Q1 2004 Earnings Call

Company Participants

- Carlos Tadeu De Costa Fraga, Production Manager, Diesel Unit
- Jose Sergio Gabrielli, CFO & IR Director
- Raul Adalberto De Campos, IR Executive Manager

Other Participants

- Brian Singer, Analyst
- Christian Audi, Analyst
- Frank Mcgann, Analyst
- Geir Sagemo, Analyst
- Katie Blacklock, Analyst
- Marcelo Prepo, Analyst
- Mark Mccarthy, Analyst

Presentation

Operator

Ladies and gentlemen thank you for standing by and welcome to the Petrobras conference call to discuss the First Quarter results. At this time all lines are in a listen-only mode. Later, there will be question and answer session and instructions will be given at that time. Should you require assistance during the call please press star, zero. As a reminder, this conference is being recorded. Today with us at Petrobras head office we have Mr. Jose Sergio Gabrielli, CFO and IR director and his staff. At this time, I'd like to turn the conference over to Mr. Raul Adalberto de Campos, Investor Relations Executive manager of Petrobras, who has some additional comments. Please go ahead Mr. Raul.

Raul Adalberto De Campos {BIO 17251399 <GO>}

Good morning, or afternoon ladies and gentlemen. Welcome to our conference call to discuss the First Quarter 2004, results. We have a simultaneous webcast on the Internet that could be accessed at the site www.petrobras.com.br/ri/english. Additionally on the webcast registration screen you may download and print the presentation and download the financial market report. Before proceeding let me mention that forward-looking statements are being made under the Safe Harbor of the Securities Litigation Reform Act of 1996. Actual performance could differ materially from those anticipated in any forward-looking comments or as a result of macroeconomic conditions, market risks and other factors. Finally, let me mention that this conference call will discuss Petrobras results prepared in accordance with Brazilian GAAP. At this moment we are unable to discuss any issues related to US GAAP results. The conference call will be conducted by our CFO and

Investor Relations Director Mr. Jose Sergio Gabrielli De Azevedo. He will comment on the company's operating and financial highlights and the main events during this quarter afterwards he will be able to answer any questions you may have. Mr. Gabrielli you may begin.

Jose Sergio Gabrielli {BIO 5474235 <GO>}

Good morning, everybody or good afternoon. You saw it on the slide number one, where we are presenting the comparison between our domestic price and the international -- the US price. The blue line represents our average realization price in Brazil, denominated in dollars according to the Brazilian exchange rate. And the red line represents a composite index of he average realization price or the price of the products sold in the United States using as weight volume sold in Brazil, is a kind of representation of the American -- the US price in Brazil according to the Brazilian volumes. As you can see during the year 2003, and the beginning of '04, we're forming what we have mentioned, our long-term relationship between the domestic price and the international price. Sometimes all price are above the composite index and sometimes it is below. In this last quarter we had a little bit below the US markets. The graph on the bottom part of the slide shows the comparison between the average quarterly -- average exchange rate in relation to the exchange rate at the end of the period. It is important for our results because when we have the two lines together means that we have a very small variation of the exchange rate within the quarter. And these will be taxably [ph]the results that -- the accounting results is on the exchange rate variation tax and on our numbers. As you can see in the last quarter we kept the exchange rate basically stable. Actually we had a depreciation of Real of 0.6% to 0.7% during the First Quarter for '04. When compared with the First Quarter for '03 when we have during the First Quarter an appreciation of Real of something around 5.1%. Slide number two, shows a bridge graph trying to compare our net income in 2004, in relation to the last result of the first -- Fourth Quarter of 2003. Our net income moved from R$3.021 billion to R$3.972 billion in '04. The main reasons why we have this change of around R$900 million was, reduction -- the absence of extraordinary items like the contractual loss in the energy business of R$1.4b. That was responsible for reduction towards increasing our net income and the negative impact on our net income, the absence of the fiscal [ph]savings as a result of payment of interest on our own capital.

During this two times, we have a reduction of our production from 2.023 million barrels per day to 1.996 million barrels a day. And we have also results of the -- perhaps I mentioned on the monetary corrections of 389 negative impacts on our results. On page three we have in our ENP a comparison of our operating profits comparing again the First Quarter of '03, and the First Quarter of '04. The most positive result is the effect of price on the net income. This basically throws surprises from our exploration production activities and to our supply activities. That also reflects some of our exports in international price, we have an increasing price that has increased our operating profit. And also we have a negative impact of an increasing price on our cost of goods sold that increased to R$405 million and also we have a negative impact on our operating expense. As you can see on the top left hand side of the graph, we have a reduction of our production from 1.513 million barrels a day to 1.5475 million in the First Quarter of '04, which affects also our unit cost as you can see on the slide number four.

On slide number four, we show the numbers of our lifting costs since the First Quarter of '02. Comparing our lifting costs without the government participation, in the First Quarter of '04 in relation to the lifting costs without government participation in the First Quarter of '03, we move from R$2.85 to R$4.22. It's important to mention that this increase of R$1.37 per barrel is a result of several different factors. 30% of this increase in cost comes from the situation of the drilling markets and the suppliers of E&P activities, their decreasing prices and these represented 30% of the increasing costs. 28% of these increasing costs comes from the appreciation of how to institute it. We had a 17% appreciation from the average exchange rates in the First Quarter of '03 to the average exchange rates of the First Quarter of '04. 15% of these increasing costs comes from increasing the services of platforms that we are arranging from third parties, 9% represent increase in our wage costs, and 9% represent a reduction of our production, which means that we have impacts coming from the acceleration of the prices of the service sector, a reduction of our production and some of our costs, including the execution of new replacements and new services to fulfill the requirements of this health and safety requirements.

On page five, we try to show the relationship in our supply business of our operating profits from these two quarters. The main positive effect is the price impact -- not the price, the reduction of the volumes in our cost of goods sold. That was important, that was not sufficient to offset the increase in our prices, the impact of price on our cost of goods sold. The price of our products increase our revenues, we have a reduction in the volume of sales, which put a negative impact on our operating results, and we have also a negative impact as I mentioned before of price of the suppliers, our wage costs, and some of the costs coming from stoppages programs, the stoppages for our refineries. Slide number six, we are trying to show the unitary refining costs and the throughput of our refineries. As you can see on the bottom of the curve, we have a very steep increase in the throughput of our refineries. In the First Quarter of '04, we increased the production using more imported crude oil and we built up inventories during the First Quarter of '04 trying to not only to recover the stock inventories level of the Third Quarter for '03, but also to prepare for a new program to maintain and establish as that's what we're to have in the next quarters of this year. The lifting cost in refine increase -- the cost of refine increase in the First Quarter of '04 in relation to the First Quarter of '03, moved from 1.9 to 1.3. This increase in cost is only about increase depending -- has an impact of because also actions rate, this would be something around 39%. We have an impact of the risk cost of 29%, and provisions for -- programmed to stop us, maintain us to stop us of 32%. Some of those decreasing cost are more recurrent to costs.

On slide number seven, we have an impact on our operating cost from distribution. We have a negative impact on revenues basically as a result of reduction of prices. We have a positive impact of reductional costs of goods sold, and a reduction in our operating expense that gives a positive impact on our operating cost, but even though we could not offset the reduction in revenues. On our international activities, we have very large increase in operating cost comparing to the First Quarter of '03. We have an increasing volume of oil and gas sold from R$3.65 to R$3.82, we've an increasing pricing on niche price from R$26.75 to R$27.40, and also we have a reduction where we have a better revenue results. Our cost of goods sold increased also, but less than the increase in revenues, and our operating expenses are much better right now, because we are not -- have a recurrent impact of the provisions that we have for loss in the Ecuador area. And as we don't have these same type of expenses right now, we have a better operating extensive result. On gas and energy, we moved from a negative position of a net loss of R$1.1 to an operating profit of R$0.22b. Most of this movement depends on the reduction of our provision for losses in the energy business, that's moved that change completely out of operating expenses reducing it in a very large amount 1.599. 1.415 out of this 1.599 billion corresponds to the provision of loss of energy that we provided last quarter.

Slide number 10, we've a leverage ratio which is 41% is pretty much in line with what we had before. We had a small reduction of our short term debt from total debt, cash and cash equivalent moved from R$24.9 billion to R$21.23 billion saturated where we can see that our financial numbers are pretty much in line with what we had in the Third Quarter of '03. In slide 11, we're trying to show how our cash sources and the use of funds in our cash movements, and we move our cash from R$24.9 billion to R$21.03b. We have a generation of operational cash by R$5b, CAPEX was R$3.5b. We have payments of dividends in an interest of owned capital R$3b. We have financing operations of R$2 billion and also-- which means that we have a reduction on our cash. These will be the result of the CAPEX and payments of dividends and financial operation. It's important to show that by our own operational activities we generate more cash than we use in our CAPEX. Slide number 12 shows what happens with our net debt. Our net debt increased from R$34.6 billion to R$37.6b. This was a result of the reduction in cash and debt amortization. We had a debt amortization of R$2b. We didn't have any big operation, debt operation in the First Quarter for '04. In terms of value added by the company, we show some small movements in the shares of company [ph], and the governmental entities are reduced from the participation in the value added from 66% to 63%. The proportion of personnel of lease cost moved from 9% to 7%, and the financial institution had increased from 8% to 11%, basically as a result of the exchange rate movements. Now we can go to the Q&A section. Thank you.

Questions And Answers

Operator

Thank you. At this time, I would like remind you all that in order to ask a question, please press star one on your telephone keypad. If you'd like to withdraw your question, please press the pound key. Thank you. Our first question is coming from Brian Singer of Goldman Sachs.

Q - Brian Singer {BIO 4404674 <GO>}

Good afternoon. Two questions somewhat unrelated to the actual quarterly results. But first on petrochemicals, could you give us an update on your thoughts regarding a further potential participation in petrochemicals?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

We are presenting to the Board of Administration of the company tomorrow. The first version of our strategic plan, I cannot address any of these conclusions right now.

Q - Brian Singer {BIO 4404674 <GO>}

Is it fair to say that petrochemical strategy would be a major part of that presentation?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

I don't know if it is a major, but one part -- an important part. Yes.

Q - Brian Singer {BIO 4404674 <GO>}

Okay. Secondly on international, you have taken a couple of stakes in some new play in the Gulf of Mexico, in terms of agreements with Exxon Mobil and with BHP Billiton in the ultra-deep south play. Could you talk about the Gulf of Mexico and further potential increases in exploration there and also what do you see with the specific Ultra-Deep Wildcat opportunities?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

Well, we have moved our operations in the Gulf of Mexico from shallow waters to deeper waters. We announced good discoveries together with BHP and Shell. We have moved prospective for goals of our exploration through to these areas, which is our frontier area. We know that, there are few companies that are in these areas that we are right now. But I am going to ask some more detailed information from our Executive Manager for the International Operations.

A - Raul Adalberto De Campos {BIO 17251399 <GO>}

Okay. Good afternoon. We have some instituted in that area, some revision of our series that would be presented tomorrow to our Board. I don't know if we could address this information now.

Q - Brian Singer {BIO 4404674 <GO>}

Okay. And lastly, could you just update on your thoughts on potentially raising fuel product prices in Brazil?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

Well, as I mentioned in the beginning, we think we are following our policy that try to keep a relationship for the domestic price of all the products that we have with international price. I made some comparison with the US price, this is one market that we're following, but the adjacent market is also that affects our Brazilian markets throughout a lot of products. We think that most of the movements in the US now depends on the demand side of the American market, that is a very important driver from the demand side. And we need to have a very clear idea of the trend, the long-run trend of pricing before we have movements in the Brazilian price.

Q - Brian Singer {BIO 4404674 <GO>}

Great, thank you.

Operator

Thank you. Our next question is coming from Frank McGann of Merrill Lynch.

Q - Frank Mcgann {BIO 1499014 <GO>}

So a good day. I was just wondering if you could speak about your expectations over the next 12 months particularly, and perhaps just a bit longer on both in terms of your cost trends in refining and on the extreme side and your production trends that you would expect to see over the next couple of quarters, given the relatively soft production in the First Quarter. If you are going to have flattish production for the year, can we expect that you will see a fairly strong increase in production going forward over the next two or three quarters?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

Hi Frank. We are projecting for 2005, an average production of 1 million to 1.8 million barrels a day. In our schedule, we have for June of '04, to begin our production analysis of Marlim south of 100,000 barrels per day. By October of '04, we have the first oil, 243 by October, 115,000 barrels per day. By December '04, 248 (inaudible) with more, 115,000 barrels per day. In the Third Quarter of '05, 250 of Roncador lasts [ph]with 118,000 barrels per day, and by the Fourth Quarter of '05, you got to face 134, 60,000 barrels per day, which means that we are expecting unto December 5, to increase our production by 640,000 barrels per day. We've seen that till -- if we increase our production next year and at the end of this year, these would impact our lifting costs, which is going to reduce our unit costs. But we know that we are facing an international market force of services for our E&P activity towards increasing cost. And we think that our increasing production is going to be the main driver for reduction of our unit costs.

Q - Frank Mcgann {BIO 1499014 <GO>}

Okay, and in terms of just production for the next couple of quarters, can we look for an increase from the First Quarter levels?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

Well, in June, we have some increase. As far as we have, the Marlim South is starting production, also we see this as even that have affected the production on the First Quarter, it starts production on, say April 17. FPSO Brazil also that's having a negative impact in February. Now, it's in full operation. We think that the problem that we had or provisional problem that we had in the First Quarter are going to be overcomed soon and then we hope that we can have some increase in production, not a dramatic increase in production but recover of what we had in the First Quarter.

Q - Frank Mcgann {BIO 1499014 <GO>}

Okay. Thank you very much.

Operator

Thank you. Our next question is coming from Marcelo Prepo [ph]of UBS.

Q - Marcelo Prepo

Hi good afternoon Gabrielli. Good afternoon Raul. My question is related to -- and again related to the present policy of the company. I was wondering if you could elaborate a little bit more on that because you said that you are following the international prosperity in general, but unfortunately your calculations are not showing that or just to give an example, you are showing in the slide number five, that should be average realization price increased during the First Quarter some 2%, 2.5%, while we are seeing your daily charted prices increasing by 13% in the quarter. So I am wondering if you can tell us what is happening there? We know that the prices of gasoline, diesel, and LPG are not adjusted, but what is happening with the order price of naphtha, fuel oil, jet fuel, etcetera? And my second question is also related is, the subject is -- what is the timeframe or the hurdle rates that you'll be looking at to say, `okay, now we'll give up these stronger levels of oil prices are going to last longer, and we will have to make a major adjustments now for us`?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

If you go back to the slide number one, I think the slide number one is the kind of example of what I was saying. And the red line again is the number that is not only gas and diesel, the red line is the composite index of different products in the US market. And the number that we have is the prices in the United States, into the mass market of United States, average price in the mass US market. And we are weighted in these numbers by the volumes that you sell in Brazil. This is not really completely right because the structure of the market in United States, the proportion of diesel and gas in the United States differs from the proportion of diesel and gas in new Brazil. The use of gas, natural gas in United States is not the same type of natural gas in Brazil. They impact -- a relative price of the gasoline and the order price in United States is not the same as in Brazil. However, these two lines shows that we sometimes, we captured three months stable price in Brazil, the blue line. That was able to capture the slight movements that they had during the year. We had some movements that we were much below the international price as in the First Quarter of '03. And now we are a little bit above again in the international price. What we capture was during this Fourth Quarter of the five quarters was a stable number that's translating to Brazil, that's completely the volatility of the international price. Since you are asking me how longer we are going to look at that, we have to analyze everyday in the market and try to see the variables that are affecting the international prices (inaudible) position that are going to stay in this level. We are going to have a longer winter, rather than they should have a longer solicitation of a cost that gives more -- gives you (inaudible) orders and going to have a longer impact of the colder weather than in the others is difficult to answer, but we have to look and try to see and forecast a more stable, long-term trend before we move into Brazilian price.

Q - Marcelo Prepo

Okay. I just have a final question to see if I understand that correctly and get more color. If we assume that our interest rates, I'm sorry, if the FX rates are maintained a bit around 3 reals and WTI prices around this 39, 40 reals, are you comfortable with your domestic price or do you see any need for increase.

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

Right. I could -- I did not get your last question. Could you repeat please?

Q - Marcelo Prepo

If you assume that the FX rate is maintained around this 3 reals and international, let's talk about the WTI price, will be maintained about this $39 or $40 per barrel level that you are seeing right now. Do you think that's -- are you comfortable with the domestic level of (inaudible) prices at the moment or do you think that there will be some need for increases in the future?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

I got the point. First, it's important to see that it's very difficult for us to translate into the Brazilian market with some simultaneous increase, a very high increase in price and very high depreciation of real. The two things together, are really difficult to put into Brazil. Second, it's important to mention that in Brazil we have the CID panel that is a kind of tax that can be used by the government not by the Petrobras. So if you add some of these, pointings and permanents short supply stocks. Right now, we don't see clearly a very defined long-term perspective, not more in relation to the change of rates in Brazil, that's more than we had two weeks ago, neither in relation to the oil finds. We have to follow into the column and see what's going to be the design that the market will give us before we've movement.

Q - Marcelo Prepo

Okay. Thank you very much.

Operator

Thank you. As a reminder, if you do have a question please press star one on your telephone keypad at this time. Our next question is coming from Katie Blacklock of Thames River Capital.

Q - Katie Blacklock {BIO 17145068 <GO>}

Hello, I just had a question on the gas and energy division. Can you give me an idea of what level of provisioning we should expect if we are, full year this year?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

Yes, we provisioned in the Fourth Quarter for full year, provisioned 1.4 something, we don't hide for all the loss that we are expecting for this industry during 2004.

Q - Katie Blacklock {BIO 17145068 <GO>}

Thank you. So no provisioning expenses through this year then?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

Yes. these are provisions that we made in last quarter of last year to be evaluated during 2004.

Q - Katie Blacklock {BIO 17145068 <GO>}

Okay. Thank you.

Operator

Thank you. Our next question is coming from Mark McCarthy of Bear Stearns. Mr. McCarthy your line is live at this time. We'll move on to our next question which is coming from Geir Sagemo of JP Morgan.

Q - Geir Sagemo {BIO 3029258 <GO>}

Hello, I wanted to ask you a question about natural gas demand and sales. You had very good growth in the First Quarter of the year in terms of your sales. I was wondering whether you could give some numbers in terms of your overall sales expectations for 2004, are there enough returns or is the 10percentage increase you are expecting and also if you could give some indication of the proportions that were contributed out from domestic production in gas from Bolivia?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

Yes, it's good mention the important proportion. Right now, we have more or less half and a half. 40% is imported from Bolivia and 60% is Brazilian production. We don't see any big movement or any big change of this proportions over the -- for sure we are having a decent market condition for the energy side. Our sales of energy increased a 122% from First Quarter of '04 in relation to the First Quarter of '03. We expected that the new market is going to be increasing the demand for energy and then we can sell more. And as such, probably we are going have a increase in sales of gas too.

Q - Geir Sagemo {BIO 3029258 <GO>}

As a follow-up, I appreciate that sales for the year will increase. I believe you reported 30% increase in natural gas sales in the First Quarter according to your press release. Is that the kind of number that you believe is represented here for the full year or is it right to suppose it to be the lower or higher for the full year please?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

I don't have the numbers right now with me and I don't have any -- I'll talk to the management from the gas sector. But, considering that we had nothing very exceptional in the First Quarters suppose that we are going to keep using type of behavior in the next quarters too.

Q - Geir Sagemo {BIO 3029258 <GO>}

Thank you.

Operator

Thank you; as a reminder if you do have a question please press star one on your telephone keypad at this time. Our next question is coming from Christian Audi of Morgan Stanley.

Q - Christian Audi {BIO 1825501 <GO>}

Hi Gabrielli, I had a couple of different questions. First one, going back to the topic of lifting cost. When you broke down the reasons why lifting cost went up, if I remove the appreciation of the Real, which you said was 28% of the difference. Is it safe to assume that the remaining issues are all recurring as we go into the Second Quarter and Third Quarter and Fourth Quarters of '04?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

I think that the recurring that you can see is in the services, that half of it was services, so the E&P probably is going to continue to be where it is now. On the wages side, however, we had some premiums that were exceptional in the First Quarter for some extra hours that we had to pay from the past.

Q - Christian Audi {BIO 1825501 <GO>}

Any new equipments at a higher cost related to platforms from the third parties so they would also be recurring given their market conditions right now?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

I don't know if it is going to continue to increase, but I don't think it to be very high prices as it is now.

Q - Christian Audi {BIO 1825501 <GO>}

Okay. Great. And the second question can you just on the production front give, and you have touched already on this, just a quick update on when we look at the main maintenance projects that led projections to come down in the Fourth Quarter and also impacted the beginning of the First Quarter. Can you just talk about the main ones and where we are with respect to them still being under maintenance or back to normal or if they are not back when you expect them to be back up for operations?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

Yes. I don't know if it is going continue to increase but it is going to be in very high prices as it is now.

Q - Christian Audi {BIO 1825501 <GO>}

Great. And the second question can you just -- on the production front give a picture really on this -- just a quick update on when we look at the main maintenance projects that lead production to come down in the Fourth Quarter and also impacted at the beginning of the First Quarter. Can you just talk about the main ones and where we are with respect to them, still being under maintenance or back to normal or if they are not back yet when do you expect them to be back for operation.

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

I'll ask Carlos Tadeu de Costa Fraga [ph], Production Manager to explain this.

A - Carlos Tadeu De Costa Fraga {BIO 20703384 <GO>}

Christian, the problems where in the First Quarter mainly I stop as the -- I don't have though numerous knowledge its normal with our basin. The second main reason was SG Sheller [ph]where we are destined and pilot about 20,000 barrels of oil equivalent, now its on line its okay again, so we don't expect more impact into next quarter.

Q - Christian Audi {BIO 1825501 <GO>}

Anything left from the First Quarter that was in maintenance then that is still not back to normal?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

No, no. Not some more.

Q - Christian Audi {BIO 1825501 <GO>}

And the last question Gabrielli had to do with, you showed on the demand side for few products year-over-year growth, which we hadn't seen in a while. First of all, what do you think has led for this growth to occur in the First Quarter? When do you expect it to continue or you are seeing that in your April beginning of May numbers that continuous growth in volumes for few products?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

Yes. In the First Quarter we had a small increase in the domestic volume of sales. And it seems that they continue to be after the 31st of March.

Q - Christian Audi {BIO 1825501 <GO>}

And that you also could talk about some -- in your press release some speculative movement in trading volume sales in the First Quarter. Could you add a bit of color as to what exactly you expect sort of movements are in the South that are impacting you or what's causing them?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

Speculative movements in GLP [ph]. In what product?

Q - Christian Audi {BIO 1825501 <GO>}

Just a overall volume for a first fuel products?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

Yes. We have seen some speculative movements of building up inventories in some areas, trying to anticipate fluctuation prices, but nothing that you would characterize are current. So we have some speculative movements in some places that we are that we suppose that are related to some anticipation of the change movements in price.

Q - Christian Audi {BIO 1825501 <GO>}

Okay. And very last question similar to the analysis that you gave on the listing cost and what caused it to go up? You did a similar exercise for refining cost? Can you also just talk about there, what in your view of the different elements that cause refining cost to go up, do you expect it to be recurring as we go into the second and Third Quarters?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

Yes. On the refining cost we have some amounts, 29% of the refining cost increase was related to lease costs, some of the lease cost are also related to some overall as payment. We have some payments also for some, increasing our actual evaluation of our pension fund. We have our increase in number of people working in the refineries. We have 300 new workers in our refineries, but also we have more than 30-programmed stoppages, (inaudible) stoppages for this year. But there are already provision in our increasing cost in the First Quarter. We think that we, yet we don't expect to decrease in our refining cost for the next few quarters.

Q - Christian Audi {BIO 1825501 <GO>}

But these are with the exception of the 39% debt that was caused by FX, so could you explain the --?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

Yes, 39% is FX, 29% to personnel and 32% by programmed maintenance stoppage?

Q - Christian Audi {BIO 1825501 <GO>}

All right. And you are saying that 32% for the program stoppages and the 29% for the wages is an aspect of refining cost that you don't expect to be recurring, you might be spending correctly? Thank you, very much Gabrielli.

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

Okay.

Operator

Thank you. As a final reminder, if you do have a question please press star one on your telephone keypad at this time. Thank you. We do have a question coming from Mark McCarthy of Bear Stearns.

Q - Mark Mccarthy {BIO 5634411 <GO>}

Hi. Yes I have just two questions. One is related to the inventory buildup, if you can talk a little bit about when it was done in the quarter? These are oil import number spiked up quite a bit and it seems as though they were processed or it seems as though your refine products inventory levels were at a higher level? And I was kind of curious as to what period in time in the quarter was built up and what your average pricing level itself is? And the timing for these shutdowns to absorbs these inventories? Second question was along the CAPEX. Why was at the level it was? And how you envision it growing for the year?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

Right. Lets start with the CAPEX. We have a 3% increase in our CAPEX in relation to the First Quarter of '03, usually Petrobras in the First Quarter we have a lots of investments extensively than in the other quarters, We've told you we are going to have an increase in the CAPEX in the second and third and Fourth Quarter. But it is our cyclical movements typical there is nothing special for 2004, but they are pretty much in line with '03. As you can see in our numbers this 3% increase in our CAPEX and we have reduction of 47% on our gas and energy CAPEX. We will have an increasing 2% of our exploration and production, 16% of our CAPEX in our energy supply, which is pretty much in line with what we are trying to do is nothing special in our CAPEX. In relation to the building up of our inventory it is important to mention that to increase our throughput our refineries process more oil, we imported more oil, crude oil, and reduced the imports of oil products. And we built up inventories for three reasons to substitute inventories that we had reduced in this previous quarter, to prepare for more than 30 programmed shutdowns that we are planning for our refinery in the future, and also to not to prepare for any type of movement in prices. We have all the different reasons, and when we did that we did that during the First Quarter, during the three months of the First Quarter.

Q - Mark Mccarthy {BIO 5634411 <GO>}

Okay. Then if you had your reasons, my curiosity is really when during the quarter it was done and what was your average price?

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

I have here the -- of our average price of oil, during the First Quarter of our price of oil. Our average price of oil in Brazil was BRL 29.67 in '03, and was BRL 29.53 during the First Quarter of '04, which is basically the same as last year. This is our average price of sales. We don't release our costs, we don't release our day-to-day costs.

Operator

Thank you. Ladies and gentlemen. there are no further questions at this time. Mr. Gabrielli, please proceed with your closing remarks.

A - Jose Sergio Gabrielli {BIO 5474235 <GO>}

I would like to thank everybody and say good day for everybody, and I hope to seeing you very soon.

Operator

Thank you. Ladies and gentlemen. your host is making today's conference available for replay starting one hour from now. You may access at the IR Web site this replay or by dialing US 1-973-341-3080 lasting till May 20. That number again is US 1-973-341-3080. At the voice prompt, enter the access code 4773213. This concludes Petrobras conference call for today. Thank you, very much for your participation, you may now disconnect.