ARACRUZ CELLULOSE S A
Form 20-F
June 30, 2003

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 20-F

|_| 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, 2002

OR

|_| TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

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)
Rua Lauro Muller, 116, 40th floor
22299-900 Rio de Janeiro, RJ, 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 regis
Class B Stock, without par value	New York Stock Exchange*
American Depositary Shares (as evidenced by American Depositary Receipts), each representing ten shares of Class B Stock	New York Stock Exchange

---

* Not for trading purposes, but only in connection with the registration of American Depositary Shares pursuant to the requirements of the Securities and Exchange Commission.

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
40,326,290	Shares of Class A Stock
536,837,131	Shares of Class B Stock

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 |_|

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

Item 17 |_| Item 18 |X|

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

Richard S. Aldrich, Jr.
Shearman & Sterling LLP
599 Lexington Avenue
New York, NY 10022

TABLE OF CONTENTS

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 Brazilian 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. at December 31, 2001 and 2002 and the corresponding Report of Independent Accountants;
- 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 (acoes preferenciais classe A) and non-voting preferred stock class B (acoes preferenciais classe B), respectively, which together are referred to as the Preferred Shares; and
- "tons" are to metric tons of 1,000 kilograms each.

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";
- all share data in this annual report have been adjusted to reflect a change effective March 17, 1997 in the number of shares of Class B Stock underlying each American Depositary Shares, or ADS, from five shares of Class B Stock per ADS to ten shares of Class B Stock per ADS, or the ADS Ratio Change; 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," "will," "will allow," "will continue," "will likely result," "should," "would be," "seek," "approximately," "intend," "plan," "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:

1

- 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,
- the development of solid wood products, 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 are 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 generally accepted accounting principles in the United States, or U.S. GAAP. Because we exported around 98% of our production in 2002 and operate in an industry that uses the U.S. dollar as its currency of reference, our management believes that the U.S. dollar is the most appropriate currency in which to present our financial statements. Accordingly, we decided to present our primary U.S. GAAP financial statements in U.S. dollars beginning in 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.

During 1997, the 36-month cumulative rate of inflation in Brazil fell below the 100% threshold, and our management determined the Brazilian economy to have ceased being a highly inflationary economy as of the fourth quarter of 1997. Accordingly, our management reevaluated our economic profile and our operations and determined that the U.S. dollar should remain as our functional currency, in accordance with the criteria established by SFAS 52. Our transition from a highly inflationary environment to a non-highly inflationary accounting environment as of and from January 1, 1998, had no financial reporting effect on our results of operations and financial position, because our reporting currency (which has been, since 1994, the U.S. dollar) was also our functional currency under highly inflationary conditions according to SFAS 52.

Pursuant to SFAS 52 as it applies to us, inventories, property, plant and equipment, accumulated depreciation and stockholders' equity are remeasured at historical rates of exchange, and other 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.

In our 1999, 2000, 2001 and 2002 financial statements, gains or losses resulting from the remeasurement of the financial statements and from foreign currency transactions have been reported in the consolidated statement of operations as single line items. The financial information presented below for the period ended December 31, 1998 has been reclassified to reflect such remeasurement. Previously, such gains or losses were allocated to the statements of operations line items to which they relate. These allocations have no effect on net income or loss.

We publish our financial statements in Brazil in accordance with accounting practices adopted in Brazil, or Brazilian GAAP, which differs in certain significant respects from U.S. GAAP. The principal differences between Brazilian GAAP and U.S. GAAP, as applied to us, are related to disclosure requirements. In addition, for all financial statements prepared for any period ended after January 1, 1996, Law No. 9,249/95 has abolished the requirement that companies apply monetary correction to their financial statements, which was previously required by Law No. 6,404 of December 15, 1976, as amended, or the Brazilian corporate law. Accordingly, our Brazilian GAAP financial statements at and for the years ended 1998, 1999, 2000, 2001 and 2002 are not adjusted to account for the effects of inflation. Our taxes and dividends are determined on the basis of Brazilian GAAP financial statements.

During the first quarter of 2001, in an effort to conform our reporting practices to those commonly used in the industry, we changed the classification of freight costs in the statement of income. As a result of this change, ocean freight and insurance charges, which had previously been classified as a reduction to export sales of eucalyptus pulp, together with inland freight charges, previously classified as selling expenses, are now classified as a component of cost of sales. Additionally, certain administrative expenses were identified as indirectly related to the production process and, beginning January 1, 2001, classified as a component of cost of sales. Historical information herein with respect to 1998, 1999 and 2000 was reclassified accordingly. Therefore, some information may differ from the condensed financial statements published elsewhere.

The following table presents our selected financial data as of the dates and for each of the periods indicated. Our U.S. GAAP financial statements as of December 31, 2000, 2001 and 2002 appear elsewhere herein, together with the report of PricewaterhouseCoopers Auditores Independentes, Rio de Janeiro, Brazil, independent accountants. The selected financial information at December 31, 1998, 1999 and 2000 has been derived from our U.S. GAAP 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			
	1998	1999	2000	
	(thousands of U.S. dollars, except number share amounts)			
Statement of Operations				
Operating Revenues				
Sales of eucalyptus pulp				
Domestic..................................	$38,449	$33,796	$43,601	$
Export....................................	503,836	596,242	800,634	5
Total sales................................	$542,285	$630,038	$844,235	$6
Sales taxes and other reductions...........	(39,490)	(43,459)	(63,240)	(
Net operating revenues.....................	$502,795	$6,579	$780,995	$5

Operating costs and expenses				
Cost of sales................................	$414,874	$375,513	$412,313	$4
Selling......................................	28,329	25,311	21,492	
Administrative...............................	29,560	18,354	22,454	
Provision for loss on ICMS credit..........	-	-	-	
(Gain)/Loss and provision for loss sale of property, plant and equipment and spare-parts inventories..................	18,902	26,153	4,826	
Other, net...................................	9,286	6,907	7,152	
Total operating costs and expenses..........	$500,951	$452,238	$468,237	$4
Operating income	$1,844	$134,341	$312,758	$
Non-operating (income) expenses				
Equity in results of affiliated company.....	-	-	1,313	
Financial income............................	$(104,840)	$(100,692)	$(64,849)	$(
Financing expense...........................	120,955	120,336	101,461	
Loss (gain) on currency remeasurement, net..	7,780	7,454	(8,812)	
Other, net..................................	(192)	(209)	(131)	
Total other income..........................	$23,703	$26,889	$28,982	$
Income (loss) before income taxes	$(21,859)	$107,452	$283,776	$
Income tax expense (benefit)				
Current.....................................	$(9,573)	$8,980	$40,461	$
Deferred....................................	(15,733)	7,699	41,604	
Total.......................................	$(25,306)	$16,679	$82,065	$
Net income..................................	$3,447	$90,773	$201,711	$

	For the Year Ended December 3			
	1998	1999	2000	2
	(thousands of U.S. dollars, except number o share amounts)			
Earnings per share(1)				
Class A Stock...............................	$0.09	$0.09	$0.20	$
Class B Stock...............................	0.00	0.09	0.20	
Common Stock................................	0.00	0.08	0.18	
Dividends per share				
Class A Stock...............................	$0.09(2)	$0.06(3)	$0.06(4)	$0
Class B Stock...............................	0.02(2)	0.02(3)	0.06(4)	0
Common Stock................................	0.02(2)	0.01(3)	0.05(4)	0

Weighted-average number of shares outstanding (thousands of shares)				
Class A Stock	41,007	40,979	40,903	4
Class B Stock	564,374	553,279	552,889	53
Common Stock	454,908	454,908	454,908	45
Total	1,060,289	1,049,166	1,048,700	1,03

(1) Holders of Class B Stock have no dividend preference. Holders of Class A Stock are entitled to an annual preferential dividend.
(2) Including the dividend declared on April 17, 1998 and paid on May 11, 1998.
(3) Including the dividend declared on March 25, 1999 and paid on April 22, 1999.
(4) Including the dividend declared on April 5, 2000 and paid on April 30, 2000.
(5) Including the dividend declared on March 30, 2001 and paid on April 12, 2001.
(6) Including the dividend declared on April 30, 2002 and paid on May 13, 2002. The annual shareholders' meeting held on April 29, 2003 defined dividends with respect to 2002 in the amount of US$107.7 million, which were paid on May 15, 2003.

	At December 31,			
	1998	1999	2000	20
	(thousands of U.S. dollars)			
Balance Sheet Data				
Cash and cash equivalents	$ 151,886	$ 312,590	$ 18,091	$ 2
Other current assets	182,028	190,889	261,815	21
Debt securities available for sale	696,404	189,480	323,032	40
Property, plant and equipment, net	1,892,451	1,702,747	1,664,322	1,91
Investment in affiliated company	-	-	79,698	8
Other assets	277,720	205,297	107,500	14
Total assets	$3,200,489	$2,601,003	$2,454,458	$2,77
Short-term debt	821,157	473,652	272,042	32
Other current liabilities	39,312	40,174	55,035	9
Long-term debt	730,939	392,354	278,873	53
Other long-term liabilities	41,917	41,511	75,387	7
Stockholders' equity	1,567,164	1,653,312	1,773,121	1,73
Total liabilities and stockholders' equity	$3,200,489	$2,601,003	$2,454,458	$2,77

Exchange Rates

The purchase and sale of foreign currency in Brazil is subject to governmental control. There are two foreign exchange markets in Brazil that are subject to regulation by the Central Bank of Brazil, or the Central Bank, both of which operate at free floating rates:

- the free rate foreign exchange market, also known as the commercial market; and o the "floating" rate foreign exchange market.

In 1999, the Central Bank unified the operational limits applicable to both markets. However, each market continues to be governed by specific regulations. Most trade and financial foreign exchange transactions are carried out on the commercial market. These transactions include the purchase or sale of Class B Stock or the payment of the dividends or interest with respect to Class B Stock. Foreign currencies may only be purchased through a Brazilian bank authorized to operate in these markets. In both markets, rates are freely negotiated but may be strongly influenced by Central Bank intervention.

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 ease, on January 15, 1999, the Central Bank allowed the real to float freely. On June 26, 2003, the commercial selling rate was R$2.8491 per US$1.00. We cannot assure you that the real will not appreciate or depreciate substantially in the near future.

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)
1998	1.1165	1.2087	1.1611
1999	1.2078	2.1647	1.8158
2000	1.7234	1.9847	1.8295
2001	1.9357	2.8007	2.3420
2002	2.2709	3.9552	2.9309

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 exchange rates (PTAX) on the last day of each month during the relevant period.

	Exchange Rate of R$ per US	
Month Ended	Low	High
December 31, 2002	3.4278	3.7980
January 31, 2003	3.2758	3.6623
February 28, 2003	3.4930	3.6580
March 31, 2003	3.3531	3.5687

April 30, 2003	2.8898	3.3359
May 31, 2003	2.8653	3.0277
June 2003 (until June 26, 2003)	2.8491	2.9780

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

We 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. Fluctuations in the exchange rate between the real and the U.S. dollar may also affect the U.S. dollar equivalent of the real price of the Class B Stock on the Brazilian stock exchange. 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.

In the past, the Brazilian government has intervened in the Brazilian economy and occasionally made drastic changes in policy. The Brazilian government's actions to control inflation and institute other policies have included wage and price controls, currency devaluations, capital controls, and limits on imports. Our business, financial condition and results of operations may be adversely affected by changes in government policies as well as general economic factors, including:

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

At the end of 2002, Brazil elected a new president from the Workers' Party, Luis Inacio Lula da Silva, known as Lula. In the period leading up to and following his election, there was substantial uncertainty relating to the policies that the new government would pursue, including the potential implementation of macroeconomic policies that differed significantly from those of the prior administration. This uncertainty resulted in a loss of confidence in the Brazilian capital markets and the continued devaluation of the real. Although the new government has not yet departed in any material way from previous policies, it is premature to determine what policies might be implemented, whether these policies will be effective, how these policies might impact us and how investors and the capital markets will react to them. Any substantial negative reaction to the policies of the Brazilian government could adversely affect our business, operations and the market price of our preferred shares and ADSs.

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 revenues and a significant portion of our assets are denominated in reais and we have U.S. dollar-denominated debt and other liabilities, we may be adversely affected by any future devaluations of the real against the U.S. dollar. The Brazilian currency has been devalued periodically during the last four decades. See "--Selected Financial Data--Exchange Rates."

Our cash operating 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 may decrease. As expressed in reais, any significant devaluation of the real may produce exchange losses on unhedged debt denominated in foreign currencies.

The real devalued against the U.S. dollar by 9.3% in 2000. During 2001, the real experienced a period of significant devaluation, due in part to the economic and political uncertainties in Argentina, the global economic slowdown and the energy crisis in Brazil. In 2001, the depreciation of the real relative to the U.S. dollar totaled 18.7%. In 2002, the depreciation of the real relative to the U.S. dollar totaled 52%, due in part to the continued economic and political uncertainties in emerging markets and the global economic slowdown. From January 1, 2003 through May 31, 2003, the real appreciated 16%.

The Central Bank has intervened occasionally to control unstable movements in the foreign exchange rate. At the present time, it is not possible to predict whether the Central Bank will continue to let the real float freely. Accordingly, it is not possible to predict what impact the Brazilian government's exchange rate policies may have on us. We cannot assure you that the Brazilian government will not in the future impose a band within which the real/U.S. dollar exchange rate could fluctuate or set a fixed exchange rate, and what impact such an event might have on our operations.

Devaluations of the real relative to the U.S. dollar also create additional inflationary pressures in Brazil that may negatively affect us. They generally curtail access to foreign financial markets and may require government intervention, including recessionary governmental policies. See "--Inflation and certain governmental measures to combat inflation may contribute significantly to economic uncertainty in Brazil and to heightened volatility in the Brazilian securities markets." Devaluations also reduce the U.S. dollar value of distributions and dividends on the ADSs and the market price of our preferred shares and ADSs.

In addition, political and economic uncertainty resulting from the new president elected in October 2002 may have an adverse effect on the Brazilian financial and capital markets, including the foreign exchange market. See "--Brazilian political and economic conditions have a direct impact on our business and the market price of our preferred shares and ADSs."

Inflation and certain governmental measures to combat 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 in the past had significant negative effects on the Brazilian economy. Our cash operating expenses are substantially denominated in reais and tend to increase with Brazilian inflation because our 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, our operating expenses may increase and, assuming constant U.S. dollar sales prices, our profit margins may decrease. In addition, high inflation generally leads to higher domestic interest rates, and, as a result, our 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 owns or controls many companies, including some of the largest in Brazil. For example, Banco Nacional de Desenvolvimento Economico e Social - BNDES, which is owned by the Brazilian government, indirectly owned approximately 12.5% of our common stock as of December 31, 2002 and has, through a subsidiary, advanced approximately 33.33% of our total consolidated indebtedness as of such date. See "Item 7B. Related Party Transactions."

Developments in other emerging markets, including Argentina and Venezuela, may adversely affect the market price of our preferred shares and ADSs.

The market for securities issued by Brazilian companies is influenced by economic and market conditions in Brazil and, to varying degrees, market conditions in other Latin American and emerging market countries. Although economic conditions are different in each country, the reaction of investors to developments in one country may cause the

capital markets in other countries to fluctuate. 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.

For example, in 2001 after a prolonged recession followed by political instability, the Argentine government announced that it would no longer continue to service its public debt. In order to address the deteriorating economic and social conditions, the Argentine government abandoned its decade-old fixed dollar-peso exchange rate, allowing the peso to float to market rate levels. In 2002, the Argentine peso experienced a 237% devaluation against the U.S. dollar. The situation in Argentina has negatively affected investors' perceptions of Brazilian securities.

The recent political crisis in Venezuela may also influence investors' perception of risk in Brazil. If market conditions in Argentina and Venezuela continue to deteriorate, they may adversely affect our ability to borrow funds at a favorable interest rate or to raise equity capital when and if there is a need. Adverse developments in Argentina, Venezuela or in other emerging market countries could lead to a reduction in both demand and the market price for our preferred shares and ADSs.

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 Sao 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 Comissao de Valores Mobiliarios, 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.

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 Sao Paulo Stock Exchange (Bolsa de Valores de Sao Paulo), or BOVESPA, the main Brazilian stock exchange, had a market capitalization of approximately US$124 billion as of December 31, 2002, and an average monthly trading volume of approximately US$4.1 billion in 2002. In comparison, the NYSE had a market capitalization of US$9.7 trillion as of December 31, 2002, and an average monthly trading volume of approximately US$859 billion for 2002.

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 46.8% of the aggregate market capitalization of BOVESPA as of December 31, 2002. The top ten stocks in terms of trading volume accounted for approximately 56.5% 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 interests relative to actions taken by our board of directors or 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.

10

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. After reaching a peak in the middle of 1995, market pulp prices continued to fall through the first quarter of 1999, due primarily to a significant drop in demand, although market prices began to increase beginning in the second quarter of 1999 and continued to increase through the second half of 1999 and early 2000. In the second half of 2000, market prices of pulp were flat for the whole period. Weak demand and excess inventories in the hands of pulp producers caused eucalyptus pulp list prices to fall at the end of March 2001. Market conditions remained difficult throughout the second quarter of 2001, especially in Europe. During the third quarter of 2001, overall demand for pulp improved and pulp prices increased in the European and Asian markets. In 2002, the average list price decreased 8% compared to the average in 2001. This was primarily due to the slowdown in the growth of the major economies which began in 2001, and continued to negatively impact the global demand for paper throughout 2002. It is possible that market prices for pulp will decline in the future, or that there will not be sufficient demand for our products to enable us to operate our production facilities in an economical manner. 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 wood.

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 bleached eucalyptus kraft market pulp, we also compete with producers in the broader segment of the pulp market. Several 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.

We are subject to stringent environmental laws and regulations in Brazil governing air emissions, effluent discharges, solid wastes, odor and reforestation, and we require permits from governmental agencies for certain of our operations. Changes in these laws and regulations could adversely affect us. If we violate or fail to comply with these laws, regulations and permits, we could be fined or otherwise sanctioned by regulators or our permits could be revoked, and our ability to operate could be suspended or otherwise adversely affected. In addition, noncompliance with these laws, regulations and permits could result in criminal sanctions for us and for our employees. We could also be responsible for related environmental remediation costs, which could be substantial.

11

It is possible that governmental agencies or other authorities will pass new laws or impose additional laws and regulations even more stringent than the ones currently in force or will seek a more stringent interpretation of existing laws and regulations that would require us to spend additional funds on environmental compliance or limit our ability to operate as we currently do. In addition, these actions could increase the costs associated with renewing existing permits or applying for new ones. There can be no assurance that these additional funds or costs will not be material or that existing permits will be renewed.

Actions by state legislature may adversely affect our operations.

In September 2001, the legislature of the State of Espirito Santo, where we own approximately 140.7 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 an injunction relief granted by Brazilian Supreme Court, in response to suits brought by the National Confederation of Industry and by the National Brazilian Confederation of Agriculture and Cattle Raising. However, there can be no assurance that other 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 Espirito Santo legislative assembly created an investigating commission (Comissao Parlamentar de Inquerito) to investigate the legality of our permits and the acquisition of our properties from the date we began our operations in Espirito Santo. As the procedures in the investigation were not concluded within the prescribed time period for investigations of this type, the commission was terminated without issuing a conclusive report. While we are confident that we have obtained all necessary permits and that all our property was legally acquired strictly in accordance with all laws and regulations, we cannot assure you that future investigations by the state government or the legislative will not be initiated in the future.

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.

We may, as part of our business strategy, acquire other businesses in Brazil or elsewhere or enter into alliances. 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 our ability to identify acquisitions and negotiate, finance and close transactions. Even if we complete future acquisitions:

- 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 new businesses or manage 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. 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.

We are controlled by a few shareholders.

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."

Various other risks could have a material adverse effect on our financial results.

Our operations are subject to various other risks that affect our forests and manufacturing processes, including fire, port closings, disease and factory explosions, which could have a material adverse effect on our financial results.

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 anonima), 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 mill are located at Rodovia Aracruz, Barra do Riacho, kilometer 25, Municipality of Aracruz, State of Espirito Santo, Brazil, and its telephone number is 55-27-3270-2122. Our principal office is located at Rua Lauro Muller, 116, 40th floor, 22299-900 Rio de Janeiro, State of Rio de Janeiro, Brazil, and its telephone number is 55-21-3820-8111. Our agent for service of process in the United States is CT Corporation, 111 Eighth Avenue, New York, NY 10011. We maintain an Internet website at www.aracruz.com.br. Information contained on our website is not part of this annual report.

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 with a nominal production capacity of approximately 400,000 tons of pulp per year. In early 1991, we completed an expansion plan, known as the 1991 Expansion Project, which increased the mill's nominal capacity (i.e., the production capacity for which the mill was designed) 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 mill's nominal capacity to 1,240,000 tons per year, as well as our production efficiency.

In 1997, as part of our strategy for diversification into other forest businesses, 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 us created in 1997 for the production of solid wood products. See "--Business Overview--Aracruz Produtos de Madeira."

In June 2000, our board of directors approved the expansion of the nominal production capacity of our facilities by 700,000 tons per year, know as the Fiberline C Expansion Project. The Fiberline C Expansion Project involves the addition of a new pulp line and certain other modifications to existing equipment at the mill 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, after being built in record time. See "--Business Overview--Fiberline C Expansion Project." In order to provide for the increased production volume resulting from the Fiberline C Expansion Project, on June 1, 2000, we acquired Terra Plana Agropecuaria Ltda., whose assets are comprised of 19,000 hectares of land appropriate for planting eucalyptus trees, entered into a three-year agreement with Veracel for the supply of wood, and acquired, together with Bahia Sul Celulose S/A, forest assets in the northern area of the State of Espirito Santo.

On October 10, 2000, we acquired a 45% stake in Veracel, a joint venture between Stora Enso OYJ and Odebrecht S.A., or Odebrecht, to build a pulp mill.

On January 31, 2003, Odebrecht sold its stake in Veracel to us and Stora Enso OYJ. Since then, Stora Enso OYJ and we each own 50% of Veracel's capital stock. The construction of Veracel's pulp mill has begun in the first semester of 2003, and its conclusion is expected to take place within two years. See "--Business Overview--Acquisition of Veracel" and Note 4 to the consolidated financial statements.

On October 3, 2001, Votorantim Celulose e Papel S.A., or VCP, one of our competitors, acquired the 28% stake holding of our common stock from Mondi Brazil Limited. See "Item 7A. Major Shareholders."

On May 30, 2003, we acquired the capital stock of Riocell S.A., or Riocell, held by Klabin S.A. and Klabin do Parana Produtos Florestais Ltda. Riocell is one of our competitors. See "--Business Overview--Competition."

Capital Expenditures

Our capital expenditures for the years 2002, 2001 and 2000 were US$260.7 million, US$421.5 million and US$138.4 million, respectively.

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

	For the years ende	
	2002	2001
	(in US$ mil	
Fiberline C Expansion Project..	US$ 185.3	US$ 35
Siviculture and other forestry investments..........................	39.5	4
Forests (includes land purchase)....................................	15.4	
Improvements/industrial investments.................................	9.4	1
Acquisition of equity participation in Veracel......................	--	
Other...	10.8	
Total...	US$ 260.7	US$ 42

The US$160.8 million decrease in capital expenditures in 2002 compared to 2001 and the US$283.1 million increase in capital expenditures in 2001 compared to 2000 were primarily due to investments in the Fiberline C Expansion Project.

During 2003, we expect to invest approximately US$114.0 million, of which US$62.0 million in the Fiberline C Expansion Project and US$52.0 million in industrial, forestry and other investments.

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 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.

We produced approximately 1,656,000 tons of bleached eucalyptus kraft market pulp in 2002, a 30% increase compared to 2001, representing approximately 8% of the total worldwide production capacity and 22% of the worldwide production capacity of bleached eucalyptus kraft market pulp during 2002. In each of 2002 and 2001, eucalyptus accounted for approximately 38% of the total worldwide production capacity of bleached hardwood kraft market pulp. In 2002, sales to customers located outside Brazil, especially in North America, western Europe and Asia, accounted for approximately 98% of our sales volume. During 2001, sales to customers located outside Brazil accounted for approximately 97% of our sales volume. See "--Markets and Customers" and "--Competition."

In 2002 we sold approximately US$669 million of eucalyptus pulp compared to US$574 million in 2001 and US$781 million in 2000.

14

In December 1999, we moved our headquarters from Rio de Janeiro to the municipality of Aracruz, in the Brazilian coastal state of Espirito Santo, where our production facilities are located. We continue to maintain executive offices in Rio de Janeiro for our financing, administrative and trading activities. Our production facilities consist of a eucalyptus pulp mill, or the Mill, which has three production units, each with two bleaching, drying and baling lines. The Mill's third production unit began production in May 2002. See "--Fiberline C Expansion Project."

Also in December 1999, we sold our electrochemical plant that services the Mill to the chemicals operating group of Canadian Occidental Petroleum Ltd., a Canadian-based global oil and gas and chemical company, for approximately US$61 million. See "--Raw Materials--Chemicals."

We own approximately 305,363 hectares of forest and other land in the State of Espirito Santo and the State of Bahia, of which 185,894 hectares are planted with eucalyptus forests. The Mill is located approximately 1.5 kilometers from the port facilities at Barra do Riacho, which are 51% owned by us. See "--History and Development of Aracruz" above.

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 planting processes,
- growing and harvesting of our trees,
- the comparatively short harvest cycle of our trees, and
- lower energy and chemical costs.

During 2001 and 2002, we were able to meet almost 65% 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 97% 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 Mill. See "--Raw Materials--Energy."

Business Strategy

The key elements of our strategy are:

- pursuing a growing position among the best global producers of forest products, concentrating on market segments of significant size and capable of adding value to us,
- generating strong returns to our shareholders,
- leveraging our competence in renewable forestry uses,
- developing products that add value to our customers while concentrating on our core business as a pulp producer, and
- creating development opportunities for our employees in order to retain our employees.

The following ongoing projects implement our business strategy:

- Economies of scale resulting from new capacity increases. The commencement of the operation of the Fiberline C Expansion Project at the end of May 2002 increased our nominal production capacity to over 2,000,000 tons per year in the middle of 2002. The Fiberline C Expansion Project relies on our technology advances and benefits from our existing overhead and management structure, which is expected to absorb the new activity without additional fixed costs. These improvements in pulp manufacturing technologies and in project development in the Fiberline C Expansion Project will enable us to reduce pulp costs and improve quality levels.
- Improvements in forestry technology using advanced genetic techniques, which will result in an increase in the forest yield.
- Optimization of transportation logistics. Since transportation of wood to the Mill comprises a large portion of the cost of our pulp production, we seek to improve our transportation logistics and costs. During 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. See "--Transportation."
- Redesign of management processes with the support of state-of-the-art information technology in order to improve efficiency and reduce costs. In 2001, we implemented new modules of the company-wide SAP R/3 enterprise system that controls, simplifies and integrates our business processes. We are currently using virtually all the modules supplied by SAP, both in the pulp mill and the sawmill operations. Recently, we have selected the mySAP.com(R) platform to improve communications with customers and suppliers.
- Diversification of our business into other forest products. We have

invested in Aracruz Produtos de Madeira S.A., a producer of solid wood products, in order to further complement our product line.

- Increase of 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.

Fiberline C Expansion Project

The Fiberline C, our pulp operational unit, began operations at the end of May 2002, after being completed in 17 months (two months ahead of schedule) at a lower cost than originally budgeted.

With nominal capacity of 700,000 tons per year, the cost of the new line will be approximately US$467 million, or US$667 per ton. The volume of production added during year 2002 by the Fiberline C totaled 340,000 tons. During November 2002, the facility reached a monthly production of 61,000 tons, representing an annual production of approximately 720,000 tons.

We entered into several supply contracts in connection with the Fiberline C Expansion Project. Under those supply contracts, the suppliers were required to provide products and services, installation and civil construction. Payments under the supply contracts are made upon the completion of milestones specified in each of the supply contracts, and the obligations of the suppliers thereunder are guaranteed by performance bonds, in each case in the amount of 10% of the contract price, issued by either a major financial institution or an insurance company.

The new production volume resulting from the Fiberline C Expansion Project will require an increase in our forest base of approximately 72,000 hectares of eucalyptus plantations. For this reason, in June 2000, we acquired Terra Plana Agropecuaria, with assets comprised of 19,000 hectares of land appropriate for planting eucalyptus trees. Through December 31, 2001, we acquired approximately 44,000 additional hectares of land through separate transactions. Additionally, in September 2002, Bahia Sul and we signed, jointly with Companhia Vale do Rio Doce and its wholly

16

owned subsidiary, Florestas Rio Doce S/A, a contract for the acquisition by Bahia Sul and us of an equal stake in forest assets comprising approximately 40,000 hectares of lands and eucalyptus-planted forests.

In order to meet the expected increase in production arising from the Fiberline C Expansion Project, we built a port facility in Caravelas, State of Bahia, and expanded our port facility in Barra do Riacho, State of Espirito Santo.

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 build a pulp mill. We entered into an agreement with Odebrecht relating to our acquisition of 40% of the total outstanding capital stock of Veracel for approximately US$72 million. We also entered into another agreement with Stora Enso Treasury Amsterdam B.V., or Stora Enso, relating to our acquisition of 5% of the total outstanding capital stock of Veracel for approximately US$9 million. 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 approximately US$9.5 million. 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 our business in the future from another operational base in Bahia that can potentially replicate our accomplishments in the State of Espirito Santo.

Under both stock purchase and sale agreements, we have agreed to indemnify the relevant counterparty for certain liabilities and/or damages which such counterparty may incur as a result of a breach by us of the representations and warranties or a default by us under a covenant under those agreements.

We have also entered into a three-year wood supply contract for a total of up to 3.85 million cubic meters with Veracel, providing wood for the Fiberline C Expansion Project until the new plantations reach harvesting time.

In May 2003, Stora Enso and we approved the construction of Veracel's pulp mill for the production of bleached eucalyptus kraft market pulp in Eunapolis, in the State of Bahia. The mill will have a nominal capacity of 900,000 tons per year, and the overall investment is budgeted at US$1.25 billion, of which US$300 million has already been invested in forestry-related activities and infrastructure investments, such as roads and a specialized harbor.

The financing for the project is expected to be 45% equity and 55% loans from Brazilian and international development agencies.

The construction of the mill will be initiated in the first semester of 2003, and it is expected to be concluded within two years. The project will be carried out under the EPC (Engineering, Procurement and Construction) concept and will require 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 will be contracted mostly from Brazilian suppliers.

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 Original Veracel Shareholders' Agreement, which sets 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. The Original 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 is given by any party to the Original Veracel Shareholders' Agreement. The Original Veracel Shareholders' Agreement will terminate automatically if the ownership by any of the Veracel Shareholders of common shares of Veracel exceeds 50%. The Original Veracel Shareholders' Agreement provides that Veracel will at all times during its term have a board of directors comprised of five members, of which (i) two will be elected from individuals appointed by Stora Enso, (ii) two will be elected from individuals appointed by us and (iii) one will be elected from individuals appointed by Odebrecht. 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 Original 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 other than (i) prior to the decision to build Veracel's pulp mill, or the Implementation Decision, and (ii) if the

Implementation Decision is made, after the second anniversary of the start-up of Veracel's pulp mill. We each have a right of first refusal if the other party wishes to transfer all of its common shares of Veracel before the Implementation Decision. Under the Original Veracel Shareholders' Agreement, Odebrecht may not transfer any of its common shares of Veracel other than (i) on or prior to December 31, 2002, if there has been no Implementation Decision, (ii) following the Implementation Decision, (iii) after the start-up date of Veracel's pulp mill (if it is built) or (iv) after the second anniversary of the start-up of Veracel's pulp mill (if it is built), provided that, in the case of the conditions described in (i), (ii) and (iii), Odebrecht will have the right to transfer all of its common shares of Veracel to the other shareholders of Veracel, for different prices, in accordance with the terms set forth in the Veracel Shareholders' Agreement. Any of the Veracel Shareholders may transfer its common shares of Veracel to an affiliate, subject to certain limitations, or with the prior written consent of each of the other Veracel Shareholders. The Original 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 Original 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 Original Veracel Shareholders' Agreement also provides that we, so long as neither we nor any of our subsidiaries is a shareholder of Veracel, will not acquire (or caused to be acquired) any interest in real property in Veracel. The same covenant applies to Veracel with respect to real property in our core area.

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 Original Veracel Shareholders' Agreement was amended. According to the amended agreement, or the Veracel Shareholders' Agreement, the board of directors of Veracel will be comprised of four members, of whom (i) two will be elected from individuals appointed by Stora Enso, and (ii) two will be elected from individuals appointed by us. The Original Veracel Shareholders' Agreement provides 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) will 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 Original Veracel Shareholders' Agreement. The Original Veracel Shareholders' Agreement will govern the management and operation of Veracel.

Aracruz Produtos de Madeira

As part of our 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., or APM, which then became our wholly owned subsidiary. The high-tech hardwood lumber sawmill, which is located in the State of Bahia, was commissioned in the first quarter of 1999 and started sales during the third quarter of 1999. APM manufactures and markets Lyptus(R), a 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 37,500 cubic meters per year. As of December 31, 2002, APM had nominated 12 sales representatives in major furniture markets in Brazil and was supplying an industrial customer base of more than 300 manufacturers.

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(R) brand of high-quality sawn wood in domestic and international markets while ensuring that its quality standards were maintained.

In 2001, we established a commercial partnership with the U.S.-based Weyerhaeuserr Co., or Weyco, one of the largest forestry companies in the world, for the exclusive distribution of Lyptus(R) in the North American markets. This new partnership arrangement has given APM access to over 70 Weyco points of sale in the U.S. and Canada, increasing the presence of Lyptus(R) 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. Another initiative that advanced the

internationalization of APM was its affiliation with the International Wood Products Association at the beginning of last year.

We have expanded the 2001 agreement with Weyco of the U.S. to extend sales of Lyptus(R) to the European and Asian markets, thus assuring the presence of the product in over 100 points of distribution in those regions.

The initial impact of this agreement was to increase Lyptus(R) sawn wood exports from 4.2% in 2001 to 10.6% in 2002, in addition to an increase of 47,223m2 of Lyptus(R) flooring. In 2002, 15% of total production was exported.

Consistent with the strategies set forth above, we may, from time to time, enter into joint venture, technological exchange, marketing or other arrangements with third parties to complement our business and competitive positions.

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, also 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. From 1992 to 2002, the market for hardwood has had an annual rate of growth in demand of 4.7%, while the market for softwood has had a 2.8% annual rate of growth in demand. Within the hardwood segment, bleached eucalyptus kraft market pulp has demonstrated the highest annual rate of growth in demand with a 5.3% annual growth in demand over the same ten-year-period.

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 48% in 2002) primarily due to its high quality, and because of properties, such as its softness, opacity and printability.

International Markets

From 1992 to 2002, the worldwide production capacity of bleached hardwood kraft market pulp is estimated to have grown an average of approximately 4.3% per year, from 13.2 million tons to 20.1 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 2.2 million tons from 2000 to 2002. 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 11.5 million tons in 1992 to 18.1 million tons in 2002. Consumption of market pulp is concentrated mainly in Europe, North America and Asia. In 2001, demand for bleached hardwood kraft market pulp amounted to approximately 7.1 million tons in Europe, 2.6 million tons in North America and 6.4 million tons in Asia, 42%, 16% and 38%, respectively, of the world's total demand. In 2002, demand for bleached hardwood kraft market pulp amounted to approximately 7.9 million tons in Europe, 2.8 million tons in North America and 6.6 million tons in Asia, 44%, 15% and 36%, respectively, of the world's total demand. In 2001, we supplied approximately 475,000 tons or 7% of the total European demand, approximately 480,000 tons or 18% of the total North American demand, and approximately 306,000 tons, or 5%, of the total Asian demand. In 2002, we supplied approximately 637,000 tons, or 8%, of the total European demand, approximately 623,000 tons or 23% of the total North American demand, and approximately 280,000 tons, or 4%, of the total Asian demand.

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 1993, the lowest price level since 1983. Prices began to increase in the second quarter of 1999 through the second half of 1999. In 1999, the average F.O.B. price per ton of bleached eucalyptus kraft market pulp delivered in the United States was US$479, an increase of approximately 4% as compared to 1998. In 2000, prices continued increasing during the first half of the year, led mainly by the strong demand in Europe.

However, in the second half of 2000, prices remained stable. The average F.O.B. price per ton of bleached eucalyptus kraft market pulp delivered in the United States was US$618, an increase of approximately 29% as compared to 1999.

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:

[CHART OMITTED]

While our volume of pulp sales during 2002 was higher than in 2001 or 2000, the price of pulp declined throughout 2002. The average list price decreased 8% in 2002 compared with the average in 2001, primarily due to the slowdown in the growth of the major economies, which began in 2001, and continued to negatively impact the global demand for paper throughout 2002.

The high level of the world pulp inventories witnessed at the beginning of the year caused prices to fall to their lowest levels by the end of the first quarter of 2002. From then on, the recovery in demand, coupled with expectations of renewed growth in the world economy during the second half of 2002 and underpinned by improved control over supply, prompted consecutive increases in the price of eucalyptus pulp, which reached US$510 per ton delivered to the United States in the third quarter of 2002.

Despite the good performance of the main consumer markets, high-quality tissue and printing and writing papers, the price of pulp began falling again at the end of 2002. Considering these factors, the average list price of eucalyptus pulp in 2002 (US$484 per ton, delivered to the United States) was even lower than the average in 2001.

Domestic Market

In 2002, we supplied approximately 27,000 tons of the aggregate domestic demand for bleached eucalyptus kraft market pulp, compared to 36,000 tons in 2001.

Demand for bleached hardwood kraft market pulp in Brazil decreased from 530,740 tons in 1998 to 511,760 tons in 1999, due to the adverse economic situation in Brazil during most of 1999. See "Item 5. Operating and Financial Review and Prospects--Brazilian Economic Environment." However, in 2000, the Brazilian economic scenario improved and the demand for bleached hardwood kraft market pulp reached 517,000 tons, an increase of 1% compared to 1999. In 2001, the demand for bleached hardwood kraft market pulp reached 489,000 tons, a 5% decrease compared to 2000, primarily due to the energy rationing in Brazil, which had a negative impact on paper production. In 2002, the demand for bleached hardwood kraft market pulp reached 512,000 tons, a 5% increase compared to 2001, primarily due to the paper production growth, mainly on the tissue segment (8.4%).

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

- Aracruz Celulose S.A.,
- Celulose Nipo-Brasileira S.A., or Cenibra,
- Bahia Sul Celulose S.A.,
- VCP,
- Jari Celulose S.A., and
- Riocell S.A.

Together the six largest Brazilian producers accounted for 64% of total domestic sales in 2002, with us accounting for 5% of total domestic sales. For the last two years, we have held approximately the same percentage of our domestic market share. Our domestic sales volume of bleached hardwood kraft market pulp was 2% of its total sales volume in 2002 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

At December 31, 2002, we owned approximately 307,300 hectares of forest and other land, of which 69,500 hectares are situated in the State of Espirito Santo near the Mill site, 71,000 hectares are situated farther north primarily in the municipalities of Sao Mateus and Conceicao de Barra in the State of Espirito Santo, and 164,600 hectares are in the southernmost region of the State of Bahia, which at their furthest point are less than 340 kilometers from the Mill. At December 31, 2002, we also owned approximately 2,004 hectares of forest and other land in the State of Minas Gerais. In 2002, we purchased 7,500 hectares, which are being prepared for new plantations. The average distance from our forest areas currently in use to the Mill site is 188 kilometers. See "--Raw Materials--Wood." 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 Mill, as discussed in "--Raw Materials--Wood." We are always evaluating opportunities for acquiring land with forest in the State of Espirito Santo that is close to the Mill in order to reduce the distance, and the associated costs, of hauling wood between the forest and the Mill 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 307,300 hectares owned by us, approximately 187,500 hectares are currently used for the planting of trees to supply pulp production and solid wood production, approximately 102,500 hectares are reserved for preservation, approximately 17,300 hectares have been used in the construction of roads and the remainder is used for research and development and other activities. Brazilian law requires that 20% of our land, at any given time, either remain uncultivated with eucalyptus trees or planted with indigenous species.

Throughout 2001, one of our principal objectives was to purchase land and establish partnerships with farmers, known as the Forestry Partners Program, for the establishment of new plantations to ensure the future supply of wood for Fiberline C. By the end of 2002, we expect to have established approximately 65,000 additional hectares of eucalyptus plantation. In 2001, we consolidated our seedling production technology at our nursery, producing gains in our productivity. A typical plantation of ours grows 42 cubic meters of pulpwood per hectare per year. A typical eucalyptus tree grows an average of approximately three inches per week and will grow to a height of 90 feet in seven years, at which point it is harvested.

We 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. Our method of cloning results in trees whose fibers are extremely homogeneous, which we believe results in a more streamlined industrial process and higher-quality pulp. Today,

approximately 89% of our 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 less 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 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 timberlands through advanced forestry and tree-cloning techniques.

In 2002, we supplied most of our 6.2 million cubic meter wood requirements from our own eucalyptus forests in the State of Espirito Santo and in the southernmost region of the State of Bahia. During the same period, we also purchased 2.2 million cubic meters of wood, which is equivalent to 35% of our wood consumption, of which approximately 905,000 cubic meters were purchased through the Forestry Partners Program, compared to 655,000 cubic meters in 2001.

Based on the current demand for pulp and our current supply of trees suitable for harvesting, we may not need to purchase wood from third-party suppliers in the future, except in certain limited circumstances. Wood purchased from independent suppliers is not always of the same quality and uniformity of fiber as wood from forests owned and managed by us. With the aim of reducing our dependence on wood supplied by traditional independent sources, during 1990 and 1991 we initiated a program to provide approximately 46.7 million seedlings (along with financial and technical assistance to ensure that the cultivated trees meet our standards) to farmers in the State of Espirito Santo who own land near the Mill in exchange for contractual commitments from the farmers that the mature trees will be sold to us. In 2002, we expanded the area of the Forestry Partners Program by 11,000 hectares. The program now encompasses over 35,000 hectares owned by 2,493 independent farmers in the States of Espirito Santo, Minas Gerais and Bahia. There was a substantial increase in the supply of wood to the Mill through this program in 2002, reaching 905,000 cubic meters of wood, approximately 38% more than in the previous year. We are obligated to purchase the mature trees from the farmers at certain agreed-upon prices not to exceed the market prices at the time of such purchases. We made our first purchases of trees under this program totaling approximately 83,000 cubic meters of wood during 1997. In response to certain restrictions contained in the permit to the Fiberline C Expansion Project, we expect to expand the farming program in the State of Espirito Santo, see "--Environmental and Other Regulatory Matters." To the extent such obligation creates any excess inventory of wood, we believe that we will be able to use any excess wood for diversification projects (such as solid wood products produced by APM). Alternatively, we may be able to sell such excess wood to third parties. See "--Business Strategy." We believe that under this arrangement we will be able to purchase from these farmers wood of quality and uniformity of fiber that is comparable to wood from our forests at a cost lower than that obtainable from traditional independent sources. In 2001, this program was subject to a legal proceeding seeking to suspend our activities within the Fiberline C licensing process. In 2002, however, we were granted an injunctive relief by a state court which denied the suspension. See "Item 8A. Consolidated Statements and Other Financial Information--Legal Proceedings." Regardless of the outcome of such legal proceeding, we believe that the wood supply from our forests alone will be sufficient to meet our pulp production needs based on current demands without further wood supply from this program.

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 4.5 solid cubic meters in 1985 to 3.8 solid cubic meters in 2001 and 3.68 solid cubic meters in 2002. The optimal time to harvest our trees is approximately seven years from the time of planting.

23

Energy

Reducing our need for outside sources of energy and chemicals is an important component of our low-cost production strategy. In 2001 and 2002, approximately 94% and 97% of our electrical energy needs were met by burning by-products generated from the pulp production process compared with 79% in 1999. The remainder of our energy needs were met through purchases of electricity, fuel oil and natural gas from third sources.

Chemicals

We use several chemicals in the pulp bleaching process. Until December 1999, we maintained and operated an electrochemical plant on the same site as the Mill 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, 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. We 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).

Under the terms of the purchase agreement, we have agreed to indemnify Nexen for certain liabilities relating to: (i) the manufacturing of electrochemical products prior to the sale, (ii) any legal proceedings that relate to the manufacture of the electrochemical products in which the basis of the claim occurred prior to the sale and (iii) any misrepresentation by us in connection with the purchase agreement. Our indemnity obligations expire, with respect to tax, labor, product liability and environmental matters, upon the passage of the relevant statute of limitations and, with respect to other matters, three years from the closing of the sale.

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. See Note 2 of the consolidated financial statements. 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.

To date, there has been one temporary shutdown of the plant during which we met our chlorine and caustic soda production requirements through purchases in the open market.

Water

Large amounts of water are 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. The reservoir 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). Wastewater undergoes a two-stage purification treatment process before it flows into the ocean.

Beginning in the latter half of 1998, the State of Espirito 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 to obtain water from the Rio Doce river through a system of canals and rivers which in turn feed into our reservoir. The project was completed in June 1999 and now provides water 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 Espirito 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. Despite the low average rainfall during 2000 and 2001, the use of water from the Rio Doce river enabled us to obtain all of our water supply requirements.

The Mill

Our pulp mill, located in the State of Espirito Santo, is the largest bleached hardwood kraft market pulp production facility in the world. Due to the successful implementation of the Modernization Project in 1999, the Mill now has a nominal production capacity of approximately 1,240,000 tons of pulp per year. In 1994, we increased our effective production capacity to 1,070,000 tons through system upgrades and productivity gains. From 1995 to 1999, we invested in the Modernization Project, increasing the nominal production capacity of the Mill to 1,240,000 tons of pulp per year. Our total production in 2002 was 1,656,000 tons (1,272,000 tons in 2001), representing approximately 8% of the total worldwide bleached hardwood kraft market pulp production capacity.

The production facility in the State of Espirito Santo consists of large receiving yards for the logs, debarking, chipping and digesting equipment, packaging and warehousing facilities capable of holding 40,000 tons of pulp and a fully computerized control system that continuously monitors the entire production process. Each of the Mill's pulp systems has five 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 site. A tree nursery capable of producing approximately 50.4 million seedlings per year and a research facility are located nearby as well. The 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. For a discussion of the sale of our electrochemical plant to Nexen, see "--Raw Materials--Chemicals."

In May 2002, the Fiberline C Expansion Project commenced operation adding a new pulp line and certain other modifications to the existing equipment at the Mill. See "--Fiberline C Expansion Project."

Pulp Production

When operating at full capacity, the Mill can process over 23,000 solid cubic meters of timber each day. We have implemented a new expansion project which has increased the Mill's nominal production capacity by 700,000 tons per year. See "--Fiberline C Expansion Project." The logs are either debarked in the forest or debarked at the Mill using tumbling drums and then cut into chips, which are transferred by conveyor 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 and to the port at Barra do Riacho, located approximately 1.8 kilometers from the Mill, for shipments abroad. See "--Transportation."

We have produced four types of pulp:

- Standard Pulp;
- ECF Pulp;
- TCF Pulp; and
- ACF Pulp.

Standard Pulp is pulp bleached with regular levels of chlorine. Standard Pulp is in high demand in North America and Asia. Although most of the production is represented by ECF Pulp and ACF Pulp, the production of Standard Pulp is still relevant because there is high demand for such pulp. During 2002, we produced approximately 203,848 tons of Standard Pulp, as compared to 284,678 tons in 2001 and 309,582 tons in 2000.

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 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 able to produce 100% ECF pulp. See "--The Mill." During 2002, approximately 83% of our production, or 1,372,172 tons, was comprised of ECF Pulp as compared to 926,356 tons during 2001 and 912,884 tons during 2000.

TCF Pulp, or Total Chlorine Free Pulp, is pulp bleached with no chlorine compounds. The demand for this kind of pulp has decreased since the bleaching process is more expensive than EFC Pulp and AFC Pulp. We produced TCF Pulp from 1991 to 1998. We no longer produce TCF Pulp.

ACF Pulp, or Aracruz Chlorine Free Pulp, was developed by us with lower levels of Organo Halogens (OX) than ECF pulp. ACF pulp is sold primarily in the European market. We have produced ACF since 1998. During 2002, approximately 5% of our production, or 80,028 tons, was comprise d of ACF Pulp as compared to 60,578 tons during 2001 and 78,796 tons during 2000.

Transportation

Wood from our three forest areas is transported by truck (owned by independent contractors) to the Mill site for processing into pulp. The distance from our main forest areas in Espirito Santo and the State of Bahia to the Mill site ranges from one to 340 kilometers with an average distance of 188 kilometers for wood currently in use.

Our pulp produced for export is transported from the Mill to the port of Barra do Riacho, which is located approximately 1.5 kilometers from the Mill site. This port is used almost exclusively to hold and load pulp and provides us with convenient access to ocean transport vessels. The port is a modern facility that currently has the capacity to handle approximately 2,000,000 tons of pulp per year. The port includes a warehouse capable of holding approximately 140,000 tons of pulp.

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.

Since the first expansion of the Mill, which was completed in 1991, the port has operated at its full capacity (2,000,000 tons per year). During 1995 and part of 1996, we and Cenibra expanded the existing quay and increased the storage capacity of the warehouse. This expansion project was completed in October 1996. In 2002, approximately 98% of our sales were shipped from the port, as compared to 97% in 2001. The remaining 2% of our sales were transported to the domestic market by truck.

Our integrated, coastal wood shipment project was completed in December 2002. It involves a system of sea-going barges and tugboats and two port terminals that link the extreme south of Bahia to the north of Espirito Santo. The port complex of Portocel, adjacent to the Mill, is to begin receiving wood from Veracel's plantations in southern Bahia via an alternative transportation system that is more efficient than truck-based highway shipments. Another improvement to our wood transportation operations was the construction and start-up of a nearly 4km-long rail spur used for unloading wood shipments directly at the Mill's yard.

We obtained all the necessary environmental and construction licenses for the wood loading and unloading terminals in Caravelas and Portocel, and we are in strict compliance with the implementation schedule for the sea-going wood transportation project. The Portocel barge terminal is ready, as are the barges and tugboat. The construction of the terminal in Caravelas and the dredging of the access channels are nearly completed. The first phase of the operation between Caravelas and Portocel, with an annual capacity for transporting 1.7 million cubic meters of wood, began at the end of 2002.

In 2002, we also carried out a review of our wood supply operations, based on a master plan for developing new ways to improve wood harvest and transportation operations.

Markets and Customers

Our principal markets are in North America, Europe, Asia and Brazil. The relative geographic distribution of our sales by volume and percentages of total production were as set forth below:

	1998		1999		2000		2001	
	Tons	% of Total	Tons	% of Total	Tons	% of Total	Tons	% of Tota
Europe..............	455.4	39%	561.0	44%	594.6	47%	475.3	37%
North America.......	390.1	34	406.4	32	433.5	34	479.8	37
Asia................	230.0	20	217.9	17	180.8	14	306.2	23
Latin America.......	9.5	1	20.6	2	9.0	1	3.6	-
Total Exports.......	1,085.0	94%	1,205.9	95%	1,217.9	96%	1,264.9	97%
Brazil..............	68.8	6%	59.4	5%	54.7	4%	36.4	3%
Total...........	1,153.8	100%	1,265.3	100%	1,272.6	100%	1,301.3	100%

The average net prices of eucalyptus pulp for 1998, 1999, 2000, 2001 and 2002 were US$435.78, US$463.20, US$611.34, US$438.10 and US$417.80, respectively.

In 2002, approximately 2% of our sales volume was sold in the domestic market (3% in 2001). In the past, Brazilian pulp prices have been subject from time to time to price restrictions imposed by the Brazilian government. There can be no assurance that the Brazilian government will not seek to impose such restrictions again.

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 2002, our ten largest customers accounted for approximately 71% of our sales and our largest customer accounted for approximately 22% of our sales (76% and 26%,

respectively, in 2001 and 73% and 34%, respectively, in 2000). In 2001 and 2002, 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 happen in the future. We believe that the loss of our largest customer could have a material adverse effect on our results of operations. Otherwise, we believe that the loss of any other customer would not have a material adverse effect on our results of operations since we will be able to replace such customer with other customers in a short time.

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.

The following table shows the breakdown by end uses of our pulp production in 1998, 1999, 2000, 2001 and 2002.

	Year Ended December 31,			
	1998	1999	2000	2001
Tissue....................................	46%	48%	51%	51%
Printing, and Writing Paper..............	27	27	28	28

Specialty Papers(1)......................	24	22	19	20
Cartonboard..............................	3	3	2	1
	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

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: