



INTERIM FINANCIAL STATEMENTS  
MARCH 31, 2018

NOTICE TO READER

*Management has compiled the unaudited interim consolidated financial information of Alvopetro Energy Ltd. consisting of the Interim Condensed Consolidated Statements of Financial Position at March 31, 2018 and December 31, 2017 and the Interim Condensed Consolidated Statements of Operations and Comprehensive (Loss) Income and the Interim Condensed Consolidated Statements of Cash Flows for the three months ended March 31, 2018 and 2017. Please note the interim financial statements have not been reviewed or audited by external auditors.*

**ALVOPETRO ENERGY LTD.****INTERIM CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION**

(Unaudited, thousands of United States dollars)

	Note	March 31, 2018	December 31, 2017
<b>ASSETS</b>			
<b>Current</b>			
Cash and cash equivalents		7,542	9,189
Restricted cash		105	106
Trade and other receivables		191	153
Prepaid expenditures		147	208
Assets held for sale	3	235	236
<b>Total current assets</b>		<b>8,220</b>	<b>9,892</b>
Exploration and evaluation assets	4	55,687	54,585
Property, plant and equipment	5	4,201	4,238
<b>Non-current assets</b>		<b>59,888</b>	<b>58,823</b>
<b>Total assets</b>		<b>68,108</b>	<b>68,715</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>			
<b>Current liabilities</b>			
Accounts payable and accrued liabilities		1,573	1,111
Current portion of decommissioning liabilities	6	19	19
<b>Total current liabilities</b>		<b>1,592</b>	<b>1,130</b>
Deferred tax liability		-	-
Decommissioning liabilities	6	1,448	1,445
<b>Total liabilities</b>		<b>3,040</b>	<b>2,575</b>
<b>Shareholders' equity</b>			
Share capital	7	151,937	151,937
Contributed surplus		1,669	1,662
Deficit		(68,396)	(67,507)
Accumulated other comprehensive loss		(20,142)	(19,952)
<b>Total shareholders' equity</b>		<b>65,068</b>	<b>66,140</b>
<b>Total liabilities and shareholders' equity</b>		<b>68,108</b>	<b>68,715</b>

Commitments and contingencies (Note 13)

See accompanying notes to these interim condensed consolidated financial statements.

**ALVOPETRO ENERGY LTD.****INTERIM CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE (LOSS) INCOME**

(Unaudited, thousands of United States dollars, except per share amounts)

		Three Months Ended	
	Note	2018	March 31, 2017
<b>Revenue</b>			
Oil sales	11	116	171
Royalties and production taxes		(13)	(17)
Oil revenue		103	154
Other income		29	46
Total revenue and other income		132	200
<b>Expenses</b>			
Production	12	236	215
Transportation		4	9
General and administrative	12	714	703
Depletion and depreciation	5	33	68
Exploration and evaluation expenses		12	63
Accretion of decommissioning liabilities	6	10	9
Share-based compensation	7	3	25
Foreign exchange loss		9	1
Total expenses		1,021	1,093
Loss before taxes		(889)	(893)
Income tax		-	-
Net loss		(889)	(893)
Exchange (loss) gain on translation of foreign operations		(190)	912
Comprehensive (loss) gain		(1,079)	19
<b>Net loss per share</b>			
Basic	7	(0.01)	(0.01)
Diluted		(0.01)	(0.01)

See accompanying notes to these interim condensed consolidated financial statements.

**ALVOPETRO ENERGY LTD.****INTERIM CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY**

(Unaudited, thousands of United States dollars)

	Note	Three Months Ended March 31,	
		2018	2017
<b>Common Shares</b>			
Balance, beginning of period		151,937	151,937
Net change		-	-
<b>Balance, end of period</b>		<b>151,937</b>	<b>151,937</b>
<b>Contributed surplus</b>			
Balance, beginning of period		1,662	1,558
Share-based compensation expense	7	3	25
Share-based compensation capitalized	7	4	7
<b>Balance, end of period</b>		<b>1,669</b>	<b>1,590</b>
<b>Deficit</b>			
Balance, beginning of period		(67,507)	(60,390)
Net loss		(889)	(893)
<b>Balance, end of period</b>		<b>(68,396)</b>	<b>(61,283)</b>
<b>Accumulated Other Comprehensive Loss</b>			
Balance, beginning of period		(19,952)	(19,330)
Other comprehensive (loss) gain		(190)	912
<b>Balance, end of period</b>		<b>(20,142)</b>	<b>(18,418)</b>

See accompanying notes to these interim condensed consolidated financial statements.

**ALVOPETRO ENERGY LTD.****INTERIM CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(Unaudited, thousands of United States dollars)

	Note	Three Months Ended March 31,	
		2018	2017
<b>Operating Activities</b>			
Net loss		(889)	(893)
Adjustments for non-cash items:			
Depletion and depreciation	5	33	68
Accretion of decommissioning liabilities	6	10	9
Share-based compensation	7	3	25
Unrealized foreign exchange loss		1	6
Settlement of decommissioning liabilities	6	-	(12)
Funds flow from operations		(842)	(797)
Changes in non-cash working capital	10	114	115
		(728)	(682)
<b>Investing Activities</b>			
Expenditures on exploration and evaluation assets		(1,274)	(2,365)
Expenditures on property, plant and equipment		(2)	(8)
Proceeds on disposition of assets		-	27
Changes in non-cash working capital	10	394	(224)
		(882)	(2,570)
<b>Change in cash and cash equivalents</b>		(1,610)	(3,252)
<b>Effect of foreign exchange on cash balances</b>		(37)	16
<b>Cash and cash equivalents, beginning of period</b>		9,189	17,788
<b>Cash and cash equivalents, end of period</b>		7,542	14,552
Cash and cash equivalents consist of:			
Cash		1,410	3,315
Cash equivalents		6,132	11,237
Supplemental information:			
Cash income taxes paid		-	-
Cash interest income received		30	34

See accompanying notes to these interim condensed consolidated financial statements.

## **ALVOPETRO ENERGY LTD.**

### **NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

As at and for the three months ended March 31, 2018

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

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#### **NOTE 1 – CORPORATE INFORMATION AND BASIS OF PRESENTATION**

Alvopetro Energy Ltd. (“Alvopetro” or “the Company”) is engaged in the exploration, development and production of hydrocarbons in Brazil. Alvopetro is a publicly traded company listed on the TSX Venture Exchange (TSX: ALV.V), was incorporated under the Business Corporations Act (Alberta) on September 25, 2013 as 1774501 Alberta Ltd., and subsequently changed its name to Alvopetro Energy Ltd. on November 19, 2013.

The Company’s head office and records are located at 1700, 525 8<sup>th</sup> Avenue S.W., Calgary, Alberta, Canada, T2P 1G1.

The interim condensed consolidated financial statements as at March 31, 2018 and December 31, 2017 and for the three months ended March 31, 2018 and March 31, 2017 have been prepared in accordance with International Financial Reporting Standards (“IFRS”) applicable to the presentation of interim financial statements, including International Accounting Standard (“IAS”) 34 *Interim Financial Reporting*. These interim condensed consolidated financial statements are prepared using the same accounting policies and methods of computation as disclosed in the audited consolidated financial statements as at and for the year ended December 31, 2017, except as discussed in Note 2 below with respect to the adoption of revised accounting standards. These statements do not contain all disclosures required for full annual financial statements and should be read in conjunction with the audited consolidated financial statements as at and for the year ended December 31, 2017.

These interim condensed consolidated financial statements were authorized for issuance by the Company’s Board of Directors on May 15, 2018.

The interim condensed consolidated financial statements are presented in U.S. dollars (“USD”) which is the parent Company’s functional currency.

#### **Segmented Operations**

All oil sales revenue is derived entirely from Brazilian operations. All exploration and evaluation assets and all material property, plant and equipment are located in Brazil. The majority of the cash and cash equivalents are held in Canada and all of the restricted cash at March 31, 2018 and December 31, 2017 is in Brazil. The Company does not have any significant income in Canada other than interest earned on cash balances.

#### **NOTE 2 – CHANGES IN ACCOUNTING STANDARDS**

##### **New and Revised Accounting Standards**

The interim condensed consolidated financial statements have been prepared following the same accounting policies and methods of computation as the 2017 annual consolidated financial statements, with the exception of IFRS 15 *Revenue from Contracts with Customers*, adopted retrospectively on January 1, 2018. This standard requires an entity to recognize revenue reflective of the transfer of goods and services for the amount it expects to receive upon transfer of control to the purchaser.

The application of IFRS 15 did not have an impact on the Company’s consolidated financial position, results of operations or cash flows but does require enhanced disclosures about the Company’s revenue transactions. Oil sales revenue, derived from crude oil production in Brazil, is recognized when the performance obligations are satisfied and revenue can be reliably measured.

##### **Standards Issued but not Yet Effective**

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

**ALVOPETRO ENERGY LTD.****NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

As at and for the three months ended March 31, 2018

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

Standard and Description	Date of Adoption	Expected Adoption Impact on Consolidated Financial Statements
IFRS 16 <i>Leases</i> – IFRS 16 was issued in January 2016 and replaces IAS 17 <i>Leases</i> . The standard introduces a single lessee accounting model for leases with required recognition of assets and liabilities for most leases.	January 1, 2019	The Company is assessing the effect of this future pronouncement on its financial statements.

**NOTE 3 – ASSETS HELD FOR SALE**

	As at	
	March 31, 2018	December 31, 2017
Balance, beginning of period	236	410
Transferred from E&E (Note 4)	-	322
Disposal – cash proceeds	-	(105)
Disposal – in exchange for drilling services	-	(396)
Foreign currency translation	(1)	5
Balance, end of period	235	236

The balance at March 31, 2018 and December 31, 2017 consists of land owned by the Company which management expects to sell within one year.

**NOTE 4 – EXPLORATION AND EVALUATION (“E&E”) ASSETS**

	As at	
	March 31, 2018	December 31, 2017
Balance, beginning of period	54,585	53,259
Capital expenditures	1,274	5,355
Capitalized share-based compensation	4	18
Change in decommissioning liabilities	-	189
Transfer to assets held for sale (Note 3)	-	(322)
Other transfers	(2)	10
Asset dispositions	-	(122)
Impairment	-	(3,189)
Foreign currency translation	(174)	(613)
Balance, end of period	55,687	54,585

General and administrative costs totaling \$0.3 million (December 31, 2017 - \$1.1 million) that were directly related to exploration and evaluation activities have been capitalized as exploration and evaluation assets.

Capital expenditures in the year ended December 31, 2017 include \$0.4 million of non-cash expenditures, largely in respect of drilling services received in exchange for assets held for sale.

**ALVOPETRO ENERGY LTD.****NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

As at and for the three months ended March 31, 2018

*All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted***NOTE 5 – PROPERTY, PLANT AND EQUIPMENT (“PP&E”)**

	As at	
	March 31, 2018	December 31, 2017
Cost, beginning of period	9,514	9,599
Capital expenditures	2	77
Capitalized share-based compensation	-	1
Foreign currency translation	(53)	(163)
Cost, end of period	9,463	9,514
Accumulated depletion and depreciation and impairment, beginning of period	(5,276)	(4,739)
Depletion and depreciation for the period	(33)	(205)
Impairment	-	(472)
Foreign currency translation	47	140
Accumulated depletion and depreciation and impairment, end of period	(5,262)	(5,276)
Net book value, end of period	4,201	4,238

General and administrative costs that were directly related to property, plant, and equipment activities have been capitalized.

**NOTE 6 – DECOMMISSIONING LIABILITIES**

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

	As at	
	March 31, 2018	December 31, 2017
Balance, beginning of period	1,464	1,399
Liabilities incurred	-	189
Obligations settled	-	(139)
Accretion	10	37
Foreign currency translation	(7)	(22)
Balance, end of period	1,467	1,464

Total undiscounted cash flows, escalated at 6.5% (December 31, 2017 - 6.5%) for inflation, required to settle the Company’s decommissioning liabilities are estimated to be \$2.3 million (December 31, 2017 - \$2.3 million) and have been discounted using an average risk-free rate of 2.8% (December 31, 2017 – 2.5%), which represents an estimated U.S. Treasury bill rate for a period of 15 years, the approximate weighted-average remaining years to abandonment.

The Company expects to incur \$0.02 million (December 31, 2017 - \$0.02 million) of decommissioning costs within one year from March 31, 2018 and accordingly this amount is classified as current on the consolidated statements of financial position.

**NOTE 7 – 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.



**ALVOPETRO ENERGY LTD.**
**NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

As at and for the three months ended March 31, 2018

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

**b) Issued and Outstanding Common Shares**

	Number of Shares	Amount (\$000s)
<b>Balance as at March 31, 2018 and December 31, 2017</b>	<b>85,166,871</b>	<b>\$ 151,937</b>

**c) Options to Purchase Common Shares**

The options outstanding at March 31, 2018 are as follows:

	Number of Options	Weighted Average Exercise Price (CAD\$)
Balance as at December 31, 2016	6,874,102	0.53
Granted	64,000	0.19
Expired	(352,166)	0.65
Forfeited	(47,000)	0.28
<b>Balance as at December 31, 2017 and March 31, 2018</b>	<b>6,538,936</b>	<b>0.52</b>

Options Outstanding at March 31, 2018				Options Exercisable at March 31, 2018		
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\$0.18 - \$0.39	3,086,500	0.25	3.26	1,976,503	0.25	3.16
CAD\$0.40 - \$0.75	1,480,000	0.42	1.76	1,468,000	0.42	1.79
CAD\$1.01 - \$1.10	1,972,436	1.02	0.73	1,972,436	1.02	0.73
<b>CAD\$0.18 - \$1.10</b>	<b>6,538,936</b>	<b>0.52</b>	<b>2.16</b>	<b>5,416,939</b>	<b>0.58</b>	<b>1.90</b>

**Share-Based Compensation**

The fair value of the stock options granted under the Alvo Petro stock option plan is estimated on the grant date using the Black-Scholes option pricing model. There were no stock option grants during the three months ended March 31, 2018 or March 31, 2017.

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 (loss) gain.

**d) Net Loss Per Share Attributable to Common Shareholders**

Net loss per share is calculated by dividing net loss by the weighted average number of common shares outstanding during the applicable period. The following table provides the number of shares used in the basic and diluted per share computations:

	Three months ended March 31,	
	2018	2017
Weighted average common shares outstanding, basic and diluted	<b>85,166,871</b>	85,166,871

**ALVOPETRO ENERGY LTD.****NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

As at and for the three months ended March 31, 2018

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

In determination of the weighted average number of diluted common shares outstanding for the three months ended March 31, 2018 and 2017, all stock options were excluded because the effect would be anti-dilutive.

**NOTE 8 – CAPITAL MANAGEMENT**

The Company's capital consists of the following:

	As at	
	March 31, 2018	December 31, 2017
Working capital	6,628	8,762
Shareholders' equity	65,068	66,140

Alvopetro manages its capital to support the Company's strategic growth objectives and maintain financial capacity and flexibility for the purpose of funding the Company's exploration and development activities.

The Company considers its capital structure to include working capital (including current restricted cash and assets held for sale) and shareholders' equity. At March 31, 2018, the Company's net working capital surplus of \$6.6 million (December 31, 2017 - \$8.8 million) included \$7.5 million (December 31, 2017 - \$9.2 million) of cash, \$0.1 million (December 31, 2017 - \$0.1 million) of current restricted cash, \$0.2 million (December 31, 2017 - \$0.2 million) of assets held for sale, net of a working capital deficit of \$1.2 million (December 31, 2017 - \$0.8 million).

Alvopetro has the ability to adjust its capital structure by issuing new equity or debt and making adjustments to its capital expenditure program, other than with respect to work commitments. The Company considers its capital structure at this time to include shareholders' equity of \$65.1 million (December 31, 2017 - \$66.1 million). In the event that adjustments to the capital structure are necessary, the Company may consider issuing additional equity, raising debt or revising its capital investment programs.

Subsequent to March 31, 2018 Alvopetro concluded the unitization process and entered into a long-term natural gas sales agreement ("GSA") with respect to our share of unit gas to be produced from our Caburé natural gas field. Alvopetro will require financing to fund its share of the capital expenditures and execute development of the field. Future capital expenditures associated with Alvopetro's work commitments on its other exploration blocks as well as development prospects on our mature fields may also require financing. Financing alternatives include project financing, vendor financing, capital leases for facilities, strategic partnerships, other debt issuances or equity issuances. The Company may also explore asset sales or farmouts to assist with funding.

The Company has a credit support facility (the "Facility") with a Canadian bank which allows for the issuance of letters of credit ("LCs") and letters of guarantee in support of financial guarantees required by the National Agency of Petroleum, Natural Gas and Biofuels (the "ANP") for Alvopetro's work commitments under the terms of its concession contracts as discussed further in Note 13. LCs and letters of guarantee issued under the Facility must be supported by either cash collateral posted by Alvopetro or through an Account Performance Security Guarantee from Export Development Canada ("EDC"). As at March 31, 2018, the total amount of LCs issued under the Facility was \$9.0 million (December 31, 2017 - \$12.1 million), the full balance of which was supported by EDC on behalf of Alvopetro. LC's supported by EDC at March 31, 2018 include a \$2.9 million LC for Block 177 which was met in 2017, approved by the ANP during the three months ended March 31, 2018 and released by all banks subsequent to March 31, 2018.

The current restricted cash of \$0.1 million (December 31, 2017 - \$0.1 million) relates to cash posted in Brazil in support of abandonment guarantees on the Bom Lugar and Jiribatuba fields. The Company does not have any other restricted cash balances as at March 31, 2018 or December 31, 2017.

The Company has not paid or declared any dividends since the date of incorporation.

**ALVOPETRO ENERGY LTD.****NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

As at and for the three months ended March 31, 2018

*All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted***NOTE 9 – FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT**

The Company's financial instruments consist of cash and cash equivalents, restricted cash, trade and other receivables and accounts payable and accrued liabilities. The nature of Alvo Petro's operations exposes the Company to credit risk, liquidity risk, and market risk. The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and to monitor market conditions and the Company's activities. The Board of Directors has overall responsibility for establishment and oversight of the Company's risk management.

*Fair Value of Financial Instruments*

The Company classifies the fair value of financial instruments according to the following hierarchy based on the amount of observable inputs used to value the instrument:

Level 1 – Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions occur in sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2 – Pricing inputs are other than quoted prices in active markets included in Level 1. Prices in Level 2 are either directly or indirectly observable as of the reporting date. Level 2 valuations are based on inputs, including quoted forward prices for commodities, time value and volatility factors, which can be substantially observed or corroborated in the marketplace.

Level 3 – Valuations in this level are those with inputs for the asset or liability that are not based on observable market data.

Assessment of the significance of a particular input to the fair value measurement requires judgment that may affect the placement within the fair value hierarchy level. Due to the short-term nature of accounts receivable and accounts payable and accrued liabilities, their carrying value approximates their fair value. The carrying values and respective fair values of Alvo Petro's financial instruments at March 31, 2018 and December 31, 2017 are set forth in the table below. The Company does not currently have any financial instruments classified as Level 2 or Level 3.

	As at			
	March 31, 2018		December 31, 2017	
	Carrying Value	Fair Value	Carrying Value	Fair Value
<b>Carried at fair value through profit or loss</b>				
Cash and cash equivalents <sup>(1)</sup>	7,542	7,542	9,189	9,189
Restricted cash – current <sup>(1)(2)</sup>	105	105	106	106
	<b>7,647</b>	<b>7,647</b>	9,295	9,295
<b>Carried at cost or amortized cost</b>				
Trade and other receivables	191	191	153	153
Accounts payable and accrued liabilities	(1,573)	(1,573)	(1,111)	(1,111)
	<b>(1,382)</b>	<b>(1,382)</b>	(958)	(958)

(1) Level 1

(2) Restricted cash balances include amounts pledged as collateral for abandonment guarantees.

*Risks Associated with Financial Assets and Liabilities*

A description of the nature and extent of risks arising from the Company's financial instruments can be found in the notes to the audited consolidated financial statements as at and for the year ended December 31, 2017 and there has been no significant change to the Company's exposure to these risks. The following financial instruments were denominated in currencies other than U.S. dollars as at March 31, 2018:

**ALVOPETRO ENERGY LTD.****NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

As at and for the three months ended March 31, 2018

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

	As at			
	March 31, 2018		December 31, 2017	
	CAD (000's)	BRL (000's)	CAD (000's)	BRL (000's)
Cash and cash equivalents	74	1,604	128	635
Restricted cash – current	-	350	-	350
Trade and other receivables	39	518	36	407
Accounts payable and accrued liabilities	(169)	(4,612)	(186)	(2,636)
Net exposure in foreign currency	(56)	(2,140)	(22)	(1,244)
Net exposure in USD (\$000s)	(43)	(644)	(18)	(376)

The Company had no forward exchange rate contracts in place as at or during the periods ended March 31, 2018 or December 31, 2017.

**NOTE 10 – CHANGES IN NON-CASH WORKING CAPITAL**

	Three months ended	
	March 31, 2018	2017
Change in:		
Trade and other receivables	(41)	140
Prepaid expenditures	45	9
Accounts payable and accrued liabilities	504	(258)
	508	(109)
Changes relating to:		
Operating activities	114	115
Investing activities	394	(224)
	508	(109)

**NOTE 11 – REVENUE**

The Company's oil sales revenues are derived from two customers, under contracts based on floating prices, specifically the Brent benchmark adjusted for contracted discounts. The discount applied to the average Brent price is a fixed cost per barrel for production from the Bom Lugar field and a fixed percentage of Brent for the Jiribatuba and Mãe-da-lua fields. In the three months ended March 31, 2018, discounts averaged 8% of the Brent price (three months ended March 31, 2017 - 10%).

As at March 31, 2018, accounts receivable included \$0.02 million of accrued sales revenue which related to March 2018 production. There were no collection issues requiring adjustment to revenue recorded in 2017.

Revenue is measured at the consideration specified in the contracts and represents amounts receivable net of discounts and sales taxes. Performance obligations associated with the sale of crude oil are satisfied when control of the product is transferred to the customer. This occurs when the oil is physically transferred to the delivery point agreed with the customer and the customer obtains legal title. Payment terms are on or before the 25<sup>th</sup> day of the month following satisfaction of the performance obligation.

**ALVOPETRO ENERGY LTD.****NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

As at and for the three months ended March 31, 2018

*All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted***NOTE 12 – NATURE OF EXPENSES**

Production expenses by nature were as follows:

	Three months ended March 31,	
	2018	2017
Production expenses:		
Personnel	84	93
Other fixed	73	61
Variable	63	21
Workover	16	40
<b>Total production expenses</b>	<b>236</b>	<b>215</b>

General and administrative expenses (“G&amp;A”) by nature were as follows:

	Three months ended March 31,	
	2018	2017
G&A expenses:		
Personnel	657	651
Travel	36	23
Office and IT	92	91
Professional fees	153	125
General corporate	85	84
Gross G&A expenses	1,023	974
Capitalized to E&E and PP&E	(309)	(271)
<b>Net G&amp;A expenses</b>	<b>714</b>	<b>703</b>

The majority of the Company’s G&A relates to personnel costs. 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.

**NOTE 13 – COMMITMENTS AND CONTINGENCIES**

The following is a summary of net contractual commitments as at March 31, 2018:

Commitments	< 1 Year	1-3 Years	Thereafter	Total
Minimum work commitments <sup>(1)</sup>				
<i>Minimum work commitments to be completed</i>				
Block 183 <sup>(2)</sup>	-	1,003	-	1,003
Block 106	343	-	-	343
Block 169 <sup>(3)</sup>	1,143	-	-	1,143
Block 255 <sup>(3)</sup>	1,368	-	-	1,368
Block 57	44	-	-	44
Block 62	44	-	-	44
Block 71	38	-	-	38
Block 145	44	-	-	44
Bom Lugar	-	-	105	105
Jiribatuba	-	-	105	105
<b>Minimum work commitments to be completed</b>	<b>3,024</b>	<b>1,003</b>	<b>210</b>	<b>4,237</b>
<b>Office leases<sup>(4)</sup></b>	<b>163</b>	<b>10</b>	<b>-</b>	<b>173</b>
<b>Total commitments</b>	<b>3,187</b>	<b>1,013</b>	<b>210</b>	<b>4,410</b>

## ALVOPETRO ENERGY LTD.

### NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

As at and for the three months ended March 31, 2018

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

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#### Notes:

- (1) Under the terms of the ANP concession contracts for each of our exploration blocks, the Company has commitments which must be completed prior to the applicable phase expiry date. The Company is required to post a performance guarantee with the ANP for all commitments in the table above.
- (2) The ANP has approved a suspension to the portion of Block 183 currently in the second exploration phase to which the above commitment is applicable. The Company will have 517 days from receipt of the environmental permit for the well to be drilled to meet the required work commitment.
- (3) Due to an ongoing injunction against unconventional activities on all 12<sup>th</sup> Brazil Bid Round Blocks, in December 2017 the Company filed a request with the ANP to cancel the Block 169 and 255 concession contracts, including the commitment noted in the table above, and return the bid round bonuses paid.
- (4) The Company is committed to future minimum payments for office space in Canada and Brazil.

Subsequent to March 31, 2018 Alvo Petro entered into a long-term GSA with respect to our share of unit gas to be produced from our Caburé natural gas field. Gas deliveries under the GSA are set to commence at the end of 2019, or earlier with mutual consent. The GSA initially provides for the sale of 5.3 mmfcpd (150,000 m<sup>3</sup>/d) on a firm basis and provides standard penalties for supply failure.

As is customary in the oil and gas industry, we may at times have work plans in place to reserve or earn certain acreage positions or wells. If we do not complete such work plans in a timely manner, the acreage positions or wells may be lost, or penalties may be applied.

The Company currently has no contingent liabilities recorded; however, in the normal course of operations, we may have disputes with industry participants for which we currently cannot determine the ultimate results. The Company has a policy to record contingent liabilities as they become determinable and the probability of loss is more likely than not.

Alvo Petro's activities in Brazil are subject to minimum local content requirements with respect to materials and supplies utilized. The specific local content requirements for the exploration phase were determined during the bidding process for each particular block and are assessed at the phase expiry date. Management undertakes considerable effort to adhere to these requirements; however, there may be circumstances when it is not advantageous, cost-effective or reasonably possible for the Company to do so. If the Company does not meet the local content requirements for a particular phase, as specified according to the respective concession contract, a penalty, which varies by concession depending on exploration phase and type of cost, will be incurred. The Company is continually monitoring its local content compliance and actual or potential penalties and, as of March 31, 2018, the potential estimated penalty was \$0.3 million (December 31, 2017 - \$0.3 million), which is included in accounts payable and accrued liabilities in the respective consolidated statements of financial position.