Southern ENERGY

Condensed Consolidated Interim Financial Statements of

SOUTHERN ENERGY CORP.

For the three and nine months ended September 30, 2022 and 2021

(unaudited)

(US Dollars)

($000s of US Dollars)	September 30, 2022	December 31, 2021
Assets		
Current assets		
Cash and cash equivalents	$ 35,573	$ 9,622
Accounts receivable and other	5,554	2,532
Prepaid expenses and deposits	560	422
Derivative assets (Note 9)	64	46
	41,751	12,622
Property, plant and equipment (Note 3)	48,210	33,242
Right-of-use assets	239	348
Total assets	$ 90,200	$ 46,212
Liabilities and Equity		
Current liabilities		
Accounts payable and accrued liabilities	7,910	3,367
Royalties payable (Note 10)	4,853	4,480
Current portion of lease liabilities	109	128
Current portion of long-term debt (Note 5)	1,108	1,183
Derivative liabilities (Note 9)	1,910	632
	15,890	9,790
Long-term liabilities		
Convertible debentures (Note 6)	3,201	6,185
Long-term debt (Note 5)	3,350	2,429
Lease liabilities	147	233
Decommissioning provisions (Note 4)	2,915	3,762
Total liabilities	25,503	22,399
Shareholders' equity (Note 7)		
Share capital	74,453	41,018
Equity component of convertible debenture	263	497
Warrants (Note 7)	2,263	2,723
Contributed surplus	4,889	4,144
Deficit	(16,344)	(23,894)
Accumulated other comprehensive income	(827)	(675)
	64,697	23,813
Total liabilities and shareholders' equity	$ 90,200	$ 46,212

Commitments (Note 14)

(See accompanying Notes to the Condensed Consolidated Interim Financial Statements)

SOUTHERN ENERGY CORP.

Condensed Consolidated Interim Statement of Earnings & Comprehensive Income (unaudited)

($000s of US Dollars, except for per share amounts)	Three months ended September 30, 2022	Three months ended September 30, 2021 (Note 15)	Nine months ended September 30, 2022	Nine months ended September 30, 2021 (Note 15)
Revenues				
Petroleum and natural gas revenue (Note 11)	$ 19,151	$ 5,198	$ 35,387	$ 12,791
Royalties	(4,318)	(1,055)	(7,619)	(2,594)
	14,833	4,143	27,768	10,197
Expenses				
Production and operating	1,904	1,307	4,793	3,640
Transportation	36	46	107	139
Depletion, depreciation and amortization (Note 3)	1,818	925	4,095	2,894
Impairment recovery	-	(7,808)	-	(7,808)
Loss on derivatives (Note 9)	2,808	2,835	7,029	3,891
Gain on dispositions (Note 3)	-	-	(398)	(189)
Financing (Note 12)	423	455	1,259	1,418
Gain on debt retirement	-	-	-	(4,543)
General and administrative	946	684	2,953	2,012
Share-based compensation (Note 7)	704	14	782	83
Transaction costs	23	1,546	81	1,937
Gain on foreign exchange	(396)	(175)	(483)	(59)
	8,266	(171)	20,218	3,415
Total net earnings for the period	6,567	4,314	7,550	6,782
Currency translation adjustment	(144)	11	(152)	(24)
Comprehensive income for the period	$ 6,423	$ 4,325	$ 7,398	$ 6,758
Net earnings per common share (Note 8)				
Basic	$ 0.05	$ 0.10	$ 0.08	$ 0.18
Diluted	$ 0.04	$ 0.07	$ 0.07	$ 0.15

Condensed Consolidated Interim Statement of Changes in Shareholders' Equity (unaudited)

($000s of US Dollars, except share amounts)	Common Shares	Shareholders' Capital	Equity Component of Convertible Debentures	Warrants	Contributed Surplus	Deficit	Accumulated Other Comprehensive Income (Loss)	Shareholders' Equity
Balance, December 31, 2020	27,596,303	$ 29,271	$ 497	$ 1,100	$ 3,944	$(33,987)	$ (582)	$ 243
Shares issued, net	17,565,847	2,799	-	-	-	-	-	2,799
Warrants issued	-	-	-	2,074	-	-	-	2,074
Share-based compensation	-	-	-	-	83	-	-	83
Net earnings	-	-	-	-	-	6,782	-	6,782
Other comprehensive loss	-	-	-	-	-	-	(24)	(24)
Balance, September 30, 2021	45,162,150	$ 32,070	$ 497	$ 3,174	$ 4,027	$(27,205)	$ (606)	$ 11,957
Balance, December 31, 2021	78,121,858	$ 41,018	$ 497	$ 2,723	$ 4,144	$(23,894)	$ (675)	$ 23,813
Shares issued, net	57,786,927	33,435	(234)	(460)	-	-	-	32,741
Share-based compensation	-	-	-	-	745	-	-	745
Net earnings	-	-	-	-	-	7,550	-	7,550
Other comprehensive income	-	-	-	-	-	-	(152)	(152)
Balance, September 30, 2022	135,908,785	$ 74,453	$ 263	$ 2,263	$ 4,889	$(16,344)	$ (827)	$ 64,697

(See accompanying Notes to the Condensed Consolidated Interim Financial Statements)

SOUTHERN ENERGY CORP.

Condensed Consolidated Interim Statement of Cash Flows (unaudited)

($000s of US Dollars)	Three months ended September 30, 2022	Three months ended September 30, 2021 (Note 15)	Nine months ended September 30, 2022	Nine months ended September 30, 2021 (Note 15)
Operating activities				
Total net earnings for the period	$ 6,567	$ 4,314	$ 7,550	$ 6,782
Changes in non-cash items:				
Depletion, depreciation and amortization (Note 3)	1,818	925	4,095	2,894
Impairment recovery	-	(7,808)	-	(7,808)
Gain on dispositions (Note 3)	-	-	(398)	(189)
Financing expense	423	455	1,259	1,418
Gain on debt retirement	-	-	-	(4,543)
Unrealized (gain) loss on derivatives (Note 9)	(885)	2,090	1,260	2,856
Unrealized gain on foreign exchange	(354)	(175)	(451)	(59)
Share-based compensation (Note 7)	704	14	782	83
Decommissioning provisions liabilities settled (Note 4)	(4)	(25)	(27)	(25)
Changes in non-cash working capital	2,567	302	271	(17)
Net cash provided by operating activities	10,836	92	14,341	1,392
Investing activities				
Capital expenditures	(3,240)	(714)	(20,216)	(807)
Proceeds from dispositions (Note 3)	-	-	759	186
Changes in non-cash working capital	(2,827)	498	1,661	451
Net cash used by investing activities	(6,067)	(216)	(17,796)	(170)
Financing activities				
Proceeds from share issuances, net	28,286	-	29,952	4,014
Paydown of long-term debt (Note 5)	(1,669)	(548)	(3,409)	(9,332)
Draw on credit facility (Note 5)	-	500	4,000	6,000
Payment of interest	(209)	(176)	(848)	(692)
Finance lease payments	(26)	(37)	(111)	(190)
Transaction costs on debt refinance	(18)	(17)	(21)	(667)
Changes in non-cash working capital	45	(150)	(79)	(189)
Net cash provided (used) by financing activities	26,409	(428)	29,484	(1,056)
Net increase (decrease) in cash and cash equivalents	31,178	(552)	26,029	166
Effect of foreign exchange rate changes	(70)	(1)	(78)	9
Cash and cash equivalents, beginning of period	4,465	1,638	9,622	910
Cash and cash equivalents, end of period	$ 35,573	$ 1,085	$ 35,573	$ 1,085

(See accompanying Notes to the Condensed Consolidated Interim Financial Statements)

1. Reporting Entity and Nature of Operations

Southern Energy Corp. ("Southern" or "Company") is an oil and natural gas exploration and production company. Southern has a primary focus on acquiring and developing conventional natural gas and light oil resources in the Southeast Gulf States of Mississippi, Louisiana, and East Texas.

On December 22, 2021, the Company completed the consolidation of the common shares ("Common Shares") on the basis of one post-consolidated Common Share for every eight pre-consolidation Common Shares (the "Consolidation"). The number of Common Shares, purchase warrants, units and share based rewards have been adjusted retrospectively to reflect the 8:1 share consolidation.

Southern's head office is located in Calgary, Alberta, Canada. Southern trades on the TSX Venture Exchange ("TSXV") under the trading symbol "SOU" and on the AIM market of the London Stock Exchange plc ("AIM") under the trading symbol "SOUC". The condensed consolidated interim financial statements were authorized for issue by the Board of Directors on November 22, 2022.

2. Basis of Presentation

a) Principles of Reporting and Consolidation

The condensed consolidated interim financial statements of Southern include the accounts of all domestic and foreign subsidiaries. Wholly-owned subsidiaries included in the Company's accounts include Southern Energy Corp., Southern Energy Corp (Delaware), Southern Energy Operating, LLC, Southern Energy CMS, LLC, Southern Energy LA, LLC and Southern Energy BWB, LLC. Southern accounts for joint operations by recognizing the Company's share of assets, liabilities, income and expenses. All intercompany balances and transactions have been eliminated.

These condensed consolidated interim financial statements have been prepared in accordance with IAS 34 – Interim Financial Reporting of the International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). The condensed consolidated interim financial statements use the accounting policies which the Company applied in its annual consolidated financial statements for the year ended December 31, 2021, with the exception of the changes in accounting policies described below. These condensed consolidated interim financial statements should be read in conjunction with Southern's consolidated financial statements for the year ended December 31, 2021, which are available on SEDAR at www.sedar.com or on Southern's website at www.southernenergycorp.com. These condensed consolidated interim financial statements are presented in United States dollars ("US dollars"). All financial information presented has been rounded to the nearest thousand unless otherwise indicated.

The Company's presentation currency is the US dollar. The functional currency of the parent company is the Canadian dollar, and its results and balance sheet items are translated to US dollars for the purposes of these condensed consolidated interim financial statements, in accordance with the Company's foreign currency translation accounting policy. The functional currency of the Company's foreign subsidiaries is the US dollar.

b) Presentation and Functional Currency

In the fourth quarter of 2021, the Company elected to change its presentation currency from Canadian dollars to US dollars. The change in presentation currency is to better reflect the Company's business activities and to improve investors' ability to compare the Company's financial results with other similar publicly traded businesses in the oil and gas industry. In making this voluntary change to the US dollar presentation currency, the Company followed the guidance in IAS 21 *The Effects of Changes in Foreign Exchange Rates* and have applied the change retrospectively as if the new presentation currency had always been the Company's presentation currency. In accordance with IAS 21, the financial statements for all years and periods presented have been translated to the new US dollar presentation currency. For the 2021 comparative balances prior to Q4 2021, assets and liabilities have been translated into the presentation currency (US dollars) at the rate of exchange prevailing at the reporting date and shareholders equity using the exchange rate at the date of transactions. The Condensed Consolidated Interim Statement of Earnings and Comprehensive Income were translated at the average exchange rates for the reporting period, or at the exchange rates prevailing at the date of transactions if the individual transaction was material. Exchange differences arising on translation were taken to the foreign currency translation reserve in shareholders' equity. See Note 15 "*Change in Presentation Currency*" for more information on the impact of the change in presentation currency.

c) Recently Announced Accounting Pronouncements

Amendments to IAS 37 – Provisions, Contingent Liabilities and Contingent Assets

Southern adopted the amendments to IAS 37, Provisions, Contingent Liabilities and Contingent Assets effective January 1, 2022. The amendments clarify that the 'costs of fulfilling a contract' when assessing whether a contract is onerous comprise both the incremental costs and an allocation of other costs that relate directly to fulfilling the contract. The amendments apply to contracts existing at the date when the amendments are first applied. On adoption of this amendment, there is no impact to the Company's condensed consolidated interim financial statements.

Amendments to IAS 1 – Presentation of Financial Statements

In October 2022, the IASB issued amendments to IAS 1, Presentation of Financial Statements, related to *Non-current Liabilities with Covenants*. These amendments are effective for annual reporting periods beginning on or after January 1, 2024 retrospectively in accordance with IAS 8. The amendments clarify that an entity classifies liabilities as current if it does not have the right at the end of the reporting period to defer settlement of the liability for at least twelve months after the reporting period. Southern is in the process of reviewing the amendments but does not anticipate any changes to the presentation of the Statement of Financial Position at this time.

Amounts in ($000s of US Dollars), except for per share amounts

3. Property, Plant and Equipment

The following table presents the reconciliation of the beginning and ending amounts of our PP&E balances including accumulated depletion, depreciation, amortization and impairment:

	Oil and Natural Gas Assets	Other	Total
Net book value as at December 31, 2021	**$ 33,195**	**$ 47**	**$ 33,242**
Additions	20,050	184	20,234
Dispositions	(366)	-	(366)
Change in decommissioning provision (Note 4)	(893)	-	(893)
Depletion, depreciation and amortization	(3,975)	(32)	(4,007)
Net book value as at September 30, 2022	**$ 48,011**	**$ 199**	**$ 48,210**

Additions

For the three and nine months ended September 30, 2022, Southern incurred $3.2 million and $20.0 million of capital additions, respectively, related to the Central Mississippi CGU (“CMS CGU”).

Dispositions

On February 1, 2022, Southern disposed of all its properties in the Smackover CGU (“SO CGU”) for net proceeds of $0.8 million. Southern recorded a gain on sale of $0.4 million related to the disposition.

Depletion and depreciation

For the three and nine months ended September 30, 2022, the Company recorded depletion expense of $1.8 million and $4.0 million, respectively. In the calculation of depletion expense an estimated $65.8 million of future development costs associated with the proven plus probable reserves were included.

Impairment

At the end of each reporting period, the Company performs an assessment to determine whether there are any indications of impairment for the CGUs that comprise oil and natural gas properties. At September 30, 2022, Southern did not identify any indicators of impairment for any of its CGUs.

Amounts in ($000s of US Dollars), except for per share amounts

4. Decommissioning Provisions

The following table presents the reconciliation of the beginning and ending aggregate carrying amounts of legal obligations associated with the retirement of property, plant and equipment:

	Total
Balance as at December 31, 2021	**$ 3,762**
Liabilities incurred	18
Liabilities settled	(27)
Changes in estimates	(893)
Accretion expense	60
Property disposal	(5)
Balance as at September 30, 2022	**$ 2,915**
Long term liability	**$ 2,915**

The Company's decommissioning provisions result from its ownership interest in petroleum and natural gas assets including well sites, gathering systems and processing facilities. The total decommissioning provision is estimated based on the Company's net ownership interest in all wells and facilities, estimated costs to reclaim and abandon these wells and facilities and the estimated timing of the costs to be incurred in future years. The total estimated, inflated undiscounted risked cash flows required to settle the provision, is approximately $5.0 million at September 30, 2022 ($4.3 million at December 31, 2021), which was inflated using a rate of 2.4% (December 31, 2021 – 2.3%) and discounted using a risk-free interest rate of 3.8% at September 30, 2022 (December 31, 2021 – 1.5%).

5. Long-term Debt

Southern had the following long-term debt obligations outstanding as at the dates indicated:

	As at Sep 30, 2022	As at Dec 31, 2021
Current Portion senior secured term loan	$ 1,340	$ 1,582
Long-term portion of the senior secured term loan	3,795	2,961
Unamortized transaction costs	(677)	(931)
Total Long-Term Debt	**$ 4,458**	**$ 3,612**

Southern Energy Corp. (Delaware), one of the wholly-owned subsidiaries of Southern, held the existing senior secured term loan ("Credit Facility") at September 30, 2022. The Credit Facility is comprised of Tranche A of $5.5 million that was advanced at closing on April 30, 2021 and effective September 1, 2022, Tranche B of $29.5 million ($4.5 million drawn as of September 30, 2022) with an availability until September 30, 2023. Interest on the Credit Facility is 12% per annum on amounts outstanding and includes a 1% per annum standby fee on the unused portion of Tranche B, both paid monthly in arrears on the last day of the month. The Credit Facility is secured against the oil and gas properties of Southern and matures on August 31, 2025. As at September 30, 2022, Southern had $5.1 million drawn on the Credit Facility.

Amounts in ($000s of US Dollars), except for per share amounts

In Q2 2022, the Company entered into amending agreements to the Credit Facility:

- on April 8, 2022 to increase Tranche B to $4.5 million and extend the availability to June 30, 2022 from April 30, 2022; and
- on May 2, 2022 to increase flexibility in payment of interest of the convertible debentures.

Effective September 1, 2022, Southern entered into the fourth amendment to the Credit Facility (the "Fourth Amendment"). The Fourth Amendment includes an increase of $25.0 million to Tranche B of the Credit Facility, with a maximum draw of $10.0 million in any rolling sixty-day period, and an extension of the commitment period and maturity of the Credit Facility to September 30, 2023 and August 31, 2025 for Tranche A and Tranche B, respectively.

In addition, quarterly positive free cash flow ("FCF") (as described below) repayments that were 50% of the previous quarter's FCF are now replaced by a quarterly FCF grid whereby quarterly repayments are X% of the preceding quarter where X is equal to 50% if the ACR (as defined below) is < 3.0x or DSCR (as defined below) is < 1.4x; or X is equal to 0% if the ACR is > 5.0x and DSCR >1.7x; otherwise is 25%. A standby fee of 1.0% per annum on any undrawn Tranche B amounts.

The Credit Facility includes a monthly repayment of the principal amount outstanding computed as the sum of: (a) outstanding amount multiplied by 1/A, where A equals the number of whole or part months remaining to the maturity date plus 12 months; and (b) on the last day of the second month following each fiscal quarter, the amount determined by the FCF grid (as described above). FCF is calculated as Earnings Before Interest, Taxes, Depreciation, Amortization, and Impairment ("EBITDAX"), less the aggregate of the Credit Facility principal and interest payments.

Below are the financial covenant calculations for the Credit Facility for September 30, 2022 and December 31, 2021:

Financial covenant	**Limit**	**As at Sep 30, 2022**	**As at Dec 31, 2021**
Asset Coverage ratio	Minimum 2.00	11.84	6.55
Debt Service Coverage ratio	Minimum 1.25	2.61	1.73

The asset coverage ratio ("ACR") of at least 2:1 is calculated as the ratio of the net present value of proved developed producing oil and gas properties as determined by an independent qualified engineer, using a price deck based on the forward commodity prices, discounted at 12% to the principle amount outstanding under the Credit Facility.

The debt service coverage ratio ("DSCR") of greater than 1.25:1 is the ratio of EBITDAX to scheduled principal payments and interest expense.

As at September 30, 2022, Southern was in compliance with the above covenants.

Amounts in ($000s of US Dollars), except for per share amounts

6. Convertible Debentures

	Number of Convertible Debentures	Liability Component	Equity Component
Balance at December 31, 2021	8,389	$ 6,185	$ 497
Conversion of debentures	(3,792)	(2,789)	(234)
Accretion of discount	-	95	-
Effect of foreign exchange rate changes	-	(290)	-
Balance at September 30, 2022	**4,597**	**$ 3,201**	**$ 263**

During the nine months ending September 30, 2022, 4.7 million Common Shares were issued to satisfy the convertible debenture rights of 3,792 convertible debentures at a price of CAD$0.80 per Common Share.

7. Shareholders' Equity

Share Capital

The authorized share capital of the Company consists of an unlimited number of voting Common Shares and an unlimited number of preferred shares.

The following table reflects the Company's outstanding Common Shares at September 30, 2022 and December 31, 2021:

	Number of Shares	**Share Capital**
Balance as at December 31, 2021	78,121,858	$ 41,018
July issuance of common shares by offering	46,371,927	30,715
Issuance of common shares to satisfy unit warrant exercise	5,425,000	1,710
Issuance of common shares to satisfy conversion of convertible debentures	4,740,000	3,023
Issuance of common shares to satisfy bonus warrant exercise	1,250,000	490
Share issuance costs	-	(2,503)
Balance as at September 30, 2022	**135,908,785**	**$ 74,453**

Southern closed an equity financing on July 7, 2022, raising aggregate gross proceeds of $31.0 million through the issuance of a total of 46,371,927 Common Shares (the "Offering"), of which $17.5 million was raised pursuant to a bought deal prospectus offering of 26.1 million Common Shares at a price of CAD$0.87 per Common Share and the remaining $13.5 million was raised pursuant to an accelerated bookbuild of 20.3 million Common Shares at a price of 54.5 pence per Common Share.

Subsequent to September 30, 2022, 1,431,250 Common Shares were issued related to the exercise of Common Share purchase warrants ("Unit Warrant") at a price of CAD$0.32 from the April 2021 non-brokered private placement for proceeds of CAD$0.5 million.

Subsequent to September 30, 2022, 388,750 Common Shares were issued to satisfy the convertible debenture conversion rights of 311 convertible debentures at a price of CAD$0.80 per Common Share.

Amounts in ($000s of US Dollars), except for per share amounts

Warrants

As at September 30, 2022, 5,587,500 Unit Warrants had been exercised at a price of CAD$0.32 for proceeds of CAD$1.8 million. There are 11,490,625 remaining Unit Warrants with an expiry date of April 30, 2023.

As at September 30, 2022, 1,250,000 purchase warrants ("Bonus Warrant") issued with the closing of the Credit Facility in April 2021 were exercised at a price of CAD$0.40 for proceeds of CAD$0.5 million. There are 3,906,250 remaining Bonus Warrants with an expiry date on the earlier of: (a) a liquidity event resulting in the sale of Southern Energy Corporation (Delaware); or (b) April 30, 2024.

As at September 30, 2022, 2,413,333 performance-based Common Share purchase warrants ("Performance Warrants") had vested as the 20-day volume weighted average trading price ("Market Price") of the Common Shares had exceeded CAD$1.20. The Performance Warrants have an exercise price of CAD$0.80.

On April 21, 2022, an amendment was adopted by the Board to the acceleration provisions of the 7,240,000 Performance Warrants issued in 2018. Pursuant to such amendment, the Performance Warrants vest and become exercisable as to one-third upon the Market Price equaling or exceeding CAD$1.20, an additional one-third upon the Market Price equaling or exceeding CAD$1.35 and a final one-third upon the Market Price equaling or exceeding CAD$1.50. In addition, in the event the Market Price equals or exceeds CAD$1.65, each Performance Warrant shall be exercisable for 1.5 Common Shares, provided that, at the time of exercise in respect of the additional 0.5 of a Common Share per Performance Warrant, the Common Shares are listed on the facilities of a recognized stock exchange (other than the TSXV) or the Common Shares are acquired for cash or for the securities of a company listed on a recognized stock exchange (other than the TSXV). These acceleration thresholds were previously set at CAD$1.20, CAD$1.60, CAD$2.00, and CAD$3.20, respectively, prior to the amendments that were adopted by the Board.

Share Awards Incentive Plan

The following table reflects the Company's outstanding common stock options at September 30, 2022 and December 31, 2021:

	Number of stock options	**Weighted average exercise price (CAD)**
Balance at December 31, 2021	3,628,125	$ 0.71
Granted	4,000,000	1.01
Balance at September 30, 2022	**7,628,125**	**$ 0.87**

The following table summarizes information regarding stock options outstanding as at September 30, 2022:

Exercise Price ($CAD/share)	Number of options outstanding (000s)	Weighted average remaining terms (years)	Weighted average exercise price for options outstanding ($CAD/share)	Number of options exercisable (000s)	Weighted average exercise price for options exercisable ($CAD/share)
$0.56 - $1.01	**7,628**	**4.0**	**$0.87**	**4,009**	**$0.84**

On September 12, 2022, Southern granted 4.0 million stock options that expire in five years and are exercisable at a price of CAD$1.01 per Common Share. The stock options vest as to one third on grant date and on third on each of the first and second anniversaries of the grant day. The fair value of the September 12, 2022, stock option grant was estimated on the date of grant using the Black-Scholes pricing model with the following assumptions:

	2022
Risk free interest rate	3.164%
Expected volatility	78%
Expected life	5.0 years
Dividend yield	nil
Expected forfeiture rate	10%
Stock price on grant date (CAD)	$1.010
Fair value per option (CAD)	$0.588

Southern recognized $0.7 million of share-based compensation expense relating to stock options during the three and nine months ended September 30, 2022.

On September 12, 2022, Southern issued 2.5 million restricted share awards ("RSAs") under its Share Award Incentive Plan. The RSAs vest as to one third on each of the first, second and third anniversaries of the grant date. On the vesting dates of such RSAs, the holder is entitled to receive a cash payment or its equivalent in fully paid Common Shares, at the Company's discretion, equal to the closing market value per Common Share on the TSXV on the business day prior to such payment. For the purpose of calculation share-based compensation, the fair value of the RSAs is based on the market value of Southern's Common Shares at each period end. The fair value is recognised as share-based compensation over the vesting period. Fluctuations in fair values are recognized as share-based compensation in the period they occur. Southern recognized $44 thousand of share-based compensation expense relating to the RSAs during the three and nine months ended September 30, 2022.

Amounts in ($000s of US Dollars), except for per share amounts

8. Earnings Per Share

The following table presents the Company's net earnings per share:

	Three months ended September 30,		Nine months ended September 30,	
	2022	2021	2022	2021
Net earnings	$ 6,567	$ 4,314	$ 7,550	$ 6,782
Dilutive impact of convertible debentures	71	130	308	503
Diluted net earnings	$ 6,638	$ 4,444	$ 7,858	$ 7,285
Basic - weighted average common shares outstanding	132,822,050	45,087,913	98,292,661	37,306,891
Dilutive impact on common shares outstanding	15,818,837	19,605,788	10,378,545	12,589,280
Diluted – weighted average common shares outstanding	148,640,887	64,693,701	108,671,206	49,896,171
Net earnings per share, basic	$ 0.05	$ 0.10	$ 0.08	$ 0.18
Net earnings per share, diluted	$ 0.04	$ 0.07	$ 0.07	$ 0.15

The calculation of diluted earnings per share for the three and nine months ended September 30, 2022, include the effect of the Unit Warrants, Bonus Warrants issued as part of the Credit Facility, options, Performance Warrants and the convertible debentures.

9. Financial Instruments and Financial Risk Management

Financial Derivative Contracts

Southern utilizes oil and natural gas derivative contracts to mitigate its exposure to commodity price risk associated with future oil and natural gas production. Typical derivative contracts could consist of options, in the form of price floors, collars or three-way collars and fixed-price swaps. The derivative financial instruments are recorded on the condensed consolidated interim statement of financial position as either an asset or a liability measured at fair value. Southern does not apply hedge accounting to its commodity derivative contracts; accordingly, changes in the fair value of these instruments are recognized in the condensed consolidated interim statement of loss and comprehensive loss in the period of change.

Amounts in ($000s of US Dollars), except for per share amounts

Southern had the following commodity derivative contracts in place as at September 30, 2022:

Natural Gas	Volume	Pricing
Fixed Price Swap		
October 1, 2022 – December 31, 2022	4,000 MMBtu/d	NYMEX – HH $3.100/MMBtu
October 1, 2022 – December 31, 2022	2,000 MMBtu/d	NYMEX – HH $4.610/MMBtu
Costless Collar		
November 1, 2022 – March 31, 2023	2,000 MMBtu/d	NYMEX – HH $3.50 - $20.00/MMBtu
Fixed Basis Swap		
October 1, 2022 – December 31, 2022	8,000 MMBtu/d	NYMEX – HH + $0.270/MMBtu

Financial Derivative Contracts Financial Statement Recognition

The Company's financial instruments that were accounted for at fair value as of September 30, 2022 and December 31, 2021 are presented below. The classification within the fair value hierarchy for these financial instruments is Level 2.

Comprised of:	As at Sep 30, 2022	As at Dec 31, 2021
Current derivative asset	$ 64	$ 46
Current derivative liability	(1,910)	(632)
Net fair value of contracts, end of period	**$ (1,846)**	**$ (586)**

Below is a reconciliation of the loss on derivatives from the condensed consolidated interim statement of earnings and comprehensive income:

	Three months ended September 30,		Nine months ended September 30,	
	2022	2021	2022	2021
Realized loss on derivatives	$ 3,693	$ 745	$ 5,769	$ 1,035
Unrealized (gain) loss on derivatives	(885)	2,090	1,260	2,856
Loss on derivative instruments	**$ 2,808**	**$ 2,835**	**$ 7,029**	**$ 3,891**

Credit Risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations.

The carrying amount of the Company's cash and cash equivalents and accounts receivable and the positive fair value of any financial derivatives represent the maximum credit exposure.

Cash and cash equivalents

The Company manages the credit exposure related to cash and cash equivalents by selecting financial institutions with high credit ratings and monitors all short-term deposits to ensure an adequate rate of return. Given these credit ratings, management does not expect any counterparty to fail to meet its obligations.

Accounts receivable

Substantially all of the Company's accounts receivable are due from purchasers of the Company's petroleum and natural gas production, joint interest partners and government agencies, and are subject to normal industry credit risk.

Significant changes in industry conditions and risks that negatively impact partners' ability to generate cash flow will increase the risk of not collecting receivables. Management of the Company believes the risk is mitigated by the size and reputation of the companies to which they extend credit.

Southern had no provision for doubtful accounts as at September 30, 2022 or December 31, 2021.

Liquidity Risk

Liquidity risk arises through excess financial obligations due over available financial assets at any point in time. The Company's objective in managing liquidity risk is to maintain sufficient capital in order to meet its current and future liquidity requirements. The financial liabilities in the statement of financial position consist of accounts payable, royalties payable, lease liabilities, financial derivative liabilities, convertible debentures and the senior secured term loan. Strategies to manage liquidity include, having adequate sources of financing available through its Credit Facilities, estimating future cash flows generated from operations based on reasonable production and pricing assumptions, adding additional commodity derivative contracts, reducing capital spending and utilizing equity to settle interest payments on Convertible Debentures. Southern may also consider sale of non-core oil and gas assets along with alternative sources of financing.

Market Risk

Market risk is the risk that changes in market prices relating to currency, commodity prices and interest rates will affect the Company's net earnings, future cash flows, the value of financial instruments, or the fair value of its asset and liabilities. The object of market risk management is to manage and control market risk exposure within acceptable parameters.

To partially mitigate exposure to commodity price risk, Southern entered into various financial derivative instruments. The instruments currently outstanding are described above. As at September 30, 2022, a 10% change in future commodity prices applied against these contracts would have a $0.4 million impact on net income.

Amounts in ($000s of US Dollars), except for per share amounts

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in interest rates. This risk is mitigated as the Credit Facility has a fixed interest rate.

10. Royalties Payable

As at September 30, 2022, Southern had $4.9 million ($4.5 million at December 31, 2021) of non-interest bearing royalty payables related to unresolved title or ownership issues. The royalty payable account is made up of balances due to approximately 5,000 royalty holders with over 95% of the balances outstanding for greater than 120 days. The royalty holders have deficiencies with their accounts that precludes Southern from making payments.

11. Oil and Natural Gas Sales

The following table presents Southern's oil and natural gas sales disaggregated by revenue source:

	Three months ended September 30,		Nine months ended September 30,	
Commodity sales from production, by product	**2022**	**2021**	**2022**	**2021**
Crude oil	$ 998	$ 930	$ 3,181	$ 2,505
Natural gas liquids	78	98	244	256
Natural gas	18,075	4,170	31,962	10,030
Total Oil and Natural Gas Sales	**$ 19,151**	**$ 5,198**	**$ 35,387**	**$ 12,791**

12. Financing

The following table presents a breakdown of Southern's financing expenses:

	Three months ended September 30,		Nine months ended September 30,	
	2022	**2021**	**2022**	**2021**
Bank debt interest	$ 209	$ 161	$ 474	$ 511
Convertible debentures interest	71	134	305	401
Accretion	134	148	451	483
Interest on lease obligations	9	12	29	23
Total Financing Expenses	**$ 423**	**$ 455**	**$ 1,259**	**$ 1,418**

13. Capital Risk Management

The Company monitors its capital based on projected cash flow from operations and anticipated capital expenditures. In order to manage its capital structure, the Company prepares annual capital expenditure and operating budgets, which are updated as necessary. The annual and updated budgets are prepared by the Company's management and approved by or reviewed with the Company's Board of Directors. The budget results are regularly reviewed and updated as required.

In order to maintain or adjust the capital structure, the Company may issue shares, seek debt financing and adjust its capital spending to manage its current and projected capital structure. The Company's ability to raise additional debt or equity financing is impacted by external conditions, including future commodity prices and global economic conditions. The Company continually monitors business conditions including changes in economic conditions, the risk of its drilling programs, forecasted commodity prices, and potential corporate or asset acquisitions.

14. Commitments

In Q3 2022, Southern entered into capital commitments for a drilling rig that includes an early termination fee if terminated by Southern to a maximum of $0.9 million.

15. Change in Presentation Currency

The impact of the change in presentation currency (see Note 2 "*Basis of Presentation – Presentation and Functional Currency*" for more information) on the condensed consolidated interim financial statements is as follows:

Restated Condensed Consolidated Interim Statement of Earnings and Comprehensive Income:

($000s, except for per share amounts)	**Three months ended September 30, 2021 (CAD)**	**Three months ended September 30, 2021 (Restated)**	**Nine months ended September 30, 2021 (CAD)**	**Nine months ended September 30, 2021 (Restated)**
Revenues				
Petroleum and natural gas revenue	$ 6,550	$ 5,198	$ 16,022	$ 12,791
Royalties	(1,329)	(1,055)	(3,248)	(2,594)
	5,221	4,143	12,774	10,197
Expenses				
Production and operating	1,647	1,307	4,555	3,640
Transportation	58	46	174	139
Depletion, depreciation and amortization	1,165	925	3,621	2,894
Impairment recovery	(9,950)	(7,808)	(9,950)	(7,808)
Loss on derivatives	3,572	2,835	4,874	3,891
Gain on dispositions	-	-	(232)	(189)
Financing	573	455	1,775	1,418
Gain on debt retirement	-	-	(5,679)	(4,543)
General and administrative	862	684	2,518	2,012
Share-based compensation	18	14	104	83
Transaction costs	1,948	1,546	2,430	1,937
Loss on foreign exchange	(221)	(175)	(75)	(59)
	(328)	(171)	4,115	3,415
Total net earnings for the period	5,549	4,314	8,659	6,782
Currency translation adjustment	224	11	169	(24)
Comprehensive income for the period	$ 5,773	$ 4,325	$ 8,828	$ 6,758
Net earnings per common share				
Basic	$ 0.12	$ 0.10	$ 0.23	$ 0.18
Diluted	$ 0.09	$ 0.07	$ 0.19	$ 0.15

Amounts in ($000s of US Dollars), except for per share amounts

Restated Condensed Consolidated Interim Statement of Cash Flows:

	Three months ended September 30, 2021		Nine months ended September 30, 2021	
	(CAD)	(Restated)	(CAD)	(Restated)
Operating activities				
Total net earnings for the period	$ 5,549	$ 4,314	$ 8,659	$ 6,782
Changes in non-cash items:				
Depletion, depreciation and amortization	1,165	925	3,621	2,894
Impairment recovery	(9,950)	(7,808)	(9,950)	(7,808)
Gain on dispositions	-	-	(232)	(189)
Financing expense	573	455	1,775	1,418
Gain on debt retirement	-	-	(5,679)	(4,543)
Unrealized loss on derivatives	2,633	2,090	3,575	2,856
Unrealized loss on foreign exchange	(221)	(175)	(75)	(59)
Share-based compensation	18	14	104	83
Decommissioning provisions liabilities settled	(31)	(25)	(31)	(25)
Changes in non-cash working capital	385	302	(14)	(17)
Net cash provided by operating activities	121	92	1,753	1,392
Investing activities				
Capital expenditures	(900)	(714)	(1,016)	(807)
Proceeds from dispositions	-	-	232	186
Changes in non-cash working capital	635	498	576	451
Net cash provided by investing activities	(265)	(216)	(208)	(170)
Financing activities				
Proceeds from share issuances, net	-	-	4,931	4,014
Repayment of long-term debt	(690)	(548)	(11,499)	(9,332)
Draw on credit facility	628	500	7,385	6,000
Payment of interest	(222)	(176)	(863)	(692)
Finance lease payments	(46)	(37)	(237)	(190)
Transaction costs on debt refinance	(22)	(17)	(820)	(667)
Changes in non-cash working capital	(191)	(150)	(236)	(189)
Net cash used by financing activities	(543)	(428)	(1,339)	(1,056)
Net increase in cash and cash equivalents	(687)	(552)	206	166
Effect of foreign exchange rate changes	39	(1)	18	9
Cash and cash equivalents, beginning of period	2,030	1,638	1,158	910
Cash and cash equivalents, end of period	$ 1,382	$ 1,085	$ 1,382	$ 1,085