ARACRUZ CELLULOSE S A
Form 20-F
March 31, 2008
20-F 1 f080331a.htm ANNUAL AND TRANSITION REPORT OF FOREIGN PRIVATE ISSUERS

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 20-F

o REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934

OR

x ANNUAL REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 for the Fiscal Year Ended December 31, 2007

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

OR

o SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

Date of event requiring this shell company report.

Commission File No. 1-11005

ARACRUZ CELULOSE S.A.

(Exact name of Registrant as specified in its charter)

Aracruz Cellulose

(Translation of Registrant s name into English)

Federative Republic of Brazil

(Jurisdiction of incorporation or organization)

Av. Brigadeiro Faria Lima, 2277, 4th floor
01452-000 São Paulo, SP, Brazil

(Address of principal executive offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act.

Title of each class:	Name of each exchange on which registered:
American Depositary Shares (as evidenced by American Depositary Receipts), each representing ten shares of Class B Stock	New York Stock Exchange

Securities registered or to be registered pursuant to Section 12(g) of the Act.

None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act.

None

Indicate the number of outstanding shares of each of the issuer s classes of capital or common stock as of the close of the period covered by the annual report.

455,390,699 Shares of Common Stock
27,958,116 Shares of Class A Stock
549,205,305 Shares of Class B Stock

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act

Yes o No x

If this report is an annual or transition report, indicated by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Securities Exchange Act of 1934.

Yes o No x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer.

Large accelerated filerx Accelerated filer o Non-accelerated filer o

Indicate by check mark which financial statement item the registrant has elected to follow.

Item 17 o Item 18 x

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

Please send copies of notices and communications from the Securities and Exchange Commission to:

Ross Kaufman
Greenberg Traurig LLP
Met Life Building
200 Park Avenue
New York, NY 10166

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INTRODUCTION

Unless otherwise specified, all references in this annual report to:

- U.S. dollars, $ or US$ are to United States dollars;
- *reais*, *real* or R$ are to Brazil *reais*, the official currency of Brazil;
- Brazilian government are to the federal government of the Federative Republic of Brazil;
- consolidated financial statements are to the Consolidated Financial Statements of Aracruz Celulose S.A. as of December 31, 2006 and 2007 and, for the three years in the period ended December 31, 2007, the corresponding Report of Independent Registered Public Accounting Firm;
- the Company, Aracruz, we, us and our are to Aracruz Celulose S.A. and its consolidated subsidiaries (unless the context otherwise requires);
- our preferred shares and our common shares are to our authorized and outstanding preferred stock and common stock, respectively;
- Class A Stock and Class B Stock are to our non-voting preferred stock class A (*ações preferenciais classe A*) and non-voting preferred stock class B (*ações preferenciais classe B*), respectively, which together are referred to as the Preferred Shares; and
- tons are to metric tons of 1,000 kilograms each.
- "Taxa de Juros de Longo Prazo" is the Long-term Interest Rate or "*TJLP*".

As used in this annual report, one hectare equals approximately 2.471 acres, one kilogram equals approximately 2.2 pounds and one kilometer equals approximately 0.621 miles.

Unless otherwise indicated,

- all references in this annual report to percentages, tons and U.S. dollar or *real* amounts of pulp are to market pulp ; and
- amounts in *reais* stated at a particular date and followed by U.S. dollar equivalents have been converted using the *reais* to U.S. dollars commercial selling rate in effect on such date.

FORWARD-LOOKING STATEMENTS

This annual report contains statements which constitute forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended. Certain such forward-looking statements can be identified by the use of forward-looking terminology such as believe, expect , may , are expected to , expect, will allow , will continue , will likely result , should , would be , seek , appro project , estimate or anticipate, or similar expressions or the negative thereof or other variations thereof of comparable terminology, or by discussions of strategy, plans or intentions. In addition, all information included herein with respect to future operations, financial condition, financial performance or other financial or statistical matters constitute forward-looking statements. Those forward-looking statements are necessarily dependent on assumptions, data or methods that may be incorrect or imprecise and that may not be realized. Such statements appear in a number of places in this annual report, including, without limitation, the information set forth under the headings Item 3D. Risk Factors , Item 4B. Business Overview and Item 5. Operating and Financial Review and Prospects , and include statements regarding our intent, belief or current expectations or those of our directors or our executive officers with respect to:

- general economic, political and business conditions, both in Brazil and in our principal export markets,
- the declaration or payment of dividends,
- our direction and future operation,
- the implementation of our principal operating strategies, including our potential participation in acquisition or joint venture transactions or other investment opportunities,
- the implementation of our financing strategy and capital expenditure plans, or
- the factors or trends affecting the pulp and paper market (including its cyclical nature and our financial condition or results of operations).

Investors are cautioned that any such forward-looking statements are not guarantees of future performance and involve risks and uncertainties, and that actual results may differ materially from those in the forward-looking statements, as a result of various factors. We do not undertake, and specifically disclaim, any obligation to update any forward-looking statements, which speak only as of the date hereof.

We make statements in this annual report about our competitive position and market share in, and the market size of, the pulp industry. We have made these statements on the basis of statistics and other information from third-party sources that we believe are reliable. We derive this third-party information principally from reports published by the International Pulp Statistical Committee, which includes the American Forest Paper Association, the Canadian Pulp & Paper Association, the Finnish Forest Industry Federation and the Brazilian Pulp and Paper Association, or Bracelpa, and reports published by Hawkins Wright Ltd., or Hawkins Wright. Although we have no reason to believe that any of this information or these reports is inaccurate in any material respect, we have not independently verified the competitive position, market share, market size or market growth data provided by third parties or by industry or general publications.

PART I

ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not applicable.

ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

ITEM 3. KEY INFORMATION

A. Selected Financial Data

Our consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America, or U.S. GAAP. Because we exported substantially all of our production, and due to the fact that we operate in an industry that uses the U.S. dollar as its currency of reference and this is the currency in which cash is primarily generated and expended, representing the economic environment in which the Company conducts its operations, our management believes that the U.S. dollar is the Company's functional currency and the most appropriate currency in which to present our consolidated financial statements. Accordingly, we have been presenting our primary U.S. GAAP consolidated financial statements in U.S. dollars since 1994. For this purpose, amounts in Brazilian currency for all periods presented have been remeasured into U.S. dollars in accordance with the methodology set forth in Statement of Financial Accounting Standards No. 52, or SFAS 52.

Pursuant to SFAS 52 as it applies to us, non-monetary assets, including inventories, property, plant and equipment, accumulated depreciation and stockholders equity are remeasured at historical rates of exchange. Monetary assets and liabilities denominated in *reais* are remeasured at period-end rates. Export sales invoiced in currencies other than the U.S. dollar are remeasured at the applicable exchange rate on the date of sale. Cost of sales, depreciation and other expenses relating to assets remeasured at historical exchange rates are calculated based on the U.S. dollar values of such assets, and other statement of operations accounts are remeasured at the rate prevailing on the date of the charge or credit to income.

For certain purposes, such as providing reports to our Brazilian shareholders, filing financial statements with the Comissão de Valores Mobiliários, or CVM, the Brazilian securities commission, and determining dividend payments and other distributions and tax liabilities in Brazil, we have prepared and will continue to be required to prepare financial statements in accordance with the accounting practices adopted in Brazil. Our financial statements prepared in accordance with the Brazilian Corporate Law are not adjusted to account for the effects of inflation.

The following table presents our selected financial data as of the dates and for each of the periods indicated. Our U.S. GAAP consolidated financial statements as of December 31, 2006 and 2007 appear elsewhere herein, together with the reports of our Independent Registered Public Accounting Firm, Deloitte Touche Tohmatsu Auditores Independentes. The selected financial information at December 31, 2003, 2004 and 2005 have been derived from our U.S. GAAP consolidated financial statements, not included in this annual report. The selected financial data should be read in conjunction with Item 5. Operating and Financial Review and Prospects.

			For the year ended December 31,		
	2003	**2004**	**2005**	**2006**	**2007**
			(thousands of U.S. dollars, except number of shares and per share amounts)		
Statement of Operations Data					
Operating Revenues					
Domestic	$42,401	$66,083	$ 62,019	$ 77,431	$ 137,086
Export	1,056,498	1,256,648	1,469,646	1,845,026	2,007,017
Gross operating revenues	$ 1,098,899	$1,322,731	$ 1,531,665	$ 1,922,457	$ 2,144,103
Sales taxes and other deductions	(95,829)	(155,618)	(186,432)	(241,624)	(260,328)
Net operating revenues	$1,003,070	$1,167,113	$ 1,345,233	$ 1,680,833	$ 1,883,775
Operating costs and expenses					
Cost of sales	$592,555	$700,333	$783,578	$1,037,896	$1,190,957
Selling	38,617	53,850	64,430	74,005	78,832
Administrative	22,762	31,072	33,820	57,020	58,708
Other, net	41,962	25,208	16,313	12,514	(38,624)
Total operating costs and expenses	$695,896	$810,463	$898,141	$1,181,435	$1,289,873
Operating income	$307,174	$356,650	$447,092	$499,398	$593,902
Non-operating (income) expenses					
Financial income	(43,037)	(56,123)	(125,439)	(181,733)	(168,037)
Financing expense	108,209	119,976	137,276	149,719	100,864
Gain on currency remeasurement, net	(41,955)	(16,197)	(21,386)	(7,641)	(908)
Other, net	(129)	(76)	(778)	(7)	(61)
Total *Non-operating (income) expenses*	$23,088	$47,580	$(10,327)	$(39,662)	$(68,142)
Income before income taxes, minority interest and equity in results of affiliated companies	$284,086	$309,070	457,419	$539,060	$662,044
Income tax expense					
Current	$106,549	$42,746	$71,086	$30,754	$41,343
Deferred	22,567	27,510	1,142	38,740	155,969
Total income tax expense	$129,116	$70,256	$72,228	$69,494	$197,312
Minority interest	$(37)	$(9)	$(31)	$(544)	$(10,522)

Equity in results of affiliated companies	$(6,844)	$(11,568)	$(44,062)	$(13,705)	$(32,141)
Net income	$148,089	$227,237	$341,098	$455,317	$422,069
Basic and diluted earnings per share(1)					
Common Stock	0.14	0.21	0.31	0.42	0.39
Class A Preferred Stock	$0.15	$0.23	$0.34	$0.46	$0.43
Class B Preferred Stock	0.15	0.23	0.34	0.46	0.43
Dividends and interest on stockholders´					
equity per share					
Common Stock	0.10(2)	0.11(3),	0.05(5),	0.06(7),	0.08(9),
		0.08(4)	0.12(6)	0.13(8)	0.14(10)
Class A Preferred Stock	$0.11(2)	$0.12(3),	$0.06(5),	$0.07(7),	$0.08(9),
		$0.09(4)	$0.13(6)	$0.15(8)	$0.16(10)
Class B Preferred Stock	0.11(2)	0.12(3),	0.06(5),	0.07(7),	0.08(9),
		0.09(4)	0.13(6)	0.15(8)	0.16(10)
Weighted-average number of shares					
outstanding (thousands of shares)					
Common Stock	454,908	454,908	454,908	454,908	454,908
Class A Preferred Stock	39,819	38,074	38,022	38,015	36,933
Class B Preferred Stock	535,969	537,711	537,739	537,665	538,747
Total	1,030,696	1,030,693	1,030,669	1,030,588	1,030,588

(1) Holders of Class B Preferred Stock have no dividend preference. Holders of Class A Preferred Stock are entitled to an annual preferential dividend.

(2) Including the dividend declared on April 29, 2003. (3)Including the dividend declared on April 29, 2004.

(4)Including the interest on stockholders' equity declared on October 19, 2004 and November 16, 2004, respectively. The interest on stockholders equity was attributed to the Compulsory Dividend relating to the year 2004, which were declared on April 29, 2005. (5)Including the dividend declared on April 29, 2005.

(6)Including the interest on stockholders' equity declared on April 19, 2005, May 19, 2005, June 20, 2005 and December 20, 2005, respectively. The interest on stockholders equity was attributed to the Compulsory Dividend relating to the year 2005, which was declared on April 28, 2006.

(7)Including the dividend declared on April 28, 2006.

(8)Including the interest on stockholders' equity declared on March 23, 2006, June 20, 2006, September 19, 2006 and December 22, 2006, respectively. The interest on stockholders equity was attributed to the Compulsory Dividend relating to the year 2006, which was declared on April 24, 2007.

(9)Including the dividend declared on April 24, 2007.

(10)Including the interest on stockholders' equity declared on March 21, 2007, June 19, 2007, September 18, 2007 and December 21, 2007, respectively. The interest on stockholders equity was attributed to the Compulsory Dividend relating to the year 2007, which is to be declared by April 30, 2008.

			At December 31,		
	2003	**2004**	**2005**	**2006**	**2007**
			(thousands of U.S. dollars)		
Balance Sheet Data					
Cash and cash equivalents	$66,284	$36,474	$34,114	$48,414	$53,321
Short-term investments	285,991	412,110	521,613	531,229	439,940
Accounts receivables, net	223,048	208,336	253,306	285,795	361,603
Inventories	131,486	126,220	173,873	202,704	225,023
Other current assets	35,925	49,973	111,899	132,782	171,513
Property, plant and equipment, net	2,270,369	2,133,896	2,068,547	2,151,212	2,518,700

Investment in affiliated company	382,318	480,940	505,975	516,771	607,429
Other non-current assets	59,012	81,709	94,678	127,021	247,334
Total assets	$3,454,433	$3,529,658	$3,764,005	$3,995,928	$4,624,863
Short-term debt	392,088	152,934	292,018	89,787	96,768
Other current liabilities	121,591	121,872	193,147	197,032	230,951
Long-term debt	979,435	1,222,728	1,010,285	1,155,050	1,312,351
Other long-term liabilities	160,358	217,837	304,132	351,636	597,675
Share capital	909,473	909,473	909,122	909,122	1,410,490
Other stockholders' equity accounts	891,488	904,814	1,055,301	1,293,301	976,628
Total liabilities and stockholders' equity	3,454,433	3,529,658	3,764,005	3,995,928	4,624,863

Exchange Rates

The purchase and sale of foreign currency in Brazil is subject to governmental control. As of March 4th, 2005, the two then existing foreign exchange markets - the free rate foreign exchange market, also known as the commercial market; and the "floating" rate foreign exchange market - were unified to become one single foreign exchange market (the "Foreign Exchange Market"). Transactions in the Foreign Exchange Market are required to comply with the provisions set forth in the Resolution 3,265 and the regulations established by the Central Bank of Brazil.

The Foreign Exchange Market includes purchase and sale transactions of foreign currency and gold-based foreign exchange trades carried out by institutions authorized to operate on the Foreign Exchange Market by the Central Bank of Brazil. From March 1995 through January 1999, the Central Bank allowed the gradual devaluation of the *real* against the U.S. dollar, pursuant to an exchange rate policy that established a band within which the *real*/U.S. dollar exchange rate could fluctuate.

Responding to pressure on the *real*, on January 13, 1999, the Central Bank widened the foreign exchange rate band. Because the pressure on the *real* did not cease, on January 15, 1999, the Central Bank allowed the *real* to float freely. On December 31, 2007, the commercial selling rate was R$ 1.7713 per US$1.00. Since January, 1999 the real exchange rate has been having an erratic trend, where the exchange rate is determined by demand and supply currency flows.

The following table shows the commercial selling rate for U.S. dollars for the periods and dates indicated.

	Exchange Rate of R$ per US$			
Year ended December 31,	**Low**	**High**	**Average**(1)	**Year - End**
1999	1.2078	2.1647	1.8158	1.7890
2000	1.7234	1.9847	1.8295	1.9554
2001	1.9357	2.8007	2.3420	2.3204
2002	2.2709	3.9552	2.9309	3.5333
2003	2.8219	3.6623	3.0715	2.8892
2004	2.6544	3.2051	2.8639	2.6544
2005	2.1633	2.7621	2.4125	2.3407
2006	2.0586	2.3711	2.1771	2.1380
2007	1.7325	2.1556	1.9483	1.7713

Source: Central Bank, PTAX. PTAX is the average of the exchange rates negotiated in the commercial rate market on a given day.

(1) Represents the average of the daily exchange rates (PTAX) during the relevant period.

	Exchange Rate of R$ per US$	
	Low	**High**

Month Ended		
January 31, 2008	1,7414	1,8301
February 29, 2008	1,6715	1,7681
March 28, 2008	1,6700	1,7456

Source: Central Bank, PTAX. PTAX is the average of the exchange rates negotiated in the commercial rate market on a given day.

We usually pay cash dividends and make other cash distributions with respect to the Class B Stock in *reais*. Accordingly, exchange rate fluctuations may affect the U.S. dollar amounts received by holders of ADSs on conversion by the depositary of our ADSs, or the Depositary, of such distributions into U.S. dollars for payment to holders of ADSs. Since November 2006 Brazilian exporters are authorized, pursuant to the terms of Law 11,371, to keep a certain amount of their export revenues in foreign financial institutions and use such revenues to make investments and pay obligations of the exporter. The Company may, from time to time and at its convenience, use revenues kept abroad pursuant to Law 11,371 to pay dividends and any other cash distributions. For additional information, see Item 10D. Exchange Controls. For information on dividends, see Item 8A. Consolidated Statements and Other Financial Information Dividend Policy and Dividends.

B. Capitalization and Indebtedness

Not applicable.

C. Reasons for the Offer and Use of Proceeds

Not applicable.

D. Risk Factors

Risk Factors Relating to Brazil

Brazilian political and economic conditions have a direct impact on our business and the market price of our preferred shares and ADSs.

The Brazilian economy has been characterized by volatile economic cycles. In addition, the Brazilian government frequently, and occasionally drastically, intervenes in the Brazilian economy. The Brazilian government has often changed monetary, taxation, credit, tariff and other policies to influence the course of Brazil's economy. For example, the Brazilian government has the authority, when a serious imbalance in Brazil's balance of payments occurs, to impose restrictions on the remittance to foreign investors of the proceeds of their investments in Brazil, and on the conversion of Brazilian currency into foreign currencies. The Company's business, financial condition and results of operations may be adversely affected by changes in policy including tariffs, exchange controls and other matters, as well as factors such as:

- currency fluctuations,
- inflation,
- price instability,
- interest rates,
- tax policy, and
- other political, diplomatic, social and economic developments in or affecting Brazil.

Rapid changes in Brazilian political and economic conditions that have already occurred and that might continue will require the Company's continued emphasis on assessing the risks associated with its activities and adjusting its business and operating strategy. Future developments in Brazilian government policies or in the

Brazilian economy, over which the Company has no control, may reduce demand for the Company's products in Brazil, and adversely affect the Company's business, financial condition and results of operations.

Exchange rate instability may adversely affect our financial condition and results of operations and the market price of our preferred shares and ADSs.

Because a portion of our expenses and a significant portion of our assets and liabilities are denominated in *reais* and we have U.S. dollar-denominated revenues, debt and other liabilities, we may be adversely affected by foreign exchange rate volatility. See Selected Financial Data Exchange Rates.

Our operating cash expenses are substantially denominated in *reais* and will generally decrease, as expressed in U.S. dollars, as a result of any devaluation of the *real*. If the rate of Brazilian inflation increases more rapidly than the rate of appreciation of the U.S. dollar against the *real*, then, as expressed in U.S. dollars, our operating expenses may increase and (assuming constant U.S. dollar sales prices), our profit margins decrease. In addition, any significant devaluation of the *real* may produce exchange gains on unhedged debt denominated in *reais*.

In 2003, Brazil started a new cycle of Real appreciation relative to the U.S. dollar and the rate in that year was 18.2% . In 2004 the appreciation of the Real relative to the U.S. dollar was 8.1%, in 2005 the Real appreciated 11.8% and in 2006 the Real appreciated approximately 9.0% . In 2007 the appreciation of the Real relative to the U.S dollar was 17.2%, representing an accumulated appreciation of 49.7% since the beginning of 2003.

Inflation and certain governmental measures to control inflation may contribute significantly to economic uncertainty in Brazil and to heightened volatility in the Brazilian securities markets.

Brazil has historically experienced extremely high rates of inflation. Inflation itself, as well as certain governmental measures to combat inflation and public speculation about possible future measures, has had significant negative effects on the Brazilian economy in the past. The Company's cash operating expenses are substantially denominated in *reais* and tend to increase with Brazilian inflation because its suppliers and providers generally increase prices to reflect the depreciation of the value of the currency. As expressed in U.S. dollars, however, these increases are typically offset at least in part by the effect of the appreciation of the U.S. dollar against the *real*. If the rate of Brazilian inflation increases more rapidly than the rate of appreciation of the U.S. dollar, then, as expressed in U.S. dollars, operating expenses may increase and (assuming constant U.S. dollar sales prices) profit margins decrease. In addition, high inflation generally leads to higher domestic interest rates, and as a result the Company's costs of *real*-denominated debt may increase. See Item 5. Operating and Financial Review and Prospects Brazilian Economic Environment.

We may be impacted by governmental actions affecting the Brazilian markets and economy.

The Brazilian government has exercised and continues to exercise substantial influence over many aspects of the private sector. The Brazilian government, for example, could impose some restrictions for the export market, by creating export duties for any product, including our main source of revenues (market pulp), affecting the margins and the profitability of the exporting companies. In addition, the Brazilian government owns or controls many companies, including some of the largest in Brazil. For example, Banco Nacional de Desenvolvimento Econômico e Social BNDES, which is owned by the Brazilian government, indirectly owned approximately 12.5% of our common stock as of December 31, 2007 and has advanced approximately 30% of our total consolidated indebtedness as of such date. See Item 7B. Related Party Transactions. .

Developments in other emerging markets may adversely affect the market price of our preferred shares and ADSs

The Brazilian securities markets are, to varying degrees, influenced by economic and market conditions in other emerging market countries, especially those in Latin America. Although economic conditions are different in each country, investors' reaction to developments in one country can have an effect on the securities of issuers in other countries, including Brazil. Developments or conditions in other emerging market countries have, at times, significantly affected the availability of credit in the Brazilian economy and resulted in considerable outflows of funds and declines in the amount of foreign currency invested in Brazil.

Similar developments in the international financial markets, in the future, especially in Latin America, may adversely affect the Company's financial condition and its ability to raise capital when needed. There can be no assurance that the Brazilian securities markets will not continue to be affected negatively by events elsewhere, especially in emerging markets, or that such events will not adversely affect the value of the Company's preferred shares or ADS.

Risks Relating to our Preferred Shares and ADSs

Exchange controls and restrictions on remittances abroad may adversely affect holders of ADSs.

You may be adversely affected by the imposition of restrictions on the remittance to foreign investors of the proceeds of their investments in Brazil and the conversion of *reais* into foreign currencies. The Brazilian government imposed remittance restrictions for a number of months in 1989 and early 1990. These restrictions would hinder or prevent the conversion of dividends, distributions or the proceeds from any sale of our preferred shares into U.S. dollars and remitting the U.S. dollars abroad. We cannot ensure that the Brazilian government will not take similar measures in the future. See Item 10D. Exchange Controls. Holders of the ADSs could be adversely affected by delays in, or a refusal to grant, any required Brazilian governmental approval for conversion of *real* payments and remittances abroad in respect of the shares of Class B Stock underlying the ADSs. In such case, the Depositary will hold the *reais* it cannot convert for the account of the ADS holders who have not been paid.

Exchanging ADSs for the underlying Class B Stock may have unfavorable consequences.

The Brazilian custodian for our Class B Stock, or the Custodian, must obtain an electronic certificate of registration from the Central Bank to remit U.S. dollars abroad for payments of dividends, any other cash distributions, or upon the disposition of the shares and sales proceeds related thereto. If you decide to exchange your ADSs for the underlying Class B Stock, you will be entitled to continue to rely for five business days from the date of the exchange on the ADS Depositary s electronic certificate of registration. Thereafter, you may not be able to obtain and remit U.S. dollars abroad upon the disposition of the Class B Stock, or distributions relating to the Class B Stock, unless you obtain your own electronic certificate of registration pursuant to Resolution No. 2,689, of January 26, 2000, of the National Monetary Council, known as Resolution 2,689, which entitles foreign investors to buy and sell on the São Paulo stock exchange. If you do not obtain a certificate of registration under Resolution 2,689, you may not be able to obtain and remit abroad U.S. dollars or other foreign currencies upon the disposition of Class B Stock or distributions with respect thereto, and you will generally be subject to less favorable tax treatment on gains with respect to the Class B Stock. If you attempt to obtain your own electronic certificate of registration, you may incur expenses or suffer significant delays in the application process. Obtaining an electronic certificate of registration involves generating significant documentation, including completing and filing various electronic forms with the Central Bank and the *Comissão de Valores Mobiliários*, or the CVM. These expenses or delays could adversely impact your ability to remit dividends or distributions relating to the Class B Stock or the return of your capital outside of Brazil in a timely manner. If you decide to exchange your Class B Stock back into ADSs once you have registered your investment in the Class B Stock, you may deposit your Class B Stock with the Custodian and rely on the Depositary s certificate of registration, subject to certain conditions. See Item 10D. Exchange Controls. We cannot assure you that the Depositary s certificate of registration or any certificate of foreign capital registration obtained by you may not be affected by future legislative or other regulatory changes, or that additional Brazilian restrictions applicable to you, the disposition of the underlying Class B Stock or the repatriation of the proceeds from disposition could not be imposed in the future.

Since November 2006 Brazilian exporters are authorized, pursuant to the terms of Law 11,371, to keep a certain amount of their export revenues in foreign financial institutions and use such revenues to make investments and pay obligations of the exporter. The Company may, from time to time and at its convenience, use revenues kept abroad pursuant to Law 11,371 to pay dividends and any other cash distributions, thus avoiding procedures to remit U.S. dollars abroad.

The relative volatility and illiquidity of the Brazilian securities markets may adversely affect holders of ADSs.

Investments in securities, such as the Class B Stock or the ADSs, of issuers from emerging market countries including Brazil involve a higher degree of risk than investing in securities of issuers from more developed countries.

The Brazilian securities market is substantially smaller, less liquid, more concentrated and more volatile than major securities markets in the United States. These features may substantially limit holders ability to sell the preferred shares underlying the ADSs at a price and time at which holders wish to do so. The companies trading at the São Paulo Stock Exchange (*Bolsa de Valores de São Paulo*), or BOVESPA, the main Brazilian stock exchange, had a market capitalization of approximately US$ 1.399 billion as of December 31, 2007, and an average daily trading volume of approximately US$ 2.555 million in 2007. In comparison, the companies trading at NYSE had a market capitalization of US$ 27.1 trillion as of December 31, 2007, and an average daily trading volume of approximately US$ 119.2 billion for 2007.

There is also significantly greater concentration in the Brazilian securities market than in major securities markets in the United States. The ten largest companies in terms of market capitalization represented approximately 51% of the aggregate market capitalization of BOVESPA as of December 31, 2007. The top ten stocks in terms of trading volume accounted for approximately 50% of all shares traded on BOVESPA.

Because we are subject to specific rules and regulations as a Brazilian Company, holders of our ADSs have fewer and less well defined shareholders rights than investors in U.S. companies.

Our corporate affairs are governed by our by-laws and the Brazilian corporate law, which differ from the legal principles that would apply if we were incorporated in a jurisdiction in the United States, such as Delaware or New York, or in certain other jurisdictions outside Brazil. In addition, your rights or the rights of holders of the preferred shares under the Brazilian corporate law, to protect your, or their, interests relative to actions taken by our board of directors or by the holders of common shares may be fewer and less well defined than under the laws of other jurisdictions outside Brazil.

Although Brazilian law imposes restrictions on insider trading and price manipulation, the Brazilian securities markets are not as highly regulated and supervised as the securities markets in the United States or certain other jurisdictions. For example, certain provisions of the U.S. Sarbanes-Oxley Act of 2002 that apply to U.S. companies do not apply to us. In addition, rules and policies against self-dealing and regarding the preservation of shareholder interests may be less well developed and enforced in Brazil than in the United States, potentially disadvantaging holders of our preferred shares and ADSs. When compared to Delaware general corporation law, the Brazilian corporate law and practice have less detailed and less well established rules and judicial precedents relating to the review of management decisions under duty of care and duty of loyalty standards in the context of corporate restructurings, transactions with related parties and sale-of-business transactions. In addition, shareholders must hold 5% of the outstanding share capital of a corporation to have the necessary standing to bring shareholders derivative suits. Shareholders ordinarily do not have standing to bring a class action.

Also, in accordance with Brazilian corporate law and our by-laws, holders of our preferred shares, and therefore of our ADSs, are not entitled to vote at meetings of our shareholders except in limited circumstances. See Item 10B. Memorandum and Articles of Association.

You may not be able to exercise preemptive rights.

You may not be able to exercise the preemptive rights relating to the Class B Stock underlying the ADSs unless a registration statement under the Securities Act is effective with respect to those rights or an exemption from the registration requirements of the Securities Act is available. We are not obligated to file a registration statement with respect to the shares relating to these preemptive rights, and we cannot assure investors that we will file any such registration statement. Unless we file a registration statement or an exemption from registration applies, investors may receive only the net proceeds from the sale of their preemptive rights by the Depositary, or if the preemptive rights cannot be sold, they will be allowed to lapse.

We are incorporated under the laws of Brazil. All of our directors and executive officers, and the experts named in this annual report, reside outside the U.S. substantially all of our assets, and our directors' and officers' assets and such experts' assets are located outside the U.S.. As a result, it may not be possible for investors to effect service of process within the U.S. upon us or our directors, executive officers or such experts, or to enforce against them or us, judgments obtained in U.S. courts based upon the civil liability provisions of the federal securities laws of the U.S.. In addition, we have been advised by our Brazilian counsel, that there is doubt that the courts of Brazil will enforce against us, our officers, directors and experts named herein, judgments obtained in the U.S. based upon the civil liability provisions of the federal securities laws of the U.S.

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or will enter judgments in original actions brought in Brazilian courts based upon the federal securities laws of the U.S.

Risk Factors Relating to Aracruz and the Pulp Industry

The market prices for our products are cyclical.

The prices we are able to obtain for our pulp depend on prevailing world prices for market pulp. Worldwide pulp prices have historically been cyclical, subject to significant fluctuations over short periods of time, due to a number of factors, including:

- worldwide demand for pulp products,
- worldwide production capacity,
- the strategies adopted by major pulp producers, and
- the availability of substitutes for our products.

All of these factors are beyond our control. In 2004, the average list price for BEKP (North America delivered) was US$ 563/t. In 2005 the international environment was favorable, marked by continued Chinese economic growth and improved economic performance of the United

States, Europe and Japan. World demand for BEKP registered a growth of 9.5% in 2005. The price of most commodities increased, including pulp. The average list price for BEKP delivered to North America in 2005 was US$ 625/t, 11% above the 2004 level.

Price level analysis concluded that the highest prices (North America delivered US$ 625) of 2005 added approximately US$115 million in net revenue for that year compared to 2004, which average list price for BEKP (North America delivered) was US$ 563/t.

Due to its quality characteristic, eucalyptus is the fiber of choice for different paper & tissue producers thus explaining the growth of its demand in the last several years above average market growth. The average level of demand growth for eucalyptus has increased significantly since 2001, to 11% per year, from 7% previously. BEKP market pulp consumption growth is expected to have reached around 17% or 1,9 million tons, in 2007, comparing to a decline of 8% in northern hardwood and of 0,4% of southern hardwood in the same year. This strong demand permitted price increase implementation for BEKP throughout the whole year 2007 achieving an average of US$ 744/t (North America delivered), that is being the highest level since 1995. The average list price for BEKP delivered to North America in 2007 was 9% above the previous year.

Discounts from list prices are frequently granted by sellers to significant purchasers. The Company has long term supply contracts with various customers and no assurance can be given that the prices for pulp or paper will stabilize or not decline further in the future, or that demand for the Company's products will not decline in the future. As a result, no assurance can be given that the Company will be able to operate its production facilities in a profitable manner in the future. The Company's results of operations would be materially adversely affected if the price of its product were to decline significantly. See also Item 4B. Business Overview Market Overview.

We face significant competition, which may adversely affect our market share.

The pulp industry is highly competitive. In the international pulp markets we compete with larger competitors that have greater financial strength, higher production capacities and access to cheaper sources of capital.

In addition, most markets are served by several suppliers, often from different countries. Many factors influence our competitive position, including plant efficiencies and operating rates in relation to our competitors, and the availability, quality and cost of wood, energy, chemicals and labor. To the extent that pulp from other hardwoods can be substituted for the more expensive BEKP, we also compete with producers in the broader segment of the pulp market. Some of our competitors in this market have greater financial, marketing and other resources, larger customer bases and greater breadth of product offerings than we do. If we are unable

to remain competitive with these producers in the future, our market share may be adversely affected. See Item 4B. Business Overview Competition.

We may be adversely affected by the imposition and enforcement of more stringent environmental regulations that would require us to spend additional funds.

The Company is subject to stringent environmental laws and regulations in Brazil on the federal, state and local levels. Changes in environmental laws and regulations or changes in the policy of enforcement of existing environmental laws and regulations could adversely affect the Company. The Company's operations are supervised by governmental agencies that are responsible for the implementation of pollution control laws and policies. These agencies can take actions against the Company if it fails to comply with applicable environmental regulations. These actions can include the imposition of fines and revocation of licenses and concessions.

Although changes in laws and regulations apply only prospectively under Brazilian law, it is possible that the relevant legislatures and/or governmental agencies will impose additional regulations or seek a more stringent interpretation of existing laws and regulations that would require the Company to spend additional funds on environmental matters or limit the Company's ability to operate as it currently does. In addition, such actions by such governmental bodies could impose additional costs to be borne by the Company when it renews existing licenses or applies for new ones.

Actions by federal or state legislature or public prosecution offices may adversely affect our operations.

In September 2001, the legislature of the State of Espírito Santo, where we owned, on December 31, 2007, 171,441 hectares of forest and other land, passed a law temporarily restricting the plantation of eucalyptus forests for purposes of pulp production within the State. In June 2002, this law was declared to be unconstitutional by a provisional decision of the Brazilian Federal Supreme Court, and injunctive relief was granted in response to suits brought by the National Confederation of Industry and by the National Brazilian Confederation of Agriculture and Cattle Raising. The Company believes that such provisional decision will be upheld by the court s definitive decision on the merits. However, there can be no assurance that such definitive decision will be favorable to the Company or that similar laws will not be enacted that would impose a limitation or restriction on plantation of eucalyptus or that would affect our licenses or permits.

On March 13, 2002, the Espírito Santo legislative assembly created an investigating commission (*Comissão Parlamentar de Inquérito*) to investigate the legality of our permits and the acquisition of our properties, since we began our operations in Espírito Santo. As the procedures in the investigation were not concluded within the prescribed time period for such a type of investigation, the commission was terminated without issuing a final report. The Company is confident that all its permits and acquisition documents are strictly in accordance with all laws and regulations. However, we cannot be certain that a governmental entity will not initiate similar or other investigations in the future that would cause us to incur significant expense and divert management's attention.

In May 2003 the Human Rights Commission of the Brazilian House of Representatives (*Câmara dos Deputados*) created a Working Group to discuss the alleged violation of economic, social, cultural and environmental rights in the eucalyptus plantations in the State of Espírito Santo. Among other issues, several complaints involving the Company were discussed. Representatives of the Company participated in a Public Hearing and presented to the Commission extensive reports, information, evidence, technical studies and governmental and judicial decisions that demonstrate that the complaints were unjustified. The Working Group was terminated without issuing a final report. However, the Company cannot be certain that a governmental entity will not initiate similar or other investigations in the future that would cause the Company to incur significant expense and divert management's attention.

In the second quarter of 2007 a number of Non-Governmental Organizations (NOGs) and the Federal Public Prosecution Office in the State Rio Grande do Sul brought two Civil Public Suits (*Ações Civis Públicas*) questioning the validity of the procedures adopted by Fundação Estadual de Proteção Ambiental - FEPAM in issuing environmental licenses for eucalyptus plantations in that State. A provisional measure was initially granted, to determine that FEPAM ceases to issue environmental licenses for eucalyptus plantations, being the competence therefore transferred to Instituto Brasileiro de Meio Ambiente - IBAMA (Brazilian Environmental Institute). The provisional measure was suspended by the Federal Court of the 4th Region at the request of the

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Government of the State Rio Grande do Sul. The Company believes that such suspension will be confirmed by the court s definitive decision on the merits. However, there can be no assurance that such definitive decision will be favorable to the Company or that similar suits will not be brought in the future that would impose a limitation or restriction on plantation of eucalyptus or that would affect our licenses or permits.

If we are unable to manage potential problems and risks related to acquisitions and alliances, our business and growth prospects may suffer. Some of our competitors may be better positioned to acquire other pulp and paper businesses.

The Company, as part of its business strategy, made a major acquisition by purchasing Riocell and may acquire other businesses in Brazil or elsewhere. In addition, the Company has made a significant joint venture investment in Veracel and may enter into other similar arrangements or alliances with third parties. Our management is unable to predict whether or when any prospective acquisitions or alliances will occur, or the likelihood of a material transaction being completed on favorable terms and conditions. Our ability to continue to expand successfully through acquisitions or alliances depends on many factors, including the availability to identify acquisitions and negotiate, finance and close transactions. Acquisitions and similar joint ventures or other arrangements have significant risks:

- we could fail to successfully integrate the operations, services and products of any acquired company;
- we could fail to select the best partners or fail to effectively plan and manage any alliance strategy;
- the acquisitions could increase our costs;
- our management s attention could be diverted from other business concerns; and
- we could lose key employees of the acquired company.

Our failure to integrate any new businesses or manage our investment in Veracel or any new alliances successfully could adversely affect our business and financial performance. Furthermore, the world pulp industry is undergoing consolidation, and many companies compete for acquisition and alliance opportunities in our industry. Some of our competitors have greater financial and other resources than we do. This may reduce the likelihood that we will be successful in completing acquisitions and alliances necessary for the expansion of our business or cause such acquisition or alliances to be possible only on less favorable terms. In addition, any major acquisition we consider may be subject to regulatory approval. We may not be successful in obtaining required regulatory approvals on a timely basis or at all.

Any downgrade in our credit ratings could adversely affect the availability of new financing and increase our cost of capital.

In 2005 and during 2006, the risk rating agencies Moody's Investor Service (Moody's), Standard & Poor's and Fitch Ratings (Fitch) both assigned an indicative rating to the Company's foreign currency debt under foreign law. After the rating agencies' confirmation, Aracruz became one of the few companies in Brazil confirmed as investment grade in foreign currency debt from three of the most important rating agencies in the world - Moody's, Standard & Poor's and Fitch Ratings -, thus reducing the Company's average cost of capital.

During 2007 our rating improved, with Moody's raising theirs an additional notch, to Baa2, which is equivalent to the ratings assigned by Standard & Poor's and Fitch (BBB). However, if the ratings were to be downgraded by the rating agencies, our cost of capital would increase. Any downgrade could also negatively affect our business and the availability of future financing.

We are controlled by a few shareholders, what can cause impasse on certain decisions.

Approximately 96.5% of our voting stock is owned by four principal shareholders, who have the ability to control the election of our board of directors and our direction and future operations, including decisions regarding acquisitions and other business opportunities, the declaration of dividends in excess of the requirements under our by-laws and Brazilian corporate law, and the issuance of additional shares and other securities. See Item 7A. Major Shareholders.

Dependence on Few Customers and the Loss of any of them can Cause a Significant Impact over our Operations

The Company's marketing strategy is to develop long-term relationships with customers that will purchase the Company's production year after year. In 2007, the Company's three largest customers accounted for approximately 57% of its sales (by volume). See "Market Overview Markets and Customers". The Company believes that the loss of any of these customers would have a material adverse effect on the Company's results of operations.

ITEM 4. INFORMATION ON ARACRUZ

A. History and Development of Aracruz

We conduct our operations under our legal and commercial name, Aracruz Celulose S.A.. We are a corporation (*sociedade anônima*), with unlimited duration, organized under the laws of the Federative Republic of Brazil. As a Brazilian corporation, we operate under the provisions of the Brazilian corporate law. Our headquarters and main operating unit are located at Rodovia Aracruz - Barra do Riacho, Kilometer 25, Municipality of Aracruz, State of Espírito Santo, Brazil, and its telephone number is 55-27-3270-2122. Our principal office is located at Av. Brigadeiro Faria Lima, 2277, 4th floor, 01452-000 São Paulo, State of São Paulo, Brazil, and our telephone number is 55-11-3301-4111. Our agent for service of process in the United States is Greenberg Traurig, LLP, 200 Park Avenue, New York, NY 10166. We maintain an Internet website at www.aracruz.com.br. Information contained on our website is not part of, or incorporated by reference into, this annual report.

Barra do Riacho Unit

Aracruz Florestal S.A., or AFSA, our predecessor, was incorporated in 1967, for an unlimited duration, to plant eucalyptus forests. AFSA became a subsidiary of Aracruz in 1972 when Aracruz was incorporated, and on July 20, 1993, AFSA was merged into Aracruz.

We commenced pulp production operations in September 1978, using a single production line (***"Fiberline A"***) with a nominal production capacity (i.e., the production capacity for which the mill was designed) of approximately 400,000 tons of pulp per year. In early 1991, we completed an expansion plan, known as the 1991 Expansion Project, which added a second production line (***"Fiberline B"***). This increased the nominal capacity of the Barra do Riacho Unit to approximately 1,025,000 tons per year. In 1994, we increased our effective production capacity to 1,070,000 tons through system upgrades and productivity gains. From October 1995 to December 1998, we implemented the Modernization Project, which increased the Barra do Riacho Unit nominal capacity to 1,240,000 tons per year, as well as our production efficiency.

We own 51% of Portocel Terminal Especializado de Barra do Riacho S.A., the company that operates the port terminal of Barra do Riacho, since January 1985. The remaining 49% of Portocel is owned by Celulose Nipo-Brasileira S.A - CENIBRA, another pulp manufacturer and one of our competitors. From the privatization of the port terminal in 1985 until 2007 Portocel increased its storage capacity from 45,000 to 217,000 tons.

In 1998 we acquired all ownership interests of Gutchess International Inc. in Tecflor Industrial S.A. (currently known as Aracruz Produtos de Madeira S.A., or APM), a joint venture between Gutchess International Inc. and Aracruz created in 1997 for the production of solid wood products. In October 2004 we sold two thirds of our shares in APM to Weyerhaeuser do Brasil Participações Ltda., a subsidiary of

Weyerhaeuser Corporation. APM s domestic sales policy remained unaltered and its overseas sales continued to be Weyerhaeuser s responsibility. We currently own one third of the shares of APM. See Business Overview Aracruz Produtos de Madeira.

In June 2000, our board of directors approved another expansion of the nominal production capacity of the Barra do Riacho Unit by 700,000 tons per year, known as the Fiberline C Expansion Project. The Fiberline C Expansion Project involved the addition of a new pulp line and certain other modifications to existing equipment at the Unit in order to further improve our cost-effectiveness. Construction began in the second semester of 2000, and the plant began operations at the end of May 2002, reaching full capacity in 2003. See Business Overview Fiberline C Expansion Project. The production volume resulting from the Fiberline C Expansion Project required an increase in the Company's forest base of approximately 65,200 hectares of eucalyptus plantations. To meet this demand, in June 2000, the Company acquired Terra Plana Agropecuária

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Ltda., with assets comprised of 19,000 hectares of land appropriate for planting eucalyptus trees. From July 2000 through December 31, 2001, the Company acquired approximately 44,000 additional hectares of land in a number of separate transactions. Additionally, in September 2002, Bahia Sul (currently denominated Suzano Papel e Celulose) and the Company signed, jointly with Companhia Vale do Rio Doce (now called Vale) and its wholly owned subsidiary, Florestas Rio Doce S/A, a contract for the acquisition of equal stakes by Bahia Sul and the Company of forest assets comprising approximately 40,000 hectares of lands and eucalyptus-planted forests. The Company also entered into a three-year wood supply contract with Veracel to provide a total of up to 3.85 million cubic meters of wood for the Fiberline C Expansion Project until the new plantations reach maturity for harvesting. This contract terminated in the first half of 2004. During 2004, we were able to meet approximately 62% of our wood fiber requirements from our own eucalyptus forests. In 2005, 2006 and 2007 we met approximately 90%, 91% and 86%, respectively, of our wood requirements from our own eucalyptus forests. In 2008 we expect to meet approximately 77% of our wood requirements from our own eucalyptus forests, due to the increase of wood coming from the Forestry Partners Program, according to our long term wood supply planning. See Business Overview Eucalyptus Forests .

Our board of directors approved in December 2005 another investment at the Barra do Riacho Unit known as Barra do Riacho Unit Optimization. The project was intended to improve the technology and performance in the pulp production process, introducing flexibility to adapt the pulp to different market requirements. These improvements are being made by modifying and/or replacing equipment at Fiberlines A, B and C, leading to a sustainable increase in nominal capacity of 200,000 tons/year. The plant investment was estimated at US$ 239 million, with US$ 199 million already spent up to 2007 and US$ 40 million expected for 2008, with 80% of the items produced domestically and 20% imported. The additional capacity of 200,000 tons/year should be attained until 2009.

Veracel

On October 10, 2000, we acquired a 45% stake in Veracel, a joint venture to grow eucalyptus trees on plantations and to build a pulp mill. On January 31, 2003, the Company acquired an additional 5% stake in Veracel, bringing its total stake to 50%. The remaining 50% interest in Veracel is owned by Stora Enso OYJ ("***Stora Enso***"). Veracel grows eucalyptus on plantations in the State of Bahia, which has diversified the sources of the Company's supply of wood for the Barra do Riacho Unit. This equity investment in Veracel achieved two objectives: (i) a guaranteed supply of wood for the Fiberline C Expansion Project during the first three years of the new production unit's operation and (ii) the opportunity to expand the Company's business in the future from an operational base in Bahia that can potentially replicate its accomplishments in the State of Espírito Santo. In May 2003, the Company and its joint venture partner decided to invest an additional US$940 million in Veracel to build a 900,000-ton capacity mill (the "***Veracel Mill***") for the production of BEKP in the State of Bahia. Construction of the Veracel Mill was started at the beginning of the second half of 2003, and the mill start up was in May 2005. A total of US$1.30 billion was budgeted to the project.

The Veracel pulp mill, from the cornerstone to the start-up at the beginning of May 2005, took 22 months to be completed. On November 6, 2005, the Veracel pulp mill officially attained its design capacity. The so called learning curve phase was considered completed after the mill had produced for 30 consecutive days at an average output of 2,543 tons per day. This was achieved 174 days after the mill's start-up. The quality curve had already been achieved in June 2005, when a level of over 97% of prime grade product had been continuously recorded for a period of 30 days. Both accomplishments represent world records for a greenfield pulp mill and are two major achievements in the successful development of the Veracel project. The year 2006 was the first full year of operation, with pulp production at a total of 975,150 metric tons, 8% above the annual nominal capacity of 900,000 metric tons, with 468,348 tons being purchased by the Company as it share. In 2007, Veracel pulp production achieved 1.051,376 metric tons, 8% above 2006 production and 16% above annual nominal capacity. The output of the new plant has been sold basically to the controlling shareholders, in the same proportion as their shareholdings (50% each).

The Veracel mill has the world s lowest production cost for bleached eucalyptus market pulp, due to its modern equipment, low average forestry operations radius (50 Km) and high forest productivity, and is one of the largest single-line pulp production facilities of its type in the world. The project makes use of modern equipment, control systems and processes to preserve the quality of the environment.

Because of its location - distant from large urban centers - Veracel s mill contributed to the creation of jobs and income in a region where there are currently few job opportunities.

Guaíba Unit

On May 30, 2003, the Company acquired all of the capital stock of Riocell S.A. ("***Riocell***"), a major producer of BEKP, from Klabin S.A. for a purchase price of US$567 million. Riocell owned and operated a BEKP pulp mill (the "***Riocell Mill***") with a capacity of approximately 400,000 tons per year and owned approximately 40,000 hectares of eucalyptus plantations in the State of Rio Grande do Sul. On January 7, 2004, Riocell was merged into the Company and the Riocell Mill and related forestry assets are now operated as the Company's Guaíba Unit. On September 15, 2004 the Company announced the Guaíba Unit Optimization. The systems involved in the modernization of the Guaíba Unit went into operation in November 2005. The optimization project allowed additional production of 30,000 tons in 2006, bringing the Guaíba Unit s nominal capacity to 430,000 tons/year. In June 2006, the Company announced that preliminary studies have been completed regarding the feasibility of the future expansion of the production capacity at its Guaíba Unit by 1.3 million tons/year, which would raise the mill s total capacity to approximately 1.8 million tons/year some time between 2010 and 2015. In June 2007, the environmental impacts study was completed and in March 2008 the preliminary environmental license concerning the expansion of the production capacity of the Guaíba Unit to 1.8 million tons/year was issued. See " Business Guaíba Unit".

Capital Expenditures

The Company's capital expenditures for 2005, 2006 and 2007 were US$ 147.9, US$ 301.0 million and US$589.7 million, respectively.

The table below sets forth a breakdown of our most significant capital expenditures for the periods indicated:

	For the years ended December 31,		
	2005	**2006**	**2007**
		(in US$ millions)	
Silviculture (Forest) and other forestry investments (includes land purchase)	US$71.4	US$219.1	US$317.8
Improvements/industrial investments	66.8	67.3	212.8
Other	9.7	14.6	59.1
Total	US$147.9	US$301.0	US$589.7

During the year 2005, we invested approximately US$147.9 million, of which US$65.2 million was devoted to forest, US$2.4 million to land purchases, US$3.8 million to other forestry investments, US$40.1 million to ongoing industrial investments, US$26.7 million to Guaíba Unit Optimization and US$9.7 million to other projects.

During the year 2006, we invested approximately US$301.0 million, of which US$113.1 million was devoted to forest, US$80.5 million to land purchases, US$25.5 million to other forestry investments, US$23.4 million to ongoing industrial investments, US$43.9 million to Barra do Riacho and Guaíba Unit Optimization and US$14.6 million to other projects.

During the year 2007, we invested approximately US$589.7 million, of which US$146.5 million was devoted to forest, US$140.4 million to land purchases, US$30.9 million to other forestry investments, US$51.6 million to ongoing industrial investments, US$161.2 million to Barra do Riacho and Guaíba Unit Optimization and US$59.1 million to other projects.

During 2008, the Company expects to invest approximately US$578 million related to industrial, forestry and other investments. Approximately 70% of the funding for these investments will derive from Company's own cash generation.

B. Business Overview

General

We are the world s largest producer of bleached hardwood kraft market pulp. We produce eucalyptus pulp, which is a high-quality variety of hardwood pulp used by paper manufacturers to produce a wide range of products, including premium tissue, printing and writing papers, liquid packaging board and specialty papers. Eucalyptus pulp s distinguishing characteristics are its softness, opacity, porosity, and suitability for printing. Market pulp is the pulp sold to producers of paper products, as opposed to pulp produced by an integrated paper producer, for use in paper production facilities. Kraft pulp is pulp produced in a chemical process using sulphate.

During 2007, we produced approximately 2,569,000 tons of BEKP (3,095,000 tons including 50% of Veracel's pulp production), representing an estimated 12% of the total worldwide production capacity of hardwood market pulp and 23% of the worldwide production capacity of BEKP for 2007. In 2007, eucalyptus accounted for an estimate of approximately 53% of the total worldwide production capacity of BHKP. In 2007 and 2006, sales to customers located outside Brazil, especially in North America, Western Europe and Asia, accounted for approximately 98% of our sales volume. See "Market Overview Markets and Customers" and "Competition".

In 2007 Aracruz s sales volume totaled 2,581,000 tons of eucalyptus pulp (3,104,000 tons including 50% of Veracel) compared to 2,547,000 tons in 2006 (3,021,000 tons including 50% of Veracel).

In 2007, we had net operating revenue of US$1,808.0 million of eucalyptus pulp compared to US$1,632.2 million in 2006 and US$1,300.2 million in 2005.

From 1979 to 2007 our pulp production volume had a compound annual growth rate of 10% per annum and it is expected to reach a total pulp production volume of 3,300,000 tons (including 50% of Veracel s pulp production) in 2008.

In December 1999, we moved our headquarters from Rio de Janeiro to the Municipality of Aracruz, in the Brazilian coastal State of Espírito Santo, where part of the Company's production facilities is located. In 2005 we moved our executive offices from Rio de Janeiro to São Paulo, where we maintain our financing, administrative and trading activities. Our production facilities consist of the Barra do Riacho Unit in Espírito Santo State, which has three production units each with two bleaching, drying and baling lines, the Guaíba Unit, located in the municipality of Guaíba, State of Rio Grande do Sul, and Veracel, located in the municipality of Eunapolis, State of Bahia, where we have a 50% stake. Our production facilities are equipped with advanced environmental protection resources.

The Barra do Riacho Unit s area totaled 360,000 hectares at the end of 2007, of which 211,000 ha were plantations and 129,000 ha were native reserves and 20,000 were for other uses. At the Guaíba Unit, there were approximately 126,000 ha of total forestry area, of which 75,000 ha were plantations and 41,000 ha were native reserves and 9,900 were for other uses. All told, Aracruz maintains a ratio of 1 hectare of native reserves for each 1.7 ha of plantations. Despite the condition of self sufficiency in wood requirements, the Company managed to have other sources of wood supply from the Forestry Partners Program, which celebrated its 16th anniversary in 2007. Last year, the total turnover of the program was almost US$27 million and we entered into almost 3,800 contracts with small, medium and large farms, covering nearly 87,000 hectares of private farm property. The program contributes to the generation of rural jobs, encourages the utilization of otherwise idle land, boosts and diversifies farm income, and at the same time ensures the Company an alternative source of wood supplies. The program helps reduce the pressure exerted by certain sectors of society, to cut down native forests in order to obtain lumber for other purposes, such as charcoal and firewood.

The Barra do Riacho Unit is located approximately 1.5 kilometers from the port facilities at Barra do Riacho (Portocel), of which we own 51%.

We believe that we are one of the lowest-cost producers of bleached kraft market pulp in the world. Our low production costs relative to some of our competitors are due to a number of factors, including:

- economies of scale,
- advanced forestry techniques in managing the processes of planting,
- growing and harvesting of our trees,
- a comparatively short harvest cycle of our trees, and
- lower energy and chemical costs.

During 2007, we were able to meet 86% of our wood fiber requirements from our own eucalyptus forests. Climate and soil conditions in Brazil enable us to harvest our eucalyptus trees in only seven years after plantation, while harvest cycles for other types of hardwood trees in the southern United States, Canada and Scandinavia can range from 25 to 70 years. Harvest cycles for our principal non-Brazilian competitors in the eucalyptus pulp market, which are located in Spain, Portugal and Chile, are approximately eight to ten years. See Raw Materials Wood" and Competition". We internally produce approximately 96% and 69%, in Barra do Riacho and Guaíba Units, respectively, of our electrical energy requirements, mainly from by-products of our pulp production process, and recycle the greater part of the chemicals used at the Units. See Raw Materials Energy.

Business Strategy

By the end of 2006 Aracruz updated its mission, vision and business principles as follows:

Mission:

ü To offer products obtained in a sustainable way from planted forests, generating economic, social and environmental benefits and, in this way, contributing to people's well-being and quality of life.

Vision:

ü To be acknowledged as leader in the global pulp market.

Business Principles

Our decisions and actions are based on ethical values and observe the following business principles, which also guide our Code of Ethics:

ü Integrity

We have a commitment to integrity:

- acting with fairness and honesty;
- respecting human rights;
- complying with legislation, internal rules, agreements and commitments;
- continuously seeking the best corporate governance practices;
- rejecting any form of corruption or illegality.

ü Commitment to shareholders

We create value for all shareholders, focusing on operational excellence:

- investing in continuous improvement and innovation throughout our operations;
- seeking to maximize return on investments;
- increasing the scale of our business;
- managing risks and pursuing a continuous reduction in the cost of capital.

ü Customer focus

We value long-term relationships:

- offering products that satisfy customer needs;
- guaranteeing the safety of our products and the reliability of their supply;
- investing in product development.

ü Valuing our employees

We value our employees:

- fostering a safe, healthy and motivating work environment and rejecting discrimination of any kind;
- respecting freedom of association;
- offering opportunities for professional and personal development;
- fostering professional growth based on merit;
- encouraging active citizenship;
- seeking to constantly improve quality of life.

ü Valuing our stakeholders

We cultivate relationships of mutual trust with our stakeholders:

- seeking engagement and cooperation;
- being sensitive to their aspirations and concerns;
- using dialogue as the first priority to resolve conflicts;
- respecting diversity and freedom of opinion and expression;
- being transparent in our actions and communications.

ü Harmony with the environment

We act in harmony with the environment and we contribute to its protection:

- using natural resources in a sustainable manner;
- adopting modern technologies and practices to make our operations more efficient and minimize their impacts;
- contributing to the preservation of biodiversity.

ü Social responsibility

We take our corporate social responsibility seriously:

o disseminating knowledge and fostering the sustainable development of communities;

o establishing partnerships, investing in projects and nurture networks with the private sector, civil society organizations and the public sector;

o contributing to the improvement of public governance;

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o supporting and strengthening the partners in our supply chain.

We encourage our business partners to adopt these principles, as we strive for the sustainability of our supply chain.

Moreover, following up actions that were initiated in 2005, during 2006 and 2007 additional measures were adopted to enhance the Code of Ethics effectiveness and to assure the more structured performance of our various management bodies, with the following highlights:

- The approval of Internal Regulations for the Executive Officers, the Board of Directors and each one of the committees that support the Board of Directors, in a manner that increases their effectiveness.
- The setting up of a Disclosure Committee whose main objective is to establish guidelines for the disclosure of results and financial, accounting and audit reports.
- The restructuring of the Sustainability Committee, which now is composed of representatives of the shareholders and independent members.
- The approval of a proposal to improve the structure of the Company s regulations, seeking to more clearly establish hierarchies and levels of approval of the documents that orient our operations.
- Revision of the Code of Ethics to better align it to the mission, vision and business principles of the Company.

Also, in 2007 the Company made progress in the implementation of its strategy of combining sustainable growth with continuous efforts to improve operational excellence. Our strategic goal is to supply 25% of world demand for hardwood market pulp - amounting around 7 million tons by 2015, and to continue be one of the lowest cost producers in the sector, adding value for shareholders and other stakeholders. The studies to implement these additional capacities are not yet completed and still depend upon Aracruz Board's approval.

Listed below, can be seen some of the projects that contributed to implement our business strategy:

- *Economies of scale resulting from new capacity increases.* Following the modernization of Fiberlines A and B, and the Excellence Project, both carried out in 1998, which improved Aracruz's operational efficiency and enabled the Company to reduce costs, and the Fiberline C Expansion Project, which in the middle of 2002 increased our nominal production capacity to over 2,000,000 tons per year, Aracruz continued to deliver growth through the acquisition from Klabin S. A. , in 2003, of Riocell, with its updated nominal production capacity of approximately 430,000 tons of bleached eucalyptus market pulp and 50,000 tons of printing and writing paper, and through the Veracel project, a pulp mill for the production of bleached eucalyptus kraft market pulp in Eunápolis, in the State of Bahia, with a nominal capacity of 900,000 tons per year, which started up in May 2005. In mid 2004, Aracruz's Board of Directors approved the Guaíba Unit optimization project, which improved operational efficiency and enabled the Unit to increase its nominal capacity from 400,000 to 430,000 tons per year. Those Projects rely on our technology advances and benefit from our existing overhead and management structure, which has absorbed the new activity without significant additional fixed costs. These enhancements will enable us to reduce pulp costs and improve quality levels in the new production unit. Following the same value drive, the Company approved in 2005 the Barra do Riacho Unit Optimization Project that will increase the nominal capacity of the three existing Fiberlines by 200,000 tons. This project was concluded in the last quarter of 2007 and will be fully operational in 2008.
- *Improvements in forestry technology using advanced genetic techniques, which will result in an increase in the forest yield.* Regarding forest technology, as a result of the traditional genetic improvement program, we recommended eleven new eucalyptus hybrid clones for operational planting, which display greater pulp productivity per hectare, in the different Company sites, as well as wood

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quality in accordance with the requirements of our products. Worthy of note is the unprecedented recommendation of hybrid clones of E. urophylla x E. dunni to Guaíba unit plantations, at Rio Grande do Sul State. Contributions to the commercial applications of new clonal propagation technologies have also been provided, as well as sustainable silvicultural practices that ensure the high performance of plantations. In Barra do Riacho Unit, soil monitoring conducted in last twenty years revealed that fertility has been improving for most of the areas, due to application of changes in nutritional management, especially from late 90's. In Guaíba Unit an important study involving soil mapping of the expansion areas was accomplished. Concerning climate studies, the results so far have demonstrate that the consumption of water by the Aracruz' eucalyptus plantations is similar to the consumption of native forests located on the Company's reserves. Aracruz biodiversity studies, started 15 years ago both in eucalypt plantations and native reserves, show that more than 11 thousand birds, of 556 different species, were registered until the end of 2007, suggesting that the silvicultural model adopted by Aracruz has allowed the maintenance of bird communities at the studied locations.

- *Optimization of transportation logistics.* Transportation of wood to the mills comprises a large portion of the cost of our pulp production. Improvements in transportation logistics and costs are a priority for the Company. At the end of 2002, we improved the logistics of our rail transportation. We also launched our Multimodal Transportation Systems Maritime and Rail , the main objective of which is to enhance logistics and further integrate our Mill-Port-Forest system. In 2005, coastal shipping delivered 17% of the total wood consumed at the Barra do Riacho Unit. With the entry into service in October, 2005 of another tug and barge, the annual shipping capacity is expected to reach 2.7 million tons in the following years, representing 36% of total wood transportation. As part of the complete system learning curve process it has already reached about 1.9 million tons in 2006, representing some 24% of the wood consumed at Barra do Riacho. In 2007, the system delivered 1.6 million tons. Each barge has a wood-carrying capacity of approximately 5,000 tons. As well as optimizing transport costs, their use eliminated some 60,000 truck journeys along the BR 101 highway in 2007, reducing traffic on the road and cutting emissions of greenhouse gases as a result of lower fossil fuel consumption.
- *Improve business process management with state-of-the-art information technology in order to improve efficiency and reduce costs.* We use mySAP. com(R) platform supplied by SAP to control, simplify and integrate our business process within all our sites and also to implement connectivity with our customers and suppliers. All our information systems are in compliance with Sarbanes-Oxley requirements. During 2007 we had implemented the new version of ERP mySAP. com (ECC6.0) . In parallel, all business processes were evaluated in order to optimize them and make use of the new functions available.
- *Increase competitiveness.*The competitiveness of our business operations, combined with our significant cash generation capabilities, has led us to evaluate from time to time various future strategic alternatives, including further increase of current pulp operations either through acquisitions or expansion of existing capacity, and/or further acquisitions of additional forests.
- *Enterprise risk management (ERM).*The Company is developing its Sustainability Plan, which comprises ERM, a wide and structured framework of the main corporate risks of the Company. Following the best practices of Corporate Governance, the Company seeks to have full control of its main corporate risks that may cause financial, operational or intangible impacts. The methodology used by the Company considers an evaluation of impact and probability under a conservative but realistic approach, being that such system has been building up through technical workshops involving the main areas of the Company.
- *Investment grade.*The Company obtained an investment grade rating in foreign currency from Moody s (Baa3, raised to an additional notch, Baa2, during 2007) and Fitch (BBB) in the early part of 2006, to add to that received from Standard & Poor s at the end of 2005 (BBB-, raised to an additional notch, BBB, during 2007). This achievement positioned Aracruz among a select group of companies in Brazil, which improved the Company s risk perception, what could result in an important reduction of Aracruz cost of capital and, consequently, value added to the shareholders.

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Acquisition of Veracel

On October 10, 2000, we entered into two stock purchase and sale agreements pursuant to which we acquired a 45% stake in Veracel, a joint venture between Stora Enso OYJ and Odebrecht to grow and manage eucalyptus plantations and to build a pulp mill. One agreement, for the amount of approximately US$72 million, was entered between the Company and Odebrecht for the acquisition of 40% of the total outstanding capital stock of Veracel. The other agreement, for the amount of approximately US$9 million, was entered between the Company and Stora Enso Treasury Amsterdam B.V. for the acquisition of an additional 5% of the total outstanding capital stock of Veracel. On January 31, 2003, Odebrecht sold its 10% stake in Veracel to Stora Enso OYJ and us. We acquired shares representing 5% of the total outstanding capital stock of Veracel for US$9.7 million, resulting in 50% stake for each shareholder. This equity investment in Veracel achieved two objectives: (i) a guaranteed supply of wood for the Fiberline C Expansion Project during the first three years of the new production unit s operation and (ii) the opportunity to grow our business in the future from an operational base in Bahia that can potentially replicate our accomplishments in the State of Espírito Santo.

In May 2003, Stora Enso and we approved the construction of Veracel s pulp mill for the production of BEKP in Eunápolis, in the State of Bahia (***Veracel Project***). The mill was projected to have a nominal capacity of 900,000 tons per year and the overall investment was budgeted at US$1.30 billion. Veracel operations started in May, 2005 and reached full capacity 174 days thereafter, in the beginning of November 2005, setting a new world record for learning curve achievement. During 2006 Veracel produced 975,150 tons of pulp. In 2007 the production achieved 1.051,376 metric tons, 8% above 2006 production and 16% above annual nominal capacity, figuring among the largest and most advanced single-line pulp mills in the world.

The Veracel Project has obtained long-term direct funding from development banks in the amount of approximately US$650 million, being US$500 million from BNDES and US$150 million from the European Investment Bank (EIB) and the Nordic Investment Bank (NIB). The funding of the Veracel Project consisted of 5% internal cash generation, 42% equity and 53% loans from Brazilian and international development agencies. NIB and EIB debt was fully pre-paid in 2007. The Company is a several guarantor of 50% of the indebtedness incurred by Veracel, including indebtedness in connection with the financing of the Veracel Project. Stora Enso is a several guarantor of the other 50% of such indebtedness. At December 31, 2007 the outstanding amount of such indebtedness guaranteed by the Company was approximately US$321.5 million.

The construction of the mill was started at the beginning of the second half of 2003, and the operational start-up was in May 2005. The project was carried out under an EPC (Engineering, Procurement and Construction) concept and required the prior implementation of a qualification program to enable the local workforce to take part in the construction of the pulp mill. The equipment and services necessary for the project have been contracted mostly from Brazilian suppliers. The implementation of the Veracel project was also successfully concluded, establishing two other global marks: the installation of the project in 22 months and the effective construction of the mill, concluded in 17 months.

In connection with the acquisition of the 45% equity participation in Veracel, on October 10, 2000, we, Stora Enso and Odebrecht, together known as the Veracel Shareholders, and Veracel entered into a shareholders agreement, or the Veracel Shareholders Agreement, which set forth, among other things, certain agreements among the parties with respect to the management and operation of Veracel and the transfer of the common shares of Veracel. In connection with the further acquisition by us and by Stora Enso, on equal basis, of the stake then held by Odebrecht in Veracel on January 31, 2003 and as a consequence of the Implementation Decision adopted by the remaining shareholders, the Veracel Shareholders Agreement was amended. The amended Veracel Shareholders Agreement has a term of 20 years from its date and can be automatically extended for successive 20-year terms thereafter unless notice to the contrary is given by any party to the Veracel Shareholders Agreement. The Veracel Shareholders Agreement will terminate automatically if the ownership by any of the Veracel Shareholders of common shares of Veracel exceeds 50%. The Veracel Shareholders Agreement provides that Veracel will at all times during its term have a board of directors comprised of 6 (six) members, of which (i) 3 (three) will be elected from individuals appointed by Stora Enso and, (ii) 3 (three) will be elected from individuals appointed by us. The directors elected by us (acting jointly) and the directors elected by Stora Enso (acting jointly) will each have the right, without any action by any other directors, to request the removal of any incumbent officer of Veracel. The Veracel Shareholders Agreement also provides that neither we nor Stora Enso may transfer (which includes the creation of liens) any of their respective common shares of Veracel to non affiliated entities other than after the second anniversary of the start-up of Veracel s pulp mill. Either of the Veracel Shareholders may transfer its common shares of Veracel to an affiliate, subject to certain limitations. The Veracel Shareholders Agreement also requires that each person

or entity who acquires shares of Veracel pursuant to the provisions thereof become a party to such agreement. The Veracel Shareholders Agreement provides that, under certain circumstances, the Veracel Shareholders may be required to make capital contributions to Veracel, on a *pro rata* basis. The Veracel Shareholders Agreement also provides that we, so long as either we or any of our subsidiaries is a shareholder of Veracel, shall not acquire (or caused to be acquired) any interest in real property in the core area of Veracel. The same covenant applies to Veracel with respect to real property in our core area.

The Veracel Shareholders Agreement provides further that if any of the shareholders, known as the Defaulting Shareholder, fails to comply with any of its obligations regarding Veracel s funding needs in connection with the business plan, the Investment Plan and Capital Contributions, the other shareholder (the Calling Shareholder) shall have the right to require the Defaulting Shareholder to transfer all (but not less than all) of its shares to the Calling Shareholder at a discounted market value calculated according to the provisions of the Veracel Shareholders Agreement.

Guaíba Unit

On June 30, 2003 the Company announced that it had acquired Riocell S.A. ("*Riocell*") from Klabin S.A., which operated the Riocell Mill situated in the Municipality of Guaíba, State of Rio Grande do Sul, in the south of Brazil, for a purchase price of US$567 million. As a consequence, Riocell was included in the financial information of the Company at and for the year ended December 31, 2003. On January 7, 2004, Riocell was merged into the Company and is now operated as the Guaíba Unit of the Company.

The nominal production capacity of the Guaíba Unit is approximately 430,000 tons of BEKP and 55,000 tons of printing and writing paper, equipped with advanced environmental protection resources. The Guaíba Unit has approximately 126,374 hectares of forest and other land and 18,300 hectares of plantations are kept in association with third parties. The average distance of the wood supply to the mill is approximately 117 kilometers.

The Guaíba unit is fully integrated into Aracruz: human resources, information technology, systems and processes. Several synergies were obtained mainly in logistics, sales and operations.

In November 2005 we started up the project to upgrade the Guaíba Unit s industrial facilities, improving production capacity from 400,000 tons to 430,000 tons of BEKP. The overall investment amounted to US$29.7 millions and the results are better than expected, as demonstrated in 2006 and 2007 when production reached around 436,000 tons. In June 2006, the Company announced that preliminary studies have been completed regarding the feasibility of the future expansion of the production capacity at Guaíba Unit by 1.3 million tons/year, which would raise the mill s total capacity to approximately 1.7 million tons/year some time between 2010 and 2015. In June 2007, the environmental impacts studies were completed and in March 2008 the preliminary environmental license concerning the expansion of the production capacity of the Guaíba Unit to 1.8 million tons/year was issued.

Aracruz Produtos de Madeira

As part of our earlier strategy of diversification into other forest product businesses, we established a joint venture with the Gutchess International group of the United States in 1997 to create a new company, Tecflor Industrial S.A., for the production of solid wood products. In 1998, we acquired all ownership interests of Gutchess International Inc. in Tecflor Industrial S.A., now called Aracruz Produtos de Madeira S.A., (***APM***), which then became our wholly owned subsidiary. APM's high-tech hardwood lumber sawmill, which is located in the State of Bahia, was commissioned in the first quarter of 1999 and sales of its products began during the third quarter of 1999. APM manufactures and markets Lyptus®, a new concept renewable, high-grade hardwood lumber produced using eucalyptus trees, computer-optimized sawing technology and advanced drying and finishing processes. The sawmill has a nominal production capacity of 44,000 cubic meters per year. As of December 31, 2007, APM had nominated 10 sales representatives in major furniture markets in Brazil and was supplying a customer base of over 400 customers including manufacturers and resale yards.

Having consolidated the production process and trained its workforce during the preceding two years, in 2001 APM sought to expand the presence of its Lyptus® brand of high-quality sawn wood in domestic and international markets while ensuring that its quality standards were maintained. In 2001, APM established a commercial partnership with the U.S.-based Weyerhaeuser Co., or Weyco, one of the largest forestry companies in the world, for the exclusive distribution of Lyptus® in the North American markets. This new partnership

arrangement gave APM access to over 70 Weyco points of sale in the U.S. and Canada, increasing the presence of Lyptus® in one of the largest markets in the world for high-quality hardwood. The first shipments to Weyco took place in the months of May and August 2001. We have expanded the 2001 agreement with Weyco to extend sales of Lyptus® to the European and Asian markets, thus assuring the presence of the product in over 100 points of distribution in those regions.

In 2004, 2005, 2006, and 2007, 30%, 40%, 50%, and 34% respectively, of APM's total production was exported. In 2004, 2005, 2006 and 2007 export sales accounted for 61%, 65%, 71%, and 55% respectively, of the revenues of APM.

Consistent with the strategies set forth above, in October 2004 we sold two thirds of our shares in APM to Weyerhaeuser do Brasil Participações Ltda., a subsidiary of Weyco, for a total purchase price of US$18.6 million. We currently own one third of the shares of APM and have certain voting rights as set forth in the APM Shareholders' Agreement.

The Board of Directors of APM approved in February 2004 a five year business plan, which comprises the expansion of the sawmill nominal production capacity to 95,000 cubic meters per year and investments in the amount of up to US$10.3 million, of which US$1.35 million have been invested in 2005. In 2006 it were invested US$ 72 thousand and in 2007 US$1.35 million.

Barra do Riacho Unit Optimization Project

Barra do Riacho Unit began its operations in 1978 with a nominal capacity of 400,000 tons in Fiberline A. In 1991 through the duplication of capacity, the Fiberline B started operations with an additional of 525,000 tons. In 2002 our third line, Fiberline C, was started with a nominal capacity of 700,000 tons. During the last 27 years, through many debottlenecking and modernization projects, Barra do Riacho Unit achieved a total production capacity of 2,130,000 tons per year.

The Barra do Riacho Unit Optimization Project, approved by our Board of Directors in December, 2005, will improve the technology and performance in the pulp production process, introducing flexibility to adapt the pulp to different market requirements. These improvements will be made by modifying and/or replacing equipments at Fiberlines A, B and C leading to a sustainable increase in nominal capacity of 200,000 tons per year.

The plant investment is estimated at US$230 million, or US$1.150 /ton, with 80% of the items produced domestically and 20% imported. The appreciation of the real against the U.S. dollar is the main reason for the increase compared to the approved Budget of US$ 192 million. There are still some disbursements to happen in 2008 related to equipment already operational. Land purchase will not be needed. The incremental wood volume will be provided basically by (1) reduction in average age of current forestry base and (2) forestry productivity increase through forestry management implemented in 1999.

Implementation commenced in the first half of 2006 and was concluded in the 4th quarter of 2007 (around 19 months since purchases), with full capacity of 2.3 million tons/year to be operational in 2008. There are still some minor items pending, to be operational in 2008, such as the gas system which is under construction and will be in place by April 2008. This item does not affect production for 2008.

Market Overview

General

Wood pulp is the principal raw material used in manufacturing paper and paperboard. Whether or not a specific type of wood pulp is suitable for a particular end-use, depends on the type of wood used to make the pulp, as well as the process used to transform the wood into pulp. Hardwood pulp is produced using hardwood trees, such as oak, eucalyptus, aspen, birch and acacia trees. Hardwood pulp has short fibers and is generally better suited for manufacturing coated and uncoated printing and writing papers, tissue and specialty papers. Softwood pulp is produced using softwood trees, such as pines. It has long fibers and is generally used to add strength to the paper. We do not produce softwood pulp.

The pulp manufacturing process also can determine a pulp s suitability for particular end-uses. Chemical pulp refers to pulp made using chemical processes to dissolve the lignin and other organic materials

holding the wood fibers together. Among the various chemical processes, the most common is the kraft process, which is used by us to produce our pulp. The kraft process helps to maintain the inherent strength of the wood fibers and thus produces a pulp especially well suited for manufacturing printing and writing papers, specialty papers and tissue papers. Pulp producers may sell their pulp in the worldwide market or use it internally to manufacture various types of papers.

Bleached pulp is used for a variety of purposes, including printing and writing papers, specialty papers and tissues. Unbleached pulp, which is brown in color, is used in the production of wrapping papers, corrugated containers and other paper and cardboard transportation materials.

As a result of the variety of wood types and processes used to produce pulp, which have evolved significantly over time, the pulp market has become increasingly specialized in terms of technical characteristics. Many of the physical and chemical properties most valued by printing and writing paper manufacturers and other bleached pulp consumers, such as opacity and brightness, are exhibited by hardwood and, particularly, eucalyptus pulp. In addition, the increasing specialization of paper manufacturers has resulted in many such manufacturers developing their own customized mix of pulp inputs (known as furnish), for use in their paper manufacturing. Furthermore, as more paper manufacturers have come to appreciate the technical characteristics of hardwood pulp and to rely on a significant hardwood pulp component in their furnish, the market for hardwood pulp has grown more rapidly than the market for softwood pulp.

Within the hardwood segment, bleached eucalyptus kraft market pulp has demonstrated the highest annual rate of growth in demand from 1997 to 2007. Over this ten-year period, the annual rate of growth in demand for bleached eucalyptus pulp was estimated at 8,5%, while the annual rate of growth in demand for hardwood pulp during the same period was estimated at 4,7% and the market for softwood pulp for the same period was estimated at a 2,5% annual rate.

Eucalyptus is only one of many types of hardwood used to make pulp. Eucalyptus trees generally grow straight and have few branches. This allows for dense growth, easy harvesting and less need for pruning. Since 1980, eucalyptus kraft market pulp has steadily increased as a percentage of the total worldwide production of bleached hardwood kraft market pulp (from 29% in 1980 to approximately 53% in 2007) primarily due to its high quality, and because of properties, such as its softness, opacity and printability.

International Markets

From 1997 to 2007, the worldwide production capacity of bleached hardwood kraft market pulp is estimated to have grown an average of approximately 4,5% per year, from 16,7 million tons to 25,8 million tons. The start-up of new or expanded production facilities has increased the total worldwide capacity for bleached hardwood kraft market pulp by approximately 9,1 million tons from 2000 to 2007. Worldwide demand for bleached hardwood kraft market pulp is strongly influenced by the demand for paper and board products, which correlates to world GDP growth. Demand for bleached hardwood kraft market pulp has grown in recent years, increasing from 15.1 million tons in 1997 to 24 million tons in 2007. Consumption of market pulp is concentrated mainly in Europe, North America and Asia.

The charts below show the estimated demand for bleached hardwood by region:

Total Bleached Hardwood Demand By Region

	2003		**2004**		**2005**		**2006**		**2007**	
	tons	**% total**	**tons**	**% total**	**tons**	**% total**	**tons**	**% total**	**tons**	**% total**
NORTH AMERICA	**2.725.000**	**14%**	**2.740.000**	**13%**	**2.915.000**	**14%**	**3.095.000**	**14%**	**3.345.000**	**14%**
EUROPE	**8.515.000**	**43%**	**8.965.000**	**43%**	**9.080.000**	**43%**	**9.570.000**	**43%**	**9.980.000**	**42%**
ASIA	**7.530.000**	**39%**	**8.195.000**	**40%**	**8.235.000**	**39%**	**8.850.000**	**39%**	**9.100.000**	**39%**
LATIN AMERICA	**805.000**	**4%**	**865.000**	**4%**	**835.000**	**4%**	**880.000**	**4%**	**1.080.000**	**5%**
TOTAL WORLD	**19.575.000**		**20.765.000**		**21.065.000**		**22.395.000**		**23.505.000**	

Source: PPPC - Oct, 2007.

Aracruz Sales and Market Share By Region

	2003		**2004**		**2005**		**2006**		**2007**	
	tons	**%Share**	**tons**	**%Share**	**tons**	**%Share**	**tons**	**%Share**	**Tons**	**%Share**
NORTH AMERICA	**767.800**	**25%**	**831.300**	**30%**	**909.300**	**31%**	**1.016.400**	**33%**	**1.050.800**	**31%**
EUROPE	**813.700**	**9%**	**1.014.400**	**12%**	**1.122.300**	**11%**	**1.175.000**	**12%**	**1.266.100**	**13%**
ASIA	**509.000**	**6%**	**533.100**	**7%**	**510.800**	**6%**	**757.400**	**9%**	**710.500**	**8%**
LATIN AMERICA	**58.500**	**7%**	**71.200**	**8%**	**48.100**	**6%**	**63.300**	**7%**	**73.000**	**7%**
Total	**2,149,0**		**2,450,0**		**2,590,6**		**3012,1**		**3,100,3**	

The market pulp industry is highly competitive and is also sensitive to changes in industry capacity, producer inventories and cyclical changes in the world s economies, all of which may significantly affect pulp prices and thereby our profitability. The price of pulp generally increases as economies expand around the world. Strong demand during most of the 1980s caused the market price per ton of bleached eucalyptus kraft market pulp delivered in the United States by us to peak in 1989 at US$775 per ton. A global recessionary environment and a substantial increase in worldwide pulp supply during the early 1990s led to a sharp decline in the prices of market pulp, reaching US$410 per ton in December l993, the lowest price level since 1983.

In the beginning of 2004 prices were depressed, but with the pick up of paper demand and adequate inventories, prices were able to reach its peak by June and July at US$595 (North America delivered). In the middle of third quarter the absence of the Chinese buyers in the market once more depressed prices which ended 2004 at US$555 (North America delivered).

The increase in demand in 2005, combined with pulp mill closures permitted the implementation of price increase in the year which reached list price of US$635 per ton (North America delivered) in April and sustained itself throughout the year. In 2006 the same scenario allowed an US$ 80 per ton price increase over the year, reaching US$ 715 per ton in December.

The trend of mill closures and strong demand for hardwood pulp observed in 2005 and 2006 continued throughout the year of 2007. This combination resulted in a tight supply and demand ratio allowing price increase implementation. Regarding BEKP, prices evolved from US$715 per ton in January to US$805 per ton (North America delivered) in December 2007.

The following chart shows, for the periods indicated, average annual prices for BEKP produced by us as compared to northern hardwood (NBHK) and southern hardwood (SBHK) prices:

BEKP -NBHK - SBHK List Prices
North America Delivered (US$/ton)

(Note: prices are expressed as simple arithmetic average for the year)

Sources: For all eucalyptus pulp prices and for 2000 southern and northern hardwood pulp prices, the Company s databank; for 2001 northern and southern hardwood pulp prices, Hawkins Wright 2001; for 1988-99 southern and northern hardwood pulp prices, Hawkins Wright, November 2000. For 2002, 2003, 2004, 2005 and 2006 eucalyptus prices, the Company s databank, and for southern and northern hardwood pulp prices, Hawkins Wright, December 2002, 2003, 2004, 2005 and 2006.

The market pulp industry has demonstrated a seasonality pattern along the years, which is strongly correlated with paper production. World paper production normally increases by the end of vacation in the Northern Hemisphere as well as during the period involving the Christmas and New Year celebrations. However, due to specific factors such as: pulp and paper machine closures, start up of new capacities, changes in the cost structure of the industry, and the increase of worldwide pulp demand, the seasonality trends observed in the pulp industry in the past can present some changes in the future.

Domestic Market

In 2006 total domestic market demand for bleached hardwood kraft reached 605.016 tons, resulting in an increase of 7% over 2005. In 2007 demand for bleached hardwood kraft market pulp in Brazil achieved 870,000, an annual growth of 43% over 2006. However, this growth was mainly due to a "definitional change" -changes in ownership of pulp and paper facilities in Brazil resulted in the reclassification of previously affiliated pulp to market pulp. In 2007, we supplied approximately 69,000 tons of the aggregated domestic demand for bleached eucalyptus kraft market pulp, compared to 53,000 tons in 2006 and 40,000 tons in 2005.

The six largest Brazilian producers of bleached hardwood kraft market pulp are:

- Aracruz Celulose S.A.,
- Celulose Nipo-Brasileira S.A., or CENIBRA,
- Votorantim Celulose e Papel S.A,
- Suzano Papel e Celulose S.A.,
- Jarí Celulose S.A., and
- Lwarcel Celulose e Papel

Together the six largest Brazilian producers accounted for 84% of total domestic sales in 2007, with Aracruz accounting for 8% of total domestic sales. Our domestic sales volume of bleached hardwood kraft market pulp was 2% of Aracruz total sales volume in 2003, 2004, 2005, 2006 and 2007 as compared to 3% in

2001, as a result of our increase in sales in international markets and other producers increasing their own share of the Brazilian market. See Competition. Although domestic pulp prices are affected to a certain degree by general economic conditions in Brazil, domestic pulp prices have been, and are expected to continue to be correlated with international pulp prices.

Eucalyptus Forests

On December 31, 2007, we owned approximately 486,197 hectares of forest and other land (not including Veracel Celulose S/A) in the Brazilian States of Espírito Santo, Bahia, Minas Gerais and Rio Grande do Sul, of which 286,099 hectares are planted with eucalyptus forests. The average distance from our forest areas currently in use to the mills at Barra do Riacho Unit is 204 kilometers, while this distance at Guaíba Unit is 117 kilometers. Because of the cost of transportation, the average distance from the forest to the mill has an important effect on our cost structure, and we have sought to reduce the distance in various ways, including by accelerating the substitution of cloned trees with higher productivity near the mills, as discussed in Raw Materials Wood. We are always evaluating opportunities for acquiring land with forest closer to the mills in order to reduce the distance, and the associated costs of hauling wood, between the forest and the mills as well as any system of logistics that could reduce the cost of transportation, such as transportation by barges using our port facility in the state of Bahia. See Business Strategy . Of the 486,197 hectares owned by us, approximately 286,099 hectares are currently used for the planting of trees to supply pulp production and solid wood production, approximately 170,191 hectares are reserved for preservation, approximately 19,931 hectares have been used in the construction of roads and the remainder is used for other activities. Brazilian law requires that 20% of our lands, at any given time, are reserved for preservation of native ecosystems (either remaining fragments or restored areas by plantation of indigenous species).

Throughout 2007, one of our main objectives was to increase the Forestry Partners Program, for the establishment of new plantations to ensure the future supply of wood for our mills. During 2007 we established approximately 12,500 additional hectares of eucalyptus plantation through this program.

At Barra do Riacho Unit we have a tree nursery capable of producing approximately 40 million seedlings per year and a research facility is located nearby as well. At Guaíba Unit, there was an expansion of capacity in 2007, and the production went from 21 million in 2006 up to 30 million in 2007.

In 2007, we supplied 9.5 million cubic meter of wood to our pulp mills, of which 8.2 million cubic meters came from our own eucalyptus forests and 1.3 million cubic meters of wood were purchased from the market, including approximately 1.0 million cubic meters purchased through the Forestry Partners Program.

The Company pioneered the use of cloned seedlings from rooted cuttings, a method also known as vegetative propagation, to carry out large-scale planting of eucalyptus trees. This method of cloning results in trees whose fibers are extremely homogeneous, which the Company believes results in a more streamlined industrial process and higher quality pulp. Today, approximately 89% of the Company's eucalyptus forests are grown from this type of seedling. Rather than growing from seeds, clones are the "offspring" of asexual propagation. By means of this type of generation, the descendant receives the entire genetic code of the original tree. Accordingly, the risk of disease and pests can be lessened by choosing parent trees better adapted to the region. Other benefits of vegetative propagation include significantly lower bark per cubic meter of wood and "self-pruning" trees with fewer branches.

Raw Materials

Wood

We rely exclusively on eucalyptus trees to meet our pulp wood requirements. Eucalyptus is a short-fibered hardwood that grows back from the stump after being cut, with each tree capable of regenerating twice. Eucalyptus trees are among the fastest growing trees in the world. Climate and soil conditions in Brazil allow for approximately six to seven-year eucalyptus tree harvest rotations as compared to eight to ten-year harvest rotations in Spain, Portugal and Chile. As part of our growth strategy, we have sought to eliminate the need for external sources of wood and to maximize both the yield and quality of fiber grown on our own plantations and in the Forestry Partners Program, through advanced forestry and tree-cloning techniques.

Through the development of cloned trees selected on the basis of certain characteristics, we were able to reduce our wood consumption per ton of pulp produced from 3.9 solid cubic meters under bark in 1985 to 3.5 solid cubic meters in 2007. The optimal age to harvest our trees is 5.5 to 6.5 years, from the time of planting.

Energy

Reducing our need for outside sources of energy and chemicals is an important component of our low-cost production strategy. At the Barra do Riacho Unit approximately 96% of our electrical energy needs in 2007 were met by burning by-products generated from pulp production compared with 98% in each of the years 2005 and 2006 and with 79% in 1999. The result of 2007 is due to periodic overhaul of one of the steam turbines. In 2007, at the Guaíba Unit, 68,8% of our electrical energy was generated internally using methods similar to the ones used in Barra do Riacho Unit and generation from coal. As in Barra do Riacho, the result of 2007 is due to the maintenance in the bigger steam turbine. The remainder of our energy needs was met through purchases of electricity, fuel oil and natural gas from third sources.

Chemicals

We use several chemicals in the pulp bleaching process. The Company has significant dependence on certain chemicals and therefore adopts strong measures to mitigate it. Until December 1999, we maintained and operated an electrochemical plant on the same site as the mill at Barra do Riacho Unit to produce some of the chemicals used in the pulp bleaching process, specifically chlorine, caustic soda and sodium chlorate.

On December 16, 1999, we entered into a series of transactions with Canadianoxy Chemicals Ltd. for the transfer of our electrochemical plant to a subsidiary of Nexen Inc., or Nexen, a Canadian company formerly known as Canadian Occidental Petroleum, for approximately US$61 million. Nexen, with head offices in Calgary, Canada, is a major producer of sodium chlorate. Its principal shareholder is Occidental Petroleum Corporation, which owns approximately 80% of its share capital. The transfer closed on December 17, 1999. The sale of the electrochemical plant, located adjacent to the mill in Barra do Riacho Unit, is part of our strategy to concentrate on our core business, transferring the production of chemicals to a specialized producer. We built the plant during the construction of the pulp mill in 1979 and subsequently expanded the plant in 1991. At the time of the sale, the electrochemical plant had the capacity to produce approximately 36,000 tons per year of sodium chlorate, 36,000 tons per year of caustic soda and 32,000 tons per year of chlorine. The plant also produces hydrochloric acid and sodium hypochlorite (liquid bleach).

As part of the sale of the electrochemical plant, we and two subsidiaries of Nexen entered into a successively renewable contract for the reciprocal supply of raw materials, services and products over a 25-year period. The agreement obligates us to provide a continuous supply of raw materials, primarily water and steam, to the electrochemical plant, and the plant to provide bleaching chemicals to us, at competitive prices. The agreement includes clauses of performance incentives, such as sharing of productivity gains, preference prices and take-or-pay obligations pursuant to which we are committed to purchase from the electrochemical plant a volume of chemical products projected for six years from the date of the agreement. If, in a given year, we purchase volumes of chemical products in excess of the minimum agreed to volume, our obligations to purchase may be reduced in subsequent years. For the take-or-pay quantities, we will pay unit prices which equal cost plus a margin as determined in the contract. The agreement also may not be assigned by a party without the consent of the other party and includes provisions relating to: (i) the extension of the agreement for an additional 10-year period upon the agreement of both parties not less than two years prior to the expiration of the initial 25-year term, (ii) the suspension of service by each party, (iii) the termination of service and (iv) the termination of the agreement by a party upon 18 months notice that such party intends to permanently cease operation at its facility. In the event of termination of the agreement or a proposed sale by Nexen, the agreement provides that we have the right of first negotiation for the acquisition of the electrochemical plant. As a result of the sale, we no longer have responsibility for the electrochemical plant and, accordingly, any interruption of the operations of the electrochemical plant could require us to seek alternative sources in the market for certain chemicals essential to our production of pulp.

The chemicals used in the pulp bleaching process in the Guaíba Unit, especially caustic soda, sodium chlorate, hydrochloric acid and chlorine dioxide, are also produced in an electrochemical plant located on site. The nominal capacities of such electrochemical plant are, respectively, 23,605 ton/year of caustic soda, 20,949 ton/year of chlorine, 9,900 ton/year of sodium chlorate, 9,000 ton/year of hydrochloric acid and 5,760 ton/year of chlorine dioxide.

Water

Water is required in the pulp production process and in the cultivation of seedlings. Water is primarily provided by several rivers, which feed into a 35 million cubic meter reservoir on the mill site in Barra do Riacho Unit. In the Guaíba Unit the water is provided by the Guaíba Lake, beside the mill. The reservoir in the Barra do Riacho Unit holds enough water to supply the mill s needs for a five-year period in the event of a drought (based on statistical information regarding periods of very low rainfall). In the Barra do Riacho Unit wastewater undergoes a two-stage purification treatment process before it flows into the ocean, and in Guaíba Unit we have a four stage purification process before it flows into the Guaíba Lake.

Beginning in the latter half of 1998, the State of Espírito Santo experienced a severe drought which reduced our water supply and caused us to pursue alternative long-term sources of water to meet our current operating needs as well as any foreseeable expansion plans. As a result, in May 1999, we, together with the municipal governments of Aracruz and Linhares, a neighboring city, began a project of public interest to obtain water from the Rio Doce river through an existing system of canals and rivers. The project was completed in June 1999 and now provides water for the local communities and for the industrial and chemical districts of the Municipality of Aracruz as well as for irrigation of agricultural activities in the northern region of the State of Espírito Santo. During 2000 and the beginning of 2001, we made the necessary adjustments in the mill to receive the water supply from Rio Doce. The project was approved by federal, state and local authorities. In 2004 due to high average rainfall, we decided to temporarily close our Rio Doce river access. During 2005 and 2006 the mill sometimes needed to use the water from Rio Doce due to maintenance of the river access. In 2007 the mill did not use the water from Rio Doce.

The Units

Our principal pulp mill, located in the State of Espírito Santo, is the largest bleached hardwood kraft market pulp production facility in the world.

In 1994, we increased our effective production capacity from 1,025,000 tons to 1,070,000 tons per year through system upgrades and productivity gains. From 1995 to 1999, we invested in the Modernization Project in Barra do Riacho Unit, successfully increasing the nominal production capacity of that mill to 1,240,000 tons of pulp per year. After the Fiberline C Expansion Project, 2002, which resulted in the construction of the mill s third production unit, the nominal capacity increased to 2,000,000 tons, in 2007 the Optimization Project increased the nominal capacity of the Barra do Riacho Unit to 2.330.000 tons. The total production of that mill was 2,031,000 tons in 2003; 2,093,000 tons in 2004; 2,134,000 tons in 2005; 2,180,000 tons in 2006 and 2,132,000 tons in 2007, due to the learning curve of the Optimization Project, representing approximately 8% of the total worldwide bleached hardwood kraft market pulp production capacity.

We also have a pulp mill in our Guaíba Unit which production capacity is of approximately 430,000 tons of BEKP per year, after full implementation of the project to upgrade the Guaíba Unit s industrial facilities. - See "B - Business Overview - Guaíba Unit".

The Company's total production in 2007 was 2,569,000 (comprising the Barra do Riacho Unit and the Guaíba Unit) and 3,095,000 tons including 50% of Veracel's pulp production (versus 2,616,000 tons in 2006), representing approximately 12% of the total worldwide bleached hardwood kraft market pulp production capacity.

The production facilities in the State of Espírito Santo and Rio Grande do Sul consist of large receiving yards for the logs, debarking, chipping and digesting equipment, packaging, warehousing facilities and a fully computerized control system that continuously monitors the entire production process. The Barra do Riacho Unit and the Guaíba Unit mills pulp systems have, respectively, six steam turbines and three steam turbines, and generators that provide a continuous power supply for that system. Fuel for the generation of steam is mainly provided by waste products from the pulp production process. External backup power supplies are also available on sites. The Barra do Riacho Unit electrochemical plant, which was transferred in December 1999 to Nexen and that provides most of the chemicals used in the pulp bleaching process, is located within the boundaries of the production facility. The Guaíba Unit also has an electrochemical plant located within its boundaries. For a discussion of the sale of our electrochemical plant to Nexen, see Raw Materials Chemicals.

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Pulp Production

When operating at full capacity, the Barra do Riacho Unit mill can process over 23,000 solid cubic meters of timber each day and the Guaíba Unit mill can process 6,700 solid cubic meters of timber each day. The logs are either debarked in the forest or debarked at the mills using tumbling drums and then cut into chips, which are transferred by conveyors system to the digesters where they are mixed with chemicals and heated under pressure. During this chemical cooking process, the lignin and cellulose are separated. Once removed, the lignin is used as fuel to produce steam and electrical energy for the milling process. The used chemicals are removed at various stages of the production process and recycled within the plant. The cellulose fibers are then washed, bleached using bleaching chemicals (which are produced on site), filtered, pressed and dried. The dried pulp is then cut into sheets, packed into bales and transported by truck to domestic destinations, for exportation. Barra do Riacho Unit is served by a private port which is administered by Portocel (of which we own 51% of the shares) located approximately 1.5 kilometers from the mill, for shipments abroad. At Guaíba Unit a barge terminal is located in the Guaíba Lake, beside the mill, and the pulp is transported by barges to Rio Grande Port for shipment abroad. See Transportation.

Since 2006 we only produce one type of pulp, which is ECF Pulp.

Standard Pulp is pulp bleached with regular levels of chlorine. Standard Pulp is in high demand in North America and Asia. During 2007 and 2006, we did not produce Standard Pulp. In 2005, 2004 and 2003 we produced 2,500 tons, 36,792 tons and 79,536 tons, respectively, of Standard Pulp. ECF Pulp, or Elemental Chlorine Free Pulp, is pulp bleached with lower levels of chlorine. ECF Pulp is in high demand in Europe, where our customers have preferred pulp that is bleached with little or no chlorine due to the environmental concerns relating to the pulp production process, particularly the bleaching process (although recently we have detected a shift in environmental concerns away from the bleaching process to forestry management and efficient control). We first produced ECF Pulp in November 1990. During the period from 1991 to 1994, we equipped the Barra do Riacho Unit mill so that it would have the capacity to produce enough ECF Pulp to meet the growing demand for ECF Pulp. From 1993 to 1997, we produced 75% ECF pulp. Commencing in 1998, with the completion of the Modernization Project, we were to produce 100% ECF pulp. See The Units. During 2007, 100% of Barra do Riacho Unit production, or 2,132,000 tons, was comprised of ECF Pulp as compared to 2,180,002 tons during 2006 and 2,132,018 tons during 2005. During 2007 the production of ECF in Guaíba Unit was approximately 436,000 tons, similar to the production in 2006.

Transportation

Wood from the forest areas is transported by trucks, railroads and sea barges (owned by independent contractors) to the mills for processing into pulp. The average distance from our forest areas to the mills at Barra do Riacho Unit is 204 kilometers, while this distance at Guaíba Unit is 117 kilometers.

The pulp produced for export at Barra do Riacho mill is transported by truck from the mill to the port of Barra do Riacho (Portocel), which is located approximately 3.25 kilometers from the mill site. This port is used to store pulp and load ocean vessels providing us convenient access to the Atlantic Ocean. The port is a modern facility that currently has the capacity to handle approximately 10 million tons of pulp and wood per year, moving up to 5.5 million tons of pulp overseas. Warehouse facilities at the port are capable of storing approximately 217,000 tons of pulp (static storage).

We own 51% of Portocel, the company that operates the port of Barra do Riacho. The remaining 49% of Portocel is owned by CENIBRA, another pulp manufacturer and one of our competitors. We do not own any ships for transportation of our pulp.

Our integrated, coastal wood shipment project was completed in December 2002. It involves an integrated tug and barge system and two port terminals. This sea transportation system links the extreme South of Bahia to the North of Espírito Santo. The port complex of Portocel, adjacent to the mill at Barra do Riacho Unit, receives wood from plantations in southern Bahia via an alternative transportation system that is more efficient and less pollutant than truck-based highway shipments. In 2007 the operation between Caravelas and Portocel was able to transport 1.6 million cubic meters of wood.

Another improvement to our wood transportation operations was the construction and start-up of a nearly 4 Km-long rail spur used for unloading wood shipments directly at the mill s yard in 2003. This

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improvement done in 2003 was important to optimize the receiving process of the wood that comes from North of Minas Gerais and other areas within the state of Espírito Santo.

At the Guaíba mill, the pulp is exported through the port of Rio Grande. The pulp is loaded in barges at a terminal facility integrated to the mill and then transported by barges along the Lagoa dos Patos. The distance from the terminal at the mill to the port in Rio Grande is 160 nautical miles.

Markets and Customers

Our main markets are in North America, Europe, Asia and Brazil. Our export sales are performed through our foreign subsidiary in Hungary. See - "Organizational Structure - Significant Subsidiaries". The Company does not have any special sales method, such as installment sales. The relative geographic distribution of our sales by volume and percentages of total production were as set forth below:

	2003		**2004**		**2005**		**2006**		**2007**	
	Tons	**% of total**	**Tons**	**% of total**	**Tons**	**% of total**	**Tons**	**% of total**	**Tons**	**% of total**
Europe	813,7	38%	1,014,4	41%	1,122,3	43%	1,175,0	39%	1,266,1	41%
North America	767,8	36%	831,3	34%	909,3	35%	1,016,4	34%	1,050,8	34%
Asia	509,0	23%	533,1	22%	510,8	20%	757,4	25%	710,5	23%
Latin America	21,4	1%	21,6	1%	8,4	1%	10	0%	4	0%
Total Exports	**2,119,9**	**98%**	**2,400,4**	**98%**	**2,550,8**	**98%**	**2,958,8**	**98%**	**3,031,4**	**98%**
Brazil	37,1	2%	49,6	2%	39,7	2%	53,3	2%	69	2%
Total	**2,149,0**	**100%**	**2,450,0**	**100%**	**2,590,6**	**100%**	**3012,1**	**100%**	**3,100,3**	**100%**

Our average net prices per ton of eucalyptus pulp for 2003, 2004, 2005, 2006 and 2007 were US$453, US$458, US$502, US$542, US$583, respectively.

In 2005, 2006 and 2007 approximately 2% of our sales volume was sold in the domestic market. One of our marketing strategies is to develop long-term relationships with customers that will purchase our production year after year. Stable long-term relationships permit us to reduce our marketing expenses, to better understand our customers needs, and to take advantage of our competitive strengths, including the consistency of our pulp and our efficient logistic and technical support to our clients. In 2007 and 2006, our ten largest costumers accounted for approximately 83% and 80% of our sales, by volume, respectively, and for those years our three largest customers accounted for approximately 57% and 55% of our sales, by volume, respectively. These customers include leading North American tissue manufacturers and leading global manufacturers of printing and writing paper. We believe that the loss of any of these customers could have a material adverse effect on our results of operations.

In 2005, 2006 and 2007, demand for our pulp has been in line with our production capacity; however, we cannot guarantee that such balance between demand and production capacity will be maintained in the future. We have long-term sales contracts with some of our customers, including several of our largest customers. These contracts generally provide for sales of specified amounts of pulp at prices announced from time to time by us, which are in line with the prevailing market prices for pulp sold to customers in the geographic area of the purchaser under the contract. Early termination is provided for in the contracts in the event of a material breach, the insolvency of one of the parties or force majeure events of extended duration. Certain sales contracts include provisions that permit us to reduce the quantities to be shipped if sales to the purchaser and our affiliates would exceed a specified percentage of our annual production capacity.

We have sought to diversify our sales among different market segments, such as consumer products (for example, tissue paper), specialty papers and high quality printing and writing papers. Producers of these products, as opposed to producers of commodity papers, value the consistency of our pulp as well as the reliability of our service.

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The following table shows the breakdown by end uses of our pulp production in 2003, 2004, 2005, 2006 and 2007.

	2003	2004	2005	2006	2007
Tissue	55%	55%	57%	57%	58%
Printing, and Writing Paper	26%	22%	22%	21%	23%
Specialty Papers(1)	18%	22%	21%	22%	19%
Cartonboard	1	1	-	-	-
	100%	100%	100%	100%	100%

(1) Includes liquid packaging board, carbonless paper, base paper for laminated paper and coated wood-free specialties.

Competition

While we compete with other producers of bleached hardwood kraft market pulp, our most direct competitors are other producers of eucalyptus pulp due to the special characteristics of this fiber. To a lesser degree, all producers of hardwood pulp compete with producers of softwood pulp and with other raw materials, such as recycled paper.

Competition is based primarily on quality (particularly consistency of product), service, price and reliability. We and other Brazilian eucalyptus pulp producers have significant cost advantages over producers in other regions. See Raw Materials Wood. We, however, do not generally compete on the basis of price alone. Instead, we emphasize quality, reliability and stable long-term relationships with customers.

If demand for recycled paper increases in the future, demand for pulp could be adversely affected. While no assurance can be given, we believe that increases in demand for recycled paper would not materially affect our results of operations, at least in the near future, because (i) it is more costly to produce recycled paper using current technology due to the high costs of sorting out wastes and de-inking the recycled fiber, and (ii) customers are predominantly manufacturers of higher-quality paper products such as premium tissue paper, coated papers and specialty papers, which are less likely to use recycled fibers for their products.

Bleached Eucalyptus Kraft Market Pulp (BEKP)

We are the largest producer and exporter of bleached eucalyptus kraft market pulp in the world. Our main competitors in this market are located in Brazil, Portugal, Chile and Spain and are listed by country (without any priority as to order) in the following table:

Producer	**Country**
Celulose Nipo-Brasileira S.A - CENIBRA Suzano Papel e Celulose S.A	Brazil Brazil
Jari Celulose S.A.	Brazil
Votorantim Celulose e Papel S.A.	Brazil
Empresa de Celulose e Papel de Portugal SGPS, S.A. (Portucel) Celulose Beira Industrial S.A.	Portugal Portugal
CMPC Papeles S.A.	Chile
Celulosa Arauco y Constituicíon SA. Empresa Nacional de Celulosas S.A. Grupo Rottneros (Miranda mill)	Chile Spain Spain

Management estimates that the five major producers of bleached eucalyptus kraft market pulp in the world (i.e., Aracruz, CENIBRA, Empresa Nacional de Celulosas S.A., CMPC, and Votorantim Celulose e Papel S.A) currently account for 55% of the total world production capacity of bleached eucalyptus kraft market pulp. Management estimates that in 2007, we accounted for 23% of the world production capacity of bleached eucalyptus kraft market pulp, 6% of the world production capacity of chemical market pulp and 12% of the world production capacity of bleached hardwood kraft market pulp.

Bleached Hardwood Kraft Market Pulp

To the extent that pulp from other hardwoods can be substituted for the slightly more expensive bleached eucalyptus kraft pulp, we also compete with producers of pulp from other hardwoods. Such competition is based more on cost and less on quality or suitability of the pulp for use in higher quality paper products. Although bleached hardwood kraft market pulp is produced in most regions of the world, the dominant producers are located in North America, Latin America, Western Europe, which in 2007 are expected to have accounted for 72% in the aggregate, and 15%, 38% and 18% respectively, of the world s total bleached hardwood kraft market pulp production capacity. Producers in the United States sold approximately 2,156,000 tons during 2005, 2,082,000 tons in 2006 and 2,032,000 in 2007 while Brazilian producers sold approximately 5,237,000, 5,774,000 and 6,700,000 tons respectively, in such periods. Several of our competitors in this market are larger than we are and may have greater economic and other resources than we do.

Worldwide production capacity for bleached hardwood kraft market pulp grew approximately 4,5% per year from 1997 to 2007, totaling 25.8 million tons, and is expected to grow at an annual rate of 8,2% during the period of 2007 to 2010 (or approximately 6,8 million tons in total during this period). Approximately 72% of this growth in capacity is expected to occur in Latin America, where bleached eucalyptus kraft market pulp capacity is expected to grow from approximately 13,7 million tons in 2007 to approximately 19,5 million tons in 2010. Worldwide demand for bleached hardwood kraft market pulp is expected to grow by 5,5% from 2007 through 2010, adding 4,2 million tons to the current demand.

Environmental and Other Regulatory Matters

Our mill and forestry operations are subject to federal, state and local laws, regulations and permit requirements relating to the protection of the environment. Federal Law No. 6,938, dated August 31, 1981 established strict liability for environmental damage, mechanisms for enforcement of environmental standards and licensing requirements for activities that are effectively or potentially damaging to the environment. Environmental laws and regulations also govern the conduct of forest operations and the protection of Brazilian fauna and flora. A violation of environmental laws and regulations may result in fines and penalties which may be material. Federal Law No. 9,605, dated February 12, 1998 provides that individuals or entities whose conduct or activities cause harm to the environment are subject to criminal and administrative sanctions and are liable for any costs to repair the damages resulting from such harm. Criminal sanctions for individuals and entities that commit environmental crimes range from fines to imprisonment (individuals) or dissolution (legal entities). In addition, Federal Law No. 9,605 also establishes that the corporate structure of a company may be disregarded if the shareholding structure impedes the recovery for harm caused to the environment. We are not aware of any successful assertion of claims against shareholders under this provision of Federal Law No. 9,605.

The States of Espírito Santo and Rio Grande do Sul have state legislation that requires local manufacturing concerns to obtain various permits including operating permits for manufacturing facilities. Pursuant to those respective state laws, state authorities are empowered to regulate a company s operations by prescribing company-specific environmental standards in such company s operating permit. The operating permits require that we maintain certain emissions, effluent and waste disposal standards.

On February 10, 1998, the State of Espírito Santo issued to us a two-year operating permit for Fiberlines A and B at Barra do Riacho Unit, which was renewed for an additional five years commencing on February 10, 2000. On July 1, 2002 the State of Espírito Santo issued to us a four-year operating permit for Fiberline C at Barra do Riacho Unit, valid until July 2006. Nevertheless, on May 6, 2005, reviewed in July, 2007, the State of Espírito Santo issued to us a unified four-year operating permit for Barra do Riacho Unit (Fiberlines A, B and C), which is valid until May 2009. During 2002, supplemental environmental licenses were obtained for Fiberline C Expansion Project relating to our industrial installations.

On June 20, 2005 the State of Rio Grande do Sul issued to us an operating permit for Guaíba Unit, valid until June 2009.

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Beginning in March 1997, we became subject to an environmental audit every three years in the State Espírito Santo. The audit is conducted by subcontracted auditors, approved by the Environmental Secretary of the State of Espírito Santo, or SEAMA. The audit was not carried out in 2000, since SEAMA has not published the result of the 1997 audit. The 2000 audit was conducted in June 2001. The most recent audit was conducted in November 2004. In the State of Rio Grande do Sul we became subject to an environmental audit every year, since the year 2002. The audit is conducted by subcontracted auditors, approved by the Brazilian Environmental Institute, or IBAMA. The audit has been regularly carried since 2002. The last audit was conducted in December 2006. In 2007 we had problems to schedule the audit. We are replanning it for first quarter of 2008.

Our forestry activities are regulated by the Brazilian federal government and the governments of the States of Espírito Santo, Minas Gerais, Bahia and Rio Grande do Sul. Our operating permit for our forest operations in Espírito Santo was renewed for a six-year period commencing on October 4, 2004. Presently the Company has obtained from the environmental state agencies from the states Espírito Santo, Minas Gerais and Bahia 21 implementation and operational permits for implanting 327 projects accounting for 67,893 hectares of eucalyptus plantations. In Rio Grande do Sul State, although the licensing process is not yet fully defined by the environmental agency, in 2007 there were 50 planting permits legally issued to Aracruz Celulose.

We also entered into contracts with farmers in the State of Espírito Santo, Minas Gerais, Bahia, Rio Grande do Sul and Rio de Janeiro according to which the farmers have agreed to grow trees for sale to us. See "Eucalyptus Forests". Regarding our operating permit for the Forestry Partners Program, the licensing process for renewing it is still under negotiation and we expect to conclude it during 2008.

Plantings may be undertaken only according to a plan presented to and approved by the appropriate governmental authorities. In accordance with federal law, at least 20% of our landholdings, at any given time, must be preserved as native ecosystems (uncultivated or restored with indigenous species). We currently exceed this requirement, since such land accounts for approximately 35% of our total landholdings.

We believe that we are in compliance in all material respects with all applicable environmental regulations. In addition, environmental considerations are fundamental to our development of new technologies. Our integrated pest management relies on biological control of pests and diseases. Soil and plant nutrients are continuously monitored to guarantee an adequate balance. At the Units, methods for the evaluation of environmental effects of effluents on receiving detriments have been developed and used. The origins of pulp and effluent toxicity have been studied, considering all possible sources, from the raw material (wood) to bleaching effluents. In addition, environmental quality is considered in the development of new technologies and products. Pulp products are continuously evaluated in terms of their possible effects on the quality of effluents in our customers paper machines as well.

In 1996, the State of Bahia granted us a permit for the location of APM, the sawmill company of which we currently hold 1/3 (one third) of the shares. In 1998, the State of Bahia granted an operating permit for APM, valid until August 2003. In June 2003, the State of Bahia renewed APM's operating permit, valid until June 2007. See Business Strategy.

As part of the licensing process in connection with the Fiberline C Expansion Project, we contracted independent consultants to prepare the required environmental impact assessment reports. Those reports were discussed in public hearings (two in Bahia and one in Espírito Santo) in 2000 as well as during six public meetings with communities in both states. There was ample discussion at each meeting of the environmental and social questions involved. The results of the discussions were taken into consideration by the government regulatory agencies in their technical analyses and their subsequent approval of the permits.

Also for the Fiberline C Expansion Project we obtained 327 project permits for forest plantations, of which 74 were incorporated in operating licenses issued by the Espírito Santo Agriculture, Cattle-Raising and Forest Protection Institute (IDAF), 235 were projects incorporated in installation licenses issued by the Bahia Environmental Resources Center (CRA-BA) and 18 projects approved for operating licenses by the Minas Gerais State Forestry Institute (IEF-MG).

Aracruz' forest management is certified by the Bureau Veritas Quality International (BVQI) in the standard NBR 14789 - Principles, Criteria and Indicators for Plantation Forests of the Brazilian System of Forest Certification (CERFLOR/PEFC System), regulated by the National Institute of Metrology (INMETRO), the federal official agency for metrology affairs. The certification process for each defined scope includes

certification audits, public meetings with local stakeholders participation, public reports publication and annual monitoring audits for the maintenance of the CERFLOR certificate.

In October 2003, BVQI approved CERFLOR certification covering all of the Company's own plantations in the State of Bahia. The certificate emitted by INMETRO was received in March 2004. We initiated this certification process in August 2003, including pre-audit, initial audit and a certification audits. The certification audit was publicized through local radio stations and newspapers as well as the sending out of letters to more than 600 persons or entities. Five public meetings were held in respect of the Certification, with the presence of more than 300 persons. In October 2004 the first annual monitoring audit for the maintenance of CERFLOR certification in Bahia took place. The certification was maintained and a new public report was made available to the general public on the internet.

The CERFLOR Certification for plantations in Espírito Santo State was approved by BVQI in June 2005. The certification process was initiated in November 2004 with the realization of six public meetings and an initial audit. The certification audit was held in January 2005. The audit report was made available for the public on the internet for 90 days. The certificate emitted by INMETRO was received in June 2005.

In October 2005, we had the second annual monitoring audit for the maintenance of CERFLOR certification in Bahia and the first annual monitoring audit for the maintenance of CERFLOR certification in Espírito Santo State. In August 2005, we started the CERFLOR Certification for plantations in Rio Grande do Sul. Four public meetings were held in respect of this Certification, with the presence of more than 60 persons. The certificate emitted by INMETRO was received in May 2006. In September 2005, we started the CERFLOR Certification for plantations in Minas Gerais State. Two public meetings were held in respect of this Certification, with the presence of more than 100 persons. The certificate emitted by INMETRO was also received in May 2006.

In 2006 "BVQI" granted to the Company the chain of custody certification for both Barra do Riacho and Guaíba Units. The chain of custody was certified by the "BVQI" in the standard NBR 14790 of the CERFLOR/PEFC System. This certification assures that at least 70% of the final product (pulp) comes from certified forests.

In 2007, the annual monitoring audits for the maintenance of CERFLOR certification in all States (Bahia, Espírito Santo, Minas Gerais and Rio Grande do Sul) were integrated, and ended up with the maintenance of all of the certificates. Today, the total amount of certified area is 357,585 ha (210,610 ha of plantations) in Barra do Riacho Unit and 100,764 ha (61,115 ha of plantations) in Guaíba Unit.

The Company presents, in the table below, its areas certified by CERFLOR as well as the base period of such certifications:

		Certified area (ha)					
		Original certified area:	**2004**	**2005**	**2006**	**2007**	**2008**
State	**Municipalities**	**Total area (plantations) (base period)**	**Total area (plantations) (base period)**	**Total area (plantations) (base period)**	**Total area (plantations) (base period)**	**Total area (plantations) (base period)**	**Total area (plantations) (base period)**
	Mucuri, Nova Viçosa,						
	Prado, Alcobaça,	166.089	166.089	166.685	170.922	172.348	172.588
Bahia	Caravelas, Ibirapuã,	(95.322)	(95.322)	(95.753)	(98.104)	(98.874)	(98.697)
	Teixeira de Freitas	(12/09/2003)	(12/09/2003)	(31/07/2004)	(31/07/2005)	(31/10/2006)	(31/10/2007)
	and Vereda						
	Aracruz, Santa Teresa,						

	Santa Leopoldina,						
	Fundão, Serra,						
	Sooretama, Vila						
	Valério, Mucurici,	147.537		147.537	168.531	170.228	170.914
Espírito	Conceição da Barra,	(93.778)		(93.778)	(107.218)	(106.837)	(105.247)
Santo	Linhares, Montanha,	(31/12/2004)		(31/12/2004)	(31/07/2005)	(31/10/2006)	(31/10/2007)
	Pinheiros, São						
	Mateus, Rio Bananal,						
	Jaguaré and Pedro						
	Canário		-				

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Minas	Nanuque and Carlos	13.617(6.410)			13.617(6.410)	14.083(6.629)	14.083(6.665)
Gerais	Chagas	(31/07/2005)			(31/07/2005)	(31/10/2006)	(31/10/2007)
			-		-		
	Guaíba, Barra do						
	Ribeiro, Butiá, Arroio						
	dos Ratos, Mariana						
	Pimentel, Eldorado do						
	Sul, Minas do Leão,						
	Pantano Grande, São						
	Jerônimo, Tapes,						
	Charqueadas, Dom					89.598	
Rio	Feliciano, Barão do	68.744			68.744		100.764
Grande	Triunfo, General	(44.192)	-	-	(44.192)	(57.430)	(61.115)
do Sul	Câmara, Triunfo,	(31/10/2005)			(31/10/2005)	(31/10/2006)	(31/10/2007)
	Sentinela do Sul,						
	Cerro Grande do Sul,						
	Cachoeirado Sul,						
	Sertão Santana, Rio						
	Pardo, Encruzilhada						
	do Sul, Camaquã,						
	Viamão and Porto						
	Alegre						

In October 2005 CERFLOR Certification has gained international endorsement through the Program for the Endorsement of Forest Certification Schemes - PEFC Council, the global assessment organization for forest certification systems. Such endorsement attests that CERFLOR certification is an independent proof that the Company's certified plantations are subject to sustainable forest management preserving the ecological, social and economical functions of forests.

Insurance

We believe that our insurance coverage of our production facilities and forests is in line with Brazilian market and international pulp industry standards.

Our forests are fully covered by insurance. The insurance limit was set at US$10 million for our forest areas based on the historically low rates of loss and the large spread of the risk.

In 2003, the Company received the Highly Protected Risk (HPR) seal of approval from FM Global. The certification, which is renowned worldwide in the field of insurance, attests to the Company s low risk of interruption of its operations as result of an industrial accident. The

Company is the first Brazilian company to earn the certificate from FM Global, the world's largest property risk insurance company and leader in the field of risk management and loss prevention.

In 2005, following the same pattern and principals of the Company's risk management practices, Veracel was also granted the HPR seal of approval from FM Global, confirming the low levels of risk in its operations.

C. Organizational Structure

Significant Subsidiaries

Our operations are conducted by Aracruz Celulose S.A., as the controlling and principal operating Company. The following table sets forth the significant subsidiaries owned directly or indirectly by us and our ownership interest in each of them as of December 31, 2007:

	As of December 31, 2007	
	Total Capital (in percentages)	Voting (in percentages)
Portocel Terminal Especializado de Barra do Riacho S.A.(1)	51%	51%
Mucuri Agroflorestal S.A.(1)	100%	100%
Aracruz Produtos de Madeira S.A. (formerly named Tecflor Industrial S.A.)(1) (8)	33,33%	33,33%
Veracel Celulose S.A.(1) (8)	50%	50%
Aracruz Trading S.A.(2)	100%	100%
Aracruz Celulose (USA), Inc.(3)	100%	100%
Aracruz (Europe) S.A.(4)	100%	100%
Aracruz Trading International Ltd.(5)	100%	100%
Riocell Trade (6)	100%	100%
Ara Pulp - Com. de Importação e Exportação, Unipessoal Ltda(7)	100%	100%
Arcel Finance Limited(9)	SPE	SPE
Aracruz International Finance Company(10)	100%	100%

(1) Incorporated in Brazil.

(2) Incorporated in the Republic of Panama.

(3) Incorporated in the United States under the laws of the State of Delaware.

(4) Incorporated in Switzerland.

(5) Incorporated in Hungary

(6) Incorporated in England

(7) Incorporated in Portugal

(8) Accounted as per the equity method.

(9) Dissolved in November, 2007. See notes 1 (b) to the consolidated financial statements.

(10) Incorporated in the Cayman Islands.

D. Property, Plant and Equipment

In December 1999, we moved our headquarters from Rio de Janeiro to the Municipality of Aracruz in the Brazilian coastal State of Espírito Santo, where our main production unit is located. We maintain offices in São Paulo for our financing, administrative and trading activities.

Our principal production facilities consist of a eucalyptus pulp mill located in Aracruz, State of Espírito Santo, which has three production units, each with three production lines. When operating at full capacity, this mill can process over 23,000 solid cubic meters of timber each day. We also have one mill in Guaíba, State of Rio Grande do Sul that has one production unit, with one production line. When operating at full capacity, this mill can process over 6,700 solid cubic meters of timber each day.

As of December 31, 2007, we had an aggregate principal amount outstanding of approximately US$426,4 million under certain loans granted to us by BNDES, which loans are secured by liens on our industrial site in the Municipality of Aracruz. See Item 7B. Related Party Transactions.

As of December 31, 2007, we owned approximately 486,197 hectares of forest and other land in the Brazilian States of Espírito Santo, Bahia, Minas Gerais and Rio Grande do Sul, of which approximately 286,099 hectares are planted with eucalyptus forests. See Business Overview Eucalyptus Forests. The pulp mill in Barra do Riacho Unit is located approximately 1.5 kilometers from the port facilities at Barra do Riacho (Portocel), of which 51% are owned by us. We have a terminal facility integrated to the Guaíba Unit mill that is used to load the barges that transport the pulp to Rio Grande port.

See Environmental and Other Regulatory Matters for the environmental rules and regulations affecting our operations.

ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS

The following discussion and analysis should be read in conjunction with our consolidated financial statements, including the respective notes thereto, included elsewhere in this annual report, and in conjunction with the discussion of the method of presentation of financial information under Item 3.

Overview

We are the world s largest producer of bleached hardwood kraft market pulp. During 2007, we produced approximately 2,569,000 tons of BEKP (3,095,000 tons including 50% of Veracel's pulp production),

an 0,3% decrease from 2006, when we had produced approximately 2,616,000 tons of BEKP (3,104,000 tons including 50% of Veracel's pulp production), an 11% increase from 2005, when we had produced approximately 2,552,000 tons of BEKP (2,786,000 tons including 50% of Veracel's pulp production), a 12% increase from 2004, when we had produced approximately 2,497,000 tons of BEKP. Pulp sales for 2007 were approximately 3,104,000 tons, a 3% increase as compared to 3,021,000 tons in 2006, a 16% increase as compared to 2,605,000 tons in 2005, which had represented a 6% increase when compared to 2004 pulp sales of 2,450,000 tons. Export pulp sales in 2007, 2006 and 2005 were approximately 98% of total sales.

In 2007, the Company sold US$ 1,808.0 million of eucalyptus pulp compared to US$ 1,632.28 million in 2006 and US$ 1,300.2 million in 2005.

The Company's volume and price of pulp sales during 2007 were higher than in 2006. The Company's average list price increased by approximately 10% in 2007 compared with the average in 2006.

The primary factors affecting our results of operations are:

- prevailing world market prices for pulp;
- the amount of pulp produced and sold by us, and
- our costs of production, which primarily consist of the costs of materials (primarily wood and chemicals) and depreciation.

The prices that we are able to obtain for our pulp depend upon prevailing world market prices, which historically have been cyclical, with prices subject to significant fluctuations over relatively short periods of time. See Item 4B. Business Overview Market Overview International Markets.

We believe that we are one of the lowest cost producers of bleached kraft market pulp in the world. Our relatively low production costs are due to economies of scale, advanced forestry techniques, a comparatively short regional harvest rotation and low energy and chemical costs. See Item 4B. Business Overview General.

Recently Issued Accounting Pronouncements under U.S. GAAP

In September 2006, the FASB issued SFAS No. 157 Fair value measurements , which defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. This Statement applies under other accounting pronouncements that require or permit fair value measurements, the Board having previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. Accordingly, this Statement does not require any new fair value measurements.

This Statement is effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The adoption of such pronouncement will not generate a material impact on the Company s financial position.

In February 2007, the Financial Accounting Standards Board (FASB) issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of SFAS No. 115 (SFAS 159). SFAS 159 permits companies to choose to measure many financial instruments and certain other items at fair value in order to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This Statement shall be effective as of the beginning of each reporting entity s first fiscal year that begins after November 15, 2007. The adoption of such pronouncement will not generate a material impact on the Company s financial position.

In December 2007, the Financial Accounting Standards Board (FASB) issued SFAS No. 141 (revised 2007), Business Combination , which replaces FASB Statement No. 141, Business Combinations. This Statement retains the fundamental requirements in Statement 141 that the acquisition method of accounting (which Statement 141 called the purchase method) be used for all business combinations and for an acquirer to be identified for each business combination. This Statement defines the acquirer as the entity that obtains control of one or more businesses in the business combination and establishes the acquisition date as the date that the acquirer achieves control. Statement 141 did not define the acquirer, although it included guidance on

identifying the acquirer, as does this Statement. This Statement s scope is broader than that of Statement 141, which applied only to business combinations in which control was obtained by transferring consideration. The result of applying Statement 141 s guidance on recognizing and measuring assets and liabilities in a step acquisition was to measure them at a blend of historical costs and fair values, a practice that provided less relevant, representationally faithful, and comparable information than will result from applying this Statement. In addition, this Statement s requirement to measure the noncontrolling interest in the acquiree at fair value will result in recognizing the goodwill attributable to the noncontrolling interest in addition to that attributable to the acquirer, which improves the completeness of the resulting information and makes it more comparable across entities. By applying the same method of accounting, the acquisition method to all transactions and other events in which one entity obtains control over one or more other businesses, this Statement improves the comparability of the information about business combinations provided in financial reports. This Statement applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. An entity may not apply it before that date. The effective date of this Statement is the same as that of the related FASB Statement No. 160, Noncontrolling Interests in Consolidated Financial Statements. The Company will apply such pronouncement on a prospective basis for each new business combination.

In December 2007, the Financial Accounting Standards Board (FASB) issued SFAS No. 160, Noncontrolling Interests in Consolidated Financial Statements an amendment of ARB No. 51 , which clarifies that a noncontrolling interest in a subsidiary is an ownership interest in the consolidated entity that should be reported as equity in the consolidated financial statements. This Statement is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008 (that is, January 1, 2009, for entities with calendar year-ends). Earlier adoption is prohibited. The effective date of this Statement is the same as that of the related Statement 141(R). This Statement shall be applied prospectively as of the beginning of the fiscal year in which this Statement is initially applied, except for the presentation and disclosure requirements. The presentation and disclosure requirements shall be applied retrospectively for all periods presented. The Company is currently evaluating the impact of such new pronouncement in its consolidated financial statements.

Discussion of Critical Accounting Policies and Estimates

In connection with the preparation of the financial statements included in this annual report, we have relied on estimates and assumptions derived from historical experience and various other factors that we deemed reasonable and relevant. We are required to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses during the reporting periods and require the disclosure of contingent assets and liabilities as of the date of the financial statements. The Company's consolidated financial statements therefore include estimates concerning such matters as the selection of useful lives of property, plant and equipment, provisions necessary for asset impairments, contingent liabilities, employee postretirement benefits and other similar evaluations. Although we review these estimates and assumptions in the ordinary course of business, the portrayal of our financial condition and results of operation often requires our management to make judgments regarding the effects of matters that are inherently uncertain on the carrying value of our assets and liabilities. Actual results may differ from those estimated under different variables, assumptions or conditions. Note 1 to the Consolidated Financial Statements includes a summary of the significant accounting policies and methods used in the preparation of the Consolidated Financial Statements. In order to provide an understanding about how management forms its judgments about future events, including the variables and assumptions underlying the estimates, and the sensitivity of those judgments to different variables and conditions, we have included below a brief discussion of the more significant accounting policies and methods used by us.

Legal Contingencies

We are currently involved in certain legal proceedings. As discussed in note 14 to our financial statements, we have accrued our estimate of the probable costs for the resolution of these claims. This estimate is based upon an analysis of potential results, assuming a combination of litigation and settlement strategies. We do not believe these proceedings will have a material adverse effect on our financial position. It is possible, however, that future results of operations could be materially affected by changes in our assumptions and the effectiveness of our strategies with respect to these proceedings.

Fair Value of Financial Instruments

With respect to financial instruments, we must make assumptions as to future foreign exchange and interest rates. For a discussion of the possible impact of fluctuations in the foreign exchange and interest rates on our principal financial instruments and positions, see Item 11. Quantitative and Qualitative Disclosures About Market Risk.

Impairment testing of goodwill

The Company annually evaluates the carrying value of goodwill during and between annual evaluations if events occur or circumstances change that would more likely than not reduce the fair value of the reporting unit below its carrying amount. Such circumstances could include, but are not limited to: (1) a significant adverse change in legal factors or in business climate, (2) unanticipated competition, or (3) an adverse action or assessment by a regulator. When evaluating whether goodwill is impaired, the Company compares the fair value of the reporting unit to which the goodwill is assigned to the reporting unit s carrying amount, including goodwill. The fair value of the reporting unit is estimated using a discounted cash flows approach. If the carrying amount of the reporting unit exceeds its fair value, then the amount of the impairment loss must be measured. The impairment loss would be calculated by comparing the implied fair value of reporting unit goodwill to its carrying amount. In calculating the implied fair value of reporting unit goodwill, the fair value of the reporting unit is allocated to all of the other assets and liabilities of that unit based on their fair values. The excess of the fair value of a reporting unit over the amount assigned to its other assets and liabilities is the implied fair value of goodwill. An impairment loss would be recognized when the carrying amount of goodwill exceeds its implied fair value. The Company s evaluation of goodwill completed during the year resulted in no impairment losses. The Goodwill registered in the Company s financial statements mainly refers to the acquisition of Riocell S.A.

Recoverability of long-lived assets

Management reviews long-lived assets to be held and used in the Company s business activities, for the purpose of determining and measuring impairment on a recurring basis or when events or changes in circumstances indicate that the carrying value of an asset or group of assets may not be recoverable. Write-down of the carrying value of assets or groups of assets is made if and when appropriate in accordance with Statement of Financial Accounting Standards Nº 144, Accounting for the Impairment or Disposal of Long-Lived Assets, or SFAS 144. SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. In accordance with SFAS 144, the carrying value of long-lived assets is considered impaired when the anticipated undiscounted cash flow from such asset is separately identifiable and is less than its carrying value. In that event, a loss is recognized based on the amount by which the carrying value exceeds the fair value of the assets. Fair value is determined primarily by using a discounted cash flow analysis. During 2007, as a consequence of the devaluation of the US dollar against Brazilian *reais*, we have performed the anticipated undiscounted cash flow test and we have concluded that the carrying amount of our assets is still recoverable.

Useful lives of property, plant and equipment

Adopted depreciation rates are based on estimated useful lives of the underlying assets, derived from historical information available to the Company, as well as known industry trends. The Company describes the depreciation rates it applies to its property, plant and equipment in Note 1(h) to its consolidated financial statements. The sensitivity of an impact in changes in the useful lives of property, plant and equipment was assessed by applying a hypothetical 10% increase in depreciation rate existing on December 31, 2007. This hypothetical change would result in an incremental increase in the annual depreciation expense of US$25 million in the year of the change.

Brazilian Economic Environment

The Brazilian economy has been characterized by volatile economic cycles. Since the introduction of the real as a Brazilian currency in July 1994, the Central Bank adopted tight monetary policy as a necessary measure to ensure the country continues to control inflation. Therefore, a more stable economic environment is clearly being observed. After January 1999, when the Central Bank adopted the free flotation of the Dollar exchange rates, the internal interest rates started to be the main tool for inflation control, and the Central Bank started to act preventively and most of the time was successful in bringing inflation back in line or little bit higher with targets.

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The Brazilian economy has also been characterized by frequent and occasionally drastic intervention by the Brazilian government. The Brazilian government has often changed monetary, taxation, credit, tariff and other policies to influence the course of Brazil s economy. For example, the Brazilian government has the authority, when a serious imbalance in Brazil s balance of payment occurs, to impose restrictions on the remittance to foreign investors of the proceeds of their investments in Brazil, and on the conversion of Brazilian currency into foreign currencies. Changes in monetary, taxation, credit, tariff and other policies could adversely affect our business, as could inflation, currency and interest rate fluctuations, social instability and other political, economic or diplomatic developments, as well as the Brazilian government s response to such developments.

Rapid changes in Brazilian political and economic conditions can continue and will require continued emphasis on assessing the risks associated with our activities and adjusting our business and operating strategy. Future developments in Brazilian government policies, including changes in the current policy and incentives adopted for financing the export of Brazilian goods, or in the Brazilian economy, over which we have no control, may materially adversely affect our business. Brazilian economic conditions may be affected negatively by events elsewhere, especially in emerging markets. See Item 3D. Risk Factors Risk Factors Relating to Brazil.

The tax reform approved a few years ago by the Brazilian government resulted in Law No. 10,833/03, extending to Brazil s Social Security Financing Contribution (*Contribuição para o Financiamento da Seguridade Social* COFINS) the non-cumulative regime already mandatory since 2002 for contributions made to Social Integration Program (*Programa de Integração Social e de Formação do Patrimônio do Servidor Público* PIS/PASEP), as per Law No. 10,637/02. Law No. 10,833/03 also provided an increase in the tax rate for COFINS now at 7.6% on revenues of Brazilian companies in general (the rate was formerly 3%). Although the tax (PIS/COFINS) is not assessed on export transactions, the Company as a result of the non-cumulative regime, presented a PIS and COFINS credit position, lowering the tax burden for the fiscal year ended in 2004, notwithstanding the increase in tax rates. In June 2005, the Brazilian government edited a Provisional Measure known as "*MP do Bem*", meaning that the proposal contained some good measures for the economy, such as suspending the collection of PIS and COFINS in the acquisition of new machines and equipment (allocated to the Company s fixed assets) by preponderantly exporting companies and granting various types of tax incentives for technological innovation. This Provisional Measure has been converted into Law No. 11,196 in November 2005. According to the definition in Law No. 11.196, the Company is a preponderantly exporting company and as such may reduce the tax burden on future investments in new machines and equipment acquired as fixed assets, benefiting from the suspension in the collection of PIS and COFINS.

As from August 2, 2004, PIS and COFINS rates were reduced to zero in relation to financial revenues obtained by legal entities subject to the non-cumulative regime (essentially large companies), exception made for financial revenues deriving from interest on net equity and hedge transactions. As from April 1, 2005, financial revenues from hedge transactions were included within such zero percent rates.

Up to December 2007, financial operations were subject to Provisional Contribution over Financial Operations (CPMF) at 0.38% tax rate. Due to the rejection by the Brazilian Senate of the proposal of extension of such tax, as from January 2008 said operations will no longer be charged.

Nevertheless, in order to compensate the loss in the tax revenues as a result of the CPMF's extinction, as of January 2008, credit, exchange and insurance operations will be subject to an additional rate of 0.38% of Tax on Financial Transactions (IOF), same rate of the extinguished CPMF. The Company believes that this change will not cause a relevant impact over it.

Effects of Inflation and Currency Exchange Fluctuations

Until July 1994, Brazil had for many years experienced high and generally unpredictable rates of inflation and steady devaluation of its currency relative to the U.S. dollar. The following table sets forth Brazilian inflation as measured by the *Indice Geral de Preço-Mercado*, the

General Market Price Index or IGP-M, and the devaluation of Brazilian currency against the U.S. dollar for the periods shown:

	2003	2004	2005	2006	2007
Inflation (General Market Price Index)	8.7%	12.4%	1.21%	3.9%	7.8%
Devaluation/(appreciation) (R$ v. US$)	(18.2)%	(8.1)%	(11.8)%	(8.7)%	(17.2)%

A. Operating Results

Results of Operations for the Year Ended December 31, 2007 Compared with the Year Ended December 31, 2006

The table below shows the Company s income statements for the years 2005, 2006 and 2007:

			US$ thousands
Statement of Operations Data	**2005**	**2006**	**2007**
Operating revenues			
Domestic	62,019	77,431	137,086
Export	1,469,646	1,845,026	2,007,017
Gross operating revenues	1,531,665	1,922,457	2,144,103
Sales taxes and other deductions	(186,432)	(241,624)	(260,328)
Net operating revenues	1,345,233	1,680,833	1,883,775
Operating Costs and expenses			
Cost of sales	783,578	1,037,896	1,190,957
Selling	64,430	74,005	78,832
Administrative	33,820	57,020	58,708
Other, net	16,313	12,514	(38,624)
Total operating Costs and expenses	898,141	1,181,435	1,289,873
Operating income	**447,092**	**499,398**	**593,902**
Non-operating (income) expenses			
Financial income	(125,439)	(181,733)	(168,037)
Financial expenses	137,276	149,719	100,864
Gain on currency remeasurement, net	(21,386)	(7,641)	(908)
Other, net	(778)	(7)	(61)
Total non-operating (income) expenses	(10,327)	(39,662)	(68,142)

Inflation and exchange rate variations have had, and may continue to have, substantial effects on our financial condition and results of operations.

Inflation and exchange rate variations affect our monetary assets and liabilities denominated in *reais*. The value of such assets and liabilities as expressed in U.S. dollars declines when the *real* devalues against the U.S. dollar and increases when the *real* appreciates. In addition, many financial instruments denominated in *reais* are indexed for inflation. In periods of devaluation of the *real*, we report (a) a remeasurement loss on *real*-denominated monetary assets, which are offset, at least in part, by monetary indexation of *real*-denominated financial instruments and (b) a remeasurement gain on *real*-denominated monetary liabilities, which is offset, at least in part, by the monetary indexation of *real*-denominated financial instruments.

At December 31, 2007, approximately 96% of our cash and cash equivalents and short-term investments were invested in *real* denominated deposits and financial assets. See Liquidity and Capital Resources Financial Strategy.

Income before income taxes, minority interest and equity in results of affiliated companies	457,419	539,060	662,044
Income tax expense	72,228	69,494	197,312
Minority interest	(31)	(544)	(10,522)
Equity in results of affiliated companies	(44,062)	(13,705)	(32,141)
Net income	**341,098**	**455,317**	**422,069**

The Company exports approximately 98% of its pulp sales volumes and its revenues are dollar-denominated. Net revenues reached a record of US$1,883.8 million, 12% higher than the amount obtained in 2006, due to an 8% increase in the average net pulp prices, representing US$127.9 million, and 3% of higher pulp sales volume, totaling US$47.9 million. The remaining US$27.2 million are related to other sales.

The cost of products sold (pulp), measured in US$/ton, was US$369/t, which represented an expansion of 11% over 2006, mainly due to US$19/t of the effect of the appreciation of the *real* against the dollar on the items of the cost structure correlated to the local currency (*real* - R$), higher pulp volume purchased from Veracel (US$8.8/t) and some raw materials, such as wood purchases from third parties, oil prices, chemicals and energy sources.

Selling (distribution and sales) expenses rose 6.5% in nominal values, reflecting the 3% increase in sales volume over the previous year and higher terminal expenses, partially offset by the effect of the appreciation of the real against the dollar over the period.

In 2007, general and administrative expenses were equivalent to 3.1% of total net revenues, compared to 3.4% in the previous year, mainly due to reductions in institutional advertising.

The result for other net operating expenses was a credit of US$38.6 million in 2007, US$51.1 million better than in the previous year, mainly due to the partial reversal of the provision for losses on ICMS tax credits, which are expected to be recovered in the short-term, considering the history of such transactions. During the year 2007, the Company sold approximately US$ 50 million in ICMS tax credits and it has the perspective of successfully closing other sales transactions.

Financial income also was favored by a gain of US$96 million on foreign exchange derivative operations for cash flow protection. In compliance with the Aracruz' financial policy as approved by the Board of Directors. This policy establishes that the Company is allowed to hedge its cash flow, utilizing a range of financial instruments (including derivatives and others), limited to a total of US$50 million in notional value per party and for a maximum period of 1 (one) year on NDF operations, as well as being restricted to banks based in G-7 countries and with a rating of "A-" or better. At the end of the year, the cash flow currency protection strategy, taking a short position in dollars totaling US$150 million, represented approximately 3 months of cash flow exposure to the local currency (real - R$).

The financial expenses in 2007 were 33% lower than in 2006, mainly due to the expenses linked to the pre-payment of the securitization program in 2006, and lower interest on loans and financing.

Currency re-measurement represented a gain of R$0.9 million, caused by the 17.1% devaluation of the dollar over the period, compared to gain of US$7.6 million in 2006, when the dollar devalued by 8.7% .

(US$ million)