accompanying notes to the interim condensed financial statements*

**HEADWATER EXPLORATION INC.**  
**Interim Condensed Statements of Cash Flows**  
(unaudited)

<b>Cash flow related to the following activities:</b>	Three months ended September 30,		Nine months ended September 30,	
<i>(Cdn\$ thousands)</i>	2024	2023	2024	2023
	\$	\$	\$	\$
<b>OPERATING</b>				
Net income	47,634	49,677	139,121	110,603
Items not involving cash:				
Unrealized (gains) losses on financial derivatives (note 12)	(392)	(1,905)	3,719	(2,995)
Stock-based compensation	1,541	1,498	6,318	4,338
Depletion and depreciation	32,015	30,723	93,501	88,721
Income tax expense	14,974	14,926	43,175	33,494
Non-cash finance charges	636	615	1,763	1,440
Settlement of decommissioning liability (note 5)	-	-	(95)	-
Income taxes paid	(10,228)	(4,348)	(49,459)	(24,638)
Change in non-cash operating working capital (note 11)	9,092	(5,618)	2,678	1,663
Cash flows provided by operating activities	95,272	85,568	240,721	212,626
<b>FINANCING</b>				
Payment of lease liability	(35)	(175)	(78)	(569)
Proceeds from exercise of stock options & warrants (note 7)	-	270	551	1,013
Dividends paid (note 7)	(23,765)	(23,586)	(71,152)	(70,517)
Proceeds from repayable contribution (note 6)	-	-	1,417	-
Cash flows provided used in financing activities	(23,800)	(23,491)	(69,262)	(70,073)
<b>INVESTING</b>				
Capital expenditures – property, plant and equipment (note 4)	(50,642)	(66,899)	(140,413)	(176,169)
Capital expenditures – exploration and evaluation (note 3)	(7,554)	(3,309)	(33,767)	(27,627)
Government grant (note 6)	-	-	354	-
Change in non-cash investing working capital (note 11)	(4,940)	8,178	(7,094)	14,798
Cash flows used in investing activities	(63,136)	(62,030)	(180,920)	(188,998)
Change in cash and cash equivalents	8,336	47	(9,461)	(46,445)
Cash and cash equivalents, beginning of period	128,255	128,955	146,052	175,447
Cash and cash equivalents, end of period	136,591	129,002	136,591	129,002

*See accompanying notes to the interim condensed financial statements*

**HEADWATER EXPLORATION INC.**  
**Interim Condensed Statements of Changes in Shareholders' Equity**  
(unaudited)

	Notes	Capital stock	Warrants	Contributed surplus	Retained earnings	Total shareholders' equity
<i>(Cdn\$ thousands)</i>		\$	\$	\$	\$	\$
<b>Balance at January 1, 2023</b>		<b>479,157</b>	<b>2</b>	<b>17,312</b>	<b>46,864</b>	<b>543,335</b>
Exercise of stock options	7	3,643	-	(2,635)	-	1,008
Exercise of warrants	7	7	(2)	-	-	5
Stock-based compensation		-	-	3,755	-	3,755
Reclassification to stock-based compensation payable	8	-	-	(563)	-	(563)
Net income		-	-	-	110,603	110,603
Dividends declared	7	-	-	-	(70,763)	(70,763)
<b>Balance at September 30, 2023</b>		<b>482,807</b>	<b>-</b>	<b>17,869</b>	<b>86,704</b>	<b>587,380</b>
<b>Balance at January 1, 2024</b>		<b>483,013</b>	<b>-</b>	<b>18,970</b>	<b>108,515</b>	<b>610,498</b>
Exercise of stock options	7	3,523	-	(2,972)	-	551
Stock-based compensation		-	-	5,577	-	5,577
Net income		-	-	-	139,121	139,121
Dividends declared	7	-	-	-	(71,261)	(71,261)
<b>Balance at September 30, 2024</b>		<b>486,536</b>	<b>-</b>	<b>21,575</b>	<b>176,375</b>	<b>684,486</b>

*See accompanying notes to the interim condensed financial statements*

# HEADWATER EXPLORATION INC.

## Notes to the Interim Condensed Financial Statements

(unaudited)

As at and for the three and nine months ended September 30, 2024, and 2023

*(All tabular amounts in thousands, unless otherwise stated)*

### 1. NATURE OF OPERATIONS

Headwater Exploration Inc. (“Headwater” or the “Company”) is a Canadian resource company engaged in the exploration for and development and production of petroleum and natural gas in Canada. Headwater is a public company existing under the Alberta Business Corporations Act with common shares listed on the Toronto Stock Exchange (“TSX”) under the symbol “HWX”.

Headwater’s principal place of business is located at 1400, 215 – 9<sup>th</sup> Avenue S.W., Calgary, Alberta, T2P 1K3 and its registered office is located at 2400, 525 – 8<sup>th</sup> Avenue S.W., Calgary, Alberta, T2P 1G1.

### 2. BASIS OF PREPARATION

These unaudited interim condensed financial statements have been prepared in accordance with IAS 34 – *Interim Financial Reporting* as issued by the International Accounting Standards Board (“IASB”). The unaudited interim condensed financial statements do not include all information required for annual financial statements and should be read in conjunction with the Company’s audited financial statements for the year ended December 31, 2023. These unaudited interim condensed financial statements have been prepared following the same accounting policies as the Company’s audited financial statements for the year ended December 31, 2023, except for the below.

The IASB issued amendments to IAS 1 “Presentation of financial statements” re: classification of liabilities as current or non-current which is effective for annual periods beginning on or after January 1, 2024. The amendment clarifies that the classification of liabilities as current or non-current should be based on rights that are in existence at the end of the reporting period. These amendments to IAS 1 did not have a material impact on the Company’s financial statements.

The timely preparation of these financial statements requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amount of assets, liabilities, income and expenses. Actual results may differ materially from these estimates. Significant judgments, estimates and assumptions made by management in these financial statements are outlined in the audited financial statements for the year ended December 31, 2023.

These unaudited interim condensed financial statements were approved and authorized for issue by the Company’s Board of Directors on November 7, 2024.

### 3. EXPLORATION AND EVALUATION (“E&E”) ASSETS

The following table reconciles the movements of the Company’s E&E assets for the periods:

	September 30, 2024	December 31, 2023
	\$	\$
Balance, beginning of period	17,930	42,872
Additions	33,767	28,556
Dispositions <sup>(1)</sup>	-	(3,750)
Transfers to PP&E	(28,044)	(49,748)
<b>Balance, end of period</b>	<b>23,653</b>	<b>17,930</b>

(1) Relates to the sale of a gross overriding royalty. No gain or loss was recorded related to the sale.

The Company concluded there are no indicators of impairment for its E&E assets as at September 30, 2024.

### 4. PROPERTY, PLANT AND EQUIPMENT (“PP&E”)

The following table reconciles the movements of the Company’s PP&E assets for the periods:

Cost	Oil and gas properties		Corporate		Total
	\$	\$	\$	\$	
Balance at December 31, 2022	835,220		2,835		838,055
Additions	213,179		38		213,217
Transfers from E&E	49,748		-		49,748
Government grant	(2,474)		-		(2,474)
Changes in decommissioning liabilities	7,425		-		7,425
<b>Balance at December 31, 2023</b>	<b>1,103,098</b>		<b>2,873</b>		<b>1,105,971</b>
Additions <sup>(1)</sup>	141,779		34		141,813
Transfers from E&E	28,044		-		28,044
Changes in decommissioning liabilities	7,918		-		7,918
<b>Balance at September 30, 2024</b>	<b>1,280,839</b>		<b>2,907</b>		<b>1,283,746</b>
<b>Accumulated depletion, depreciation and impairment</b>					
Balance at December 31, 2022	367,717		2,296		370,013
Depletion and depreciation expense	119,510		73		119,583
<b>Balance at December 31, 2023</b>	<b>487,227</b>		<b>2,369</b>		<b>489,596</b>
Depletion and depreciation expense	93,355		52		93,407
<b>Balance at September 30, 2024</b>	<b>580,582</b>		<b>2,421</b>		<b>583,003</b>
<b>Net book value at December 31, 2023</b>	<b>615,871</b>		<b>504</b>		<b>616,375</b>
<b>Net book value at September 30, 2024</b>	<b>700,257</b>		<b>486</b>		<b>700,743</b>

(1) Includes capitalized general and administrative expenses of \$3.1 million (nine months ended September 30, 2023 - \$2.7 million) and capitalized stock-based compensation of \$1.4 million (nine months ended September 30, 2023 - \$1.2 million).

The Company concluded there are no indicators of impairment for its PP&E assets as at September 30, 2024.

## 5. DECOMMISSIONING LIABILITY

The following table reconciles the movements of the Company's decommissioning liability for the periods:

	September 30, 2024	December 31, 2023
	\$	\$
Balance, beginning of period	40,951	32,343
Additions	8,793	12,975
Liabilities incurred	(95)	-
Change in estimate <sup>(1)</sup>	(875)	(5,550)
Accretion	1,052	1,183
<b>Balance, end of period</b>	<b>49,826</b>	<b>40,951</b>
<b>Key assumptions</b>		
Risk free rate	3.1%	3.0%
Inflation rate	1.6%	1.6%

(1) Relates to changes in the inflation rate and risk-free rate. This amount is the result of an increase in the risk-free rate over the period from 3.0% at December 31, 2023 to 3.1% at September 30, 2024.

The Company has estimated the net present value of its total decommissioning liabilities to be \$49.8 million as at September 30, 2024 (December 31, 2023 - \$41.0 million). The total future inflated and undiscounted amount of estimated cash flows required to settle these obligations is \$118.4 million (December 31, 2023 - \$97.4 million). Management estimates the settlement of these obligations will occur over the next 25 to 40 years.

## 6. REPAYABLE CONTRIBUTION (NRCan ERF)

In 2022 and 2023, the Company received approval of a total of four claims pursuant to a repayable contribution agreement with the Department of Natural Resources Canada ("NRCan"), under the Emissions Reduction Fund ("ERF") Onshore Program. As at September 30, 2024, all funds were received by the Company (December 2023 - \$1.8 million related to the holdback amount).

The Company has recognized a repayable contribution of \$14.2 million, undiscounted, and \$12.1 million discounted as at September 30, 2024 (December 31, 2023 - \$14.2 million and \$11.4 million respectively), with respect to claims submitted to the ERF and confirmed by NRCan. The Company discounts the repayable contribution at a weighted average interest rate of 7.7%. The undiscounted repayable portion of the funds received are to be repaid as follows: 10% on June 30, 2025, 33% on June 30, 2026, and 57% on June 30, 2027.

	September 30, 2024	December 31, 2023
	\$	\$
Balance, beginning of period	11,405	6,720
Repayable contribution	-	4,195
Interest	655	490
<b>Balance, end of period</b>	<b>12,060</b>	<b>11,405</b>
Current portion of repayable contribution	1,347	-
Long-term portion of repayable contribution	10,713	11,405

The Company is in compliance with all terms and conditions of the repayable contribution agreement.

## 7. CAPITAL STOCK

### a) Issued, authorized and outstanding

	September 30, 2024		December 31, 2023	
	Number of shares	Amount	Number of shares	Amount
Balance, beginning of period	236,580	\$ 483,013	233,920	\$ 479,157
Exercise of stock options	1,085	3,523	2,654	3,849
Exercise of warrants	-	-	6	7
Balance, end of period	237,665	486,536	236,580	483,013

### **Stock Options**

During the nine months ended September 30, 2024, 1.9 million stock options were exercised for 0.9 million common shares on a cashless basis and 144 thousand stock options were exercised for 144 thousand common shares for total proceeds of \$551 thousand. Contributed surplus related to the options exercised of \$3.0 million was transferred to capital stock.

During the nine months ended September 30, 2023, 2.7 million stock options were exercised for 1.9 million common shares on a cashless basis and 0.6 million stock options were exercised for 0.6 million common shares for total proceeds of \$1.0 million. Contributed surplus related to the options exercised of \$2.6 million was transferred to capital stock.

### b) Per share amounts

Basic per share amounts are calculated using the weighted average number of shares outstanding. The Company uses the treasury stock method to determine the impact of dilutive securities. The reconciling items between basic and diluted average common shares outstanding are stock options, warrants, RSUs, PSUs and accrued dividends on RSUs and PSUs.

	Three months ended September 30,		Nine months ended September 30,	
	2024	2023	2024	2023
Weighted average shares outstanding				
Basic	237,484	236,191	236,285	235,305
Diluted	239,735	239,167	238,427	237,683

### c) Dividends

On November 3, 2022, Headwater announced its inaugural quarterly cash dividend of \$0.10 per common share (\$0.40 per common share annualized). The first dividend was paid on January 16, 2023, to shareholders of record at the close of business on December 30, 2022. In 2023, Headwater declared \$94.4 million related to its quarterly cash dividend.

During the nine months ended September 30, 2024, the Company declared \$71.3 million (nine months ended September 30, 2023 - \$70.8 million) related to its quarterly cash dividend. Included in current liabilities is the dividend payable of \$23.8 million for the dividend declared on July 25, 2024, and paid out on October 15, 2024.



## 8. STOCK-BASED COMPENSATION

### a) Share awards

The Company has an awards plan (the “Awards Plan”) which provides for grants of restricted share units (“RSUs”) and performance share units (“PSUs”) to officers, employees and consultants of the Company. Generally, one third of the RSUs will vest on each of the first, second and third anniversaries of the date of grant and all PSUs will vest on the third anniversary of the date of grant, unless otherwise determined by the Board of Directors. RSUs are cash settled and PSUs are equity settled.

#### **RSUs (Cash Settled)**

The following table summarizes the changes in the RSU liability for the periods:

	September 30, 2024	December 31, 2023
Balance, beginning of period	1,188	-
Reclassified from contributed surplus	-	563
Increase in liability/fair value adjustment <sup>(1)</sup>	1,236	968
Payout <sup>(1)</sup>	(1,024)	(343)
Balance, end of period	1,400	1,188
Current portion of stock-based compensation payable	948	690
Long-term portion of stock-based compensation payable	452	498

(1) Includes dividend adjustment.

The RSU liability as at September 30, 2024 of \$1.4 million is based on a fair value of \$6.33 per RSU which is the Company’s closing share price on September 30, 2024.

The following table summarizes the changes in the number of outstanding RSUs for the periods:

	September 30, 2024	December 31, 2023
Outstanding, beginning of period	377	179
Granted	205	274
Forfeited	(14)	(22)
Exercised	(135)	(54)
Outstanding, end of period	433	377

#### **PSUs (Equity Settled)**

The following table summarizes the changes in the number of outstanding PSUs for the periods:

	September 30, 2024	December 31, 2023
Outstanding, beginning of period	1,917	838
Granted	827	1,082
Forfeited	-	(3)
Outstanding, end of period	2,744	1,917

For the nine months ended September 30, 2024, with respect to RSUs and PSUs outstanding, the Company recorded gross stock-based compensation expense of \$6.6 million, of which \$1.4 million was capitalized.

Subsequent to September 30, 2024, the Board of Directors approved the change from equity settlement to cash settlement for Headwater’s outstanding PSUs.

b) Deferred share units (“DSUs”)

The Company has a DSU plan (the “DSU Plan”) which provides for grants of DSUs to non-management directors. Each DSU vests on the date of grant; however, settlement of the DSU occurs when the individual ceases to be a director of the Company. DSUs are to be settled in cash or by payment in common shares acquired through the facilities of the TSX. It is the intention of the Company to settle DSUs in cash.

The following table summarizes the changes in the DSU liability for the periods:

	September 30, 2024	December 31, 2023
	\$	\$
Balance, beginning of period	1,741	825
Increase in liability/fair value adjustment <sup>(1)</sup>	905	916
Balance, end of period	2,646	1,741
Current portion of stock-based compensation payable	2,646	1,741

(1) Includes dividend adjustment.

The DSU liability as at September 30, 2024 of \$2.6 million is based on a fair value of \$6.33 per DSU which is the Company’s closing share price on September 30, 2024.

The following table summarizes the changes in the number of outstanding DSUs for the periods:

	September 30, 2024	December 31, 2023
Outstanding, beginning of period	264	141
Granted	124	123
Outstanding, end of period	388	264

c) Stock options

The Company has an old and new stock option plan (the “Option Plans”) under which options to purchase common shares of the Company may be granted to directors, officers, employees and consultants of the Company. The Company does not intend to grant any further options under the Option Plans.

The following table summarizes the changes in the outstanding stock options for the periods:

	Nine months ended September 30, 2024		Year ended December 31, 2023	
	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price
Options outstanding, beginning of period	2,508	\$ 3.88	6,086	\$ 2.74
Forfeited or expired	-	-	(8)	\$ 2.39
Exercised <sup>(1)</sup>	(2,056)	\$ 3.74	(3,570)	\$ 1.94
Options outstanding, end of period	452	\$ 4.49	2,508	\$ 3.88
Options exercisable, end of period	369	\$ 4.40	1,383	\$ 3.60

(1) The Company’s weighted average share price, at the date of exercise, for stock options exercised during the nine months ended September 30, 2024 was \$7.34 per common share (nine months ended September 30, 2023 - \$6.51 per common share).

There were no stock options granted in the nine months ended September 30, 2024, or in the year ended December 31, 2023.

The range of exercise prices of stock options outstanding and exercisable as at September 30, 2024 is as follows:

Exercise prices	Outstanding options			Exercisable options	
	Number of options outstanding	Weighted average remaining term (years)	Weighted average exercise price	Number of options exercisable	Weighted average exercise price
\$ 2.39 - \$ 3.00	25	0.21	\$ 2.39	25	\$ 2.39
\$ 3.01 - \$ 5.23	427	0.62	\$ 4.62	344	\$ 4.55
<b>Total</b>	<b>452</b>	<b>0.60</b>	<b>\$ 4.49</b>	<b>369</b>	<b>\$ 4.40</b>

For the nine months ended September 30, 2024, with respect to stock options outstanding, the Company recorded gross stock-based compensation expense of \$197 thousand, of which \$40 thousand was capitalized.

## 9. SALES

The following table presents the Company's sales disaggregated by revenue source:

	Three months ended September 30,		Nine months ended September 30,	
	2024	2023	2024	2023
	\$	\$	\$	\$
Heavy oil	157,760	147,368	447,711	359,875
Natural gas	77	1,330	6,364	9,714
Natural gas liquids	468	819	1,591	2,097
Gathering, processing and transportation	77	115	1,031	1,122
	158,382	149,632	456,697	372,808

Included in accounts receivable as at September 30, 2024 is \$47.8 million (December 31, 2023 - \$36.3 million) of accrued sales related to September 2024 production.

## 10. INTEREST INCOME AND OTHER EXPENSE

Interest income and other expense consists of the following:

	Three months ended September 30,		Nine months ended September 30,	
	2024	2023	2024	2023
	\$	\$	\$	\$
Interest income	1,398	1,519	4,507	4,886
Realized and unrealized foreign exchange gains (losses)	(1)	(290)	33	(520)
Accretion on decommissioning liability	(387)	(295)	(1,052)	(822)
Interest on repayable contribution	(223)	(124)	(655)	(362)
Interest on lease liability	(21)	(15)	(51)	(33)
	766	795	2,782	3,149

(1) Included within non-cash finance charges in the statement of cash flows is unrealized foreign exchange gains (losses), accretion on decommissioning liability, interest on repayable contribution and interest on lease liability.

## 11. SUPPLEMENTAL CASH FLOW INFORMATION

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2024	2023	2024	2023
	\$	\$	\$	\$
Change in non-cash operating working capital:				
Accounts receivable	8,054	(13,573)	(4,991)	(8,505)
Inventories	(55)	(329)	(87)	271
Prepays and deposits	933	84	136	(162)
Accounts payable and accrued liabilities	315	8,231	8,644	10,371
Stock-based compensation payable	(155)	(31)	(1,024)	(312)
	9,092	(5,618)	2,678	1,663
Change in non-cash investing working capital:				
Accounts receivable	(5,547)	-	(21,188)	-
Accounts payable and accrued liabilities	607	8,178	14,094	14,798
	(4,940)	8,178	(7,094)	14,798
Cash income taxes paid	10,228	4,348	49,459	24,638
Cash standby fees paid	88	44	191	120
Cash interest received	1,591	1,565	4,802	5,038

## 12. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Financial instruments of the Company include cash and cash equivalents, restricted cash, accounts receivable, financial derivative receivable/liability, deposits, contribution receivable, accounts payable and accrued liabilities, dividends payable and repayable contribution. The Company is exposed to financial risks arising from its financial assets and liabilities that include credit risk and liquidity risk in addition to market risks associated with commodity prices and foreign exchange rates.

a) The Company is exposed to the following risks:

i) Commodity price risk

Headwater enters into financial derivative commodity contracts to manage the risks associated with fluctuations in commodity prices. All such transactions are conducted in accordance with the Company's established risk management policies. The Company does not use derivative financial instruments for speculative purposes.

The Company had the following outstanding financial derivative commodity contracts as at September 30, 2024:

Commodity	Index	Type	Term	Daily Volume	Contract Price
Natural Gas	AGT <sup>(1)</sup>	Fixed	Dec 2024 - Jan 2025	2,500 mmbtu	Cdn\$13.75/mmbtu
Natural Gas	AGT	Fixed	Dec 2024 - Mar 2025	5,000 mmbtu	Cdn\$11.98/mmbtu
Natural Gas	AGT	Fixed	April 2025	2,500 mmbtu	Cdn\$4.13/mmbtu
Natural Gas	AECO 5A	Fixed	October 2024	2,000 GJ	Cdn\$2.12/GJ
Natural Gas	AECO 5A	Fixed	Nov 2024 - Mar 2025	3,000 GJ	Cdn\$2.49/GJ
Natural Gas	AECO 5A	Fixed	Jan 2025 – Dec 2025	1,000 GJ	Cdn\$2.17/GJ
Natural Gas	AECO 5A	Fixed	Apr 2025 – Oct 2025	2,000 GJ	Cdn\$2.78/GJ
Crude Oil	WCS Basis <sup>(2)</sup>	Differential	Oct 2024 - Dec 2024	1,000 bbl	US\$15.00/bbl
Crude Oil	WCS Basis	Differential	Nov 2024 - Dec 2024	2,500 bbl	US\$14.30/bbl
Crude Oil	WCS Basis	Differential	Jan 2025 - Dec 2025	1,000 bbl	US\$13.95/bbl

(1) AGT = Algonquin city-gates

(2) WCS = Western Canadian Select

The following table summarizes the Company's financial derivative gains (losses) on commodity contracts for the periods:

	Three months ended September 30,		Nine months ended September 30,	
	2024	2023	2024	2023
	\$	\$	\$	\$
Gains (losses) on financial derivatives:				
- realized gains		345	294	5,670
- unrealized gains (losses)		392	1,905	(3,719)
<b>Gains on financial derivatives</b>		<b>737</b>	<b>2,199</b>	<b>1,951</b>
				<b>10,858</b>

The following table summarizes the fair value as at September 30, 2024 and the change in fair value for the nine months ended September 30, 2024:

	Commodity contracts	Foreign exchange contracts	Total
	\$	\$	\$
Net financial derivative receivable, beginning of period	3,662	17	3,679
Unrealized change in fair value <sup>(1)</sup>	(3,719)	(17)	(3,736)
<b>Net financial derivative liability, end of period</b>	<b>(57)</b>	<b>-</b>	<b>(57)</b>

(1) Unrealized change in fair value related to the Company's foreign exchange contracts is included in interest income and other expense.

The fair value of the net financial derivative liability related to the Company's commodity contracts of \$57 thousand as at September 30, 2024 is based on estimated future natural gas and crude oil prices as of that date. The fair values of these financial derivative commodity contracts are sensitive to changes in the natural gas and crude oil reference prices. Holding other assumptions constant, if the AECO 5A and AGT price increased by 10% and the WCS differential to WTI decreased by 10%, the fair value of the net financial derivative liability would increase (decrease) by \$2.4 million.

#### ii) Foreign currency risk

As of April 1, 2024, all of Headwater's revenue contracts are settled in Canadian dollars. However, the Company is exposed to fluctuations in the Canadian to U.S. dollar exchange rate given realized pricing is directly influenced by U.S. dollar denominated benchmark pricing and from exposure to its U.S. dollar denominated WCS commodity contracts. Headwater may decide to mitigate a portion of this risk by periodically entering into foreign exchange contracts. As at September 30, 2024, Headwater did not have any foreign exchange contracts outstanding.

#### *Fair Value Measurement*

The Company classifies fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The Company maximizes the use of observable inputs when preparing calculations of fair value, where possible.

The fair value of cash and cash equivalents, restricted cash, accounts receivable, deposits, accounts payable and accrued liabilities and dividends payable approximate their carrying value due to the short term to maturity of these instruments. The repayable contribution has been discounted at an estimated market rate and therefore carrying value approximates fair value.

The Company's financial derivative receivable/liability is considered Level 2 in the fair value hierarchy.

### iii) Credit risk

At September 30, 2024, the expected credit loss on the Company's accounts receivable was \$nil. As at September 30, 2024, the Company's receivables consisted of \$47.8 million (December 31, 2023 - \$36.3 million) from crude oil and natural gas marketers, \$0.1 million from commodity contract counterparties (December 31, 2023 - \$4.8 million), \$24.7 million (December 31, 2023 - \$3.9 million) from joint venture partners and \$0.3 million (December 31, 2023 - \$1.7 million) related to accrued interest and other.

During the year ended December 31, 2023, Headwater entered into an agreement to construct a natural gas gathering system. Once commissioned, which is expected to occur late 2024, the Company is entitled to be reimbursed the capital costs. Included in the joint venture receivable balance at September 30, 2024, is a balance outstanding related to this agreement in the amount of \$24.7 million. As this amount is expected to be collected during the year ended December 31, 2024, it has been recorded as a current asset and included within accounts receivable in the Interim Condensed Statements of Financial Position. Except for this joint venture receivable, trade receivables generally have a 30-day term.

### iv) Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. The Company manages liquidity risk through its working capital and an actively managed operating and capital expenditure budgeting process. The Company entered into a \$100.0 million credit facility in the fourth quarter of 2022 and increased the associated borrowing base from \$100.0 million to \$200.0 million in the second quarter of 2024, to add further liquidity. As at September 30, 2024, the Company held cash of \$136.6 million.

### **Credit Facilities**

During the fourth quarter of 2022, the Company entered into an agreement with the National Bank of Canada and the Bank of Montreal (the "Lenders") providing for senior secured revolving syndicated credit facilities. The extendible revolving credit facilities are comprised of a \$20.0 million operating facility and an \$80.0 million syndicated facility. During the second quarter of 2024, the Company increased the total borrowing base to \$200.0 million from \$100.0 million. Pursuant to the increase in borrowing base, and so long as no event of default has occurred, the Company may request one or more increases in the commitment amount from the current commitment amount of \$100.0 million to a maximum total commitment amount of \$200.0 million. Each increase may not be less than \$1.0 million and the Lenders have no obligation to participate in any requested increase in commitment.

As at September 30, 2024, Headwater had not drawn on the credit facilities.

The credit facilities have a revolving period of 364 days, extendible annually at the request of the Company, subject to approval of the Lenders. If not extended, the credit facilities will automatically convert to a term loan and all outstanding obligations will be repayable one year after the expiry of the revolving period. The borrowing base is subject to semi-annual redeterminations occurring by May 31<sup>st</sup> and by November 30<sup>th</sup> of each year. The credit facilities are secured by a demand debenture in the amount of \$500 million. Repayments of principal are not required until the maturity date, provided that the borrowings do not exceed the authorized borrowing base and the Company is in compliance with all covenants, representations and warranties.

The credit facilities bear interest at a floating market rate with margins charged by the Lenders linked to the Company's senior debt to EBITDA ratio. EBITDA, for the purposes of calculating the senior debt to EBITDA ratio, is calculated as net income adjusted for non-cash items, interest expense and income taxes. Senior debt, for the purposes of calculating the senior debt to EBITDA ratio, is calculated as any debt of the Company excluding the financial derivative liability and repayable contribution.

The credit facilities are not subject to any financial covenants. Additionally, distributions are permitted subject to compliance with a Board approved distributions policy.

## b) Management of capital

The Company's objectives when managing capital are to i) deploy capital to provide an appropriate return on investment to its shareholders; ii) maintain financial flexibility in order to preserve the Company's ability to meet financial obligations; and iii) maintain a capital structure that provides financial flexibility to execute strategic acquisitions. To aid in managing the capital structure, the Company monitors adjusted working capital and adjusted funds flow from operations.

On November 3, 2022, Headwater announced its inaugural quarterly cash dividend of \$0.10 per common share (\$0.40 per common share annualized). The first dividend was paid on January 16, 2023, to shareholders of record at the close of business on December 30, 2022. In 2023, Headwater declared \$94.4 million related to its quarterly cash dividend.

On July 25, 2024, Headwater declared a cash dividend of \$0.10 per common share. The dividend was paid on October 15, 2024, to shareholders of record at the close of business on September 27, 2024. During the nine months ended September 30, 2024, Headwater declared \$71.3 million related to its quarterly cash dividend.

The Company's strategy is designed to maintain a flexible capital structure consistent with the objectives as stated above and to respond to changes in economic conditions and the risk characteristics of the underlying crude oil and natural gas assets. Key indicators of changing economic conditions include adjusted working capital and adjusted funds flow from operations. Headwater considers its capital structure to include shareholders' equity and working capital. In order to maintain or adjust its capital structure, the Company may from time to time issue new common shares, seek debt financing, change its future dividend policy and adjust its capital spending to manage working capital.

In order to facilitate the management of its capital expenditures and working capital, the Company prepares annual budgets which are updated quarterly depending upon varying factors including current and forecast crude oil and natural gas prices, capital expenditures and general industry conditions. The annual and updated budgets are approved by the Board of Directors.

### i) Adjusted working capital

Management considers adjusted working capital to be a key measure to assess the Company's liquidity and capital management.

	As at September 30, 2024	As at December 31, 2023
	\$	\$
Working capital	74,925	78,610
Repayable contribution	(10,713)	(11,405)
Financial derivative receivable	(921)	(3,758)
Financial derivative liability	1,120	79
<b>Adjusted working capital</b>	<b>64,411</b>	<b>63,526</b>

### ii) Adjusted funds flow from operations

Management considers adjusted funds flow from operations to be a key measure to assess the Company's management of capital. Adjusted funds flow from operations is an indicator as to whether adjustments are necessary to the level of capital expenditures. For example, in periods where adjusted funds flow from operations is negatively impacted by reduced commodity pricing, capital expenditures may need to be reduced or curtailed to preserve the Company's capital and dividend policy. Management believes that by excluding the impact of changes in non-cash working capital and adjusting for current income taxes in the period, adjusted funds flow from operations provides a useful measure of Headwater's ability to generate the funds necessary to manage the capital needs of the Company.

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2024	2023	2024	2023
	\$	\$	\$	\$
Cash flows provided by operating activities	95,272	85,568	240,721	212,626
Changes in non-cash working capital	(9,092)	5,618	(2,678)	(1,663)
Current income taxes	(12,223)	(14,647)	(38,848)	(29,322)
Income taxes paid	10,228	4,348	49,459	24,638
Adjusted funds flow from operations	84,185	80,887	248,654	206,279

Adjusted working capital and adjusted funds flow from operations are not standardized measures and therefore may not be comparable with the calculation of similar measures of other entities.

### 13. SUBSEQUENT EVENTS

#### a) Dividend

Subsequent to September 30, 2024, the Company declared a cash dividend of \$0.10 per common share. The dividend will be paid on January 15, 2025, to shareholders of record at the close of business on December 31, 2024.

#### b) Financial derivative contracts

Subsequent to September 30, 2024, Headwater entered into the following commodity contracts:

Commodity	Index	Type	Term	Daily Volume	Contract Price
Natural Gas	AECO 5A	Fixed	Jan 2025 - Dec 2025	1,000 GJ	Cdn\$2.15/GJ
Crude Oil	WCS Basis	Differential	Jan 2025 - Dec 2025	1,000 bbl	US\$12.95/bbl