ZENITH ENERGY LTD.
MANAGEMENT'S DISCUSSION AND ANALYSIS
THREE MONTHS ENDED JUNE 30, 2017

This management's discussion and analysis (the "MD&A") dated August 14, 2017 of Zenith Energy Ltd. ("Zenith" or the "Company", is presented in Canadian dollars and should be read in conjunction with the June 30, 2017 unaudited condensed interim consolidated financial statements as well as the March 31, 2017 audited consolidated financial statements of Zenith, together with the accompanying notes.

The consolidated financial statements have been prepared by management and approved by Zenith's Board of Directors on the recommendation of the Audit Committee. These statements are based on certain estimates and assumptions and involve risks and uncertainties. Actual results may differ materially. The financial data included in this MD&A is in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and interpretations of the International Financial Reporting Interpretations Committee ("IFRIC") that are effective as at April 1, 2015. The Company has presented its financial statements on a going concern assumption, which assumes that the Company will be able to continue to finance its operations for the foreseeable future and will be able to realize its assets and discharge its liabilities in the normal course of business. Refer to the Business Risks and Uncertainties section of this MD&A for additional information related to identified risks, estimates and uncertainties.

The functional currency of the Company is the Canadian dollar ("CAD"); the functional currency Company's Argentine subsidiaries is the Argentine Peso; the functional currency of the Company's Italian subsidiary is the Euro; the functional currency of the Company's Azerbaijan is the Manat; the functional currency of the Company's Swiss subsidiary is the Swiss Franc and the functional currency of the Company's United States subsidiaries is the United States dollar. The Company's presentation currency is the CAD. In this MD&A, unless otherwise noted, all dollar amounts are expressed in CAD. References to "USD" are to United States dollars, references to "€" are Euros and references to "GBP" are to Britain Pounds, references to "AZN" are to Azerbaijan Manat and references to "CHF" are to Swiss Franc.

The amounts are shown in thousands Canadian dollars (CADS'000), British Pounds (£'000) and US Dollars (USD$'000), where not disposed differently.

Additional information related to the Company's business and activities can be found on SEDAR at www.sedar.com.

BOE Presentation – Production information is commonly reported in units of barrels of oil equivalent ("boe"). For purposes of computing such units, natural gas is converted to equivalent barrels of oil using a conversion factor of six thousand cubic feet ("mcf") to one barrel of oil ("bbl"). This conversion ratio of 6:1 is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. Such disclosure of boe may be misleading, particularly if used in isolation. Readers should be aware that historical results are not necessarily indicative of future performance.

Special Note Regarding Non-IFRS Measures – This MD&A may include references to certain financial measures, as described below, which do not have standardized meanings prescribed by IFRS, however, as these measures are commonly used in the oil and gas industry, the Company believes that their inclusion is useful to investors and they are measures that the Company uses to evaluate its performance. Investors are cautioned that these non-IFRS measures should not be construed as an alternative to the measures calculated in accordance with IFRS, given their non-standardized meanings; they may not be comparable to similar measures presented by other issuers. The term "field netback" is defined as petroleum and natural gas sales less royalties and less operating and transportation costs. The term "funds from (used in) operations", defined as the cash flow from operating activities, before the change in non-cash working capital and abandonment expenditures, should not be considered an alternative to, or more meaningful than, cash flow from operating activities or net income (loss) as determined in accordance with IFRS as an indicator of performance. The Company's determination of funds from operations may not be comparable to that reported by other companies.

Cautionary Statement regarding Forward-Looking Information

Certain information in this MD&A is forward-looking and related to anticipated financial performance, events and strategies. When used in this context, words such as “will”, “anticipate”, “believe”, “plan”, “intend”, “target” and “expect” or similar words suggest future outcomes. By their nature, such statements are subject to significant risks, assumptions and uncertainties, which could cause the Company’s actual results and experience to be materially different than the anticipated results. In particular, forward-looking information and statements include, but are not limited to: (i) expectations related to crude oil and petroleum products prices and demand; (ii) the state of capital markets; (iii) expectations related to operating costs in Azerbaijan and Italy; (iv) variations in the US dollar, Euro, Manat, and Canadian dollar exchange rates; (v) expectations related to regulatory approvals; (vi) management’s analysis of applicable tax legislation; (vii) expectations that the currently applicable and proposed tax laws will not change and will be implemented; (viii) expectation that management will continue to focus its efforts towards acquiring large exploration permits, which offer high exploration potential and the opportunity to act as operator at least for the initial exploration period; (ix) expectation that management will consider acquiring additional producing assets; (x) the capital expenditures required in order to re-commence production on both the Torrente Vulgano and Canaldente properties; (xi) the ability of the Company to re-commence production on both the Torrente Vulgano and Canaldente properties by late 2017; (xii) the price of natural gas and of the electricity in Italy; (xiii) the ability of the Company to comply with certain regulatory requirements in Italy; (xiv) the Company’s ability to increase its oil and gas production in the year 2017; (xv) expectations related to the properties producing oil in Azerbaijan named Muraxkhanli, Jafarli and Zardab, owned by Zenith Aran Oil Company and (xvi) business strategy and outlook.

These statements are based on certain assumptions and analysis made by the Company in light of its experience and perception of historical trends, current conditions and expected future developments and other factors it believes are appropriate. The material factors and assumptions used to develop these forward-looking statements include, but are not limited to: (i) increased competition; (ii) assumption that operating costs in Azerbaijan and Italy may be reduced in future months and that the oil price in the international markets will continue to improve; (iii) additional financing of the Company is subject to the global financial markets and economic conditions; (iv) the Company will evaluate certain properties located within Azerbaijan and will focus on managing the properties acquired in 2016 with the intention to increase production and cash flows; (v) assumptions related to international oil and natural gas prices; (vi) ability to obtain regulatory approvals; (vii) costs of exploration and development; (viii) availability and cost of labour and management resources; (ix) performance of contractors and suppliers; (x) availability and cost of financing; and (xi) the Company’s business strategy and outlook.

Whether actual results, performance or achievements will conform to the Company's expectations and predictions is subject to a number of known and unknown risks and uncertainties which could cause actual results to differ materially from the Company's expectations. Such risks and uncertainties include, but are not limited to risks and uncertainties relating to: (i) volatility of and assumptions regarding commodity prices; (ii) product supply and demand; (iii) market competition; (iv) risks inherent in the Company’s operations; (v) potential disruption or unexpected technical difficulties in developing or maintaining facilities; (vi) risks associated with technology; (vii) Company’s ability to generate sufficient cash flow from operations to meet its current and future obligations; (viii) the Company’s ability to secure external sources of debt and equity as needed; (ix) changes in royalty, tax, environmental, greenhouse gas, carbon, accounting and other laws or regulations or the interpretation of such laws or regulations; (x) political and economic conditions in the countries in which the Company operates; (xi) terrorist threats; (xii) risks associated with potential future lawsuits and regulatory actions made against the Company; (xiii) the performance of counterparties in meeting their obligations under agreements; (xiv) economic conditions; (xv) equipment and labour shortages and inflationary costs; (xvi) fluctuations in foreign exchange rates; (xvii) the effect of weather conditions on operations and facilities; and (xviii) stock market volatility.

Readers are cautioned not to place undue reliance on forward-looking statements as actual results could differ materially from the plans, expectations, estimates or intentions expressed in the forward-looking statements. Forward-looking statements are provided for the purpose of presenting information about management’s current expectations and plans relating to the future and readers are cautioned that such statements may not be appropriate for other purposes.

Except as required by law, the Company disclaims any intention and assumes no obligation to update any forward-looking statement.

Critical Accounting Estimates and Judgements

The Company makes estimates and assumptions concerning the future. The resulting estimates will, by definition, seldom equal the related achieved amounts. The estimates and assumptions that have significant risk of causing material adjustments and assumptions to the carrying amounts of assets and liabilities are disclosed below.

In relation to the valuation of the assets and liabilities associated with the Azerbaijan acquisition, this assessment involves:

- Future revenues and estimated development and exploration costs;
- The discount rate to be applied for the purposes of deriving a recoverable value;
- The expected tax rate; and
- The expected oil price.

During the years recognized value of assets and associated liabilities for its Azerbaijan Assets acquired, including the payments due in respect of the acquisition relating to royalties, work and exploration programmes and taxation. The valuations of the assets and of the liabilities have been based on the Net Present Value (“NPV”) of future cash flows included in the Competent Persons Report prepared on behalf of the Company by professionals, using appropriate rate of discount.

Any changes to the estimates may result in a material impact to the carrying value of both the assets and liabilities, arising in respect of the acquisitions.

NATURE OF OPERATIONS, ACQUISITON AND EXPLORATION ACTIVITIES

The Company was incorporated under the Business Corporations Act (British Columbia) (“BCBCA”) on September 20, 2007. The registered business address is 15th Floor, Bankers Court, 850 - 2nd Street S.W., Calgary, Alberta T2P 0R8, Canada. Zenith’s website is www.zenithenergy.ca. The Company is involved in the exploration for, development of and production of petroleum and natural gas in Azerbaijan and Italy and exploration for oil & gas in central Asia.

On March 10, 2010, Zenith formed Ingenieria Petrolera del Rio de la Plata S.r.l. (“IPRP”), a wholly owned subsidiary of Zenith. IPRP was initially incorporated in Buenos Aires, Argentina, to negotiate management agreements to operate existing producing properties. However, as described in following paragraphs, after Petrolera Patagonia S.r.l. was acquired, management saw no immediate needs for IPRP and the company was kept in a dormant state and held in trust by Zenith’s trustees in Argentina until late 2011.

On July 20, 2010, Zenith incorporated a wholly owned US subsidiary, Ingenieria Petrolera Patagonia Ltd. (“IPP”), to act as the potential acquirer of two US based companies controlling Central Patagonia S.r.l., renamed as Petrolera Patagonia S.r.l., the owner of two producing oil fields in the Chubut Province in Argentina.

On July 22, 2010, Zenith acquired two US based companies, namely Central Patagonia Corporation (renamed Petrolera Patagonia Corporation or “PPC”) and CPC Holdings (renamed PP Holdings Inc. or “PPH”) owning respectively 95% and 5% of Central Patagonia S.r.l. (renamed Petrolera Patagonia S.r.l. or “PPS”), thereby acquiring two adjacent oil producing properties in Argentina.

On March 23, 2011, Zenith established Canoel Italia S.r.l. (“Italia S.r.l”), a wholly owned subsidiary of the Company, so that it would have an operating entity if the Company was awarded the oil and gas properties being posted for auction by the Ministry of Economic Development.

On August 27, 2011, Italia S.r.l was awarded two gas properties, which were previously on production but currently shut-in, and the auction by the Ministry of Economic Development. Zenith’s bid was accepted on the basis of its technical presentation and proposed program to place the properties back on stream. The properties are Torrente Vulgano, located in the Puglia region, and Canaldente, located in the Basilicata region. Both regions are located in southern Italy, which is where the majority of hydrocarbons are produced.

In mid-2012, in line with the Company’s strategy to increase its involvement in Italy through its Italian subsidiary, Zenith commenced negotiations to purchase producing and exploratory permits from a well-established gas producing company, Mediterranean Oil & Gas Plc, a British company with activities in Italy, France and Malta whose shares trade on the London AIM Stock Exchange.

On June 6, 2013, the Company completed the acquisition of various working interests in 13 Italian producing and exploration properties (the “Assets”) from Medoilgas Italia S.P.A. and Medoilgas Civita Limited, each a subsidiary of Mediterranean Oil and Gas Plc (collectively, "MOG”) after receiving the final approval from the Italian Ministry of Economic Development to the change of ownership. The Assets are comprised of (i) 6 operated onshore gas production concessions: Masseria Grottavecchia (20% working interest), San Teodoro (100% working interest), Torrente Cigno (45% working interest), Misano Adriatico (100% working interest), Sant’Andrea (40% working interest) and Masseria Petrilli (50% working interest); (ii) 3 non-operated onshore gas production concessions: Masseria Acquasalsa (8.8% working interest), Lucera (13.6% working interest) and San Mauro (18% working interest) (collectively, the “Gas Licenses”); (iii) an operated exploration permit: Montalbano (57.15% working interest) (the “Exploration Permit”); and (iv) 3 exploration permit applications: Serra dei Gatti (100% working interest), Villa Carbone (50% working interest) and Colle dei Nidi (25% working interest) (the “Exploration Applications”).

Most of the Gas Licenses are located onshore in southern Italy, in the Regions of Puglia, Basilicata, Molise, Abruzzo and Marche. The Exploration Permit and Exploration Applications are located in southern Italy and cover an area of 1,285 square kilometres.

On October 1, 2015, the Company acquired co-generation equipment and facilities from the owner of the plant that treats gas from the Masseria Vincelli 1 well in the Torrente Cigno concession in Italy. The acquisition enables the company to produce electricity from the gas produced by the Masseria Vincelli 1 well and sell it directly into the national energy grid.

In September 2015, the Company opened an office in Baku, the capital of Azerbaijan. In October 2015, the Republic of Azerbaijan issued a Presidential Decree which authorized the State Oil Company of the Republic of Azerbaijan (“SOCAR”) to negotiate a Rehabilitation, Exploration, Development and Production Sharing Agreement (“REDPSA”) with Zenith pursuant to which Zenith would receive the rights and obligations to an 80% participating interest in current and future production from three producing onshore oil fields named Muraxkhanli, Jafarli and Zardab, known as the Muraxkhanli Area (the “Area”), covering an area of 642.4 square kilometres.

The REDPSA was executed on March 16, 2016 between SOCAR, Zenith Aran and SOCAR Oil Affiliate (“SOA”), a 100% owned subsidiary of SOCAR. On June 20, 2016, upon ratification by the Parliament of the Republic of Azerbaijan the REDPSA a became binding in law in Azerbaijan.

On August 11, 2016, the handover of the Azerbaijan assets was formally completed with the necessary signatures on related documents and the Company commenced crude oil production of approximately 275 barrels of oil per day in Azerbaijan under Zenith’s ownership hence the REDPSA became effective on August 11, 2016.

See Operational Update – Azerbaijan for further details.

On February 20, 2017, Zenith announced the sale of its operations in Argentina to a group of local energy investors. Termination of activities in Argentina will enable Zenith's management to more effectively direct its focus on its Italian operations and especially towards Azerbaijan, where the Company’s most important assets are located, and where a systematic programme of field rehabilitation has begun. This re-alignment reflects the Board's aversion to operational overstretch and the Company’s preference for a strong, concentrated focus towards the achievement of its production objectives in Azerbaijan.

On March 30, 2017 Zenith acquired a Swiss company, Altasol SA; the acquired entity is a non-operating company, which was purchased with the prospective of developing an oil trading subsidiary of Zenith Energy Ltd.

DEVELOPMENT AND EXPLORATION ACTIVITIES

The Company conducted the following development and exploration activities in Argentina, Azerbaijan and Italy as noted below:

	Three months ended June 30 (CAD$’000)	
Capital additions	**2017**	2016
Argentina	**$ -**	-
Azerbaijan	**-**	-
Italy	**-**	20
	$ -	$ 20

HIGHLIGHTS FOR THE THREE MONTHS AND YEAR ENDED MARCH 31, 2017 INCLUDE THE FOLLOWING:

Operational:

- During the three months ended June 30, 2017 the Company sold 23,390 bbls of oil from its properties in Azerbaijan. This data is not comparable to the past year.

  At the end of June 2017, there were 131 bbls of unsold oil production in Azerbaijan held in inventory which were sold in subsequent months. Total oil sales, transfers of produced volumes to the Termap Oil Storage and oil held in inventory at the end of the period correspond to an average daily production rate for the three months ended June 30, 2017 of 273 bbls of oil per day. The average daily production rate is not comparable with past year.

- During the three months ended June 30, 2017, the Company sold 4,790 mcf of natural gas from its Italian properties as compared 9,561 mcf of natural gas in the 2016 similar period, with a decrease of 50%, due to the stop of the production in the Lucera and Acquasalsa concessions for urgent maintenance.

- During the three months ended June 30, 2017, the Company sold 223 bbls of condensate from its Italian properties as compared to 184 of condensate in the 2016 similar periods, with an increase of 21%.

- During the three months ended June 30, 2017, the Company sold 2,522 MWh of electricity from its Italian properties as compared to 2,718 MWh of the 2016 similar period, with a decrease of 7%, due a production disruption in June 2017 for maintenance of the plant.

Financial:

- The Company generated oil and natural gas revenue, net of royalties, of $1,540k and $127k of electricity in the three months ended June 30, 2017 versus of $100k and $141k, respectively, in the comparative 2016 period.

- On May 25, 2017, the Group announced that following the its announcement on February 22, 2017 that a Director of the Group had exercised an option to acquire 1,000,000 new Common Shares in the capital of the Group, the Option Shares have been issued on May 23, 2017 following confirmation by Mr. Regis Milano of the custodian to whom they should be issued.
- On June 29, 2017, an investor in the Company has exercised warrants to acquire 1,019,250 new common shares of no par value in the capital of the Company. The exercise price of the warrant was C$0.15 per share, and the total consideration received C$15k (approximately £91k).
- On April 05, 2017, the Group's wholly-owned subsidiary, Zenith Aran, entered into a general line of credit agreement with Rabitabank Open Joint Stock Company ("Rabitabank") up to an amount of USD $320k (CAD $416), for industrial and production purposes. The loan drawn down in one tranche and as at 06 April 2017 it was fully drawn down. Rabitabank can postpone or suspend the facility if there is a decline in oil production under the REDPSA of more than 30% from production levels as at the date of first drawdown or if the REDPSA is terminated.
  This Credit Agreement bears interest at a rate of 11% per annum. The loan is guaranteed by the Group. The loan granted for one-year period. The 25% of the principal amount should be paid on quarterly basis. The amount of interest to be paid on monthly basis. As of June 30, 2017, the amount of USD $320k (CAD $416) plus accrued interest was still outstanding, it is classified as a current liability.
  On July 06, 2017, the terms of the repayment of the USD $320k (CAD $416) Credit Agreement were amended and first repayment of principal of USD $80k has been moved to the end of July.
  On July 31, 2017 USD $20k (CAD $21) were repaid, and the balance of US $60k (CAD $63) will be paid on September 1, 2017.
- On April 12, 2017, Zenith Aran entered into a general line of credit agreement with Rabitabank up to an amount of USD $200k (CAD $260). The Seventh Credit Agreement bears interest at a rate of 10% per annum. The loan granted for one-year period and the principal amount of the loan will be paid at the end of the period. The amount of interest is paid monthly. The loan is guaranteed by the Group.
  As of June 30, 2017, the amount of USD $200k (CAD $260) plus accrued interest was still outstanding, it is classified as a current liability.

Corporate and Administrative:

- The Company continues to improve its accounting and administrative functions within the organization.
- During April 2017, there were 2,750,000 options granted to Zenith's officers, directors, employees and consultants. Each option entitles the holder to acquire one share for $0.15 per share for the period ending April 2022. These were also valued using the Black Scholes model. The inputs to the calculation were as follows; stock price of CAD $0.07, exercise price of CAD $0.15, volatility of 100% and a monthly risk-free rate of 0.53%.
- The Company capitalized general and administrative expenses, related to the acquisition of assets in Azerbaijan and its admission to the London Stock Exchange listing, for CAD$1,781k. (see details in note 8 of the Financial Statements.)

Subsequent event highlights:

a) On July 06, 2017, the terms of the repayment of the USD $320k (CAD $416) Credit Agreement were amended and first repayment of principal of USD $80k has been moved to the end of July.

On July 31, 2017 USD $20k (CAD $21) were repaid, and the balance of US $60k (CAD $63) will be paid on September 1, 2017.

b) On July 14, 2017 the Company entered into an agreement to proceed with a brokered private placement to raise gross proceeds of GBP 265k (approximately CDN$ 438k) through the issue of 3,533,333 new common shares of no par value in the capital of the Company at a price of £0.075 (approximately CDN$ 0.123956) per share. The Company also paid finder's fee for GBP 13k (approximately CDN$ 22k).

c) On August 2, 2017 the Company entered into an agreement to proceed with a brokered private placement to raise gross proceeds of £250k (approximately CDN$ 410k) through the issue of 3,333,333 new common shares of no par value in the capital of the Company at a price of £0.075 (approximately CDN$ 0.1230606) per share. The Company also paid finder's fee for GBP 12k (approximately CDN$ 21k).

OPERATIONAL UPDATE

ITALY

In August 2009, the Italian Ministry of Economic Development posted an invitation for bidding on three previously producing gas properties owned and operated by Eni, the Italian multinational oil and gas company. Zenith's wholly owned subsidiary, Canoel Italia S.r.l ("Canoel Italia"), participated in the bidding process for two properties and was later selected as one of the finalists for both.

On August 30, 2011, the Company announced that the Italian "Ministero per lo Sviluppo Economico" (the Ministry of Economic Development) confirmed in writing that Zenith's technical submission and proposal to re-establish production from the two properties was successful.

These two natural gas properties are in proximity to each other and are located in southern Italy, an area which is currently producing a large portion of Italian hydrocarbons. The first property, named "Torrente Vulgano", is located in the Puglia Region, while the second one, named "Canaldente", and is located in the Basilicata Region. Both properties are already connected to the Italian national gas distribution grid; therefore, there is no need to install new gas pipelines.

The Torrente Vulgano and Canaldente properties were previously produced by Eni. Before the agreement to return the field to the Ministry of Economic Development, in the last 4 years of production (1997-2000), the Torrente Vulgano property was producing an average of 7,900 standard cubic meters (m3) per day (278,949 standard cubic feet (mcf) per day, using a conversion rate of 1 m3 = 35.31 mcf).

Canoel Italia will have to comply with certain Italian regulatory obligations before field start-up. Production will commence after all the necessary approvals have been received, which the Company expects to occur by late 2017. However, there are no assurances that production of the Torrente Vulgano and Canaldente properties will be at the same levels that they were previously producing. It is worth noting that the Canaldente reservoir appears to be a good candidate for gas storage when the well will be eventually shut-in at the end of commercial production.

On August 27, 2011, Canoel Italia was approved in its role as operator by the Italian relevant authorities and is currently submitting environmental reports and conducting the final assessment of on-site equipment.

On June 6, 2013, the Company completed the acquisition of various working interests in 13 Italian producing and exploration properties from Medoilgas Italia S.P.A. and Medoilgas Civita Limited, each a subsidiary of Mediterranean Oil and Gas Plc after receiving the final approval from the Italian Ministry of Economic Development to the change of ownership.

On October 1, 2015, the Company acquired co-generation equipment and facilities which will enable the company to produce electricity from the gas produced by the Masseria Vincelli 1 well and sell it directly into the national energy grid.

The Company's share of estimated total proved plus probable natural gas net reserves were assessed at 15,366 Mmscf and condensate net reserves were assessed at 241 Mbbls as of March 31, 2017.

AZERBAIJAN

On June 8, 2015, the Company and SOCAR (State Oil Company of Azerbaijan Republic) signed a confidential memorandum of understanding ("MOU") regarding the Muraxkhanli Area. Formal approval of the MOU was subsequently granted by the President of Azerbaijan through Decree No. 1439, dated October 7, 2015 ("Presidential Decree") which authorised SOCAR to prepare and execute a Rehabilitation, Exploration, Development and Production Sharing Agreement ("REDPSA") for the Muraxhanli Area between the Company and SOCAR on behalf of the Republic of Azerbaijan.

The REDPSA was executed on March 16, 2016 between SOCAR, Zenith Aran and SOCAR Oil Affiliate ("SOA"), a 100% owned subsidiary of SOCAR. The REDPSA became effective on June 20, 2016, upon ratification by the Parliament of the Republic of Azerbaijan whereby the REDPSA and the Company's rights and obligations under the REDPSA became binding in law in Azerbaijan.

The REDPSA covers approximately 642 square kilometres and include the active Muraxkhanli, Jafarli and Zardab oil fields located in the Lower Kura Region, about 300 kilometres inland from the city of Baku, Azerbaijan. Pursuant to the REDPSA, the Company holds an 80% participating interest both the Contract Rehabilitation Area and the Contract Exploration Area; SOA holds the remaining 20% participating interest. Together, the Company and SOA will form the contractor group.

The term of the REDPSA is 25 years from the date of SOCAR's approval of the contractor's development program. The term of each Area may be extended by an additional five years at the option of SOCAR.

On June 14, 2016 the Agreement on the Rehabilitation, Exploration, Development and Production Sharing ("REDPSA") for the Area Including the Muradkhanly, Jafarli and Zardab Oil Fields in the Republic of Azerbaijan has been ratified by the Azerbaijan Parliament.

In June 2016, the Company started the operation to establish Aran Oil Operating Company Ltd., an 80% owned subsidiary of Zenith Aran, to serve as operator of the REDPSA.

On June 24, 2016, the President of the Republic of Azerbaijan signed the REDPSA into law, after the approval by Parliament on the 14th of June 2016.

On August 11, 2016 the handover of the Azerbaijan assets, physically completed in June 2016, formally completed with the necessary signatures on related documents, and the Company commenced crude oil production of approximately 275 barrels of oil per day in Azerbaijan under Zenith's ownership.

The Company's share of estimated total proved plus probable natural oil net reserves were assessed at 32,103 MSTB as of March 31, 2017.

OTHER ACTIVITIES

In addition to its activities discussed above, the Company is constantly reviewing opportunities for potential acquisition of other oil and gas producing properties in established oil production environments.

On March 30, 2017, the Company acquired a Swiss company, Altasol SA. The acquired company does not have any oil and gas assets and was purchased with the intention of developing an oil trading subsidiary of Zenith Energy Ltd.

FINANCIAL PERFORMANCE

The following table summarizes key financial indicators for the three months ended June 30:

	Three months ended June 30	
	2017	2016
Oil and gas revenue, net of royalties ($'000)	**1,540**	100
Oil and gas revenue, net of royalties – per boe ($)	**63.08**	34.16
Total daily oil and gas sales volumes per boe	**268**	32
Electricity revenue ($'000)	**127**	141
Electricity gas sales volumes per mcf ($)	**6.85**	7.68
Net income (loss) ($'000)	**691**	(617,419)
Net income (loss) per share – basic ($)	**0.01**	11.56
Net income (loss) per share – diluted ($)	**0.01**	6.49
Capital expenditures ($'000)	**-**	20
Weighted average number of shares – basic	**115,944,111**	53,429,628
Weighted average number of shares – diluted	**164,386,936**	53,429,628

Production

	Three months ended June 30	
	2017	2016
Total volumes		
Oil (bbls) (1)	**23,390**	1,161
Condensate (bbls) (3)	**223**	184
Gas (mcf) (2)	**4,790**	9,561
Total oil and gas sales volumes (boe)	**24,411**	2,939
Electricity (gas) sales volumes (mcf)	**18,547**	18,336
Total sales volumes (boe)	**27,502**	5,995
Daily volumes		
Oil (bbls/day) (1)	**257**	13
Condensate (bbls/day)	**2**	2
Gas (mcf/day)	**53**	105
Total daily oil and gas sales volumes	**268**	32
Daily gas sales volumes for electricity	**204**	201
Total daily sales volumes (boe/day)	**302**	66

- During the three months ended June 30, 2017 the Company sold 23,390 bbls of oil from its properties in Azerbaijan. This data is not comparable to the past year.

At the end of June 2017, there were 131 bbls of unsold oil production in Azerbaijan held in inventory which were sold in subsequent months. Total oil sales, transfers of produced volumes to the Termap Oil Storage and oil held in inventory at the end of the period correspond to an average daily production rate for the three months ended June 30, 2017 of 273 bbls of oil per day. The average daily production rate is not comparable with past year.

- During the three months ended June 30, 2017, the Company sold 4,790 mcf of natural gas from its Italian properties as compared 9,561 mcf of natural gas in the 2016 similar periods, with a decrease of 50%, due to the stop of the production in the Lucera and Acquasalsa concessions for urgent maintenance.
- During the three months ended June 30, 2017, the Company sold 223 bbls of condensate from its Italian properties as compared to 184 of condensate in the 2016 similar period, with an increase of 21%.
- During the three months ended June 30, 2017, the Company sold 2,522 MWh of electricity from its Italian properties as compared to 2,718 MWh of the 2016 similar period, with a decrease of 7%, due a temporary production disruption in June 2017 for maintenance of the plant.

<u>Azerbaijan Oil production</u>

On March 16, 2016, the Company's wholly-owned subsidiary, Zenith Aran, entered the REDPSA with SOCAR and SOA. The REDPSA covers 642 square kilometres which include the active Muraxkhanli, Jafarli and Zardab oil fields located in the Lower Kura Region, about 300 kilometres inland from the city of Baku (the "Azerbaijani Operations").

The delivery of the capital assets, previously used in respect of the petroleum operations at the Azerbaijani Operations, from the previous operating company to Aran Oil, was officially completed on August 11, 2016, and the production started under Zenit's ownership. The Company now has operational control of the Azerbaijani Operations. The transfer of operational control did not involve any interruption of petroleum production.

Following successful handover on August 11, 2016 production under Zenith ownership commenced at the Azeri operations. During the period from August 11 to September 30, 2016 the Company achieved a production of about 275 barrels of oil per day. Gas is also produced, but in low quantities and is used at the sites.

The Company, which is free to sell/export oil without restrictions, sells its oil through the Marketing and Operations Department of SOCAR ("SOCARMO"). A commission of 1% of total sales is payable to SOCARMO.

During the three months ended June 30, 2017 the Company sold 23,390 bbls of oil from its properties in Azerbaijan. This data is not comparable to the past year.

At the end of June 2017, there were 131 bbls of unsold oil production in Azerbaijan held in inventory which were sold in subsequent months. Total oil sales, transfers of produced volumes to the Termap Oil Storage and oil held in inventory at the end of the period correspond to an average daily production rate for the three months ended June 30, 2017 of 273 bbls of oil per day. The average daily production rate is not comparable with past year.

<u>Italy Gas Production</u>

During the three months ended June 30, 2017, the Company sold 4,790 mcf of natural gas from its Italian properties as compared 9,561 mcf of natural gas in the 2016 similar periods, with a decrease of 50%, due to the stop of the production in the Lucera and Acquasalsa concessions for urgent maintenance.

Daily gas sales volumes for electricity from Torrente Cigno per day for three months ended June 30, 2017 were respectively 204 mcf/d and 201 mcf/d.

<u>Italy Condensate Production</u>

During the three months ended June 30, 2017, the Company sold 223 bbls of condensate from its Italian properties as compared to 184 of condensate in the 2016 similar periods, with an increase of 21%.

Italy Electricity production

During the three months ended June 30, 2017, the Company sold 2,522 MWh of electricity from its Italian properties as compared to 2,718 MWh of the 2016 similar period, with a decrease of 7%, due a production disruption in June 2017 for maintenance of the plant.

The Electricity production remained steady for all the quarters since the cogeneration plant acquisition, as detailed in the following table.

Italy Electricity Production	Production MWh
I quarter 2017	2,718
II quarter 2017	2,620
III quarter 2017	2,774
IV quarter 2017	1,524
I quarter 2018	2,552

Revenues

	Three months ended June 30	
	2017	2016
Commodity Prices		
Gain Oil and gas prices		
Oil (Argentina $/bbl)	**n.a.**	63.08
Oil (Azerbaijan $/bbl)	**61.91**	n.a.
Condensate ($/bbl)	**125.56**	120.75
Gas ($/mcf)	**7.86**	0.51
Total oil and gas ($/boe)	**63.08**	34.16
Electricity ($/mcf)	**6.85**	7.68
Revenues (CAD$'000)		
Oil and gas revenue		
Oil (Argentina)	**-**	73
Oil (Azerbaijan)	**1,448**	n.a.
Condensate (Italy)	**28**	22
Other (Italy)	**27**	-
Gas (Italy)	**37**	5
Total oil and gas (CAD$)	**1,540**	100
Electricity (CAD$)	**127**	141
Total (CAD$)	**1,667**	241

Condensate Revenue

The price per bbl received for condensate during the three months ended June 30, 2017 was $125.56 per bbl as compared to $120.75 per bbl earned on condensate sales during the three months ended June 30, 2016, respectively. The condensate price per bbl in the last three months is higher in the 2017 period due to an increase in the base price of Brent crude which is used in the formulas to establish the price of condensate.

Gas Revenue

The price per mcf received for natural gas is higher in the three months ended June 30, 2017 as compared to the three months ended June 30, 2016.

In general, gas prices are also impacted by fluctuations in the base price of European gas rates which is used in the formulas to establish the price of natural gas.

Electricity Revenue

The difference in the gross revenues achieved is only for the electricity selling price that is determined by the market.

Italy Electricity Production	Production MWh	Gross Revenues	Average Price CAD$/MWH
I quarter 2017	2,718	$ 140,813	$ 51.80
II quarter 2017	2,620	$ 141,848	$ 54.14
III quarter 2017	2,774	$ 194,767	$ 70.21
IV quarter 2017	1,524	$ 96,747	$ 63.48
I quarter 2018	2,552	$ 126,710	$ 49.65

In the first quarter of the 2017 fiscal year, the selling price was lower than the previous quarters due to the lower average price collected from the market in the period. Due to necessary maintenance of the plant, production was stopped in June for 10 days.

Royalties and Operating Expenses

	Three months ended June 30 **2017**	2016
Royalties ($)	**-**	**7,500**
% of Argentine revenues [1]	**-**	**9%**
$/bbl of oil	**-**	**6.50**
$/boe (total Company)	**-**	**1.25**
Operating and transportation ($'000)		
Argentina	**-**	157
Azerbaijan	**745**	110
Italy	**158**	42
Total	**903**	309
Argentina $/bbl	**-**	135.34
Azerbaijan $/bbl	**31.85**	-
Italy $/boe	**38.42**	8.72
Total $/boe	**32.83**	51.61

[1] Royalties were charged on Argentine oil revenues only.

Royalties

No royalties are charged on Azerbaijan oil production and on Italian gas and condensate production.

Operating and transportation costs

Operating costs per boe in Italy for the three months June 30, 2017 (CAD$158k) are higher than the same period of the prior year (CAD$42) due to extraordinary maintenance in some concessions.

Netbacks

	Three months ended June 30	
	2017	2016
Argentina ($/bbl)		
Revenue	**-**	**63.08**
Royalties	**-**	**(6.50)**
Operating expenses	**-**	**(135.34)**
Field netback	**-**	**(78.76)**
Azerbaijan ($/bbl)		
Revenue	**61.90**	**-**
Operating expenses	**(31.82)**	**-**
Field netback	**30.05**	-
Italy ($/boe)		
Revenue	**53.25**	34.75
Operating expenses	**(38.42)**	(8.72)
Field netback	**14.83**	26.03
Total Company ($/boe)		
Revenue	**60.61**	43.94
Royalties	**-**	-
Operating expenses	**(32.83)**	(79.35)
Field netback	**27.78**	(35.41)

General and Administrative Expenses ("G&A")

General and administrative expenses for the three months ended June 30 are composed of the following:

	Three months ended June 30	
	2017 **CAD$'000**	2016 CAD$'000
Professional fees	**535**	58
Office	**148**	103
Administrative	**226**	65
Salaries and benefits	**348**	173
Travel	**110**	204
Capitalization of expenses	**(1,781)**	-
	(414)	603

G&A expenses increased in the three months ended June 30, 2017 versus the 2016 comparative period, due to the expenses of the employees and professional in Azerbaijan, and the payment of the expenses related to the audit that in the previous year were recorded in subsequent quarters.

Professional fees were higher in the three months ended June 30, 2017 due to business development and fundraising activities. Office expenses are higher in the three months ended June 30, 2017 than the 2016 comparative periods due to an increase in Canadian, Azerbaijan and Italian office costs. Administrative expenses and Salaries and benefits are higher in the three months ended June 30, 2017 than the comparative 2016 period due to the addition of Azerbaijan expenses.

Travel costs are lower in the three months ended June 30, 2017 due to a decrease in travel activities, particularly in relation to negotiations in Azerbaijan and the establishment of an Azerbaijan office, and for the Admission to the London Stock Exchange listing.

Capitalized expenses

On August 24, 2016, the Group announced the start of crude oil production of approximately 300 barrels of oil per day in Azerbaijan under Zenith's banner. This milestone marked the successful completion of the handover process and the transfer of operatorship to Aran Oil Operating Company, a 100% subsidiary of Zenith Energy Ltd ("Zenith Aran").

The formal handover process largely encompassed the transfer and registration of assets, including infrastructure, oil facilities, oil service vehicles and oil wells in the name of Aran Oil Operating Company.

Azerbaijan represents an unprecedented opportunity for energy development and the Directors are committed to a long-term relationship. The support of the Government and SOCAR throughout the process of establishing the Rehabilitation, Exploration, Development and Production Sharing Agreement (REDPSA) has helped the Group establish its presence. The Group now seeks to demonstrate Zenith's strengths as an operator in one of the largest and most-storied oil and gas countries in the world and have turned the Group's focus to increasing the daily production of oil from the Muradxanli, Zardab and Cafarli fields.

On January 11, 2017 Zenith Energy Ltd. announced that its entire Common Share capital, consisting of 98,564,867 Common Shares, was admitted to the standard listing segment of the Official List and to trading on the London Stock Exchange's Main Market under the ticker symbol "ZEN".

To achieve these 2 important milestones, the Company paid expenses that were recorded in past quarters and capitalised during the three months ended June 30, 2017 as follows:

	Azerbaijan Costs between Sept 2014 and Aug 2016 specific to Azerbaijan	**LSE Listing** All costs between March 2016 and March 2017 specific to LSE
Total Consulting	484	147
Total Travel	36	355
Total Legal	38	377
Total Accounting and bookkeeping	-	108
Total LSE Listing	-	236
TOTAL (CAD$'000)	**558**	**1,223**

	CAD $'000
Carrying amount at April 1, 2017	**-**
Additions	1,781
Depreciation	(89)
Foreign exchange differences	-
Carrying amount at June 30, 2017	**1,692**

Depletion and depreciation

	Three months ended June 30	
	2017	2016
	CAD$'000	CAD$'000
Argentina	**-**	10
Azerbaijan	**203**	n.a.
Italy	**32**	43
Other	**90**	-
Total	**325**	53
Argentina $/bbl	**-**	-
Azerbaijan $/bbl	**8.68**	-
Italy $/boe	**7.78**	13.36
Other $/boe	**n.a.**	n.a.
Total $/boe	**11.73**	14.40

The depletion rate for the Italian properties in the three months ended June 30, 2017 is lower than comparative 2016 period due to the lower production.

Oil production commenced in Azerbaijan during the period. There is no 2016 comparative period.

Net income (loss)

The Company reported net and net income of $691K for the three months ended June 30, 2017 versus net income of $617,419k for the three months ended June 31, 2016.

SUMMARY OF QUARTERLY INFORMATION

The following is a summary of selected financial information for the Company for the past eight quarters.

	Net revenue	**Net income (loss)**	**Per share** *
	CAD$'000	CAD$'000	$
2018			
First quarter ended June 30, 2017	1,667	691	0.01
2017			
Fourth quarter ended March 31, 2017	1,512	(47,335)	(0.41)
Third quarter ended December 31, 2016	1,924	(1,556)	(0.03)
Second quarter ended September 30, 2016	818	(1,150)	(0.02)
First quarter ended June 30, 2016	242	617,419	0.11
2016			
Fourth quarter ended March 31, 2016	251	(5,568)	(0.14)
Third quarter ended December 31, 2015	284	(889)	(0.03)
Second quarter ended September 30, 2015	525	(869)	(0.03)

The sum of quarterly amounts per share may not add to the year-to-date figure due to rounding.

- The net revenues increased in the first quarter of the 2018 fiscal year; the capitalization of general and administrative expenses, fully paid in past quarters and relating the Azerbaijan acquisition and the listing to the LSE, allow the Company to partially recover the past losses;
- The loss of the last quarter of the year ended March 31, 2017 was largely caused by Italian impairment, loss on Argentinian disposal and a revision to the valuation of the Azeri assets per the August 2016 CPR. In the Q1 statements, the assets were valued from the March 2016 CPR. All these amounts are non-cash items, and loss

is not related to the profitability of the Company.

- In the third quarter of fiscal 2017 the Company recorded the first full quarter of the oil production in Azerbaijan, which has been very consistent; in fact, the revenues of the Company are more than double than those of the last 10 quarters.
- In the second quarter of fiscal 2017, following successful handover on August 11, 2016, production under Zenith ownership commenced at the Azeri operations. Production has been relatively consistent at approximately 275 barrels per day resulting in total production of 14,010 bbls for the period and gross revenue of CAD $659,000
- Net revenues decreased in the first quarter 2017 due to a lack of oil sales in Argentina. Net loss excluding gain on business combination increased due to the decrease in net revenues combined with an increase in general and administrative expenses.
- Net revenue decreased in the fourth quarter 2016 due to a lack of oil sales in Argentina, partially offset by an increase in electricity revenue in Italy. Net loss increased due primarily to an increase in G&A expenses and inventory impairment and a $5,025k impairment related to the Company's Italian properties.
- Net revenue decreased in the third quarter ended December 31, 2015 due to a decrease in sales volumes, primarily oil sales volumes, combined with a decrease in the price earned for oil. Net loss increased due to the decrease in net revenues combined with an increase in general and administrative expenses.
- Net revenue decreased in the second quarter ended September 30, 2015 due to a decrease in sales volumes and in commodity prices for natural gas and NGLs. Net loss increased due to the decrease in net revenues combined with an increase in operating costs.

LIQUIDITY RISK AND CAPITAL RESOURCES

As at June 30, 2017 the Company has a deficit working capital of ($1,870k) (June 30, 2016 – deficit ($6,191k)), negative cash flows from operating activities from continuing operations of $1,132k (June 30, 2016 - $881k) and an accumulated surplus of $556,556k (June 30, 2016 - $603,773k).

As of June 30, 2017, the contractual cash flows, including estimated future interest, of current and non-current financial liabilities mature as follows:

	Carrying Amount	Contractual cash flow	Due on or before 30 June 2018	Due on or before 30 June 2019	Due after 30 June 2019
	CAD $'000	CAD $'000	CAD $'000	CAD $'000	CAD $'000
Trade and other payables	2.881	2.881	2.881	-	-
Loan payable	5.669	6.621	998	3.109	2.514
Bonds payable	385	423	45	378	-
Deferred consideration	484.474	1.191.428	1.544	10.076	1.179.808
	493.409	1.201.353	5.468	13.563	1.182.322

Note: the deferred consideration payable related to opportunities of development in Azerbaijan for the Company, but they are not commitments. In these amount are included all the capital expenses that, according to the CPR Reserve Report, will be paid by the Company, in the next 24 years, as investments to develop its properties in Azerbaijan.

SUBSEQUENT EVENTS

a) On July 06, 2017, the terms of the repayment of the USD $320k (CAD $416) Credit Agreement were amended and first repayment of principal of USD $80k has been moved to the end of July.

On July 31, 2017 USD $20k (CAD $21) were repaid, and the balance of US $60k (CAD $63) will be paid on September 1, 2017.

b) On July 14, 2017 the Company entered into an agreement to proceed with a brokered private placement to raise gross proceeds of GBP 265k (approximately CDN$ 438k) through the issue of 3,533,333 new common shares of no par value in the capital of the Company at a price of £0.075 (approximately CDN$ 0.123956) per share. The Company also paid finder's fee for GBP 13k (approximately CDN$ 22k).

c) On August 2, 2017 the Company entered into an agreement to proceed with a brokered private placement to raise gross proceeds of £250k (approximately CDN$ 410k) through the issue of 3,333,333 new common shares of no par value in the capital of the Company at a price of £0.075 (approximately CDN$ 0.1230606) per share. The Company also paid finder's fee for GBP 12k (approximately CDN$ 21k).

GOING CONCERN

The Group's business activities, together with facts likely to affect its future operations and financial and liquidity positions are set out in the Chairman's Statement and Strategic Report and also note 1 of the financial statements. In addition, note 22) to the financial statements discloses the Group's financial risk management policy and note 1 details out further considerations made by the Director in respect of going concern.

The Directors having made due and careful enquiry, are of the opinion that the Group has adequate working capital to execute its operations over the next 12 months. The Directors therefore have made an informed judgment, at the time of approving the financial statements, that there is a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. As a result, the Directors have adopted the going concern basis of accounting in the preparation of the annual financial statements.

SHARES AND CONVERTIBLE, EXERCISABLE AND EXCHANGEABLE SECURITIES

The Company is authorized to issue an unlimited number of common shares and an unlimited number of preferred shares issuable in series.

As at June 30, 2017 and the date of this MD&A, the Company's issued share capital and the outstanding securities that are convertible or exercisable for any voting or equity securities of the Company are as follows:

	Number of common shares	Number of warrants	Number of stock options
Balance – March 31, 2017	115,577,230	56,995,908	5,000,000
Issued	2,019,250	-	2,750,000
Options Exercised		(1,019,250)	
Expired	–	(7,533,833)	–
Balance – March 31, 2017	117,596,480	48,442,825	7.750,000
Issued	6,866,666		
Expired		(1,293,334)	
Balance – Date of MD&A	124,463,146	47,149,491	7,750,000

NUMBER OF COMMON SHARES

a) On May 25, 2017, the Group announced that following the its announcement on February 22, 2017 that a Director of the Group had exercised an option to acquire 1,000,000 new Common Shares in the capital of the Group, the Option Shares have been issued on May 23, 2017 following confirmation by Mr. Regis Milano of the custodian to whom they should be issued.

b) On June 29, 2017, an investor in the Company has exercised warrants to acquire 1,019,250 new common shares of no par value in the capital of the Company. The exercise price of the warrant was C$0.15 per share, and the total consideration received C$153k (approximately £91k).

Post Balance Sheet Event

a) On July 14, 2017 the Company entered into an agreement to proceed with a brokered private placement to raise gross proceeds of GBP 265k (approximately CDN$ 438k) through the issue of 3,533,333 new common shares of no par value in the capital of the Company at a price of £0.075 (approximately CDN$ 0.123956) per share. The Company also paid finder's fee for GBP 13k (approximately CDN$ 22k).
b) On August 2, 2017 the Company entered into an agreement to proceed with a brokered private placement to raise gross proceeds of £250k (approximately CDN$ 410k) through the issue of 3,333,333 new common shares of no par value in the capital of the Company at a price of £0.075 (approximately CDN$ 0.1230606) per share. The Company also paid finder's fee for GBP 12k (approximately CDN$ 21k).

NUMBER OF WARRANTS

As at June 30, the Group had 48,442,828 warrants outstanding (relating to 48,442,828 shares) and exercisable at a weighted average exercise price of $0.20 per share with a weighted average life remaining of 0.90 years. Subsequent to June 30, 2017 there were warrant expirations in July for no.1,293,334. These warrants had an exercise price of $0.25 per share.

NUMBER OF STOCK OPTIONS

The Group has a share option plan (the "**Plan**") for the benefit of directors, employees and consultants. The maximum number of shares available under the Plan is limited to 10% of the issued and outstanding common shares at the time of granting options. Granted options are fully vested on the date of grant, at which time all related share-based payment expense is recognised in the consolidated statements of income (loss) and comprehensive income (loss). Share options expire five years from the date of granting.

	Number of options	**Weighted average exercise price**
Balance – 31 March 2016	-	-
Granted	6,000,000	0.10
Exercised	(1,000,000)	(0.10)
Expired	-	-
Balance – 31 March 2017	5,000,000	0.10
Granted May 17, 2017	2,750,000	0.15
Balance – 30 June 2017	7,750,000	0.12

On November 18, 2016, the Group granted Options to certain of its Directors and employees to acquire a total of 6,000,000 Common Shares pursuant to its Stock Option Plan. Each Option granted entitles the relevant holder to acquire one Common Share for an exercise price of CAD $0.10 per Common Share.

The expiry date of the Options is the date falling five years from the date of grant, being 18 November 2021.

The Stock Options Plan was approved by shareholders of the Group at the Annual General Meeting held on January 20, 2017.

On February 22, 2017, the Group announced that a Director of the Group has announced the intention to exercise his stock options to purchase 1,000,000 common shares in the capital of the Group at a price of CAD$0.10 per Common Share and a total cost of CAD$100k.

On May 17, 2017, the Group granted additional Options to certain of its Directors and employees to acquire a total of 2,750,000 Common Shares pursuant to its Stock Option Plan. Each Option granted entitles the relevant holder to acquire one Common Share for an exercise price of CAD $0.15 per Common Share. The expiry date of the Options is the date falling five years from the date of grant, being May 17, 2022.

On May 25, 2017, the Group announced that following the Group's announcement on February 22, 2017 that a Director of the Company had exercised an option to acquire 1,000,000 new Common Shares in the capital of the Group, the Option Shares have been issued on May 23, 2017 following confirmation by Mr. this Director of the custodian to whom they should be issued.

RELATED PARTY TRANSACTIONS

Related party transactions are considered to be in the normal course of operations and are initially recognised at fair value. Related party transactions during the three months ended June 30, 2017 and 2016 not disclosed elsewhere in these consolidated financial statements are as follows:

a) Included in general and administrative expenses for the three months ended 30 June 2017 is CAD $41k (2016 – CAD $41k) charged by a director of the Group for administrative services. As at June 30, 2017 CAD $ nil (2016 – CAD $Nil) was included in trade and other payables in respect of these charges.

b) Included in trade and other payables is CAD $ nil (2016 – CAD $37k) due to a Director of the Group in respect of general and administrative expenditures made on behalf of the Group for which the officers and directors will be reimbursed.

c) Included in trade and other payables is CAD $ nil (2016 – CAD $30k) due a Director of the Group in respect of salaries.

OFF-BALANCE SHEET ARRANGEMENTS

The Company has not entered into any off-balance sheet financing arrangements.

OUTLOOK

As noted earlier, the Company's cash and cash equivalent balance is not sufficient to meet the Company's obligations and additional funds will have to be raised through the issuance of debt and equity financing. There is no assurance that such additional funds can be raised on reasonable terms, or at all.

The Company plans to continue to focus on both international oil and natural gas exploration opportunities as well as continuing its search for smaller producing assets in North America, Italy and Azerbaijan. Management intends to focus its efforts toward acquiring large exploration permits, which offer high exploration potential and the opportunity to act as operator.

The Company's plans for fiscal 2017 include:

(a) Italy: After the acquisition of 9 producing licenses and 4 exploration applications from Mediterranean Oil & Gas Plc., Zenith has evaluated drilling opportunities on these permits and will formalize plans to either participate directly in such potential operations or farm-out its interest to third parties. The company's technical team has conducted in depth geological, geophysical and engineering evaluations on all these properties. Natural gas from two properties which is not suitable for transportation in the national pipeline grid will now be produced to generate electricity with the use of gas turbines. New seismic data has defined a very interesting structure on the Macchia Nuova property and plans are being made to drill this prospect in the future. Drilling plans for side-track drilling operations at the Masseria Petrilli property and drilling of a new well at the San Teodoro field are also being evaluated. These activities are expected to increase Zenith's gas production in Italy.

Submission of extensive environmental reports relating to the commencement of production of the Torrente Vulgano and Canaldente gas properties has been completed and preliminary approval has been received. The Company is now looking forward to finally place on production these wells after the final approval is received. Production of natural gas from the Torrente Vulgano and Canaldente properties is now expected to commence in late 2017.

Improvements of facilities at San Teodoro will be completed by the tie-in of new dehydration equipment. While the field has been capable of production, a lack of regional infrastructure had limited additional expansion in the past. In December 2014, Zenith reached an agreement with Basengas S.r.l., a successful retail marketer of natural gas within Italy, to handle forthcoming production from this 100% owned field, which is anticipated to restart production in December 2017. Production from the existing wellbore is expected to commence at 3,000 cubic meters/day (106 mcf/d or 18 boepd), increasing Zenith's current daily production in Italy by 25%, to over 100 boepd. Costs of the refurbishment and commencing production are anticipated at €300,000 and will be paid through an equipment leasing facility.

Zenith is also evaluating the possibility of drilling a deviated well into the crestal area of the Torrente Salsola structure, where the Company has a 100% working interest, in order to unlock residual reserves. The Company has an ambitious program to enhance the Italian daily gas production rate in the Puglia Region by 100% through a technical program employing additional workovers.

Zenith is planning to implement an innovative plan for the exploitation of the Traetta 1 well in the Masseria Grottavecchia concession (20% working interest) through the sweetening of the produced gas so that it can be sold through the national pipeline grid. This development plan will be submitted to the Ministry, for its analysis and required prior approval. Approval is expected to be received in December 2017.

(b) **Azerbaijan:** On June 20, 2016, the REDPSA ("Rehabilitation, Exploration, Development and Production Sharing Agreement") for the Area in the Republic of Azerbaijan was ratified by the Parliament of the Republic of Azerbaijan and converted into an official law of the country signed by the President of the Republic of Azerbaijan. The Area covers an area of 642.4 square kilometres, and at the time of the formal finalization of the transaction the production in Azerbaijan was about 275 barrels per day of oil, having however produced significantly larger quantities in previous years. Minor quantities of natural gas are also produced and used at the site. In the subsequent months the Company has achieved an increase of production. The current production from the assets in Azerbaijan is about 295 barrels of oil per day.

The term of the REDPSA is 25 years from the date of SOCAR's approval of the contractor's development program. The term of each Area may be extended by an additional five years at the option of SOCAR.

Zenith's corporate office in Baku, the capital of Azerbaijan, is a two-and-a-half-hour drive from the operational office presently used to manage the producing fields, which are in the southern region of Azerbaijan. Azeri management familiar with the properties will initially be supplemented by new technical and operational personnel from Zenith, however the Company will also begin to actively identify international management and specialists willing to relocate to Azerbaijan as part of its strategy to grow production from the Area. Zenith Aran, the Company's wholly-owned subsidiary, will act as the operating entity for the management of the Azerbaijan oil properties.

On August 11, 2016 the handover of the Azerbaijan assets, physically completed in June 2016, was formally completed with the necessary signatures on related documents and the Company commenced crude oil production of approximately 275 barrels of oil per day in Azerbaijan under Zenith's ownership. The Company plans to evaluate the performance of key wells and will then implement a program of work-overs and facilities improvements.

The Company sells its oil through the SOCAR's Marketing and Operations Department ("SOCARMO"). A related commission of 1% of total sales is payable to SOCARMO.

Between 2017 and 2019, the Company plans to workover a total of 44 existing wells in Azerbaijan which are currently inactive or produce at low rates (< 5 STB/d) to bring rates up to 10 to 15 STB/d per well using improved technology, non-damaging fluids and optimised treatments. It is estimated that 10 wells will be worked over in 2017, 16 wells in 2018 and 18 wells in 2019. This programme has commenced using the existing workover rig in the field and the Company intends to purchase an additional modern workover rig to optimise the workover of the wells, within the next four years.

In addition to the marginal producing wells, five non-producing wells in the Maykop zone in the Zardab field in Azerbaijan are expected to be worked over in 2017 and to be returned to production once the existing wellbore and sand production issues have been resolved.

The Company intends to acquire one modern drilling rig capable of drilling 4,500m to carry out a fifteenyear drilling programme. It is anticipated that five new wells will be drilled in 2018 and ten wells in each year thereafter until the anticipated drilling programme is complete in 2032.

During the first four years of the REDPSA it is estimated that US$2,500k will be spent upgrading the gathering system and central facilities in Azerbaijan to improve safety, efficiency and handle higher production rates. During the same period, 39 active wells currently producing at marginal rates will be worked over at an estimated cost averaging $50k per well, using the existing workover rig.

It is anticipated that in 2017 five shut-in wells completed in the Maykop formation will be worked over to control sand production, at an estimated cost of US$100k per well, and returning to an increase of production at a total of 200STBl/d.

On January 24, 2017, the Company announced the signing of a well workover contract and engagement of highly experienced local drilling company to initiate and execute the workover of first two wells in the programme (M-195 and M-45).

It is envisaged that development drilling will commence in 2018 and continue until 2032. It has been estimated that each well with proved reserves will cost approximately US$4,000k. This cost will include the direct cost of materials, fuel, salaries, etc. to drill the well and an allocation for the purchase of one drilling rig, well completion and tie-in.

Proved reserves are those reserves that can be estimated, by competent professional, with a high degree of certainty to be recoverable. The estimate of the reserves is related to a given date, based on analysis of drilling, geological, geophysical and engineering data; the use of established technology, and; specified economic conditions, which are generally accepted and being reasonable, and shall be disclosed.

In addition to the costs anticipated for the wells with proved reserve, wells in the proved plus probable category have an additional allocation for the purchase and maintenance of a second drilling rig and expansion and modernisation of the field facilities.

In all 145 wells are expected to be drilled over 16 years, of which 58 of these are anticipated to be horizontal wells

CONTRACTUAL OBLIGATIONS AND COMMITMENTS

In the ordinary course of business, the Company and its subsidiaries may enter into contracts which contain indemnification provisions, such as service agreements, leasing agreements, asset purchase and sale agreements, joint venture agreements, operating agreements, and land use agreements. In such contracts, the Company may indemnify counterparties to the contracts if certain events occur. These indemnification provisions vary on an agreement by agreement basis. In some cases, there are no pre-determined amounts or limits included in the indemnification provisions and the occurrence of contingent events that will trigger payment under them is difficult to predict. Therefore, the maximum potential future amount that the Company could be required to pay cannot be estimated.

The Company subleases premises in London, UK, under an operating lease on a month to month basis which requires payments of approximately CAD$50k per annum.

BUSINESS RISKS AND UNCERTAINTIES

The Company has production operations in Azerbaijan and Italy, and focuses the majority of its activities on exploration in these countries. Some of the Company's operations and related assets are located in countries which carry a higher degree of political and economic risk.

Oil and natural gas are commodities whose prices have fluctuated widely in recent years and are determined based on world demand, supply and other factors, all of which are beyond the control of the Company.

The Company operates in the petroleum, natural gas and electricity industry which is subject to numerous risks that can affect the amount of cash flow from operating activities and the ability to grow. These risks include but are not limited to:

- Global economic uncertainty;
- Risks associated with operating in foreign jurisdictions;
- Competition with more established companies and the availability of services;
  Volatility in commodity pricing, exchange and interest rates;
- Government and regulatory risk with respect to royalty and income tax regimes;
- Operation risks that may affect the quality and recoverability of reserves;
- Geological risks associated with accessing and recovering new quantities of reserves;
- Ability to capitalize on farm-in and farm-out opportunities as they arise;
- Production risks associated with the ability to extract commercial quantities of petroleum and natural gas;
- Transportation risk with respect to the ability to transport petroleum and natural gas to market;
- Third party credit risk and the resulting ability to collect amounts owed;
- Capital markets risk and the ability to finance future growth;
- Uncertainty as to the nature of evolving environmental legislation that is likely to result in stricter standards and enforcement; and
- Environmental risk with respect to the ability to remedy spills, releases or emissions of various substances produced in association with petroleum and natural gas operations.

The Company will seek to minimize these business risks by:

- Employing management, technical staff and consultants with extensive industry experience;
- Maintaining a low-cost structure;
- Maintaining prudent financial practices;
- Controlling timing and magnitude of operating and capital costs;
- Working with established industry partners; and
- Maintaining insurance in accordance with industry standards to address the risk of liability for pollution, blow-outs, property damage, personal injury and other hazards.

OTHER

Additional information related to the Company's business and activities can be found on SEDAR at **www.sedar.com**.