

Driving regional integration

INTERVIEW WITH JOSÉ SERGIO GABRIELLI DE AZEVEDO

PRESIDENT & CEO, PETRÓLEOS BRASILEIROS S.A. (PETROBRAS)



JOSÉ SERGIO GABRIELLI is a native of Salvador and a graduate of the Federal University of Bahia. He received a PhD in Economics from Boston University in 1987 and has spent the early part of his career in academic institutions, including the University of Bahia and the London School of Economics as Visiting Research Scholar (2000-01). He was appointed Financial Director of Petrobras in February 2003 and served until July 2005 when he was appointed President of the Company.

Brazil is on course to achieve self-sufficiency in oil production in 2006. How significant is this achievement for the country, and for Petrobras?

Self-sufficiency in the production of crude oil is an achievement that will safeguard the Brazilian consumer at times of high volatility in international prices, such as those we are seeing at the moment. Fluctuations in the market can be fine-tuned with less pressure in a scenario where internal production is greater than demand. This comfortably balanced internal situation in the energy sector is a privilege that few industrialised countries in the world can boast, as the majority are heavily dependent on oil. Petrobras will have greater peace of mind to analyse external factors that influence price, albeit without ignoring what is occurring on the international market. With self-sufficiency, Petrobras – which has never allowed the country to suffer a lack of oil, even at times of global crisis in supplies – will be practically immune to any potential international shortage. The Company will not only be able to supply the domestic market, which is our main focus, but also significantly increase the volume of exports, with positive impacts on Brazil's balance of trade and the reduction of exchange rate volatility. By producing more than we require for internal consumption, Petrobras will have greater operational flexibility, thereby being in a position to manage the margins on refining and the commercialisation of oil. In international terms, energy stability will improve the global perception of Brazil and Petrobras, contributing to enhancement of the participation of the Company in the global market, and also in obtaining more advantageous finance terms.

The oil industry is a risky business at the best of times, and being at the cutting edge even more so. What measures and systems has Petrobras put in place to prevent the sort of major accidents that we saw five or six years ago from re-occurring, and to mitigate their impact when they do?

Environmental conservation, occupational health and operational safety have been an overriding concern of Petrobras throughout its history and in all its areas of activity. The ongoing rapid expansion of the Company that has occurred over the past few decades has increased its responsibility in these areas, leading to a process of integration and re-structuring of its mod-

els of operational safety and environmental management. As part of this strategy, Petrobras created the Excellence in Environmental Management and Operational Safety Programme – known by the acronym 'Pegaso'. The programme began to be implemented in 2000 and rapidly became the largest of its kind in the oil industry, with investments to the order of US\$ 4 billion. It involves four thousand projects, ranging from the revision of systems, construction and expansion of installations through to automation of the entire Company pipeline network. New Environmental Defense Centres, known locally as CDAs, have been set up alongside the main areas of activity of the Company, and systems for the reduction of residues and emissions from all units have been upgraded.

Seven years after losing its monopoly, Petrobras achieved its best ever set of financial results in 2005. Is this mainly a reflection of the high price of oil, or has the Company been significantly re-engineered in the intervening period?

The excellent financial results posted by the Company in 2005 reflect, among other things, the increase in oil production and the price of oil products, greater processing of domestic heavy crude in our refineries, enhanced use of the Company refining capacity and an increase in the export of oil and oil products. The 12 per cent appreciation in the value of the Real against the Dollar was another positive factor.

Seen from a broader perspective, the results are a reflection of the decisions taken over the past few years by the senior management of Petrobras, reversing the tendency of downsizing the Company that occurred in the first few years after losing its monopoly. As of 2003, Petrobras was once again structured as an integrated and united corporate system. From then onwards, the Company has seen marked growth in all segments and has become consolidated on the capital markets. The areas of exploration and production had been in decline, whereas today we have a portfolio of 131 exploratory blocks, as opposed to a mere 58 back in 2002. The effort exerted by the Company in the appropriation of reserves over these past three years has led to the building of a portfolio of over 30 projects for production and development. Never in its history has Petrobras had such a large portfolio of projects, both in exploration and production as well

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as in supply. This even includes the construction of a new refinery, which had not occurred since 1980, in addition to the expansion of existing units and the construction of 42 oil tanker vessels.

The intensification of exploratory investments by the Company has led to the discovery of five billion barrels of light crude, gas and heavy crude in the past two years and to our finding two new oil-rich provinces in Brazil. We have resumed investments in mature fields, which had seen a decline in production, that now contribute with over 500,000 barrels per day. Our proven reserves have increased over the past three years from 11 billion to approximately 15 billion barrels of oil equivalent (boe). These efforts, in conjunction with a commitment to quality and the constant quest to overcome challenges that are the hallmark of the Petrobras workforce, are undoubtedly responsible to a great extent for the excellent results in 2005.

Is the fact that the Brazilian Government retains a controlling stake in Petrobras an asset or a liability in terms of the Company's dealings with the international capital markets?

The participation of the Federal Government, which retains a controlling stake of 56 per cent of the voting capital, has not interfered in the operational and financial performance of Petrobras, as can be seen in the excellent results, nor in recognition by the international financial market, where the Company's classification was upgraded to investment grade tier for its foreign currency bond ratings by Moody's Investor Services in 2005. This recognition has made the Company more competitive thanks to the lower cost of capital, thereby increasing the opportunities for the development of new projects and consequently improving returns for our investors. It is important to remember that over 60 per cent of the capital of the Company is in private hands, while the ADR programme of the New York Stock Exchange is equivalent to 40 per cent of Petrobras' total capital.

Petrobras will invest US\$28 billion in E&P by 2010



PETROBRAS IMAGE BANK

Petrobras has for many years been the prime mover of energy integration in Latin America. How do you see this process moving forward in the light of proposed mega-projects such as the Venezuela-Argentina gas pipeline?

Petrobras not only believes that the energy integration of Latin America is a positive process for all the nations and companies involved, but has also been making concrete moves to achieve it by increasing its activities on the continent being now present in seven countries. We have been participating in preliminary studies seeking to integrate the supply of gas in South America and we believe that the concept is viable and may be achieved.

To what extent was the ongoing dispute with Bolivia (regarding the re-negotiation of existing gas supply contracts) a factor in getting the Venezuela-Argentina project fast-tracked?

We are increasing activities both in Venezuela and Argentina and are ready to sign a memorandum of understanding with Bolivia, thereby establishing a new form of partnership with the state oil company Yacimientos Petrolíferos Fiscales Bolivianos (YPFB). Subsequently, workgroups from both companies will sit down to outline details of cooperation and partnership. The important thing for Petrobras is to ensure the supply of Bolivian gas in the long term, in accordance with the prevailing contract. We are confident that an understanding can be reached to protect the interests of both parties. We need Bolivian gas and Bolivia needs the Brazilian market.

The ownership and exploitation of hydrocarbon resources is still an extremely sensitive issue in many parts of Latin America. How does a company like Petrobras avoid being seen as an "imperialist multinational"?

By associating with companies in our neighbouring countries, our intention is naturally to expand international activities, which is one of the premises in our Strategic Plan. However, we want this expansion to occur for our partners as well. For this reason, in tandem with our corporate interests, we make it abundantly clear in our strategy that we are concerned with contributing to the development of the countries in which we operate.

Petrobras and its partners have made significant gas discoveries in Brazil in recent years. What role do you see natural gas playing in the Company's future development?

Natural gas has experienced the highest percentage growth of any fuel in Brazil and the forecast is for 14.2 per cent growth per year through to 2010, by which

time we will be consuming approximately 100 million cubic metres of gas per day, which is double the current demand. Recognising this challenge, we have upped our total investments by 150 per cent in this segment in our Business Plan for 2006 through 2010, relative to previous plans. In order to consolidate the infrastructure that the gas and energy market will require, approximately US\$ 6.5 billion will be invested through to 2010, the bulk of which will be in gas pipelines. Funds earmarked by the Company for oil and gas exploration and production activities, which are not included in this total, will amount to US\$ 28 billion through to 2010. Our current daily production supplies 50 per cent of existing demand, which is to the order of 50 million cubic metres per day, and the shortfall is imported from Bolivia. The volume of future production from the natural gas reservoirs discovered over the past few years, mainly in the Santos Basin, should be added to these figures. Bolivia will continue to be an important external source to complement domestic production, although the contribution of other external sources located in South America has not been ruled out.

Is there a limit to how far companies can assume the responsibilities of governments? To what extent have the inequalities in Brazilian society influenced the way Petrobras relates to the communities in which it operates?

Petrobras is a corporation with shares traded on Brazilian and foreign stock exchanges, in which the government holds a 33 per cent stake in the total capital stock and 56 per cent of the voting capital. The Company operates in a traditional competitive market and does not assume the typical responsibilities or functions of government. Our strategy, adopted in the communities in which we operate, is to ensure conditions of sustainability in the projects that we sponsor, so that the community proper is able to take over the control and management of the programmes with time. One such project is the Petrobras Zero Hunger Campaign, the basic tenet of which is that the process of social inclusion should be conducted over a period of time, effecting change in living conditions in a sustainable manner, rather than simply attempting to eradicate hunger and poverty with the provision of food or traditional paternalist measures. With investments in the order of US\$140 million over four years, the project involves five major lines of activity in different areas: education, professional training and employment for youths and adults; providing employment and income; ensuring the rights of children and adolescents; social entrepreneurship, and volunteer social assistance. Petrobras also participates intensely in training programmes for suppliers to the oil and gas

industry. These actions are reflected not only in the image but also in the performance of the Company, to the extent that they contribute in stimulating the economy, as well as promoting the maturity of the market and strengthening Brazilian industry.

How did Petrobras become involved in the United Nations' Global Compact initiative, and what do you regard as the programme's greatest achievements to date?

Petrobras signed up to the Global Compact in 2003, assuming the commitment to stand by its principles and promote them among employees, shareholders, consumers, suppliers and other stakeholders. After joining, Petrobras was invited to participate in a selection process among 1200 companies and 350 business schools from around the world. At the end of the selection process, 24 institutions (12 companies and 12 schools) were chosen. This group is developing pioneering methodology to be adopted by the UN to train new corporate leaders worldwide to apply concepts and principles of corporate social and environmental responsibility in the management and administration of their companies. Selection of the participants was conducted by the European Foundation for Management Development, in association with the Global Compact/UN. Petrobras was the first company chosen for its involvement and professional handling of corporate social responsibility (CSR) matters in Company projects, both in Brazil and abroad.

Is CSR simply a means of offsetting the negative impact of any large-scale industrial activity, or is there a demonstrable benefit to businesses of conducting themselves in a more responsible manner?

Mitigation of the impact arising from its activities is not the basic premise of Petrobras actions in the area of social responsibility. This is witnessed by the fact that thousands of projects in the social, cultural, environmental and sports areas are not restricted to the scope of the communities in which the Company has operations. Its actions are of a local, regional and national nature, some of which achieve international renown, such as the backing of the Brazilian film production industry, which projects Brazil on the world market. Petrobras is the single biggest sponsor of culture in Brazil, and in international terms it is the oil company that has invested most in operational safety and environmental protection programmes over the past four years. Since it decided to become a benchmark in these areas some three years ago, Petrobras has been posting record financial and operational results, thereby proving the feasibility of combining corporate development with social and environmental responsibility. ■

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