



INTERIM FINANCIAL STATEMENTS
MARCH 31, 2021

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, 2021 and December 31, 2020 and the Interim Condensed Consolidated Statements of Operations and Comprehensive Loss, the Interim Condensed Consolidated Statements of Changes in Equity and the Interim Condensed Consolidated Statements of Cash Flows for the three months ended March 31, 2021 and 2020. 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, 2021 | December 31, 2020 |
|---|------|-------------------|----------------------|
| ASSETS | | | |
| Current | | | |
| Cash and cash equivalents | | 4,983 | 5,159 |
| Restricted cash | | 123 | 125 |
| Trade and other receivables | | 3,328 | 2,802 |
| Prepaid expenditures | | 471 | 273 |
| Assets held for sale | 3 | - | 128 |
| Total current assets | | 8,905 | 8,487 |
| Exploration and evaluation assets | 4 | 2,845 | 32,262 |
| Property, plant and equipment | 5 | 51,899 | 25,843 |
| Right-of-use assets | 6 | 7,552 | 8,092 |
| Deferred tax asset | | 3,852 | 4,576 |
| Other assets | 7 | 969 | 1,128 |
| Non-current assets | | 67,117 | 71,901 |
| Total assets | | 76,022 | 80,388 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | | |
| Current liabilities | | | |
| Accounts payable and accrued liabilities | | 2,592 | 2,390 |
| Lease liabilities | 6 | 476 | 483 |
| Decommissioning liabilities | 8 | 62 | 63 |
| Other liabilities | | - | 12 |
| Total current liabilities | | 3,130 | 2,948 |
| Lease liabilities | 6 | 7,710 | 7,827 |
| Credit facility | 9 | 13,029 | 15,423 |
| Decommissioning liabilities | 8 | 993 | 1,080 |
| Total liabilities | | 24,862 | 27,278 |
| Shareholders' equity | | | |
| Share capital | 10 | 156,822 | 156,755 |
| Contributed surplus | | 2,879 | 2,821 |
| Deficit | | (72,260) | (71,172) |
| Accumulated other comprehensive loss | | (36,281) | (35,294) |
| Total shareholders' equity | | 51,160 | 53,110 |
| Total liabilities and shareholders' equity | | 76,022 | 80,388 |

Commitments and contingencies (Note 16)

See accompanying notes to these interim condensed consolidated financial statements.

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

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

| | | Three Months Ended | |
|--|------|--------------------|----------|
| | | March 31, | |
| | Note | 2021 | 2020 |
| Revenue | | | |
| Natural gas, oil and condensate sales | 11 | 6,939 | 61 |
| Royalties | | (645) | (8) |
| Net natural gas, oil and condensate revenue | | 6,294 | 53 |
| Other income | | 8 | 24 |
| Total revenue and other income | | 6,302 | 77 |
| Expenses | | | |
| Production | 12 | 710 | 44 |
| General and administrative | 12 | 851 | 640 |
| Depletion and depreciation | 5,6 | 1,674 | 62 |
| Impairment | 5 | - | 1,381 |
| Finance expenses | 12 | 994 | 276 |
| Share-based compensation | 10 | 89 | 28 |
| Risk management gains | 14 | (58) | - |
| Foreign exchange | | 2,065 | 9 |
| Gain on disposition of assets | 5 | (3) | - |
| Total expenses | | 6,322 | 2,440 |
| Loss before taxes | | (20) | (2,363) |
| Deferred tax expense | | (1,068) | - |
| Net loss | | (1,088) | (2,363) |
| Exchange loss on translation of foreign operations | | (987) | (8,352) |
| Comprehensive loss | | (2,075) | (10,715) |
| Net loss per share | | | |
| Basic | 10 | (0.01) | (0.02) |
| Diluted | | (0.01) | (0.02) |

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, | |
|---|------|---------------------------------|----------|
| | | 2021 | 2020 |
| Common Shares | | | |
| Balance, beginning of period | | 156,755 | 156,355 |
| Issue of common shares – options exercised | 10 | 67 | 146 |
| Share issuance costs | | - | (3) |
| Balance, end of period | | 156,822 | 156,498 |
| Contributed surplus | | | |
| Balance, beginning of period | | 2,821 | 2,790 |
| Share-based compensation expense | 10 | 89 | 28 |
| Share-based compensation capitalized | 4,5 | 7 | 9 |
| Options exercised | | (38) | (152) |
| Balance, end of period | | 2,879 | 2,675 |
| Deficit | | | |
| Balance, beginning of period | | (71,172) | (76,878) |
| Net loss | | (1,088) | (2,363) |
| Balance, end of period | | (72,260) | (79,241) |
| Accumulated Other Comprehensive Loss | | | |
| Balance, beginning of period | | (35,294) | (26,393) |
| Other comprehensive loss | | (987) | (8,352) |
| Balance, end of period | | (36,281) | (34,745) |

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, | |
|---|------|---------------------------------|--------------|
| | | 2021 | 2020 |
| Operating Activities | | | |
| Net loss | | (1,088) | (2,363) |
| Adjustments for non-cash items: | | | |
| Depletion and depreciation | 5,6 | 1,674 | 62 |
| Impairment | 5 | - | 1,381 |
| Finance expenses | 12 | 994 | 276 |
| Share-based compensation | 10 | 89 | 28 |
| Gain on disposition of assets | 5 | (3) | - |
| Foreign exchange | | 2,067 | (20) |
| Unrealized risk management gains | 14 | (44) | - |
| Deferred tax | | 1,068 | - |
| Settlement of decommissioning liabilities | 8 | (1) | (1) |
| Funds flow from operations | | 4,756 | (637) |
| Changes in non-cash working capital | 15 | (452) | (267) |
| | | 4,304 | (904) |
| Financing Activities | | | |
| Credit Facility (repayments) advances | 9 | (2,500) | 8,000 |
| Interest on credit facility | 9 | (354) | (36) |
| Issue of common shares, net of share issuance costs | | 30 | 48 |
| Lease liabilities payments | 6 | (474) | (56) |
| Repayment of other liabilities | | - | (111) |
| Changes in non-cash working capital | 15 | (6) | (92) |
| | | (3,304) | 7,753 |
| Investing Activities | | | |
| Expenditures on exploration and evaluation assets | 4 | (736) | (427) |
| Expenditures on property, plant and equipment | 5 | (128) | (1,136) |
| Proceeds on dispositions | 3,5 | 125 | 158 |
| Change in restricted cash | | (9) | 117 |
| Changes in non-cash working capital | 15 | (16) | (377) |
| | | (764) | (1,665) |
| Change in cash and cash equivalents | | 236 | 5,184 |
| Effect of foreign exchange on cash balances | | (412) | (178) |
| Cash and cash equivalents, beginning of period | | 5,159 | 1,215 |
| Cash and cash equivalents, end of period | | 4,983 | 6,221 |
| Cash and cash equivalents consist of: | | | |
| Cash | | 2,457 | 5,968 |
| Cash equivalents | | 2,526 | 253 |
| Supplemental information: | | | |
| Cash income taxes paid | | - | - |
| Cash interest income received | | 2 | 4 |

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, 2021 (unaudited)

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

NOTE 1 – CORPORATE INFORMATION AND BASIS OF PRESENTATION

Alvopetro Energy Ltd. (“Alvopetro” or “the Company”) is engaged in the exploration for, and the acquisition, development and production of, hydrocarbons in the Recôncavo basin onshore 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.

The interim condensed consolidated financial statements as at March 31, 2021 and December 31, 2020 and for the three months ended March 31, 2021 and March 31, 2020 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, 2020. 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, 2020.

These interim condensed consolidated financial statements were authorized for issuance by the Company’s Board of Directors on May 12, 2021.

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

Use of Estimates, Judgments and Assumptions and Estimation Uncertainty

The timely preparation of the consolidated interim financial statements requires management to make estimates, judgments and assumptions that may affect the reported amounts of assets and liabilities, disclosures of contingencies and the reported amounts of expenses during the period. Details on these estimates, judgments and assumptions are included in the audited consolidated financial statements as at and for the year ended December 31, 2020.

Impact of the COVID-19 Pandemic

The economic uncertainty created by the COVID-19 pandemic has significantly disrupted global commercial activity resulting in commodity price and foreign exchange volatility. For Alvopetro, the most significant estimates, judgments and assumptions potentially affected by COVID-19 relate to the valuation of property, plant and equipment. Amounts recorded for depletion and depreciation, decommissioning provision and deferred taxes are also based on several assumptions and estimates with respect to oil and natural gas reserves, which are impacted by the worldwide economic climate. Any potential direct and indirect impact to the Company has been considered in management’s estimates at the period end; however, there could be material impacts in future periods, the extent of which is unknown.

Property, Plant & Equipment

During the three months ended March 31, 2021, management determined that the Gomo asset had satisfied the conditions for technical feasibility and commercial viability in accordance with the Company’s accounting policies and as such, its \$30.0 million carrying value was transferred from E&E assets to the Caburé cash-generating unit (“CGU”) within PP&E assets. This determination involves significant estimates and assumptions and requires management’s interpretation of accounting standards for exploration and evaluation assets. This transfer has resulted in higher depletion expense with the incremental depletable base for the Caburé CGU.

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

As at and for the three months ended March 31, 2021 (unaudited)

*All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted***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 2020 annual consolidated financial statements. The Company has not early adopted any standard, interpretation, or amendment that has been issued but is not yet effective.

NOTE 3 – ASSETS HELD FOR SALE

| | As at | |
|------------------------------|-------------------|----------------------|
| | March 31, 2021 | December 31, 2020 |
| Balance, beginning of period | 128 | 332 |
| Impairment | - | (4) |
| Disposition | (119) | (158) |
| Foreign currency translation | (9) | (42) |
| Balance, end of period | - | 128 |

During the three months ended March 31, 2021, the Company disposed of land for proceeds equal to the carrying value, resulting in no gain or loss on the transaction.

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

| | As at | |
|--|-------------------|----------------------|
| | March 31, 2021 | December 31, 2020 |
| Balance, beginning of period | 32,262 | 35,971 |
| Capital expenditures | 736 | 992 |
| Capital expenditures – non-cash | - | 3 |
| Capitalized share-based compensation | 5 | 10 |
| Change in decommissioning liabilities (Note 8) | 7 | - |
| Transfer (to) from PP&E (Note 5) | (29,976) | 99 |
| Other transfers | - | (1) |
| Impairment | - | 21 |
| Foreign currency translation | (189) | (4,833) |
| Balance, end of period | 2,845 | 32,262 |

The amount transferred to PP&E in the three months ended March 31, 2021 represents the Company’s carrying value of its Gomo natural gas asset which includes the 183(1) and 197(1) wells on Blocks 183 and Block 197, respectively. Proved plus probable reserves have been assigned to the Gomo gas project since December 31, 2018 and the Company continued to evaluate the technical feasibility and commercial viability of the property since that time. In early 2020 Alvo Petro completed a stimulation and initial production test on the 183(1) well and another production test was completed in early 2021. Following this test, the Company made the decision to declare commerciality on Block 183, which was ultimately filed in April 2021. Given the results of the stimulation and production testing, reserves assigned to date and additional prospects on this project, to which the Company has been assigned contingent and prospective resources, there was no impairment on this E&E asset at the time of the transfer.

The Company holds equipment inventory which has been predominantly used for exploration wells and accordingly, its carrying value of \$1.5 million (December 31, 2020 - \$1.1 million) is included in E&E assets.

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

As at and for the three months ended March 31, 2021 (unaudited)

*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, 2021 | December 31, 2020 |
| Cost, beginning of period | 31,189 | 34,354 |
| Capital expenditures – cash | 128 | 2,425 |
| Capital expenditures – non-cash | - | 394 |
| Capitalized share-based compensation | 2 | 12 |
| Transfer from (to) E&E assets (Note 4) | 29,976 | (99) |
| Asset disposition | (7) | - |
| Foreign currency translation | (3,321) | (5,897) |
| Cost, end of period | 57,967 | 31,189 |
| Accumulated depletion, depreciation and impairment, beginning of period | (5,346) | (3,370) |
| Depletion and depreciation for the period | (1,430) | (1,496) |
| Impairment | - | (1,381) |
| Asset disposition | 4 | - |
| Foreign currency translation | 704 | 901 |
| Accumulated depletion, depreciation and impairment, end of period | (6,068) | (5,346) |
| Net book value, end of period | 51,899 | 25,843 |

General and administrative costs totaling \$0.1 million (December 31, 2020 - \$0.5 million) and finance expenses of \$nil (December 31, 2020 - \$0.6 million) that were directly related to property, plant, and equipment activities have been capitalized.

At the onset of the COVID-19 pandemic the Company determined that indications of impairment existed as at March 31, 2020 and an impairment test resulted in a \$1.4 million impairment charge on the Company’s Bom Lugar field.

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

As at and for the three months ended March 31, 2021 (unaudited)

*All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted***NOTE 6 – 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 | |
|--------------------------------------|-------------------|----------------------|
| | March 31, 2021 | December 31, 2020 |
| Net book value, beginning of period | 8,092 | 219 |
| Additions | 13 | 8,494 |
| Depreciation of ROU assets | (244) | (574) |
| Foreign currency translation | (309) | (47) |
| Net book value, end of period | 7,552 | 8,092 |
| Net Book Value by Asset Class | | |
| Natural gas facility | 7,390 | 7,890 |
| Office space | 78 | 105 |
| Surface land access | 84 | 97 |
| Total Net Book Value | 7,552 | 8,092 |

The Company’s lease liabilities are as follows:

| | As at | |
|--|-------------------|----------------------|
| | March 31, 2021 | December 31, 2020 |
| Lease liabilities, beginning of period | 8,310 | 163 |
| Additions | 13 | 8,494 |
| Finance expense | 356 | 706 |
| Lease payments | (474) | (1,014) |
| Foreign currency translation | (19) | (39) |
| Lease liabilities, end of period | 8,186 | 8,310 |
| Current | 476 | 483 |
| Non-current | 7,710 | 7,827 |
| Total | 8,186 | 8,310 |

The majority of the right-of-use assets and the lease liabilities are related to the lease component contained in Alvo Petro’s 10-year contract (the “Gas Treatment Agreement”) with Enerflex Ltd. (“Enerflex”).

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

As at and for the three months ended March 31, 2021 (unaudited)

*All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted***NOTE 7 – OTHER ASSETS**

Other assets represents the unamortized portion of the Company's deferred financing costs associated with the Company's Credit Facility.

| | As at | |
|--|-------------------|----------------------|
| | March 31, 2021 | December 31, 2020 |
| Balance, beginning of period | 1,128 | 1,790 |
| Amortization of deferred financing costs | (158) | (650) |
| Foreign currency translation | (1) | (12) |
| Balance, end of period | 969 | 1,128 |

NOTE 8 – DECOMMISSIONING LIABILITIES

Decommissioning liabilities are 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 | |
|------------------------------|-------------------|----------------------|
| | March 31, 2021 | December 31, 2020 |
| Balance, beginning of period | 1,143 | 1,380 |
| Liabilities incurred | 7 | - |
| Obligations settled | (1) | (5) |
| Accretion | 20 | 80 |
| Foreign currency translation | (114) | (312) |
| Balance, end of period | 1,055 | 1,143 |
| Current | 62 | 63 |
| Non-current | 993 | 1,080 |
| Total | 1,055 | 1,143 |

Total undiscounted cash flows, escalated at 5.5% (December 31, 2020 - 5.5%) for inflation, required to settle the Company's decommissioning liabilities are estimated to be \$5.4 million (December 31, 2020 - \$5.8 million). These estimated cash flows are discounted using an average risk-free rate of 7.5% (December 31, 2020 - 6.9%).

NOTE 9 – CREDIT FACILITY

| | As at | |
|-------------------------------------|-------------------|----------------------|
| | March 31, 2021 | December 31, 2020 |
| Balance at beginning of period | 15,423 | 5,027 |
| (Repayments) draws on Facility | (2,500) | 10,000 |
| Accrued interest due upon repayment | 106 | 396 |
| Balance at end of period | 13,029 | 15,423 |

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

As at and for the three months ended March 31, 2021 (unaudited)

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

The Credit Facility contains certain customary financial and non-financial covenants, standard representations and warranties, and events of default. Financial covenants include a minimum debt service ratio of 1.30:1 and a maximum leverage ratio of 2.25:1. As at March 31, 2021 the Company was in compliance with all covenants.

Subsequent to March 31, 2021, the Company negotiated an amendment to the Credit Facility which consists of a one-year extension of the maturity date to October 8, 2023, elimination of the 3% per annum interest payable upon repayment (effective April 15, 2021), and relaxation of covenants with respect to dividend payments.

NOTE 10 – 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

| | Number of Shares | Amount (\$) |
|-------------------------------------|---------------------|----------------|
| Balance as at December 31, 2019 | 97,849,788 | 156,355 |
| Exercise of stock options | 1,611,612 | 403 |
| Share issue costs | - | (3) |
| Balance as at December 31, 2020 | 99,461,400 | 156,755 |
| Exercise of stock options | 264,911 | 67 |
| Share issue costs | - | - |
| Balance as at March 31, 2021 | 99,726,311 | 156,822 |

At March 31, 2021, there were 8,432,868 warrants outstanding that are exercisable into an equal number of common shares with a weighted average life of 1.47 years that are exercisable at USD\$0.60 per warrant.

b) Options to Purchase Common Shares

Alvopetro has a stock option 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 at March 31, 2021 are as follows:

| | Number of Options | Weighted Average Exercise Price (CAD\$) |
|--|----------------------|---|
| Balance as at December 31, 2019 | 8,038,750 | 0.38 |
| Granted | 1,308,000 | 0.81 |
| Exercise of options for common shares | (1,611,612) | 0.29 |
| Adjustment for net settlement of options | (859,711) | 0.40 |
| Adjustment for cash settlement of options | (123,677) | 0.40 |
| Balance as at December 31, 2020 | 6,751,750 | 0.47 |
| Exercise of options for common shares | (264,911) | 0.29 |
| Adjustment for net settlement of options | (91,089) | 0.29 |
| Balance as at March 31, 2021 | 6,395,750 | 0.48 |
| Percentage of common shares outstanding | 6% | |

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

As at and for the three months ended March 31, 2021 (unaudited)

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

| Options Outstanding at March 31, 2021 | | | | Options Exercisable at March 31, 2021 | | |
|---------------------------------------|-------------------|---|---|---------------------------------------|---|---|
| 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 | 2,817,750 | 0.26 | 1.4 | 2,817,750 | 0.26 | 1.4 |
| CAD\$0.40 - \$0.75 | 2,270,000 | 0.57 | 3.1 | 1,190,004 | 0.52 | 2.9 |
| CAD\$0.76 - \$1.00 | 1,308,000 | 0.81 | 5.0 | - | - | - |
| CAD\$0.18 - \$1.00 | 6,395,750 | 0.48 | 2.7 | 4,007,754 | 0.34 | 1.8 |

c) Share-Based Compensation

The fair value of the stock options and restricted share units (“RSUs”) granted under AlvoPetro’s share based compensation plans is estimated on the grant date using the Black-Scholes option pricing model. There were no stock option or RSU grants during the three months ended March 31, 2021 or March 31, 2020.

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.

d) Net Loss Per Share

Net loss per share is calculated by dividing net loss by the weighted average number of common shares outstanding during the applicable period.

| | Period ended March 31, | |
|---|------------------------|------------|
| | 2021 | 2020 |
| Weighted average common shares outstanding, basic and diluted | 99,705,489 | 98,307,766 |

(1) Exercise price of warrants with USD-denominated exercise price translated to CAD at the period-end rate.

In determination of the weighted average number of diluted common shares outstanding for the three months ended March 31, 2021 and 2020, all stock options and warrants were excluded because the effect would be anti-dilutive.

NOTE 11 – REVENUE FROM CONTRACTS WITH CUSTOMERS

| | Period ended March 31, | |
|-------------|------------------------|------|
| | 2021 | 2020 |
| Natural gas | 6,373 | - |
| Condensate | 566 | 34 |
| Oil | - | 27 |
| Total | 6,939 | 61 |

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 Brazilian Real (“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.

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

As at and for the three months ended March 31, 2021 (unaudited)

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

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.

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 period ended March 31, 2021 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.

NOTE 12 – NATURE OF EXPENSES

Production expenses by nature were as follows:

| | Period Ended March 31, | |
|----------------------------------|------------------------|-----------|
| | 2021 | 2020 |
| Personnel | 60 | 15 |
| Facility and pipeline | 372 | - |
| Other fixed | 225 | 23 |
| Variable | 34 | 6 |
| Workover | 19 | - |
| Total production expenses | 710 | 44 |

General and administrative expenses ("G&A") by nature were as follows:

| | Period Ended March 31, | |
|------------------------------|------------------------|------------|
| | 2021 | 2020 |
| Personnel | 517 | 608 |
| Travel | 1 | 11 |
| Office and IT costs | 32 | 34 |
| Professional fees | 169 | 82 |
| General corporate | 236 | 116 |
| Gross G&A expenses | 955 | 851 |
| Capitalized to PP&E (Note 5) | (62) | (96) |
| Capitalized to E&E (Note 4) | (42) | (115) |
| Net G&A expenses | 851 | 640 |

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.

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

As at and for the three months ended March 31, 2021 (unaudited)

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

Finance expenses by nature are as follows:

| | Period Ended March 31, | |
|---|------------------------|-------|
| | 2021 | 2020 |
| Lease interest (Note 6) | 356 | 2 |
| Accretion of decommissioning liabilities (Note 8) | 20 | 19 |
| Amortization of deferred financing costs (Note 7) | 158 | 160 |
| Interest on Credit Facility (Note 9) | 460 | 267 |
| Gross finance expenses | 994 | 448 |
| Capitalized to PP&E | - | (112) |
| Capitalized to E&E | - | (60) |
| Net finance expenses | 994 | 276 |

The portion of interest on the Credit Facility and the amortization of deferred financing costs that were directly attributable to eligible PP&E and E&E projects in 2020 were capitalized to those assets.

NOTE 13 – CAPITAL MANAGEMENT

The Company's capital consists of the following:

| | As at | |
|----------------------------------|-------------------|----------------------|
| | March 31, 2021 | December 31, 2020 |
| Cash and cash equivalents | 4,983 | 5,159 |
| Non-cash working capital surplus | 792 | 380 |
| Credit Facility | (13,029) | (15,423) |
| Net debt | (7,254) | (9,884) |
| Lease liabilities – non-current | (7,710) | (7,827) |
| Shareholders' equity | 51,160 | 53,110 |

Alvopetro may adjust its capital structure by issuing new equity or debt and adjusting its capital expenditure program, as allowed pursuant to contracted work commitments.

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, other liabilities, risk management contracts and the Credit Facility.

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. A description of the nature and significance 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, 2020 with updated information for the current period as follows:

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

As at and for the three months ended March 31, 2021 (unaudited)

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

Market uncertainty associated with the COVID-19 pandemic is incorporated into management's risk assessments but given the lack of precedence continues to be difficult to accurately predict.

Foreign Currency Risk

Alvopetro's long-term gas sales agreement ("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:

| | Period Ended | |
|---|-------------------|------|
| | March 31, 2021 | 2020 |
| Increase (decrease) to natural gas revenues from: | | |
| 5% Appreciation of BRL to USD | 335 | - |
| 10% Appreciation of BRL to USD | 708 | - |
| 5% Depreciation of BRL to USD | (303) | - |
| 10% Depreciation of BRL to USD | (579) | - |

To manage exposure to foreign exchange volatility with respect to the BRL, the Company has entered into BRL/USD forward exchange rate contracts. As of March 31, 2021, the Company has a total of BRL2.0 million forward exchange contracts with settlements based on fixed rates between 5.12 and 5.42 and settlement dates occurring until July 2021. The Company recognizes the fair value of these contracts in the statement of financial position, included with trade and other receivables or other liabilities, with changes in fair value recognized as an unrealized gain or loss included in earnings. Realized gains or losses are recognized in the period the contracts are settled.

The fair value of the risk management contracts as at March 31, 2021 was an asset of \$0.03 million (December 31, 2020 – liability of \$0.01 million).

The realized and unrealized gains recognized in the three months ended March 31, 2021 are as follows:

| | Period Ended March 31, | |
|------------------|------------------------|------|
| | 2021 | 2020 |
| Realized gains | 14 | - |
| Unrealized gains | 44 | - |
| Total | 58 | - |

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

As at and for the three months ended March 31, 2021 (unaudited)

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

The following financial instruments are denominated in currencies other than the USD:

| | As at | | | |
|--|----------------|-------------|-------------------|-------------|
| | March 31, 2021 | | December 31, 2020 | |
| | CAD (000's) | BRL (000's) | CAD (000's) | BRL (000's) |
| Cash and cash equivalents | 107 | 14,392 | 64 | 4,282 |
| Restricted cash – current | - | 699 | - | 651 |
| Trade and other receivables | 49 | 18,467 | 40 | 14,156 |
| Other assets | - | 170 | - | - |
| Accounts payable and accrued liabilities | (431) | (12,610) | (415) | (10,371) |
| Other liabilities | - | - | - | (65) |
| Net exposure in foreign currency | (275) | 21,118 | (311) | 8,653 |
| Net exposure in USD (\$000s) | (219) | 3,707 | (244) | 1,665 |

In addition, a portion of the Company's receivable from its Brazilian subsidiary is considered to be an investment that is not long term or permanent in nature. As a result, the Company recorded a foreign exchange loss of \$1.7 million for the three months ended March 31, 2021 (March 31, 2020 – nil) related to the change in the BRL to USD exchange rate on this balance.

Credit Risk

The Company is subject to increased credit risk as the Company has one customer for its natural gas production contributing to economic dependence on this one counterparty. There were no expected credit losses recognized in the three months ended March 31, 2021 and the majority of the accounts receivable balance was collected subsequent to the end of the quarter.

Fair Value of Financial Instruments

There were no transfers of any financial instruments between levels within the fair value hierarchy during the period ended March 31, 2021.

Given the short term to maturity of the Company's financial assets and liabilities the carrying values approximate their fair values.

NOTE 15 – CHANGES IN NON-CASH WORKING CAPITAL

| | Three Months Ended | |
|--|--------------------|-------|
| | March 31, 2021 | 2020 |
| Change in: | | |
| Trade and other receivables | (469) | (61) |
| Prepaid expenditures | (269) | 195 |
| Accounts payable and accrued liabilities | 264 | (870) |
| | (474) | (736) |
| Changes relating to: | | |
| Operating activities | (452) | (267) |
| Financing activities | (6) | (92) |
| Investing activities | (16) | (377) |
| | (474) | (736) |

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

As at and for the three months ended March 31, 2021 (unaudited)

*All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted***NOTE 16 – COMMITMENTS AND CONTINGENCIES**

The following is a summary of contractual commitments as at March 31, 2021:

| Commitments | < 1 Year | 1-3 Years | Thereafter | Total |
|---|--------------------|------------------|-------------------|---------------|
| Minimum work commitments ⁽¹⁾ | | | | |
| Block 183 | 585 | - | - | 585 |
| Bom Lugar | - | 61 | - | 61 |
| Mãe-da-lua | - | - | 61 | 61 |
| Minimum work commitments | 585 | 61 | 61 | 707 |
| Gas Treatment Agreement | 1,036 | 2,073 | 6,477 | 9,586 |
| Total commitments | 1,621 | 2,134 | 6,538 | 10,293 |

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.

Amounts presented above for the Gas Treatment Agreement represent the monthly service fees for operation and maintenance of the Facility and Alvo Petro's 11-kilometre transfer pipeline.

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