

Q2 2015 Earnings Call

Company Participants

- Blener Mayhew, New Business Development and Investor Relations Officer

Other Participants

- Unidentified Participant

Presentation

Operator

Good afternoon ladies and gentlemen. Welcome to the conference call for the Second Quarter 2015 Results of PetroRio Participacoes. Thank you for standing by. At this time, all participants are in listen-only mode. Later we will conduct a question-and-answer session for analysts and investors, wherein instructions to participate will be given at that time. (Operator Instructions)

This event is also being broadcasted simultaneously over the Internet and may be accessed through PetroRio's Investor Relations website at www.petroriosacom.br/ir by clicking on the banner 2Q 15 Earnings Release. As a reminder, this conference is being recorded and the presentation is available to download shortly after it's presented, also through PetroRio's Investor Relations website.

Before proceeding, let me mention that forward-looking statements that may be made during this conference call related 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 which 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. Blener Mayhew, New Business Development and Investor Relations Officer of PetroRio. Mr. Mayhew, you may go ahead.

Blener Mayhew {BIO 19502444 <GO>}

Good afternoon, everybody. I would like to thank all of you for joining this conference call and for your attention, we're here today to present to you our latest achievements and the results of the second quarter, and also to share with you our expectations for the foreseeable future.

Firstly, I would like to start that PetroRio is the whole new company now, different from the old HRT which was very much focused on exploration both in our commercial model and in our business model as well as in our people and organizational culture. Our company is now using merit-based system. We have a goal and we've optimized, and we have a huge financial discipline because of that, in the latest results that we have achieved with the restructuring of the first quarter in our cost reduction initiative.

I must remind you that we currently have a challenging macroeconomic environment worldwide. Brent price is very volatile, commodity prices have dropped more than 50% in the last 12 months. For a company whose main revenue -- the only revenue source is the sale of commodities which will engage a challenging movement. Also related to the price of commodities in the recent weeks and months, we have new information.

Second, governing the way an increase in the Brent oil price. We see China slowdown, we see the end of (inaudible) and is in critical crisis in Brazil, all of that increased the challenge of the company to generate cash. However, we remain very optimistic, because we were able to lower the lifting cost to \$50 in it, the price of the oil barrel drop, we will renegotiate our contract, first to be able to renegotiate and reduce our costs even further.

The moment of stress in the market as we are living now that's one good opportunity that's simply derived particularly to buy production assets which otherwise would not be available for sale. We are considering assets not only belonging to Petrobras, but good players in Brazil as well, and as it was announced previously in the Northern city.

As you can see from the first and the second quarter, there was a substantial cost reduction, a good deal about [ph] the contract, which was renegotiated in the first quarter, contracts where suppliers, employee termination, international offices abroad which were closed down, a good deal of the (inaudible) negotiations were starting to happen in June and July of this year. So now in the second quarter and in the third quarter, that's when we'll start seeing a cost reduction in full effect.

Oil lifting cost for the period was \$33 per barrel and this was indeed a very good achievement for the company. This was due not only through a cost reduction, but also due given the natural production decline at the field, and this plays against us in this equation. And as an example, in 2014, the company has to sell oil at \$95, minus \$10 of discount, and our revenue was \$85 in a Brent costing \$95 and practically all of that money would go to pay for our expenses at Polvo, project expenses and corporate expenses.

Back then in 2014, if we work today with the same cost structure with the Brent costing \$50 per barrel, the company would have a considerable cash burn. So this comes to show how management was really thinking ahead and already thinking before what would

FINAL

happen even before the Brent price fell so much, and we were positive in getting cost reduction, so that we can get this result of \$33 per barrel.

Just to give you an example, Polvo, at the time of the old operator, in 2013, it cost \$230 million. Our cost today for 2015 is \$115 million. So 50% of the cost of 2013. Now obviously this is not something which (inaudible). We reduced the level in 2015, continued in this asset in 2015 and we believe that we are quite close to achieving a maximum reduction in cost for Polvo. We want to reduce from \$115 million to \$110 million. This will be a reduction of over 50% compared to the cost in the hands of the old operator in 2013. And just like we are pursuing an improvement in operating costs year-after-year, we improved our uptime goal, uptime is the time that the field is working and producing oil. Our uptime in 2015 is 98.5%, it is the best in the Brazilian industry in the Campos Basin. We surpassed our own record of last year of 93%. On average, the uptime of the old operator was 80%, 80. All of that is achieved not only because we are better than these old operator or because we have more financial discipline, this is not yet always our only asset, which is only method [ph] we can be more focused and be more attention (inaudible) to another operator did not mean so much. That is a small company as an independent producer, we pay full attention to Polvo.

Now talking about Polvo. The company tends to make an investment in re-entries of Polvo and the application of polymer, the company is ready already to make this kind of investment. The only thing that is holding us back is the negotiation with Maersk. Maersk does not want to develop the Polvo field and the approval of the deal with Maersk is fundamental, not only for the company to own a 100% of the assets, but also for the company to invest in the field as planned. Hopefully by year end, we will have three re-entries, we will invest in polymers, we are talking about investing \$13 million with that endeavor.

Now, I don't want to give you any guidance in terms of production increase, because that will depend a lot on the geology involved. We are still working with very conservative figures. And we did some talking about this, the Maersk deal, we are continuing our conversations with the ANP. This is an ongoing effort and we're trying to put together a provision for the future abandonment proposal, but we won't -- we don't want this to hit investment of the company and the cash position of the company, these conversations haven't [ph] followed since January, or it actually started in April of 2013.

With the reduction in Brent prices, negotiations become another direction, and now we are trying to have ANP to accept more flexible points, so that we can finally complete the purchase from Maersk. We hope that by year-end this will be resolved.

Talking about Bijupira and Salema fields. The company acquired the 20% remaining stake which belongs to Petrobras. We acquired 80% from Shell, 20% from Petrobras and now we will own a 100% in Bijupira and Salema fields, and also a few FPSO Fluminense. It's important to remind you that the 20% stake of Petrobras were negotiated with an effective date of January 1st of 2015, the same date negotiated with Shell was approved from January to date, part of the remaining balance that we should pay for the asset is already been paid by the fields production. So when ANP approved, as a deal of the 125 million will be already paid by the sale of oil commitment in that daily sales.

FINAL

As for Solimoes, ANP has approved the sale of the blocks to Rosneft on July 1. We expect to receive 50% of that amount now in the third quarter of 2015, the second portion of the remaining 50% should be due in May of next year. The company was very, very pleased with this transaction, with this deal, it was quickly approved by ANP and this cash paid by Rosneft will reinforce our cash, and this can be converted in M&A projects, acquisition of fields or even investments in Bijupira and Salema fields. So this is -- funds that will be better used by PetroRio, if compared to investing in exploring Solimoes at least in accordance with our current strategy.

In Namibia, there were some renegotiated conditions with the local government to renew certain exploratory licenses. These pre-conditions were negotiated, at the same time that initial licenses were given, if I'm not mistaken in 2012. However, the scenario is totally different now, international pattern [ph] have changed, international oil prices had declined and these conditions will still impact to the old scenario. This will give you remained -- interested in renewing licenses in Namibia.

However, we will not fulfill the minimum exploration activity that the Namibian government is now requiring, but this was applicable to an old scenario. So now the company is engaging in conversations with the local government to get some flexibility, and once we get to a common denominator, we would be interested in renewing certain exploratory licenses. At the current conditions, it would be infeasible, not only for PetroRio, but for all other companies to invest in Namibia.

This company has a good cash position BRL356 million showing that the company is focused on not spending cash. Our cash level has remained stable quarter-on-quarter and quarter after quarter, and this is constant hard work by all of our departments to maintain our cash position at the current Brent price. We believe that with Bijupira and Salema fields, the cost composition of the company will change, we will have a second asset to send on and Bijupira and Salema have a bigger area than Polvo. The oil discount is lower around \$4, for Polvo its \$10. And in Bijupira, we own the FPSO, in other words, we will not have to pay to leave the equipment. So at these two points when we're talking about cost of about \$25 per barrel in Bijupira and Salema fields.

And this considering the asset of this in the hands of Shell, if you think about potential cost reduction that we applied at Polvo, the sky is the limit. And so, these two assets combined for 2016, and the company expects that we will be able to generate cash, even with Brent price at \$50.

And I'd like to go back to something I mentioned in the beginning. If the market remains at \$50 for one, two, three years, for this industry is very dynamic, the industry we work (inaudible) and service costs will decline substantially and this will allow the company to renegotiate contract even more and to get even higher margins if the Brent price remains at \$50. However, we do not to believe that prices will remain depreciated for a lot longer. We believe that in the beginning of 2016 we will start [ph] new recovery in international prices.

Now with that, I end and we remain available for questions-and-answers, we have Guilherme Marques with me, our CFO and he would like to entertain your questions. Thank you.

Questions And Answers

Operator

Ladies and gentlemen, we will now begin the Q&A session for analysts and investors. (Operator Instructions) Our first question comes from Jeffrey [ph]. Please go ahead sir.

Q - Unidentified Participant

Good afternoon. I would like to know, what is the company's strategy for the 13th ANP Round? And is the company remains interested in Petrobras assets which might be sold as part of the Petrobras investment plan? Thank you.

A - Blener Mayhew {BIO 19502444 <GO>}

Yes, we will be participating in ANP's 13th round. And this was published last week by ANP, we were approved in their selection list, but since, the company's main focus now is production, as opposed to exploration, we will be minority players in these blocks. I will not disclose more detail on that, because that's a very strategic for the company that exploration risk will be small, will remain small at PetroRio at least for now. As for Petrobras, yes, we remain engaged in conversations with them. We are looking at some Petrobras assets, production assets, but so far there is nothing found [ph], we are just engaged in informal conversation.

Operator

(Operator Instructions) You may proceed.

A - Blener Mayhew {BIO 19502444 <GO>}

Well again, I would like to thank everybody for your availability, time and attention. If you have any further questions, we will remain available through our IR department. Thank you very much. Have a good day.

Operator

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

This transcript may not be 100 percent accurate and may contain misspellings and other inaccuracies. This transcript is provided "as is", without express or implied warranties of any kind. Bloomberg retains all rights to this transcript and provides it solely for your personal, non-commercial use. Bloomberg, its suppliers and third-party agents shall have

no liability for errors in this transcript or for lost profits, losses, or direct, indirect, incidental, consequential, special or punitive damages in connection with the furnishing, performance or use of such transcript. Neither the information nor any opinion expressed in this transcript constitutes a solicitation of the purchase or sale of securities or commodities. Any opinion expressed in the transcript does not necessarily reflect the views of Bloomberg LP. © COPYRIGHT 2022, BLOOMBERG LP. All rights reserved. Any reproduction, redistribution or retransmission is expressly prohibited.

FINAL

Bloomberg Transcript