

Trickle Research

Every raging river, every great lake, every
deep blue sea starts ... with a trickle



Q1F24 Earnings Update



Alvopetro Energy Ltd.

(TSXV:ALV.V; OTC:ALVOF)

<http://alvopetro.com/>

Report Date: 05/13/24

12- 24 month Price Target: USD \$7.25

Allocation: 7

Closing Stock Price at Initiation (Closing Px: 11/07/18): USD \$1.14 (Post Split)

Closing Stock Price at Allocation Upgrade (Closing Px: 05/17/19): USD \$1.26 (Post Split)

Closing Stock Price at Target Upgrade (Closing Px: 05/26/20): USD \$1.56 (Post Split)

Closing Stock Price at Price Target and Allocation Upgrade (Closing Px: 02/11/21): USD \$1.87 (Post Split)

Closing Stock Price at Target Upgrade (Closing Px: 09/29/21): USD \$3.57

Closing Stock Price at This Allocation Upgrade (Closing Px: 03/15/22): USD \$3.75

Closing Stock Price at Price Target Increase (Closing Px: 03/27/23): USD \$5.30

Closing Stock Price at Target Increase & Allocation Decrease (Closing Px: 08/15/23): USD \$7.90

Closing Stock Price at Allocation Upgrade (Closing Px: 02/01/24): USD \$4.33

Closing Stock Price at Target Decrease (Closing Px: 03/22/24): USD \$2.97

Closing Stock Price at Target Increase (Intraday Px: 04/05/24): USD \$3.77

Closing Stock Price at This Update (Closing Px: 05/13/24): USD \$3.86

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Trickle Research**

Disclosure: Portions of this report are excerpted from Alvopetro's filings, website(s), presentations or other public collateral. We have attempted to identify those excerpts by *italicizing* them in the text.

For Q1F24, Alvopetro reported revenue of \$11.8 million and eps of \$.12. Those compared to our estimates from our update of 04/05/24 of \$12.7 million and \$.18. Despite lower revenue volumes, which were associated with lower unit sales than we anticipated, operating expenses were \$1.736 million higher than we anticipated and that was related to a handful of items. For instance, production costs included some additional workover expense, SG&A was about \$200,000 higher than our estimate, which the filing attributed in part to inflationary pressures, so we have made appropriate forward adjustments in that regard. In addition, they reflected some exploration and evaluation expenses, most of which we believe tend to get capitalized, and the biggest portion of the elevated operating expenses were in foreign exchange (loss), which we do not attempt to project but tends to smooth over several periods. All in, expenses were modestly elevated versus our estimates, which is not particularly impactful or concerning one way or the other. Clearly, the consternation around the numbers continues to be focused on lower unit sales, so we will spend a moment or two on that issue.

In short, Q1F24 results seem to be validating the recent headwinds around Alvopetro, which are essentially that a). their customer appears to be experiencing lower overall gas demand, and b). recent development data continue to lack validation around the potential for Murucutu to replace depleting resources at Caburé. Given the information we have seen of late, those are both reasonable concerns. That said, here is our view of those issues.

First, it is difficult for us to assess the ongoing demand for natural gas in Brazil. However, we know that Brazil continues to rely on imports to satisfy its ongoing natural gas demand, and everything we read suggests that is not going to change any time soon. To translate, given what we know today, it seems likely to us that Alvopetro will ultimately sell all the gas it can produce, but that does bring us to another observation.

While the Company generally suggests otherwise, we continue to believe that their collar (ceiling) price may sometimes put them at the higher end of the pricing spectrum than at the lower end. If that is the case, it would make sense that their customer might demand less gas from Alvopetro *if they are occasionally able to get gas cheaper elsewhere*. Here again, this is a difficult notion to assess, especially for those of us who are not industry experts, and perhaps more specifically, experts on Brazil's energy market. For instance, it is difficult to conclude that \$12+ per Mcf is sustainable over the long term when we often see natural gas prices in the U.S. in the sub \$3 and even \$2 ranges. In reality, we know natural gas prices around the world differ significantly depending on where one sits in relation to gas production. That is, the US produces more natural gas than it can consume in a day, so its prices are often dramatically lower than in places that do not produce their own, or enough of their own gas, ala Brazil. However, the Henry Hub U.S. gas price is part of Alvopetro's pricing calculation, so sooner or later, that pricing does impact Alvopetro's derived pricing.

We saw a bit of that as realized pricing in Q1F24 was a bit lower than Q4F23, ostensibly following the scheduled reset on February 1, 2024. From the 10,000 foot view, our sense is that over longer samples of time, when Alvopetro gets a new pricing reset (February 1 and August 1 of each year) that may impact resulting demand, because for instance, higher prices generally translate into lower demand, so our assessment in that regard is not particularly provocative. We realize there are other issues at play here, which include by the way, the potential of Brazil's overall natural gas demand to ebb and flow because of weather, domestic production etc., as well as the variability of gas markets in one area to the next (although we also believe the addition of LNG infrastructure across the globe is beginning to, or at least ultimately will reduce that variability). The point is, since the Company began selling gas in 2HF20, the unit sales numbers have been largely growing in a nice linear and increasing trajectory, but we are not sure it is reasonable to assume that will continue to be the case for every quarter going forward. Again, we are not sure the Company would agree with that assessment, but it just seems more likely to us. That said, while we submit, we may not be able to completely predict how much gas Alvopetro will sell one quarter to the next, we are very confident that they will ultimately have a market for *every Mcf they produce* which brings us to our next point.

The Company continues to provide information regarding the prospects for new production, primarily at Murucututu and to a lesser degree from new development at Caburé (which we happen to think is being largely discounted, especially since the redetermination gives them a larger share of whatever they may find there). As we noted, we understand that concern, especially as results from Murucututu have to this point be underwhelming (a point we have noted several times now). However, the reserve reports continue to suggest that the Company will be able to rely on Murucututu to ultimately replace the current levels of production from Caburé. Succinctly, if that proves accurate, we are confident suggesting that the stock price at current levels is measurably undervalued. People will need to make their own assessments around the ultimate accuracy of reserve reports.

Lastly, this morning, (05/13/24) the Company reported that a requested arbitration from their Caburé partner regarding the recent redetermination that ended in Alvopetro's favor was essentially denied. While we assume that was the outcome most were expecting, we suppose it could have been an assumed risk that is now (once again) behind Alvopetro. As an aside, the order in that regard stipulated that their partner pay 70% of the legal fees associated with the arbitration request, so that was positive as well.

We reiterate our allocation of 7 for Alvopetro shares as well as reaffirming our 12-24 month price target of \$7.25. As always, we will revisit each as new data points emerge.

Projected Operating Model

Alvopetro Energy Ltd.					
Projected Operating Model (in USD - '000s)					
By Trickle Research LLC					
	Actual	Estimate	Estimate	Estimate	Estimate
	3/31/24	6/30/24	9/30/24	12/31/24	Fiscal 2024
Oil & Gas Sales	\$ 11,752	\$ 13,807	\$ 16,813	\$ 18,154	\$ 60,526
Royalties and Production Taxes	\$ (312)	\$ (276)	\$ (336)	\$ (363)	\$ (1,287)
Net Oil & Gas Revenue	\$ 11,440	\$ 13,530	\$ 16,477	\$ 17,791	\$ 59,239
Other Income	\$ 398	\$ 250	\$ 250	\$ 250	\$ 1,148
Total Revenue and Other Income	\$ 11,838	\$ 13,780	\$ 16,727	\$ 18,041	\$ 60,387
Production	\$ 1,201	\$ 1,138	\$ 1,326	\$ 1,326	\$ 4,991
General & Administrative	\$ 1,423	\$ 1,395	\$ 1,470	\$ 1,604	\$ 5,892
Depletion and Depreciation	\$ 1,847	\$ 1,930	\$ 1,942	\$ 2,037	\$ 7,756
Impairment	\$ 91	\$ -	\$ -	\$ -	\$ 91
Exploration and Evaluation	\$ 96	\$ -	\$ -	\$ -	\$ 96
Finance Expenses and Interest	\$ 383	\$ 350	\$ 350	\$ 350	\$ 1,433
Accretion of Decommissioning Liabilities	\$ -	\$ -	\$ -	\$ -	\$ -
Share Based Compensation	\$ 287	\$ 200	\$ 200	\$ 200	\$ 887
Foreign Exchange Loss	\$ 1,170	\$ -	\$ -	\$ -	\$ 1,170
Loss on Disposition of Assets	\$ -	\$ -	\$ -	\$ -	\$ -
Risk Management Expenses	\$ -	\$ -	\$ -	\$ -	\$ -
Total Operating Expenses	\$ 6,498	\$ 5,013	\$ 5,288	\$ 5,517	\$ 22,317
Interest Expenses	\$ -	\$ -	\$ -	\$ -	\$ -
Other Non-Operating Expenses	\$ -	\$ -	\$ -	\$ -	\$ -
Total non-operating Expenses	\$ -	\$ -	\$ -	\$ -	\$ -
Gain (Loss) Before Taxes	\$ 5,340	\$ 8,767	\$ 11,438	\$ 12,524	\$ 38,070
Income Tax Charge (Recovery)	\$ 790	\$ 1,337	\$ 1,744	\$ 1,910	\$ 5,781
Net Income	\$ 4,550	\$ 7,430	\$ 9,694	\$ 10,614	\$ 32,289
Exchange (loss) gain on translation of foreign operations	\$ (1,462)	\$ -	\$ -	\$ -	\$ (1,462)
Comprehensive (loss) gain	\$ 3,088	\$ 7,430	\$ 9,694	\$ 10,614	\$ 30,827
Net Gain (Loss) per share					
Basic	\$ 0.12	\$ 0.20	\$ 0.26	\$ 0.29	\$ 0.87
Diluted	\$ 0.12	\$ 0.20	\$ 0.26	\$ 0.28	\$ 0.86
Shares O/S - Basic	37,281,649	37,066,651	36,855,868	36,649,219	36,963,347
Shares O/S - Diluted	37,975,282	37,773,293	37,575,265	37,381,119	37,676,240

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Alvopetro has paid fees to present at investor conferences that Trickle Research Co-sponsored.

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Rating System Overview:

There are no letters in the rating system (Buy, Sell Hold), only numbers. The numbers range from 1 to 10, with 1 representing 1 "investment unit" (for my performance purposes, 1 "investment unit" equals \$250) and 10 representing 10 investment units or \$2,500. Obviously, a rating of 10 would suggest that I favor the stock (at respective/current levels) more than a stock with a rating of 1. As a guideline, here is a suggestion on how to use the allocation system.

Our belief at Trickle is that the best way to participate in the micro-cap/small cap space is by employing a diversified strategy. In simple terms, that means you are generally best off owning a number of issues rather than just two or three. To that point, our goal is to have at least 20 companies under coverage at any point in time, so let's use that as a guideline. Hypothetically, if you think you would like to commit \$25,000 to buying micro-cap stocks, that would assume an investment of \$1000 per stock (using the diversification approach we just mentioned, and the 20-stock coverage list we suggested and leaving some room to add to positions around allocation upgrades. We generally start initial coverage stocks with an allocation of 4. Thus, at \$1000 invested per stock and a typical starting allocation of 4, your "investment unit" would be the same \$250 we used in the example above. Thus, if we initiate a stock at a 4, you might consider putting \$1000 into the position ($\$250 * 4$). If we later raise the allocation to 6, you might consider adding two additional units or \$500 to the position. If we then reduce the allocation from 6 to 4 you might consider selling whatever number of shares you purchased with 2 of the original 4 investment units. Again, this is just a suggestion as to how you might be able to use the allocation system to manage your portfolio.

For those attached to more traditional rating systems (Buy, Sell, Hold) we would submit the following guidelines.

A Trickle rating of 1 thru 3 would best correspond to a "Speculative Buy" although we would caution that a rating in that range should not assume that the stock is necessarily riskier than a stock with a higher rating. It may carry a lower rating because the stock is trading closer to a price target we are unwilling to raise at that point. This by the way applies to all of our ratings.

A Trickle rating of 4 thru 6 might best (although not perfectly) correspond to a standard "Buy" rating.

A Trickle rating of 7 thru 10 would best correspond to a "Strong Buy" however, ratings at the higher end of that range would indicate something that we deem as quite extraordinary..... an "Extreme Buy" if you will. You will not see a lot of these.