Aracruz Celulose S.A.

Consolidated Financial Statements at December 31, 2004 and for the Year then ended and Report of Independent Registered Public Accounting Firm

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of
Aracruz Celulose S.A.

We have audited the accompanying consolidated balance sheet of Aracruz Celulose S.A. and subsidiaries ("the Company") as of December 31, 2004, and the related consolidated statements of income, changes in stockholders' equity and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the consolidated financial statements based on our audit. The financial statements of the Company for the years ended December 31, 2003 and 2002, were audited by other auditors whose report, dated January 12, 2004, expressed an unqualified opinion on those statements and included an explanatory paragraph that described a matter regarding the utilization of a fiscal benefit granted by the Northeast Development Agency (Agência de Desenvolvimento do Nordeste "ADENE"), discussed in Note 17 to the financial statements.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, based on our audit, such consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Company as of December 31, 2004, and the consolidated results of its operations and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

Rio de Janeiro, Brazil
January 11, 2005

Aracruz Celulose S.A.

Consolidated Balance Sheets

Expressed in thousands of United States dollars
(Except number of shares)

	December 31,	
Assets	**2003**	**2004**
Current assets		
Cash and cash equivalents	66.284	36.474
Short-term investments	285.991	412.110
Accounts receivable, net		
Related party	3.174	
Other	219.874	208.336
Inventories, net	131.486	126.220
Deferred income tax, net	13.181	9.853
Recoverable income and other taxes	20.464	36.984
Prepaid expenses and other current assets	2.280	3.136
	742.734	833.113
Property, plant and equipment, net	2.270.369	2.133.896
Investment in affiliated company	174.257	273.890
Goodwill	208.061	207.050
Other assets		
Long-term investments		1.601
Advances to suppliers	38.197	50.685
Deposits for tax assessments	14.319	17.369
Recoverable income and other taxes	1.548	6.675
Other	4.948	5.379
	59.012	81.709

	December 31,	
Liabilities and stockholders' equity	**2003**	**2004**
Current liabilities		
Suppliers	79.673	52.869
Payroll and related charges	16.245	15.486
Income and other taxes	24.120	42.123
Current portion of long-term debt		
Related party	55.190	51.567
Other	212.472	89.706
Short-term borrowings - export financing and other	118.306	3.767
Accrued finance charges	6.120	7.894
Interest on stockholders' equity payable		10.433
Other accruals	1.553	961
	513,679	274,806
Long-term liabilities		
Long-term debt		
Related party	208.076	178.588
Other	771.359	1.044.140
Tax assessments and litigation contingencies	94.500	130.846
Deferred income tax, net	26.467	50.645
Suppliers	15.222	14.118
Other	23.877	21.928
	1.139.501	1.440.265
Contingencies and Commitments (Note 16)		
Minority interest	292	300

Aracruz Celulose S.A.

Consolidated Balance Sheets

Expressed in thousands of United States dollars
(Except number of shares) **(Continued)**

		Stockholders' equity		
		Share capital - no-par-value shares authorized and issued		
		Preferred stock		
		Class A - 2003 – 38.137.170 shares: 2004 - 38.022.178 shares	31.199	31.105
		Class B - 2003 - 539.026.251 shares: 2004 - 539.141.243 shares	583.297	583.391
		Common stock - 2003 and 2004 - 455.390.699 shares	297.265	297.265
		Treasury stock		
		Class B preferred stock – 2003 and 2004 – 1.378.000 shares: and		
		Common stock – 2003 and 2004 - 483.114 shares	(2.288)	(2.288)
		Total share capital	909.473	909.473
		Appropriated retained earnings	334.246	619.527
		Unappropriated retained earnings	557.242	285.287
			1.800.961	1.814.287
3.454.433	3.529.658		3.454.433	3.529.658

The accompanying notes are an integral part of these consolidated financial statements.

Aracruz Celulose S.A.

Consolidated Statements of Income

Expressed in thousands of United States dollars
(Except number of shares and per-share amounts)

	Year ended December 31,		
	2002	**2003**	**2004**
Operating revenues			
Sales of eucalyptus pulp			
Domestic	17,126	42,401	66,083
Export	700,622	1,056,498	1,256,648
	717,748	1,098,899	1,322,731
Sales taxes and other deductions	(48,765)	(95,829)	(155,618)
Net operating revenues	668,983	1,003,070	1,167,113
Operating costs and expenses			
Cost of sales	468,875	592,555	700,333
Selling	28,242	38,617	53,850
Administrative	22,302	22,762	31,072
Provision for loss on ICMS credit	45,093	23,178	22,859
Other, net	8,968	18,784	2,349
	573,480	695,896	810,463
Operating income	95,503	307,174	356,650
Non-operating (income) expenses			
Equity in results of affiliated companies	(6,076)	6,844	11,568
Financial income	(61,611)	(43,037)	(56,123)
Financial expenses	82,014	108,209	119,976
Gain on currency remeasurement, net	(14,888)	(41,955)	(16,197)
Other, net	(212)	(129)	(76)
	(773)	29,932	59,148
Income before income taxes and minority interest	96,276	277,242	297,502
Income tax expense (benefit)			
Current	(23,988)	106,549	42,746
Deferred	8,415	22,567	27,510
	(15,573)	129,116	70,256
Minority interest in losses (earnings) of subsidiary	64	(37)	(9)
Net income	111,913	148,089	227,237

Aracruz Celulose S.A.

Consolidated Statements of Income

Expressed in thousands of United States dollars
(Except number of shares and per-share amounts) **(Continued)**

	Year ended December 31,		
	2002	**2003**	**2004**
Basic and diluted earnings per share			
Class A preferred stock	0.11	0.15	0.23
Class B preferred stock	0.11	0.15	0.23
Common stock	0.10	0.14	0.21
Weighted-average number of shares outstanding (thousands)			
Class A preferred stock	40,395	39,819	38,074
Class B preferred stock	536,768	535,969	537,711
Common stock	454,908	454,908	454,908

The accompanying notes are an integral part of these consolidated financial statements.

Aracruz Celulose S.A.

Consolidated Statements of Cash Flows

Expressed in thousands of United States dollars

	Year ended December 31,		
	2002	**2003**	**2004**
Cash flows from operating activities			
Net income	111,913	148,089	227,237
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and depletion	171,527	191,508	206,952
Equity in results of affiliated companies	(6,076)	6,844	11,568
Deferred income tax	8,415	22,567	27,510
Gain on currency remeasurement, net	(14,888)	(41,955)	(16,197)
Loss on sale of equipment	1,077	1,903	325
Loss on sale of investment			5,125
Other	(1,346)		
Decrease (increase) in assets			
Accounts receivable, net	(50,557)	(24,199)	8,449
Inventories, net	(11,868)	(23,556)	1,082
Interest receivable on short-term investments	54,817	(15,540)	(81,639)
Recoverable income taxes	10,246	68,848	(18,904)
Other	6,708	(2,725)	(2,905)
Increase (decrease) in liabilities			
Suppliers	10,437	(38,554)	(39,907)
Payroll and related charges	(1,537)	6,460	(1,420)
Income and other taxes and tax assessments and litigation contingencies	(3,751)	25,641	39,793
Accrued finance charges	(9,927)	(3,689)	1,714
Other	1,061	14,783	(1,296)
Net cash provided by operating activities	276,251	336,425	367,487
Cash flows from investing activities			
Short-term investments	27,927	75,194	(12,754)
Proceeds from sale of investment			17,276
Proceeds from sale of equipment	1,199	699	805
Investments in affiliate		(110,158)	(99,000)
Acquisition of Riocell (net of cash received)		(563,208)	
Additions to property, plant and equipment	(260,658)	(118,663)	(94,541)
Net cash used in investing activities	(231,532)	(716,136)	(188,214)

Aracruz Celulose S.A.

Consolidated Statements of Cash Flows

Expressed in thousands of United States dollars **(Continued)**

	Year ended December 31,		
	2002	**2003**	**2004**
Cash flows from financing activities			
Short-term debt, net	(78,789)	104,486	(109,503)
Long-term debt			
Issuances			
Related parties	112,199		
Other	250,000	612,512	362,488
Repayments			
Related parties	(43,309)	(52,719)	(54,630)
Other	(203,756)	(133,080)	(211,881)
Treasury stock acquired	(2,175)	(3)	
Dividends and Interest on Stockholders´ Equity paid	(73,765)	(109,310)	(198,668)
Net cash provided by (used in) financing activities	(39,595)	421,886	(212,194)
Effect of changes in exchange rates on cash and cash equivalents	225	(1,365)	3,111
Increase in cash and cash equivalents	5,349	40,810	(29,810)
Cash and cash equivalents, beginning of year	20,125	25,474	66,284
Cash and cash equivalents, end of year	25,474	66,284	36,474
Supplementary cash flow information			
Interest paid	60,412	64,828	138,011
Income taxes paid	140	2,186	9,340

The accompanying notes are an integral part of these consolidated financial statements.

Aracruz Celulose S.A.

Consolidated Statements of Changes in Stockholders' Equity

Expressed in thousands of United States dollars
(except number of shares and per-share amounts)

	Year ended December 31					
	2002		2003		2004	
	Shares	US$	Shares	US$	Shares	US$
Share Capital						
Preferred stock – Class A						
Balance, January 1	40.479.797	33.087	40.326.290	32.990	38.137.170	31.199
Treasury stock cancelled	(35.301)					
Conversion to Class B stock	(118.206)	(97)	(2.189.120)	(1.791)	(114.992)	(94)
Balance, December 31	40.326.290	32.990	38.137.170	31.199	38.022.178	31.105
Preferred stock - Class B						
Balance, January 1	582.049.217	581.409	536.837.131	581.506	539.026.251	583.297
Treasury stock cancelled	(45.330.292)					
Conversion from Class A stock	118.206	97	2.189.120	1.791	114.992	94
Balance, December 31	536.837.131	581.506	539.026.251	583.297	539.141.243	583.391
Common stock						
Balance, January 1 and December 31	455.390.699	297.265	455.390.699	297.265	455.390.699	297.265
Treasury stock						
Balance, January 1 – Common stock	(45.848.707)	(57.807)	(1.857.114)	(2.285)	(1.861.114)	(2.288)
Treasury stock cancelled – Common stock	45.365.593	57.697				
Treasury stock acquired – Class B Preferred stock	(1.374.000)	(2.175)	(4.000)	(3)		
Balance, December 31	(1.857.114)	(2.285)	(1.861.114)	(2.288)	(1.861.114)	(2.288)
Total share capital	1.030.697.006	909.476	1.030.693.006	909.473	1.030.693.006	909.473

Aracruz Celulose S.A.

Consolidated Statements of Changes in Stockholders' Equity

Expressed in thousands of United States dollars
(except number of shares and per-share amounts) **(Continued)**

	Year ended December 31					
	2002		2003		2004	
	Shares	US$	Shares	US$	Shares	US$
Balance brought forward	1,030,697,006	909,476	1,030,693,006	909,473	1,030,693,006	909,473
Net unrealized gain on						
Available-for-sale securities						
Balance, January 1		10,920				
Unrealized gain (loss) on available-for-sale						
securities, net of reclassification adjustments		(16,299)				
Tax effect on above		5,379				
Balance December 31,						
Fiscal-incentive reserve						
Balance, January 1						34,934
Transfer from unappropriated retained earnings				34,934		18,885
Balance, December 31				34,934		53,819
Investments reserve						
Balance, January 1		242,121		81,520		240,509
Treasury stock cancelled		(57,697)				
Transfer from (to) unappropriated retained earnings		(102,904)		158,989		241,504
Balance, December 31		81,520		240,509		482,013
Legal reserve						
Balance, January 1		52,985		35,653		58,803
Transfer from (to) unappropriated retained earnings		(17,332)		23,150		24,892
Balance, December 31		35,653		58,803		83,695
Total appropriated retained earnings		117,173		334,246		619,527
Balance carried forward	1,030,697,006	1,026,649	1,030,693,006	1,243,719	1,030,693,006	1,529,000

Aracruz Celulose S.A.

Consolidated Statements of Changes in Stockholders' equity

Expressed in thousands of United States dollars

(except number of shares and per-share amounts) **(Continued)**

	Year ended December 31,					
	2002		2003		2004	
	Shares	US$	Shares	US$	Shares	US$
Balance brought forward	1.030.697.006	1.026.649	1.030.693.006	1.243.719	1.030.693.006	1.529.000
Unappropriated retained earnings						
Balance, January 1		577.750		733.914		557.242
Net income		111.913		148.089		227.237
Cash dividends (per share: 2002 - US$ 0.08 to Class A preferred stock and US$ 0.07 to both Class B preferred and common stock: 2003 - US$ 0.11 to Class A preferred stock and US$ 0.09 to both Class B preferred and common stock: 2004 - US$ 0.12 to both Class A preferred and Class B preferred stock and US$ 0.11 to common stock)		(75.985)		(107.688)		(122.720)
Interest on Stockholders´ Equity (per share: 2004 - US$ 0.92 to both Class A and B preferred stock and US$ 0.84 to common stock)						(91.191)
Transfer from (to) reserves		120.236		(217.073)		(285.281)
Balance, December 31		733.914		557.242		285.287
Total stockholders' equity	1.030.697.006	1.760.563	1.030.693.006	1.800.961	1.030.693.006	1.814.287
Comprehensive income is comprised as follows:						
Net income		111.913		148.089		227.237
Net unrealized gain on available-for-sale securities						
Increase(decrease)in the unrealized gain arising during the year, net of taxes		(10,920)				
Total comprehensive income		100.993		148.089		227.237

The accompanying notes are an integral part of these consolidated financial statements.

1 Summary of significant accounting policies

The consolidated financial statements of Aracruz Celulose S.A. and its subsidiaries (the Company) have been prepared in conformity with accounting principles generally accepted in the United States of America ("US GAAP"), which require management 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; actual results may vary from estimates.

(a) Basis of presentation

The consolidated financial statements have been prepared in accordance with US GAAP, which differ in certain respects from the Brazilian accounting principles applied by the Company in its statutory financial statements prepared in accordance with Brazilian corporate legislation.

The Company has reported its financial statements in U.S. dollars since 1994 when the U.S. Securities and Exchange Commission permitted foreign registrants to report in U.S. dollars rather than in the currency of the country in which they are incorporated. The U.S. dollar amounts have been remeasured from Brazilian Reais (R$) in accordance with the criteria set forth in Statement of Financial Accounting Standards Nº 52 - "Foreign Currency Translation" ("SFAS 52"). The U.S. Dollar is used as the Company's functional currency as this has been, and remains, in the opinion of the Company's Board of Directors and Management, the currency in which it principally operates as well as being the Company's primary unit of economic measure. Translation gains and losses are recognized in the income statement, rather than in shareholders' equity; and non-monetary assets and liabilities (such as inventory and fixed assets) are converted at the historical exchange rate rather than at the end of period exchange rate.

The impact of the exchange variation of the Brazilian Real in relation to the U.S. dollar on the Company's monetary assets and liabilities denominated in Brazilian Reais in 2004 was a net gain of US$ 16.2 million (US$ 42.0 million in 2003 and US$ 14.9 million in 2002). The exchange rates at December 31, 2004, 2003 and 2002 were, respectively: US$ 1: R$ 2.6544, R$ 2.8892 and R$ 3.5333.

Stockholders' equity included in the consolidated financial statements presented herein differs from that included in the Company's statutory accounting records as a result of the variations in the U.S. dollar exchange rate, the indexation mandated over the years up to December 31, 1995 for statutory financial statements and adjustments made to reflect the requirements of US GAAP.

(b) Basis of consolidation

The financial statements of majority-owned subsidiaries have been consolidated, and all significant intercompany accounts and transactions have been eliminated. Accordingly, the following companies were consolidated: Aracruz Trading S.A., Aracruz Celulose (USA) Inc., Portocel – Terminal Especializado de Barra do Riacho S.A., Mucuri Agroflorestal S.A., Aracruz Produtos de Madeira S.A.(partially sold in November 2004), Riocell Trade Limited Partnership (Riocell Trade), Ara Pulp - Com. de Importação e Exportação, Unipessoal Ltda. and Aracruz Hungary Trading Ltd.

(c) Cash and cash equivalents

Cash and cash equivalents represent cash, bank accounts and short-term financial investments with a ready market and maturities when purchased of 90 days or less, and are stated at cost plus accrued interest, which approximates market value due to the short-term nature of the investments.

(d) Concentration of risk

Financial instruments which potentially subject the Company to concentrations of credit and performance risk are cash and cash equivalents, time deposits and trade accounts receivable. The Company limits its credit and performance risk associated with cash and cash equivalents and time deposits by placing its investments with highly rated financial institutions and in very short-term securities. An allowance for doubtful accounts is established to the extent the Company’s trade receivables are estimated not to be fully collectible.

The Company's pulp sales are made substantially to the paper industry; consequently, its performance is dependent upon that industry's worldwide demand for pulp and the related supply, as well as fluctuations in the market price for pulp which can be significant.

(e) Inventories

Inventories are stated at the lower of the average cost of purchase or production, and replacement or realizable values. Cost is determined principally on the average-cost method. Allowances for slow-moving or obsolete inventories are recorded when considered appropriate.

(f) Investments in affiliated companies and other investments

The Company uses the equity method of accounting for its long-term investment (Veracel Celulose S.A.) in which it owns 50% of the investee's voting stock and has the ability to exercise significant influence over operating and financial policies of the investee and for its long-term investment in Aracruz Produtos de Madeira S.A. in which it owns 33.3% of the investee's voting stock and also has the ability to exercise significant influence over operating and financial policies. The equity method requires periodic adjustments to the investment account to recognize the Company's proportionate share in the investee's results, reduced by receipt of investee dividends and, up to January 1, 2002, amortization of goodwill.

The Company accounts for its investment securities having a quoted market price (other than those accounted for under the equity method) in accordance with SFAS No. 115 "Accounting for Certain Investments in Debt and Equity Securities" ("SFAS 115"). The Company considers these investments to be trading securities and recognizes changes in the market value of such investments in results of operations.

(g) 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.

(h) Property, plant and equipment

Timber resources are stated at cost, less accumulated depletion. Forest development and maintenance costs are capitalized. Depletion is determined on the unit-of-production basis, excluding from the amount to be depleted the portion of tree-development costs that benefits future harvests; such costs are capitalized and included in the cost of those harvests.

Other property, plant and equipment are recorded at cost, including interest incurred on financing during the construction period of major new facilities. Interest on local currency borrowings is determined as that part of the total finance cost incurred on borrowings exclusive of the foreign currency translation adjustments arising on such borrowings, and, on foreign currency borrowings (including those denominated in U.S. dollars) at the contractual interest rates.

Depreciation is computed on the straight-line basis at rates, which take into consideration the useful lives of the assets, principally an average of 25 years for buildings, 10 years for improvements and installations, and 4 to 25 years for machinery and equipment and other assets.

Maintenance expenses, including those related to programmed maintenance of the Company's facilities, are charged to the cost of production as incurred.

(i) Environmental costs

Expenditures relating to ongoing programs for compliance with environmental regulations are generally expensed but may be capitalized under certain circumstances. Capitalization is considered appropriate when the expenditures relate to the acquisition and installation of pollution control equipment. These ongoing programs are designed to minimize the environmental impact of the Company's pulp-producing activities.

(j) Research and development

Expenditures for research and development for the year ended December 31, 2004 were US$ 3.7 million (US$ 3.8 million in 2003 and 2002). All such costs are expensed as incurred.

(k) Recoverability of long-lived assets

In accordance with SFAS 144 – "Accounting for the Impairment or Disposal of Long-Lived Assets", management reviews long-lived assets, primarily property, plant and equipment to be held and used in the business, for the purposes of determining and measuring impairment or when events or changes in circumstances indicate that the carrying value of an asset or group of assets may not be recoverable. Management did not identify the need for a provision for impairment in 2002, 2003 or 2004.

(l) Advances to suppliers

Advances to suppliers are basically amounts advanced (either in cash, seeds, technical assistence or other assets that will be used to grow eucalyptus plants) to small private producers that live in the sates of Espírito Santo, Bahia, Minas Gerais and Rio Grande do Sul, as part of a program called "Programa Produtor Florestal". In exchange, the Company agrees to purchase all of the eucalyptus plants grown by these small private producers.

(m) Employee retirement and post-employment benefits

The cost of the retirement benefits plans is accrued currently. Employee postretirement and post-employment benefits as defined by SFAS 106 - "Employers' Accounting for Postretirement Benefits other than Pensions" and SFAS 112 - "Employers' Accounting for Post-employment Benefits", respectively, are not significant. The Company is required by law to provide severance benefits to employees terminated without just cause. The costs of severance benefits are accrued on a monthly basis.

(n) Compensated absences

The liability for employees' future vacation compensation is accrued as vacation vests during the year.

(o) Revenues and expenses

Revenues arise from annual and long-term contracts and from spot sales and are recognized on an accrual basis when the products have been delivered or shipped to the customer and the risk of ownership has passed to the customer. The Company's selling prices are fixed or determinable and collectibility is reasonably assured. ly assure. Expenses and costs are accrued as incurred.

The Company reflects value-added taxes as a reduction of gross operating revenues.

(p) Shipping and handling fees

Amounts billed to customers in a sale transaction related to shipping and handling are classified as revenue. Such costs incurred related to shipping and handling are classified as costs of sale.

(q) Accounting for derivatives and hedging activities

The Company accounts for derivative financial instruments pursuant to SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities", as amended. This standard requires that all derivative instruments be recognized in the financial statements and measured at fair value regardless of the purpose or intent for holding them. Changes in the fair value of derivative instruments are recognized periodically in income since the Company recognizes all derivative financial instruments as non-hedge transactions.

(r) Income taxes

The Company recognizes deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the tax bases and financial reporting bases of assets and liabilities, as well as on the effects of adjustments made to reflect the requirements of US GAAP. A valuation allowance is provided to reduce deferred tax assets when management considers that realization is not reasonably assured.

(s) Basic and diluted earnings per share

Basic and diluted earnings per share are computed by dividing net income by the weighted average number of all classes of shares outstanding during the year, net of treasury stock, after taking into consideration the dividend provisions applicable to Class A and Class B preferred stocks, assuming that all earnings for the year are fully distributed. There were no dilutive securities outstanding in 2002, 2003 and 2004. See note 13.

(t) Comprehensive income

SFAS No. 130 "Reporting Comprehensive Income" ("SFAS 130") requires that companies display changes in the equity of a business enterprise during a period resulting from transactions and other events and circumstances from non-owner sources. The Company has adopted SFAS 130 for all years presented and has included a comprehensive income (loss) statement as part of the consolidated statements of changes in stockholders' equity.

(u) Statements of cash flows

Cash flows relating to overnight financing and investments are reported on a net basis. Short-term investments that have a ready market and original maturity, when purchased, of 90 days or less are considered to be cash equivalents.

(v) Segment information

SFAS No. 131 "Disclosures about Segments of Enterprise and Related Information" ("SFAS 131") requires that a business enterprise supplementally disclose certain financial information among its various and distinct operating activities. Such information is to be presented from the point of view of how operating and financial decisions are made for each business sector. See presentation of exports by geographic information in note 22.

(w) Guarantees

The Company has disclosed its guarantees to third parties in accordance with FASB Interpretation No. 45 "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others" ("FIN 45") in Note 18. FIN 45 requires certain disclosures to be made by a guarantor in its interim and annual financial statements about its obligations under certain guarantees that it has issued. FIN 45 also requires a guarantor to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. The initial recognition and measurement requirements of FIN 45 are effective for guarantees issued or modified after December 31, 2002.

2 Business Combination – Acquisition of Riocell S.A.

On July 2, 2003, the Company completed the acquisition of all outstanding shares of Riocell S.A. and its subsidiaries ("Riocell") from Klabin S.A. and Klabin do Paraná Produtos Florestais Ltda. for the amount of US$ 610,500. The final price paid is within the market value evaluation made by independent appraisers.

After the completion of the due diligence process, the initial purchase price of US$ 610,500 was reduced to US$ 567,296.

The Company determined the fair value of Riocell's assets and liabilities with the assistance of an independent appraiser. This determination was completed on December 23, 2003, and after the final allocation of the purchase price to the net assets acquired, the company recognized goodwill in the amount of US$ 192,035 at December 31, 2003; there were no intangible assets identified in the acquisition.

Expressed in thousands of United States dollars

Unaudited pro-forma results of operations for the year ended December 31, 2003 as if the acquisition of Riocell had taken place at the beginning of 2003 is presented below. Riocell was incorporated on November 30, 2002 and, accordingly no financial information is available for the year ended December 31, 2002. The pro-forma results of operations include estimates and assumptions which management believes are reasonable. However, pro forma results do not include any anticipated cost savings and are not necessarily indicative of the results which could have occurred if the business combination had been in effect on the dates indicated or which may result in the future.

	2003 (Unaudited)
Operating revenues	1,104,350
Net income	148,577
Earnings per share, basic and diluted :	
Preferred shares	0.15
Common shares	0.14

3 Recently issued accounting pronouncements

In November 2004, the FASB issued SFAS No. 151, Inventory Costs an amendment of ARB No. 43, Chapter 4, which amends Chapter 4 of ARB No. 43 that deals with inventory pricing. The Statement clarifies the accounting for abnormal amounts of idle facility expenses, freight, handling costs, and spoilage. Under previous guidance, paragraph 5 of ARB No. 43, chapter 4, items such as idle facility expense, excessive spoilage, double freight, and rehandling costs might be considered to be so abnormal, under certain circumstances, as to require treatment as current period charges. This Statement eliminates the criterion of “so abnormal” and requires that those the costs of conversion be based on the normal capacity of the production facilities. The provisions of this Statement shall be effective for inventory costs incurred during fiscal years beginning after items be recognized as current period charges. Also, this Statement requires that allocation of fixed production overheads to June 15, 2005. Earlier application is permitted for inventory costs incurred during fiscal years beginning after the date this Statement is issued. The provisions of this Statement shall be applied prospectively. Management is analyzing the requirements of this new Statement and believes that its adoption will not have any significant impact on the Company’s financial position, results of operations or cash flows.

In December 2004, the FASB issued SFAS No. 153, Exchanges of Nonmonetary Assets an amendment of APB No. 29. This Statement amends Opinion 29 to eliminate the exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. The Statement specifies that a nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. This Statement is effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. Earlier application is permitted for nonmonetary asset exchanges occurring in fiscal periods beginning after the date this Statement is issued. Retroactive application is not permitted. Management will apply this Statement in the event exchanges of nonmonetary assets occur in fiscal periods beginning after June 15, 2005.

In September 2004, the FASB issued FSP EITF Issue 03-1-1, which delayed the effective date of paragraphs 10-20 of EITF Issue No. 03-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments. Paragraphs 10-20 of EITF Issue No. 03-1 give guidance on how to evaluate and recognize an impairment loss that is other that temporary. Application of these paragraphs has been deferred pending issuance of proposed FSP EITF Issue 03-1a. Management has concluded that EITF Issue No. 03-01 is not applicable to its current operations since it does not have any investments classified as available-for-sale or held-to-maturity, or other investments carried at cost.

At its March 31, 2004 meeting, the Emerging Issues Task Force (EITF) reached final consensus on EITF Issue No. 03-6, Participating Securities and the Two-Class Method under FASB Statement No. 128, Earnings per Share. Typically, a participating security is entitled to share in a company's earnings, often via a formula tied to dividends on the company's common stock. The issue clarifies what is meant by the term participating security, as used in Statement 128. When an instrument is deemed to be a participating security, it has the potential to significantly reduce basic earnings per common share because the two-class method must be used to compute the instrument's effect on earnings per share. The consensus also covers other instruments whose terms include a participation feature. The consensus also addresses the allocation of losses. If undistributed earnings must be allocated to participating securities under the two-class method, losses should also be allocated. However, EITF 03-6 limits this allocation only to situations when the security has (1) the right to participate in the earnings of the company, and (2) an objectively determinable contractual obligation to share in net losses of the company.

The consensus reached in EITF 03-6 is effective for fiscal periods beginning after March 31, 2004 (effectively the second fiscal quarter for calendar year-end companies). EPS in prior periods must be retroactively adjusted in order to comply with the consensus decisions reached in EITF 03-6. The Company does not expect that this consensus will have any impact on its calculation of Basic and Diluted EPS.

Aracruz Celulose S.A.

Notes to Consolidated Financial Statements

Expressed in thousands of United States dollars
(unless otherwise stated)

4 Taxes

4.1 Income taxes

Income taxes in Brazil comprise federal income tax and social contribution (which is an additional federal income tax). The statutory rates applicable for federal income tax and social contribution for the years ended December 31, 2002, 2003 and 2004 are presented as follows:

Federal income tax rate	25.0%
Social contribution (*)	9.0%
Composite tax rate	34.0%

The amounts reported as income tax expense in the consolidated statements of income are reconciled to the statutory rates as follows:

	Year ended December 31,		
	2002	**2003**	**2004**
Income before income taxes and minority interest	96,276	277,242	297,493
Federal income tax and social contribution at statutory rates	32,734	94,262	101,148
Adjustments to derive effective tax rate:			
Effects of differences in remeasurement from reais to U.S. dollars, using historical exchange rates and indexing for tax purposes:			
Depreciation on difference in asset basis	40,746	25,893	23,674
Translation effect for the period	(74,793)	31,472	46,776
Fiscal incentive – income tax (*)		(34,934)	(15,680)
Results in subsidiaries with different tax rates	(19,301)	24,322	(50,911)
Reversal of income tax and social contribution related to “plano verão”		(9,106)	
Interest on stockholders´ equity			(33,111)
Others	5,041	(2,793)	(1,640)
Income tax expense (benefit) in the consolidated statements of income	(15,573)	129,116	70,256

(*) See note 17.

Expressed in thousands of United States dollars

The major components of the deferred tax accounts in the balance sheet are as follows:

	December 31,	
	2003	**2004**
Assets (liabilities)		
Deductible temporary differences	48,596	29,835
Other capitalized investments	(75,063)	(80,480)
Unrealized profits on intercompany transactions	13,181	9,853
	(13,286)	(40,792)
Current assets	13,181	9,853
Long-term assets (liabilities)	(26,467)	(50,645)

Although realization of net deferred tax assets is not assured, management believes that such realization is more likely than not to occur and, therefore, has not recognized any valuation allowances.

4.2 Other taxes

Since the promulgation of the Federal Law nº. 87, on September 13, 1996, the Company has been accumulating ICMS (state sales tax) credits resulting from ICMS paid on purchases, credited to its books and not compensated against ICMS on sales because export sales are exempted from ICMS. The Company has the legal right, not contested by the state authorities, to claim those credits against the state of Espírito Santo. However, due to the priority given by the state government of Espírito Santo to financially restructure its public accounts, the Company does not foresee a short-term solution to the utilization of the credits.

Accordingly, the Company decided in October 2002 to increase its original valuation allowance from 25% to 100% of the existing credits related to the Barra do Riacho Plant, as well as to make similar provisions related to any future credits to be accumulated. At December 31, 2004, the Company had ICMS credits in the amount of US$ 128,433 (US$ 96,435 at December 31, 2003), of which the amount of US$ 125,287 had a provision for loss (US$ 92,010 at December 31, 2003).

Expressed in thousands of United States dollars

5 Cash and cash equivalents

	December 31,	
	2003	**2004**
Brazilian reais	3,307	5,558
United States dollars	61,775	30.587
Other European currencies	1,202	329
	66,284	36,474

Cash equivalents denominated in Brazilian Reais and in United States dollars represent principally investments in certificates of deposit placed with major financial institutions.

6 Short-term investments

At December 31, 2004 and 2003, the Company held shares in two private investment funds basically comprised of certificates of deposit with prime financial institutions in Brazil, debentures issued by public companies and notes issued by the Brazilian federal government, with final maturities ranging from April 2005 to April 2008. The securities included in the portfolio of the private investment funds have daily liquidity and are marked to market on a daily basis. The Company considers these investments as securities held for trading with changes in the fair value reflected in results of operations.
These private investment funds do not have significant financial obligations. Any financial obligation are limited to service fees to the asset management company employed to execute investment transactions, audit fees and other similar expenses. There are no consolidated assets of the Company that are collateral for these obligations and the creditors of the funds do not have recourse against the general credit of the Company.

Expressed in thousands of United States dollars

7 Accounts receivable, net

	December 31,	
	2003	**2004**
Customers - pulp sales		
Domestic	7,383	9,829
Export	196,911	185,505
Advances to suppliers	4,258	786
Other	18,007	16,078
	226,559	212,198
Allowance for doubtful accounts	(3,511)	(3,862)
Total, net	223,048	208,336

At December 31, 2004, two customers accounted for 45.8% of total customer receivables (44.% at December 31, 2003) and no other accounted for more than 10%.

Export receivables are denominated in the following currencies:

	December 31,	
	2003	**2004**
United States dollars	193,599	184,362
European currency units – EURO	3,312	1.143
	196,911	185,505

Export receivables in currencies other than U.S. dollars are swapped into U.S. dollars through forward foreign exchange contracts as discussed in Note 19.

Expressed in thousands of United States dollars

8 Inventories, net

	December 31,	
	2003	**2004**
Finished products	67,903	70,128
Work in process	1,380	
Timber	3,872	
Raw materials	24,059	17,948
Spare parts and maintenance supplies, less allowance for loss of US$ 562 (2003 – US$ 2,109)	34,272	38,144
	131,486	126,220

9 Property, plant and equipment

	December 31, 2003		
	Cost	**Accumulated depreciation**	**Net**
Land	295,364		295,364
Timber resources	341,054	75,087	265,967
Buildings, improvements and installations	563,872	326,633	237,239
Equipment	2,606,971	1,193,750	1,413,221
Information technology equipment	55,926	41,303	14,623
Other	153,480	125,652	27,828
	4,016,667	1,762,425	2,254,242
Construction in progress	16,127		16,127
Total	4,032,794	1,762,425	2,270,369

Expressed in thousands of United States dollars

	December 31, 2004		
	Cost	Accumulated depreciation	Net
Land	292,960		292,960
Timber resources	356,972	88,691	268,281
Buildings, improvements and installations	559,837	327,630	232,207
Equipment	2,464,413	1,211,889	1,252,524
Information technology equipment	53,216	42,019	11,197
Other	175,679	128,662	47,017
	3,903,077	1,798,891	2,104,186
Construction in progress	29,710		29,710
Total	3,932,787	1,798,891	2,133,896

As of December 31, 2004 and 2003 fixed assets securing financial obligations was represented by the whole Company mill.

Acquisition of Florestas Rio Doce S.A.

In September 2002, Aracruz Celulose S.A., together with Suzano Bahia Sul Celulose S.A. (previously denominated Bahia Sul Celulose S.A.), signed an agreement with Companhia Vale do Rio Doce S.A. (CVRD) and its subsidiary Florestas Rio Doce S.A. (FRDSA), for the acquisition of the assets of FRDSA, located in the Municipality of São Mateus, in the State of Espírito Santo. Such assets are comprised of approximately 40,000 hectares of land and eucalyptus forests with amount of R$ 193.3 million – (US$ 49.6 million) net of the assignment to the buyers of the rights of a preexisting wood supply agreement (R$ 49.5 million - US$ 13.3 million), with a combined net price of R$ 143.8 million (approximately US$ 36.3 million).

The net purchase price will be paid in 12 quarterly installments and the Company recorded its share in the agreement (50%) as a liability (supply agreement) and as an asset (land and forests). Aracruz Celulose S.A. and Suzano Bahia Sul S.A. each will separately control its share of the assets. The Company has paid 8 installments through December 31, 2004.

10 Investment in affiliated company

Veracel Celulose S.A.

On October 10, 2000, the Company acquired a 45% interest in Veracel Celulose S.A. ("Veracel") for US$ 81,011. Veracel is growing eucalyptus plantations in the state of Bahia in Brazil and did not begin operations until January 2002. Stora Enso OYJ ("Stora Enso") and Odebrecht S.A. ("Odebrecht") owned the remaining 45% and 10%, respectively. Upon closing of the purchase agreement, the Company and Veracel entered into a three-year wood supply contract to provide wood for the Company´s mill expansion. Under the terms of the contract, which began in January 2002, Veracel supplies up to 3.85 million cubic meters of wood. Currently, Aracruz has a contractual agreement with Veracel to purchase up to 1.04 million cubic meters of wood, with initial delivery commencing in June 2004 and ending in 2005.

During the first quarter of 2003, the Company acquired, together with Stora Enso, the 10% Odebrecht's ownership on a 50/50 ratio, paying the amount of US$ 9,658, including US$ 443 of unallocated goodwill, for the acquisition of its portion of the additional investment in Veracel.

The Company accounts for its investment in Veracel using the equity method of accounting. At December 31, 2004 the Company's investment in Veracel included unamortized goodwill of US$ 15,015. In 2004, the Company recognized an equity loss of US$ 11,568 (2003 - loss of US$ 6,844).

In May 2003, the Company and Stora Enso jointly decided to proceed with the planned construction of Veracel´s own green field plant which will have a capacity 900,000 tons of pulp per year and will require investments of approximately US$ 1,250 million of which US$ 300 million were already invested in forestry and infrastructure including roads and a specialized maritime terminal.

Aracruz Produtos de Madeira S.A. (APM)

In October 2004, the Company sold to a third party 2/3 of the shares of APM; the remaining 1/3 of the shares of APM are being accounted for by the Company under the equity method of accounting. APM will be operated as a joint venture. The terms of the negotiation also establish that the Company will supply saw logs and render certain services to APM pursuant to long term agreements.

Expressed in thousands of United States dollars

The sale price was R$ 53.4 million (equivalent to US$ 18.6 million). After adjustments to reflect variations agreed among the parties, the Company received the cash amount of R$ 49.6 million (equivalent to US$ 17.3 million) in October 2004 and recognized a loss of US$ 5.1 million. The remaining interest in APM was tested for impairment but no adjustment resulted from it.

12 Short-term borrowings and long-term debt

(a) Short-term borrowings - export financing and other

The Company's short-term borrowing if from a real denominated operation with annual interest rate of 8.75%.

At December 31, 2004, US$ 3.8 million of short-term borrowings fall due within 90 days (US$ 118.3 million as of December 31, 2003).

(b) Long-term debt

	December 31,	
	2003	**2004**
Denominated in Brazilian currency – BNDES term loans with varying interest rates; principally the "Long-term Interest Rate" (TJLP) plus 7.8% to 9.3% (2003 – 7.8% to 10.0%), due 2005 to 2009	210,955	195,403
Denominated in foreign currencies		
BNDES Term loans – 10.41% (2003 – 2.33 to 10,41%), due 2005 to 2009	89,813	38,519
International Finance Corporation (IFC) - 5.44% due 2007 to 2014		25,000
Securitization of export receivables – 5.99% to 7.05% (2003 – 5.99 to 7.05%) due 2005 to 2012	650,000	783,500
Import financing – 2.06% to 7.08% (2003 – 1.43% to 7.08%), due 2005 to 2007	16,317	10,346
Pre-export financing – 2.42% to 4.80% (2003 - 2.51% to 4.33%) due 2005 to 2010	280,012	315,000
	1,036,142	1,172,365
Total	1,247,097	1,367,768
Less current maturities	(267,662)	(145,040)
	979,435	1,222,728

a) Loan from Related Party – BNDES

As of December 31, 2004, the Company had an outstanding balance of BNDES loans in the amount of R$611 million (equivalent to US$ 230 million), denominated in Brazilian Reais and basket of foreign currencies, with annual interest rates ranging from 7.80% to 9.30%, to be repaid from 2004 through 2009.

b) Debt of Aracruz Trading S.A. and Aracruz Trading Hungary Ltd.

During June 2001, Aracruz Trading S.A. obtained long term financing of US$ 100 million, with maturities from May 2004 to June 2004 with contractual clauses of early maturity and annual interest rates ranging from 2.72% to 2.74%, secured against future export sales receivables. Aracruz Trading S.A. pre-paid the amounts of US$ 37.5 million in December 2002 and US$ 25.0 million in May 2003. The outstanding balance was paid on maturity: US$ 25.0 million in May 2004 and US$ 12.5 million in June 2004.

In February 2002, the Company, through Aracruz Trading S.A., signed a financing agreement with a special-purpose entity (SPE) under which such entity received and advanced to the Company US$ 250 million, as an issuance of Senior Secured Export Notes. In August 2003, a second tranche of Senior Secured Export Notes was issued, in the amount of US$ 400 million under the same securitization program established in February 2002. In May 2004, a third tranche of Senior Secured Export Notes was issued, in the amount of US$ 175 million under the same securitization program. In return, the Company securitized the financing by selling to the SPE 95% of its current and future export accounts receivables. In June 2003 this obligation was reduced to 80% of such receivables. In February 2004, Aracruz Trading Hungary Ltd. was included in the securitization program, in addition to Aracruz Trading S.A.. Each month the collections in excess of contractual funding requirements are transferred to Aracruz Trading S.A and Aracruz Trading Hungary Ltd..

Expressed in thousands of United States dollars

The table below summarizes the terms of the three tranches under the securitization programs:

	Original line of credit	Annual charges	Due date	Outstanding balance (principal amounts) December 2003	December 2004
Tranche					
February 2002	250,000	5.984%	March/2009	250,000	208,500
August 2003	400,000	7.048%	September/2011	400,000	400,000
May 2004	175,000	6.361%	May/2012		175,000
	825,000			650,000	783,500

c) International Finance Corporation (IFC)

In December 2004, the Company signed a US$ 50 million loan agreement with International Finance Corporation (IFC), the private sector arm of the World Bank Group. The loan has floating interest rate based on LIBOR, semi-annual payments starting in December 2007 and final maturity in 2014. A first tranche of US$ 25 million was disbursed in December 2004 with annual interest rate of 5.44%.

d) Long-term portion payment schedule

The long-term portion of the Company's debt at December 31, 2004 becomes due in the following years:

2006	256,790
2007	336,774
2008	264,920
2009	137,012
2010 and thereafter	227,232
Total	1,222,728

13 Stockholders' equity

At December 31, 2004, the Company's principal common stockholders and their common stock ownership interests, either direct or indirect are as follows: Arapar S.A. , SODEPA. - Sociedade de Empreendimentos, Publicidade e Participação S.A. (SODEPA) (an affiliate of Banco Safra S.A.), and Votorantim Celulose e Papel (VCP) with 28% each; Banco Nacional de Desenvolvimento Econômico e Social – BNDES with 12.5%.

At December 31, 2004, SODEPA and the Banco Nacional de Desenvolvimento Econômico e Social - BNDES also owned preferred stocks which in total amounted to 14.9% and 7.7%, respectively, of the total preferred stocks.

Treasury stock

At the Ordinary General Meeting held on July 29, 2002, management decided to cancel 45,365,593 preferred shares (35,301 class "A" shares and 45,330,292 class "B" shares), all held in treasury. The cancellation of shares did not result in a reduction of subscribed capital.

Basic and diluted earnings per share

Basic and diluted earnings per share ("EPS") as of December 31, 2004, 2003 and 2002, as presented in the Company's statement of income, have been calculated on the following basis taking into consideration the Dividend Allocation between Class A and Class B preferred stock and common stock as discussed below:

Class A preferred stock may be converted into Class B preferred stock at any time at the option of the stockholder. Preferred stock does not have voting rights but has priority in the return of capital in the event the Company is liquidated and has the right to receive cash dividends in an amount 10% higher than dividends attributable to each common stock. Stock dividends payable to Class A preferred stockholders are effected through issuance of Class B preferred stock. Class A preferred stock has priority in the distribution of a minimum annual cash dividend equivalent to 6% of the related capital.

Additionally, in order to comply with Law 9457/97, the Company's By-laws were changed to grant Class B preferred stock the right to receive an annual dividend in an amount that is 10% higher than dividends paid to common stockholders (the "Dividend Allocation").

Expressed in thousands of United States dollars

Earnings, if any, in excess of the Class A preferred stock minimum dividend will be distributed as dividends to Class B preferred stock and common stock, up to the equivalent on a per-share basis of those paid to Class A preferred stock, while maintaining the Dividend Allocation between Class B preferred stock and common stock. Any earnings remaining for distribution thereafter are shared ratably among Class A preferred, Class B preferred and common stocks while maintaining the Dividend Allocation between Class A and Class B preferred stock and common stock. In the event that Class A preferred stock is not paid dividends for three consecutive years, holders of that stock are entitled to voting rights until the dividends in arrears for those three years are paid.

The following presents the earnings per share calculations:

	2002	2003	2004
Net income	111,913	148,089	227,237
Less priority Class A preferred stock dividends	(1,233)	(1,488)	(1,548)
Less Class B preferred stock and common stock dividends up to a limit equivalent to the Class A preferred stock dividends on a per-share basis while maintaining the Dividend Ratio	(29,007)	(35,483)	(38,676)
Remaining net income to be equally allocated to Class A and Class B preferred stock and common stock while maintaining the Dividend Ratio	(81,673)	(111,118)	(187,013)
Weighted average number of shares outstanding (thousands)			
Class A preferred	40,395	39,819	38,074
Class B preferred	536,768	535,969	537,711
Common	454,908	454,908	454,908
Basic and diluted earnings per share			
Class A preferred	0.11	0.15	0.23
Class B preferred	0.11	0.15	0.23
Common	0.10	0.14	0.21

Brazilian law permits the payment of cash dividends only from retained earnings and certain reserves registered in the Company's statutory accounting records. At December 31, 2004, after considering appropriated retained earnings which can be transferred to unappropriated retained earnings, the earnings and reserves available for distribution as dividends, upon approval by the Company's stockholders, amounted to the equivalent of US$ 479 million.

Retained earnings that represent unrealized income (principally inflationary income recognized up to December 31, 1995 in the Company's statutory financial statements) are transferred to unrealized income reserve and are transferred back to unappropriated retained earnings as financial resources become available for dividend distribution.

The fiscal-incentive reserve consists of the appropriations from retained earnings equivalent to the cumulative amounts by which income tax rates have been reduced each year as a result of the Barra do Riacho operations of the Company being located in a development are (see note 17). The fiscal-incentive reserve may be used to increase capital and absorb losses, but is not available as cash dividends.

The investments reserve represents discretionary appropriations, ratified by the stockholders, for plant expansion and other capital projects, the amount of which is based on an approved capital budget presented by management. After completion of the projects, the Company may elect to retain the appropriations until the stockholders vote to transfer all or a portion of the reserve to capital or to retained earnings, from which a cash dividend may then be paid.

The legal reserve results from appropriations from retained earnings of 5% of annual net income recorded in the statutory accounting records. Such appropriations are required until the balance reaches 20% of the balance of capital stock, based on the statutory accounting records. At December 31, 2004, such capital stock was R$ 1,854 million and the balance in the legal reserve was R$ 222 million. The legal reserve may be used to increase capital and to absorb losses, but is not available for distribution as cash dividends.

Dividends and interest on stockholders' equity

The Company's by-laws guarantee a minimum annual dividend equal to 25% of the adjusted net income for the year, as required by the Brazilian Corporate Law.

Brazilian law permits the payment of cash dividends only from retained earnings. As of January 1, 1996, Brazilian corporations are allowed to attribute interest on stockholders' equity. The calculation is based on the stockholders' equity amounts as stated in the statutory accounting records and the interest rate applied may not exceed the long-term interest rate ("TJLP") determined by the Brazilian Central Bank (approximately 10%, 11.50% and 9.81.% for years 2002, 2003 and 2004, respectively). Also, such interest may not exceed the greater of 50% of net income for the year or 50% of retained earnings plus revenue reserves, determined in each case on the basis of the statutory financial statements. The amount of interest attributed to stockholders is deductible for corporate income tax purposes.

The Company paid US$ 82.8 million of interest on stockholders' equity during the year ended December 31, 2004 and accrued US$ 9.9 million of interest on stockholders' equity for payment in 2005.

14 Pension plan

The Company sponsors a contributory defined contribution pension plan, ARUS – Fundação Aracruz de Seguridade Social, which covers substantially all of its employees. The principal objective of the pension plan is to supplement the social security pension benefits of the employees of the Company ("Sponsors").

The Sponsors and eligible employees make monthly contributions under the plan to ARUS, which manages (or places with a trustee) its investments and other assets, which comprised, principally, of bank certificates of deposit, investments funds and marketable equity securities.

Contributions made by the Company to the plan amounted to US$ 989, US$ 1,287 and US$ 1,714 in 2002, 2003 and 2004, respectively, and represented the annual pension expense of the Company for the plan.

15 Employee benefits

In addition to the pension plan, the Company makes monthly contributions, based on total payroll, to government pension, social security and severance indemnity plans and such payments are expensed as incurred. Also, certain severance payments are due on dismissal of employees, principally notice of one month's salary and a severance payment calculated at 40% of the accumulated contributions made to the government severance indemnity plan on behalf of the employee. Based on current operating plans management does not expect that amounts of future severance indemnities will be material.

16 Contingencies and Commitments

(a) Contingencies

(i) Labor proceedings

At December 31, 2004, the Company had a total provision recorded for other cases of US$ 12.3 million (US$ 13.3 million in 2003) based on the Court's computation framework and existing labor jurisprudence and a corresponding deposit in an escrow account of US$ 5.6 million (US$ 3.9 million in 2003).

(ii) Fiscal proceedings

In March 1997, the Company received notification from the INSS (the Brazilian Social Security System) relating to the value of housing allowances paid to certain employees over a period of several years. At December 31, 2004, the Company is contesting this notification and has placed approximately US$ 6.4 million in an escrow account to cover this claim. Based on the opinion of its legal advisors, Company's management does not believe that the ultimate resolution of this matter will have a material adverse impact on the Company, and accordingly, no provision has been made therefor.

(iii) Income tax and social contribution related to the "Plano Verão"

In December 1994, the Company petitioned the Regional Federal Tribunal of the 2nd Region (the "Tribunal") to include, in the determination of its income tax and social contribution liabilities the effects of the variation in the IPC (Consumer Price Index) in January 1989 of 70.28% ("Plano Verão"). The Tribunal subsequently accepted the use of a variation of 42.72%. Beginning in the third quarter of 2000, with the substantially full utilization of the Company's net operating losses in Brazil, the Company began to determine and pay income tax using 42.72% deduction and made a provision for contingencies to cover the effects of the use of this deduction. In March 2003, the Company obtained a final court ruling and, consequently, made a reversal of this provision, which includes interest and monetary variation, against income tax expense and financial expense in the amounts of US$ 9,106 and US$ 6,832, respectively.

(iv) PIS and COFINS contributions

The Company is taking action in court against certain changes in the rates and rules for the calculation of the PIS (Social Integration Program) and COFINS (Social Fund) contributions determined by Law 9.718/98, the basis of calculation of which includes financial income and exchange and monetary variations. At December 31, 2004, the provision for contingencies included US$ 51.3 million related to PIS and COFINS on exchange gains on U.S. dollar denominated debt resulting from the appreciation of the Real against the U.S. dollar that occurred following the significant devaluation in early 1999.

After analyzing certain legal decisions on similar legal actions of other companies and their implications for Aracruz's case, the Company decided to cancel part of the legal action, regarding the rate increase and the basis of calculation modifications (except for foreign exchange variation), and decided to pay the accrued amount in installments according to a special program of tax collection called PAES, enacted by the law 10.684/2003. As of December 31, 2004 the remaining balance amounted to US$ 21,572 (US$ 21,694 as of December, 2003) and is recorded in other current and long-term liabilities.

(v) Value-Added Tax Credit

In 2002, the Company took action in court against the government of the State of Espírito Santo to confirm the legal right to use its accumulated ICMS credits arising from fixed assets, raw material and other goods acquired for utilization in the process of pulp production. As of December 31, 2004, the balance recorded as a tax asset was US$ 128 million, of which the amount of US$ 125 million had a provision for loss.

(vi) Social Contribution

On September 10, 2003, the Company obtained a preliminary Court Order giving it the right not to pay Social Contribution on profits generated by export sales from January 2002 as well as the right to recognize the amounts of tax credits previously compensated in this regard. Pending final determination, the Company has accrued a provision of US$ 54.7 million as of December 31, 2004 (US$ 34.0 million in 2003).

(viii) Others

The Company has, based on an analysis of the disputes involved and consultation with its legal counsel, recorded additional provisions in the amount of US$ 11.6 million relating to several other legal disputes and has also made deposits in the amount of US$ 5.3 million in escrow accounts.

(b) Commitments

(i) Indian Communities - Terms of settlement

The Company has been involved in an administrative claim regarding the enlargement of Indian reservations in an area owned by the Company. In April 1998, the Indian communities signed two Terms of Settlement recognizing the legitimacy of the Ministry of Justice Edicts 193, 194 and 195, dated March 6, 1998, that restricted expansion of the reservation to 2,571 hectares of land belonging to the Company. Additionally, the Company committed itself to a financial aid program to be implemented through social, agricultural, educational, shelter and health projects, up to an amount of approximately R$ 13.5 million (equivalent to US$ 5.1 million at December 31, 2004), monetarily restated by one of the official inflation indexes, to be disbursed within a twenty-year period, conditioned to the accomplishment of certain obligations by the Indian communities.

If the Indian communities breach any of their obligations, Aracruz will be released from the obligations defined by the Terms of Settlement. Decrees approving the enlargement of the Indian reservations have extinguished the aforementioned administrative claim. As of December 31, 2004, the Company had donated to the Indian Associations approximately R$ 8.8 million – equivalent to US$ 4.0 million (R$ 6.8 million – equivalent to US$ 3.3 million up to December 31, 2003) under the Terms of Settlement.

(ii) "Take-or-pay" contract

In connection with the sale of its electrochemical plant to Nexen Chemicals Holdings International Limited – NEXEN (formerly Canadian Oxy Chemicals Holding Ltd.) in 1999, the Company and NEXEN entered into a long-term contract for chemical products supply. The contract includes clauses of performance incentives such as sharing of productivity gains, preference prices and "take-or-pay", by which the Company is committed to acquire from the electrochemical plant purchased by NEXEN a volume of chemical products conservatively projected for 6 years from 2000 on. Volumes purchased by the Company in addition to the minimum agreed for a given year may be compensated with lower volumes acquired in subsequent years. For the take-or-pay quantities, the Company will pay unit prices which equal cost plus margin as determined in the contract. The Company has been meeting the minimum quantitative commitments under the contract.

(iii) Compliance with regulations

The Company's forestry and manufacturing operations are subject to both Federal and State government environmental regulations. The Company's management believes that it is in compliance, in all material respects, with all applicable environmental regulations.

17 Fiscal incentives

The Barra do Riacho operations are located within the geographic area of ADENE (Agency for the Development of the Northeast). Decree No. 4213, of April 16, 2002, recognizes the pulp and paper sector as a priority in the development of the region, thus entitling Aracruz to benefit from reductions in corporate income tax.

In October 2002, the Company signed the respective agreement with ADENE, which was formally approved by Internal Revenue Service on December 13, 2002, awarding the Company the right to reduced income tax rates on its operating profits, as follows:

(i) Profits corresponding to the volumes of Fiberline C, limited to 780 thousand tons/year, for 10 years: 75% reduction of the statutory tax rate, as from 2003 through 2012;

(ii) Profits corresponding to the volumes of Plants A and B, limited to 1,300 thousand tons/year, for 10 years: 37.5% reduction of the statutory rate through 2003, 25% reduction from 2004 through 2008 and 12.5% reduction from 2009 through 2013.

On January 9, 2004, the Company was notified by ADENE of its decision to cancel the fiscal benefits to which the Company had been entitled. Later, through Decree Nro. 065/04, of March 11, 2004 ADENE nullified this notification, agreeing with the arguments of the Company.

Subsequently, the following legal instruments and acts occurred in respect of the ADENE incentives:

- Decree Nro. 58 of Julne 15, 2004: annulling the right to fiscal benefit;

- ADENE notification nº 83/04 of July 8, 2004: granting Aracruz 10 days to present comments on the administrative process;

- ADENE notification nº 733/04 as of September 6, 2004: annulling the basis for the fiscal incentives;

- ADENE notification of September 17, 2004: confirming that the basis for the fiscal incentives is still in force;

- Decree Nro. 159 of December 22, 2004, published in December 29, 2004: nullifies prior notification by ADENE in favor of the Company.

On January 3, 2005, the Company appealed to the National Integration Ministry, responsible for ADENE, requesting the maintenance of the fiscal-incentive and the repeal of ADENE's decision.

Company's management, based on the advice of external legal counsel, believes that ADENE's decision does not invalidate the benefits recorded (R$ 142,858 on December 31, 2004, credited to "Capital reserve" account). Thus, at December 31, 2004 and December 31, 2003, no provisions for loss were booked for the amounts of the benefits recognized though those dates.

The Company, supported by legal instruments, will seek to maintain its full entitlement to these fiscal benefits.

18 Guarantees of Veracel third-party debt

As of December 31, 2004, the Company is contingently liable as a several guarantor with respect to 50% of indebtedness of Veracel Celulose S.A., an entity under joint control with another company. Such company is the several guarantor of the additional 50% of indebtedness of Veracel Celulose S.A.. The total amount guaranteed by the Company is US$ 251.6 million. The expiration of the guarantees range from 2005 to 2015. At any time through those dates, the Company will be obligated to perform under the guarantees by primarily making the required payments, including late fees and penalties, limited to its proportion of the guarantees, if and whenever Veracel shall default in the payment of any of the guaranteed obligations, after the date of communication of default by the creditor pursuant to the terms and conditions of the relevant agreements.

19 Derivative instruments, hedging and risk management activities

The Company is engaged in the exportation of market pulp to various markets throughout the world. Management considers the Company's functional currency to be the U.S. dollar and approximately 22% of the Company's indebtedness was Real-denominated, consisting of loans bearing interest at variable rates.

These activities expose the Company to credit, currency and interest rate risks. The responsibilities of the Treasury include the proposal of risk management strategy and its implementation, and the evaluation of the effectiveness of the Company's overall risk management strategy. The Treasury reports to the Chief Financial Officer.

The Company may use derivative and non-derivative instruments to implement risk management strategy. However, by using derivative instruments, the Company exposes itself to credit and market risk. Credit risk is the failure of a counterparty to perform under the terms of the derivative contract. Market risk is the adverse effect on the value of a financial instrument that results from a change in interest rates, currency exchange rates, or commodity prices. The Company addresses credit risk by restricting the counterparties to such derivative financial instruments to major financial institutions. Market risk is managed by the Treasury.

(a) Foreign currency risk management

The Company's foreign currency risk management strategy may use derivative instruments to protect against foreign exchange rate volatility, which may impair the value of certain of the Company's assets. The Company has been using foreign currency forward and futures contracts to implement this strategy.

(b) Interest rate risk management

The Company's strategy for interest rate management has been to maintain a balanced portfolio of fixed and floating interest rates in order to optimize cost and volatility. The Company's interest rate risk management strategy may use derivative instruments to reduce earnings fluctuations attributable to interest rate volatility. The Company may use interest rate swaps to implement this strategy. At December 31, 2004 the Company had no outstanding interest rate swap contracts.

(c) Commodity price risk management

The Company is exposed to commodity price risks through the fluctuation of pulp prices. The Company currently does not utilize derivative financial instruments to manage its exposure to fluctuations in commodity prices, but may utilize them in the future.

20 Nonderivative financial instruments

Fair value - the Company considers that the carrying amount of its financial instruments generally approximates fair market value. Fair value has been determined as follows:

Cash - the carrying amount of cash is a reasonable estimate of its fair value.

Cash equivalents and short-term investments and bank deposits - cash equivalents are represented, principally, by short-term investments. Their fair value and that of other bank deposits not meeting the definition of cash equivalents were estimated using the rates currently offered for deposits of similar remaining maturities and approximates its carrying value.

Short-term debt and long-term debt - interest rates that are currently available to the Company for issuance of debt with similar terms and remaining maturities are used to estimate fair value, which approximates the carrying value at December 31, 2004 and 2003. The Company's financial structure does not require any substitution of such financing or the contracting of similar fundings.

The estimated fair value amounts have been determined by the Company using available market information and appropriate valuation methodologies. However, considerable judgment is necessarily required in interpreting market data to develop the estimates of fair value.

21 Variable interest entities

The Company employs investment funds to invest in underlying portfolios managed by the Company's treasury function. A third-party asset management Company is used to execute the operating and financial decisions related to the investment funds, including acquisition and disposition of the underlying securities, on behalf of the Company. The Company funds and owns the entire economic interest of the investment funds. These funds are considered to be variable interest entities as defined by FIN 46 (revised) and the Company is considered to be the primary beneficiary. Adoption of FIN 46 (revised) in 2004 did not have any material impact on the Company's financial position, results of operations or cash flows since the private investment funds have been classified as short-term investments prior to such adoption and fair value changes have been reflected in results of operations in the period of change. See note 6.

22 Geographical information

The Company has adopted SFAS No. 131 "Disclosures about Segments of an Enterprise and Related Information" ("SFAS 131") with respect to the information it presents about its operating segments and geographical information. SFAS 131 introduces a "management approach" concept for reporting segment information, whereby financial information is required to be reported on the same basis that the top decision-maker uses such information internally for evaluating segment performance and deciding how to allocate resources to segments.

The Company has four officials in its Board of Executive Officers (including the Chief Executive Officer). Each one of them is responsible for a sector: Operations, Commercial and Financial.

The way that the Board of Executive Officers is organized, no business segment was identified.

Sales by geographic area are determined based on the location of the customers.

Expressed in thousands of United States dollars

The Company's exports from Brazil, classified by geographic destination, are as follows:

	Year ended December 31,		
	2002	**2003**	**2004**
North America	278,988	408,699	464,740
Europe	290,877	402,822	525,290
Asia	119,966	229,376	247,417
Other	10,791	15,601	19,201
Total	700,622	1,056,498	1,256,648

Sales to two unaffiliated customers represented 42% of net sales in 2004. Two unaffiliated customers represented 42% and 35% in 2003 and 2002, respectively. No other individual customers represented more than 10% of net sales.

23 Related parties

Transactions with related parties resulted in the following balance sheet and income statement balances:

	December 31,			
	2003		**2004**	
	Assets	**Liabilities**	**Assets**	**Liabilities**
Balance sheet				
Current assets				
Cash and cash equivalents	51		1	
Accounts receivable	3,174			
Current liabilities – suppliers				8
Long-term debt (including current portion and accrued finance charges)		264,434		231,154
	3,225	264,434	1	231,162

Expressed in thousands of United States dollars

	Year ended December 31,					
		2002		**2003**		**2004**
	Income	**Expense**	**Income**	**Expense**	**Income**	**Expense**
Income statement						
Operating revenues	31,016		22,963			
Financial expenses		129,424		79,676		43,879
	31,016	129,424	22,963	79,676		43,879

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