

Trickle Research

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



Price Target Increase



Alvopetro Energy Ltd.

(TSXV:ALV.V; OTC:ALVOF)

<http://alvopetro.com/>

Report Date: 05/13/21

12- 24 month Price Target: USD *\$1.50

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 Price Target and Allocation Upgrade (Closing Px: 02/11/21): USD \$.622

Closing Stock Price at This Price Target Upgrade (Closing Px: 05/13/21): USD \$.78

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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.

Yesterday (05/12/21) AlvoPetro reported earnings for Q1-F21. Those numbers were largely in line with our estimates. Revenues were better than our estimates at \$6.9 million versus our estimate of \$6.1 million. Specifically, production was more robust than we anticipated. Second, pre-tax income (loss) was **<\$21,000>** versus our estimate of **+\$2.026 million**. However, the actual numbers included a foreign exchange charge (loss) of **<\$2.065 million>**. To be clear, we do not attempt to model forex items, and without this particular one, they would have reported pre-tax income of \$2.041 million versus our estimate of \$2.026 million, so we feel good about the operating numbers. We would add, they also reflected higher (non-cash) depletion and depreciation charges than we anticipated. Some of that was related to the higher production but they also moved some assets around resulting in a larger depreciable base. That nuance makes up the difference for what would have been even better pre-tax numbers associated with the higher revenues. To translate, the other operating expenses were in-line with our estimates.

On the forex charge, we would add, as the chart below illustrates the Brazilian Real/USD exchange rate was under pressure through most of Q1. That situation has largely rectified itself at least through the first half of Q2. As most of our readers know, we have been pounding the table and shaking our heads about the value of AlvoPetro for some time now. We submit, concerns about Brazil's economy (largely in the face of rising Covid infections) are valid. Certainly, for those who think Brazil is going to be inordinately compromised over the intermediate/long term, then perhaps AlvoPetro will look less compelling. We tend to think those things are more likely to ebb and flow (ala the chart below), but we admit, forex is always a macro risk when owning an asset denominated in a foreign currency.



The above noted, while we thought the quarter was quite positive, in our view, the more telling piece of news came from the Company a few days earlier:

Alvopetro Announces Debt Refinancing

CALGARY, AB, May 3, 2021 /CNW/ - Alvopetro Energy Ltd. (TSXV: ALV); (OTCQX: ALVOF) announces a favorable amendment to our existing senior secured credit facility (the "Facility"). The maturity date of the Facility has been extended by one year to October 8, 2023, the 3% per annum interest payable in kind ("PIK") has been eliminated effective April 15, 2021, and the covenants pertaining to the payment of dividends have been relaxed. With the elimination of the PIK interest, the effective interest rate declines from 12.5% to 9.5%, a 24% savings. The Facility will continue to be repayable at maturity or earlier at Alvopetro's option without penalty.

Corey Ruttan, President and Chief Executive Officer, commented:

"This amendment allows us to continue our valued relationship with Cordiant Capital and recognizes the strong operating and financial results being generated by our Caburé project. This refinancing is a key prerequisite to accelerating our balanced stakeholder return and reinvestment model. Following the drilling of our two high impact exploration prospects (183-B1 and 182-C1), scheduled to start drilling at the end of June 2021, we expect to be in a position to define our 2022 capital expenditure budget and in turn, our stakeholder return model."

Stephen Foss, Managing Director, Cordiant Capital, commented:

"We are pleased to continue our valued relationship with Alvopetro, to provide on-going support as it expands its operations in Brazil. With its strategic initiatives and its demonstrated commitment to ESG principles, we believe the company is well positioned to continue its growth trajectory."

This an issue we have raised of late with some of our subscribers and this announcement validates that view, which is that the Company's transition to production, positive cash flow and positive earnings, is constructive beyond the obvious. We have argued that their improved financial performance would likely ultimately allow them to refinance the credit facility noted above. That in turn, would likely defer (and reduce) the debt service and in turn accelerate the timing of dividends to shareholders. Succinctly, we think the market will have a more difficult time ignoring the value of the enterprise if they start paying meaningful dividends. Moreover, if the resulting dividends are as they anticipate, the yield will be extraordinary relative to the current share price.

Lastly, as the release above alludes, the prospect of added Gomo production is becoming more visible. Recognize, our model does not reflect Gomo production. Frankly, that is the primary reason why our price targets reflect discounts to some of the resource NPV analysis the Company has provided along the way. What we *have done* in our model, is assume some **theoretical** ongoing longer-term revenue via utilization of the midstream assets (tolling fees). To be clear, we have always believed they would ultimately continue to utilize the infrastructure to move their own resources. However, given the lack of reserve data, we were not comfortable building those assumed resources into our targets. At the same time, we felt like the model also needed to reflect the value of the infrastructure they have built beyond the identified resources at Caburé. To edify, we expect the coming clarity regarding Gomo production to provide us a basis to argue new/higher price targets in the not-too-distant future. However, in the meantime, we are also once again establishing a new (higher) 12-24 month price target of *US\$1.50 (versus US\$1.35) based on a handful of improving existing fundamentals including higher production, better resource prices and progress at Gomo, as well as reducing our discount rates in our NPV models based on what we see as continued de-risking of the project. Thinking of the discount rate in terms of cost of capital, the adjustment to the credit facility clearly reflects a lower cost of capital which supports or lower discount rate approach as well.

For now, we are maintaining our allocation of 6, but we will revisit that as visibility improves.

Projected Operating Model

Alvopetro Energy Ltd.					
Projected Operating Model (in USD - '000s)					
By Trickle Research LLC					
	Actual	Estimate	Estimate	Estimate	Estimate
	3/31/21	6/30/21	9/30/21	12/31/21	Fiscal 2021
Oil & Gas Sales	\$ 6,939	\$ 7,491	\$ 8,393	\$ 8,803	\$ 31,626
Royalties and Production Taxes	\$ (645)	\$ (674)	\$ (755)	\$ (792)	\$ (2,867)
					\$ -
Oil & Gas Revenue	\$ 6,294	\$ 6,817	\$ 7,637	\$ 8,011	\$ 28,759
Midstream Transportation Revenues	\$ -	\$ -	\$ -	\$ -	\$ -
Other Income	\$ 8	\$ -	\$ -	\$ -	\$ 8
Total Revenue and Other Income	\$ 6,302	\$ 6,817	\$ 7,637	\$ 8,011	\$ 28,767
					\$ -
Production	\$ 710	\$ 755	\$ 764	\$ 772	\$ 3,001
Transportation	\$ -	\$ -	\$ -	\$ -	\$ -
General & Administrative	\$ 851	\$ 864	\$ 887	\$ 897	\$ 3,499
Depletion and Depreciation	\$ 1,674	\$ 1,606	\$ 1,605	\$ 1,604	\$ 6,490
Impairment	\$ -	\$ -	\$ -	\$ -	\$ -
Exploration and Evaluation	\$ -	\$ 33	\$ 33	\$ 13	\$ 78
Finance Expenses and Interest	\$ 994	\$ 925	\$ 883	\$ 883	\$ 3,685
Accretion of Decommissioning Liabilities	\$ -	\$ -	\$ -	\$ -	\$ -
Share Based Compensation	\$ 89	\$ 116	\$ 130	\$ 146	\$ 481
Foreign Exchange Loss	\$ 2,065	\$ -	\$ -	\$ -	\$ 2,065
Loss on Disposition of Assets	\$ (3)	\$ -	\$ -	\$ -	\$ (3)
Risk Management Expenses	\$ (58)	\$ -	\$ -	\$ -	\$ (58)
					\$ -
Total Operating Expenses	\$ 6,322	\$ 4,300	\$ 4,301	\$ 4,314	\$ 19,238
					\$ -
Interest Expenses	\$ -	\$ -	\$ -	\$ -	\$ -
Other Non-Operating Expenses	\$ -	\$ -	\$ -	\$ -	\$ -
Total non-operating Expenses	\$ -	\$ -	\$ -	\$ -	\$ -
					\$ -
Gain (Loss) Before Taxes	\$ (21)	\$ 2,518	\$ 3,336	\$ 3,696	\$ 9,529
					\$ -
Income Tax Charge (Recovery)	\$ 1,068	\$ 273	\$ 362	\$ 401	\$ 2,104
					\$ -
Net Loss	\$ (1,089)	\$ 2,244	\$ 2,974	\$ 3,295	\$ 7,425
					\$ -
Exchange (loss) gain on translation of foreign operations	\$ (987)	\$ -	\$ -	\$ -	\$ (987)
					\$ -
Comprehensive (loss) gain	\$ (2,076)	\$ 2,244	\$ 2,974	\$ 3,295	\$ 6,438
					\$ -
Net Gain (Loss) per share					
					\$ -
Basic	\$ (0.01)	\$ 0.02	\$ 0.03	\$ 0.03	\$ 0.06
Diluted	\$ (0.01)	\$ 0.02	\$ 0.03	\$ 0.03	\$ 0.06
					\$ -
Shares O/S - Basic	99,726,311	99,851,311	99,976,311	100,101,311	99,913,811
Shares O/S - Diluted	103,674,932	104,808,423	105,820,469	106,724,082	105,256,977

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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.