BRAZILIAN PETROLEUM CORP
Form 6-K
June 13, 2005
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 6-K

REPORT OF FOREIGN PRIVATE ISSUER

PURSUANT TO RULE 13a-16 OR 15d-16 UNDER

THE SECURITIES EXCHANGE ACT OF 1934

For the month of June 2005

Commission File Number 1-15106

PETRÓLEO BRASILEIRO S.A. PETROBRAS

(Exact name of registrant as specified in its charter)

Brazilian Petroleum Corporation PETROBRAS

(Translation of Registrant s Name Into English)

Avenida República do Chile, 65

20035-900-Rio de Janeiro, RJ

Federative Republic of Brazil

(Address of principal executive offices)

(Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F.)

(Check One) Form 20-F x Form 40-F ¨

(Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934.)

(Check One) Yes ¨ No x

(If Yes is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b). 82-.)

Table of Contents

PETROBRAS ANNOUNCES FIRST QUARTER OF 2005 RESULTS

(Rio de Janeiro June 13, 2005) PETRÓLEO BRASILEIRO S.A. PETROBRAS today announced its consolidated results stated in U.S. dollars, prepared in accordance with U.S. GAAP.

PETROBRAS reported consolidated net income of U.S.$ 2,046 million and consolidated net operating revenues of U.S.$ 10,734 million for the first quarter of 2005, compared to consolidated net income of U.S.$ 1,337 million and consolidated net operating revenues of U.S.$ 7,935 million for the first quarter of 2004.

COMMENTS FROM THE CEO, MR. JOSE EDUARDO DE BARROS DUTRA

In the first quarter of 2005, we continued to consolidate our strategy and solidify the foundation to achieve impressive growth in our production. The positive results are a combination of favorable macroeconomic factors and our excellent operating performance.

In the quarter, U.S.$ 2,132 million was invested in Brazil and abroad, including project finance investments. The Exploration and Production and Supply areas received 58.6% and 18.3%, of the total amount invested, respectively.

We also managed to advance on several operating and corporate fronts in line with our Strategic Plan, some of which I highlight below:

Oil production began at FPSO P-48 on February 28, 2005. This unit, the second of the Barracuda and Caratinga project to begin operations, has the capacity to produce 150 thousand barrels of oil per day;

The start-up of FPSO P-48 and certain other projects combined with operational measures that seek to improve production capacity at our facilities, allowed us to achieve a new daily oil production record in Brazil. On March 30, 2005, our production was 1,651 thousand barrels per day. Several production records were subsequently surpassed, reinforcing our belief that we will be able to increase our average production to 1,700 thousand barrels per day in 2005;

The execution of contracts for U.S.$ 910 million in financing to implement the Director Plan for Oil Treatment and Transport in the Campos Basin (PDET). This plan includes assets associated with oil production and transportation from five platforms to be installed in the Campos Basin;

New discovery of light oil on the coast of the state of Espírito Santo, in wells drilled in the Golfinho field;

Discovery of light oil 33-grade API in the Santos Basin, located in the state of Rio de Janeiro, which also allowed us to book the natural gas discoveries made previously at well 1-RJ-587 as proved reserves;

Our refineries in Brazil broke records in the daily processing of oil with a volume of 1,870 thousand barrels per day. This result, achieved on March 9, 2005, is due to the integrated work of our teams, which seek to assure profitability and meet market needs according to the most advanced standards of environmental preservation; and

The start of exploration activities in Libya, which is the fourth African country in which we conduct operations.

Page: 1

Table of Contents

We close the first quarter of 2005 with the certainty of having achieved many of our objectives, mainly those focused on growth of the production of oil, natural gas and by-products.

We continue our preparations to achieve average daily production of 3,421 thousand barrels of oil equivalent in Brazil and abroad by 2010. This production volume will place us among the largest oil companies in the world.

Each quarter, with the consolidation of our goals and repeated record-breaking, we are even more certain that our future   thanks to the creativity and determination of our workforce   is to obtain profitable and sustainable growth for all of our shareholders.

Page: 2

Table of Contents

Financial Highlights

4Q-2004		For the first quarter of 2005	For the first quarter of 2004
	Income statement data		
14,722	Sales of products and services	14,782	11,176
10,701	Net operating revenues	10,734	7,935
552	Financial income (expense), net	(32)	(387)
1,707	Net income	2,046	1,337
1.56	Basic and diluted earnings per common and preferred share	1.87	1.22
	Other data		
41.5	Gross margin (%) [1]	51.5	48.9
16.0	Net margin (%) [2]	19.1	16.8
64	Debt to equity ratio (%) [3]	62	67
	Financial and Economic Indicators		
44.00	Brent crude (U.S.$/bbl)	47.50	31.95
2.7862	Average Commercial Selling Rate for U.S. Dollars (R$/U.S.$)	2.6672	2.8985
2.6544	Period-end Commercial Selling Rate for U.S. Dollars (R$/U.S.$)	2.6662	2.9086

(1) Gross margin equals net operating revenues less cost of sales divided by net operating revenues.

(2) Net margin equals net income divided by net operating revenues.

(3) Debt to equity ratio equals total liabilities divided by the sum of total liabilities and total shareholders equity.

	U.S. $ million			
	03.31.2005	12.31.2004	Percent Change (03.31.2005 versus 12.31.2004)	03.31.2004
Balance sheet data				
Total assets	64,589	63,082	2.4	53,782
Cash and cash equivalents	6,576	6,856	(4.1)	6,838
Short-term debt	1,014	547	85.4	759
Total long-term debt	12,918	13,344	(3.2)	13,135
Total project financings	5,719	5,712	0.1	5,908
Total capital lease obligations	1,315	1,335	(1.5)	1,536
Net debt [1]	14,390	14,082	2.2	14,200
Shareholders equity[2]	24,397	22,506	8.4	17,596
Total capitalization [3]	45,363	43,444	4.4	38,934

	U.S. $ million		
	03.31.2005	12.31.2004	03.31.2004
Reconciliation of Net debt			
Total long-term debt	12,918	13,334	13,135
Plus short-term debt	1,014	547	759
Plus total project financings	5,719	5,712	5,908
Plus total capital lease obligations	1,315	1,335	1,536
Less cash and cash equivalents	6,576	6,856	6,838
Less Junior Notes[4]			300
Net debt [1]	14,390	14,082	14,200

(1) Our net debt is not computed in accordance with U.S. GAAP and should not be considered in isolation or as a substitute for total long-term debt calculated in accordance with U.S. GAAP. Our calculation of net debt may not be comparable to the calculation of net debt by other companies. Management believes that net debt is an appropriate supplemental measure that helps investors assess our liquidity and assists management in targeting leverage improvements. Please see the table above for a reconciliation of net debt to total long-term debt.

(2) Shareholders equity includes unrecognized losses in the amount of U.S.$ 1,967 million at March 31, 2005, U.S.$ 1,975 million at December 31, 2004 and U.S.$ 1,578 million at March 31, 2004, in each case related to Amounts not recognized as net periodic pension cost .

(3) Total capitalization means shareholders equity plus short-term debt, total long-term debt, total project financings and total capital lease obligations

(4) In May 2004, PFL and the PF Export Trust, executed an amendment to the Trust Agreement allowing the Junior Trust Certificates to be set-off against the related Notes.

Page: 3

Table of Contents

OPERATING HIGHLIGHTS

		For the first quarter of	
4Q-2004		2005	2004
	Average daily crude oil and gas production		
1,680	Crude oil and NGLs *(Mbpd)* [1]	1,707	1,643
1,511	Brazil	1,543	1,475
169	International	164	168
2,160	Natural gas *(Mmcfpd)* [2]	2,184	2,118
1,602	Brazil	1,596	1,566
558	International	588	552
	Crude oil and NGL average sales price *(U.S. dollars per bbl)*		
35.11	Brazil [3]	37.48	29.53
27.18	International	31.31	25.37
	Natural gas average sales price *(U.S. dollars per Mcf)*		
2.14	Brazil	1.95	1.89
1.29	International	1.33	1.18
	Lifting costs *(U.S. dollars per boe)*		
	Crude oil and natural gas Brazil		
12.50	Including government take [4]	13.54	9.73
4.76	Excluding government take [4]	5.95	4.30
2.90	Crude oil and natural gas International	2.55	2.45
	Refining costs *(U.S. dollars per boe)*		
1.61	Brazil	1.82	1.22
1.22	International	1.26	1.14
	Refining and marketing operations *(Mbpd)*		
2,125	Primary Processed Installed Capacity	2,114	2,106
	Brazil		
1,996	Installed capacity	1,985	1,977
1,727	Output of oil products	1,708	1,726
89%	Utilization	87%	88%
	International		
129	Installed capacity	129	129
106	Output of oil products	108	99
83%	Utilization	83%	75%
77	**Domestic crude oil as % of total feedstock processed**	79	77
	Imports *(Mbpd)*		
452	Crude oil imports	322	417
132	Oil product imports	46	74
126	Import of gas, alcohol and others	115	105
	Exports (Mbpd)		
137	Crude oil exports	161	191
193	Oil product exports	235	196
10	Fertilizer and other exports	11	4
370	Net imports	76	205
	Sales Volume *(thousand bpd)*		
1,625	Oil Products	1,546	1,489
34	Alcohol and Others	29	28
227	Natural Gas	214	194
1,886	Total	1,789	1,711

614	Distribution	531	430
(548)	Inter-company sales	(488)	(386)
1,952	Total domestic market	1,832	1,755
341	Exports	406	391
272	International sales	253	250
114	Other operations [5]	166	132
727	Total international market	825	773
2,679	Total	2,657	2,528

(1) Includes production from shale oil reserves.

(2) Does not include liquefied natural gas. Includes reinjected gas.

(3) Crude oil and NGL average sales price in Brazil includes intra-company transfers and sales to third parties.

(4) Government take includes royalties, special government participation and rental of areas.

(5) Includes third-party sales by our international subsidiary, Petrobras International Finance Company (PIFCo).

Page: 4

Table of Contents

ANALYSIS OF OPERATING HIGHLIGHTS

Exploration and Production

Crude Oil and NGLs

Domestic crude oil and NGL production increased 4.6% to 1,543 thousand barrels per day for the first quarter of 2005, as compared to 1,475 thousand barrels per day for the first quarter of 2004. This increase was primarily due to: (1) the production start-up of FPSO-MLS (Marlim Sul) in June 2004; and (2) the anchoring and initial test production of platforms P-43 (Barracuda) and P-48 (Caratinga) in December 2004 and February 2005, respectively. These projects allowed us to achieve a record daily oil production in Brazil of 1,651 thousand barrels on March 30, 2005. In April 2005, we reached a new average oil production record of 1,704 thousand barrels per day.

International crude oil and NGL production decreased 2.4% to 164 thousand barrels per day for the first quarter of 2005, as compared to 168 thousand barrels per day for the first quarter of 2004, principally due to the decline in production in some mature fields at the facilities Argentina.

Natural Gas

Domestic natural gas production increased 1.9% to 1,596 million cubic feet per day (Mmcfpd) for the first quarter of 2005, as compared to 1,566 Mmcfpd for the first quarter of 2004. This increase was primarily the result of the Cabiúnas project, which is a program designed to meet the petrochemical sector s increased demands for natural gas.

International gas production increased 6.5% to 588 million cubic feet per day for the first quarter of 2005, as compared to 552 million cubic feet per day for the first quarter of 2004, principally due to increased production in Bolivia as a result of increased demand in Brazil and Argentina.

Lifting Costs

Our lifting costs in Brazil, excluding government take (comprised of royalties, special government participation and rental of areas), increased 38.4% to U.S.$ 5.95 per barrel of oil equivalent for the first quarter of 2005, from U.S.$ 4.30 per barrel of oil equivalent for the first quarter of 2004. This increase was primarily due to: (1) greater consumption of chemical products for the removal of obstructions and elimination of toxic gases, principally at Marlim; (2) increased expenses for specialized technical services for restoration and maintenance, mobilization of building structures and equipment; (3) additional costs for personnel transport, vessel support and undersea operations; and (4) increased personnel expenses primarily related to: (a) overtime payments as set forth in our collective bargaining agreement, (b) an increase in our workforce, and (c) a revision in the actuarial calculations relating to future health care and pension benefits.

Our lifting costs in Brazil, including government take, increased 39.2% to U.S.$ 13.54 per barrel of oil equivalent for the first quarter of 2005, from U.S.$ 9.73 per barrel of oil equivalent for the first quarter of 2004, due primarily to: (1) the increased operating expenses mentioned above; (2) increased expenses from special governmental participation due to the higher average reference price for domestic oil, which is based on international market prices; and (3) the 8.0% decrease in the average Real/U.S. dollar exchange rate for the first quarter of 2005 as compared to the average Real/U.S. dollar exchange rate for the first quarter of 2004.

Our international lifting costs increased 4.1% to U.S.$ 2.55 per barrel of oil equivalent for the first quarter of 2005, as compared to U.S.$ 2.45 per barrel of oil equivalent for the first quarter of 2004. This increase was primarily due to increased maintenance and third-party services expenses in Argentina and the United States.

Refining

The feedstock processed (output of oil products) by refineries in Brazil decreased 1.0% to 1,708 Mbpd during the first quarter of 2005, from 1,726 Mbpd during the first quarter of 2004, as a result of a planned

Table of Contents

stoppage of the distillation, cracking and propane units of the Capuava refinery (RECAP).

Refining costs

Domestic unit refining costs increased 49.2% to U.S.$ 1.82 per barrel of oil equivalent for the first quarter of 2005, as compared to U.S.$ 1.22 per barrel of oil equivalent for the first quarter of 2004. This increase was primarily due to: (1) increased personnel expenses primarily related to: (a) overtime payments as set forth in our collective bargaining agreement, (b) an increase in our workforce; and (c) a revision in the actuarial calculations relating to future health care and pension benefits; (2) costs associated with planned stoppages at certain refineries; and (3) third-party services, mainly for corrective maintenance.

International unit refining costs increased 10.5% to U.S.$1.26 per barrel of oil equivalent for the first quarter of 2005, as compared to U.S.$ 1.14 per barrel of oil equivalent for the first quarter of 2004. This increase was primarily due to increased personnel expenses, increases in the refineries gas and electricity consumption, and contracted services for facility maintenance in Argentina.

Sales Volume

Our domestic sales volume, consisting primarily of sales of diesel oil, gasoline, jet fuel, naphtha, fuel oil and liquefied petroleum gas, increased 4.4% to 1,832 thousand barrels per day for the first quarter of 2005, as compared to 1,755 thousand barrels per day for the first quarter of 2004. The increase was primarily due to the rise in sales of diesel oil and gasoline. The increase was partially offset by a reduction in the sales of naphtha and fuel oil due to lower demand for these oil by-products.

Page: 6

Table of Contents

ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

We earn income from:

- domestic sales, which consist of sales of oil products (such as diesel oil, gasoline, jet fuel, naphtha, fuel oil and liquefied petroleum gas), natural gas and petrochemical products;
- export sales, which consist primarily of sales of crude oil and oil products;
- international sales (excluding export sales), which consist of sales of crude oil, natural gas and oil products that are purchased, produced and refined abroad; and
- other sources, including services, investment income and foreign exchange gains.

Our expenses include:

- costs of sales (which are comprised primarily of labor expenses, cost of operating and purchases of crude oil and oil products); maintaining and repairing property, plants and equipment; depreciation and amortization of fixed assets and depletion of oil fields, and costs of exploration; ;
- selling, general and administrative expenses; and
- interest expense, monetary and foreign exchange losses.

Fluctuations in our financial condition and results of operations are driven by a combination of factors, including:

- the volume of crude oil, oil products and natural gas we produce and sell;
- changes in international prices of crude oil and oil products, which are denominated in U.S. dollars;
- related changes in domestic prices of crude oil and oil products, which are denominated in Reais;

fluctuations in the Real/U.S. dollar exchange rate;

Brazilian political and economic conditions; and

the amount of taxes and duties that we are required to pay with respect to our operations, by virtue of our status as a Brazilian company and our involvement in the oil and gas industry.

Table of Contents

RESULTS OF OPERATIONS FOR THE FIRST QUARTER OF 2005 COMPARED TO THE FIRST QUARTER OF 2004

The comparison between our results of operations for the first quarter of 2005 and the first quarter of 2004 has been affected by the 8.0% decrease in the average Real/U.S. dollar exchange rate for the first quarter of 2005 as compared to the average Real/U.S. dollar exchange rate for the first quarter of 2004. For ease, we refer to this change in the average exchange rate as the 8.0% increase in the value of the Real against the U.S. dollar in the first quarter of 2005, as compared to the first quarter of 2004.

Revenues

Net operating revenues increased 35,3% to U.S.$ 10,734 million for the first quarter of 2005, as compared to U.S.$ 7,935 million for the first quarter of 2004. This increase was primarily attributable to an increase in prices and sales volume in both the domestic market and outside Brazil, and to the 8.0% increase in the value of the Real against the U.S. dollar in the first quarter of 2005, as compared to the first quarter of 2004.

Consolidated sales of products and services increased 32.3% to U.S.$ 14,782 million for the first quarter of 2005, as compared to U.S.$ 11,176 million for the first quarter of 2004, primarily due to the increases mentioned above.

Included in sales of products and services are the following amounts which we collected on behalf of the federal or state governments:

- Value-added and other taxes on sales of products and services and social security contributions. These taxes increased 29.4% to U.S.$ 3,386 million for the first quarter of 2005, as compared to U.S.$ 2,616 million for the first quarter of 2004, primarily due to the increase in prices and sales volume of products and services; and

- CIDE, the per-transaction tax due to the federal government, which increased 5.9% to U.S.$ 662 million for the first quarter of 2005, as compared to U.S.$ 625 million for the first quarter of 2004. This increase was primarily attributable to the increase in sales volume of products and services and to the 8.0% increase in the value of the Real against the U.S. dollar in the first quarter of 2005, as compared to the first quarter of 2004.

Cost of sales

Cost of sales for the first quarter of 2005 increased 28.3% to U.S.$ 5,206 million, as compared to U.S.$ 4,058 million for the first quarter of 2004. This increase was principally a result of:

- a U.S.$ 516 million increase in the cost of imports due to higher prices for the volumes imported;

a U.S.$ 160 million increase in costs associated with our international trading activities, due to increases in volume and prices from offshore operations, conducted by PIFCo;

a U.S.$ 161 million increase in costs associated with a 4.4% increase in our domestic sales volumes;

a U.S.$ 81 million increase in taxes and charges imposed by the Brazilian government totaling U.S.$ 809 million for the first quarter of 2005, as compared to U.S.$ 728 million for the first quarter of 2004, including an increase in the special participation charge (an extraordinary charge payable in the event of high production and/or profitability from our fields) to U.S.$ 421 million for the first quarter of 2005, as compared to U.S.$ 366 million for the first quarter of 2004, as a result of higher international oil prices and increased levels of production; and

the 8.0% increase in the value of the Real against the U.S. dollar in the first quarter of 2005, as compared to the first quarter of 2004.

Page: 8

Table of Contents

Depreciation, depletion and amortization

We calculate depreciation, depletion and amortization of exploration and production assets on the basis of the units of production method. Depreciation, depletion and amortization expenses increased 25.7% to U.S.$ 670 million for the first quarter of 2005, as compared to U.S.$ 533 million for the first quarter of 2004. This increase was primarily attributable to the following:

- Increase in the depreciation rates from the Roncador, Marlim Sul and Jubarte Fields as a result of increased production;
- Increased property, plant and equipment (PP&E) expenditures associated with our crude oil and natural gas production; and
- the 8.0% increase in the value of the Real against the U.S. dollar in the first quarter of 2005, as compared to the first quarter of 2004.

Exploration, including exploratory dry holes

Exploration costs, including exploratory dry holes decreased 11.4% to U.S.$ 109 million for the first quarter of 2005, as compared to U.S.$ 123 million for the first quarter of 2004. This decrease was primarily attributable to a decrease of U.S.$ 70 million in dry holes expenses, which was partially offset by an increase of U.S.$ 50 million in geophysical and geological expenses.

Page: 9

Table of Contents

Selling, general and administrative expenses

Selling, general and administrative expenses increased 53.2 % to U.S.$ 875 million for the first quarter of 2005, as compared to U.S.$ 571 million for the first quarter of 2004.

Selling expenses increased 51.7% to U.S.$ 440 million for the first quarter of 2005, as compared to U.S.$ 290 million for the first quarter of 2004. This increase was primarily attributable to the following:

- an increase of U.S.$ 99 million in expenses mainly associated with the transportation costs of oil products; and
- the 8.0% increase in the value of the Real against the U.S. dollar in the first quarter of 2005, as compared to the first quarter of 2004.

General and administrative expenses increased 54.8% to U.S.$ 435 million for the first quarter of 2005, as compared to U.S.$ 281 million for the first quarter of 2004. This increase was primarily attributable to the following:

- an increase of approximately U.S.$ 77 million in expenses related to technical consulting services in connection with our increased outsourcing of selected non-core general activities;
- an increase of approximately U.S.$ 41 million in employee expenses due to the increase in our workforce and salaries; and an increase in the actuarial calculations relating to future health care and pension benefits; and
- the 8.0% increase in the value of the Real against the U.S. dollar in the first quarter of 2005, as compared to the first quarter of 2004.

Research and development expenses

Research and development expenses increased 44.2% to U.S.$ 75 million for the first quarter of 2005, as compared to U.S.$ 52 million for the first quarter of 2004. This increase was primarily related to additional investments in programs for environmental safety, deepwater and refining technologies of, approximately, U.S.$ 18 million and to the 8.0% increase in the value of the Real against the U.S. dollar in the first quarter of 2005, as compared to the first quarter of 2004.

Other operating expenses

Other operating expenses increased to an expense of U.S.$ 89 million for the first quarter of 2005, as compared to an expense of U.S.$ 62 million for the first quarter of 2004.

The most significant charges for the first quarter of 2005 were:

a U.S.$ 51 million expense related to idle capacity from thermoelectric power plants;

a U.S.$ 24 million expense for unscheduled stoppages of plant and equipment; and

a U.S.$ 14 million increase in contractual losses from compliance with our ship or pay commitments with respect to our investments in the OCP pipeline in Ecuador.

The charges for the first quarter of 2004 were:

a U.S.$ 38 million expense for unscheduled stoppages of plant and equipment;

a U.S.$ 19 million operating expense related to idle capacity from thermoelectric power plants; and

a U.S.$ 5 million increase in contractual losses from compliance with our ship or pay commitments with respect to our investments in the OCP pipeline in Ecuador.

Equity in results of non-consolidated companies

Equity in results of non-consolidated companies decreased 57.4% to a gain of U.S.$ 23 million for the first quarter of 2005, as compared to a gain of U.S.$ 54 million for the first quarter of 2004.

Table of Contents

This decrease was mainly attributable to a gain of U.S.$ 7 million for the first quarter of 2005, as compared to a gain of U.S.$ 28 million for the first quarter of 2004, from our investments in natural gas distribution activities.

Financial income

We derive financial income from several sources, including interest on cash and cash equivalents. The majority of our cash equivalents are short-term Brazilian government securities, including securities indexed to the U.S. dollar. We also hold U.S. dollar deposits.

Financial income increased to U.S.$ 390 million for the first quarter of 2005 as compared to U.S.$ 146 million for the first quarter of 2004. This increase was primarily attributable to fair value adjustments on gas hedge transactions, which resulted in a mark-to-market gain of U.S.$ 232 million for the first quarter of 2005. See Note 7 to our unaudited consolidated financial statements as of March 31, 2005 for a breakdown of financial income and expenses.

Financial expense

Financial expense decreased 15.0% to U.S.$ 431 million for the first quarter of 2005, as compared to U.S.$ 507 million for the first quarter of 2004. This decrease was primarily attributable to the following:

- a U.S.$ 2 million expense relating to repurchases of our own securities for the first quarter of 2005, as compared to an expense of U.S.$ 58 million for the first quarter of 2004.; and

- a U.S.$ 48 increase in our interest expense capitalized as part of the cost of construction and development of crude oil and natural gas production projects.

Monetary and exchange variation on monetary assets and liabilities, net

Monetary and exchange variation on monetary assets and liabilities, net generated a gain of U.S.$ 9 million for the first quarter of 2005, as compared to a loss of U.S.$ 26 million for the first quarter of 2004. The increase in monetary and exchange variation on monetary assets and liabilities, net is primarily attributable to the effect of the 0.4% depreciation of the Real against the U.S. dollar during the first quarter of 2005, as compared to the 0.7% depreciation of the Real against the U.S. dollar during the first quarter of 2004.

Employee benefit expense

Employee benefit expense consists of financial costs associated with expected pension and health care costs. Our employee benefit expense increased 20.0% to U.S.$ 192 million for the first quarter of 2005, as compared to U.S.$ 160 million for the first quarter of 2004. This increase in costs was primarily attributable to an increase of U.S.$ 19 million from the annual actuarial calculation of our pension and health care plan liability; and to the 8.0% increase in the value of the Real against the U.S. dollar in the first quarter of 2005, as compared to the first quarter of 2004.

Other taxes

Other taxes, consisting of miscellaneous value-added, transaction and sales taxes, decreased 19.8% to U.S.$ 81 million for the first quarter of 2005, as compared to U.S.$ 101 million for the first quarter of 2004. This decrease was primarily attributable to the decrease of U.S.$ 28 million in the PASEP/COFINS taxes on financial income, due to a reduction in the applicable rate as of August 2, 2004. This decrease was partially offset by the 8.0% increase in the value of the Real against the U.S. dollar in the first quarter of 2005, as compared to the first quarter of 2004.

Other expenses, net

Other expenses, net are primarily composed of gains and losses recorded on general advertising and marketing expenses, legal reserves, community investments and certain other non-recurring charges. Other expenses, net increased to an expense of U.S.$ 191 million, for the first quarter of 2005, as compared to an expense of U.S.$ 41 million for the first quarter of 2004.

Table of Contents

The most significant charges for the first quarter of 2005 were:

- a U.S.$ 132 million expense for legal liability and contingencies related to pending lawsuits; and
- a U.S.$ 72 million expense for general advertising and marketing expenses unrelated to direct revenues as well as certain cultural projects.

The most significant charges the first quarter of 2004 were:

- a U.S.$ 38 million expense for general advertising and marketing expenses unrelated to direct revenues; and
- a U.S.$ 6 million expense for legal liability and contingencies related to pending lawsuits.

Income tax (expense) benefit

Income before income taxes, minority interest and accounting changes increased to U.S.$ 3,237 million for the first quarter of 2005, as compared to U.S.$ 1,901 million for the first quarter of 2004. As a result, we recorded an income tax expense of U.S.$ 1,201 million for the first quarter of 2005, as compared to an expense of U.S.$ 557 million for the first quarter of 2004.

The reconciliation between the tax calculated based upon statutory tax rates to income tax expense and effective rates is shown in Note 3 to our unaudited consolidated financial statements as of March 31, 2005.

Table of Contents

THE PETROLEUM AND ALCOHOL ACCOUNT

Prior to 2002, the Petroleum and alcohol account was a special account that reflected the impact on us of the Brazilian government s regulatory policies for the Brazilian oil industry and its fuel alcohol program. To facilitate the eventual settlement of the account, the Brazilian government issued National Treasury Bonds-Series H in our name, which were placed with a federal depositary to support the balance of the account.

In accordance with Brazilian legislation, the fuel market was deregulated in its entirety in January 2002. On March 31, 2005 the balance of the Petroleum and alcohol account was U.S.$ 282 million.

Under Brazilian law, the settlement of the Petroleum and alcohol account with the Brazilian government should have occurred by June 30, 2004. On July 2, 2004, the Government effected a deposit in the amount of U.S.$ 56 million corresponding to the National Treasury Bonds-Series H, as they had expired, in partial guarantee of the amount of the accounts, of which U.S.$ 3 million were made available to us and the remaining U.S.$ 53 million was placed in an account, in our favor, although we are prevented from withdrawing or transferring these bonds. We have continued discussions with the National Treasury Secretary in order to conclude the settlement process.

The value of the Petroleum and alcohol account may be paid by issuing National Treasury shares in an amount equal to the final value of the account or by canceling amounts that we may owe to the Federal Government, including taxes or a combination of the foregoing options.

The following summarizes the changes in the Petroleum and Alcohol Account for the first quarter of 2005:

	U.S. $ million
Balance as of December 31, 2004	282
Financial income	1
Translation loss	(1)
Balance as of March 31, 2005	**282**

Table of Contents

BUSINESS SEGMENTS

NET INCOME BY BUSINESS SEGMENT

	U.S. $ million For the first quarter of	
	2005	**2004**
Exploration and Production [1]	1,804	1,175
Supply [1] [2]	590	399
Gas and Energy	75	(86)
International [2]	122	35
Distribution	59	38
Corporate	(455)	(304)
Eliminations	(149)	80
Net income	2,046	1,337

[1] Beginning in 2005, revenues from the sale of oil to third parties are classified in accordance with the points of sale, which are either the Exploration & Production or Supply segments. Before 2005, revenues from the sale of oil were solely allocated to Exploration & Production. The change in classification generated no significant impact on the results reported for these segments. Segment information has not been restated, as it is impractical to gather and collect data for prior periods as to points of sale.

[2] Net operating revenues and cost of sales with respect to periods prior to the third quarter of 2004 were reclassified from the International segment to the Supply segment in relation to certain offshore operations. There was no significant impact on the results reported for these segments.

Table of Contents

Exploration and Production

Our exploration and production segment includes our exploration, development and production activities in Brazil, sales and transfers of crude oil in the domestic and foreign markets and transfers of natural gas to our Gas and Energy segment.

Consolidated net income for our exploration and production segment increased 53.5% to U.S.$ 1,804 million for the first quarter of 2005, as compared to U.S.$ 1,175 million for the first quarter of 2004. This increase was primarily attributable to:

- a U.S.$ 1,302 million increase in net operating revenues, primarily related to the positive effects of higher international oil prices on the sales/transfer prices of domestic oil, the 4.6% increase in oil and NGL production, and the 1.9% increase natural gas production, despite the more moderate price increases of heavy crude oil in the international market compared to lighter crude oil. The spread between the price of domestic oil sold/transferred and the average Brent price rose from U.S.$ 2.42/bbl in the first quarter of 2004, to U.S.$ 10.02/bbl in the first quarter of 2005.

These effects were partially offset by the following items:

- a U.S.$ 339 million increase in cost of sales as a result of an increase in our production costs because the 4.6% increase in oil and NGL production, the 1.9% increase in natural gas production and the 8.0% increase in the value of the Real against the U.S. dollar in the first quarter of 2005, as compared to the first quarter of 2004; and

- a U.S.$ 26 million increase in depreciation, depletion and amortization expenses, primarily attributable to increased rates in the depreciation of Roncador, Marlim Sul and Jubarte fields as a result of increased production, increased PP&E expenditures associated with our crude oil and natural gas production and the 8.0% increase in the value of the Real against the U.S. dollar in the first quarter of 2005, as compared to the first quarter of 2004.

Supply

Our supply segment includes refining, logistics, transportation and the purchase of crude oil, as well as the purchase and sale of oil products and fuel alcohol. Additionally, this segment includes the petrochemical and fertilizers division, which includes investments in domestic petrochemical companies and our two domestic fertilizer plants.

Our supply segment registered net income of U.S.$ 590 million for the first quarter of 2005, an increase of 47.9% as compared to net income of U.S.$ 399 million for the first quarter of 2004. This increase was primarily a result of:

- an increase of U.S.$ 2,598 million in net operating revenues, primarily related to the 3.8% increase in sales volume in the domestic market, the increase in the average realization value of oil products sold in the domestic and foreign markets and the 8.0% increase in the value of the Real against the U.S. dollar in the first quarter of 2005, as compared to the first quarter of 2004.

These effects were partially offset by the following items:

- an increase of U.S.$ 2,034 million in the cost of sales, mainly attributable to: (1) an increase in the cost to acquire oil and oil products because of higher international prices despite the increased spread between heavy and light crude; (2) increased freight costs; (3) higher refining costs; and (4) a 3.8% increase in the volume of oil products sold in the domestic market;

- a U.S.$109 million expense related to contingencies for legal proceedings;

- an increase of U.S.$ 63 million in selling, general and administrative expenses, primarily related to the increase in sales expenses arising from increased volumes sold and additional freight costs; and

- an increase of U.S.$ 85 million in depreciation, depletion and amortization resulting from additional investments in refining facilities in order to optimize production and increase processing capacity.

Table of Contents

Gas and Energy

Our gas and energy segment consists principally of the purchase, sale, transportation and distribution of natural gas produced in or imported into Brazil. Additionally, this segment includes our participation in domestic electricity production, including investments in domestic natural gas transportation companies, state owned natural gas distributors and thermoelectric companies.

Our gas and energy segment registered net income of U.S.$ 75 million for the first quarter of 2005, as compared to a net loss of U.S.$ 86 million in the first quarter of 2004. This increase was primarily a result of:

- a U.S.$ 197 million increase in net operating revenues primarily due to: (1) the 10.3% increase in the volume of natural gas sold, reflecting the continued expansion of natural gas consumption in Brazil in the industrial, automotive and thermal generation segments; (2) the increase in revenues from energy commercialization, and (3) the effects of the 8.0% increase in the value of the Real against the U.S. dollar in the first quarter of 2005, as compared to the first quarter of 2004; and

- financial income, net, of U.S.$ 182 million in the first quarter of the 2005 as compared to financial expenses, net, of U.S.$ 82 million in the first quarter of 2004. This financial income was primarily attributable to the recognition of a U.S.$ 232 million gain with respect to a fair value adjustment on a gas hedge transaction.

These effects were partially offset by the following items:

- an increase of U.S.$ 51 million in operating expense as a result of certain thermoelectric power plants remaining unexpectedly idle; and

- an increase of U.S.$ 45 million in selling, general and administrative expenses, mainly as a result of an increase in expenses relating to personnel as well as technical and consulting services.

International

The international segment represents our international activities conducted in 13 countries, which include Exploration and Production, Supply, Distribution and Gas and Energy.

Consolidated net income for our international segment was U.S.$ 122 million in the first quarter of 2005, as compared to U.S.$ 35 million in the first quarter of 2004. This increase was primarily a result of:

- an increase of U.S.$ 300 million of net operating revenues, which primarily reflects the effects of increased international oil prices, increased gas sales from Bolivia to Brazil, and sales of natural gas from Bolivia to Argentina that began in mid-2004.

These effects were partially offset by the following items:

- an increase of U.S.$ 197 million in cost of sales, principally related to the increased sales volume and an increase in the refining costs; and

- financial expenses, net of U.S.$ 155 million in the first quarter of 2005 as compared to U.S.$ 131 million in the first quarter of 2004, primarily as a result of the Argentine Peso/U.S. dollar exchange rate as well as from losses associated with PEPSA s hedge operations that totaled U.S.$ 25 million.

Distribution

Our distribution segment represents the oil product and fuel alcohol distribution activities conducted by our majority owned subsidiary, Petrobras Distribuidora S.A. - BR in Brazil. In accordance with our strategic objectives to increase market share in the LPG distribution segment and consolidate the automotive fuels distribution market in certain regions of Brazil, our distribution business now includes the operations of Liquigás Distribuidora S.A (formerly known as Sophia do Brasil S.A. and Agip do Brasil S.A.), which was acquired on August 9, 2004.

Our participation in the Brazilian fuel distribution market in the first quarter of 2005 represented 35.1% of all sales as compared to 32.1% in the first quarter of 2004.

Consolidated net income for our distribution segment increased 55.3% to U.S.$ 59 million for the first quarter of 2005, as compared to U.S.$ 38 million for the first quarter of 2004,

Table of Contents

primarily attributable to the U.S.$ 1,223 million increase in net operating revenues, which resulted from the 22.0% increase in sales volume and the effects of the 8.0% increase in the value of the Real against the U.S. dollar in first quarter of 2005, as compared to the first quarter of 2004.

These effects were partially offset by the following items:

- an increase of U.S.$ 1,100 million in the cost of sales, mainly attributable to the 22.0% increase in sales volume and due to the effects of the 8.0% increase in the value of the Real against the U.S. dollar in the first quarter of 2005, as compared to the first quarter of 2004; and

- an increase of U.S.$ 58 million in selling, general and administrative expenses, mainly due to increased expenses for distribution of products.

Corporate

Our corporate segment includes those activities not attributable to other segments, including corporate financial management, overhead related to central administration and other expenses, including actuarial expenses related to our pension and health care plans.

Consolidated net loss for the units that make up our corporate segment increased 49.7% to U.S.$ 455 million in the first quarter of 2005, as compared to a net loss of U.S.$ 304 million in the first quarter of 2004. This increase in net loss was primarily attributable to:

- a U.S.$ 119 million decrease in gains associated with income tax benefit, principally deferred tax;

- an increase of U.S.$ 66 million in selling, general and administrative expenses, mainly as a result of the increase in expenses related to technical consulting services in connection with our increased outsourcing of selected non-core general activities and an increase in our expenses with employees due to the increase in our workforce and salaries, an increase in the actuarial calculations relating to future health care and pension;

- an increase of U.S.$ 31 million in employee benefit expense, primarily attributable to an increase of U.S.$ 19 million from the annual actuarial calculation of our pension and health care plan liability; and

- to the 8.0% increase in the value of the Real against the U.S. dollar in the first quarter of 2005, as compared to the first quarter of 2004.

These effects were partially offset by a U.S.$ 104 million reduction in financial expenses, net, primarily attributable to reduced repurchases of our own securities during the first quarter of 2005 as compared to the first quarter of 2004, and to the 8.0% increase in the value of the Real against the U.S. dollar in the first quarter of 2005, as compared to the first quarter of 2004.

Table of Contents

LIQUIDITY AND CAPITAL RESOURCES

Overview

Our principal uses of funds are for capital expenditures, dividend payments and repayment of debt. We have historically met these requirements with internally generated funds, short-term debt, long-term debt, project financings and sale and lease back agreements. We believe these sources of funds, together with our strong cash and cash equivalents on hand, will continue to allow us to meet our currently anticipated capital requirements.

Financing Strategy

The objective of our financing strategy is to help us achieve the targets set forth in our new Strategic Plan released on May 14, 2004, which provides for capital expenditures of U.S.$ 53.6 billion from 2004-2010. We also aim to increase the average life of our debt portfolio and reduce our cost of capital through a variety of medium and long-term financing arrangements, including supplier financing, project financing, bank financing, securitizations and the issuances of debt and equity securities.

Government Regulation

The Ministry of Planning, Budget and Management controls the total amount of medium and long-term debt that we and our Brazilian subsidiaries are allowed to incur through the annual budget approval process (*Plano de Dispêndio Global*, or PDG). Before issuing medium and long-term debt, we and our Brazilian subsidiaries must also obtain the approval of the National Treasury shortly before issuance.

All of our foreign currency denominated debt, as well as the foreign currency denominated debt of our Brazilian subsidiaries requires registration with the Central Bank. The issuance of debt by our international subsidiaries, however, is not subject to registration with the Central Bank or approval by the National Treasury. In addition, all issuances of medium and long-term notes and debentures require the approval of our board of directors. Borrowings that exceed the approved budget amount for any year also require approval from the Brazilian Senate.

Sources of Funds

Our Cash Flow

At March 31, 2005, we had cash and cash equivalents of U.S.$ 6,576 million as compared to U.S.$ 6,838 million at March 31, 2004.

Operating activities provided net cash flows of U.S.$ 3,375 million for the first quarter of 2005, as compared to providing U.S.$ 1,541 million for the first quarter of 2004. Major effect to cash generated by operating activities were net operating revenues of U.S.$ 10,734 million, non-cash provisions of U.S.$ 670 million for DD&A and U.S.$ 345 million for deferred tax.

Investing activities used net of cash of U.S.$ 2,191 million for the first quarter of 2005, as compared to using U.S.$ 1,372 million for the first quarter of 2004. This increase was due primarily to our investments in capital expenditures associated with our operating activities, which used U.S.$ 2,132 million of cash, including U.S.$ 1,249 million in relation to Campos Basin projects.

Financing activities used net cash of U.S.$ 1,450 million in the first quarter of 2005, as compared to using net cash in the amount of U.S.$ 1,706 million in the first quarter of 2004. Levels of financing activities from the first quarter of 2004 to the first quarter of 2005 remained significantly unchanged. Dividends paid in the first quarter of 2005 were U.S.$ 1,277 million. Additionally, in the first quarter of 2005, we increased our short-term debt position by taking advantage of better market conditions in Argentina.

Short-Term Debt

Our outstanding short-term debt serves mainly to support our imports of crude oil and oil products, and is provided almost completely by international banks. At March 31, 2005, our short-term debt (excluding current portions of long-term obligations)

Table of Contents

increased to U.S.$ 1,014 million as compared to U.S.$ 547 million at December 31, 2004. This increased use of short-term credit facilities was due to advantageous market conditions in Argentina, as explained immediately above.

Long-Term Debt

Our outstanding long-term debt consists primarily of the issuance of securities in the international capital markets and debentures in the domestic capital markets and amounts outstanding under facilities guaranteed by export credit agencies and multilateral agencies, as well as financing from the Banco Nacional de Desenvolvimento Econômico e Social (the Brazilian National Development Bank, or BNDES) and other financial institutions. Outstanding long-term debt, plus the current portion of our long-term debt, totaled U.S.$ 12,918 million at March 31, 2005, as compared to U.S.$ 13,344 million at December 31, 2004. This decrease was a result of our decision to pay down U.S.$ 525 million of our long-term obligations.

Project Finance

Since 1997, we have utilized project financings to provide capital for our large exploration and production and related projects, including some natural gas processing and transportation systems. All of these projects, and their related debt obligations, are on-balance sheet and accounted for under the line item Project Financings . Under typical contractual arrangements, we are responsible for completing the development of the oil and gas fields, operating the fields, paying all operating expenses relating to the projects and remitting a portion of the net proceeds generated from the fields to fund the special purpose companies debt and return on equity payments. At the end of each financing project, we have the option to purchase the project assets from the special purpose company or, in some cases, acquire control over the special purpose company itself.

Outstanding project financing, plus the current portion of our project financing, totaled U.S.$ 5,719 million at March 31, 2005, as compared to U.S.$ 5,712 million at December 31, 2004.

Thermoelectric liabilities

The balance of thermoelectric liabilities was U.S$ 831 million and U.S.$ 1,095 million at March 31, 2005 and December 31, 2004, respectively. These thermoelectric obligations resulted from thermoelectric plants owned by us, which we consolidated pursuant to FIN 46. All thermoelectric obligations are on balance sheet and accounted for under the line item Thermoelectric liabilities.

Extinguished securities

At March 31, 2005 and December 31, 2004, we had amounts invested abroad in an exclusive investment fund that held debt securities of some of our group companies in the amount of U.S.$ 2,037 million and U.S.$ 2,013 million, respectively. Once these securities are purchased by the fund, the related amounts, together with applicable interest are removed from the presentation of marketable securities and long-term debt. See note 6 to our unaudited consolidated financial statements as of March 31, 2005.

Off Balance Sheet Arrangements

At March 31, 2005, we had no off-balance sheet arrangements that have, or are reasonably likely to have, a material effect on our financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

Uses of Funds

Capital Expenditures

In the pursuit of the goals outlined in our strategic plan we continue to prioritize capital expenditures for the development of crude oil and natural gas production projects through internal investments and through structured undertakings with partners.

We invested a total of U.S.$ 2,132 million in the first quarter of 2005, a 61.1% increase from our investments in the first quarter of 2004. Our investments in the first quarter of 2005 were primarily directed towards increasing our production capabilities in the Campos Basin, modernizing our refineries and expanding our pipeline transportation and distribution systems. Of the total amount of capital expenditures in the first quarter of

Table of Contents

2005, U.S.$ 1,249 million were made in connection with exploration and development projects mainly in the Campos Basin (58.6%), which includes investments financed through project financing structures.

The following table sets forth our consolidated capital expenditures (including project financings and investments in thermoelectric power plants) for each of our business segments for the first quarters of 2005 and 2004:

Activities

	U.S.$ million For the three-month period ended March 31,	
	2005	**2004**
Exploration and Production	1,249	845
Supply	390	248
Gas and Energy	181	39
International:		
Exploration and Production	142	119
Supply	5	12
Distribution	2	3
Gas and Energy	24	
Distribution	42	24
Corporate	97	33
Total capital expenditures	**2,132**	**1,323**

Page: 20

Table of Contents

Income Statement

(in millions of U.S. dollars, except for share and per share data)

4Q-2004		For the first quarter of 2005	2004
14,722	Sales of products and services	14,782	11,176
	Less:		
(3,349)	Value-added and other taxes on sales and services	(3,386)	(2,616)
(672)	CIDE	(662)	(625)
10,701	Net operating revenues	10,734	7,935
(6,257)	Cost of sales	(5,206)	(4,058)
(667)	Depreciation, depletion and amortization	(670)	(533)
(176)	Exploration, including exploratory dry holes	(109)	(123)
(65)	Impairment		
(912)	Selling, general and administrative expenses	(875)	(571)
(68)	Research and development expenses	(75)	(52)
(84)	Other operating expenses	(89)	(62)
(8,229)	Total costs and expenses	(7,024)	(5,399)
31	Equity in results of non-consolidated companies	23	54
366	Financial income	390	146
(303)	Financial expense	(431)	(507)
489	Monetary and exchange variation on monetary assets and liabilities, net	9	(26)
(182)	Employee benefit expense	(192)	(160)
(95)	Other taxes	(81)	(101)
(31)	Other expenses, net	(191)	(41)
275		(473)	(635)
2,747	Income before income taxes and minority interests and accounting change	3,237	1,901
	Income tax expense:		
(647)	Current	(856)	(594)
20	Deferred	(345)	37
(627)	Total income tax expense	(1,201)	(557)
(413)	Minority interest in results of consolidated subsidiaries	10	(7)
1,707	Net income for the period	2,046	1,337
	Weighted average number of shares outstanding		
634,168,418	Common/ADS	634,168,418	634,168,418
462,369,507	Preferred/ADS		