TERRACE ENERGY CORP.
(the "Company", "Corporation" or "Terrace")
MANAGEMENT'S DISCUSSION AND ANALYSIS
OF THE COMPANY'S FINANCIAL CONDITION AND RESULTS OF OPERATIONS
FOR THE YEAR ENDED JANUARY 31, 2020 AND 2019*

As of May 29, 2020

Introduction

The following management discussion and analysis of the financial condition and results of operations ("MD&A") of the Company has been prepared by management, in accordance with the requirements of National Instrument 51-102 as at May 29, 2020 and should be read in conjunction with the audited consolidated financial statements for the years ended January 31, 2020 and 2019 and the related notes contained therein, which have been prepared under International Financial Reporting Standards ("IFRS"). The information contained herein is not a substitute for detailed investigation or analysis on any particular issue and is not intended to be a comprehensive review of all matters and developments concerning the Company. Additional information relevant to the Company's activities including the appraisal report on proved and probable reserves can be found on SEDAR at www.sedar.com and the Company's website at www.terraceenergy.net.

All financial information in this report has been prepared in accordance with IFRS and all monetary amounts referred to herein, are in United States dollars, unless otherwise stated.

Caution Regarding Use of Barrels of Oil Equivalent (BOEs)

BOEs/boes may be misleading, particularly if used in isolation. A BOE conversion ratio of six (6) Mcf to one (1) bbl is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. As the value ratio between natural gas and crude oil based on the current prices of natural gas and crude oil is significantly different from the energy equivalency of 6:1, utilizing a conversion on a 6:1 basis may be misleading as an indication of value.

Cautionary Statement Regarding Forward Looking Statements

This discussion and analysis contains "forward-looking information" and "forward-looking statements" within the meaning of applicable Canadian securities laws and the United States Private Securities Litigation Reform Act of 1995, respectively (together, "forward-looking information"), concerning the Corporation's plans for its projects, production, capital, operating and cash flow estimates, anticipated financial performance, business prospects and strategies and other general matters. These statements are subject to certain risks and uncertainties that could cause actual results to differ materially from those included in the forward-looking information. The use of words such as "intend", "anticipate", "continue", "estimate", "expect", "may", "will", "project", "should", "believe" and similar expressions are intended to identify forward-looking information. Such statements are included, among other places, in this discussion and analysis under the headings "*Executive Overview of Operations*", "*Outlook*", "*Exploration and Development Assets*", "*Financial Condition, Liquidity and Capital Resources*" and "*Risk Factors*". Statements relating to "reserves" are also forward-looking information, as they involve the implied assessment, based on certain estimates and assumptions, including that the reserves described can be profitably produced in the future. These statements and information are only predictions based on current information and knowledge. Actual future events or results may differ materially. In addition, this discussion and analysis may contain forward-looking information attributed to third party industry sources. Undue reliance should not be placed on such forward-looking information, as there can be no assurance that the plans, intentions or expectations upon which they are based will occur. By its nature, forward-looking information involves numerous assumptions, known and unknown risks and uncertainties, both general and specific, that contribute to the possibility that the predictions, forecasts, projections and other forward-looking information will not be realized. In addition, the exploration and development of oil and gas properties involves certain significant risks, not within the control of management, which can adversely impact the Company's plans and expectations (see "Risk Factors").

In particular, this discussion and analysis contains forward-looking information pertaining to the following:

- expectations regarding the Corporation and/or its co-venturers' ability to satisfy capital expenditure requirements to maintain the Corporation's projects in good standing;
- plans for selling project interests and/or sharing expenditure requirements with new joint venture partners;
- performance characteristics of the Corporation's producing properties;
- crude natural gas, natural gas liquids and oil production estimates and targets;
- the size of the Corporation's natural gas, natural gas liquids and oil reserves;
- planned capital expenditure programs and estimates;
- timing of commencement of fracture stimulations and drilling of additional wells and the Corporation's expectations as to the outcomes of the foregoing;
- hypotheses regarding the geology of the basins in which the Corporation has operations and is conducting exploratory work;
- expectations regarding the potential number of additional drilling locations on the Corporation's projects;
- projections of market prices and costs;
- expectations regarding future supply and demand for oil and natural gas;
- expectations regarding the ability to attract and retain appropriately qualified employees and consultants;
- expectations regarding the ability to raise capital and to add to reserves through acquisitions and development; and
- anticipated treatment under governmental regulatory regimes and tax laws.

This forward-looking information is based on a number of assumptions, including, but not limited to, the following:

- assumptions set out herein and, in the Corporation's, most recently filed Form 51-101F1 oil and gas report;
- stability in the credit markets and continued willingness of lenders to lend capital to issuers such as the Corporation;
- continuing availability of funds for capital expenditures through internally generated cash and/or equity raises or debt raises;
- that the Corporation will continue to satisfy its covenants and meet its obligations under the terms of its outstanding debt;
- stability of the political and fiscal regimes in the countries in which the Corporation has operations;
- ability of the Corporation to hold the mineral leases and projects in which it has interests and to find suitable industry partners to assume or share capital expenditure requirements necessary to keep various of the Corporation's projects in good standing, if and as needed;
- stable future costs;
- availability of equipment and personnel when required for operations;
- future strong demand for oil and natural gas;
- that the Corporation will not experience unforeseen delays, unexpected geological, environmental or other natural occurrences, equipment failures, permitting delays or delays in procurement of required equipment or personnel;
- that the Corporation will not experience labour or contract disputes;
- that the Corporation's financial condition and development plans and those of its co-venturers will not substantially change;
- the assumptions underlying estimates of reserves;
- that indications of early results are reasonably accurate predictors of the prospectiveness of the hydrocarbon bearing strata;
- that environmental and other regulations affecting the Corporation will not substantially change, and that required regulatory approvals will be available when required;
- that expected production from future wells can be achieved as modeled and that declines will match the modeling;

- that rates of return as modeled can be achieved;
- that reserve recoveries are consistent with management's expectations;
- that additional wells are actually drilled and completed;
- expectations and assumptions regarding future growth, results of operations, production, future capital and other expenditures (including the amount, nature and sources of funding thereof);
- plans for and results of drilling activity; and
- assumptions regarding business prospects and opportunities.

Actual results could differ materially from those anticipated in forward-looking information as a result of the risks and uncertainties set forth below and elsewhere in this discussion and analysis:

- the risk that the Corporation is unable to access required capital or conclude agreements with new industry partners to fund or assist in funding capital expenditure requirements to maintain projects in good standing and to discharge outstanding debt as it becomes due;
- continued volatility in, and depressed market prices for, oil and natural gas;
- risks inherent in oil and gas operations;
- uncertainties associated with estimating oil and natural gas reserves;
- competition for, among other things, capital, acquisitions of reserves, undeveloped lands and skilled personnel;
- incorrect assessments of the value of acquisitions;
- geological, technical, drilling and processing problems;
- uncertainties associated with the utilization of hydraulic fracturing in relation to the Corporation's existing and/or future properties;
- fluctuations in foreign exchange or interest rates and stock market volatility;
- rising costs of labour and equipment;
- inherent uncertainties involved in the legal dispute resolution process;
- changes in income tax laws or changes in tax laws and incentive programs relating to the oil and gas industry;
- tightening of the credit markets, global economic uncertainty, and counterparty risk;
- equipment failures, permitting delays, delays in procurement of required equipment or personnel, and labour or contract disputes;
- changes in the Corporation's financial condition and development plans or those of its co-venturers;
- risks relating to disagreements or disputes with joint venture partners, including any failure of a joint venture partner to fund its obligations;
- risks and uncertainties associated with securing necessary regulatory approvals, including the risk that the Corporation or its subsidiaries is not able for any reason to obtain and provide the information necessary to secure required approvals or that required regulatory approvals are otherwise not available when required;
- risks and uncertainties associated with potential changes in environmental or other regulations, permitting processes or taxation;
- the risk that the Corporation will be unable to successfully renegotiate the terms of contracts as may be necessary in order for the Corporation to maintain its interest in its projects;
- the risk that unexpected geological results are encountered, completion techniques require further optimization or production rates do not match the Corporation's assumptions; and
- other factors discussed under "*Risk Factors*" below.

Although the Corporation has attempted to identify important factors that could cause actual actions, events or results to differ materially from those described in forward-looking information, there may be other factors that cause actions, events or results not to be as anticipated, estimated or intended. There can be no assurance that forward-looking information will prove to be accurate, as actual results and future events could differ materially from those anticipated in such information. The reader is cautioned not to place undue reliance on forward-looking information. The forward-looking information contained herein is presented for the purpose of assisting investors in understanding the Corporation's expected financial and operating performance and the Corporation's plans and objectives in making an investment decision and may not be appropriate for other purposes. All forward-looking information is expressly qualified in its entirety by this cautionary statement. The Corporation disclaims any obligation to update forward-looking information to reflect events or circumstances after the date of such statements, or to reflect the occurrence of anticipated or unanticipated events, except as required by law.

Cautionary Note to United States Investors

This discussion and analysis and the Company's consolidated financial statements are prepared and presented in accordance with the rules and regulations that govern Canadian reporting issuers, as required by the TSX Venture Exchange (the "Exchange") and applicable securities laws in Canada. The Company does not report to the United States Securities and Exchange Commission, and, in its public disclosure, it may use terms which are not permitted terminology in the United States. In addition, United States investors are cautioned that the Company's consolidated financial statements do not conform with, nor are they reconciled to, accounting principles generally accepted in the United States.

Company Overview

Terrace Energy Corp. (the "Company" or "Terrace") was incorporated on July 6, 2006 under the Business Corporations Act (British Columbia) and previously named Terrace Resources Inc.

The Company is in the business of acquiring, exploring and developing onshore oil and gas properties in the United States. The Company has a limited history of revenues and operating cash flows. The operations of the Company are therefore dependent upon its future profitable operations and its ability to raise additional capital as required, neither of which is assured. The Company's head office is located at 25511 Budde Road, Suite 601, The Woodlands, Texas 77380 where all its operating activities are managed. Its registered and records office is located at 10th Floor, 595 Howe Street, Vancouver, British Columbia V6C 2T5.

The following table lists the Company's principal operating subsidiaries, their jurisdiction of incorporation and its percentage ownership of their voting securities as of the date of this report:

Name of subsidiary	Place of Incorporation	Percentage ownership
Terrace US Holdings LLC	USA	100%
Terrace Investment Holdings Inc.	USA	100%
TEC Olmos, LLC	USA	100%

During the year ended January 31, 2019, Terrace Operating LLC and TEC Operating, LLC were dissolved. See "Exploration and Evaluation Assets" for the Company' interest in BlackBrush Terrace LP.

Executive Overview of Operations

The Company is continuing its efforts to further reduce overhead and operating costs and consider steps to reorganize its capital. These steps are ongoing and will take time to conclude.

Due to the drastic deterioration of energy commodity prices resulting from the COVID 19 Pandemic and the collapse of world-wide oil demand, the Company has determined that its partnership interest in its Maverick County exploration program no longer holds any commercially viable value. The Company had previously classified its partnership interest in the BTLP as an Asset Held for Sale; however, discussions with all apparent potential buyers have been unsuccessful. In light of current and forecasted commodity prices, the Company has determined that there is no reasonable likelihood that a viable buyer can be identified or that a transaction will occur. Consequently, the Company has elected to cease activities including seeking a potential buyer. The Maverick County exploration program was the Company's sole remaining oil & gas project. Concurrent with this filing, the Company will also file a Form NI 51-101F5 noticing cessation of oil & gas activities.

The Company is presently obligated to pay note holders approximately CDN $35.2 million in 2021 and only has working capital of approximately CDN $1.0 million to meet the Company's current and future obligations as they arise. The Company will require additional funds which cannot be assured at this time.

Results of Operations

For the year ended January 31, 2020 and 2019

Net loss for the year ended January 31, 2020 was $7,683,530 compared to net loss of $2,291,640 for the year ended January 31, 2019. The results are summarized as follows:

	2020	2019
Expenses		
General and administrative expenses	$ 210,903	$ 397,019
Salaries and benefits	94,769	282,911
Depreciation	-	18,098
	(305,672)	(698,028)
Finder's fee	-	1,000,000
Financing costs	(3,996,163)	(3,846,254)
Foreign exchange gain	1,342,813	1,354,516
Equity loss in partnership	(4,724,508)	(101,874)
Net loss for the period	$ (7,683,530)	(2,291,640)

General and administrative expenses for the year ended January 31, 2020 were $210,903 compared to $397,019 for the year ended January 31, 2019. These expenses are comprised primarily of office costs, accounting services, professional fees for legal and audit services and transfer agent and Exchange fees. These expenses have decreased due to reduced activity and rent.

Financing costs for the year ended January 31, 2020 were $3,996,163 compared to $3,846,254 for the year ended January 31, 2019 and represents the accretion of the discount on the convertible notes.

Foreign exchange gain for the year ended January 31, 2020 was a gain of $1,342,813 compared to a gain of

$1,354,516 for the year ended January 31, 2019. The change in foreign exchange was due to fluctuations in the USD exchange rate during the period.

Salaries and benefits for the year ended January 31, 2020 were $ 94,769 compared to $282,911 for the year ended January 31, 2019. In prior period salaries were offset by consulting income of from a third-party consulting practice which was curtailed in the prior year.

Finder's fee for the year ended January 31, 2019 was $1,000,000 from a third party upon that party acquiring assets previously evaluated by the Company. No such transaction occurred in 2020.

Equity loss in partnership represents the Company's pro-rata share of income or loss of the BlackBrush Terrace LP. For the year ended January 31, 2020 the Company's share of the partnership loss was $4,724,508 compared to $101,874 for the year ended January 31, 2019.

Due to the deterioration of energy commodity prices resulting from the COVID 19 Pandemic and the collapse of world-wide oil demand the Company has recorded a loss of $4,724,508 related to its interest in the BlackBrush Terrace LP. As a result of the loss, the value of the partnership at January 31, 2020 is $nil. The Maverick County exploration program was the Company's sole remaining oil & gas project. Concurrent with this filing, the Company will also file a Form NI 51-101F5 noticing cessation of oil & gas activities.

Selected Annual Information

The following financial represents selected information of the Company for the three most recently completed financial years:

	Year ended January 31, 2020	Year ended January 31, 2019	Year ended January 31, 2018
Oil and gas revenues (net of royalties)	$ -	$ -	$ -
Net income (loss) for the year	$ (7,683,530)	$ (2,291,640)	$ (3,497,824)
Basic and diluted income (loss) per share	$ (0.03)	$ (0.02)	$ (0.04)
Total assets	$ 1,453,542	$ 6,511,395	$ 6,346,609
Total current liabilities	$ 569,091	$ 595,692	$ 630,868
Total long-term liabilities	$ 21,734,288	$ 18,076,882	$ 17,328,649

Net loss for the year ended January 31, 2020 primarily relate to the non-cash accretion of the valuation discount on the convertible notes of $3,996,163. Other non–cash transactions include a foreign exchange gain of $1,342,813. Equity loss in partnership was $4,724,508.

Net loss for the year ended January 31, 2019 primarily relate to the non-cash accretion of the valuation discount on the convertible notes of $3,846,254, a foreign exchange gain of $1,354,516. Equity loss in partnership was $101,874.

Net loss for the year ended January 31, 2018 primarily relate to the non-cash accretion of the valuation discount on the convertible notes of $2,991,233 and administration and salaries and benefits. Other non–cash transactions include a foreign exchange gain of $918,914. Equity loss in partnership was $279,315.

For the three months ended January 31, 2020 and 2019

Net loss for the three months ended January 31, 2020 was $5,572,127 compared to net loss of $1,061,878 for the three months ended January 31, 2019. The results are summarized as follows:

	2020	2019
Expenses		
General and administrative expenses	$ 95,963	$ 214,373
Salaries and benefits	23,371	(38,880)
	(119,334)	(175,493)
Financing costs	(1,127,071)	(874,378)
Foreign exchange gain	340,447	(6,161)
Equity loss in partnership	(4,666,169)	(5,846)
Net loss for the period	$ (5,572,127)	$ (1,061,878)

General and administrative expenses for the three months ended January 31, 2020 were $95,963 compared to $124,373 for the three months ended January 31, 2019. These expenses are comprised primarily of office costs, accounting services, and transfer agent and Exchange fees.

Financing costs for the three months ended January 31, 2020 were $1,127,071 compared to $874,378 for the three months ended January 31, 2019 and represents the accretion of the discount on the convertible notes.

Foreign exchange gain for the three months ended January 31, 2020 was a gain of $340,447 compared to a loss of $6,161 for the three months ended January 31, 2019. The change in foreign exchange was due to fluctuations in the USD exchange rate during the period.

Salaries and benefits for the three months ended January 31, 2020 were $ 23,371 compared to $38,880 for the three months ending January 31, 2019

Equity loss in partnership represents the Company's pro-rata share of income or loss of the BlackBrush Terrace LP. For the quarter ended January 31, 2020, the Company's share of the equity loss in partnership was $4,666,169. For the quarter ended January 31, 2019 the Company's share of the equity loss in partnership was $5,846.

Summary of Quarterly Results

The results of the Company's most recent eight quarters are set out below:

	January 31, 2020	October 31, 2019	July 31 2019	April 30, 2019
Net loss	(5,572,127) [1]	(1,041,259) [2]	(1,054,399) [3]	(15,745) [4]
Assets held for sale	-	4,666,169	4,668,469	4,698,124
Total assets	1,453,542	6,215,171	6,293,495	6,366,511
Loss per share – basic and diluted	(0.05)	(0.01)	(0.01)	(0.01)

	January 31, 2019	October 31, 2018	July 31 2018	April 30, 2018
Loss	(1,050,186)[5]	(1,093,583)[6]	(53,478)[7]	(94,393)[8]
Assets held for sale	4,724,508	4,718,663	-	-
Property and equipment	-	-	-	9,489
Investment in partnership[9]	-	-	4,577,653	4,789,213
Total assets	6,511,395	6,657,625	6,585,885	6,028,292
Loss per share – basic and diluted	(0.01)	(0.01)	(0.00)	(0.00)

Notes:

1) Net loss during this period includes a non-cash deduction of $1,127,071 for financing costs as well as $342,167 for foreign exchange gain.
2) Net loss during this period includes a non-cash deduction of $1,000,099 for financing costs as well as $1,108 for foreign exchange gain.
3) Net loss during this period includes a non-cash deduction of $974,438 for financing costs as well as $10,838 for foreign exchange loss.
4) Net loss during this period includes a non-cash deduction of $894,555 for financing costs as well as $1,010,376 for foreign exchange gain.
5) Net loss during this period includes a non-cash deduction of $874,378 for financing costs as well as $6,161 for foreign exchange loss.
6) Net loss during this period includes a non-cash deduction of $1,013,063 for financing costs as well as $19,280 for foreign exchange gain.
7) Net loss during this period includes a non-cash deduction of $9,340 for depreciation, $1,123,273 for financing costs as well as $310,415 for foreign exchange gain.
8) Net loss during this period includes a non-cash deduction of $8,883 for depreciation, $835,540 for financing costs as well as $1,030,982 for foreign exchange gain.
9) The carrying value represents the Company's share of costs to organize, acquire and fund certain agreed upon exploration and evaluation activities to-date plus the Company's share of the changes in net assets of the partnership.

Fluctuations in reported earnings during the prior quarters are primarily due to changes in oil and gas production, depletion and revenues, asset impairment charges, share-based payments, foreign exchange adjustments, asset divestitures and professional fees. The time during which the Company acquires, develops, disposes or abandons projects materially impacts the results of operations from fiscal quarter to quarter.

Financial Condition, Liquidity and Capital Resources

As at January 31, 2020, the Company had a working capital of $884,451 (January 31, 2019 – working capital of $1,191,195), which was comprised of cash of $1,432,708, accounts receivable of $4,446 and prepaid expense of $16,388, offset by accounts payable and accrued liabilities of $569,091.

As at January 31, 2020, and the date of this report, the Company had outstanding long-term convertible notes in the principal amount of CAD $35,232,000 (January 31, 2019 – CAD $35,532,000). On May 13, 2016, the Company completed an exchange of the previously outstanding notes which required quarterly interest payments calculated at 8% per annum and were due April 2, 2018 with new non-interest bearing notes, which are secured by the assets of the Terrace Energy Corp. with an extended maturity date of April 2, 2021. As part of the exchange, the outstanding, unpaid interest owed to the noteholders was forgiven. A more detailed description of the notes exchange transaction is set out in Note 6 to the Company's Consolidated Financial Statements for the year ended

January 31, 2020.

As outlined above, energy commodity prices have deteriorated significantly further due to the collapse of world-wide oil demand, stemming at least in part from the economic pressures created by the COVID 19 Pandemic. Management has subsequently concluded that there is no reasonable likelihood that a viable buyer for its sole remaining oil and gas development asset can be identified or that a transaction will occur. Consequently, the Company has elected to cease all oil and gas development activity activities including seeking a potential buyer for its investment in the BTLP.

The Company will need to raise additional capital or seek other strategic alternatives to meet its debt obligations. There are no guarantees that the Company will be able to raise such additional capital or develop viable strategic alternatives when needed.

Off Balance Sheet Arrangements

Except as described herein, there are no off-balance sheet arrangements to which the Company is committed.

Key Management Personnel Compensation

Key management personnel include executive officers and directors of the Company. Compensation of the Company's key management personnel is comprised of the following:

Year ended January 31,	**2020**	**2019**
Short-term compensation	$ 56,528	$ 290,871
Recoveries from consulting and management services revenues	-	(69,856)
	$ 56,528	$ 221,015

As at January 31, 2020 and 2019:

The Company established a third-party consulting practice to cover salaries for technical personnel in prior years which resulted in $69,856 recovered in 2019. This practice was discontinued in the period ending October 31, 2018

At January 31, 2020, convertible notes held by key management personnel and their close family members totalled CAD $3,230,000 (2019 - CAD $3,230,000). No interest was paid on these convertible notes in 2020 and 2019.

At January 31, 2020, the accounts payable owing to key management personnel totalled $4,275 (2019 - $4,070)

Proposed transactions

There are no proposed transactions that have not been disclosed herein.

Adoption of new accounting standards and amendments

The following are new accounting standards and amendments adopted by the Company effective January 1, 2019.

IFRS 16 *Leases*

Effective January 1, 2019, the Company adopted IFRS 16 *Leases* ("IFRS 16") using the modified retrospective approach. The comparative figures for the 2018 reporting period have not been restated and are accounted for under IAS 17 *Leases*, ("IAS 17") and IFRIC 4 *Determining Whether an Arrangement Contains a Lease*, as permitted under the specific transitional provisions in the standard. IFRS 16 requires lessees to recognize assets and liabilities for most leases. For lessors, there is little change to the existing accounting in IAS 17, *Leases*. The adoption of IFRS 16 *Leases* did not have an impact on the Company's consolidated financial statements as the Company does not have any long-term lease agreements.

Accounting standards that will become effective in future periods

The IASB or International Financial Reporting Interpretation Committee have issued pronouncements effective for accounting periods beginning on or after February 1, 2020. The Company has not early adopted the following new and revised standards, amendments and interpretations:

IFRS 17 Insurance Contracts

IFRS 17 is a new standard that requires insurance liabilities to be measured at a current fulfillment value and provides a more uniform measurement and presentation approach for all insurance contracts. These requirements are designed to achieve the goal of a consistent, principle-based accounting for insurance contracts. IFRS 17 supersedes IFRS 4, *Insurance Contracts*, and related interpretations.

This standard will be effective for the Company's annual period beginning January 1, 2021. The Company has assessed that the impact of IFRS 17 on its consolidated financial statements would not be significant.

Critical accounting estimates and judgments

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

Following are the accounting policies subject to such judgments and the key sources of estimation uncertainty that the Company believes could have the most significant impact on the reported results and financial position.

Assets held for sale and discontinued operations

Judgment is required in determining whether an asset meets the criteria for classification as "assets held for sale" in the consolidated statements of financial position. Criteria considered by management include the existence of and commitment to a plan to dispose of the assets, the expected selling price of the assets, the expected timeframe of the completion of the anticipated sale and the period of time any amounts have been classified within assets held for sale. The Company reviews the criteria for assets held for sale each quarter and reclassifies such assets to or from this financial position category as appropriate. In addition, there is a requirement to periodically evaluate and record assets held for sale at the lower of their carrying value and fair value less costs to sell.

Judgment is applied in determining whether disposal groups represent a component of the entity, the results of which should be recorded as discontinued operations in the consolidated statements of loss and comprehensive loss.

Joint arrangements

Judgment is required to determine when the Company has joint control over an arrangement, which requires an assessment of the relevant activities and when the decisions in relation to those activities require unanimous consent.

Judgment is also required to classify a joint arrangement. Classifying the arrangement requires the Company to assess their rights and obligations arising from the arrangement including whether the arrangement is structured through a separate vehicle, in which case, judgment is also required to assess the rights and obligations arising from the legal form of the separate vehicle, terms of the contractual arrangement, and other relevant facts and circumstances. This assessment often requires significant judgment, and a different conclusion on joint control and whether the arrangement is a joint operation or a joint venture, may materially impact the accounting. Management has assessed the investment in partnership as a joint venture.

Convertible debentures

In accordance with the substance of the contractual arrangement, convertible debentures are compound financial instruments that are accounted for separately by their components: a financial liability and an equity instrument.

The identification of convertible debenture components is based on interpretations of the substance of the contractual arrangement and therefore requires judgment from management. The separation of the components affects the initial recognition of the convertible debenture at issuance and the subsequent recognition of interest on the liability component. The determination of the fair value of the liability is also based on a number of assumptions, including contractual future cash flows, discount factors, and the presence of any derivative financial instruments.

Functional currency

The determination of the functional currency for the Company and each of its subsidiaries was based on management's judgment of the underlying transactions, events and conditions relevant to each entity.

Going concern

The assessment of the Company's ability to continue as a going concern and to raise sufficient funds to pay its ongoing operating expenditures, meet its liabilities for the ensuing year, and to fund planned and contractual exploration programs, involves significant judgment based on historical experience and other factors, including expectation of future events that are believed to be reasonable under the circumstances.

Income taxes

Related assets and liabilities are recognized for the estimated tax consequences between amounts included in the consolidated financial statements and their tax basis using substantively enacted future income tax rates. Timing of future revenue streams and future capital spending changes can affect the timing of any temporary differences, and accordingly, affect the amount of the deferred tax asset or liability calculated at a point in time. These differences could materially impact earnings.

Risk Factors

Management of the Company considers the following risks to be the most significant in connection with the business and outlook for the Company, but such risks do not necessarily comprise all those associated with the Company's operations. Additional risks and uncertainties not currently known to management of the Company may also have an adverse effect on the Company's business. If any of these risks actually occur, the Company's business, financial condition, capital resources, results and/or future operations could be materially adversely affected. In such a case, the market value of the securities of the Company could decline and investors may lose all or part of their investment.

Additional Funding Requirements and Going Concern

As of January 31, 2019, the Company had working capital of approximately $880,000. However, the Company had negative cash flow from operating activities from operations of $333,441 and $391,382 for the year ended January 31, 2020 and 2019, respectively. Terrace's financial resources will not be sufficient to fund its long-term convertible note obligations and ongoing activities beyond the near term. These conditions indicate the existence of material uncertainties that may cast significant doubt about the Company's ability to continue as a going concern. The Company will need to sell assets and/or raise additional capital to meet its note obligations and to carry out its future oil and gas acquisition, exploration and development activities. Failure to obtain such capital on a timely basis could cause the Company to forfeit its interest in certain properties, miss certain acquisition opportunities and reduce or terminate its operations. Any additional financing is likely to involve the issuance of securities which could be substantially dilutive.

The Company's ability to meet its current and future debt obligations and to fund its operations, including its obligations in order to earn into its project interests, will depend on numerous factors, including the ability to sell assets and/or raise additional capital, the success of its acquisition activities, development and exploration drilling success, cost of lease extensions and renewals, the cost and rates of success of re-completing or drilling wells, future production levels, the terms (including price) and conditions that it is able to negotiate with purchasers of production from its properties, and the results of exploration activities. None of these factors can be predicted with certainty. Accordingly, the timing and amount of required capital may vary from management expectations. In addition, the Company may be required by the holders of the outstanding convertible promissory notes to pre-pay the outstanding principal amount owing under the notes if an event of default under the notes occurs. As a result, in such circumstances the Company may be required to pay the entire outstanding principal owing on the notes in advance of the maturity date of April 2, 2021, failing which the note holders could take action to realize on their general security interest over the Company's assets. Further, because the Company's operations are conducted through U.S. subsidiaries, the Company's ability to meet its debt service obligations with cash from operations will depend on generating cash flows from operations of its U.S. subsidiaries and may be subject to contractual or other restrictions and other business considerations.

Any additional equity financing will be dilutive to the holders of the Company's outstanding common shares and may not be on terms that the Company finds attractive, if available at all. Any additional debt financing, if available, may restrict the Company's future financing and operating activities. The Company may be unable to obtain additional financing on acceptable terms if market and economic conditions, the financial condition or operating performance of the Company or investor sentiment are unfavourable. If the Company's cash flow is insufficient to meet its current and future debt obligations or if the Company fails to obtain sufficient funds for operations and earn in obligations on a timely basis, the Company may have to forfeit its interest in certain properties, sell assets, miss certain acquisition opportunities, and reduce or terminate its acquisition, exploration and development programs, which would have a material adverse effect on the Company's results of operations and could result in a loss of some projects. The inability of the Company to meet its current and future debt obligations or to fund its operations could have a material adverse effect on the Company's financial condition, results of operations and prospects.

Prices and Markets for Oil and Natural Gas

Oil and natural gas are commodities whose prices are determined based on world demand, supply and other factors, all of which will be beyond the control of the Company. World prices for oil and natural gas have fluctuated widely in recent years and have dropped precipitously since late 2014. The recent decline in prices has resulted in a significant reduction of net production revenue. Additional decreases could result in further decreases of revenue. Certain wells have become uneconomic as a result of a decline in world oil prices or natural gas prices, leading to a reduction in the volume of the Company's oil and gas reserves. Additional material declines would result in more wells becoming uneconomic with corresponding reductions to reserves. The Company might also elect not to produce from certain wells at lower prices. All of these factors could result in a material decrease in the Company's future net production revenue, causing a reduction in its oil and gas acquisition and development activities. Prices for oil and gas are subject to large fluctuations in response to relatively minor changes in the supply of and demand for oil and gas, market uncertainty and a variety of additional factors beyond the control of the Company. These factors include economic conditions, in the United States and Canada, the actions of OPEC, governmental regulation, political stability in the Middle East and elsewhere, the foreign supply of oil and gas, risks of supply disruption, the price of foreign imports and the availability of alternative fuel sources. Any substantial and extended decline in the price of oil and gas would have an adverse effect on the Company's carrying value of its reserves, borrowing capacity, revenues, profitability and cash flows from operations and may have a material adverse effect on the Company's business, financial condition, results of operations and prospects.

Exploration, Development and Production Risks

Oil and natural gas exploration involves a high degree of risk and there is no assurance that expenditures made on future exploration by the Company will result in new discoveries of oil or natural gas in commercial quantities. The Company, through its subsidiaries, has the right to earn working interests in various oil and gas properties described herein. To earn such interests the Company must incur certain specified expenditures to evaluate and complete a number of prospective wells capable of producing oil and gas in paying quantities. No assurance can be given that the Company will be successful in completing wells capable of producing oil and gas. The long-term commercial success of the Company depends on its ability to find, acquire, develop and commercially produce oil and natural gas reserves. Without the continual addition of new reserves, any existing reserves the Company may have at any particular time and the associated production if any there from will decline over time as the reserves are exploited. A future increase in the Company's reserves will depend not only on its ability to explore and develop any properties it may have from time to time, but also on its ability to select and acquire suitable producing properties or prospects. No assurance can be given that the Company will be able to continue to locate satisfactory properties for acquisition or participation. Exploration and development activities may be delayed or adversely affected by factors outside the control of the Company including adverse climatic and geographic conditions, labour disputes, compliance with governmental requirements, shortage or delays in installing and commissioning plant and equipment or import or customs delays. Drilling may involve unprofitable efforts, not only with respect to dry wells, but also with respect to wells, though yielding some oil or gas, are not sufficiently productive to justify commercial development or cover operating and other costs. Oil and natural gas exploration, development and production operations are subject to all the risks and hazards typically associated with such operations, including hazards such as fire, explosion, blowouts, cratering, sour gas releases and spills, each of which could result in substantial damage to oil and natural gas wells, production facilities, other property and the environment or in personal injury.

No Assurance of Title

Title to oil and gas interests is often not capable of conclusive determination without incurring substantial expense. The nature of the oil and gas leasing and title regime in the U.S. is such that interests in tracts of acreage may be represented by many leases and other agreements affecting oil and gas rights and access and obtaining absolute confirmation of chain of title would be time consuming and expensive. While the Company will conduct a title review of a particular area prior to commencement of drilling there can be no assurance of title. Title may be subject to unregistered liens and other defects which, if affecting a core area, could have a material adverse effect on the Company, its financial condition, results of operations and prospects.

Permits and Licenses

The activities of the Company are subject to government approvals, various laws governing prospecting, development, land resumptions, production taxes, labor standards and occupational health, safety, toxic substances and other matters, including issues affecting local native populations. Although the Company believes its planned development work is in accordance with all applicable rules and regulations, no assurance can be given that new rules and regulations will not be enacted or that existing rules and regulations will not be applied in a manner which could limit or curtail production or development. Amendments to current laws and regulations governing operations and activities of oil and gas exploration and development, or more stringent implementation thereof, could have a material adverse impact on the business, operations and financial performance of the Company. Further, the exploration and development permits and licenses that have and may be issued in respect of each project may be subject to conditions which, if not satisfied, may lead to the revocation of such permits and licenses. In the event of revocation, the value of the Company's investments in such projects may decline.

Reserve Estimates

There are numerous uncertainties inherent in estimating quantities of oil, natural gas and natural gas liquids reserves and resources and associated cash flows, including many factors beyond the Company's control. In general, estimates of economically recoverable oil and natural gas reserves and the future net cash flows from them are based upon a number of variable factors and assumptions, such as historical production from the properties, production rates, ultimate reserve recovery, timing and amount of capital expenditures, marketability of oil and natural gas, royalty rates, the assumed effects of regulation by governmental agencies and future operating costs, all of which may vary from actual results. The Company's actual production, revenues, taxes and development and operating expenditures with respect to its reserves will vary from estimates thereof and such variations could be material.

Lack of Adequate Insurance

In the course of exploration, development and production of oil and gas properties, certain risks, and in particular, unexpected or unusual geological operating conditions including rock bursts, cave-ins, fires, flooding and earthquakes may occur. It is not always possible to fully insure against such risks and the Company may decide not to take out insurance against such risks as a result of high premiums or other reasons. Should such liabilities arise, they could reduce or eliminate any future profitability and result in increasing costs and a decline in the value of the securities of the Company.

Reliance upon Third Party Operators and Risks Associated with Joint Operating Agreements

The Company is not the operator on any of its projects. The Company therefore has limited ability to exercise influence over operations of the projects or their associated costs. The Company's dependence on the operator and other working interest owners and its limited ability to influence operations and associated costs could materially and adversely affect the Company's financial performance. The success and timing of the Company's activities on assets operated by others therefore will depend upon a number of factors outside of the Company's control, including the timing and amount of capital expenditures, timing and amount of operating and maintenance expenditures, the operator's expertise and financial resources, approval of and funding by other participants, selection of technology and risk management practices.

In addition, the Company owns certain of its interests, including its interests in the Maverick County Project, through joint venture or similar arrangements. Joint ventures involve risks not otherwise present when exploring and developing properties directly, including, for example, that the joint venture partner may not pay its share of obligations, the Company may incur liabilities as a result of an action taken by its joint venture partners and the Company may be required to devote significant management time to the requirements.

Disputes with third party operators, joint venture partners and other participants in projects may result in delays, litigation or operational impasses. The risks described above or the failure to resolve disagreements could result in significant cost and delay, or adversely affect the ability of the parties to operate and develop the relevant projects, which would have a material adverse effect on the Company.

Environmental Risks

All phases of the oil and natural gas business present environmental risks and hazards and are subject to environmental regulation pursuant to a variety of international conventions and federal, state and municipal laws and regulations. Environmental legislation provides for, among other things, restrictions and prohibitions on spills, releases or emissions of various substances produced in association with oil and gas operations. The legislation also requires that wells and facility sites be operated, maintained, abandoned and reclaimed to the satisfaction of applicable regulatory authorities. Compliance with such legislation can require significant expenditures and a breach may result in the imposition of fines and penalties, some of which may be material. Environmental legislation is evolving in a manner expected to result in stricter standards and enforcement, larger fines and liability and potentially increased capital expenditures and operating costs. There is no assurance that future changes in environmental regulation, if any, will not adversely affect the Company's operations or prevent operations all together. Government approvals and permits are currently, and may in the future be, required in connection with the Company's operations, which could potentially make operations expensive or prohibit them altogether. To the extent such future approvals are required and not obtained, the Company may be curtailed or prohibited from proceeding with planned exploration or development of its projects or from commencing production.

Availability of Drilling Equipment and Access Restrictions

Oil and natural gas exploration and development activities are dependent on the availability of drilling and related equipment in the particular areas where such activities will be conducted. Demand for such limited equipment or access restrictions may affect the availability of such equipment to the Company and may delay exploration and development activities.

Global Financial Conditions

The COVID 19 Pandemic has been largely responsible for a substantial negative impact on the world economy. This has been especially impactful to the oil and gas industry through a drastic shrinking of global energy demand and the subsequent collapse of energy commodity prices.

Additionally, many industries, including the oil and gas industry, are impacted by global market conditions. Some of the key impacts of financial market turmoil can include contraction in credit markets resulting in a widening of credit risk, devaluations and high volatility in global and specifically natural resource equity markets, commodity, foreign exchange and precious metal markets, and a lack of market liquidity. A slowdown in the financial markets or other economic conditions, including but not limited to, reduced consumer spending, increased unemployment rates, deteriorating business conditions, inflation, deflation, volatile fuel and energy costs, increased consumer debt levels, lack of available credit, lack of future financing, changes in interest rates and tax rates may adversely affect the Company's operations and business plans. Any of these factors may impact the ability of the Company and its joint venture partners or potential partners to obtain equity or debt financing in the future and, if obtained, on favourable terms. Additionally, any such occurrence could cause decreases in asset values that are deemed to be other than temporary, which may result in impairment losses.

Geopolitical Risks

The marketability and price of oil and natural gas that may be acquired or discovered by the Company is and will continue to be affected by political events throughout the world that cause disruptions in the supply of oil. Conflicts, or conversely peaceful developments, arising in the Middle East, and other areas of the world, have a significant impact on the price of oil and natural gas. Any particular event could result in a material decline in prices and therefore result in a reduction of the Company's net production revenue.

Transportation Costs

Disruption in or increased costs of transportation services could make oil and natural gas a less competitive source of energy or could make the Company's oil and natural gas less competitive than other sources. The industry depends on rail, trucking, ocean-going vessels, pipeline facilities, and barge transportation to deliver shipments, and transportation costs are a significant component of the total cost of supplying oil and natural gas. Disruptions of these transportation services because of weather related problems, strikes, lockouts, delays or other events could temporarily impair the ability to supply oil and natural gas to customers and may result in lost sales. In addition, increases in transportation costs, or changes in transportation costs for oil and natural gas produced by competitors, could adversely affect profitability. To the extent such increases are sustained, the Company could experience losses and may decide to discontinue certain operations forcing the Company to incur closure and/or care and maintenance costs, as the case may be. Additionally, lack of access to transportation may hinder the expansion of production at some of the Company's properties and the Company may be required to use more expensive transportation alternatives.

Reliance on Key Individuals

The Company's success depends to a certain degree upon certain key members of the management team. It is expected that these individuals will be a significant factor in the Company's growth and success. The loss of the service of members of management and certain key employees could have a material adverse effect on the Company.

Conflicts of Interest

Certain of the Company's directors are also directors, officers or shareholders of other companies that are engaged in the business of acquiring, developing and exploiting natural resource properties. Such associations may give rise to conflicts of interest from time to time. Such a conflict poses the risk that the Company may enter into a transaction on terms which place the Company in a worse position than if no conflict existed. The directors are required by law to act honestly and in good faith with a view to the best interest of the Company and to disclose any interest which they may have in any project or opportunity of the Company. However, each director has similar obligations to other companies for which such director serves as an officer or director. If a conflict of interest arises at a meeting of the board of directors, any director in a conflict is required disclose his interest and abstain from voting on such matter. In determining whether or not the Company will participate in any project or opportunity, the board of directors will primarily consider the degree of risk to which the Company may be exposed and its financial position at that time.

Financial Instruments

The Company's risk exposure and the impact on the Company's financial instruments are summarized below:

Fair value

The carrying values of cash and accounts payable and accrued liabilities approximate their fair values due to the short-term maturity of these financial instruments.

Credit risk

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

The Company's credit risk is primarily attributable to its cash. The credit risk associated with cash is mitigated since the cash is held at major financial institutions with high credit ratings. At January 31, 2019 and January 31, 2019, the Company has no trade receivables, and therefore is no longer exposed to credit risk from these financial assets.

Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate due to changes in the market prices. Market risk is comprised of three types of risk: interest rate risk, foreign currency risk and other price risk.

(i) Interest rate risk

To the extent that payments made or received on the Company's monetary assets and liabilities are affected by changes in prevailing market interest rates, the Company is exposed to interest rate cash flow risk.

To the extent that changes in prevailing market interest rates differ from the interest rates in the Company's monetary assets and liabilities, the Company is exposed to interest rate price risk.

The Company's exposure to interest rate risk is minimal.

(ii) Foreign currency risk

Foreign currency risk is the risk that the future cash flow of financial instruments will fluctuate as a result of changes in foreign exchange rates. The Company's functional currency is CAD and its subsidiaries' functional currencies are CAD. Transactions relating to its oil and gas properties are in USD. Therefore, the Company is impacted by changes in the exchange rate between Canadian and US dollars.

The assets and liabilities with exposure to foreign currency risk are those that are denominated in a different currency than the currency determined to the functional currency of the respective entity as of the end of the period.

The following assets and liabilities represent the Company's exposure to foreign currency risk:

	January 31, 2020	**January 31, 2019**
Cash	$ 1,372,302	$ 1,765,558
Accounts payable and accrued liabilities	(569,091)	(518,573)
Net	$ 803,211	$ 1,246,985

Based on the above net exposure as at, a 5% change in the Canadian/US exchange rate would impact the Company's net loss and comprehensive loss by approximately $42,770 (January 31, 2019 - $59,649).

(iii) Other price risk

Other price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate due to changes in the market prices, other than those arising from interest rate risk or foreign currency risk. The Company is not exposed to significant other price risk.

Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulty in satisfying financial obligations as they become due. The Company manages liquidity risk through maintaining sufficient cash on hand to meet its obligations as they become due. As at January 31, 2020, the Company had cash of $1,432,708 (2019 - $1,765,776), accounts receivable of $4,446 (2019 - $3,819), and current liabilities of $569,091 (2019 - $595,692). Current liabilities of $69,091 are due within three months of January 31, 2020. The remaining $500,000 balance relates to a contingent liability recorded for provision of the asserted liquidated damages. A more detailed description of the contingent liability is set out in Note 10 to the Company's Consolidated Financial Statements for the year ended January 31, 2020.

The Convertible Notes of the Company represent a long-term debt obligation that will mature in 2021. The Company has determined that its sole remaining oil and gas development asset is no longer commercially viable. Consequently, the Company will cease all oil and gas development activities and seek alternatives for addressing this obligation. There are, however, no assurances that the Company's plans will produce sufficient net revenues to pay out this debt.

The Company has remaining cash of approximately CAD $1 million. The Company will need to raise additional capital or seek other strategic alternatives to meet its debt obligations. There are no guarantees that the Company will be able to raise such additional capital or develop viable strategic alternatives when needed.

Classification of financial instruments

The following table sets forth the Company's financial assets and financial liabilities measured at fair value by level within the fair value hierarchy as at January 31, 2020.

	Level 1	Level 2	Level 3
Cash	$ 1,432,708	$ -	$ -
Accounts payable and accrued liabilities	(569,091)		
Convertible notes	(217,343)	-	-
	$ 646,274	$ -	$ -

The following table sets forth the Company's financial assets and financial liabilities measured at fair value by level within the fair value hierarchy as at January 31, 2019.

	Level 1	Level 2	Level 3
Cash	$ 1,765,776	$ -	$ -
Accounts payable and accrued liabilities	(595,692)	$ -	$ -
Convertible notes	(270,329)	-	-
	$ 899,755	$ -	$ -

Shareholder's Equity and Outstanding Share Data

The authorized share capital of the Company consists of an unlimited number of common shares. As of January 31, 2020, there were 94,560,821 common shares outstanding.

During the year ended January 31, 2020, the Company issued 600,000 common shares on the conversion of CAD $300,000 convertible notes.

As of the date of this report there were 95,480,821 common shares outstanding

During the year ended January 31, 2019, the Company issued 5,466,000 common shares on the conversion of CAD $2,733,000 convertible notes.

As of the date of this report, the Company had no stock options outstanding:

Restricted Share Units

The Company has a restricted share unit plan, which provides that the Board of Directors of the Company may from time to time, in its discretion, and in accordance with Exchange requirements, issue to directors, officers, employees and technical consultants to the Company, restricted share units ("RSUs"). The aggregate number of common shares of the Company that may be issued under the plan may not exceed 3,682,182 shares. In addition, common shares reserved for issuance of RSUs will reduce the number of shares that may be made subject to the incentive stock options under the Company's 10% rolling option plan. The number of common shares reserved for issuance, together with any other compensation arrangements, to any one person in any 12-month period will not exceed 5% of the issued and outstanding common shares. The number of common shares reserved for issuance together with any other compensation arrangements granted to all technical consultants and will not exceed 2% of the issued and outstanding common shares. The number of RSUs granted to any one person cannot exceed 5% of the issued and outstanding common shares.

The Company has issued 350,000 RSUs outstanding as of January 31, 2020 (January 31, 2019 - 350,000). Each RSU, upon vesting, gives the holder the right to receive one common share. Unless otherwise approved by the Company's Board of Directors, all of the RSUs will vest upon the occurrence of a "change of control transaction"; as such term is defined in the RSU award agreements. In the absence of a change of control transaction or other acceleration of vesting by the Company's Board of Directors, unvested RSUs will expire ten years from the date of grant. Vested RSUs will be settled, at the election of the Company, by way of: (i) issuance of common shares from treasury; (ii) payment to the RSU holder of an amount of cash equal to the market price of the common shares on the vesting date; or (iii) any combination thereof.

Reserves Data and Other Oil and Gas Information

Our independently prepared reserves assessment and evaluation of oil and gas properties effective January 31, 2020 have been prepared in accordance with mandated National Instrument 51-101 *Standards of Disclosure for Oil and Gas Activities of Canadian Securities Administrators*. A summary of our reports is available on SEDAR at www.sedar.com.

Internal Controls Over Financial Reporting

Changes in Internal Control over Financial Reporting ("ICFR")

In connection with National Instrument 52-109, Certification of Disclosure in Issuer's Annual and Interim Filings ("NI 52-109") adopted in December 2008 by each of the securities commissions across Canada, the Chief Executive Officer and Chief Financial Officer of the Company will file a Venture Issuer Basic Certificate with respect to financial information contained in the unaudited interim financial statements and the audited annual financial statements and respective accompanying Management's Discussion and Analysis. The Venture Issue Basic Certification does not include representations relating to the establishment and maintenance of disclosure controls and procedures and internal control over financial reporting, as defined in NI52-109.

Contingencies

There are no contingent liabilities.

Management's Responsibility for Financial Statements

The information provided in this report, including the consolidated financial statements, is the responsibility of management. In the preparation of these statements, estimates are sometimes necessary to make a determination of future values for certain assets or liabilities. Management believes such estimates have been based on careful judgments and have been properly reflected in the consolidated financial statements.

Other MD&A Requirements

Additional disclosure of the Company's technical reports, material change reports, news releases and other information can be obtained on SEDAR at www.sedar.com.

Directors and Officers

David Gibbs	President, Chief Executive Officer and Director
Dan Carriere	Director and Non-Executive Chairman
Murray Oliver	Director
William McCartney	Director
Ken Shannon	Director
Jennie Choboter	Chief Financial Officer
Anthony Alvaro	Vice President Corporate Development
Deborah Cotter	Secretary

Contact Person

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