

Q3 2002 Earnings Call

Company Participants

- Carlos Enrique
- Joao Nogueira Batista, CFO Investor Relations Director
- Mariana Crespo

Other Participants

- Bryan Singer, Analyst
- Carlos De Leon, Analyst
- Emerson Leite, Analyst
- Frank J. McGann, Analyst
- Luiz Otavio B. Laydner, Analyst
- Mark M. McCarthy, Analyst

Presentation

Operator

Ladies and gentlemen. welcome to the Thomson Financial/Petrobras teleconference. Please be aware that each of your lines is in a listen-only mode. At the conclusion of the presentation, we will open the floor for questions. At that time, instructions will be given as to the procedure to follow if you would like to ask a question.

I would now like to turn the conference over to Mariana Crespo. You may begin.

Mariana Crespo

Good morning, ladies and gentlemen. Welcome to Petrobras' conference call to discuss Third Quarter 2002 results. There will be a playback facility for this call. For instructions in accessing the playback, please contact us in New York at 212-807-5016.

Before proceeding, let me mention that forward-looking statements are being made under the safe harbor of the Securities Litigation Reform Act of 1996. Actual performance could differ materially from those anticipated in any forward-looking comments as a result of macroeconomic conditions, market risks and other factors.

Finally, let me mention that this conference call will discuss Petrobras' results prepared in accordance with Brazilian GAAP. At this moment Petrobras executives are unable to discuss questions related to the U.S. GAAP results, which will be released shortly.

With us today in Rio de Janeiro is Mr. Joao Nogueira Batista, CFO and Investor Relations Director. First, Mr. Nogueira Batista will comment on the company's performance during the Third Quarter of 2002. After that, he and his team will be available to answer any questions you may have. Mr. Nogueira Batista, you may now begin.

Joao Nogueira Batista {BIO 21373970 <GO>}

FINAL

Bloomberg Transcript

Thank you, Mariana. Good afternoon, to everybody. So we're back to discuss another quarter result and-- which again is a quarter which was marked by very volatile markets and turbulence in the external scenario and enhanced-- which have enhanced along the year the scenario-- the local scenario and also, of course, the effects of the election process in Brazil and the uncertainty that has caused in the eyes of the external world and the internal world. So this all has created a very turbulent scenario in which not only ourselves but all other corporations in Brazil have had to manage the best they can. And we are happy with the results because they represent, we think, the best possible results in view of this scenario.

So before entering into more details of the results, I think it's worthwhile to mention what were these main variables that have impacted the Third Quarter results. And they were affected by, of course, facts related to the prices of oil in the world markets, which had a positive effect; the devaluation of the real vis-a-vis the dollar, with a very negative impact; and the pass-through, albeit partial, of these factors on to the domestic prices of oil products.

During the Third Quarter compared to the second, the following may be noted. An increase of 7.6% in the average prices of the brand from 25.04 to 26.95, as a result, as you all know fundamentally, of the expectations of military activity in Iraq and low inventories of oil and oil products in the industrialized countries. The currency devaluation of 37% during the quarter as compared to 22.4% during the previous quarter. This is a formidable, very dramatic fluctuation, which has, of course, serious impacts on the balance sheet. A reduction in dollar terms of the average realization price of 8.7% over the quarter. However, in reals, the same indicator increased by about 14.8% from roughly 69 reals to roughly 70, almost 80 reals, which is a reflection of the sharp devaluation.

And in relation to the oil product prices, the price increases that were put in place at the end of the Second Quarter, exactly on June 30, the increases in gasoline and diesel and the reduction of 12.4% of the residential LPG are noteworthy. They were put in place at the end of the previous period and had the impact during the period in assessment.

So this was a positive impact, offset, of course, by the fact that we have practiced, as we already have discussed many times, a more conservative pricing policy during the Third Quarter in view of the extreme volatility that we had in the markets, not only oil products but mainly the foreign exchange situation in Brazil. And so the conservative pricing policy put in place did not permit us to pass through all that we should have passed through if we were to pursue strictly the pricing policy that we had established for ourselves. But this was a conscious move and as we have discussed many times and it's a move that was done to protect the model in the long term, as we have discussed many times. But this had, of course, an impact during the Third Quarter, as expected. Prices of other products, on the other hand, all other products besides those three main products were readjusted in line with the concept of import parity during the quarter.

On a year-on-year basis, we have to consider that-- take into account the average brand price rose from 25.3 to 26.95 per barrel, which represents a 6.5% increase in average and the devaluation of the currency in this same period of 2001 was only 16% against, as already mentioned, 37% this quarter, which is a dramatic, dramatic change.

If we move to the next slide, what I would like to point out is that the net operating revenues, as we can see, were up 34% over the same quarter of last year in spite of the fact that the domestic prices were only partially reflected the higher international levels, as mentioned. And the impact of devaluation of the real against the U.S. dollar and the combination of these things were-- also reflect-- the result of this increase in operating revenues was also a result of the 14% increase in domestic oil and gas production, which made it possible to increase the exports of crude and other oil products by 59%. So the increase in exports had and the overall sales were an important compensation for the more conservative pricing policy and the devaluation of the real against the U.S. dollar on a year-on-year base.

In relation to the Second Quarter, the increase of 7.6% in the brand price resulted in an increase of 35% in the net operating income, which, of course, would have been higher if we had passed fully all, as already mentioned, the prices and the exchange rate volatility. The greater oil and oil product exports and the exchange gain, foreign exchange gains on overseas operations also contributed to the growth in net operating income.

Although gross profit for the Third Quarter of '02 was up 19%, operating profit before financial income and expenditures and the effect of exchange rate adjustments on net worth fell by 4% in relation to the previous quarter. And this is due basically to the following facts, which we would like to highlight. The main one, of course, is the increase in tax charges, tax burdens such as (passep) and (coffines), which are related to non-operational revenues, mainly financial revenues, which amounted in this quarter to R\$ 354 million reais alone. This is on the foreign exchange gains on the cash positions and the capital gains position.

The administrative expenses were higher, R\$ 181 million reais due to higher expenses with outsourcing of services and the impact of the foreign exchange devaluation on the overseas expenses. The overseas expenses were basically the same, stable in dollars. But, of course, in reais, due to the 37% devaluation, the impact is high.

We had non-reimbursable contractual contingencies. An easier name for that is the capacity payments that we have to make for the thermo power plants, the merchant power plants, (Electrobolt) and (Machia), which are generating losses and these capacity payments amounted to R\$ 307 million reais during the Third Quarter and R\$ 432 million reais if we consider the nine months period ending in September.

The increase of 45% in net profit over the same quarter of last year was due basically to the increase of 13% in total production of oil and gas. This is a very important factor behind the maintenance of our performance. We are producing at a rhythm which is well above the average rhythm of growth of the industry and this is what makes our position in the medium and long term a solid position.

The tax benefit for the provision of payment of interest on owned capital -- this is also an important feature in the Third Quarter since a similar provision was made in the previous quarter in the previous year. So this makes the change have an impact on the Third Quarter when we compare it.

And the gains on investments in overseas subsidiaries totaling roughly R\$ 1 billion, 465 million reais is a result, again, of the 37% devaluation against 16% devaluation in the previous quarter, the comparable quarter. And this gain was partially offset by losses in equity holdings in the petrochemical sector and, again, negatively affected by the exchange rate movements and by some of the maintenance stoppages in one of the petrochemical plants, which has participation in (PKU).

In the next slide, a comparison of the Third Quarter results with those for the Second Quarter requires, I think, the following comment. I think you have probably noticed that there are some sharp variations which need some clarification.

The 45% increase in cost of product sold was due basically, again, to the effect of the 30% devaluation of the real on the portion of these costs which are paid for in foreign currency, including imported oil and products. And I think it's important to remember that 70% of the cost of goods sold are in foreign currency. So the impact is significant of the devaluation.

The increase in government take due to the increase in international oil prices and the devaluation of the real and the increase in the productivity in the (Marlene Albacordo) and (Marlene Sou) fields, which have a significant impact in special participation payments of these government takes. So

both the devaluation and the increase in production, in productivity and production, have entailed an increase in these government takes, which are significant in the quarter.

The increase in the cost of imports, as a whole, not only in terms of volume but also in terms of price, has an important impact in the Third Quarter. And significantly when it concerns our foreign subsidiaries, the methodology used to convert these accounts, their accounts utilizes the exchange rate of the last working day of the quarter. So this reflects fully the 30% devaluation, which is, of course, higher than the average devaluation in the period.

Under the caption operating expenses, it is important to note that in the Second Quarter of this year a number of non-recurring reversions and revisions totaling R\$ 318 million reals were included, which were covered during the Second Quarter conference already. We dealt with this subject at that moment.

So when we look at this line now and we see almost a 6800% variation, we have to recalculate the departure basis so that we can eliminate the effect and make it a more reasonable comparison and the result is, then, a 210% variation of these other operating expenses. And this 210% variation is explained by basically a R\$ 307 reals million resulting from this capacity payments that we mentioned already from the thermo power plants, the exchange rate differences of a series of accounts mainly dealing with the way that foreign exchange valuation along the years were accounted for Braspetro and Petrobras International in the-- Petrobras America, sorry, which were mistakes, basically accounting mistakes in the past which were corrected since the holding company took over the accounting department of Braspetro and Petrobras America. We have undertaken a review and correction of these statements and since Braspetro was incorporated at the end of the quarter, we had to basically finalize this review and take into consideration all the corrections that had to be made. And this amounted to R\$ 194 reals million. That's a once and non-recurrent event, a once and for all event.

The remaining expenses are in line with those of the First Quarter, including about R\$ 200 million relating to actuarial expenses with our pension fund and health benefits and maintenance stoppages, which were not foreseen.

The increase of 115% in the results of our net worth equivalents in the consolidated Third Quarter is due to foreign exchange gains in the conversion of net worth of our foreign subsidiaries.

And finally, we can highlight that reduction of 51% of the income tax and the social contribution is due to the reduction in the operating profit in the Third Quarter, roughly R\$ 799 million reals when compared with the Second Quarter, which generated a reduction in the income tax of roughly R\$ 272 million reals and, besides that, the provision for the interest on owned capital in the amount of R\$ 369 million reals, which was undertaken in this quarter. And had been done in the previous quarter last year. So this has an impact here.

(audio interference)

In the next slide, we show this-- we compare ourselves to our peers in terms of total production and we see here what I referred to before, how we out-performed all our major competitors and we have been maintaining this strong growth in production. Here this 12% increase, this is 13% of domestic oil production and 12% includes gas production-- all the production, including gas, which had a small reduction. So the overall oil and gas production was 12%, which is well above the average of the industry.

The 18% reduction in Brazilian lifting cost, excluding the government participations, achieved during this quarter, Third Quarter, compared to the same quarter a year ago, results from both increased production, productivity. But mainly due to the conversion of local costs to U.S. dollars as a direct

result of the sharp devaluation of the local currency. It is noteworthy that including government take lifting costs actually increased by 4% on a year-on-year basis as a result of increased productivity.

On the next slide, again some operational results and here mainly our performance in terms of imports and exports. We continue to move towards becoming a net exporter of oil and oil products and this year we have moved steadily in that direction although there was a small increase in the Third Quarter due to higher imports of lighter oils and products. But our overall trade balance is becoming positive slowly and our contribution toward the trade balance of Brazil as a whole is significant and if we consider the estimates for the Brazilian trade balance for the year of roughly, I think, \$11 or \$10-1/2 billion of trade surplus, Petrobras alone will be contributing with 25% of that positive trade balance. So this is a major contribution to the reduction of vulnerability over the Brazilian balance of payments.

Just quickly discussing our financial position, the leverage position, we see here that our short-term position continues to be at an adequate level of 21%. So any sort of roll-over risk is definitely out of question. We've been facing these fantastic liquidity crunch which resulted from this global risk aversion process initiated in corporate America. We have been managing this situation very comfortably due to our low level of short-term debt and we have managed to find good alternatives for financing on a long-term basis in the local capital markets.

And on the overall leverage of the company, we see, of course, you have the negative effect of the devaluation. Again this has a very snap photo effect, which is very hard on the net debt position. But this is something that smooths away, finds a point of equilibrium over time and if looked at one moment it has been increased to 46%.

Just quickly, before I pass on to questions, I'd like to comment on some of the relevant events that happened after the close of the Third Quarter and some that happened during the Third Quarter.

As you all know, we finalized the acquisitions of both Santa Fe and Perez Companc, which undoubtedly are very important moves and substantial moves in our internationalization strategy. This is a process which has no come back and these acquisitions set a dramatic change in our point in the history of the company and we will now have to-- we have started already to deal with the integration of our business in Argentina and we'll continue and during 2003 we'll have a big challenge of consolidating the position that we have achieved as the major regional player in the oil and gas field in Latin America or in South America.

We have recently also announced the new proposal for the acquisition of the outstanding shares held by the public of our subsidiary, Petrobras Distribuidora and we aim at closing its capital thereafter. This is an important measure towards-- basically, the logic behind it is a capital markets logic. It's to have everybody focusing on only the shares of the holding company and providing the shareholders of Petrobras Distribuidora with a more liquid share and with a longer, with a much better longer-term perspective. And we would also align the structure of our company to that of our peers where there is only one company listed in the stock exchanges.

And finally, one fact which I mentioned already but is important that happened during the Third Quarter was the incorporation of Braspetro into Petrobras. So Braspetro no longer exists as a subsidiary in Brazil. And the process what is behind this is a much deeper process which will be explained to all of you in a release that we expect to send to you shortly explaining the whole reorganization of our international business and making it much more transparent.

In very simple terms while the process entailed the closing and the creation and the incorporation of many companies. But basically what happened in very simple terms is that we transferred the head office of Braspetro to Holland. So what we have now is a holding company for the international business, Braspetro Holland, which will own all the subsidiaries and all the operations related to our international activity.

So in the future when you look at the balance sheet of the Braspetro Holland, you will be looking at the result of our international activity. We will-- the only difference will be that the results of Braspetro Holland will not, for the time being, incorporate the results of our Argentinean business. Perez Companc, yes, because it was-- Petrobras Holland owns Petrobras-- Perez Companc. But it does not own EG3 [ph] and Petrobras Argentina, which will have to be incorporated over time for fiscal reasons.

But those were the facts that I wanted to mention to end my part of the conference and now open for your questions. Thank you.

Questions And Answers

Operator

Thank you. Ladies and gentlemen. we will now begin the question-and-answer session. If you have a question or comment, please press the star key followed by the one key on your Touch-Tone phone now. If at any time you would like to remove yourself from the questioning queue, simply press star followed by two. Please restrict your questions to two at a time.

Our first question comes from Carlos de Leon from Deutsche Banc.

Q - Carlos De Leon {BIO 21527222 <GO>}

Hi. It's Carlos de Leon, Deutsche Bank. I just had two questions. Firstly, I wonder if you could give us the date for the commercial startup of FPSO Brazil [ph] at (Juancador) and also say whether you already have the necessary environmental license for this platform? And secondly, I wonder if you could just briefly share with us the progress, if any, that management has done in view of the company's plans to add new refining capacity in the U.S.?

A - Joao Nogueira Batista {BIO 21373970 <GO>}

Okay. Hi, Carlos. To your first question, the FPSO Brazil, from what I am informed, we expect to be receiving a license in roughly 10 to 15 days and immediately thereafter operations will start. The wells are already connected so it's basically just a question of receiving the operating license. We don't expect any problem and, therefore, we estimate that we will receive that in the next 10 to 15 days. Of course, there's a proviso there that unexpected problems might arise in this licensing process. It's not expected. But I think it will happen in the next two weeks.

Concerning the acquisition of refining capacity outside Brazil, the progress there is not as brilliant as we would have expected. We have not been able to find a suitable object at a suitable price. We had found an object but it was not at a suitable price so we will continue to endeavor our best efforts to find something suitable at a suitable price. But we will not do that in a hurry. But we hope to achieve that sometime in the next six months or so. But it's a question of opportunity and price and we are working hard but I don't think we will manage to do that this year.

Q - Carlos De Leon {BIO 21527222 <GO>}

Thanks.

Operator

Thank you for your question, sir. Our next question comes from Luiz Laydner from Banco Pactual.

Q - Luiz Otavio B. Laydner

My question is regarding the price limits for the stock of Petrobras with respect to the formula used to calculate the separation with Distribuidora. I'm basically concerned with the forecast level

that could trigger the operation. Is that price level adjusted for the payments of dividends or payments of interest on shareholders' equity today? In other words, is that price limit going to be reduced by 1 real per share or not?

A - Joao Nogueira Batista {BIO 21373970 <GO>}

No, these-- the offer for the exchange is based on-- the economic valuation of the company is based on position on June 30. So these are the economic valuations of both companies. That was the basis of the exchange offer and so we don't expect to make any change there.

And I don't really understand why you are worried with that. That is something that protects the shareholders of Petrobras and so it's-- it will only go through if-- The formula is designed to protect-- to align interests, avoid speculation on the Distribuidora shares and if there is any speculation that results in price increase of the share of Petrobras, it's in the interests of all of its shareholders. So I think the formula was clever in that sense that it aligns the interests of all parties.

Q - Luiz Otavio B. Laydner

Okay. I have a second question, which is does Petrobras does intention to access that market once again before the year end?

A - Joao Nogueira Batista {BIO 21373970 <GO>}

To-- what was the question again? To tap the local capital markets, you're saying?

Q - Luiz Otavio B. Laydner

Local or abroad.

A - Joao Nogueira Batista {BIO 21373970 <GO>}

Well, from today's perspective we don't see the capital markets scenario-- international capital markets scenario changing that much. So we don't foresee any major capital markets transaction before year end except some trade-related financing, which we are discussing and we might able to close before year end.

And in terms of the capital markets, all we could theoretically foresee is another local markets bond issue, which is possible. We are still examining. But there's no decision taken.

Q - Luiz Otavio B. Laydner

Okay. Thank you.

Operator

Thank you for your question, sir. Our next question comes from Frank McGann from Merrill Lynch.

Q - Frank J. McGann {BIO 1499014 <GO>}

Hi. Good afternoon. Just a couple questions. One, in terms of the capacity payments for the thermo plants, is your expectation that future quarters will see similar type payments? I know it's very uncertain. But I would expect that there's a fair risk of that and if you could clarify your view on that? And then secondly, related to two numbers in the financial statements, both the equity income number, which was R\$ 1.27 billion reals and the minority interest of a positive R\$ 851 million reals. Could you clarify exactly how much of each of those numbers is due to foreign exchange effects and how much would be due to other factors and in which subsidiaries or other operations would those amounts have arisen?

A - Joao Nogueira Batista {BIO 21373970 <GO>}

Okay. I'll address the capacity payments issue and pass your second question to Carlos Enrique [ph] and he can--

But you are right, I think the capacity-- the capacity payments are recurrent events. They will continue to happen. I think it would be fair to say, although I will ask our Luciana to confirm to you this later on. But I think the level of capacity payments reached in the Third Quarter is more or less the peak. You have to forget the foreign exchange effect of that but if looked at in dollar terms, it would have reached the peak because during the Third Quarter they were not dispatched and we had to pay the full capacity.

In reals, it will depend on the foreign exchange and the foreign exchange devaluation. But I think the level in dollar terms of capacity payments with those two merchant plants has reached more or less the peak. But Luciana will confirm to you that information in due course. But in dollar terms, it's the peak.

And, Carlos Enrique [ph], can you address the other question, please?

A - Carlos Enrique {BIO 1891275 <GO>}

Related to gains from investment in subsidiaries, we have R\$ 1.5 billion reals. Related to gain in exchange rate to the devaluation of the dollar related to reals, we have a loss R\$ 119 million reals related to petrochemical companies in this period. And about minority interests, this is related to BR Distribuidora and (inaudible) related from Braspetro.

Q - Frank J. McGann {BIO 1499014 <GO>}

Okay. Thank you, very much.

A - Joao Nogueira Batista {BIO 21373970 <GO>}

Okay. Thank you, Frank.

Operator

Thank you for your question, sir. Our next question comes from Bryan Singer from Goldman Sachs.

Q - Bryan Singer {BIO 3297046 <GO>}

Good afternoon. Two questions. First, if you could just give us the number--

A - Joao Nogueira Batista {BIO 21373970 <GO>}

Could you speak louder, Bryan, please?

Q - Bryan Singer {BIO 3297046 <GO>}

Sorry, Joao. First, if you could give us an update on production and cap ex assumptions that you're using for 2003? And second, a lot of the arguments that you made on why to close the capital out of BR Distribuidora could be applied to Perez Companc. However, you've expressed the lack of interest in acquiring the remaining shareholders of Perez Companc and I was wondering if you could just rationalize the arguments between why to acquire one and not the other?

A - Joao Nogueira Batista {BIO 21373970 <GO>}

Okay. Your first question related to production targets and cap ex for 2003. We will-- we are finalizing the review of the strategic planning and we expect to have this official information for you

before year end, at least beginning of next year. I think still this year we will finalize the strategic planning and we will have these numbers available.

To your second question, you are right. The logic would apply. The only difference is that Perez Companc is a recent acquisition. We did not have the intention to have an extra burden on our acquisition payments by buying out the minority interest at this point. And we will have to examine, in due course, the convenience of doing that or not and we want to keep the company publicly listed for the time being to see how it behaves in initial phase and deal with this problem in the future.

There are many ways to capture the synergies without moving to closing the capital at this stage but this does not exclude that doing something similar to what we are doing with BR might be done in the future if it makes sense from a market point of view to do an exchange offer. I wouldn't see in the near future any move to do a simple cash buy-out. That was the main reason why we didn't even consider that at this stage. But over time, who knows, it might make sense to do the same if an exchange offer would make sense in the future.

Q - Bryan Singer {BIO 3297046 <GO>}

Great. Thanks.

A - Joao Nogueira Batista {BIO 21373970 <GO>}

It's an open question.

Operator

Thank you for your question. Our next question comes from Rodrigo Geis [ph] from Bear Stearns.

Q - Mark M. McCarthy {BIO 5634411 <GO>}

Hey, Joao, this is Mark McCarthy from Bear Stearns. Just two questions kind of following up on the cap ex question really more for the Fourth Quarter. You're well below plan for this year in a dollar perspective. I'm wanting to understand your guidance for Fourth Quarter spending and, let's say, initial part of 2003, given your existing production plans.

The second question is more to do with the regulatory approval of the Perez deal. I know you've typically explained the deal as being closed. But, correct me if I'm wrong. But it is still pending regulatory approval and I'm curious as to your expected time frame with regard to that, if that is really required, in the early part of next year? And well, do you have any other insight into how that process will work?

A - Joao Nogueira Batista {BIO 21373970 <GO>}

Okay. In terms of cap ex for this year I'm not sure what you are referring to. I can't imagine that the answer to your question is, if I recall correctly from the last figures I saw is that we are, if you look at the Third Quarter numbers, there is, vis-a-vis the target for the year still a long way to go. But you have to consider that the acquisitions are mainly-- and mainly Perez Companc were closed after the end of the Third Quarter. So this will all be accounted for in the cap ex numbers of the final quarter of the year. So alone there, you will have, from the acquisitions, you would have approximately \$1 billion coming into that cap ex figure, plus the investments, the normal investments, in the production that were foreseen.

So we will-- our expectation is that we will close the year roughly, basically in line with our cap ex projections. There will be some changes intra-areas. For example, we will invest less in the thermo power plant program and there will be some-- at the end, some extra investments in E&P, for example. But we will close to the year target.

Q - Mark M. Mccarthy {BIO 5634411 <GO>}

So you're planning on wrapping in the acquisition financing, then, the acquisition costs into cap ex that they were previously excluded?

A - Joao Nogueira Batista {BIO 21373970 <GO>}

Sorry? What was that?

Q - Mark M. Mccarthy {BIO 5634411 <GO>}

The acquisition costs had previously been excluded in targets and what you're suggesting is that it should all be wrapped in together. So you'll end the year at about 5 million with everything?

A - Joao Nogueira Batista {BIO 21373970 <GO>}

Yes. That's basically-- I don't have the numbers with me now. But we will be basically on target. Yes. I don't recall the acquisitions being excluded from our cap ex targets. The acquisitions are included. But, Okay, we will be basically on target. All-in considered, we will close the year basically on target or slightly-- if below, slightly below only.

And to the question which was related to the regulatory approval, we have taken all-- of course, we are pending approval of (CNDC) in Argentina. But we have taken control of the company, have paid for the company with all the necessary guarantees and we expect this to happen soon. It's hard to predict when it's going to happen. But we expect it to happen soon.

We have said, I think, the maximum time it can take is one year according to all the mechanisms of protection included in the closing agreement. But we expect that to happen much, much earlier than that. But we are working on that. Our people in Argentina are working on that. We filed for that approval already and we expect that to happen rather quickly.

Operator

Thank you for your question. Ladies and gentlemen. as a reminder, if you would like to pose a question, please press the star key followed by the one key on your Touch-Tone phone now. If at any time you would like to remove yourself from the questioning queue, press star followed by two.

Our next question comes from Rodrigo Geis from Bear Stearns.

Q - Mark M. Mccarthy {BIO 5634411 <GO>}

Hey, Joao, as a follow-up -- this is Mark McCarthy again. Going back to the capacity payments, suggesting that this is a peak, can you just explain what the overall outstanding liability represents if you calculate that? And to what extent or at what point do you stand to, in effect, take over the equity of these two plants if that is even a consideration?

A - Joao Nogueira Batista {BIO 21373970 <GO>}

The first part of your question was if I could estimate what exactly, sir?

Q - Mark M. Mccarthy {BIO 5634411 <GO>}

The overall liability, projected liability, associated with these contractual payments.

A - Joao Nogueira Batista {BIO 21373970 <GO>}

Okay. I think this is the peak level, as I think I answered Frank, the peak level of liability in terms of capacity. Let me just ask here my colleagues something. One moment.

The liability is basically-- if we estimate-- you can estimate that for the time frame that you would like. But moving forward the scenario is no dispatch and 100% of the capacity, this would be more or less the level on a recurrent basis. And so that would be our liability with these two plants.

And your other question, the owner of (Machia) is El Paso and there is no discussion there for the time being on any rearrangement. And the owner of the other plant, of (Electrobolt) is Enron, financed by a consortium of banks. And as far as I know, this-- they are having discussions between themselves on how-- who owns what there and at a certain point in time this will include Petrobras as the main guarantor. But from today's perspective, there is no clear solution yet, foreseeable solution yet. But we expect that we will reach some sort of solution.

And if we find a way to take advantage of any specific situation to change the concepts of these contracts, we will do so, because, of course, they are-- as they are presently structured they are harmful to our results. If it all is kept the way it is today in five years, I think at the end of five years, we would have-- they will be owned-- we end the capacity payments. But they will be 100% owned by their present owners, which would be a disastrous situation, to say the least.

Q - Mark M. McCarthy {BIO 5634411 <GO>}

If I could just ask one follow-up question. You don't provide a divisional breakdown of debt. But you do provide a divisional breakdown of financial expense. Does that-- or basically the question is, what percentage of that financial expense that is reported is actually foreign exchange losses versus actual debt costs? I think it was reported at R\$ 1.1 billion reals for nine months.

A - Joao Nogueira Batista {BIO 21373970 <GO>}

You're talking about the financial expenses?

Q - Mark M. McCarthy {BIO 5634411 <GO>}

Just in the gas and energy business.

A - Joao Nogueira Batista {BIO 21373970 <GO>}

Oh at the gas and energy business. Sorry. What was your question again?

Q - Mark M. McCarthy {BIO 5634411 <GO>}

The gas and energy business reported R\$ 1.1 billion reals of financial expenses. The question is, you don't provide a breakdown of the debt by division, which is understandable. But my question is--

A - Joao Nogueira Batista {BIO 21373970 <GO>}

But those are-- those are debts which are specifically earmarked for those power plants or energy or gas products, Okay? The same happens in the E&P business. If you have a private finance which is earmarked for the financing or development of any oil field, it is accounted for directly in the business segment. The only indebtedness which is not accounted for per business area is the indebtedness which is not earmarked for any specific business. Then it's accounted for at corporate level.

Q - Mark M. McCarthy {BIO 5634411 <GO>}

Well, even better. Are you able to provide us the breakdown of the debt just attributable to the gas and energy business?

A - Joao Nogueira Batista {BIO 21373970 <GO>}

Yes. I wouldn't see why we couldn't do that, yes. For example, in the thermo power plants -- and these two, (Electrobolt) and (Machia) I can tell you we have no indebtedness at our level, Okay?

Because the indebtedness is at the level of the SPCs or whatever at Enron level or El Paso level. Okay? We only have the obligation of the capacity payments. So there is, in those two cases, there is no related indebtedness.

For other structures we have private financing in place which are accounted for if these financings are taken by the thermo power plants themselves, (inaudible) or name them all, they are accounted for at the level of these companies, which are thermo power plants. So they will not be at Petrobras' level. In those cases we would have-- our obligation is through the contracts to purchase, the PPAs to purchase the energy. That's where our obligation will come from and if you look at our F-20, we disclosed very clearly what were our liabilities in terms of purchases of energy. That is where our liability lies. At the indebtedness level in terms of gas and energy, we have no specific liability in our balance sheet.

Is that clear?

Q - Mark M. McCarthy {BIO 5634411 <GO>}

Okay. Do you know what percentage of this financial expense was corresponding to foreign exchange losses or is it all associated with financial expense?

A - Joao Nogueira Batista {BIO 21373970 <GO>}

I can't answer you that question now.

Q - Mark M. McCarthy {BIO 5634411 <GO>}

Okay.

A - Joao Nogueira Batista {BIO 21373970 <GO>}

We can answer-- we can answer you that later on, Okay?

Q - Mark M. McCarthy {BIO 5634411 <GO>}

Okay. No problem. I'll follow up.

A - Joao Nogueira Batista {BIO 21373970 <GO>}

I don't have that breakdown, Okay? Follow-up with Luciana and her team. They will give you the specific answer on that question.

Q - Mark M. McCarthy {BIO 5634411 <GO>}

Dynamite. Thanks.

Operator

Thank you for your question, sir. Our final question comes from Emerson Leite from Credit Suisse First Boston.

Q - Emerson Leite {BIO 4003528 <GO>}

Hi, Joao. Just one question with regard to the meeting that Petrobras had last week with the transition team from the next administration, from the Luna government. I'm not sure if you, in person, attended this meeting but I guess Francisco will share his views with you. Could you share with us what were your impressions regarding this meeting and what could we expect from this transition team in terms of next steps with regard to Petrobras?

A - Joao Nogueira Batista {BIO 21373970 <GO>}

I did not attend the meeting myself. The meeting was attended exclusively by our CEO and I would not-- I would not like to share with you the contents of that meeting because I think the only ones that can discuss that publicly are the-- is the head of the integration team himself, Mr. Palosi [ph], because it would impolite to disclose the contents of that private conversation. So that would be something that has to be done by Mr. Palosi [ph] himself.

But what I can say to you is that we continue to be optimistic that there will be no major change in the way the company has been managed in the recent past. All of the declarations are in the direction that confirm that the major aspects of the policies, be it pricing or whatever, will be maintained in place. So we are optimistic that logic, hope and rationality will prevail at the end, as we have always said from the beginning.

Q - Emerson Leite {BIO 4003528 <GO>}

Okay, Joao, still on this issue, do you see any possibility of a settlement of the oil account happening before year end and, therefore, closing this window, this potential window for future liabilities for the next administration?

A - Joao Nogueira Batista {BIO 21373970 <GO>}

Yes, certainly. We are discussing this already with the national treasury. The auditing group which has to audit all the items in this (PP) account will finalize their investigations by the end of this month, November. So that we will have a final number, a final balance. And then we will finalize with the national treasury the settlement of this balance. This will not be something that will be left over.

Q - Emerson Leite {BIO 4003528 <GO>}

That's good news. Thank you, very much.

A - Joao Nogueira Batista {BIO 21373970 <GO>}

Thank you.

Operator

Thank you for your question, sir. Sir, there are no more questions at this time. You may proceed with your closing statement.

A - Joao Nogueira Batista {BIO 21373970 <GO>}

Well, thanks again for your attention and I think all our team, as usual, will be available for any further detailing or questioning that you may still have and look forward to talking to you soon. Thanks. Thanks, again. Bye-bye.

Operator

Ladies and gentlemen. your host is making today's conference available for replay, starting one hour from now and lasting through November 27th. You may access the replay by dialing 1-800-858-5309. That number again is 1-800-858-5309. At the voice prompt, enter your access code, 40469, followed by the passcode, 97898.

International participants may access the replay as well by dialing 334-323-7226 and entering the same access code and passcode. The replay will be available approximately one hour from now.

This does conclude our Petrobras conference for today. Thank you, very much for your participation. You may now disconnect.

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