

Annual Report 2006



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Profile

Petrobras is a publicly listed company that operates on an integrated and specialized basis in the following segments of the oil, gas and energy sector: exploration and production; refining, commercialization, transportation and petrochemicals; the distribution of oil products; natural gas and energy. Founded in 1953, Petrobras is now the world's 14th largest oil company, according to the publication *Petroleum Intelligence Weekly*. The leader in the Brazilian hydrocarbons sector, the company has been expanding, in order to become an integrated energy business with international operations, and the leader in Latin America.

Mission

To operate safely and profitably, in a socially and environmentally responsible manner, within the oil, gas and energy sector, both domestically and abroad, supplying products and services that meet the needs of the customers, thereby contributing to the development of Brazil and the other countries in which Petrobras operates.

Vision 2015

Petrobras will be an integrated energy company with a strong international presence, the leader in Latin America, with its focus on profitability and social and environmental responsibility.

Values

- Giving importance to the company's principal stakeholders: shareholders, customers, employees, society, government, partners, suppliers and the communities within which the company operates;
- An enterprising spirit and the ability to meet challenges;
- A focus on quality in the results;
- An innovative and competitive spirit, focused on providing outstanding services and maintaining high technological standards;
- Quality and leadership in the issues of health, safety and environmental preservation;
- A constant quest for business leadership.

Conduct

- An ethical posture in all business dealings;
- Leadership by example;
- An emphasis on integration and teamwork;
- A focus on attaining and sustaining a competitive edge;
- Close scrutiny of results, with performance recognition and responsibility;
- Transparency in the relations with shareholders, employees, communities and other stakeholders.

Highlights

Operational summary – 2006

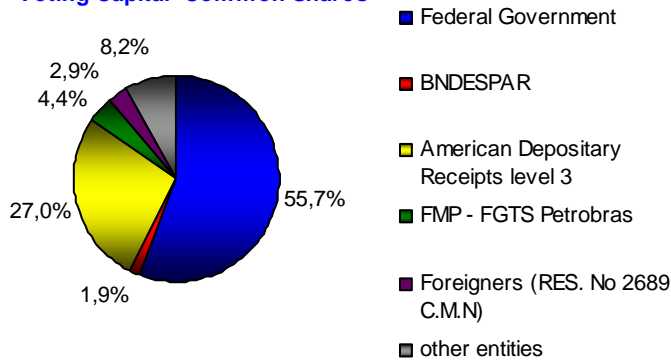
	2005	2006
PROVEN RESERVES – SPE criteria - (billions of barrels of oil equivalent – boe) ^{(1) (2)}	14.9	15.0
Oil and condensate (billion barrels)	12.3	12.3
Natural gas (billion boe)	2.6	2.7
AVERAGE DAILY PRODUCTION (thousand boe) ⁽¹⁾	2,217	2,298
• Oil and NGL (thousands of barrels per day - bpd)	1,847	1,920
Onshore	396	367
Offshore	1,451	1,552
• Natural gas (thousands of boed)	370	378
Onshore	213	206
Offshore	157	172
PRODUCING WELLS (oil and natural gas) – December 31 st ⁽¹⁾	12,557	12,895
Onshore	11,860	12,170
Offshore	697	725
DRILLING RIGS – December 31 st	64	63
Onshore	22	19
Offshore	42	44
PRODUCING PLATFORMS – December 31 st	97	103
Fixed	73	76
Floating	24	27
SHIPPING FLEET – December 31 st		
Vessels – company owned	50	51
– chartered	75	104
Tonnage (million deadweight tons – dwt)	8.2	11.1
TERMINALS – December 31 st		
Number	66	66
Storage capacity (million m ³) ⁽³⁾	10.4	10.4
REFINERIES – December 31 st ⁽¹⁾⁽⁵⁾		
Number	15	16
Nominal installed capacity (thousand bpd)	2,114	2,227
Average throughput (thousand bpd)	1,830	1,872
Brazil	1,727	1,746
Abroad	103	126
Average production of oil products (thousand bpd)	1,839	1,892
IMPORTS (thousand bpd)		
Oil	352	370
Oil products	94	118
EXPORTS (thousand bpd)		
Oil	263	335
Oil products	260	246
COMMERCIALIZATION OF OIL PRODUCTS (thousand bpd)		
Brazil	1,644	1,697
INTERNATIONAL SALES (thousand bpd)		
Oil, gas and oil products	385	503
NATURAL GAS SOURCE (million m ³ per day) ⁽⁴⁾	45	46
Domestic gas	23	23
Bolivian gas	22	24
NATURAL GAS MARKET DISTRIBUTION (million m ³ per day) ⁽⁴⁾	45	46
Distributors	31	33
Thermoelectric plants	7	6
Domestic consumption	7	7
ENERGY ⁽¹⁾		
Number of thermoelectric plants ^{(5) (6)}	9	10
Installed capacity (MW) ⁽⁵⁾⁽⁶⁾	3,203	4,126
Energy sales (TWh)	16.64	17.57
Number of hydroelectric plants	2	2
Installed capacity (MW) ⁽⁵⁾	285	285
Transmission lines (km)	15,414	15,414
Energy distribution (TWh/year)	13	13
FERTILIZERS ⁽¹⁾		
Production units	3	3

- (1) Includes information from abroad, corresponding to Petrobras' stake in each partnership
(2) Proven reserves are calculated according to SPE (Society of Petroleum Engineers) criteria
(3) Only includes Transpetro's terminals
(4) Excludes flare off, own E&P consumption, liquefaction and reinjection
(5) Only includes assets in which Petrobras has an equity stake of 50% or more
(6) Only includes natural gas powered thermoelectric plants

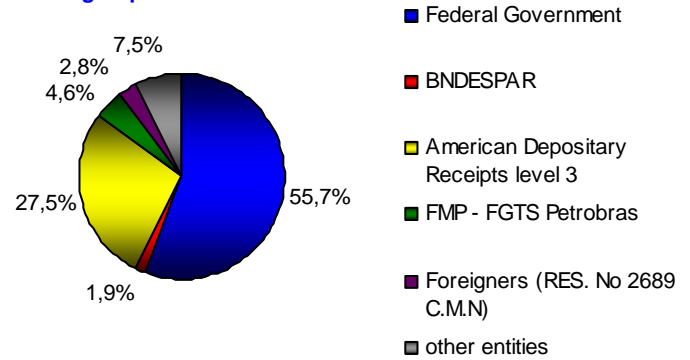
Shareholding structure at the end of 2006

Shareholding structure at the end of 2005

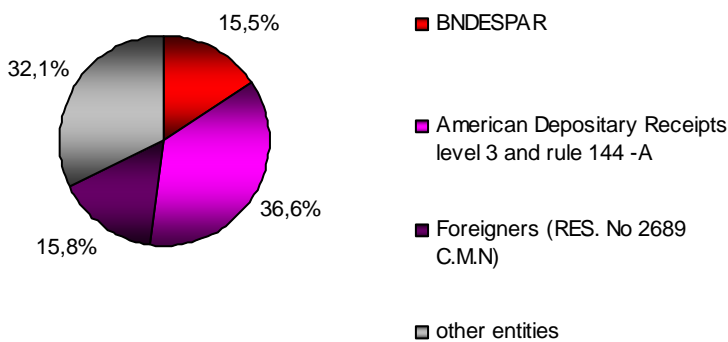
Voting Capital - Common Shares



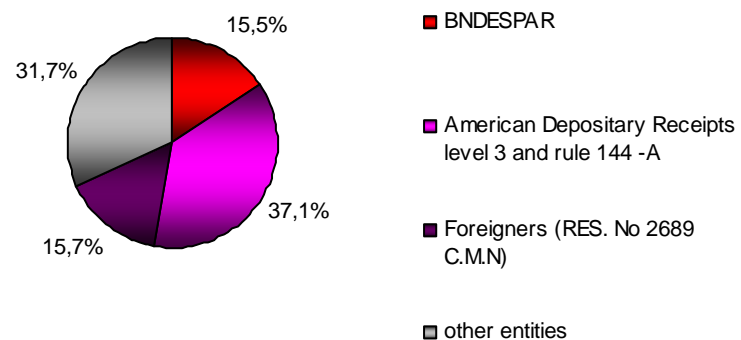
Voting Capital - Common Shares



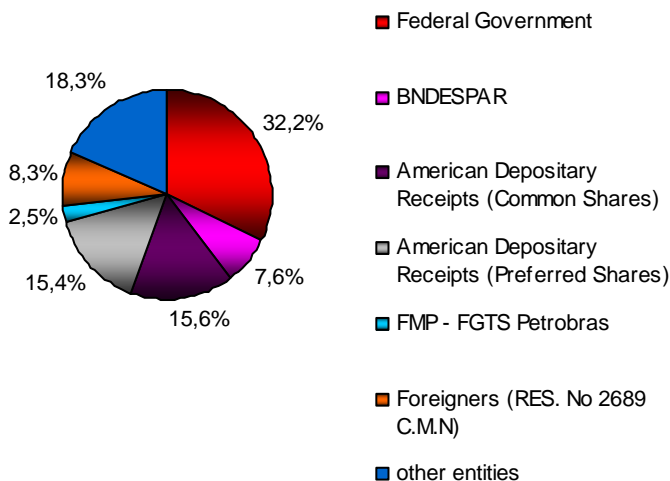
Non-Voting Capital - Preferred Shares



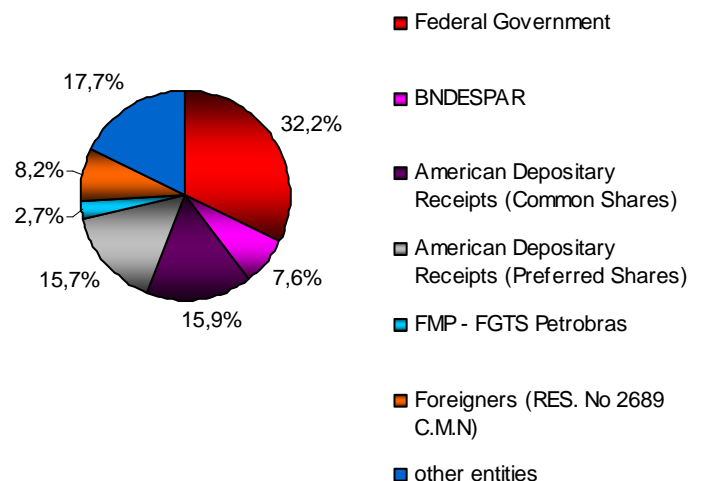
Non-Voting Capital - Preferred Shares



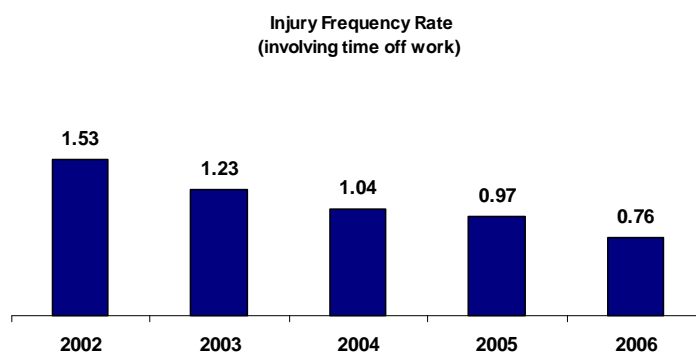
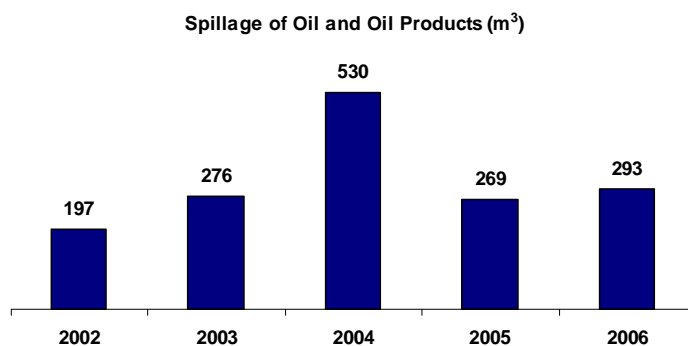
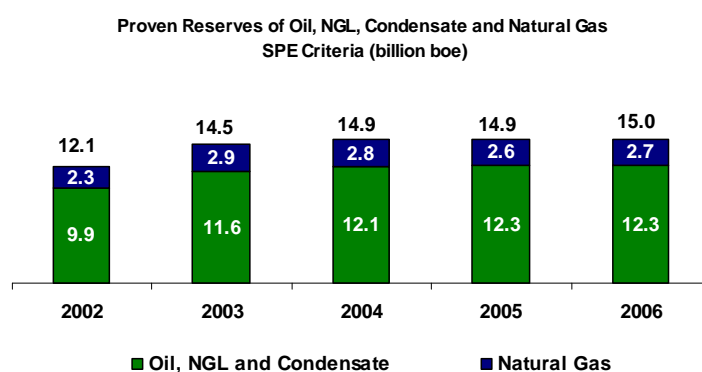
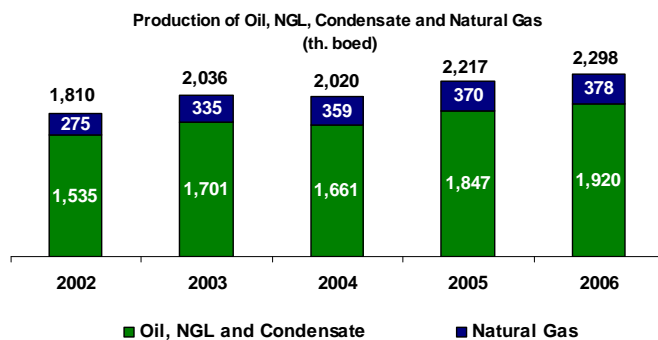
Capital Stock



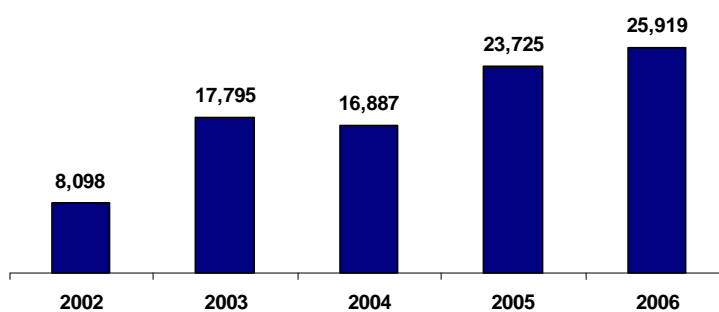
Capital Stock



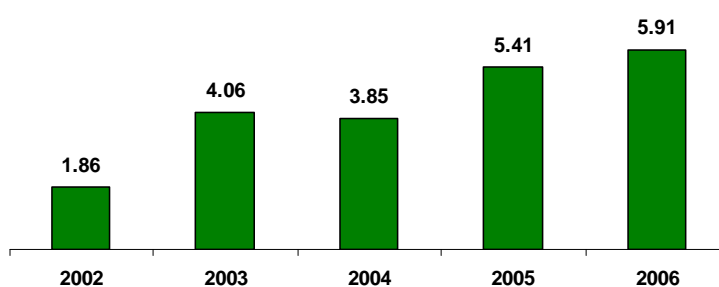
Consolidated Information



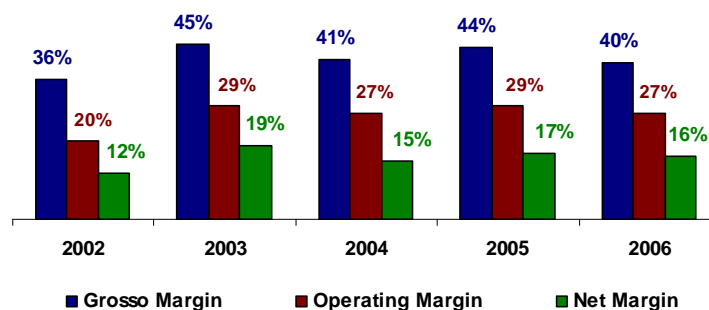
Net Income Consolidated⁽¹⁾ - BR GAAP Criteria
R\$ million



Earnings/Share - BR GAAP Criteria
Consolidated(R\$/share)⁽¹⁾⁽²⁾

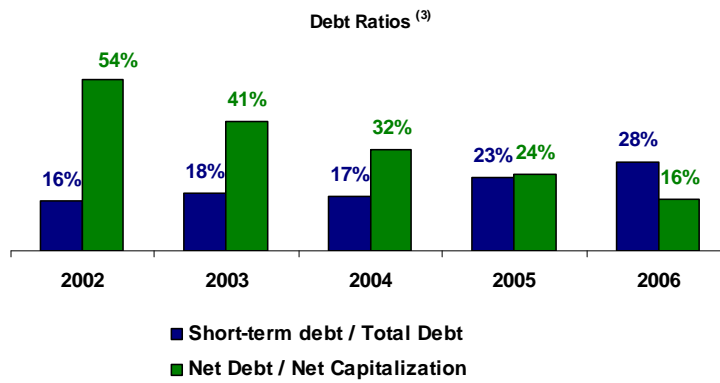
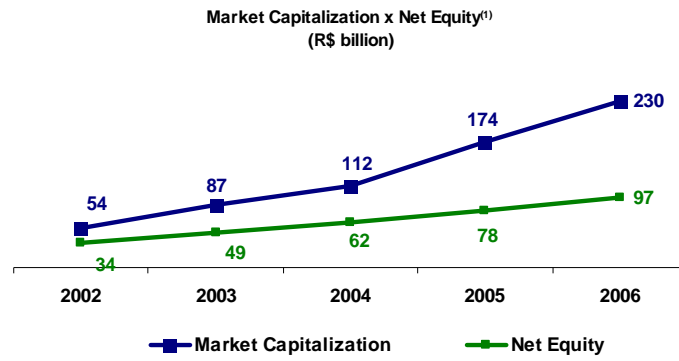


Gross, Operating and Net Margin⁽¹⁾
BR GAAP Criteria - Consolidated



(1) The fiscal years 2004, 2005 and 2006 include the figures for Special Purpose Companies (SPCs) whose activities are controlled, directly or indirectly, by Petrobras.

(2) For the purpose of comparison, the Earnings per Share for the previous fiscal years have been recalculated, to reflect the share split approved of the EGM of July 22, 2005.



(1) The fiscal years 2004, 2005 and 2006 include the figures for Special Purpose Companies (SPCs) whose activities are controlled, directly or indirectly, by Petrobras.

(3) The fiscal years 2002 and 2003 include debt incurred by the SPCs which Petrobras used to structure project finance and consortia. The fiscal years 2002 until 2006 include leasing contracts.

Message from the CEO

The year 2006 was one of achievement and new prospects for Petrobras. In addition to the record results – consolidated earnings of R\$ 25.9 billion and investments of R\$ 33.7 billion – and a 4% increase in total production of oil and natural gas, the company is girding itself for a new challenge, set down in the Business Plan 2007-2011: to maintain its rapid rate of growth. The targets are ambitious ones, leading Petrobras, for the first time, to plan its production over the long term: a total of 4 million 556 thousand barrels a day (bpd) of oil and natural gas will be produced in Brazil and abroad in 2015. The planned investments are in keeping with the grandeur of the projects, amounting to the sum of US\$ 87.1 billion by 2011.

Domestic production grew by 5.0% in 2006, due to a 340 thousand bpd increase in production capacity, as a result of the P-34, FPSO-Capixaba and P-50 platforms all coming on-stream. The production record of 1 million 912 thousand 733 bpd of oil, achieved in October, brought the company very close to the 2 million bpd mark in Brazil.

As a guarantee of a solid foundation for future growth, for every barrel that was produced during the year 1.739 barrels were added to the reserves. This was reinforced by the 27 new areas that had their commercial viability confirmed, with the total volume of recoverable oil estimated at 2.5 billion barrels of oil equivalent (boe). New exploration prospects arose with the discovery of light oil below a layer of salt in the Santos Basin.

On top of the strong performance in oil, progress was also made in the area of natural gas. Along with a 1.5% increase in domestic production, Petrobras announced its Plan to Advance the Production of Natural Gas (Plangás), which will raise the supply of natural gas in the southeast of Brazil from the present 15.8 million m³ to 40 million m³ a day by 2008. The plan, which also includes projects for the processing and transportation of natural gas, aims to increase the share of Brazilian gas in the domestic demand. Following the company's strategy to guarantee safety and flexibility in supplying the Brazilian market, Petrobras sanctioned its entry into the liquefied natural gas (LNG) market as an importer and continued with its expansion of the gas pipeline network.

Other milestones in 2006 were the launching of Diesel Podium and the development of H-Bio – a pioneering technology from Petrobras that combines vegetable oil with fractions of mineral oil in the manufacturing of diesel fuel. The company also augmented the supply of diesel S500, with its reduced sulfur content, to eight metropolitan areas. In order to further raise the quality of its fuels and add value to the country's heavy oil, Petrobras continued to make improvements at its refineries, with the installation of new hydrotreatment and conversion units, which reduce the sulfur content in our oil products and optimize the output of diesel fuel from Brazilian oil. In this way, the company enhances the value of domestic oil and meets the most rigorous environmental specifications, while at the same time opening up new export markets.

In line with its social and environmental commitments, Petrobras fortified its biodiesel program, beginning the construction of three plants, which will produce an annual total of 171 million liters, thus meeting 20% of the country's demand in 2008. As well as generating

employment and income for family subsistence farmers, the product will help to reduce imports of diesel fuel and light oil.

Despite the high prices and volatility of the oil market, the company's results were sustained by production growth, without passing on the price instability to the domestic market. A barrel of Brent oil hit a peak of US\$ 78.63 in August, but closed the year down 25%, back around the US\$ 60 level, the same as when Petrobras announced its last readjustment in the price of gasoline and diesel fuel, in September 2005.

The company's excellent results in Brazil are mirrored by its performance abroad. In addition to strengthening activities in the countries where it is already established, Petrobras augmented its involvement in focus areas such as Africa and the American sector of the Gulf of Mexico. Furthermore, it expanded its activities in international refining, with the acquisition of a 50% stake in the Pasadena refinery, in the United States, and is looking at other refining prospects abroad. The objective is to add value to the heavy oil the company produces, offering a mix of more esteemed and higher quality products to the market.

The investors' confidence was reflected in the 34% appreciation of Petrobras' shares and the lower cost of securing funding. As a result, the company's the market capitalization, for the first time, attained a monthly average of more than US\$ 100 billion, in December, and its first global securities issue since becoming investment grade was at the lowest ever funding cost for a 10-year maturity.

These successes alone would be ample reward for the endeavors of the employees and the confidence of the shareholders, but Petrobras also won further important recognition of its performance: its selection for the Dow Jones Sustainability Index and the ISE (Bovespa Corporate Sustainability Index), and the classification of its shares as investment grade by the rating agency Standard & Poor's.

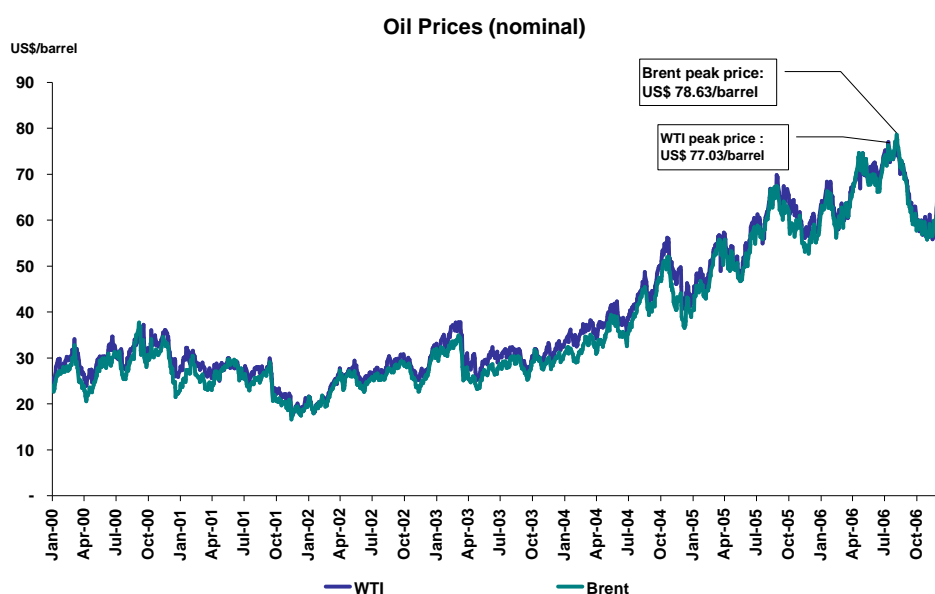
These accomplishments all strengthen our faith that Petrobras is on the right path and will continue to grow, profitably and showing social and environmental responsibility.

José Sergio Gabrielli de Azevedo

President and CEO

Oil market overview

The year 2006 saw a break in the continuous upward movement of oil prices, which began in 2002. Although the price of Brent oil reached a peak of US\$ 78.63 a barrel in August, it had fallen back 25% by the year end. The average price, over the course of the year, was US\$ 11 higher than that of 2005, while the market has become more volatile.



As in previous years, there was a supply surplus in 2006, with an accumulation of inventories, and yet prices remained high. Despite a slowing of the growth in world demand, influenced by the high prices, oil continued to earn a risk premium, due to the geopolitical instability provoked by events such as Israel's incursion into the Lebanon and the nuclear issue in Iran. Aware that geopolitical questions in the Middle East would keep prices high, OPEC maintained its production quotas at the same level for most of the year, thus favoring the building up of inventories.

The upward price trend began to be reversed when August went by and fears that the Atlantic hurricane season would be as devastating as that of 2005 were not realized. Amid controversy over the influence of speculation on prices, the lack of major hurricanes obliged OPEC to announce cuts in production, for the first time since December 2004 and the biggest reduction since 2002. The first announcement was made in September and the second came in December, effective as of February 2007.

Another factor pushing down prices, towards the end of 2006, was the abnormally mild winter temperatures in the northern hemisphere, with a consequent reduction in oil consumption. This led the market to feel the supply surplus more acutely, and could be another sign that the upward price spiral of the last four years may be coming to an end.

Ever since the August peak, the market has been characterized by what analysts call a "correction movement" – with prices oscillating downwards, as the market seeks a new balance between supply and demand, against a backdrop of changing sentiment regarding potential

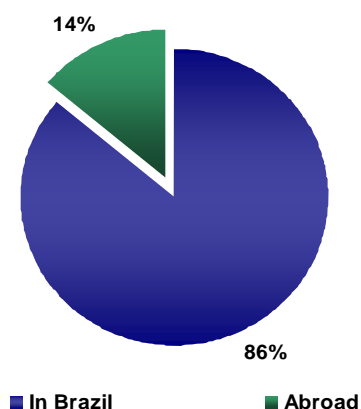
shortages brought about by a disruption in supply. This downward movement in oil prices has, once again, shown how susceptible prices are to the impact of unforeseeable events – something the world oil market has always had to live with.

Corporate Strategy

Petrobras has retained its aggressive growth targets in its Business Plan 2007-2011. For the first time, the company has released estimates of its oil and natural gas production for 2015 and listed the main projects that will support its growth after 2011. The company's strategic positioning places emphasis on the expansion of refining in Brazil, so as to add value to the country's increasing oil production – whether by augmenting sales to the growing Brazilian market or by expanding the export of oil products. Petrobras thus seeks to strike a long term balance between production growth and refining capacity. In the renewable energy market, the focus is on biofuels, within a corporate strategy of leadership in the production of biodiesel in Brazil and augmenting sales of ethanol.

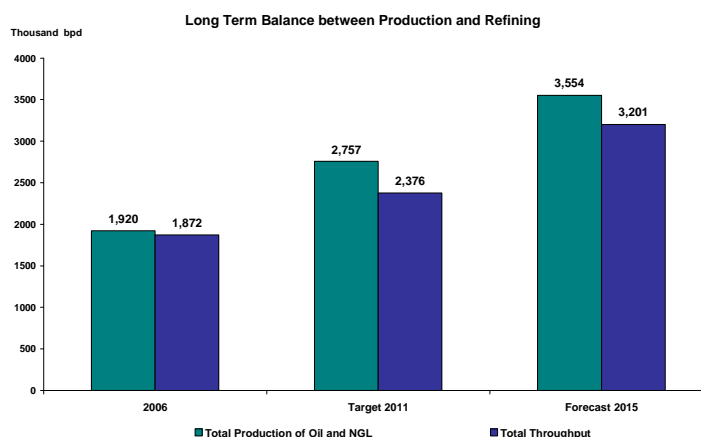
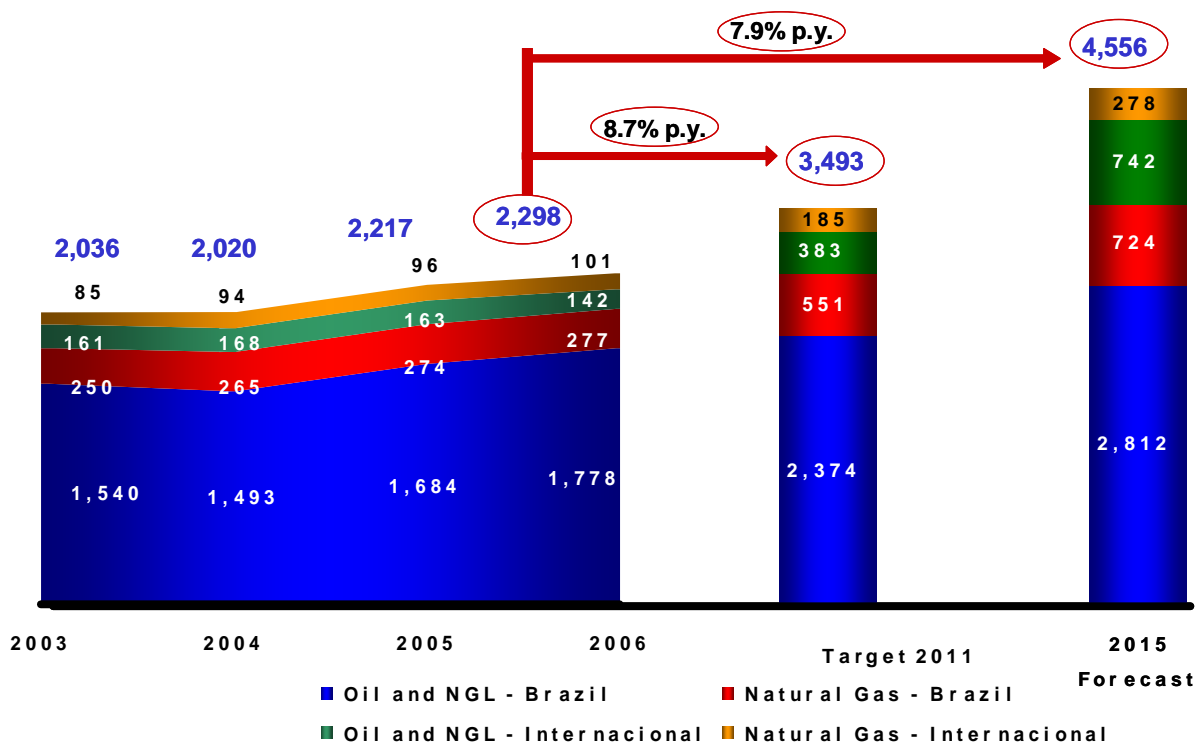
Brazilian production of oil and natural gas will reach 2 million 925 thousand boed by 2011. Paralleling this increase, the country's refineries will be processing 1 million 877 thousand bpd. The daily throughput of Brazilian oil, which in 2006 amounted to 1 million 388 thousand bpd, will rise to 1 million 710 thousand bpd. With this expansion, the company will raise the proportion of domestic oil processed in the refineries from the current 78% to 91%, thereby consolidating the country's self-sufficiency. Sales of the surplus, which in 2006 amounted to 337 thousand bpd, will reach 584 thousand bpd by 2011.

Of the total planned investment for the period 2007-2011 – amounting to US\$ 87.1 billion, an average of US\$ 17.4 billion a year –, US\$ 75 billion (86%) is to be invested in Brazil, leading to the creation of 838 thousand direct and indirect job positions. The greatest investment will be in the areas of Exploration & Production and Gas & Energy and in the Downstream area of Supplies. With US\$ 12.1 billion (14%) earmarked for investment abroad, 65% will go into Latin America, western Africa and the Gulf of Mexico – which are all a priority within Petrobras' strategy for international expansion.



Annual Report 2006

Area	Petrobras Investment 2007-2011
E&P	40.7
Downstream	23.1
G&E	7.2
International	12.1
Distribution	2.2
Corporate	1.7
Total	87.1



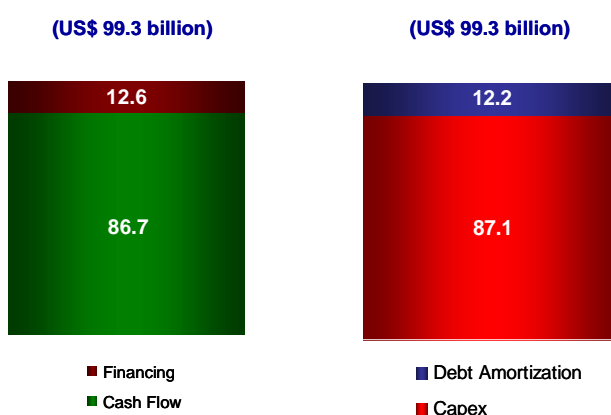
Petrobras' production abroad, which in 2006 amounted to 243 thousand boed of oil and natural gas, will increase to 568 thousand boed by 2011, while the company's throughput in refineries outside Brazil will reach 499 thousand bpd.

This growth in the production of oil and NGL and in the throughput of the refineries, in addition to preserving the balance between Exploration & Production, on the one hand, and the company's Downstream area, on the other, will also present opportunities for vertical integration, owing to the substantial volume of the company's activities in Brazil and abroad.

As part of its corporate strategy for consolidation as an integrated energy business with international reach, Petrobras is placing greater emphasis on its renewable energy goals. By

2011, the company should be making available 855 thousand m³/year of biodiesel and exporting 3.5 million m³ of ethanol. The capacity of the thermoelectric and co-generation plants, meanwhile, will have reached 4,554 MW.

Petrobras has retained the policy of keeping its prices aligned with those of the international market. The company's forecast cash flow generation for the period 2007 to 2011, of US\$ 86.7 billion, will be sufficient to meet almost all its investment needs. The raising of funds in the financial markets and the amortization of debt will be in alignment with the company's policy of extending its debt profile and reducing its financial leverage. The average Return on Capital Employed (ROCE) for the period should be 16%.



In line with its commitment to social and environmental responsibility and being at the technological cutting edge, the company will invest a total of US\$ 6.2 billion in Health, Safety and the Environment (SMS), technology, telecommunications and Information Technology (IT) during the period 2007 to 2011.

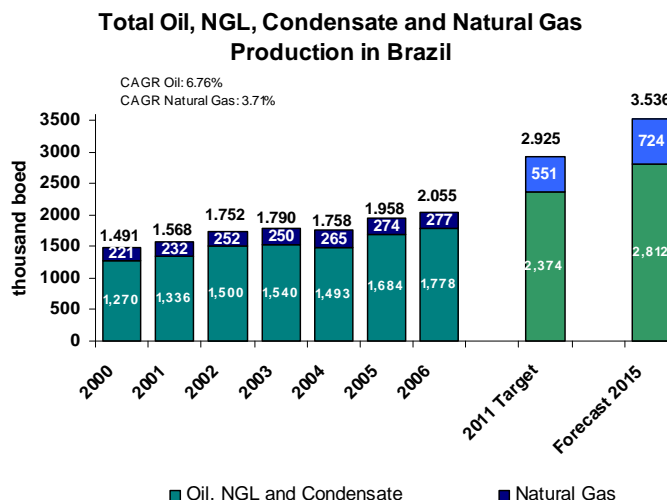
Petrobras is pursuing its endeavors to apply in the social and environmental spheres the level of quality achieved in its business performance, and remains committed to the principles of transparency and responsibility in its relations with the various stakeholders and other interested parties. Already internationally recognized for its standard of excellence in the production of oil, natural gas and oil products, the company continues to strive to raise those standards higher still and to enhance its reputation as a Brazilian business that is dedicated to overcoming the challenges of producing energy on the international stage.

OUR BUSINESSES

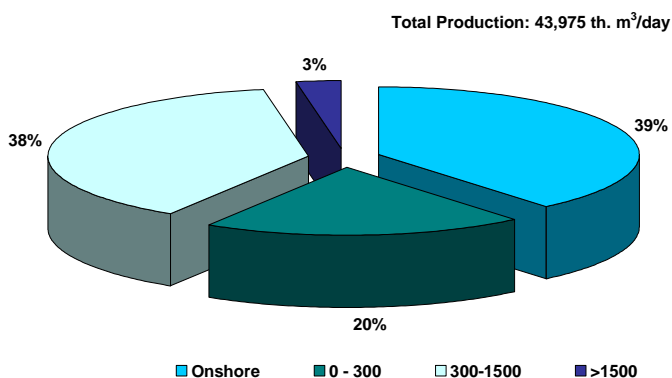
Exploration & Production

The increase in domestic oil production in 2006 represented another advance in Petrobras' growth strategy. The company's Brazilian output totalled 1 million 778 thousand

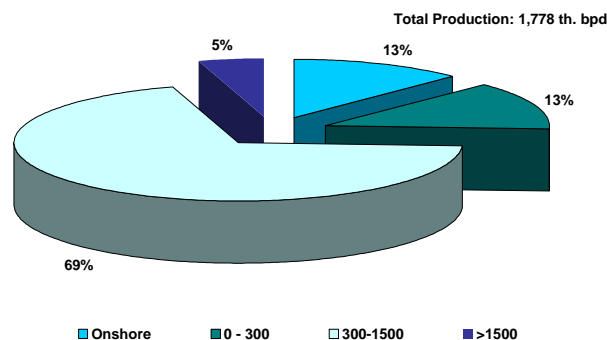
barrels per day (bpd) of oil, natural gas liquids (NGL) and condensate – up 5.6% in relation to the 2005 production figure, of 1 million 684 thousand bpd.



Domestic Production of Natural Gas by depth of water



Domestic Production of Oil, NGL and Condensate by depth of water



Two of the three major new projects contributing to the production increase are located in the Campos Basin: platform P-50, in operation since April 21st, and the platform vessel FPSO P-34, in operation since December 17th. In the Espírito Santo Basin, the FPSO “Capixaba” came into operation on May 6th. With the addition of these new projects, Petrobras’ production capacity was raised by 340 thousand bpd. The P-50, operating in the Albacora Leste (East Albacore) field, has a production capacity of 180 thousand bpd; the FPSO “Capixaba”, in the Golfinho (Dolphin) field, and the P-34, in the Jubarte (Humpback whale) field, can process 100 thousand bpd and 60 thousand bpd, respectively.

Despite the higher production in 2006, the annual average was 5.4% lower than the target, of 1 million 880 thousand bpd, that had been set for the year. This shortfall was due to delays in the operational start-up of P-50 and P-34.

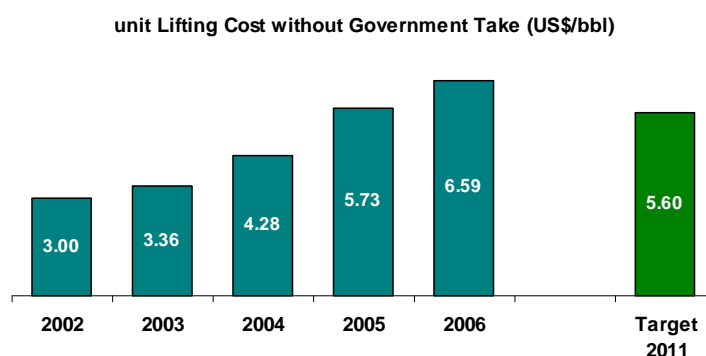
However, new production records have brought us to the threshold of the 2 million barrels per day mark. On October 23rd, the company produced 1,912,733 barrels – 31 thousand more than the previous record, set on May 29th. In addition to the output of the P-50 and the other

platforms in the Campos Basin, a contribution to these production peaks came from the Recage program (Program for the Rejuvenation of Heavily Exploited Fields), which helps to minimize the decline of mature production areas.

The company's production of natural gas (excluding NGL) also increased in 2006, attaining an average of 44 million m³/day, a 1% rise in relation to the 43.5 million m³/day of the previous year. This growth was maintained as a result of continued efforts to expand the supply of domestic gas, in line with the corporate strategy of ensuring a reliable supply of the product to the Brazilian market.

In the Espírito Santo Basin, a major gas project came into operation on February 22nd: the Peroá platform (production of around 1 million m³/day). In Rio Grande do Norte, the Guamaré UPGN III (production of 1.5 million m³/day) came on-stream, following a pre-operational phase that kicked off in December 2005.

The average lifting cost in 2006, not including the government's allocation, came to US\$ 6.59 per barrel of oil equivalent (boe) – an increase of 15% over the previous year's figure. The increase was mainly due to an 11% appreciation of the local currency (real) against the US dollar and to contractual readjustments, particularly drilling contracts, as well as to the strong market for oil, enlargement of the workforce, in line with the Business Plan forecast, and the coming on-stream of the platforms P-50, FPSO "Capixaba" and P-34.



The Challenge Of Growth

The targets set down in Petrobras' latest business plan provide for 15 major oil and 10 natural gas production projects to come on-stream by 2011, when the company's average production of oil and natural gas in Brazil is estimated to reach 2 million 925 thousand boed.

During 2007, the following platforms will come on-stream in the Campos Basin: the FPSO "Cidade do Rio de Janeiro" (100 thousand bpd), in the Espadarte (Swordfish) field; the P-52 and P-54 (180 thousand bpd, each), in the Roncador (Grunt) field; the SSP 300 (20 thousand bpd), in the Piranema (Marbled Grouper) field; and the FPSO "Cidade de Vitória" (100 thousand bpd), in module 2 of the Golfinho field. In Bahia, the Manati (Manatee) platform (6 million m³/day) will come into operation in 2007, augmenting the company's production of natural gas.

Two more platforms destined for the Campos Basin are currently under construction: the P-51 and P-53 (180 thousand bpd, each), with operational start-up scheduled, respectively, for 2008 and 2009, in the Marlim Sul and Marlim Leste (South and East Marlin) fields. Additionally, an FPSO will be leased in 2008, for use in the Jabuti (Turtle) area of the Marlim Leste field.

Looking ahead to 2009, Petrobras is expecting to start production under the “Parque das Conchas (Seashells Park)” Project, with a capacity of 100 thousand bpd. 2010 should see the start-up of the Frade (Black Angelfish) platform (100 thousand bpd) and in 2011 the P-57 platform (180 thousand bpd), under phase 2 of the Jubarte field, and the P-55 (180 thousand bpd), in module III of the Roncador field, will both come on-stream.

The exploration and production of natural gas is also being intensified, under Plangás (Plan to Advance the Production of Natural Gas), which is fundamental to ensuring the supply of natural gas to the markets in the south and southeast of Brazil. In the southeast, the supply will rise from the present 15.8 million m³/day to 40 million m³/day by the end of 2008. In the Espírito Santo Basin, Plangás provides for the expansion of the Peroá (Triggerfish) project to 9.4 million m³/day and the development of the Canapu (Itajara) and Camarupim (Tarpon) fields, in addition to expansion of the Cacimbas Gas Processing Complex to 20 million m³/day. The first phase of this expansion (5.4 million m³/day) will be completed in early 2007, when the Peroá Gas Processing Plant comes into operation. In the Campos Basin, Plangás gives priority to the production of non-associated gas from a variety of reservoirs located not far from existing infrastructure within the Albacora, Roncador and Marlim Sul fields, as well as initial development of the Jabuti field. In the Santos Basin, the Merluza platform's output will be expanded to 2.5 million m³/day, with increased production from the Merluza (Silver Hake) field and initial development of the Lagosta (Lobster) field. Plangás foresees the expansion of gas supplies in the southeast to a total of 55 million m³/day, by 2010, with the Mexilhão (Mussel) project (2009) and Uruguá and Tambaú project (2010), located in the Santos Basin, both coming into operation, in addition to the Caraguatatuba Gas Processing Plant, whose first module will come on-stream in 2009, followed by the second module in 2010.

Discoveries

In 2006, Petrobras reported the commercial viability of 27 discoveries to the ANP (National Oil, Natural Gas and Biofuels Agency). Some of these areas – 18 of which are located offshore and 9 onshore – were classified as new oil and natural gas fields, while others were incorporated within neighboring fields. The exploration highlight was the discovery of light oil and gas in extremely deep waters in the Santos Basin block BM-S-11.

Estimates of Petrobras' stake in the new commercially viable areas indicate a total volume in the region of 2 billion 440 million boe, but this figure is subject to a more precise assessment. Of this total, 2 billion 387 million boe lie in offshore accumulations and 53 million boe are to be found onshore. Ten of the 27 areas are located in the Campos Basin; four are in

the Santos Basin; seven are in the Espírito Santo Basin; and six are located in basins in the north and northeast of Brazil.

In the Santos Basin, three areas operated by Petrobras were declared commercially viable and reclassified as the oil and natural gas fields of Tambuatá (Rock Beauty), Pirapitanga (Red Pacu) and Carapiá (Needlefish). A fourth area was incorporated within the Mexilhão field. The total volume is estimated at 560 million boe. In addition to these four areas, the company has a 40% stake in two other areas that were also reported to the ANP as being commercially viable.

What is more, the discovery of light oil and gas in block BM-S-11, in which Petrobras has a 65% stake, opens up promising new prospects not only for operations in the Santos Basin but for operations in extremely deep waters in other regions. In order to reach the oil and gas, in waters with a depth of two thousand meters, the company had to bore through a layer of salt that was more than two thousand meters thick.

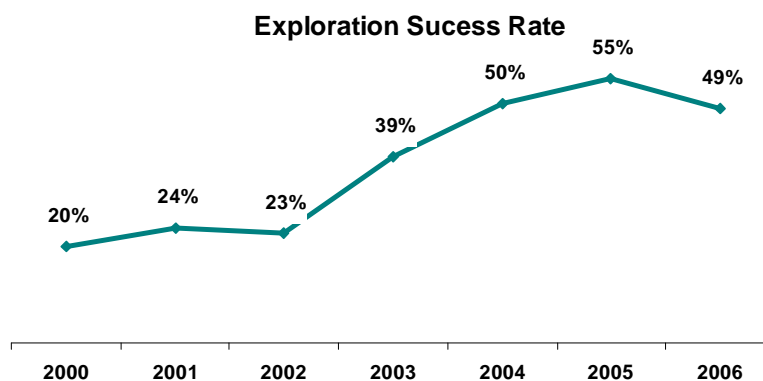
In the Espírito Santo Basin, four offshore and three onshore areas operated by Petrobras were declared commercially viable. On the continental shelf, where the new discoveries are estimated at 168 million boe, two areas were reclassified as the Carapó (Knifefish) and Camarupim gas fields and two areas containing gas and light oil were incorporated within the Golfinho and Canapu fields. The declaration of the onshore areas resulted in the creation of three new fields – Saíra (Tanager), Seriema (Crested Seriema) and Tabuiaia (Heron) –, with a total estimated volume of 7.4 million boe, which will help to maintain the level of onshore production.

With regard to the Campos Basin, the commercial declarations covered ten areas. Seven of these were reclassified as new fields: Maromba (Sardilella), Carataí (Cocosoda Catfish), Carapicu (Mojarra), Catuá (Coney), Caxaréu (Whale), Mangangá (Scorpion Fish) and Pirambu (Margate). One area was incorporated within the Baleia Azul (Blue Whale) field and two others into the Viola (Guitarfish) and Marlim Leste fields. The total estimated volume comes to 1 billion 510 million boe. Another important discovery was made in the Roncador field, in reservoirs below the productive seam.

Five declarations of commercial viability were made by Petrobras for onshore areas in coastal basins in the northeast of Brazil. Three were classified as fields: Tangará (Manakin), in the Bahia section of the Recôncavo Basin; and Pintassilgo (Siskin) and Jaçanã (Jaçana), in the Potiguar Basin. The other two areas were incorporated within the existing fields of Baixa do Juazeiro and Canto do Amaro, which are both located in the Potiguar Basin. In addition to those declared, three other onshore areas were discovered in the Sergipe-Alagoas Basin and two in the Recôncavo Basin. In the Solimões Basin, the company declared the commercial viability of the Araracanga field – a natural gas discovery made in 1997.

During the year, a total of 331 wells were drilled and completed for the development of production – 283 onshore and 48 offshore. For exploratory purposes, 80 wells were drilled – 50 onshore and 30 offshore. The exploration success rate was 48.7%, as 39 of the 80 wildcat wells

that achieved their geological objective show good prospects of becoming discoveries or producers of oil or natural gas.



New Concessions

At the ANP's Eighth Bidding Round, held in November, Petrobras proceeded with restructuring and extending the profile of its portfolio of exploration areas. The company acquired 21 of the 22 areas for which it bid, covering a total of 7,841.21 km². The new concessions that have been added to its exploration portfolio – 13 onshore, in the Tucano Basin, and eight in the Santos Basin – will be important to the attainment of the oil and gas production levels called for in the company's Business Plan 2007-2011.

The winning bids made by Petrobras and its partners in the eighth round came to a total of R\$ 276,924,361.00, of which the company's share was R\$ 248,227,933.50. Petrobras has exclusive rights to seven of the 21 blocks acquired, and is the operator in two of them, in partnership with other companies. In the other 12 blocks, the operations will be carried out by partners.

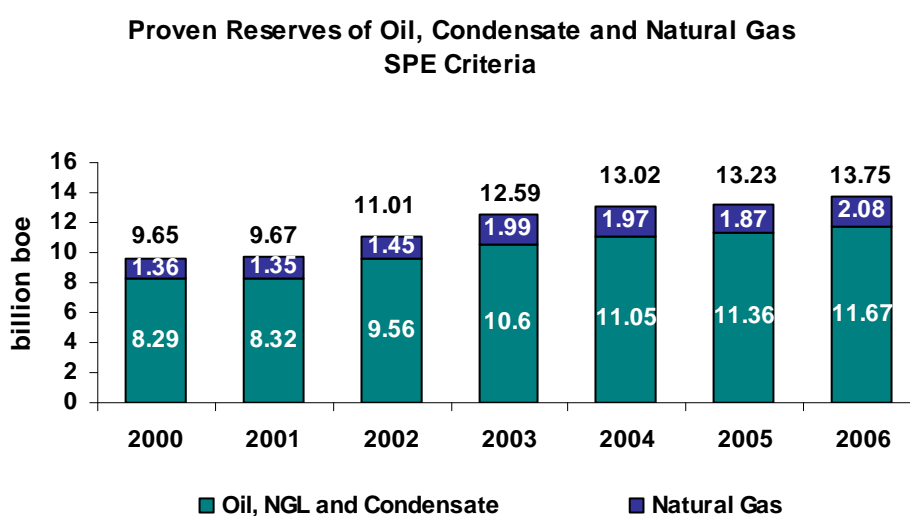
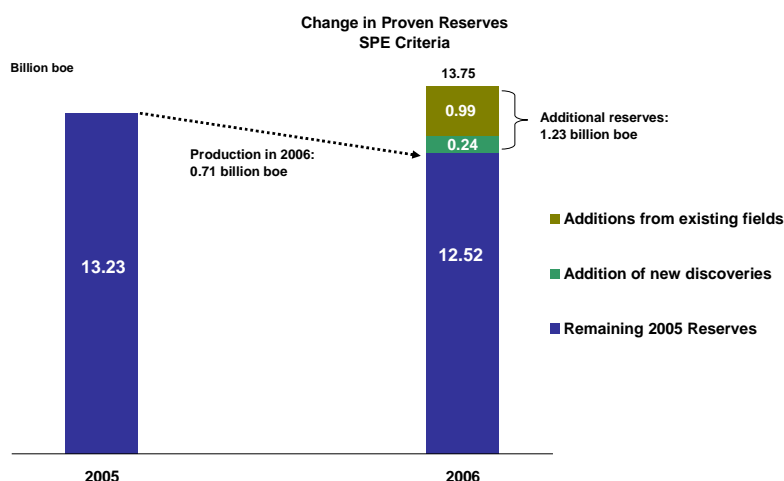
The offshore concessions acquired in the Santos Basin, covering a total area of 5,553.03 km², are considered to offer great potential. The onshore concessions in the Tucano Basin, covering a total of 2,288.15 km², are in frontier areas, with potential for the discovery of deep accumulations natural gas. When the contracts are signed, these concessions will probably be grouped by the ANP in various blocks.

With the various acquisitions and areas handed back over the course of the year, the company's portfolio of exploratory concessions comprises 144 blocks, covering a total area of 149.2 thousand km². Adding to this the ten areas with discovery evaluation plans (3.6 thousand km²) in operation, Petrobras' present exploration area covers a total of 152.8 thousand km².

Proven Reserves

Petrobras' proven reserves of oil, condensate and natural gas in Brazil amounted, at the end of 2006, to 13 billion 753 million boe, following ANP/SPE criteria – representing an increase of 3.9% in relation to the previous year. A total of 1 billion 226 million boe was added to the reserves over the course of 2006, against an accumulated production volume of 705 million boe, generating a Reserve Replacement Index (IRR) of 174%. This means that for every barrel of oil equivalent produced during the year, 1.74 barrels were added to the company's reserves. Meanwhile, the reserves/production (R/P) ratio is at 19.5 years.

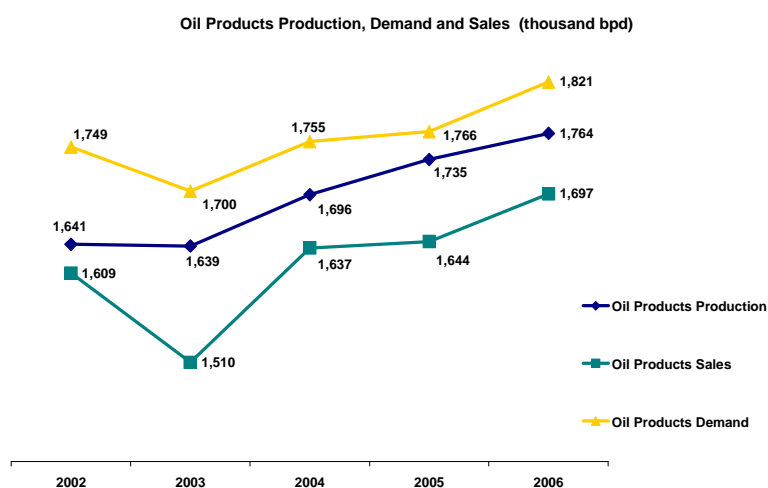
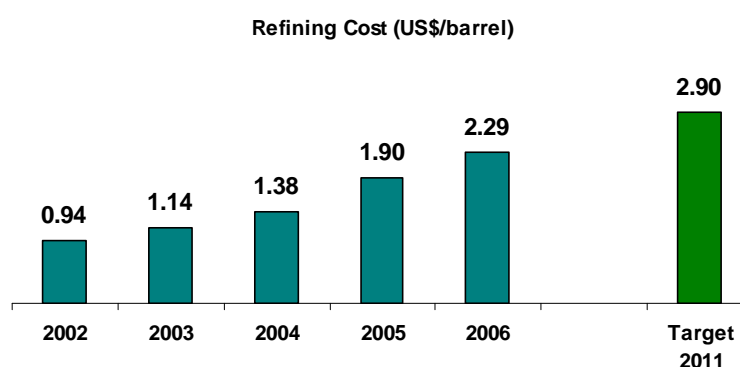
Two factors underlie the increase in proven reserves – one being due to the appropriation of amounts discovered in fields declared commercially viable during the course of 2006. Some of these declared areas are close to fields that are in the development phase and were, therefore, included within the figures for those fields. The other contributing factor arises from reservoir management practices in discovered fields that are already in the development or production phase.



Refining & Commercialization

Refining

In 2006, Petrobras set new records for refining and the production of oil products in Brazil. The average processed throughput (primary processing) of the company's 11 Brazilian refineries amounted to 1 million 746 thousand bpd of oil, while the production of oil products totaled 1 million 764 thousand bpd – representing increases of 1% and 2%, respectively, in relation to the previous year. The 80 % share of domestic oil in the total 2006 processed throughput is a reflection of the operational reliability of the units, which were working at an average of 89 % of their refining capacity.



The company proceeded with its investments to adapt the country's refineries to process the heavy oils that are produced in Brazil. New catalytic cracking and retarded coking units came on-stream at the Alberto Pasqualini Refinery (Refap) and a new coking unit will start operating at the Duque de Caxias Refinery (Reduc) in 2007. With the coking units, Petrobras is able to optimize the rendering of domestic oil into diesel fuel.

As part of the company's strategy for improving the quality of its fuels, Petrobras pressed ahead with the installation of hydrotreatment units (HDTs) at nine refineries. The

process of treatment with hydrogen, which reduces the sulfur content of the oil products, will meet the most stringent environmental specifications that are to come into effect as from 2009. At the same time, this will open up new export markets, such as the USA and the EU.

The launching of Podium Diesel and the development of H-Bio were milestones for quality and environmental protection in 2006. As with Podium gasoline, the new diesel fuel offers improved performance with less engine wear and lower sulfur content. H-Bio, a pioneering process from Petrobras, blends vegetable oil with oil fractions for the production of diesel fuel. The company also expanded the supply of S500 diesel fuel to eight new metropolitan areas - Curitiba, Salvador, Recife, Fortaleza, Belém, Vitória, Aracaju and Porto Alegre, all state capitals. This product, launched in 2005, has a sulfur content that is just one quarter that of ordinary diesel fuel.

Parallel with the growth in domestic oil production, Petrobras is developing two major projects – the Abreu Lima Refinery, in the state of Pernambuco, with a capacity of 200 thousand bpd, is a US\$ 4.0 billion undertaking that is being studied, together with Petr6leoos de Venezuela (PDVSA); and the Premium Refinery, with a capacity of 500 thousand bpd, will be the largest in the country. With operational start-up scheduled for 2011 and 2014, respectively, these new refineries will cope with the growing domestic demand, reduce imports of diesel fuel and bolster the country's exports of oil products, adding value to any surpluses of Brazilian oil.

Commercialization

In 2006, Petrobras sold an average of 1 million 697 thousand bpd of oil products in the Brazilian market – a 3% increase in relation to 2005. The leading products, in terms of sales volume, were gasoline, naphtha, fuel oil, diesel fuel, liquefied petroleum gas (LPG) and aviation fuel.

Gasoline registered the biggest increase in sales, by 7%, mainly due to the reduction, in March, of the percentage of anhydrous alcohol that is mixed with the gasoline sold at service stations, from 25% to 20%. In November, it was raised to 23%. Another factor was the expansion of the gasoline powered vehicle fleet, including the users of *flex fuel* vehicles who chose to use gasoline. Working in the opposite direction were a 5.1% real increase in the pump price and the growing use of natural gas to power vehicles.

There was a 5% increase in sales of naphtha. Faced with growing demand from the petrochemical centers, Petrobras expanded its production and partially substituted imports, thereby securing increased business.

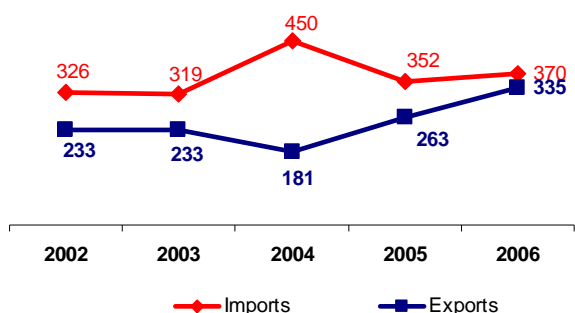
After several years of declining business in the fuel oil segment, sales were up 1%, helped by gains in market share and the response to new consumers. Among the sectors showing strong demand were manufacturing in the state of Par and the new thermoelectric power plants in the state of Amazonas.

Sales of diesel fuel were also up 1%, lagging behind the country's GDP growth. The principal reason was the poor performance of the agribusiness sector, which is still recovering from crisis in 2005/2006 and the appreciation of the real against other important currencies.

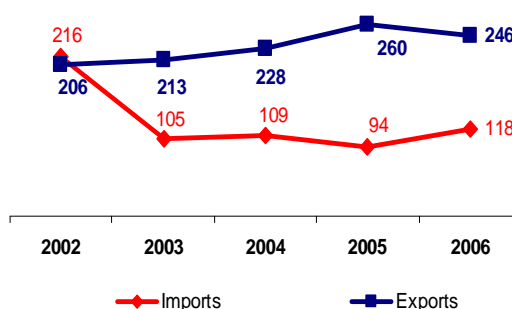
LPG saw an increase of 1.5% in sales, in response to a growing population and their improved purchasing power, brought about by a higher minimum wage and broad government measures to ensure household incomes. Sales of aviation fuel remained stable in relation to those of 2005.

The increase in domestic oil production, the optimization of the company's logistical structure and the opening up of new commercial opportunities enabled Petrobras to set new records in international sales and consolidate its position as the country's leading exporter. Oil exports hit a record 484 thousand bpd in November and closed the year at an average of 335 thousand bpd, an increase of 27% in relation to the previous year. Exports of oil products were down 5.4% compared with 2005, at an average of 246 thousand bpd. Imports averaged 370 thousand bpd of oil and 118 thousand bpd of oil products. In financial terms, the company recorded a deficit of US\$ 23 million.

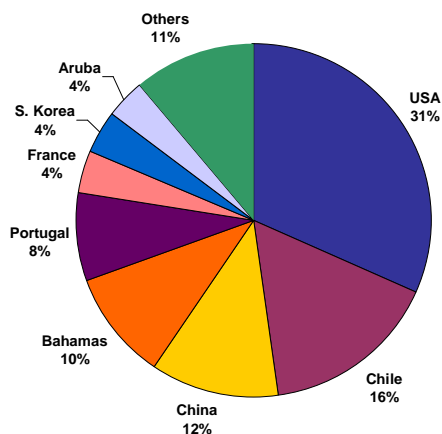
Oil Imports and Exports (thousand bpd)



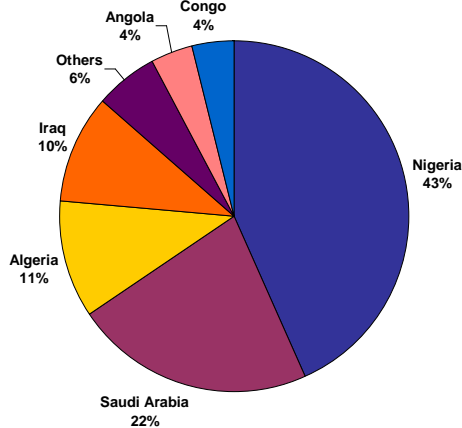
Oil Products Imports and Exports (thousand bpd)

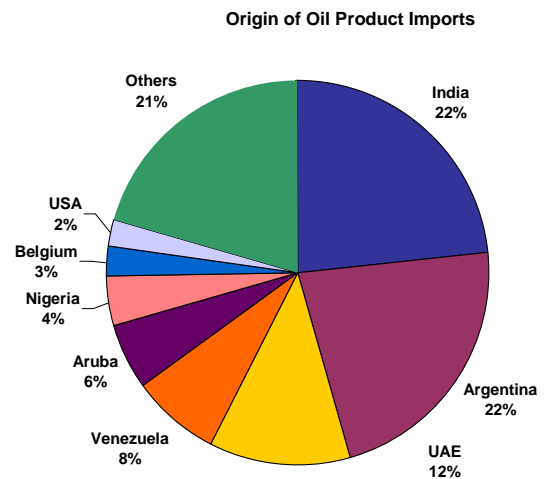
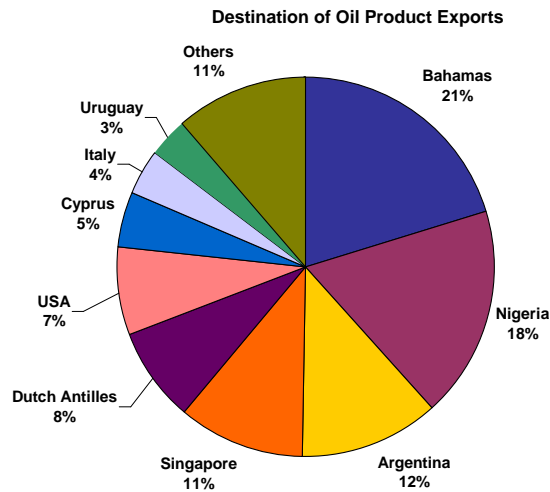


Destination of Oil Exports

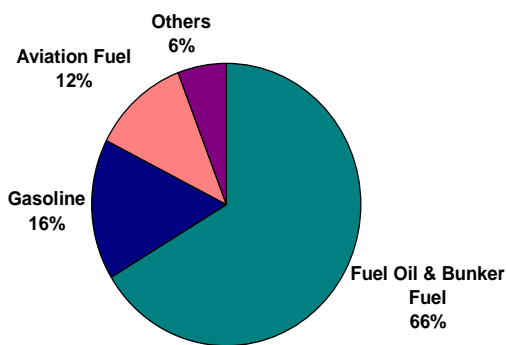


Origin of Oil Imports

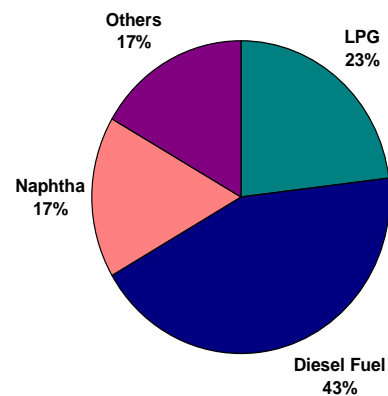




Oil Products Exports per type



Oil Product Imports per type



Petrochemicals

Petrochemicals are of strategic importance to Petrobras, providing diversification of the product portfolio and adding value to the oil and natural gas, in synergy with the company's other operations. Petrobras' activities in the sector, under the aegis of its subsidiary Petrobras Química S.A (Petroquisa), have been selectively built up for the production, in association with partners, of basic inputs and thermoplastic resins.

Petroquisa, which in 2006 became a wholly-owned subsidiary of Petrobras, has a stake in all the country's petrochemical hubs, through companies whose products are of strategic interest to Petrobras, such as calcined petroleum coke and catalytic agent for cracking oil. Petroquisa's net earnings for the year came to R\$ 133.5 million.

Notable among the various units that are being planned is the Rio de Janeiro Petrochemical Complex (Comperj), to be constructed in the municipalities of Itaboraí and São Gonçalo, in partnership with the Ultra Group and the Brazilian Development Bank (BNDES), at an estimated cost of US\$ 8.3 billion. The technical and economic studies for the project were completed in March.

This complex will process up to 150 thousand bpd of heavy oil, for the production of petrochemical raw materials and oil products, with an annual output of 1.3 million tons of ethylene, 880 thousand tons of propylene, 600 thousand tons of benzene and 700 thousand tons of p-xylene, as well as other oil by-products, especially coke. In addition to the basic petrochemical unit (UPB), the utilities center and the second generation units, Comperj will be equipped with a business and employee training center and a distribution center for channeling liquid products to loading terminals on the shores of Guanabara Bay. The operational start-up is scheduled for the beginning of 2012.

The second generation units will use as raw material the basic petrochemicals produced at the UPB, for the annual production of 880 thousand tons of polyethylenes, 850 thousand tons of polypropylene, 500 thousand tons of styrene, 600 thousand tons of ethylene glycol and 600 thousand tons of purified terephthalic acid (PTA).

Another undertaking that is under way is the industrial unit of Petroquímica Paulínia S.A., in an association between Petroquisa, which holds a 40% equity stake, and Braskem, at an estimated cost of US\$ 328 million. Located in the municipality of Paulínia (SP), next to the Paulínia Refinery (Replan), this unit will produce 300 thousand tons per year of polypropylene, using propylene supplied by the neighboring refinery and by the Henrique Lage Refinery (Revap). With an environmental license granted towards the end of 2006, construction of the production plant is going ahead and the unit is scheduled to go into operation in 2008.

Petrobras is proceeding with the technical, economic and environmental evaluation of the Minas Gerais integrated acrylic complex – a US\$ 540 million undertaking for the annual production of 160 thousand tons of raw acrylic acid and certain by-products. The complex, a pioneering initiative in Latin America, is scheduled for operational start-up in 2011.

Petroquisa has taken further steps in the project to set up a purified terephthalic acid (PTA) unit in Pernambuco, with the founding of Companhia Petroquímica de Pernambuco - PetroquímicaSuape. The industrial unit, involving the investment of US\$ 514 million, will have a production capacity of 640 thousand tons per year, and is scheduled to start operations in 2009. The raw material for the process will be paraxylene, which at first will be imported, but will subsequently be supplied by the Rio de Janeiro Petrochemical Complex.

Within the production chain to be created by the activities of PetroquímicaSuape, some of the PTA will serve as raw material for Companhia Integrada Têxtil de Pernambuco – CITEPE.

This company, in which Petroquisa has a 40% stake, was founded in 2006, with a view to setting up an industrial plant to produce polyester fiber (POY). The unit, budgeted at US\$ 273 million, will produce 215 thousand tons of the product annually, and is scheduled to go into production in 2009.

Petroquisa Equity Holdings

Company	Product	Voting Capital (%)	Total Capital (%)
Braskem S.A.	Basic, intermediate and final petrochemicals	9.8	8.3
Copesul – Companhia Petroquímica do Sul	Basic petrochemicals	15.6	15.6
Petroquímica União S.A.	Basic petrochemicals	17.5	17.4
Riopol – Rio Polímeros S.A.	Polyethylenes, ethylene and propylene	16.7	16.7
Metanor S.A. – Metanol do Nordeste	Methanol and by-products	49.5	34.3
Deten Química S.A.	Linear alkyl benzene and sulfonated I	28.6	27.7
Fábrica Carioca de Catalisadores S.A.	Catalysts	50	50
Petrocoque S.A. Indústria e Comércio	Calcined petroleum coke	40	40
Petroquímica Triunfo S.A.	Low density polyethylene, ethylene co	70.5	85
Petroquímica Paulínia S.A.	Polypropylene	40	40
Companhia Petroquímica de Pernambuco - PetroquímicaSuape	Purified terephthalic acid (PTA)	50	50
Companhia Integrada Têxtil de Pernambuco- CITEPE	Polyester fibers (POY)	40	40
NITROCLOR Produtos Químicos Ltda.	In the process of being wound up	38.8	38.8

Fertilizers

Petrobras pushed ahead with the modernization of its fertilizer production plants and the development of new projects to expand the production of nitrogen compounds, in line with the strategy of increasing its activities in the segment. In 2006, sales of ammonia e urea generated US\$ 350 million in gross revenue for the company – an increase of 6% in relation to the previous year.

The company's fertilizer plants, located in the states of Bahia and Sergipe, received R\$ 92 million of investment in projects to improve their operational reliability, logistics and product quality, as well as in Health, Safety and the Environment (SMS). In Sergipe, completion of the

new urea warehouse, with a capacity of 30 thousand tons, doubled the unit's storage capacity and brought added flexibility to the logistical operations.

In a fifth successive year of sales growth, the two plants sold 213 thousand tons of ammonia in the domestic market. In the urea fertilizer segment, Petrobras retained its leadership in the Brazilian market, with 710 thousand tons sold in 2006. As a result of the investment in reliability, the Bahia plant achieved its highest production figure in the last seven years, of 285 thousand tons.

A new urea granulation unit will come on-stream at the Sergipe plant in 2007, with an output of 600 tons a day. In order to substitute imports of nitrogenated fertilizers, Petrobras went ahead with the conceptual design of a new industrial plant – the UFN-3, which will use natural gas as a raw material. At an estimated cost of US\$ 822 million, this unit should produce 1 million tons of urea and 760 thousand tons of ammonia a year, as from 2012.

Another project that is being studied is the construction, at the Bahia plant, of an industrial plant with the capacity to produce 120 thousand tons of nitric acid a year for the Camaçari Petrochemical Complex. The unit would come on-stream in 2009.

Transportation

For the transportation and storage of oil, oil products, alcohol and natural gas, Petrobras works through its fully-owned subsidiary Petrobras Transporte S. A. - Transpetro, which operates 53 ships, 44 terminals and 9,958 kilometers of pipeline. This company fulfills a strategic role, providing the integrated logistical solutions and operational flexibility that give Petrobras a competitive edge.

Shipping fleet

Transpetro is the largest shipowner in South America, with a total deadweight capacity of 2.6 million tons (dwt). The company has a fleet of 46 oil tankers and leases the rest from third parties on bareboat charters. On this basis, contracts were signed in 2006 for the Navion Stavanger (Suezmax) and two other vessels, which will be received in 2007. The fleet also includes a Floating Storage and Offloading unit (FSO) and an AHTS-type support vessel.

Transpetro operates at a high level of reliability, providing quality services at competitive prices and an excellent level of compliance with Health, Safety and the Environment (SMS) standards. The vessels are regularly inspected under the Navio 1000 Program, which evaluates the fleet management, operating conditions and safety, in accordance with international regulations.

As part of its strategy to expand the services it provides to Petrobras, in line with the increasing domestic oil production, Transpetro proceeded in 2006 with its Fleet Modernization and Expansion Program. Having completed the first phase tendering process, 26 vessels have

been ordered from shipyards with Brazilian operations. Under the second phase of the program, a further 16 tankers will be built.

The first 26 vessels, divided into five tendering lots, represent a total investment of US\$ 2.5 billion, and comprise ten vessels of the Suezmax type; five Aframax; four Panamax; four oil product carriers and three liquefied-gas tankers. In the negotiations with the shipyards, the company managed to obtain a 14% price reduction, bringing the average price to around the level it would have paid if the orders had been placed abroad. Having the vessels built in Brazil aids the recovery of the country's large-scale shipbuilding industry, as well as developing a new supply center for Petrobras.

Terminals and oil pipelines

The operator of the majority of Petrobras' oil pipelines, land-based and waterway terminals, Transpetro transported 654 million cubic meters (m³) of oil, oil products and alcohol in 2006. During the year, the waterway terminals handled an average of 350 vessels a month.

The network operated by Transpetro comprises 7 thousand kilometers of oil and multi-product pipelines. The 44 terminals have the storage capacity of 65 million barrels (10.3 million m³).

In order to modernize and extend the network, adjusting it to the future requirements of both Petrobras and the country as a whole, the company is engaged in a number of initiatives. One of these is the Master Plan for Pipelines in São Paulo, covering a total of 27 municipalities, under which the network will be redesigned, keeping it away from more densely populated areas and thus improving operational safety. The new logistical infrastructure will be integrated with the expansion of Petrobras' petrochemicals, thermoelectric generation, refining capacity and natural gas supplies.

With planned investments totaling more than R\$ 2 billion, the plan includes the establishing of new pipeline courses and the extension of existing ones, the construction of 500 kilometers of pipeline and the deactivating of 110 kilometers of pipeline courses and 280 kilometers of pipelines in the Greater São Paulo metropolitan area. The Guararema terminal is to be expanded and a new one will be built Mauá. A total of 28 thousand direct and indirect jobs will be created by these works.

The company completed the studies for implementation of the Ethanol Export Corridor, which will raise the alcohol transportation potential from the present 1.2 million m³/year to 4 million m³/year in 2010. The first three projects – part of the plan to invest US\$ 600 million over six years – will connect Replan by pipeline to Guararema and the “Triângulo Mineiro (Minas Triangle region)”, via Ribeirão Preto, as well as establishing integration with the Tietê-Paraná waterway, connecting São Paulo with the country's Mid-Western region.

The Transpetro Ethanol Program has aroused the interest of other countries in Brazil's experience with the transportation of alcohol, creating opportunities for developing partnerships

in Latin America, the United States, Europe, Africa and Asia. In 2006, more than 80 thousand m³ of alcohol were exported to Venezuela, as a result of a bilateral agreement.

Yet another initiative is the Underground Water Treatment Program, which provides a logistical response to the growing quantity of water produced by Petrobras' fields, due to the increased production, together with the maturing of reservoirs and the technical methods used to recover the oil. In the area of tank storage, in order to eliminate logistical bottlenecks, Transpetro is augmenting its storage capacity by 500 thousand m³.

Natural gas

In the natural gas segment, Transpetro transported an average of 34 million m³ per day in 2006. In addition to expanding the system, with the integration of two new delivery points and a new gas pipeline (Dow-Camaçari), the company transferred the operation of its Espírito Santo and Bahia networks to the National Operational Control Center (CNCO), which operates all the pipelines by remote control.

The company is preparing the way for the integration into the system, in 2007, of 1.8 thousand kilometers of gas pipelines that are under construction. A further 1.6 thousand kilometers of gas pipeline that is on the drawing board should come into operation between 2008 and 2011, when the volume of natural gas transported by Transpetro will reach the milestone of 100 million m³ a day, including imported liquefied natural gas (LNG).

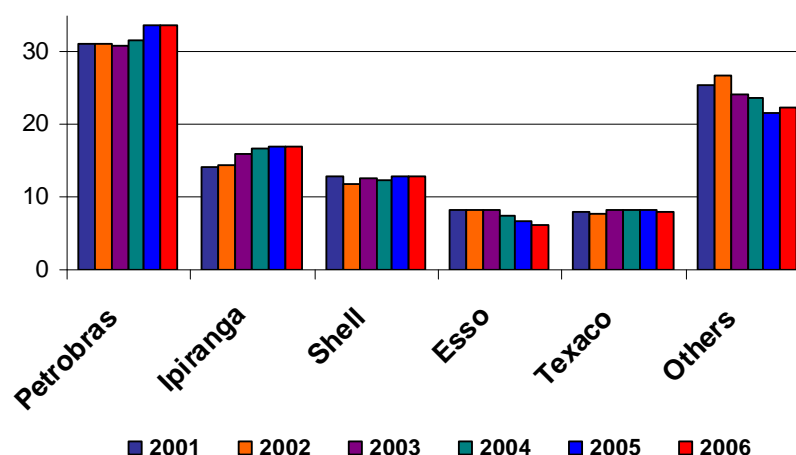
The Cabiúnas Terminal (RJ), Brazil's largest center for the processing of natural gas, will also see its capacity augmented in 2007, from the current 14.9 million m³ to 17 million m³ a day. Two new projects under way at the center will further raise the processing capacity, to 22.4 million m³ a day.

Distribution

Petrobras operates in the distribution of fuels through its subsidiary Petrobras Distribuidora, the market leader, with the country's largest network of service stations. Of the 5,870 BR service stations located all over Brazil, 638 belong to the company and the other 5,232 are run by dealers representing the Petrobras brand.

BR revenues in 2006 from products and services came to a total of R\$ 47.1 billion – up 8.0% in relation to the previous year, due to higher sales, which established a new record in October. The company's share of the distribution market reached 33.6% - 0.2 percentage points below the figure for 2005, as a result of the fierce competition in this sector during 2006. In the second half of the year BR managed to regain market share and in December accounted for 34.9% of sales.

Market Share of Fuel Distributors in Brazil



The leading position in sales of vehicular natural gas (VNG) is also held by BR. Its market share in 2006 was 23.7%, with the product available at 355 service stations. In the liquefied petroleum gas (LPG) market, operating through Liquigás Distribuidora, Petrobras had a market share of 21.7% – a dip of -0.1% in comparison with 2005.

Network of Active Service Stations	Number
BR outlets	5,870
Urban	4,560
Highway	1,282
Maritime	28
Own outlets	638
Third-party outlets	5,232
Convenience stores	740
VNG outlets	355

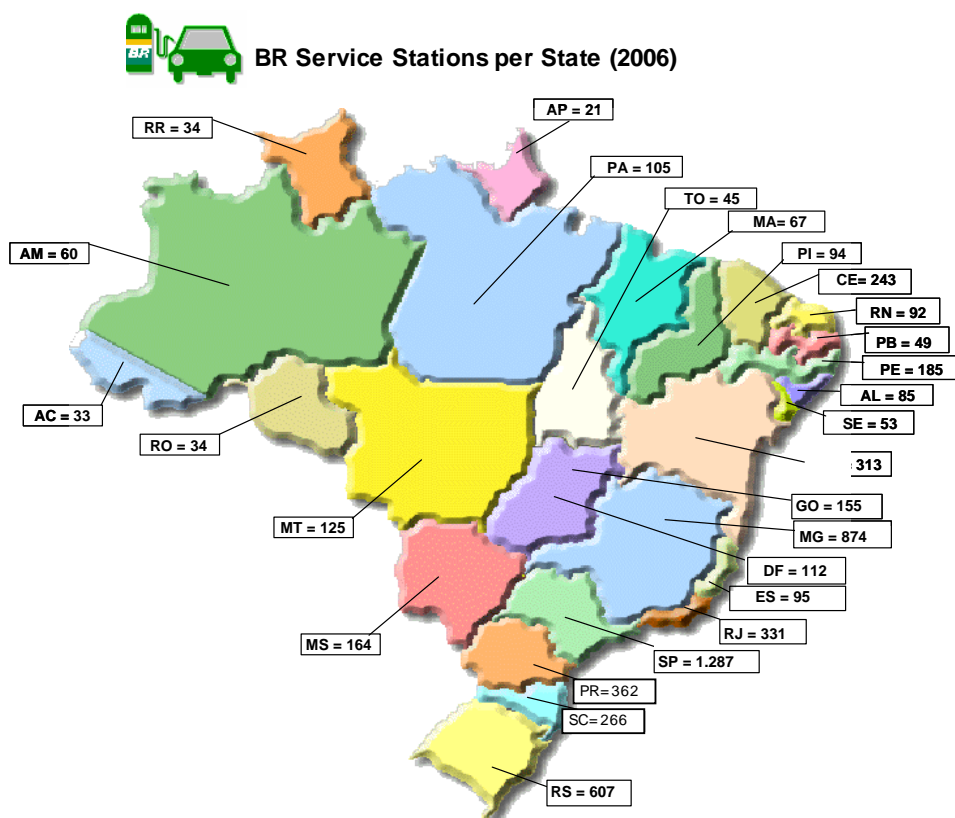
One of the distinctive features of the network in 2006 was the increased supply of biodiesel. In line with the company's strategy of retaining its position as the consumer's favorite brand and adding value for the Petrobras System, the distributor made the product available at 3,740 service stations all over Brazil. Biodiesel should be available throughout the entire network by June 2007.

The arrival of biodiesel at the pumps reinforced the public association of BR with virtues such as innovation, quality and social and environmental responsibility. Also launched in 2006 were Diesel Podium, with its low sulfur content; the Evolua line of cleaning and protective products; and new lubricants. The distributor also invested in the expansion and modernization of the service stations, bringing them into compliance with the latest safety and environmental protection standards.

To further please its customers, BR extended projects such as the “Cartão Petrobras” card, carried out promotions and trained its attendants, under the “Capacidade Máxima” program. In terms of its relationship with dealers and end consumers, the company organized regular visits by commercial representatives and gatherings for the presentation of plans and strategies, as well as distributing the “Jornal do Revendedor” newsletter.

Petrobras Distribuidora has a 45.5% share of the direct consumer market, with notable participation in the segments of aviation products (53.5%), asphalt (29.4%) and retail road transportation (40.4%). During 2006, the company developed new services to gain customer loyalty in the transport sector.

Since 2005, BR has been investing in the adaptation of the installations of its distribution network – the largest in Brazil – to handle biodiesel. Its 56 strategically positioned bases and terminals ensure ample reach for the placing of Petrobras products. The network also allows the integration of transport and storage solutions with service quality, thereby giving the company a competitive edge.



Natural Gas

The natural gas market continues to grow, with average sales to distributors reaching 38.7 million m³/day in 2006 – an increase of 7% in relation to the previous year. This increased

consumption is driven by factors such as the expansion of the logistics infrastructure, the entry of new large-scale consumers into the market and a sharp increase in the natural gas (VNG) powered vehicle fleet (GNV). The increase also reflects the consumer's growing recognition of the product's technological, operational, environmental and economic qualities.

Supplies

To supplement domestic production, in order to meet the level of demand, Petrobras imported an average of 24.7 million m³/day of natural gas – an increase of 9% in relation to the volume in 2005.

Following its strategy of developing and consolidating the market, Petrobras set in motion its Plan to Advance the Production of Natural Gas (Plangás). The supply of domestic gas to the southeast of Brazil will be augmented in two stages – in the first, up to 2008, from the current 15.8 million m³/day to 40 million m³/day; in the second, up to 2010, the volume will reach 55 million m³/day.

To ensure that the increasing level of consumption in the country is sustainable, Petrobras is preparing the way for its entry into the global liquefied natural gas (LNG) market as an importer. For the conversion of the LNG into gas (gasification) and its delivery to the transport network, the company is studying the possibility of setting up two floating gasification terminals, one in the state of Ceará and one in Rio de Janeiro.

Transportation

Implementation of the Brazilian Natural Gas Transportation Network (RBTGN) proceeded through 2006. The putting together of a supply system that is flexible, safe and competitive – a network of interconnected gas pipelines extending from Fortaleza to Porto Alegre and from São Paulo to Bolivia – is in strategic alignment with the development of production in the Campos Basin and the exploration of the company's offshore blocks, allowing the immediate channeling of production from new discoveries.

One of the leading RBTGN projects that is under way is the Northeast-Southwest Interconnection Gas Pipeline (Gasene) – comprising three stretches of pipeline: Cabiúnas–Vitória (Gascav), Cacimbas–Vitória and Cacimbas–Catu (Gascac). In 2006, Petrobras closed two financing deals with the Brazilian Development Bank (BNDES), for the specific purpose company Transportadora Gasene S.A., which is responsible for the project, for the total sum of R\$ 1.36 billion.

The 131-kilometer stretch in the state of Espírito Santo (Cacimbas–Vitória), will be operational in early 2007. Work on the stretch connecting Rio de Janeiro and Espírito Santo (Cabiúnas–Vitória) began in June and are scheduled to be completed in October 2007. The Cacimbas–Catu stretch, between Espírito Santo and Bahia, is at the tendering stage, and should be ready in the second half of 2009.

In the north, construction of the 670-kilometer Urucu–Manaus Gas Pipeline was started in June and is scheduled for completion in the first quarter of 2008. In the northeast, the Atalaia–Itaporanga pipeline, in the state of Sergipe, and the Dow–Aratu–Camaçari pipeline, in Bahia, both came into operation. Another three pipelines – the Carmópolis–Pilar, between Sergipe and Alagoas, Itaporanga–Carmópolis (SE) and Catu–Itaporanga, connecting Bahia and Sergipe – should start up in 2008.

ENERGY

Electricity

Petrobras has increased its participation in the thermoelectric energy segment, following a strategy of consolidation as an integrated energy business. The company is involved in the entire thermoelectric energy generating production chain, as well as in the process of commercialization.

At an energy auction organized by the National Electricity Agency (Aneel) in October, Petrobras sold 205 MW produced by its plants. As a result, the company has secured a stable revenue stream of R\$ 103 million/year, for a period of 15 years, beginning in 2011.

In 2006, Petrobras completed its acquisition of the merchant power plants, with the purchase of the UTE Mário Lago (formerly Macaé Merchant). This takeover, along with the acquisitions of the MPX Termoceará and Eletrobolt power plants, puts an end to the legal controversy surrounding the consortium contracts signed in 2001 and 2002, under which the company was obliged to make contingency payments in regard to taxes, fees, tariffs, operating expenses, maintenance and investment in the event that the plants did not earn sufficient revenue. The plants have reduced their expenses and guarantee full receipt of the revenue from power generation, in accordance with Petrobras' guidelines for its participation in the electricity sector.

Petrobras also purchased the UTE Bahia I (31MW), a fuel oil powered thermoelectric plant, to serve as a generation back-up. With the same intent, the company closed a contract for the provision of services by the UEG Araucária (428MW), which also allows for the efficient allocation of the natural gas, due to its adjusted cycle.

Two thermoelectric plants are under construction – Termoçu (RN) and Cubatão (SP) – , within co-generation projects that are in synergy with Petrobras' activities in these regions. Projects are also under way for cycle closure and the conversion of thermoelectric plants to dual fuel (natural gas and diesel), bringing enhanced efficiency and reliability in the supply of fuel to the power plants.

Renewable Energy

Attaining leadership in the domestic production of biodiesel and expanding its ethanol business have become priorities for. To this end, the company has developed a variety of activities in the field of renewable energy, with a view to hitting the audacious targets set down in the Business Plan 2007-2011 – during which period a total of US\$ 700 million will be invested in renewable sources of energy.

The generation of electricity by wind farms and small-scale hydroelectric plants are other areas in which Petrobras is investing in the field of renewable energy. According to the goals defined in 2006, by 2011 the company will be producing 850 million liters of biodiesel, exporting 3.5 billion liters of ethanol and generating 240 MW of electricity through renewable sources.

Biodiesel

In order to attain leadership in Brazilian biodiesel production and strengthen its position as an integrated energy business, Petrobras threw itself into large-scale production in 2006, by beginning the construction of three plants. Representing a total investment of R\$ 227 million, the units, located in Candeias (BA), Montes Claros (MG) and Quixadá (CE), will have a combined annual production capacity of around 57 million liters of biodiesel and will be inaugurated before the end of 2007.

These undertakings are in alignment with the National Program for the Production and Use of Biodiesel. As from January 2008, it will become compulsory for diesel fuel to have a 2% biodiesel content. In order to obtain the necessary ingredients – soybeans, cotton, castor beans and oil palm fruit, as well as animal fat –, the company is entering into partnerships with entities formed by small-scale farmers, thereby gaining the tax benefits allowed under the “Selo Combustível Social (Seal of Approval for Socially Responsible Fuels)”, granted to biodiesel companies that generate work and income for subsistence farmers.

Petrobras aims to produce 850 million liters of biodiesel a year by 2011. In order to attain this level of production, the company is analyzing some fifteen other projects in various parts of the country, in partnerships with investors ranging from large corporate groups to rural workers' cooperatives.

Biodiesel provides reduced emissions of greenhouse gases, sulfur and particulates, as well as improving engine performance. In addition to the environmental and social benefits, in harmony with the growing use of sustainable sources of energy, this product will hasten the end of diesel imports.

Ethanol

Petrobras' strategy for its ethanol business is focused on exports, with a view to opening up new markets and developing long-term relationships with the clients, in increasing synergy with the company's International area. In 2006, earnings from foreign sales of ethanol

exceeded US\$ 14 million. The volume sold, amounting to more than 80 million liters, helped to consolidate the logistical corridor for the exporting of ethanol from the south-central region, through the Ilha D'Água Maritime Terminal, via the Paulínia Refinery.

Concern over the imbalance between supplies and the growing demand for the product in the first few months of the year led the company, out of a sense of responsibility and commitment to sustaining domestic supplies, to export ethanol only in the second half of the year, when the situation had stabilized and domestic demand was being met. This meant that the export volume was lower than had initially been forecast for the year.

To encourage the consolidation of the international ethanol market, Petrobras joined the board of the recently formed International Ethanol Trading Association (IETHA) and set up a joint-venture, Brazil-Japan Ethanol (BJE), based in Tokyo, devoted to developing the Japanese market for the product. The company also reached agreements with the Central Energy Fund (CEF), of South Africa, and with Mitsui, of Japan, for the exporting of ethanol.

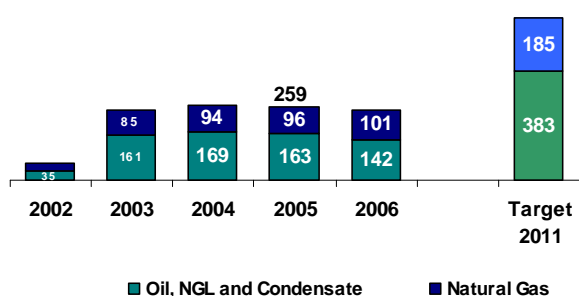
International Activities

With business activities in 19 foreign countries, Petrobras is consolidating its position as an integrated energy business an international presence and leadership in Latin America. The company is involved in the entire chain of activities in the Latin American oil, natural gas and electricity sectors, while at the same time augmenting its stake in undertakings in North America, Africa and Asia.

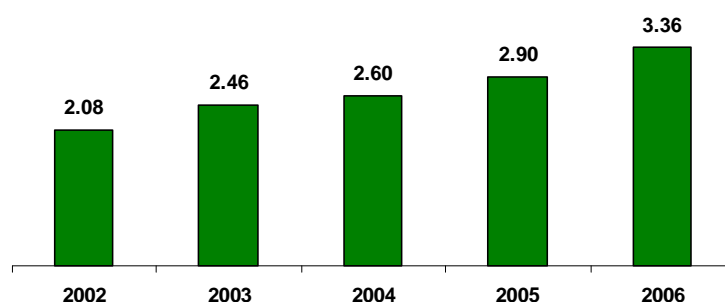
The activities in the International Business Area encompass oil and gas exploration and production in 14 foreign countries – Argentina, Bolivia, Colombia, Ecuador, Peru, Venezuela, Mexico, the United States, Angola, Equatorial Guinea, Nigeria, Tanzania, Iran and Libya.

In February 2007, Petrobras acquired stakes in exploration blocks in Senegal and Pakistan, marking the company's initial foothold in these countries.

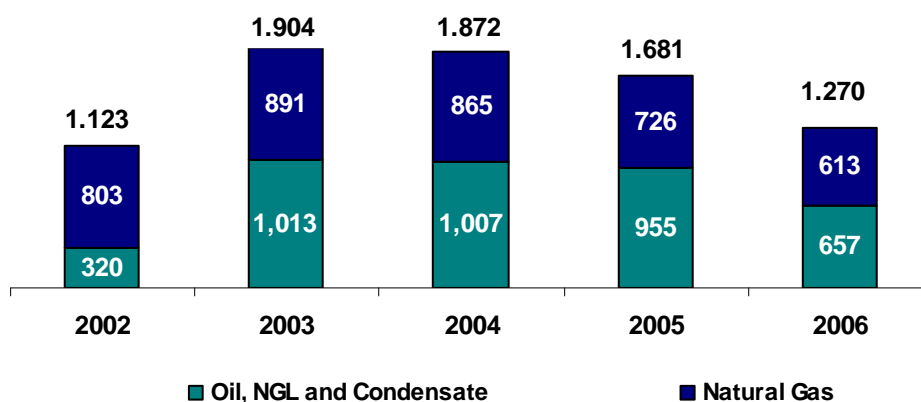
International Production of Oil, NGL, Condensate and Natural Gas (thousand boed)



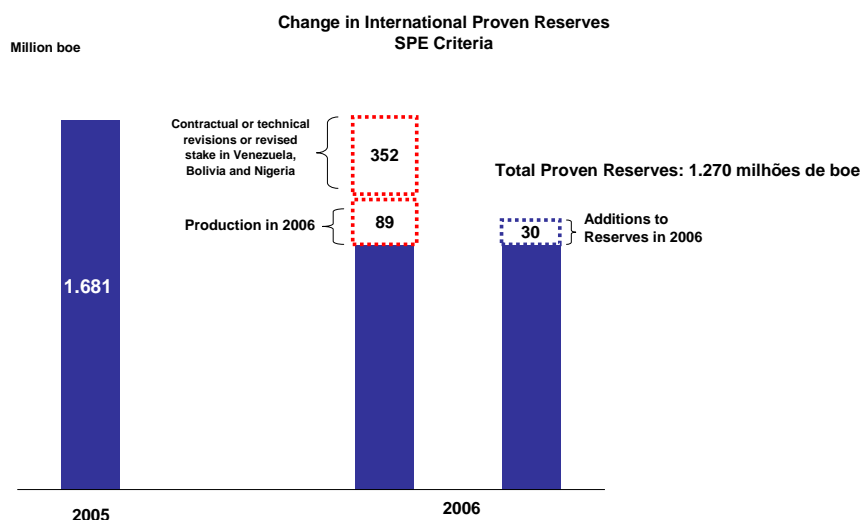
International Lifting Cost (US\$/barrel)



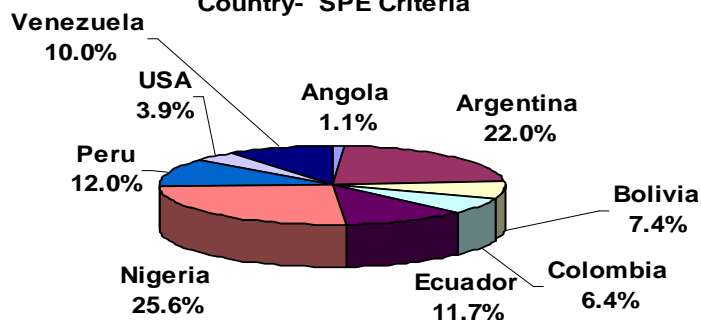
International Proven Reserves of Oil, NGL, Condensate and Natural Gas SPE Criteria (Million boe)



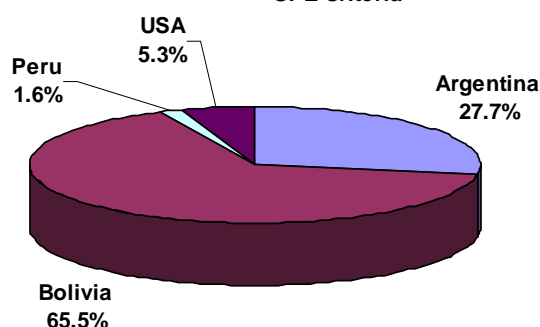
The company's proven reserves outside Brazil, according to SPE criteria, showed a reduction in relation to 2005 of 411 million boe (-24.4%), because the addition of new proven reserves during 2006 was exceeded by the year's production and contractual revisions, notably with regard to Venezuela.



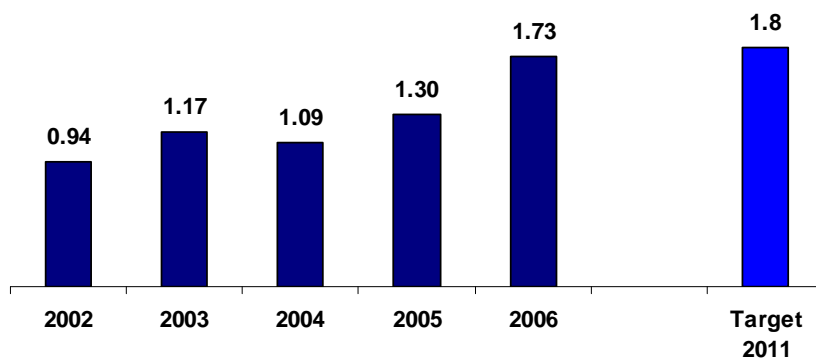
International Proven Reserves of Oil and Condensate per Country- SPE Criteria



International Proven Reserves of Natural Gas per Country SPE Criteria



International Refining Cost (US\$/barrel)



The strategy for growth abroad provides for the bolstering of the company's activities in countries where it is already present, such as Argentina, while opening up new business fronts in other markets, such as refining in the USA. In the areas of exploration and production, the priority regions are the Gulf of Mexico and Africa, where Petrobras is girding itself to produce oil in deep and extremely deep waters off the Niger River Delta, in Nigeria, and is pursuing exploration opportunities in frontier regions, such as the extremely deep waters off the coast of Tanzania.

In the area of refining, the goal is to augment the company's activities through investment in the expansion and conversion of the Pasadena refinery, in the United States, and seeking opportunities for new refineries abroad. The objective is to add value to the heavy oil produced by the company, providing the market with a product mix combining enhanced value and improved quality. To this end, investments will be focused on the adoption of technology that will enable refineries that were originally built to handle light oil to be able to process heavier throughput.

South America

Argentina

As an integrated energy business, Petrobras is present throughout the entire value chain for oil and natural gas, together with electricity generation. The company's 2006 production in Argentina – its highest outside Brazil – attained an average of 62.1 thousand bpd of oil and NPG and 45.8 thousand boed of natural gas, making a total of 107.9 thousand boed. Petrobras had a stake and operated in 17 blocks that are in production and in 10 that are in the exploration phase and initiated its exploration of deep waters off the Argentinean coast. The lifting cost was US\$ 4.4 per boe.

In the areas of petrochemicals and fertilizers, Petrobras owns the Puerto General San Martin, Zarate and Campana plants and has a 40% stake in Petroquímica Cuyo. The operations in Argentina are tied in with the southern Brazilian state of Rio Grande do Sul, where its subsidiary Innova turns out products such as styrene, polystyrene and UAN.

Petrobras distributes oil products through a network of 719 service stations, which sold 48 thousand bpd of fuels and lubricants in 2006 and has a 13.8% share of the gasoline and diesel market and 11.1% of the lubricants market. The number of service stations operating under the Petrobras banner increased from 457 to 492 during the year. Reflecting the growing brand presence, sales increased by an average of 2.7%. The company has a 50% stake in the parent company of Transportadora de Gás Del Sur (TGS), which owns the country's largest network of gas pipelines.

In the area of electricity generation, Petrobras has full ownership of the Genelba thermoelectric plant, which uses natural gas, and of the Pichi Picún Leufú hydroelectric plant. It also has a 27.3% stake in Edesur, the distributor for the central area of Buenos Aires. Petrobras is negotiating the sale of its equity stake in Transener, the country's leading electricity transmission company.

Petrobras has a 34% equity stake in Cia. Mega, which works in oil products and logistical services. In 2006, this company sold 1 million 433 thousand tons of ethane, propane, butane and natural gasoline.

Bolivia

The Bolivian production of natural gas for export is essential to sustaining the growing consumption in Brazil. In 2006, Petrobras sold 7.27 million m³/day – 23.4% of the country's total exported. Of the company's exports, 6.25 million m³/day went to the Brazilian market and 0.55 million m³/day to the Argentinean market.

In 2006, as a result of the Hydrocarbons Law, introduced the previous year, the nationalization of foreign assets imposed significant changes on the sector, with taxation, operational and financial impacts. Even with the new regulatory framework established by the

nationalization decree, signed in May 2006, Petrobras remains the largest oil and natural gas company in Bolivia, and contributed 22% of the country's taxation revenue for the year.

The decree tied companies' continuation in Bolivia to the signing of new contracts. In its negotiations with the government regarding exploration and production activities, Petrobras reached the following understanding agreements: contracts will be for shared production, and not for the provision of services; the company will bear the full cost and risk of all oil operations; payment of royalties and other government quotas is to be made through Yacimientos Petrolíferos Fiscales Bolivianos (YPFB), through which the production is channeled, and amounts to some 80% of revenue; compensation will be paid by YPFB, to be calculated based on the recovery of costs, prices, volumes and investments, net of due taxes. Moreover, Petrobras retains responsibility for operations in the San Alberto, Rio Hondo, Ingre and Irenda blocks, ownership of the assets and rights to the reserves that are to be posted by the company. The contracts, approved by the Bolivian Congress in November, are valid for 30 years.

The new regulations reduce to 49.9% the proportion of Petrobras' stake in the refineries of Gualberto Villaroel, in Cochabamba, and Guillermo Elder Bell, in Santa Cruz de La Sierra, which process a total of 39.9 thousand bpd. The company's refining activities are now performed as a provision of services. Negotiations are still under way with the Bolivian government over the amount of compensation to be paid to Petrobras.

In the area of oil product sales, YPFB has become the only wholesale distributor. Petrobras has fully withdrawn its EBR (Empresa Boliviana de Refinación) brand and currently retains just 26 service stations under the Petrobras brand.

With regard to natural gas, in February 2007 it was decided that no changes would be made in the volumes or in the formula for calculating the purchase price of natural gas from Bolivia contained in the present contract between YPFB and Petrobras (GSA). The company agreed to pay YPFB, at the prevailing international market prices, for the net hydrocarbon fractions (ethane, butane, propane and natural gasoline) present in the natural gas effectively delivered that raise its calorific value to over 8,900 kilocalories (kcal) per m³, equivalent to 1,000 BTU per cubic foot. YPFB will ensure that the minimum calorific value of 9,200 kcal/m³ is met, and Petrobras will study the best way to exploit these components in the future.

In the area of transportation, in addition to its stake in GTB, operator of the Bolivian stretch of the Bolivia-Brazil gas pipeline, Petrobras retains its stakes in the Yacuiba-Rio Grande (Transierra) gas pipeline, as operator, and in the San Marcos gas pipeline.

Colombia - In the area of exploration and production, Petrobras has a stake in 16 contracts – seven for production and 9 for exploration –, and is the operator in ten of these. In 2006, the average production amounted to 16,843 bpd of oil and NGL and 6.25 thousand m³/day of natural gas, making a combined total of 16,880 boed. One of the highlights is the company's involvement as operator of the Tayrona block, the country's only offshore block, in partnership with Exxon and the state-owned company Ecopetrol. Following a 50% contractual devolution,

the block still covers an area of more than 22,000 km². The first wildcat well is to be drilled in 2007. The company has also formed a consortium with Ecopetrol for the revitalization of the Tibu field. The investment, which will raise the production from 2,000 bpd to 15,000 bpd, is estimated at US\$ 500 million over the next six years, with the consortium members having the option to withdraw from the contract at the end of the first or second year, having made investments of US\$ 20 or US\$ 40 million, respectively.

Chile - Petrobras continues to seek business opportunities in this country, through a representative office in Santiago that was opened in 2005. The company sells the lubricant Lubrax here, with sales amounting to 848 m³ in 2006.

Ecuador - Petrobras, operating in two blocks, produced 11.9 thousand boed of oil and NGL in the country in 2006. At the beginning of 2007, the company received government approval for the sale of 40% of its stakes in Block 18, which is in production, and Block 31, which is in the exploration phase, to the Japanese company Teikoku. Petrobras is also negotiating with the government for EIA approval of the development of Block 31.

Paraguay - In 2006, Petrobras entered the segment of oil product distribution. The company presently owns 131 service stations and 45 convenience stores. The network has annual sales of 317 thousand m³ of oil products. Among the assets acquired are installations for the sale of LPG and the marketing of aviation products.

Peru - The company has a stake in six blocks – one of them in production (Lot X) and the others in the exploration phase. In 2006, the average production amounted to 12.7 thousand bpd of oil and 1.8 thousand boed of gas, making a total of 14.6 thousand boed.

Uruguay - Petrobras entered the oil product distribution segment, taking over 89 service stations, racking up annual sales of 330 thousand m³ of oil products, in addition to maritime products, asphalt and aviation products. The company is also involved in the distribution of natural gas, in the province of Montevid u and in the interior of the country, selling a total of 120 thousand m³/day of gas.

Venezuela - The new legal framework for the country's oil industry introduced a new contractual model for the activities of companies operating mature fields under a provision of services contract. As from April 2006, the fields in this country operated by private national or foreign companies under this type of contract will be operated by mixed companies under the control of Petr oleos de Venezuela S.A (PDVSA), which will have a 60% stake. Petrobras, which operated the Oritupano-Leona, Acema, Mata and La Concepci n fields, became a partner in the corresponding mixed companies, with stakes ranging between 22% and 36 %.

Petrobras continues to operate the Moruy II block, in the Gulf of Venezuela, for the exploration natural gas. Moreover, the company is studying a partnership with Petr leos de Venezuela (PDVSA) for the production of extremely heavy oil from Carabobo I, in the Orinoco Strip; and for the production of natural gas in Mariscal Sucre, in the Venezuelan sector of the Caribbean. The agreements also embrace studies for the setting up of a mixed company to produce oil from five mature fields, onshore, in the Oriente and Maracaibo basins.

North America

United States

The company has stakes on 302 blocks within the American sector of the Gulf of Mexico, and is the operator in 149 of them. In an auction held in September, Petrobras secured the greatest number of blocks – 34 –, at a cost of US\$ 45 million.

The company has begun exploration work, in the extreme west of the Gulf of Mexico, to test new geological possibilities. The first well drilled indicated the presence of natural gas, but the thickness of the reservoir was not sufficient to make it commercially viable. Nevertheless, the result demonstrated the potential of the area, where at least one more well will be drilled in 2007.

Petrobras' average production in the Gulf was 4.0 thousand boed, below the forecast for the year, largely due to the effects of the hurricane season, towards the end of 2005. Normal production was restored only in August 2006.

In extremely deep waters, the company managed to obtain a larger stake in the discoveries of Cascade and Chinook, becoming the operator for the two projects. The production, with start up scheduled for 2009, will make use of a Floating Production, Storage and Offloading (FPSO) platform ship. Putting into practice a project of this kind, embracing new technology, represents a landmark in the American oil industry.

In deep waters, in the Garden Banks Quadrant, Petrobras pushed ahead with the development of the Cottonwood field, in which it has assumed full control, having bought out its partner's 20% stake. Production began in February 2007.

At the Pasadena Refinery, in Texas, in which the company has a 50% equity stake, studies are proceeding for the doubling of the processing capacity, from the present 100 thousand bpd, and the installation of units for the processing of heavy oils. The investment is estimated at US\$ 2 billion.

Mexico - Petrobras is participating, in partnership with Teikoku, of Japan, and Diasvaz, of Mexico, in two contracts for the provision of multiple services to Pemex, in the Cuervito and Fronterizo blocks. The services include exploration, production development and production. Petrobras has a 45% stake in each of these contracts.

During 2006, 12 wells were drilled and the company obtained ISO 14001 and OHSAS 18001 certification of the process of "development, infrastructure and maintenance in the operation of fields for the production of non-associated gas".

Europe

Turkey - Petrobras is in a partnership with the Turkish state-owned company TPAO for exploration and production in two Black Sea blocks with potential for holding large reserves - the Kirklarelli block, in the western part of the Turkish sector, under 1,200 meters of water; and the Sinop block, to the east, with a depth of 2,200 meters.

Africa

Nigeria - The Agbami and Akpo projects – giant fields in the Niger Delta – continue to be implemented, with start-up scheduled for 2008. Production at Agbami should attain 250 thousand bpd, the company's part being 37 thousand bpd. Akpo will produce 185 thousand bpd, with Petrobras' share amounting to 36 thousand bpd. The company has already invested US\$ 930 million in the projects, of a budgeted total of US\$ 1.9 billion.

In Block OML 130, in which it has a 16% stake, Petrobras received an indemnity of US\$ 354 million from the Nigerian company *South Atlantic Petroleum* (Sapetro), which sold its stake (45%) to *China National Offshore Oil Company* (CNOOC). This compensation, provided for in the contract, corresponds to 50% of the investments made by the company, which will be responsible for 20% of the future investment.

The existence of significant accumulations of oil in the block has been confirmed, following the drilling of four wells at the Egina hub. Testing of the field's commercial viability will be carried out in 2007. As the operator of Block OPL 324, in the Gulf of Guinea, Petrobras drilled a 6,091 meter well in 2,670 meters of water depth – a new record for the Gulf of Guinea –, but without finding hydrocarbons.

The company expanded its activities in the Gulf of Guinea, strengthening its presence in deep waters off the West African coast. With a 45% stake, Petrobras is the operator of Block OPL 315, along with partners Statoil, of Norway, and Ask Petroleum, of Nigeria. Studies are in progress to place the block in its regional geological context, with a view to drilling the first exploration wells.

In support of the use of alcohol (ethanol) as a fuel in this country, Petrobras continued its negotiations with the Nigerian National Petroleum Corporation (NNPC) to supply the product. The accords include the providing of technical support for adding the product to the country's gasoline.

Angola - With a stake in four more contracts, Petrobras had a total of six E&P assets in this country at the end of 2006 – among them, Block 2 of the Lower Congo Basin, where the company produced 5.4 thousand bpd. In Block 34, despite not finding oil in two wells that have

been drilled, technical analyses have led to the conclusion that deeper geological layers present good prospects, with the result that the exploration deadline has been extended, with another well planned to be drilled in 2007. Petrobras is the operator, for the first time in Angola, in the new exploration blocks 6, 18/06 and 26, and is a partner in Block 15/06.

Equatorial Guinea - In negotiations with the government, Petrobras has extended for another two years the contract to explore Block L, with no obligation to drill an exploration well.

Libya - The company proceeded with its exploration of Area 18 in the Libyan sector of the Mediterranean. Partnered by Oil Search Limited, of Papua New Guinea, Petrobras is the operator, with a 70% stake, and has a contract for the sharing of the production with the state-owned company National Oil Company (NOC). In the event of exploration success, NOC will assume 51% of the investment.

Tanzania - Petrobras completed the seismic surveying of blocks 5 and 6, in extremely deep waters of the Máfia Basin, having signed the contract for Block 6 in December. The company has full rights over the blocks and, depending on the seismic analysis and technical and economic evaluation, could take on a partner, while working as the operator. The company's presence in this country reinforces its position in a frontier of exploration off the east coast of Africa. Petrobras has 20.2 thousand km² under full concession and operation rights.

Mozambique - Petrobras bought a 17% stake in the Zambezi Delta block, off the coast of Mozambique, in its first opportunity for investment in this African nation. The commitments undertaken provide for the acquisition of 2D seismic data and the drilling of a well in 2007. Petrobras' effective entry into the consortium is still awaiting authorization by the local government, which ought to be granted in 2007.

Asia

Iran - In November, the company started drilling the first of two exploration wells in the Tusan block, in shallow waters in the south of the Persian Gulf. Petrobras is the operator holding a 100% stake, according to a contract closed in 2004 with the National Iranian Oil Company (Nioc).

Social and Environmental Responsibility

Because of its socially and environmentally responsible performance, Petrobras was selected in September for the Dow Jones Sustainability Index (DJSI) – a yardstick for investors who are concerned about social and environmental responsibility, provided by the New York stock market. In Brazil, since December, the company's shares have been included in the Corporate Sustainability Index of the São Paulo Stock Exchange (Bovespa). The company's inclusion in these indices is recognition of Petrobras' commitment to ideals such as environmental equilibrium, social justice, economic efficiency and good corporate governance.

Petrobras made further advances in its alignment with the ten principles of the United Nations (UN) Global Compact, addressing themes such as human rights, working conditions, the environment and fighting corruption. In 2006, the company joined the Compact's Council and assumed the vice-presidency of the Brazilian arm of this initiative. This participation is an extension of the company's pioneering attitude, in voluntarily signing up to this global agreement, back in 2003, driven by its commitment to the reduction of social inequality, environmental conservation and ecological efficiency.

In December, the Executive Board gave approval to supporting the Extractive Industry Transparency Initiative (Eiti), as Petrobras has been a member of the Eiti International Advisory Group since 2005. In January 2007, the company joined the World Business Council for Sustainable Development (WBCSD), a coalition of 180 international corporations that are dedicated to sustainable development.

Petrobras' international involvement also extended into other forums. The company joined the ISO 26000 committee, as the representative of Brazil, which is leading, together with Sweden, the preparation of international rules for social responsibility, to be issued in 2008. Within Arpel (Regional Association of Oil and Natural Gas Companies in Latin America and the Caribbean), where it already presides over the de Corporate Social Responsibility Committee, the company has joined the working group for Relations with Indigenous Peoples.

Another accomplishment by Petrobras was to pick up three of the five prizes awarded at the International Pipeline Conference & Exhibition (IPCE), one of the most important global events in the area of pipeline transportation, held in Canada. Winner of the main prize, the "Agricultura Familiar em Faixa de Dutos (Family Subsistence Farming in the Pipeline Strip)" project has become a model around the world in terms of community relations.

The company was also awarded the "Selo Pró-Eqüidade de Gênero (Pro Gender Equality Seal)" 2007 by the federal government's Special Secretariat for Women's Issues (SPM), for promoting sexual equality. The Petrobras Gender Commission saw its mandate extended, becoming the Commission for Diversity.

At the international level, the company chose as the focus of its social activities the question of the Rights of Children and Adolescents. In addition to this principal line of support, the Business Units are able to define other priorities abroad, in accordance with local needs in a regional context.

Human resources

The most recent version of the Strategic Plan 2015 singles out human resources as one of the key factors in the implementation of the company's strategies. An outgrowth of the corporate strategic objectives was the consolidation, in 2006, of the HR Strategic Project, with objectives and initiatives specific to the role, which will contribute to attaining the corporate targets for 2011. The challenge is aligned with the Petrobras Vision and may be defined as "to be an international benchmark, for the energy sector, in personnel management, with the employees as our most precious asset".

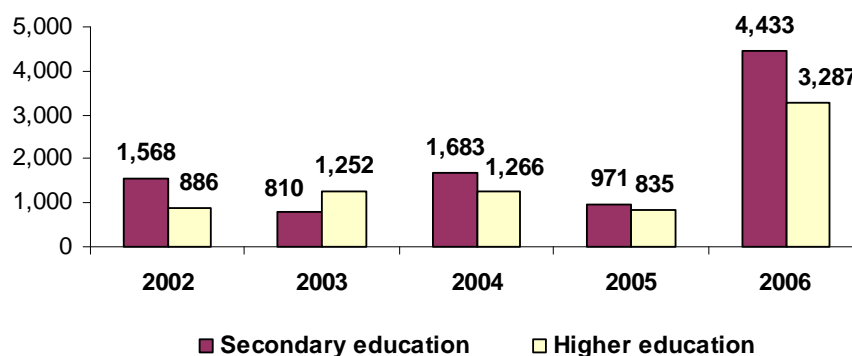
Code of Ethics

The Petrobras System's Code of Ethics has been revised, by means of a transparent and participative process that involved the clients, suppliers, executive board, board of directors and workforce of the company's various organizational units, with the aim of bringing it into alignment with the values specified in the Strategic Plan, the prevailing business context and the requirements of the Sarbanes-Oxley Law. The adopted themes were those of the Ethos Institute's Corporate Social Responsibility Indicators.

Admissions

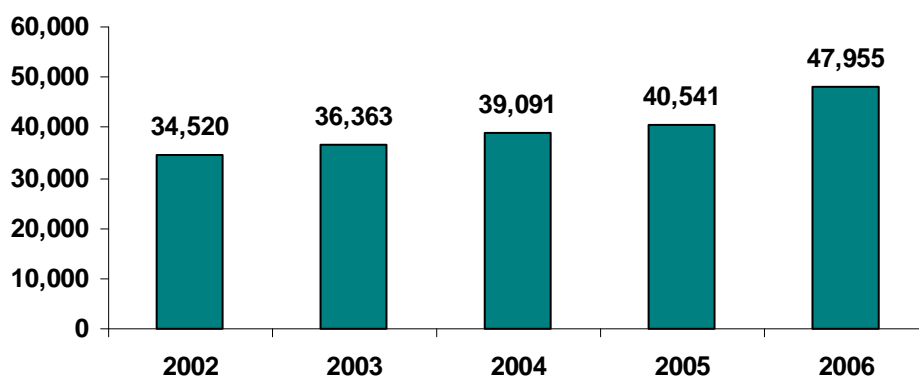
In order to keep up with and sustain the increasing expansion of the company's activities and areas of operation, public selection processes have been systematically carried out, in order to have the right permanent staff to meet the needs of the Strategic Plan. During 2006, a total of 8,006 new employees were taken on, 4,655 of them with a secondary education background and 3,351 of university level or higher.

Admissions



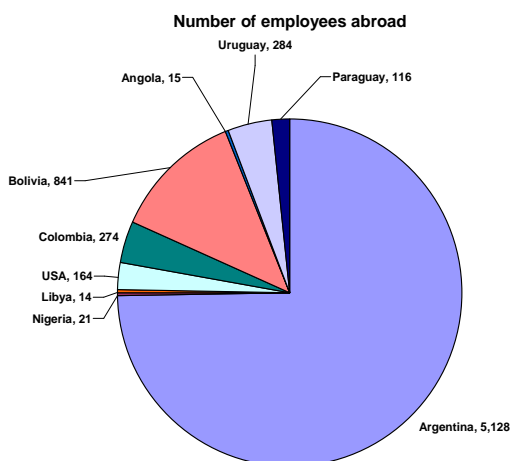
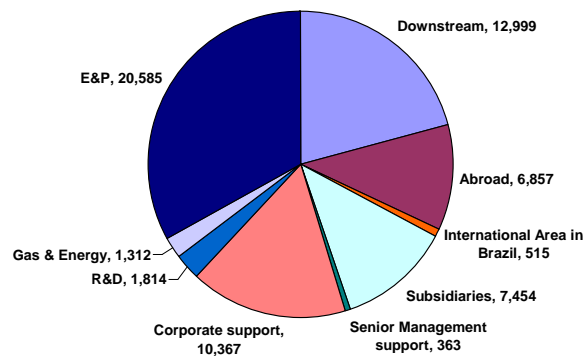
As a result, the company's permanent staff has steadily increased, from 34,520 in 2002 to 47,955 at the end of 2006.

Petrobras Parent Company – employee numbers

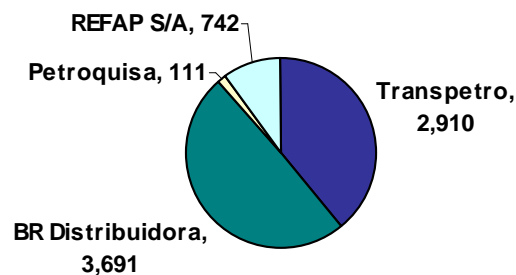


The total number of staff employed within the Petrobras System, which includes the subsidiaries in Brazil and the companies abroad, grew by 15% in 2006. Among the companies abroad, the increase was 11%.

Petrobras System – number of employees



Subsidiaries – number of employees



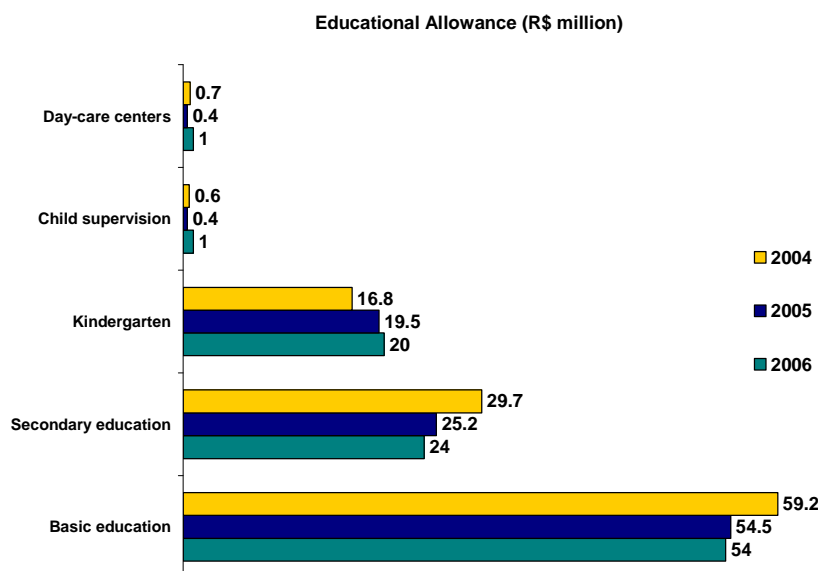
Remuneration Policy

The personnel expenses at the parent company amounted to R\$ 7,337 million, based on the fixed remuneration, which comprises salaries, extras, bonuses and the respective payroll taxes.

The variable remuneration includes profit and results sharing schemes, which are linked to the achievement of corporate results, so as to stimulate the employees' commitment to the goals of the Strategic Plan. As in previous years, the employees received their allocations in relation to the 2005 profits and results, divided in two payments, one in January and the other in July.

Educational Benefits

The educational benefits paid by the company are of a supplementary nature, in the form of an allowance to complement the beneficiary's own payments for these services, which comprise day-care centers or child supervision, kindergarten, basic education and secondary education. The corresponding cost amounted to R\$ 107 million, including taxes.



Health Care

The Multidisciplinary Health Care Scheme (AMS), covering current and retired employees and their dependents, made a total of 112 thousand attendances, through a network of 21 thousand accredited establishments throughout Brazil, including hospitals, laboratories and dental and medical offices and clinics, including specialized areas such as psychology and phonoaudiology. The net cost to the company of the medical appointments, examinations and internments was R\$ 510 million.

Under the Collective Labor Agreement, Petrobras has taken on the commitment to implement a Pharmacy Benefit, which is to be added to the generous range of benefits already provided by the company.

Pension Scheme

In 2006, Petrobras presented a proposed new Supplementary Pension Model, the fruit of the combined efforts of the company, Petros and the employee representatives. The proposal aims to stabilize the financial situation of the existing Petros Plan, resolving the structural problems and providing it with a sustainable future, as well as providing a new supplementary pension scheme to employees who do not have one.

The new supplementary pension scheme, which is close to approval by the official bodies, is of the variable or mixed contribution kind, purely for pension purposes, with defined

risk, guaranteed minimum benefit, a lifetime income option and contribution defined annually by the participant.

Collective Labor Agreement

The ongoing process of negotiations with the union bodies aims to align the employees' expectations with those of the company, thus facilitating the putting together of a Collective Labor Agreement that is satisfactory to all parties.

In 2006, this process took as its basis the Collective Agreement signed in 2005, which is valid for two years, with the exception of the economic clauses. These were the focus of the negotiations between Petrobras and the employee representatives, which led to an adjustment of 2.80%, making up for losses due to inflation, as measured by the ICV-Dieese index, plus a collective increase of one level on the salary scale and a gratuity payment equivalent to 80% of monthly remuneration.

Career Plan

As part of the process of adjusting the career plan structure to meet the challenges of the Strategic Plan 2015, the company approved the new structure for middle level employees. Technical studies are proceeding regarding the plan for upper level employees, as well as for defining job descriptions and values and the rules governing career progress.

Professional Training

The Petrobras University, devoted to the education and training of the company's technical and administrative staff, had a total of 2,469 new employees enrolled in its training program during 2006. Based on the results it has achieved, the Petrobras Training Program was chosen as one of the five finalists in the Petroleum Economist Awards 2006, in the category Best Educational Program for Young People in the Energy Industry.

During the year, the Petrobras University had 2,275 people enrolled on its project management development and specialization courses, which, added to all the other courses on offer, brought total enrollments to more than 50 thousand.

A Petrobras invested R\$ 302 million, over the course of 2006, in human resources development, and the total amount of training provided by the Petrobras University came to 3.2 million man-hours.

Corporate Culture

Alignment between the corporate values laid down in the Strategic Plan and those embedded within the culture of the organization is extremely important to the attainment of the company's objectives.

To this end, discussions were initiated to disseminate and expand upon the results of the cultural analysis carried out during the period 2004/2005. This study identified the

characteristic traits of the Petrobras corporate culture, its essential values – the oil company's "way" –, as well as tracing newly emerging values within the company environment.

Health, Safety and the Environment

The management of Health, Safety and the Environment (SMS) at Petrobras aims to consolidate SMS considerations as values that are intrinsic to the company's planning and management processes. The company's SMS policy, laid out in the Strategic Plan, contains 15 corporate guidelines, approved by the Executive Board, which have been expanded into different levels of standards, all compiled in a management handbook.

These guidelines orientate the development and implementation of corporate action plans and specific plans for the Business and Service Units, so that the SMS policy objectives will be met at all levels of the company. The visible commitment of the senior management and professional training are also among the issues addressed by the corporate guidelines. The senior management, executive managers or general managers participated in 1,143 SMS audits during 2006. This involved field trips to the operational front lines in order to observe the activities and correct any errors or omissions. The CEO or directors participated in 28 of these visits.

Petrobras' strategic agenda includes the Strategic Project for SMS Quality, which aims to ensure that, by 2015, the company has attained performance levels equivalent to those of the best companies in the world's oil and gas sector, by means of corporate action across six focus areas: Integrated SMS Management; Ecological Efficiency of Operations and Products; Prevention of Accidents, Incidents and Failures; Health of the Workers; readiness for Emergencies; and Minimizing Risks and Exposure.

Petrobras invested R\$ 3.21 billion in SMS during 2006. Of this total, R\$ 1.77 billion was directed to programs, projects and other activities in the area of safety; R\$ 1.20 billion to the environmental area, and R\$ 238 million into health. These amounts do not include spending on the Multidisciplinary Health Care Scheme nor the sponsorship of environmental programs and projects developed by third sector organizations.

Part of this spending – R\$ 850 million – was channeled through the Program for Quality in Environmental Management and Operational Safety (Pegaso), for the purpose of eliminating the risks and exposure in the company's installations and activities. This initiative – one of the most important of its kind in the industry – has absorbed investments and operating expenses amounting to R\$ 10.49 billion since 2000.

Pegaso also includes expenditure of R\$ 373 million by Transpetro, of which R\$ 90 million was allocated to the Pipeline Integrity Program and invested in the inspection, testing, appraisal, repair and restoration of oil and gas pipelines.

The implementation of SMS policy at Petrobras is overseen by the SMS Management Evaluation Program. In 2006, appraisals were conducted at 27 operational units in Brazil,

Argentina, Bolivia, Venezuela and Colombia, representing 96% of the total appraisals scheduled for the period. These appraisals are based on the company's corporate guidelines and the ISO 14001 and OHSAS 18001 standards, which have certified the health, safety and environmental management systems at 159 installations in Brazil and a further 20 abroad, representing approximately 84% of the certifiable installations in Brazil and 100% of those located abroad.

Operational Safety

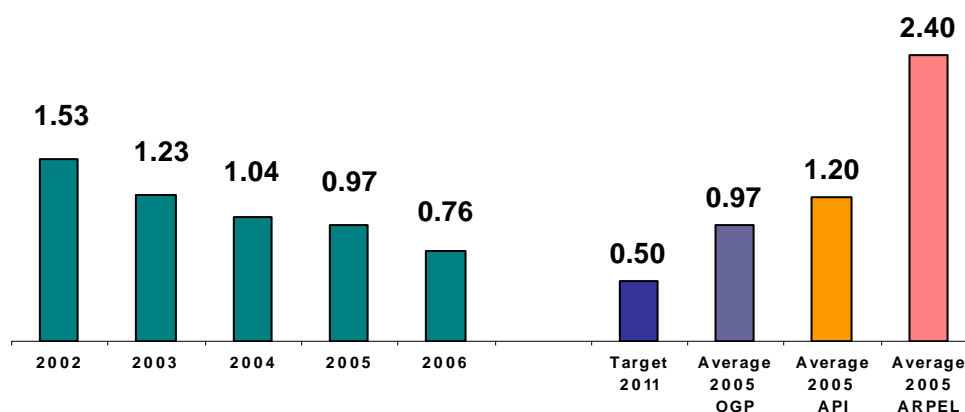
Petrobras continues to cut down the Frequency Rate of Injuries resulting in Time Off work (TFCA) and the Fatal Accident Rate (TAF), to a level comparable with that of the international oil and gas sector benchmarks. The TFCA recorded in 2006 is below the ceiling of 0.81 that had been set for the year.

The number of fatalities was down in relation to 2005. The company special attention to this detail, as the corporate target for this type of incident is zero.

This reduction in the number of injuries and fatalities occurred at the same time as the company's activities are augmenting – the total number of man-hours of exposure to risk increased from 533 million to 564 million.

Frequency Rate of Injuries resulting in Time Off work (TFCA)

Compound TFCA



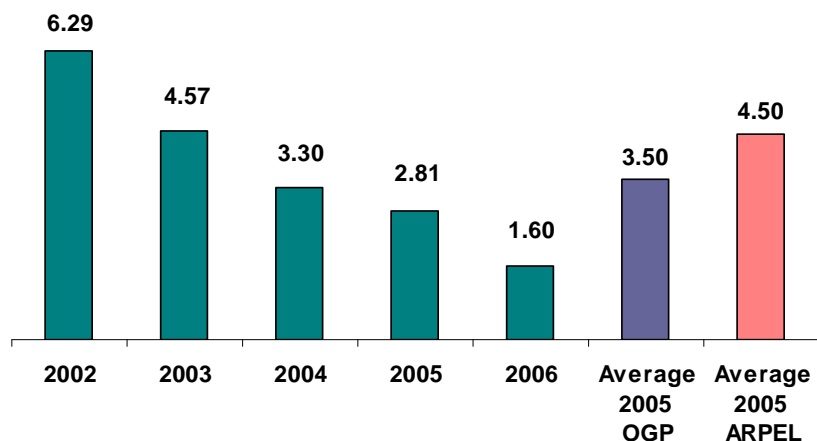
Number of injuries resulting in time off work per million man-hours of exposure to risk, covering the company's own employees and outsourced workers.

Source: OGP – Oil and Gas Producers – Safety performance indicators – 2005 data

API – American Petroleum Institute – 2005 Survey on petroleum industry occupational injuries, illnesses, and fatalities summary report

Arpel – Association of Oil and Gas Companies in Latin America and the Caribbean – Accident statistics for the oil and gas industry of Latin America and the Caribbean 2005

Fatal Accident Rate (TAF)



Number of fatalities per 100 million man-hours of exposure to risk, covering the company's own employees and outsourced workers.

Number of Fatalities



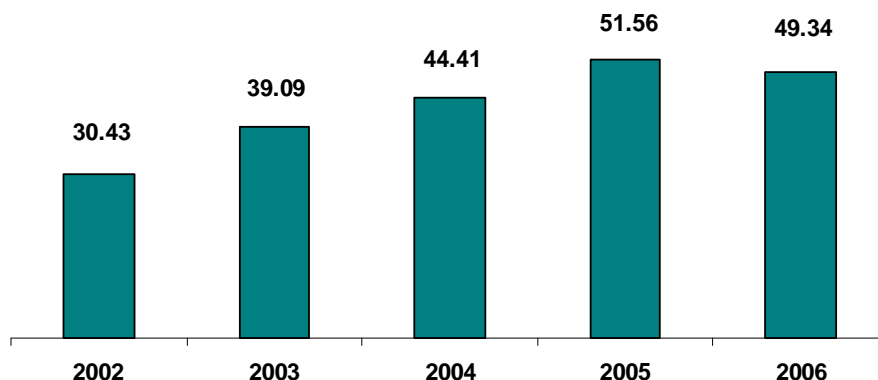
Environment

Activities in 2006 in the area of environmental responsibility were related mainly to controlling atmospheric emissions, water resources, liquid effluents and waste; the appraisal and monitoring of ecosystems; the recuperation of affected areas and ensuring that the company's installations and operations are in compliance with the legal requirements.

Emissions

Through its System for Controlling Atmospheric Emissions (Sigea), Petrobras monitors the principal greenhouse gases (carbon dioxide, methane and nitrogen monoxide) – that are emitted as a result of its activities. This monitoring is extended also to carbon monoxide, sulfur and nitrogen oxides, volatile organic compounds and particle matter.

Greenhouse Gas Emissions (million tons of CO₂ equivalent)



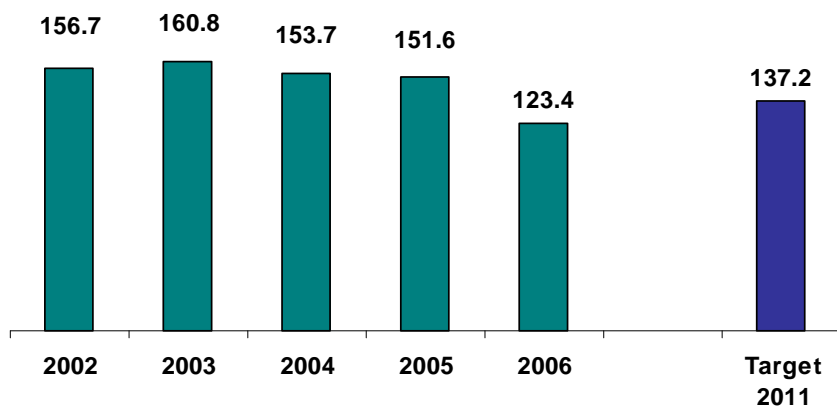
Total emissions directly or indirectly connected with Petrobras' operations in Brazil and abroad.

Preliminary data.

The emissions level recorded in 2005 was related to operational problems, a large number of production platforms coming on-stream and changes in production, the quality of the throughput and the specification of the products in the refineries.

In 2006, Petrobras introduced the indicator Prevented Emissions of Greenhouse Gases (EEGEE), in order to monitor the results of its efforts to reduce emissions of these gases in its operations. In the first half of the year, the company prevented the emission of 1.98 million tons of CO₂ equivalent, exceeding the full year target for 2006, of 1.13 million tons. The company is committed to the 2011 goal of preventing the emission of 3.93 million tons (CO₂ equivalent) of greenhouse gases. Between 2006 and 2011, the emission of a total of 18.5 million tons of CO₂ equivalent will have been prevented.

Emissions of Sulfur Oxide – Sox (tons)



Preliminary data

Energy Efficiency

The In-House Energy Conservation Program is responsible for the development, coordination and implementation of activities related to energy efficiency, promoting a proportional reduction in the flaring off of fossil fuels and, consequently, of the emission of CO₂, one of the principal greenhouse gases.

In order to meet the established targets for the reduction of energy consumption and emissions, in addition to the projects mentioned, energy analyses have been carried out at the company's industrial units, and this will be extended to the business units that will operate future production platforms, so that the basic designs can be also developed with a view to energy efficiency.

The program's activities brought about a saving of approximately 2,500 barrels of oil equivalent a day in 2005. The gain is not just economic, but also environmental, since the company reduced its CO₂ emissions, through a proportional decline in electricity consumption and the flaring off of fossil fuels.

Water Resources and Effluents

In 2006, Petrobras approved the corporate standard for the management of water resources and effluents, embracing the reutilization and optimal use of water in its operations and the protection of bodies of water within its areas of influence.

The drawing up of detailed statements of water resources for the refineries and fertilizer plants is one of the activities aligned with the requirements of the standard. The studies, which include assessing the tolerance capacity of the water bodies that receive effluents from these units, should be completed in 2007.

In the area of Exploration & Production, one project is aiming to make the Campos Basin platforms self-sufficient in fresh water, which will reduce the volume of water taken from the River Macaé by 1.1 thousand m³/day. Another initiative, concluded in 2006, promotes the reinjection of the water from oil production at the Fazenda Belém field, thus reducing by 2 thousand m³/day the amount of water removed from the Açu aquifer, the principal water reservoir serving that semi-arid region.

Solid Waste

The company produced 315 thousand tons of hazardous solid waste, in Brazil and abroad, in 2006. During this period, 268 thousand tons of hazardous waste were treated or disposed of in an environmentally appropriate manner.

Biological Diversity

In 2006, Petrobras approved the corporate standard for the control of the potential impact of the company's activities on biological diversity, based on the strategic commitment to

apply the principles of environmental responsibility in all stages of its projects, including planning, construction, operation and decommissioning.

The standard envisages the definition of the protected or environmentally sensitive areas that are influenced by the company's operations, with a view to protecting, mitigating the impact on biological diversity and recuperation of these areas. To this end, backed by an investment of around R\$ 9 million, a study has been under way since March 2005 to make an assessment of the various ecosystems of the Guanabara Bay area, in Rio de Janeiro. Approximately 75% of the work of characterizing the fauna behind the bay, included in the study, has already been completed. In the Amazon region, studies carried out along with universities and research institutes assess the potential impact of Petrobras' operations on the surrounding ecosystems.

Emergency Readiness

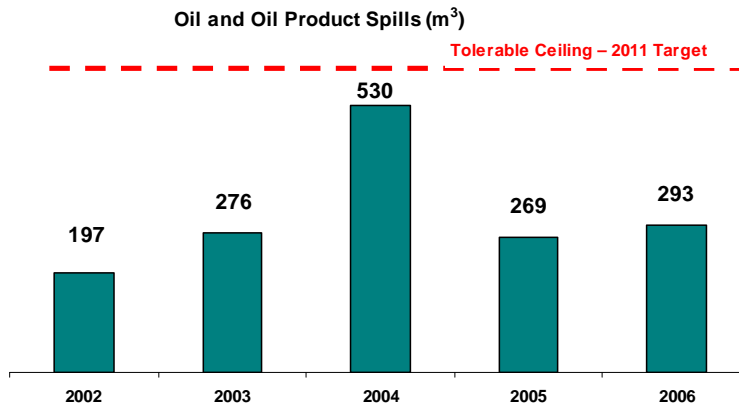
Petrobras' strategy for dealing with emergencies is based upon the integration of the contingency resources of its business units with vessels dedicated for this purpose, operating along the Brazilian coastline, and the company's Environmental Protection Centers (CDAs). The CDAs operate around the clock, staffed by trained professional and equipped to react quickly and effectively to any situation. Their resources include special vessels, oil collectors and contention and absorption barriers.

There are nine CDAs located in Brazil, comprising six outposts in the north, one in Natal, one at the Mocanguê naval base, in Rio de Janeiro, and one in Uberaba. This network of protection against the potential repercussions of accidents, which can also count on the resources of public agencies and local communities, has emergency contingency plans covering the whole country and is regularly tested by means of simulated exercises. During 2006, seven regional exercises were conducted, with the participation of the Brazilian navy, the Civil Defense Corps, the fire brigade, the police, environmental bodies, local governments and communities. Two exercises were also conducted at units in Argentina.

The company has three vessels for dealing with emergencies that operate around the clock in the Guanabara Bay, off the coast of the state of São Paulo and off the coast of the states of Sergipe and Alagoas.

Spills

The volume of oil and oil product spills in 2006 remained at the same level as in 2005, an excellent result by the standards of the world oil and gas industry. The volume was below the ceiling of 475 m³ that had been set for the year. The 2011 ceiling for oil and oil product spills has been set at 601 m³, taking into account the forecast increase in production and the addition to this indicator of potential new sources of leakages, such as the tank trucks working for Petrobras Distribuidora.

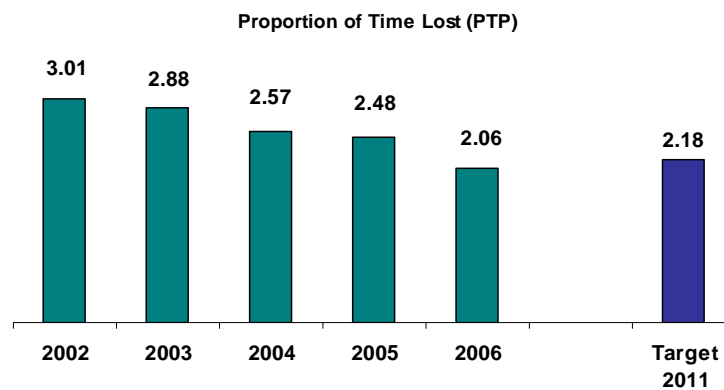


Spills exceeding 1 barrel (0.159 m³) that have affected the environment beyond the installation perimeter.

Health

The promotion by Petrobras of good health and the prevention of illness among the workers is based on the concept of integral health – inside and outside the workplace. The company's programs and other endeavors in this area are guided by the epidemiological analysis of information on, for example, mortality, morbidity and the prevalence of risk factors.

This systematic approach has yielded positive results in terms of the health of the workers. In 2006, the indicator Proportion of Time Lost (PTP), based on the employees' time off work due to illness or accidents, continued the downward trend of recent years. The figure was below the ceiling that had been established for the year, of 2.34%. The ceiling for 2011 has been set at 2.18%.



Percentage of the total potential working hours lost due to medically authorized time off (for illness, occupational or otherwise, or accidents in the workplace); counting only the company's own employees.

Non-occupational illness, unrelated to work activities, predominated among the reasons for employees' time off work in 2006, as in previous years. This explains the emphasis given by the company to the Program for the Promotion of Health, which encourages employees to adopt healthy lifestyles. Petrobras also motivates and monitors the participation of all its employees in the annual medical check-ups and encourages them to follow the recommendations of the doctors.

Reasons For Time Off Work

Through its Occupational Hygiene and Ergonomics Program, the company is able to identify, control and eliminate occupational hazards at all its units. The procedures to ensure the health of employees on trips, which include check-ups prior to traveling and medical observation following their return, are also being standardized.

In order to provide a better standard of health for its workers and their families, Petrobras has trained 500 health professionals, through the São Caetano do Sul Center for the Study of Physical Aptitude, to promote physical activities among its employees, following Health Ministry guidelines.

The company also has a corporate policy for addressing HIV/aids. In trying to further the well-being of all its workers, without distinction as to background, race, gender, creed or sexual choice, Petrobras collaborates in an affirmative manner to promote an appropriate attitude to this illness. Moreover, both in Brazil and abroad, the company maintains relations with government and non-government organizations devoted to monitoring, assistance and research with regard to HIV/aids.

Sponsorship

Social Projects

The Petrobras Zero Hunger Program, which completed its third year, has invested a total of R\$ 385 million in projects devoted to generating employment and income, to education and professional training, and to protecting the rights of children and adolescents. In the 2006 public selection process, 76 projects were chosen for sponsorship, from a total of 4,517 registered. These initiatives, synchronized with public policies for the eradication of poverty and hunger, also seek to promote racial and sexual equality and concern for the handicapped. During 2006, R\$ 175.8 million was invested in the program.

One of the program's projects is "Molhar a Terra (Irrigate the Soil)", under which inactive oil wells are used to supply drinking water to communities in the country's semi-arid region. Another activity is "Mova Brasil (Mobilize Brazil)", which, in a joint educational and work-related effort, in partnership with the Paulo Freire Institute, the Oilworkers' Federation (FUP) and the federal government, has taught 46 thousand young people and adults how to read and write. In stimulating cooperativism, in addition to the Family Subsistence Farming in the Pipeline Strip project, mentioned earlier, the company helps some 10 thousand autonomous collectors of recyclable materials in different parts of the country to organize themselves, in an initiative that combines the goals of social inclusion and environmental protection.

Through the Petrobras Zero Hunger Program, which, since 2003, has drawn corporate efforts together in the fight against hunger and misery, Petrobras has accumulated a wealth of institutional relationships covering more than 15 thousand governmental and non-governmental partnerships. More than 10 million people have been assisted by these sponsored projects, which are contributing to the building of social justice in Brazil.

Another activity in the social area is passing on resources to the Fund for Childhood and Adolescence (FIA). In 2006, a total of R\$ 48.6 million was provided to projects in more than 200 municipalities in almost every state. These actions, in partnership with the Special Secretariat for Human Rights and the National Council for the Rights of Children and Adolescents (Conanda), seek to prevent the sexual exploitation of children and teenagers and put a stop to child labor and the unlawful employment of teenagers. The sponsorships also include initiatives to reduce school drop out rates and for the social inclusion of people with special needs.

Environmental Projects

Em 2006 a Petrobras investiu R\$ 44,6 milhões em projetos ambientais.

In its second public selection process, the Petrobras Environmental program received 856 applications and chose to sponsor 36 new projects, **que receberão investimentos de R\$ 48 milhões nos próximos 2 anos.** The program retained the theme of “Water: bodies of fresh and salt water and their biological diversity”, to preserve the focus defined in the first selection process, in 2004, when the sum of R\$ 40 million was invested. The theme was chosen because Brazil, which accounts for 12% of the volume of water in all the planet’s rivers, has a considerable proportion of the world’s available fresh water.

Because it gives importance to sharing responsibility for the protection of water resources, the company also supports initiatives that develop awareness and promote the rational use of water, the preservation and restoration of the vegetation bordering streams and rivers and the protection of marine environments. The projects, which embrace a variety of ecosystems, river basins and landscapes, are developed in all the country’s biomes, notably the Amazon Rainforest, the Caatinga, the Cerrado, the Atlantic Forest and the Pantanal.

The activities of the Petrobras Environmental program, launched in 2003, cover more than 5 thousand species of Brazilian fauna and flora. Sponsorship has enabled the setting up of 15 databases and 12 Geographical Information Systems (SIG), as well as the publication of 70 specialized works, with 220 thousand copies distributed. The initiatives reach out to 250 municipalities, having an area of influence of over 900 thousand hectares, and benefit 20 million Brazilians – 3 million of them directly. The work involved in the projects provides an income for more than 5 thousand people.

Other programs are also developed by Petrobras, which has been investing in the environmental sphere for decades, with the disbursement of R\$ 103 million in environmental

sponsorship just since 2004. To help marine biological diversity, the company sponsors projects and behavioral studies, as well as the protection of endangered species, such as the manatee, the humpback and right whales, the spinner dolphin and the marine turtle (the Tamar Project has been active on Brazil's coast for over 20 years). Under the "De Olho no Ambiente (Keep an Eye on the Environment)" program, 335 communities neighboring the operational units are encouraged to plan the area's sustainable development, introducing at the local level the global commitments of the UN's Agenda 21.

Cultural Projects

Petrobras continues to be the country's greatest cultural sponsor, making an annual investment of R\$ 288 million and with a portfolio of more than one thousand ongoing projects. The company's policies and guidelines for this area emphasize the Brazilian culture and seek more opportunities for the creation, distribution and fruition of projects, in addition to the preservation of a permanent Brazilian cultural legacy.

Sponsorship is structured under the Petrobras Cultural program, which earmarks 75% of its resources for projects by public selection and 25% for those chosen directly. In 2006, of the 4,700 projects registered in the public selection process, just 230, in the fields of the cinema, the scenic and visual arts, cultural heritage, artistic legacy and music, received a total of R\$ 46 million in sponsorship. The support to another hundred projects, chosen directly, amounted to R\$ 15 million.

The fourth edition of the Petrobras Cultural (2006-2007) was launched in December, with R\$ 80 million in funding, and a new feature, sponsorship directed at education in the arts. The public selection process covered action for cultural preservation, cinema production and dissemination, the sustaining of theater and dance groups, and the recording and distribution of popular and classical music. The projects chosen directly include the cinema, scenic arts, visual arts, music and the maintenance of archeological sites, such as those at Xingó (SE) and Serra da Capivara (PI).

The company stimulates the registration of projects from all over the country through the Petrobras Cultural Caravan, which visits the state capitals between September and January. In 2005, a project workshop was added to the caravan, to help the producers of cultural activities in the development of their proposals. In this way, Petrobras has managed to extend the reach of its sponsorship to all parts of the country.

Sports Sponsorship

Petrobras is one of Brazilian sport's greatest partners and a sponsor of the XV Pan-American Games, to be held in Rio in 2007. A total of R\$ 58,197 million went into supporting sporting activities in 2006. The company bolstered its partnership with the Brazilian Olympic Committee (COB), strengthening the association of the Petrobras name with the ideals of the

Olympic movement and with sports promotion, recognizing the important role sport plays in the development of young people. The Pan-American Games, attracting athletes from 42 different countries, is the greatest sporting event in the Americas.

In motor racing, Petrobras continues to support the Williams Formula 1 team, the Petrobras Lubrax team in rallying, the Action Power team in stock car racing, Team Scud Petrobras in motorcycle racing, the Petrobras “Seletiva de Kart”, “Formula Truck” and the SAE competitions “Baja” and “Fórmula”. The development of products for motor racing is part of the company’s strategy to use the race tracks as laboratories.

With its sponsorship of the 3rd edition of the Petrobras Tennis Cup, held in Brazil, Argentina, Colombia, Uruguay and Chile, Petrobras reinforced the dissemination of its brand name in Latin America. The company also maintained its support for the Brazilian Handball Confederation (CBH) and the Brazilian national team – this sport is the one most widely played in the country’s state schools. Support for surfing, associated with the characteristics of youth and energy, has also been continued. In soccer, sponsorship of the Rio club Flamengo kept the Petrobras name in the spotlight.

Intangible Assets

The management of a company’s intangible assets is essential to the creation of value and development of a competitive edge, contributing decisively to the attainment of sustainable results. At Petrobras, these assets are divided into four types of capital: human, organizational, relationship and technological. The company is studying the definition of quantitative and qualitative valuation criteria for measuring the contribution of each intangible asset in the development of the business.

Petrobras took a pioneering step in the management of technological know-how, when, in 1963, it set up the Leopoldo Américo Miguez de Mello Research Center (Cenpes). And management of this asset is the basis of the company’s acknowledged technological excellence, which is reflected in its market capitalization and makes the company a sought after partner for the world’s major oil companies.

The sustaining of technological quality is upheld by investment in developing the employees’ technical and management skills. This constant process of up-grading is conducted through the Petrobras University, as is the acceleration of the learning curve of new workers.

The management of organizational and relationship capital has gained ground in recent years. At the same time as it progresses in the control of systems and key processes, the company refines the management of its relations with customers, suppliers, partners, shareholders and the general public. The outside perception of the strength of the management

of intangible assets opens up the possibility of partnerships, influences the decision making of investors and boosts the results of Petrobras.

Technological Capital

The mastery of technological know-how is a constant challenge for Petrobras, which has been expanding the installations of Cenpes, on the Ilha do Fundão campus of the Federal University of Rio de Janeiro (UFRJ). With over 1,800 employees, 30 pilot plants and 137 laboratories, in an area of 122 thousand m², the Center has been anticipating and supplying the company's technological needs since 1963. It plays a decisive role in the corporate strategy of growth allied with social and environmental responsibility.

Research into biological fuels was the highlight of 2006. A mixture of vegetable oils and mineral diesel oil, the H-Bio technology was tested on a pilot scale at the Gabriel Passos (Regap), Alberto Pasqualini (Refap) and Presidente Getúlio Vargas (Repar) refineries, with a view to starting commercial production in 2007. Biodiesel, made with vegetable oils or oleaginous seeds, it is being produced at two experimental plants in the state of Rio Grande do Norte, using innovative technology. Another new development was the laboratory production of alcohol fuel (ethanol) from sugar cane bagasse, which would enable an increase in the production of alcohol without having to increase the planted area.

The technologies developed by Cenpes have also led to improvements in the quality of the fuels. At the end of the year, Petrobras launched Diesel Podium, a cleaner diesel fuel containing only 200 parts per million (ppm) of sulfur, thus taking another step forward in the innovations relating to this product, which began in 2005, with the commercialization of diesel with 500 ppm.

Another advance in the refining area was the development, by Cenpes, of technology to optimize the use of the heavy oil from the Campos Basin. One of these developments, which increases the production of ethylene and propylene, will be utilized at the Rio de Janeiro Petrochemical Complex; another, already tested on an industrial scale, will be utilized at the Northeastern Refinery, increasing the production of diesel fuel from heavy oil by 30%. The conceptual designs for both the Rio de Janeiro Petrochemical Complex and the Northeastern Refinery were completed by Cenpes.

Important technological advances helped to augment the company's proven reserves of oil and gas. In the Marlim field, in the Campos Basin, the use of chemical tracers in the process of defining the reserves – the first time this has been done in deep waters – added 500 million barrels of oil to the field's reserves. Cenpes also developed, together with suppliers, new equipment and new technology for separating the oil, gas and water at the maritime units.

Three basic platform designs were completed by Cenpes in 2006: Mexilhão 1 (PMXL1), to be installed in the Santos Basin; and, for the Campos Basin, the P-55 (Roncador field) and

the P-57 (Jubarte field). Another challenge that was overcome during the year relates to the technology for drilling wells, in about 2 thousand meters of water in the Santos Basin, through thick layers of salt. The technique made it possible to identify accumulations of light oil at a depth of over 6,400 meters.

In the area of environmental protection, Cenpes has completed the prototype of a hybrid robot, given the name Chico Mendes, designed for environmental monitoring in the Amazon region. A collaborator in the efforts to preserve the world's largest tropical forest, Petrobras, in liaison with other scientific and technological organizations, proposes to create a Petrobras Center of Environmental Quality in the Amazon. Cenpes was also an active participant in an international seminar on carbon sequestration and climate change, which brought together specialists from 17 different countries in Rio de Janeiro.

Significant advances in the development of new technology for the reutilization of effluents and the reduction of water consumption to a minimum have made it possible to meet the necessary environmental requirements for the new refining projects, with a saving, in terms of water catchment and the release of effluents equivalent to a city of 300 thousand inhabitants.

With a view to Cenpes and the operational units working more closely with one another, Petrobras inaugurated the Experimental Center for Renewable Energy, in the state of Rio Grande do Norte. Two more centers should start up in 2007, one in Ceará and the other in Minas Gerais. As part of the company's strategy for relations with the Brazilian scientific community, Cenpes launched a new partnership concept, in 2006. The new model involves the participation of 76 institutions from 18 units of the Brazilian federation, organized into 38 thematic networks and 7 regional centers. By 2008, Petrobras should have invested about R\$ 1 billion in this new model.

Patents

Petrobras is the company that files the most patents in Brazil and is also the Brazilian company with the most patents filed in the USA. In 2006, a total of 14 patents were granted to the company in Brazil. Seventy-seven new patent applications were filed during the course of the year – among them, the company's thousandth, for the process of producing ethanol from vegetable refuse, developed at Cenpes. Outside Brazil, in 2006, a total of 81 applications were filed and 69 patents were obtained.

With all these technological innovations, Petrobras is constantly refining its processes, so as to be able to guarantee to meet society's demands in a sustainable manner.

Organizational Capital

Brands

The Petrobras brand is managed as a strategic asset, due to its importance and its potential to add value to products and services. The Marketing and Brand Committee, linked to the Business Committee, is responsible for devising a management model with guidelines for the utilization of the brand throughout the Petrobras System.

The defining of the rules, allied to the legal defense of this asset in the various markets, provides even more protection for the Petrobras brand. The global management of this asset follows a strategy of giving the company a higher profile and strengthening the identity of its products and services. This management is aligned, in the corporate sphere, with the uniform appearance of the installations and the standardization of the company's communication activities.

A survey by the international consulting firm Interbrand demonstrated the success of the company's brand management, which is associated with technological and quality leadership and social and environmental responsibility. In 2003, the firm calculated the value of the Petrobras brand at US\$ 286 million, which surged to US\$ 485 million the following year and hit US\$ 554 million in 2005, an increase of 94% in just two years. The Petrobras brand was the one whose value increased the most in Brazil between 2003 and 2005.

Management Practices

In 2006, the Management Quality Assessment Program continued to encourage the adoption of program for improvements at the operational units. The assessments are guided by the Petrobras Management for Quality Handbook, which combines the criteria of the National Quality Award with the specific requirements of the company, derived from the policies of the Strategic Plan.

Petrobras entered into a formal agreement with the National Quality Foundation for the dissemination of the corporate model of management quality. Among the resources developed under this partnership are 'quality' notebooks and a program that simplifies the process of self-assessment by the units, stimulating improvements to be made more quickly. Petrobras participates, both in Brazil and abroad, in various movements and bodies devoted to management quality, productivity and competitiveness.

Human Capital

Knowledge management

In 2006, Petrobras consolidated the methodology for preparing knowledge management programs for the business units in Brazil, based on the International Area's Program for the Integration of Knowledge. This program strengthens operational, management and

technological expertise, disseminating knowledge and accelerating the development of new employees.

In the Exploration & Production area, the Communities of Practice Program is disseminating knowledge and best practices in four more fields of activity. Specialists in the 'communities' of reservoir definition, well engineering, naval engineering, lifting and off-loading, water management and operational practices are all now sharing their experience. Overcoming organizational boundaries, the program embraces 2.5 thousand employees at units in Brazil and abroad.

The participation of the employees in passing on technical, cultural and business know-how is showcased in the project "Petrobras Stories", which collects personal narratives and case studies. The project systematically organizes information relating to historical milestones, thereby spreading strategic know-how, as well as an understanding of the company's past. The first themes to be tackled are the backgrounds of the oil producing area of Urucu, in the Amazon, and the Guando field, in Colombia.

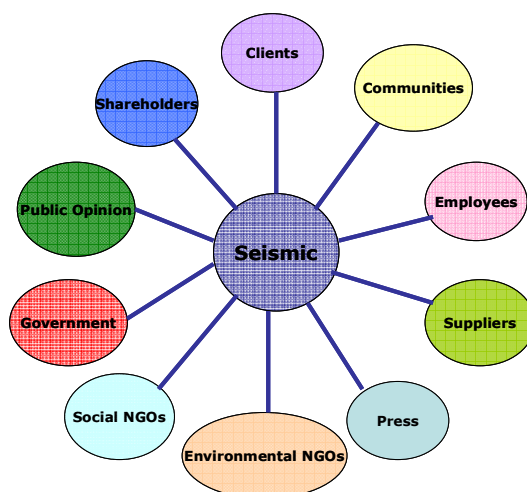
As part of the ongoing improvement of the company's relationship with general society, it has set up the Communication area's Collaboration Network (ReCol). This initiative highlights good practices developed at the units, reinforcing the understanding and implications of the corporate communication guidelines.

Petrobras participates in two Knowledge Management study groups coordinated by the American Productivity & Quality Center (APQC), with a view to refining its own internal practices in the light of the example of world-class corporations. In the 2006 edition of the Most Admired Knowledge Enterprise (Make), an award presented by the British institution Know Network for outstanding achievement in the area of business knowledge, Petrobras came fourth, among the world's 18 largest companies in the oil sector. It was the only Latin American company among the 55 finalists.

Relationship Capital

Petrobras has been conducting ever more wide ranging opinion surveys, in order to know how its practices and projects are viewed and assessed by the stakeholders. These surveys, which have provided the company with considerable insight into the socio-economic environment in which it operates, are based upon 18 indicators that make it possible to evaluate the perceptions regarding its management, competitiveness, growth, activities abroad, vision of the future, social support, ethics, and social and environmental responsibility.

The weighted average of the points awarded for each indicator in the public opinion segment provides a general indicator value. The information from the surveys is consolidated in the Corporate Image Monitoring System (Sísmico). Using this company reputation monitoring tool, the management can follow changes in Petrobras' image and appropriately adjust its communication policies and actions, as well as its management practices different areas.

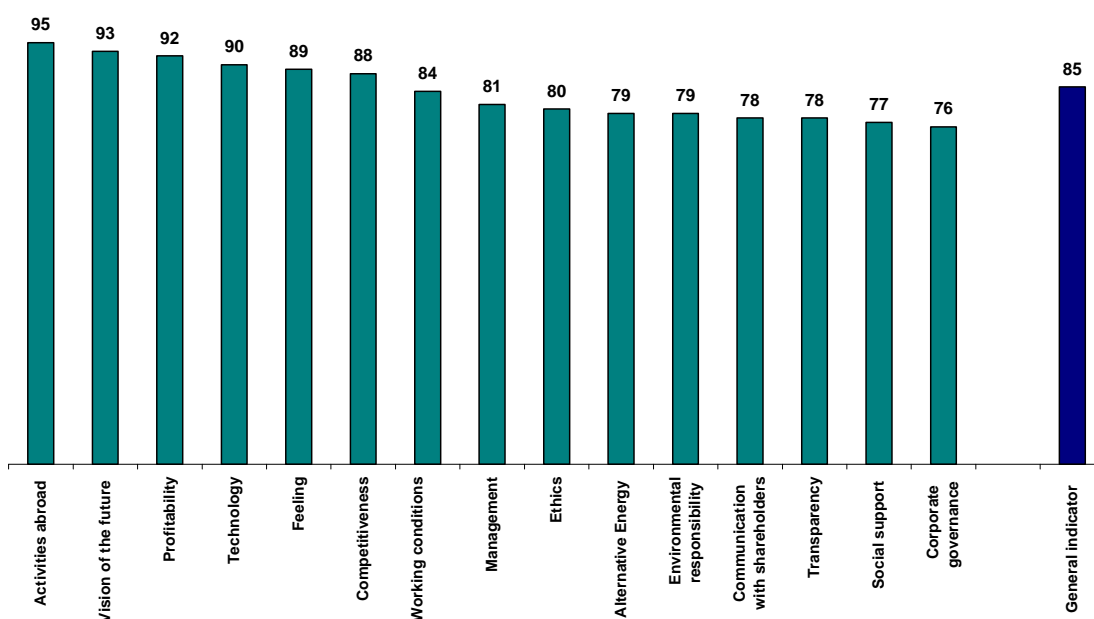


Investor Relations

At the end of 2006, the company had more than 350 thousand shareholders and investors in funds devoted to Petrobras shares. In order to refine its relationship with these parties, the company has an ongoing program directed at the investors, through road shows, open meetings, conference calls, chats, a shareholders' newsletter, telephone and e-mail response, specialized events, website, and numerous other means of communication.

What is more, the company conducts an annual survey which assesses the quality of the service and the perception of Petrobras in terms of profitability, competitiveness, management, vision of the future, corporate governance, ethics, technology, transparency, and social and environmental responsibility.

Survey of Shareholder Approval Ratings



Relationship with Suppliers

In 2006, Petrobras retained the system of listing the companies that provide outsourced materials and services all together in a single register of suppliers, in alignment with the corporate Health, Safety and the Environment (SMS) and Social Responsibility guidelines. In a process of standardizing its methodology and rationalizing its efforts, the company refined the technical, legal-fiscal and economic-financial criteria for registration, in addition to adopting new centralized and regional procedures for evaluation and ratification.

The new registration form also contains questions relating to social responsibility, prepared by the Ethos Institute for Companies and Social Responsibility. The purpose of this inquiry is to form a picture of the practices developed in this area by the suppliers and stimulate them to give due importance to such initiatives and to show appreciation of existing efforts, as well as to make improvements in them.

The Registration Portal was set up by the company to use the internet as a tool for developing closer relations with suppliers. Petrobras currently has around 5 thousand companies registered in its database for the acquisition of goods and services for its operations or new projects. Moreover, there are approximately 40 thousand firms, located throughout the country, that supply goods and services on a small scale to the company's operating units.

For the acquisition of goods, the new Terms of Materials Supply (CFM) apply to all contracts signed since November 1, 2005. The product of liaison between Petrobras and associations representing suppliers, the CFM adapted the contractual clauses to the prevailing legislation and market practices. The company has also adopted new terms of payment for goods that have a long manufacturing timeframe supplied by Brazilian companies.

Petrobras continued its partnership with the Brazilian Service for the Support of Small and Medium-Sized Enterprises (Sebrae), to encourage the competitive insertion of small businesses in the production chain for oil, natural gas and electricity. The agreement covers the 12 states that have Petrobras business units and is worth R\$ 12 million over a period of three years – R\$ 6 million of which is invested by Sebrae. Due to the enthusiastic response to this initiative, the investments of the participating companies, initially put at R\$ 3 million, have risen to R\$ 16.7 million.

Procurement

Petrobras made direct purchases of goods and services to the sum of US\$ 20.8 billion in 2006, of which US\$ 4 billion was for the acquisition of materials and US\$ 16.8 billion for the hiring of services. Of these totals, 88% of the materials purchases and 70% of the services were acquired from suppliers located in Brazil, who thus had a 73% overall share of the purchases made in 2006.

Part of the procurement was carried out through the on-line trading portal Petronect, which has a total of 22,719 registered suppliers in Brazil, Argentina, Bolivia, Colombia, Ecuador, Peru, Singapore, the USA and Venezuela. Since October 2003, the companies of the Petrobras System have completed 216 thousand purchases, 125 direct auctions and 274 reverse auctions using the Petronect portal.

BUSINESS MANAGEMENT

Business Performance

Oil prices in the international market hit extremely high levels during 2006. The Brent average (US\$ 65.14/barrel) was up 19.8% in relation to the previous year, having hit a peak monthly average of US\$ 73.66/barrel in July. This rise had a direct impact on the lifting cost of domestic oil and the cost of imported oil, which represented, on average, 20.5% of the fresh throughput at the refineries.

The pricing policy adopted in 2005 was maintained, so as to avoid immediately passing on to the consumer the volatility of the international prices. The average realization price of oil products in the domestic market was R\$ 154.45/barrel – 8% higher than in the previous year.

The main underlying reasons were the increase in gasoline and diesel prices, in September 2005; the commercialization of Diesel S500 – of superior quality – from the beginning of 2005; and the adjustment of the prices for other oil products, notably naphtha, fuel oil and aviation fuel, in line with the fluctuations in international prices.

Petrobras' total sales – including natural gas, alcohols, nitrogen compounds, exports and international sales – amounted to 3 million 48 thousand boe, a 9% increase over the 2 million 808 thousand boe sold in 2005.

The company's sales in the domestic market were up by 3%. Sales of natural gas increased by 7%, driven by the growth of the market in the south/southeast, while sales of oil products rose by 3%. Electricity sales grew 8.7%, due to contracts signed in previous years coming into effect, coupled with increased sales under contracts already in effect.

Higher Revenues

The consolidated gross operating revenue amounted to R\$ 205.4 billion, while the net operating revenue was R\$ 158.2 billion – amounts that exceeded the 2005 figures by 15% and 16%, respectively. Underlying the result were the higher prices in the domestic and international markets and the increases of 3% in domestic sales and 19% in international sales.

In the domestic market, net revenue was up by R\$ 10.9 billion (12.3%), due mainly to higher revenue from diesel fuel (11.6%), gasoline (18.8%) and naphtha (12.2%). Gasoline sales increased by 7.3% (21 thousand barrels/day) – stimulated, above all, by the reduction, in March,

of the anhydrous alcohol –, outstripping the increase in sales of diesel fuel, up 1.1% (7 thousand barrels/day), and of naphtha, up 5.1% (8 thousand barrels/day). The impact of the price rises was greatest for diesel fuel, which saw an increase of 11% (R\$ 0.11/liter), while gasoline and naphtha saw respective increases of 9.1% (R\$ 0.08/liter) and 6.5% (R\$ 0.08/liter).

The net revenue in foreign markets was up by R\$ 3 billion, led by oil exports, which increased by 29% in relation to 2005, while the revenue from oil products declined by 2.3%.

Economic and Financial Results

The operating profit amounted to R\$ 42.2 billion – 6% higher than that obtained in the previous year. This was basically due to the increases in net operating revenue and production and the processing of more domestic oil, which pushed the cost of goods and services sold by 23%, whereas the increase in the benchmark price of Brent oil was 19.8%. Net earnings were R\$ 25.9 billion, 9% higher than the figure for 2005.

As a result, EBITDA (earnings before deducting interest, taxes, amortization and depreciation) was R\$ 50.9 billion, 9% higher than that of 2005. The return on capital employed (Roce) was 23% – down one percent in comparison with the previous year.

The financial result for 2006 was a net expense of R\$ 1.3 billion, compared to a net expense of R\$ 2.8 billion in 2005. The result was affected by the much greater appreciation of the real against the principal currencies with which Petrobras works than was seen in 2005.

Petrobras' total assets amounted to R\$ 210.5 billion, an increase of 15% over the figure for 2005. The value of the company's fixed assets increased by 14.4%, while current assets were up by 11.6% and long term assets by 16%. Cash and short term financial investments alone accounted for 63% of the variation in current assets.

The corresponding change in liabilities was accounted for mainly by net equity, which increased by 23.8%, the principal item being a 45% increase in realized capital. With regard to the company's debt, the leverage (net debt to net capitalization ratio) was reduced to 16%, from 24% in 2005.

Capital Expenditure

Petrobras made investments amounting to R\$ 33.7 billion – 31% more than in 2005 –, in line with the Strategic Plan 2015. Capital expenditure in the area of Exploration & Production came to R\$ 15.3 billion, with priority being given to augmenting production and reserves. In the Downstream area, a total of R\$ 4.2 billion was invested, with the aim of adding value to the company's oil and natural gas. The capital expenditure in the International area, of R\$ 7.2 billion, was invested in pursuing the strategy of leadership, as an integrated business, of the Latin American energy market.

Of the total figure, R\$ 3.5 billion was invested through specific purpose companies (SPCs), which was up 47% in comparison with the amount invested through SPCs in 2005.

Capital Markets

Share Performance

It was a good year for Petrobras on the stock markets. The nominal appreciation of the company's shares – of 31.94% for the common stock (PETR3) and 33.83% for the preferred stock (PETR4) – was in line with the overall performance of the Ibovespa (the São Paulo Stock Exchange index), which rose by 33% in 2006. However, taking into account the dividends paid out over the course of the year (in relation to the 2005 fiscal year), the appreciation of Petrobras' shares amounted to 38% (common) and 41% (preferred).

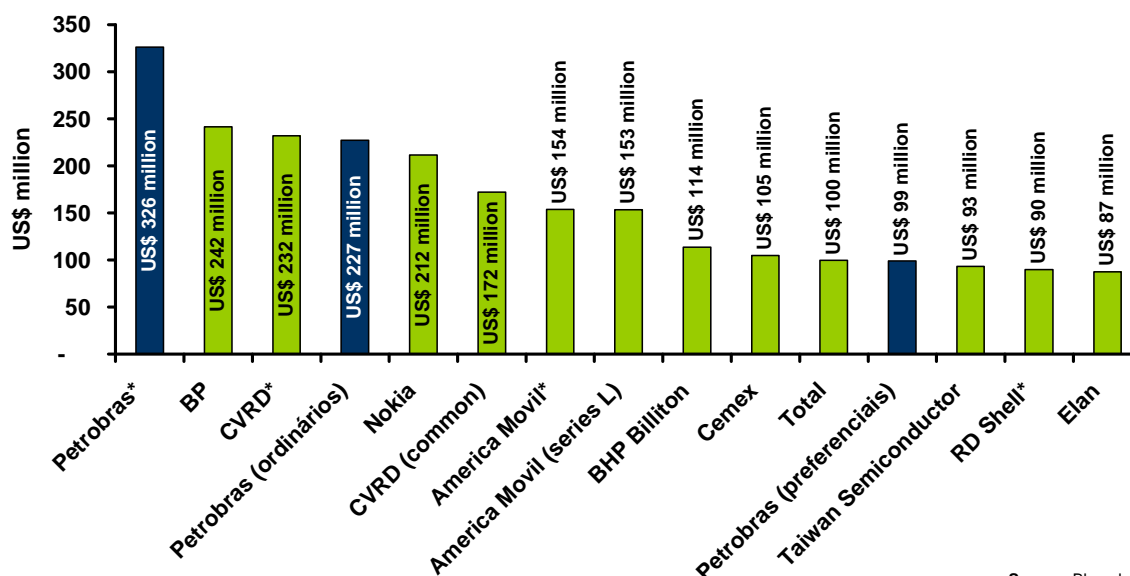
The company's preferred stock showed the greatest liquidity, in terms of volume traded and number of trades, with a respective daily average of R\$ 282 million and 4,414. This performance placed Petrobras at the top of the ranking, as the company with the biggest weighting in the Ibovespa theoretical portfolio – with 13.80% for the period January - April 2007. Taking the combined figures for common and preferred stock, the company had a daily turnover of R\$ 336 million, representing over 16% of the average Bovespa trading volume in 2006.

At the New York Stock Exchange (NYSE), the return to Petrobras shareholders was even greater, due to the appreciation of the real against the dollar. The receipts (ADRs) representing common shares (PBR) showed a nominal appreciation of 45%, while those for preferred shares (PBRA) were up 44%. The Petrobras stock outperformed the major indices: the Dow Jones (+ 16%), the US market's leading benchmark; the Amex Oil Index (20%), comprising major companies in the oil and gas sector; and the NYSE's International 100 (21%), which brings together the 100 most liquid ADRs.

Petrobras was the most heavily traded non-American company on the New York Stock Exchange, taking the combined daily average trading volume of the two classes of receipt. The average daily NYSE turnover of the company's common receipts came to US\$ 227 million, and for the preferred receipts it was US\$ 99 million.

Top ADR: turnover (traded volume) in NYSE

2006 daily average

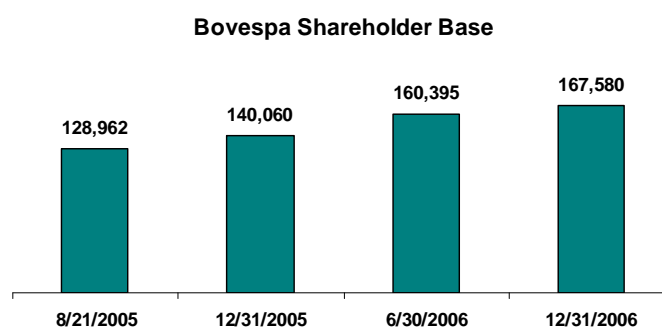


* All firm's ADR programs

Source: Bloomberg

In 2006, for the first time, Petrobras' monthly average market capitalization passed US\$ 100 billion (in December), closing the year at US\$ 108 billion. This is the largest amount of any publicly traded Latin American company, and is up by 45% in relation to the 2005 figure (US\$ 74 billion) and by 155% compared to 2004 (US\$ 42 billion). In reais, the company's market capitalization amounted to R\$ 230 billion at the end of 2006, compared to R\$ 174 billion in 2005 and R\$ 112 billion in 2004.

Over the course of the year, the company's Bovespa shareholder base grew by 20%, closing 2006 with a total of 168 thousand shareholders. This is not only of the outcome of action carried out in 2005, which made the shares more accessible to small investors, but also a reflection of the growing confidence of investors in Petrobras' management model.



In April, the company listed its common and preferred shares at the Buenos Aires Stock Exchange, thereby opening up the possibility for Argentinean investors to have direct access to Petrobras shares, as well as enabling the company to broaden its shareholder base and strengthen its brand name among the local population.

The quality of Petrobras' corporate governance, which is fully committed to the principles of ethics, transparency and social and environmental responsibility, secured the company a place on the select Dow Jones Global Sustainability Index. This is the world's most important sustainability index, which serves as a parameter for socially and environmentally responsible investors. In November, it was announced that Petrobras' shares had also been included in the Bovespa Corporate Sustainability Index.

Share Buyback

A share buyback program was announced in December, which will allow the company to repurchase up to 91.5 million preferred shares – 4.9% of the total preferred shares in circulation – up to December 2007. This decision reflects the management's belief that the company's shares are undervalued, in view of Petrobras' prospects for growth and profitability, and is aimed at reducing the company's short term financial costs.

Dividends

During the year, Petrobras shareholders received dividends in relation to the 2005 base year equivalent to R\$ 1.6562 per common or preferred share. This represents an increase of 39% in comparison with the dividends paid out in relation to the previous year, which is in line with the 40% rise in the company's net earnings. For the 2006 fiscal year, the Board of Directors proposes to pay out R\$ 7,897 million in dividends, equivalent to R\$ 1.80 per share, which is up 8.7%, in line with the profit increase.

Corporate Finance

Petrobras retained its high degree of liquidity in 2006 and obtained more favorable terms in its fund raising, which received a boost from the investment grade ratings assigned by Moody's Investor Services in October 2005 and Standard & Poor's in January 2007. Within this scenario, the company developed strategies for managing its liabilities that included the prepayment of debt, the renegotiation of contractual terms and strategic new fund raising.

With regard to the early repayment of debt, in March, Petrobras prepaid two series of the Program for the Securitization of Bunker Fuel and Fuel Oil, reducing the outstanding principal to US\$ 577.6 million. The company also obtained the consent of the investors in the remaining series for: the withdrawal of bunker fuel from the program; a reduction in the insurance cost; a reduction in the minimum daily average exports. The terms of other financial contracts were also revised, resulting in lower interest rates and the exclusion of certain insurance mechanisms (political risk insurance and letters of credit).

In the international capital markets, operating through its subsidiary PIFCo, the company repurchased securities in July with a total value of US\$ 888 million. Including the amount already repurchased by Petrobras, this operation has led to the canceling of US\$ 1,215 million of the company's debt. In February 2007, an operation was carried out for the exchanging of five series of old PIFCo securities for new securities maturing in 2016, with a total face value of US\$ 399,053,000.

In September, PIFCo carried out a private 10-year bond issue in Japan, denominated in yen, for the equivalent of US\$ 300 million, at a rate of 2.15% p.a. and partially guaranteed by JBIC, with the objective of reopening the Japanese market and diversifying the company's investor base.

In October 2006, PIFCo made its first issue of Global Notes since the company obtained its investment grade, in order to establish a new benchmark for the group's funding costs. The issue represented the lowest ever cost to PIFCo for a ten year maturity (a rate of 6.125% p.a., with a return to investors of 6.185% p.a.) and most of the demand was high grade. Moreover, the company introduced improvements to its covenants.

In transactions with the Brazilian Development Bank (BNDES), Petrobras drew down US\$ 314 million, through its subsidiary PNBV, for the construction of the P-51 and P-52 platforms.

Under lines of credit in the international banking market, the company raised a total of US\$ 2,112 million, 20% more than in 2005, 97% of which was earmarked as support for the operations of subsidiaries, with the remainder going into the commercialization of oil and oil products.

In order to provide the company with a liquidity cushion, PIFCo has secured, since 2004, a total of US\$ 675 million in standby facilities. These allow the company to draw down any amount, up to the contract limit, over a period of two years, and gives the company a year to repay the principal.

With regard to bank guarantees, the total amount under contract to Petrobras and its subsidiaries amounted to US\$ 4,126 million – 107.86% more than at the end of 2005.

Structured Projects

Through structured project finance operations, the company secured funding in the Brazilian and foreign financial markets for its undertakings in the Downstream, Exploration & Production, and Gas & Energy areas, using Specific Purpose Companies (SPCs) set up for each project.

In the Downstream area, Petrobras closed the project finance contracts, in May, for the modernization of the Henrique Lage refinery (Revap), amounting to US\$ 900 million.

The ABN AMRO bridge loan on the project for the construction of the P-53 platform, to go into production in the Campos Basin's Marlim Leste field, was renewed in

August and the syndicated loan was refinanced in September. The total amount of these operations comes to US\$ 1.1 billion, of which US\$ 350 million corresponds to the bridge loan and US\$ 750 million to the syndicated loan.

In the area of Exploration & Production, the refinancing of a syndicated commercial bank loan in relation to the Master Plan for the Delivery and Treatment of Oil from the Campos Basin (PDET) was concluded in September. The improvement in Petrobras' credit rating since the original structuring of the financing, in March 2005, enabled the company to obtain a reduced spread and the cancellation of the political and commercial risk insurance on the transaction.

In the area of Gas & Energy, two additional bridge loans for the Southeast-Northeast Gas Pipeline Interconnection (Gasene) were arranged with the Brazilian Development Bank (BNDES) in December. One of the loans, amounting to R\$ 1.05 billion, will be used to purchase pipeline for the stretch between Cacimbas (ES) and Catu (BA); the other, for R\$ 312 million, will be used for the stretch between Cabiúnas (RJ) and Vitória (ES).

In November, Petrobras Netherlands BV (PNBV) signed a financing contract (a Co-Financing Term Loan Facility Agreement) with the Export-Import Bank of Korea – K-Exim (the official credit institution for South Korea) and BNPParibas. The contract, for the amount of US\$ 360 million for a term of eight years, is to finance Petrobras' investment in two oil production platforms to be constructed by the South Korean shipyards of Hyundai Heavy Industries and Daewoo Shipyard & Marine Engineering. The platforms will be used in foreign oilfields in which Petrobras has a financial stake.

Structured Projects

Project	Year Structured	Amount US\$ million
Marlim	1998	1500
Albacora	2000	410
Barracuda/Caratinga	2000	3100
Cabiúnas	2000	850
Espadarte, Voador and Marimbá (EVM)	2000	1076
Nova Marlim	2001	834
Pargo, Congo, Garoupa, Cherne and Carapeba (PDCG)	2001	85.5
Networks	2003	1000
CLEP (Oil Equipment Leasing Company)	2004	1250
PDET (Master Plan for the Delivery & Treatment of Oil from the Campos Basin)	2005	1.270 ¹
CRI Macaé – Certificate of Real State Receivables	2005	200 ²
Modernization of the REVAP refinery	2006	900

Note: 1. Due to increased costs, the total amount for the project went from US\$ 910 million to US\$ 1.27 billion.
2. Amount in reais (R\$)

Projects being structured

Projetos	Amount US\$ million
Urucu-Coari-Manaus gas pipeline and Manaus thermoelectric plant (Amazonas)	1,300
Construction of P-53 platform (Marlim Leste)	1,180
GASENE	2,000
Mexilhão	595

Risk Management

Petrobras manages its risks in an integrated manner, taking advantage of any possible natural forms of protection. The company seeks to attain a suitable balance between its goals of growth and return on investment, on the one hand, and its level of exposure to the risks inherent to its operations or stemming from the context in which it operates.

By the very nature of its activities, Petrobras is subject to a whole series of market risks, such as variations in the prices of oil and oil products, in foreign exchange rates and in interest rates. Through its risk management policy, aligned with its corporate goals and objectives, the company seeks the security of its operations and the execution of its planned investments, so as to be able to maintain its profitability and grow in a sustainable manner.

Any proposals for the management of risk are put before the Risk Management Committee, comprising executives from the company's business and corporate areas. This allows an integrated view of the issues and makes it easier for the Executive Board and the Board of Directors to comprehend the risk exposure and take the appropriate decisions.

In the management of oil and oil product market risks, following the premise of regular and systematic evaluation of the consolidated net exposure to price risk, operations using derivatives have consequently been limited to specific short term transactions (up to six months), involving futures contracts, swaps and options and utilizing control methodologies in accordance with specific risk management guidelines, in order to safeguard the results of its physical operations.

Credit Risk

In line with the recent alterations in the country's regulatory environment, Petrobras has adapted its credit policy to the new market circumstances. This has preserved the attractiveness of sales on credit, without unnecessarily raising the company's exposure to credit risk.

In order to analyze these operations, in 2006, the company set up the Petrochemicals Area Credit Committee, following the model of the committees for the Downstream and Gas & Energy areas, set up in 2004, when a system of credit flow analysis was also introduced.

Outside Brazil, in line with Petrobras' growing sales, the processes for analyzing and conceding credit to customers (exports and the provisioning of vessels) were standardized and centralized in 2006.

Insurance

In 2006, the final premium on the company's principal insurance policies – major fire/operational risk and risk petroleum – was raised to US\$ 34.5 million, from US\$ 29.4 million in 2005, an increase of 17%. On the other hand, the value of the company's insured assets increased by 32%, from US\$ 32.7 billion to US\$ 43.2 billion.

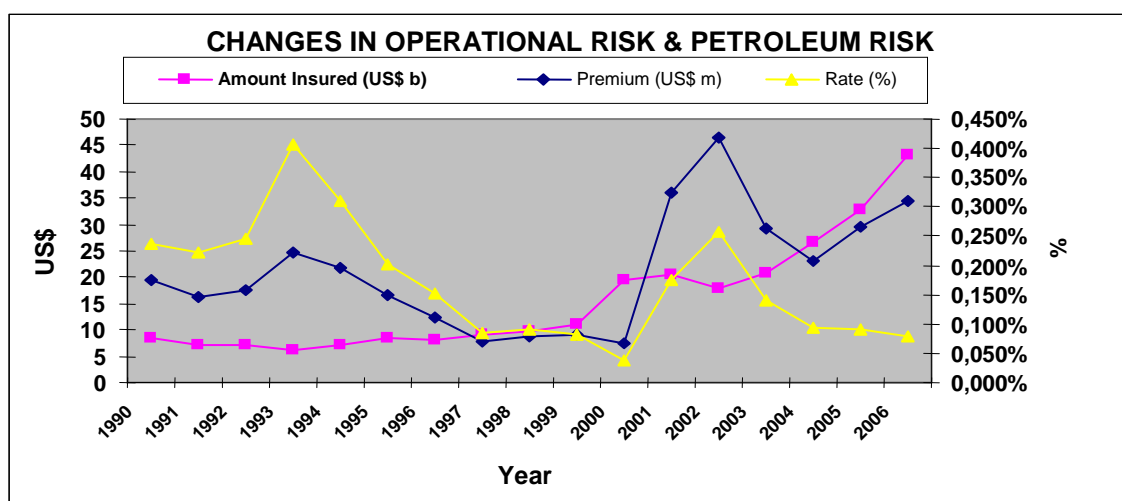
Most of Petrobras' risk is reinsured in the international market. The company has a fixed policy of publicizing its risk management practices, in Brazil and abroad. Pertinent information regarding losses and improvements made are promptly and candidly passed on to the insurance market.

Like other large oil companies, Petrobras bears a significant portion of the risk, with insurance exemptions as high as US\$ 40 million. The company does not insure against lost profits and wellhead controls in Brazil, nor does it insure its pipeline network.

Platforms, refineries and other installations have insurance cover against major fire/operational risk and petroleum risk. The movement of cargoes is covered by transportation insurance policies and the vessels are covered by hull and machinery insurance. Civil liability and environmental risks are covered by one or more policies, according to the circumstances. Projects and installations under construction, where the maximum likely damages would exceed US\$ 40 million, are covered against engineering risks under a policy taken out by Petrobras or by the contractors.

For insurance purposes, the company's assets are valued at replacement cost. Based on the maximum likely damages at each installation, the maximum indemnity in the major fire/operational risks policy has been fixed at US\$ 600 million.

Most of the company's activities abroad are insured or reinsured by the Bear Insurance Co. Ltd., based in Bermuda. As a captive insurance company, Bear retains none of the risk, but passes it on in full to the market.



Corporate Governance

Petrobras is constantly striving to perfect its corporate governance practices and relations with shareholders, customers, suppliers, employees and other stakeholders. The company adopts management procedures that are compatibles with the regulations governing the markets in which it operates and continually monitors the application of these procedures.

In Brazil, Petrobras is subject to the rules of the Brazilian Securities Commission (CVM) and the São Paulo Stock Exchange (Bovespa). Outside Brazil, it obeys the rules of the Securities and Exchange Commission (SEC) and the New York Stock Exchange (NYSE), in the USA, and of the Madrid Stock Exchange (Latibex), in Spain. As from 2006, with its listing in Argentina, the company is also subject to the rules of the Argentinean Securities Commission (CNV) and the Buenos Aires Stock Exchange.

Petrobras is studying the process for formally adhering to the Bovespa's differentiated levels of corporate governance and, since changes were made to its by-laws, in 2002, the company has been in full compliance with the practices and regulations defined therein.

The training program in corporate governance for executives and staff whose functions are directly linked to relations with the companies of the Petrobras System, which continued through 2006, fosters awareness of the importance of this topic and disseminates the best practices adopted in Brazil and abroad.

The process of reviewing the Petrobras System's Code of Ethics, which involved the participation of the employees, was concluded in 2006. The aim of the process was to update this important tool and bring it into alignment with the requirements of the Sarbanes-Oxley Law (SOX) regarding specific items in the Codes of Ethics of companies listed with the New York Stock Exchange.

As one of the SOX requirements, Petrobras discloses in Form 20-F (the Annual Report, an SEC requirement) that one of the nine members of its Board of Directors, elected at a General Meeting of the Shareholders held on April 3, 2006, is a financial specialist.

Corporate Governance Structure

Petrobras' corporate governance structure comprises the Board of Directors and its advisory committees, the Executive Board, the Statutory Audit Committee, the Internal Auditors, the Ombudsman, the Business Committee and the Management Committees.

Board of Directors

An independent collegial body with powers and responsibilities laid down in the law and in the company's by-laws, whose main duties are to define the company's strategic guidelines and supervise the actions of the Executive Board. There are nine board members, elected at a General Meeting of the Shareholders for a term of one year, with the possibility of reelection. Seven of the board members represent the controlling shareholder; one represents the minority common shareholders; and one represents the preferred shareholders.

Executive Board

The Executive Board runs the business, in line with the mission, objectives, strategies and guidelines defined by the Board of Directors. The Executive Board consists of a President/CEO and six directors chosen by the Board of Directors for a term of three years, with the possibility of reelection, who may be removed at any time. Only the CEO is a member of the Board of directors, but may not preside over that body.

Statutory Audit Committee

A permanent body, independent of the company's management, as laid down in Brazilian Corporate Law, the Statutory Audit Committee comprises five members, with terms of one year, with the possibility of reelection. One of the members represents the minority shareholders; another represents the preferred shareholders; and three act in the name of the federal government – one of these is appointed by the Finance Minister, as the representative of the National Treasury. It is incumbent on the Statutory Audit Committee to represent the shareholders in a supervisory capacity, monitoring the actions of the company's management to verify compliance with their legal and statutory obligations, as well as defending the interests of the company and its shareholders.

Internal Auditors

The Internal Auditors plan, execute and evaluate the company's internal auditing procedures and assist the senior management and external control bodies. The company also has outside auditors, appointed by the Board of Directors, who are restricted as to the consulting services they may provide. It is mandatory that the outside auditors be changed every five years, on a rotation basis.

Ombudsman

The Ombudsman, directly linked to the Board of Directors, plans, guides, coordinates and evaluates activities aimed at gathering the opinions, suggestions, criticism, complaints and accusations of interested parties having some form of relationship with the company, and arranges for investigations to be carried out and appropriate steps to be taken. In compliance with the requirements of the Sarbanes-Oxley Law, this office must also serve as a channel to receive and process accusations regarding accounting, internal control and auditing issues, including confidential and anonymous tip-offs from employees.

Board Advisory Committees

There are three Advisory Committees: for Auditing; the Environment; and Remuneration and Succession. Their members belong to the Board of Directors and assist the Board in carrying out its responsibility to provide the company with high level guidance and direction.

Auditing Advisory Committee

In full compliance with the requirements of the Sarbanes-Oxley Law, this committee comprises three independent Board members and its president needs to be a financial specialist – in accordance with SEC definitions. The committee's function is to analyze questions regarding the integrity of the company's US GAAP financial reports and the effectiveness of its internal controls, as well as supervising Petrobras' outside and internal auditors.

Business Committee

This committee is a forum for integration, seeking to align business development, management of the company and the guidelines of the Plan Strategic, in support of the senior management's decision making process.

Management Committees

These are forums for delving deeper into issues that are to be presented to the Business Committee, with which it liaises. Such integration also exists between the Management Committees themselves and in their relations with the Board Advisory Committees.

At present, the company has the following Management Committees: Exploration & Production; Downstream; Gas & Energy; Human Resources; Health, Safety & the Environment; Organization and Management Analysis; Information Technology; Internal Controls; Risk; Petrobras Technology; Social and Environmental Responsibility; and Marketing & Brands.

Internal Controls

The Program of Integrated Internal Control Systems and Methods (Prisma), included in Petrobras' strategic agenda and currently assimilated in the company's General Management of Internal Controls, concluded the work for compliance with the requirements of Section 404 of the Sarbanes-Oxley Law.

The activities carried out in 2006, under the guidance of the Committee for the Management of Internal Controls and monitored by the Auditing Advisory Committee, consisted of completion of the charting, documenting and maintenance of the internal control structure for the mitigation of risks relating to the Petrobras System's consolidated financial reports.

Petrobras' General Management of Internal Controls, basically following the guidelines of the Public Company Accounting Oversight Board (PCAOB), the Committee of Sponsoring Organizations of the Treadway Commission (Coso) and the Control Objectives for Information and Related Technology (Cobit), continued to implement the best practices in corporate governance and the control over the business, service, financial and information technology processes.

Petrobras, along with the independent auditors, endorsed the design of the processes and controls that have a substantial impact on the Consolidated Financial Reports. All shortcomings that could significantly or materially jeopardize the certification of the company's internal controls were rectified. The System's Internal Auditors, directly linked to the Boards of Directors, conducted further tests of the effectiveness of the controls, and no problems were found that might compromise the evaluation of the company's control structure, both in terms of the whole entity and in terms of processes and information technology.

Documentation of the design of the processes, controls and tests is being regularly stored in an integrated system of internal control management, which automatically monitors the changing roles and responsibilities, making it possible to visualize the internal control structure, from the managers who are directly responsible for

the controls all the way up to the senior levels, even to the financial director and the CEO of Petrobras. Hence, the managers, the General Management of Internal Controls, the Internal Auditors, senior management and the Auditing Advisory Committee can see, at any given moment, an up-to-date analysis of the position of the Petrobras System's internal controls.

Information about the rendering of services by the independent auditor other than those of the external auditing – CVM Instruction n° 381/2003

Petrobras' corporate management strictly adheres to the company's Code of Ethics, Code of Good Practice and Corporate Governance Guidelines.

Article 29 of the company's by-laws specifies that the independent auditors may not provide consulting services to Petrobras during the period that its auditing contract is in force.

The company has engaged KPMG Auditores Independentes to provide Specialized Technical Services in the Auditing of Accounts for the 2006, 2007 and 2008 financial years, which they have been doing since April 2006.

During 2006, the following services were rendered to Petrobras and its subsidiaries and affiliates by Ernst & Young Auditores Independentes S/S., in relation to the 2005 financial year, and by KPMG Auditores Independentes, in relation to the 2006 financial year:

	R\$ – thousand
Auditing of Accounts.....	15,191
SOX Audit	2,063
Audit-related services	3,011
Tax Audit	1,467
Other services.....	<u>928</u>
Total	22.660

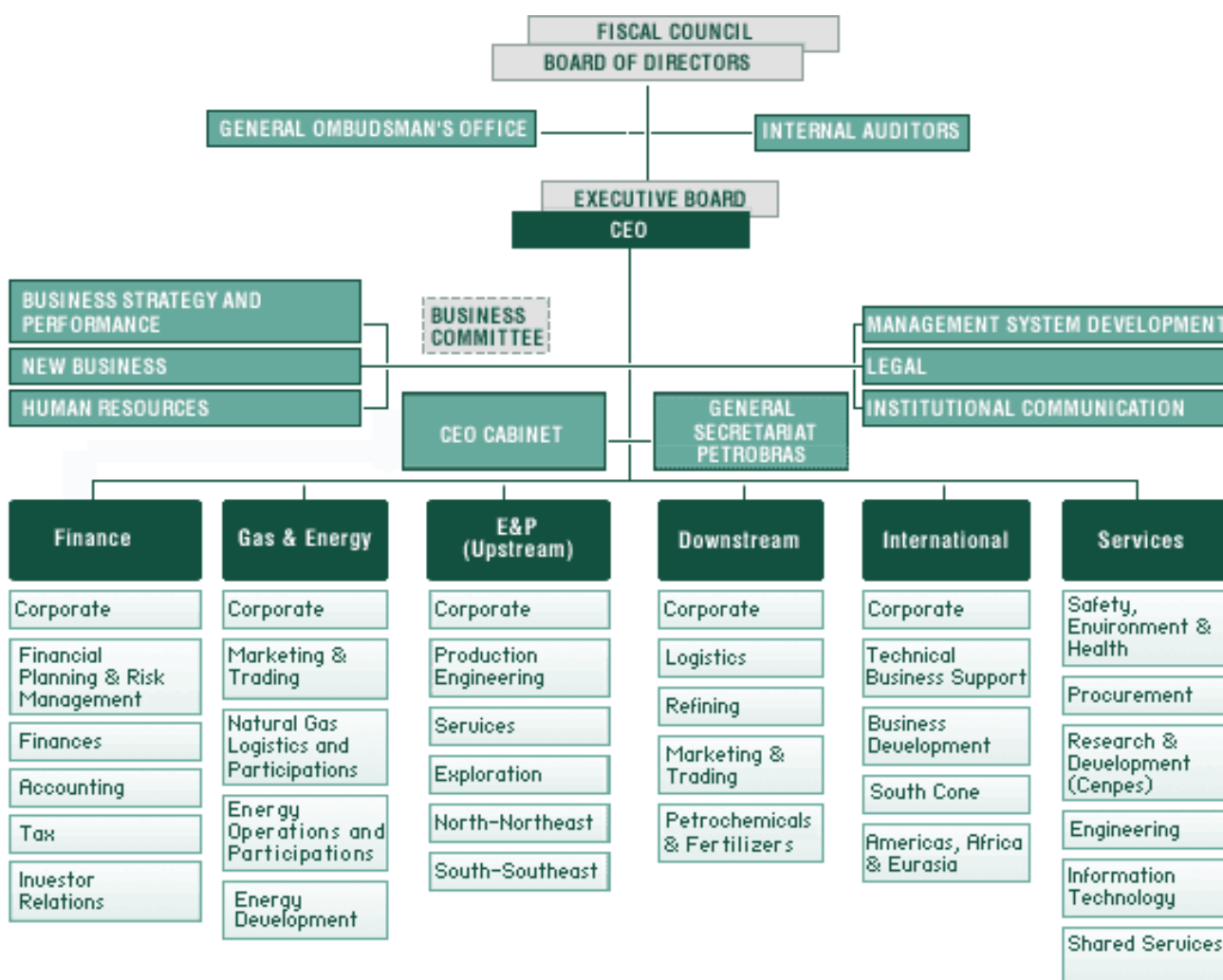
Information Disclosure

In line with its policy of transparency in its relationship with the capital markets, the company holds quarterly open meetings at which it announces its results and releases its quarterly BR GAAP and US GAAP balance sheets. Due to the listing of the company's shares in Argentina, as of the year end 2006, Petrobras will now also disclose its annual US GAAP balance sheet reconciled to the Argentinean standard.

Petrobras has an internal document formally defining the controls and procedures for the disclosing of information, that is to be followed by all the company's staff. This ensures that the information released to the market has been recorded, processed, developed and made available in compliance with the legal rules and time limits.

Petrobras Organization Model

The Petrobras organization model, ratified by the Board of Directors in October 2000, is constantly being refined in order to tailor it to the Strategic Plan. Changes in the company's organizational structure in 2006 resulted in, among other things, the reorganization of the Gas & Energy business area and the setting up of the Santos Basin Exploration & Production business unit. Furthermore, reviews were carried out of the organization and management model for the International business area and of some business unit structures abroad, in addition to the implementation of a new organizational structure for the Financial area.



Board of Directors

Dilma Vana Rousseff

Chairwoman

Silas Rondeau Cavalcanti Silva

Board Member

Guido Mantega

Board Member

José Sérgio Gabrielli de Azevedo

Board Member

Gleuber Vieira

Board Member

Arthur Antonio Sendas

Board Member

Roger Agnelli

Board Member

Fábio Colletti Barbosa

Board Member

Jorge Gerdau Johannpeter

Board Member

Executive Board

José Sérgio Gabrielli de Azevedo

President & CEO

Almir Guilherme Barbassa

Financial & Investor Relations Director

Renato de Souza Duque

Director of Services

Guilherme de Oliveira Estrella

Director of Exploration & Production

Paulo Roberto Costa

Director of the Downstream Area

Ildo Luís Sauer

Director of Gas & Energy

Nestor Cuñat Cerveró

Director of the International Area

Fiscal Council

Titular members

Maria Lúcia de Oliveira Falcón

Nelson Rocha Augusto

Túlio Luiz Zamin

Erenice Alves Guerra

Marcus Pereira Aucélio

Substitute members

Celso Barreto Neto

Maria Auxiliadora Alves da Silva

Marcelo Cruz

Edison Freitas de Oliveira

Eduardo Coutinho Guerra