Initiation Report
June 24, 2008

Royale Energy, Inc.

NASDAQ: ROYL

Recent Price: $9.72
52 Week Range:
$2.18 – $11.59
Price Target: NA
Rating: NA

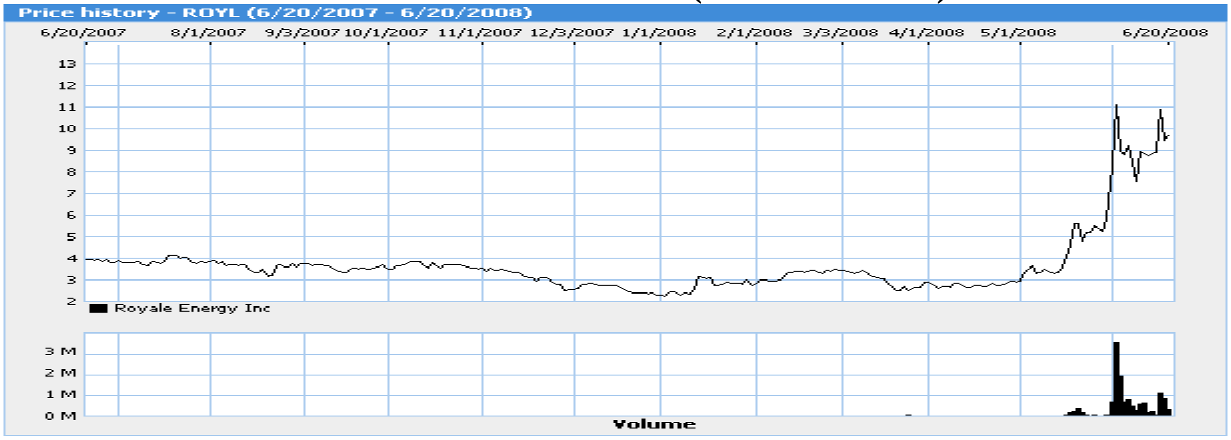
Lead Analyst:
Mohammad Sharifzadeh, PhD., CFA
msharif@alphabetaresearch.com
(949) 933 0780
Associate Analyst:
Simin Hojat, M.Phil.
simin@alphabetaresearch.com

KEY STATISTICS*

Shares outstanding, basic	**7.92**	**million**	**Proved reserves(1P)**	**3.9**	**Bcfe**
Market capitalization	**$76.98**	**million**	**Proved developed reserves**	**3.6**	**Bcfe**
Enterprise value	**$ 94.48**	**million**	**Standardized measure**	**$10.6**	**million**
Price /EBITDAX	**32.4 X**		**Production**	**875.7**	**MMcfe**
Price/Book value	**6.7 X**		**Market capitalization/1P**	**$21.38**	**per Mcfe**
Price/Revenue	**4.6 X**		**Reserve replacement ratio**	**NM**	

*Price and market values as of June 20, 2008. Reserves, production, and book values as of December 31, 2007

52-Week Price and Volume Chart (Source: msn.com)



FINANCIAL HIGHLIGHTS

All Amounts in $	2008 (Q1)	2007	2006	2005
Revenue	2,990,257	16,557,399	24,869,043	25,643,378
Operating income	(1,321,506)	(3,885,144)	(3,188,616)	2,257,444
Operating margin (%)	-44.2%	-23.5%	-12.8%	8.8%
Net income	(927,460)	(2,779,207)	(2,649,701)	1,185,903
Net margin (%)	-31.0%	-16.8%	-10.7%	4.6%
Earning per share, basic	(0.12)	(0.35)	(0.33)	0.15
EBITDAX[1]	245,223	2,366,063	12,500,379	7,444,463
EBITDAX margin[2] (%)	8.2%	14.3%	50.3%	29.0%
EBITDAX per basic share	0.03	0.30	1.58	0.95
Cash and cash equivalents	2,713,561	3,848,968	7,377,604	4,716,772
Property and equipment, net	23,989,091	23,389,741	20,525,960	31,220,651
Long-term debt	5,525,045	5,175,974	3,810,000	6,630,598
Stockholders' equity	11,476,039	12,384,810	15,548,314	18,318,290
Total assets	31,676,948	32,571,374	33,715,203	43,042,581
Long-term debt/Total assets (%)	17.4%	15.9%	11.3%	15.4%
EBITDAX/Interest expense	2.9 X	15.5 X	23.9 X	16.8 X
Net working capital	(6,482,964)	(4,846,444)	772,379	(2,141,034)
Cash flow from operating activities	746,608	4,427,012	3,406,393	6,395,442

1-For our method of calculating EBITDAX see page 17 in this report
2-That is EBITDAX divided by revenue

SUMMARY

Royale Energy Inc. (hereinafter called “ROYL” or the “Company”) is an independent exploration and development (E&P) oil and gas company; incorporated in California in 1986 and began operations in 1988. The Company’s principal lines of business are production and sale of natural gas, acquisition of oil and gas lease interests and proved reserves, drilling of both exploratory and development wells, and sales of fractional working interests in wells to be drilled by the Company.

Royale Energy Inc. has working interests in oil and gas properties in North California (Sacramento Basin and San Joaquin Basin), in Central California, in Utah, in Texas, and in Louisiana.

As of December 31, 2007, ROYL owned a total of 12,899.86 net developed acres and a total of 19,070.86 net undeveloped acres working interests in oil and gas properties. About 70% of the Company’s developed properties are located in California; whereas over 81% of the Company’s undeveloped properties are located in States other than California.

Royale Energy Inc. generally operates the wells it completes. As of December 31, 2007, ROYL operated 54 natural gas wells in California, had ownership interests in and operated two natural gas wells in Utah, and had non-operating interests in oil and gas wells; 17 in Texas, three in Oklahoma, two in California, and two in Louisiana.

Royale Energy Inc. is primarily a natural gas E&P company. As of December 31, 2007 ROYL had 23,866 Bbls (barrels) proved oil reserves (143,196 Mcfe gas equivalent) and natural gas proved reserves of 3,771,967 Mcf (thousand cubic feet), making it a total gas equivalent of 3,915,163 Mcfe (thousand cubic feet gas equivalent). Most of the Company's proved reserves are developed reserves.

As of December 31, 2007 over 90% of ROYL's proved reserves were proved developed reserves. The Company's standardized measure of proved reserves at December 31, 2007 was $10.6 million.

During the year 2007, ROYL's net gas production was 791,195 Mcf and its net production of crude oil was 14,088 Bbl. Total net production on the gas equivalent basis for the year 2007 was 875,723 Mcfe. For the first quarter of 2008, ROYL's net gas production was 175,822 Mcf and its net crude oil production was 3,069 Bbl, making it a total of 194,236 Mcfe of net production.

ROYL sells most of its California natural gas production through PG&E pipelines to independent customers on a monthly contract basis. The Company also sells some gas through privately owned pipelines to independent customers. Generally the entire month's production is sold to the highest bidder.

Royal Energy Inc. funds its operations and most of its capital expenditure needs through cash provided by operating activities. The Company has a $15 million revolving line of credit under a loan agreement with Guaranty Bank, FSB, which can draw on in case internal cash resources fall short of cash needed for new investments. On June 10, 2008 ROYL issued and sold, through a private placement, an aggregate of 547,945 shares of its common stock to an institutional investor at the price of $7.30 per share, for the gross proceeds of about $4 million.

ROYL has a low debt leverage compared to the industry. As of March 31, 2008, the Company's total long-term debt was $5.5 million; making a debt leverage ratio of 17.4%.

For the year ended December 31, 2007, ROYL reported $0.35 loss per basic share. However, the EBITDAX per basic share, which is a more appropriate measure of performance for oil and gas E&P companies, was $0.30 per basic share.

In its June 23, 2008 press release the Company reported that it expects to return to regular quarterly profitability in the second quarter ending June 30th, 2008 and continuing for the foreseeable future.

The Company's common stock trades on the NASDAQ National Market System under the symbol ROYL.

Over the past 12 months common shares of ROYL have outperformed the Jefferies North American Small/Midcap E & P Index by almost two times, on both an annual and on a daily basis. Since Early, 2008, the trading volume of ROYL's common stock has increased substantially. Whereas prior to June 2008 average daily volume was below 100,000 shares, recent daily volume has been as high as 3.5 million shares.

ROYL'S REVENUE MODEL

Royale Energy Inc. derives its revenues from three sources: sale of produced oil and gas, supervisory fees, and turnkey drilling contracts.

The Company generally operates the wells it completes and receives fees set by industry standards from the owners of fractional interests in the wells and from expense reimbursements.

In turnkey drilling contracts the Company sells fractional interests in undeveloped wells, recognizes gross revenue for the amount paid by the purchaser, and agrees to pay the drilling and development expenses of the wells for the participants. The Company calls this source of revenue direct working interest (WDI) sale to high net worth individuals.

Part of the money received from the WDI relates to pre-drilling costs which are non-refundable and recognized as revenue upon signing of the contract. The remaining amount is held by the Company as deferred revenue until drilling is completed. Drilling is usually completed within 10-30 days.

For the year ended December 31, 2007 the mix of revenue was 36.9% from sale of oil and gas, 56.8% from turnkey drilling contracts, and 6.3% from supervisory services. Similarly, for the first quarter of 2008 the mix of revenue was 57.4% from sale of oil and gas, 36.6% from turnkey drilling contracts, and 6.0% from supervisory services.

ROYL'S OIL AND GAS PROPERTIES

Royal Energy Inc. has working interests in oil and gas properties in North California (Sacramento Basin and San Joaquin Basin), in Central California, in Utah, in Texas, and in Louisiana. As of December 31, 2007, ROYL owned a total of 12,899.86 net developed acres and a total of 19,070.86 net undeveloped acres working interests in oil and gas properties. About 70% of the Company's developed properties are located in California; whereas over 81% of the Company's undeveloped properties are located in States other than California.

The following table summarizes the Company's developed and undeveloped gross and net leasehold acreage. Undeveloped acreage includes leased acres on which wells have not been drilled or completed to a point that would permit the production of commercial quantities of oil and gas, regardless of whether or not such acreage contains proved reserves.

ROYL's Leasehold Acreage						
	Developed		Undeveloped		Total	
	Gross	Net	Gross	Net	Gross	Net
California	15,585.58	9,092.28	4,513.64	3,511.27	20,099.22	12,603.55
All other States	10,986.21	3,807.58	30,431.13	15,559.59	41,417.34	19,367.17
Total	26,571.79	12,899.86	34,944.77	19,070.86	**61,516.56**	**31,970.72**

In the oil and gas business the term “working interest” or “leasehold interest” means an interest in an oil and gas lease that gives the owner of interest the right to drill for and produce oil and gas on the leased acreage (or wells). Gross acres (or wells) are acres (or wells) in which the Company has a working interest. Net acres (or wells) are the Company’s aggregate working interests in the gross acres (or wells).

The following table provides information about ROYL’s drilling activities during the years ended December 31, 2005, 2006 and 2007.

	Gross Wells			Net Wells	
2005	**Producing**	**Dry**	**Total**	**Producing**	**Dry**
Exploratory	3	3	6	0.7633	1.4791
Developmental	6	3	9	1.444	0.8148
2006					
Exploratory	3	3	6	0.3292	1.0801
Developmental	7	3	10	2.5921	1.0801
2007					
Exploratory	4	0	4	1.8424	0
Developmental	2	1	3	0.6007	0.4613

Exploratory Well means a well drilled to find and produce oil or gas reserves not classified as proved, to find a new production reservoir in a field previously found to be productive of oil or gas in another reservoir, or to extend a known reservoir.

Development Well means a well drilled within the proved area of an oil or gas reservoir to the depth of a stratigraphic horizon known to be productive.

Dry Hole or **Dry Well** means a well found to be incapable of producing hydrocarbons in sufficient quantities such that proceeds from the sale of such production exceed production expenses and taxes.

ROYL'S OIL AND GAS RESERVES

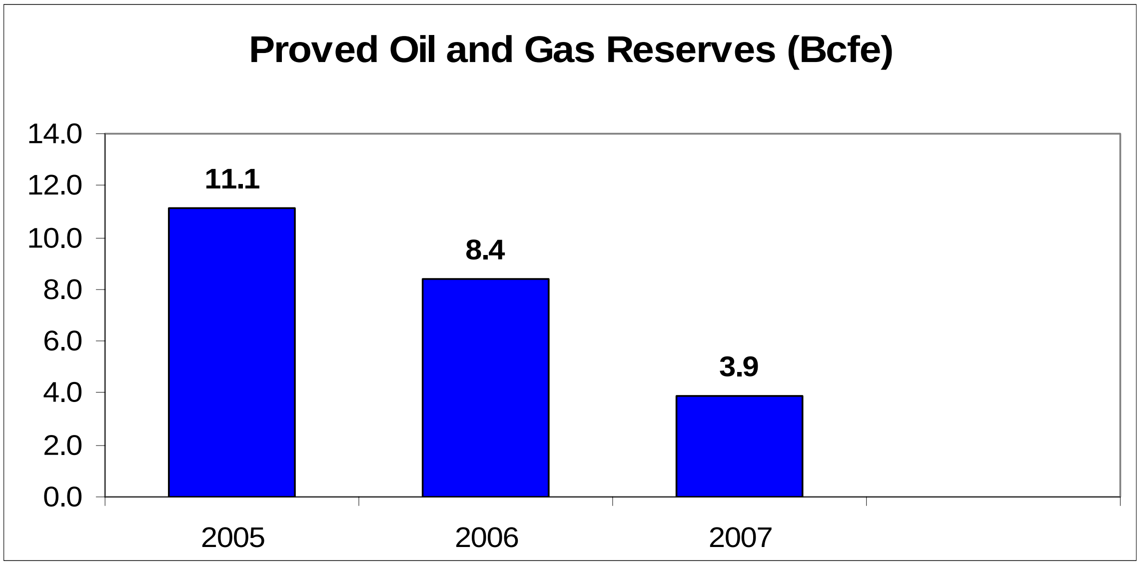
As of December 31, 2007 ROYL had 23,866 Bbls proved oil reserves (143,196 Mcfe gas equivalent) and natural gas proved reserves of 3,771,967 Mcf making it a total gas equivalent of 3,915,163 Mcfe. The Company's oil and gas proved reserves as of December 31, 2007 was about 53.6% lower than its oil and gas proved reserves as of December 31, 2006. The main reason for this decline in proved reserves estimate was 4,048,438 Mcf downward revisions of previous gas estimates. Extension, discoveries, and improved recoveries added 784,392 Mcf to the Company's proved gas reserves in 2007 which was almost the same as the Company's net production of 875,723 Mcfe for that year.

The gas equivalent of oil is calculated by converting one barrel of oil to six thousand cubic feet of gas, that is:

1 Bbl of oil = 6 Mcf of natural gas

The following table and chart show historical trend of ROYL's total proved reserves of oil and gas as of its fiscal years ending December 31, 2005 through 2007. The abbreviation Bcfe stands for billion cubic feet gas equivalent.

Proved reserves	2007	2006	2005
Oil (Bbl)	23,866	37,000	91,000
Gas (Mcf)	3,771,967	8,160,000	10,564,000
Total (Mcfe)	3,915,163	8,382,000	11,110,000



Proved reserves are classified into proved developed and proved undeveloped reserves. Proved developed reserves (PD) are reserves that are expected to be recovered through existing wells with existing equipment and operating methods. Proved undeveloped reserves (PUD) are reserves that are expected to be recovered from new wells on undrilled acreage, or from existing wells where a relatively major expenditure is required for recompletion.

Proved developed reserves could be producing or nonproducing. Proved developed producing (PDP) reserves are reserves that are expected to be recovered from the currently producing acreage under existing production methods. Proved developed nonproducing (PDNP) reserves consist of (i) proved reserves from wells which have been completed and tested but are not producing due to lack of market or minor completion problems which are expected to be corrected and (ii) proved reserves currently behind the pipe in existing wells and which are expected to be productive due to both the well log characteristics and analogous production in the immediate vicinity of the wells.

As of December 31, 2007 over 90% of ROYL's proved reserves were proved developed reserves. The following table shows the structure of ROYL's proved reserves based on the above categories.

Reserve category	Oil (Bbl)	Gas (Mcf)	Total (Mcfe)	% of total
Proved developed reserves	23,866	3,413,578	3,556,774	90.8%
Proved undeveloped reserves	0	358,389	358,389	9.2%
Total	**23,866**	**3,771,967**	**3,915,163**	**100.0%**

It should be noted that reserve estimates, including proved reserve estimates, are not precise because the estimates are based upon certain factors considered and assumptions made and may change as the underlying factors and assumptions change.

Oil and Gas companies are not permitted to discuss their non-proved (probable and possible) reserves in their SEC filings. But, they can provide that information to the public in the press releases or their corporate presentations. However, we did not see any information on ROYL's non-proved reserves being provided to the public at the time of preparing this report.

Below are definitions of proved, probable, and possible reserves as per The Society of Petroleum Engineers (SPE):

Proved Reserves

> "Proved reserves are those quantities which, by analysis of geological and engineering data, can be estimated with reasonable certainty to be commercially recoverable, from a given date forward, from known reservoirs and under current economic conditions, operating methods, and government regulations. Proved

reserves can be categorized as developed or undeveloped. If probabilistic methods are used, there should be at least a 90% probability that the quantities actually recovered will equal or exceed the estimate".

Proved reserves are also referred to as **1P** reserves in the industry.

Probable Reserves:

"Probable reserves are those unproved reserves which analysis of geological and engineering data suggests are more likely than not to be recoverable. In this context, when probabilistic methods are used, there should be at least a 50% probability that the quantities actually recovered will equal or exceed the sum of estimated proved plus probable reserves".

Proved plus probable reserves are referred to as **2P** reserves in the industry.

Possible Reserves:

"Possible reserves are those unproved reserves which analysis of geological and engineering data suggests are less likely to be recoverable than probable reserves. In this context, when probabilistic methods are used, there should be at least a 10% probability that the quantities actually recovered will equal or exceed the sum of estimated proved plus probable plus possible reserves".

Proved plus probable plus possible reserves are referred to as **3P** reserves in the industry.

Standardized Measure and PV-10 of Proved Reserves

Companies in the oil and gas exploration and production are required by the SEC to estimate the present value of their future net cash flows related to **proved reserves**, called **the standardized measure**, in accordance with SFA No. 69 prepared by the Financial Accounting Standard Board (FASB). As per SFA No. 69 the standardized measure should be calculated by applying current year end prices to estimated future production (considering fixed and determinable price changes only to the extent provided by contractual arrangements or law), less future expenditures (based on current costs) to be incurred in developing proved undeveloped and proved producing oil and gas reserves and less future income taxes and net abandonment costs. The resulting future net cash flows should then be discounted using a rate of 10% per annum to arrive at present net discounted cash flows, or the standardized measure. Because of keeping future prices and costs the same as current ones and the arbitrary discount rate of 10% it should be noted that **the standardized measure is merely a legal requirement and does not necessarily reflect a fair estimate of an oil and gas company's value**.

Some oil and gas E&P companies calculate a similar measure called **PV-10** in addition to the standardized measure. The PV-10 is calculated similar to the standardized measure except that it doe not include the estimated future income taxes and net abandonment costs that are unique for each company. The PV-10 is, therefore, a more realistic measure than the standardized measure for comparing the value of proved reserves of companies across the industry. Nevertheless, because of keeping future prices and costs the same as current ones and the arbitrary discount rate of 10%, PV-10 does not necessarily represent a fair estimate of an E&P company's value also.

As of December 31, 2007 the ROYL's standardized measure of proved reserves was $10,644,882. ROYL did not report PV-10 of proved reserves. However, in its December 31, 2007 SEC 10K, the Company reported that "According to the reserve report furnished to Royale Energy by Netherland, Sewell & Associates, Inc., Royale Energy's independent petroleum engineers, the net reserve value of its proved developed and undeveloped reserves was approximately $19.9 million at December 31, 2007, based on natural gas prices ranging from $3.83 per Mcf to $7.77 per Mcf".

PRODUCTION

Historically Royale Energy Inc. has been primarily a gas producing company. During the year 2007, ROYL's net gas production was 791,195 Mcf (26% less than 2006) and its net production of crude oil was 14,088 Bbl (34% less than 2006). Total net production on the gas equivalent basis* for the year 2007 was 875,723 Mcfe which was 27% below total net production of 2006. "Net" production is production that Royale Energy Inc. owns either directly or indirectly through partnership or joint venture interests after deducting royalty, limited partner, or other similar interests.

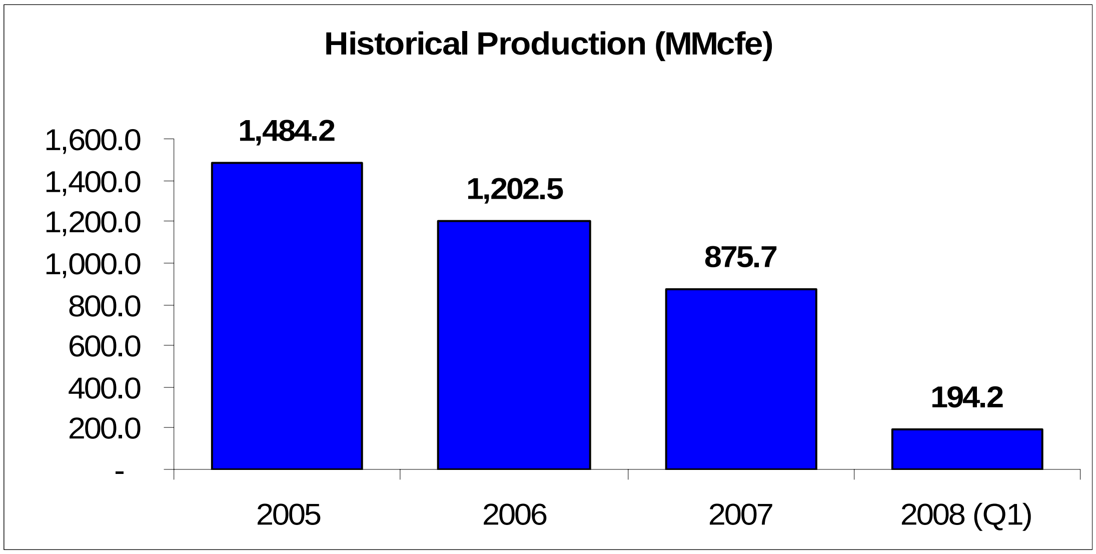
The following table shows ROYL's annual production volumes, weighted average realized prices, and unit costs for the years ended December 31, 2005 through 2007 and for the first quarter of 2008.

The table contains production and DD&A costs per Mcfe of production. Comparison of production and DD&A costs with the weighted average realized prices provides useful information about the trend in margin of profitability in production of oil and gas.

	Net Production			
Production	**2008 (Q1)**	**2007**	**2006**	**2005**
Gas (Mcf)	175,822	791,195	1,074,573	1,384,860
Oil (Bbls)	3,069	14,088	21,325	16,558
Total production (Mcfe)*	194,236	875,723	1,202,523	1,484,208
Average realized prices				
Gas($/Mcf)	$ 8.22	$ 6.56	$ 6.21	$ 7.48
Oil ($/Bbl)	$ 88.44	$ 65.02	$ 60.34	$ 51.95
Weighted average oil and gas ($/Mcfe)	$ 8.84	$ 6.97	$ 6.62	$ 7.56
Oil and gas costs ($/Mcfe produced)				
Production cost**	$ 3.52	$ 2.42	$ 1.64	$ 1.85
DD&A***	$ 4.18	$ 3.89	$ 4.61	$ 2.60

* Our calculation of Mcfe differs from the Company's calculation in that we apply the ratio of 6:1 to convert each Bbl of oil to Mcfe of natural gas, whereas the Company uses a 10:1 ratio of the price per barrel of oil to price per Mcf of natural gas.
** Lease operating costs per Mcfe.
*** Does not include DD&A of Turnkey Drilling Services

The following chart shows ROYL's total net production on the gas equivalent basis for the years ended December 31, 2005 through 2007 and for the first quarter of 2008 (MMcfe stands for million cubic feet gas equivalents).



DEVELOPMENTAL CAPITAL EXPENDITURES

In order to continue generating revenues, oil and gas E&P companies should continually engage in exploration activities to enhance their proved reserves as well as incur capital expenditures to develop and produce their existing prove reserves. During the past three years ended December 31, 2007, 2006, and 2005, Royale Energy Inc. spent $2,093,810, $2,492,985, and $2,428,069, respectively, to drill and develop reserves that were classified as proved undeveloped reserves.

The following table summarizes the Company's planned capital expenditures to develop its existing proved reserves in the futures.

Development cost related to:	**2008**	**2009**	**2010**
Proved developed reserved	$ -	$ -	$ -
Proved non-producing reserves	172,400	12,100	-
Proved undeveloped reserves	649,300	225,000	-
Total	821,700	237,100	17,300

COMPETITIVE LANDSCAPE

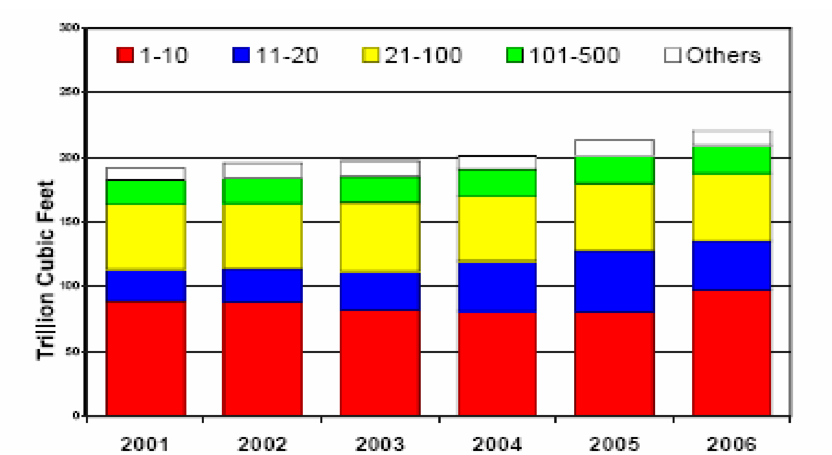
The U.S. upstream oil and gas industry segment (the E&P) is highly concentrated and has an oligopoly structure. The industry segment consists of a few large corporations, the Majors, which control reserves and productions, and numerous small independent companies entering into the industry as a result of the lucrative energy market in recent years.

The U.S. Energy Information Administration (EIA) ranks the reporting companies according to total production size and then places the companies into 5 size classes; Class 1-10, containing the top 10 largest producing companies, Class 11-20, containing the second largest 10 producing companies, Class 21-100 containing next 80 largest companies, Class 101- 500 containing the next 400 largest companies, and Class Others which contains 14,658 small companies.

According to the EIA survey,

> In 2006, the top 20 operators (Class 1-10 and Class 11-20) producing companies had 61 percent of the proved reserves of natural gas. The next two size classes contain 80 and 400 companies and account for 24 and 10 percent of the U.S. natural gas proved reserves, respectively. The top 20 operators had an increase of 19 percent in their natural gas proved reserves from 2001 to 2006. The rest of the operators in (Class 21-100, Class 101-500, and Class Other) had an increase of 7 percent in their reserves in the same time period. In 2006, the top 20 operators' natural gas reserves had an increase of 6 percent from 2005. (EIA 2005 Annual Report)

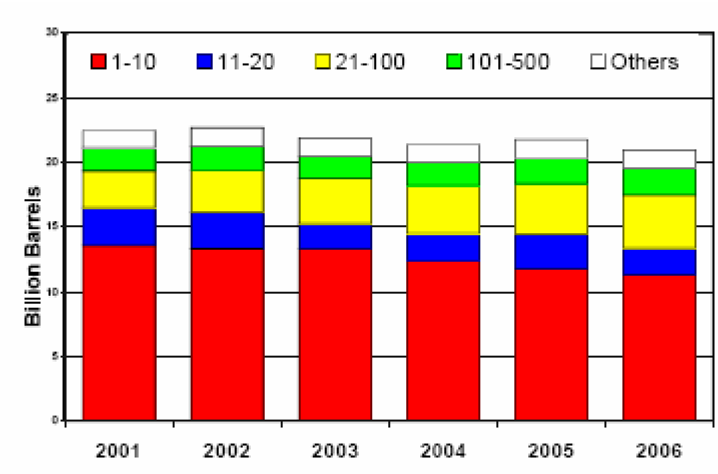
The following chart shows distribution of U.S. proved reserves of natural gas according to the company size for the period 2001-2006:



Source: EIA 2006 Annual Report

The EIA also reports that in the year 2006 the same top 10 producing companies had 54% of the US proved reserves of crude oil. The 20 largest oil and gas producing companies in 2006 had 64% of proved reserves of crude oil.

The following chart shows distribution of U.S. proved reserves of crude oil according to the company size for the period 2001-2006:

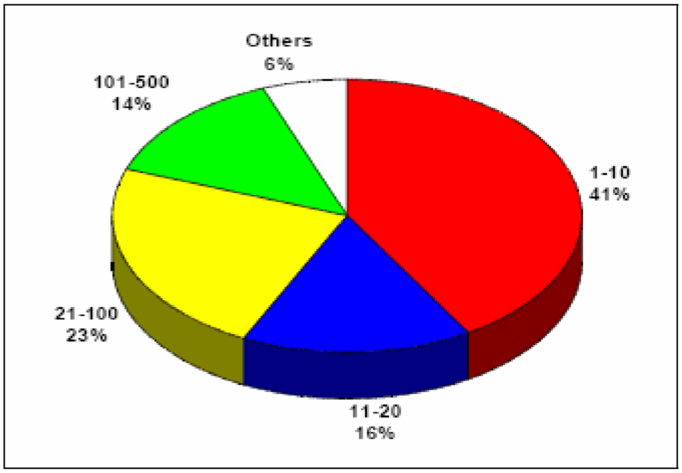


Source: EIA 2006 Annual Report

Similar size distributional numbers hold for production of crude oil and natural gas.

According to the EIA, in the year 2006 the top 20 largest U.S. companies accounted for 57%of wet U.S. natural gas production. The next two size classes had 23% and 14% of wet natural gas production, respectively. Smaller companies (the others) accounted for only 6% of U.S. wet natural gas production in 2006

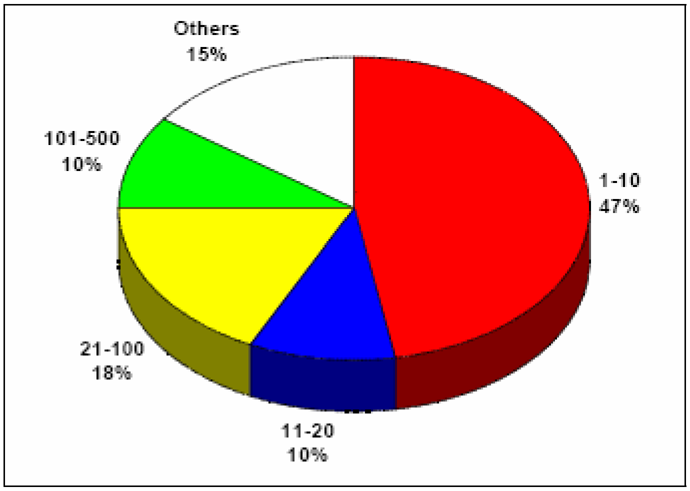
The chart below shows distribution of US natural gas production according to the company size for the year 2006:



Source: EIA 2006 Annual Report

Similarly, the 20 largest oil and gas producing companies had 60% of U.S. production of crude oil in 2006.

The chart below shows distribution of U.S. crude oil production according to the company size for the year 2006:



Source: EIA 2006 Annual Report

Given the commodity nature of oil and natural gas and the fact that prices are uniquely determined by the market, internationally for crude oil, and regionally and nationally for natural gas, it is not possible for independent oil and gas companies to establish competitive advantage through product differentiation and price advantage. Competitive advantage through cost reduction is also not viable for these companies because they are small and it is the major oil companies that enjoy the economies of scale.

The key to competitive advantage in the independent upstream oil and gas industry segment is, therefore, to discover or acquire new opportunities with high potentials, secure them, and act upon them in a timely manner.

OPERAING HIGHLIGHTS

ROYL's Statement of Operation Highlights

	For the Quarter Ended March 31		For the Year Ended December 31		
Revenues	**2008**	**2007**	**2007**	**2006**	**2005**
Oil and gas sales	$1,716,392	$1,685,981	$ 6,110,092	$ 7,965,633	$ 11,228,537
Turnkey drilling	1,096,196	581,349	9,408,103	15,711,550	13,066,800
Supervisory fees and others	177,669	251,507	1,039,204	1,218,860	1,348,041
Total Revenues	**$ 2,990,257**	**$ 2,518,837**	**$ 16,557,399**	**$ 24,896,043**	**$ 25,643,378**
Operating expenses					
Lease operating (Production)	684,062	791,512	2,116,977	1,968,269	2,751,441
Depreciation, depletion, and amortization (DD&A)	854,844	928,453	3,585,682	5,833,904	4,062,587
General and administrative	991,204	1,174,300	4,712,624	5,129,074	4,877,168
Turnkey drilling development	994,686	604,480	4,977,811	9,628,394	8,111,248
Lease impairment	-	-	2,106,670	6,191,417	742,642
Geological and geophysical expenses	-	-	423,459	400,306	381,790
Other operating expenses[1]	759,144	364,108	2,383,924	2,196,663	2,459,058
Total costs and expenses	**4,283,940**	**3,862,853**	**20,307,147**	**31,348,027**	**23,385,934**
Gain (loss) on sale of assets	**(27,823)**	**-**	(135,396)	3,263,368	**-**
income (loss) from operations	**$ (1,321,506)**	**$ (1,344,016)**	**$ (3,885,144)**	**$ (3,188,616)**	**$ 2,257,444**
Interest expense	83,423	36,530	152,547	523,139	444,271
Income tax expense (benefit)	(477,469)	(468,536)	(1,258,484)	(1,062,054)	627,270
Net income	**$ (927,460)**	**$ (912,010)**	**$ (2,779,207)**	**$ (2,649,701)**	**$ 1,185,903**
Net income per share: Basic	**$ (0.12)**	**$ (0.12)**	**$ (0.35)**	**$ (0.33)**	**$ 0.15**
Weighted average shares outsanding, Basic	7,918,659	7,916,408	7,917,543	7,932,198	7,860,341

1- Includes Legal and accounting and marketing expenses.

Royale Energy Inc. derives its revenues from three sources: sale of produced oil and gas, supervisory fees, and turnkey drilling contracts. In turnkey drilling contracts the Company sells fractional interests in undeveloped wells, recognizes gross revenue for the amount paid by the purchaser and agrees to pay the expense of drilling and development of the wells for the participants. Part of the capital received from the sale of turnkey contract relates to pre-drilling costs which are non-refundable and recognized as revenue upon signing of the contract. The remaining amount is held by the Company as deferred revenue until drilling is completed. Drilling is usually completed within 10-30 days. The Company generally operates the wells it completes and receives fees set by industry standards from the owners of fractional interests in the wells and from expense reimbursements.

With regard to capital expenditure on oil and gas properties, ROYL has adopted the Successful Efforts (SE) method of accounting, in contrast to Full Cost (FC) method for its oil and gas properties. In the FC method all costs associated with acquisition, exploration, and development of oil and gas reserves, including directly related overhead costs are capitalized and subsequently amortized on the unit-of-production method using estimates of proved reserves. The SE method, on the other hand, allows only costs incurred in successful exploration activities to be capitalized and subsequently amortized according to the unit of production method. Therefore, companies adopting the SE method may write off part of their capitalized costs under lease impairment or exploration cost (geological and geophysical costs) if the company hits a dry hole or if certain properties or prospects become no longer commercially viable.

In 2007, total revenues were $16.6 million, a decline of about 33% as compared to total revenues of $24.9 million in 2006. The main reason for this decline was decrease in the turnkey drilling revenue form $15.7 million in 2006 to $9.4 million in 2007 coupled with decline in oil and gas sales due to lower production in 2007. In 2007 ROYL's share of revenues from oil and gas sales and turnkey drillings were 36.9% and 56.8%, respectively. Similar numbers for 2006 were 31.9% oil and gas sales and 63.1% turnkey drilling revenues.

Total operating expenses in 2007 were $20.3 million, a decline of about 35% over 2006 operating expense of $31.3 million. Major items in ROYL's operating expenses are oil and gas production (also called lease operating expenses), depreciation depletion and amortization (DD&A), general and administrative expenses, lease impairment, and turnkey drilling development expenses. Main reason for the decline in 2007 operating expenses was decline in oil and gas production volume as well as fewer number of wells under turnkey drilling in 2007 as compared with 2006.

Operating loss for 2007 was $3.9 million as compared to operating loss of $3.2 million in 2006. Net loss for 2007 was $2.8 million versus net loss of $2.6 for 2006 leading to loss per share of 0.35 and 0.33 for 2007 and 2006, respectively.

In the first quarter of 2008 ended March 31, 2008 total revenues were $2.99 million, an increase of about 18.7% total revenue of $2.52 million in the first quarter of 2007. This increase was mostly due to increase in turnkey drilling revenue. In the first quarter of 2008 ROYL's share of revenues from oil and gas sales and turnkey drillings were 57.4% and 36.6%, respectively. Similar numbers for the first quarter of 2007 were 66.9% oil and gas sales and 23.1% turnkey drilling revenues.

The net sales volume of natural gas for the first quarter 2008 was 175,822 Mcf with an average price of $8.22 per Mcf, compared to 219,148 Mcf with an average price of $6.77 per Mcf for the first quarter of 2007. The net sales volume for oil and condensate (natural gas liquids) production was 3,069 barrels with an average price of $88.44 per barrel for the first quarter of 2008, compared to 3,886 barrels at an average price of $52.23 per barrel for the first quarter of 2007. The decrease in net sales volume of natural gas and oil and condensate were mainly due to the natural declines in production from existing wells.

Total operating expenses in the first quarter 2008 were $4.3 million, an increase of about 10% over first quarter 2007 operating expenses of $3.9 million. Main reason for the increase in operating costs in first quarter 2008 as compared to first quarter 2007 was increase in turnkey development costs because the Company drilled and completed one well during first quarter 2008 and did not drill any new wells during the period in 2007.

Operating loss for first quarter 2008 was $1.32 million as compared to operating loss of $1.34 million in first quarter 2007. Net loss for first quarter 2008 was $927,460 versus net loss of $912,010 for first quarter 2007 leading to loss per share of 0.12 and 0.12 for the first quarters 2008 and 2007, respectively.

In its June 23, 2008 press release the Company reported that it expects to return to regular quarterly profitability in the second quarter ending June 30th, 2008 and continuing for the foreseeable future.

During the first and second quarters of 2008, the Company processed the permits on several wells in California, and expects to participate in the drilling of one well during the second quarter 2008 and approximately five wells during the third quarter 2008.

ROYL classifies its operations into two principal segments; Oil and Gas Producing and Exploration Activities, and Turnkey Drilling Services. The following table shows some key financials for the first quarter of 2008 and for year ended December 31, 2007 based on the above segments.

	For the Quarter Ended March 31, 2008			For the Year Ended December 31, 2007		
	Oil and Gas Producing and Exploration	Turnkey Drilling Services	Total	Oil and Gas Producing and Exploration	Turnkey Drilling Services	Total
Revenues from external customers	$ 1,716,392	$ 1,096,196	$ 2,812,588	$ 6,110,092	$ 9,408,103	$ 15,518,195
Supervisory fees	157,953	-	157,953	847,603	-	847,603
Interest revenue	9,858	9,858	19,716	95,800	95,801	191,601
Interest expense	41,712	41,711	83,423	76,274	76,273	152,547
Expenditures for segment assets	1,582,546	1,846,550	3,429,096	5,868,775	8,746,020	14,614,795
DD&A	812,102	42,742	854,844	3,406,398	179,284	3,585,682
Lease impairment	-	-	-	2,106,670	-	2,106,670
Gain (loss) on sale of assets	(27,823)	-	(27,823)	(67,698)	(67,698)	(135,396)
Income tax expense (benefit)	(238,735)	(238,734)	(477,469)	(629,242)	(629,242)	(1,258,484)
Net Income (Loss)	$ (341,245)	$ (586,215)	$ (927,460)	$ (3,843,078)	$1,063,871	$ (2,779,207)
Net margin	-18.2%	-53.5%	-31.2%	-55.2%	11.3%	-17.0%
Total assets	$ 31,676,948	-	$ 31,676,948	$ 32,571,374	-	$ 32,571,374

We think traditional performance metrics like net operating margin and net margin ratios are not useful indicators to assess an oil and gas E&P company or compare different E&P companies. This is because different oil and gas companies use different accounting methods to capitalize or expense their exploration and development costs. Instead we think a better metric to assess the performance of E&P companies is the EBITDAX, EBITDAX margin, and EBITDAX per share.

EBITDAX is computed in slightly different ways by different companies or different analyst. We compute the EBITDAX by adding back to **operating income**, which is the traditional definition of EBIT, the exploration expense, the DD&A expense, and the impairment of property and equipment. **Thus by computing EBITDAX metrics, we**

assess the companies' performance independent of financing policies, accounting policies, and non-operating results.

The following table contains some supplementary information about ROYL's operating performance including EBITDAX metrics.

Production	2008 (Q1)	2007	2006	2005
Gas (Mcf)	175,822	791,195	1,074,573	1,384,860
Oil (Bbls)	3,069	14,088	21,325	16,558
Total production (Mcfe)*	194,236	875,723	1,202,523	1,484,208
Average realized prices				
Gas($/Mcf)	$ 8.22	$ 6.56	$ 6.21	$ 7.48
Oil ($/Bbl)	$ 88.44	$ 65.02	$ 60.34	$ 51.95
Weighted average oil and gas ($/Mcfe)	$ 8.84	$ 6.97	$ 6.62	$ 7.56
Oil and gas costs ($/Mcfe produced)				
Production cost	$ 3.52	$ 2.42	$ 1.64	$ 1.85
DD&A	$ 4.18	$ 3.89	$ 4.61	$ 2.60
Operating metrics				
EBITDAX ($million)	$ 245,223	$ 2,366,063	$ 12,500,379	$ 7,444,463
EBITDAX/Mcfe production	$ 1.39	$ 2.99	$ 11.63	$ 5.38
EBITDAX per basic share	$ 0.03	$ 0.30	$ 1.58	$ 0.95
EBITDAX margin	8.2%	14.3%	50.3%	29.0%
Operating margin	-44.2%	-23.5%	-12.8%	8.8%
Net margin	-31.0%	-16.8%	-10.7%	4.6%

* Our calculation of Mcfe differs from the Company's calculation in that we apply the ratio of 6:1 to convert each Bbl of oil to Mcfe of natural gas, whereas the Company uses a 10:1 ratio of the price per barrel of oil to price per Mcf of natural gas.

As can be seen from above table, Royale Energy Inc. has historically had positive EBITDAX metrics, which signifies that the Company has been able to generate adequate liquidity to meet its operating and interest expenses. However, in oil and gas E&P companies, specially the ones that employ successful effort method of accounting, EBITDAX could be quite variable from period to period. This is because of the occasional lease impairment, which affects the DD&A number also, and reclassification of exploration cost from capitalized to expense due to dry hole. **The important thing for an E&P oil and gas entity is to have positive EBITDAX**

The following table explains our method of calculating EBITDAX for Royale Energy Inc.

	2008 (Q1)	2007	2006	2005
Operating income	$ (1,321,506)	$ (3,885,144)	$ (3,188,616)	$ 2,257,444
Lease Impairment	684,062	2,106,670	6,191,417	742,642
Geological and geophysical expenses	-	423,459	400,306	381,790
(Gain) Loss on sale of property and equipment	27,823	135,396	3,263,368	-
Depreciation, depletion, and amortization (DD&A)	854,844	3,585,682	5,833,904	4,062,587
EBITDAX	**$ 245,223**	**$ 2,366,063**	**$ 12,500,379**	**$ 7,444,463**

CAPITAL RESOURCES AND LIQUIDITY

Over the past few years Royale Energy Inc. has been able to fund its operations and most of its capital expenditure needs through cash provided by operating activities. The Company has a $15 million revolving line of credit under a loan agreement with Guaranty Bank, FSB, secured by all of its oil and gas properties. As of March 31, 2008, the Company had an outstanding indebtedness of about $4.8 million on this loan. Total long-term debt as of March 31, 2008 was $5.5 million; making a leverage ratio of 17.4% which is quite on the low side in the oil and gas E&P industry segment.

The following table provides information on ROYL's capital resources and liquidity

All Amounts in $	**2008 (Q1)**	**2007**	**2006**	**2005**
Cash and cash equivalents	2,713,561	3,848,968	7,377,604	4,716,772
Net working capital	(6,482,964)	(4,846,444)	772,379	(2,141,034)
Cash flow from operating activities	746,608	4,427,012	3,406,393	6,395,442
Long-term debt	5,525,045	5,175,974	3,810,000	6,630,598
EBITDAX	245,223	2,366,063	12,500,379	7,444,463
EBITDAX/Interest expense	2.9 X	15.5 X	23.9 X	16.8 X
Long-term debt/Total assets (%)	17.4%	15.9%	11.3%	15.4%

On June 10, 2008, the Company closed a private placement agreement with an institutional investor. Pursuant to the private placement agreement, ROYL issued and sold an aggregate of 547,945 shares of its common stock to the institutional investor at the price of $7.30 per share, for the gross proceeds of about $4 million. The private placement also included a warrant, which expires on June 10, 2013, exercisable for an aggregate of 191,781 Warrant Shares at an exercise price of $7.30 per Warrant Share.

STOCK PRICE BEHAVIOR

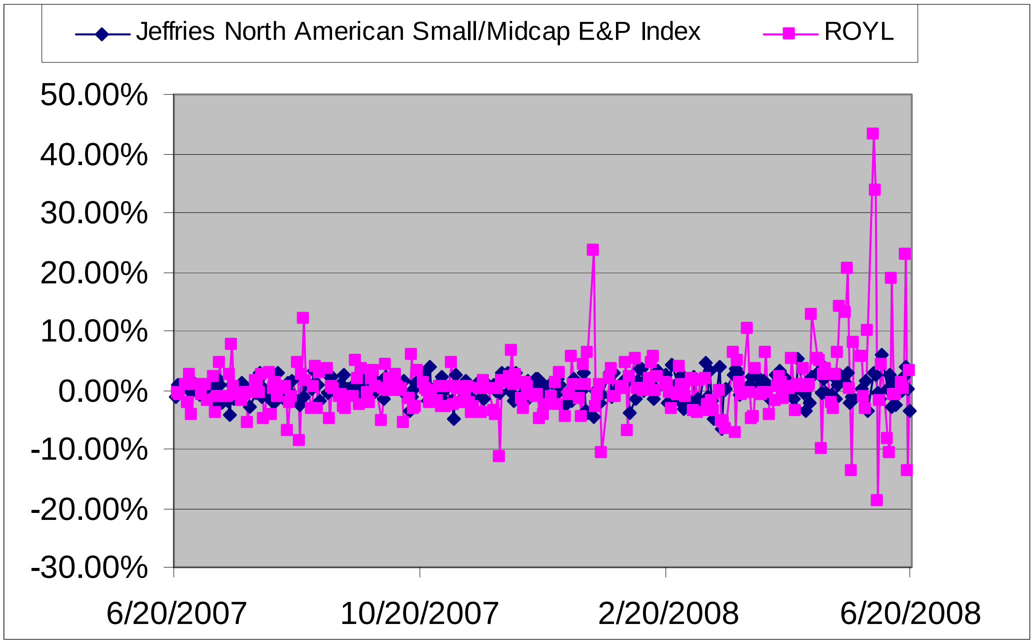
The 52 -Week price and volume behavior of CWEI from June 20, 2007 to June 20, 2008 is exhibited below:

Source: MSN.com

During the one-year period, ROYL was trading in the $2.18 to $11.59 range. The average daily volume for the one year period was about 180,000 shares. For the most recent 90 days the stock was trading in the $2.51 to $11.59 range with an average daily volume of around 477,000 shares. With 7.9 million common shares of ROYL outstanding as of March 31, 2008 the one-year average daily volume represents about 2.3% of the company's outstanding shares and the 90-day average daily volume represents 6.1% of the Company's outstanding shares. Trading volume has substantially increased since June 3, 2008.

We think a suitable benchmark to assess price return behavior of ROYL is the Jefferies North American Small/Midcap E&P Index℠. Unlike the S&P E&P index that incorporates all capitalizations including integrated oil and gas companies, the Jefferies North American Small and Midcap E&P Index contains only small and midcap exploration and production oil and gas companies and ,therefore, it is a more suitable benchmark to evaluate return behavior of ROYL.

The figure below shows daily price return volatility of ROYL versus Jefferies North American Small and Midcap E&P Index during the one year period:



Analysis of daily prices of ROYL from June 20, 2007 to June 20, 2008 indicates a daily price return volatility of 5.98% with average daily price rate of return of 0.52%. For the same period of time, the return-risk profile for the Jefferies North American Small and Midcap E&P Index shows an average daily price volatility of 2.00%.with an average daily rate of return of 0.23%.

The following table summarizes price return of ROYL versus the Jefferies North American Small and Midcap E&P Index for the period June 20, 2007 to June 20, 2008.

	Jeffries North American Small/Midcap E&P Index	ROYL
Total one year price return	69.10%	129.50%
Average daily price return	0.23%	0.52%
Daily price return volatility	2.00%	5.98%
Daily price return /volatility	0.114	0.087

As the above risk-return profile indicates, in the past twelve months, common shares of ROYL have outperformed the Jefferies North American Small/Midcap E & P Index by about two times, both on an annual and on a daily basis. However, the daily price volatility of ROYL has also been almost three times higher than the daily price volatility of the Jefferies North American Small/Midcap E & P Index.

RISK FACTORS

In its 10K SEC filings Royale Energy Inc. has provided detailed descriptions of its business risks. Below we pin point some of the major risks investors should be aware of when investing in common shares of ROYL.

The Company's future profitability is highly sensitive to oil and natural gas prices, which are solely determined by the market. Oil and gas prices are historically very volatile and highly correlated with economic cycles. Possible slow down in domestic and global economic activity could lead to decline in oil and natural gas prices which not only will lower the profitability margin but could also make portions of the Company's gas reserves commercially not recoverable.

Even with the current stage of 3-D seismic and other advanced technologies, exploratory drilling is still a highly speculative activity. There is always the possibility of hitting a dry hole which leads to substantial loss of capital.

E&P activity is a very capital intensive business and the Company might need additional external funding to acquire new properties or develop its undeveloped properties and expand future operations. There is no assurance that the Company would be able to raise additional capital if needed in the future

The oil and gas E&P industry segment is highly competitive industry with integrated oil companies dominating reserves and production. Long-term growth of the Company depends on acquiring new properties and adding to its reserves, which given the highly competitive nature of the E&P industry segment may not be viable.

Reserve estimates may be subject to downward or upward revision based upon actual production performance, results of future development and exploration, and prevailing oil and gas prices. Therefore, projections made on the basis of current reserves estimates may have to be modified if there would be revisions in the reserves estimates.

Oil and gas companies are subject to various governmental and environmental regulations which in the future might impose substantial costs on these companies. Particularly, there is the risk of possible future regulations in favor of alternative energy which might pose serious competition on the oil and gas industry.

Finally, future success and growth of the Company depends, among other things, on the availability of qualified personnel, which is becoming more difficult with the current pace of activities in the oil and gas E&P industry segment. Moreover, ROYL business is highly dependent on its president Donald Hosmer and on its executive vice president and chief financial officer, Stephen Hosmer, who have solid background and experience in the oil and gas industry and the Company does not have employment agreements with either Donald or Stephen Hosmer. The Homer family also has controlling position in the stock of Royale Energy Inc. As of December 31, 2007 the Hosmer family collectively owned 35.48% of the common shares of ROYL.

ANALYST CERTIFICATION

We, **Mohammad Sharifzadeh, PhD, CFA and Simin Hojat, M.Phil** are, the Research Analyst responsible for the preparation of this Research Report hereby certify that:

(1) the views and opinions expressed in this Research Report are based on PUBLICLY AVAILABLE information and accurately reflect the Research Analysts' personal views concerning any and all securities and issuers that are discussed herein and are the subject matter of this Research Report.

(2) the compensation payable to the Research Analysts, is not, has not, and will not, directly or indirectly, be related to the specific views and opinions expressed by the Research Analysts in this Research Report.

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Mohammad Sharifzadeh, PhD, CFA, is a member of CFA Institute, Los Angeles CFA, and GARP.

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Rating and Price Target Methodology

In arriving at an investment rating and price target, we use the following analytical measures:

1) Potentials and opportunities: Competitive advantage, market potentials, patents, properties, reserves.

2) Risk factors: Regulatory approvals, R&D results, ability to raise capital, going concern issues, competition, industry prospects.

3) Evaluation of the stocks fair value given the company’s potentials and risks through various valuation metrics.

RESEARCH RATING SYSTEM

STRONG BUY	**(5)**
BUY	**(4)**
SPECULATIVE BUY	**(3)**
HOLD	**(2)**
SELL	**(1)**
AVOID	**(1)**

DEFINITION OF OUR RATINGS

STRONG BUY (5): Company's stock price appears to be substantially undervalued relative to its future growth potential.

BUY (4): Shares appear to be undervalued in light of several factors.

***SPECULATIVE BUY (3):** Shares appear to offer potential gains though risk is considerably higher. Such a company may have "going concern" problems, or company's future prospects may hinge on critical assumptions, such as (but not limited to) the company's ability to compete effectively in the marketplace, achieve most or all of its stated business goals, maintain sufficient financial liquidity and resources for daily operations, for expansion, and for the avoidance of legal or other pitfalls.

HOLD (2): Shares appear to be fairly valued and while there is no incentive to add such shares, there are similarly no current known compelling factors that would warrant selling absent a subsequent trading drop in value.

SELL (1): At present, shares appear to be overvalued.

AVOID (1): At present, shares appear to be significantly overvalued

***What does "speculative" mean in a rating?**

Companies with meager or no historical data or that are at the development stage, are generally considered highly SPECULATIVE. Such companies may even have "going concern" problems and an analyst recommendation should be considered only as a part of a total investigative process by anyone considering purchase. A speculative buy opinion generally refers to future valuations only if the company is able to achieve most or all of its business goals and avoid most or all of the possible risks, including raising sufficient capital and effectively competing in its marketplace.