

Conference Call Transcription
First Quarter 2010 Results
May 18, 2010

Operator:

Ladies and gentlemen, thank you for standing by. And welcome to the Petrobras conference call to discuss the 1Q10 results. At this time, all lines are in a listen-only mode. Later, there will be a question and answer session and instructions will be given at that time. Should you require assistance during the call, please press *0. As a reminder, this conference is being recorded.

Today with us we have Mr. Almir Guilherme Barbassa, Petrobras CFO and Investor Relations Officer, and his staff. At this time, I would like to turn the conference over to Mr. Theodore Helms, Investor Relations Executive Manager of Petrobras, who has some additional comments. Please, go ahead, Mr. Theodore, the floor is yours, sir.

Theodore Helms:

Good afternoon, ladies and gentlemen. Welcome to our conference call to discuss 1Q10 results. We have a simultaneous webcast on the Internet that could be accessed at the site www.petrobras.com.br/ri/english.

Before proceeding, I would like to draw your attention to the slide two. We may make forward-looking statements that are identified by the use of the words “will”, “expect” and similar that are based on the beliefs and assumptions of Petrobras management on information currently available to the Company.

Finally, let me mention that this conference call will discuss Petrobras’ results prepared in accordance with the International Financial Reporting Standards, IFRS, and Brazilian Legislation. At this moment, we are unable to discuss any issues related to U.S. GAAP results.

The conference call will be conducted by our CFO, Mr. Almir Guilherme Barbassa. He will comment on the Company’s operating and financial highlights and the main events during this quarter, and he will be available to answer any questions you may have. Mr. Barbassa, you may begin.

Almir Guilherme Barbassa:

Good afternoon. Thank you for joining our conference call to discuss 1Q results. As compared to the prior quarter, net income and EBITDA increased 4% and 5% respectively. These results reflect the combination of greater sales volume, higher realization prices for our exports and core products sold in Brazil, and stable operating cost.

Investment spending grew as we continue to expand on our integrated basis. We began the Extended Well Test in Tiro and Sidon, discoveries made only in 2008, and we continue to find more oil balls in frontier areas and new horizon and develop fields. Our Board has approved the branch of capital expanding during the next five years, of between US$200 billion and US$220 billion and has authorized us to continue these plans to increase our capitalization. I will discuss the capitalization later during the call.



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Next, in the 1Q total oil and gas production was 2,547,000 BOE per day, up 3% over year over year and down 1% sequentially. Our total production in the 1Q was reduced by shutting off 78,000 BOE daily of gas capacity, due to limited domestic demand. In April, we set a monthly production record for Brazilian oil of 2,033,000 barrels per day and a single day record of 2,084,000 barrels per day.

The next slide is a review of units to be installed in 2010; you may add them to 375,000 barrels per day of new oil production capacity and 33.2 million m^3 per day of new capacity as well. Tiro and Sidon are promising light oil discoveries in a post-salt semi-stone reservoir, located in the shallow waters of Santos Basin. We are beginning a test of this reservoir less than two years following the discovery. Our ability to produce so quickly from our new reservoir is an example of the flexibility of our operations and the broadness of our resource base.

I would also like to highlight that we will install Brazil's two major non-associated gas systems this year in Mexilhão and Uruguá-Tambaú. Together they have a combined capacity of 55,000 barrels of oil equivalent per day. This year we are also completing our natural gas infrastructure, which will be capable of delivering offshore gas production anywhere the Brazilian markets demands; all that will be missing now is gas demand, currently restricted by both average rainfall, which has limited the need for thermal electric power. Overtime, as the Brazilian economy grows, we fully expect non-associated gas to play an important role in Brazil's energy matrix.

Next slide please. In the pre-salt we continue with activities we had previously announced. Results continue to meet or exceed our expectations. We are now drilling five appraisal wells in Santos pre-salt. We will begin an extended well test in Tupi Northeast, using FPSO Cidade de São Vicente, which is being relocated from Tupi. The pilot production system for Tupi will begin production in the 4Q of this year. We have recently signed a letter of intent to charter a unit for Guará; the first charter units will be built principally in Brazil. The AMP has made promising announcements about the Franco well, drilled by us outside our own concession, and we recently (7:53) in on a second stratographic well to increase knowledge of this area.

Let me turn now to volumes and prices, which are the key determinants of our results. As one can see from the graph on the left, the average price of Brent was virtually flat quarter to quarter, while they continue the narrowing of light-heavy differential increased the value of our oil by US$3 per barrel. Year over year the price of our oil has increased from US$32 to US$73 per barrel. The increase in value placed on our head oil is reflected in higher exports revenues.

From the graph on the right one can see that average realization price for products sold in Brazil increased slightly due to those products that adjust biweekly to international prices. You can also see that the difference between our average realization price and the international price continues to converge although we still benefit from higher margin.

The fact that our realization price in Reais was higher during the 1Q09 than is today, while the price in USD of our own crude oil has more than doubled has led to important shifts in the earnings of our upstream and downstream segment. For the Company as a whole our pricing policy has stabilized our cash flow and highlights the importance of our integrated model.



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Next, lifting costs remained stable despite the price of our oil increasing by US$41 per barrel in the past year, lifting cost increased by less than US$2. Even this small increase is largely explained by the strengthening of the Real against the USD.

Next please. Brazilian GDP growth bottomed during the 1Q09 and has rebounded sharply since then. Diesel has increased to due to GDP growth and an exceptional harvest this year. Gasoline consumption is at 25% because of higher price of sugar reduced ethanol supply. Thereby increasing ethanol price and reducing demand from flex fuel cars. The reduction of anhydrous ethanol from 25% to 20% in regular gasoline also contributed to higher gasoline sales. Natural gas consumption by the industrial sector has recovered in line with GDP, but demand from the thermoelectric sector continues to be limited.

Net exports have increased year over year due largely to growth in oil production exceeding internal demand. This trend should continue over time. During 1Q10 planned refinery shutdown lead to higher export volumes and lower import volumes of crude oil. The decline in refinery output and the growing demand for diesel, gasoline, jet fuel, and LPG was met by increasing imports. Year over year, the Company had swung from a financial deficit to a surplus in trade balance due to higher net volumes, as well as the reduced differential between light and heavy crude oil, as well as lower crack spread between the products we export and the products we import.

Next please. Turning to financial results, net revenue increased due to higher sales volume in Brazil and slightly higher realization price. The 3% average devaluation of the Real against the USD and it reduced light-heavy differential contributed to higher exports revenues. The increase in cost of goods sold was largely the result of higher volume.

Operating expense declined by 9%, despite provisioning of a series of judicial claims of nearly R$1 billion. In the 4Q09, operating expenses were higher due to expensing of dry holes and impairment, primarily at the Pasadena refinery.

The combined results of these factors led to an increase in operating income of 20% from the previous quarter. Higher operating income was partially offset by higher financial expense. In the 1Q Real weakened 2% against USD, versus a strengthening of 2% during the 4Q09.

During the past year, the net liability position of assets and liability subject to exchange valuation has increased from R$12.7 billion positive to R$32.3 billion negative, due to an increase in debt that is denominated or linked to USD. Because of this increase in net liability subject to financial variation our financial expense in Reais has become more volatile, although our income in our USD financial statement will not reflect this volatility. Taxes increased as a result of higher operating income and less provision for interest on our own capital in the 1Q10. The increase in minority interest expense is a result of improving gains from consolidated subsidiary, namely in financial results. Net profit for the quarter was R$7.7 billion and an increase of 4% from the prior quarter.

Next, please. Higher international prices, primarily from the reduction in the light-heavy differential contributed positively to our Brazilian exploration and production segments earnings. Stable lifting costs and abscess of dry hole expenses and other impairment typically taken in the 1Q also contributed to the gain in operating income.



Next please. Operating income for our Brazilian downstream segment was reduced as realization price in Brazil moved closer to international levels. Higher sales volume and a small increase in average price did not fully offset increased costs due to higher international price for crude oil and products. Domestic cracking spreads, however still exceeds those of the Gulf Cost as they have done since November 2008. More program maintenance during the period led to reduced throughput also contribute to higher per units cost. Programmed maintenance reduced the utilization rate from 94% in the prior year to 90% in the 1Q of this year.

Our remaining business segments contributed positively to earnings, gas and power continues to increase earnings despite limited thermoelectric generation. Greater supply of natural gas and a more developed gas infrastructure permitted higher sales of contract energy, increasing natural gas consumption from industry also contributed to the improvement.

The International segments earning increased primarily because of higher pricing during the period. The international segment also benefited from absence of wipe-offs that are typically recognized in the 1Q.

Our distribution segment continued to generate reliable earnings and margins, generating R$566 million in operating income as they grew market share from 38.6% to 39.5%. Capital spending increased to R$17.8 billion during the 1Q10, and 23% increase from the same period a year earlier. Most of the increase was concentrated in refining. As capital expenditure for upgrade and for regulatory requirement accelerated, while construction of Abreu, Lima, and Comperj refineries have began. Spending was supported by our strong EBITDA of R$15.1 billion versus R$13.5 billion during the period a year earlier.

Our operating cash flow during the quarter was R$9.7 billion versus R$13.7 billion in the prior quarter and R$12.4 billion from the period a year ago. The sequentially lower operating cash flow occurred despite higher EBITDA, as higher cash generation was offset by an increase in networking capital as a result of increasing accounts receivable, inventory, credits to suppliers, and reduction in short-term tax liabilities. Despite the reduced operating cash flow and increased CAPEX, we have maintained our comfortable liquidity position with R$27 billion in cash and equivalent at the quarter end.

As a result of our increased capital spending, net debt/net book capital increased to 32%, while the net debt/EBITDA annualized was 1.35x. Both these ratios are comfortably with the financial target set by our Board of 25% to 35% net debt/net book cap and 2.5x EBITDA.

Now, let me discuss the capitalization, which I assume is what everybody has been waiting for. I would like to first note that we have made every effort to keep all our shareholders informed of our plans and our thinking, but since the form of capitalization does not depend entirely upon us, and certain elements depend upon information that is still not available, we have been limited in the guidance we can provide.

The next step would be for our Board to convoke an Extraordinary General Assembly of our voting shareholders. The convocation must occur at least 30 days prior to the Assembly. As customarily done in similar public offering related transactions in Brazil the convocation will request the authorization from our shareholders to grant the authority to our Board to increase our voting and non-voting stock up to a



certain limit and determine the final size in terms of capitalization, and to take all other necessary steps as required.

We do yet not know whether the capitalization will be with or without the transfer of rights. The valuation of corresponding barrels has not been agreed nor had we yet finalized our business plan for our 2010/2014. Therefore the amount of capital increase that the General Shareholder Meeting would authorize our Board of Directors to approve would be for a maximum that should accommodate all reasonable outcomes. If we are to meet our deadline for completing the capitalization during July, we would need to file in the first part of June the required documentation, as well as the first draft of the Brazilian prospectus with CVM and a prospect supplement with SEC.

As per CVM regulation, CVM would have a 20-business day period to review and make initial comments. On the final documentation and related Brazilian prospectus, the information submitted to the CVM and the SEC will be public, although, it is not expect to include final details of the transaction such as the evaluation of the barrels or other terms of the transfer of rights. Once the CVM has reviewed and agreed to the disclosure within the Brazilian prospectus, we would be able to begin marketing the transaction; aiming at completing the transaction by the end of July, marketing we would need to begin in the first half of July.

Just to review some key elements in the timetable and when we hope to have additional information we may share. First, as customarily done in similar public offering related transactions in Brazil, our Board would convoke the Extraordinary General Assembly of our voting shareholders. The Extraordinary General Assembly towards the end of June would grant powers to the Board of Directors to approve the capital increase, as it is the standard prerequisite for the preparation of Brazilian public offering.

The market will know at the same time as Petrobras whether or not the transfer of rights is approved by the Congress. A vote is scheduled for the next week, but we will have to wait and see what happens. The 2010/2014 business plan is expected to be approved and released by the Board of Directors in the first half of June.

Finally, if the capitalization is with the transfer of right, the value of the corresponding barrels the methodology applied to reach that valuation and the terms by which the transfer of rights may be revalued will also be disclosed before or simultaneously with the marketing of the public offering.

There are a number of other details not mentioned here, but are detailed in our prior release. What I had tried to focus on here is the general timetable and our best understanding of when information will become available.

Thank you. I would be happy to answer any questions that you may have.

Paul Cheng, Barclays Capital:

Thank you. Gentlemen, have you decided whether it is going to be a rights offering or a normal secondary offering? And also the timeline you are talking about May, the announcement of the Extraordinary Shareholder Meeting. When the Board is going to – I assume you already have a day



when you are going to actually announce it. I know you went through that. Can you give a little bit more definitive timeline in terms of which week that we expect that it is going to happen?

Almir Guilherme Barbassa:

The convocation of the General Assembly maybe addressed to the Board soon. We do not have yet a date, but as soon as they approve we will be releasing information about that. We hope before the end of the month we will have some news on that.

Paul Cheng:

And so, before the end of the month?

Almir Guilherme Barbassa:

And we have for the first question that you have done, we have announced already that we have decide to go for a public offering, no longer a rights offering as we have announced back in the begin of this process. So, the decision and the indication that our Board has given to us is to go ahead with a public offering.

Paul Cheng:

Almir, can I just ask a quick one in here, with the uncertainty on the transfer right and how much you have to pay order with the Presidential election coming up in October and it depends on who is going to be the winner there, even if the oil law being passed this year that they may get resubmitted at the Congress, I presume potentially next year. With all the uncertainties, is there any particular reason why it is so important that you get this equity offering done within such a short period of time?

Almir Guilherme Barbassa:

First of all, we have time enough to do this offering and to conclude it by July. We do not think we are short in time at this moment. By all the measure, all the timetable we are putting in place here and looking at, we have timed enough. What of course we are depending is the approval of the Congress, and this is a more difficult item to control. We have no control at all. We hope the bill that has been sent to the Congress is going to be voted before the end of the month.

As I said, there is an announcement that they are going to vote next week. We hope they will be concluding this process by then. If so, we have plenty of time. We can do it in these 90 days or just 75 days that we have up to the end of the July. And this is the best we can do because we have a large budget. We are executing this year R$88.5 billion. And as you have seen, our leverage has increased 1% in the course of the 1Q. And as we can project keeping this high level of investments and compare with our EBITDA operational cash flow, our ratios would be going towards some stress and we prefer having such big plan ahead of us, with such a large company and so successful in doing all the operations we are carrying on to keep the best way the financial of the Company. And this requires us to do this transaction by the end of July. This is the best, because after that there is the vacation of capital market and in September we will be with a very important election in Brazil, September that may last



during October, if there is a second round. So we will have at least three months that may not be there for this transaction. So, the best is to do it right now.

Paul Cheng:

OK. Thank you.

Neil McMahon, Sanford Bernstein:

Hi. Actually, not a question at all on the capitalization, but a question really on the strategy of the Company. It seems from your press releases, including the one today, that Petrobras obviously has got a massive CAPEX commitment within Brazil itself, not just drilling wells in their post-salt and pre-salt and also in the downstream. But also making investments quite a number in Portugal, and also this morning from in Saudi Arabia as well.

So, maybe if you could just tell us how this fits into the overall strategy of the Company, as it seems to be becoming a bit of a diverse strategy and not as focused as was originally the case.

Almir Guilherme Barbassa:

I understand we are keeping our previous strategy. The announcement of today, regarding Saudi Arabia is very deeply connected with our domestic operations, where we are producing today green coke and we are looking for opportunities to add value to it. And this is why we are developing and studying; it is not a final decision, but a decision to go ahead with studies.

And this is not going to require too much capital. It is a very small amount. Regarding Portugal biofuels, it is in line with what we have announced, that we are looking for increasing the production of biofuels in Brazil, either the sugar cane or the biodiesel. And it requires not much money as well. So, we are keeping our strategy. I understand we are not diversifying from what we had said.

Neil McMahon:

Maybe just a follow-up question on Portugal, it also looks like you are getting interested in evaluating Portugal from an exploration point of view, and so maybe you could go into that. Plus also is there any relationship developing with Galp? There were some market rumors a number of months ago about the potential of swapping your Eni's interest in Galp with yourself. I do not know if you have any comment on that? Thank you.

Almir Guilherme Barbassa:

So far regarding Galp, we had not established yet. There have been many rumors. We are always looking for opportunity. Galp is a company that is close to us, their main assets are here in Brazil. And we have the opportunity here to develop these biofuels but this is the only deal we have in place so far. And we are doing exploration offshore Portugal. We are in deep waters offshore Portugal associated with Galp as well.



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Neil McMahon:

Thank you.

Frank McGann, Bank of America:

Hello, good day. Just two very mundane questions actually. One is the gasoline sales were very strong in the 1Q; I am just wondering what your trends are so far in the 2Q and how you see that developing? And lifting costs, do you see any reason at the level that we saw in the 1Q for pure lifting costs would not be continued as you go through the year?

Almir Guilherme Barbassa:

The gasoline demand is going to reduce in the 2Q because at the end of April the mix between gasoline and anhydrous ethanol has changed to 25% again of ethanol, and the new crop of sugarcane is starting now. So, more ethanol shall be offered to the market and the demand for gasoline is expected to go back to the normal volumes that we used to sell.

And lifting costs, we are working in different ways to keep it as well controlled as we can. And as has been shown, we are for about two years or more than one year with about the same level of lifting cost. But we have here our colleague from E&P, Hugo Costa. Would you like to add something regarding the lifting cost, please?

Hugo Costa:

Well, I think that during this last year the lifting costs, we have been able to keep the same level based on both the reduction on material and services, the improvement in the scale of the operations and also helped with the exchange rate and the performance of the entire operation in the Campos Basin.

Frank McGann:

OK. Thank you very much.

Ricardo Cavanagh, Raymond James:

Yes. Well, good morning and thanks for the call. I have two questions that relate to association between investments and the equity capitalization. The first question, if the capitalization is done in the next few months I assume certain cash disbursements are likely to accelerate. Could this mean that in upstream there could be an acceleration of investments in development to augment production and in downstream, could it affect the pace of planned investments for the year?

And the second question, also on investments, under a scenario where capitalization might have to be postponed until 2011, would there be any flexibility to reconsider planned investments for the year, or rather Petrobras will allow to temporarily operate close to maximum leverage levels? Thank you.



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Almir Guilherme Barbassa:

Starting from the final question, I would say that we had already decided to go for the capitalization in this next quarter, July. And this is a decision not to postpone it to next year. We are aiming to keep the level of capitalization and the ratios of the Company in a sound basis. So, at this moment we do not consider the other alternative to do it in 2011.

The first question was regarding the adjustment of our CAPEX, so there is no possibility of adjustment of CAPEX this year because of no capitalization. We had a certain level of flexibility to adjust the CAPEX but we are not considering it. Of course, as further in time is our project more flexibility we have, if we consider the current year we have less to adjust, even though we are not taking this into our account because we are considering to do it in June, July.

Ricardo Cavanagh:

OK, and thank you for that. And then on the first one, assuming the capitalization goes through, can we see an acceleration of investments in upstream or downstream, or the Company is already investing at the pace you would like to be investing for the rest of the year? Meaning in other words would the capitalization provoke an acceleration?

Almir Guilherme Barbassa:

Yeah, on the same way, we are not considering to reduce our budget for the year, there is no possibility to accelerate as well. We have done our budget, it considers the best we can do for the Company at this point in time. And it is a challenge to do all these investments in a year. The 1Q was 17.7, 17.8, it means that 4x that is not 88.5, as we are aiming at. So, with time we normally grew the volume per quarter of CAPEX, but acceleration is almost impossible. We are doing it in a very high speed and high level, and doing the capitalization would not change this program. It is part of our program to do the capitalization and to realize what we have announced.

Ricardo Cavanagh:

OK. Well, thank you very much again.

Paula Kovarsky, Itaú Securities:

Hi, good morning, everyone. I have two questions. The first one on the capitalization process again, I would like to understand, Barbassa, what exactly is the approval that you guys will be seeking from the shareholders' meeting, meaning is there going to be a range kind of a minimum range, which will probably match the follow-on with no barrels and the maximum range that will match the inclusion or the acquisition of those barrels?

And also if the approval touches on the structure of the capital increased or if it is stated that there has to be a follow-on or if there is any route that can be used to go ahead with the capital increase in any other way, so that is question number one.



And the second question has to do a little bit with the valuation of the barrels and the adjustment mechanism be it once AMP gets it report from its consultancy firm or the one or two years scheduled review. Could you take us through a little bit at least on the thinking of how this reevaluation is going to happen in the case of AMP if the idea is to do with barrels, how does that affect the potential size of the capital increase? So, I would like to get a little bit more color on that as well.

Almir Guilherme Barbassa:

OK, Paula. What we are looking from our Board and from our General Assembly is to increase the authorized capital, "capital autorizado", of the Company. And we have to say how much we went and the total we are looking as a ceiling and the capital increase can be done inside that ceiling for any amount. For example, if there is no rights transferring, we can do only the capitalization that would be much less than both transactions together. This is what we are aiming now and this is what we need, just opening space to do whatever we are going to do. And doing one or two transactions depends first on the Congress and then, as the capitalization is a decision, we are going to do it. And this is what we are going to look for at the shareholders' assembly.

Paula Kovarsky:

Yeah, but the original idea, I guess, is that the Government subscription would somehow match the valuation of the barrels, meaning so that the Government would contribute with the bonds and then pay the barrels with those bonds. So is there a situation where you go for what we call the drive follow-on, the follow on with no barrels now, and in the future, once the bill is approved, you can use cash to buy the barrels? Or then you would call for a second capital increase and then the Government subscribes with the bonds; is that the idea?

Almir Guilherme Barbassa:

I am supposing that if the transfer of rights is not approved now, it is going to be rejected. So, what lasts in the table is the capitalization only. I do not count on a situation where the bill that is in the Congress will remain there forever with no voting. I believe the Congress is going to go vote it, either to approve or to reject.

Paula Kovarsky:

OK.

Almir Guilherme Barbassa:

And the second question is regarding the value of the barrel?

Paula Kovarsky:

Yeah, the revaluation.



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Almir Guilherme Barbassa:

And the revaluation. The revaluation that shall the happening one to two years after the transaction is going to be based on a formula that shall be in the contract, because the transfer of rights from the Union in Brazil, the National to Petrobras shall be regulated by a contract. And the contract, we are already discussing with the Government. We already have a first draft of this contract we started discussing it.

One item of this contract is the item that will bear the formula for reappraisal of the price of the barrel. And we hope we do not have yet this formula, a final formula, but we are aiming to have it in a way that there is no difficulty to apply whether one year or two years later. Just looking to some indexes or prices or whatever it is going to comprise for and apply it and adjust the numbers. How it is going to be set if we are going to pay back to Government or receive more from the Government, I do not know yet, how it is going to be established in the contract also.

Paula Kovarsky:

OK. But in the case of the AMP short-term revision, is there a structure or an agreed way to do it or?

Almir Guilherme Barbassa:

No. There is no way to agree. This is going to be the main discussion on where we are going to establish the price of the acquisition that shall be using the right transfer.

Paula Kovarsky:

OK. And presumably this information will be made available during the road show or whatever, right?

Almir Guilherme Barbassa:

Yes, if we have it done by then. If not, it is going to be at least by the road show. We hope to have the reports from the engineering company that is under contract with Petrobras, and we hope they are going to produce their report in due time. So, we hope to make these release to the shareholders informing them what is the price we are seeing. And considering the situation of his transaction, where there is no risk of reservoir, so we expect any other appraisal on that value would not differ much from the figure we are going to have. That is what we believe would give more information and give the shareholders the comfort of the transaction.

Paula Kovarsky:

OK. Thank you very much.

Arthur Byrnes, Deltec:

Sir, does the BP problem in the Gulf of Mexico affect in any way the risk of your harvesting the deep reserves that you have offshore Brazil?



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Almir Guilherme Barbassa:

I am going to ask Hugo to help me in this question. Please, Hugo.

Hugo Costa:

OK. Well, I think it is still early to evaluate the consequence and really to understand what happened, really happened in the Gulf of Mexico. But Petrobras applies the best knowledge, the best technology, and the best practices in all of our operations and we work with the best companies in the world, like TransOcean, Nobel, Diamond, drilling companies and the service companies. And based on this we are not considering any change in these procedures and we will keep following the API, the American Petroleum Institute standards and the best practices preconized by this institute. Today we think that we have to wait until we best understand of what happens there and to reconsider any of these procedures.

Arthur Byrnes:

Thank you very much.

Marc McCarthy, Wexford Capital:

Hi, guys. I had I guess a more general question; it is an easy one, Almir. In listening to your sort of sending the message that it is full steam ahead, but clearly the market in the world has changed and continues to change, it is amazing, the dynamics for a deal like this have weakened and continue to do so. If oil prices, Euro crisis, this new offshore thing with BP, and of course your sort of tabled with the elections in the fall. Petrobras has clearly shown that it has access to capital, all different forms, and those loans from the Chinese a few years back were a good proof of that. And I continue to believe that they are still around.

But pricing of this deal, of course, has to be always enough to motivate investors to participate, and as you pointed out you do not want to get into the summer months of August, you need as many folks to be participating and given the size of this to be motivated to participate.

So, it brings to me to the question of price, you are going to have tons of advisors helping you make this decision, but how much is price consideration here in terms of moving forward with the public offering? And then I sort of move back, if you are not satisfied with price, it seems to me that you still have an option on the table and that is to form down some of your positions with those same other folks that are always happy to give you money.

Has that been brought up as a consideration in this period, in order to raise those equity USD? I bring that up because all the investors that want to participate in this capital increase I imagine want to buy the E&P side of the story, they do not want to buy the downstream. It has always been the case. But they have to buy this package deal. So I guess the question is, might you consider, if the pricing erodes, if oil prices are US$60 tomorrow and the Euro is about to explode, and Greece is about to fail, and you still want to get this deal done, what is your backup plan? I know you have said you do not have a backup plan, but.



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Almir Guilherme Barbassa:

I guess you have answered. Yes, of course...

Marc McCarthy:

You do not need Government approval to fund down your anchorage, right?

Almir Guilherme Barbassa:

Right, yeah. As you have said at the beginning, going ahead in full steam but with very good radar as well. You have to deviate whenever you feel that your route is not the best one. And that is why we are trying to look ahead with time doing our best in our business plan and looking where we are aiming. At this moment, as part of the fuel we need for our boat, is to add some capital.

Marc McCarthy:

Right. And I guess what I am also trying to address here, Almir, is I do not think anybody wants to see is you, and you can easily do this, get another US$10 billion, US$15 billion loan or short-term loan from another export deal or even an asset back deal, because of the impact that would have to the ratios. You could do that same deal with those same parties for equity, I guess is my question.

I do not see much impact of the timing of this spending; it seems like that is pretty much set in stone.

Almir Guilherme Barbassa:

I did not exploit these alternatives. We have been successful in accessing many different sources of financing in terms of debt, and this is one of the characteristics of Petrobras. We have been successfully raised last year US$42 billion, which is an amazing amount. This year we added some extra debt as well. But we did not explore this alternative of, let us stay, strategic partner. We would like much better to go the broad market and to have a well-spread base of shareholders.

Marc McCarthy:

OK. Just as a technical thing because this is now viewed as a public offering as opposed to a capitalization there is no preferential right given to existing shareholders; is that right? So, there is no record date or issues as it would relate to a traditional rights offering.

Almir Guilherme Barbassa:

Yeah, but there is no rights offering as we were doing if we were to conduct the rights offering. But we are going to give a privilege, a priority to the current shareholders. They would the first ones to get the opportunity to make their proposals.



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Marc McCarthy:

And would the record date for those shareholders be determined on the date of the Extraordinary Shareholders Meeting?

Almir Guilherme Barbassa:

We do not know.

Theodore Helms:

Hello, Marc. I do not think that process and when and how you can do it has not been decided yet.

Marc McCarthy:

OK. Thanks, guys.

Paul Cheng, Barclays Capital:

Hey, guys. A number of quick questions. Almir, I think in the past the assumption is that the Government will serve as a back stopper for any amount that you want to raise in the event that the minority share that do not subscribe they go into Company and fully subscribe for that. Did we get any specific guarantee from the Government that, or understanding from the Government this is what they are going to do here?

Almir Guilherme Barbassa:

If we do only the capitalization with no transferring of rights, the Government is not going to be diluted. Their decision is to follow with their proportionate share.

Paul Cheng:

Right, but I am saying that in addition to not only diluted, if the demand because of all the uncertainties running with both the companies, as well as in the macro environment, in the event if the market condition is tougher and we do not have sufficient minority shareholders subscribe to, their corresponding share of their capital structure. Did the Government have any kind of expression that they would come in and fully backstop the transaction for you?

Almir Guilherme Barbassa:

Yeah, I do not have this information from the Government. If there is a right transferring, yes they have said already they would like to increase and they are there to buy the offering in a large proportion and they have shares. But regarding only the capitalization, if there is only one transaction in the capitalization, I do not have any information. The only thing that I can tell you is that they would not be diluted, they will fall at least on the ground of their proportion on the total of share.



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Paul Cheng:

Right. And, Almir, should we assume that in this public offering that the plan is to issue the same ratio of the common and the preferred share as the existing capital structure?

Almir Guilherme Barbassa:

Yes, we are going to maintain the current ratio between OM and PM in the offering.

Paul Cheng:

OK. Three final short questions; one, under the International Financial Reporting Standard, I presume now that everything is reported under the FIFO and you are not using the average cost structure in your downstream?

Almir Guilherme Barbassa:

Let me see with Alves if he can help me in this question, please Alves?

Alves:

No, the change in accounting principles do not include change in terms of evaluation of inventories, the supply will continue using average cost. There is no change in this issue.

Paul Cheng:

OK. And, Almir, when looking at your production target right now for 2010, say 2.1 million barrel per day in Brazil, based on the 1Q production and also that project coming on stream even assuming the project will be essentially up to the full production within the same quarter that they start. It seems it is still a pretty aggressive number. What kind of underlying fuel decline curve there are you assuming in here? And also if there is any major maintenance in the 1Q that have made 1Q production to be lower than otherwise it will be?

Almir Guilherme Barbassa:

Paul, Hugo is going to answer you.

Hugo Costa:

Hi Paul. There is always a lot of challenges something that is always on the operations, and the target has always some level of challenge related to the operations. But considering the numbers of production and the projects and what is scheduled to come on stream on the 2H of this year and Tupi pilot and some new projects that will come, we are keeping the target and working to achieve 2.1 million barrels a day as an average for the year.



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Theodore Helms:

We got to move on. Paul, let us move on, we got a lot of other people to ask questions.

Paul Cheng:

OK, that is great. Thank you.

Sergio Torres, JPMorgan:

Hello, everybody. I have two questions. One, if you could give us your current estimate, even if it is raw, about how much money do you think you will need just to cover any budget deficit to finance the existing business plan as we know it. And just for us to know how much you would need to raise either from the equity markets or from the debt markets combined?

And the second question would be if you could talk to us and give us more information about the Franco discovery whether – I think AMP has said that it is comparable to the Tupi find or to the original estimate of the Tupi find. But I do not know if you could elaborate on that, whether these 4.5 billion barrels that has been estimated, if it is a P-50 number? What is the range and whether there is an implicit recovery ratio associated to this number that is comparable in fact to the Tupi discovery? Thank you.

Almir Barbassa:

Regarding the additional money we need to fund our budget of this year, I do not have it now. But we are looking not to the year but we are looking for the five-year plan of how much we may need to have this five-year plan and properly execute it, maintaining our financial standards and financial sustainable ratios. But I do not have the answer for the current year. Hugo, please, regarding the Franco well.

Hugo Costa:

OK. This well Petrobras drilled for AMP, and AMP is disclosing the kind of information they consider adequate or they are considering necessary to move forward in their strategy of disclosure.

We cannot say anything else than what is known. It is a very good well and the results will be disclosed by agency. It is quite difficult to make any comparison, even between Tupi because we have a good knowledge in Tupi and we do not have the necessary knowledge related to this field.

Sergio Torres:

OK. I guess related to the Franco discovery, should we expect that at the time of the road show, if this deal is approved should we expect that at the time of the road show this information would be made available to shareholders?

And second, yes, Almir, I was referring to your estimate on the five-year business plan, whether you had an estimate of the size of the budget gap that you would need to fill. Thanks.



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Almir Barbassa:

No. I do not have it yet but I hope by mid-June we will have it with the business plan approved after the Board review and approval. Before that, any number I would give you would be a speculation, and I prefer not to give this figure to you.

Sergio Torres:

Thank you.

Jeffery Grossman, Hutton May:

Hello. Good afternoon and thank you for taking the question. Just going back to the public offer mechanism, can you just confirm that your TDR holders will get priority right as well in any offering?

Almir Barbassa:

Yes, they would. Of course the priority has to be exercised, they have to place the order at market price. If they can do this, yes they will be granted the right, the priority as well.

Jeffrey Grossman:

Through JPMorgan, the depository?

Almir Barbassa:

I do not know the answer, Ted.

Theodore Helms:

There is a depository, although I think that, the question of the priority is how – there is still lot of details to work out. I think leave at that. But just to answer your question JPMorgan is the depository.

Jeffrey Grossman:

Is there any difference between Brazilian right and U.S. ADR holder right?

Almir Guilherme Barbassa:

No, there is none. We can give the same right to everyone. It is a matter of local legislation. If they are they allowed to place an order, for example, subject to a price that shall be established by the book building later on, I know that in Brazil we can do that; I am not sure if there is a way to do this same kind of proposal or place an order in the United States. And in order that will be subject to a future price. If they can do this in one or another way, they will have the same priority.



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Jeffrey Grossman:

In the event that there are leftover shares, will existing holders get priority to take those up?

Almir Guilherme Barbassa:

There will be difference rounds. In the first round, the current shareholders would place the order and can tell if they will be prepared to take some shares that are not sold, the excess not sold. So, they can increase the participation. So, this is part of the first proposal, they are going to offer to the book building.

Jeffrey Grossman:

Just to clarify, if there is no transferable was it that the Government did not express its intentions yet? Is that what was said, in terms of dilution?

Almir Guilherme Barbassa:

No, the Government is going to participate at the same time as every other shareholder. So, I do not know how they are going to manage their shares, if they are going to increase or not, if they are going to candidate themselves to buy more shares, if there is no right transferring. This is a subject that will be dealt by the Government, I do not know.

Theodore Helms:

Can we have the next question, if you could?

Jeffrey Grossman:

Thank you.

Gustavo Gattass, BTG:

Guys, Jeffrey just asked my most important question. Let me just ask you one very quick question, Almir. In the basket of ratios that the agencies look at for investment grades, I just want to understand how important is a net debt/reserve ratio? Is that something that you guys think as relevant for the decision making process, or is that one that is not that relevant?

Almir Guilherme Barbassa:

Maybe the rate agents do not follow only one ratio. They have many different ones. And I believe that net debt/EBITDA is maybe more important than net debt/net cap.

Gustavo Gattass:

I was not even thinking about net cap; I was thinking about reserves, net debt/proven reserves?



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Almir Guilherme Barbassa:

Yes, they look at that too but that is a very good – we are not concerned on that. Petrobras is a very cheap company at this moment, regarding these index. And tends to keep these ratio because as you all know we have a very large potential of new reserves to be incorporated as proved reserves. And as I said, we are going to receive another seven rigs for ultra deep waters during the course of this year, and we have seven operating now. So, imagine how many new wells we are going to do and how would be the speed of for new reserves incorporated in the proved reserves. And then this is not ratio that concerns us.

Gustavo Gattass:

OK. Thank you.

Operator:

Yes, thank you. That thus concludes today's Q&A session. At this time I will hand the conference over to Mr. Barbassa. Please, proceed with your closing remarks, sir.

Almir Guilherme Barbassa:

Thank you very much for being with us in this opportunity to see the results of the 1Q of this year. They were very good, you were much more interested in the capitalization and I understand that. It is very important for us and for all the shareholders. We hope we will be adding information as soon as we get them, regarding this capitalization process. And hope to have you soon here for the next quarter results. Thank you very much.

Operator:

Thank you, sir, for you time. Ladies and gentlemen, your host is making today conference available for replay, starting one hour from now. You may access this replay at the Company's IR website at www.petrobras.com.br/ri/english. This concludes Petrobras' conference call for today. We thank you all very much for your participation. You may now disconnect.