

Q1 2017 Earnings Call

Company Participants

- Hugo Repsold, Head-Human Resources, HSE and Services Director
- Isabela Mesquita Carneiro da Rocha, Executive Manager-Investor Relations
- Ivan de Souza Monteiro, Chief Financial & Investor Relations Officer
- Jorge Celestino Ramos, Chief Refining & Natural Gas Officer
- Luiz Nelson Guedes de Carvalho, Chairman
- Solange da Silva Guedes, Chief Exploration & Production Officer

Other Participants

- André Hachem, Analyst
- André Natal, Analyst
- Christian Audi, Analyst
- Lilyanna Yang, Analyst
- Luiz Felipe Carvalho, Analyst
- Luiz Felipe Guanais, Analyst
- Rodolfo de Angele, Analyst
- Vicente Falanga Neto, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good morning, ladies and gentlemen. Welcome to Petrobras Conference Call with Analysts and Investors for the presentation concerning the first quarter of 2017 results. We would like to inform you that participants will be listening to the conference only during the company's presentation which will be conducted in Portuguese with simultaneous translation into English. Following the presentation, a Q&A session will begin in Portuguese and in English, during which instructions on how to participate will be provided.

Today with us, we have Mr. Ivan de Souza Monteiro, Petrobras' Chief Financial and Investor Relations Officer; Ms. Solange da Silva Guedes, Chief Exploration and Production Officer; Mr. Jorge Celestino Ramos, Chief Refining and Natural Gas Officer; Mr. Hugo Repsold Jr., Chief Human Resources Agency and Services Officer; and Mr. Nelson Luiz Costa Silva, Chief Strategy Organization and Management System Officer as well as other company executives.

We would like to remind you that this meeting is being recorded, and please be mindful of slide number two which contains a notice to shareholders and investors. The words believe, expect, and similar ones related to projections and targets are mere forecasts based on the expectations of the executives regarding the future of Petrobras.

To begin, we will hear Mrs. Isabela Cameiro da Rocha, Executive Manager of Investor Relations, who will start the presentation about the first quarter of 2017 results. Afterwards, questions from participants will be answered. Please, Mrs. Isabela Cameiro da Rocha, you may proceed.

Isabela Mesquita Carneiro da Rocha {BIO 19730664 <GO>}

Good afternoon, everyone. I would like to thank you all for your presence and go into detail about the results of the first quarter of 2017. The main highlights of the quarter on slide number three. The first one is the most important metric which is the safety metrics when we reached a total recordable injury frequency rate of 1.24, a reduction of 26% on a year-on-year basis.

Talking about the economic financial results, we have an ongoing improvement compared to last year, the same period, in which we have a BRL 4.45 billion net income reversing the previous loss. Operating income, BRL 14.27 billion, 75% higher on a year-on-year basis. And the highlight, the EBITDA increase of 19%, reaching BRL 25.25 billion, and this is a major highlight because this is the highest historically recorded ever. The EBITDA margin, 37%, which is also the highest since the second quarter of 2011. Free cash flow, BRL 13.37 billion, positive for eight quarters in a row and represent six times the amount posted in the same period last year.

The effort of deleveraging with prepayment and amortizations of debt and the active liability management leads to a reduction of 5% in gross debt in reais and 3% in dollars. Comparing to December 2016, we had an increase in the average debt duration from 7.46 to 7.61 years. And a reduction in our metrics, a very important financial metric, which is the net debt EBITDA ratio which went from 3.54 to 3.24, reducing our leverage to 54%.

Going to the next slide, we can see the operating highlights and we would like to highlight our total production of 2.8 kbpd per day, 7% higher than the previous year. And considering only the production of oil in Brazil, we reached 2.182 million barrels per day, 10% higher than the first quarter of 2016. There was a drop of 5% in the sale of oil products in Brazil. We sold about 1.9 million barrels per day of oil products. Petrobras consolidates its position as strong net exporter due to the increase in exports, 72%, and reduction also in imports by 40%. And the higher exports of oil had higher prices in the market be it because of the higher Brent price, be it because of the appreciation of the domestic oil stream which can be seen by the average discount of our basket of \$3 per barrel for Brent. And these factors helped offset the drop in sales in the domestic market.

In terms of efficiency, our cost efficiency is also a major relevance this quarter and reduced 18% in our manageable operating costs and 27% in SG&A. And also, we highlight the reduction in our head count by 17% during this period. So these are the main financial

highlights and operating highlights, and now we would like to talk about slide number six with more details in which we talk about growth of production, 2.8 million barrels of oil equivalent per day.

Even after the disposal of our company in Argentina that occurred last year, we saw an increase in production. And a special highlight is the pre-salt that we expect with a profile of growth as you can see on this chart. We had a record of 1.34 million barrel of oils per day in the pre-salt layer operated by Petrobras which has been contributing to our experience in this layer and the learning process.

Going to slide number seven. We see the new units that will come onstream this year. Two units in Lula field, P-66 that is already there in location waiting for the environmental agency to start production, and P-67 which is in the shipyard in China finishing the commissioning and should start operation this year. We have the production of Libra through the extended well tests. In July, we should have the first oil coming from this unit. And also our platform that is in Tataruga Verde field that should start operations in the fourth quarter as well of this year.

Now going to slide number eight. We have the integration of upstream with downstream and with the participation of domestic oil in the throughput, 95%. And below, you can see the production of more noble oil product - gasoline, diesel, and jet fuel - around 70% of yield in these oil products. On the right, you see the production of oil products, 1.8 million barrels per day, a reduction of 8% vis-à-vis last year due to the reduction in the volume of sales, 1.9 million barrels per day in this quarter. And this reduction of the sales volume is due to two factors, the drop in demand and this factor was more important in the case of diesel, and also the higher import by third party vendors which was very important in the case of gasoline.

Now going to slide number nine, we have the balance of liquids. Export of 609,000 barrels per day of oil and 170,000 barrels per day of oil products. 779,000 barrels per day of exports. A growing trend of exports and decrease in imports. We had a positive liquid balance of 489,000 barrels per day. Basically, import of oil that happened in the first quarter was only for the production of lubricant. There was no diesel imports, and import of gasoline was very small.

On slide number 10, we talk about the supply and demand balance for natural gas and the highlights were the higher supply of gas and the new demand of thermoelectric, 73 million cubic meters per day of demand. 52 million cubic meters per day were met by production of Petrobras in Brazil, 19 million cubic meters per day imported from Bolivia, and a minimum import of liquefied natural gas. So this has been the profile of supply and demand with the increase in profitability of the business in this area of gas and energy.

Now going to the indicators on slide number 12. We highlight the Brent and the exchange rate increases with the raise in Brent. \$54 on average for the quarter and BRL 3.15 exchange rate.

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Now, going to our results on the next slide. We highlight our gross profit of BRL 23.8 billion, quite higher to the previous one. And also, in spite of the lower sales of oil products in Brazil, there were three important factors coming into play. The increase in production, increase in exports at better prices in the market, and lower expenses with the import of oil and natural gas. In terms of the operating income, reduction of operating expenses that we will be focusing afterwards. BRL 14.5 billion (sic) [BRL 14.3 billion] of operating income, a very important increase vis-à-vis last year. And the net financial result, we had an impact of the exchange rate variation between the dollar and the euro, and our higher exposure is to the euro in our financial result.

In terms of net income, BRL 4.45 billion in the quarter, much higher than last year and reversing the loss of last year, in fact. And in terms of net income, I would like to highlight the BR net income, our distribution company, positive for the second consecutive quarter after a period of successive losses. And even with a small reduction of market share, we had good results in our BR Distribuidora.

On slide 14, we see that the growth of the EBITDA reached record historical level of BRL 25.25 billion, and this is due to lower expenses with the import of gas and oil and lower operating expenses. And the EBITDA margin was the highest since the second quarter of 2009.

Now, going to slide number 15. We have the free cash flow, BRL 13.4 billion, positive for the eighth quarter in a row. Thanks to the increase in our operating generation and reduction in investments of 34%. I would like to mention that the free cash flow was more than enough to cover interest expense payments of BRL 5.2 billion, and we had something left over for our deleverage.

Now, slide number 16 where we show manageable operating expenses with an important drop of 18% vis-à-vis last year, and we would like to highlight that this level will not persist for the following reasons. Reduction in our head count by means of our voluntary separating incentive plan, represents a sustainable gain and 65,220 employees at the end of this quarter. We will expect withdrawals up to the middle of this year if we consider this reduction was 60,000 people between our own employees and service providers.

In talking about selling expenses, this reduction that we saw came from the volume sold and also from the effect of the exchange rate, and for the next two quarters we're finalizing that this should be repeated because of the payment of the tariff to NTS that has the south and southeast area and we sold to Brookfield. So we have 10% stake in this company. And as the close was on April 4, part of the second quarter will have this additional expense.

Regarding G&A, there was a drop and benefiting from a parcel of reversion vis-à-vis a provision made by the collective bargaining agreement. So part of this drop has a non-recurring part, so that is to say a part that will not be repeated. I would like to mention the exploratory cost that were lower because there have been no write-offs of dry holes or sub-commercial wells which is not natural. What is natural is to have some recognition of dry holes. So because of all these reasons, we expect a reduction of the manageable

costs reflecting our efforts, but we do not expect this level to be as low as we had this quarter.

On the next slide, we also had the contribution to this drop in operating costs. The drop in lifting cost from BRL 32.8 per barrel in this quarter, and here we have the amount in dollar and in reais. And net of the exchange rate effect, there was a drop in dollars in the lifting cost and the refining cost was impacted by the reduction of the throughput in refineries. And the cost of refining is, of course, in reais. Most of it is personnel and another collective bargaining agreement with an increase in wages and productivity gains linked to activities be it of exploration.

And now going to the next slide. We bring the reduction of our leverage and our liability management and with the extension of duration. Without an increase in the average cost, as you can see on the lower part, and the continuous effort of reducing the debt by prepayment and amortization helps us in reducing our leverage, as you can see, in terms of gross debt and net debt as well

On the next slide, we talk about the net debt EBITDA ratio, 3.24 times from 5.11 times. On the next slide, the debt amortization schedule for the next few years. We see still a concentration of debt in 2019 but the schedule has a level of amortization that is possible when it is in our plan. It's important to say that we have at our disposal all funding alternatives with decreasing costs even in spite of the loss of the investment grade.

And on the last slide, we talk about liquidity for this year. Our projection maintained the same level of Brent that we had in the first quarter. We expect an operating generation of BRL 30 billion (sic) [\$30 billion], and earmarking BRL 5 billion (sic) [\$5 billion] for judicial guarantees, and this cost is in dollars. Interest and amortization, \$17 billion, being \$6 billion in the tender offer that we have already carried out in the first quarter in terms of investment expected. We are projecting \$17 billion for the year, divestment of \$8 billion, highlighting the fact that all these divestments have already been signed and we're only waiting for the closing and the inflow of cash so there is no risk in the start of divestment for this year. The level of borrowings, \$4 billion, already carried out in the first quarter with a cash balance of \$19 billion, very comfortable for this year.

I would like to thank you very much for your attention, and now we would like start our Q&A session.

Q&A

Operator

Now, we will start the Q&A session. We would like to ask each participant to ask two questions maximum in a clear manner. So that the executives may answer them, we would like to ask you not to use the speaker phone. Questions asked in English will be heard by all participants in the original language and answered by the executives in Portuguese with simultaneous translation into English. Our first question comes from Rodolfo Angele, JPMorgan.

Q - Rodolfo de Angele {BIO 1541593 <GO>}

Hello. I have two questions. First, I would like to ask the management. Now that the company will have a few days to choose to participate or not in the pre-salt auctions, I don't think that you can tell us everything that you're going to do, but I think that we would like to hear how are you seeing these options? How do you differentiate between the two pre-salt auctions? What can we expect in terms of strategy for us to see your decisions to bid or not in the upcoming auctions? That's my first question.

My second question, and I want to contextualize it. We have seen investors very concerned about crude oil prices and, of course, we see that you're sparing no efforts to control your expenses. So what else is there in the pipeline? Can we expect more coming up? Isabela explained some effects that we can expect for the first quarter. But in terms of costs, what else can we expect particularly because we see the company facing now a lower crude oil price?

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

This is Ivan speaking, Rodolfo. Thank you for the questions. I'm going to give the floor to Solange to answer your first question.

A - Solange da Silva Guedes {BIO 16088234 <GO>}

This is Solange. Good morning, Rodolfo. As we said yesterday in our press conference, Petrobras is following opportunities up close, opportunities offered by the Brazilian Petroleum Agency, ANP, in the first two sharing rounds and the concession rounds, the so-called 14th round that will take place soon. Petrobras intends to rebuild its exploration portfolio, and in that sense we're following these projects with a lot of attention. Our strategy, it will become clearer as the auctions come up.

A - Operator

Rodolfo, good morning. Obviously, now as you mentioned, the first results of a project to reduce cost and to generate value through those four pillars of the plan: revenue, OpEx, CapEx reduction, partnerships and divestments. We adopted the zero-based budget method because it was one way to reboot the company, not only because of the problems that we had but because of the strong adjustment that we had to make given a lower Brent price. And we're just getting started in this journey. Our focus remains the same, both to reduce our accidents and also to improve our financial indicators. This effort will continue. Zero-based budget continues to be the methodology used particularly to reduce costs. Not only do we look at reducing costs of each and every activity, but we're also discarding everything that does not contribute to the delivery of the plan and to improve our indirect indices.

These are the first steps in a journey. I am glad that the positive results are surfacing but we're not going to relax our efforts. They will continue. Efforts to do only the activities that will help us deliver our plan and to improve safety of our employees, and we'll continue to make an effort to reduce costs, improve productivity through the renegotiation of contracts, and techniques that will allow us to do everything that needs to be done at lower costs and less capital investment.

Our next question comes from Felipe Guanais, Bradesco.

Q - Luiz Felipe Guanais {BIO 19933939 <GO>}

Good morning. I would like to get an update in terms of drivers in the FPSO to reduce accidents because we saw that some accidents happened in recent months. I would like to know have these been solved and could these accidents happen in other units that deal with extraction of oil, lifting of oil, and CO2.

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

Felipe, I'm sorry to interrupt but we could not understand your first question. The sound is muffled. Could you please repeat and, perhaps, speak slowly and repeat the first question? And I'm sorry to interrupt you.

Q - Luiz Felipe Guanais {BIO 19933939 <GO>}

Better now, Ivan?

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

Yes. Better. Thank you.

Q - Luiz Felipe Guanais {BIO 19933939 <GO>}

My first question is related to an accident in the risers of the FPSO at Lula. Some accidents were reported to be linked to corrosion, and I would like to understand if this has been solved and whether this can happen in other units that deal with high CO2 concentration oils. My second question has to do with the cutting down of costs. Could you give us more granularity regarding the factors leading to such strong cost cuts that we find in the first quarter. And since Nelson is here, perhaps he could give us more color on the zero-based budget, ZBB.

And another question, if I may, regarding CapEx. CapEx annualized will be \$12.5 billion, way below the guidance for 2017. So could you please explain the reason leading to that? And the reason I ask is that another concern of investors is how sustainable is this low CapEx vis-à-vis the impact on production later on in the future, more long-term?

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

Thank you, Felipe. The first and third questions, Solange will answer. And then the second question will be answered by Officer Nelson.

A - Solange da Silva Guedes {BIO 16088234 <GO>}

Good morning, Felipe. This is Solange speaking. I will try to answer your first question because I understood, I guess, part of the question that you asked. It seems that you're referring to some events related to the risers in the pre-salt. What I can share with you is there were two events linked to a new phenomenon which happened in a non-operating riser. It happened in the end of 2016 with a riser that was not being used, and now in January of 2017 with another riser, both being used for gas injection. So we're working

very intensely with our manufacturers, with labs, with both Brazilian and international technicians.

Apparently, this is a new event in the industry. In the first assessment we had, it is restricted only to a very particular situation, events that have very particular conditions that can happen in very specific situations of gas handling, and handling of gas with high concentration of CO2. Again, these are localized events. We are overseeing some other risers that operate in the same operating conditions but, again, this is something that we're working on. It's part of our operational assessment. This was not an accident. One of the risers, as I mentioned, was not being used, was not operational. There was no impact to the environment or to production.

In your third question, I think you were referring to investments, that we're investing less now compared to what was in the guidance. Our conclusion was that, objectively speaking, in the first quarter of 2017, fortunately we had a reduction and one quarter of that reduction is linked to the execution at lower cost. Actually, this is one of the pillars of our plan, to have efficient CapEx. There's a small amount, about 20% related to delays in environmental licensing and the rest is linked to the delay or postponement of payments that have no relationship with production. So our better assessment today is that in the short-term in 2017 there will be no impact of this reduction in CapEx and we have no justifications to change the estimates other than what was in the plan.

A - Luiz Nelson Guedes de Carvalho {BIO 7487095 <GO>}

This is Nelson, Felipe. Giving more color in how we are operating, there was that first effort to have the scorecards - more than 7,000 scorecards - and a lot of goals, sub-goals so as to deliver our top metrics, reducing leverage and safety. But in addition to the 7,000 scorecards, I would like to remind you that every Petrobras employee is being managed with their own individual goals. We're very much focused on delivering on our metrics and goals.

How does this works? We have a leadership committee and this committee meets weekly to see if we're deviating from our metrics, the ones that I mentioned. And this committee works and acts whenever we find a deviation, and we have to find the root cause whenever possible we find the root cause. And then at the level of the management, we have a directive committee with the participation of all the management officers, the members of the leadership committee, and all of that contribute firstly on the standard metrics.

And ZBB. We're measuring performance always adjusted to the assumptions of the plan. So we remove exchange rate and other things that are out of our control so that we can have the right assessment. And then once every quarter, we discuss this at the board level our quarterly results. So as you can see, this is very thorough work with weekly control levels. Obviously, we have daily control at the operational level. So this is very granular work involving from the Board of Directors every three months, to the management once a month, the leadership committee, and ZBB team weekly, in addition to the daily assessment that we do at the operational level. This is how we work.

Q - Luiz Felipe Guanais {BIO 19933939 <GO>}

This is perfect. Thank you. One follow-up question about ZBB. Is there any expectation then zero-based budget will be 100% implemented or it is implemented?

A - Operator

Here, we have the execution discipline, Felipe. The methodologies implemented, but over time we can refine it. This is the first quarter, as I said. These are just the first steps of a very long journey, and execution is the key of our success to deliver the plan. The cost reduction results that we had in this quarter are fortunately going a little beyond what we had expected in the plan, but it doesn't mean that we're not going to continue to do everything in our power to continue to capture cost reductions in the future.

We would like to ask the participants to ask their questions slowly.

A question coming from Christian Audi with Santander.

Q - Christian Audi {BIO 1825501 <GO>}

Good morning and congratulations even on the results. I have two questions. The first is related to deleverage and sale of assets. Do you continue to deleverage the company even without selling assets, I guess, right? So my question is, could this lead to an adjustment of your goals to sell assets or not given that you're able to deleverage the company even without selling assets more recently, and do you expect to resume sale of assets more towards the second half of the year?

My second question is related to production CapEx. It became clear on slide 21 that you lowered the CapEx to this level of \$17 billion, and I would like to understand the reasons behind that. And the impact of that, none on 2017 production. But if it is a continuous CapEx reduction, perhaps the impact will be felt in 2018 production. Could Solange enlighten me, please, about that?

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

Thank you, Christian. No, there will be no changes. The last material fact about divestments of the company confirmed our goal of \$21 billion. There was no change to that. And it's always important to mention the program in a context. It has a strategic context in our business and management plan. The company declared that we will prioritize investments in E&P and in the pre-salt. In addition, the company, in its material fact disclosure, we mentioned some assets, Pasadena, and some assets in Africa that the company will divest from.

So the fact that we had a better performance will not change the attitude of the company given our strategic decision or our goal to deleverage. We have to reach the goal by December 2018. As our CEO, Pedro Parente mentioned, even if we reach that goal beforehand, still we would be in a uncomfortable condition in terms of the goals to deleverage. So we will definitely not stop this trajectory. This is the first landmark, great. If

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we can bring things forward, great. But the company will not stop there because compared to the industry, we still need to improve our metrics as you probably know.

And as for your question about CapEx, I will turn the floor to Officer Solange.

A - Solange da Silva Guedes {BIO 16088234 <GO>}

Good morning, Christian. Thank you for the question and your comments. In answering a question prior to yours, I was explaining the events that led us to change our projection from \$20 billion to \$17 billion investment in 2017. I've stressed, and I repeat, that there is a part of that coming from optimization and a part of that coming from postponements. And these delays and postponements are not necessarily linked to production, but to disbursements and payments that Petrobras planned to do along 2017, but these payments will not be made in 2017. And this is one of the reasons that led to this reduction. Of those events, for example, related to environmental licensing processes that made us stop allocating resources and payments because the licensing process is not complete, with possible impact on production, we're mitigating these impacts.

In that sense, I'll stress that we maintain our production curve estimate for 2017. We do not envision any significant impact in our goals announced in the horizon, our business and management plan.

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

Christian, just to add to your question. Something I forgot before. This is Ivan speaking. Regarding when we're going to have a return, the company has been working intensely since the decision by TCU, the federal auditing court decision. We've been working, I don't know if you will remember, we decided to resume all projects and to apply a systematic approach to all of them. In the beginning, we have to identify the assets and we have to prepare assets. We have to identify the strategy together with the business area of the company, and how to best present the strategy to the market. Then, we have to define the criteria on how to prepare the teasers and we're working intensely and expect that we can disclose information to the market in the first half of the year in terms of which assets will be part of our divestiture portfolio.

Q - Christian Audi {BIO 1825501 <GO>}

Okay. Thank you very much.

A - Operator

Thank you, Christian.

Our next question comes from André Natal, Credit Suisse.

Q - André Natal

Thank you very much for allowing these questions. And, again, I'd like to join the others in congratulating you on very strong results. My first question is about the Voluntary

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Separation Incentive program, PIDV. I'd like you to talk about the program because we started seeing people joining last year, but people are leaving the company little by little. You have provisioned most of the cost for this last year. And as I understood, now there were some reversals of that. I understand that these are people who decided not to join the program. So I guess the cost reduction coming from PIDV is coming little by little. So could you explain how many people left along the first quarter, how many people gave it up, and how many people are expected to leave along the second quarter? How much of the intended cost reduction that you announced at the beginning of the program has materialized and to what extent this can materialize in the coming quarters? Because I understand that the first time that we would see a quarter with a complete benefit of this would be the third quarter. I don't know if I understood this right, but that's what I understood.

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

André, this is Ivan. I'll give the floor to Officer Hugo. Thank you for the congratulations. I'll give your questions to Officer Hugo.

Q - André Natal

Well my goal was to ask only one question, but I guess asked too many.

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

No problem. Officer Hugo will answer your question.

A - Hugo Repsold {BIO 19059342 <GO>}

André, thank you for the nice words. I will try to give you a general overview of PIDV. The Voluntary Separation Incentive program, actually, there were two programs. One that started in 2014, and it hasn't finished yet - in other words, there are still employees that will leave as a consequence of joining the PIDV in 2014, and there was a second one created on 2016. So I'm going to give you the numbers for the 2014 PIDV and for the 2016 PIDV. And you're correct when you say that the deadline for PIDV would be May, but we're still going to take June and July to operationalize some of employees leaving because there was a greater concentration more towards close to the deadline. So to operationalize these terminations, we should use June and July for that. And then for the third quarter, that's when we're going to see the global effect of that.

So the 2014 numbers, we had a total of - actually, we are in a position where we have 6,871 people who have already left and there are still 292 to leave the company. 420 people gave it up, and we had a total of about 7,600 people leaving under the 2014 PIDV. For the 2016, 7,659 have left, 2,591 still have to leave the company. That's why it's so difficult to handle all of these terminations in these last few months, and that's why we should take until June, July to end everything. Of this program, 1,400 people - 1,415 to be exact - gave it up.

So to give you global numbers, so far 14,500 people have left Petrobras through the PIDV. Adding both programs, there are still 2,883 people who are leaving the company soon and 1,835 gave it up, had joined and went back. We should have about 19,500 people

altogether leaving. Again, there are some inaccuracies here because some people died and some people got sick and cannot be terminated. So there are some differences, but the global number would be 19,500, 14,500 have left, and the remaining will leave by the end of July.

Now, the objective effect of these people leaving on cost, I cannot give you this effect now but we can calculate and we can give it to you later.

Q - André Natal

Excellent. Thank you very much.

A - Operator

André, your second question? What was your second question?

Q - André Natal

I believe my question will be to Mrs. Guedes, Solange Guedes. It has to do with the exploratory expenses that were quite lower than the historical levels. So it will be very useful if you could explain the reasons why this figure was so much lower. Is it because you decided to decelerate exploration for some time and should this number continue to be low in the next quarter or was this just a one-off situation?

And related to this, I would like to understand what kind of consequences we could expect for the necessary rig fleet. Ms. Solange said about 30 as a minimum level necessary to carry out the plan, and this was based on a reality that was quite different from the one now with efficiency of drilling and et cetera. So I would like to understand with this new productivity data, a more recent data that you have. And together with that, when we include this lower exploratory expenses, what would be the new minimum level of fleet necessary to carry out the plan?

A - Solange da Silva Guedes {BIO 16088234 <GO>}

Good morning, André. Thank you for the question. Well this was quite an unprecedented situation regarding exploration expenses in this quarter, but I believe that Isabela was able to explain in her presentation that it was a one-off situation. It was a non-recurrent event because during the first months of 2017, we have all the internal processes in order to write-off some wells, and this is the reason why we didn't have this effect on the balance sheet of 2016, and this is the only reason why they do not appear in the first quarter of 2017. We do not expect this to be repeated in the second and the third and the fourth quarter of this year. It might be an amount lower than 2016, but anyway they will have to do with the write-off of those exploratory events.

Then you asked about our requirement for rigs, and you mentioned a level of rigs that would meet the requirement of Petrobras; this is the gist of your question. So you are correct in part when you make this association, but it's not because of the exploratory events. Because we are maintaining a decision that was made regarding a reduction of

our exploratory activities and there has been no change whatsoever in this dynamic, and this was a one-off effect regarding the accounting write-off in the first quarter.

When you talk about the increase in productivity, we are having increasing productivity in our operation of wells, and this allows us to have a more and more effective fleet management. And this leads us to postponed contracts that are ending now in 2017 and we evaluate with more attention and more carefully this return to the market because of this increase in productivity that is already happening and that has been contributing a lot to our results.

Q - André Natal

Thank you very much, Solange. And very quickly, I would like to make a follow-up on the first question that I asked. We learned through the press about a measure that you took regarding offering employees an option of reduction in their work day with a rebate in the salaries. So could you give just an update about this Voluntary Separation Incentive Plan and what kind of cost reduction could come from this?

A - Operator

André, this is a program. There is an enrollment deadline and we already have with our target audience of these people who are under administrative regime and that have the opportunity to reduce this to six hours. This is an optional reduction. We have already about 50% enrolled of our target audience and we still have one month for enrollment to be possible, and we believe that around 70%, 80% of these employees should enroll. And by that, we will have a reduction of about BRL 300 million to BRL 400 million per year with this reduction in the working hours per day.

Q - André Natal

Congratulations again. Thank you very much.

A - Operator

Thank you, André.

Next question, Lilyanna Yang, HSBC.

Q - Lilyanna Yang {BIO 14003234 <GO>}

Thank you for the opportunity. One first question. You have already signed a financing with a Chinese bank one year ago. So what is the interest rate? Do you have certain oil prices and what is the date? And the second question is the following. In relation to the assets that are in your divestment plan, in the case of the gas pipeline, are you more interested in the northeast than in the southeast in terms of gas pipelines? And what about the interest event in BR in the past? What could be changed in order to make these assets more interesting and with the potential of a better competition and be harder. Though the margins are better, but they are still lower than their peers. And in your diagnosis, is there room for improvement in efficiency and do you have a plan for BR underway right now of operational efficiency?

A - Operator

Could you repeat the first question, please, because it was not understood by the company.

Q - Lilyanna Yang {BIO 14003234 <GO>}

Financing of \$10 billion with the Chinese banks. Have you already signed it? What is the implicit cost of this credit facility? And in terms of the oil supply commitment, what is the definition of price for this commitment of supplying oil?

A - Operator

I will answer your first question and Mr. Jorge Ramos will talk about distribution [Technical Difficulty] (51:29) of which we have already disbursed [ph] \$5 million (51:35). Our commitment is to export oil, Petrobras exporting oil and this commitment is already underway. I don't know whether you're following this because the volume of exports grew substantially and this started in the fourth quarter and it was even stronger in the first quarter of 2017. So we are fully complying with our agreement.

And regarding the second part, that is the \$5 billion, we will start the process to discuss with the Chinese Development Bank regarding the second part. It's another alternative of funding such as others that Petrobras has on the table right now. I have to warn you, I would like to repeat your question afterwards. Could you please repeat your question afterwards?

A - Jorge Celestino Ramos {BIO 19059339 <GO>}

Good morning, Lilyanna. Regarding the BR margins, we have already improved the BR margins and we have been making comparisons with our peers, and we're implementing a sound program for margin improvement. This program includes three actions. One action regarding the cost of goods sold, COGS; the balance of the product mix to meet our client's need; and another one that has to do with capturing margin vis-à-vis our client sale distribution and in which we implement and we improve the overall margins of this segment. This is a program with quite a lot of actions in this direction. And also, another program for the reduction of operating costs. With reduction of cost of our operations and transportation and also with the Voluntary Separation Incentive Plan, and this has been reflected on our EBITDA margins. And in spite of a lower market in 2017, walking sideways so to say, we will be able to tap into better margins in distribution.

Could you repeat your second question please? About the gas pipelines?

Q - Lilyanna Yang {BIO 14003234 <GO>}

In the case of NTS, I would like to understand what prevented prospective buyers? Was it something in the contract or was it because of the amount involved? Because now you have more people interested in your northeast gas pipelines.

A - Operator

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The NTS process was a competitive one. If I'm not mistaken, we sent teasers to over 50 companies and, ultimately, we had the engagement with Brookfield, exclusive one, and with disbursement on April 4 for Petrobras. And when a decision is made about the next assets in our divestment program, this will be very useful in terms of the learning curve because this asset belonged to Petrobras alone in Brazil, practically, and there is a law, a specific law, in which Petrobras would not be able to make new investments if Petrobras did not dispose of this asset. This is very recent law in Brazil, so the whole array of norms and regulations regarding these assets in Brazil is very different from what we see in Canada, in the U.S., and in Europe, and the objective is to continue to develop the market, accelerate the development of the market. And in itself, this movement - well you know very well that the pre-salt has a very big gas component and there will be a very big volume of gas in Brazil, and we'll need infrastructure in order to transport that, and you will have to encourage consumers by means of the local distributors for the participation of gas in the Brazilian energy matrix. This is a natural trend and, by itself, when the time comes it should lead to a higher interest in the NTN (56:27) asset.

Q - Lilyanna Yang {BIO 14003234 <GO>}

Thank you very much. And what about the \$5 billion?

A - Operator

Well, we do not disclose that. Petrobras only carries out operations in which we will have a cost below or similar to your cost in the long-term secondary market. Thank you.

Our next question is from Luiz Carvalho, UBS.

Q - Luiz Felipe Carvalho {BIO 18040760 <GO>}

Good morning, everyone. I have a couple of questions, three. The first is geared to Celestino. Looking at the press conference presentation yesterday, I thought that you updated the chart on the refining cost. It was showing a drop yesterday, but you kind of fixed it. So my question is, looking at your utilization rate close to 77%, refining cost tends to show an upward trend if we'll continue to look at the utilization factor. So, Celestino, I want to understand. Given the pricing policy, utilization policy, what would be the minimum utilization rate given your fixed costs in your refining facilities?

My second question goes to Ivan. Ivan, we know that the discussion of transfer of rights is close to being resolved, at least in the perspective of the Minister of Planning and Mines in the Gaffney, Cline and Associates report is almost ready. So we discussed Petrobras' option to produce the first 5 billion barrels. So I would like to understand, how is this going to influence the negotiation? What do you see about this right? How could you monetize this and how is this being handled with the committee of minority shareholders?

And if I may, one last question to Ivan. As you said it yourself, regarding the profile of the debt and this agreement with a Chinese bank, now it seems that the company is taking on a more exporting approach. So I would like to know about your discussion with CVM about hedge accounting. And if you could give us a timing perspective, that would be interesting too. Thank you.

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A - Operator

Thank you, Luiz. I would like to ask Isabela to correct what you stated about the chart. Isabela?

A - Isabela Mesquita Carneiro da Rocha {BIO 19730664 <GO>}

Hello, Luiz. This is Isabela. I just want to clarify. We did not fix the numbers compared to those figures that we presented yesterday. The figures are exactly the same. However, we added the perspective in dollars and reais. So the refining cost in reais is exactly the same as yesterday, but we now added information in dollars, and Jorge Celestino will make a comment on that.

A - Jorge Celestino Ramos {BIO 19059339 <GO>}

Okay. Luiz, good morning. Regarding the operation of our refining park, and what is the minimum utilization factor. Well, you have to understand this. Our model to operate our park, always runs trying to get the maximum profitability for the park possible. So, obviously, we look at market share, we look at the utilization factor for our refineries. We look at the margins, we look at the spreads, Brent, crude oil. And based on the set of variables, we decide what is the refining capacity that we're going to use, what volumes we're going to import, what volumes we're going to export, and what will be the trade options that we will have. So the number that we're operating the park with is quite comfortable in terms of profitability.

Considering this set of assumptions that we mentioned to you, so we can get good profitabilities, good margins given the market conditions at this point. If market conditions change, in other words, if margins and spreads change, it is possible that I will need to use another utilization factor for the refineries. Let me give you an example, if spreads starts to drop and the Brent gasoline difference would be \$2 to \$3 per barrel, then that would have a different impact on refining costs and on margins. So the set up of the refining park has to work and take into account those set of assumptions so that we can decide what the best option is.

A - Operator

Luiz, as for the transfer of rights, the one leading this discussion at Petrobras internally is Officer Solange. So she will answer your question.

A - Solange da Silva Guedes {BIO 16088234 <GO>}

Good morning, Luiz Carvalho. You asked about our rights in the contract signed for the transfer of rights?

Q - Luiz Felipe Carvalho {BIO 18040760 <GO>}

Actually, Solange, my question is regarding your option to produce the first 5 billion barrels. This is in the initial contract, and this option to produce the first 5 billion barrels and, perhaps, leave the rest for 30 years, this option has a value. And I would like to understand how do you see this option? How do you see the possibility to monetize this and are you discussing this with the committee of minority shareholders?

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A - Solange da Silva Guedes {BIO 16088234 <GO>}

Thank you for clarifying. This has been great so that I can answer exactly what you expect from us. Petrobras has the right in five areas to produce up to 5 billion barrels of oil equivalent. This is in the contract. You know it well. You just mentioned it. Possible surplus, anything above the 5 billion barrels, this will not be produced unless we come to an agreement. So what we're assessing today, what could be beneficial both for the company and for the government, is that somehow we can find alternatives and possibilities that can help us monetize possible surplus, any production beyond this volume of 5 billion. But this is what we call eventual discussions as a way of getting a reimbursement.

The committee of minority shareholders exists in the company for discussions of the related parties, which is the case, and this committee will follow these discussions up close. As you probably know, these discussions have not happened yet and ANP has not decided yet regarding the findings of the consulting company that they hired to support the positions of the government regarding the updating of the amounts paid at the time. As soon as the report from ANP is sent to the federal government, that's when the formal discussions will begin and that's when Petrobras and the committee of minority shareholders will be involved.

A - Operator

Luiz, regarding hedge accounting, the company has submitted its defense at the collegiate of CVM. I'd like to remind you that the technical area of CVM had given the company an authorization to publish the balance sheet based on the methodologies that we've been using which we believe is correct. We submitted our defense. The collegiate has another deadline to manifest their opinion, and we're waiting. And we remain available to CVM to answer any questions that they might have.

Q - Luiz Felipe Carvalho {BIO 18040760 <GO>}

Okay. Thank you very much.

Operator

Our next question comes from Vicente Falanga with Bank of America Merrill Lynch.

Q - Vicente Falanga Neto {BIO 16406266 <GO>}

Hello. Hello, everyone. Could you please remind us what is the average dollar rate and the average petroleum crude oil price that you're using for your 2017 projections? Thank you.

A - Operator

Isabela will answer.

A - Isabela Mesquita Carneiro da Rocha {BIO 19730664 <GO>}

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Vicente, we're using Brent at the same level of the first quarter, about \$54 per barrel and the exchange rate of about BRL 3.2.

Q - Vicente Falanga Neto {BIO 16406266 <GO>}

Thank you, Isabela.

Operator

Our next question comes from André Hachem with Itaú BBA.

Q - André Hachem

Hello, everyone. In terms of liability management, you've been doing excellent work to manage this debt. What would be a good amortization schedule looking forward which would be a comfortable payment schedule?

A - Operator

André, your question is very good because as I mentioned yesterday in the press conference, this is the first time since this management took over. But we have a number of alternatives, then all of them available at the same time. It includes the Brazilian capital markets, foreign capital markets, bilateral banks, Brazilian commercial banks, bilateral agreements with global banks, agency to foster experts, and development agencies of many countries. It's all available, and Petrobras looks at those both in two ways: first, to reduce the cost of debt and the cost of funding, and then redistributing the payment of the debt. And I think that this links with the EBITDA of the company, the CapEx of the company, and the free cash flow of the company.

What we did in this period was there was a mismatch between what the company in the past projected in terms of its oil production curve and the profile of maturities based on that projection. You might remember that at the very beginning, we made an important change in the projection of our oil production. In 2016, we delivered exactly what we have projected to the market and that links to the profile of the debt which, in our view, was too concentrated and mismatched comparing to the new production curve profile. So you should continue to see we've made important operations for active liability management, and this will continue.

The upside is that we now have more alternatives for these transactions and these deals, and have a clear willingness and a change in our relationship with commercial banks. All of them. Not only domestic but foreign as well for future maturities. And they're approaching the company to discuss possible changes, possible prepayments and possible rescheduling to match the new production curve and to match the new free cash flow of the company which, for us, is extremely positive.

Q - André Hachem

Perfect. Thank you very much and congratulations on the results.

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A - Operator

Thank you, André.

Thank you very much. We're now closing the Q&A session. I now turn the floor back to Mr. Ivan de Souza Monteiro who will make his final remarks. Mr. Monteiro, please go ahead.

A - Ivan de Souza Monteiro {BIO 16420543 <GO>}

Thank you very much. I would like to thank you all for participating in this event and I and our RI department (sic) [IR department] is available to answer any further questions you might have. I wish you a great day.

Operator

Thank you. Ladies and gentlemen, the audio of this conference call for replay and slides presentation will be available at the Petrobras IR website at www.petrobras.com.br/ir. This concludes today's conference call. Thank you very much for your participation. Please hang up your telephones now and have a great day.

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