Trickle Research

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

Allocation and Price Target Upgrade

ALVOPETRO

Alvopetro Energy Ltd.

(TSXV:ALV.V; OTC:ALVOF)

http://alvopetro.com/

Report Date: 02/12/21

12- 24 month Price Target: **USD $1.35

Allocation: *6

Closing Stock Price at Initiation (Closing Px: 11/07/18): USD $.38

Closing Stock Price at Allocation Upgrade (Closing Px: 05/17/19): USD $.42

Closing Stock Price at Target Upgrade (Closing Px: 05/26/20): USD $.52

Closing Stock Price at ate (Closing Px: 02/11/21): USD $.622

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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.

This may be a bit atypical for us in terms of an update on an individual company, but we will go there anyway because we think we have a compelling argument here for raising our allocation for Alvopetro.

Briefly, Alvopetro has an integrated natural gas asset in Brazil. The asset includes ownership/participation in producing gas wells, a midstream gathering and delivery system for that gas into a primary distribution system and a (downstream) gas sales agreement. They are also developing some additional upstream resources that provide additional value to the overall project but could also be enhanced by additional development/discoveries as that process moves forward. Our prior research covers the project in detail so we will not recast that here, however, to summarize, they have been developing the entire turnkey operation for some time now, and the 3QF20 quarter marked their transition of that project from development to commercialization as the quarter reflected the first of what we expect to be sequential quarters of marked revenue and cashflow generation. To translate, much of the risk associated with the project at the time of our initiation is now behind them, so the story has transitioned to a much more visible exercise of measuring and evaluating the value and future deployment of that cash flow. As we alluded, that analysis will include the prospective addition of potential resources which we believe could provide a basis for additional valuation legs beyond the identifiable cashflow piece. However, in our view the current operation represents a considerable premium on its own to the current valuation of the stock, regardless of what future development might uncover.

Specifically, as some may recall, the Company's gas sale agreement includes specific floor pricing that the Company will receive for its gas, regardless of prevailing energy prices. That floor price is recalculated every 6 months to determine the ultimate price they receive, but regardless of that computation, they will not receive less than the computed floor price. We use the term "computed" because the floor price includes an inflation escalator over time so it is not completely static. To edify the 6 month calibration is derived from a basket of prices for worldwide energy prices including Brent Crude, Henry Hub natural gas prices etc. The computation is also weighted to include prior derived pricing amounts, so if energy prices are steadily increasing, the pricing computation gradually increases as well as older (presumably lower) computations are dropped from the equation and are replaced by more recent/higher inputs. In the current environment (steadily increasing energy prices) that clearly bodes well for the prices Alvopetro will receive for its gas in future periods. To reiterate, our current price targets are essentially based on floor prices, but it looks to us like Alvopetro is very likely to get markedly better prices for its gas under the agreement as we move forward, which should lead to better valuations as are result of increased cashflow beyond our current target assessments.

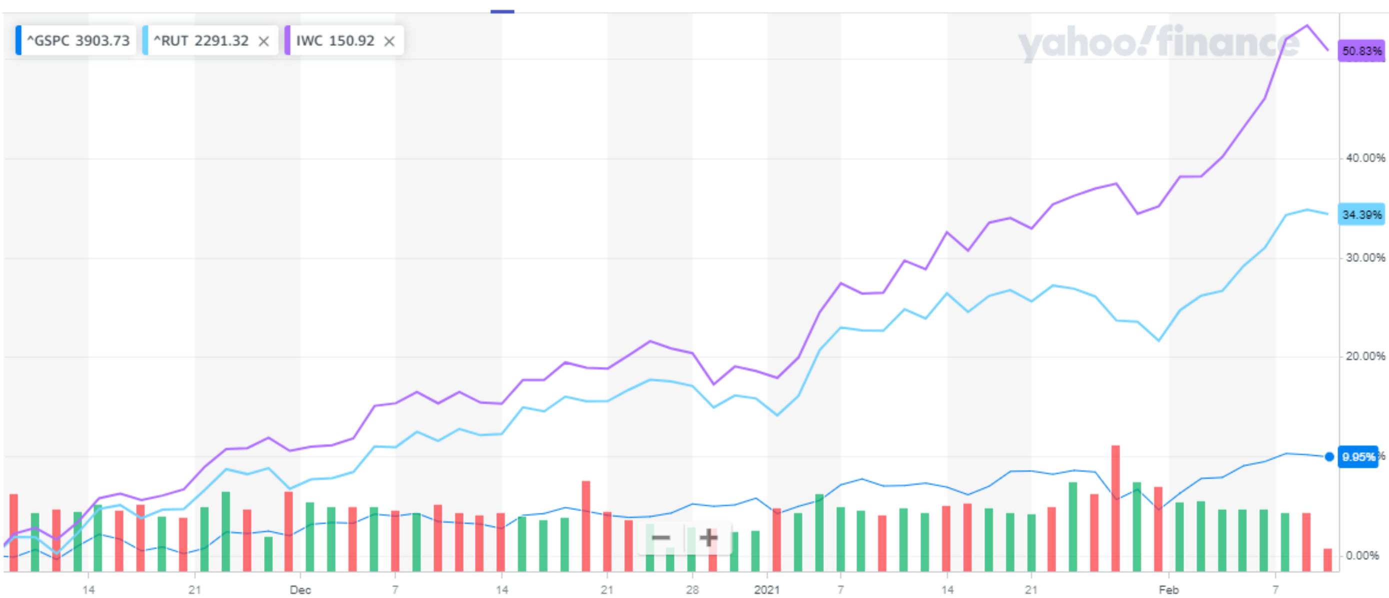
From a macro perspective, US energy policy as telegraphed by the new US administration looks to be far less accommodating to overall US energy production which we think has and will likely continue to encourage higher global energy prices for the foreseeable future. We do not pretend to know where that points ultimately other than to suggest that even current prices will lead to higher prices for Alvopetro. If our math is correct, we think current prices could lead to pricing for Alvopetro that could be 20% to 25% higher than our current model forecasts. Obviously, that will have a considerably positive impact on their cash flow and out target conclusion.

That said, here is the "atypical" macro analysis we mentioned above.

As most of our readers are aware, we are microcap generalists. We follow small companies across a wide variety of industries, and our coverage universe reflects that diversity. Obviously, Alvopetro is one of those companies. As such, we tend not to focus on sectors or industries, but rather on size, and more specifically, we look for companies that we think may have some unique characteristics that may make them successful regardless of what may be going on in the overall market. For instance, we are of the view that even if the equity markets are not performing well, if we (hypothetically) find a small biotech that gets an FDA approval or a new cancer therapy the stock will probably react well regardless of the overall market. We are stock pickers looking for company specific catalysts.

Frankly, that can be a lonely approach at particular times in the market, in part because these company specific catalysts are not always apparent and they often take longer (and more capital) than we expect them to, so we spend a good portion of our time looking wrong about our analysis as we wait for these catalysts to unfold. Sometimes they don't unfold at all, which turns the perception of us being wrong into a reality. On the other hand, when we prove to be correct, the outcomes and associated returns can be extraordinary, which is why we do what we do.

As part of that process, we become keenly aware of impact that macro issues have on microcap stocks in general. That is a broad conversation for another time and place, but for one thing, microcap and small cap markets are *in the aggregate* often impacted (in an outsized way) by things like the risk appetite of the prevailing market, the returns being achieved by larger equity names and the general overall liquidity in equities across the board. Specifically, in the aggregate, microcap and small cap proxies tend to log their best returns during periods of maximum liquidity, which is often marked by larger cap then midcap proxies performing to levels/valuations where investors begin to "reach down" for smaller names. That is where we appear to be today. The illustration below (from Yahoo Finance) reflects that dynamic. The chart below labeled "IWC" represents the iShares Micro-Cap ETF, which we sometimes use as a micro proxy. As the illustration points out, over the past 3 months, small companies represented by the Russell 2000 (RUT below) have performed markedly better than the larger cap S&P 500 (GSPC below), but in turn, the even smaller companies represented by IWC performed even better:



From our perspective, the activity in microcap stocks in the aggregate over the past 90 days have been stunning. Frankly, the appreciation of many in the space is disconcerting. Succinctly, we think the recent surge has pushed many microcap stocks into overbought territory and some of them alarmingly so. While a bit perplexing to us, Alvopetro has for whatever reason not responded as well as many of these, and as such in conjunction with some of the positive emerging issues we noted about as well as its recent emergence into profitability, we think Alvopetro represents a better relative value than the vast majority of microcap companies on our radar. As a result, we are raising our allocation of Alvopetro shares from 5 to *6 to reflective what we see as that relative value. We are also establishing a new (higher) 12-24 month price target of **USD$1.35.

Projected Operating Model

Alvopetro Energy Ltd.										
Projected Operating Model (in USD - '000s)										
By Trickle Research LLC										
	Actual	Actual	Actual	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate
	3/31/20	**6/30/20**	**9/30/20**	**12/31/20**	**Fiscal 2020**	**3/31/21**	**6/30/21**	**9/30/21**	**12/31/21**	**Fiscal 2021**
Oil & Gas Sales	$ 61	$ 40	$ 5,320	$ 5,666	$ 11,087	$ 6,143	$ 6,476	$ 6,964	$ 7,205	$ 26,788
Royalties and Production Taxes	$ (8)	$ (5)	$ (456)	$ (510)	$ (979)	$ (553)	$ (583)	$ (627)	$ (648)	$ (2,411)
					$ -					$ -
Oil & Gas Revenue	$ 53	$ 35	$ 4,864	$ 5,156	$ 10,108	$ 5,590	$ 5,893	$ 6,337	$ 6,557	$ 24,377
Midstream Transportation Revenues	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Other Income	$ 24	$ 20	$ 14	$ -	$ 58	$ -	$ -	$ -	$ -	$ -
Total Revenue and Other Income	$ 77	$ 55	$ 4,878	$ 5,156	$ 10,166	$ 5,590	$ 5,893	$ 6,337	$ 6,557	$ 24,377
					$ -					$ -
Production	$ 44	$ 36	$ 648	$ 671	$ 1,399	$ 671	$ 657	$ 664	$ 671	$ 2,663
Transportation	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
General & Administrative	$ 640	$ 1,032	$ 654	$ 792	$ 3,118	$ 804	$ 812	$ 824	$ 830	$ 3,270
Depletion and Depreciation	$ 62	$ 50	$ 931	$ 1,044	$ 2,087	$ 1,026	$ 993	$ 984	$ 975	$ 3,978
Impairment	$ 1,381	$ -	$ -	$ -	$ 1,381	$ -	$ -	$ -	$ -	$ -
Exploration and Evaluation	$ -	$ -	$ -	$ 33	$ 33	$ 33	$ 33	$ 33	$ 13	$ 111
Finance Expenses and Interest	$ 276	$ 69	$ 996	$ 977	$ 2,318	$ 935	$ 935	$ 893	$ 893	$ 3,656
Accretion of Decommissioning Liabilities	$ -	$ -	$ -	$ 10	$ 10	$ -	$ -	$ -	$ -	$ -
Share Based Compensation	$ 28	$ 39	$ 74	$ 85	$ 226	$ 96	$ 107	$ 120	$ 134	$ 457
Foreign Exchange Loss	$ 9	$ (3)	$ (15)	$ -	$ (9)	$ -	$ -	$ -	$ -	$ -
Loss on Disposition of Assets	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Total Operating Expenses	$ 2,440	$ 1,223	$ 3,288	$ 3,612	$ 10,563	$ 3,565	$ 3,536	$ 3,518	$ 3,516	$ 14,134
Interest Expenses	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Other Non-Operating Expenses	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Total non-operating Expenses	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Gain (Loss) Before Taxes	$ (2,363)	$ (1,168)	$ 1,590	$ 1,545	$ (396)	$ 2,026	$ 2,357	$ 2,819	$ 3,040	$ 10,243
Income Tax Charge (Recovery)	$ -	$ -	$ (4,893)	$ -	$ (4,893)	$ 220	$ 256	$ 306	$ 330	$ 1,111
Net Loss	$ (2,363)	$ (1,168)	$ 6,483	$ 1,545	$ 4,497	$ 1,806	$ 2,101	$ 2,513	$ 2,711	$ 9,131
Exchange (loss) gain on translation of foreign operations	$ (8,352)	$ (1,412)	$ (1,056)	$ -	$ (10,820)	$ -	$ -	$ -	$ -	$ -
Comprehensive (loss) gain	$ (10,715)	$ (2,580)	$ 5,427	$ 1,545	$ (6,323)	$ 1,806	$ 2,101	$ 2,513	$ 2,711	$ 9,131
Net Gain (Loss) per share										
Basic	$ (0.02)	$ (0.01)	$ 0.07	$ 0.02	$ (0.06)	$ 0.02	$ 0.02	$ 0.03	$ 0.03	$ 0.09
Diluted	$ (0.02)	$ (0.01)	$ 0.06	$ 0.02	$ (0.06)	$ 0.02	$ 0.02	$ 0.02	$ 0.03	$ 0.09
Shares O/S - Basic	98,432,818	98,442,412	99,122,412	99,247,412	98,811,264	99,372,412	99,497,412	99,622,412	99,747,412	99,559,912
Shares O/S - Diluted	99,151,563	99,455,171	99,880,275	101,420,337	99,976,837	102,795,392	104,023,120	105,119,306	106,098,043	104,508,965

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Trickle Research co-sponsors two microcap conferences each year. Trickle Research encourages its coverage companies to present at those conferences and Trickle charges them a fee to do so. Companies are under no obligation to present at these conferences.

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

Portions of this publication excerpted from company filings or other sources are noted in *italics* and referenced throughout the report.

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.