Brazil’s political and economic scenario and O&G sectorial trends

Ricardo Sennes
PRESENTING PROSPECTIVA

AREAS OF OPERATION

- Strategic consulting for public policies
- Intelligence & Analysis
- Market-oriented institutional actions

38

Experienced Professionals on our team
Political & Economic Context
FRAGMENTED POLITICAL SYSTEM

- Weak party programs and identity
- Incentives for creating new parties
- Complex governability
- Hard to build a majority

House of Representatives
25 Parties

<table>
<thead>
<tr>
<th>Party</th>
<th>Seats</th>
</tr>
</thead>
<tbody>
<tr>
<td>PROS</td>
<td>7</td>
</tr>
<tr>
<td>PSOL</td>
<td>6</td>
</tr>
<tr>
<td>REDE</td>
<td>4</td>
</tr>
<tr>
<td>PTdoB</td>
<td>3</td>
</tr>
<tr>
<td>PEN</td>
<td>3</td>
</tr>
<tr>
<td>PSL</td>
<td>2</td>
</tr>
<tr>
<td>PMB</td>
<td>2</td>
</tr>
<tr>
<td>PSC</td>
<td>7</td>
</tr>
<tr>
<td>PPS</td>
<td>8</td>
</tr>
<tr>
<td>PHS</td>
<td>7</td>
</tr>
<tr>
<td>PV</td>
<td>6</td>
</tr>
</tbody>
</table>

Outros (55)

Senate
18 Parties

<table>
<thead>
<tr>
<th>Party</th>
<th>Seats</th>
</tr>
</thead>
<tbody>
<tr>
<td>PCdoB</td>
<td>1</td>
</tr>
<tr>
<td>PPS</td>
<td>1</td>
</tr>
<tr>
<td>PRB</td>
<td>1</td>
</tr>
<tr>
<td>PSC</td>
<td>2</td>
</tr>
<tr>
<td>PTC</td>
<td>1</td>
</tr>
<tr>
<td>PV</td>
<td>1</td>
</tr>
<tr>
<td>REDE</td>
<td>1</td>
</tr>
<tr>
<td>S/Partido</td>
<td>1</td>
</tr>
</tbody>
</table>
THREE FACTORS HAVE CONTRIBUTED TO THE DEEPENING OF THE CRISIS

**FISCAL AND INVESTMENT CRISIS**

Public Sector Indicators (%GDP)

<table>
<thead>
<tr>
<th>Year</th>
<th>Primary result</th>
<th>Net dbt</th>
</tr>
</thead>
<tbody>
<tr>
<td>2009</td>
<td>42.1</td>
<td></td>
</tr>
<tr>
<td>2010</td>
<td>39.1</td>
<td></td>
</tr>
<tr>
<td>2011</td>
<td>36.4</td>
<td></td>
</tr>
<tr>
<td>2012</td>
<td>35.3</td>
<td></td>
</tr>
<tr>
<td>2013</td>
<td>33.9</td>
<td></td>
</tr>
<tr>
<td>2014</td>
<td>36.8</td>
<td></td>
</tr>
<tr>
<td>2015</td>
<td>36.2</td>
<td></td>
</tr>
<tr>
<td>2016</td>
<td>40.5</td>
<td></td>
</tr>
</tbody>
</table>

**BURSTING OF TWO BUBBLES**

**Automobile**
- Production: reduction of 22.8% between 2014 and 2015
- Work stations: reduction of 10.2% in the same period

**Housing**
- Financed units: 538 thousand in 2014, 319 thousand in 2015

**INFRASTRUCTURE AND OIL CRISIS**

**Oil**
- Layoffs: 260 thousand since 2014
- Royalties: reduction of 25% in the collection from 2014 to 2015

**Construction**

Sources:
- Focus (07/mar)
- Abecip
- Anfavea
- Valor Econômico
- Petronotícias
TEMER HAS GOOD POLITICAL SKILLS

- Temer and Rousseff: similar allied coalitions
- Better governability

SUPPORT IN NUMBERS

- 79% of members of the house came out in favor of the government for at least 75% of votes

Source: Basômêtro; second mandate
TEMER’S MINISTERIAL APPOINTMENTS ACROSS PARTY LINES COVERS 70% OF ALL PARTIES IN CONGRESS

24 MINISTRIES

<table>
<thead>
<tr>
<th>Parties</th>
<th>Ministers</th>
<th>Represent.</th>
<th>Senators</th>
</tr>
</thead>
<tbody>
<tr>
<td>PMDB</td>
<td>7</td>
<td>67</td>
<td>18</td>
</tr>
<tr>
<td>PSDB</td>
<td>3</td>
<td>51</td>
<td>11</td>
</tr>
<tr>
<td>PP</td>
<td>2</td>
<td>47</td>
<td>7</td>
</tr>
<tr>
<td>PSD</td>
<td>2</td>
<td>34</td>
<td>4</td>
</tr>
<tr>
<td>DEM</td>
<td>1</td>
<td>29</td>
<td>4</td>
</tr>
<tr>
<td>PR</td>
<td>1</td>
<td>40</td>
<td>4</td>
</tr>
<tr>
<td>PTB</td>
<td>1</td>
<td>19</td>
<td>3</td>
</tr>
<tr>
<td>PPS</td>
<td>2</td>
<td>9</td>
<td>1</td>
</tr>
<tr>
<td>PRB</td>
<td>1</td>
<td>22</td>
<td>1</td>
</tr>
<tr>
<td>PSB</td>
<td>1</td>
<td>31</td>
<td>7</td>
</tr>
<tr>
<td>PV</td>
<td>1</td>
<td>7</td>
<td>1</td>
</tr>
<tr>
<td><strong>11 parties</strong></td>
<td><strong>356 (69%)</strong></td>
<td><strong>61 (75%)</strong></td>
<td></td>
</tr>
</tbody>
</table>

Simple majority | 257 | 41
PEC (3/5) | 308 | 49

11 States
COHESIVE ECONOMIC TEAM REVAMPS THE ECONOMIC TRIPOD

ILAN GOLDFAJN
President of the Central Bank

DYOGO OLIVEIRA
Minister of Planning (acting)

PEDRO PARENTE
President of Petrobrás

HENRIQUE MEIRELLES
Minister of Finance

MARIA SILVIA BASTOS MARQUES
President of BNDES

JORGE RACHID
Secretary of Federal Revenue

MANSUETO DE ALMEIDA
Secretary of Economic Monitoring/MF
Temer’s two main agendas

**Adjustments**
- Administrative
- Fiscal / Social
- Industrial
- Social Security

**Positive agenda**
- Labor
- Tributary
- Business Environment
- Infrastructure + O&G
- Foreign Commerce
## ADJUSTMENT AGENDA DEPENDANT ON CONGRESS

<table>
<thead>
<tr>
<th>TYPE</th>
<th>MEASURES</th>
<th>LEGISLATIVE PROCESS</th>
<th>PERSPECTIVE</th>
</tr>
</thead>
</table>
| Administrative    | Reduction of ministries from 31 to 24                                    | • HOUSE OF REP. symbolic vote.  
                                                        • SENATE 44 x 6                                                               | ✔           |
|                  | End stability of careers for public servants                          | • Will be sent to the Congress  
                                                        • Strikes                                                                   | ✗           |
| Fiscal / Social  | Reduction of goal                                                       | • 2016 approved: BRL170 billion  
                                                        • 2017 approved: BRL139 billion                                               | ✔           |
|                  | Roof for expenditure increase                                           | • House of Rep. approved  
                                                        • Senate: November-December                                                  | ✔           |
|                  | Unbundling government revenue (DRU)                                      | • HOUSE OF REP. 340 x 96  
                                                        • SENATE 54 x 15                                                             | ✔           |
| Industrial       | End subsidies                                                           | • Depends exclusively on the government                                           | !           |
|                  | Raise taxes                                                             | • End of 2017                                                                   | !           |
| Social Security  | Social Security reform                                                  | • Will be sent by the end of November  
                                                        • House of Rep. 6 months; Senate 3 months                                      | ✗           |

- ✔ approved/easy to approve
- ✗ hard to approve/highly controversial
- ! medium difficulty for approval/resistance
# POSITIVE AGENDA IS EASIER TO IMPLEMENT

<table>
<thead>
<tr>
<th>TYPE</th>
<th>MEASURES</th>
<th>LEGISLATIVE PROCESS</th>
<th>PERSPECTIVE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Workers rights</td>
<td>Prevalence of negotiations over legislation</td>
<td>• 2017’s second semester</td>
<td>✗</td>
</tr>
<tr>
<td></td>
<td>Regulation of outsourcing</td>
<td>• 2016’s second semester</td>
<td>!</td>
</tr>
<tr>
<td>Taxes</td>
<td>Tax simplification with ICMS reform</td>
<td>• 2017’s first semester</td>
<td>✗</td>
</tr>
<tr>
<td></td>
<td>Pis/Cofins</td>
<td>• 2017’s first semester</td>
<td>✗</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Proposals: 2017</td>
<td></td>
</tr>
<tr>
<td>Business environment</td>
<td>Autonomy of regulatory agencies</td>
<td>• Senate: approved by special Committee</td>
<td>✗</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• House of Rep. has to vote on the issue</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Public Companies Responsibility Law</td>
<td>• Signed into law</td>
<td>✓</td>
</tr>
<tr>
<td></td>
<td>Central Bank autonomy</td>
<td>• 2017’s first semester</td>
<td>✓</td>
</tr>
<tr>
<td>Infrastructure O&amp;G</td>
<td>Expansion of concession opportunities</td>
<td>• Depends exclusively on the government</td>
<td>✓</td>
</tr>
<tr>
<td></td>
<td>“New Pre-Salt Law”</td>
<td>• End of 2016</td>
<td>✓</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• HOUSE OF REP. 292 x 101</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>• SENATE 40 x 26</td>
<td></td>
</tr>
<tr>
<td>Foreign trade</td>
<td>Opening of new markets</td>
<td>• Easier to implement</td>
<td>✓</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Argentina, Colombia, Chile, Mexico, USA, Europe, China</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Change in Mercosur model</td>
<td>• Complex negotiations. Support from Argentina</td>
<td>!</td>
</tr>
</tbody>
</table>
RECOVERY OF ENTREPRENEURIAL CONFIDENCE

CONFIDENCE OF THE INDUSTRIAL ENTREPRENEUR

Source: ICEI/CNI

CONFIDENCE OF THE CONSUMER

Source: INEC/CNI
EXPECTATION OF RECOVERY IN 2017

GDP GROWTH (%)

2015
• Lower family consumption rate → inflation, unemployment, high interest rates
• Lower government expenditure, but even lower revenue

2016
• Increase in government’s expenditures (short-term) → acquire political support
UNEMPLOYMENT ON THE RISE IN 2016

UNEMPLOYMENT RATE (> 14 YEARS OLD)

Source: IBGE

2015
• 1.5 million jobs lost - more than 1 million in industrial sector
• Only agribusiness had a positive result (9.8 thousand, CNI)

2016
• Unemployment rises steadily
• 11.8% is the highest unemployment rate in last five years
MARPET EXPECTATION: DEVALUATION

EXCHANGE RATE (BRL/USD)

Source: Central Bank

Focus and Bradesco forecasts
- **2016**: 3.30
- **2017**: 3.40
- **2018**: 3.35
- **2019**: 3.45
- **2020**: 3.55
INFLATION AND INTEREST RATE: GRADUAL REDUCTION

**Focus and Bradesco forecasts**
- **2016**: 6.80
- **2017**: 4.93
- **2018**: 4.54
- **2019**: 4.50
- **2020**: 4.50

**IPCA (%)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Jan</th>
<th>Feb</th>
<th>Mar</th>
<th>Apr</th>
<th>May</th>
<th>Jun</th>
<th>Jul</th>
<th>Aug</th>
<th>Sep</th>
<th>Oct</th>
<th>Nov</th>
<th>Dec</th>
</tr>
</thead>
</table>

**SELIC RATE (% A.A.)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Jan</th>
<th>Feb</th>
<th>Mar</th>
<th>Apr</th>
<th>May</th>
<th>Jun</th>
<th>Jul</th>
<th>Aug</th>
<th>Sep</th>
<th>Oct</th>
<th>Nov</th>
<th>Dec</th>
</tr>
</thead>
</table>

Source: IBGE
O&G - Sectorial perspective
MULTISECTORIAL ROLE DURING LULA-DILMA

1. Fiscal Policy (onerous transfer)
2. Monetary Policy (fuel price controls)
3. Naval & off shore industry (domestic contend)
4. Industrial Policy (innovation and investment policies)

STRONG PRESSURE ON PETROBRAS
MODEL IS UNDER REVISION BY THE TEMER ADMINISTRATION!
NEW DYNAMICS FOR THE O&G SECTOR

PETROBRAS

• Lack of financial conditions to keep investments → demand for private sector participation
• High debt situation: sale of assets → strategy to improve fiscal balance

ECONOMIC MEASURES

• Government’s initiatives for Brazil’s economic recovery: main features of Temer’s administration
• O&G: sector chosen as a priority

SECTORIAL MEASURES

• Pro-market measures + more liberal regulatory policies
• Attraction of companies to segments previously dominated by Petrobras
HIGHLY TECHNICAL AND LIBERAL TEAM IN STRATEGIC O&G INSTITUTIONS

PEDRO PARENTE
Petrobras’ President

- Crisis management ability
- Reverse the debt of **BRL 450 billion**
- Negotiate *privatization*

DÉCIO ODDONE
National Oil Agency Director (ANP)

- Experience with international investors
- May redesign *regulatory framework*
- Defends an *open O&G market*
HIGHLY TECHNICAL AND LIBERAL TEAM IN STRATEGIC O&G INSTITUTIONS

LUIZ AUGUSTO BARROSO
Energy Research Company Director (EPE)

- May increase **gas and wind energy** in the energy matrix
- ANEEL’s and Eletrobras’ development

FERNANDO COELHO FILHO
Minister of Mines and Energy (MME)

- Advocates for development in the Northeast
- Ministry **deeply influenced** by senator Fernando Coelho and PMDB
REGULATORY ISSUES RELAXED

Next bidding rounds are expected to be held by July, 2017

PRE SALT LAW

• End of Petrobras’ obligation to participate in the exploration of pre-salt oil (approved by Congress)

• Flexibility in Petrobras’s participation + unitization of oil and gas fields: over USD 120 billion in investments

LOCAL CONTENT POLICY

• Current local content rules should be relaxed to create competitiveness

• Next bidding round should happen under the new rules
# PETROBRAS’S DIVESTMENT PLAN

## ASSETS SOLD

<table>
<thead>
<tr>
<th>Description</th>
<th>Details</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nova Transportadora Sudeste’s (90%)</td>
<td>→ Brookfield</td>
<td>USD 5.19 billion</td>
</tr>
<tr>
<td>Innova’s price adjustment + Colombian assets</td>
<td></td>
<td>USD 92 million</td>
</tr>
<tr>
<td>Carcará oil block (66%)</td>
<td>→ Statoil Brasil Óleo e Gás</td>
<td>USD 2.5 billion</td>
</tr>
<tr>
<td>Okinawa refinery</td>
<td>→ Grupo Ultra</td>
<td>USD 129.3 million</td>
</tr>
<tr>
<td>Liquigás</td>
<td>→ Grupo Ultra</td>
<td>USD 2.8 billion</td>
</tr>
<tr>
<td><strong>Assets in Argentina</strong></td>
<td>Companhia Geral de Combustíveis</td>
<td>USD 101 million</td>
</tr>
<tr>
<td>Gaspetro (49%)</td>
<td>Mitsui Gás e Energia do Brasil</td>
<td>USD 540 million</td>
</tr>
<tr>
<td>Petrobras Argentina (67.19%)</td>
<td>Pampa Energía</td>
<td>USD 897 million</td>
</tr>
<tr>
<td>Chile Distribución (PCD)</td>
<td>Southern Cross Group</td>
<td>USD 464 million</td>
</tr>
</tbody>
</table>
56.4% OF THE TARGET WAS REACHED

PETROBRAS’ DIVESTMENT PLAN: MAIN ASSETS SOLD

Divestment Plan (2017-2018)
GOAL: USD 19.5 billion in assets

Sale of Nova Transportadora do Sudeste (Gas Transporter)
USD 5.19 billion

Sale of Carcará Oil Block
USD 2.5 billion

Strategic Plan Revision (2017-2021)

Until Now
USD 11 billion raised

AROUND 56% OF PLAN’S TARGET

- Target will hardly be achieved
- Pressure to ease negotiations

Until Now
USD 11 billion raised

56.4% OF THE TARGET WAS REACHED

PETROBRAS’ DIVESTMENT PLAN: MAIN ASSETS SOLD

Divestment Plan (2017-2018)
GOAL: USD 19.5 billion in assets

Sale of Nova Transportadora do Sudeste (Gas Transporter)
USD 5.19 billion

Sale of Carcará Oil Block
USD 2.5 billion

Strategic Plan Revision (2017-2021)

Until Now
USD 11 billion raised

AROUND 56% OF PLAN’S TARGET

- Target will hardly be achieved
- Pressure to ease negotiations

Until Now
USD 11 billion raised

56.4% OF THE TARGET WAS REACHED

PETROBRAS’ DIVESTMENT PLAN: MAIN ASSETS SOLD

Divestment Plan (2017-2018)
GOAL: USD 19.5 billion in assets

Sale of Nova Transportadora do Sudeste (Gas Transporter)
USD 5.19 billion

Sale of Carcará Oil Block
USD 2.5 billion

Strategic Plan Revision (2017-2021)

Until Now
USD 11 billion raised

AROUND 56% OF PLAN’S TARGET

- Target will hardly be achieved
- Pressure to ease negotiations

Until Now
USD 11 billion raised

56.4% OF THE TARGET WAS REACHED

PETROBRAS’ DIVESTMENT PLAN: MAIN ASSETS SOLD

Divestment Plan (2017-2018)
GOAL: USD 19.5 billion in assets

Sale of Nova Transportadora do Sudeste (Gas Transporter)
USD 5.19 billion

Sale of Carcará Oil Block
USD 2.5 billion

Strategic Plan Revision (2017-2021)

Until Now
USD 11 billion raised

AROUND 56% OF PLAN’S TARGET

- Target will hardly be achieved
- Pressure to ease negotiations

Until Now
USD 11 billion raised

56.4% OF THE TARGET WAS REACHED

PETROBRAS’ DIVESTMENT PLAN: MAIN ASSETS SOLD

Divestment Plan (2017-2018)
GOAL: USD 19.5 billion in assets

Sale of Nova Transportadora do Sudeste (Gas Transporter)
USD 5.19 billion

Sale of Carcará Oil Block
USD 2.5 billion

Strategic Plan Revision (2017-2021)

Until Now
USD 11 billion raised

AROUND 56% OF PLAN’S TARGET

- Target will hardly be achieved
- Pressure to ease negotiations

Until Now
USD 11 billion raised

56.4% OF THE TARGET WAS REACHED

PETROBRAS’ DIVESTMENT PLAN: MAIN ASSETS SOLD

Divestment Plan (2017-2018)
GOAL: USD 19.5 billion in assets

Sale of Nova Transportadora do Sudeste (Gas Transporter)
USD 5.19 billion

Sale of Carcará Oil Block
USD 2.5 billion

Strategic Plan Revision (2017-2021)

Until Now
USD 11 billion raised

AROUND 56% OF PLAN’S TARGET

- Target will hardly be achieved
- Pressure to ease negotiations

Until Now
USD 11 billion raised

56.4% OF THE TARGET WAS REACHED

PETROBRAS’ DIVESTMENT PLAN: MAIN ASSETS SOLD

Divestment Plan (2017-2018)
GOAL: USD 19.5 billion in assets

Sale of Nova Transportadora do Sudeste (Gas Transporter)
USD 5.19 billion

Sale of Carcará Oil Block
USD 2.5 billion

Strategic Plan Revision (2017-2021)

Until Now
USD 11 billion raised

AROUND 56% OF PLAN’S TARGET

- Target will hardly be achieved
- Pressure to ease negotiations

Until Now
USD 11 billion raised
OPPORTUNITIES FOR THE PRIVATE SECTOR

PETROBRAS’ DIVESTMENT PLAN: MAIN ASSETS ON SALE

Companhia Petroquímica de Pernambuco (PetroquímicaSuape)

Companhia Integrada Têxtil de Pernambuco (Citepe)

Stake in BR Distribuidora (fuel distributor)

36% Stake at Braskem

Liquefied Natural Gas (LNG) terminals and associated thermal power plants

Onshore and shallow water oil and gas fields

Ethanol, biodiesel and other fertilizer plants
HISTORICAL OPPORTUNITIES FOR OPENING TWO NEW MARKETS

DOWNSTREAM

- Petrobras’ news focus on exploration and production sectors
- Improving the environment for private companies in the refinery, transportation and distribution segments

GAS SEGMENT

- End of Petrobras’ *de facto* gas monopoly
- Regulation should be adapted for private companies
- Greater competitiveness: opening of a brand new sector to foreign investors
IMPROVEMENTS NOW WOULD AVOID A PRIVATE OLIGOPOLY AND FUTURE RESTRICTIONS

DEMAND FOR A BETTER REGULATORY ENVIRONMENT

- Security in the gas supply
- Sectorial tariffs

MARKET ARGUES FOR THE CREATION OF “NATIONAL GAS OPERATOR”

- Similar to the National System Operator (ONS) - manages production, transmission, distribution and consumption of energy
- Not in Congress’ agenda
- Would fit government's agenda

National Petroleum Agency (ANP) and Ministry of Mines and Energy can set these regulations

Congress has to approve it
Government could edit a provisional measure to induce a decision
# EVOLUTION OF REGULATORY FRAMEWORKS IN NATURAL GAS POLICY

<table>
<thead>
<tr>
<th><strong>Art. 177 Federal Constitution</strong></th>
<th>• Establishes that every natural gas transportation operation is considered a Union monopoly</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Petroleum Act (9.478/97)</strong></td>
<td>• <strong>It did not include</strong> the intrinsic characteristics of the natural gas industry</td>
</tr>
<tr>
<td><strong>Gas Law (11.909/09)</strong></td>
<td>• Focused on natural gas transportation activities</td>
</tr>
<tr>
<td></td>
<td>• Pipeline transportation operations exclusively made under <strong>concession contracts or federal authorization (30 years)</strong></td>
</tr>
<tr>
<td></td>
<td>• Regulated the <strong>free access for third party users</strong> to the pipelines</td>
</tr>
<tr>
<td></td>
<td>• Except LNG</td>
</tr>
<tr>
<td><strong>Decree 7.382/2010</strong></td>
<td>• Filled the gaps of the Gas Law on issues that lacked regulation, especially on gas commercialization activities under regulation and authorization of the ANP</td>
</tr>
<tr>
<td><strong>ANP Resolution Nº 11/2016</strong></td>
<td>• Regulated third party access to pipelines, providing greater transparency, competition in the commercialization and entrance of new players.</td>
</tr>
<tr>
<td></td>
<td>• Operational exchange (swap)</td>
</tr>
</tbody>
</table>

- Reduction of regulatory vacuum (ex: dispute resolution)
- Greater legal stability and attractiveness to new investors
- Increased competition among industry players.
- Flexible Contract Options for LNG (flexibility of the ‘take or pay’ concept)
SÃO PAULO
R. Diogo Moreira, 135 • Pinheiros
05423-010 • São Paulo • Brasil
+55 11 3816-36363

BRASÍLIA
SBS QD 02, Bloco E, Sl 1109/1110 • Ed. Prime Business
70070-120 • Brasília • Brasil
+55 61 3344-3780

RIO DE JANEIRO
Av. Nilo Peçanha, n° 50. 16° Andar Sala 1609 • Centro • CEP 20020-960

MIAMI
150 SE 2nd Ave. Suite 1403
Miami, FL 33131
+1 305 600-4462

prospectiva@prospectiva.com