

(Convenience Translation into English from the Original Previously Issued in Portuguese)

SARAIVA S.A. LIVREIROS EDITORES

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2005 AND 2004
(Amounts in thousands of Brazilian reais - R\$, unless otherwise stated)

1. OPERATIONS

Saraiva S.A. Livreiros Editores (the “Company”) is engaged in the publication of elementary and high school textbooks, supplementary textbooks, legal books and economics/management books.

The Company experiences seasonality in its business, with 80% of its sales concentrated at the first and last quarters of the year. This sales concentration is due to two factors: (a) the back-to-school period in the first quarter; and (b) the sale of elementary and high school textbooks to the government in the fourth and first quarters of the year.

2. PRESENTATION OF FINANCIAL STATEMENTS

The individual and consolidated financial statements have been prepared in accordance with Brazilian accounting practices, and standards established by the Brazilian Securities Commission (CVM).

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

3. SIGNIFICANT ACCOUNTING PRACTICES

a) General principles

Results of operations are determined on the accrual basis of accounting. Sales revenues and the corresponding costs are recorded upon the transfer of risks and benefits.

b) Current and long-term assets

- Temporary cash investments

Stated at cost plus income earned through the balance sheets dates.

- Allowance for doubtful accounts

Recorded in an amount considered sufficient to cover potential losses on the realization of trade accounts receivable. Uncollectible receivables are charged directly to income.

- Inventories

Stated at the lower of average acquisition or production cost or market.

- Other current and long-term assets

Stated at net realizable value.

c) Permanent assets

- Investments

Investment in subsidiary is accounted for under the equity method, and other investments are stated at cost, less a valuation allowance.

- Property, plant and equipment

Recorded at acquisition or construction cost, plus monetary restatement for inflation through December 31, 1995. Depreciation and amortization are computed under the straight-line method based on the useful lives of the assets.

- Deferred charges

Stated at cost, less amortization, and include unamortized goodwill, preoperating expenses associated with commercial assignment and expenses incurred prior to the start-up of new stores.

Preoperating expenses are amortized over five years or over the terms of the lease contracts, beginning upon the start-up of the stores.

The goodwill resulting from the acquisition of investments is based on the projected earnings capacity of the acquired businesses over the estimated period for return on investment and is amortized using the straight-line method in 60 monthly installments.

d) Current and long-term liabilities

- Copyrights

Recognized when sales are made and, in some cases, when publication rights are acquired. In the first case, copyrights are considered selling expenses and, in the second case, production cost.

- Other current and long-term liabilities

Stated at known or estimated amounts plus charges, monetary and/or exchange variations incurred through the balance sheet dates, if applicable.

e) Income and social contribution taxes

Taxes on net income (loss) include current and deferred amounts.

Income tax is calculated at the rate of 15% on taxable income plus a 10% surtax, and social contribution tax is calculated at the rate of 9% on taxable income.

Deferred income and social contribution taxes are recorded in current and long-term assets and in current and long-term liabilities, as stated in Note 13, to reflect future tax effects on temporary differences between the reported amounts of assets and liabilities and their tax bases, and tax loss carryforwards.

Deferred tax assets are based on expected future taxable income at the tax rates in effect at yearend, and are reviewed annually and adjusted to reflect any substantial change in expected profits.

f) Earnings per share

Computed based on the number of shares outstanding at the balance sheet dates.

4. CONSOLIDATED FINANCIAL STATEMENTS

The consolidated financial statements include the accounts of the Company and its subsidiary Livraria e Papelaria Saraiva S.A. in which the Company has a 99.91% equity ownership.

The consolidated financial statements have been prepared in accordance with Brazilian accounting practices and standards established by CVM, which comprise:

- Elimination of intercompany balances and transactions.
- Elimination of the Company's investment against the subsidiary's shareholders' equity.
- Minority interest in shareholders' equity and net income (loss) of the subsidiary is reported separately in the balance sheets and statements of income, respectively.

5. TRADE ACCOUNTS RECEIVABLE

	<u>Company</u>		<u>Consolidated</u>	
	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>
Trade accounts receivable	57,295	32,151	56,484	32,325
Credit cards	50	35	31,151	20,771
Checks receivable	3,356	3,623	4,288	4,958
Allowance for doubtful accounts	<u>(1,488)</u>	<u>(1,669)</u>	<u>(1,879)</u>	<u>(2,159)</u>
	<u>59,213</u>	<u>34,140</u>	<u>90,044</u>	<u>55,895</u>

6. INVENTORIES

	<u>Company</u>		<u>Consolidated</u>	
	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>
Finished products	33,514	39,774	33,514	39,774
Goods for resale	28	6	40,108	32,808
Work in process	18,697	17,786	18,697	17,786
Raw materials	9,814	7,724	9,814	7,724
Packing and consumption materials	<u>386</u>	<u>612</u>	<u>684</u>	<u>842</u>
	<u>62,439</u>	<u>65,902</u>	<u>102,817</u>	<u>98,934</u>

7. INVESTMENTS

	<u>Company</u>		<u>Consolidated</u>	
	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>
Investments in subsidiaries	52,644	46,578	-	-
Other investments	1,810	1,810	2,480	2,480
Valuation allowance	<u>(1,402)</u>	<u>(1,402)</u>	<u>(1,937)</u>	<u>(1,937)</u>
	<u>53,052</u>	<u>46,986</u>	<u>543</u>	<u>543</u>

Investments in subsidiaries refers to the equity interest in Livraria e Papelaria Saraiva S.A. and the main information is as follows:

	<u>2005</u>	<u>2004</u>
Number of shares - thousand	57,540	57,540
Number of shares held - thousand	57,490	57,490
Ownership interest - %	99.91	99.91
Capital	51,210	51,210
Shareholders' equity - R\$	52,690	46,618
Investment value - R\$	<u>52,644</u>	<u>46,578</u>
Net income (loss) - basis to calculate equity in subsidiary	6,072	(2,858)
Equity in subsidiary	<u>6,066</u>	<u>(2,855)</u>

The statements of operations of the subsidiary Livraria e Papelaria Saraiva S.A. for the years ended December 31, 2005 and 2004 are as follows:

	<u>2005</u>	<u>2004</u>
Gross sales	281,306	261,890
Deductions (ICMS, PIS and COFINS)	<u>(28,191)</u>	<u>(38,737)</u>
Net sales	253,115	223,153
Cost of sales	<u>(154,277)</u>	<u>(140,732)</u>
Gross profit	<u>98,838</u>	<u>82,421</u>
Operating expenses:		
Selling	68,444	65,213
Administrative	12,584	11,625
Management fees	1,353	1,101
Financial expenses	3,053	3,318
Financial income	(2,174)	(181)
Depreciation and amortization	4,865	6,107
Other expenses (income)	<u>474</u>	<u>(667)</u>
	<u>88,599</u>	<u>86,516</u>
Income (loss) from operations	10,239	(4,095)
Nonoperating expenses	<u>(194)</u>	<u>(107)</u>
Income (loss) before taxes on income	10,045	(4,202)
Income and social contribution taxes	<u>(3,299)</u>	<u>1,344</u>
Income (loss) before management profit sharing	6,746	(2,858)
Management profit sharing	<u>(674)</u>	<u>-</u>
Net income (loss)	<u>6,072</u>	<u>(2,858)</u>

8. PROPERTY, PLANT AND EQUIPMENT

	Annual depreciation rate - %	Company			
		2005		2004	
		<u>Cost</u>	<u>Depreciation</u>	<u>Net book value</u>	<u>Net book value</u>
Land	-	2,029	-	2,029	2,029
Buildings	4	8,172	(3,338)	4,834	5,127
Machinery and equipment	10	14,764	(11,903)	2,861	3,512
Furniture, fixtures and installations	10	21,503	(18,218)	3,285	3,919
Vehicles	20	3,649	(1,789)	1,860	1,527
Software and IT equipment	20	22,436	(15,598)	6,838	8,969
Advances to suppliers	-	336	-	336	293
Other	-	<u>606</u>	<u>-</u>	<u>606</u>	<u>600</u>
		<u>73,495</u>	<u>(50,846)</u>	<u>22,649</u>	<u>25,976</u>

	Annual depreciation rate - %	Consolidated			
		2005		2004	
		Cost	Depreciation	Net book value	Net book value
Land	-	2,032	-	2,032	2,032
Buildings	4	9,613	(3,910)	5,703	6,287
Machinery and equipment	10	15,051	(12,141)	2,910	3,587
Furniture, fixtures and installations	10	69,367	(53,317)	16,050	15,878
Vehicles	20	3,807	(1,908)	1,899	1,590
Software and IT equipment	20	33,862	(23,169)	10,693	12,961
Advances to suppliers	-	565	-	565	394
Other	-	1,219	-	1,219	1,224
		<u>135,516</u>	<u>(94,445)</u>	<u>41,071</u>	<u>43,953</u>

9. DEFERRED CHARGES

	Company		Consolidated	
	2005	2004	2005	2004
Preoperating expenses and other deferred charges	2,691	2,691	25,404	25,404
Unamortized goodwill	10,066	10,066	10,066	10,066
Accumulated amortization	(10,615)	(9,820)	(30,900)	(29,374)
	<u>2,142</u>	<u>2,937</u>	<u>4,570</u>	<u>6,096</u>

Due to the merger of the subsidiaries Editora Atual S.A., on August 2, 1999, and Formato Editorial Ltda., on February 3, 2004, the amounts of R\$7,931 and R\$2,135, respectively, were transferred to deferred charges. Goodwill is amortized under the straight-line method in 60 monthly installments, starting after the merger dates.

10. LOANS AND FINANCING

	<u>Company</u>		<u>Consolidated</u>	
	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>
Current:				
Loans:				
Bank overdraft facilities	-	4,807	-	4,807
BACEN Resolution No. 2,770	-	<u>31,268</u>	-	<u>31,268</u>
	-	36,075	-	36,075
Financing:				
In local currency - BNDES - FINEM	551	996	2,875	4,108
In foreign currency - IFC	<u>2,710</u>	<u>6,149</u>	<u>2,710</u>	<u>6,149</u>
	<u>3,261</u>	<u>43,220</u>	<u>5,585</u>	<u>46,332</u>
Long term-				
Financing:				
In local currency - BNDES - FINEM	7,510	502	8,591	3,775
In foreign currency - IFC	-	<u>3,063</u>	-	<u>3,063</u>
	<u>7,510</u>	<u>3,565</u>	<u>8,591</u>	<u>6,838</u>

BACEN - Banco Central do Brasil (Central Bank of Brazil).

BNDES - Banco Nacional de Desenvolvimento Econômico e Social (Brazilian National Bank for Economic and Social Development).

FINEM - Financiamento à Empresa (Enterprises Financing).

IFC - International Finance Corporation.

Maturities of long-term debt in 2005 are as follows:

	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>Total</u>
Company	<u>209</u>	<u>2,503</u>	<u>2,503</u>	<u>2,295</u>	<u>7,510</u>
Consolidated	<u>1,048</u>	<u>2,745</u>	<u>2,503</u>	<u>2,295</u>	<u>8,591</u>

The loans represented by an overdraft account, fully settled in 2005, were subject to interest calculated based on the CDI (Brazilian interbank deposit rate) variation.

Loans obtained pursuant to BACEN Resolution No. 2,770 represent onlending of funds raised abroad and were settled in January 2005. Annual interest was added to the principal, which was updated based on the U.S. dollar variation through the settlement date. Loans were hedged by interest rate swap transactions, equivalent to the CDI variation (see Note 16), and were collateralized by promissory notes.

The financing obtained by the Company from BNDES - FINEM is subject to annual interest of 3.5%, plus the Brazilian long-term interest rate (TJLP), and was used for the acquisition and implementation of an integrated business management system (ERP) and for the construction of a Distribution Center. Fixed assets items were pledged as collateral.

The financing obtained by the subsidiary Livraria e Papelaria Saraiva S.A., also from BNDES - FINEM and fully guaranteed by the Company, is subject to annual interest between 3% and 3.5%, plus the TJLP, and was allocated to investment in mega stores and the modernization of the subsidiary's conventional stores.

The financing obtained from IFC is subject to the U.S. dollar variation and annual interest of 3% above LIBOR. The agreement is free from any collateral, provided that, through its full settlement, expected for June 2006, the Company maintains its current interest in Livraria e Papelaria Saraiva S.A., and controlling shareholders hold, together, at least 50% of the Company's common voting shares. In addition, the agreement establishes compliance with performance indicators related to: (a) current ratio; (b) debt-asset ratio; and (c) interest coverage ratio. In the period, the Company had performance indicators in compliance with specific obligations provided for in the agreement. This financing was allocated to the investment in mega stores and the modernization of the subsidiary's conventional stores.

On November 1, 2005, the Company entered into a credit facility agreement with the BNDES whereby it raised funds in the amount of R\$32,500 to invest in the Publishing Plan for the period from 2005 to 2007 and in information systems to improve internal controls and management tools and to optimize sales efforts. The first portion, in the amount of R\$7,500, was released on December 16, 2005. The financing, collateralized by mortgaged land, buildings and equipment, whose net book value as of December 31, 2005 is R\$6,237, and bank guarantees, is subject to annual interest of 4% plus the TJLP, payable quarterly from November 2005 to November 2007, and monthly beginning in December 2007 with repayment of the principal.

11. LOYALTY PROGRAM - SARAIVA PLUS

The subsidiary Livraria e Papelaria Saraiva S.A. maintains a customer loyalty program ("Saraiva Plus") whereby purchases made by customers in stores and the Company's website earn points that can be discounted in future purchases. Accumulated points, net of redemptions, are accrued considering redemption estimates. As of December 31, 2005, the subsidiary has a provision for the loyalty program in the amount of R\$1,108, recorded under the caption "Other payables".

12. RELATED-PARTY TRANSACTIONS

Transactions with related parties include purchase and sale operations and loan agreements. Loans from the subsidiary Livraria e Papelaria Saraiva S.A. will be repaid in 2006, as stated in the loan agreement. The main balances and transactions with related parties are as follows:

	<u>2005</u>	<u>2004</u>
Balances:		
Current assets-		
Accounts receivable	1,041	16
Current liabilities-		
Loans	11,446	11,736
Transactions:		
Sales of products	9,174	8,212
Purchases of products	25	22
Financial expenses	629	-

13. DEFERRED INCOME AND SOCIAL CONTRIBUTION TAXES

Deferred income and social contribution taxes arise from:

	<u>Company</u>		<u>Consolidated</u>	
	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>
Current assets	<u>-</u>	<u>210</u>	<u>4,853</u>	<u>1,409</u>
Current liabilities (recorded in the caption "Taxes payable")	<u>18</u>	<u>-</u>	<u>18</u>	<u>-</u>
Long-term assets:				
Tax loss carryforwards	-	-	1,023	3,182
Tax credit on temporarily nondeductible item - reserve for contingencies	<u>651</u>	<u>495</u>	<u>5,660</u>	<u>5,371</u>
	<u>651</u>	<u>495</u>	<u>6,683</u>	<u>8,553</u>
Long-term liabilities:				
Allowance for losses on book inventories - Law No. 10,753/03	3,802	4,508	3,802	4,508
Deferral of accelerated depreciation	13	98	13	98
Unamortized goodwill - article 7 of Law No. 9,532/97	<u>-</u>	<u>165</u>	<u>-</u>	<u>165</u>
	<u>3,815</u>	<u>4,771</u>	<u>3,815</u>	<u>4,771</u>

The Company, based on the opinion of its outside lawyers, considered the tax incentive established by Law No. 10,753/03, as amended by Law No. 10,833/03, relating to the deductibility of the allowance for losses on inventories, as a temporary difference between the book and tax bases, recognizing the tax effect according to CVM Regulatory Instruction No. 371/02.

Based on the expectation of future taxable income and positive cash flows discounted to present value, pursuant to CVM Instruction No. 371/02, the Company and its subsidiary, Livraria e Papelaria Saraiva S.A., maintained in their financial statements the deferred tax asset.

Management considers the carrying amount of the Company's deferred tax assets from temporary differences realizable according to the final resolution of lawsuits.

Considering the final resolution of the lawsuits, the estimate of realization of the subsidiary's deferred tax asset is as follows:

	<u>Realization of deferred tax asset</u>	<u>Deferred tax asset</u>
Balance of deferred tax asset as of December 31, 2005	-	10,885
December 31, 2006	3,472	7,413
December 31, 2007	6,529	884
December 31, 2008	884	-

Reconciliation of the tax expense calculated by applying the combined tax rate and the tax expense charged to income is as follows:

	<u>Company</u>		<u>Consolidated</u>	
	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>
Income before taxes on income	46,853	17,894	50,831	16,549
Reversal of interest on capital	<u>10,129</u>	<u>9,351</u>	<u>10,129</u>	<u>9,351</u>
	56,982	27,245	60,960	25,900
Combined tax rate - %	34	34	34	34
Taxes computed at the combined tax rate	<u>(19,375)</u>	<u>(9,264)</u>	<u>(20,727)</u>	<u>(8,806)</u>
Permanent add-backs:				
Nondeductible expenses	(145)	(202)	(202)	(286)
Equity in subsidiary	-	(971)	-	-
Permanent deductions:				
Interest on capital	3,383	3,124	3,383	3,124
Other deductions	304	182	365	182
Equity in subsidiary	2,063	-	-	-
Other items	<u>196</u>	<u>115</u>	<u>308</u>	<u>113</u>
	<u>(13,574)</u>	<u>(7,016)</u>	<u>(16,873)</u>	<u>(5,673)</u>
Income and social contribution taxes:				
Current	(14,294)	(2,827)	(19,221)	(2,827)
Deferred	<u>720</u>	<u>(4,189)</u>	<u>2,348</u>	<u>(2,846)</u>
	<u>(13,574)</u>	<u>(7,016)</u>	<u>(16,873)</u>	<u>(5,673)</u>
Effective tax rate - %	<u>23.8</u>	<u>25.8</u>	<u>27.7</u>	<u>21.9</u>

14. RESERVE FOR CONTINGENCIES

The Company and its subsidiary Livraria e Papelaria Saraiva S.A. are challenging in court the constitutionality of federal taxes, such as PIS and COFINS (taxes on revenue), IR (income tax) and CSLL (social contribution tax). Escrow deposits were made for the PIS/COFINS lawsuits, which are recorded in a specific account in long-term assets. The residual contingent liability is composed of:

	<u>Company</u>		<u>Consolidated</u>	
	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>
PIS/COFINS - expansion of tax basis and rate increase	512	180	9,504	9,065
IR/CSLL - "Plano Real" (economic plan) - Law No. 8,880/94	<u>2,148</u>	<u>2,020</u>	<u>3,681</u>	<u>11,396</u>
	<u>2,660</u>	<u>2,200</u>	<u>13,185</u>	<u>20,461</u>

In view of the Federal Supreme Court's decision that acknowledged the constitutionality of the increase in COFINS rate established by Law No. 9,718/98, the Company, based on its legal counsel's opinion, reversed a portion of the recorded liability against the respective escrow deposits as of December 31, 2003. The subsidiary's COFINS lawsuit is still unresolved and the respective reserve for contingencies is maintained.

In October 2005, the subsidiary transferred to the caption "Taxes payable" part of the provision related to lawsuits challenging the IR/CSLL - "Plano Real", in the amount of R\$8,381 (R\$1,968 and R\$6,413, in current and long-term liabilities, respectively), on the basis of a petition for the payment in installments of the amounts due, filed with the Office of the National Treasury Attorney-General, and is awaiting the granting of the request for paying such debt in installments.

15. SHAREHOLDERS' EQUITY

a) Capital

A capital increase to R\$46,405 was approved at the Extraordinary Shareholders' Meeting on April 26, 2005, through the absorption of the profit reserve in the amount of R\$4,428, without any change in the number of shares.

Fully paid-up capital as of December 31, 2005 is R\$46,405, represented by 23,269,203 shares, of which 9,622,313 are common and 13,646,890 are preferred without par value. The Company is authorized to increase its capital by up to 10,000,000 shares through the issuance of new shares for subscription, regardless of amendment to bylaws.

Preferred shares cannot exceed 2/3 of total shares issued; are nonvoting, except in the circumstances specified by law or bylaws; are nonconvertible into common shares; and entitle their holders to: (a) special treatment in the event of sale of control of the Company, according to the terms of the bylaws; (b) dividends equal to those paid on common shares; and (c) share in the distribution of bonus shares resulting from capitalization of reserves, retained earnings and any other funds, under the same conditions as the holders of common shares.

Any change in preference, rights and advantages of preferred shares is subject to prior approval, or ratification, for a nonextendible term of one year, of the holders of more than a half of these shares at a special meeting.

All shares are entitled to a minimum dividend of 25% of adjusted net income for each year.

The remaining balance of retained earnings is prior to Law No. 6,404/76.

b) Treasury shares - CVM Instruction No. 10/80 and No. 298/97

According to bylaws, at the Board of Directors' Meeting held on September 22, 2005, the Company was authorized to purchase 500,000 of its own preferred shares to be held in treasury.

The Company has 332,500 preferred shares in treasury acquired for R\$2,870 and whose market value is R\$5,719 (R\$17.20 per share - price on December 29, 2005). No new share purchases were performed in the year ended December 31, 2005.

c) Interest on capital and dividends

In accordance with the Company's bylaws, interest on capital attributed to mandatory dividends will be net of income tax.

At the Board of Directors' Meeting held on February 21, 2006, the Board approved the payment of interest on capital to the shareholders in the amount of R\$10,129 (including withholding tax of R\$1,519), and the amount of R\$8,610 will be attributed to the mandatory dividends.

In addition to interest on capital, at the Annual Shareholders' Meeting management will propose the payment of dividends in the amount of R\$919 referring to 2005, totaling a payment to shareholders of R\$11,048 (R\$0.43788706 per share).

Mandatory dividends were calculated as follows:

Net income	40,025
Legal reserve	(2,001)
Prescribed dividends - reversal of unclaimed interest on capital	<u>91</u>
	<u>38,115</u>
Mandatory minimum dividends - 25%	<u><u>9,529</u></u>

Interest on capital was recorded, for tax purposes, as financial expenses and subsequently eliminated from the statement of income and recorded in shareholders' equity, according to CVM Resolution No. 207/96.

The effect on the calculation of the provision for income and social contribution taxes for the year was a reduction of R\$3,383 (R\$3,124 in 2004).

16. FINANCIAL INSTRUMENTS

a) Derivative transactions

The Company enters into transactions recorded in balance sheet accounts in order to meet its operating needs and hedge against risks of foreign currency and interest rate changes. These transactions are conducted with sound financial institutions and managed by the finance area by setting position and exposure limits and monitoring the risks involved.

Derivative transactions conducted by the Company in the year were as follows:

- Currency swap contracts to hedge the last three installment payments of the financing obtained from the IFC. The swap transactions, in the amount of US\$2,430,000, entered into in August 2004 and April 2005 and settled in June and December 2005, respectively, resulted in a loss of R\$1,280, recorded in financial expenses. The swap transaction in the amount of US\$1,160,000, entered into in September 2005 and maturing in June 2006, had a gain of R\$51 as of December 31, 2005, recorded as financial income as a corresponding entry to “Other receivables”.

The last installment of the agreement with the IFC, maturing in June 2006, amounts to US\$1,153,846, equivalent to R\$2,701.

- Interest rate swap contracts entered into in 2003 and 2004 and settled in January 2005 to hedge loans obtained pursuant to BACEN Resolution No. 2,770. Financial expenses recorded in the period were R\$70 (R\$2,354 in 2004), equivalent to the CDI variation.

The fair values of swap operations as of December 31, 2005 approximate carrying amounts.

b) Other financial instruments

The carrying amounts and fair values of the financial instruments recorded in the consolidated balance sheet as of December 31, 2005 are as follows:

	<u>Carrying amount</u>	<u>Fair value</u>
Cash and cash equivalents	20,194	20,194
Loans and financing:		
In local currency	11,466	11,176
In foreign currency	2,710	2,775

Criteria, assumptions and limitations used in calculating fair values:

- Cash and cash equivalents

Cash and cash equivalents are represented by demand bank deposits and temporary cash investments.

- Loans and financing

The carrying amounts of loans and financing refer mainly to financing from BNDES and IFC. The fair values of such financing do not differ significantly from the carrying amounts as of December 31, 2005.

- Limitations

The fair values were estimated at a specific time, based on relevant market information. Changes in assumptions may significantly affect those estimates.

c) Market risks

- Credit risk - In order to minimize possible losses on the default of their customers, the Company and its subsidiary adopt a strict credit granting policy, consisting of careful analyses of customer profile, as well as the timely monitoring of balances receivable.
- Risk of inventory obsolescence - product discontinuity and new technologies may lead to excess and obsolete inventories. In order to minimize these conditions, the Company and its subsidiary periodically monitor inventory levels and take the necessary action for its realization.

17. FINANCIAL INCOME (EXPENSES)

Financial income and expenses are comprised of:

	<u>Company</u>		<u>Consolidated</u>	
	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>
Financial expenses - operations under BACEN Resolution No. 2,770	70	2,354	70	2,354
Loss on temporary cash investments - hedge	1,280	1,105	1,280	1,105
Interest and monetary/exchange variation on loans and financing	(483)	269	141	1,234
Other interest and monetary variation	3,056	3,371	3,168	4,155
CPMF (tax on bank transactions)/IOC (exchange operations tax)	1,081	953	2,259	1,992
Other financial expenses	<u>498</u>	<u>410</u>	<u>1,008</u>	<u>939</u>
	<u>5,502</u>	<u>8,462</u>	<u>7,926</u>	<u>11,779</u>
Income from temporary cash investments	1,379	39	2,756	39
Gains on temporary cash investments - hedge	51	100	51	100
Interest on trade accounts receivable	449	495	476	514
Other financial income	<u>155</u>	<u>361</u>	<u>296</u>	<u>523</u>
	<u>2,034</u>	<u>995</u>	<u>3,579</u>	<u>1,176</u>

18. INSURANCE

As of December 31, 2005, the Company and its subsidiary had insurance coverage against fire and sundry risks for fixed assets and inventories, in amounts considered sufficient to cover potential losses.

19. SUBSEQUENT EVENTS

In the Extraordinary Shareholders' Meeting held on January 6, 2006, an increase of R\$35,369 in capital was approved, through the capitalization of capital and profit reserves. 2,326,920 preferred shares were granted as bonus shares to the holders of common and/or preferred shares in the proportion of 0.10 preferred shares for each common or preferred share held through the closing of the trading session at BOVESPA on January 6, 2006. As of that date, capital is represented by 25,596,123 shares, of which 25,230,373 are outstanding shares and 365,750 are treasury shares.

On February 10, 2006, the Company published a significant event notice disclosing its intention to request CVM registration of the primary and secondary distribution of shares in a public offering.
