



INTERIM FINANCIAL STATEMENTS SEPTEMBER 30, 2017

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 September 30, 2017 and December 31, 2016 and the Interim Condensed Consolidated Statements of Operations and Comprehensive Loss and the Interim Condensed Consolidated Statements of Cash Flows for the three and nine months ended September 30, 2017 and 2016. 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	September 30, 2017	December 31, 2016
ASSETS			
Current			
Cash and cash equivalents		11,385	17,788
Restricted cash	3	110	108
Trade and other receivables		319	431
Prepaid expenditures		137	196
Assets held for sale	4	247	410
Total current assets		12,198	18,933
Exploration and evaluation assets	5	56,447	53,259
Property, plant and equipment	6	4,795	4,860
Non-current assets		61,242	58,119
Total assets		73,440	77,052
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities			
Accounts payable and accrued liabilities		2,199	1,878
Current portion of decommissioning liabilities	7	19	78
Total current liabilities		2,218	1,956
Decommissioning liabilities	7	1,500	1,321
Total liabilities		3,718	3,277
Shareholders' equity			
Share capital	8	151,937	151,937
Contributed surplus		1,640	1,558
Deficit		(65,428)	(60,390)
Accumulated other comprehensive loss		(18,427)	(19,330)
Total shareholders' equity		69,722	73,775
Total liabilities and shareholders' equity		73,440	77,052

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

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

		Three months ended September 30,		Nine months ended September 30,	
	Note	2017	2016	2017	2016
Revenue					
Oil sales		120	74	377	353
Royalties and production taxes		(12)	(8)	(41)	(37)
Oil revenue		108	66	336	316
Other income		13	29	113	83
Total revenue and other income		121	95	449	399
Expenses					
Production	12	186	264	651	983
Transportation		6	4	19	22
General and administrative	12	669	854	1,971	2,735
Depletion and depreciation	6	70	87	183	312
Impairment	5	2,384	4,491	2,384	7,480
Exploration and evaluation expenses		120	61	177	213
Accretion of decommissioning liabilities	7	10	6	28	19
Share-based compensation	8	20	37	66	89
(Gain) loss on disposition of assets	4,5	(2)	41	16	41
Foreign exchange (gain) loss		(11)	10	(8)	(19)
Total expenses		3,452	5,855	5,487	11,875
Loss before taxes		(3,331)	(5,760)	(5,038)	(11,476)
Income tax (recovery) expense		-	(68)	-	731
Net loss		(3,331)	(5,692)	(5,038)	(12,207)
Exchange gain (loss) on translation of foreign operations		1,525	(453)	903	6,709
Comprehensive loss		(1,806)	(6,145)	(4,135)	(5,498)
Net loss per share					
	8				
Basic		(0.04)	(0.07)	(0.06)	(0.14)
Diluted		(0.04)	(0.07)	(0.06)	(0.14)

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)

		Nine Months Ended September 30,	
	Note	2017	2016
Common Shares			
Balance, beginning of period		151,937	151,937
Net change		-	-
Balance, end of period		151,937	151,937
Contributed surplus			
Balance, beginning of period		1,558	1,444
Share-based compensation expense	8	66	89
Share-based compensation capitalized	8	16	29
Balance, end of period		1,640	1,562
Deficit			
Balance, beginning of period		(60,390)	(47,812)
Net loss		(5,038)	(12,207)
Balance, end of period		(65,428)	(60,019)
Accumulated Other Comprehensive Loss			
Balance, beginning of period		(19,330)	(24,837)
Other comprehensive gain		903	6,709
Balance, end of period		(18,427)	(18,128)

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)

		Three months ended September 30,		Nine months ended September 30,	
		2017	2016	2017	2016
Operating Activities					
Net loss		(3,331)	(5,692)	(5,038)	(12,207)
Adjustments for non-cash items:					
Depletion and depreciation	6	70	87	183	312
Impairment		2,384	4,491	2,384	7,480
Accretion of decommissioning liabilities	7	10	6	28	19
Share-based compensation	8	20	37	66	89
Deferred tax		-	(68)	-	731
(Gain) loss on disposition of assets	4,5	(2)	41	16	41
Unrealized foreign exchange loss		3	5	21	6
Settlement of decommissioning liabilities	7	(113)	(62)	(139)	(160)
Funds flow from operations		(959)	(1,155)	(2,479)	(3,689)
Changes in non-cash working capital	11	376	593	(125)	320
		(583)	(562)	(2,604)	(3,369)
Investing Activities					
Expenditures on exploration and evaluation assets		(1,599)	(3,412)	(4,508)	(6,960)
Expenditures on property, plant and equipment		(11)	(373)	(41)	(726)
Proceeds on disposition of assets	4,5	78	311	160	311
Change in restricted cash	3	-	(108)	-	2,180
Changes in non-cash working capital	11	920	2,082	389	1,373
		(612)	(1,500)	(4,000)	(3,822)
Change in cash and cash equivalents		(1,195)	(2,062)	(6,604)	(7,191)
Effect of foreign exchange on cash balances		1	110	201	285
Cash and cash equivalents, beginning of period		12,579	23,779	17,788	28,733
Cash and cash equivalents, end of period		11,385	21,827	11,385	21,827
Cash and cash equivalents consist of:					
Cash		2,693	5,621	2,693	5,621
Cash equivalents		8,692	16,206	8,692	16,206
Supplemental information:					
Cash income taxes paid		-	-	-	-
Cash interest income received		21	22	112	71

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 and nine months ended September 30, 2017

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, 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 8th Avenue S.W., Calgary, Alberta, Canada, T2P 1G1.

The interim condensed consolidated financial statements as at September 30, 2017 and December 31, 2016 and for the three and nine months ended September 30, 2017 and September 30, 2016 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, 2016, 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, 2016.

These interim condensed consolidated financial statements were authorized for issuance by the Company’s Board of Directors on November 15, 2017.

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 September 30, 2017 and December 31, 2016 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 2016 annual consolidated financial statements with the exception of amendments made to IAS 7, *Statement of Cash Flows* which were effective January 1, 2017. The revisions require additional disclosures relating to changes in liabilities arising from financing activities, including changes arising from cash flow and non-cash changes. The adoption of these amendments had no impact on the amounts recorded in the Company’s interim condensed consolidated financial statements

Standards issued but not yet effective

The Company has reviewed the following new and revised accounting pronouncements that have been issued but are not yet effective that 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 and nine months ended September 30, 2017

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 2 <i>Share-based Payment</i> – In June 2016, the IASB issued amendments to IFRS 2 to clarify the classification and measurement of share-based payment transactions.	January 1, 2018	The Company does not expect the amendments to have a material impact on the financial statements.
IFRS 15 <i>Revenue from Contracts with Customers</i> – The new standard will replace existing revenue guidance. It requires entities to recognize revenue reflective of the transfer of goods and services for the expected consideration received, upon transfer of control to the purchaser. The standard aims to report useful information to financial statement users about the nature, amount, timing and uncertainty of revenue and cash flows arising from a contract with a customer.	January 1, 2018	The Company is finalizing the assessment of its sales contracts and does not expect IFRS 15 to have a material impact on the consolidated financial statements, with the exception of expanded note disclosure that will be required to comply with this standard upon adoption.
IFRS 9 <i>Financial Instruments</i> – As of July 2015, the IASB completed the final elements of IFRS 9 which supersedes IAS 39 <i>Financial Instruments: Recognition and Measurement</i> . IFRS 9 introduces new models for classification and measurement of financial instruments, hedge accounting and impairment of financial assets.	January 1, 2018	The Company does not expect the new standard to have a material impact on the financial statements.
IFRS 16 <i>Leases</i> - IFRS 16 was issued 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 – RESTRICTED CASH AND CREDIT FACILITY

	As at	
	September 30, 2017	December 31, 2016
Restricted cash – current	110	108
Restricted cash – non-current	-	-
Balance, end of period	110	108

The Company has a credit support facility (the “Facility”) with a Canadian bank which allows for the issuance of letters of credit (“LC’s”) 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. LC’s 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 September 30, 2017, the total amount of LC’s issued under the Facility was \$14.1 million (December 31, 2016 - \$14.1 million), the full balance of which was supported by EDC on behalf of Alvopetro. The current restricted cash as at December 31, 2016 and September 30, 2017 relates to cash posted for abandonment guarantees in Brazil for the Bom Lugar and Jiribatuba fields. These guarantees are posted locally in Brazil, are not part of the Facility and are not eligible for EDC coverage.

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

As at and for the three and nine months ended September 30, 2017

*All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted***NOTE 4 – ASSETS HELD FOR SALE**

	As at	
	September 30, 2017	December 31, 2016
Balance, beginning of period	410	-
Transferred from E&E (Note 5)	322	410
Disposal – cash proceeds	(105)	-
Disposal – in exchange for drilling services	(396)	-
Foreign currency translation	16	-
Balance, end of period	247	410

In several separate transactions during the nine months ended September 30, 2017, the Company disposed of equipment inventory classified as held for sale. Upon transfer to held for sale, all inventory was written down to the estimated recoverable amount and a nominal gain resulted from these dispositions. All dispositions were to third parties of Alvopetro and the drilling services received in exchange were measured at fair value. The balance at September 30, 2017, transferred from exploration and evaluation assets during the third quarter of 2017, consists of land owned by the Company which management plans to sell within a year.

NOTE 5 – EXPLORATION AND EVALUATION (“E&E”) ASSETS

	As at	
	September 30, 2017	December 31, 2016
Balance, beginning of period	53,259	48,409
Capital expenditures - cash	4,508	7,625
Capital expenditures - in exchange for assets	449	-
Capitalized share-based compensation	14	27
Change in decommissioning liabilities (Note 7)	189	164
Transfer to PP&E (Note 6) and operations	-	(185)
Transfer to assets held for sale (Note 4)	(322)	(410)
Asset dispositions	(135)	(300)
Impairment	(2,384)	(7,531)
Foreign currency translation	869	5,460
Balance, end of period	56,447	53,259

General and administrative costs totaling \$0.9 million (December 31, 2016 - \$1.0 million) that were directly related to exploration and evaluation activities have been capitalized as exploration and evaluation assets. Capital expenditures in the nine months ended September 30, 2017 include \$0.4 million of non-cash expenditures, largely in respect of drilling services received in exchange for assets held for sale.

During the nine months ended September 30, 2017 the Company disposed of equipment inventory classified as E&E in several separate transactions, all to third parties of Alvopetro. Proceeds, including both cash and non-cash consideration, totaled \$0.1 million, resulting in a loss of \$0.02 million.

During the three months ended September 30, 2017 the 177(A1) well was drilled on Block 177. No commercial quantities of hydrocarbons were discovered and the well was abandoned. Due to limited prospectivity on the block, an impairment loss of \$2.4 million was recorded to bring the carrying value of this block to \$nil at September 30, 2017. All costs incurred subsequent to the well abandonment have been recorded as exploration and evaluation expenditures on the consolidated statements of operations and comprehensive loss, including \$0.1 million recognized in the three months ended September 30, 2017 in respect of costs to fulfill the remaining work commitments on the block.

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

As at and for the three and nine months ended September 30, 2017

*All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted***NOTE 6 – PROPERTY, PLANT AND EQUIPMENT (“PP&E”)**

	As at	
	September 30, 2017	December 31, 2016
Cost, beginning of period	9,599	8,120
Capital expenditures	41	769
Transferred from E&E (Note 5)	-	114
Asset dispositions	-	(68)
Capitalized share-based compensation	2	7
Change in decommissioning liabilities	-	73
Foreign currency translation	315	584
Cost, end of period	9,957	9,599
Accumulated depletion and depreciation and impairment, beginning of period	(4,739)	(3,827)
Depletion and depreciation for the period	(183)	(416)
Asset dispositions	-	16
Impairment	-	(292)
Foreign currency translation	(240)	(220)
Accumulated depletion and depreciation and impairment, end of period	(5,162)	(4,739)
Net book value, end of period	4,795	4,860

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

NOTE 7 – 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	
	September 30, 2017	December 31, 2016
Balance, beginning of period	1,399	1,079
Liabilities incurred	189	320
Revisions to obligations	-	(83)
Obligations settled	(139)	(175)
Accretion	28	28
Foreign currency translation	42	230
Balance, end of period	1,519	1,399

Total undiscounted cash flows, escalated at 6.5% (December 31, 2016 - 6.5%) for inflation, required to settle the Company’s decommissioning liabilities are estimated to be \$2.2 million (December 31, 2016 - \$2.1 million) and have been discounted using an average risk free rate of 2.5% (December 31, 2016 – 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, 2016 - \$0.1 million) of decommissioning costs within one year from September 30, 2017 and accordingly this amount is classified as current on the consolidated statements of financial position.

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

As at and for the three and nine months ended September 30, 2017

*All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted***NOTE 8 – 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.

b) Issued and Outstanding Common Shares

	Number of Shares	Amount (\$000s)
Balance as at September 30, 2017 and December 31, 2016	85,166,871	\$ 151,937

c) Options to Purchase Common Shares

The options outstanding at September 30, 2017 are as follows:

	Number of Options	Weighted Average Exercise Price (CAD\$)
Balance as at December 31, 2015	6,843,436	0.66
Granted	2,461,500	0.24
Expired	(1,141,330)	0.84
Forfeited	(1,289,504)	0.42
Balance as at December 31, 2016	6,874,102	0.53
Granted	44,000	0.18
Expired	(279,166)	0.72
Balance, end of period	6,638,936	0.52

Options Outstanding at September 30, 2017				Options Exercisable at September 30, 2017		
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	3,138,500	0.25	3.75	847,670	0.29	3.29
CAD\$0.40 - \$0.75	1,528,000	0.42	2.30	1,181,330	0.43	2.31
CAD\$1.01 - \$1.10	1,972,436	1.02	1.23	1,972,436	1.02	1.23
CAD\$0.18 - \$1.10	6,638,936	0.52	2.67	4,001,436	0.69	1.99

Share-Based Compensation

There were no stock option grants during the three months ended September 30, 2017. The fair value of the stock options granted under the Alvopetro stock option plan is estimated on the grant date using the Black-Scholes option pricing model. Weighted average assumptions and resultant fair values for stock options granted are as follows:

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

As at and for the three and nine months ended September 30, 2017

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

	Three months ended September 30,		Nine months ended September 30,	
	2017	2016	2017	2016
Risk free interest rate (%)	-	0.60	0.87	0.45
Expected term (years)	-	4.0	4.0	2.2
Expected volatility (%)	-	45.0	45.0	49.7
Dividend per share (%)	-	-	-	-
Forfeiture rate (%)	-	5.0	5.0	5.0
Weighted average fair value (CAD\$)	-	0.09	0.06	0.10

Total share-based compensation of \$0.02 million and \$0.08 million was computed for the three and nine months ended September 30, 2017 (September 30, 2016 - \$0.05 million and \$0.1 million) related to the Alvopetro stock option plan. 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 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 and nine months ended September 30,	
	2017	2016
Weighted average common shares outstanding, basic and diluted	85,166,871	85,166,871

In determination of the weighted average number of diluted common shares outstanding for the three and nine months ended September 30, 2017 and 2016, all stock options were excluded because the effect would be anti-dilutive.

NOTE 9 – CAPITAL MANAGEMENT

The Company's capital consists of the following:

	As at	
	September 30, 2017	December 31, 2016
Working capital	9,999	17,055
Shareholders' equity	69,722	73,775

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 September 30, 2017, the Company's net working capital surplus of \$10.0 million (December 31, 2016 - \$17.1 million) included \$11.4 million (December 31, 2016 - \$17.8 million) of cash, \$0.1 million (December 31, 2016 - \$0.1 million) of current restricted cash, \$0.2 million (December 31, 2016 - \$0.4 million) of assets held for sale, net of a working capital deficit of \$1.7 million (December 31, 2016 - \$1.3 million).

EDC currently supports \$14.1 million of LC's provided in respect of Alvopetro's exploration work commitments in Brazil as discussed further in Note 13. LC's supported by EDC at September 30, 2017 include \$7.9 million of LC's on commitments which have been met or farmed out, subject to ANP approval. LC's for work commitments satisfied in 2016 and 2017 include LC's on Block 256 (\$0.4 million), Block 198 (\$1.5 million) and Block 177 (\$2.9 million). The LC for the work commitment associated with

ALVOPETRO ENERGY LTD.

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

As at and for the three and nine months ended September 30, 2017

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

Block 107 (\$3.1 million) was farmed out to a third party in 2016 and the work commitment was met during the three months ended September 30, 2017, subject to ANP approval.

The current restricted cash of \$0.1 million (December 31, 2016 - \$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 September 30, 2017 or December 31, 2016.

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 \$69.7 million (December 31, 2016 - \$73.8 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. Alvopetro expects that financing will be required to execute the full development of the Caburé field and may also be required to fund future capital expenditures on our existing exploration and evaluation assets and mature fields. Such funding may be facilitated through project financing, vendor financing, other debt issuances or equity issuances.

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

NOTE 10 – 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 Alvopetro'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 Alvopetro's financial instruments at September 30, 2017 and December 31, 2016 are set forth in the table below. The Company does not currently have any financial instruments classified as Level 2 or Level 3.

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

As at and for the three and nine months ended September 30, 2017

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

	As at			
	September 30, 2017		December 31, 2016	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Carried at fair value through profit or loss				
Cash and cash equivalents ⁽¹⁾	11,385	11,385	17,788	17,788
Restricted cash – current ⁽¹⁾⁽²⁾	110	110	108	108
	11,495	11,495	17,896	17,896
Carried at cost or amortized cost				
Trade and other receivables	319	319	431	431
Accounts payable and accrued liabilities	(2,199)	(2,199)	(1,878)	(1,878)
	(1,880)	(1,880)	(1,447)	(1,447)

(1) Level 1

(2) Restricted cash balances include amounts pledged as collateral for abandonment guarantees (Note 3).

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 for the year ended December 31, 2016 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 September 30, 2017:

	As at			
	September 30, 2017		December 31, 2016	
	CAD (000's)	BRL (000's)	CAD (000's)	BRL (000's)
Cash and cash equivalents	124	590	208	1,064
Restricted cash – current	-	351	-	351
Trade and other receivables	25	948	-	1,403
Accounts payable and accrued liabilities	(235)	(6,253)	(248)	(4,434)
Net exposure in foreign currency	(86)	(4,364)	(40)	(1,616)
Net exposure in USD (\$000s)	(69)	(1,378)	(30)	(496)

The Company had no forward exchange rate contracts in place as at or during the periods ended September 30, 2017 or December 31, 2016.

NOTE 11 – CHANGES IN NON-CASH WORKING CAPITAL

Change in:	Three months ended September 30,		Nine months ended September 30,	
	2017	2016	2017	2016
Trade and other receivables	143	65	181	23
Prepaid expenditures	94	81	64	188
Accounts payable and accrued liabilities	1,059	2,529	19	1,482
	1,296	2,675	264	1,693
Changes relating to:				
Operating activities	376	593	(125)	320
Investing activities	920	2,082	389	1,373
	1,296	2,675	264	1,693

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

As at and for the three and nine months ended September 30, 2017

*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 September 30,		Nine months ended September 30,	
	2017	2016	2017	2016
Production expenses:				
Personnel	88	59	274	266
Production facilities rental	-	-	-	277
Other fixed	58	48	178	178
Variable	40	31	91	136
Workover	-	126	108	126
Total production expenses	186	264	651	983

The majority of the Company's production expenses relate to personnel costs and, in 2016, production facilities rental costs for the 182(B1) well. This rental contract was cancelled during the three months ended June 30, 2016.

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

	Three months ended September 30,		Nine months ended September 30,	
	2017	2016	2017	2016
G&A expenses:				
Personnel	670	795	1,959	2,286
Travel	33	46	88	129
Office and IT	96	109	279	354
Professional fees	132	202	397	485
General corporate	66	76	135	359
Gross G&A expenses	997	1,228	2,858	3,613
Capitalized to E&E and PP&E	(328)	(374)	(887)	(878)
Net G&A expenses	669	854	1,971	2,735

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 that are directly attributable to exploration and development projects, primarily being personnel costs, are capitalized.

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

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*All tabular amounts are expressed in thousands of United States dollars, except per share amounts or as otherwise noted***NOTE 13 – COMMITMENTS AND CONTINGENCIES**

The following is a summary of contractual commitments as at September 30, 2017:

Commitments	< 1 Year	1-3 Years	Thereafter	Total
Minimum work commitments ⁽¹⁾				
<i>Minimum work commitments to be completed</i>				
Block 183	1,052	-	-	1,052
Block 106	360	-	-	360
Block 169	1,199	-	-	1,199
Block 255	1,436	-	-	1,436
Block 57 ⁽²⁾	-	280	-	280
Block 62 ⁽²⁾	-	280	-	280
Block 71 ⁽²⁾	-	191	-	191
Block 145 ⁽²⁾	-	280	-	280
Bom Lugar	-	-	110	110
Jiribatuba	-	-	110	110
Minimum work commitments to be completed	4,047	1,031	220	5,298
<i>Minimum work commitments incurred or farmed out</i>				
Block 107 ⁽³⁾	2,399	-	-	2,399
Block 177 ⁽⁴⁾	1,319	-	-	1,319
Block 198 ⁽⁵⁾	1,199	-	-	1,199
Minimum work commitments incurred or farmed out	4,917	-	-	4,917
Total minimum work commitments	8,964	1,031	220	10,215
Office leases⁽⁶⁾	207	62	-	269
Total commitments	9,171	1,093	220	10,484

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) Alvo Petro holds a 65% interest in each of these blocks and the amounts provided in the table above represent Alvo Petro's share of the related commitments.
- (3) In 2016, the Company entered into a farmout agreement with respect to Block 107. Under the terms of the agreement, the Farmee is responsible to satisfy the work commitment included in the table above. The work commitment was satisfied during the three months ended September 30, 2017, subject to ANP approval.
- (4) In the three months ended September 30, 2017, the Company drilled the 177(A1) well and incurred costs related to other work in satisfaction of the work commitment on Block 177, subject to ANP approval.
- (5) In the first quarter of 2017, the Company completed drilling the 198(A1) well in satisfaction of the work commitment in the table above, subject to ANP approval.
- (6) The Company is committed to future minimum payments for office space in Canada and Brazil.

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

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

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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 September 30, 2017, the potential estimated penalty was \$0.3 million (December 31, 2016 - \$0.2 million), which is included in accounts payable and accrued liabilities in the respective consolidated statements of financial position.