ALVOPETRO ENERGY LTD.

CONSOLIDATED FINANCIAL STATEMENTS
As at and Years Ended December 31, 2023 and 2022

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INDEPENDENT AUDITORS' REPORT

To the Shareholders and Board of Directors of Alvopetro Energy Ltd.

Opinion

We have audited the consolidated financial statements of Alvopetro Energy Ltd. (the Entity), which comprise:

- the consolidated statements of financial position as at December 31, 2023 and 2022
- the consolidated statements of operations and comprehensive income for the years then ended
- the consolidated statements of changes in equity for the years then ended
- the consolidated statements of cash flows for the years then ended
- and notes to the consolidated financial statements, including a summary of material accounting policies information

(Hereinafter referred to as the "financial statements").

In our opinion, the accompanying financial statements present fairly, in all material respects, the consolidated financial position of the Entity as at December 31, 2023 and 2022, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with IFRS Accounting Standards.

Basis for Opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the "***Auditor's Responsibilities for the Audit of the Financial Statements***" section of our auditor's report.

We are independent of the Entity in accordance with the ethical requirements that are relevant to our audit of the financial statements in Canada and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements for the year ended December 31, 2023. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

We have determined the matters described below to be the key audit matters to be communicated in our auditor's report.

Assessment of the impact of estimated proved and probable oil and gas reserves on the depletion of property, plant and equipment ("PP&E")

Description of the matter

We draw attention to Note 3 and Note 6 to the financial statements. The Entity depletes natural gas and oil assets, which are included within PP&E, using the unit-of-production method using the ratio of production in the period to the related proved and probable oil and gas reserves before royalties. The depletion base includes estimated forecasted future development costs to be incurred in developing proved and probable oil and gas reserves. Depletion and depreciation expense on PP&E was $6,491 thousand for the year ended December 31, 2023.

The estimate of proved and probable oil and gas reserves requires the expertise of independent third party reserve evaluators and includes significant assumptions related to:

- Forecasted natural gas and oil prices
- Forecasted production
- Forecasted operating costs
- Forecasted royalty costs
- Forecasted future development costs.

The Entity engages independent third party reserve evaluators to estimate the proved and probable oil and gas reserves.

Why the matter is a key audit matter

We identified the assessment of the impact of estimated proved and probable oil and gas reserves on the depletion of PP&E as a key audit matter. Significant auditor judgment was required to evaluate the results of our audit procedures regarding the estimate of proved and probable oil and gas reserves.

How the matter was addressed in the audit

The following are the primary procedures we performed to address this key audit matter:

We assessed the depletion expense calculation for compliance with IFRS Accounting Standards.

With respect to the estimate of proved and probable oil and gas reserves:

- We evaluated the competence, capabilities and objectivity of the independent third party reserve evaluators engaged by the Entity
- We compared forecasted natural gas and oil prices to those published by other independent third party reserve evaluators
- We compared the 2023 actual production, operating costs, royalty costs and development costs of the Entity to those estimates used in the prior year's estimate of proved oil and gas reserves to assess the Entity's ability to accurately forecast
- We evaluated the appropriateness of forecasted production and forecasted operating costs, royalty costs and future development costs assumptions by comparing to 2023 historical results. We took into account changes in conditions and events affecting the Entity to assess the adjustments or lack of adjustments made by the Entity in arriving at the assumptions.

Other Information

Management is responsible for the other information. Other information comprises the information included in Management's Discussion and Analysis filed with the relevant Canadian Securities Commissions.

Our opinion on the financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit and remain alert for indications that the other information appears to be materially misstated.

We obtained the information included in Management's Discussion and Analysis filed with the relevant Canadian Securities Commissions as at the date of this auditor's report. If, based on the work we have performed on this other information, we conclude that there is a material misstatement of this other information, we are required to report that fact in the auditor's report.

We have nothing to report in this regard.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRS Accounting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Entity's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Entity or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Entity's financial reporting process.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit.

We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion.

  The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Entity's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Entity's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Entity to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.
- Provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the group Entity to express an opinion on the financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.
- Determine, from the matters communicated with those charged with governance, those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor’s report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our auditor’s report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this auditor’s report is Shane Doig.

KPMG LLP

Chartered Professional Accountants

Calgary, Canada
March 19, 2024

ALVOPETRO ENERGY LTD.

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

(Thousands of United States dollars)

	Note	**December 31, 2023**	December 31, 2022
ASSETS			
Current			
Cash and cash equivalents		**18,326**	19,784
Restricted cash		**72**	296
Trade and other receivables	10	**6,859**	7,154
Prepaid expenditures		**738**	393
Total current assets		**25,995**	27,627
Exploration and evaluation assets	5	**13,785**	16,114
Property, plant and equipment	6	**59,812**	42,460
Right-of-use assets	7	**8,240**	8,701
Deferred tax asset	12	**1,993**	3,525
Total assets		**109,825**	98,427
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities			
Accounts payable and accrued liabilities		**6,662**	7,595
Dividend payable	9	**5,127**	4,357
Lease liabilities	7	**959**	855
Decommissioning liabilities	8	**130**	122
Total current liabilities		**12,878**	12,929
Lease liabilities	7	**7,722**	8,573
Decommissioning liabilities	8	**1,017**	517
Total liabilities		**21,617**	22,019
Shareholders' equity			
Share capital	9	**43,461**	42,933
Contributed surplus		**52,235**	51,361
Retained earnings		**33,570**	25,521
Accumulated other comprehensive loss		**(41,058)**	(43,407)
Total shareholders' equity		**88,208**	76,408
Total liabilities and shareholders' equity		**109,825**	98,427

The accompanying notes are an integral part of these consolidated financial statements.

Approved by:

"signed"

John D. Wright
Chairman of the Board of Directors

"signed"

Firoz Talakshi
Chairman of the Audit Committee

ALVOPETRO ENERGY LTD.

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME

(Thousands of United States dollars, except per share amounts)

		Year ended December 31,	
	Note	**2023**	2022
Revenue			
Natural gas, oil and condensate sales	10	**59,687**	63,508
Royalties		**(1,663)**	(4,486)
Net natural gas, oil and condensate revenue		**58,024**	59,022
Other income	11	**1,795**	923
		59,819	59,945
Expenses			
Production	11	**4,205**	3,550
General and administrative	11	**4,936**	4,984
Depletion and depreciation	6,7	**7,668**	7,003
Impairment	5,6	**10,986**	6,338
Exploration & evaluation		**82**	-
Finance expenses	11	**1,553**	2,378
Share-based compensation		**1,147**	861
Risk management loss		**-**	92
Foreign exchange gain	14	**(3,557)**	(2,706)
		27,020	22,500
Income before taxes		**32,799**	37,445
Income tax expense			
Current	12	**2,520**	1,317
Deferred	12	**1,754**	4,396
Total		**4,274**	5,713
Net income		**28,525**	31,732
Exchange gain on translation of foreign operations		**2,349**	3,116
Comprehensive income		**30,874**	34,848
Net income per share	9		
Basic		**0.77**	0.92
Diluted		**0.76**	0.86

The accompanying notes are an integral part of these consolidated financial statements.

ALVOPETRO ENERGY LTD.

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(Thousands of United States dollars)

	Note	Common Shares	Contributed Surplus	Retained Earnings	Accumulated Other Comprehensive Loss	Total
Balance, December 31, 2022		**42,933**	**51,361**	**25,521**	**(43,407)**	**76,408**
Issue of common shares	9	**175**	**(91)**	**-**	**-**	**84**
Share restructuring	9	**357**	**-**	**-**	**-**	**357**
Shares repurchased	9	**(4)**	**(5)**	**(14)**	**-**	**(23)**
Share-based compensation		**-**	**970**	**-**	**-**	**970**
Net income		**-**	**-**	**28,525**	**-**	**28,525**
Other comprehensive income		**-**	**-**	**-**	**2,349**	**2,349**
Dividends declared	9	**-**	**-**	**(20,462)**	**-**	**(20,462)**
Balance, December 31, 2023		**43,461**	**52,235**	**33,570**	**(41,058)**	**88,208**
Balance, December 31, 2021		39,481	51,580	6,486	(46,523)	51,024
Issue of common shares	9	3,452	(921)	-	-	2,531
Share-based compensation		-	702	-	-	702
Net income		-	-	31,732	-	31,732
Other comprehensive income		-	-	-	3,116	3,116
Dividends declared	9	-	-	(12,697)	-	(12,697)
Balance, December 31, 2022		42,933	51,361	25,521	(43,407)	76,408

The accompanying notes are an integral part of these consolidated financial statements.

ALVOPETRO ENERGY LTD.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Thousands of United States dollars)

	Note	Year ended December 31, 2023	2022
Operating Activities			
Net income		**28,525**	31,732
Adjustments:			
Depletion and depreciation	6,7	**7,668**	7,003
Impairment	5,6	**10,986**	6,338
Finance expenses	11	**1,553**	2,378
Share-based compensation		**1,147**	861
Foreign exchange		**(3,541)**	(2,823)
Deferred tax	12	**1,754**	4,396
Settlement of decommissioning liabilities	8	**(62)**	(6)
Funds flow from operations		**48,030**	49,879
Changes in non-cash working capital	15	**(328)**	(2,345)
		47,702	47,534
Financing Activities			
Dividends paid	9	**(19,692)**	(10,374)
Issue of common shares	9	**84**	2,531
Share restructuring	9	**357**	-
Repurchase and cancellation of common shares	9	**(23)**	-
Lease liabilities payments	7	**(2,274)**	(2,027)
Interest on Credit Facility		**-**	(306)
Credit Facility repayments		**-**	(6,545)
Changes in non-cash working capital	15	**(192)**	175
		(21,740)	(16,546)
Investing Activities			
Expenditures on exploration and evaluation assets	5	**(6,091)**	(18,545)
Expenditures on property, plant and equipment	6	**(21,358)**	(6,250)
Proceeds on dispositions		**-**	5
Change in restricted cash		**264**	(110)
Changes in non-cash working capital	15	**(567)**	2,129
		(27,752)	(22,771)
Change in cash and cash equivalents		**(1,790)**	8,217
Effect of foreign exchange on cash balances		**332**	98
Cash and cash equivalents, beginning of year		**19,784**	11,469
Cash and cash equivalents, end of year		**18,326**	19,784
Cash and cash equivalents consist of:			
Cash		**2,273**	4,498
Cash equivalents		**16,053**	15,286
Supplemental information:			
Cash income taxes paid		**2,730**	1,029
Cash interest income received		**1,262**	324

The accompanying notes are an integral part of these consolidated financial statements.

NOTE 1 – NATURE OF OPERATIONS

Alvopetro Energy Ltd. ("Alvopetro" or "the Company") is engaged in the exploration for, and the acquisition, development and production of, hydrocarbons in Brazil. Alvopetro is incorporated under the Business Corporations Act (Alberta) and is a publicly traded company listed on the TSX Venture Exchange (TSX: ALV.V) and is also traded on the OTCQX® Best Market in the United States (OTCQX: ALVOF).

The Company's head office and records are located at 1920, 215 9th Avenue S.W., Calgary, Alberta, Canada, T2P 1K3.

NOTE 2 – BASIS OF PRESENTATION

Basis of Measurement and Statement of Compliance

These consolidated financial statements have been prepared in accordance with IFRS Accounting Standards ("IFRS") and were authorized for issuance by the Company's Board of Directors on March 19, 2024.

The consolidated financial statements are presented in U.S dollars ("USD") which is the parent Company's functional currency.

Use of Judgments, Estimates and Assumptions

The preparation of financial statements in accordance with IFRS requires management to make judgments, estimates and assumptions that impact the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities, if any, as at the date of the consolidated statements of financial position as well as the reported amounts of revenue, expenses and cash flows during the periods presented. Management makes judgments regarding the application of IFRS for each accounting policy. Estimates and assumptions relate primarily to unsettled transactions and events as of the date of the consolidated financial statements and actual results could differ materially from estimated amounts. These estimates and associated assumptions are based on historical experience and other factors that are considered relevant. Judgments, estimates and assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and on a prospective basis. Estimates are subject to measurement uncertainty and changes in such estimates in future years could require a material change in the consolidated financial statements.

Current Environment and Estimation Uncertainty

Market uncertainty created by global events, including geopolitical factors, international conflicts and bank collapses can have a significant impact on global commodity prices, even more so when such events involve a country that is a major exporter of oil or natural gas. Global markets have been experiencing a period of heightened economic uncertainty with more volatile commodity prices and currency exchange rates, as well as inflationary pressure. It is difficult to reliably estimate the length or severity of the financial impact of these events in their entirety.

The growing demand for and global advancement of alternative energy sources can affect several assumptions used to determine the recoverable amount of the Company's exploration and evaluation assets and property, plant and equipment and the timing and settlement of decommissioning obligations. The time global energy markets will take to transition from carbon-based sources to alternative energy is unknown.

Emissions, carbon and other regulations impacting climate and climate related matters are constantly evolving. Furthermore, the increased focus on environmental, social and governance matters has a multitude of potential implications for the Company including, but not limited to, reduced access to capital markets and increased costs with respect to insurance and financial and human resources required to comply with new regulations.

For Alvopetro, the most significant estimates, judgments and assumptions potentially affected by the situations above, are the valuation of Alvopetro's exploration and evaluation assets and property, plant and equipment. Amounts also recorded for depletion and depreciation, the decommissioning provision and deferred taxes, because they are based on several assumptions and estimates with respect to oil and natural gas proved plus probable reserves, are also impacted by the worldwide economic climate. The potential resulting direct and indirect impact to the Company of these uncertainties has been considered in management's estimates at the period end; however, there could be further material impact in future periods.

Redetermination of Working Interest in the Caburé Natural Gas Field

Substantially all of Alvopetro's natural gas and condensate sales to date have been from the Caburé natural gas field. The field extends across four blocks in the Recôncavo Basin (the "Unit") in the state of Bahia in Brazil, two of which are held by Alvopetro and two of which are held by Alvopetro's third-party partner (the "Partner"). As of December 31, 2023 and the date of these consolidated financial statements, Alvopetro's share of the unitized area (the "Unit") is 49.1% with the Partner holding 50.9%. Under the terms of the Unit Operating Agreement ("UOA"), each party is entitled to nominate for their working interest share of field production and for any natural gas not nominated for by the other party. Once a party produces their share of estimated recoverable hydrocarbons from the Unit ("Unit Recoverable Volumes") as determined by Alvopetro and the Partner, they will no longer be entitled to further production allocations. Natural gas liquids production from the Unit (relating to condensate production) is split based on working interest.

Under the terms of the UOA, the working interest to each party is subject to redeterminations, the first of which commenced in the fourth quarter of 2023. In accordance with the UOA the parties engaged an independent expert (the "Expert") to evaluate the redetermination and select a single final proposal (between the two partner's respective final proposals), which, in the Expert's opinion, provides the most technically justified result of the application of the relevant information and data and material provided to the Expert consistent with the UOA and all related documents. The decision of the Expert is expected near the end of the first quarter of 2024. As of the date of these consolidated financial statements, the outcome of the Expert's decision and the resulting working interest to Alvopetro following the decision is uncertain. The impact on Alvopetro's working interest will be effective on the first calendar day of the second month following the date of the decision of the Expert, subject to any government approvals that may be required. Given the effective date of the Expert decision, there is no impact on the consolidated financial statements as at and for the year ended December 31, 2023 and all amounts presented herein are based on Alvopetro's working interest share as of December 31, 2023. Once the new working interests are effective, the following financial statement items will be affected:

Property, Plant & Equipment
Pursuant to the UOA, an adjustment will be calculated to update each party's share of capital costs relating to historical capital expenditures of the Unit. If Alvopetro's working interest increases, the Company will incur PP&E additions and an additional liability for the incremental amount. If Alvopetro's working interest is reduced, PP&E will be decreased and a receivable will be recorded by Alvopetro from the Partner.

Depletion Expense
Because this adjustment will impact the Company's working interest related to its Caburé reserves there will be an effect on depletion expense and accumulated depletion (PP&E). If Alvopetro's working interest increases resulting in an increase in future reserves attributable to Alvopetro, the depletion rate and resulting depletion expense will go down, the effect on depletion expense being offset by the increase in PP&E as discussed above. If Alvopetro's working interest and reserves decrease following the Expert decision, the depletion rate will go up with the decrease in capital discussed above offsetting the depletion expense.

Asset Retirement Obligations
As the Company records asset retirement obligations based on its working interest in wells and infrastructure, a change in working interest for Caburé will result in a revised obligation which will affect PP&E as well as decommissioning liabilities.

Impairment
The change in working interest will affect the reserves and future estimated cash flows to Alvopetro from the Unit. To the extent Alvopetro's working interest is reduced following the Expert decision, while such a reduction may be an indication of impairment, Alvopetro does not expect that the estimated recoverable amount following a working interest reduction would be less than the carrying value at December 31, 2023. However, the reduced working interest would impact future impairment assessments and an impairment may be required in the future.

Revenues
Under the terms of the UOA each party is entitled to nominate natural gas deliveries based on their working interest share plus any natural gas not nominated by the other party. To the extent Alvopetro's working interest is reduced following the Expert decision, Alvopetro will be entitled to lower natural gas deliveries from the Unit resulting in lower revenues going forward. To the extent Alvopetro's working interest is increased following the Expert decision, Alvopetro will be entitled to higher natural gas deliveries from the Unit and may be entitled to higher revenues, subject to demand. As revenues have an impact on the Company's working capital, a change in working interest will affect liquidity and potentially the Company's ability to fund future capital plans and the discretionary dividends.

Condensate sales from the Unit are split based on working interest. Under the terms of the UOA, following a redetermination each party will be entitled to their new working interest share plus or minus an adjustment to recover past volumes of condensate sales at the revised working interest share compared to the original working interest share.

Once a party produces their share of Unit Recoverable Volumes as determined by Alvopetro and the Partner, they will no longer be entitled to further production allocations. The outcome of the redetermination will change the Company's share of the overall Unit Recoverable Volumes and a reduction in the total volumes allocated to Alvopetro would reduce the reserve life. Once fully depleted, Alvopetro would no longer be entitled to production allocations from the Unit.

Judgments, estimates and assumptions made by management that have the most significant effect on the amounts recognized in the consolidated financial statements are discussed further in Note 3.

NOTE 3 – MATERIAL ACCOUNTING POLICIES

Consolidation

These consolidated financial statements include the accounts of Alvopetro and its controlled subsidiaries. Intercompany transactions and balances are eliminated on consolidation. As at December 31, 2023 and 2022, the Company controls 100 percent of its subsidiaries (see Note 16).

Joint Operations

The Company has oil and gas exploration activities that are conducted jointly with others and these consolidated financial statements reflect the Company's proportionate share of the assets, liabilities, revenues, expenses and cash flows from such activities. A joint arrangement is either a joint operation, whereby the parties have rights to the assets and obligations for the liabilities, or a joint venture, whereby the parties have rights to the net assets. The determination of a joint arrangement requires management's judgment and interpretation of IFRS. The classification of a joint arrangement between joint operations and joint venture, which requires further judgment and interpretation, will affect how the financial position and results of the joint arrangement are accounted for.

Exploration and Evaluation ("E&E") Assets

Pre-exploration and pre-licensing costs associated with the investigating, bidding and acquisition of petroleum properties are expensed as exploration and evaluation expense when the targeted petroleum lease or concession is not obtained.

Costs incurred subsequent to obtaining the rights to explore, and prior to establishing commercial viability and technical feasibility, are classified as E&E assets. Such costs include land and license acquisition, technical services and studies, exploration drilling and testing, and directly attributable employee compensation. E&E assets also include equipment inventory, some of which is used for future exploration wells and some of which is transferred to PP&E for development projects. E&E assets are not depleted and are classified as such until they are considered technically feasible and commercially viable.

When E&E assets are considered technically feasible and commercially viable, they are reclassified to PP&E. Technical feasibility and commercial viability is initially indicated by the assignment of proved and/or probable reserves and then further subject to management judgement considering all relevant factors. Upon determination of technical feasibility and commercial viability, the E&E assets are tested for impairment and the estimated recoverable amount is transferred to PP&E.

The determination of technical feasibility and commercial viability and the impairment assessment requires significant judgment, estimates and assumptions with respect to future prospects, drilling success, well results from other activities including completions and stimulations, existing commitments and expiry of rights to explore, available funds, projected production rates, future market conditions and other significant changes (technological, economic, legal, regulatory).

Property, Plant and Equipment ("PP&E")

PP&E consists primarily of natural gas and oil development and production assets and, to a lesser extent, operational equipment and corporate assets.

Natural gas and oil assets, which are included in property, plant and equipment, include all costs directly associated with the development of natural gas and oil reserves. These expenditures include proved property acquisitions, geological and geophysical costs, development drilling and completions on productive and non-productive wells, infrastructure, decommissioning liabilities, directly attributable employee compensation and transfers from exploration and evaluation assets where technical feasibility and commercial viability has been established.

Natural gas and oil assets are accumulated on a cash generating unit ("CGU") basis. Costs accumulated within each CGU are depleted using the unit-of-production method using the ratio of production in the period to the related proved and probable oil and gas reserves before royalties as determined annually by independent third-party reserves evaluators. The depletion base consists of capitalized costs and estimated future development costs to be incurred in developing proved and probable reserves.

Costs related to replacing parts of assets included in PP&E are capitalized only when they increase the future economic benefits to be derived from the specific asset to which they relate. All other expenditures are recognized as an expense in the consolidated statements of operations and comprehensive income as incurred. The carrying amount of any replaced or sold component is derecognized.

The Company uses estimated proved and probable oil and gas reserves to deplete PP&E, to assess for indicators of impairment or impairment reversal on the Company's CGUs and if any such indicators exist, to perform an impairment test to estimate the recoverable amount of the CGU. The estimation of proved and probable oil and gas reserves, is an inherently complex process which involves professional judgment and geoscientific interpretation as well as determination of forecasted production, forecasted natural gas and oil prices and the timing and amount of forecasted operating costs, forecasted future development costs and forecasted royalties, all of which are subject to uncertainty. Key estimates used in determining future cash flows from proved and probable oil and gas reserves include:

> *Reserves* – Assumptions that are valid at the time of reserve estimation may change significantly when new information becomes available. Changes in forecasted natural gas and oil prices, production costs, required development costs or recovery rates may change the economic status of reserves and may ultimately result in reserves being revised.
>
> *Natural gas and crude oil prices* – Forward price estimates are used in the discounted cash flow model. These prices are adjusted for quality differentials, heat content and other factors. Commodity prices can fluctuate for a variety of reasons including supply and demand fundamentals, inventory levels, exchange rates, weather, economic and geopolitical factors.
>
> *Discount rate* – The discount rate used to calculate the net present value of cash flows is based on estimates of an industry peer group weighted average cost of capital as appropriate for each CGU being tested. Changes in the general economic environment could result in significant changes to this estimate.

Impairment

E&E assets, which are comprised of the accumulated expenditures for each block for which technical feasibility and commercial viability has not yet been determined, are reviewed quarterly for indicators of impairment and at the time of transfer to PP&E. Indicators of impairment consist of facts and circumstances suggesting that the carrying amount of an exploration and evaluation asset may exceed its recoverable amount. Where the carrying amount exceeds the estimated recoverable amount, the unrecoverable costs are charged to the consolidated statements of operations and comprehensive income.

PP&E assets are grouped for impairment purposes by CGU and reviewed quarterly for indicators of impairment. An impairment test is performed whenever events or changes in circumstances indicate that the carrying value of the asset or CGU may not be recoverable. The CGU's recoverable amount is the greater of its fair value less costs of disposal and its value-in-use. Fair value less costs of disposal incorporates management's judgment, determined using discounted future cash flows of reserves at forecasted prices and costs. The value-in-use is determined by estimating the present value of the future net cash flows expected to be derived from the continued use of the asset or CGU. If the carrying amount exceeds the estimated recoverable amount, the CGU is written down with an impairment loss recorded in the consolidated statement of operations and comprehensive income.

Impairment losses from previous periods are assessed at each reporting date for indications that the impairment loss no longer exists or has decreased. Impairment losses can be reversed if there is a change in the estimates used to determine the recoverable amount but cannot exceed the carrying value of the asset prior to impairment less any depreciation and depletion that would have been taken if no impairment had been recognized.

Leases

A contractual arrangement where a party has the right to control the use of an identified asset in exchange for consideration is or contains a lease. The Company recognises a right-of-use asset and a corresponding lease liability with respect to all lease arrangements in which it is the lessee, except for short-term leases (defined as leases with a lease term of 12 months or less) and leases of low value assets. For these leases, the Company recognises the lease payments as an operating expense on a straight-line basis over the term of the lease unless another systematic basis is more representative of the time pattern in which economic benefits from the leased assets are consumed.

At commencement, determined to be when the leased asset is available for use, the lease liability is recognized, measured at the present value of the lease payments that are not paid at the commencement date and discounted using the implicit lease rate or Alvopetro's incremental borrowing rate when the implicit rate is not readily determinable. A corresponding right-of-use ("ROU") asset is recognized. The ROU asset is based on the initial measurement of the corresponding lease liability, lease payments made at or before the commencement day, less any lease incentives received and any initial direct costs. ROU assets are subsequently measured at cost less accumulated depreciation and impairment losses.

The ROU asset is depreciated over the shorter of: 1) the asset's useful life; and 2) the lease term on a straight-line basis. Adjustments to the ROU asset are made if the contractual arrangement includes costs to dismantle the asset.

The lease liability is remeasured when there is a change in future lease payments arising from a change in rate, a change to the Company's expected residual value guarantee payable, or changes in the assessment for exercising a purchase, termination or extension option. Lease payments are allocated between repayment of the lease liability and finance expense which is charged to the consolidated statements of operations and comprehensive income.

The measurement of lease obligations is subject to management's judgements, including the applicable incremental borrowing rate, based on assessment of the economic environment, term and underlying risk inherent to the asset. The carrying balance of the right-of-use assets, lease obligations, and the resulting interest and depletion and depreciation expense may differ due to changes in the market conditions and expected lease terms.

Decommissioning Liabilities

The Company recognizes the present value of the estimated future decommissioning liabilities related to statutory, contractual or other legal obligations associated with the retirement of assets. A corresponding increase to the carrying amount of the related asset is recorded.

Decommissioning liabilities are based on the estimated costs to abandon and reclaim all wells, facilities and pipelines as required under the terms of concession contracts and laws and regulations within Brazil. The liability is discounted using the risk-free rate based on Brazil government bond rate for maturities coinciding as closely as possible with the estimated remaining years to abandonment.

In estimating future decommissioning liabilities various assumptions are required with respect to the amount and timing of abandonment and reclamation costs, inflation factors, future interest rates and potential changes in the legal, regulatory, environmental and political environments.

Revenue Recognition

The Company's revenues are primarily derived from the production of natural gas and to a lesser extent condensate and oil production. Revenue is recognized when the performance obligations are satisfied and revenue can be reliably measured. The performance obligations are satisfied upon delivery, when control of the product has transferred to the customer, being when the product has been physically transferred to the contracted delivery point. Revenue is measured at the consideration specified in the contract and represents amounts receivable for the hydrocarbons sold, net of discounts and sales taxes.

Income Taxes

Income tax expense is comprised of current and deferred income taxes. Income tax expense is recognized in the consolidated statements of operations and comprehensive income except to the extent that it relates to items recognized directly in equity.

Current tax expense is based on estimated taxable income and tax rates which are determined pursuant to tax law enacted or substantively enacted at the reporting date, adjusted for any available tax incentives or benefits which reduce current tax otherwise payable.

The Company follows the liability method of accounting for deferred taxes. Under this method, deferred income tax assets or liabilities are recorded to reflect the difference between the accounting and tax base of assets and liabilities and unused tax losses. Deferred income taxes are measured using tax rates that are expected to apply to the period when the deferred tax asset is realized or the deferred tax liability is settled, based on tax rates and tax laws that have been enacted or substantively enacted by the end of the reporting period. The impact of tax benefits and incentives which may reduce the Company's income tax expense are considered in determining the expected future rates.

Deferred income tax assets are recognized for deductible temporary differences to the extent it is probable that future taxable profit will be available. The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent it is no longer probable that sufficient taxable profits will be available to allow the assets to be recovered. Deferred income tax assets and liabilities are offset only if there is a legally enforceable right to offset and they relate to income taxes levied by the same tax authority on the same taxable entity or on different tax entities to the extent they could be realized simultaneously.

The determination of deferred taxes requires interpretation of complex laws and regulations involving multiple jurisdictions. The measurement of income tax expense and deferred tax assets and liabilities is based on judgment in applying tax law and estimates on the applicable tax rates, available tax incentives, and the timing, likelihood and reversal of temporary differences between the accounting and tax bases of assets and liabilities as well as the expected recoverability of deferred tax assets. The extent to which deferred tax assets are recognized are based on estimates of future profitability which are based on estimated future commodity prices and estimates of reserves, all of which are subject to management estimates, judgments and assumptions. Tax interpretation, regulations, and legislation in both Canada and Brazil are subject to change and interpretation which can affect the timing of the reversal of temporary tax differences, the tax rates in effect when such differences reverse and the Company's ability to utilize tax losses and other tax pools in the future. All tax filings are subject to audit and potential reassessment after the lapse of considerable time. If any of these judgments and estimates prove to be inaccurate, actual results may differ significantly from that estimated and recorded by management and future earnings may be impacted.

Foreign and Reporting Currency

The Company's functional currencies are the BRL for all Brazil entities and the USD for all Canadian entities. Alvopetro has chosen to present its consolidated financial statements in USD.

The designation of the Company's functional currencies is a judgment made by management based on the currency of the primary economic environment in which the Company operates. Despite the fact that the contracted price for natural gas under the Company's long-term natural gas sales agreement is derived from international benchmark prices in USD and the benchmark price for oil and condensate is set in USD, due to the business environment as well as foreign exchange and banking regulations in Brazil, management is of the opinion that the primary economic environment influencing the Company's labour, material and other costs as well as actual cash receipts from sales is Brazil.

Transactions in currencies other than the entity's functional currencies are recognized at the rates of exchange prevailing on the date of the transactions. At the end of each reporting period, monetary assets and liabilities denominated in foreign currencies are translated at the exchange rate in effect at the reporting period date. Non-monetary assets, liabilities, revenues and expenses are translated at transaction date exchange rates. Any exchange gains or losses are included in the determination of net income on the consolidated statement of operations and comprehensive income.

The assets and liabilities of all Brazil entities are translated to USD at exchange rates at the reporting date. The income and expenses of foreign operations are translated to USD at exchange rates at the date of the transactions. Resultant foreign currency differences are recognized in other comprehensive income on the consolidated statements of operations and comprehensive income.

Amounts receivable from a foreign operation are considered part of the reporting entity's net investment when settlement is neither forecasted nor likely to occur in the foreseeable future. Foreign exchange gain or losses related to such items are recognized in other comprehensive income and presented in accumulated other comprehensive income in equity. Such amounts are retained in accumulated other comprehensive income and released to earnings where the Company has disposed of its entire interest in the foreign operation or loses control, joint control or significant influence over a foreign operation. Where any amounts receivable from a foreign operation are expected to be settled in the foreseeable future, foreign exchange gains or losses related to such items are recognized in the consolidated statements of income and comprehensive income from the date the Company determines such future settlement is likely to occur.

The determination of the timing and quantum of any anticipated settlement of amounts receivable from foreign operations and the resulting treatment of any foreign exchange gains or losses on such intercompany amounts is subject to judgment based on management estimates and assumptions of future profitability and capital and other activities, all of which are subject to additional uncertainties.

Financial Instruments

The Company's financial instruments consist of cash and cash equivalents, restricted cash, trade and other receivables, accounts payable and accrued liabilities and dividends payable. These financial instruments are measured at amortized cost.

Fair Value Hierarchy

The fair value of financial instruments and certain other non-financial items recorded fair value are categorized using a three-level hierarchy which reflects the inputs available for measurement:

Level 1 – values based on quoted prices in active markets for identical assets or liabilities;

Level 2 – values based on quoted market prices for similar instruments in markets that are not active or model inputs that are observable either directly or indirectly; and

Level 3 – values based on inputs that are unobservable for the asset or liability.

The estimated fair value of the Company's financial instruments approximates their carrying value due to their short term to maturity.

Derivative Instruments

The Company may at times use derivative instruments to manage its exposure to fluctuations in commodity prices, foreign currency exchange rates or interest rates. Alvopetro does not use financial derivatives for trading or speculative purposes. Derivative instruments, when employed, are recorded at fair value with changes in the fair value of the instruments recognized in the consolidated statements of operations.

As the delivery and receipt of a non-financial item is the underlying premise of the Company's long-term gas sales agreement ("GSA") it is accounted for as an executory contract. As such, it is not considered to be a financial asset or liability and settlements on the physical deliveries are recognized as natural gas revenue in the period the product is delivered to the sales point.

Impairment of Financial Assets

At each reporting date the Company assesses any objective evidence that a financial asset carried at amortized cost is impaired. Management uses judgment in making these assumptions, taking into consideration past loss history, existing market conditions and forward-looking estimates at the end of each reporting period. Any impairment is recorded in the consolidated statements of operations.

Segmented Operations

All natural gas, oil and condensate sales revenue is derived from Brazilian operations. All exploration and evaluation assets and all material property, plant and equipment are located in Brazil. Cash and cash equivalents are held in both Canada and Brazil and all of the restricted cash at December 31, 2023 and 2022 is held in Brazil. The Company does not have any revenue in Canada other than interest earned on cash balances.

NOTE 4 – CHANGES IN ACCOUNTING STANDARDS

On January 1, 2023 the Company adopted amendments to IAS 1, *Presentation of Financial Statements* which requires the disclosure of 'material' rather than 'significant' accounting policies. The amendments became effective for annual periods beginning January 1, 2023 and have been applied prospectively by the Company. The amendments did not have an impact on the accounting polices themselves or the consolidated financial statements as at and for the year ended December 31, 2023.

The Company has reviewed the following new and revised accounting pronouncements that have been issued but are not yet effective and may have a potential impact on the consolidated financial statements of the Company:

Standard and Description	Date of Adoption	Expected Impact on Consolidated Financial Statements
IAS 1 *Presentation of Financial Statements* – amended to clarify the requirements for presentation of liabilities in the statement of financial position and to modify how an entity classifies debt and other financial liabilities as current or non-current in particular circumstances.	January 1, 2024	The Company is evaluating the expected impact on the financial statements.

All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted

NOTE 5 – EXPLORATION AND EVALUATION ASSETS

	As at	
	December 31, 2023	December 31, 2022
Balance, beginning of year	**16,114**	3,713
Capital expenditures	**6,091**	18,545
Capitalized share-based compensation	**8**	66
Change in decommissioning liabilities	**191**	90
Transfer to PP&E (Note 6)	**(3,025)**	(155)
Asset dispositions & other transfers	**(22)**	(4)
Impairment	**(6,748)**	(6,338)
Foreign currency translation	**1,176**	197
Balance, end of year	**13,785**	16,114

During the year an impairment loss of $6.7 million (2022 - $6.3 million) was recognized on Block 182. The 182-C1 well, drilled in 2022, indicated non-commercial amounts of hydrocarbons during testing and the well was subsequently abandoned and written down to a $nil carrying value at December 31, 2022. The 182-C2 well was drilled to re-test the prospect, however it was later found to be water-saturated, and management has determined there are limited further prospects for this block. Alvopetro plans to decommission the 182-C2 well in 2024 and the carrying value of the block was impaired to a $nil value at December 31, 2023.

General and administrative costs totaling $0.1 million (December 31, 2022 - $0.9 million) that were directly related to exploration and evaluation activities have been capitalized as exploration and evaluation assets.

Included in E&E assets is equipment inventory with a carrying value of $6.4 million (December 31, 2022 - $3.3 million).

NOTE 6 – PROPERTY, PLANT AND EQUIPMENT

	As at	
	December 31, 2023	December 31, 2022
Cost, beginning of year	**57,144**	47,766
Capital expenditures	**21,358**	6,250
Capitalized share-based compensation	**131**	40
Transfer from E&E assets (Note 5)	**3,025**	155
Other transfers	**-**	(5)
Change in decommissioning liabilities	**338**	(106)
Foreign currency translation	**4,770**	3,044
Cost, end of year	**86,766**	57,144
Accumulated depletion, depreciation and impairment, beginning of year	**(14,684)**	(7,986)
Depletion and depreciation	**(6,491)**	(5,961)
Impairment	**(4,238)**	-
Foreign currency translation	**(1,541)**	(737)
Accumulated depletion, depreciation and impairment, end of year	**(26,954)**	(14,684)
Net book value, end of year	**59,812**	42,460

General and administrative costs totaling $1.3 million (December 31, 2022 - $0.6 million) that were directly related to property, plant, and equipment activities have been capitalized.

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At the end of each reporting period the Company assesses impairment and impairment reversal indicators for each CGU. The lower than-anticipated production volumes from the BL-06 well, which came on production in the fourth quarter of 2023, triggered an impairment indicator for Bom Lugar. An impairment test indicated that the carrying value for this block exceeded the recoverable amount. Impairment of $4.2 million was recorded to reduce the carrying value to the estimated recoverable amount of $4.6 million. The estimated recoverable amount was determined using the fair value less costs of disposal calculations, considered to be a Level 3 fair value measurement with management's best estimates forming the key assumptions. In determining the estimated recoverable amount, the Company incorporated the net present value of the future cash flows from proved plus probable reserves estimated by the Company's independent third-party reserves evaluator. The key assumptions used to determine the recoverable amounts for purposes of the impairment test were commodity prices, the after-tax discount rate of 18%, timing and cost of future capital plans, anticipated foreign exchange rates and an expected tax rate of 15.25%. The Company utilized forecasted oil prices from its independent third-party reserves evaluator as follows:

Year	Brent ($/bbl)[1] As at December 31, 2023
2024	**77.00**
2025	**79.50**
2026	**81.49**
2027	**82.58**
2028	**84.19**
2029	**85.90**
Thereafter – escalated at	**2.0%**

(1) Actual prices used in the computation of discounted future cash flows were adjusted for quality differentials and negotiated discounts under the Bom Lugar oil sales contract.

The actual recoverable amount will be different from what was estimated for the purposes of determining impairment. The most significant variances are commodity prices and the discount rate. The following table depicts the impact differences in these assumptions would have on the estimated recoverable amount for Bom Lugar at December 31, 2023.

	Increase (Decrease) December 31, 2023
Commodity price – 5% higher	**530**
Commodity price – 5% lower	**(491)**
Discount rate – 5% higher	**(1,195)**
Discount rate – 5% lower	**1,789**

NOTE 7 – RIGHT-OF-USE ("ROU") ASSETS AND LEASE LIABILITIES

The Company's contracts that contain leases or lease components include equipment for processing natural gas and access to land for midstream development in Brazil as well as office space in both Canada and Brazil. The net book value of the Company's ROU assets is as follows.

	As at December 31, 2023	December 31, 2022
Net book value, beginning of year	**8,701**	7,153
Additions	**26**	1,930
Depreciation	**(1,177)**	(1,042)
Foreign currency translation	**690**	660
Net book value, end of year	**8,240**	8,701

All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted

Net Book Value by Asset Class		
Natural gas facility	**8,094**	8,477
Office space	**71**	138
Surface land access	**75**	86
Total net book value	**8,240**	8,701

The Company's lease liabilities are as follows:

	As at	
	December 31, 2023	December 31, 2022
Lease liabilities, beginning of year	**9,428**	7,979
Additions	**26**	1,930
Finance expense	**1,495**	1,525
Lease payments	**(2,274)**	(2,027)
Foreign currency translation	**6**	21
Lease liabilities, end of year	**8,681**	9,428
Current	**959**	855
Non-current	**7,722**	8,573
Total	**8,681**	9,428

The majority of the right-of-use assets and the lease liabilities are related to the lease component contained in Alvopetro's 10-year contract (the "Gas Treatment Agreement") with Enerflex Ltd. ("Enerflex") expiring in July 2030. Under the Gas Treatment Agreement, Enerflex constructed, maintains, operates and warranties the onstream performance of the natural gas treatment facility ("the Facility") to process natural gas from the Company's Caburé and Murucututu natural gas fields. The additions in 2022 relate primarily to incremental monthly equipment costs associated with the Facility expansion.

The right-of-use assets are depreciated over the lease term. The present value of future minimum lease payments were discounted using a rate of 17%.

Not included in the lease component of the Gas Treatment Agreement is the contracted monthly service fees of approximately $1.6 million per year. The estimated total to the end of the contract is $10.4 million, calculated based on the USD equivalent of the BRL-denominated payments at December 31, 2023.

NOTE 8 – DECOMMISSIONING LIABILITIES

The decommissioning liabilities were estimated based on the net ownership interest of wells, facilities and pipelines, management's estimates of costs to abandon and reclaim those wells and infrastructure, and the potential future timing of the costs to be incurred.

	As at	
	December 31, 2023	December 31, 2022
Balance, beginning of year	**639**	568
Liabilities incurred	**33**	84
Revisions to obligations	**496**	(100)
Obligations settled - cash	**(62)**	(6)
Obligations settled – non cash	**(21)**	-
Accretion	**58**	51
Foreign currency translation	**4**	42
Balance, end of year	**1,147**	639

Current	**130**	122
Non-current	**1,017**	517
Total	**1,147**	639

Total undiscounted cash flows, escalated at 3.5% (December 31, 2022 - 3.1%) for inflation, required to settle the Company's decommissioning liabilities are estimated to be $14.9 million (December 31, 2022 - $11.8 million). These estimated cash flows are discounted using an average risk-free rate of 8.9% (December 31, 2022 – 8.1%).

NOTE 9 – SHARE CAPITAL

a) Authorized

Alvopetro has an unlimited number of common shares authorized for issuance. The Company is also authorized to issue preferred shares in one or more series.

Issued and Outstanding Common Shares

	Year Ended December 31,			
	2023		**2022**	
	Number of Shares	**Amount ($000)**	Number of Shares	Amount ($000)
Balance, beginning of year	**36,311,579**	**42,933**	33,903,629	39,481
Exercise of stock options	**310,961**	**175**	326,334	217
Exercise of warrants(1)	**-**	**-**	2,081,616	3,235
Share restructuring	**-**	**357**	-	-
Repurchase and cancellation of shares	**(4,600)**	**(4)**	-	-
Balance, end of year	**36,617,940**	**43,461**	36,311,579	42,933

(1) All outstanding warrants were exercised in 2022 and no warrants were outstanding on December 31, 2023 or December 31, 2022.

In 2023 Alvopetro received approval from the TSX Venture Exchange ("TSXV") for a normal course issuer bid (the "NCIB"). During the year a total of 4,600 Alvopetro Energy common shares were repurchased and subsequently cancelled through the Company's TSXV-approved automatic share purchase plan. The NCIB expired on January 5, 2024 with no further share repurchases in 2024. The average per-share value in the share capital account prior to the repurchase was applied to the number of shares cancelled to reduce share capital. The difference between the reduction in share capital and the amount paid for the shares repurchased has been allocated to contributed surplus and retained earnings.

In 2021 Alvopetro completed a 2,100:1 share consolidation immediately followed by a 1:700 split (the "Share Restructuring"), resulting in an effective 3:1 share consolidation. Pursuant to the Share Restructuring, shareholders who held less than 2,100 shares immediately prior to the Share Restructuring (the "Non-Continuing Shareholders") were entitled to cash consideration upon surrender of their shares. Under the court approved transaction, Non-Continuing Shareholders had two years from the date of the Share Restructuring to provide the documentation required to receive the cash payment. At the time of the Share Restructuring, Alvopetro deposited a total of $1.1 million with a depositary for payments to be made to Non-Continuing Shareholders. In September 2023, following the two-year anniversary date of the Share Restructuring, a total of $0.4 million of the initial deposit remained unclaimed and was returned to Alvopetro in 2023.

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b) Options to Purchase Common Shares

Alvopetro has a share-based compensation plan whereby the Company may grant stock options to its directors, officers, employees and consultants as part of the Company's long-term incentive plan to align compensation with shareholders' interests. The options outstanding are as follows:

	Number of Options	Weighted Average Exercise Price (CAD$)
Balance as at December 31, 2021	1,445,108	2.58
Granted	550,000	6.94
Exercise of options	(430,112)	2.07
Balance as at December 31, 2022	1,564,996	4.25
Granted	**638,000**	**8.01**
Exercise of options	**(384,556)**	**1.83**
Options forfeited	**(17,000)**	**7.21**
Balance as at December 31, 2023	**1,801,440**	**6.07**
Percentage of common shares outstanding	**4.9%**	

	Options Outstanding at December 31, 2023			**Options Exercisable at December 31, 2023**		
Exercise Price	Number of Options	Weighted Average Exercise Price (CAD$)	Weighted Average Remaining Contractual Life (Years)	Number of Options	Weighted Average Exercise Price (CAD$)	Weighted Average Remaining Contractual Life (Years)
CAD$2.25 - $3.99	374,441	2.41	2.1	267,775	2.40	1.6
CAD$4.00 - $5.99	260,666	4.84	2.9	154,670	4.84	2.9
CAD$6.00 - $7.99	532,333	6.95	3.9	94,669	6.96	3.9
CAD$8.00 - $8.01	634,000	8.01	4.9	-	-	-
CAD$2.25 - $8.01	**1,801,440**	**6.07**	**3.7**	**517,114**	**3.96**	**2.4**

c) Restricted Share Units and Deferred Share Units

Alvopetro has a share-based compensation plan whereby the Company may grant RSUs, DSUs and performance share units ("PSUs") to purchase common shares of the Company.

	Number of RSUs & DSUs
Balance as at December 31, 2021	563,165
Granted	166,123
Balance as at December 31, 2022	**729,288**
Granted	**152,253**
Balance at December 31, 2023	**881,541**
Percentage of common shares outstanding	**2.4%**
Weighted average remaining contractual life (years)	**3.7**

All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted

d) Share-Based Compensation

The fair value of the DSUs and RSUs is estimated based on the share price on the grant date. The fair value of the stock options is estimated on the grant date using the Black-Scholes option pricing model. Weighted average assumptions and resultant fair values for stock options granted were as follows:

	Year ended December 31,	
	2023	2022
Risk free interest rate (%)	**4.3**	3.9
Expected term (years)	**4.0**	4.0
Expected volatility (%)	**30.0**	45.0
Expected annual dividend per share ($)	**0.56**	0.32
Weighted average forfeiture rate (%)	**5.2**	5.0
Weighted average fair value (CAD$)	**0.89**	1.41

Share-based compensation that was directly related to exploration and evaluation assets and property, plant and equipment has been capitalized with the remainder recognized as share-based compensation expense on the consolidated statements of operations and comprehensive income.

e) Net Income Per Share

Net income per share is calculated by dividing net income by the weighted average number of common shares outstanding during the applicable period. Pursuant to the treasury stock method, where dilutive instruments are vested and require little or no further consideration to be exercised, the impact of such instruments is included in the computation of weighted average basic shares outstanding. Accordingly, the computation in the table below includes all DSUs and all vested RSUs in basic shares for the purposes of the net earnings per share calculations.

The following reconciles the number of shares used in the basic and diluted net earnings per share calculations:

	Year ended December 31,	
	2023	2022
Weighted average basic	**37,121,109**	34,642,260
Dilutive securities		
Stock options	**525,658**	517,677
Warrants(1)	**-**	1,183,195
RSUs	**122,930**	575,940
Weighted average diluted	**37,769,697**	36,919,072

(1) All outstanding warrants were exercised in 2022.

All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted

f) Dividends

Dividends declared and paid were as follows:

		Year Ended December 31, 2023		
Period Declared	**Dividend per share ($)**	**Total Declared**	**Total Paid**	**Date Paid**
Three months ended December 31, 2022	0.12	-	**4,357**	January 13, 2023
Three months ended March 31, 2023	0.14	**5,104**	**5,104**	April 14, 2023
Three months ended June 30, 2023	0.14	**5,109**	**5,109**	July 14, 2023
Three months ended September 30, 2023	0.14	**5,122**	**5,122**	October 13, 2023
Three months ended December 31, 2023	0.14	**5,127**	-	January 15, 2024
Total		**20,462**	**19,692**	

		Year Ended December 31, 2022		
Period Declared	**Dividend per share ($)**	**Total Declared**	**Total Paid**	**Date Paid**
Three months ended December 31, 2021	0.06	-	**2,034**	January 14, 2022
Three months ended March 31, 2022	0.08	**2,716**	**2,716**	April 14, 2022
Three months ended June 30, 2022	0.08	**2,728**	**2,728**	July 15, 2022
Three months ended September 30, 2022	0.08	**2,896**	**2,896**	October 14, 2022
Three months ended December 31, 2022	0.12	**4,357**	-	January 13, 2023
Total		**12,697**	**10,374**	

The declaration, timing, amount and payment of future dividends remain at the discretion of the Board of Directors and there is no certainty that dividends will be paid at the intended rate or at any rate in the future.

NOTE 10 – REVENUE FROM CONTRACTS WITH CUSTOMERS

	Year ended December 31,	
	2023	2022
Natural gas	**56,433**	59,165
Condensate	**3,109**	4,167
Oil	**145**	176
Total	**59,687**	63,508

The Company's natural gas price is set semi-annually (in February and August) using a trailing weighted average basket of USD benchmark prices, with a floor and a ceiling price adjusted based on United States inflation. The natural gas price is then translated to BRL based on the average BRL relative to USD and fixed in BRL until the next price re-set date. As all invoices are issued in BRL, actual receipts and revenue recognized in equivalent USD will be subject to exchange rate variations.

The Company's oil and condensate sales revenues are derived under contracts with customers based on floating prices, specifically the Brent benchmark oil price adjusted for contracted discounts at a fixed percentage of Brent in the case of oil sales and at fixed premiums to Brent in the case of condensate sales.

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Contracted payment terms are on or before the 25th day of the month following satisfaction of the performance obligation and payments for condensate are often made in advance of shipment. For the year ended December 31, 2023 the natural gas sales revenue has been collected within the timing expected. There is no indication of potential collection issues with Bahiagás, the local distribution company in the state of Bahia in Brazil and sole customer of the Company's natural gas production. Amounts receivable from contracts with customers by commodity are as follows:

	As at December 31,	
	2023	2022
Natural gas	**6,486**	6,935
Condensate	**13**	18
Oil	**-**	-
Total	**6,499**	6,953

NOTE 11 – NATURE OF OTHER INCOME AND EXPENSES

a) Other Income

	Year Ended December 31,	
	2023	2022
Interest income	**1,277**	367
Tax recoveries from operations	**507**	449
Water disposal income & other	**11**	107
Total other income	**1,795**	923

b) Production Expenses

	Year Ended December 31,	
	2023	2022
Personnel	**360**	233
Facility and pipeline	**1,638**	1,719
Other fixed	**1,738**	1,319
Variable	**387**	279
Workover	**82**	-
Total production expenses	**4,205**	3,550

c) General and Administrative ("G&A") Expenses

	Year Ended December 31,	
	2023	2022
Personnel	**3,287**	3,799
Travel	**185**	152
Office and IT costs	**298**	224
Professional fees	**830**	722
General corporate	**1,721**	1,573
Gross G&A expenses	**6,321**	6,470
Capitalized to E&E (Note 5)	**(107)**	(876)
Capitalized to PP&E (Note 6)	**(1,278)**	(610)
Net G&A expenses	**4,936**	4,984

General corporate expenses include public company costs, corporate insurance, directors' fees and other miscellaneous expenses. G&A expenses directly attributable to exploration and development projects, primarily being personnel costs, are capitalized.

All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted

d) Finance Expenses

	Year Ended December 31,	
	2023	2022
Lease interest (Note 7)	**1,495**	1,525
Accretion of decommissioning liabilities (Note 8)	**58**	51
Amortization of deferred financing costs	**-**	496
Interest on Credit Facility[1]	**-**	306
Total finance expenses	**1,553**	2,378

(1) The Credit Facility was terminated when it was fully repaid in 2022.

NOTE 12 – TAXES

Alvopetro computes Brazil corporate income tax under the actual profit regime. Under this regime, the corporate tax rate on taxable income is 34%, comprised of corporate income tax of 15%, surtax of 10%, and a social contribution tax of 9%. Tax losses may be carried forward indefinitely; however, any utilization of losses in a subsequent taxation year is limited to 30% of the taxable income in that period.

In 2021, the Company received approval from tax authorities in Brazil for Supertintendência de Desenvolvimento do Nordeste ("SUDENE"), a regional tax incentive offered for Bahia State. Pursuant to the incentive, the Company may reduce its corporate tax and surtax liability by 75% for profits arising on qualifying natural gas projects, resulting in an effective tax rate of 15.25% where profits for SUDENE purposes align with taxable income under the actual profit regime. The SUDENE incentive applies to profit from natural gas and, as of 2023, profits from condensate earned by Alvopetro for a period of ten taxation years, commencing January 1, 2021 and ending December 31, 2030 (the "SUDENE period").

Deferred tax assets and liabilities are measured using substantively enacted tax rates that are expected to apply when temporary differences are expected to reverse. As the Company expects the majority of temporary differences to reverse in the SUDENE period, the Company has measured its deferred tax assets at the SUDENE tax rate of 15.25%.

Income tax expense differs from the amount that would have been expected by applying the statutory income tax rate to loss before taxes. The principal reasons for this difference are as follows:

	Year ended December 31,	
	2023	2022
Income before taxes	**32,799**	37,445
Statutory income tax rate	**34%**	34%
Expected income tax expense	**11,152**	12,731
(Decrease) increase resulting from:		
Effect of tax incentives and lower local tax rates	**(8,474)**	(9,039)
Non-deductible amounts for tax purposes	**783**	2,297
Change in estimated tax pools	**(52)**	(129)
Share-based compensation	**390**	293
Change in unrecognized deferred tax asset	**457**	(583)
Impact of foreign exchange fluctuations and other	**18**	143
Income tax expense	**4,274**	5,713

All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted

The components of income tax expense are as follows:

	Year ended December 31,	
	2023	2022
Current tax expense	**2,520**	1,317
Deferred tax expense	**1,754**	4,396
Total income tax expense	**4,274**	5,713

The change in the Company's deferred tax asset balance is as follows:

	Year ended December 31,	
	2023	2022
Deferred tax asset, beginning of the year	**3,525**	5,305
Recognized in deferred income tax expense	**(1,754)**	(4,396)
Recognized in other comprehensive income – initial recognition	**(57)**	2,172
Impact of foreign exchange fluctuations and other	**279**	444
Deferred tax asset, end of year	**1,993**	3,525

The components of the Company's deferred tax assets and liabilities arising from temporary differences and loss carry-forwards as well as the associated amount of deferred tax recovery or expense recognized in the Company's consolidated statements of operations and comprehensive loss are outlined below.

Deferred tax (liability) asset	PP&E, E&E and ROU assets	Decommissioning liabilities	Tax loss carryforwards	Other tax pools	Unrecognized deferred tax asset	Total
As at December 31, 2021	(673)	127	4,604	3,070	(1,823)	5,305
Deferred tax (expense) recovery	(699)	(37)	(1,107)	(3,136)	583	(4,396)
Recognition in OCI	(57)	-	-	2,229	-	2,172
Foreign currency translation	12	8	203	221	-	444
As at December 31, 2022	(1,417)	98	3,700	2,384	(1,240)	3,525
Deferred tax recovery (expense)	**1,353**	**68**	**(1,616)**	**(1,102)**	**(457)**	**(1,754)**
Recognition in OCI	**(57)**	**-**	**-**	**-**	**-**	**(57)**
Foreign currency translation	**(9)**	**10**	**87**	**191**	**-**	**279**
As at December 31, 2023	**(130)**	**176**	**2,171**	**1,473**	**(1,697)**	**1,993**

An unrecognized deferred tax asset of $1.7 million exists at December 31, 2023 (December 31, 2022 - $1.2 million), all of which relates to Canada. Total tax loss carry-forwards include $5.2 million attributable to Brazil, which carryforward indefinitely but are limited to annual utilization of up to 30% of taxable income in subsequent periods, and $8.3 million attributable to Canada which expire between 2033 and 2043.

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NOTE 13 – CAPITAL MANAGEMENT

The Company's capital consists of the following:

	As at December 31,	
	2023	2022
Cash and cash equivalents	**18,326**	19,784
Working capital[(1)] deficit, excluding cash and cash equivalents	**(5,209)**	(5,086)
Working capital	**13,117**	14,698
Lease liabilities – non-current	**(7,722)**	(8,573)
Shareholders' equity	**88,208**	76,408

(1) Working capital is calculated as total current assets less total current liabilities.

Alvopetro has the ability to adjust its capital structure by issuing new equity or debt and making adjustments to its capital and dividend programs to the extent the capital expenditures are not committed. There are no external restrictions on how the Company manages its capital.

NOTE 14 – FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT

Overview

The Company's financial instruments, classified as financial assets and liabilities, consist of cash and cash equivalents, restricted cash, trade and other receivables, accounts payable and accrued liabilities and dividends payable.

Financial Risk

The Company is exposed to risks arising from the volatility of commodity prices, foreign exchange rates and interest rates, resulting in market risks, credit risk and liquidity risk. Risk management strategies are employed to ensure that any exposures are within risk tolerance levels compatible with the Company's business objectives. Alvopetro's Board of Directors has overall responsibility for establishment and oversight of the Company's risk management policies and activities.

Market Risk

Market risk is the risk that changes in market factors will affect the Company's cash flows, net income, comprehensive income, liquidity or the value of financial instruments. Market uncertainly associated with financial institution instability, international conflicts, geopolitical factors and pandemics is incorporated into management's risk assessments but given the lack of precedence, is difficult to accurately predict with confidence.

Foreign Currency Risk

Foreign currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign currency exchange rates. The Company's natural gas, oil and condensate sales are denominated in BRL based on USD benchmark prices, unused tax pools in Brazil are in BRL and all operational, administrative and capital activities related to the Brazil properties are transacted primarily in BRL. Alvopetro's GSA is exposed to fluctuations in the USD to the BRL as the natural gas price, although benchmarked to USD, is set semi-annually in BRL (based on historical foreign exchange rates) and billed monthly in the set BRL price until the next price redetermination. The following table denotes the overall impact on natural gas revenues of a 5% and 10% appreciation and depreciation of the BRL relative to the USD:

	Year Ended December 31,	
	2023	2022
Increase (decrease) to natural gas revenues from:		
5% Appreciation of BRL to USD	**2,970**	3,114
10% Appreciation of BRL to USD	**6,270**	6,574
5% Depreciation of BRL to USD	**(2,687)**	(2,817)
10% Depreciation of BRL to USD	**(5,130)**	(5,378)

Management closely monitors foreign exchange rates and will determine the currency and location of cash held based on funding needs and opportunities to optimize on foreign currency and local interest rates. The following financial instruments are denominated in currencies other than the USD:

	As at			
	December 31, 2023		December 31, 2022	
	CAD$ (000's)	**BRL (000's)**	CAD$ (000's)	BRL (000's)
Cash and cash equivalents	**197**	**28,095**	386	27,582
Restricted cash – current	**-**	**350**	-	1,546
Trade and other receivables	**93**	**32,598**	45	36,921
Accounts payable and accrued liabilities	**(948)**	**(25,686)**	(1,695)	(31,333)
Net exposure in foreign currency	**(658)**	**35,357**	(1,264)	34,716
Net exposure in USD ($000s)	**(498)**	**7,303**	(933)	6,654

Based on financial instruments held at December 31, 2023 and 2022, sensitivity to fluctuations in the exchange rates as indicated below would have the following estimated effect on net income and other comprehensive income:

	Year Ended December 31,	
	2023	2022
Effect of 5% appreciation in CAD and BRL to USD		
Decrease to net income	**(25)**	(47)
Increase to other comprehensive income	**384**	350
Effect of 5% depreciation in CAD and BRL to USD		
Increase to net income	**25**	47
Decrease to other comprehensive income	**(348)**	(317)

Commodity Price Risk

For the year ended December 31, 2023 approximately 95% (December 31, 2022 – 93%) of natural gas, oil and condensate sales was related to natural gas sales, mainly from the Company's Caburé field. Fluctuations in natural gas prices may have a significant impact on the carrying value of this property as well as cash flows and the Company's resultant ability to execute planned capital expenditures and meet ongoing obligations. Changes in commodity prices can also affect the Company's ability to obtain future financings and the terms of those future financings. Alvopetro's natural gas volumes are sold pursuant to its GSA at a natural gas price, set semi-annually, based on average historical international USD benchmark commodity prices. The GSA includes both a USD floor and ceiling price, based on three benchmark price indices (see Note 10), limiting the Company's exposure to commodity price risk.

The Company did not have any forward commodity price contracts in place as at or during the years ended December 31, 2023 and 2022 but may consider such in the future to protect cash flows and manage this risk.

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Interest Rate Risk

The Company is exposed to interest rate cash flow risk on cash and cash equivalents and restricted cash due to fluctuations in market interest rates applied to such balances.

Credit Risk

Credit risk is the risk of financial loss to the Company if counterparties do not fulfill their contractual obligations. This exposure for Alvopetro potentially affects restricted cash and trade and other receivables.

Alvopetro is subject to credit risk by virtue of having only one customer for its natural gas production, creating economic dependence on this counterparty. At December 31, 2023, $6.5 million of accounts receivable (December 31, 2022 - $6.9 million) or 97% (2022 - 97%) is related to natural gas production sold to this counterparty (see Note 10), the full balance of which was received subsequent to December 31, 2023. Alvopetro is paid for its production monthly and has assessed the risk of nonpayment from this customer, the distribution company for the state of Bahia, as very low. To date there have been no issues with respect to recoverability of the accounts receivable from Alvopetro's natural gas customer nor any significant issues recovering amounts from oil or condensate customers. As such, the risk of non-collection from this counterparty and any of Alvopetro's counterparties is not expected to have a material impact on the financial statements.

The Company closely monitors other trade receivables, recognizing a provision when collection is in doubt. There were no material expected credit losses recognized in 2023 or 2022. The maximum exposure to credit risk is equal to the carrying value of the financial assets.

Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations when due. The Company manages this risk by forecasting cash flows for a minimum period of twelve months which involves preparation of capital expenditure, operating and general and administrative budgets, all of which are monitored and updated as considered necessary. All obligations in 2023 were satisfied with the Company's cash balances and cash flows from operating activities. In the event the Company experiences a decline in cash flows, dividend payments are at the discretion of the Board of Directors and with the exception of work commitments, Alvopetro has flexibility with respect to capital activities planned.

NOTE 15 – CHANGES IN NON-CASH WORKING CAPITAL

	Year ended December 31,	
	2023	2022
Change in:		
Trade and other receivables	**862**	(2,720)
Prepaid expenditures	**(296)**	1,025
Accounts payable and accrued liabilities	**(1,653)**	1,654
	(1,087)	(41)
Changes relating to:		
Operating activities	**(328)**	(2,345)
Financing activities	**(192)**	175
Investing activities	**(567)**	2,129
	(1,087)	(41)

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NOTE 16 – RELATED PARTY TRANSACTIONS

Key management personnel are comprised of Alvopetro's directors and officers. Compensation for these individuals is set forth as follows:

	Year ended December 31,	
	2023	2022
Short-term benefits	**1,282**	1,862
Share-based compensation	**1,017**	590
Total	**2,299**	2,452

The following table lists the Company's subsidiaries and their respective places of incorporation, each owned 100% directly and indirectly at December 31, 2023:

Subsidiary Name	**Country of Incorporation**
Alvopetro Oil and Gas Investments Inc.	Canada
Alvopetro S.A. Extração de Petróleo e Gás Natural	Brazil