

## MANAGEMENT REPORT

To our shareholders:

Management of Saraiva S.A. Livreiros Editores submits for your appreciation the Management Report and the related financial statements, with the Independent Auditors' Report, for the year ended December 31, 2006.

Saraiva Group operates in the publishing segment, through Editora Saraiva (Saraiva S.A. Livreiros Editores), and in the retail segment, through Livraria Saraiva (Livraria e Papelaria Saraiva S.A.).

The Company's operating and financial information is consolidated and stated in Brazilian reais, in accordance with corporate law. All comparisons are made in relation to 2005, except where otherwise specified.

### MESSAGE FROM MANAGEMENT

In 2006, we made major advances in the process of consolidating our main operations and strengthening competitive capacity.

Consolidated net income totaled R\$ 46.5 million, in the third consecutive year of record levels, growing 16.1% in relation to 2005. Consolidated gross revenue from sales reached R\$ 587.3 million, 16.2% higher than the prior year, favored by the performance of Livraria Saraiva, with growth of 25.2%. Adjusted EBITDA (Earnings Before Interest, Taxes, Depreciation and Amortization, adjusted for extraordinary expenses and provision - not representing cash outflow - for redemption of "Saraiva Plus" bonuses) totaled R\$ 77.8 million, representing a 0.4% increase in relation to 2005.

In management of the capital structure, we expanded our partnership with the National Bank for Economic and Social Development (BNDES) by obtaining, through Livraria, long-term financing of R\$ 22.1 million (whose first release, of R\$ 4.4 million, occurred in December 2006), intended for the store expansion and renovation project for 2005 to 2008. This event, along with the agreement signed with Editora at the end of 2005, contributed to lowering our weighted average cost of capital and favors capacity to invest in projects with attractive return expectations.

We remained focused on controlling spending, and increasing operating efficiency with the continuity of the cash management program, through which actions are carried out to generate expense and cost savings. The measures adopted in 2006 provided for estimated consolidated annual savings of R\$ 2.4 million. This result, along with that obtained in the last two years, has allowed for successive gains in the ratio of operating expenses to net revenues. This ratio, which reached 46.2% in 2003, was lowered to 39.6% in 2006.

We ended 2006 well positioned to accelerate sustained growth. The Company adhered to the Level 2 Differentiated Corporate Governance Practices of Bovespa (São Paulo Stock Exchange), strengthening its positioning as a company with a deep commitment to transparency and quality of information disclosed to the market, as well as holding modern mechanisms to protect minority shareholders' rights. We successfully conducted a capital increase, which strengthened cash to make new investments. In addition, we developed other initiatives with the capital market promoting strong growth in the liquidity of the Company's shares, evidenced by

Saraiva's inclusion in the "Brazil Index" (IBrX-100), composed of 100 shares selected among the most traded on Bovespa.

In the domestic educational scenario, 2006 proved to be especially important. The Basic Education Maintenance and Development and Education Professionals Valuing Fund (Fundeb) was approved, providing for a gradual increase in government funds for education. With the estimate to involve R\$ 56 billion beginning in the fourth year of implementation, Fundeb will benefit 48 million students, from daycare to high school.

Another noteworthy event was the release of Resolution No. 1, of 01/15/07, by the National Fund for the Development of Education (FNDE), defining the schedule for progressive compliance with the complete high school curriculum for all public schools (approximately 8 million students). Begun as a pilot project in 2004, the National High School Textbook Program (PNLEM) began serving, although partially, a segment that was not included in government textbook purchasing programs. The Resolution's release is significant, since it indicates the Federal government's commitment\* for the program to be recurring and fully serve all high school grades and subjects. This fact is important for **Editora Saraiva**, which has a significant share of this market and was leader in contracts for the 2007 school year, both in sales to the Federal government under the PNLEM (approximately 27% of total books purchased), and under the "Books in School" program, by the Minas Gerais State Education Department (around 24%).

\* Actual purchase of books, as set forth in the Resolution, depends on budget appropriation.

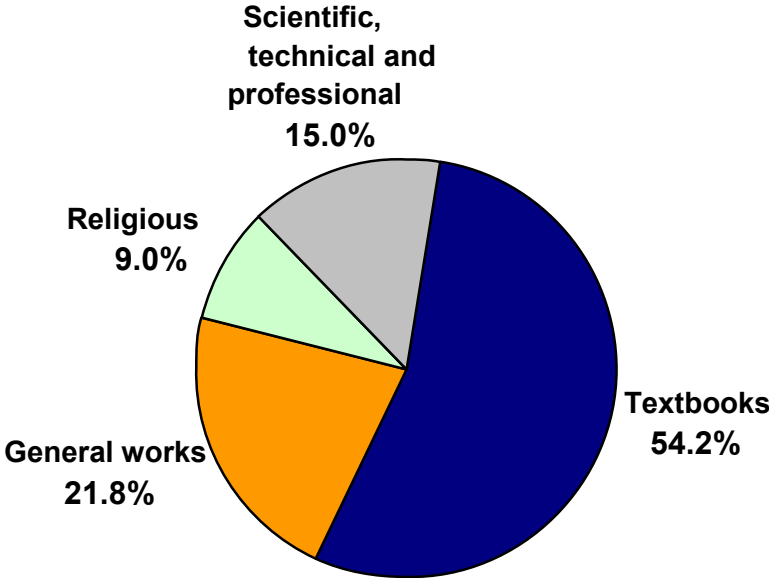
The year 2006 also represented significant growth in the **Livraria Saraiva's** activities. We consolidated the recovery process begun in 2005 and structured operations to gain scale and accelerate value generation.

We invested in improving logistics and services in the electronic retail division, which displayed robust growth of 52.5% in sales. We negotiated the contracting of five new units to be opened in the first half of 2007. We successfully expanded the mix of product categories. We intensified investments in marketing and surpassed the mark of 1.1 million customers affiliated with our "Saraiva Plus" loyalty program.

In line with our pioneering tradition and in order to increasingly be each consumer's best experience and first memory in seeking culture, entertainment and information, we signed a partnership agreement to be home to one of the first two Starbucks stores in Brazil. In early December a Starbucks store was opened inside the Saraiva Mega Store in Shopping Morumbi, in São Paulo. Starbucks is the world's leading brand in retail of specialty coffees.

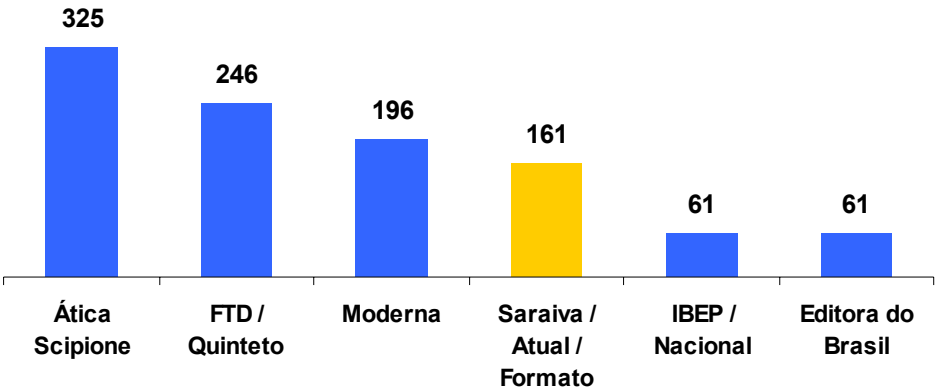
Highlights of the publishing and bookstore market and positions of the main participants:

**Publishing Market - 2005**  
**Composition of Gross Sales - R\$1.8 billion**



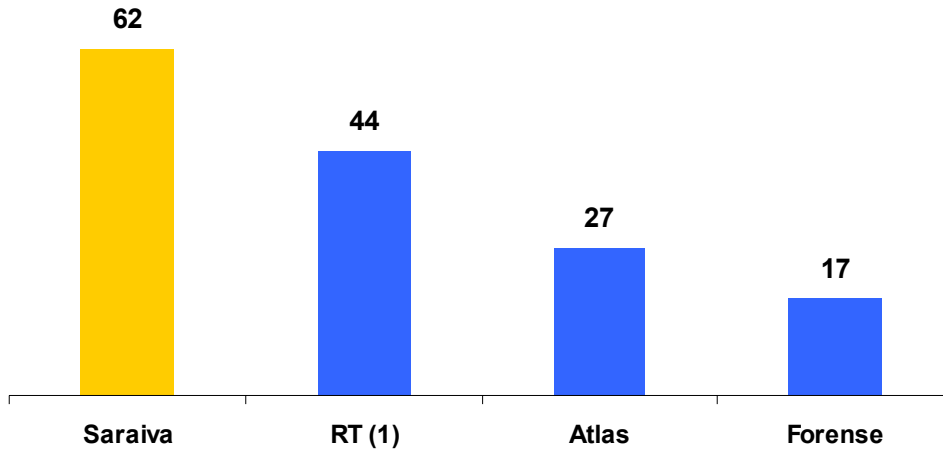
Source: CBL (Brazilian Book Chamber)

**Textbook Market - 2005**  
**Main Publishers by Net Sales - R\$ million**



Source: Published balance sheets and Serasa

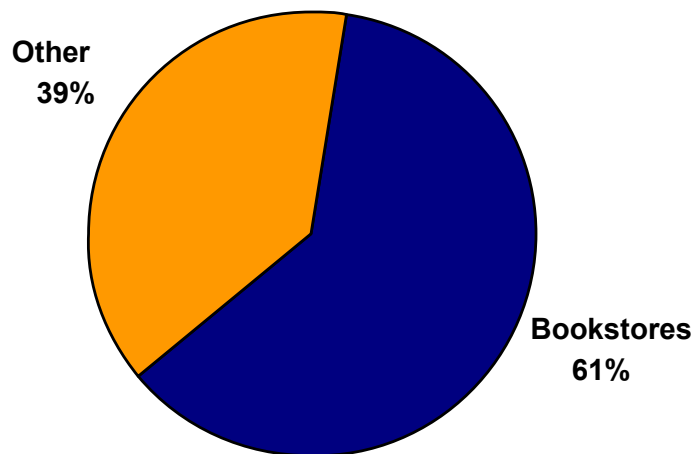
**Legal Book Market - 2005**  
**Main Publishers by Net Sales - R\$ million**



(1) 2004

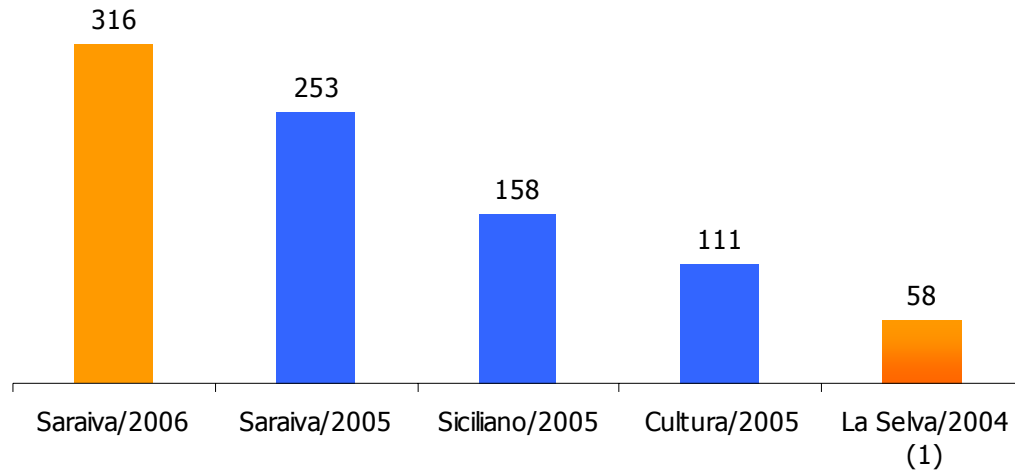
Source: Published balance sheets, Saraiva and Serasa

**Book Market - 2005**  
**Gross Sales by Sales Channel - R\$ 2.6 billion**



Source: CBL (Brazilian Book Chamber)

**Main Bookstores  
Net Sales - R\$ million**



(1) 2005 not available  
Sources: Saraiva and Serasa

**EDITORA SARAIVA (SARAIVA S/A LIVREIROS EDITORES)**

Editora Saraiva is the parent company of Livraria Saraiva, with 99.91% of shares - the companies have separate activities and corporate names.

The table below summarizes the main data on Editora's economic and financial performance:

Description	2006		2005		HA %
	R\$ 000	VA %	R\$ 000	VA %	
Gross Revenue	247,770	100.1	233,516	100.1	6.1
Net Revenue	247,507	100.0	233,330	100.0	6.1
Gross Profit	167,688	67.8	161,594	69.3	3.8
Operating Expenses	118,090	47.7	107,286	46.0	10.1
Adjusted EBITDA (1)	57,225	23.1	60,350	25.9	-5.2
Net Financial Expenses	(2,278)	-0.9	3,468	1.5	-165.7
Net Income before equity in Subsidiaries	39,139	15.8	33,959	14.6	15.3
Net Income	46,469	18.8	40,025	17.2	16.1

(1) Adjusted by extraordinary expenses on provision for terminations with shut-down of printing unit (R\$ 1,870 thousand) plus expenses related to public offering (R\$ 536 thousand).



## Elementary School

Grade	# of Students (million)	Subjects	Market Potential # of Books (million)	% of Market Potential acquired each year		
				PNLD2007	PNLD2008	PNLD2009
1 <sup>st</sup> Grade	4.1	Literacy, Portuguese, Mathematics, Science, History and Geography	24.7	100%	100%	100%
2 <sup>nd</sup> - 4 <sup>th</sup> Grades	11.1	Portuguese, Mathematics, Science, History, Geography and Regional Books	60.7	100%	12%*	12%*
5 <sup>th</sup> - 8 <sup>th</sup> Grades	13.4	Portuguese, Mathematics, Science, History and Geography	66.9	12%*	100%	12%*

Source: FNDE/MEC/INEP (2006 School Census)

\* Historical Percentage of Replacement

Saraiva's textbook sales in the PNLD/07 represent market share of approximately 8.4%, below the historical average for 1<sup>st</sup> to 4<sup>th</sup> grade books. The selection of books for 5<sup>th</sup> to 8<sup>th</sup> grade students (PNLD/08) is scheduled for 2007, a segment in which Saraiva's catalog has had higher market share than in the 1<sup>st</sup> to 4<sup>th</sup> grade segment.

For **high school**, nearly 8 million public school students began being served in 2004, through a Federal government pilot project, the PNLEM/05. In the following two years the government purchased books to partially meet the curriculum. With the release of the FNDE's Resolution, the government shows the commitment to serve high school, which began having a progressive book purchasing schedule until at least 2012.

The year 2006 was positively influenced by sales under the PNLEM/07. Saraiva's sales correspond to a market share of approximately 27% of total books purchased by the Federal government. Also in the high school segment, similar performance was achieved in the "Books in School" program, by the Minas Gerais State Education Department (history and geography books), in which Saraiva had a 24% share of total books purchased.

The overall evolution of the Company's sales to the government in recent years is as follows:

Program by School Year		Recorded Sales (fiscal year)	
Elementary (+) High School	Total Sales (Amount of Contracts)	2006	2005
2005 (1) (2)	83.3	-	24.7
2006 (1)	65.0	14.8	50.3
2007 (1) (3)	82.6	63.5	-
<b>TOTAL FOR THE YEAR</b>		<b>78.3</b>	<b>75.0</b>

R\$ million

(1) Includes PNLD, PNLEM, "Books in School" program - SEE/MG, PNBE (National School Library Program)

(2) R\$ 58.6 million in sales was recorded in 2004

(3) R\$ 19.1 million in sales is being recorded in 2007

## Gross Profit

Gross profit totaled R\$ 167.7 million, up 3.8% in relation to the prior year. The gross profit margin decreased from 69.3%, in 2005, to 67.8%, in 2006, influenced by the larger volume of new purchases under the PNLD. The years in which new purchases occur (PNLD/07, contracted in 2006) require a quantity of new purchases higher than years in which only replacement books are purchased (PNLD/06, contracted in 2005), according to the government purchasing cycle.

## Operating (Expenses) Income

Operating expenses totaled R\$ 118.1 million, corresponding to a 10.1% increase. Some extraordinary events impacted the total of operating expenses:

- Provision for terminations related to the shut-down of the printing unit in the amount of R\$ 1.9 million (see comment in Investments section);
- Administrative expenses in the amount of R\$ 0.5 million, related to the public offering of shares conducted in April 2006 (not including brokerage expenses).

In addition to the aforementioned factors, the Company's management decided to invest more in marketing, compared to prior years, in order to increasingly strengthen the relationship with teachers and have positive effects on results for 2007.

Saraiva continues making continuous efforts based on the cash management program, in order to gain efficiency and competitiveness. In 2006, this program generated measures with expected annual savings of R\$ 0.9 million.

The "operating expenses to net revenue" ratio went from 46.0% in 2005 to 47.7% in 2006. Disregarding extraordinary expenses, the ratio fell to 46.7% in 2006. The table below shows this ratio's evolution over the last four years.

% Ratio of Operating expenses to Net Revenue	2003	2004	2005	2006*
	52.4%	49.1%	46.0%	46.7%

\* excluding extraordinary events

## EBITDA

Adjusted EBITDA totaled R\$ 57.2 million in 2006, and the EBITDA margin on net revenue, 23.1% in 2006, lower than the 25.9% in 2005.

Reconciliation of EBITDA - R\$ 000	2006	2005	Chg.
Income from Operations after Net Financial Expenses	52,013	50,891	2.2%
(+) Depreciation and Amortization	5,084	5,991	-15.1%
(+) Financial Income (Expense), net	-2,278	3,468	-165.7%
(=) EBITDA	54,819	60,350	-9.2%
(+) Extraordinary Expenses (1)	2,406	0	
(=) Adjusted EBITDA	57,225	60,350	-5.2%

### Financial Income (Expenses)/Capital Structure

Financial income (expenses) evolved from a net expense of R\$ 3.5 million to a net revenue of R\$ 2.3 million. The entry of funds with the capital increase in the net amount of R\$ 63.6 million in April 2006 provided for an average cash position much higher than in 2005, generating a significant increase in financial income and more than made up for the impact of expense of R\$ 2.4 million related to the financial intermediation of the public offering of shares.

The financial position evolved from a net debt of R\$ 2.1 million, at the end of 2005, to net cash of R\$ 77.8 million, resulting from the operating cash generation and capital increase.

Over the course of 2006, R\$ 11.4 million was released in BNDES financing, to carry out the investment plan from 2005 to 2007. The total agreement provides for R\$ 32.5 million, of which R\$ 18.9 million has already been released.

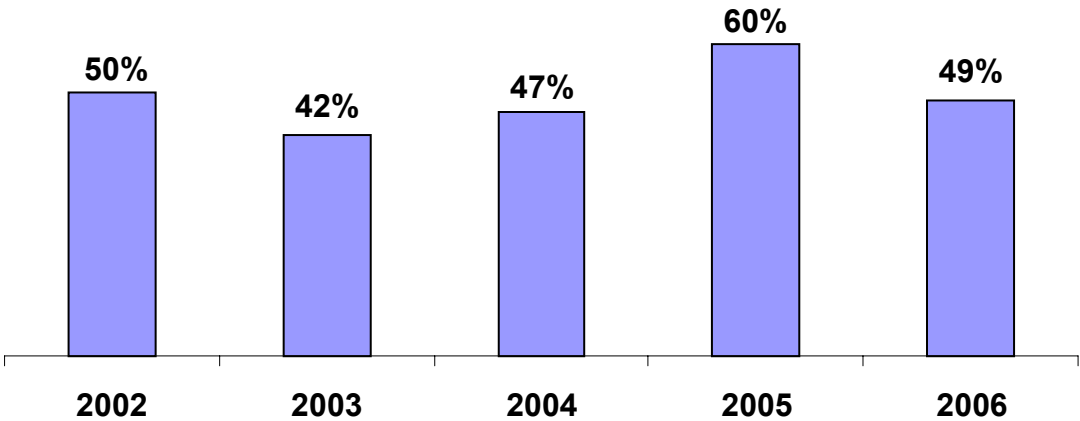
### Nonoperating Income (Expenses)

Nonoperating income (expenses) for 2006 was favored by extraordinary events in the net amount of R\$ 5.3 million, mainly related to gain on the sale of assets due to the project to shut down the printing unit.

### Net Income

Net income before equity in the subsidiary Livraria Saraiva totaled R\$ 39.1 million, up 15.3% from the result obtained in the prior year. Editora's return on equity for 2006 reached 49.0%, in line with the average return on equity for the last five years.

Editora Saraiva - Return on Equity\*



Return on Equity = Net Income before equity in subsidiary / Shareholders' Equity at beginning of year, less the investment in Livraria Saraiva.

## New Business

One of the Company's strategic growth drivers consists of forming associations and partnerships with high potential for synergy with current operations. Over the course of 2006, important steps were taken, such as:

- Agreement for co-publishing and distribution with the publisher Letras & Lucros, specialized in the promising segment of personal finance;
- Partnership for exclusive distribution of works of Saint Paul, a publisher with recognized bestsellers in the area of finance and business;
- Co-publishing and distribution agreement in the area of legal books with the publisher Rio, belonging to the Universidade Estácio de Sá group, Brazil's largest private teaching institution.

In addition to these partnerships, sales of the "Saraiva Legal Conferences" product continued in the distance-learning segment, and the customized editions system was expanded, bringing together quality content and special conditions for tailor-made supply to companies and teaching institutions.

## Awards

In 2006, four Saraiva publications (*Contabilidade - Teoria e Prática Básicas*, *Ética e Responsabilidade Social nos Negócios*, *Gestão de Negócios Internacionais* and *Gestão do Fator Humano*) were awarded the Economic Culture trophy, granted by *Jornal do Comércio* of Porto Alegre and *Caixa - RS*.

## LIVRARIA SARAIVA (LIVRARIA E PAPELARIA SARAIVA S.A.)

Livraria is mainly engaged in retail sale of books, DVDs, music, stationery, and computer and electric-electronic products.

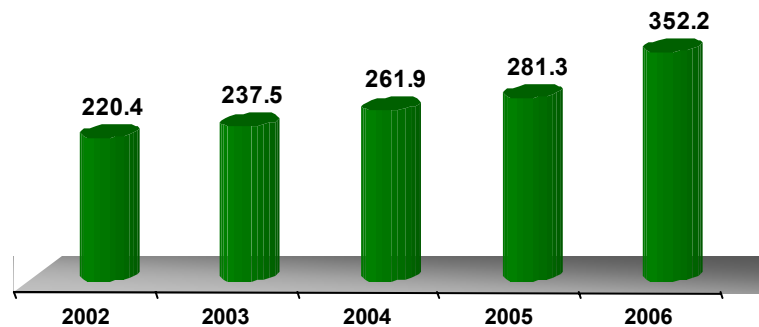
The table below presents the main data on economic and financial performance.

Description	2006		2005		HA %
	R\$ 000	VA %	R\$ 000	VA %	
Gross Revenue	352,202	111.4	281,306	111.1	25.2
Net Revenue	316,116	100.0	253,115	100.0	24.9
Gross Profit	115,344	36.5	98,838	39.0	16.7
Operating Expenses	100,081	31.7	87,246	34.5	14.7
Adjusted EBITDA	20,560	6.5	17,091	6.8	20.3
Net Financial Expenses	2,290	0.7	879,000	0.3	160.5
Net Income	6,662	2.1	6,072	2.4	9.7

## Gross revenue

Livraria' gross revenue totaled R\$ 352.2 million, up 25.2% in relation to 2005.

### Gross Revenue (R\$ million)



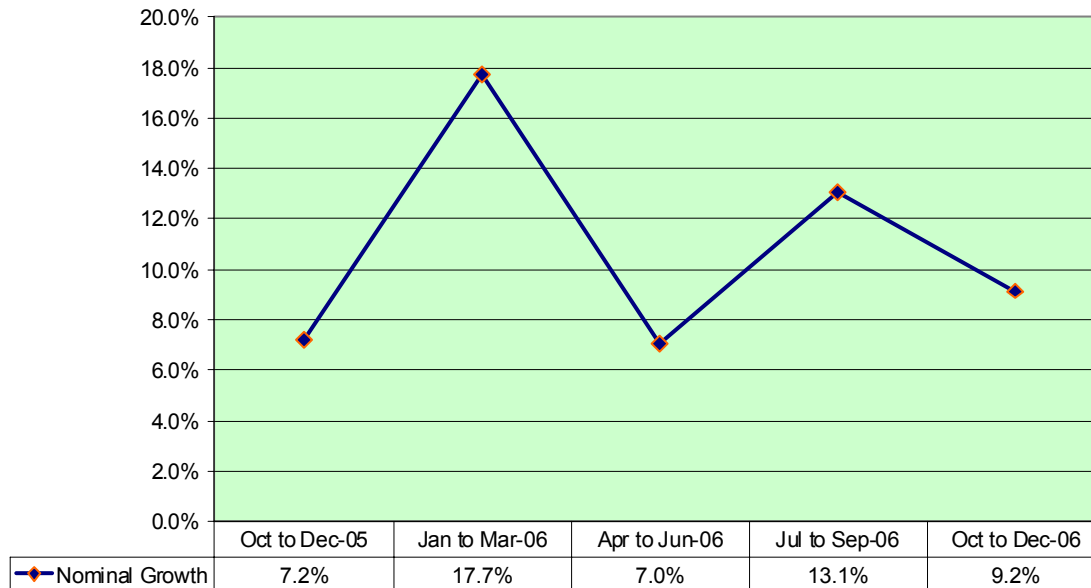
The sales growth was favored by the performance both in the electronic retail division (+52.5%) and in physical stores (+17.2%). The analysis of comparable sales (physical stores + Saravia.com) also showed positive performance, with growth of 21.1%. Comparable sales of physical stores only had a 11.8% increase.

Nominal growth in the book, newspaper, magazine and stationery sector, released by the Brazilian Institute of Geography and Statistics (IBGE) in the monthly survey of commerce revealed growth of 5.6% in 2006, lower than Saraiva's growth in these segments, which reached 13.7% and demonstrates the gain in market share.

The sales growth obtained in 2006 is the result of a set of actions adopted beginning in 2005. New product categories were added to the sales mix, notably the areas of computers, electric-electronic products, and imported books, which together accounted for 12.4% of the Company's total sales. In addition, marketing investments were remodeled and intensified, including the creation of the successful loyalty program "Saraiva Plus", and the lengthening of payment terms offered to customers. Further, investments were reinforced in personnel selection and training, in order to adjust the profile of store attendants to each unit's target public.

The graph below shows the evolution of comparable physical store sales, analyzing the growth in quarterly revenue from the same period of the prior year.

### Nominal growth of comparable stores - by quarter



### Gross Profit

Gross profit totaled R\$ 115.3 million, up 16.7% from the result obtained in the prior year. The gross margin declined from 39.0% in 2005 to 36.5%, due to the greater share of the computer and electric-electronic product categories in the sales mix. As planned by management, the introduction of these segments added important value to the growth in gross profit in absolute amounts, even though they are products with lower margins than books.

With the rapid growth observed in these categories' sales volume, Saraiva has already begun to have greater clout with suppliers, providing opportunities to intensify partnerships and possibly increase sales margins.

### Income from Operations

As a result of rationalization actions, conducted based on the cash management programs developed in recent years, and the gains of scale obtained with the significant increase in sales, the ratio of operating expenses to net revenue had a significant drop, as can be seen below.

% Ratio of Operating expenses to Net Revenue	2003	2004	2005	2006
	37.9%	37.7%	34.5%	31.7%

The measures adopted in the cash management program in 2006 provided estimated annual savings of R\$ 1.5 million. The Company's management understands that effective control of costs is essential to gain competitive capacity in high-competition segments. With this purpose, other measures are under analysis, and the implementation of another cash management program is scheduled for 2007 for operating performance to continue being improved.

## EBITDA

Adjusted EBITDA reached R\$ 20.6 million, corresponding to a 20.3% increase in relation to the prior year. The adjusted EBITDA margin went from 6.8% to 6.5%.

Reconciliation of EBITDA - R\$ 000	2006	2005	Chg.
Income from Operations after Net Financial Expenses	11,746	10,239	14.7%
(+) Depreciation and Amortization	4,950	4,865	1.7%
(+) Net Financial Expense	2,290	879	160.5%
(=) EBITDA	18,986	15,983	18.8%
(+) Provision for Saraiva Plus Bonus Points Redemption (1)	1,574	1,108	42.1%
(=) Adjusted EBITDA	20,560	17,091	20.3%

(1) Refers to provision related to future redemption of bonus. No represents actual cash flow.

## Financial Income (Expenses)/Capital Structure

Net financial expenses increased from R\$ 0.9 million in 2005 to R\$ 2.3 million in 2006. The financial position, at the end of 2006, was equivalent to a net cash of R\$ 6.4 million, compared to R\$ 8.1 million at the end of 2005.

Within the strategy designed to increase sales and average ticket, a tool that has proven to be effective is offering differentiated conditions to customers, increasing payment terms. As expected, this measure also led to the variation observed in financial income (expenses) and the net financial position.

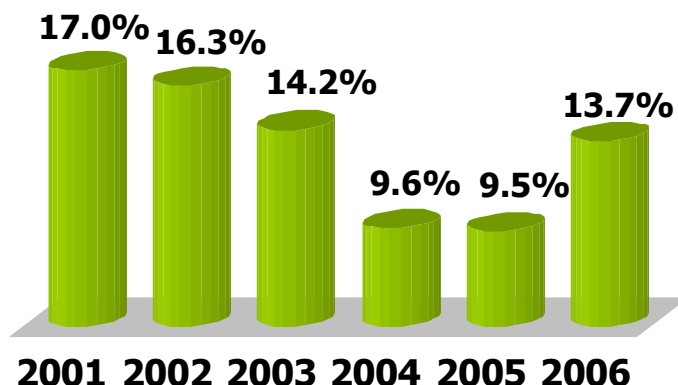
In order to optimize the capital structure to finance new investments, Livraria obtained BNDES financing in the amount of R\$ 22.1 million, intended for the physical store chain expansion project (underway) in the period from 2005 to 2008, and the project to renovate and modernize some important units of the chain. The first release of funds occurred in December 2006, in the amount of R\$ 4.4 million.

## Working Capital

In recent years the Company has invested heavily in gaining efficiency in working capital management. Efforts were made to improve logistics, better adapt each store's product mix, and renegotiate and intensify partnerships with suppliers. This work has yielded fruits that have allowed for adopting a more aggressive policy in the collection period, as part of a set of measures that are providing significant gains in market share.

The graph below shows the evolution of the ratio of working capital invested to gross revenue in recent years. After several years of significant gains, the result for 2006 received the impact of the new policy on average payment terms granted to customers, which was extended by 18 days, compared to the prior year. The Company's management understands that there are opportunities for new gains in inventory turnover, which may support with even greater efficiency the strategy of financing sales to customers.

### Working Capital (1)/Gross Revenue (2)



- (1) Inventories + Trade accounts receivable - Trade accounts payable (monthly average for the last 12 months)  
(2) Gross revenue from sales in the last 12 months

### Net Income

Net income reached R\$ 6.7 million, rising 9.7% in relation to the prior year.

### Marketing/Partnerships

The year 2006 was marked by major events in the area of marketing, and partnership agreements signed, as described below:

- The consolidation of the “Saraiva Plus” loyalty program as a major tool in attracting and retaining customers. The membership base grew 124%, and at the end of December 2006 had 1,146 thousand members.
- In line with the history of pioneering spirit in its business, a partnership agreement was signed with Starbucks, the world’s leading brand in specialty coffee retail. In December 2006, one of the first two Starbucks stores in Brazil was opened inside Saraiva Mega Store at Shopping Morumbi, in São Paulo.
- Holding of over 2 thousand cultural events in the chain of stores, among book, CD and DVD launches, live sets, roundtable sessions, mini-courses, debates and children’s activities, which represented a 110% increase in relation to the quantity of events in the prior year and contributed to attracting greater flow of people to stores.
- Contracting of the advertising agency Taterka, which became responsible for organizing communication with customers and adding to the visual identity of stores and the web site.
- Launch of the magazine “Almanaque”. With a monthly average press run of 70 thousand copies, this publication highlights Saraiva’s main events, in addition to the most important publishing, music and movie launches.
- Expansion of the partnership with Ticketmaster, the world’s leader in the sale of tickets for concerts and events. Ticketmaster is currently present in five Saraiva stores, which reinforces the Company’s vision of offering the latest in entertainment, culture and convenience.

## Saraiva.com - Livraria Saraiva's Electronic Retail Division

Brazilian electronic commerce continues growing at exuberant rates (the quantity of people buying over the Internet grew 46%) and Saraiva has actively participated in this process. The gain of scale obtained in 2006 was significant.

Indicators - Saraiva.com	2006	2005	Chg.
Gross Revenue (R\$000)	97,349	63,826	52.5%
Operating Expenses (SG&A)	19,307	14,228	35.7%
Adjusted EBITDA (R\$000) (1)	10,901	8,787	24.1%
Active Customers (000) (2)	941	851	10.5%
% of Gross Sales - Livraria	27.6%	22.7%	21.8%
Average Ticket (R\$)	111.93	81.03	38.1%

(1) Adjusted EBITDA: includes in calculation the provision for future redemption of "Saraiva Plus" bonus (R\$ 256 thousand in 2006 and R\$ 252 thousand in 2005), which does not represent cash outflow

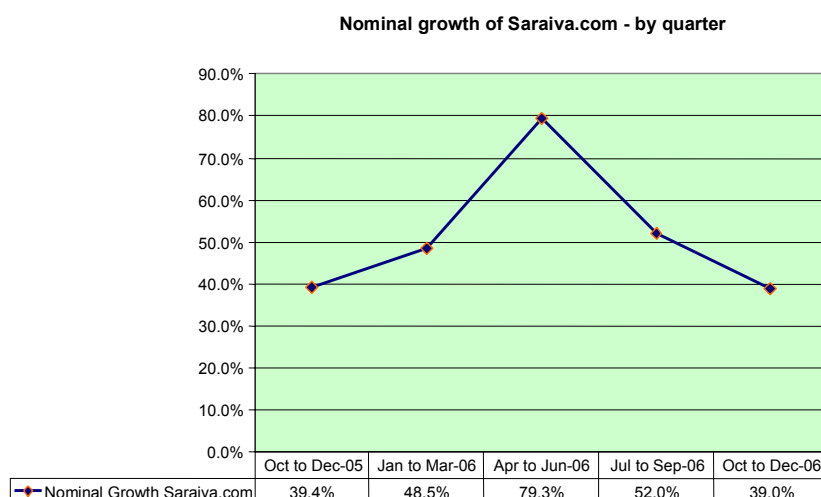
(2) Active customers: users who have made at least one purchase per year in the last two years

The strategy of expanding product categories, begun in the second half of 2005 and intensified over the course of 2006, has significantly contributed to sales growth, notably the areas of computers, electric-electronic products and imported books. Together, these segments account for 23.6% of the web site's total sales in 2006, compared to 7.6% in 2005. There are currently over 1.5 million registered as available for sale.

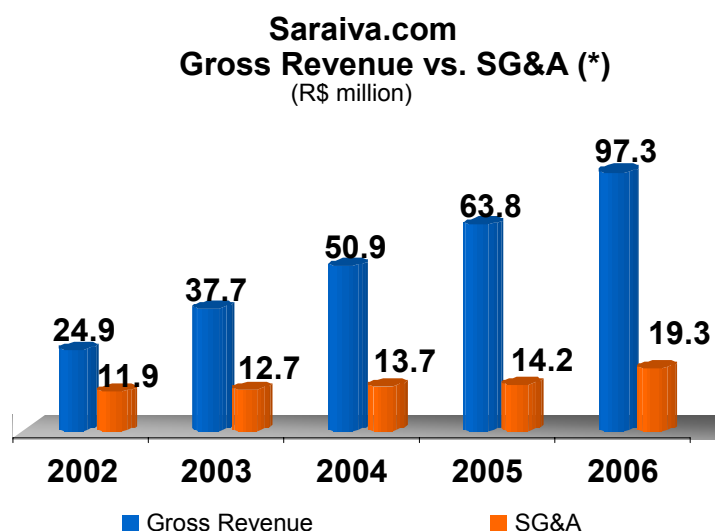
Another important action adopted in 2006 was the strategy of operating with emphasis on the textbook segment, benefiting from Saraiva's recognition as the most complete bookstore, especially during the back-to-school season. The Company's management will make efforts to intensify this action beginning in 2007.

Along with the aforementioned factors, the increase in the customer base and expansion of marketing actions, including the increase in partnerships with the main search sites, led to a 38.1% increase in the average ticket and contributed to the 52.5% increase in gross revenue.

The graph below shows the quarterly evolution of sales growth compared to the same quarter of the prior year.



The graph below clearly shows the gains of scale obtained with the increase in operations in recent years.



(\*) Selling, General and Administrative Expenses

In August 2006, Saraiva.com was classified as a “Diamond” company (the highest possible) in a service quality and excellence evaluation, conducted by the company *e-bit*, specialized in the Internet.

## CONSOLIDATED

The table below presents the main data on consolidated economic and financial performance.

R\$ 000	2006	2005	Chg.
Gross Revenue	587,290	505,623	16.2%
Net Revenue	550,941	477,246	15.4%
Gross Profit	282,978	260,407	8.7%
<b>Gross Margin</b>	<b>51.4%</b>	<b>54.6%</b>	
Income from Operations (EBIT) (a)	63,772	65,477	-2.6%
<b>Operating Margin</b>	<b>11.6%</b>	<b>13.7%</b>	
Financial Expenses, Net	(13)	(4,347)	-99.7%
Net Income	46,469	40,025	16.1%
<b>Net Margin</b>	<b>8.4%</b>	<b>8.4%</b>	
Adjusted EBITDA (b)	77,786	77,441	0.4%
<b>EBITDA Margin</b>	<b>14.1%</b>	<b>16.2%</b>	
Total Assets	425,744	290,506	46.6%
Shareholders' Equity	231,436	132,955	74.1%
Cash (Indebtedness), Net	84,147	6,069	1,286.5%

(a) Earnings before interest and taxes

(b) Earnings before interest, taxes, depreciation and amortizations, adjusted for extraordinary expenses and provision for redemption of "Saraiva Plus" bonus

## Mix of Consolidated Gross Revenue



### Gross Revenue

Consolidated gross revenue from sales totaled R\$ 587.3 million, growing 16.2% in relation to 2005, mainly reflecting the increase in sales by Livraria Saraiva.

### Gross Profit

Consolidated gross profit reached R\$ 283.0 million, growing 8.7% from 2005. The consolidated gross margin reflected Livraria's greater weighted share in the consolidated result, as well as the lower margins observed in Editora and Livraria, going from 54.6% in 2005 to 51.4% in 2006.

### Income from Operations

Income from operations before financial income (expenses) (EBIT) totaled R\$ 63.8 million in 2006, compared to R\$ 65.6 million in the prior year.

### EBITDA

Adjusted EBITDA totaled R\$ 77.8 million, indicating a slight 0.4% rise in relation to the prior year. With Livraria's greater weighted share, the adjusted EBITDA margin went from 16.2% to 14.1%.

Reconciliation of EBITDA - R\$ 000	2006	2005	Chg.
Income from Operations after Net Financial Expenses	63,759	61,130	4.3%
(+) Depreciation and Amortization	10,034	10,856	7.6%
(+) Net Financial Expense	13	4,347	-99.7%
(=) EBITDA	73,806	76,333	-3.3%
(+) Adjustments (1)	3,980	1,108	259.2%
(=) Adjusted EBITDA	77,786	77,441	0.4%

(1) In 2006: provision for redemption of "Saraiva Plus" bonus, provision for terminations with shut-down of printing unit and administrative expenses related to public offering. In 2005: provision for redemption of "Saraiva Plus" bonus.

## **Financial Income (Expenses)**

Consolidated net financial expenses had a significant decrease of approximately R\$ 4.3 million, due to the rise observed in Editora's financial income arising from capital increase that provided for a major increase in the cash position.

## **Net Income**

Consolidated net income reached record levels for the third consecutive year: totaling R\$ 46.5 million and surpassing that for 2005 by 16.1%. The final result was favored by Livraria's growth, the improvement in Editora's financial income (expenses) and the nonoperating income (expenses) obtained on the shut-down of the printing unit.

## **CAPITAL STRUCTURE**

The consolidated financial position, reflecting the operating cash flow and net inflow of R\$ 63.6 million related to funds from the capital increase, evolved from net cash of R\$ 6.1 million at the end of 2005 to R\$ 84.1 million at the end of 2006.

The last installment of the financing from the IFC was paid in June 2006, allowing for zeroing out the Company's financial liabilities in foreign currency.

In line with the strategy of adapting the capital structure to meet the necessary investment project for continued sustainable growth, the Company has signed major partnership agreements to obtain long-term BNDES financing, both by Editora and Livraria. In consolidated terms, R\$ 15.8 million was released over 2006.

## **INVESTMENTS/SUBSEQUENT EVENTS**

In 2006, R\$ 6.6 million was invested to carry out projects with expected return higher than the Company's cost of capital.

In **Editora**, R\$ 1.5 million was invested, mainly in information technology projects.

Both in the decision to make new investments and in the monitoring of the carrying-out of those already made, the Company's management conducts evaluations supported by concepts of the value-based management system, using GVA® methodology (shareholder value management).

Based on the evaluation that the technological update of the Company-owned printing unit would require high investments, and considering that the Brazilian printing infrastructure is quite modernized and has been greatly expanded in recent years, the Company's management decided, at the end of 2006, to shut down the Company-owned printing unit (carried out at the end of January 2007), with the sale of all its equipment.

In **Livraria**, R\$ 5.1 million was invested, notably in two of the five stores already scheduled to be opened in the first half of 2007, according to the plan to expand the chain of stores:

- Store located in Norte Shopping in the city of Rio de Janeiro, with 620 m<sup>2</sup> of sales area and opened in January 2007;
- Store located in the building of the college IBMEC, in the city of Rio de Janeiro, with a total area of 200 m<sup>2</sup>, opened at the end of February 2007;
- Renovation of the Mega Store located at Shopping Morumbi, in São Paulo, adapting the store's space to include the Starbucks, and aligning it with the new concept of Mega Store developed by management, which exploits product categories supplementing books;
- Closing of the unit in the traditional format, located in Shopping West Plaza, since the store's future outlook does not indicate potential for generating value.

With the opening of another two stores in Rio de Janeiro, Saraiva totals eight units in that city, and consolidates its leading position in this important consumer market. In addition to these stores opened in early 2007, another three units will be opened in the first half of 2007, at privileged locations in the cities of Florianópolis (Shopping Iguatemi) and Salvador (Shopping Salvador), in addition to a store in inland São Paulo State.

## CAPITAL MARKET

We present below a summary of the changes in Saraiva's shares over the last two years.

INDICATORS	2006	2005	Chg.
Number of Trades <sup>(1)</sup>	28,164	1,724	1,533.6%
Participation in Trading Sessions - % <sup>(1)</sup>	100.0	76.7	23.3 p.p.
Quantity Traded - thousand shares <sup>(1)</sup>	20,314	4,957	309.8%
Volume Traded - R\$ 000 <sup>(1)</sup>	410,861	63,289	549.2%
Share Price - R\$ <sup>(1)</sup> <sup>(2)</sup>	23.90	17.20	39.0%
Total Shares Outstanding - 000 <sup>(2)</sup> <sup>(3)</sup>	28,230	22,937	23.1%
<b>Market Value - R\$ million <sup>(2)</sup></b>	<b>674.7</b>	<b>394.5</b>	<b>71.0%</b>

Source: Bovespa

<sup>(1)</sup> Referring to preferred shares (SLED4)

<sup>(2)</sup> At end of year

<sup>(3)</sup> There was a bonus of 2,326,920 preferred shares on 1/6/06, pursuant to decision in Extraordinary Shareholders' Meeting. 3,000,000 preferred shares were issued in April 2006.

The initiatives developed by Saraiva in the capital market, during 2006, have improved good practices of corporate governance even more and promoted strong growth in liquidity of the Company's shares:

- As decided in the Extraordinary Shareholders' Meeting held on January 6, 2006, a bonus was approved, attributing 2,326,920 preferred shares to the holders of common and/or preferred shares, in the proportion of 0.10 preferred share for every preferred or common share held;

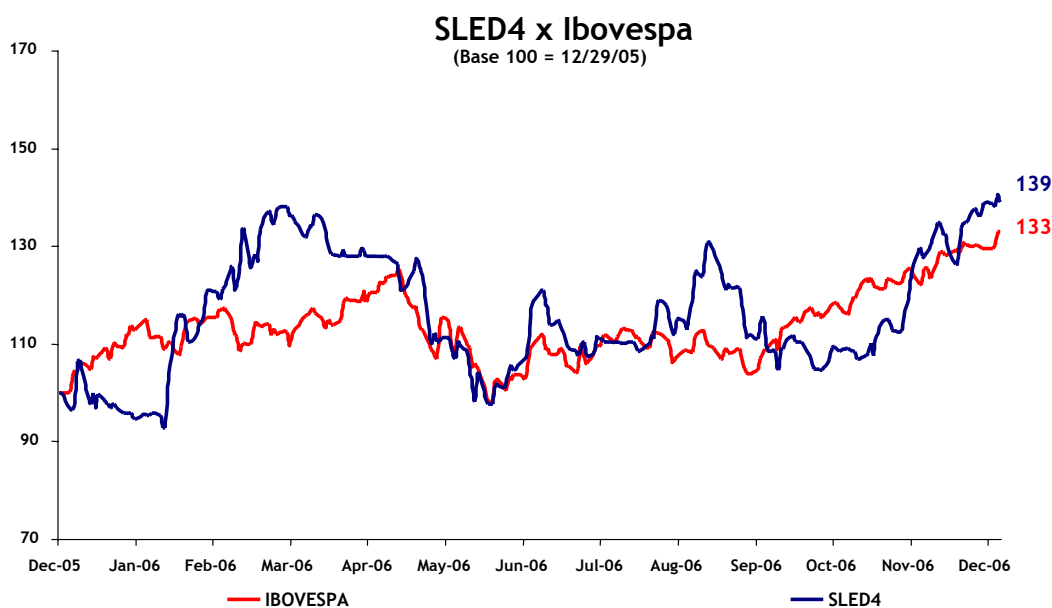
- Adhesion, in March 2006, to Bovespa's Level 2 Differentiated Corporate Governance Practices\*;
- Successful primary distribution, in April 2006, of 3 million preferred shares, strengthening the Company's financial position for the development of studies and implementation of investment projects;
- Secondary distribution of shares, also in April 2006, conducted by some preferred shareholders, which benefited the dilution of the investor base;

\* With the adhesion to Level 2, the Company, its shareholders, officers and members of the Fiscal Council assume the obligation to resolve, by means of arbitration, all conflicts established in the Commitment Clause contained in the bylaws, pursuant to the Regulation of the Bovespa Market Arbitration Chamber.

The fruits of the ongoing work by management to strengthen the relationship with the capital market have been visible over the course of the year, as described below:

- In September 2006 Saraiva became part of the "Brazil Index" (IBrX-100), composed of 100 shares selected among the most traded on Bovespa.
- Saraiva received Honorable Mention in two categories (best program and best investor relations executive in small & mid cap companies) of the awards granted by IBRI (Brazilian Investor Relations Institute) and *IR Magazine*, in association with PR Newswire and *Revista RI*, during IR Magazine Awards 2006 Brazil.
- Saraiva received the Association of Capital Market Investment Analysts and Professionals (Apimec) Assiduity Seal, granted to companies that continuously hold public meetings with investors.
- For the first time in its history, Saraiva's shares were traded in all of Bovespa's trading sessions.

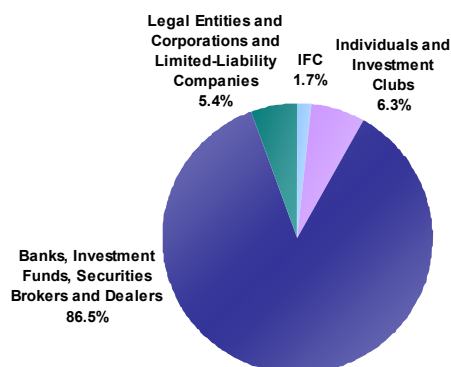
The appreciation of preferred shares (SLED4) reached 39.0%, surpassing Ibovespa's (32.9%).



## SHAREHOLDING STRUCTURE

Saraiva's subscribed and paid-up capital was R\$ 147,774,184.00 as of December 31, 2006, represented by 28,596,123 registered shares, without par value, of which 9,622,313 are common shares (ON) and 18,973,810 are preferred shares (PN).

COMPOSITION OF FREE FLOAT - SLED4  
(December 2006)



## PAYMENT TO SHAREHOLDERS

The Board of Directors, in a meeting held on February 28, 2007, approved the payment of R\$ 14.0 million (R\$ 0.49549281/share) to shareholders, in the form of interest on capital, already attributing this amount to mandatory minimum dividends. This amount is equivalent to 30.1% of income for the year and represents a dividend yield of 2.1% on the price of preferred shares as of 12/31/06.

## HUMAN RESOURCES

Consolidated headcount ended the year at 2,342, representing an additional 31 employees in relation to the prior year, due to the hiring of temporary employees to handle government programs for the 2007 school year.

Productivity indicated by the ratio of revenue to average employees evolved 17.9% and reached R\$ 252.4 thousand, in 2006.

The main fundamentals guiding the Company's human resources policies are the promotion of continuous learning and recognition, in order to create an environment that stimulates the development of skills and overcoming of challenges. With this focus, over the course of the year Saraiva invested in 482 activities, with 9,459 enrollments in 29 thousand hours of training.

## **SOCIAL RESPONSIBILITY**

It is Saraiva Group's philosophy to properly contribute to the quality of life of its employees and communities related with the Company. With this spirit, Saraiva has conducted various community action and solidarity campaigns, in addition to supporting and investing in the social activities of *Instituto Jorge Saraiva*, which works with social insertion of needy children.

Editora Saraiva has participated in the campaign promoted by *Itaú Criança* and donated 2 thousand children's books to *Pastoral da Criança*, and entity serving needy children with support from Unicef.

It is important to mention the plan developed for shutting down the printing unit, involving various support actions and outplacement of professionals - several professionals were invited to join the company that purchased the equipment.

## **INDEPENDENT AUDITORS**

In compliance with Brazilian Securities Commission (CVM) Instruction No. 381/2003, we inform that the current agreement with the independent auditors only entails external audit work.

## **SUBSEQUENT EVENT**

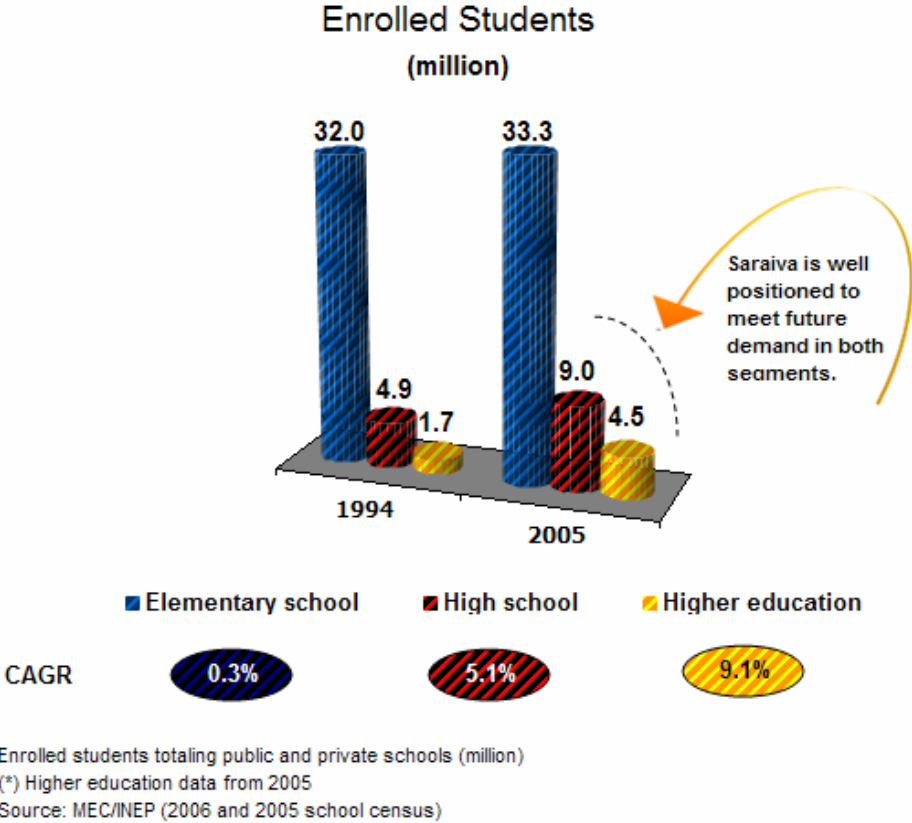
In line with the philosophy of aligning interests between the Company's officers and shareholders, the Saraiva's Stock Option Plan Management Committee approved, in a meeting held on March 5, 2007, based on a recommendation by the Board of Directors in a meeting held on February 28, 2007, the conditions and beneficiaries of the Third Program of this Plan, granting stock options of 123,800 preferred shares to officers and employees. The options will be exercised through issuance of new shares and/or sale of treasury shares held by the Company.

## **OUTLOOK**

Saraiva is strongly positioned to continue sustainable expansion of its business models, through organic growth of its activities and occasional opportunities for strategic opportunities both in the publishing segment and in retail.

Supported by a solid financial platform and the endless search for cost reductions and expansion of productivity, as well as the professional team’s excellence, the Company is mobilized to implement a consistent plan for growth and generation of value.

In **Editora**, the outlook expanded with the approval of Fundeb, which should significantly contribute to the advance of education quality in the medium and long terms. In addition, the regulation of the book purchasing program for public high school students is yet another major step for this segment to be served regularly and increasingly. The graph below shows the significant increase in the number of students over the last decade. Although there are still significant deficiencies in the quality of education, the investments that the government has made in education favor the scenario of growth potential for companies linked to education and culture and that are well structured and positioned to take advantage of the opportunities that should be generated.



Other factors that favor Editora’s outlook are the significant investments that have been made in the ongoing work of strengthening the relationship with teachers, renewing the catalog and attracting new authors. The forecast is to launch 261 titles (between new works and reformulated ones) over the course of 2007.

In **Livraria** the outlook is positive both for the expansion of the chain of physical stores and for the electronic commerce segment.

The project to accelerate organic growth includes the opening of 11 new stores between 2007 and 2008. The target consists of reaching a sales area 30% greater upon the conclusion of this expansion phase, which should provide for significant gains of scale and profitability.

The expectations of strong growth for electronic commerce remain present. According to the company *e-bit*, the number of electronic consumers grew 46% in 2006 alone, and several ingredients contribute to the popularization of this market. For 2007, *e-bit's* forecast is for Brazilian electronic commerce revenue to increase 45%. Saraiva successfully implemented new product categories in its electronic retail platform last year, and there are opportunities to expand the range of products offered even further, which favors the potential for generating value.

In parallel with this scenario, customer relationship actions will be improved, through the successful “Saraiva Plus” program and the intensification of partnerships that add even more value to Saraiva customers’ shopping experience.

## **ACKNOWLEDGEMENTS**

Saraiva remains optimistic about its business and the investments it has made in favor of education in Brazil. Our employees continue motivated and alert to new investment opportunities that may yield better returns for our shareholders. Finally, we thank all our shareholders, customers, suppliers, financial institutions, authors, employees and communities for the support given in 2006, without which we would not have achieved the excellent results obtained.

São Paulo, March 9, 2007

MANAGEMENT