Q3 2020 Earnings Call

Company Participants

- Emiliano Fernandes Lourenco Gomes, Vice Chairman
- Francisco Francilmar Fernandes, Chief Operating Officer
- Roberto Bernardes Monteiro, Chief Executive Officer and Chief Financial Officer

Other Participants

- Bruce Barbosa, Analyst
- Rafael Ragazi, Analyst
- Rodrigo Reis de Almeida, Analyst
- Unidentified Participant
- Victor Schmidt, Analyst

Presentation

Operator

Good afternoon, ladies and gentlemen, and welcome to PetroRio's Conference Call to discuss Third Quarter 2020 Results. Thank you for standing by. At this time, all participants are in listen-only mode during the presentation. Later, we will conduct the question-and-answer session for analysts and investors when further instructions to participate will be provided. (Operator Instructions) This event is also being broadcast simultaneously over the Internet and may be accessed through that PetroRio's Investor Relations website at ir.petroriosa.com.br, by clicking on the banner Q3 '20 Earnings Release.

Before proceeding, let me mention that forward-looking statements that might be made during this conference call relative to the company's business perspective, projections and operating and financial goals are based on the beliefs and assumptions of PetroRio's management and on information currently available to the company. Forward-looking statements are not a guarantee of success. They involve risks, uncertainties and assumptions as they are related to future events and, therefore, depend on circumstances that may or may not occur in the future. Investors should understand that general economic conditions, industry conditions and other operating factors could also affect the future results of PetroRio and could cause results to differ materially from those expressed in such forward-looking statements.

I would now like to turn the conference over to Mr. Roberto Monteiro, CEO, CFO and New Business Officer; Mr Francilmar Fernandes, COO; and Mr Emiliano Fernandes, Legal and Administrative Officer.

Mr. Monteiro, please go ahead, sir.

Roberto Bernardes Monteiro {BIO 16616322 <GO>}

Thank you very much. Good day, everyone. Thank you for joining us in our third quarter earnings conference call. I will make a brief introduction regarding our results and then, I'm going to turn the floor to Francilmar, who will give you more detail on our production in the third quarter. And then I will be back to speak about our financial highlights.

I would like to begin, once again highlighting our culture. Our culture is very much focused on efficiency, financial and operational discipline and ours is a culture of resilience to achieve results. Our culture, our way of seeing our business once again was a determining factor for us to achieve our results as we will see in a minute.

The first highlight, I would like to mention has to do with safety and health. We had another quarter with fairly stable and safe operation, both in terms of operating safety and in terms of the health of our workforce. And this obviously minimized the impact of COVID-19 on our company, on PetroRio.

In this quarter, we started operating Tubarao Martelo, TBMT. ANP authorized the start-up of the operation of TBMT. We handled this transition very efficiently as Francilmar will tell you. And we also resumed the project to interconnect TBMT with Polvo. And Francilmar will be giving you more on that later.

In the third quarter, we sold 2.4 million barrels of oil generating around BRL490 million in revenue. Another important point as regard to oil offtakes, has to do with our fourth quarter sales. During the third quarter, we already contracted the sale of 4 million barrels of oil to be shipped along the fourth quarter. So, this is definitely going to be a historical quarter for the company, from the point of view of oil derived revenue.

If we remember at the beginning of the year with the COVID pandemic, one of the pillars of our strategy was to hold back on oil offtakes, so we would not sell in a very depressed market. But now we are resuming sales during the fourth quarter and we have already contracted the sale of 4 million barrels approximately, with hedges locking the minimum price for these offtakes at $43.5 per barrel.

And the discounts that we have received are already at 2019 levels. In some cases, even levels prior to IMO 2020. IMO 2020 was a treaty. Perhaps, we can call it an agreement among countries to reduce the level of sulfur and the diesel and in the fuel used by ships called bunker fuel. In the beginning of the year, we had a slight impact of that, but now even this impact is wearing off, not only the COVID-19 effect but also the IMO 2020 effect. So, this would definitely be a quarter with strong revenues for the company.

Now moving to the next slide. Slide 4, please. Here I will speak about another three important highlights of the quarter. And again later, Francilmar will give you more detail on each one of them. But the three important things to mention are our lifting costs. For another quarter, our lifting cost reduced from $13.7 per barrel to $12.8 companywide.

Our production with TBMT increased by 25% on average during the quarter. And finally, our leverage metric, our indebtedness level. In other words, our net debt over EBITDA ratio decreased from 2.1 times to 1.9 times. So again, another reduction of our leverage.

Overall, so far this has been a very challenging year or a year of many great challenges, but these indicators show quite well how the company is reacting to these challenges so far. The company is totally under control, operating according to our culture and according to our business model and achieving fairly good ratios and marks even in such a difficult and uncertain landscape.

With this, I turn the floor to Francilmar to speak about our operation and then I will be back to speak about our financials.

Thank you. Francilmar, over to you.

Francisco Francilmar Fernandes {BIO 21185801 <GO>}

Thank you, Roberto. Hello, everyone.

Let us move to the operating highlights, starting on Slide 5. As Roberto has already mentioned, one of the most important highlights was the reduction of the company's lifting cost, now at $12.9 per barrel. I will detail all these figures a little more later on.

PetroRio's daily production was 33,000 barrels and that is excluding the 30% working interest of Frade Field, but already including the start up of Tubarao Martelo Field. We started operating the field since the beginning of August, as well as had the start of production of Tubarao Martelo number four well, with well completion and its connection to the FPSO, leading to a 40% production increase at TBMT Field.

We also had the first offtake at OSX-3 with a record mark of 2.5 million barrels sold in one single quarter of the company, the best mark ever for the company. We resumed the tieback project between Polvo Alpha platform and the OSX-3 FPSO located at Tubarao Martelo, with a physical progress of around 17%. And I will be giving you more on that in a minute. Another very important highlight in Q3 was the maintenance of our production and operating efficiency levels, as well as the health and well-being of all our workforce operating at our units even in this COVID-19 pandemic scenario. This comes to show the resilience of our people and the efficiency of all of the procedures we have adopted to prevent problems.

Moving to Slide 6. I'll detail the performance of our assets. Overall, I would like to draw your attention to the production of Manati Field. After a marked drop in production in Q2 due to a reduced demand for gas, we again have a good demand for the commodity and are practically at the limit of production at the field. The productions at Polvo and Frade fields will be detailed momentarily. But by and large, with the start up of TBMT Field in Q3, we had a total production increase for the company of around 25%.

Moving to Slide 7. We can see on the left-hand corner graph showing the evolution and steady reduction of our lifting costs. The factors influencing this reduction in lifting costs are related to a rationalization of all of the resources we have onboard. And here, I mean, our employees, third-party contractors. We started this action last year and intensified it along this year.

We also had an increased production at Polvo Field, as well as the start up of Tubarao Martelo, the start-up of well TBMT number four, coupled with synergies that we captured in the operations of the field. All of these factors have helped us achieve this lifting cost reduction. The challenge now is to keep it at that level, as now we should resume some maintenance services that were postponed for preventive reasons and to reduce people on board. To give you an idea, we were working with 50% of the normal people on board, POB. We have increased it recently and are now at around 60%, 65%. This scenario should last until the completion of the tieback of both the platform with FPSO OSX-3, when we should see another total reduction in the lifting cost.

Moving on, I will give you more detail on the operating efficiency and performance of Frade Field. Well, the fields continues to have an excellent operating efficiency, 99.4%. We had few problems there. Production had a slight decline. But financial reasons, nothing exceptional happening in the quarter.

Moving to Polvo Field on Slide 9 here. Yes, we had some excitement, some unscheduled emergency stoppages at the FPSO at Polvo, with an impact on operating efficiency at 94%. This was somewhat offset by an increased production at the field. So after we mastered a little more of the flow [ph] process, particularly at well 45 of the Eocene reservoir, we had an increase in production. Now, we are working to increase the levels of operating efficiency.

Moving forward to Slide number 10. I will give you an update on the revitalization program of Polvo Field. The producing well in the Eocene reservoir has been showing excellent behavior with steady pressures compared to what we expected initially and confirming and even going beyond our expectations. The reservoir proved to be a little bigger than we thought, giving us confidence to move ahead with the project. We should complete the studies in the first half of 2021, and we should have data to drill some wells in that reservoir.

On Slide 11, I'll give you more detail on the operating performance of Tubarao Martelo Field. The field achieved a 97.5% operating efficiency in the quarter, with a good part of that under the operatorship of PetroRio. We took over the field since the beginning of August. So the whole operational part of the FPSO and the subsurface management, including subsea and wells being handled by PetroRio's technical staff.

The transition went [ph] really smoothly and eventually, maintaining all safety and efficiency levels and showing the resilience and capacity of the company in this kind of transition. During this same period, we also finalized the completion and connection of TBMT well number four, which increased the production at the field by around 3,000 barrels, totaling 10,000 barrels. This well is located in a reservoir that was already producing, so it should have a greater decline and we already see some signs of that happening.

On the lower chart, we can have a general and systematic view of the tieback project. So, we have the fixed Polvo Alpha platform. There is a flexible line that will be connected to the FPSO OSX-3 at TBMT and here we are. And here are the subsea wells at TBMT.

Well number 10 is closer to Polvo, and it is a future target for us to go ahead with the completion and connection with the vessel. This project is unfolding well. We have made physical and financial progress according to schedule and ended the third quarter with around 17%. We are a little beyond that now and the project is unfolding as planned. We expect to finalize everything by the end of the first half of next year.

With this, I end my part and turn the floor back to Roberto.

Roberto Bernardes Monteiro {BIO 16616322 <GO>}

Thank you, Francilmar.

Well, from the financial standpoint, I would like to draw your attention to our great revenue and EBITDA increase, even operating in this difficult and uncertain well scenario with the Brent oil price dropping from $60 to negative values and then going back to $45, $43, now dropping again, so you see. This has been a very volatile and uncertain year. So, I'd like to draw your attention to our net revenue and EBITDA, which have a lot to do with our offtakes of 2.5 million barrels or almost 2.5 million barrels along the quarter, resulting in a cash position of $136 million at the close of the third quarter. We had a reduction of our leverage, our net debt over EBITDA ratio and a reduction of the company's net debt from $270 million to $239 million.

And finally, I'd like to point out once again and I spoke about this during my initial remarks. Our contracted offtakes for the fourth quarter of approximately 4 million barrels, approximately right, with a hedged price or perhaps we can call it a minimum price of $43.5 per barrel.

Please go to Slide 13. Here I will show you our income statement and the results of the company. We can see an increase compared to 2019 in practically all line items; revenue, operating result, EBITDA, and so on and so forth. I would like to underscore two points. The first has to do with general and administrative expenses, with a slight increase even over the second quarter. And a good part of that is explained by salaries returning to normal levels. You will remember that during the second quarter, we had our wages temporarily reduced during the COVID-19 pandemic, a 25% salary reduction across the company and a 50% reduction for the management. And now the salaries are returning to normal levels.

The second point has to do with insurance. Once a year, we have to pay insurance. This is an expense that we incur in one given month and it applies to 12 months. But it is all recognized at the moment that we actually pay for it. So, we had a slight increase, a slight

G&A increase, the salary effect amounting to around BRL3 million and the insurance effect of approximately BRL4 million in the quarter.

Another thing, the second thing I'd like to underscore is our EBITDA margin. Our EBITDA margin is 42%. Here on the left bottom corner, we see a 42% adjusted EBITDA margin. And this has a lot to do with the way in which we accounted for Tubarao Martelo so far.

And now, I'm going to go to Slide 14 because here we show how we accounted for TBMT. If we look at the right-hand corner, we can see the part of TBMT's revenue, part of the TBMT result, according to our contract was accounted for as other operating expenses, other operating revenues. In the quarter, BRL22 million. Year-to-date, BRL127 million approximately.

And this was the chartering of OSX-3 that was accounted for this revenue for the company. And then this was coupled with the wells that we received when we got approval by ANP. So, we did, what we call a price adjustment. But the fact here is that oil was accounted for by the company at a somewhat higher cost because we had already recognized part of this "benefit" that we have since February with the chartering of OSX-3.

So, when we do an EBITDA adjustment and for this line item of other operating expenses, revenues is derived from the EBITDA, we changed this margin a bit. But what matters here is that looking forward in the coming quarters, there will be no longer this effect of other operating expenses linked to the chartering of OSX-3. From now on, we don't charter OSX-3 anymore. So, we will start to see an improvement in the margins because of TBMT. You see, this is just the technical explanation, but I just wanted to mention it because it might mislead you to think that we are losing a little bit of margin when we actually are not losing margin. It's just because of the way in which we accounted for it the Tubarao Martelo deal.

Now moving to the next slide. I would like to speak a little about, what we call funding. It's actually the company's indebtedness. Here not much has changed compared to what we posted in the second quarter, except for the loans that we paid -- we repaid. We continued with the vendor finance with Chevron as the main funding source for the company.

This vendor finance was renegotiated in the beginning of the pandemic. Here we have the new amortization schedule, $15 million in November, $30 million in May, $97 million in November of next year under [ph] Prisma. During that period, when we were thinking about that -- about issuing a bond when the company went to market to try to issue a bond in the US, that market, we held back for a while on the negotiation with Prisma. We stopped working on the Prisma deal. Both parties stopped because if we were successful with the bond that we were going to prepay that debt with Prisma, but since we decided not to go forward with the bond issuance, we resumed negotiations with Prisma to transform the short-term debt into a project finance.

So, I'd say that in Q3, after the bond moment in recent months, just last month perhaps, that was the moment when we advanced the most. I should say we are 80% ready. Like I said before, this is a big long-term contract, and we're on our way to turn it into a long-term project finance. And we think we should have this matter settled by year-end.

And then we have the prepayment of imports with ICBC, which remains in the regular amortization schedule. So nothing much here. What is worth paying attention to and highlighting is the company's deleveraging. Once again, we reduced our leverage. We are at 1.9 times net debt over EBITDA, and this does not take into account some effects.

For example, in the case of Tubarao Martelo, in the third quarter, we had one month operating TBMT or little over a month of operating the field and generating an EBITDA. And EBITDA was impacted by what I mentioned earlier, related to the way in which we accounted for the deal, but we have the whole debt, right, related to the acquisition.

Another point relates to Frade, the acquisition of the 30% stake from Petrobras. We paid the lump sum to Petrobras in the past, but so far no EBITDA was generated. So, we disbursed the cash for the investment or at least, a part of it has been disbursed with no corresponding EBITDA and so on and so forth. So, there are some corrections that can be made here. If we were to make these adjustments, so we will have a much lower leverage level.

And something else to highlight is our oil inventory. In the first nine months of the year, we somewhat postponed our oil sales. So, we wouldn't sell at such low prices in the beginning of the year, but now we have this oil available to the market. So, that's something else that explains why we've not generated all the EBITDA, we could have generated along this period.

If we were to make all of these adjustments, our leverage would be under 1 time. So it is an indicator that remains comfortable. The company remains comfortable with these figures. In other words, I think that this is what really matters here. It is not really about the size of the debt, but rather how comfortable the company's operation is with that level of debt. And I think we are very comfortable in that regard.

Moving to the next slide, Slide 16. I'll speak about the next steps. And here, I don't mean necessarily the next steps in financial terms. I'm talking about the next steps for the company. What is important? And we will continue to do it, is to keep our focus on safety, to keep our focus on health, so as to protect our operation, so as to protect our employees and so on and so forth.

So, this is an ongoing focus of ours. Also in the next quarter in Q4, we expect to complete the acquisition of the 30% stake of Frade Field acquired from Petrobras a year ago. We are waiting for ANP approval. We have here, as I mentioned twice today, the strong offtakes totaling 4 million barrels of oil to be sold along Q4. We also expect the conversion of the Prisma loan into a project finance, and that will turn a short-term debt into a long-term debt.

The tieback project of TBMT and Polvo, and the connection of the new TBMT 10 well, we expect these projects to continue so that we can finalize the tieback by mid-2021. And the company remains attentive to M&A opportunities. We see the market picking up again. During the most acute phase of COVID-19, our pipeline was considerably reduced, but now we see several opportunities appearing again out there. So the company will follow its DNA -- a DNA of acquisitions.

With this, I would like to close the presentation. We will now open the floor to questions. But before I do that, I would like to publicly thank the whole PetroRio team for their perseverance, discipline and resilience that they have shown so far. I think that this has been a very challenging year. I guess we'll agree on that, lots of challenges.

But at the same time, the company achieved marks, figures, record numbers, a record production, record profitability and so on. And this is a big achievement by all employees of PetroRio.

Thank you very much. And let's start the Q&A.

Questions And Answers

Operator

Ladies and gentlemen, we will now begin the question-and-answer session for analysts and investors. (Operator Instructions) Our first question is from Mr. Rodrigo Almeida with Santander.

Q - Rodrigo Reis de Almeida {BIO 20698362 <GO>}

Good afternoon, Roberto, Francilmar, Emiliano. I have two questions. One has to do with the sale price. When we look at the selling price that you mentioned in the press release, it is a little different when we do the reverse calculation with the amount sold. So, I'd like to understand how you got to that actual price and perhaps you could break it down by field, so we could understand better how each operation is performing?

And my second question is related to working capital. That increase in the suppliers' account. Perhaps this is related to investments that are being made for the tieback project and for Frade. So perhaps you could give us more color on that? These are my two questions. Thank you.

A - Roberto Bernardes Monteiro {BIO 16616322 <GO>}

Thank you, Rodrigo. Good afternoon. Thank you for the questions. I will start with the selling price. Of course, we can give you more color on that. Regarding the third quarter, it is important to remember that we had some offtakes from Frade and Polvo/TBMT, but still not with the discounts that I mentioned during the presentation, not with the 2019 discounts pre-pandemic and pre-IMO 2020.

So, we still had some impacts by the COVID effect. We had some trades at Polvo/TBMT. So, we had a discount of $6 to $7 perhaps a little more. And for Frade, the discount was around $4 discount, perhaps a little less than $4. And one thing that you have to consider, you have to disregard gas from Manati. I will ask Jose Gustavo to get in touch with you and perhaps give you more detail regarding that. And then you can improve your report. But these were the offtakes and these were the discounts. So, we have to get to the average Brent oil price for the month, we applied this discount and that is it.

As regard working capital, I think you were very precise. We had an increase in the suppliers' account because we are starting to contract some items. Most of these items. Well, there are two effects in practice. You have TBMT expenses. So, we add another operation that has few expenses. But there are some expenses, so that increases the suppliers' account.

But the bulk comes from CapEx to connect Polvo and TBMT. It's unfolding well. But the CapEx has to be there, so that we can be ready for the final tieback by mid-2021.

Operator

Our next question will be by Mr. Bruce Barbosa.

Q - Bruce Barbosa {BIO 20917674 <GO>}

Hello, everyone. Congratulations on the results. And thank you for allowing my question. If you can, could you break down the costs because half of your costs are in Brazilian reals? And what about the lifting cost? Can you break down how much of the lifting cost is specifically in Brazilian reals, BRL?

A - Roberto Bernardes Monteiro {BIO 16616322 <GO>}

Hello, Bruce [ph]. The lifting cost perhaps is a little less than 50% in reals, just under 50%, I would say. Perhaps 40% in Brazilian reals. It's around 40%, 50%, around 40% to 50% of our costs are incurred in Brazilian reals.

Q - Bruce Barbosa {BIO 20917674 <GO>}

Understood. Thank you. May I ask a second question? You mentioned about M&A opportunities in the end of the presentation. Do you have anything in mind, anything happening? Can you tell us anything about it?

A - Roberto Bernardes Monteiro {BIO 16616322 <GO>}

Well, of course, in addition to the Petrobras deals, there is one Albacora, which was important given its size. But in our pipeline, we have perhaps another four or five M&A opportunities, in addition to this opportunity with Petrobras. So, what we see is that after COVID, our pipeline is again fuller as it was before the COVID 19 pandemic. And so it's a little of everything in our pipeline. There are things not related to Petrobras. There are some possible deals related to Petrobras, such as the deals that you know about. We have a possibility to divest. So, I should say that our pipeline has become a lot more active in the last two months.

Q - Bruce Barbosa {BIO 20917674 <GO>}

Understood. Thank you.

A - Roberto Bernardes Monteiro {BIO 16616322 <GO>}

It has also to do with the reduction in oil price.

Q - Bruce Barbosa {BIO 20917674 <GO>}

How do you see the Brent oil price in the middle -- the mid-term post pandemic?

A - Roberto Bernardes Monteiro {BIO 16616322 <GO>}

Well, we've had two more marked reductions in the oil price. One was in 2016 and one was this year. And what we normally see that in the most acute phase of the oil price reduction, normally the M&A pipeline, the number of deals shrink. Of course, we normally negotiate with major companies. They tend to hold still. They tend not to so in acute phases of price reduction. This is what happened back in 2016 and now. But then when the oil price starts going up again, which is happening now, then these oil companies start thinking about selling again, thinking about M&A. This is what you've seen.

And then as regards to the oil price that is hard to say. I haven't got an expertise to speak about that because it involves a little bit of geopolitics and it's hard for anyone to say that they are experts in predicting oil price. But when you look at the future curves for our projections, the curve that is available to the market, so we look at that. At the end of the day, that's related to inventory, plus expectation of production and demand in the short term.

But we think that, well, we have a constructive approach to oil. We don't think that the oil price will be very, very high, $70, $80 a barrel. We don't know. So, there is research pointing in every direction, but we tend to be constructive. We believe that the COVID pandemic will pass and the world will go back to demanding more oil. Now, how much of that will bring structural changes? Some people say there will be. We don't know. But we have a constructive view of oil.

Q - Bruce Barbosa {BIO 20917674 <GO>}

All right. Thank you very much.

Operator

Our next question comes from the web by Mr. Rodrigo Sequeira [ph]. Could you please give us an expectation of the closing of the 30% working interest of Petrobras, such as amounted to be paid at the closing, cash flow generated at the period data after closing and remaining oil inventory?

A - Emiliano Fernandes Lourenco Gomes

Hello, Rodrigo [ph]. This is a Emiliano. First, I would like to highlight that the transfer of rights, which is the most important event has happened. Now, ANP is analyzing the proposals of guarantee for abandonment. And based on the track record of the agency similar processes, we expect this process to be finalized by year-end in 2020. Regarding the amount to be paid at the closing, we are thinking about paying $25 million to $30 million with an oil inventory equivalent to $10 million to $15 million. So, these are the main points to answer your question. I am not the best person to answer about cash flow.

Operator

Our next question comes from Mr. Rodrigo Sequeira [ph].

Q - Unidentified Participant

Two questions. Can you speak a little about the company's growth strategy and expected time for organic growth tieback, Polvo campaign and Frade campaign? And can you speak about inorganic growth M&A? New Polvo campaigns will happen only after the tieback, or is it possible to drill new wells, infill drilling in the Eocene before the tieback? And when are you expecting to connect TBMT-10H?

A - Roberto Bernardes Monteiro {BIO 16616322 <GO>}

Hello, Rodrigo [ph]. I will try to divide growth into organic and inorganic growth as you did it yourself. Organic growth, what's the easiest to speak about? It will happen in the following way. We are now implementing the tieback project between Polvo and Tubarao Martelo. And this should be completed by mid-2021. And together with this project, we will start operating TBMT 10 well.

With TBMT 10, we can expect perhaps something a little better than what we had in TBMT 4, that we started producing recently. And why do we think it's going to be better? TBMT 10 is a totally different reservoir to TBMT 4. It's in a reservoir where we already had two producing wells and that's why TBMT 10 well will be more productive. So there is two things, both the tieback project and Tubarao Martelo number 10. These two projects will happen by mid-2021.

In the second half of 2021, we still have to make a decision whether we will be drilling an additional well in the Eocene reservoir at Polvo Field or whether we will move straight to Frade Field. But this is a decision that remains to be made. In the coming months, we should make a decision. There are pros and cons. Polvo, for example, requires little investment and you invest little and fast. But you have daily production of oil and reserves, which are well lower than what we have at Frade.

So, we haven't made a decision yet, but we'll be deciding later on perhaps along first quarter of next year. So in the next four months, I should say. But this tieback project, plus TBMT 10 will happen now. And then in the second half of next year, we should have either Polvo drilling another well or two new wells and then Frade. And our thinking is that we'll start working on Frade Field in the second half of next year. At the most in the end of next year. So, this is our idea about organic growth.

Now inorganic growth is a little harder because this is related to M&A projects and we cannot give you too much color on that, given the confidentiality nature of the business. What I can tell you though is that we have some possibilities in our pipeline and we expect we'll be successful at least in some of them in the coming months. But again, the company is rather diversified and rich. We are looking at some possible deals and it would be strange for PetroRio to be able to grow inorganically in the next six months to eight months.

Operator

Next question from Mr. Bruce Barbosa with Nord Research.

Q - Bruce Barbosa {BIO 20917674 <GO>}

Hello. Me again. Well, since people are following the US elections, let me ask more questions. How do you see the market for the issuance of that bond that you consider it in the past? And can you comment on the demand for capital, in case of a possible acquisition? So what are your plans for funding?

A - Roberto Bernardes Monteiro {BIO 16616322 <GO>}

Of course, regarding the bond, we went to the market. The conditions we found were not ideal. They were not the conditions we would have liked. And since we were thinking about refinancing the debt, we thought it would not be worthwhile getting a much more expensive debt, just because we would have a safer rollout. And that's why we didn't go through with the bond issue. It was a matter of cost.

Now, what is important is that now the company is 100% ready to issue, if we want to issue a bond 20 days from now. If we think that this makes sense that there is a demand, but the market changed or whatever, we can update the prospectus and very quickly, perhaps in a matter of 20 days. And we can access the market again. So the company is 100% ready to do it.

In terms of governance, in terms of auditing and everything, we've gone through all of the stages. So, we are 100% prepared. Regarding our capital structure, we always emphasize this. Our main indicator is net debt over EBITDA ratio. It's at 1.9 times. We had a moment when we were higher than 2.5 times, but we don't want to be at greater than 2.5 times or 2.75 times. I mean it might happen if we make an acquisition.

So, of course, you take on debt and you don't have the corresponding EBITDA, but these are technical things. But if we look at our business, we never want to have our net debt over EBITDA ratio greater than 2.5 times or 2.7 times. So, our capital structure will fit the size of the opportunity if it's something bigger.

Of course, in order to maintain this kind of debt, we'll have to go to the equity market, which is another market that we are ready to access. We have our income statement to revise, revisited for 2018, '19 and even the 2017 balance sheet and income state. It all fits the initial 2018 balance sheet. So it's all aligned. It's all sorted out. And we are ready to go one way or the other way. It really depends on a timing of the market. If we think it makes sense and depending on the size of the opportunity, if it's a smaller deal, perhaps we can fund it with the company's cash flow, close [ph] little debt that we can take on. So if it's a bigger deal, then we'll think about going to accessing the equity market.

Q - Bruce Barbosa {BIO 20917674 <GO>}

It's understood and it's very clear. Thank you very much.

Operator

Next question from the web, Mr. Rodrigo Sequeira [ph].

Q - Unidentified Participant

What is the strategy in Manati? Can you divest just like the other concessionaire did recently? Or are we thinking about buying Petrobras' working interest?

A - Roberto Bernardes Monteiro {BIO 16616322 <GO>}

Rodrigo, Manati Field is an asset that perhaps will change its operation. Instead of extracting gas, it can become a gas storage operation. In that context, of course, we consider. We have looked in the past that the possibility of acquiring more stake of Manati. I was always thinking about reducing costs, optimizing expenses, et cetera. But given this new possible modality, we have been thinking about the possibility of selling our stake of the asset at similar conditions. This would make sense for the company. This is something we've been discussing at the Board of Directors. But I would say that today, our trend would be to sell the asset if possible, rather than buying more interest of the asset.

Q - Unidentified Participant

Our next question comes from the web, Mr. Rodrigo Sequeira [ph]. Estimated CapEx for 2021 is around $314 million, which would go for the tiebacks connection of TBMT-10H three wells in Polvo and three wells in Frade. Is that correct?

A - Francisco Francilmar Fernandes {BIO 21185801 <GO>}

Hello, Rodrigo [ph]. This is Francilmar speaking. Let me try to clarify that. What we have today approved in certain in terms of next years' CapEx is the tieback between the fields. This is already happening. And that would cost $42 million in completion, in connection of TBMT 10, another $23 million. So that is already happening. The other projects, the Eocene reservoir wells at Polvo and the revitalization, considering three initial wells to be drilled at Frade, this is still to be defined. And we will decide on the sequence of these projects. So, that is the current scenario.

Operator

The next question is from Mr. Victor Schmidt of Fourth Sail Capital.

Q - Victor Schmidt {BIO 16519019 <GO>}

Why is it that the new TBMT wells started producing 10,000 barrels a day, but then dropped to 7,000 barrels daily and then increased again to 8,000? What can we expect looking forward?

A - Roberto Bernardes Monteiro {BIO 16616322 <GO>}

Hello, thank you for the question. It's a possibility for me to clarify. You see, TBMT 10 started operating, adding about 3,000 barrels of oil a day. And TBMT as a whole achieved 10,000 barrels. But then we started having a natural decline process. This reservoir was already producing via two wells. So the first -- the well started producing more, but then it follows the decline of the other two wells that shared the reservoir. It's currently at around 9,000 barrels or 9,200 barrels and it should remain at that level for a while. This is what to be expected until we have TBMT 10 producing. And that is a new reservoir and that should increase the production a little more. And this should happen by the end of the first half of 2021 or beginning of the second half of next year.

Operator

Our next question from the web, Mr. Rafael Ragazi with Nord Research.

Q - Rafael Ragazi

Hello. Despite a reduction in lifting cost, cost of goods sold grew more than the revenue in the quarter. Could you comment on that, more specifically on the acquisition of oil for resale and the reduction in the royalties line item, even with an increased production? Thank you.

A - Roberto Bernardes Monteiro {BIO 16616322 <GO>}

Rafael, regarding the lifting cost, it is exactly that slide that I explained on Tubarao Martelo. When we acquired the field, according to the contract, part of the economics of the field came with the chartering of the FPSO from Dommo in this quarter. A part of the economics came from that and not from the low cost. Because when you look at the cost of goods sold, COGS at Tubarao Martelo would be taking into account the chartering of the FPSO. So in the COGS, you have the chartering, increasing the COGS, negative value and then later you have positive values, the rental FPSO. So it's just accounting and we have to follow the contract. Since this was the agreement we had with Dommo in the past, this is what we did.

But the moment that we no longer have the FPSO chartered, the FPSO will no longer be chartered. It belongs to the company. It belongs to PetroRio now. So, we are going to see an improvement in the margin of Tubarao Martelo. So, this is the difference. It is what I tried to explain on that slide. I think it was number 13 or 14, not sure at. It was all because of the way in which we accounted for Tubarao Martelo.

As for the royalties, we paid 10% royalties on everything, with the exception of Manati, which is 7.5%, with the exception of Polvo. This last well that was drilled in the Eocene speaks a lot about it. It started producing 3,000 barrels. For that one. we paid 5%

royalties. And it is this mix, considering 5% of Polvo, 7.5% from Manati. This gives us the average royalties payment that you could see in our release.

Operator

Our next question comes from Mr. Bruce Barbosa with Nord Research.

Q - Bruce Barbosa {BIO 20917674 <GO>}

Hello again. I have a quick question regarding Frade Field. In the release, you wrote that we can expect approval in for coming months. I'll be waiting for CADE to approve this. Can we expect this for the fourth quarter or would this be for 2021? And with Frade starting production, we are going to have another strong reduction in lifting cost, right?

A - Emiliano Fernandes Lourenco Gomes

Okay. This is Emiliano. No, we don't need CADE's approval for that. In this case, we are awaiting authorization and approval by ANP. Both ANP approvals, including the approval of the transfer of rights has happened and the CADE approval has happened already before. We are just waiting for the analysis of the guarantee for abandonment, which is a fundamental phase for the closing. We estimate this -- we expect this to happen by year end.

A - Roberto Bernardes Monteiro {BIO 16616322 <GO>}

And there was a question about the lifting cost. And you're right, when we had this asset, we should have more reduction in our lifting cost. When we look at Frade and the Tubarao Martelo/Polvo, Frade has a more competitive lifting cost because we don't have a chartered FPSO. So, Frade should bring another little reduction in the lifting cost. So, we can have this additional reduction and another reduction in lifting cost that should happen in mid-2021, when we increase production with TBMT number 10 and when we stop leasing the FPSO at Polvo.

Q - Bruce Barbosa {BIO 20917674 <GO>}

Are you giving your guidance on the lifting cost considering TBMT, as well as the last part of Frade?

A - Roberto Bernardes Monteiro {BIO 16616322 <GO>}

No. But you can do it easily. When we get to mid-2021, our lifting cost in absolute terms should be between a little under $70 million a year for Frade and a little under $70 million for the Polvo plus Tubaro Martelo system. So, we should get a consolidated number of $114 million annually for the whole operation. And then, you divide that by the number of barrels of oil. And then, we'll give you a number.

Today, we are running 100% of Frade at $63 million, and the Tubaro Martelo plus Polvo cluster, we are running at a lifting cost of $120 million a year. When we have the Polvo FPSO, we have the leasing plus diesel, plus personnel, that should cost about $50 million.

So it will drop from $120 million to $70 million. So, I think $70 million plus $70 million, that will give us $140 million per year.

Q - Bruce Barbosa {BIO 20917674 <GO>}

I understood. Thank you very much.

A - Roberto Bernardes Monteiro {BIO 16616322 <GO>}

Thank you.

Operator

We are now closing the question-and-answer session. I will turn the floor to Mr. Roberto Monteiro, to proceed with his closing statements. Please go ahead, sir.

A - Roberto Bernardes Monteiro {BIO 16616322 <GO>}

I'd like to thank all of you for participating in another conference call. Thank you very much for your support to the company. My special thanks go again to PetroRio's employees. We see that many of them are participating in this conference call. Most of our employees are shareholders of the company. So, thank you very much to all of you and I hope to see you again in three months.

Operator

That does conclude PetroRio's conference call for today. Thank you very much for your participation and have a good day.