

Best Oil Bet Seen Supported by Political Shift: Corporate Brazil  
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(To set an alert for Corporate Brazil: SALT BZCORP)

By Peter Millard and Julia Leite

Aug. 26 (Bloomberg) – Petroleo Brasileiro SA, the state-run oil company that has rallied with President Dilma Rousseff's weakening poll numbers, still has room to gain if the incumbent loses, according to fund managers from Mirae Asset Global Investments to ING Groep NV.

Petrobras, as the best-performing major oil stock in the past six months is known, could extend the gain by as much as 30 percent if either of the two main other candidates prevails in October elections, according to Teorica Investimentos. The stock will also benefit if an opposition candidate pulls ahead in opinion polls, according to ING and Guide Investimentos SA.

Investors are betting an easing of fuel price caps under a new administration will deliver better profitability next year, according to Mirae Asset Global Investments.

The biggest producer in waters deeper than 1,000 feet (300 meters) has posted \$44 billion in operational losses at its refining division since it started subsidizing imported fuel in

2011 as part of a wider policy to curb inflation. The company has said it needs parity with international prices to pursue about \$40 billion a year in planned investments. Petrobras has surged as weaker crude prices weigh on other major producers.

"The rally we've seen is the market paying up for an increased probability of change in political leadership,"

Oliver Leyland, a portfolio manager at Mirae who owns the stock and has been buying, said by phone from New York. A new government "would bring a greater chance of a change in critical policies, such as the fuel price policy, and the way in which the company is run."

#### 'Unpopular Measures'

Petrobras declined to comment on the impact the presidential election has had and would continue to have on the stock price in an e-mailed response to questions. The press offices for Rousseff and opposition candidates Marina Silva and Aécio Neves didn't respond to e-mailed requests for comment.

"It's a lot easier for an opposition candidate to take unpopular measures and say 'hey, this is because of the last government,'" Felipe Rocha, an analyst at Guide Investimentos, said by telephone from Curitiba, Brazil. "It's more complicated for a candidate who is re-elected."

Brazil's domestic diesel and gasoline prices have trailed international rates by 10 percent to 20 percent, depending on swings in the exchange rate, Moody's Investors Service said in a July 29 research report. The pricing policy has put a "significant drag" on Petrobras's profitability, the debt-rating agency said.

#### Profit Miss

Profits have missed analyst estimates in three of the past four quarters as the company continued to subsidize imported fuel. The government controls Petrobras through a majority of voting shares. Finance Minister Guido Mantega is its chairman.

Rising Brazilian demand for gasoline and diesel is leading the state-run producer to increase refinery output and export less oil. Overseas sales of crude fell 14 percent from a year earlier in the second quarter, while the refining boost wasn't enough to prevent a 56 percent surge in fuel imports.

The company plans to start operations at a new refinery in November. That will help reduce the amount of fuel imports in the second half of this year, Petrobras said in a presentation on Aug. 11. Crude exports are also set to rise as production increases at recently installed offshore platforms, it said.

Petrobras rose 5.4 percent in Sao Paulo yesterday on speculation a new presidential poll will show rising support for opposition candidate Marina Silva, said Alvaro Bandeira, a partner at Orama Asset Management. A new poll by Ibope may be released as soon as today.

### Race Upended

Silva's entry into the contest as a replacement for Eduardo Campos, who died in an Aug. 13 plane crash, has upended the race, with polls showing her attracting previously undecided voters.

Her pledges to slow inflation, grant central bank autonomy and check rising spending that led the country's debt rating to be cut appeal to the mainly affluent supporters of rival Neves, while her personal story as a former maid appeals to poorer voters, said Rafael Cortez, a political analyst at research company Tendencias Consultoria Integrada.

Silva criticized Rousseff's management of the economy in an Aug. 20 news conference. Her economic adviser, Eduardo Giannetti, said the previous day that policies to contain energy prices are "extremely harmful" in the short term.

### Biggest Return

Silva would win in a run-off against Rousseff with 47 percent of the vote, compared with 43 percent for the incumbent, according to a Datafolha poll published Aug. 18. Rousseff's 36 percent lead in the poll for the first round of balloting, compared with 21 percent for Silva and 20 percent for Neves, wouldn't be enough to ensure a victory. To win in the first round a candidate needs more votes than the other competitors combined.

Petrobras returned 62 percent in dollar terms in the past six months, the biggest gain among the 20 most valuable oil producers. The average gain over the same span was about 15 percent.

Investors betting Petrobras will surge if Rousseff is voted out of office in October elections have a large chance of losing their money even if she is defeated, said Robbert van Batenburg, director of market strategy at broker-dealer Newedge USA LLC.

They had better wait for evidence a challenger would swiftly phase out Rousseff's expensive fuel subsidies to improve profitability at the most-indebted publicly traded oil company, Batenburg said in a phone interview from New York.

### Too Early

It's too early to anticipate that Rousseff will be defeated and the stock could still swing in either direction leading up to the election, said Paul Christopher, chief international strategist at Wells Fargo Advisors, which manages \$1.4 trillion.

"Dilma is losing support, but I don't think she's running clearly behind," Christopher said by phone from St. Louis.

Petrobras, based in Rio de Janeiro, is seeking to close the gap between international and local fuel prices, Chief Executive Officer Maria das Gracas Foster wrote in an Aug. 8 earnings report. "I reassure investors and stockholders that the increasing production of oil, natural gas and derivatives, especially diesel and gasoline, is already a reality on a daily basis," she said at the time.

The stock's increased volatility since Silva replaced Campos highlights how politics is driving stock performance, Eric Conrads, who helps oversee about \$500 million in Latin American stocks as a money manager at ING, said.

“It’s a very binary view for the stock, either it goes back down or continues to rally,” Conrads said. “It’s becoming a proxy for the elections.”

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