BRASKEM SA
Form 20-F
June 23, 2006
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# SECURITIES AND EXCHANGE COMMISSION

**Washington, D.C. 20549**

# FORM 20-F

¨ **REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR 12(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, 2005**

**OR**

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
¨ **SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
**Commission file number: 001-14862**

# BRASKEM S.A.

**(Exact Name of Registrant as Specified in its Charter)**

**N/A**

**(Translation of Registrant s name into English)**

**Federative Republic of Brazil**

**(Jurisdiction of Incorporation or Organization)**

**Av. das Nações Unidas, 4777**

**São Paulo, SP CEP 05477-000 Brazil**

**(Address of principal executive offices) (Zip code)**

**Securities registered pursuant to Section 12(b) of the Exchange Act:**

| Title of Each Class | Name of Each Exchange on which Registered |
| --- | --- |
| Preferred Shares, Class A, no par value per share, each represented by American Depositary Receipts | New York Stock Exchange |

**Securities 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**

The total number of issued shares of each class of stock of BRASKEM S.A. as of December 31, 2005 was: 120,860,099 Common Shares, no par value per share, 240,855,683 Preferred Shares, Class A, no par value per share, and 803,066 Preferred Shares, Class B, no par value per share.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes x No ¨

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. Yes ¨ No x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨

Indicate by check mark which financial statement item the registrant has elected to follow. Item 17 ¨ Item 18 x

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

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# INTRODUCTION

All references herein to the real, reais or R$ are to the Brazilian *real,* the official currency of Brazil. All references to U.S. dollars, dollars or US$ are to U.S. dollars.

All references herein (1) to we, us or our company are references to Braskem S.A. and its consolidated subsidiaries and (2) to Braskem are references solely to Braskem S.A.

On June 22, 2006, the exchange rate for *reais* into U.S. dollars was R$2.239 to US$1.00, based on the selling rate as reported by the Central Bank of Brazil (*Banco Central do Brasil*), or the Central Bank. The selling rate was R$2.341 to US$1.00 at December 31, 2005 and the commercial selling rate was R$2.654 to US$1.00 at December 31, 2004 and R$2.889 to US$1.00 at December 31, 2003, in each case, as reported by the Central Bank. The *real*/U.S. dollar exchange rate fluctuates widely, and the selling rate at June 22, 2006 may not be indicative of future exchange rates. See Item 3. Key Information Exchange Rates for information regarding exchange rates for the Brazilian currency since January 1, 2001.

Solely for the convenience of the reader, we have translated some amounts included in Summary Summary financial and other information, Capitalization, Selected financial and other information and elsewhere in this annual report from *reais* into U.S. dollars using the selling rate as reported by the Central Bank at December 31, 2005 of R$2.341 to US$1.00. These translations should not be considered representations that any such amounts have been, could have been or could be converted into U.S. dollars at that or at any other exchange rate. Such translations should not be construed as representations that the *real* amounts represent or have been or could be converted into U.S. dollars as of that or any other date.

**Financial Statements**

***Braskem Financial Statements***

We maintain our books and records in *reais.*

Our consolidated financial statements at December 31, 2005 and 2004 and for each of the years ended December 31, 2005, 2004 and 2003 have been audited, as stated in the report appearing herein, and are included in this annual report.

We prepare our consolidated financial statements in accordance with accounting practices adopted in Brazil, or Brazilian GAAP, which are based on:

Brazilian Law No. 6,404/76, as amended by Brazilian Law No. 9,457/97 and Brazilian Law No. 10,303/01, which we refer to collectively as the Brazilian Corporation Law;

the rules and regulations of the Brazilian Securities Commission (*Comissão de Valores Mobiliários*); and

the accounting standards issued by the Brazilian Institute of Independent Accountants (*Instituto dos Auditores Independentes do Brasil*).

Brazilian GAAP differs in certain respects from accounting principles generally accepted in the United States, or U.S. GAAP. For a discussion of certain differences relating to these financial statements, see note 31 to our audited consolidated financial statements included elsewhere in this annual report.

Consistent with Brazilian GAAP, our consolidated financial statements at December 31, 2005 and 2004 and for the years ended December 31, 2005, 2004 and 2003 have been prepared in accordance with Brazilian Securities Commission Instruction No. 247/96, as amended by Brazilian Securities Commission Instruction Nos.

269/97, 285/98 and 319/99, which we refer to collectively as Instruction 247. Instruction 247 requires our company to proportionally consolidate jointly controlled companies that are not our subsidiaries, but which we jointly control with one or more other shareholders.

Our consolidated financial statements reflect reclassifications in 2004 and 2003 of the following items to provide a better comparison among 2005, 2004 and 2003:

Prior to 2005, our management was considering strategic alternatives with respect to the capital stock that we own in Petroflex Indústria e Comércio S.A., or Petroflex, including the possible sale of this capital stock. In 2005, our management decided to maintain its investment in Petroflex. At December 31, 2005, we owned 20.1% of the total and voting share capital of Petroflex. As a result, we have proportionally consolidated Petroflex in our consolidated financial statements at and for the year ended December 31, 2005. In previous years, we recorded our investment in Petroflex as an investment in an associated company. In order to provide a better comparison among 2005, 2004 and 2003, we have proportionally consolidated Petroflex in our consolidated financial statements at December 31, 2004 and for the years ended December 31, 2004 and 2003.

Beginning on January 1, 2005, pursuant to Brazilian Securities Commission (*Comissão de Valores Mobiliários*, or CVM) Instruction 408, we are required to fully consolidate special purpose entities in our consolidated financial statements if specific criteria are met. These special purpose entities include, among others, Chemical Credit Rights Investment Fund (*Chemical Fundo de Investimento em Direitos Creditórios*) and Chemical Credit Rights Investment Fund II (*Chemical II Fundo de Investimento em Direitos Creditórios*). In order to provide a better comparison between 2005 and 2004, we have fully consolidated our special purpose entities in our consolidated financial statements at and for the year ended December 31, 2004. We have not made a similar reclassification for the year ended December 31, 2003 because our only transaction with a special purpose entity during 2003 was reflected in our consolidated balance sheet at December 31, 2003. See notes 2 and 4 to our consolidated financial statements.

Prior to 2005, we proportionally consolidated Companhia de Desenvolvimento Rio Verde, or Codeverde, in our consolidated financial statements. At December 31, 2005, we owned 35.5% of the total share capital and voting share capital of Codeverde. In 2005, the CVM granted our request for authorization to record our investment in Codeverde as an investment in an associated company pursuant to Instruction 247. In order to provide a better comparison between 2005 and 2004, we have recorded our investment in Codeverde as an investment in an associated company in our consolidated financial statements at and for the year ended December 31, 2004. We have not made a similar reclassification at and for the year ended December 31, 2003 because such a reclassification would not be material. See notes 2 and 4 to our consolidated financial statements.

Prior to December 31, 2004, judicial deposits were recorded as long-term receivables. Pursuant to CVM Deliberation No. 489, we now state contingent liabilities net of the corresponding judicial deposits. In our 2004 consolidated balance sheet, we have reclassified R$170.3 million as long-term taxes and contributions. See notes 2 and 17 to our consolidated financial statements.

For U.S. GAAP purposes the effects of proportional consolidation for those companies that are not jointly controlled by all voting shareholders were eliminated.

***Copesul Financial Statements***

We have included separate consolidated financial statements of Copesul Companhia Petroquímica do Sul, or Copesul, in this annual report because Copesul constitutes a significant jointly controlled company, accounting for 49.5% of our income from continuing operations before income taxes in 2005. Copesul maintains its books and records in *reais* and prepares its financial statements in accordance with Brazilian GAAP. Copesul s consolidated financial statements at December 31, 2005 and 2004 and for each of the years ended

December 31, 2005, 2004 and 2003 included in this annual report have been audited, as stated in the report appearing herein. Copesul s consolidated financial statements are proportionally consolidated into the Braskem s consolidated financial statements under Brazilian GAAP, as described above under Braskem Financial Statements.

**Share Splits**

On October 20, 2003, we authorized the split of all of our issued common shares, class A preferred shares and class B preferred shares into 20 shares for each issued share. This 20-for-one share split was effective on October 21, 2003. As a result of this share split, the ratio of our class A preferred shares to American Depository Shares, or ADSs, changed from 50 class A preferred shares per ADS to 1,000 class A preferred shares per ADS.

On March 31, 2005, we authorized the reverse split of all of our issued common shares, class A preferred shares and class B preferred shares into one share for each 250 issued shares. This reverse share split became effective on May 16, 2005. In connection with this reverse share split, we authorized a change in the ratio of our ADSs. Upon the effectiveness of our reverse share split and the ratio change, the ratio of our class A preferred shares to ADSs changed from 1,000 class A preferred shares per ADS to two class A preferred shares per ADS.

All references to numbers of shares and dividend amounts in this annual report have been adjusted to give effect to the 20-for-one share split and the one-for-250 reverse share split.

**Market Share and Other Information**

We make statements in this annual report about our market share in the petrochemical industry in Brazil and our production capacity relative to that of other petrochemical producers in Brazil and Latin America. We have made these statements on the basis of information obtained from third-party sources that we believe are reliable. We have calculated our Brazilian market shares with respect to specific products by dividing our domestic net sales volumes of these products by the total Brazilian domestic consumption of these products estimated by the Brazilian Association of Chemical Industry and Derivative Products (*Associação Brasileira de Indústrias Químicas e de Produtos Derivados*). We derive information regarding the production capacity of other companies in the Brazilian petrochemical industry and the estimated total Brazilian domestic consumption of petrochemical products principally from reports published by the Brazilian Association of Chemical Industry and Derivative Products. Although we have no reason to believe that any of this information is inaccurate in any material respect, neither we nor the initial purchasers have independently verified the production capacity, market share, market size or similar data provided by third parties or derived from industry or general publications.

**Production Capacity and Sales Volume**

As used in this annual report:

production capacity means the annual projected capacity for a particular facility, calculated based upon operations for 24 hours each day of a year and deducting scheduled downtime for regular maintenance; and

ton means a metric ton, which is equal to 1,000 kilograms or 2,204.62 pounds.

**Rounding**

We have made rounding adjustments to reach some of the figures included in this annual report. As a result, numerical figures shown as totals in some tables may not be arithmetic aggregations of the figures that precede them.

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## CAUTIONARY STATEMENT WITH RESPECT TO FORWARD-LOOKING STATEMENTS

This annual report contains forward-looking statements. Some of the matters discussed concerning our business operations and financial performance include forward-looking statements within the meaning of the Securities Act or the U.S. Securities Exchange Act of 1934, or the Exchange Act.

Statements that are predictive in nature, that depend upon or refer to future events or conditions or that include words such as expects, anticipates, intends, plans, believes, estimates and similar expressions are forward-looking statements. Although we believe that these forward-looking statements are based upon reasonable assumptions, these statements are subject to several risks and uncertainties and are made in light of information currently available to us.

Our forward-looking statements may be influenced by factors, including the following:

- general economic, political and business conditions in our company s markets, both in Brazil and abroad, including demand and prices for petrochemical products;
- interest rate, commodity price, inflation and exchange rate volatility;
- the cyclical nature of the Brazilian and global petrochemical industries;
- our ability to obtain financing on satisfactory terms;
- competition;
- actions taken by our major shareholders and other shareholders with convertible securities entitling them to acquire significant numbers of our shares;
- prices of naphtha and other raw materials;
- decisions rendered in pending major tax, labor and other legal proceedings; and
- other factors identified or discussed under Item 3. Key Information Risk Factors.

Our forward-looking statements are not guarantees of future performance, and our actual results or other developments may differ materially from the expectations expressed in the forward-looking statements. As for forward-looking statements that relate to future financial results and other projections, actual results will be different due to the inherent uncertainty of estimates, forecasts and projections. Because of these uncertainties, potential investors should not rely on these forward-looking statements.

We undertake no obligation to publicly update any forward-looking statement, whether as a result of new information, future events or otherwise.

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# PART I

## ITEM 1. IDENTITY OF DIRECTOR, SENIOR MANAGEMENT AND ADVISER

Not applicable.

## ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

## ITEM 3. KEY INFORMATION

### Selected Financial Information

The following selected financial data has been derived from our consolidated and combined financial statements.

The selected financial data at December 31, 2005 and 2004 and for the three years ended December 31, 2005 have been derived from our consolidated financial statements included in this annual report. The selected financial data at December 31, 2003, 2002 and 2001 and for the years ended December 31, 2002 and 2001 has been derived from our audited consolidated and combined financial statements that are not included in this annual report.

Our consolidated and combined financial statements are prepared in accordance with Brazilian GAAP, which differs in certain respects from U.S. GAAP. For a discussion of certain differences relating to these financial statements, see note 31 to our audited consolidated financial statements included in this annual report.

This financial information should be read in conjunction with Item 5. Operating and Financial Review and Prospects and our consolidated financial statements in this annual report.

| | At and for the year ended December 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2005(1) | 2005 | 2004 | 2003(2) | 2002(2)(3) | 2001(2)(3) |

| | (in millions of US$, except financial ratios) | (in millions of *reais*, except financial ratios) | | | | |
|---|---|---|---|---|---|---|
| **Statement of Operations Data** | | | | | | |
| ***Brazilian GAAP:*** | | | | | | |
| Net sales revenue | US$ 5,585.3 | R$ 13,075.1 | R$ 12,389.5 | R$ 10,300.2 | R$ 7,576.6 | R$ 4,459.5 |
| Cost of sales and services rendered | (4,426.2) | (10,361.7) | (9,223.0) | (8,224.6) | (6,175.5) | (3,637.6) |
| Gross profit | 1,159.1 | 2,713.4 | 3,166.5 | 2,075.6 | 1,401.1 | 821.9 |
| Selling, general and administrative expenses | (336.2) | (787.1) | (677.0) | (488.4) | (577.7) | (210.3) |
| Investment in associated companies, net(4) | (46.9) | (109.8) | (107.6) | (170.5) | (251.7) | (214.3) |
| Depreciation and amortization | (151.9) | (355.6) | (359.7) | (193.5) | (222.4) | (111.3) |
| Financial expenses | (288.7) | (675.8) | (1,307.2) | (720.8) | (3,481.5) | (801.2) |
| Financial income | (14.4) | (33.6) | 68.6 | 9.2 | 619.6 | 294.7 |
| Zero-rated IPI credit | | | | | 1,030.1 | |
| Other operating income, net | 9.7 | 22.8 | 43.0 | 55.5 | 102.6 | 103.3 |
| Operating income (loss) | 330.7 | 774.3 | 826.6 | 567.1 | (1,379.9) | (117.2) |
| Non-operating expenses, net | (10.8) | (25.2) | (29.8) | (4.5) | (98.0) | (120.8) |
| Income (loss) before income tax and social contribution (current and deferred) and minority interest | 319.9 | 749.1 | 796.8 | 562.6 | (1,477.9) | (238.0) |
| Income tax and social contribution (current and deferred) | (75.8) | (177.4) | (85.1) | (121.3) | (89.8) | (77.6) |
| Income (loss) before minority interest | 244.1 | 571.7 | 711.7 | 441.3 | (1,567.7) | (315.6) |
| Minority interest | 23.1 | 54.1 | (24.6) | (226.2) | 189.0 | (108.9) |
| Net income (loss) | US$ 267.2 | R$ 625.8 | R$ 687.1 | R$ 215.1 | R$ (1,378.7) | R$ (424.5) |

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| | At and for the year ended December 31, | | | | | |
|---|---|---|---|---|---|---|
| | **2005(1)** | **2005** | **2004** | **2003(2)** | **2002(2)(3)** | **2001(2)(3)** |
| | **(in millions of US$, except financial ratios)** | **(in millions of *reais*, except financial ratios)** | | | | |
| Number of shares outstanding at year end, excluding treasury shares (in thousands): | | | | | | |
| Common shares | | 120,860 | 120,860 | 102,432 | 98,087 | 51,735 |
| Class A preferred shares | | 240,860 | 240,373 | 170,379 | 168,491 | 86,371 |
| Class B preferred shares | | 803 | 842 | 916 | 916 | 916 |
| Net income (loss) per share at year end | 0.74 | 1.73 | 1.90 | 0.79 | (5.15) | (3.05) |
| Net income (loss) per ADS at year end | 1.48 | 3.46 | 3.80 | 1.57 | (10.31) | (6.11) |
| Dividends declared per share: | | | | | | |
| Common shares | 0.38 | 0.90 | 0.56 | | | 0.43 |
| Class A preferred shares | 0.38 | 0.90 | 0.56 | | 0.13 | 0.52 |
| Class B preferred shares | 0.24 | 0.56 | 0.56 | | 0.13 | 0.52 |
| Dividends declared per ADS | 0.77 | 1.80 | 1.12 | | | 1.04 |
| ***U.S. GAAP:*** | | | | | | |
| Net sales | US$ 5,129.3 | R$ 12,007.8 | R$ 11,644.1 | R$ 9,454.8 | R$ 7,071.8 | R$ 4,236.0 |
| Gross profit | 1,003.4 | 2,349.0 | 2,704.1 | 1,792.3 | 1,151.0 | 717.6 |
| Operating Income | 483.2 | 1,131.2 | 1,816.9 | 1,316.9 | 1,573.3 | 527.7 |
| Net income (loss) for the year | 314.9 | 737.1 | 887.8 | 378.1 | (1,144.0) | (471.0) |
| Basic earnings (loss) per share (weighted average): | | | | | | |
| Common shares | 0.87 | 2.04 | 2.77 | 1.41 | (11.93) | (6.68) |
| Class A preferred shares | 0.87 | 2.04 | 2.83 | 1.37 | | |
| Class B preferred shares | 0.27 | 0.63 | 0.56 | 0.44 | | |
| Basic earnings (loss) per ADS (weighted average) | 1.74 | 4.08 | 5.66 | 2.74 | | |
| Diluted earnings (loss) per share (weighted average): | | | | | | |
| Common shares | 0.83 | 1.94 | 2.54 | 1.41 | (11.93) | (6.68) |
| Class A preferred shares | 0.83 | 1.94 | 2.54 | 1.37 | | |
| Class B preferred shares | 0.27 | 0.63 | 0.56 | 0.44 | | |
| Diluted earnings (loss) per ADS (weighted average) | 1.66 | 3.88 | 5.08 | 2.40 | | |
| **Balance Sheet Data** | | | | | | |
| ***Brazilian GAAP:*** | | | | | | |
| Cash, cash equivalents and other investments | US$ 974.6 | R$ 2,281.5 | R$ 1,815.6 | R$ 1,221.2 | R$ 821.0 | R$ 513.2 |
| Short-term trade accounts receivable | 637.9 | 1,493.3 | 1,630.6 | 1,241.0 | 959.0 | 484.1 |
| Short-term inventories | 669.6 | 1,567.5 | 1,562.4 | 1,092.3 | 889.1 | 667.8 |
| Property, plant and equipment, net | 2,547.7 | 5,964.2 | 5,457.6 | 5,090.9 | 5,296.7 | 4,429.7 |
| Total assets | 6,659.9 | 15,590.8 | 15,050.4 | 14,005.6 | 13,898.2 | 9,555.3 |
| Short-term loans and financing (including current portion of long-term debt) | 382.3 | 895.0 | 1,785.9 | 2,764.1 | 2,746.1 | 1,966.4 |
| Short-term debentures | 4.0 | 9.3 | 5.0 | 353.4 | 32.1 | 26.2 |
| Short-term related party debt | 1.3 | 3.1 | | 5.5 | 8.2 | 88.7 |
| Long-term loans and financing | 1,220.6 | 2,857.5 | 3,059.6 | 3,628.0 | 3,891.6 | 3,101.7 |
| Long-term debentures | 683.2 | 1,599.3 | 1,167.9 | 1,143.0 | 1,190.2 | 473.6 |
| Long-term related party debt | 1.3 | 3.0 | 115.8 | 177.6 | 189.3 | 626.7 |
| Minority interest | 51.8 | 121.2 | 203.1 | 554.4 | 433.1 | 738.0 |
| Share capital | 1,453.7 | 3,403.0 | 3,403.0 | 1,887.4 | 1,845.4 | 1,201.6 |
| Shareholders equity | 1,937.5 | 4,535.8 | 4,183.7 | 2,112.6 | 1,821.8 | 1,729.0 |
| ***U.S. GAAP*** | | | | | | |
| Total assets | US$ 5,886.0 | R$ 13,779.2 | R$ 12,821.0 | R$ 11,058.2 | R$ 10,531.7 | R$ 7,803.0 |
| Shareholders equity | 1,308.7 | 3,063.6 | 2,588.9 | 7.8 | (415.2) | 291.4 |
| **Other Financial Information** | | | | | | |

| | | | | | | |
|---|---|---|---|---|---|---|
| ***Brazilian GAAP*:** | | | | | | |
| ***Cash Flow Data:*** | | | | | | |
| Net cash provided by (used in): | | | | | | |
| Operating activities | US$ 734.5 | R$ 1,719.4 | R$ 1,916.0 | R$ 596.9 | R$ 790.0 | R$ 1,453.9 |
| Investing activities | (447.7) | (1,048.0) | (1,014.4) | (469.4) | (646.7) | (862.2) |
| Financing activities | (140.8) | (329.7) | 166.0 | 379.1 | (237.2) | (404.9) |
| ***Other Information:*** | | | | | | |
| Capital expenditures: | | | | | | |
| Property, plant and equipment | US$ 333.5 | R$ 780.7 | R$ 442.2 | R$ 223.7 | R$ 419.9 | R$ 318.0 |
| Investments in other companies | 14.5 | 34.0 | 23.6 | 71.7 | 13.1 | 1,172.3 |

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| | At and for the Year Ended December 31, | | | | |
|---|---|---|---|---|---|
| | 2005 | 2004 | 2003 | 2002 | 2001 |
| **Operating Data**(5): | | | | | |
| Ethylene: | | | | | |
| Domestic sales volume (in thousands of tons) | 1,169.8 | 1,098.9 | 1,047.3 | 994.8 | 1,064.8 |
| Average domestic price per ton (in R$) | 2,204 | 2,095 | 1,655 | 1,292 | 1,135 |
| Propylene: | | | | | |
| Domestic sales volume (in thousands of tons) | 497.5 | 446.8 | 403.4 | 415.2 | 421.1 |
| Average domestic price per ton (in R$) | 2,132 | 1,833 | 1,477 | 1,106 | 829 |
| Polyethylene(6): | | | | | |
| Domestic sales volume (in thousands of tons) | 502.3 | 498.7 | 446.1 | 491.7 | 199.3 |
| Average domestic price per ton (in R$) | 3,072 | 2,987 | 2,567 | 2,007 | 2,114 |
| Polypropylene(6): | | | | | |
| Domestic sales volume (in thousands of tons) | 419.9 | 418.5 | 374.9 | 395.1 | 140.4 |
| Average domestic price per ton (in R$) | 3,344 | 3,155 | 2,689 | 1,931 | 1,969 |
| PolyvinylchlorideC(7): | | | | | |
| Domestic sales volume (in thousands of tons) | 378.9 | 394.4 | 342.4 | 350.1 | 125.9 |
| Average domestic price per ton (in R$) | 2,747 | 3,042 | 2,390 | 2,034 | 1,612 |
| Number of employees (at period end) | 3,262 | 2,996 | 2,868 | 2,817 | 1,424 |

(1) Translated for convenience only using the selling rate as reported by the Central Bank at December 31, 2005 for *reais* into U.S. dollars of R$2.341=US$1.00.
(2) Does not give effect to reclassification of Codeverde. See Introduction Financial Statements.
(3) Does not give effect to reclassification of Petroflex. See Introduction Financial Statements.
(4) Investment in associated companies, net comprises equity in the results, amortization of goodwill, net, foreign exchange variation and tax incentives and other.
(5) Including intra-company sales within Braskem. Intra-company sales of ethylene totaled approximately 588,700 tons in 2005, 537,100 tons in 2004 and 488,300 tons in 2003. Intra-company sales of propylene totaled approximately 89,300 tons in 2005, 31,300 tons in 2004 and 4,300 tons in 2003.
(6) Represents the sum of the sales volumes of Polialden Petroquímica S.A. and OPP Química S.A. for 2001.
(7) Represents the sales volume of Trikem S.A. for 2001.

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**Exchange Rates**

Prior to March 14, 2005, there were two principal foreign exchange markets in Brazil:

- the commercial rate exchange market; and

- the floating rate exchange market.

Most trade and financial foreign-exchange transactions were carried out on the commercial rate exchange market. The floating rate exchange market generally applied to transactions to which the commercial market rate did not apply.

On March 4, 2005, the National Monetary Council (Conselho Monetário Nacional) enacted Resolution No. 3,265, as well as additional regulations, that consolidated the two foreign exchange markets into a single foreign exchange market, effective as of March 14, 2005, in order to make foreign exchange transactions more straight-forward and efficient. Consequently, all foreign exchange transactions in Brazil are now carried out in this single foreign exchange market through authorized financial institutions. We cannot predict the impact of the enactment of any new regulations on the foreign exchange market.

Foreign exchange rates continue to be freely negotiated, but may be influenced from time to time 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. In January 1999, the Central Bank allowed the *real*/U.S. dollar exchange rate to float freely. Since then, the *real*/U.S. dollar exchange rate has been established mainly by the Brazilian interbank market and has fluctuated considerably. From December 31, 2000 through December 31, 2002, the *real* depreciated by 44.6% against the U.S. dollar. From December 31, 2002 through December 31, 2005, the *real* appreciated by 50.1% against the U.S. dollar. At June 22, 2006, the selling rate for U.S. dollars was R$2.239 per US$1.00. In the past, the Central Bank has intervened occasionally to control unstable movements in foreign exchange rates. We cannot predict whether the Central Bank or the Brazilian government will continue to allow the *real* to float freely or will intervene in the exchange rate market through a currency band system or otherwise, or that the exchange market will not be volatile as a result of political or economic instability or other factors. We also cannot predict whether the *real* will depreciate or appreciate in value in relation to the U.S. dollar in the future.

The following table shows the commercial selling rate or selling rate, as applicable, for U.S. dollars for the periods and dates indicated. The information in the Average column represents the average of the exchange rates on the last day of each month during the periods presented.

| | ***Reais* per U.S. dollar** | | | |
|---|---|---|---|---|
| **Year** | **High** | **Low** | **Average** | **Period end** |
| 2001 | R$ 2.801 | R$ 1.936 | R$ 2.353 | R$ 2.320 |
| 2002 | 3.995 | 2.271 | 2.998 | 3.533 |
| 2003 | 3.662 | 2.822 | 3.071 | 2.889 |
| 2004 | 3.205 | 2.654 | 2.909 | 2.654 |
| 2005 | 2.762 | 2.163 | 2.413 | 2.341 |

| | *Reais* per U.S. Dollar | |
|---|---|---|
| **Month** | **High** | **Low** |
| December 2005 | R$ 2.374 | R$ 2.180 |
| January 2006 | 2.346 | 2.211 |
| February 2006 | 2.222 | 2.118 |
| March 2006 | 2.224 | 2.107 |
| April 2006 | 2.154 | 2.089 |
| May 2006 | 2.371 | 2.059 |

*Source:* Central Bank

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**Risk Factors**

***Risks Relating to Brazil***

*Brazilian political and economic conditions, and the Brazilian government s economic and other policies, may negatively affect demand for our products as well as our net sales revenue and overall financial performance.*

The Brazilian economy has been characterized by frequent and occasionally extensive intervention by the Brazilian government and unstable economic cycles. The Brazilian government has often changed monetary, taxation, credit, tariff and other policies to influence the course of Brazil s economy. The Brazilian government s actions to control inflation and implement other policies have at times involved wage and price controls, blocking access to bank accounts, imposing capital controls and limiting imports into Brazil.

Our results of operations and financial condition may be adversely affected by factors such as:

- fluctuations in exchange rates;
- exchange control policies;
- interest rates;
- inflation;
- tax policies;
- expansion or contraction of the Brazilian economy, as measured by rates of growth in gross domestic product, or GDP;
- liquidity of domestic capital and lending markets; and
- other political, diplomatic, social and economic developments in or affecting Brazil.

A presidential election will be held in Brazil in October 2006. The President of Brazil has considerable power to determine governmental policies and actions that relate to the Brazilian economy and, consequently, affect the operations and financial performance of businesses, such as our company. The run-up to the presidential election may result in changes in existing governmental policies, and the post-election administration even if President Luiz Inácio Lula da Silva is reelected may seek to implement new policies. We cannot predict what policies will be adopted by the Brazilian government and whether these policies will negatively affect the economy or our business or financial performance.

*The Brazilian government s actions to combat inflation may contribute significantly to economic uncertainty in Brazil and reduce demand for our products.*

Historically, Brazil has experienced high rates of inflation. Inflation, as well as government efforts to combat inflation, had significant negative effects on the Brazilian economy, particularly prior to 1995. The inflation rate, as measured by the General Price Index Internal Availability (*Índice Geral de Preços Disponibilidade Interna*), reached 2,708% in 1993. Although inflation rates have been substantially lower since 1994 than in previous periods, inflationary pressures persist. Inflation rates were 10.4% in 2001, 26.4% in 2002, 7.7% in 2003, 12.1% in 2004 and 1.2% in 2005, as measured by the General Price Index Internal Availability. The Brazilian government s measures to control inflation have often included maintaining a tight monetary policy with high interest rates, thereby restricting availability of credit and reducing economic growth. Inflation, actions to combat inflation and public speculation about possible additional actions also contributed materially to economic uncertainty in Brazil and to heightened volatility in the Brazilian securities markets.

Brazil may experience high levels of inflation in future periods. Increasing prices for petroleum, the depreciation of the *real* and future governmental measures seeking to maintain the value of the *real* in relation to the U.S. dollar may trigger increases in inflation in Brazil. Periods of higher inflation may slow the rate of growth of the Brazilian economy, which would lead to reduced demand for our products in Brazil and decreased net sales revenue. Inflation also is likely to increase some of our costs and expenses, which we may not be able to pass on to our customers and, as a result, may reduce our profit margins and net income. In addition, high inflation generally leads to higher domestic interest rates, and, as a result, the costs of servicing our *real*-denominated debt may increase, causing our net income to be reduced. Inflation and its effect on domestic interest rates can, in addition, lead to reduced liquidity in the domestic capital and lending markets, which could adversely affect our ability to refinance our indebtedness in those markets. Any decline in our net sales revenue or net income and any deterioration in our financial condition would also likely lead to a decline in the market price of our class A preferred shares and the ADSs.

*Fluctuations in interest rates could raise the cost of servicing our debt and negatively affect our overall financial performance.*

Our financial expenses are affected by changes in the interest rates that apply to our floating rate debt. At December 31, 2005, we had, among other debt obligations, R$1,320.9 million of loans and financing and debentures that were subject to the TJLP (*Taxa de Juros de Longo Prazo*), a long-term interest rate, R$893.1 million of loans and financing and debentures that were subject to the CDI (*Certificado Depositário Interbancário*), an interbank rate, and R$638.4 million of loans and financing that were subject to LIBOR. The TJLP includes an inflation factor and is determined quarterly by the Central Bank. In particular, the TJLP and the CDI rate have fluctuated significantly in the past in response to the expansion or contraction of the Brazilian economy, inflation, Brazilian government policies and other factors. For example, in 2005 the CDI rate increased from 17.75% per annum at December 31, 2004 to 19.75% per annum at its peak in July 2005, followed by a decline to 18.00% at December 31, 2005. See Item 11. Quantitative and Qualitative Disclosures About Market Risk. A significant increase in any of these interest rates could adversely affect our financial expenses and negatively affect our overall financial performance.

*Fluctuations in the real/U.S. dollar exchange rate could increase inflation in Brazil, raise the cost of servicing our foreign currency-denominated debt and negatively affect our overall financial performance.*

The exchange rate between the *real* and the U.S. dollar and the relative rates of depreciation and appreciation of the *real* have affected our results of operations and may continue to do so.

The Brazilian currency has devalued often during the last four decades. Throughout this period, the Brazilian government has implemented various economic plans and various exchange rate policies, including sudden devaluations, periodic mini-devaluations (during which the frequency of adjustments has ranged from daily to monthly), exchange controls, dual exchange rate markets and a floating exchange rate system. From time to time, there have been significant fluctuations in the exchange rate between the Brazilian currency and the U.S. dollar and other currencies. For example, the *real* appreciated in value against the U.S. dollar by 22.3% in 2003, 8.9% in 2004 and 13.4% in 2005.

Devaluation of the *real* relative to the U.S. dollar also could result in additional inflationary pressures in Brazil by generally increasing the price of imported products and services and requiring recessionary government policies to curb demand. In addition, a devaluation of the *real* could weaken investor confidence in Brazil and reduce the market price of our class A preferred shares and the ADSs. On the other hand, further appreciation of the *real* against the U.S. dollar may lead to a deterioration of the country s current account and the balance of payments and may dampen export-driven growth.

We had total foreign currency-denominated debt obligations in an aggregate principal amount of R$2,746.6 million (US$1,173.3 million) at December 31, 2005, representing 51.2% of our indebtedness, excluding related party debt, on a consolidated basis. At December 31, 2005, we had US$548.5 million in U.S. dollar-denominated cash equivalents and other investments. At December 31, 2005, we did not have any foreign currency derivative instruments. A significant devaluation of the *real* in relation to the U.S. dollar or other currencies could reduce our ability to meet debt service requirements of our foreign currency-denominated obligations, particularly as our net sales revenue is primarily denominated in *reais*.

In addition, any significant devaluation of the *real* will increase our financial expenses as a result of foreign exchange losses that we must record. For example, the 34.3% devaluation of the *real* in 2002 substantially increased our financial expenses and was a significant factor in our net loss for that year.

The prices of naphtha, our most important raw material, and of some of our other raw materials are denominated in or linked to the U.S. dollar. In 2005, 71.7% of our direct and indirect consolidated cost of sales and services rendered represented the cost of naphtha. When the *real* depreciates against the U.S. dollar, the cost in *reais* of our U.S. dollar-linked raw materials increases, and our operating income in *reais* decreases to the extent that we are unable to pass on these cost increases to our customers.

*Brazilian government exchange control policies could increase the cost of servicing our foreign currency-denominated debt and impair our liquidity.*

The purchase and sale of foreign currency in Brazil is subject to governmental control. In 1990, the Central Bank centralized certain payments of principal on external obligations. Many factors could cause the Brazilian government to institute more restrictive exchange control policies, including the extent of Brazil s foreign currency reserves, the availability of sufficient foreign exchange on the date a payment is due, the size of Brazil s debt service burden relative to the economy as a whole, Brazil s policy towards the International Monetary Fund and political constraints to which Brazil may be subject. A more restrictive policy could increase the cost of servicing (and thereby reduce our ability to pay) our foreign currency-denominated debt obligations and other liabilities. Our foreign-currency denominated debt represented 51.2% of our indebtedness on a consolidated basis at December 31, 2005. If we fail to make payments under any of these obligations, we will be in default under those obligations, which could reduce our liquidity as well as the market price of our class A preferred shares and the ADSs.

*Changes in tax laws may result in increases in certain direct and indirect taxes, which could reduce our gross margin and negatively affect our overall financial performance.*

The Brazilian government implements from time to time changes to tax regimes that may increase our and our customers tax burdens. These changes include modifications in the rate of assessments and, on occasion, enactment of temporary taxes, the proceeds of which are earmarked for designated governmental purposes. In April 2003, the Brazilian government presented a tax reform proposal, which was mainly designed to simplify tax assessments, to avoid internal disputes within and between the Brazilian states, and to redistribute tax revenues. Certain elements of this proposal were adopted, while other elements have been stalled and are unlikely to be enacted. We cannot predict the changes to Brazilian tax law that may be proposed and enacted in the future. However, future changes in Brazilian tax law may result in increases in our overall tax burden, which could reduce our gross margin and negatively affect our overall financial performance.

***Risks Relating to Our Company and the Petrochemical Industry***

*The cyclical nature of the petrochemical industry may reduce our net sales revenue and gross margin.*

The Brazilian petrochemical industry, including the markets in which we compete, is cyclical and sensitive to changes in supply and demand that are, in turn, affected by political and economic conditions in Brazil and elsewhere. This cyclicality may reduce our net sales revenue and gross margin. In particular:

- downturns in general business and economic activity may cause demand for our products to decline;
- when demand falls, we may face competitive pressures to lower our prices; and
- if we decide to expand our plants or construct new plants, we may do so based on an estimate of future demand that never materializes or materializes at levels lower than we predicted.

The global petrochemical industry is also cyclical. Historically, the international petrochemical markets have experienced alternating periods of limited supply, which have caused prices and profit margins to increase,

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followed by expansion of production capacity, which has resulted in oversupply and reduced prices and profit margins. The Brazilian petrochemical industry has become increasingly integrated with the global petrochemical industry for a number of reasons, including increased demand for, and consumption of, petrochemical products in Brazil and the ongoing integration of regional and world markets for commodities. We establish the prices for the products we sell in Brazil with reference to international market prices. Our net sales revenue and gross margin are increasingly linked to global industry conditions that we cannot control.

*We face competition from producers of polyolefins, vinyls and other petrochemical products.*

We face competition in Brazil from Brazilian and international producers of polyethylene, polypropylene, vinyls and other petrochemical products. In addition, we generally set the prices for our second generation products with reference to the prices charged for these products by foreign producers in international markets. We anticipate that we may experience increasingly intense competition from other producers of polyolefins and vinyls products, both in Brazil and in selected foreign markets in which we sell these products. Many of our foreign competitors are substantially larger and have substantially greater financial, manufacturing, technological and marketing resources than our company.

We face significant competition in the polyethylene market. Rio Polímeros S.A., or Rio Polímeros, a Brazilian petrochemical company, commenced operations of a major petrochemical plant in Brazil in 2005. The maximum annual capacity of this plant is 520,000 tons of ethylene, 75,000 tons of propylene and 540,000 tons of polyethylene. This plant is in the process of ramping up its production towards its annual capacity. In addition, Solvay Indupa do Brasil S.A., or Solvay, expanded its annual polyvinylchloride, or PVC, production capacity in Brazil by 35,000 tons in December 2005. Actions by our competitors, including any future increases in their capacity, may make it increasingly difficult for us to maintain our domestic market share in our thermoplastic products (i.e., polyethylene, polypropylene and PVC).

*Higher naphtha costs would increase our cost of sales and services rendered and may reduce our gross margin and negatively affect our overall financial performance.*

Naphtha, a crude oil derivative, is the principal raw material of our Basic Petrochemicals Unit and, indirectly, of our other business units. In 2005, naphtha accounted, directly and indirectly, for approximately 70% of our consolidated cost of sales and services rendered. The price of naphtha supplied by Petróleo Brasileiro S.A. Petrobras, or Petrobras, is linked to the Amsterdam-Rotterdam-Antwerp market price of naphtha and to the *real*/U.S. dollar exchange rate. The price of naphtha that we purchase from other international suppliers is also linked to the Amsterdam-Rotterdam-Antwerp market price. The Amsterdam-Rotterdam-Antwerp market price of naphtha fluctuates primarily based on changes in the U.S. dollar-based price of crude oil in the international markets.

During 2005, the price of naphtha in U.S. dollars increased by 28.8%, from US$387.05 per ton in December 2004 to US$498.35 per ton in December 2005. The U.S. dollar price of naphtha was volatile during 2005, increasing substantially through March, declining in April and May, increasing through September, declining through November and increasing again in December. The U.S. dollar price of naphtha remained volatile in the first five months of 2006, increasing sharply in January and April 2006, increasing moderately in May 2006 and decreasing moderately in February 2006. The price of naphtha may continue its upward trend or the *real* may devalue significantly in the future. Any increase in naphtha costs would reduce our gross margin and negatively affect our overall financial performance to the extent that we are unable to pass on these increased costs to our customers and could result in reduced sales volumes of our products.

*We do not hedge against changes in naphtha prices, so that we are exposed to fluctuations in the price of our primary raw material.*

We currently do not hedge our exposure to fluctuations in naphtha prices, which are linked to the *real*/U.S. dollar exchange rate. Although we attempt to pass on increases in naphtha prices through higher prices for our

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products, in periods of high volatility in the U.S. dollar price of naphtha or the *real*/U.S. dollar exchange rate, there is usually a lag between the time that the U.S. dollar price of naphtha increases or the U.S. dollar appreciates and the time that we may effectively pass on those increased costs in *reais* to our customers in Brazil. As a result, if the U.S. dollar price of naphtha increases precipitously or the *real* depreciates precipitously against the U.S. dollar in the future, we may not immediately be able to pass on all of the corresponding increases in our naphtha costs to our customers in Brazil, which would likely reduce our gross margin and net income.

*We depend on Petrobras to supply us with the substantial portion of our naphtha requirements.*

Petrobras currently is the only Brazilian supplier of naphtha and supplied 69.2% of the naphtha consumed by our company in 2005. Petrobras produces most of the naphtha it sells to us and imports the balance. Our production volume and net sales revenue would likely decrease and our overall financial performance would likely be negatively affected in the event of:

- significant damage to Petrobras refineries or to the port facilities through which Petrobras imports naphtha, or to any of the pipelines connecting our plants to Petrobras facilities, whether as a consequence of an accident, natural disaster, fire or otherwise; or
- any termination by Petrobras of the naphtha supply contract with our company, which provides that Petrobras may terminate the contract for a number of reasons, including as a result of a national emergency affecting the supply of petroleum derivatives in Brazil.

In addition, although regulatory changes have ended Petrobras monopoly in the Brazilian naphtha market and have allowed us to import naphtha, any reversal in the continuing deregulation of the oil and gas industry in Brazil could increase our production costs.

*Our Polyolefins and Vinyls Units depend on our Basic Petrochemicals Unit and Copesul to supply them with their ethylene and propylene requirements.*

Our Basic Petrochemicals Unit is the only supplier of ethylene to our Vinyls Unit, and our Basic Petrochemicals Unit and Copesul are the only suppliers of ethylene and propylene to our Polyolefins Unit. Because the cost of storing ethylene and propylene is substantial and there is inadequate infrastructure in Brazil to permit the importation of large quantities of these products, our production volumes of, and net sales revenue from, vinyls and polyolefins products would decrease, and our overall financial performance would be negatively affected, in the event of:

- significant damage to our Basic Petrochemicals Unit s or to Copesul s facilities through which ethylene or propylene is produced, or to the pipeline or other facilities that connect these units to our Basic Petrochemicals Unit or Copesul, whether as a consequence of an accident, natural disaster, fire or otherwise;
- any termination by Copesul of the ethylene and propylene supply contracts with our company; or
- any significant reduction in the supply of naphtha to our Basic Petrochemicals Unit or to Copesul, as naphtha is the principal raw material used in the production of ethylene and propylene.

In addition, any significant expansion of the production capacity of our Polyolefins Unit in the petrochemical complex located in Triunfo in the State of Rio Grande do sul, which we refer to as the Southern Complex, will depend on our ability to obtain additional ethylene and propylene from Copesul.

*Any downgrade in the ratings of our company or our debt securities would likely result in increased interest and other financial expenses related to our borrowings and debt securities and could reduce our liquidity.*

Standard & Poor s Ratings Services, a division of The McGraw-Hill Companies, Inc., or Standard and Poor s, and Fitch, Inc., or Fitch, maintain ratings of our company and our debt securities. Currently, Standard and

Poor s and Fitch maintain ratings of our company on a local and a global basis. Standard and Poor s maintains a rating of our company on a local basis of br AA/Stable Outlook and Fitch maintains a national rating for our company of AA- (bra)/Stable Outlook. On a global basis, Standard and Poor s maintains a local currency rating for our company of BB and a foreign currency rating for our company of BB, while Fitch maintains a local currency rating for our company of BB+/Stable Outlook and a foreign currency rating for our company of BB/Positive Outlook. Any decision by these or other rating agencies to downgrade the ratings of our company or of our debt securities in the future would likely result in increased interest and other financial expenses relating to our borrowings and debt securities and could significantly reduce our ability to obtain such financing on satisfactory terms or in amounts required by us and our liquidity.

*Some of our shareholders may have the ability to determine the outcome of corporate actions or decisions, which could affect the holders of our class A preferred shares and the ADSs.*

As of June 22, 2006, a group of companies controlled by the Odebrecht family, or the Odebrecht Group, through Odebrecht S.A., or Odebrecht, its wholly-owned subsidiary, ODBPAR Investimentos S.A., or ODBPAR Investments, their subsidiary, Nordeste Química S.A. Norquisa, or Norquisa, and our subsidiary, Braskem Participações S.A., own 74.6% of our voting share capital. The Odebrecht Group s designees currently constitute a majority of the members of our board of directors. Petrobras Química S.A., or Petroquisa, a subsidiary of Petrobras, has veto and other rights under a shareholders agreement as described under Item 7. Major Shareholders and Related Party Transactions Major Shareholders Shareholders Agreements. As a result, the Odebrecht Group and Petroquisa may have the ability to determine the outcome of major corporate actions or decisions requiring the approval of our shareholders or our board of directors, which could affect the holders of our class A preferred shares and the ADSs.

*We may face conflicts of interest in transactions with related parties.*

We maintain trade accounts receivable and current and long-term payables with some of our affiliates and other related parties, including Petrobras (which is our sole domestic supplier of naphtha), and Copesul in the Southern Complex (which supplies us with ethylene and propylene). As of June 22, 2006, Petrobras, through Petroquisa, is the indirect holder of 9.8% of our voting share capital and 8.3% of our total share capital. These accounts receivable and accounts payable balances result mainly from purchases and sales of goods, which are at prices and on terms equivalent to the average terms and prices of transactions that we enter into with third parties. We also engage in financial and other transactions with some of our shareholders. These and other commercial and financial transactions between us and our affiliates could result in conflicting interests.

*We may make significant acquisitions which, if not successfully integrated with our company, may adversely affect our operating results.*

We may make significant acquisitions in the future to continue our growth. Acquisitions involve risks, including the following:

- failure of acquired businesses to achieve expected results;
- possible inability to retain or hire key personnel of acquired businesses;
- possible inability to achieve expected synergies and/or economies of scale;

- unanticipated liabilities; and
- antitrust considerations.

If we are unable to integrate or manage acquired businesses successfully, we may not realize anticipated cost savings, revenue growth and levels of integration, which may result in reduced profitability or operating losses.

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*Future adjustments in tariffs on imports that compete with our products could cause us to lower our prices.*

We take into account, when setting the domestic prices for our products, tariff rates imposed by the Brazilian government on imports of similar products and the products of our customers. We currently benefit from tariffs that allow us to charge domestic prices for our polyolefins and vinyls products that include a factor based on the tariffs levied on comparable imports of those products. However, the Brazilian government has in the past used import and export tariffs to effect economic policies, with the consequence that tariffs can vary considerably, especially tariffs on petrochemical products. For example, in 2004 the Brazilian government lowered the tariffs applicable to most of the thermoplastic products that we produce by 1.5%. Future adjustments of tariffs could cause us to lower our domestic prices, which would likely result in lower net sales revenue and could negatively affect our overall financial performance.

*Our business is subject to stringent environmental regulations, and imposition of new regulations could require significant capital expenditures and increase our operating costs.*

Our company, like other Brazilian petrochemical producers, is subject to stringent Brazilian federal, state and local environmental laws and regulations concerning human health, the handling and disposal of solid and hazardous wastes and discharges of pollutants into the air and water. Petrochemical producers are sometimes subject to unfavorable market perceptions as a result of the environmental impact of their business, which can have an adverse effect on their results of operations. As environmental laws become more stringent in Brazil and worldwide, the amount and timing of future expenditures required for us to remain compliant could increase substantially and could decrease the availability of funds for other capital expenditures and other purposes.

*We manufacture products that are subject to the risk of fire, explosions and other hazards.*

Our operations are subject to hazards, such as fires, explosions and other accidents, associated with the manufacture of petrochemicals and the storage and transportation of feedstocks and petrochemical products. These hazards can cause personal injury and loss of life, severe damage to or destruction of property and equipment and environmental damage. A sufficiently large accident at one of our plants or storage facilities could force us to suspend our operations temporarily and result in significant remediation costs and lost net sales revenue. Although we maintain insurance coverage for losses due to fire damage and for losses of income resulting from shutdowns due to fire, explosion or electrical damage, those insurance proceeds may not be available on a timely basis and may be insufficient to cover all losses.

*Unfavorable outcomes in pending litigation may reduce our liquidity and negatively affect our financial performance and financial condition.*

We are involved in numerous tax, civil and labor disputes involving significant monetary claims. If unfavorable decisions are rendered in one or more of these lawsuits, we could be required to pay substantial amounts, which could materially adversely affect our financial condition and results of operations. For some of these lawsuits, we have not established any provision on our balance sheet or have established provisions only for part of the amounts in question, based on our judgments or opinions of our legal counsel as to the likelihood of winning these lawsuits.

The lawsuits for which we have not established provisions or have established only partial provisions include the following:

*Social contribution on net income*. We and some of our subsidiaries have challenged the constitutionality of the Brazilian federal Social Contribution on Net Income (*Contribuição Social Sobre o Lucro Líquido*). A Brazilian Federal Supreme Court (*Supremo Tribunal Federal*) decision in our favor was overruled in a subsequent rescission action filed by the Brazilian tax authorities, and our appeal of that suit is pending. We believe that it is reasonably possible that we will lose our appeal. If we lose our appeal, we believe that we would be required to pay Social Contribution on Net Income only from the date that a final decision is published. However, as Brazilian law allows rescission actions to relate back to, and to take effect from, the date of the initial decision, we believe that it is reasonably possible that we will be required to pay this tax from the date of the original decision, in which case our total estimated exposure at December 31, 2005, including interest, would be R$651.7 million. This amount does not include approximately R$175.0 million in penalties at December 31, 2005 that we believe we would not be required to pay because we relied upon a judicial decision in not paying the Social Contribution on Net Income. We believe that there is a possibility that we will be required to pay related interest and a remote possibility that we will be required to pay fines as a result of this tax litigation. We have not established a provision for these lawsuits.

*Cost of living adjustments on workers wages*. The unions that represent employers and workers at the facilities located in the petrochemical complex located in Camaçari in the State of Bahia, which we refer to as the Northeastern Complex, are involved in a lawsuit over the indices we and other companies have used for cost of living adjustments on workers wages since early 1990. For a description of the legal bases of this suit, see Item 8. Financial Information Legal Proceedings Labor Proceedings. The Brazilian Federal Supreme Court has held in favor of the employers union, but has accepted a divergence appeal requesting the resolution of conflict between the decisions given by the Brazilian Federal Supreme Court under this proceeding and prior decisions given by another panel of the Brazilian Federal Supreme Court. Accordingly, the decision of the Brazilian Federal Supreme Court in our favor is not yet final and does not address damages. We believe it is reasonably possible that the employers union will lose the divergence appeal, which could adversely affect us. While we believe that it is possible, although unlikely, that an adverse judgment against the employers union could impact wages that we paid from April 1990 to the present, we believe that any judgment would most likely impact wages that we paid from April 1990 to September 1990 (the effective date of the next collective bargaining agreement). As we believe that it is not probable that the employers union will lose this suit, we have not recorded a provision in respect of this suit. If the employers union loses this suit and we are required to pay damages from April 1990 to September 1990, we estimate that we could be subject to liability of up to R$35.0 million, although additional claims would have to be brought by the workers union or individual employees to quantify the amount of damages that we would be required to pay.

In addition, we and some of our subsidiaries believe that our chances of success are remote in a series of lawsuits in which we challenged the constitutionality of an increase in the federal Contribution for Social Security Financing (*Contribuição para Financiamento da Seguridade Social COFINS*), or COFINS, tax rate. For a description of the legal bases of these suits, see Item 8. Financial Information Legal Proceedings Tax Proceedings. We had established total provisions of R$316.1 million at December 31, 2005 for all of our lawsuits relating to the Social Integration Program (*Programa de Integração Social*), or PIS, and COFINS, including separate lawsuits challenging the basis of calculation of PIS and COFINS. Because we have deposited only R$39.1 million of this amount with the courts, we would be required, in the event we and our subsidiaries receive final, unfavorable decisions, to pay the remaining amounts for which we have not made deposits.

We are also parties to a number of lawsuits seeking tax credits that we believe the Brazilian tax authorities have disallowed or limited in violation of the Brazilian Constitution and/or applicable law. In some cases in which we have received favorable lower court decisions, we have used these credits to offset other tax obligations and have established provisions in an equivalent amount until a final decision is rendered (adjusting these provisions based on the *Sistema Especial de Liquidação e de Custódia*, or SELIC, interest rate). These provisions totaled R$1,332.6 million at December 31, 2005. If we ultimately lose any of these lawsuits, we would be required to pay the tax obligations we had previously offset with those credits, which could materially reduce our liquidity. We believe that losses related to some of these lawsuits are reasonably possible.

For more information about our legal proceedings, see Item 8. Financial Information Legal Proceedings.

***Risks Relating to Our Class A Preferred Shares and the ADSs***

*Our class A preferred shares and the ADSs have limited voting rights.*

Under the Brazilian Corporation Law and our by-laws, holders of our class A preferred shares and, consequently, the ADSs are not entitled to vote at meetings of our shareholders, except in very limited circumstances. These limited circumstances directly relate to key rights of the holders of class A preferred shares, such as modifying basic terms of our class A preferred shares or creating a new class of preferred shares with superior rights. Holders of preferred shares without voting rights are entitled to elect one member and his or her respective alternate to our board of directors and our fiscal council. Holders of our class A preferred shares and the ADSs are not entitled to vote to approve corporate transactions, including mergers or consolidations of our company with other companies.

*Holders of the ADSs may find it difficult to exercise even their limited voting rights at our shareholders meetings.*

Holders may exercise the limited voting rights with respect to our class A preferred shares represented by the ADSs only in accordance with the deposit agreement relating to the ADSs. There are practical limitations upon the ability of ADS holders to exercise their voting rights due to the additional steps involved in communicating with ADS holders. For example, we are required to publish a notice of our shareholders meetings in certain newspapers in Brazil. To the extent that holders of our class A preferred shares are entitled to vote at a shareholders meeting, they will be able to exercise their voting rights by attending the meeting in person or voting by proxy. By contrast, holders of the ADSs will receive notice of a shareholders meeting by mail from the depositary following our notice to the ADR depository requesting the ADR depository to do so. To exercise their voting rights, ADS holders must instruct the depositary on a timely basis. This noticed voting process will take longer for ADS holders than for holders of class A preferred shares. If it fails to receive timely voting instructions for all or part of the ADSs, the depositary will assume that the holders of those ADSs are instructing it to give a discretionary proxy to a person designated by us to vote their ADSs, except in limited circumstances.

In the limited circumstances in which holders of the ADSs have voting rights, they may not receive the voting materials in time to instruct the depositary to vote our class A preferred shares underlying their ADSs. In addition, the depositary and its agents are not responsible for failing to carry out voting instructions of the holders of the ADSs or for the manner of carrying out those voting instructions. Accordingly, holders of the ADSs may not be able to exercise voting rights, and they will have no recourse if the class A preferred shares underlying their ADSs are not voted as requested.

*Exchange controls and restrictions on remittances abroad may adversely affect holders of the ADSs and the underlying class A preferred shares.*

The Brazilian government may impose temporary restrictions on the conversion of Brazilian currency into foreign currencies and on the remittance to foreign investors of proceeds of their investments in Brazil. Brazilian law permits the government to impose these restrictions whenever there is a serious imbalance in Brazil s balance of payments or there are reasons to foresee a serious imbalance. The Brazilian government imposed remittance restrictions for approximately six months in 1990.

These restrictions could hinder or prevent the Brazilian custodian of the class A preferred shares underlying the ADSs or holders who have exchanged the ADSs for the underlying class A preferred shares from converting dividends, distributions or the proceeds from any sale of such shares into U.S. dollars and remitting such U.S. dollars abroad. In such an event, the Brazilian custodian for our class A preferred shares will hold the *reais* that it cannot convert for the account of holders of the ADSs who have not been paid. Neither the custodian nor the depositary will be required to invest the *reais* or be liable for any interest.

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*Holders of the ADSs may face difficulties in protecting their interests because we are subject to different corporate rules and regulations as a Brazilian company and our shareholders may have fewer and less well-defined rights.*

Holders of the ADSs are not direct shareholders of our company and are unable to enforce the rights of shareholders under our by-laws and the Brazilian Corporation Law.

Our corporate affairs are governed by our by-laws and the Brazilian Corporation Law, which differ from the legal principles that would apply if we were incorporated in a jurisdiction in the United States, such as the State of Delaware or New York, or elsewhere outside Brazil. Even if a holder of ADSs surrenders its ADSs and becomes a direct shareholder, its rights as a holder of our class A preferred shares underlying the ADSs under the Brazilian Corporation Law to protect its interests relative to actions by our board of directors may be fewer and less well-defined than under the laws of those other jurisdictions.

Although insider trading and price manipulation are crimes under Brazilian law, the Brazilian securities markets are not as highly regulated and supervised as the U.S. securities markets or the markets in some other jurisdictions. In addition, rules and policies against self-dealing or for preserving shareholder interests may be less well-defined and enforced in Brazil than in the United States and certain other countries, which may put holders of our class A preferred shares and the ADSs at a potential disadvantage. Corporate disclosures also may be less complete or informative than for a public company in the United States or in certain other countries.

*Holders of the ADSs may face difficulties in serving process on or enforcing judgments against us and other persons.*

We are a corporation (sociedade anônima) organized under the laws of Brazil, and all of our directors and executive officers and our independent public accountants reside or are based in Brazil. Most of our assets and those of these other persons are located in Brazil. As a result, it may not be possible for holders of the ADSs to effect service of process upon us or these other persons within the United States or other jurisdictions outside Brazil or to enforce against us or these other persons judgments obtained in the United States or other jurisdictions outside Brazil. Because judgments of U.S. courts for civil liabilities based upon the U.S. federal securities laws may only be enforced in Brazil if certain conditions are met, holders may face greater difficulties in protecting their interests in the case of actions by us or our directors or executive officers than would shareholders of a U.S. corporation.

*Actual or anticipated sales of a substantial number of class A preferred shares could decrease the market prices of our class A preferred shares and the ADSs.*

Sales of a substantial number of our class A preferred shares could negatively affect the market prices of our class A preferred shares and the ADSs. If, in the future, substantial sales of shares are made by the Odebrecht Group, Petroquisa or other existing or future holders of class A preferred shares, the market price of our class A preferred shares and, by extension, the ADSs may decrease significantly. As a result, holders of the ADSs may not be able to sell the ADSs at or above the price they paid for them.

*Holders of the ADSs may be unable to exercise preemptive rights with respect to our class A preferred shares underlying the ADSs.*

Holders of the ADSs will be unable to exercise the preemptive rights relating to our class A preferred shares underlying 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 or to take any other action to make preemptive rights available to holders of the ADSs, and we may not file any such registration statement. If we do not file a registration statement or if we and the depositary decide not to make preemptive rights available to holders of the ADSs, those holders may receive only the net proceeds from the sale of their preemptive rights by the depositary, or if they are not sold, their preemptive rights will be allowed to lapse.

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*Holders of the ADSs could be subject to Brazilian income tax on capital gains from sales of ADSs.*

Historically, any capital gain realized on a sale or other disposition of ADSs between non-Brazilian holders outside Brazil was not subject to Brazilian income tax. However, Brazilian law provides that, commencing on February 1, 2004, the acquiror, individual or legal entity resident or domiciled in Brazil, or the acquiror s attorney-in-fact, when such acquirer is resident or domiciled abroad, shall be responsible for the retention and payment of the income tax applicable to capital gains earned by the individual or legal entity resident or domiciled abroad who disposes of property located in Brazil. The Brazilian tax authorities have recently issued a normative instruction confirming that they intend to assess income tax on capital gains earned by non-Brazilian residents whose assets are located in Brazil. In our view, ADSs representing class A preferred shares, which are issued by the depositary outside Brazil, will not be deemed to be property located in Brazil for purposes of this law. However, we cannot assure holders of our ADSs whether Brazilian tax authorities will attempt to tax any capital gains arising from the sale or other disposition of ADSs, even when the transaction is consummated outside Brazil between non-Brazilian residents.

*The relative volatility and liquidity of the Brazilian securities markets may decrease the liquidity and market price of our class A preferred shares and the ADSs.*

The Brazilian securities markets are substantially smaller, less liquid and more volatile than major securities markets in the United States. The São Paulo Stock Exchange (*Bolsa de Valores de São Paulo*), which is the principal Brazilian stock exchange, had a market capitalization of US$482.1 billion (or R$1,128.5 billion) at December 31, 2005 and an average daily trading volume of US$666.6 million for 2005. In comparison, the New York Stock Exchange had a market capitalization of US$21.2 trillion at December 31, 2005 and an average daily trading volume of US$56.1 billion for 2005. There is also significantly greater concentration in the Brazilian securities markets. The ten largest companies in terms of market capitalization represented approximately 52% of the aggregate market capitalization of the São Paulo Stock Exchange at December 31, 2005. The ten most widely traded stocks in terms of trading volume accounted for approximately 51% of all shares traded on The São Paulo Stock Exchange in 2005. These market characteristics may substantially limit the ability of holders of the ADSs to sell class A preferred shares underlying ADSs at a price and at a time when they wish to do so and, as a result, could negatively impact the market price of the ADSs themselves.

*Developments in other emerging markets may decrease the market price of our class A preferred shares and the ADSs.*

The market price of the ADSs may decrease due to declines in the international financial markets and world economic conditions. Although economic conditions are different in each country, investors reaction to developments in one country can affect the securities markets and the securities of issuers in other countries, including Brazil. Brazilian securities markets are, to varying degrees, influenced by economic and market conditions in other emerging market countries, especially those in Latin America. Any return to economic turmoil in Argentina or adverse economic developments in other emerging markets may adversely affect investor confidence in securities issued by Brazilian companies, causing their market price and liquidity to suffer. Any such developments could immediately affect our ability to raise capital when needed and the market price of our class A preferred shares and the ADSs.

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## ITEM 4. INFORMATION ON THE COMPANY

We are the leading petrochemical company in Latin America, based on average annual production capacity in 2005. We are also one of the three largest Brazilian-owned private sector industrial companies, based on net sales revenue. We recorded net income of R$625.8 million in 2005 on net sales revenue of R$13,075.1 million, in each case under Brazilian GAAP. We produce a diversified portfolio of petrochemical products and have a strategic focus on polyethylene, polypropylene and PVC. We have integrated first and second generation petrochemical production facilities, with 14 plants in Brazil following the Politeno acquisition described below.

Our registered office is at Rua Eteno, 1561, CEP 42810-000, Camaçari, Bahia, Brazil, and our telephone number at this address is 55-71-3632-5102. Our principal executive office is at Avenida das Nações Unidas, 4777, São Paulo, SP, CEP 05477-000, Brazil, and our telephone number at this address is 55-11-3443-9000.

### History and Development of Our Company

We were founded in 1972 as Petroquímica do Nordeste Copene Ltda. to plan, execute and coordinate the activities of the Northeastern Complex. The construction of the Northeastern Complex formed part of a development policy of the Brazilian government implemented in the early 1970 s to diversify the geographical distribution of industrial assets and to promote economic growth across different regions of Brazil. On June 18, 1974, we were incorporated as a corporation *(sociedade anônima)* under the laws of Brazil (with Brazilian company registry No. 29300006939) and were renamed Copene Petroquímica do Nordeste S.A.

Prior to August 1995, Petroquisa, the petrochemical subsidiary of Petrobras, owned 36.2% of our total share capital, representing 48.2% of our voting share capital. At that time, Norquisa owned 17.3% of our total share capital, representing 47.6% of our voting share capital, and the remainder of our share capital was owned by various Brazilian private sector groups, pension funds, banks and our employees.

#### *Privatization of Our Company*

In August 1995, as part of the Brazilian government s privatization program, Petroquisa sold 14.8% of our total share capital, representing 32.8% of our voting share capital, through an auction. Norquisa acquired 5.5% of our total share capital, representing 10.8% of our voting share capital, in this auction, and the remaining shares were acquired by various Brazilian pension funds. At the time of this auction, Norquisa was controlled by several second generation producers in the Northeastern Complex. As a result of this auction, Norquisa became our controlling shareholder.

#### *Auction of Banco Econômico s Petrochemical Assets*

On July 25, 2001, the Central Bank, as liquidator of Banco Econômico S.A., a Brazilian financial institution that collapsed in 1995, or Banco Econômico, conducted an auction of the petrochemical assets that had been owned by Banco Econômico. This auction was part of a broader initiative of the Brazilian government to restructure the Brazilian petrochemical sector.

In order to increase its investment in the Brazilian petrochemical industry, the Odebrecht Group participated in this auction through Conepar  Companhia Nordeste de Participações do Nova Camaçari Participações S.A., or Nova Camaçari, a holding company which acquired the petrochemical assets being auctioned. In addition, Nova Camaçari acquired additional petrochemical assets from the Odebrecht Group, a group of Companies controlled by the Mariani family, or the Mariani Group, and other entities which were entitled to sell assets to Nova Camaçari under the terms of various shareholder agreements.

Immediately following these transactions, we acquired Nova Camaçari from the Odebrecht Group in order to expand the scope of our operations and become a vertically integrated producer of petrochemical products. Following these transactions, we owned indirectly
(1) Conepar  Companhia Nordeste de Participações, which,

in turn, held 66.7% of the voting share capital of Polialden Petroquímica S.A., or Polialden, and 35.0% of the voting share capital of Politeno Indústria e Comércio S.A., or Politeno, and (2) Proppet S.A., or Proppet. In connection with these transaction, the Odebrecht Group purchased shares of Norquisa from one of Norquisa s other shareholders in order to increase its percentage ownership of Norquisa. Following these transactions, the Odebrecht Group owned 39.7% of the voting share capital of Norquisa and, together with the Mariani Group, held a combined 55.8% of the voting share capital of Norquisa. In order to streamline our corporate structure, in September 2001, we merged Proppet into our company.

***Acquisition of OPP Química, Nitrocarbono and Interest in Copesul***

In order to continue to implement our strategy of vertically integrating our operations and to further expand the scope of our operations, on August 16, 2002, we acquired from the Odebrecht Group and Pronor Petroquímica S.A., or Pronor, a member of the Mariani Group:

- 81.3% of the total share capital of OPP Química S.A., or OPP Química, including 100% of its voting share capital. OPP Química, in turn, owned 41.6% of the total share capital of Trikem S.A., or Trikem, representing 64.4% of its voting share capital;
- 29.5% of the total share capital and voting share capital of Copesul; and
- 92.3% of the total share capital of Nitrocarbono S.A., or Nitrocarbono, representing 95.5% of its voting share capital.

Upon completing these transactions, we changed our corporate name to Braskem S.A.

In connection with these transactions, we issued shares representing 43.7% of our voting and total share capital to the Odebrecht Group and issued shares representing 3.6% of our voting and total share capital to Pronor. In October and December 2002, we acquired all of OPP Química s total share capital that we did not own.

In February 2003, we commenced a public exchange offer for the remaining voting share capital of Nitrocarbono not owned by our company. On February 13, 2003, immediately following our exchange of the shares tendered in this exchange offer for 128,973 of our class A preferred shares, we owned 93.8% of the total share capital of Nitrocarbono, including 99.99% of its voting share capital. On March 31, 2003, we merged with Nitrocarbono. In connection with this merger, we issued 5,415 of our class A preferred shares to the holders of shares of Nitrocarbono other than our company.

On March 31, 2003, we merged with OPP Química. As a consequence of our merger with OPP Química, we acquired ownership of the share capital of Trikem previously owned by OPP Química.

On June 30, 2003, we entered into an agreement under which we assumed debt of Copene Participações S.A. (formerly Conepar Companhia Nordeste de Participações) owed to Polialden in the amount of R$30.2 million as well as debt of Copene Participações S.A. owed to the Brazilian National Bank for Economic and Social Development (Banco Nacional de Desenvolvimento Econômico e Social, or BNDES) in the amount of R$38.9 million. In return, we received the shares of Polialden and Politeno owned by Copene Participações S.A. As a result, all of our equity interests in Polialden and Politeno were, and continue to be, held directly by our company, and Copene Participações S.A. no longer owns material assets or conducts any material operations.

***Acquisition of Common Shares of Trikem and Polialden Held by Mitsubishi and Sojitz***

In order to acquire the remaining outstanding common shares of Polialden and substantially all of the remaining outstanding common shares of Trikem, on July 14, 2003, we entered into (1) a share purchase and sale agreement with Odebrecht and Mitsubishi Chemical Corporation, or Mitsubishi, and (2) a memorandum of understanding with Odebrecht and Sojitz Corporation (formerly known as Nissho Iwai Corporation), or Sojitz.

Under the share purchase and sale agreement, Mitsubishi agreed to sell to us all of the share capital of Trikem and Polialden it owned, consisting of 16.7% of Polialden s voting share capital and 13.4% of Trikem s voting share capital for R$44.2 million. We paid a portion of the purchase price in cash, and we were obligated to pay the remaining US$13.5 million to Mitsubishi on July 31, 2007, or earlier if before that date we met certain financial tests. We prepaid the remainder of the purchase price on July 29, 2005. Under this agreement, we are required to make an additional payment to Mitsubishi in an amount that is contingent upon the outcome of pending litigation filed against Polialden by certain of its preferred shareholders. We assumed the defense of this litigation as a result of our merger with Polialden on May 31, 2006. The amount of the additional payment that we are obligated to pay to Mitsubishi is (1) R$21.6 million if we prevail in this litigation or if a definitive settlement is reached, or (2) R$5.4 million if we lose this litigation. In either event, we will convert the amount of this additional payment (as adjusted for inflation at the Indice Geral de Perços Mercado, or IGP-M, rate from July 31, 2003 until the date that this litigation is finally adjudicated or settled) into U.S. dollars on the final adjudication or settlement date. We are required to make this additional payment, plus interest from the date of this agreement at an annual rate of LIBOR plus 3.0%, within 60 days after the date on which this litigation is finally adjudicated or settled. Odebrecht has guaranteed our obligation to pay Mitsubishi the additional payment in connection with the Polialden shareholders rights litigation.

Under the memorandum of understanding with Odebrecht and Sojitz, we agreed to purchase all of the share capital of Trikem and Polialden that Sojitz owned, consisting of 16.7% of Polialden s voting share capital and 10.1% of Trikem s voting share capital, in exchange for 4,345,162 of our common shares. As a result of this transaction, which closed on July 31, 2003, and after giving effect to the purchase from Mitsubishi described above, we increased our direct and indirect ownership of Trikem s voting share capital to 87.9% and increased our ownership of Polialden s voting share capital to 100%.

***Merger of Trikem into Braskem***

On November 3, 2003, we commenced a public exchange offer for the remaining voting share capital of Trikem not owned by our company. On December 4, 2003, immediately following our exchange of the shares tendered in this exchange offer for 1,753,080 of our class A preferred shares, we owned, directly and indirectly, 53.8% of Trikem s total share capital, including 99.9% of its voting share capital.

At an extraordinary shareholders meeting on January 15, 2004, our shareholders approved our merger with Trikem, an amendment to our by-laws to permit the conversion of our class A preferred shares into common shares upon the approval of the majority of our voting share capital, and the conversion of 487,793 of our class A preferred shares into 487,793 of our common shares in order to maintain the required minimum ratio of our common shares to preferred shares in accordance with the Brazilian Corporation Law after completion of our merger with Trikem. In connection with this merger, we issued 592 of our class A preferred shares in exchange for 514,366 of Trikem s common shares and 32,544,069 of our class A preferred shares in exchange for 28,260,456,441 of Trikem s preferred shares.

***Exchange of Polialden Shares for Our Class A Preferred Shares***

On December 15, 2004, we exchanged 2,020,201 of our class A preferred shares which were held in our treasury for 47,846,610 preferred shares issued by Polialden held by certain of the shareholders of Polialden. The shareholders of Polialden participating in this exchange were parties to suits brought against Polialden claiming, among other things, that certain dividends were owed to these shareholders. In connection with the exchange of shares, these claims were relinquished by the Polialden shareholders participating in the exchange. As a result of this exchange, we increased our interest in the total share capital of Polialden from 56.3% to 63.7%.

***Politeno Acquisition***

On April 6, 2006, we purchased all of the common and preferred shares of Politeno that were owned by SPQ Investimentos e Participações Ltda., or SPQ, a subsidiary of Suzano Petroquímica S.A., or Suzano,

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Sumitomo Chemical Company Limited, or Sumitomo, and Itochu Corporation, or Itochu. We refer to this transaction as the Politeno acquisition. As a result of the Politeno acquisition, we now own 100% of the voting share capital and 96.2% of the total share capital of Politeno.

*Merger of Polialden into Braskem*

At an extraordinary shareholders meeting on May 31, 2006, our shareholders approved our merger with Polialden and the conversion of 2,632,043 of our class A preferred shares into 2,632,043 of our common shares in order to maintain the required minimum ratio of our common shares to preferred shares in accordance with the Brazilian Corporation Law after completion of our merger with Polialden. In connection with this merger, we issued 7,878,825 of our class A preferred shares in exchange for 264,886,083 of Polialden s preferred shares.

*Current Corporate Structure*

The following chart presents the corporate structure of our principal subsidiaries and equity investments following the transactions described above. The percentages in bold italics represent the percentage of the voting share capital owned directly and indirectly by the parent company of each entity, and the percentages not in bold italics represent the percentage of the total share capital owned directly and indirectly by the parent company of each entity. All of these companies are organized under Brazilian law.

**Our Principal Subsidiary and Jointly Controlled Companies**

Our principal subsidiary is Politeno, which is a corporation (*sociedade anônima*) organized under the laws of Brazil. As a result of the Politeno acquisition on April 6, 2006, we now own 100% of the voting share capital and 96.2% of the total share capital of Politeno. Politeno is engaged in the manufacturing, processing, selling, importing and exporting of low density polyethylene, or LDPE, medium density polyethylene, high density polyethylene, or HDPE, linear low density polyethylene, or LLDPE, linear medium density polyethylene, ethyl vinyl acetate copolymer and other special resins. Politeno operates two industrial units in the Northeastern Complex. For information concerning these operations, see Jointly Controlled Companies and Joint Venture Politeno.

We hold equity investments in Copesul and Petroflex, which are jointly controlled with third parties. We proportionally consolidate the results of these jointly controlled companies in our consolidated financial statements, which has a significant impact on these financial statements. For a description of our jointly controlled companies, see Jointly Controlled Companies and Joint Venture.

**Petrochemical Industry Overview**

*Structure*

The petrochemical industry transforms crude oil by-products, principally naphtha, or natural gas into widely used industrial and consumer goods. The Brazilian petrochemical industry is generally organized into first, second and third generation producers based on the stage of transformation of various petrochemical raw materials, or feedstocks.

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*First Generation Producers*

Brazil s first generation producers, which are referred to as crackers, break down or crack naphtha or natural gas, their principal feedstock, into basic petrochemicals. Three of these crackers purchase naphtha, which is a by-product of the oil refining process, primarily from Petrobras, as well as from other suppliers located outside of Brazil. The fourth, Rio Polímeros, purchases natural gas from Petrobras. The basic petrochemicals produced by the crackers include:

- olefins, primarily ethylene, propylene and butadiene; and
- aromatics, such as benzene, toluene and xylenes.

We, Copesul, Petroquímica União and Rio Polímeros operate Brazil s four crackers and sell basic petrochemicals to second generation producers, including, in our case, second generation producers that are part of our company. The basic petrochemicals, which are in gaseous or liquid form, are transported primarily via pipelines to the second generation producers plants, generally located near the crackers, for further processing.

*Second Generation Producers*

Second generation producers process the basic petrochemicals obtained from the crackers to produce intermediate petrochemicals. These petrochemicals include:

- polyethylene, polystyrene and PVC (each produced from ethylene);
- polypropylene and acrylonitrile (each produced from propylene);
- caprolactam (produced from benzene); and
- polybutadiene (produced from butadiene).

There are 36 second generation producers operating in Brazil. Intermediate petrochemicals are produced in solid form as plastic pellets or powders and are transported primarily by truck to third generation producers, which generally are located far from the second generation producers. We and Rio Polímeros are the only integrated first and second generation petrochemical company in Brazil.

*Third Generation Producers*

Third generation producers, known as transformers, purchase the intermediate petrochemicals from second generation producers and transform them into final products including:

- plastics (produced from polyethylene, polypropylene and PVC);
- acrylic fibers (produced from acrylonitrile);
- nylon (produced from caprolactam);
- elastomers (produced from butadiene); and
- disposable containers (produced from polystyrene).

Third generation producers manufacture a variety of consumer and industrial goods, including containers and packaging materials, such as bags, film and bottles, textiles, detergents, paints, automobile parts, toys and consumer electronic goods. There are over 6,000 third generation producers operating in Brazil.

*Petrochemical Complexes*

The production of first and second generation petrochemicals in Brazil centers around four major complexes. These complexes include:

- the Northeastern Complex located in Camaçari in the State of Bahia, where we operate the cracker;

the Southern Complex located in Triunfo in the State of Rio Grande do Sul, where Copesul operates the cracker;

the São Paulo Complex located in Capuava in the State of São Paulo, or the São Paulo Complex, where Petroquímica União operates the cracker; and

the Rio de Janeiro Complex located in Duque de Caxias in the State of Rio de Janeiro, or the Rio de Janeiro Complex, where Rio Polímeros operates the cracker.

Each complex has a single first generation producer, also known as the raw materials center, and several second generation producers that purchase feedstock from the raw materials center.

The Northeastern Complex began operations in 1978. The Northeastern Complex consists of 15 second generation producers situated around the raw materials center operated by our company. At December 31, 2005, our raw materials center had an annual ethylene production capacity of 1,280,000 tons, which we estimate accounted for approximately 37.3% of Brazil s ethylene production capacity.

The Southern Complex began operations in 1982. Copesul, in which we have a 29.5% equity interest, is the raw materials center at the Southern Complex and supplies first generation petrochemicals to seven second generation producers, including our Polyolefins Unit. At December 31, 2005, Copesul had an annual ethylene production capacity of 1,135,000 tons.

The São Paulo Complex, which is the oldest petrochemical complex in Brazil, began operations in 1972. Petroquímica União is the raw materials center at the São Paulo Complex and supplies first generation petrochemicals to 20 second generation producers, including our company. At December 31, 2005, Petroquímica União had an annual ethylene production capacity of 500,000 tons.

The Rio de Janeiro Complex commenced operations in 2005. Rio Polímeros, a Brazilian petrochemical company, is the raw materials center at the Rio de Janeiro Complex and supplies first generation petrochemicals to two second generation producers. At December 31, 2005, Rio Polímeros had a maximum annual ethylene production capacity of 520,000 tons. This plant is in the process of ramping up its production towards its annual capacity.

***Role of the Brazilian Government***

The current structure of the Brazilian petrochemical industry reflects the Brazilian government s plan, developed during the 1970 s, to establish a domestic petrochemical industry to serve Brazilian markets. First and second generation producers, including our company, are located within close proximity of each other to allow the common use of facilities, such as utilities, and to facilitate the delivery of feedstocks. Prior to their privatization by the Brazilian government, the expansion of production capacity at the crackers and the second generation producers was coordinated to ensure that the supply of petrochemicals met expected demand. The infrastructure developed around the complexes fostered the interdependence of first and second generation producers, as limited facilities were constructed for purposes of transportation and storage of feedstocks for import or export. Following their privatization, this interdependence has increased as second generation producers, which continue to rely upon the crackers for feedstocks and utilities, have increased their ownership of, and participation in the management of, the crackers.

The Brazilian government developed the Brazilian petrochemical industry generally by promoting the formation of three-way joint ventures among the Brazilian government, foreign petrochemical companies and private Brazilian investors. In these joint ventures, Petrobras subsidiary, Petroquisa, participated as the representative of the Brazilian government, with Petrobras as the supplier of naphtha; a foreign petrochemical company provided technology; and a Brazilian private sector company provided management.

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In 1992, the Brazilian government began a privatization program to reduce significantly its ownership of the petrochemical industry. This program was designed to increase private investment in the petrochemical industry and to improve its efficiency. As a result of the privatization program, the Brazilian government s ownership of our common shares, and of the common shares of Copesul and Petroquímica União, was significantly reduced, replaced by private sector entities. As a result of a similar privatization process, private ownership of the second generation producers increased.

The following table sets forth the percentage of the indirect ownership interests held in the crackers voting shares by Petroquisa, private sector entities and other investors before the privatization of the crackers and at December 31, 2005.

| | Before privatization | | | | At December 31, 2005 | | |
|---|---|---|---|---|---|---|---|
| | Date of privatization | Petroquisa | Private sector groups | Other investors(1) | Petroquisa | Private sector groups | Other investors(1) |
| Copesul | May 15, 1992 | 67.2% | 2.1% | 30.7% | 15.6% | 58.9% | 25.4% |
| Petroquímica União | January 24, 1994 | 67.8 | 31.9 | 0.3 | 17.4 | 60.8 | 21.8 |
| Braskem | August 15, 1995 | 48.2 | 50.4 | 1.4 | 10.0 | 74.1 | 15.9 |
| Rio Polímeros | | | | | 16.7 | 66.6 | 16.7 |

(1) Pension funds, banks and individual investors.

*Role of Petrobras*

Prior to 1995, Brazil s Constitution granted a monopoly to the Brazilian government, exercised through Petrobras, over the research, exploration, production, refining, importing and transporting of crude oil and refined petroleum products (excluding petrochemical products) in Brazil. The Brazilian Constitution also provided that by-products of the refining process, such as naphtha, could only be supplied in Brazil by or through Petrobras. Naphtha is the principal feedstock used in Brazil for the production of basic petrochemicals such as ethylene and propylene. In 1995, the Brazilian Constitution was amended to allow petroleum and petroleum related activities to be carried out by private companies, by concession or authorization from the Brazilian government. Since 1995, the Brazilian government has taken several measures to liberalize the petrochemical industry in Brazil.

In 1997, Law No. 9,478/97 implemented the 1995 constitutional amendment by creating the Brazilian Energy Policy Council (*Conselho Nacional de Política Energética*) and the National Petroleum Agency (*Agência Nacional de Petróleo*), which were charged with regulating and monitoring of the oil industry and the Brazilian energy sector. Following the creation of the National Petroleum Agency, new rules and regulations have been implemented, aimed at gradually ending Petrobras monopoly. Since 1997, our company and Copesul have imported naphtha from trading companies and oil and gas producers located abroad.

During 2005, Petrobras produced and sold approximately 72% of the naphtha consumed by our company and Copesul, and the remaining naphtha consumed by our company and Copesul was imported.

*Tariffs*

We set prices for a majority of the ethylene, the principal first generation petrochemical product, that we sell to third party second generation producers using a margin sharing system. See Basic Petrochemicals Unit Sales and Marketing of Our Basic Petrochemicals Unit. Prices paid by second generation producers for imported first generation petrochemical products partly reflect transportation and tariff costs. We establish the prices of ethylene by-products, such as butadiene, by reference to several market factors, including the prices paid by second generation producers for imported products, which also take into account transportation and tariff costs.

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Second generation producers, including our company, generally set prices for their petrochemical products by reference to several market factors, including the prices paid by third generation producers for imported products. Prices paid for such imports also reflect transportation and tariff costs.

The Brazilian government has frequently used import tariffs to implement economic policies. As a result, import tariffs generally vary significantly, especially those imposed on petrochemical products. Imports and exports within the free trade area composed of Argentina, Brazil, Paraguay and Uruguay in South America, or Mercosul (*Mercado Comum do Sul*), have not been subject to tariffs since December 2001. The following table shows the fluctuation of the tariffs on certain basic petrochemicals and second generation petrochemicals from 1996 through 2005. The tariff rates shown are those applicable at the end of the respective years, except where indicated.

| (%) | 2005 | 2004 | 2003 | 2002(1) | 2001(2) | 2000 | 1999 | 1998 | 1997(3) | 1996 |
|---|---|---|---|---|---|---|---|---|---|---|
| **First generation petrochemicals:** | | | | | | | | | | |
| Ethylene | 2.0 | 2.0 | 3.5 | 3.5 | 4.5 | 5.0 | 5.0 | 5.0 | 5.0 | 2.0 |
| Propylene | 2.0 | 2.0 | 3.5 | 3.5 | 4.5 | 5.0 | 5.0 | 5.0 | 5.0 | 2.0 |
| Caustic soda | 8.0 | 8.0 | 9.5 | 9.5 | 10.5 | 11.0 | 11.0 | 11.0 | 11.0 | 8.0 |
| **Second generation petrochemicals:** | | | | | | | | | | |
| Polyethylene | 14.0 | 14.0 | 15.5 | 15.5 | 16.5 | 17.0 | 17.0 | 17.0 | 17.0 | 14.0 |
| Polypropylene | 14.0 | 14.0 | 15.5 | 15.5 | 16.5 | 17.0 | 17.0 | 17.0 | 17.0 | 14.0 |
| PVC(4) | 14.0 | 14.0 | 15.5 | 15.5 | 16.5 | 17.0 | 17.0 | 17.0 | 17.0 | 14.0 |
| Caprolactam | 12.0 | 12.0 | 13.5 | 13.5 | 14.5 | 15.0 | 15.0 | 15.0 | 15.0 | 12.0 |

(1) In 2002, the official tariff was 1.5% less than the rate shown. An additional surcharge of 1.5% assessed on imported products is included in the rate shown.
(2) In 2001, the official tariff was 2.5% less than the rate shown. An additional surcharge of 2.5% assessed on imported products is included in the rate shown.
(3) An additional tariff of 3% was assessed commencing on November 13, 1997, which is included in the rate shown.
(4) Imports of suspension PVC from the U.S and Mexico have been subject to tariffs of 16% and 18%, respectively, since 1992 as a result of the imposition of anti-dumping duties by the Brazilian Foreign Trade Chamber (*CAMEX-Câmara de Comércio Exterior*) of the Ministry of Development, Industry and Trade. These duties will expire on December 14, 2010, unless extended.

*Source:* Brazilian Association of Chemical Industry and Derivative Products.

***Operating Environment***

The Brazilian markets in which we compete are cyclical and are sensitive to relative changes in supply and demand. Demand for petrochemical products is significantly affected by general economic conditions in Brazil and other countries in Mercosul, particularly Argentina. The Brazilian markets are also impacted by the cyclical nature of international markets as prices for petrochemical products in Brazil are determined in part with reference to international market prices for these products and by the prices, including tariff and transportation costs, paid by importers of petrochemical products into Brazil. Reductions in tariffs and other trade barriers have increasingly exposed the Brazilian petrochemical industry to price competition in the international markets.

Traditionally, the second and third calendar quarters have been the periods of the year with the highest sales for the petrochemical industry in the Brazilian market. The increase during this six-month period is tied in part to the production of consumer goods for sale during the year-end holiday season.

Brazilian GDP increased by 2.3% in 2005. The moderate growth of Brazilian GDP in 2005 contributed to a 2.9% increase in domestic polypropylene consumption, slight growth in domestic consumption of PVC and a 4.9% decline in domestic consumption of polyethylene. Domestic consumption of thermoplastic resins increased

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for certain applications, such as automotive parts and durable goods, including cellular phones and home appliances. Although imports represent a small percentage of total Brazilian domestic consumption, in 2005, imports of polyolefins increased by 7.2% and imports of PVC increased by 26.5%. In 2005, Brazil s exports of PVC increased by 75.7% and its exports of polyolefins increased by 27.9%. As a result of increased production capacity of Brazilian producers, including our company, higher rates of capacity utilization, and the continuing appreciation of the *real* against the U.S. dollar in 2005, Brazilian petrochemical producers significantly improved their sales in 2005.

We anticipate that demand for our products in Brazil may grow due to increasing consumption of plastic-based products, as well as population growth and expected general economic growth in Brazil. In addition, Brazilian per capita consumption of second generation petrochemicals has been modest compared to per capita consumption in many other more developed countries, which we believe suggests a potential for future growth in demand in Brazil. However, that growth could be hindered by the factors described in Item 3. Key Information Risk Factors Risks Relating to Brazil and Item 3. Key Information Risk Factors Risks Relating to Our Company and the Petrochemical Industry.

The following table sets forth information relating to our production, the estimated production of other Brazilian companies and exports and imports of the products included therein for the years indicated.

| (thousands of tons) | Total Brazilian production | Our total production | Total production of other Brazilian companies | Total Imports | Total exports | Estimated total Brazilian domestic consumption |
|---|---|---|---|---|---|---|
| Olefins(1) | | | | | | |
| 2005 | 4,775.2 | 1,889.9 | 2,885.2 | 18.5 | 120,0 | 4,672.7 |
| 2004 | 4,779.0 | 1,809.6 | 2,969.4 | 19.9 | 121.5 | 4,677.3 |
| 2003 | 4,444.0 | 1,678.6 | 2,765.4 | 24.0 | 127.8 | 4,340.2 |
| Aromatics(2) | | | | | | |
| 2005 | 1,518.0 | 733.7 | 784.3 | 47.6 | 453.8 | 1,111.8 |
| 2004 | 1,562.4 | 714.8 | 847.6 | 100.4 | 317.8 | 1,345.0 |
| 2003 | 1,475.4 | 638.3 | 837.1 | 105.2 | 345.5 | 1,235.1 |
| Polyolefins(3) | | | | | | |
| 2005 | 3,148.3 | 1,289,2 | 1,859.1 | 379.9 | 782.8 | 2,745.4 |
| 2004 | 3,042.6 | 1,175.1 | 1,867.5 | 354.4 | 651.4 | 2,745.7 |
| 2003 | 2,854.4 | 1,101.7 | 1,752.7 | 324.4 | 717.6 | 2,461.1 |
| PVC | | | | | | |
| 2005 | 640.3 | 449.3 | 191.0 | 119.5 | 65.6 | 694.2 |
| 2004 | 629.7 | 420.7 | 209.1 | 94.5 | 44.1 | 680.1 |
| 2003 | 604.1 | 392.1 | 212.0 | 86.4 | 75.7 | 614.8 |
| PET | | | | | | |
| 2005 | 352.6 | 69.7 | 282.9 | 178.4 | 32.6 | 498.3 |
| 2004 | 357.6 | 72.6 | 285.0 | 137.1 | 62.0 | 432.7 |
| 2003 | 339.0 | 55.3 | 283.6 | 136.2 | 44.5 | 430.6 |
| Caprolactam | | | | | | |
| 2005 | 49.7 | 49.7 | | 4.1 | 16.2 | 37.5 |
| 2004 | 50.5 | 50.5 | | 6.4 | 7.6 | 49.3 |
| 2003 | 48.8 | 37.6 | 11.3 | 4.9 | 8.1 | 45.6 |

(1) Includes ethylene, propylene and butadiene.
(2) Includes benzene, toluene, xylenes and, during 2002 only, solvent C9.
(3) Includes polyethylene, HDPE, low density polyethylene, linear low density polyethylene and polypropylene.

*Sources:* Brazilian Association of Chemical Industry and Derivative Products and Braskem.

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The above estimates of total domestic consumption assume that all domestic production is immediately sold in the market and that there has been no change in total domestic inventory.

**Overview of Our Company s Operations**

We are the leading petrochemical company in Latin America, based on average annual production capacity in 2005. We are also one of the three largest Brazilian-owned private sector industrial companies, based on net sales revenue in 2004 (the most recent year for which comparative information is currently available). We recorded net income of R$625.8 million in 2005 on net sales revenue of R$13,075.1 million. We produce a diversified portfolio of petrochemical products in our 14 plants in Brazil and have a strategic focus on polyethylene, polypropylene and PVC. We were the first Brazilian company with integrated first and second generation petrochemical production facilities.

We have grown over the past five years primarily as the result of the integration of the operations of six Brazilian petrochemical companies: our company; OPP Química; Polialden; Trikem; Proppet; and Nitrocarbono. Our business operations are organized into four business units, which correspond to our principal production processes and products:

- Basic Petrochemicals, which accounted for R$7,226.7 million, or 53.5%, of the net sales revenue of all segments, including net sales to our other business units, and had an operating margin of 12.4% in 2005;

- Polyolefins, which accounted for R$3,919.0 million, or 29.0%, of the net sales revenue of all segments and had an operating margin of 14.1% in 2005;

- Vinyls, which accounted for R$1,794.1 million, or 13.3%, of the net sales revenue of all segments and had an operating margin of 24.5% in 2005; and

- Business Development, which accounted for R$569.0 million, or 4.2%, of the net sales revenue of all segments and had an operating margin of 1.2% in 2005.

We believe the integration of the operations of the companies that formed our company has produced, and will continue to provide, significant synergies and cost savings from reductions in taxes, procurement and logistics expenses, general and administrative expenses and other operating expenses.

**Strategy**

Our vision is to strengthen our position as a world-class petrochemical company. We seek to reinforce our leading position in the Latin American petrochemical market, with a focus on polyethylene, polypropylene and PVC and integration with our production of ethylene and propylene. Our business model focuses on enhancing shareholder value, with strategic drivers consisting of market leadership, cost competitiveness and technological autonomy.

We are the first Brazilian company to integrate first and second generation petrochemical production facilities. Our competitive advantages are derived from our leadership position in the Latin American market and on our favorable cost structure, resulting from our production scale and synergies realized from integration of the companies that formed our company.

We are committed to providing technological support to our customers through the Braskem Technology and Innovation Center, which develops processes, products and applications for the sector.

The formation of our company marked a milestone in the restructuring of an industrial sector that is vital to Brazil s economic development. We supply petrochemical products with application in a wide variety of industries, such as food packaging, automotive parts, paints, construction, agriculture, fabrics and personal care products.

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The key elements of our strategy include:

*Focus on customer relationships:* We seek to establish close, long-term relationships with our customers. We serve as partners with our customers in developing new products and applications and, consequently, business opportunities for them. We recognize the cyclical nature of the markets for our petrochemical products and believe that, by focusing on relationships with our customers, we can foster customer loyalty even during periods of lower demand. Our growth strategy is centered on increasing customers consumption of our products, and enabling them to substitute non-plastic materials with thermoplastics.

Our Polyolefins Unit and our Vinyls Unit maintain technology and innovation centers that seek to:

optimize customers processing of our products;

identify new products and applications to meet our clients needs; and

increase customers productivity.

*Pursuit of selected business opportunities:* We are pursuing new business opportunities by, for example:

manufacturing new products such as: UTEC, our ultra high molecular weight polyethylene, or UHMWP, product that is used in technical applications; Braskem Flexus®, a high-performance polyethylene product used for specialized packaging; and Braskem Symbios®, a high-performance flexible packaging sealant. We are the world s second largest producer of UHMWP, which we sell mainly in the United States;

manufacturing LLDPE and LDPE using a specialized production process that permits us to produce thermoplastics with distinctive characteristics for the flexible packaging industry, including greater resistance to impact and punctures, improved polish and greater transparency; and

replacing traditional materials such as glass, wood, steel and paper, with our thermoplastics products.

*Expansion of our production capacity:* We plan to expand the production capacity of our business units during the next several years based on anticipated growth in demand for our products. We plan to expand our production capacity in the short-term principally through efficiency enhancements at our plants and by modernizing our production technology, although from time to time we may consider acquisitions of second generation producers that currently compete with us or produce products that are complementary to ours or enter into joint ventures with others to build new petrochemical plants.

On April 6, 2006, we purchased all of the common and preferred shares of Politeno that were owned by SPQ, a subsidiary of Suzano, Sumitomo and Itochu. As a result of the Politeno acquisition, we now own 100% of the voting share capital and 96.2% of the total share capital of Politeno.

We have entered into a joint venture with Petroquisa for the construction of a polypropylene plant in Paulínia, in the State of São Paulo, with an initial annual production capacity of 300,000 tons. In addition, we have entered into a memoranda of understanding with Petroquímica de Venezucla, S.A., or Pequiven, the petrochemical subsidiary of Petrobrás de Venezuela S.A., to evaluate (1) the feasibility of entering into a joint venture for the construction of a polypropylene plant in the El Tablazo Petrochemical Complex in the State of Zulia, Venezuela, with an annual production capacity of approximately 400,000 tons and (2) the feasibility of entering into a joint venture for the construction of the Jose Project, a petrochemical complex including an ethylene cracker that will use natural gas as its primary raw material, with an annual production capacity in excess of 1.2 million tons, as well as integrated plants to produce polyethylene and other second-generation petrochemicals. We are also evaluating the feasibility of entering into a joint venture with other companies for the construction of a new integrated polyethylene production center in Brazil close to the Brazilian-Bolivian border that would use Bolivian natural gas as a feedstock and have an annual production capacity of approximately

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600,000 tons of polyethylene. We believe that additional capacity developed by our company, together with joint venture partners, will enable us to maintain and expand our leadership position in Latin America and support our expansion into strategic export markets.

*Continued Reductions in Operating Costs and Increases in Operating Efficiencies:* As a result of the integration of our facilities and large production scale, we believe that we are a low-cost producer of second generation petrochemicals. We have an ongoing program the Braskem+ program to increase operating efficiencies and to reduce operating costs. We also continue to realize synergies from our integration process.

Our cost reduction program is linked to initiatives to purchase feedstocks at competitive prices. We began to import lower-cost naphtha in 2002, and during 2005, we imported approximately 30% of our feedstock requirements, primarily from North Africa.

*Commitment to Our Employees and Communities:* We are focused on our human resources, which are vital to our competitiveness and growth. We continue to train our employees to develop skills necessary to operate an internationally competitive, vertically integrated petrochemical company. We have adopted a policy that makes all of our directors, officers, and employees responsible for worker safety and for preserving the environment. We are also committed to sustainable development and to improving the quality of life in the communities in which our facilities are located.

**Braskem+ Program**

We are in the process of implementing an operational excellence program named Braskem+ . This program is designed to build upon the experience that Braskem has accumulated through the process of capturing operational synergies during its integration process. The Braskem+ program seeks to:

- improve our operating performance and productivity;
- reduce our operating and maintenance costs; and
- position Braskem among the most competitive petrochemical companies in the world.

In connection with the development of the Braskem+ program, we engaged a leading consulting firm to analyze our industrial practices and compare them to benchmarking practices in the global petrochemical sector. Through this analysis, we have identified 210 initiatives designed to further improve, among other things, our capacity utilization and variable and fixed costs.

The implementation of the Braskem+ program is being performed by several teams, including:

- a team for each industrial plant that includes the vice president of the respective business unit and the industrial, plant and maintenance managers of that industrial plant, as well as liaisons to our management team; and a corporate management team specifically dedicated to overseeing and coordinating the implementation of the overall program.

We monitor the ongoing results of our implementation of the Braskem+ program, to determine our success in meeting scheduled milestones, perform follow-up activities and determine our progress in meeting the objectives of this program.

**Formula Braskem**

In 2005, we commenced a new program named Formula Braskem to implement a comprehensive integrated management system. Formula Braskem is intended to incorporate the best practices in the international petrochemical industry in our management systems and the most recent technological developments available in the marketplace. This program, together with the Braskem+ program, is designed to support our expansion and

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future internationalization, and we expect to realize productivity and efficiency gains through their implementation. In addition, we believe that the implementation of Formula Braskem will assist us with our compliance with the requirements of the U.S. Sarbanes-Oxley Act of 2002 in a manner consistent with our commitment to transparency and corporate governance.

We anticipate that Formula Braskem will be operational by October 2006. We have engaged SAP Brasil Ltda., or SAP, and Accenture do Brasil Ltda., or Accenture, to assist us in implementing Formula Braskem under agreements that provide for (1) the payment of bonuses to SAP and Accenture in the event that we achieve identified annual cost savings as a result of the implementation of Formula Braskem in excess of those identified in our calculations of the projected net present value of this project, and (2) the payment of bonuses to SAP in the event that Formula Braskem is operational prior to its target date. Conversely, these agreements provide for the payment of penalties by Accenture and the forfeiture of any bonuses by SAP in the event that Formula Braskem does not become operational until after the target date. We have a dedicated team of approximately 110 employees working together with SAP and Accenture on the implementation of Formula Braskem which we expect to implement at a cost of approximately R$130 million. We cannot assure holders of our class A preferred shares and the ADSs that we will realize the full benefit of the identified annual cost savings in upcoming years. To the extent that we fail to do so in any year, our results of operations for that year may be adversely affected.

**Basic Petrochemicals Unit**

At December 31, 2005, our Basic Petrochemicals facilities had one of the largest average annual production capacities of all first generation producers in Latin America. Our Basic Petrochemicals Unit accounted for R$7,226.7 million, or 53.5%, of the net sales revenue of all segments in 2005, including net sales to our other business units. Our Basic Petrochemicals Unit produces:

- olefins, such as ethylene, polymer and chemical grade propylene, butadiene, isoprene and butene-1;
- aromatics, such as benzene, toluene, para-xylene and ortho-xylene;
- fuels, such as automotive gasoline and liquefied petroleum gas, or LPG; and
- methyl tertiary butyl ether, or MTBE, solvent C9 and pyrolysis C9.

The products of our Basic Petrochemicals Unit are used primarily in the manufacture of intermediate second generation petrochemical products, including those manufactured by our other business units. We also supply utilities to other plants located in the Northeastern Complex and render services to the operators of those plants. In 2005, 87.5% of our Basic Petrochemicals Unit s sales (including intra-company sales) were derived from the sale of basic petrochemicals, 6.8% from the sale of utilities and services, and 5.7% from the sale of fuels.

We believe that our Basic Petrochemicals Unit is well positioned to take advantage of increasing demand for basic petrochemicals products in Brazil, both by our other business units and by third parties. We anticipate that long-term growth for these products in Brazil will continue due to increasing demand for consumer products.

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***Products of Our Basic Petrochemicals Unit***

The following chart shows the major products produced by our Basic Petrochemicals Unit, their derivative intermediate products and their most common end uses.

| Our basic petrochemical products | Intermediate products derived from our basic petrochemical products | Common end uses |
|---|---|---|
| **Olefins** | | |
| Ethylene | LDPE /LLDPE(1) | Garbage bags, packaging film, toys, housewares, electrical insulation, paper coatings |
| | HDPE(1) | Blow-molded plastic bottles (such as milk bottles) |
| | UHMWP(1) | Technical parts, industrial applications, medical applications, parts for automotive industry products |
| | Ethyl vinyl acetate copolymer(1) | Shoe soles, hot melt, plastic film for special applications |
| | Ethylene oxide, used to produce ethylene glycol | Polyester fibers and PET resin |
| | Ethylene dichloride, used to produce PVC(2) | Pipes, home siding, upholstery, floor coverings |
| | Ethylbenzene, used to produce styrene monomer and then polystyrene | Disposable cups and containers, high-impact plastics |
| Propylene (polymer and chemical grade) | Polypropylene(1) | Carpet-backing, luggage, bottles, diapers, raffia bags |
| | Acrylonitrile | Clothing, plastics |
| | Propylene oxide | Polyurethane foams for furniture and insulation, cleaning compounds and coatings |
| Butadiene | Synthetic rubber, elastomers, resins | Tires, shoes, hoses, surgical gloves |
| Butene-1 | LLDPE(1) | Garbage bags, packaging film, toys, housewares, electrical insulation, paper coatings |
| **Aromatics** | | |
| Benzene | Ethylbenzene (used to make styrene monomer/polysterene) | Disposable cups, containers, high-impact plastics |
| | Cumene | Epoxies |
| | Cyclohexane and cyclohexanone(3) | Nylon |
| | Linear alkyle benzene | Detergents |
| | Caprolactam(3) | Nylon |
| | Ammonium sulfate(3) | Fertilizers |
| Isoprene | Styrene-isoprene-styrene (SIS) | Adhesive |
| Toluene | Toluenediisocianate | Urethane foams |
| | | Solvents |
| Para-xylene | Purified terephthalic acid and DMT(3) | Polyester film and fibers, PET resin(3) |
| Ortho-xylene | Phthalic anhydride and plasticizers | Flexible products from PVC |
| **Others** | | |
| MTBE | | Octane booster for gasoline |
| Solvent C9 | | Solvents and thinners |
| Pyrolysis C9 | | Octane booster for gasoline |
| **Fuels** | | |
| Automotive Gasoline | | Fuel for internal combustion engines |

| | |
|---|---|
| LPG | Cooking gas |

(1) Produced by our Polyolefins Unit.
(2) Produced by our Vinyls Unit.
(3) Produced by our Business Development Unit.

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The following table sets forth a breakdown of the sales volume and net sales revenue of our Basic Petrochemicals Unit (including our intra-company sales) by product line and by market for the years indicated.

| | Years ended December 31, | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2005 | | | 2004 | | | 2003 | | |
| | Quantities sold(1) | Net sales revenue | | Quantities sold(1) | Net sales revenue | | Quantities sold(1) | Net sales revenue | |
| | (thousands of *tons*) | (millions of *reais*) | (%) | (thousands of *tons*) | (millions of *reais*) | (%) | (thousands of *tons*) | (millions of *reais*) | (%) |
| Domestic net sales: | | | | | | | | | |
| Ethylene | 1,169.8 | R$ 2,578.2 | 40.8% | 1,098.9 | R$ 2,302.2 | 40.1% | 1,047.3 | R$ 1,733.1 | 41.9% |
| Propylene | 497.5 | 1,060.9 | 16.8 | 446.8 | 819.1 | 14.3 | 403.4 | 595.9 | 14.4 |
| Para-xylene | 171.0 | 385.0 | 6.1 | 148.7 | 319.6 | 5.6 | 117.3 | 195.5 | 4.7 |
| Benzene | 199.9 | 439.8 | 7.0 | 216.7 | 522.6 | 9.1 | 217.9 | 298.3 | 7.2 |
| Butadiene | 150.2 | 331.3 | 5.2 | 160.0 | 296.0 | 5.2 | 150.3 | 278.7 | 6.7 |
| Mixed xylenes | 35.4 | 61.7 | 1.0 | 74.5 | 126.4 | 2.2 | 53.7 | 83.4 | 2.0 |
| Ortho-xylene | 41.3 | 87.0 | 1.4 | 52.7 | 109.9 | 1.9 | 49.9 | 80.0 | 1.9 |
| Toluene | 29.5 | 48.0 | 0.7 | 33.2 | 57.4 | 1.0 | 38.9 | 51.4 | 1.2 |
| Others | 203.8 | 380.1 | 6.0 | 255.3 | 405.0 | 7.1 | 195.8 | 324.6 | 7.9 |
| Total domestic net sales of basic petrochemicals | 2,498.4 | 5,372.0 | 85.0 | 2,486.8 | 4,958.2 | 86.4 | 2,274.5 | 3,640.9 | 87.9 |
| Total export net sales of basic petrochemicals | 535.0 | 950.0 | 15.0 | 436.6 | 778.9 | 13.6 | 405.9 | 490.7 | 11.9 |
| Total net sales of basic petrochemicals | 3,033.4 | 6,322.0 | 100% | 2,923.4 | 5,737.1 | 100% | 2,680.4 | 4,131.6 | 100% |
| Automotive gasoline and utilities(2) | | 904.7 | | | 742.9 | | | 633.7 | |
| Total Basic Petrochemicals Unit net sales revenue(3) | | R$ 7,226.7 | | | R$ 6,480.0 | | | R$ 4,765.3 | |
| % of the total net sales revenue of all segments | | | 53.5% | | | 52.1% | | | 47.8% |

(1) Includes the following intra-company sales:

- approximately 588,700 tons of ethylene in 2005, 537,100 tons in 2004 and 488,300 tons in 2003;
- approximately 89,300 tons of propylene in 2005, 31,300 tons in 2004 and 4,300 tons in 2003;
- approximately 45,6000 tons of para-xylene in 2005, 48,200 tons in 2004 and 39,700 tons in 2003; and
- approximately 60,800 tons of benzene in 2005, 62,300 tons in 2004 and 60,000 tons in 2003.

(2) Utilities include electric power, steam, treated water and compressed air.

(3) Includes basic petrochemicals, fuels and utilities.

*Olefins*

Olefins are relatively unstable hydrocarbons characterized by a structure that is chemically active and permits other chemically reactive elements, such as oxygen, to be added. Ethylene and propylene, which are types of olefins, are the chemical backbone for many plastic resins used to manufacture consumer products. Our primary olefins products include polymer grade ethylene and propylene, also known as monomers. Different combinations of monomers are polymerized, or linked together, to form polymers or plastic resins with different properties and characteristics.

*Aromatics*

Aromatics are hydrocarbons identified by one or more benzene rings or by chemical behavior similar to benzene. Aromatics readily react to add other active molecular groups, such as nitrates and sulfonates.

*Fuels*

Our company has been authorized by the National Petroleum Agency to produce and sell automotive gasoline since August 15, 2000 and LPG since October 2, 2001, both domestically and for export. We have been producing and selling both automotive gasoline and LPG since these dates.

*Utilities*

We produce electric power, steam, compressed air and clarified drinking and demineralized water, some of which are by-products of our production of basic petrochemicals. We use these utilities in our own production processes, including those of our Polyolefins Unit and our Vinyls Unit, and sell these utilities to approximately 40 companies in the Northeastern Complex. Our utilities facilities include units for thermoelectric power generation, water treatment and the production of steam and compressed air.

We self-generate approximately 70% of the Northeastern Complex s energy consumption requirements, and the remainder is furnished by Companhia Hidro Elétrica do São Francisco CHESF, a Brazilian government-owned electric power generation company located in the State of Bahia, and by Companhia de Eletricidade do Estado da Bahia COELBA.

***Production Facilities of Our Basic Petrochemicals Unit***

We believe that the technological processes we use at our basic petrochemicals plants are among the most advanced in the world. We currently own and operate five major Basic Petrochemicals units (Olefins 1, Olefins 2, Aromatics 1, Aromatics 2 and Energy and Services), each of which is located at the Northeastern Complex. Our Basic Petrochemicals Unit defines the term unit to mean several plants that are linked together to produce olefins, aromatics or utilities. As a result, the production capacity of Aromatics units 1 and 2 is the sum of the production capacities of the various plants that form these units. At December 31, 2005, our basic petrochemicals plants had total annual production capacity of 1,280,000 tons of ethylene and 550,000 tons of propylene.

The table below sets forth the name, primary products, annual production capacity at December 31, 2005 and annual production for the years presented for each of our principal Basic Petrochemicals units and plants.

| | | Annual production | Production year ended December 31, | | |
|---|---|---|---|---|---|
| **Name** | **Primary products** | **capacity** | **2005** | **2004** | **2003** |
| | | **(in tons, except automotive gasoline)** | **(in tons, except automotive gasoline)** | | |
| Olefins units 1 and 2 | Ethylene | 1,280,000 | 1,165,319 | 1,105,610 | 1,040,858 |
| | Propylene | 550,000 | 562,048 | 542,359 | 486,959 |
| Plants of aromatics units 1 and 2: | | | | | |
| Butadiene plants 1 and 2 | Butadiene | 175,000 | 162,586 | 161,616 | 150,719 |
| MTBE plants 1 and 2 | MTBE | 140,000 | 129,345 | 130,079 | 113,996 |
| Butene-1 plant | Butene 1 | 35,000 | 25,515 | 29,093 | 27,022 |
| Isoprene plant | Isoprene | 19,000 | 16,140 | 16,396 | 16,396 |
| | Dicyclopentadiene | 24,000 | 25,245 | 21,306 | 20,459 |
| Sulfolane plants 1, 2 and 3 | Coperaf 1(1) | 120,000 | 86,066 | 112,249 | 110,769 |
| BTX fractionation plants 1 and 2 | Benzene | 427,000 | 428,796 | 393,737 | 364,762 |
| | Toluene(2) | 42,000 | 38,505 | 58,502 | 41,757 |
| C8+ fractionation plant | Mixed xylenes(2) | 40,000 | 50,487 | 87,208 | 65,932 |

| | | | | | |
|---|---|---|---|---|---|
| | Ortho-xylene | 62,000 | 57,441 | 53,966 | 54,475 |
| | Solvent C9(1) | 30,000 | 20,011 | 20,405 | 25,650 |
| Parex plant | Para-xylene | 203,000 | 158,461 | 124,455 | 116,203 |
| Blending plant | Automotive gasoline(3) | 600,000 | 457,334 | 394,591 | 365,256 |
| | LPG | 25,000 | 15,822 | 18,767 | 17,403 |

(1) Solvents.
(2) Actual production may exceed production capacity of certain plants when excess capacity of other plants in the Aromatics units is utilized.
(3) Automotive gasoline in cubic meters per year.

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***Raw Materials of Our Basic Petrochemicals Unit***

*Naphtha*

Naphtha, a crude oil derivative, is the principal raw material that we use to produce our basic petrochemical products and represents the principal production and operating cost of our Basic Petrochemicals Unit. The price of naphtha that we purchase varies primarily based on changes in the U.S. dollar-based, international price of crude oil.

Both of our olefins plants are capable of using naphtha as a feedstock, and our Olefins 1 unit also uses petroleum condensate. Until the early 1980 s, gas oil represented approximately 60% of the feedstock used by first generation producers in Brazil and naphtha represented the remainder, but the increased use of diesel fuel by trucks and buses in Brazil in the 1980 s reduced the supply of gas oil available to petrochemical producers. Currently, we use naphtha as our primary feedstock, and in 2005, naphtha accounted for (1) 86.6% of the total cost of sales of our Basic Petrochemicals Unit and (2) 71.7% of our direct and indirect consolidated cost of sales and services rendered. However, due to the high price of naphtha, we have also used petroleum condensate as an alternative and more competitively priced feedstock. We have recently reduced our use of petroleum condensate while we evaluate the efficiency of the use of this feedstock in our plants.

The following table shows the average Amsterdam-Rotterdam-Antwerp market price of naphtha for the periods indicated.

| | **Amsterdam-Rotterdam-Antwerp market price of naphtha** | | | |
|---|---|---|---|---|
| **(in U.S. dollars per ton)** | **2006** | **2005** | **2004** | **2003** |
| Average(1) | US$ 539.48 | US$ 476.04 | US$ 377.40 | US$ 274.63 |
| Month ended: | | | | |
| January | 561.81 | 394.86 | 329.74 | 319.00 |
| February | 529.67 | 416.23 | 309.52 | 359.00 |
| March | 528.65 | 477.43 | 327.26 | 267.00 |
| April | 588.84 | 471.62 | 333.31 | 203.00 |
| May | 601.91 | 421.26 | 373.71 | 231.00 |
| June | | 439.32 | 350.16 | 254.00 |
| July | | 468.43 | 373.95 | 253.50 |
| August | | 528.00 | 420.40 | 269.00 |
| September | | 572.77 | 421.39 | 258.00 |
| October | | 545.43 | 469.14 | 275.00 |
| November | | 478.82 | 433.16 | 294.00 |
| December | | 498.35 | 387.05 | 313.00 |

(1) The information in the Average row represents the mean average of average monthly naphtha prices during the years presented.

*Source*: Bloomberg L.P.

Our Basic Petrochemicals Unit is located:

- 36 kilometers from the Madre de Deus Port Terminal (located in the City of Madre de Deus in the State of Bahia), a port terminal owned and operated by Petrobras;

- 27 kilometers from Refinaria Landulfo Alves (located in the State of Bahia), one of the largest refineries in Brazil, which is owned and operated by Petrobras; and

- 22 kilometers from the port terminal of Aratú (located in the State of Bahia).

We use the Madre de Deus Port Terminal to unload naphtha imported by Petrobras or that is shipped from other Petrobras refineries located outside the State of Bahia. A pipeline owned and operated by Petrobras transports naphtha from the Madre de Deus Terminal to Refinaria Landulfo Alves where it interconnects with the refinery s naphtha pipeline system. Refinaria Landulfo Alves naphtha pipeline system interconnects with the pipeline system of the port terminal of Aratú, through which naphtha and petroleum condensate are transported to our basic petrochemicals plants.

At the port terminal of Aratú, we use (1) the Terminal Químico de Aratú (which is owned by Terminal Químico de Aratú S.A. TEQUIMAR, a subsidiary of Ultrapar Participações S.A, a Brazilian LPG distribution company) to distribute our products in liquid form, (2) the Terminal de Gases (which is owned by Tegal Terminal de Gases Ltda., one of our subsidiaries) to distribute our products in gaseous form, and (3) the Raw Materials Terminal (which is owned by our company) to import naphtha and condensate.

Following the end of Petrobras monopoly over the supply of naphtha, we invested approximately US$39.2 million in our transportation infrastructure to enable our port facilities at Aratú to receive shipments of imported naphtha.

*Supply Contracts and Pricing*

Our Basic Petrochemicals Unit purchased:

- from Petrobras: approximately 3,084,000 tons of naphtha in 2005, representing 69.2% of our naphtha requirements; approximately 2,734,000 tons of naphtha in 2004, representing 62.3% of our naphtha requirements; and approximately 2,691,000 tons of naphtha in 2003, representing 68.8% of our naphtha requirements; and

- from suppliers located primarily in North Africa: approximately 1,372,500 tons of naphtha in 2005, representing 30.8% of our naphtha requirements; approximately 1,654,000 tons of naphtha in 2004, representing 37.7% of our naphtha requirements; and approximately 1,220,000 tons of naphtha in 2003, representing 31.2% of our naphtha requirements.

On June 22, 1978, we and Petrobras entered into a Naphtha and Gas Oil Purchase and Sale Contract (which was amended in February 1993, February 2003 and May 2005). This contract has a term of 10 years, expiring in 2008, and is automatically renewable for further 10-year periods, unless either party notifies the other party in writing at least one year prior to the expiration of the contract that it does not intend to renew the contract. Under this contract:

- Petrobras has agreed to sell and deliver naphtha and gas oil to our basic petrochemicals plants in the Northeastern Complex exclusively for our use as a raw material;

- we provide Petrobras with a firm commitment order for naphtha and fuel oil each month, together with an estimate of the volume of naphtha and fuel oil that we will purchase over the following six months;

- if we request to purchase volumes of naphtha and gas oil that exceed the minimum volumes we establish, Petrobras must use its best efforts to attempt to meet our higher demand;

- if we fail to purchase the minimum volumes that we establish for a given year, we are required to pay damages to Petrobras, and if Petrobras fails to deliver the minimum volumes, Petrobras is required to pay damages to us;

Petrobras may suspend deliveries, in whole or in part, or may terminate this contract without penalties if required by the National Petroleum Agency as a result of a national contingency plan that adversely affects the supply of petroleum derivatives in Brazil; and

Petrobras may rescind the contract, without prior notice, if: (1) we violate any provision of the contract; (2) we declare bankruptcy, or we are declared bankrupt or are liquidated; (3) we transfer all or part of our rights and obligations under the contract to a third party without Petrobras consent; or (4) we are involved in a reorganization or merger.

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Petrobras has provided us with a R$570.0 million credit line to purchase naphtha and gas oil that it produces.

On August 9, 2000, regulations issued by the National Petroleum Agency ended Petrobras monopoly over the supply of naphtha in Brazil. These regulations also established a policy of free negotiation of naphtha prices. After a series of negotiations, the Brazilian basic petrochemicals producers and Petrobras entered into a pricing agreement for naphtha sales. According to this agreement, the price of naphtha supplied by Petrobras is linked to the Amsterdam-Rotterdam-Antwerp market price for naphtha and to the *real*/U.S. dollar exchange rate.

La Société Nationale pour la Recherche, la Production, le Transport, la Transformation et la Commercialisation des Hydrocarbures SONATRACH (the Algerian national petroleum company), or SONATRACH, is our most important supplier of imported naphtha. We and SONATRACH entered into a Contract for the Sale and Purchase of Naphtha, which became effective on January 1, 2002. This contract has a one-year term and is renewable based on the mutual agreement of the parties for further one-year periods. We have renewed this contract three times, and are currently negotiating the fourth renewal of this contract for 2006. Under this contract:

- SONATRACH has agreed to sell and deliver naphtha to us exclusively for our use as a raw material; and
- we agreed to purchase, and SONATRACH agreed to sell, a minimum annual volume of naphtha up to a maximum annual volume.

On December 15, 2005, we entered into a purchase and sale agreement with Petróleos de Venezuela, S.A. (the Venezuelan national petroleum company), or PDVSA, which became effective on March 1, 2006. This contract has an initial six-month term and is renewable for one year, unless terminated by one of the parties. Under this agreement:

- PDVSA has agreed to sell naphtha to us for our use as a raw material; and
- we agreed to purchase, and PDVSA agreed to sell, a minimum monthly volume of naphtha with an option to purchase additional naphtha, subject to a monthly maximum volume.

If our contracts with SONATRACH or PDVSA are not renewed or are otherwise terminated, we believe that we could purchase sufficient quantities of naphtha from other suppliers, including Petrobras, to meet our supply needs.

On April 26, 2005, our company entered into an import note assignment agreement with certain financial institutions. Under this agreement, we issue short-term non-interest bearing promissory notes, or import notes, to designated trading companies outside Brazil (including our subsidiary Braskem Incorporated Limited) to evidence our obligation to pay for purchases of naphtha and petroleum condensate from these trading companies. These designated trading companies had the right through August 31, 2005 to assign up to an aggregate principal amount of US$150.0 million of these import notes to the financial institutions. These assignments were made at a discount based on a rate of LIBOR plus 1.00% per annum, and these companies could use the proceeds of these assignments to purchase imported naphtha or petroleum condensate or refinance existing obligations in respect of imported naphtha or petroleum condensate incurred within 90 days prior to the date of the assignment. The designated trading companies were required to pay participation and commitment fees to the financial institutions, which fees were deducted from the discounted purchase price of the import notes.

On December 15, 2005, our company entered into a revolving import note discount program with certain financial institutions. Under this program, our company and, subject to our guarantee of its obligations and certain other conditions, Copesul are permitted for three years to issue short-term non-interest bearing notes, or import notes, in an aggregate principal amount of up to US$400 million outstanding at any time prior to the expiration of this program to designated trading companies outside Brazil to evidence our and Copesul s respective obligation to pay for purchases of naphtha and petroleum condensate from these trading companies.

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These designated trading companies have the right to assign these import notes to the specified financial institutions during the term of the program. These assignments are made at a discount based on a rate of LIBOR plus 0.75% per annum during the first year of this program, and LIBOR plus 0.85% per annum to 1.25% per annum, based on fluctuations in the Emerging Markets Bond Index  Brazil, therafter. These companies may use the proceeds of these assignments to purchase imported naphtha or petroleum condensate. In the event that the aggregate amount of import notes issued during the first year of the program is less than US$30 million multiplied by the number of months elapsed under the program, we are required to pay a commitment fee on the unused amount. In addition, we are required to pay a commitment fee upon the termination of this program in the event that the aggregate amount of import notes outstanding at any time following the first anniversary of the commencement of this program is less than US$350 million.

***Technology of Our Basic Petrochemicals Unit***

We use engineering process technology from a variety of sources that we implemented in constructing or upgrading the manufacturing facilities of our Basic Petrochemicals Unit, including the following technology:

- ABB Lummus Global technology; technology developed jointly by CENPES (Petrobras) Research Center and TECHNIP; and technology developed by Linde AG, each of which we use in our olefins plants; and
- technology developed by Nippon Zeon, a Japanese petrochemical company, which we use in our butadiene plants.

These non-exclusive contracts generally provided for payment to those companies at stages specified in the contracts, but we do not pay ongoing royalties under these contracts.

We also use technology under non-exclusive arrangements from a variety of sources for specific production processes, including the following:

- Petroflex technology, which we use in our MTBE plants;
- technology developed by Japan Synthetic Rubber Company, which we use in our isoprene plant;
- technology developed by Universal Oil Products, or UOP, which we use in our sulfolane plants, our parex plant and our BTX fractionation plants; and
- technology licensed from Mobil, which we use in the conversion of toluene to benzene and xylenes.

Our Basic Petrochemicals Unit also uses technology developed by our company. We do not pay any continuing royalties under any of these arrangements, except for the technology licensing agreement with Mobil. We paid an initial royalty under these arrangements (excluding our agreement with Mobil). If any of these arrangements were terminated or no longer available to us, we believe that we would be able to replace this technology with comparable or better technology from other sources.

***Sales and Marketing of Our Basic Petrochemicals Unit***

We sell our basic petrochemical products principally in Brazil, mainly to second generation petrochemical producers located in the Northeastern Complex, as well as to customers in the United States and Europe. Our Basic Petrochemicals Unit also produces utilities for its own use and for sale to approximately 40 companies, including companies located outside of the Northeastern Complex.

As is common with other first generation petrochemical producers, our Basic Petrochemicals Unit has a high concentration of sales to a limited number of customers. Net sales to our 10 largest customers (excluding intra-company sales) accounted for approximately 64.5% of our Basic Petrochemicals Unit s total net sales revenue (excluding intra-company sales) during the year ended December 31, 2005.

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As part of our commercial strategy, our Basic Petrochemicals Unit has focused on developing longer-term relationships with our customers. We have entered into long-term supply contracts with several second generation producers located in the Northeastern Complex, including Oxiteno, Polibrasil Resinas S.A., or Polibrasil, and Petroflex. These supply contracts generally have an initial 10-year term and are automatically renewable for five-year periods unless one party notifies the other of its intention not to renew. These contracts also provide for minimum and maximum quantities to be purchased and monthly deliveries. We also sell automotive gasoline and LPG to Petrobras and fuel distribution companies.

We determine the prices for our olefins and aromatics products with reference to several market indicators. The price of ethylene that we charged our two largest customers, which represented 90.4% of our ethylene sales to third parties in 2005, was based on a margin sharing system. Under this system, the benefit or burden of higher or lower international market prices for naphtha and for ethylene derivatives, such as polyethylene, is shared with our customers. The margin shared by first and second generation producers is calculated for second generation products based on the market price charged by the second generation producer for its products and its production costs. The market price for ethylene is based on benchmark costs imputed to, and actual costs incurred by, both first and second generation producers for the production of second generation products. The variable-cost portion of these production costs reflects costs effectively incurred, while the fixed-cost portion of these production costs and depreciation expenses is determined based on benchmark costs. The benchmark costs are determined based on costs incurred by leading first and second generation producers located in the United States. This margin is then divided between the relevant first and second generation producers pro rata based on a return on capital invested by each such producer. Accordingly, the price of ethylene for these customers is calculated based on the weighted average price for ethylene obtained in the process of dividing the margin of each of these customers, taking into consideration the amount of ethylene consumed by each customer. The actual margins received by the first and second generation producers vary depending on the degree to which their actual costs compare with the benchmark costs used in the pricing formula to calculate the margin.

Prior to 2005, we used a margin sharing system for all of our ethylene customers, including our other business units. In 2005, we determined the prices that we charged our ethylene customers, other than our two largest ethylene customers, by reference to international market prices. In addition, we are negotiating with those ethylene customers which still use the margin sharing system to terminate the margin sharing system of ethylene pricing and to institute a market pricing system.

We calculate the monthly price of propylene by multiplying our monthly ethylene price (including Brazilian taxes) by the ratio of the European contract price for propylene to the European contract price for ethylene. We determine the price of butadiene and para-xylene by using the contract price for these products in the United States, and our prices for butadiene and para-xylene, unlike our prices for our other basic petrochemical products, include freight costs. We set the prices of benzene and ortho-xylene monthly by determining the mean average of European contract prices and U.S. contract prices for those products as set forth in specialized trade publications. We set the prices of solvents and fuels with reference to Brazilian market prices for these products. We set the prices of utilities based on our production costs.

We are focused on maintaining our leading position in the Brazilian market, while continuing to use our exports to hedge our operations and adjust the imbalances between demand and production. In 2005, export net sales of basic petrochemicals (which exclude utilities and automotive gasoline) represented 15% of our Basic Petrochemicals Unit s net sales revenue. We exported basic petrochemicals mainly to customers in the United States and in Europe.

The following table sets forth our export sales and export volumes of basic petrochemicals for the years indicated:

| | Year ended December 31, | | |
|---|---|---|---|
| | 2005 | 2004 | 2003 |
| Export sales (in millions of *reais*) | 950.0 | 778.9 | 490.7 |
| As % of total net sales revenue of Basic Petrochemicals Unit | 15.0 | 13.6 | 11.9 |
| Export volumes (thousands of tons) | 535.2 | 436.6 | 405.9 |
| As % of total sales volume of Basic Petrochemicals Unit (excluding automotive gasoline) | 17.6 | 14.9 | 15.1 |

Since August 15, 2000, we have been authorized by the National Petroleum Agency to produce and sell automotive gasoline. Our net sales revenue from automotive gasoline was R$412.9 million in 2005, and our net export sales revenue from automotive gasoline was R$109.9 million in 2005. We sold approximately 443,900 cubic meters of type A automotive gasoline in 2005.

We set export prices for:

- benzene, toluene, MTBE, dicyclopentadiene and automotive gasoline with reference to market prices prevailing in the U.S. Gulf market; and
- propylene, para-xylene, ortho-xylene, butene-l and isoprene with reference to market prices prevailing in the European market.

In addition to basic petrochemicals and fuels, we produce electric power, steam, treated water and compressed air for our own use and for sale to other second generation producers in the Northeastern Complex. In 2005, our net sales revenue from sales of utilities (including sales to our other business units) was R$491.8 million. We also provide storage services to companies located in the Northeastern Complex through our subsidiary Tegal Terminal de Gases Ltda., providing storage for gaseous petrochemical products. Tegal Terminal de Gases Ltda. operates in the port terminal of Aratú in the State of Bahia.

***Competition***

Although there are currently four major petrochemical complexes in Brazil, our basic petrochemical customers, which are mostly second generation petrochemical producers with plants located in the Northeastern Complex, would have difficulty obtaining their feedstocks from other sources at lower prices due to the high cost of transportation of these products, as well as other logistical difficulties. In addition, because Brazil produces sufficient quantities of olefins to meet domestic demand, imports of these products are generally sporadic and usually related to scheduled plant maintenance shutdowns or to meet unsatisfied domestic demand, as is the case with imports of para-xylene.

**Polyolefins Unit**

At December 31, 2005, our polyolefins production facilities had the largest average annual production capacity of all second generation producers of polyolefins products in Brazil and elsewhere in Latin America. Our Polyolefins Unit accounted for R$3,919.0 million, or 29.0%, of the net sales revenue of all segments in 2005. Our Polyolefins Unit has historically been comprised of the operations conducted by our company and Polialden. On May 31, 2006, Polialden merged with and into our company.

Prior to the Politeno acquisition on April 6, 2006, we owned 35.0% of Politeno s voting share capital and 34.0% of its total share capital. As a result, at dates and for periods prior to April 6, 2006, we proportionally consolidated Politenos results in our consolidated financial statements and did not include Politeno s results in

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our Polyolefins segment. As a result of the Politeno acquisition on April 6, 2006, we now own 100% of the voting share capital and 96.2% of the total share capital of Politeno, and will fully consolidate Politeno s results in our consolidated financial statements and include Politeno s results in our Polyolefins segment at dates and for periods following this acquisition.

Our Polyolefins Unit produces:

- polyethylene, including LDPE, LLDPE, HDPE, UHMWP and, following the Politeno acquisition, ethyl vinyl acetate copolymer, or EVA; and
- polypropylene.

Approximately three-fifths of our Polyolefins Unit s sales volume in 2005 was derived from the sale of polyethylene products, and most of the remainder was derived from the sale of polypropylene products.

We manufacture a broad range of polyolefins products for use in consumer and industrial applications, including:

- plastic films for food and industrial packaging;
- bottles, shopping bags and other consumer goods containers;
- automotive parts; and
- household appliances.

In 2005, we had an approximate 30% share of the Brazilian polyethylene market and an approximate 42% share of the Brazilian polypropylene market, based on sales volumes. We anticipate that domestic growth in demand for these products will continue to increase due to:

- greater consumption of plastic-based consumer products, as Brazil s consumption of plastic-based products on a per-capita basis is low when compared to the United States and many European countries; and
- the trend towards substitution of plastics for more traditional packaging materials, such as glass and paper.

***Products of Our Polyolefins Unit***

The following table sets forth a breakdown of the sales volume and net sales revenue of our Polyolefins Unit by product line and by market for the years indicated.

| | Year ended December 31, | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2005 | | | 2004 | | | 2003 | | |
| | Quantities sold | Net sales revenue | | Quantities sold | Net sales revenue | | Quantities sold | Net sales revenue | |
| | (thousands of tons) | (millions of *reais*) | (%) | (thousands of tons) | (millions of *reais*) | (%) | (thousands of tons) | (millions of *reais*) | (%) |
| Domestic net sales: | | | | | | | | | |
| Polypropylene | 419.9 | R$ 1,404.2 | 35.8% | 418.5 | R$ 1,320.3 | 37.8% | 374.9 | R$ 1,008.0 | 29.8% |
| LDPE | 143.1 | 443.7 | 11.3 | 134.7 | 404.2 | 11.6 | 120.4 | 314.9 | 9.3 |
| LLDPE | 156.2 | 476.4 | 12.2 | 148.6 | 444.4 | 12.7 | 119.8 | 311.0 | 9.2 |
| HDPE | 201.9 | 618.1 | 15.8 | 214.1 | 635.5 | 18.2 | 204.6 | 515.0 | 15.2 |
| UHMWP | 1.0 | 5.1 | 0.1 | 1.4 | 5.7 | 0.3 | 1.2 | 4.2 | 0.1 |
| Total domestic net sales | 922.1 | 2,947.5 | 75.2 | 917.3 | 2,810.1 | 80.6 | 820.9 | 2,153.1 | 63.6 |
| Total export net sales | 363.6 | 971.5 | 24.8 | 248.3 | 679.3 | 19.4 | 288.1 | 1,233.7 | 36.4 |
| Total polyolefins net sales | 1,285.7 | R$ 3,919.0 | 100% | 1,165.6 | R$ 3,489.4 | 100% | 1,109.0 | R$ 3,386.8 | 100% |
| % of the total net sales revenue of all segments | | | 29.0% | | | 28.0% | | | 33.9% |

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We provide technical assistance to our customers to meet their specific needs by adapting and modifying our polyethylene and polypropylene products. In particular, we develop customized value-added polypropylene compounds for use by our customers in their specialized applications. We believe that the variety of technological processes at our polyolefins plants provides us with a competitive advantage in meeting our customers needs.

*Polyethylene Products*

Polyethylene has the simplest chemical structure of all commercial polymers and is a very versatile material. Global production volume of polyethylene is the highest among all commercial plastics. Polyethylene is used to manufacture a wide variety of products.

Our customers purchase different polyethylene resins depending on the manufacturing process that they employ and the desired physical characteristics of the end products that they manufacture. LDPE is the most flexible of polyethylene products and is used in a variety of plastic or film applications and in food packaging, trash bags and shopping bags. LLDPE is used in applications that require greater sealing capacity and better mechanical resistance, including plastic films and flexible food packaging. HDPE is used for applications that require higher mechanical resistance. UHMWP is used mainly for technical parts and other applications that require greater mechanical resistance. EVA is used in applications that require greater sealing capacity, flexibility, impact resistance and color adherence, including shoe soles, hot melt and film for special applications.

While each form of polyethylene is used for different applications, there is some overlap in the uses of these resins, and with certain modifications, polyethylene resins may be substituted for each other in certain end product manufacturing processes. For example, demand for LLDPE has grown since it was first introduced in 1989 and has resulted in reduced demand for LDPE, as manufacturers of certain containers and plastic film applications have switched their production processes and technology to use LLDPE in a blend with LDPE. We expect that part of the consumption of LDPE will be substituted in the packaging segment over the next few years by LLDPE. As a result, we believe that consumption growth of LLDPE will continue to be strong, while consumption growth of LDPE should be moderate.

*Polypropylene Products*

Polypropylene is a versatile polymer with a high strength-to-weight ratio. This thermoplastic resin may be manufactured with a variety of properties that permit its use in different processes, such as injection, extrusion, blow molding and thermoforming. Through these processes, polypropylene may be used as a primary raw material for many applications, including the manufacture of carpet fibers, non-woven fabrics for diapers, injection molded parts for durable packaging and automobiles, medical instruments, flexible packaging for candy, pasta and cookies, as well as bottles for beverages. The balance between the mechanical properties and the high thermal resistance of polypropylene is a primary reason why this thermoplastic resin has begun to replace engineering materials such as acrylonitrile-butadiene-styrene (known as ABS), polycarbonate and nylon in domestic appliances and machinery. The lack of toxicity and high chemical resistance of polypropylene permits it to be used in applications with strict sanitary specifications, including in the food and pharmaceutical industries.

In 2004, we launched Braskem Symbios®, a high-performance flexible packaging sealant. We introduced advances in the use of polypropylene containers as a substitute for glass containers for spreadable cream cheese and launched a polypropylene fiber used to manufacture tiles and fiber-cement water cisterns. We also developed a new resin and patent-protected equipment for the production of disposable polypropylene cups, which have a significant competitive advantage over the same product made from polystyrene. We have licensed this technology to one of our customers. Finally, we introduced a new polypropylene resin for use as a substitute for glass and paper in packaging non-carbonated beverages.

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***Production Facilities of Our Polyolefins Unit***

At December 31, 2005, we owned seven polyolefins production facilities. Five of these plants are located in the Southern Complex, and two of these plants are located in the Northeastern Complex. During 2004, we expanded the annual production capacity of our polypropylene plants in the Southern Complex by an aggregate of 100,000 tons. During 2005, we expanded the annual production capacity of one of our polyethylene plants in the Northeastern Complex by 30,000 tons.

The table below sets forth the location, the primary products, annual production capacity at December 31, 2005, and annual production for the years presented of each of our polyolefins plants.

| | | | Production year ended December 31, | | |
|---|---|---|---|---|---|
| **Location (Complex)** | **Primary products** | **Annual production capacity** | **2005** | **2004** | **2003** |
| | | **(in tons)** | | **(in tons)** | |
| Triunfo (Southern) | LDPE | 215,000 | 207,174 | 209,140 | 195,637 |
| | Polypropylene(1) | 100,000 | | | |
| | Polypropylene(2) | 560,000 | 528,980 | 463,077 | 438,746 |
| | HDPE/LLDPE(3) | 265,000 | 237,262 | 235,028 | 229,237 |
| Camaçari (Northeastern) | HDPE/LLDPE(3) | 210,000 | 211,625 | 175,436 | 152,087 |
| | HDPE/UHMWP | 144,000 | 124,382 | 128,312 | 99,720 |

(1) This plant is currently inactive.
(2) Reflects the combined production capacity and annual production of two polypropylene plants located in the Southern Complex.
(3) Plant with swing line capable of producing two types of resins. Capacity varies depending on actual production.

As a result of the Politeno acquisition, we now own 96.2% of the total share capital of Politeno, representing 100% of its voting share capital. Politeno owns an LPDE plant in the Northeastern Complex with an annual production capacity of 150,000 tons and a plant with a swing line with a combined annual production capacity of 210,000 tons of LLDPE and HDPE.

***Raw Materials of Our Polyolefins Unit***

*Ethylene and Propylene*

The most significant direct costs associated with our production of polyethylene and polypropylene are the costs of purchasing ethylene and propylene, which together accounted for approximately 90% of our Polyolefins Unit s total variable cost of sales in 2005. In 2005, approximately 35% of these raw materials were supplied by our Basic Petrochemicals Unit and approximately 65% were supplied by Copesul. Our Polyolefins Unit is highly dependent on ethylene and propylene supplied by our Basic Petrochemicals Unit and by Copesul because the costs of storing and transporting ethylene and propylene are substantial and there is inadequate infrastructure in Brazil to import large quantities of ethylene and propylene.

At December 31, 2005, Copesul had an annual ethylene production capacity of 1,135,000 tons and an annual propylene production capacity of 581,000 tons. Copesul is our main supplier of propylene.

*Supply Contracts and Pricing*

We have entered into a long-term ethylene and propylene supply contract with Copesul that extends through 2007 and is automatically renewable for additional five-year terms. We own 29.5% of the total share capital of Copesul. Under this contract, we are required to purchase an annual minimum of 268,200 tons of ethylene and an annual maximum of 451,000 tons, as well as an annual minimum of 262,200 tons of propylene and an annual maximum of 439,500 tons, in each case subject to daily and monthly limits. In 2005, we purchased 426,500 tons of ethylene and substantially all of our requirements of propylene (approximately 445,000 tons) from Copesul for our polyolefins operations in the Southern Complex. In 2005, we exceeded our annual maximum propylene purchases as a result of production efficiencies at Copesul.

We negotiate the prices for the feedstocks for our polyolefins products with Copesul, based upon a pricing formula developed by the Brazilian petrochemical industry. The pricing formula provides for full cost margin sharing between the first generation and second generation petrochemical producers located at the respective petrochemical complexes. The prices Copesul charges for ethylene that it supplies to our Polyolefins Unit are calculated based on a formula similar to the formula that our Basic Petrochemicals Unit uses to determine prices for its two largest ethylene customers. See Basic Petrochemicals Unit Sales and Marketing of Our Basic Petrochemicals Unit. Our Polyolefins Unit purchases ethylene from our Basic Petrochemicals Unit at prices determined by reference to international market prices for ethylene.

The following table sets forth the average prices per ton in reais paid by our company for ethylene and propylene for the years indicated:

| | Year ended December 31, | | |
|---|---|---|---|
| **(R$ per ton)** | **2005** | **2004** | **2003** |
| Ethylene supplied by our Basic Petrochemicals Unit | R$ 2,206 | R$ 2,350 | R$ 1,786 |
| Ethylene supplied by Copesul | 2,527 | 2,313 | 1,769 |
| Propylene supplied by Copesul | 2,405 | 2,017 | 1,608 |

We also use butene and hexene as raw materials in the production of LLDPE. Butene is supplied by Copesul and by our Basic Petrochemicals Unit, and we import hexene from suppliers located in South Africa.

*Other Materials*

In addition to overhead costs such as labor and maintenance, our other costs associated with the production of polyethylene and polypropylene include our purchase of chemical catalysts, solvents and utilities, such as electric power, water, steam and nitrogen.

Our Unipol® Plant in the Northeastern Complex uses catalysts supplied to us by Univation Technologies under a license that expires in 2007. Our HDPE slurry plant in the Northeastern Complex produces its own catalysts, and we purchase the inputs that we need to produce our own catalysts from various suppliers at market prices. We purchase most of the catalysts that we use in our polypropylene plants from Basell Polyolefins Company N.V, or Basell, and we also import some catalysts from suppliers in the United States and Europe.

Our Basic Petrochemicals Unit supplies our Polyolefins Unit s facilities in the Northeastern Complex with steam and water, and Copesul supplies these utilities to our Polyolefins Unit s facilities in the Southern Complex. In addition, we purchase electric power at both complexes from third parties pursuant to long-term power purchase agreements and, in the Northeastern Complex, from our Basic Petrochemicals Unit. Our polyolefins plants in the Northeastern Complex are able to purchase electric power from alternative sources if our Basic Petrochemicals Unit is unable to meet our total demand for electric power. In general, we believe that there are sufficient alternative sources available at reasonable prices for each of these other inputs used in our polyolefins production process such that the loss of any single supplier would not have a material adverse effect on our operations.

***Technology of Our Polyolefins Unit***

*Rights to Use technology*

We have entered into several non-exclusive agreements with a number of leading petrochemical companies to use certain technology and catalysts for our Polyolefins Unit.

We obtained technology from Mitsubishi in 1978, under a licensing agreement we continue to use in our HDPE slurry plant in the Northeastern Complex. Although this technology is our oldest, we have

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regularly upgraded and improved it, and we use this technology to produce UHMWP in this plant. We have fully paid all royalties due under the terms of our license agreement with Mitsubishi and are no longer subject to the confidentiality provisions of this agreement.

We entered into an agreement with a predecessor of Univation Technologies in 1988 (effective in 1992) to use Unipol® technology to produce polyethylene. We made a lump sum payment at the time of execution of this license agreement, in lieu of additional royalty payments. We use the Unipol® technology to produce low density polyethylene and high density polyethylene in the Northeastern Complex.

We entered into agreements with Basell Technology Company B.V., the largest polypropylene manufacturer in the world and a leader in polypropylene technology, in 1987 (effective in 1991) to use Spheripol® technology for the construction and operation of our first polypropylene plant in the Southern Complex. Under these agreements, we may use this technology for our current and future plants. We built a second plant based on this technology, which commenced operations in 1997. We have fully paid all royalties due under the terms of these license agreements.

We entered into agreements with Basell Polyolefine GmbH in 1995 (effective in 1999) to use Spherilene® technology. We pay royalties on a quarterly basis under these license agreements based on the amounts of polyethylene that we produce using this technology at our swing HDPE/ LLDPE plant located at the Southern Complex.

We entered into an agreement with Univation Technologies in 2003 to use metallocene process and product technology and related catalysts. We pay quarterly royalties based on amounts of LLDPE and very low density polyethylene that we produce using metallocene technology at our Unipol® polyethylene plant located at the Northeastern Complex.

We entered into an agreement with Basell Polyolefine Italia S.p.A. in 2004 to use an updated Spheripol® technology for the construction and operation of the Paulínia polypropylene plant. Under this agreement, we may use this technology for our existing and future plants.

Politeno entered into an agreement with Sumitomo in 1974 to use a high pressure autoclave process to produce LDPE and ethyl vinyl acetate copolymer at a plant in the Northeastern Complex. Politeno has fully paid all royalties due under the terms of this license agreement.

Politeno entered into an agreement with Du Pont Canada, now Nova Chemicals, in 1987 to use Sclairtech technology to produce LLDPE and HDPE at a plant in the Northeastern Complex. Politeno has fully paid all royalties due under the terms of this license agreement.

If any of these licenses were terminated, we believe that we would be able to replace the relevant technology with comparable technology from other sources.

*Research and Development*

Our Polyolefins Unit coordinates and maintains a research and development program, which includes (1) the Braskem Center for Technology and Innovation, (2) pilot plants, (3) catalysis, polymerization and polymer sciences laboratories, and (4) process engineering and automation centers.

The Braskem Center for Technology and Innovation at the Southern Complex includes a staff of approximately 160 employees, which seek to:

- develop new products and applications in response to our customers requirements;
- upgrade or improve the properties and processability of our products;
- identify new product market opportunities;
- implement improvements in our production processes and reduce our operating costs; and
- expand and optimize the capacity and the flexibility of production at our plants.

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We have developed most of our new polyolefins products and applications at the Braskem Center for Technology and Innovation, including Braskem Flexus® and Braskem Symbios® in 2004. Prior to the development of these products at the Braskem Center for Technology and Innovation, these products were only available in Brazil through imports.

Our Polyolefins Unit maintains seven pilot plants located in the Southern Complex and the Northeastern Complex that use Spheripol®, Spherilene® and Unipol® technology. Two of our Polyolefins Unit pilot plants operate at approximately 1/150 of the scale of our full-scale plants, and our other pilot plants operate at approximately 1/400 of the scale of our full-scale plants. Our Polyolefins Unit uses these pilot plants to (1) produce small quantities of new products to test them in our laboratories and with our customers, (2) develop new conditions and formulations for the creation of new products, and (3) increase the efficiency of our production processes. We believe that these pilot plants give us a competitive advantage over our competitors in Latin America, which do not have similar resources.

Our Polyolefins Unit maintains catalysis, polymerization and polymer sciences laboratories in the Southern Complex and the Northeastern Complex. These laboratories enable us to identify new and to improve existing licensed catalysts. We have developed or improved upon a majority of the polyethylene and polypropylene grades that we sell based on technology that we have created or improved.

Our Polyolefins Unit maintains process engineering and automation centers in the Southern Complex and the Northeastern Complex. These centers assist us in developing advanced process control technology, reducing our variable costs, achieving operational stability and increasing our production of polyolefins.

Our Polyolefins Unit is in regular contact with international process technology licensors to acquire new technologies and improvements. We test new processes on a regular basis, and we follow advances and trends in the petrochemical industry through our relationships with Brazilian and international research universities and consortia. In addition, we maintain ongoing contracts with licensors that permit us to upgrade our technology in order to receive and install improvements developed for our existing processes.

*Sales and Marketing of Our Polyolefins Unit*

We sell our polyethylene and polypropylene products to approximately 1,100 customers, and sales by our Polyolefins Unit accounted for 29.0% of our net sales revenue of all segments in 2005. We have a diversified product mix that allows us to serve a broad range of end users in several industries. Our customers generally are third generation petrochemical producers that manufacture a wide variety of plastic-based consumer and industrial goods.

Net sales revenue to our ten largest customers accounted for 31.0% of our Polyolefins Unit s total net sales revenue during the year ended December 31, 2005. No customer accounted for more than 6.0% of our total net sales revenue during 2005, 2004 or 2003.

*Domestic Sales*

We are focused on developing longer-term relationships with our customers. Given the cyclical nature of the markets for our petrochemical products, we believe that we can strengthen customer loyalty during periods of reduced demand for polyethylene or polypropylene by providing a reliable source of supply to these customers during periods of high demand. We work closely with our customers to determine their needs, to provide technical assistance and to coordinate the production and delivery of our products. Customers submit annual proposals giving their estimated monthly requirements for the upcoming year for each of our polyolefins products, including technical specifications, delivery terms and proposed payment conditions. We evaluate these proposals on a monthly basis to make any required adjustments and to monitor and attempt to ensure adequate supply for each customer.

In addition to direct sales to our customers, our Polyolefins Unit sells our products in Brazil through exclusive independent distributors. These distributors sell our polyethylene and polypropylene products to manufacturers with lower production requirements and are able to aggregate multiple orders for production and delivery to customers that would otherwise be uneconomical for us to serve. Furthermore, by serving smaller customers through a network of distributors, account managers in our Polyolefins Unit focus their efforts on delivering high quality service to a smaller number of large, direct customers. We have selected our distributors based on their ability to provide full service to their customers, including the ability to prepare our products on a customized basis.

In 2005, our Polyolefins Unit concluded the implementation of its new policy concerning distributors, and our distribution network was reorganized. We now have eight distributors (three of which belong to a group of related companies), and have entered into agreements with terms of five years with five of these distributors.

*Export Sales*

Our volume of export sales has generally varied based upon the level of domestic demand for our products. Export sales represented 24.8% of our Polyolefins Unit s net sales revenue in 2005. Our primary export market for polyolefins is other countries in South America, particularly the Mercosul countries, and we intend to increase our export sales in the Mercosul countries as well as in Chile. We have established a strategic position in the Southern Cone countries through regular sales to local distributors and agents who understand their respective markets. Our strategy to increase our presence in the Southern Cone is intended, among other things, to reduce our exposure to the cyclicality of the international spot market for polyolefins through the development of long-term relationships with customers in neighboring countries.

The following table sets forth export sales and export volumes of our Polyolefins Unit for the years indicated.

| | **Year ended December 31,** | | |
|---|---|---|---|
| | **2005** | **2004** | **2003** |
| Net export sales revenue (in millions of *reais*) | 971.5 | 678.6 | 1,233.7 |
| As % of total net sales revenue of Polyolefins Unit | 24.8 | 19.4 | 36.4 |
| Export volumes (thousands of tons) | 363.6 | 248.5 | 288.1 |
| As % of total production of Polyolefins Unit | 28.3 | 21.3 | 26.0 |

The main focus of our Polyolefins Unit is to maintain our leading position in the Brazilian market while continuing to export in order to manage the relationship between our production capacity and domestic demand for our products. Currently, we target an annual average production that is approximately 20% in excess of anticipated Brazilian market demand in order to meet variations in local demand and to respond to production fluctuations, seasonality and export product sales. As a result, we believe that our continued presence in export markets is essential to help manage any overcapacity in the Brazilian market and to maintain our position as leader in the supply of polyolefins in South America.

*Prices and Sales Terms*

We determine the prices for our polyethylene and polypropylene products with reference to international market prices. Our customers in Brazil may pay in full on delivery or elect credit terms that require payment in full within 14 to 63 days following delivery. We charge interest based on prevailing market rates to our Brazilian customers that elect to pay on credit.

We generally conduct our export sales to buyers in countries outside the Southern Cone through the international spot market. Our customer base in these markets consists primarily of trading houses and distributors, most of which have operations in Europe, the United States or in Asia, principally Hong Kong.

Pricing is based on international spot market prices. We make all sales in these markets with letters of credit. Export prices for polyolefins sales in the Southern Cone countries are based on regional prices and sales are generally made either with letters of credit or through direct bank collections.

*Competition*

We compete with regional polyolefins producers located in Brazil and Argentina and, to a lesser extent, with other importers of these products. In the Brazilian polyethylene market, we compete with a number of companies that produce one or two of the products in our production line. LDPE is produced in Brazil by Polietilenos União with an annual production capacity of 130,000 tons, Dow Brasil S.A. with 144,000 tons and, Petroquímica Triunfo S.A. with 160,000 tons, compared to our annual production capacity of 365,000 tons.

In the HDPE and LLDPE markets, we compete with the following producers in Brazil:

- Rio Polímeros, with a maximum annual production capacity of 540,000 tons of LLDPE and HDPE;
- Ipiranga Petroquímica S.A., or Ipiranga, with a plant with a swing line with a combined annual production capacity of 150,000 tons of LLDPE and HDPE and another plant with an annual production capacity of 400,000 tons of HDPE; and
- Solvay, with an annual capacity of 150,000 tons of HDPE.

We have (1) a combined annual production capacity of 695,000 tons at three swing line plants capable of producing LLDPE and HDPE, one of which is located in the Southern Complex and two of which are located in the Northeastern Complex and (2) an additional 144,000 tons of annual production capacity of HDPE and UHMWP at another plant in the Northeastern Complex. We are currently expanding the production capacity of one of our HDPE plants in the Northeastern Complex by an aggregate amount of 30,000 tons annually through efficiency enhancements. See Capital Expenditures.

In the Brazilian polypropylene market, we compete with Ipiranga and Suzano Petroquímica S.A., or Suzano. Ipiranga has annual production capacity of 150,000 tons and Suzano has annual production capacity of 625,000 tons, compared to our annual production capacity of 660,000 tons.

We do not have any domestic competitors in the Brazilian UHMWP market. Internationally, our primary competitor in this market is Ticona, which is a member of the Celanese Group, a German chemical company that has approximately 52% of the worldwide production capacity of UHMWP.

Traditionally, we have not faced substantial competition from imports of polyethylene and polypropylene due to tariff rates, transportation costs for imported products and other factors relating primarily to the logistics involved in importing these products. In 2005, imports of polyethylene into Brazil represented 17.8% of Brazil s total consumption of polyethylene, and imports of polypropylene into Brazil represented 8.6% of Brazil s total consumption of polypropylene. We expect competition from international producers to increase substantially in selected foreign markets in which we intend to attempt to increase our sales of polyolefins products.

**Vinyls Unit**

We are the leading producer of PVC in Brazil, based on sales volumes in 2005. At December 31, 2005, our PVC production facilities had the largest average annual production capacity in Latin America. Our Vinyls Unit accounted for R$1,794.1 million, or 13.3%, of our net sales revenue of all segments in 2005.

Our Vinyls Unit is the only vertically integrated producer of PVC in Brazil. Our PVC production is integrated through our production of chlorine and other raw materials. Our Vinyls Unit also manufactures caustic soda, which is used by producers of aluminum and paper; ethylyne dichloride, or EDC; and chlorine, which we use to manufacture EDC. In 2005, 64.5% of our Vinyls Unit s net sales revenue was derived from the sale of PVC products, 25.5% was derived from the sale of caustic soda and 5.4% from the sale of EDC and the remainder from the sale of other products.

In 2005, we had an approximate 55% share of the Brazilian PVC market, based on sales volumes.

***Products of Our Vinyls Unit***

The following table sets forth a breakdown of the sales volume and net sales revenue of our Vinyls Unit by product line and by market for the years indicated.

| | Years ended December 31, | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2005 | | | 2004 | | | 2003 | | |
| | Quantities sold | Net sales revenue | | Quantities sold | Net sales revenue | | Quantities sold | Net sales revenue | |
| | (thousands of tons) | (millions of *reais*) | (%) | (thousands of tons) | (millions of *reais*) | (%) | (thousands of tons) | (millions of *reais*) | (%) |
| Domestic sales: | | | | | | | | | |
| PVC suspension | 360.4 | R$ 959.9 | 53.5% | 372.4 | R$ 1,116.8 | 60.1% | 323.6 | R$ 756.5 | 55.1% |
| PVC emulsion | 18.5 | 81.0 | 4.5 | 22.0 | 82.8 | 4.4 | 18.8 | 61.7 | 4.5 |
| Caustic soda | 455.6 | 449.4 | 25.1 | 444.0 | 342.1 | 18.4 | 426.6 | 290.4 | 21.2 |
| Other(1) | 125.3 | 82.9 | 4.6 | 134.0 | 60.9 | 3.3 | 126.0 | 59.5 | 4.3 |
| Total domestic sales | 959.8 | 1,573.2 | 87.7 | 972.4 | 1,602.6 | 86.2 | 895.0 | 1,168.1 | 85.2 |
| Total exports | 194.3 | 220.9 | 12.3 | 191.0 | 256.2 | 13.8 | 215.6 | 203.7 | 14.8 |
| Total vinyl net sales | 1,154.1 | R$ 1,794.1 | 100% | 1,163.3 | R$ 1,858.8 | 100% | 1,110.6 | R$ 1,371.8 | 100% |
| % of the total net sales revenue of all segments | | | 13.3% | | | 14.9% | | | 13.7% |

(1) Includes chlorine, hydrogen, caustic soda flake and sodium hypochlorite.

*PVC*

PVC is a versatile polymer, and global production volume of PVC is the second highest among all commercial plastics. We produce suspension and paste PVC in various grades, which are sold in various sized bags or in bulk to third generation producers and transported by truck, rail or, in some cases, ship.

Approximately 95% of our PVC production is in the form of suspension PVC. The grades of PVC produced by the suspension production process are the most widely used, including for use in the manufacture of pipes and fittings, laminated products, shoes, sheeting, flooring, cable insulation, electrical conduit, packaging and medical applications. The grades of paste PVC are more specialized products and are used in the manufacture of toys, synthetic leather, flooring materials, bottle caps and seals, automobile corrosion prevention treatments and wallpaper coatings.

Our Vinyls Unit also produces EDC, the principal feedstock used in the production of PVC. We used approximately 72% of our EDC production in 2005 for further processing into PVC and exported the remainder to Asia.

In 2004, we launched Plastwood, a product made of PVC and wood for finishing ceilings and special patio decks, in partnership with one of our customers in Brazil. We also developed new PVC applications for the Brazilian construction sector, such as prefabricated house and window frame solutions. In 2005, we launched Vinisol, a paste PVC product for the export market with applications for special paints and varnishes.

*Caustic Soda and Chlorine*

Our Vinyls Unit also produces caustic soda and chlorine. Caustic soda is a basic commodity chemical that is sold to producers of aluminum, pulp and paper, petrochemicals and other chemicals, soaps and detergents and to

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waste treatment plants. Caustic soda is also used in the textile industry to make fabrics more absorbent and to improve the strength of dyes, as well as in food processing and electroplating. We sell to third parties almost all of the caustic soda that our Vinyls Unit produces and consume only approximately 6% of our caustic soda production.

Chlorine is a basic chemical commodity that is used in a large variety of industries, including applications in water treatment and chemical and pharmaceutical production. We consume approximately 80% of our chlorine production in our production of EDC and sell most of our remaining chlorine to a company located in the Northeastern Complex that is connected to one of our plants via a specialized pipeline.

***Production Facilities of Our Vinyls Unit***

We own five vinyls production facilities. Two of our facilities are located in the Northeastern Complex, and two others are located in the State of Alagoas. Our fifth facility is located in the City of São Paulo. In December 2005, we expanded the annual production capacity of our PVC plant in Alagoas by 50,000 tons. The following table sets forth the name and location, primary products, annual production capacity at December 31, 2005, and annual production for the years presented for each of our vinyls plants.

| Location (Complex) | Primary products | Annual production capacity | Production year ended December 31, 2005 | 2004 | 2003 |
|---|---|---|---|---|---|
| | | (in tons) | | (in tons) | |
| Camaçari (Northeastern) | PVC | 250,000 | 225,563 | 206,978 | 181,780 |
| Camaçari (Northeastern) | Caustic Soda | 73,000 | 76,219 | 76,517 | 72,458 |
| | Chlorine | 64,000 | 66,587 | 66,644 | 63,857 |
| Maceió (Alagoas) | Caustic Soda | 460,000 | 419,673 | 416,100 | 386,967 |
| | Chlorine | 400,000 | 387,510 | 381,464 | 360,677 |
| | EDC | 520,000 | 499,256 | 495,827 | 475,024 |
| Marechal Deodoro (Alagoas) | PVC | 240,000 | 198,125 | 189,810 | 193,150 |
| Vila Prudente (São Paulo) | PVC | 26,000 | 23,689 | 24,830 | 21,897 |

***Raw materials of Our Vinyls Unit***

*Ethylene*

The most significant direct cost associated with the production of PVC and EDC is the cost of ethylene, which accounted for 68.1% of our variable cost of PVC sales in 2005 and 80.9% of our EDC sales in 2005. Our Basic Petrochemical Unit supplies all of the ethylene required by our Vinyls Unit. Ethylene is delivered to our Alagoas plant via a 477 kilometer pipeline that we own, and to our PVC plant in the Northeastern Complex via a separate pipeline. Because the cost of storing and transporting ethylene is substantial and there is inadequate infrastructure in Brazil to permit the importation of large quantities of ethylene, our Vinyls Unit is highly dependent on ethylene that is supplied by our Basic Petrochemicals Unit. For a description of the pricing of ethylene purchased by our Vinyls Unit from our Basic Petrochemicals Unit, see Basic Petrochemicals Unit Sales and Marketing of Our Basic Petrochemicals Unit. Our São Paulo plant receives vinylchloride monomer (a raw material used in manufacturing PVC) by ship from our plant in the Northeastern Complex.

*Electric Power*

Electric power is a significant cost component in our production of chlorine and caustic soda. Electric power accounted for 69.4% of our Vinyls Unit s cost of caustic soda sales in 2005 and 17.9% of our Vinyls Unit s total cost of sales in 2005. Our Vinyls Unit obtains its electric power requirements from various generators under long-term power purchase agreements. Our caustic soda plants at Camaçari and Alagoas and our PVC plant at Camaçari purchase their electric power requirements from CHESF under a long-term contract that expires in 2010. Companhia Energética de Alagoas S.A., or CEAL, distributes electric power to our PVC plant in Alagoas. Our São Paulo plant obtains its electric power from Eletropaulo Metropolitana-Eletricidade de São Paulo S.A., or

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Eletropaulo. The power purchase agreements with CEAL and Eletropaulo are renewable contracts with automatic rolling three-year extensions. These agreements provide us with the option to purchase our total electric power requirements based on an annual estimate. The price terms of these contracts are based upon tariffs regulated by the Brazilian National Electrical Energy Agency (Agência Nacional de Energia Elétrica).

*Salt*

We used approximately 853,000 tons of salt during 2005 in our production of chlorine and caustic soda. Salt accounted for 4.7% of our variable costs of caustic soda sales in 2005 and 1.0% of our Vinyls Unit s total cost of sales in 2005. We have exclusive salt exploration rights at a salt mine located near our Alagoas plant. We estimate that the salt reserves of this mine are sufficient to allow us to produce chlorine at expected rates of production for approximately 40 to 50 years. We enjoy significant cost advantages when compared to certain of our competitors due to low extraction costs of rock salt (particularly compared to sea salt), low transportation costs due to the proximity of the salt mine to our production facility and the higher purity of rock salt as compared to sea salt.

*Other Utilities*

All of our Vinyls Unit s facilities in the Northeastern Complex are supplied with other required basic utilities, including steam, purified and demineralized water, compressed air and nitrogen, by our Basic Petrochemicals Unit. Most basic utilities are supplied to our Alagoas PVC plant by our subsidiary, Companhia Alagoas Industrial. Our chlorine and caustic soda plants in Alagoas and our PVC plant in São Paulo supply their own utilities requirements.

*Technology of Our Vinyls Unit*

We have entered into several non-exclusive agreements with a number of leading petrochemical companies to use technology for our Vinyls Unit. We have been granted the right to use vinylchloride monomer manufacturing technology from Oxyvinyls Company and PVC technology from Mitsubishi. We also have chlorine manufacturing technology agreements with Denora (used in Bahia), Eltech (used in Alagoas) and EVC (used to produce ethylene dichloride in Alagoas). In addition, we own 25 patents and six trademarks in Brazil related to our PVC business.

We do not pay any continuing royalties under any of these license agreements, but we paid an initial fee under these agreements. If any of these arrangements were terminated or no longer available to us, we believe that we would be able to replace the relevant technology with comparable or better technology from other sources.

Our plant in the Northeastern Complex uses mercury cell technology to produce chlorine, which technology can no longer be used in new petrochemical production facilities under Brazilian legislation due in part to environmental concerns regarding mercury emissions resulting from this manufacturing process. The Brazilian government may require us to shift to newer diaphragm technology, which we use in our Alagoas plant, or membrane technology. We have not shifted to these newer technologies yet, in part because the return from the capital expenditures associated with this shift would not be as high as those from other potential investments that we may undertake.

*Pilot Plant and Research Center*

Our Vinyls Unit maintains a pilot plant for PVC research and development in the State of Bahia and a research center in the State of São Paulo. This center currently employs 11 engineers and nine technicians specialized in plastics. At this center and in our pilot plant, we produce new PVC resins, develop and improve PVC production technology, render support services to our customers, train our customers personnel and develop new applications for PVC in Brazil, including vertical blinds, coatings for industrial PVC pipes and resins used in automotive parts and in the manufacture of doors, windows and other building components. In 2004, our research and development center developed Plastwood and new PVC applications for the Brazilian construction sector.

*Sales and Marketing of Our Vinyls Unit*

Net sales to our ten largest Vinyls Unit customers accounted for approximately 47.2% of our Vinyls Unit s total net sales revenue during 2005. One customer accounted for approximately 10.7% of our Vinyls Unit s total sales revenue during 2005 and 14.6% of our Vinyls Unit s total sales revenue during 2004. No customer accounted for more than 12% of the total net sales revenue of our Vinyls Unit during 2003. One customer accounted for 95.4% of our total external EDC sales in 2005, 69.2% in 2004 and 73.0% in 2003, and our largest caustic soda customer accounted for 14.9% of total caustic soda sales in 2005, 11.6% in 2004 and 13.4% in 2003.

There is a structural link between the PVC and caustic soda markets that exists because caustic soda is a by-product of the production of chlorine required to produce PVC. When demand for PVC is high, then greater amounts of caustic soda are produced, leading to an increase in supply and generally lower prices for caustic soda. Conversely, when demand for PVC is low, prices for caustic soda tend to rise.

*Domestic Sales*

In 2005, our Vinyls Unit had domestic net sales revenue of R$1,573.2 million, which accounted for 87.7% of our Vinyls Unit net sales revenue. In 2005, 66.2% of domestic net sales revenue was attributable to sales of PVC, 28.6% was attributable to sales of caustic soda and 5.3% was attributable to sales of other products.

We make most of our domestic sales of PVC and caustic soda directly to customers without the use of third party distributors. However, our Vinyls Unit maintains contractual relationships with three distribution centers located in Paulínia and Barueri, both in the State of São Paulo, and Joinville in the State of Santa Catarina that provide logistical support. In addition, we operate three warehouse facilities for PVC and six terminal tank facilities for caustic soda strategically located along the Brazilian coast to enable us to deliver our products to our customers on a just-in-time basis. Our Vinyls Unit develops its business through close collaboration with its customers, working together to improve existing products as well as to develop new applications for PVC. Our marketing and technical assistance groups also advise customers and potential customers that are considering the installation of manufacturing equipment for PVC end products.

*Export Sales*

In 2005, our Vinyls Unit had export net sales revenue of R$220.9 million, which accounted for 12.3% of our Vinyls Unit s total net sales revenue. Our export sales of PVC and EDC vary from year to year, influenced principally by domestic market demand and product availability.

The following table sets forth export sales and export volumes of our Vinyls Unit for the years indicated.

| | Year ended December 31, | | |
|---|---|---|---|
| | **2005** | **2004** | **2003** |
| Net export sales revenue (in millions of *reais*) | 220.9 | 256.2 | 203.7 |
| As % of total net sales revenue of Vinyls Unit | 12.3 | 13.8 | 14.8 |
| Export volumes (thousands of tons) | 194.3 | 191.0 | 215.6 |
| As % of total production of Vinyls Unit | 16.8 | 16.4 | 19.4 |

We have an ongoing obligation, which terminates during the first half of 2006, to export PVC and EDC under a supply agreement with Sojitz, which exports accounted for 47.1% of our total export sales PVC and EDC during 2005. Under this supply agreement, we have agreed to supply, and Sojitz has agreed to purchase,

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minimum annual volumes of 6,000 tons of PVC during this agreement s term, and minimum annual volumes of EDC, which decline over time from 100,000 to 80,000 tons. The export receivables generated under this supply agreement are collateral for an export prepayment facility that we have entered into. Any PVC, EDC or caustic soda that is made available by our Vinyls Unit for export is sold in the spot market at the best available prices.

We use a variety of methods to distribute our exports, depending generally on the total size of the export market, including direct sales, independent distributors, negotiations conducted through trading companies and sales on the spot market.

We exported 14.3% of our PVC sales volume in 2005. Our export sales of PVC are focused primarily on the South American, Southeast Asian and United States markets and to a lesser extent on Europe.

*Prices and Sales Terms*

We determine the domestic prices for our PVC resins with reference principally to the prices paid by third generation producers in Brazil for imports of PVC plus additional service charges. Our export price for PVC is generally equal to the international market price but also takes transportation costs into account. Delivery time, quality and technical service also affect the levels of sales of PVC resins. We establish our domestic price for caustic soda based on international market prices and prices charged by our three domestic competitors, taking into account any import duties and freight costs. Approximately 70% of our caustic soda sales are effected pursuant to agreements that are generally for one- to three-year terms and may include floor and ceiling prices. As with PVC, our export prices for EDC are generally determined according to international market prices but also take import duties and freight costs into account.

Prices that we charge for our vinyls products in the Brazilian market are traditionally higher than the prices that we obtain for our exports of these products. The difference in prices between the Brazilian and export markets results generally from:

- transportation costs;
- tariffs, duties and other trade barriers;
- a pricing premium reflecting the tighter demand/supply relationship in Brazil; and
- our reliability of supply, coupled with the technical support that we provide.

Our customers in Brazil may pay in full on delivery or elect credit terms that require payment in full within seven to 90 days following delivery. We charge interest based on prevailing market rates to our customers in Brazil that elect longer payment options. Sales terms for exports generally require payment between 90 and 120 days following delivery. We usually require irrevocable letters of credit for export sales made on the spot market.

***Competition***

*PVC*

We and Solvay are the only two producers of PVC in Brazil. Solvay s total Brazilian installed annual production capacity is 270,000 tons, compared to our annual production capacity of 516,000 tons. In December 2005, we expanded our annual PVC production capacity by 50,000 tons, and Solvay expanded its annual PVC production capacity by 30,000 tons. Solvay s two production facilities are located in São Paulo and, therefore, are closer than our facilities to the primary PVC market in Brazil. However, we believe that our vertical production capabilities, our modern PVC suspension plants, our strong relationship with our customers and our technical assistance programs enable us to compete effectively with Solvay.

We also compete with importers of PVC. Imports accounted for approximately 17.3% of Brazil s total PVC consumption in 2005. Domestically produced PVC is currently competitively priced with imported PVC after taking into account transportation costs and import duties. Solvay, which has an additional plant in Argentina, is also our principal competitor in the PVC market both in Brazil and elsewhere in South America.

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In addition, we compete with other producers of thermoplastics that manufacture the same line of vinyls products or products that are substitutes for our vinyls product line. Thermoplastics principally consist of polyethylene and polypropylene and are used in certain applications as substitutes for PVC. Wood, glass and metals also are used in some cases as substitutes for PVC.

*Other Products*

The four largest Brazilian producers of caustic soda account for approximately 72.7% of Brazilian production. Our company and Dow Chemical operate in this market throughout Brazil, while the other domestic producers of caustic soda generally operate on a local or regional basis. Imports accounted for approximately 27.4% of Brazil s total caustic soda consumption in 2005. We do not believe that imports of caustic soda will increase substantially because of the high cost of transporting caustic soda, which is usually sold in suspension form. In the caustic soda market, we compete mainly on the basis of price and timeliness of delivery.

Our principal competitors in the caustic soda market elsewhere in South America are Dow Chemical, Solvay and producers located on the U.S. Gulf Coast.

**Business Development Unit**

Our Business Development Unit accounted for R$569.0 million, or 4.2%, of the net sales revenue of all segments in 2005. Our Business Development Unit produces PET resin, dimethyl terephthalate, or DMT, caprolactam, cyclohexane, cyclohexanone and ammonium sulfate. In 2005, 37.1% of our Business Development Unit s net sales revenue was derived from the sale of PET products and 48.2% was derived from the sale of caprolactam.

In 2005, we estimate that we had an approximate 12% share of the Brazilian PET market, based on sales volumes.

***Products of Our Business Development Unit***

The following table sets forth a breakdown of the sales volume and net sales revenue of our Business Development Unit by product and by market for the years indicated.

| | Year ended December 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2005 | | 2004 | | 2003 | |
| | Quantities sold | Net sales revenue | Quantities sold | Net sales revenue | Quantities Sold | Net sales revenue |

| | (thousands of tons) | (millions of *reais*) | (%) | (thousands of tons) | (millions of *reais*) | (%) | (thousands of tons) | (millions of *reais*) | (%) |
|---|---|---|---|---|---|---|---|---|---|
| Domestic Sales: | | | | | | | | | |
| PET | 56.6 | R$ 200.7 | 35.3% | 66.2 | R$ 238.5 | 38.4% | 55.1 | R$ 168.3 | 37.0% |
| Caprolactam | 33.0 | 197.2 | 34.7 | 42.9 | 229.9 | 37.0 | 42.5 | 180.1 | 39.6 |
| Ammonium sulfate | 94.2 | 33.5 | 5.9 | 92.4 | 41.4 | 6.7 | 96.9 | 29.7 | 6.5 |
| Others | 16.7 | 49.8 | 8.7 | 15.6 | 54.2 | 8.7 | 15.0 | 42.9 | 9.4 |
| Total domestic sales | 200.5 | 481.2 | 84.6 | 217.1 | 564.0 | 90.8 | 209.5 | R$ 421.0 | 92.5 |
| Total exports | 19.1 | 87.8 | 15.4 | 14.3 | 56.8 | 9.2 | 9.1 | 34.3 | 7.5 |
| Total net sales | 219.6 | R$ 569.0 | 100% | 231.4 | R$ 620.8 | 100% | 218.6 | R$ 455.3 | 100% |
| % of total net sales revenue of all segments | | | 4.2% | | | 5.0% | | | 4.6% |

PET is one of the most widely used polymers in industry today and is used in manufacturing packaging for soft drinks, medications, cleaning products, mineral water and food products. Caprolactam is a raw material that

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forms the basis for the production of Nylon-6 textile thread, engineering resins and film, and is a structural material in the motor and electronics industries. We also produce DMT for use in PET production, ammonium sulfate for use as a fertilizer, and cyclohexane and cyclohexanone, both for use in paint solvents, pesticides, natural resins, oils and rubber.

***Production Facilities of Our Business Development Unit***

Our Business Development Unit operates two plants at the Northeastern Complex. At December 31, 2005, our Business Development Unit plants had a total annual production capacity of 78,000 tons of PET and 62,000 tons of caprolactam.

The table below sets forth the location, primary products, annual production capacity at December 31, 2005, and annual production for the years presented for each of our Business Development Unit plants.

| Location (Complex) | Primary products | Annual production capacity | Production year ended December 31, 2005 | 2004 | 2003 |
|---|---|---|---|---|---|
| | | (in tons) | | (in tons) | |
| Camaçari (Northeastern) | PET | 78,000 | 66,233 | 72,194 | 56,288 |
| | DMT | 80,000 | 70,954 | 76,985 | 63,369 |
| Camaçari (Northeastern) | Caprolactam | 62,000 | 49,981 | 50,483 | 48,850 |
| | Cyclohexane | 72,000 | 65,057 | 66,292 | 63,712 |
| | Cyclehexanone | 55,000 | 46,590 | 48,282 | 47,813 |
| | Ammonium sulfate | 114,000 | 94,855 | 92,617 | 97,157 |

***Raw Materials of Our Business Development Unit***

The most significant direct cost associated with the production of caprolactam is the cost of benzene, which accounted for approximately 47.2% of our Business Development Unit s variable caprolactam production costs in 2005. All of the benzene that we use in producing caprolactam is supplied by our Basic Petrochemicals Unit.

The most significant direct cost associated with our production of PET is the cost of para-xylene, which accounted for approximately 47.1% of our Business Development Unit s variable PET production costs in 2005. All of the para-xylene that we use in producing PET is supplied by our Basic Petrochemicals Unit.

***Technology of Our Business Development Unit***

We have entered into several non-exclusive agreements with a number of leading petrochemical companies to use technology for our Business Development Unit. The technology of our Business Development Unit includes:

- hydroxylammonium phosphate oximation, or HPO, technology, licensed by Dutch State Mines, which we use at our caprolactam plant;
- Dynamite Nobel technology, which we use at our DMT plant; and
- DuPont and UOP Sinco S.r.l. technologies, licensed by Chemtex International Inc., which we use in the production of polyester bottle grade chips from DMT.

We do not pay any continuing royalties under any of these license agreements, but we paid an initial fee under these license agreements. If any of these arrangements were terminated or no longer available to us, we believe that we would be able to replace the relevant technology with comparable or better technology from other sources.

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*Sales and Marketing of Our Business Development Unit*

Our Business Development Unit sells its products primarily in northeastern Brazil, mainly to third generation petrochemical producers located in the Northeastern Complex. We determine the prices for the products of our Business Development Unit with reference to several market factors that include the prices paid by third generation producers for imports of these products and prevailing market prices in Brazil.

Our Business Development Unit sells its products to a highly concentrated customer base. Four customers accounted for approximately 71.3% of our total PET sales during the year ended December 31, 2005. Our Business Development Unit s caprolactam customer base is even more concentrated, as one customer accounted for approximately 67% of our total caprolactam sales during the year ended December 31, 2005.

*Competition*

Monomeros Colombo Venezolanos S.A., or Monomeros, is the only manufacturer, other than our company, of caprolactam in South America, with an annual production capacity of 30,000 tons. Monomeros supplied approximately 3,614 tons of caprolactam in 2005, or approximately 9.7% of the caprolactam sold in Brazil.

The textile industry consumed the most caprolactam in Brazil during 2005 (approximately 22,200 tons), and the engineering plastics and plastic films segments of the petrochemical industry consumed an aggregate amount of approximately 10,500 tons of caprolactam in 2005.

There are two other producers of PET in Brazil: Rhodia-ster S.A., or Rhodia-ster (a subsidiary of Mossi & Ghisolfi Group); and Vicunha Têxtil S.A., or Vicunha Têxtil. In 2005, Rhodia-ster and Vicunha Têxtil had annual production capacities of 290,000 tons and 24,000 tons, respectively, as compared to our annual production capacity of 70,000 tons. In addition, M&G Finanziaria Industriale S.p.A. has commenced construction of a PET plant in Ipojuca, Pernambuco, with an annual production capacity of 450,000 tons of PET, which is expected to commence operations in late 2006. We also compete with importers of PET. Imports accounted for approximately 35.8% of Brazil s total PET consumption in 2005. Although international producers of PET have greater economies of scale than our company, we are able to compete with these producers due to the high transportation costs and import duties applicable to PET imports. Our PET production is aimed principally at the bottled water segment of the PET market, and we believe that our quality products will continue to remain competitive in the Brazilian PET market.

**Jointly Controlled Companies and Joint Venture**

*Copesul*

At December 31, 2005, we owned, directly and indirectly, 29.5% of the voting and total share capital of Copesul, the cracker based in the Southern Complex. Copesul, which is a corporation (*sociedade anônima*) organized under the laws of Brazil, is the second largest petrochemical cracker in Brazil based on production capacity, with approximately 33.0% of Brazilian production capacity of ethylene.

Copesul was formed in 1976 with Petroquisa as its majority shareholder and commenced operations in 1982. In May 1992, as part of the Brazilian government s efforts to privatize the Brazilian petrochemical industry, Petroquisa auctioned a portion of its interest in Copesul to private investors. At December 31, 2005, a consortium, including the Odebrecht Group and Ipiranga and its affiliates, owned 58.9% of the total share capital of Copesul. Petroquisa continued to own 15.6% of the total share capital of Copesul.

Copesul s net sales revenue on a consolidated basis was R$5,552.6 million in 2005, R$5,374.1 million in 2004 and R$4,177.9 million in 2003, as adjusted to conform to our accounting policies. Copesul s net income on a consolidated basis was R$566.0 million in 2005, R$558.4 million in 2004 and R$149.9 in 2003, as adjusted for the effects of unrealized tax incentives to conform to our accounting policies. We account for our interest in Copesul in our Brazilian GAAP financial statements using the proportional consolidation method.

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Copesul is the second largest petrochemical cracker in Brazil based on production capacity, with approximately 39% of Brazilian production capacity of ethylene. It provides petrochemical feedstocks to second generation petrochemical producers located in the Southern Complex, including our Polyolefins Unit s plants located there. Copesul s manufacturing operations in the Southern Complex and the products that it produces are similar to the products of our Basic Petrochemicals Unit.

Copesul s annual ethylene production capacity is 1,135,000 tons and its annual propylene production capacity is 581,000 tons. In 2005, Copesul produced approximately 1,078,000 tons of ethylene and approximately 581,000 tons of propylene. Actual production of Copesul s plants, like the plants in our Basic Petrochemicals Unit, may exceed their stated annual production capacity.

Copesul s main customers are the second generation petrochemical producers located in the Southern Complex, including our company. Copesul has long-term supply contracts with its major customers, including our Polyolefins Unit.

We have entered into a shareholders agreement with Ipiranga relating to our shares of Copesul. Ipiranga owns 29.5% of the voting and total share capital of Copesul. Under the Copesul shareholders agreement, we and Ipiranga jointly control Copesul. We have agreed to consult with Ipiranga prior to any meeting of Copesul s board of directors or shareholders and to vote our shares together with Ipiranga on specified matters, including policies relating to the allocation of excess amounts of raw materials, policies relating to the distribution of profits, the election of members to Copesul s board of directors, amendments to Copesul s by-laws, approval of indebtedness of Copesul in excess of certain limits, sales of assets in excess of specified limits, investments in excess of certain limits, and the merger of Copesul with another company. We have also agreed that neither we nor Ipiranga will vote to approve any of the above matters unless we and Ipiranga vote 75% of the shares collectively held by us in favor of that action at a meeting between Ipiranga and our company or, if no quorum is obtained at such a meeting, of 75% of the shares present at a second meeting called for this purpose.

The Copesul shareholders agreement also provides a right of first refusal for transfers or sales of the voting share capital of Copesul to third parties, except for transfers and sales of Copesul voting share capital to companies directly or indirectly controlled by the selling shareholder.

Third-party purchasers of common shares of Copesul from our company or Ipiranga also must agree to comply with the Copesul shareholders agreement. The shareholders agreement also includes provisions designed to ensure that each of our company and Ipiranga will continue to own the same proportion of shares of Copesul if either of us so elects.

The Copesul shareholders agreement provides that we will vote with Ipiranga in a manner designed to ensure that both we and Ipiranga are able to elect the maximum possible number of members of Copesul s board of directors. The shareholders agreement is effective until August 2022. We have agreed with Ipiranga not to enter into another shareholders agreement regarding Copesul with any other shareholders of Copesul.

***Politeno***

At December 31, 2005, we owned 34.0% of Politeno s total share capital, including 35.0% of its voting share capital. Politeno, which is a corporation (*sociedade anônima*) organized under the laws of Brazil, is a second generation petrochemical producer operating in the Northeastern Complex.

On April 6, 2006, we purchased all of the common and preferred shares of Politeno that were owned by SPQ, a subsidiary of Suzano, Sumitomo and Itochu. As a result of the Politeno acquisition, we now own 100% of the voting share capital and 96.2% of the total share capital of Politeno.

Politeno s net sales revenue was R$1,169.9 million in 2005, R$1,119.4 million in 2004 and R$943.9 million in 2003, as adjusted to conform to our accounting policies. Politeno s net income was R$63.4 million in 2005,

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R$96.5 million in 2004 and R$67.2 million in 2003, as adjusted for the effects of revaluation of property, plant and equipment to conform to our accounting policies. We account for our interest in Politeno in our Brazilian GAAP financial statements using the proportional consolidation method. We will fully consolidate Politeno s results in our consolidated financial statements at dates and for periods following the Politeno acquisition.

Politeno produces polyethylene grades which are widely used in the flexible and rigid packaging industries. Politeno produces LDPE, medium density polyethylene, HDPE, LLDPE, linear medium density polyethylene, ethyl vinyl acetate copolymer and other special resins.

The production facility of Politeno is comprised of two industrial plants, a LDPE facility and an linear polyethylene facility. The LDPE facility produces LDPE and ethyl vinyl acetate copolymer, with an annual production capacity of 150,000 tons. The linear polyethylene facility produces LLDPE and HDPE and has an annual production capacity of 210,000 tons.

The principal raw materials used in Politeno s production processes are ethylene and propylene, which are primarily supplied by our Basic Petrochemicals Unit. Politeno also uses butadiene, benzene and toluene. Politeno s principal customers are third generation petrochemical producers.

***Petroflex***

At December 31, 2005, we owned 20.1% of the total and voting share capital of Petroflex. Petroflex, which is a corporation (*sociedade anônima*) organized under the laws of Brazil, is the leading producer of synthetic rubber in Latin America and produces approximately 360,000 tons of more than 70 types of elastomers per year.

Petroflex was formed in 1976 with Petroquisa as its majority shareholder. In 1992, as part of the Brazilian government s efforts to privatize the Brazilian petrochemical industry, Petroquisa auctioned a portion of its equity interest in Petroflex to private investors. At December 31, 2005, we and Suzano Química Ltda., an affiliate of Suzano, each owned 20.1% of the voting and total share capital of Petroflex and Unipar União de Indústrias Petroquímicas S.A. owned 10.1% of Petroflex s voting share capital.

Petroflex s net sales revenue was R$1,373.2 million in 2005, R$1,306.0 million in 2004 and R$1,091.8 million in 2003, as adjusted to conform to our accounting policies. Petroflex s net income was R$88.3 million in 2005, R$98.6 million in 2004 and R$60.5 million in 2003, as adjusted for the effects of revaluation of property, plant and equipment to conform to our accounting policies. We account for our interest in Petroflex in our Brazilian GAAP financial statements using the proportional consolidation method.

Petroflex operates three plants in Brazil located in Duque de Caxias, Rio de Janeiro; Cabo, Pernambuco; and Triunfo, Rio Grande do Sul. Petroflex sells its products to customers in approximately 70 countries. The main customers of Petroflex are manufacturers of tires, shoes, adhesives and sealants.

The major raw materials used in Petroflex s production process are butadiene and styrene. Petroflex purchases butadiene from us from which it produces styrene-butadiene, polybutadiene, liquid hidroxylated polybutadiene and other elastomers. Due to high naphtha prices in 2005, the price of butadiene increased by 18% in the Brazilian market and the price of styrene increased by 3%. However, the recovery of synthetic rubber prices in *reais,* due to increases in international market prices, allowed Petroflex to pass on most of these increased costs to its customers.

We have entered into a shareholders agreement with Suzano and Unipar União de Indústrias Petroquímicas, Unipar, with respect to our shares of Petroflex. Suzano owns 20.1% of Petroflex s total and voting share capital; and Unipar owns 10.1% of Petroflex s total and voting share capital. Such proportion is required to be maintained even if any of the controlling shareholders acquires new shares issued by Petroflex. The Petroflex shareholders agreement contains provisions governing voting, transfer and preemptive rights. We have the right to elect two of the nine members of Petroflex s board of directors.

We have agreed in the Petroflex shareholders agreement to reach unanimous decisions with the other parties with respect to certain actions to be taken by Petroflex s board of directors or shareholders, including: changes to Petroflex s by-laws, subject to certain exceptions; Petroflex s dissolution or liquidation; the merger of Petroflex with or into another company; transactions involving the repurchase, amortization and redemption of Petroflex s shares.

The Petroflex shareholders agreement also provides a right of first refusal for transfers or sales of the controlling shares of Petroflex to third parties, except for transfers and sales of Petroflex share capital to companies affiliated to the selling shareholder. Third-party purchasers of the controlling shares of Petroflex also must agree to enter into and comply with the Petroflex shareholders agreement.

***Paulinia***

At December 31, 2005, we owned 60.0% of Paulínia s total and voting share capital. Paulínia, which is a corporation (*sociedade anônima*) organized under the laws of Brazil, was incorporated on September 16, 2005 and is a joint venture between our companies for the construction and operation of a polypropylene plant to be located in Paulínia, in the State of São Paulo.

We anticipate that Paulínia s plant will have an initial annual production capacity of 300,000 tons of polypropylene and expect that this plant will commence operations in late 2007. We contributed the process technology that will be used by this plant under an agreement with a 20-year term. Petrobras will supply Paulínia with polymer-grade propylene, the primary feed stock to be used in Paulínia s production processes, through its refineries in Paulínia and Henrique Lage under an agreement with an initial 20-year term. The agreement with Petrobras is automatically renewable for consecutive two-year terms following the intial term, unless terminated by one of the parties.

We are a party to a shareholders agreement with Petroquisa with respect to our shares of Paulínia. Petroquisa owns 40.0% of Paulínia s total and voting share capital. The Paulínia shareholders agreement, which has a 20-year term, provides that:

- so long as we own at least 60% of Paulínia s total share capital, we have the right to nominate a majority (three members) of Paulínia s board of directors (and their respective alternates) and two of its three executive officers;
- so long as Petroquisa owns at least 40% of Paulínia s total share capital, Petroquisa has the right to nominate two members of Paulínia s board of directors (and their respective alternates) and one of its three executive officers;
- if the interest in the total share capital of Paulínia of our company or Petroquisa s falls below 40% (but exceeds 20%), we or Petroquisa will have the right to elect one member of Paulínia s board of directors; and
- if the interest in the total share capital of Paulínia of our company or Petroquisa s falls below 10% (if we and Petroquisa are Paulínia s only shareholders at the time, or below 20% if Paulínia has additional shareholders at the time), we or Petroquisa will no longer have the right to elect members of Paulínia s board of directors.

We have agreed with Petroquisa to attempt to reach unanimous decisions with respect to certain actions to be taken by Paulínia s board of directors or shareholders, including (1) transactions involving the purchase, sale, assignment or encumbrance of fixed assets of Paulínia in excess of specified amounts; (2) Paulínia s incurrence of indebtedness in excess of certain specified levels; (3) investments in other companies in any form; and (4) the merger, spin-off, consolidation or any other type of reorganization involving Paulínia s jointly controlled companies, affiliates and subsidiaries, as well the dissolution or liquidation or the declaration of bankruptcy by any of these companies. We have also agreed with Petroquisa to attempt to reach decisions by an 80%

supermajority with respect to certain actions to be approved by Paulínia s shareholders, including (1) the merger, spin-off, consolidation or any other type of reorganization involving Paulínia; (2) Paulínia s dissolution or liquidation; (3) the declaration of bankruptcy by Paulínia; (4) the issuance of securities by Paulínia; (5) changes to Paulínia s by-laws; (6) changes to propylene supply agreement between Petrobras and Paulínia, the technology contribution agreement between Paulínia and our company, or other operating agreements entered into between Paulínia and Petrobras or our company; and (7) any capital increase by our company and Petroquisa to complete the construction and implementation of the polyethylene plant, if construction has already commenced but Paulínia lacks sufficient funds to complete construction.

Under the Paulínia shareholders agreement, we and Petroquisa granted to each other a right of first offer and a right of first refusal in respect of sales, transfers or assignment to unrelated third parties of share capital of Paulínia owned directly or indirectly by either of us. In addition, if an impasse occurs in respect of certain actions that require the approval of a super-majority of Paulínia s shareholders, both Petroquisa and our company may offer to purchase the shares of the other or may offer to sell the shares to the other. If either Petroquisa or our company offers to sell the shares to the other party and the other party rejects the offer, then the offering party may sell the shares to a third party. If both Petroquisa and our company desire to sell our shares in Paulínia, these shares will be jointly sold (including through an auction process) to one or more third parties. In each case, the sales price will be determined based on an appraisal process specified in the shareholders agreement.

**Capital Expenditures**

Our capital expenditures on property, plant and equipment were R$780.7 million in 2005, R$442.2 million in 2004 and R$223.7 million in 2003. Additionally, our investments in interests in other companies were R$34.0 million in 2005, R$23.6 million in 2004 and R$71.7 million in 2003. Our principal capital expenditures projects during 2003 through 2005 consisted of the following:

- the adaptation of the maritime pier located at Aratú and the construction of pipelines, storage tanks and other facilities necessary to receive and transport imported naphtha to our basic petrochemicals plants. This project was undertaken between 2001 and 2003 at a total cost of R$83.5 million;

- the expansion of the annual ethylene production capacity of one of our pyrolysis plants at the Northeastern Complex by 80,000 tons. This project was undertaken in 2003 at a total cost of R$237.1 million;

- an efficiency enhancement project at one of our polypropylene plants in the Southern Complex that increased our annual polypropylene production capacity by 100,000 tons. This project was undertaken in 2003 and 2004 at a total cost of R$21.0 million;

- an automation project in our PVC plants in Alagoas and the Northeastern Complex that is expected to increase the reliability of the operation of and modernize these plants, improve the operational performance of these plants, and increase the safety of our production processes at these plants. We invested R$29.6 million in this project in 2003, 2004 and 2005. This project was completed at our Alagoas PVC plant in 2004 and we expect to complete this project at our PVC plant in the Northeastern Complex in the second half of 2006;

- the first stage of our modernization and improvement project at our Aromatics 1 and 2 units in the Northeastern Complex that increased our annual para-xylene production capacity by 50,000 tons. This project was undertaken in 2004 at a total cost of R$25.1 million;

- an efficiency enhancement at our Alagoas PVC plant that increased its annual production capacity by 50,000 tons. This project was undertaken in 2004 and 2005 at a total cost of R$111.8 million;

an efficiency enhancement project at one of our polyethylene plants in the Northeastern Complex that increased its annual production capacity by 30,000 tons. This project was undertaken in 2004 and 2005 at a total cost of R$9.2 million;

an efficiency enhancement project at our other polyethylene plant in the Northeastern Complex that we believe will increase its annual production capacity by 30,000 tons. We invested R$3.1 million in this project in 2004 and 2005 expect to complete this project in the first half of 2006 at a total cost of approximately R$9.9 million; and

an efficiency enhancement project at our Aromatics 2 unit in the Northeastern Complex that we believe will increase our annual isoprene production capacity by 18,000 to 26,500 tons. We expect to complete this project by the end of 2006 at a total cost of approximately R$81.9 million.

In 2004, we began implementation of our Braskem+ program. This program identified 210 specific initiatives, each with its own performance goals and implementation schedule. At December 31, 2005, we had made capital expenditures of R$140.7 million related to the implementation of this program and anticipate that this program will require us to make additional capital expenditures of approximately R$232.7 million in 2006 and R$87.9 million in 2007.

In 2005, we commenced our Formula Braskem program to implement a new integrated management system intended to incorporate the best practices in the international petrochemical industry in our management systems and the most recent technological developments available in the marketplace. At December 31, 2005, we had made capital expenditures of R$28.4 million related to the implementation of Formula Braskem and anticipate that Formula Braskem will require us to make additional capital expenditures of approximately R$101.6 million in 2006.

In 2005, we approved the expansion of our raw material stocking unit to increase its capacity by 60,000 cubic meters. We expect that this expansion will allow us realize economies of scale in maritime freight by enabling us to increase the quantities of raw material that we can receive in a single shipment and to achieve gains in operational efficiency by allowing us to optimize the operation of our cracker and process higher quality raw materials. We expect to complete this project in the first half of 2007 at a total cost of approximately R$40 million.

On September 16, 2005, we and Petroquisa incorporated Paulínia as a joint venture company for the construction and operation of a polypropylene plant to be located in Paulínia, in the State of São Paulo, with an initial annual production capacity of 300,000 tons. We own 60% of the total and voting share capital of Paulínia, and Petroquisa owns the remaining total and voting share capital. The initial total budgeted cost of this plant was approximately US$240 million. We expect that 30% of the cost of this plant will be financed through equity contributions by the shareholders of Paulínia, and the remaining 70% will be expected to be financed under the terms of a long-term financing arrangement. Our share of these equity contributions is 60%. This plant is expected to commence operations in late 2007. We can provide no assurances that the actual cost of the construction of this plant will not exceed the budgeted cost. The shareholders of Paulínia will finance 30% of any cost overruns in the form of equity contributions.

On April 6, 2006, we purchased all of the common and preferred shares of Politeno that were owned by SPQ, a subsidiary of Suzano, Sumitomo and Itochu. We paid a portion of the purchase price for these shares in an aggregate amount of the *real*-equivalent of US$111.3 million (US$60.6 million to SPQ and a total of US$50.7 to Sumitomo and Itochu) on April 6, 2006. The remainder of the purchase price for these shares will be calculated based on an earn-out formula that will take into account Politeno s operating performance, measured by fluctuations in polyethylene and ethylene margins in the Brazilian petrochemical market during the 18 months following the execution date of this agreement. As a result of the Politeno acquisition, we now own 100% of the voting share capital and 96.2% of the total share capital of Politeno.

In December 2005, we entered into an action plan agreement with Pequiven under which our company would form a joint venture with Pequiven for the construction and operation of a polypropylene plant to be located in the El Tablazo Petrochemical Complex in the State of Zulia, Venezuela, with an annual production

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capacity of approximately 400,000 tons. This agreement sets forth the preliminary understanding of the parties on an action plan for the implementation of the project, including the following:

- this joint venture would be implemented through a new company;
- Pequiven would be responsible for obtaining a supply of propylene, the primary feed stock of this plant, for the new company;
- the estimated total cost of this project to the new company would be approximately US$350 million;
- the contributions of the parties to the new company may consist of cash, equity in other companies in the petrochemical sector and/or key technology and know-how; and
- this project would commence operations in 2008.

We are continuing to negotiate with Pequiven regarding the corporate structure of this project and expect that the new joint venture company will be formed by the end of 2006. We can provide no assurances that these negotiations will be successful or that if we reach a final agreement with respect to this joint venture with Pequiven, such agreement will be upon the terms currently anticipated by our management.

Our ability to compete in the Brazilian and foreign markets that we serve depends on our ability to integrate new production processes developed by our company and third parties in order to lower our costs and offer new thermoplastic products. In addition, our relationships with our customers are enhanced by our ability to develop new products and customize existing products to meet their needs. To meet these challenges, we maintain a research and development program that is primarily implemented at the Braskem Center for Innovation and Technology in the Southern Complex. We invested R$47.2 million, R$59.2 million and R$35.5 million in research and development during 2005, 2004 and 2003, respectively.

We currently are budgeting total capital expenditures of approximately R$900 million for 2006. Our principal capital expenditures for 2006 consist of, in addition to the projects referred to in the preceding paragraphs, approximately R$202 million for health, environmental and quality improvement projects, approximately R$202 million for the replacement of depreciated equipment, approximately R$118 million for productivity improvements and approximately R$378 million for plant modernization and information systems.

We are currently evaluating projects that could entail significant capital expenditures in the future.

**Maintenance**

Most of our maintenance is performed by third-party service providers. For example, we have contracts with Construtora Norberto Odebrecht S.A., a company in the Odebrecht Group, Asea Brown Boveri Ltd. and other service providers to perform maintenance for our Basic Petrochemicals Unit and our Business Development Unit. We also perform some of our ordinary course maintenance with our small team of maintenance technicians, which also coordinate the planning and execution of maintenance services performed by third parties.

Because we have two independent Olefins units and two independent Aromatics units, we may continue production of basic petrochemicals without interruption, even while we perform certain maintenance services. We occasionally undertake other brief shutdowns of our operations that do not materially affect our production output, primarily for maintenance purposes, catalyst regeneration and equipment cleaning.

Regular basic petrochemicals plant maintenance requires complete plant shutdowns from time to time, and these shutdowns usually take approximately 30 days to complete. Since commencing operations in July 1978, our largest basic petrochemicals plant (Olefins 1) has undergone seven scheduled major maintenance services as part of our regular maintenance activities. The last general maintenance shutdown of our Olefins 1 unit was carried out in July and August 2001 and lasted for 25 days. This shutdown permitted inspection and maintenance of this unit, which had been operational for almost six years without a shutdown. This shutdown was intended to improve the plant s efficiency and production capacity. The cost of servicing the unit was approximately R$39.8 million (not including the value of lost production during this shutdown). The next general shutdown of our Olefins 1 unit has been scheduled for July 2007 with an estimated duration of approximately 30 days.

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In 2002, we shut down our Olefins 1 unit for 92 days in order to increase its production capacity and to modernize and upgrade its technology. This shutdown reduced our Basic Petrochemical Unit s ethylene and propylene production in 2002. The cost of these improvements to this Unit was approximately R$142.8 million (not including lost production).

The last general maintenance shutdown of our Aromatics 2 and Olefins 2 units (which form part of the same basic petrochemicals facility) was carried out in January and February 2004 and lasted 36 days. This shutdown permitted inspection and maintenance of this unit, which had been operational for almost six years without a shutdown. This shutdown was intended to improve the plant s efficiency and production capacity. In addition, we implemented various improvements to ensure the reliability and continuous operation of these units and to minimize the environmental impact of our operations. The cost of servicing this unit was approximately R$89 million (not including the value of lost production during this shutdown). The next general shutdown of our Aromatics 2 and Olefins 2 units has been scheduled for 2010 with an estimated duration of approximately 25 days.

The last general maintenance shutdown of our Aromatics 1 unit was carried out in August 2005 and lasted 30 days. This shutdown permitted inspection and maintenance of this unit, which had been operational for three years without a shutdown, and the implementation of new projects to increase productivity. This shutdown was also intended to improve the efficiency and production capacity of the plants in this unit and resulted in the development of new solvents and substantial growth in our production of aromatics. The cost of servicing this unit was approximately R$21 million (not including the value of lost production during this shutdown or investments in productivity enhancements). The next general shutdown of our Aromatics 1 unit has been scheduled for 2008 with an estimated duration of approximately 30 days.

We have a regular maintenance program for each of our polyolefins plants. Production at each of our polyolefins plants generally is shut down for seven to 20 days every two years to allow for regular inspection and maintenance. In addition, we undertake other brief shutdowns for maintenance purposes that do not materially affect our production of polyolefins. We coordinate the maintenance cycles of our polyolefins plants with those of our basic petrochemicals plants. While our basic petrochemicals facilities must be shut down for up to 30 days for maintenance, our polyolefins facilities may be shut down for shorter periods because these facilities are less complex to operate and maintain than our basic petrochemicals facilities.

We have a regular maintenance program for each of our vinyls plants. Our Camaçari and Alagoas PVC plants are generally shut down for 20 days every two years to allow for regular inspection and maintenance. The last general maintenance shutdown of our PVC plant in Camaçari was carried out in May 2006 and lasted for 14 days. The next general maintenance shutdown of this plant is scheduled for April 2008. The last general maintenance shutdown of our PVC plant in Alagoas was carried out in November 2005 and lasted for seven days. The next general maintenance shutdown of this plant is scheduled for March 2007. Our São Paulo PVC plant generally shuts down for five days of maintenance each year. Our caustic soda and chlorine plant in Alagoas generally shuts down for 15 days of maintenance every two years. The last general maintenance shutdown of this plant was carried out in February 2004 and lasted for 12 days. The next general maintenance shutdown of this plant is scheduled for May 2006. Our caustic soda and chlorine plant in Camaçari does not require prolonged maintenance shutdowns and is shut down for two or three days each year.

Regular maintenance of our Business Development Unit plants usually requires plant shutdowns every two years that take approximately 20 days to complete. The last general maintenance shutdown of our caprolactam plant was carried out in October 2005 and lasted 28 days. The cost of this maintenance shutdown was approximately R$13 million (not including lost production value). Prior to this general maintenance shutdown, the last general maintenance shutdown of our caprolactam plant was in March 2003, during which we changed certain production equipment, which (together with other measures that we have adopted) will extend the periods between general maintenance shut downs of this plant from two to three years. The last general maintenance shutdown of our Business Development Unit s DMT and polyethylene teraphthalate, or PET, plants was carried

out in April 2005 and lasted for 27 days. The cost of this shutdown was R$10.0 million (not including lost production value). Prior to this general maintenance shutdown, the last general maintenance shutdown of our DMT and PET plants was in June 2003, during which we successfully upgraded the PET plant s reactor, resulting in resin quality improvements as well as increasing the plant s annual production capacity from 60,000 tons to 70,000 tons. We also implemented operational improvements in our PET plant in 2004, which further increased the plant s annual production capacity from 70,000 tons to 78,000 tons. The next general maintenance shutdown of our PET and DMT plants is scheduled for April 2007.

Beginning January 1, 2006, in accordance with IBRACON Technical Interpretation 01/2006, we recorded all programmed maintenance shutdown expenses in property, plant and equipment, as Machinery, equipment and facilities . Such expenses occur at scheduled intervals from one to six years and are depreciated to production cost until the beginning of the next maintenance shutdown. In addition, the retrospective effects of depreciation with the adoption of this interpretation will be recognized in shareholders equity. Accordingly, for periods ending after January 1, 2006, we will reclassify the amount of R$356.1 million from deferred charges to property, plant and equipment, and recognize the amount of R$164.9 million in shareholders equity.

**Environmental Regulation**

We are subject to Brazilian federal, state and local laws and regulations governing the discharge of effluents and emissions into the environment and the handling and disposal of industrial waste and otherwise relating to the protection of the environment.

Under federal and state environmental laws and regulations, we are required to obtain operating permits for our manufacturing facilities. State authorities in the State of Bahia issued operating permits for our plants in the Northeastern Complex in 2000, which were renewed in 2005 for a six-year term. Our environmental operating permit obligates us to engage in systematic measures for the treatment of wastewater and hazardous solid waste. State authorities in the State of Rio Grande do Sul, where our Southern Complex plants are located, regulate our operations by prescribing specific environmental standards in our operating permits, which must be renewed every four years. State authorities in the States of Alagoas and São Paulo have issued permits for our plants in those respective complexes, which also must be renewed every four years. If any of our environmental licenses and permits lapse or are not renewed or if we fail to obtain any required environmental licenses and permits, we may be subject to fines ranging from R$50.0 to R$50.0 million, and the Brazilian government may partially or totally suspend our activities and impose civil and criminal sanctions on our company or both. All our environmental licenses and permits are in full force and effect.

All projects for the installation and operation of industrial facilities in the Northeastern Complex are subject to approval by the Council for Environmental Protection of the State of Bahia or by the Environmental Resources Center, the State s Environmental Protection Council s technical office, depending on the complexity of the facility. The State s Research and Development Center and other outside consultants act as technical advisors to the Environmental Resources Center. The State s Environmental Protection Council must approve installed projects prior to their commencement of operations and must renew such approval every five years thereafter.

The Brazilian government enacted an Environmental Crimes Law in 1998 that imposes criminal penalties on corporations and individuals causing environmental damage. Corporations found to be polluting can be fined up to R$50.0 million, have their operations suspended, be prohibited from government contracting, be required to repair damage that they cause and lose certain tax benefits and incentives. Executive officers, directors and other individuals may be imprisoned for up to five years for environmental violations.

Cetrel treats wastewater generated by our company and the other petrochemical producers at the Northeastern Complex at a liquid effluents treatment station located in the Northeastern Complex. This treatment station also includes a system for the collection and disposal of contaminated wastewater. Cetrel also stores and incinerates, treats and disposes of hazardous solid waste. For other kinds of solid waste, Cetrel maintains a

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landfill. In 1998, Cetrel installed a hazardous solid waste incinerator with an annual incineration capacity of 4,400 tons. Another Brazilian company co-processes hazardous solid waste in a cement kiln located in the city of Pedro Leopoldo, State of Minas Gerais.

In January 1996, Cetrel obtained its BS 7750 environmental certification (British Standard) and in September 1996 became one of the first companies in the world to receive the ISO 14001 certification, an international standard for environmental control. In 1998, Cetrel obtained certification of its laboratory by the ISO Guide 25 standards system from the Brazilian Institute of Metrology and Industrial Quality.

We believe our operations are in compliance in all material respects with applicable environmental laws and regulations currently in effect. Some environmental studies that we have commissioned have indicated instances of environmental contamination at certain of our plants. In addition, we and certain of our subsidiaries and executive officers of our company and of our subsidiaries have received notices from time to time of minor environmental violations and are or have been subject to investigations or legal proceedings with respect to certain alleged environmental violations. These environmental issues, and any future environmental issues that may arise, could subject us to fines or other civil or criminal penalties imposed by Brazilian authorities. We are addressing all environmental issues of which we are aware, and we believe that none of these issues will have a material adverse effect on our business, financial condition or operations.

Our consolidated annual expenditures on environmental control were R$71.7 million during 2005, R$58.1 million during 2004 and R$51.7 million during 2003. To dispose of our industrial wastewater and solid hazardous waste, we contract our jointly controlled company Cetrel at the Northeastern Complex, our subsidiary Companhia Alagoas Industrial  Cinal at Alagoas, Companhia Riograndense de Saneamento, a state-owned environmental company at the Southern Complex and other third parties. These companies treat our industrial waste immediately after this waste is generated and dispose of our solid waste. Our consolidated environmental expenses relate to our continuous control and monitoring policies, and we do not have any material future environmental liabilities related to our ongoing operations. Accordingly, we have not established a provision for environmental contingencies. However, our environmental compliance costs are likely to increase as a result of the projected increase in our production capacity and projected increases in unit costs for treatment and disposal of industrial waste as well as the cost of compliance with future environmental regulations.

Our environmental compliance in 2005 included the following results:

- no significant environmental accidents in 2005; and

- no fines were levied on any of our plants by state environmental authorities during 2005.

In September 2002, we created a Health, Safety and Environment Committee, composed of leaders of each of our business units and other members of our management. This committee supports and monitors our environmental, health and safety efforts. In February 2003, our board of directors approved a comprehensive health, safety and environment policy, as we recognize that sustainable development and ethical practices are essential to our continued growth and performance. As part of this policy, we are committed to:

- expanding our relationship with the communities in which we operate;

- continually improving the health, safety and environmental aspects of our processes, products and services by promoting innovation and complying with evolving health, safety and environmental standards;

implementing preventive measures to promote (1) the health and quality of life of people in the communities in which we operate, and (2) the safety of our workers, third parties and others involved or affected by our processes; and

the efficient use of natural resources.

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**Safety and Quality Control**

*Safety*

We have adopted a policy that makes all of our officers, directors and employees responsible for the safety of our workers and for preserving the environment.

We participate in the Responsible Care program, which establishes international standards for environmental, occupational health and safety practices for chemical manufacturers. Through our participation in this program, we adopted policies and procedures that require us to follow detailed instructions in matters of health, safety and the environment. We seek to maintain these environmental standards and have qualified each of our plants for NBR-ISO 9001 and 14001 certification, which includes internationally prescribed environmental management practices. We are currently implementing health, safety and environmental standards based on OHSAS 18001 and standards issued by the U.S. Occupational Safety and Health Administration.

Our safety record ranks above the average of companies in the Brazilian chemical industry. The following table illustrates our progress in terms of our safety record and compares our safety record to the average for the Brazilian chemical industry:

| | Year ended December 31, | | | |
|---|---|---|---|---|
| | 2005 | 2004 | 2003 | 2003(1) |
| | Braskem | | | Brazilian chemical industry average |
| **Safety Indicator** | | | | |
| Index of Accident Frequency (accidents/200,000 man-hours) | 0.2 | 0.4 | 0.6 | 3 |
| Index of Severity (lost and deducted days/200,000 man-hours) | 4.0 | 11.0 | 5.0 | 40 |

(1) Brazilian petrochemical industry average of the members of Brazilian Association of Chemical Industry and Derivative Products for 2004, as reported by the Brazilian Association of Chemical Industry and Derivative Products.

Our safety record in 2005 included the following results:

- a 50% reduction in our rate of personal accidents of all types, compared to 2004;
- nine of our 13 units had no accidents causing injuries requiring a worker to be absent from work during 2005; and
- our total cost resulting from accidents was approximately 30% lower than in 2004.

Each of our industrial plants are equipped with a comprehensive firefighting safety system. At the Northeastern Complex, water is available from a 200,000 cubic meter artificial lake, connected to the industrial plants by a pumping station and a distribution network and built according to international safety standards. We and the other companies in the Northeastern Complex maintain emergency equipment and trained safety crews. The safety plan for the Northeastern Complex provides for firefighting brigades of all companies in the complex to jointly assist in the event of any major accidents. The Northeastern Complex has safety standards for construction density and the design of pipelines and highways. Similar systems are employed at the Southern Complex, our plant in the State of Alagoas and our plant in the State of São Paulo (except with respect to safety standards for construction density and design of pipelines and highways, as we do not have such facilities in São Paulo).

***Quality Control***

Our quality control management uses ISO 9001/00, an internationally recognized quality control standard, and ISO 14001, an internationally recognized environmental control standard, as its base. We have instituted systematic improvement processes in our operational areas, focusing on integrating production, maintenance, inventory management, customer satisfaction and profitability.

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***ISO Certifications***

We have obtained ISO 9001 certifications for all of our products. We have also obtained ISO 14001 certifications for all of our industrial plants. These certifications take into account both the quality of our products and the quality of our operating procedures.

**Property, Plant and Equipment**

Our properties consist primarily of petrochemical production facilities in Camaçari in the State of Bahia, in Maceió in the State of Alagoas, in Triunfo in the State of Rio Grande do Sul and in São Paulo in the State of São Paulo. Our principal executive offices are located in São Paulo in the State of São Paulo, and we have an administrative support office in the City of Rio de Janeiro. We also have equity interests in investments located in other parts of the country. We own all our production facilities, but we generally rent our administrative offices.

The following table sets forth our properties and the properties of our principal subsidiary by location of facilities, products produced and size of plant.

| Type of Product | Location of Facilities | Size of Plant |
|---|---|---|
| | | (in hectares (1)) |
| Basic petrochemicals | Camaçari | 94.0 |
| Polyethylene | Triunfo | 5.8 |
| Polypropylene | Triunfo | 6.7 |
| Polyethylene | Camaçari | 8.4 |
| PVC/caustic soda/chlorine | Camaçari | 26.2 |
| Caustic soda/EDC/chlorine | Maceió | 10.9 |
| PVC | Marechal Deodoro | 6.0 |
| PVC | Vila Prudente/Capuava | 2.1 |
| PET | Camaçari | 3.8 |
| Caprolactam | Camaçari | 4.8 |

(1) One hectare equals 10,000 square meters.

The descriptions of each of our business units above contain detailed charts showing the location, primary products, annual production capacity and historical annual production for each of our company s production facilities.

We believe that all of our production facilities are in good operating condition. At December 31, 2005, the consolidated net book value of our property, plant and equipment was R$5,964.2 million. Without giving effect to the proportional consolidation of our jointly controlled companies, the net book value of our property, plant and equipment was R$5,359.6 million.

Certain of our properties located in the Northeastern Complex (including our DMT and PET plants and all of the equipment located in these plants) and two of our polyolefins plants in the Southern Complex are mortgaged or pledged to secure certain of our financial transactions.

**Insurance**

We carry insurance for our plants against material damage and consequent business interruption through all risks policies with a total replacement value of US$4.7 billion. Our insurance coverage is underwritten in the Brazilian insurance market by large Brazilian insurance companies. Approximately 89% of our insurance coverage is reinsured in the international insurance market. Our existing all risks policies are in force until November 30, 2006 and are renewed annually.

The material damage insurance provides insurance coverage for losses due to accidents resulting from fire, explosion and machinery breakdown, among others. This coverage has a maximum indemnification limit of US$1.9 billion per event (combined material damage and business interruption coverage) and has deductibles of up to US$5 million depending on the plant. The business interruption coverage provides insurance for losses resulting from interruptions due to any material damage covered by the policy. This coverage is calculated to insure against losses up to US$832 million due to shutdowns extending beyond 60 days. The losses are covered until the plant and production are fully re-established, with maximum indemnity periods ranging from 12 to 24 months.

We also have a third-party liability policy, which covers losses for damages caused to third parties from our operations, including sudden environmental pollution, up to a limit of US$60 million per loss or occurrence.

In addition to these policies, we maintain other insurance policies for specific risks, including directors and officers liability coverage, marine and transportation insurance, automotive insurance and other kinds of coverages that are not covered by our all risks policies.

We do not anticipate having any difficulties in renewing any of our insurance policies and believe that our insurance coverage is reasonable in amount and consistent with industry standards applicable to chemical companies operating in Brazil.

**Antitrust Matters**

Under Brazilian Law No. 8,884/94, any transaction that results in a concentration of market share equal to or greater than 20.0% of any relevant market or that involves any company or group of companies with annual gross sales of R$400.0 million or more must be submitted to and approved by the Brazilian antitrust authorities, which consist of three entities:

- the Administrative Council for Economic Defense *(Conselho Administrativo de Defesa Econômica)*, or CADE, an independent agency consisting of a president and six members;
- the Economic Law Office of the Ministry of Justice *(Secretaria de Direito Econômico)*, or SDE; and
- the Economic Monitoring Office of the Ministry of Finance *(Secretaria de Acompanhamento Econômico)*, or SEAE.

CADE is the antitrust authority responsible for reviewing and authorizing transactions that may lead to economic concentration. SEAE and SDE analyze the economic and legal implications of mergers and acquisitions under Brazilian antitrust law. As part of the antitrust review process, SDE, SEAE, the attorney general of CADE and the Brazilian federal public prosecutor each render preliminary opinions, which are delivered to the members of CADE. The members of CADE then render a final decision.

We completed the Politeno acquisition on April 6, 2006, subject to the final approval of the Brazilian antitrust authorities as permitted by Brazilian law. We submitted the terms and conditions of the Politeno acquisition to the Brazilian antitrust authorities on April 27, 2006. The antitrust authorities will determine whether this transaction adversely impacts competitive conditions or negatively affects consumers in the markets in which we compete. The Brazilian antitrust authorities would have the authority to impose conditions or performance commitments on our company in connection with this transaction.

A favorable non-binding opinion recommending the unconditional approval of the Politeno acquisition, was issued by the SEAE in May 2006. The SDE and CADE are still reviewing these transactions and may disagree with the opinion of the SEAE and may impose conditions on our company.

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**ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS**

*The following discussion of our financial condition and results of operations should be read in conjunction with our audited consolidated financial statements at December 31, 2005 and 2004 and for the three years ended December 31, 2005 included in this annual report, as well as with the information presented under Introduction and Item 3. Key Information Selected Financial Information.*

*The following discussion contains forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from those discussed in the forward-looking statements as a result of various factors, including those set forth in Cautionary Statement with Respect to Forward-Looking Statements and Item 3. Key Information Risk Factors.*

The discussion and analysis of our financial condition and results of operations has been organized to present the following:

- a brief overview of our company and the principal factors that influence our results of operations, financial condition and liquidity;
- a review of our financial presentation and accounting policies, including our critical accounting policies;
- a discussion of the principal factors that influence our results of operations;
- a discussion of our results of operations for the years ended December 31, 2005, 2004 and 2003;
- a discussion of developments since the end of 2005 that may materially affect our results of operations, financial condition and liquidity;
- a discussion of our liquidity and capital resources, including our working capital at December 31, 2005, our cash flows for the years ended December 31, 2005, 2004 and 2003, and our material short-term and long-term indebtedness at December 31, 2005;
- a discussion of our off-balance sheet arrangements;
- a discussion of our capital expenditures and our contractual commitments; and
- a qualitative and quantitative discussion of market risks that we face.

**Overview**

We are the leading petrochemical company in Latin America, based on average annual production capacity in 2005. We are also one of the three largest Brazilian-owned private sector industrial companies, based on net sales revenue in 2004 (the most recent year for which comparative information is currently available). We recorded net income of R$625.8 million in 2005 on net sales revenue of R$13,075.1 million. We produce a diversified portfolio of petrochemical products in our 14 plants in Brazil and have a strategic focus on polyethylene, polypropylene and PVC. We were the first Brazilian company with integrated first and second generation petrochemical production facilities.

Our results of operations have been influenced and will continue to be influenced by a variety of factors, including:

- the growth rate of Brazilian GDP, which affects the demand for our products and, consequently, our domestic sales volume;
- the international market price of naphtha, our principal raw material, which significantly affects the cost of producing our products;
- the expansion of global production capacity for the products that we sell and the growth rate of the global economy;
- the exchange rate of the Brazilian *real* against the U.S. dollar;

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- the level of our outstanding indebtedness and the interest rates we pay on this indebtedness, which affects our net financial expenses;

- the results of operations of those companies in which we have or had minority equity interests, such as Copesul, Politeno and Petroflex, a portion of which are consolidated into our results of operations as required by Brazilian GAAP;

- the tax policies adopted by, and resulting tax obligations to, the Brazilian government and the governments of the Brazilian states in which we operate; and

- our implementation of our corporate competitiveness programs, named Braskem+ and Formula Braskem, which we anticipate will result in meaningful operational improvements and the realization of annual recurring cost reductions over the next few years.

Our financial condition and liquidity is influenced by a variety of factors, including:

- our ability to generate cash flows from our operations;

- prevailing Brazilian and international interest rates and movements in exchange rates, which affect our debt service requirements;

- our ability to continue to be able to borrow funds from Brazilian and international financial institutions and to sell our debt securities in the Brazilian and international securities markets, which is influenced by a number of factors discussed below; and

- our capital expenditure requirements, which consist primarily of maintenance of our operating facilities, expansion of our production capacity and research and development activities.

**Financial Presentation and Accounting Policies**

***Presentation of Financial Statements***

We have prepared our consolidated financial statements at December 31, 2005 and 2004 and for the three years ended December 31, 2005 in accordance with Brazilian GAAP, which differs in certain respects from U.S. GAAP. See note 31 to our audited consolidated financial statements included elsewhere in this annual report.

Our consolidated financial statements have been prepared in accordance with Brazilian Securities Commission Instruction No. 247/96, as amended by Brazilian Securities Commission Instruction Nos. 269/97, 285/98 and 319/99, which we refer to collectively as Instruction 247. Instruction 247 requires our company to proportionally consolidate jointly controlled companies that are not our subsidiaries, principally Copesul, Petroflex and, prior to April 6, 2006, Politeno.

***Reclassifications***

Our consolidated financial statements included in this annual report reflect reclassifications in 2004 and 2003 of some items to provide for a better comparison among 2005, 2004 and 2003. For more information about these reclassifications, see Introduction Financial Statements.

***Business Segments and Presentation of Segment Financial Data***

We have implemented an organizational structure that we believe reflects our business activities and corresponds to our principal products and production processes. We report our results by four market segments to reflect this organizational structure:

*Basic petrochemicals* This segment includes our production and sale of basic petrochemicals and our supply of utilities to second generation producers, including some producers owned or controlled by our company;

*Polyolefins* This segment includes our production and sale of polyethylene and polypropylene;

*Vinyls* This segment includes our production and sale of PVC, caustic soda and chlorine; and

*Business development* This segment includes our production and sale of other second generation petrochemical products, such as PET and caprolactam.

In 2005, sales by our Basic Petrochemicals Unit, our Polyolefins Unit, our Vinyls Unit and our Business Development Unit represented 53.5%, 29.0%, 13.3% and 4.2%, respectively, of our net sales revenue of all segments before reflecting the proportional consolidation of our jointly controlled companies.

We evaluate and manage business segment performance based on information generated from our statutory accounting records, which are maintained in accordance with Brazilian GAAP, and, accordingly, the segment data included in this annual report is presented under Brazilian GAAP. We have included a reconciliation of the operating results of our segments to our consolidated results under Results of Operations below.

***Critical Accounting Policies***

The presentation of our financial condition and results of operations in conformity with Brazilian GAAP requires us to make certain judgments and estimates regarding the effects of matters that are inherently uncertain and that impact the carrying value of our assets and liabilities. Actual results could differ from these estimates. In order to provide an understanding about how we form our judgments and estimates about certain future events, including the variables and assumptions underlying the estimates, and the sensitivity of those judgments to different variables and conditions, we have included comments related to the following critical accounting policies under Brazilian GAAP:

*Provision for doubtful accounts.* We record a provision for doubtful accounts in an amount considered sufficient to cover estimated losses on the realization of the receivables, taking into account the Company s loss experience, and includes amounts in litigation. In order to determine the overall adequacy of the allowance for doubtful accounts, we evaluate the amount and characteristics of our accounts receivable on a quarterly basis.

*Impairment and depreciation and amortization of permanent assets*. We perform annual cash flow studies to determine if the accounting value of our assets, primarily our property, plant and equipment, goodwill and other intangible assets, is compatible with the profitability resulting from the respective business units. If the expected cash flows are lower than the accounting value, we record a provision for impairment of the asset s value. In order to estimate future cash flows, we must make various assumptions about matters that are highly uncertain, including future production and sales, product prices (which we estimate based on current and historical prices, price trends and related factors), future taxes payable and operating costs. We regularly recognize expenses related to the depreciation of our property, plant and equipment and to the amortization of our deferred charges, goodwill and other intangible assets. The rates of depreciation or amortization are based on our or on third-party estimates of the useful lives of the fixed assets or otherwise over the periods during which these assets can be expected to provide benefits to us.

*Valuation of investments other than temporary impairment on investment.* We record long-term investments at cost or under the equity accounting method, depending on our participation in voting capital and the degree of influence that we exercise over the operations of the companies involved. We evaluate the fair value of investments for impairment whenever the performance of the underlying entity indicates that impairment may exist. In such cases, the fair value of the investments is estimated principally based on discounted estimated cash flows using assumptions. Arriving at assumptions and estimates concerning these cash flows is a complex and often subjective process involving estimation of future revenues, costs and taxes.

*Valuation of derivative instruments*. We use swaps, non-deliverable forwards, non-deliverable options and other derivative instruments to manage risks from changes in foreign exchange and interest rates. We record these instruments at their estimated fair market value based on market quotations for similar instruments, and based on standard mark-to-market practices, which take into account reliable market curves for interest rates, foreign exchange rates and volatility.

*Pension plans*. For defined benefit plans that we sponsor, we calculate our funding obligations based on calculations performed by independent actuaries using assumptions that we provide about interest rates, investment returns, levels of inflation, mortality rates and future employment levels. These assumptions directly impact our liability for accrued pension costs and the amounts we record as pension costs. In June 2005, we announced that we intend to withdraw as a sponsor of our defined benefit plans. Unrecognized actuarial gains and losses are amortized either over the estimated future service period of employees or over the estimated period of the plan final settlement, whichever is less.

*Deferred taxes*. We recognize deferred tax assets and liabilities based on the differences between the financial statement carrying amounts and the tax basis of assets and liabilities using prevailing tax rates. We regularly review any deferred tax assets for recoverability and reduce their carrying value, as required, based on our historical taxable income, projected future taxable income and the expected timing of any reversals of existing temporary differences. If one of our subsidiaries operates at a loss or is unable to generate sufficient future taxable income, or if there is a material change in the actual effective tax rates or the time period within which the underlying temporary differences become taxable or deductible, we evaluate the need to reduce partially or completely the carrying value of our deferred tax assets.

*Contingencies*. We are currently involved in numerous judicial and administrative proceedings, as described under Item 8. Financial Information Legal Proceedings and in notes 10, 17, 18 and 21 to our consolidated financial statements. We record accrued liabilities for contingencies that we deem probable of creating an adverse effect on the result of operations or financial condition. We believe that these contingencies are properly recognized in our financial statements. We are also involved in judicial and administrative proceedings that are aimed at obtaining or defending our legal rights with respect to taxes that we believe to be unconstitutional or otherwise not required to be paid by our company. We believe that these proceedings will ultimately result in tax credits or benefits, which we do not recognize in our financial statements until the contingency has been resolved. When, based on favorable but appealable court decisions, we use tax credits or benefits in dispute to offset current tax obligations, we establish a provision equal to the amount used and maintain the provision until a final decision on those credits or benefits. Our provisions include interest on the tax obligations we have offset with disputed credits or benefits at the interest rate defined in the relevant tax law.

**Principal Factors Affecting Our Results of Operations**

***Growth of Brazil s Gross Domestic Product and Domestic Demand for Our Products***

Sales in Brazil represented 79.8% of our net sales revenue in 2005. As a Brazilian company with substantially all of our operations in Brazil, we are significantly affected by economic conditions in Brazil. Our results of operations and financial condition have been, and will continue to be, affected by the growth rate of GDP in Brazil because our products are used in the manufacture of a wide range of consumer and industrial products.

Because of our significant market share in many of the Brazilian markets in which our petrochemical products are sold, fluctuations in Brazilian demand for polyethylene, polypropylene and PVC affect our production levels and net sales revenue. GDP in Brazil grew at a compound average annual rate of 2.2% from 1996 through 2005. From 1996 through 2005, the consumption volumes in Brazil of polyethylene, polypropylene and PVC increased at compound average annual rates of 4.3%, 7.3% and 2.0%, respectively.

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In 2003, GDP in Brazil declined by 0.2%. In 2003, Brazilian consumption volumes of polyethylene decreased by 2.1%, polypropylene increased by 2.9% and PVC decreased by 12.4%, respectively, compared to 2002. The decreased consumption volumes of polyethylene and PVC were primarily a result of reduced economic activity.

In 2004, GDP in Brazil increased by 5.2%, the highest annual growth rate since 1994. In 2004, Brazilian consumption volumes of polyethylene increased by 13.9%, polypropylene increased by 11% and PVC increased by 11.7%, respectively, compared to 2003. The increased consumption volumes of these thermoplastics resulted primarily from the recovery of economic activity in Brazil.

In 2005, GDP in Brazil increased by 2.3%. In 2005, Brazilian consumption volumes of polyethylene decreased by 1.7%, polypropylene increased by 2.9% and PVC increased by 2.4%, respectively, compared to 2004. The modest increase in Brazilian consumption of polypropylene and PVC resulted from GDP growth that was lower than expected.

Brazilian GDP growth has fluctuated significantly, and we anticipate that it will likely continue to do so. Our management believes that economic growth in Brazil should positively affect our future net sales revenue and results of operations. However, continued low growth or a recession in Brazil would likely reduce our future net sales revenue and have negative impacts on our results of operations.

Our management believes that there has been a trend in Brazil during the last several years toward the substitution of plastics for more traditional materials, such as steel, aluminum, glass and paper. Our management anticipates that this trend will continue to stimulate the domestic demand for petrochemical products suitable for use in a variety of applications, including construction, industrial processes, agriculture and packaging. However, trends in the substitution of materials depend on many factors beyond our control, and the current beliefs of our management may prove to be incorrect.

***Effects of Fluctuations in Naphtha Prices***

Fluctuations in the international market price of naphtha have significant effects on our costs of goods sold and the prices that we are able to charge our customers for our first and second generation products.

*Effects on Cost of Sales*

Naphtha is the principal raw material used by our Basic Petrochemicals Unit and, indirectly, in our other business units. Purchases of naphtha represented 86.6% of the total cost of sales and services rendered of our Basic Petrochemicals Unit in 2005. Naphtha represented 71.7% of our direct and indirect consolidated cost of sales and services rendered in 2005, both directly and indirectly through the cost of basic petrochemicals that we purchased from Copesul.

The cost of naphtha varies in accordance with international market prices, which fluctuate depending upon the supply and demand for oil and other refined petroleum products. We purchase naphtha under a long-term supply contract with Petrobras, and we import naphtha through our terminal at Aratú. The prices that we pay for naphtha under all of these arrangements are based on the Amsterdam-Rotterdam-Antwerp market price. As a result, fluctuations in the Amsterdam-Rotterdam-Antwerp market price for naphtha have a direct impact on the cost of our first generation products.

Because the primary raw materials of our Polyolefins and Vinyls Units, principally ethylene and propylene, are first generation products produced by our Basic Petrochemicals Unit and Copesul, fluctuations in the Amsterdam-Rotterdam-Antwerp market price for naphtha result in similar fluctuations in the cost of the primary raw materials of these units.

The international price of naphtha has fluctuated significantly in the past, and we expect that it will continue to do so in the future. Significant increases in the price of naphtha and, consequently, the cost of producing our products, would likely reduce our gross margins and our results of operations to the extent that we are unable to pass all of these increased costs on to our customers and could result in reduced sales volumes of our products. Conversely, significant decreases in the price of naphtha and, consequently, the cost of producing our products, would likely increase our gross margins and our results of operations and could result in increased sales volumes if this lower cost leads us to lower our prices. In periods of high volatility in the U.S. dollar price of naphtha, there is usually a lag between the time that the U.S. dollar price increases or decreases and the time that we are able to pass on increased or reduced costs to our customers in Brazil. These pricing mismatches decrease when the the U.S. dollar price of naphtha is less volatile.

We do not currently hedge our exposure to changes in the prices of naphtha because a portion of our sales are exports payable in foreign currencies and linked to the international market prices of naphtha and also because the prices of our polyethylene, polypropylene and PVC products sold in Brazil generally reflect changes in the international market prices of these products.

*Effects on Prices of Our Products*

In 2005, the price of ethylene that we charged Politeno and one of our other large customers, which collectively represented 90.4% of our ethylene sales to third parties in 2005, was based on a margin sharing system described in Item 4. Information on the Company Basic Petrochemicals Unit Sales and Marketing of Our Basic Petrochemicals Unit. These prices reflect both the international market prices for naphtha and the international and domestic prices for second generation products. Prior to 2005, we used a margin sharing system for all of our ethylene customers, including our other business units. In 2005, we determined the prices that we charged our ethylene customers, other than our two largest ethylene customers, by reference to international market prices. In addition, we are negotiating with those ethylene customers which still use the margin sharing system to terminate the margin sharing system of ethylene pricing and to institute a market pricing system.

The prices that we charge some of our customers for propylene are based on our ethylene prices and the ratio of the European contract price for propylene to the European contract price for ethylene. Over the past several years, this ratio has increased. For the remainder of our customers, our prices for propylene are based on the European contract price and prevailing prices set by U.S. Gulf producers. We are applying this market pricing methodology to a growing number of our customers. The prices that we charge for butadiene and para-xylene are based on the United States contract price for these products. The prices that we charge for benzene and ortho-xylene are based on the contract prices for these products in the United States and Europe. Because European producers of basic petrochemical products primarily use naphtha as a raw material, changes in the European contract prices are strongly influenced by fluctuations in international market prices for naphtha. As our cost structures are similar to the cost structures of European producers, to the extent that our prices are based on the European contract prices for our products, the prices that we charge for these products are significantly influenced by international market prices for naphtha.

We negotiate the *real* prices for certain of our products, principally polyethylene, polypropylene and PVC, on a monthly basis with our domestic customers. We attempt to revise our prices to reflect changes in the international market prices of these products and the appreciation or depreciation of the *real* against the U.S. dollar. However, during periods of high volatility in international market prices or exchange rates, we are sometimes unable to reflect these changes fully in our prices quickly.

The international market prices of our petrochemical products have fluctuated significantly, and we believe that they will continue to do so. Significant increases in the international market prices of our petrochemical products and, consequently, the prices that we are able to charge, would likely increase our net sales revenue and our results of operations to the extent that we are able to maintain our operating margins and increased prices do not reduce sales volumes of our products. Conversely, significant decreases in the international prices of our petrochemical products, and, consequently, the prices that we charge, would likely reduce our net sales revenue and our results of operations if we are unable to increase our operating margins or these reduced prices do not result in increased sales volumes of our products.

***Cyclicality Affecting the Petrochemical Industry and Capacity Utilization***

*Capacity Expansions*

Global consumption of petrochemical products has increased significantly over the past 30 years. Due to this growth in consumption, producers have experienced periods of insufficient capacity for these products. Periods of insufficient capacity, including some due to raw material shortages, have usually resulted in increased capacity utilization rates and international market prices for our products, leading to increased operating margins. These periods have often been followed by periods of capacity additions, which have resulted in declining capacity utilization rates and international selling prices, leading to declining operating margins.

We expect that these cyclical trends in international selling prices and operating margins relating to global capacity shortfalls and additions will likely persist in the future, principally due to the continuing impact of four general factors:

- cyclical trends in general business and economic activity produce swings in demand for petrochemicals;
- during periods of reduced demand, the high fixed cost structure of the capital intensive petrochemicals industry generally leads producers to compete aggressively on price in order to maximize capacity utilization;
- significant capacity additions, whether through plant expansion or construction, can take two to three years to implement and are therefore necessarily based upon estimates of future demand; and
- as competition in petrochemical products is generally focused on price, being a low-cost producer is critical to improved profitability. This favors producers with larger plants that maximize economies of scale, but construction of plants with high capacity may result in significant increases in capacity that can outstrip demand growth.

Rio Polímeros, a Brazilian petrochemical company, commenced operations of a major petrochemical plant in Brazil in 2005. The maximum annual capacity of this plant is 520,000 tons of ethylene, 75,000 tons of propylene and 540,000 tons of polyethylene. This plant is in the process of ramping up its production towards its annual capacity. In addition, Solvay expanded its annual PVC production capacity by 30,000 tons in December 2005. In 2004, Polibrasil commenced operation of polypropylene facility in Mauá, São Paulo with an annual capacity of 300,000 tons. In 2004, we increased our annual production capacity of polypropylene by 100,000 tons and our annual production capacity of para-xylene by 50,000 tons. In 2005, we increased our annual production capacity of PVC by 50,000 tons and our annual production capacity of polyethylene by 30,000 tons.

Based on historical growth of Brazilian domestic demand for polyethylene, polypropylene and PVC, we believe that this additional capacity will be absorbed by the domestic market over the next several years. Although there may be a short period of overcapacity in the domestic market for several of our petrochemical products following Rio Polímeros commencement of operations, we believe that export opportunities will be available for the sale of these products not sold domestically. We cannot assure you, however, that the additional capacity will be so absorbed by the domestic market or that satisfactory export opportunities will be available for products not sold domestically. In the event that this additional production is not absorbed domestically or sold in export markets, there may be resulting pressure on prices for the affected products, which could adversely affect our net sales revenues, gross margins and overall results of operations.

*Capacity Utilization*

Our operations are capital intensive. Accordingly, to obtain lower unit production costs and maintain adequate operating margins, we seek to maintain a high capacity utilization rate at all of our production facilities.

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The table below sets forth capacity utilization rates with respect to the production facilities for some of our principal products for the years ended December 31, 2005, 2004 and 2003.

| | Year ended December 31, | | |
|---|---|---|---|
| | 2005 | 2004 | 2003 |
| Ethylene | 91% | 87% | 84% |
| Polyethylene(1) | 94 | 91 | 83 |
| Polypropylene | 94 | 96(2) | 95(2) |
| PVC(3) | 95 | 90 | 85 |

(1) Without giving effect to a 30,000 ton increase of our annual production capacity in November 2005.
(2) Without giving effect to a 100,000 ton increase of our annual production capacity in July 2004.
(3) Without giving effect to a 50,000 ton increase of our annual production capacity in December 2005.

The utilization rate of our ethylene production capacity was adversely affected:

- during 2003 as a result of an unscheduled shutdown of one of our olefins units for 11 days due to a maintenance problem; and
- during 2004 as a result of the shutdown of the Olefins 2 unit of our Basic Petrochemicals Unit for 36 days for scheduled maintenance and inspection.

***Effect of Export Levels on Our Financial Performance***

We generally obtain higher prices in Brazil for our products than the prevailing international prices. The difference in prices between the Brazilian and export markets results from:

- high costs of transporting products to and within Brazil;
- warehousing, and other logistics costs; and
- tariffs and duties.

In addition, we are generally able to charge higher prices for our products than the *real* price of imports because we are able to provide better product customization services to our customers than sellers of imported products.

During periods in which the domestic demand for our products is reduced, we actively pursue export opportunities for our products in order to maintain capacity utilization rates. During periods of increased domestic demand for our products, our export sales volumes may decline as we increase domestic sales of our products.

In 2005, 20.2% of our net sales revenue was derived from export sales of our products as compared with 19.1% of our net sales revenue in 2004. Net sales revenues derived from export sales increased by 11.5% in 2005, as a result of the implementation of our strategy to increase our presence in foreign markets.

In 2005, exports to other countries in the Americas accounted for 67% of our export sales, with the remainder of our exports sold in Europe, which accounted for 21% of our export sales, and the Far East, which accounted for 12% of our export sales. Aggregate exports of polyethylene, polypropylene and PVC to Argentina increased by 11% in 2005, reflecting improvements in the Argentine economy.

Our ability to export to other South American countries is a function of the level of economic growth in these countries and other economic conditions, including prevailing inflation rates. We believe that significant growth in the global economy would likely lead to increased global demand and international market prices for our products, and consequently increased domestic prices for our products. In addition, increased global demand for our products would enhance our ability to export our products in the event that the Brazilian economy does not similarly expand. Conversely, slow or negative growth of the global economy would have the opposite effects on our company.

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***Effects of Fluctuations in Exchange Rates Between Real and U.S. Dollar***

Our results of operations and financial condition have been, and will continue to be, affected by the rate of depreciation or appreciation of the *real* against the U.S. dollar because:

- a substantial portion of our net sales revenue is linked to U.S. dollars;
- our costs for some of our raw materials, principally naphtha and certain catalysts required in our production processes, are incurred in U.S. dollars or are U.S. dollar-linked;
- we have operating expenses, and make other expenditures, that are denominated in or linked to U.S. dollars; and
- we have significant amounts of U.S. dollar-denominated liabilities that require us to make principal and interest payments in U.S. dollars.

Virtually all of our sales are of petrochemical products for which there are international market prices expressed in U.S. dollars. We generally attempt to set prices that take into account the international market prices for our petrochemical products and variations in the *real*/U.S. dollar exchange rate. As a result, although a significant portion of our net sales revenue is in *reais,* substantially all of our products are sold at prices that are based on international market prices that are quoted in U.S. dollars.

The price of naphtha, our principal raw material, is linked to the U.S. dollar. Our naphtha purchase contract with Petrobras provides that the prices that we pay to Petrobras for naphtha in any month are established based on the average Amsterdam-Rotterdam-Antwerp market price for naphtha in U.S. dollars during the previous month, converted into *reais* at the *real*/U.S. dollar exchange rate in effect on the last day of the previous month. Fluctuations in the *real* affect the cost of naphtha and other U.S. dollar-linked or imported raw materials.

When the *real* depreciates against the U.S. dollar, assuming naphtha costs and international market prices of our products remain constant in U.S. dollars, the production cost for our products increases and we generally attempt to increase the prices for our products in *reais* (to the extent possible in light of then-prevailing market conditions in Brazil), which may result in reduced sales volumes of our products. To the extent that our price increases are not sufficient to cover the increased costs for raw materials, our operating margin decreases. Conversely, when the *real* appreciates against the U.S. dollar, assuming naphtha costs and international market prices of our products remain constant in U.S. dollars, the production cost for our products decreases and we generally decrease the prices for our products in *reais*, which may result in increased sales volumes of our products. In periods of high volatility in the *real*/U.S. dollar exchange rate, there is usually a lag between the time that the U.S. dollar appreciates or depreciates and the time that we are able to pass on increased or reduced costs in *reais* to our customers in Brazil. These pricing mismatches decrease when the *real*/U.S. dollar exchange rate is less volatile.

Our consolidated U.S. dollar-denominated indebtedness represented 51.2% of our outstanding indebtedness at December 31, 2005, excluding related party debt. As a result, when the *real* depreciates against the U.S. dollar:

the interest costs on our U.S. dollar-denominated indebtedness increase in *reais*, which negatively affects our results of operations in *reais*;

the amount of our U.S. dollar-denominated indebtedness increases in *reais*, and our total liabilities and debt service obligations in *reais* increase; and

our financial expenses tend to increase as a result of foreign exchange losses that we must record.

Conversely, when the *real* appreciates against the U.S. dollar:

the interest costs on our U.S. dollar-denominated indebtedness decrease in *reais*, which positively affects our results of operations in *reais*;

- the amount of our U.S. dollar-denominated indebtedness decreases in *reais*, and our total liabilities and debt service obligations in *reais* decrease; and

- our financial expenses tend to decrease as a result of foreign exchange gains that we must record.

Any major devaluation of the *real* against the U.S. dollar would significantly increase our financial expenses and our short-term and long-term indebtedness, as expressed in *reais*. Conversely, any major appreciation of the *real* against the U.S. dollar would significantly decrease our financial expenses and our short-term and long-term indebtedness, as expressed in *reais*.

Export sales, which enable us to generate receivables payable in foreign currencies, tend to provide a hedge against a portion of our U.S. dollar-denominated debt service obligations, but they do not fully match them. Accordingly, we often enter into hedges to mitigate exchange rate fluctuations in our U.S. dollar-denominated indebtedness. To further mitigate our exposure to exchange rate risk, we try, where possible, to enter into trade finance loans for our working capital needs, which funding is generally available at a lower cost because it is linked to U.S. dollar exports. However, future U.S. dollars that we generate from exports may not be in an amount sufficient to cover all of our U.S. dollar trade finance liabilities.

Inflation affects our financial performance by increasing some of our operating expenses denominated in *reais* (and not linked to the U.S. dollar). A significant portion of our costs of sales and services rendered, however, are linked to the U.S. dollar and are not substantially affected by the Brazilian inflation rate. In addition, some of our *real*-denominated debt is indexed to take into account the effects of inflation. Under this debt, the principal amount generally is adjusted with reference to the General Price Index Market (IGP-M), an inflation index, so that inflation results in increases in our financial expenses and debt service obligations. In addition, a significant portion of our *real*-denominated debt bears interest at the TJLP or the CDI rate, which are partially adjusted for inflation.

***Effect of Level of Indebtedness and Interest Rates***

At December 31, 2005, our total outstanding consolidated indebtedness on a consolidated basis, excluding related party debt, was R$5,361.1 million. The level of our indebtedness results in significant financial expenses that are reflected in our statement of operations. Financial expenses consist of interest expense, exchange variations of U.S. dollar- and other foreign currency-denominated debt, foreign exchange losses or gains, and other items as set forth in notes 15 and 23 to our consolidated financial statements. In 2005, we recorded total financial expenses of R$675.8 million, of which R$347.0 million consisted of interest expense and R$556.9 million consisted of foreign exchange gains. By contrast, in 2004, we recorded total financial expenses of R$1,307.2 million, of which R$595.3 million consisted of interest expense and R$425.4 million consisted of foreign exchange gains. The interest rates that we pay depend on a variety of factors, including prevailing Brazilian and international interest rates and risk assessments of our company, our industry and the Brazilian economy made by potential lenders to our company, potential purchasers of our debt securities and the rating agencies that assess our company and its debt securities.

Standard & Poor s and Fitch maintain ratings of our company and our debt securities. On a global basis, Standard & Poor s maintains a local currency rating of our company of BB and a foreign currency rating for our company of BB, and on a local basis Standard & Poor s maintains a rating for our company of br AA/Stable Outlook. On a global basis, Fitch maintains a local currency rating for our company of BB+/Stable Outlook and a foreign currency rating for our company of BB/Positive Outlook, and on a local basis Fitch maintains a national rating of our company of AA- (bra)/Stable Outlook. We have not been informed of any proposed actions by either of these rating agencies to further modify their ratings on our company or its indebtedness. Any rating downgradings in the future would likely result in increased interest and other financial expenses relating to borrowings and debt securities and could adversely affect our ability to obtain such financing on satisfactory terms or in amounts required by us.

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***Results of Operations of Jointly Controlled Companies***

We own 29.5% of the voting and total share capital of Copesul. At December 31, 2005, we also owned 34.0% of Politeno s total share capital, including 35.0% of its voting share capital. The operations of Copesul are similar to the operations of our Basic Petrochemicals Unit and the operations of Politeno are similar to the operations of our Polyolefins Unit. Accordingly, the results of operations of these companies are influenced by factors similar to the factors that influence our results of operations. However, Copesul has, and prior to the Politeno acquisition, Politeno had, management that is independent from ours and a capital structure, including levels of indebtedness and corresponding levels of financing costs, different from ours. In addition, we own 20.1% of the voting and total share capital of Petroflex. Petroflex has management that is independent from ours and a capital structure, including levels of indebtedness and corresponding levels of financing costs, that is different from ours. For more information about the operations of Petroflex, see Item 4. Information on the Company Jointly Controlled Companies and Joint Venture Petroflex.

As a result of the application of Instruction 247 to our consolidated financial statements, we are required to proportionally consolidate the results of jointly controlled companies that are not our subsidiaries, such as Copesul, Politeno and Petroflex. Consequently, our results of operations are subject to fluctuations that depend on the results of these jointly controlled companies. However, in evaluating our results of operations, cash flows and liquidity, our management relies on financial information that does not include the effects of proportional consolidation, principally because we have limited, if any, control over the operations and policies of the companies whose results we are required to proportionally consolidate with our own. In our discussion of our results of operations and our discussion of our liquidity and capital resources, we have provided supplemental information drawn from our accounting records with respect to our results of operations, working capital, cash flows and indebtedness without giving effect to this proportional consolidation to provide holders of bonds with information that our management believes more accurately reflects the results of operations and financial position of our company.

As a result of the Politeno acquisition described under Recent Developments, we will fully consolidate Politeno s results in our consolidated financial statements at dates and for periods following this acquisition.

***Effect of Taxes on Our Income***

We are subject to a variety of generally applicable Brazilian federal and state taxes on our operations and results.

*Tax Exemptions*

We are generally subject to Brazilian federal income tax at an effective rate of 25%, which is the standard corporate tax rate in Brazil. We have available certain federal tax exemptions based upon federal law that offers tax incentives to companies that locate their manufacturing operations in the Brazilian states of Bahia and Alagoas. These exemptions have been granted for varying lengths of time to each of our manufacturing plants located in these states.

We are exempt from corporate income tax on the profits arising from the sale of PVC manufactured at our Alagoas and PET manufactured at our plant in the Northeastern Complex until December 31, 2008. In addition, we are entitled to pay only 25% of the statutory income tax rate on the profits arising from the sale of:

PVC manufactured at our plant in the Northeastern Complex until December 31, 2014;

polyethylene manufactured at our polyethylene plants in the Northeastern Complex and basic petrochemical products manufactured in the Northeastern Complex, until December 31, 2011; and

caustic soda, chlorine and EDC produced at our plants in the Northeastern Complex and Alagoas, and caprolactam manufactured in the Northeastern Complex until December 31, 2012.

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Each of our exemptions entitles us to pay only 87.5% of the statutory income tax rate on the profits arising from products manufactured at these plants for a period of one or more years after the dates set forth above.

At the end of each year, if we or any of our affected subsidiaries has taxable profit resulting from the operations described above, income tax expense is calculated without giving effect to the exemption or reduction and the income tax benefit of the exemption or reduction is deducted from income tax payable and credited to a capital reserve, which can only be used to increase capital, absorb losses which exceed retained earnings and profits reserves as defined in the Brazilian Corporation Law or redeem or repurchase share capital or participation certificates. We used R$463.2 million of this capital reserve to absorb all of our retained losses in December 2004.

Due to operating losses sustained by us in the past, we had R$167.9 million of deferred tax assets arising from R$671.5 million of tax loss carryforwards available at December 31, 2005. Income tax loss carryforwards available for offset in Brazil do not expire. However, the annual offset is limited to 30% of our adjusted net income. This limit also affects the Social Contribution on Net Income.

Our export sales are currently exempt from PIS (a federal value-added tax), COFINS (a federal value-added tax), IPI (a federal value-added tax on industrial products) and the Tax on the Circulation of Merchandise and Services (*Imposto Sobre a Circulação de Mercadorias e Serviços*), or ICMS (a state value-added tax on sales and services), under generally available exemptions, subject to our compliance with the requirements of these exemptions.

The eventual expiration of the income tax exemptions will not affect our net income because we record the full amount of the income tax in our income statement and credit the amount of the income tax exemptions to a reserve account in shareholders equity to increase our capital or absorb our losses.

*Tax Disputes*

We pay IPI tax on industrial products that we manufacture. The regulations governing the IPI tax assess this tax on a non-cumulative basis, which means that companies may offset their IPI tax obligations with the amount of IPI taxes paid by suppliers earlier in the production chain. The Brazilian federal tax authorities have asserted that purchases of raw materials that are tax-exempt, non-taxable or taxed at a zero percent rate do not generate IPI tax credits, because they maintain that there is no legal provision that expressly authorizes these credits. We believe that this interpretation is contrary to Article 153, paragraph 3 of the Brazilian Constitution, which sets forth the principle of non-cumulative taxation in a broad manner and does not exclude purchases of raw materials that are tax-exempt, non-taxable or taxed at a zero percent rate. OPP Química brought a suit against the Brazilian government claiming that it had the right to IPI tax credits on its purchases of raw materials that are in a zero percent tax bracket. In December 2002, the Brazilian Federal Supreme Court ruled in favor of OPP Química in this suit.

The Brazilian government appealed the decision of the Brazilian Federal Supreme Court. As the appeal does not challenge the validity of IPI tax credits, but only the method of calculating monetary adjustments on those credits and the time period for appealing the decision of the Brazilian Federal Supreme Court has expired, we believe that (1) the decision acknowledging the validity of the IPI tax credits is no longer subject to appeal, and (2) it is reasonably possible that we could lose the appeal regarding the method of calculating monetary adjustments on those credits. If the Brazilian Government prevails in this appeal, we could lose all or part of the IPI tax credits attributable to monetary adjustments. We recognized IPI tax credits in an aggregate amount of R$1,030.1 million in December 2002. Of this total tax credit, we used R$265.6 million during the year ended December 31, 2002, R$364.9 million during the year ended December 31, 2003 and the remainder during the year ended December 31, 2004 to offset IPI and other federal tax obligations.

Although the ruling of the Brazilian Federal Supreme Court only applies to our operations in the State of Rio Grande do Sul, we have also brought litigation against the Brazilian government in respect of our purchases of raw materials in the States of São Paulo, Bahia and Alagoas seeking to obtain a similar tax credit. We have not recognized any assets or gains in relation to our claims in these states.

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We are currently involved in numerous tax proceedings. We have established provisions based on our obligations under current legislation, utilization of the contingent IPI tax credits, and our estimated costs of resolving other claims in which we believe we have a probable tax loss. The tax contingencies relate primarily to the Social Contribution on Net Income, PIS, COFINS and IPI. If any of these legal proceedings is decided adversely to us, our results of operations or financial condition could be materially adversely affected. For more information on our tax proceedings, the amounts claimed by governmental authorities and the amounts we have reserved against some of these claims, see Item 8. Financial Information Legal Proceedings Tax Proceedings.

***Corporate Competitiveness Programs***

*Braskem+ Program*

In 2004, we commenced implementation of a corporate and operational excellence program called Braskem+. The Braskem+ program seeks to:

- improve our operating performance and productivity;
- reduce our operating and maintenance costs; and
- position Braskem among the most competitive petrochemical companies in the world.

We anticipate that this program will allow us to create value in all stages of the petrochemical cycle.

In connection with the development of the Braskem+ program, we engaged a leading consulting firm to analyze our industrial practices and compare them to benchmarking practices in the global petrochemical sector. Through this analysis, we identified 210 initiatives designed to further improve, among other things, our capacity utilization and variable and fixed costs. We implemented 59 of these initiatives at a total cost of R$23.5 million in 2004 and 39 of these initiatives at a total cost of R$117.2 million in 2005, resulting in an aggregate of approximately R$256.0 million in cost savings on a recurring annual basis, as estimated by our management. We cannot assure holders of our class A preferred shares and the ADS that we will realize the full benefit of the identified annual cost savings in upcoming years. To the extent that we fail to do so, for any reason, in any year, our results of operations for that year may be adversely affected.

*Formula Braskem*

In 2005, we commenced a new program that we call Formula Braskem to implement a comprehensive integrated management system. Formula Braskem is intended to incorporate the best practices in the international petrochemical industry in our management systems and the most recent technological developments available in the marketplace. This program, together with the Braskem+ program, is designed to support our expansion and future internationalization, and we expect to realize productivity and efficiency gains through their implementation. In addition, we believe that the implementation of Formula Braskem will assist us with our compliance with the requirements of the U.S. Sarbanes-Oxley Act of 2002 in a manner consistent with our commitment to transparency and corporate governance.

We anticipate that Formula Braskem will be operational by October 2006. We have engaged SAP an affiliate of SAP AG, and Accenture, an affiliate of Accenture Ltd., to assist us in implementing Formula Braskem under agreements that provide for (1) the payment of bonuses to SAP and Accenture in the event that we achieve identified annual cost savings as a result of the implementation of Formula Braskem in excess of those identified in our calculations of the projected net present value of this project, and (2) the payment of bonuses to SAP in the event that Formula Braskem is operational prior to its target date. Conversely, these agreements provide for the payment of penalties by Accenture and the forfeiture of any bonuses by SAP in the event that Formula Braskem does not become operational until after the target date. We have a dedicated team of approximately 110 employees working together with SAP and Accenture on the implementation of Formula Braskem which we expect to implement at a cost of approximately R$130 million. We cannot assure holders of our class A preferred shares and the ADSs that we will realize the full benefit of the identified annual cost savings in upcoming years. To the extent that we fail to do so, for any reason, in any year, our results of operations for that year may be adversely affected.

**Recent Developments**

On April 6, 2006, we purchased all of the common and preferred shares of Politeno that were owned by SPQ, a subsidiary of Suzano, Sumitomo and Itochu. We paid a portion of the purchase price for these shares in an aggregate amount of the *real*-equivalent of US$111.3 million (US$60.6 million to SPQ and a total of US$50.7 to Sumitomo and Itochu) on April 6, 2006. The remainder of the purchase price for these shares will be calculated based on an earn-out formula that will take into account Politeno s operating performance, measured by fluctuations in polyethylene and ethylene margins in the Brazilian petrochemical market during the 18 months following the execution date of this agreement. As a result of the Politeno acquisition, we now own 100% of the voting share capital and 96.2% of the total share capital of Politeno.

On April 28, 2006, we issued and sold US$200.0 million aggregate principal amount of our 9.00% Perpetual Bonds. Interest on these bonds is payable quarterly in arrears in January, April, July and October in each year. We may, at our option, redeem these bonds, in whole or in part, at 100% of their principal amount plus accured interest and additional amounts, if any, on any interest payment date on or after April 28, 2011, provided that, if we redeem these bonds in part, at least US$100 million aggregate principal amount of these bonds must remain outstanding following any partial redemption.

On May 4, 2006, we announced that our board of directors has authorized a share buy-back program under which we may repurchase up to 13,896,133 class A preferred shares and up to 1,400,495 common shares. We are authorized to purchase these shares at market prices over the São Paulo Stock Exchange at any time and from time to time prior to October 31, 2006. Shares that are repurchased may be held in treasury and subsequently resold or cancelled.

At an extraordinary shareholders meeting on May 31, 2006, our shareholders approved our merger with Polialden and the conversion of 2,632,043 of our class A preferred shares into 2,632,043 of our common shares in order to maintain the required minimum ratio of our common shares to preferred shares in accordance with the Brazilian Corporation Law after completion of our merger with Polialden. In connection with this merger, we issued 7,878,825 of our class A preferred shares in exchange for 264,886,083 of Polialden s preferred shares.

**Results of Operations**

The following discussion of our results of operations is based on our consolidated financial statements prepared in accordance with Brazilian GAAP.

The discussion of the results of our business segments is based upon financial information reported for each of the four segments of our business, as presented in the table below. There are certain differences between the concepts used by our company in preparing information about segments and the requirements of Brazilian GAAP as applied in the statutory financial statements. The principal differences are:

investments in certain jointly controlled companies which are required to be proportionally consolidated under Brazilian GAAP are not considered as part of any segment for segment reporting purposes; and

operating income for segment reporting purposes does not consider the results of investments in associated companies and financial income and expenses, whereas such results and income and expenses are classified as operating items for statutory reporting purposes.

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The following tables set forth the operating results of each of our segments and the reconciliation of these results of our segments to our consolidated results of operations. This segment information was prepared on the same basis as the information that our senior management uses to allocate resources among segments and evaluate their performance. We evaluate and manage the performance of our segments based on information generated from our statutory accounting records maintained in accordance with Brazilian GAAP and reflected in our consolidated financial statements. However, the operating income presented in the following tables does not include financial expenses, financial income and investment in associated companies.

| | Year ended December 31, 2005 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| **(in millions of *reais*)** | **Basic Petro- chemicals** | **Polyolefins** | **Vinyls** | **Business Develop- ment** | **Total segments** | **Elimi- nations** | **Total prior to CVM 247** | **CVM 247** | **Consoli- dated** |
| Net sales revenue | R$ 7,226.7 | R$ 3,919.0 | R$ 1,794.1 | R$ 569.0 | R$ 13,508.8 | R$ (1,894.2) | R$ 11,614.6 | R$ 1,460.5 | R$ 13,075.1 |
| Cost of sales and services rendered | (6,138.5) | (3,182.8) | (1,271.9) | (552.9) | (11,146.1) | 1,827.6 | (9,318.5) | (1,043.2) | (10,361.7) |
| Gross profit | 1,088.2 | 736.2 | 522.2 | 16.1 | 2,362.7 | (66.6) | 2,296.1 | 417.3 | 2,713.4 |
| Operating expenses: | | | | | | | | | |
| Selling, general and administrative | (250.3) | (229.0) | (89.2) | (18.2) | (586.7) | (89.7) | (676.4) | (110.7) | (787.1) |
| Depreciation and amortization | 0.0 | (6.9) | (0.8) | (0.3) | (8.0) | (342.2) | (350.2) | (5.4) | (355.6) |
| Other, net | 57.1 | 53.0 | 6.6 | 9.2 | 125.9 | (56.1) | 69.8 | (47.0) | 22.8 |
| Operating income | R$ 895.0 | R$ 553.3 | R$ 438.8 | R$ 6.8 | R$ 1,893.9 | R$ (554.6) | R$ 1,339.3 | R$ 254.2 | R$ 1,593.5 |

| | Year ended December 31, 2004 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| **(in millions of *reais*)** | **Basic Petro- chemicals** | **Polyolefins** | **Vinyls** | **Business Develop- ment** | **Total segments** | **Elimi- nations** | **Total prior to CVM 247** | **CVM 247** | **Consoli- dated** |
| Net sales revenue | R$ 6,480.0 | R$ 3,489.4 | R$ 1,858.8 | R$ 620.8 | R$ 12,449.0 | R$ (1,404.8) | R$ 11,044.2 | R$ 1,345.3 | R$ 12,389.5 |
| Cost of sales and services rendered | (5,330.1) | (2,523.0) | (1,157.1) | (564.9) | (9,575.1) | 1,269.4 | (8,305.7) | (917.3) | (9,223.0) |
| Gross profit | 1,149.9 | 966.4 | 701.7 | 55.9 | 2,873.9 | (135.4) | 2,738.5 | 428.0 | 3,166.5 |
| Operating expenses: | | | | | | | | | |
| Selling, general and administrative | (213.8) | (199.1) | (80.1) | (24.9) | (517.9) | (62.8) | (580.7) | (96.3) | (677.0) |
| Depreciation and amortization | (2.6) | (5.9) | (0.6) | (0.7) | (9.8) | (344.0) | (353.8) | (5.9) | (359.7) |
| Other, net | 22.2 | 6.3 | 14.9 | 2.6 | 46.0 | (10.8) | 35.2 | 7.8 | 43.0 |
| Operating income | R$ 955.7 | R$ 767.7 | R$ 635.9 | R$ 32.9 | R$ 2,392.2 | R$ (553.0) | R$ 1,839.2 | R$ 333.6 | R$ 2,172.8 |

| | Year ended December 31, 2003 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| **(in millions of *reais*)** | **Basic Petro-** | **Polyolefins** | **Vinyls** | **Business Develop-** | **Total** | **Elimi-** | **Total prior to** | **CVM 247** | **Consoli-** |

| | chemicals | | | ment | segments | nations | CVM 247 | | dated |
|---|---|---|---|---|---|---|---|---|---|
| Net sales revenue | R$ 4,765.3 | R$ 3,386.8 | R$ 1,371.8 | R$ 455.3 | R$ 9,979.2 | R$ (788.3) | R$ 9,190.9 | R$ 1,109.3 | R$ 10,300.2 |
| Cost of sales and services rendered | (4,111.5) | (2,719.7) | (1,007.0) | (416.8) | (8,255.0) | 913.4 | (7,341.6) | (883.0) | (8,224.6) |
| Gross profit | 653.8 | 667.1 | 364.8 | 38.5 | 1,724.2 | 125.1 | 1,849.3 | 226.3 | 2,075.6 |
| Operating expenses: | | | | | | | | | |
| Selling, general and administrative | (196.0) | (139.3) | (54.8) | (19.2) | (409.3) | 7.8 | (401.5) | (86.9) | (488.4) |
| Depreciation and amortization | (9.0) | (0.9) | | (0.5) | (10.4) | (177.8) | (188.2) | (5.3) | (193.5) |
| Other, net | 51.1 | 2.6 | 3.7 | 10.0 | 67.4 | (16.2) | 51.2 | 4.3 | 55.5 |
| Operating income | R$ 499.9 | R$ 529.5 | R$ 313.7 | R$ 28.8 | R$ 1,371.9 | R$ (61.1) | R$ 1,310.8 | R$ 138.4 | R$ 1,449.2 |

**In the following discussion, references to increases or decreases in any year or period are made by comparison with the corresponding prior year or period, except as the context otherwise indicates.**

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***Year ended December 31, 2005 Compared with Year Ended December 31, 2004***

*Consolidated Results*

The following table sets forth consolidated financial information for the years ended December 31, 2005 and 2004.

| | Year ended December 31, | |
|---|---|---|
| **(In millions of *reais*)** | **2005** | **2004** |
| Net sales revenue | R$ 13,075.1 | R$ 12,389.5 |
| Cost of sales and services rendered | (10,361.7) | (9,223.0) |
| Gross profit | 2,713.4 | 3,166.5 |
| Selling, general and administrative expenses | (787.1) | (677.0) |
| Investment in associated companies, net(1) | (109.8) | (107.6) |
| Depreciation and amortization | (355.6) | (359.7) |
| Financial expenses, net | (709.4) | (1,238.6) |
| Other operating income, net | 22.8 | 43.0 |
| Operating income | 774.3 | 826.6 |
| Non-operating expenses, net | (25.2) | (29.8) |
| Income before income tax and social contribution and minority interest | 749.1 | 796.8 |
| Income tax and social contribution | (177.4) | (85.1) |
| Income before minority interest | 571.7 | 711.7 |
| Minority interest | 54.1 | (24.6) |
| Net income | R$ 625.8 | R$ 687.1 |

(1) Investment in associated companies, net comprises the following line items in our consolidated statement of operations: equity in the results, amortization of goodwill (negative goodwill), net, foreign exchange variation and tax incentives and other.

*Net Sales Revenue*

Net sales revenue increased by 5.5% in 2005, primarily as a result of 11.5% growth in net sales revenue of our Basic Petrochemicals segment and 12.3% growth in net sales revenue of our Polyolefins segment. Without giving effect to the proportional consolidation of our jointly controlled companies, our net sales revenue increased by 5.2% in 2005.

*Cost of Sales and Services Rendered and Gross Profit*

Cost of sales and services rendered increased by 12.3% in 2005, primarily as a result of 15.2% growth in cost of sales and services rendered of our Basic Petrochemicals segment and 26.2% growth in the cost of sales of our Polyolefins segment. The increases in cost of sales and services rendered for each of these segments was primarily related to the higher overall direct and indirect cost of naphtha as a result of higher international market prices of naptha. Without giving effect to the proportional consolidation of our jointly controlled companies, our cost of sales and services rendered increased by 12.2% in 2005.

As a result, gross profit declined by 14.3% in 2005. Without giving effect to the proportional consolidation of our jointly controlled companies, gross profit declined by 16.2% in 2005.

Gross profit as a percentage of net sales revenue, or gross margin, for 2005 was 20.8% compared to 25.6% in 2004. Without giving effect to the proportional consolidation of our jointly controlled companies, gross margin decreased to 19.8% for 2005 compared to 24.8% in 2004.

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*Selling, General and Administrative Expenses*

Selling, general and administrative expenses increased by 16.3% in 2005, primarily as a result of (1) an increase of R$59.6 million in the provision for profit sharing and (2) an increase of R$22.8 million in personnel expenses due to annual salary adjustments at the end of 2004.

Selling, general and administrative expenses represented 6.0% of net sales revenue in 2005 compared to 5.5% of net sales revenue in 2004. Without giving effect to the proportional consolidation of our jointly controlled companies, selling, general and administrative expenses increased by 16.5% in 2005, and selling, general and administrative expenses represented 5.8% of net sales revenue in 2005 compared to 5.3% of net sales revenue in 2004.

*Investment in Associated Companies, Net*

Investment in associated companies, net, increased by 2.0% in 2005, primarily as a result of the incurrence of other expense of R$1.4 in 2005 compared to other income of R$16.6 million in 2004 and a R$5.8 million reduction of tax incentive benefits, partially offset by the incurrence of a R$3.6 million foreign exchange gain in 2005 compared to a R$9.6 million foreign exchange loss recorded in 2004 and the absence of a provision for investment losses in 2005. Without giving effect to the proportional consolidation of our jointly controlled companies, investment in associated companies, net, declined by 14.6% in 2005.

*Depreciation and Amortization*

Depreciation and amortization declined by 1.1% in 2005. Without giving effect to the proportional consolidation of our jointly controlled companies, depreciation and amortization decreased by 1.0% in 2005.

*Financial Expenses, Net*

Financial expenses, net, decreased by 42.7% in 2005, primarily as a result of the effects of the *real*/U.S. dollar exchange rate on our U.S. dollar-denominated and U.S. dollar-indexed assets. As a result of the 13.4% appreciation of the *real* against the U.S. dollar in 2005, we recorded:

- financial income of R$556.9 million related to the exchange rate effect on our U.S. dollar-denominated and U.S. dollar-indexed liabilities; and

- financial expense of R$288.8 million related to the exchange rate effect on our U.S. dollar-denominated assets.

As a result of the 8.9% appreciation of the *real* against the U.S. dollar in 2004, we recorded:

financial income of R$425.4 million related to the exchange rate effect on our U.S. dollar-denominated and U.S. dollar-indexed liabilities; and

financial expense of R$335.3 million related to the exchange rate effect on our U.S. dollar-denominated assets.

Without giving effect to the proportional consolidation of our jointly controlled companies, financial expenses, net decreased by 43.4% in 2005.

*Other Operating Income, Net*

Other operating income, net decreased by 47.0% in 2005, primarily as a result of a decrease in recovery of taxes and compulsory deposits to R$3.4 million in 2005 from R$16.5 million in 2004. Without giving effect to the proportional consolidation of our jointly controlled companies, other operating income, net increased by 98.3% in 2005.

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*Operating Income*

Operating income decreased by 6.3% in 2005. Operating income represented 5.9% of net sales revenue in 2005 compared to 6.7% of net sales revenue in 2004. Without giving effect to the proportional consolidation of our jointly controlled companies, operating income increased by 0.1% in 2005 and represented 6.3% of net sales revenue in 2005 compared to 6.6% of net sales revenue in 2004.

*Non-Operating Expenses, Net*

Non-operating expenses, net decreased by 15.4% in 2005, primarily as a result of the effect of gains on investments recognized in 2005. Without giving effect to the proportional consolidation of our jointly controlled companies, non-operating expenses increased to R$24.7 million in 2005 compared to R$29.2 million in 2004.

*Income Tax and Social Contribution*

Income tax and social contribution increased by 108.5% in 2005. This increase resulted primarily from a deferred income tax loss of R$29.7 million recorded in 2005 compared to a deferred income tax benefit of R$141.4 million recorded in 2004, primarily as a result of a deferred income tax benefit that we recorded in 2004 in connection with our merger with Trikem. Without giving effect to the proportional consolidation of our jointly controlled companies, income tax and social contribution was an expense of R$87.7 million in 2005 compared to a benefit of R$10.5 million in 2004.

*Minority Interest*

Minority interest resulted in a gain of R$54.1 million in 2005 compared to an expense of R$24.6 million, primarily as a result of the allocation of Polialden s accumulated profit reserves to our company through the payment of dividends on Polialden s common shares in the amount of R$58.1 million in 2005, which generated a loss to the holders of preferred shares of Polialden. Without giving effect to the proportional consolidation of our jointly controlled companies, minority interest was a gain of R$54.1 million in 2005 compared to an expense of R$24.6 million in 2004.

*Net Income*

We recorded net income of R$625.8 million, or 4.8% of net sales revenue, in 2005 compared to net income of R$687.1 million, or 5.5% of net sales revenue, in 2004.

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*Business Segment Results*

The following table sets forth consolidated financial information for our business segments for the years ended December 31, 2005 and 2004.

| | Year ended December 31, | |
|---|---|---|
| **(in millions of *reais*, except percentages)** | **2005** | **2004** |
| **Basic Petrochemicals** | | |
| Net sales revenue | R$ 7,226.7 | R$ 6,480.0 |
| Cost of sales and services rendered | (6,138.5) | (5,330.1) |
| Gross profit | 1,088.2 | 1,149.9 |
| Operating income(1) | 895.0 | 955.7 |
| Gross margin (%) | 15.1% | 17.7% |
| Operating margin (%) | 12.4% | 14.7% |
| **Polyolefins** | | |
| Net sales revenue | R$ 3,919.0 | R$ 3,489.4 |
| Cost of sales | (3,182.8) | (2,523.0) |
| Gross profit | 736.2 | 966.4 |
| Operating income(1) | 553.3 | 767.7 |
| Gross margin (%) | 18.8% | 27.7% |
| Operating margin (%) | 14.1% | 22.0% |
| **Vinyls** | | |
| Net sales revenue | R$ 1,794.1 | R$ 1,858.8 |
| Cost of sales | (1,271.9) | (1,157.1) |
| Gross profit | 522.2 | 701.7 |
| Operating income(1) | 438.8 | 635.9 |
| Gross margin (%) | 29.1% | 37.8% |
| Operating margin (%) | 24.5% | 34.2% |
| **Business Development** | | |
| Net sales revenue | R$ 569.0 | R$ 620.8 |
| Cost of sales | (552.9) | (564.9) |
| Gross profit | 16.1 | 55.9 |
| Operating income(1) | 6.8 | 32.9 |
| Gross margin (%) | 2.8% | 9.0% |
| Operating margin (%) | 1.2% | 5.3% |

(1) Operating income does not include financial income, financial expense and investment in associated companies.

*Basic Petrochemicals*

Net Sales Revenue. Net sales revenue of the Basic Petrochemicals segment increased by 11.5% in 2005. Significant factors contributing to this increase were:

a R$269.2 million, or 16.5%, increase in net sales revenue generated by sales to our other business units (which net sales revenue is eliminated in preparation of our consolidated financial statements);

a R$128.4 million, or 17.4%, increase in domestic net sales revenue generated by sales of propylene to third parties;

a R$115.0 million, or 9.9%, increase in domestic net sales revenue generated by sales of ethylene to third parties; and

a R$91.0 million, or 28.3%, increase in net sales revenue generated by sales of automotive gasoline to third parties.

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Net sales revenue generated by sales of basic petrochemicals by our Basic Petrochemicals segment to our other segments increased by 16.9% in 2005 to R$1,763.0 million from R$1,508.1 million in 2004, and net sales revenue generated by sales of utilities by our Basic Petrochemicals segment to our other segments increased by 11.5% in 2005 to R$138.2 million from R$123.9 million in 2004. Net sales revenue generated by sales of utilities to third parties increased by 20.4% in 2005 to R$353.6 million from R$293.6 million in 2004. Net sales revenue generated by export sales of the Basic Petrochemicals segment increased by 12.0% in 2005 to R$1,059.9 million from R$946.1 million in 2004.

Domestic sales volume of propylene to third parties declined by 1.8% to approximately 408,200 tons in 2005 from approximately 415,600 tons in 2004. Average domestic prices for propylene increased by 19.5% to R$2,124 per ton in 2005 from R$1,777 per ton in 2004.

Domestic sales volume of ethylene to third parties increased by 3.4% to approximately 581,100 tons in 2005 from approximately 561,800 tons in 2004. Average domestic prices for ethylene increased by 6.3% to R$2,187 per ton in 2005 from R$2,057 per ton in 2004.

Sales volume of automotive gasoline to third parties increased by 10.0% to approximately 444,300 cubic meters in 2005 from approximately 403,800 cubic meters in 2004. Domestic sales volume of automotive gasoline to third parties increased by 57.9% in 2005, while export sales volume of automotive gasoline declined by 40.5%. Average domestic prices for automotive gasoline increased by 24.1% to R$926 per cubic meter in 2005 from R$746 per cubic meter in 2004 and average export prices for automotive gasoline increased by 10.4% to R$940 per cubic meter in 2005 from R$851 per cubic meter in 2004.

Cost of Sales and Services Rendered and Gross Profit. Cost of sales and services rendered of the Basic Petrochemicals segment increased by 15.2% in 2005. This increase was primarily attributable to the increase in the average cost of naphtha to R$1,178.4 per ton in 2005 from R$1,077.2 per ton in 2004 as well as the increase in sales volume in 2005. Naphtha accounted for 86.6% of the Basic Petrochemicals segment s cost of sales in 2005 and 82.4% in 2004.

Gross profit of the Basic Petrochemicals segment decreased by 5.4% in 2005 and gross margin decreased to 15.1% in 2005 compared to 17.7% in 2004.

Operating Income. Operating income of the Basic Petrochemicals segment (which excludes financial income, financial expense and results from investment in associated companies) decreased by 6.4% in 2005, principally as a result of a R$61.7 million decline in gross profit and a 17.1% increase in selling, general and administrative expenses, primarily as a result of our investment in 2005 in new supply chain and technology departments that we expect will provide greater efficiencies in these areas. These effects were partially offset by an increase in other operating income, net, to R$57.1 million in 2005 compared to R$22.2 million in 2004, principally as a result of our recovery of an account receivable in 2005 in the amount of R$18.6 million that we had previously written off. Operating margin of the Basic Petrochemicals segment in 2005 was 12.4% compared to 14.7% in 2004.

*Polyolefins*

Net Sales Revenue. Net sales revenue of the Polyolefins segment increased by 12.3% in 2005. This increase was primarily attributable to:

a 15.1% increase in net sales revenue generated by sales of polypropylene, principally as a result of the increase in our annual polypropylene capacity from approximately 463,100 tons in 2004 to approximately 529,000 tons in 2005; and

a 10.5% increase in net sales revenue generated by sales of polyethylene, led by a 59.4% increase in net sales revenue generated by export sales of LLDPE.

Net sales revenue generated by export sales of the Polyolefins segment increased by 43.2% to R$971.5 million in 2005 from R$678.6 million in 2004.

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Sales volume of polypropylene increased by 12.3% to approximately 517,500 tons in 2005 from approximately 461,000 tons in 2004. Domestic sales volume of polypropylene increased by 0.3% in 2005, principally due to low Brazilian economic growth, increased competition from polypropylene imports and reduced demand for polypropylene products in the agricultural sector as a result of the poor Brazilian harvest, while exports sales volume of polypropylene increased by 129.6%. Average domestic prices for polypropylene increased by 6.0% to R$3,344 per ton in 2005 from R$3,155 per ton in 2004, while average export prices for polypropylene stated in *reais* declined by 4.6% to R$2,487 per ton in 2005 from R$2,604 per ton in 2004, primarily as a result of the appreciation of the *real* against the U.S. dollar during 2005.

Sales volume of polyethylene increased by 9.0% to approximately 768,200 tons in 2005 from approximately 704,700 tons in 2004. Domestic sales volume of polyethylene increased by 0.7% in 2005, principally due to low Brazilian economic growth, while exports sales volume of polyethylene increased by 29.1%. Average domestic prices for polyethylene increased by 2.9% to R$3,072 per ton in 2005 from R$2,987 per ton in 2004, while average export prices for polyethylene stated in *reais* declined by 0.3% to R$2,725 per ton in 2005 from R$2,733 per ton in 2004, primarily as a result of the appreciation of the *real* against the U.S. dollar during 2005.

Cost of Sales and Gross Profit. Cost of sales of the Polyolefins segment increased by 26.2% in 2005 compared to 2004, primarily as a result of (1) the effect of the significant increase in the price of naphtha on ethylene and propylene, which are the principal raw materials of our Polyolefins Unit, and (2) our increased sales volume of polypropylene due to the 65,000 ton increase in our annual polypropylene capacity. Our average cost for ethylene increased by 9.2% during 2005, and our average cost for propylene increased by 19.3% during 2005.

Gross profit of the Polyolefins segment declined by 23.8% in 2005 and gross margin declined to 18.8% in 2005 compared to 27.7% in 2004.

Operating Income. Operating income of the Polyolefins segment (which excludes financial income, financial expense and results from investment in associated companies) decreased by 27.9% in 2005, primarily as a result of a R$230.2 million decrease in gross profit and, to a lesser extent, a 15.0% increase in selling, general and administrative expenses, primarily as a result of (1) an increase in personnel expenses due to annual salary adjustments at the end of 2004 and 2005, and (2) an increase in royalty expenses as a result of our increased production of LLDPE and very low density polyethylene using metallocene technology. This effect was partially offset by an increase in other operating income, net, to R$53.0 million in 2005 compared to R$6.3 million in 2004, primarily as a result of a recorded gain of R$58.2 million related to the contribution of our polypropylene production process technology to Paulínia. Operating margin of the Polyolefins segment decreased to 14.1% in 2005 compared to 22.0% in 2004.

*Vinyls*

Net Sales Revenue. Net sales revenue of the Vinyls segment decreased by 3.5% in 2005. This decrease was primarily attributable to a 9.5% decline in net sales revenue generated by sales of PVC and a 45.5% decline in net sales revenue generated by export sales of EDC. The effects of these declines was partially offset by a 33.7% increase in net sales revenue generated by sales of caustic soda. Net sales revenue generated by export sales of this segment declined by 13.8% to R$220.9 million in 2005 from R$256.2 million in 2004.

Sales volume of PVC increased by 3.3% to approximately 441,900 tons in 2005 from approximately 427,700 tons in 2004. Domestic sales volume of PVC decreased by 3.9% in 2005, principally due to our loss of market share, increased imports of PVC resins and our decision not to lower prices during the first half of 2005, while export sales volume of PVC increased by 89.1%. Average domestic prices for PVC decreased by 9.7% to R$2,747 per ton in 2005 from R$3,042 per ton in 2004, while average export prices for PVC declined by 22.7% to R$1,852 per ton in 2005 from R$2,397 per ton in 2004.

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Export sales volume of EDC decreased by 22.4% to approximately 122,200 tons in 2005 from approximately 157,600 tons in 2004, due to the reduction of the portion of our EDC production that was available for sale because of our increased use of EDC for our own PVC production. Average export prices for EDC declined by 29.7% to R$786 per ton in 2005 from R$1,118 per ton in 2004.

Domestic sales volume of caustic soda increased by 2.6% to approximately 455,600 tons in 2005 from approximately 444,000 tons in 2004, principally due to an increase in our market share. Average domestic prices for caustic soda increased by 28.0% to R$986 per ton in 2005 from R$770 per ton in 2004.

Cost of Sales and Gross Profit. Cost of sales of the Vinyls segment increased by 9.9% in 2005 compared to 2004, primarily as a result of an 8.4% increase in the cost of ethylene.

Gross profit of the Vinyls segment declined by 25.6% in 2005, while gross margin decreased to 29.1% in 2005 from 37.8% in 2004.

Operating Income. Operating income of the Vinyls segment (which excludes financial income, financial expense and results from investment in associated companies) declined by 31.0% in 2005, primarily as a result of a R$179.5 million decrease in gross profit. The operating margin of the Vinyls segment declined to 24.5% in 2005 from 34.2% in 2004.

*Business Development*

Net Sales Revenue. Net sales revenue of our Business Development segment declined by 8.3% in 2005. This decrease was primarily attributable to a 20.2% decrease in net sales revenue generated by sales of PET during 2005, the effects of which were partially offset by a 5.3% increase in net sales revenue generated by sales of caprolactam during 2005. Net sales revenue generated by export sales of this segment increased to R$87.8 million in 2005 from R$56.8 million in 2004.

Sales volume of PET declined by 18.6% to approximately 60,400 tons in 2005 from approximately 74,300 tons in 2004, primarily as a result of our reduced production as a result of a general maintenance shutdown of our PET plant in April 2005. Domestic sales volume of PET decreased by 14.5% in 2005 primarily as a result of competition from low-price PET imports, while exports sales volume of PET declined by 52.7%. Average domestic prices for PET decreased by 1.6% to R$3,547 per ton in 2005 from R$3,605 per ton in 2004, while average export prices for PET declined by 15.8% to R$2,723 per ton in 2005 from R$3,235 per ton in 2004.

Sales volume of caprolactam declined by 1.8% to approximately 48,300 tons in 2005 from approximately 49,100 tons in 2004. Domestic sales volume of caprolactam decreased by 23.2% in 2005, while exports sales volume of caprolactam increased by 147.8%. Average domestic prices for caprolactam increased by 11.7% to R$5,975 per ton in 2005 from R$5,349 per ton in 2004, and average export prices for caprolactam increased by 1.8% to R$5,059 per ton in 2005 from R$4,971 per ton in 2004.

Cost of Sales and Gross Profit. Cost of sales of the Business Development segment decreased by 2.1% in 2005.

Gross profit of the Business Development segment decreased by 71.2% in 2005, resulting in a gross margin of 2.8% in 2005 compared to 9.0% in 2004.

Operating Income. Operating income of the Business Development segment (which excludes financial income, financial expense and results from investment in associated companies) declined by 79.3% in 2005, principally as a result of a R$39.8 million decrease in gross profit. The effects of this decrease were partially offset by a 26.9% decrease in selling, general and administrative expenses and an increase in other operating income, net to R$9.2 million in 2005 compared to R$2.6 million in 2004. Operating margin of the Business Development segment decreased to 1.2% in 2005 from 5.3% in 2004.

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***Year Ended December 31, 2004 Compared with Year Ended December 31, 2003***

*Consolidated Results*

The following table sets forth consolidated financial information for the years ended December 31, 2004 and 2003.

| | Year ended December 31, | |
|---|---|---|
| **(In millions of *reais*)** | **2004** | **2003** |
| Net sales revenue | R$ 12,389.5 | R$ 10,300.2 |
| Cost of sales and services rendered | (9,223.0) | (8,224.6) |
| Gross profit | 3,166.5 | 2,075.6 |
| Selling, general and administrative expenses | (677.0) | (488.4) |
| Investment in associated companies, net(1) | (107.6) | (170.5) |
| Depreciation and amortization | (359.7) | (193.5) |
| Financial expenses, net | (1,238.6) | (711.6) |
| Other operating income, net | 43.0 | 55.5 |
| Operating income | 826.6 | 567.1 |
| Non-operating expenses, net | (29.8) | (4.5) |
| Income before income tax and social contribution and minority interest | 796.8 | 562.6 |
| Income tax and social contribution | (85.1) | (121.3) |
| Income before minority interest | 711.7 | 441.3 |
| Minority interest | (24.6) | (226.2) |
| Net income | R$ 687.1 | R$ 215.1 |

(1) Investment in associated companies, net comprises the following line items in our consolidated statement of operations: equity in the results, amortization of goodwill (negative goodwill), net, foreign exchange variation and tax incentives and other.

*Net Sales Revenue*

Net sales revenue increased by 20.3% in 2004, primarily as a result of the growth in net sales revenue in each of our segments (as discussed below), particularly the 36.0% growth in net sales revenue of our Basic Petrochemicals segment and the 35.5% growth in net sales revenue of our Vinyls segment. Without giving effect to the proportional consolidation of our jointly controlled companies, our net sales revenue increased by 20.2% in 2004.

*Cost of Sales and Services Rendered and Gross Profit*

Cost of sales and services rendered increased by 12.1% in 2004, primarily as a result of the 29.6% growth in cost of sales and services rendered of our Basic Petrochemicals segment, as well as the 14.9% growth in cost of sales of our Vinyls segment and the 35.5% growth in the cost of sales of our Business Development segment. The increases in cost of sales and services rendered of each of these segments was primarily related to the higher overall direct and indirect cost of naphtha as a result of higher international market prices of naptha. Without giving effect to the proportional consolidation of our jointly controlled companies, our cost of sales and services rendered increased by 13.1% in 2004.

As a result, gross profit increased by 52.6% in 2004. Without giving effect to the proportional consolidation of our jointly controlled companies, gross profit increased by 48.1% in 2004.

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Gross profit as a percentage of net sales revenue, or gross margin, for 2004 was 25.6% compared to 20.2% in 2003. Without giving effect to the proportional consolidation of our jointly controlled companies, gross margin increased to 24.8% for 2004 compared to 20.1% in 2003.

*Selling, General and Administrative Expenses*

Selling, general and administrative expenses increased by 38.6% in 2004, primarily as a result of:

- growth in variable expenses associated with our increased sales volume in 2004 with an impact of approximately R$30 million;
- an increase of R$28.2 million in provision for doubtful accounts in 2004 compared to 2003 as a result of the application of our credit policy to the increased accounts receivable balance;
- non-recurring gains of approximately R$40 million recorded in 2003 due to the positive effect caused by the reversal of a provision for doubtful accounts recorded in 2002 to meet certain potential credit risks in Argentina;
- non-recurring expenses of approximately R$33 million recorded in 2004 related to the development of a new information technology platform, in part to prepare to comply with the U.S. Sarbanes-Oxley Act of 2002, and professional fees incurred in connection with our public equity offering; and
- the effects of inflation on recurring expenses, which amounted to approximately R$46 million.

Selling, general and administrative expenses represented 5.5% of net sales revenue in 2004 compared to 4.7% of net sales revenue in 2003. Without giving effect to the proportional consolidation of our jointly controlled companies, selling, general and administrative expenses increased by 44.6% in 2004, and selling, general and administrative expenses represented 5.3% of net sales revenue in 2004 compared to 4.4% of net sales revenue in 2003.

*Investment in Associated Companies, Net*

Investment in associated companies, net, decreased by 36.9% in 2004, primarily as a result of a decrease in amortization of goodwill, principally related to Copesul and Politeno, partially offset by reduced tax incentive benefits and by the R$9.6 million foreign exchange loss recorded in 2004 compared to the R$22.4 million foreign exchange gain recorded in 2003. Without giving effect to the proportional consolidation of our jointly controlled companies, investment in associated companies, net, was a gain of R$73.7 million in 2004 compared to an expense of R$119.4 million in 2003.

*Depreciation and Amortization*

Depreciation and amortization increased by 85.9% in 2004, primarily as a result of:

- increased depreciation of property, plant and equipment and amortization of deferred charges following the reclassification of goodwill to these lines upon our merger with Trikem in January 2004;

- the non-recurring effect resulting from the full amortization of deferred expenses related to our 10th and 11th issues of debentures, which were redeemed in full in 2004;

- the increased amortization of deferred charges as a result of the increase in our deferred charges related to scheduled maintenance stoppages that occurred in 2003 and 2004.

Without giving effect to the proportional consolidation of our jointly controlled companies depreciation and amortization increased by 88.0% in 2004.

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*Financial Expenses, Net*

Financial expenses, net, increased by 74.1% in 2004, primarily as a result of the effects of the *real*/U.S. dollar exchange rate on our U.S. dollar-denominated and U.S. dollar-indexed assets and liabilities and the increased principal amount of foreign-currency denominated debt in 2004. As a result of the 8.9% appreciation of the *real* against the U.S. dollar in 2004, we recorded:

- financial income of R$425.4 million related to the exchange rate effect on our U.S. dollar-denominated and U.S. dollar-indexed liabilities; and

- financial expense of R$335.3 million related to the exchange rate effect on our U.S. dollar-denominated assets.

As a result of the 22.3% appreciation of the *real* against the U.S. dollar in 2003, we recorded:

- financial income of R$972.1 million related to the exchange rate effect on our monetary liabilities; and

- financial expense of R$213.4 million related to the exchange rate effect on our monetary assets.

Without giving effect to the proportional consolidation of our jointly controlled companies, financial expenses, net increased by 79.8% in 2004.

*Other Operating Income, Net*

Other operating income, net decreased by 22.5% in 2004, primarily as a result of:

- a decline in insurance recoveries recorded in 2004 to R$1.6 million from R$11.6 million in 2003;

- a decrease in recovery of taxes and compulsory deposits to R$16.5 million in 2004 from R$28.8 million in 2003; and

- a decrease in sales of sundry materials to R$11.3 million in 2004 from R$16.9 million in 2003.

These effects were partially offset by a decrease in taxes on intercompany sales as we were no longer required to record taxes on intercompany sales to OPP Química and Nitrocarbono following the mergers of these companies with us in 2004, which taxes amounted to R$24.2 million in 2003. Without giving effect to the proportional consolidation of our jointly controlled companies, other operating income, net decreased by 31.3%.

*Operating Income*

Operating income increased by 45.8% in 2004. Operating income represented 6.7% of net sales revenue in 2004 compared to 5.5% of net sales revenue in 2003. Without giving effect to the proportional consolidation of our jointly controlled companies, operating income increased by 37.0% in 2004 and represented 6.6% of net sales revenue in 2004 compared to 5.8% of net sales revenue in 2003.

*Non-Operating Expenses, Net*

Non-operating expenses, net increased to R$29.8 million in 2004 compared to R$4.5 million in 2003. This increase resulted primarily from a reversal of a loss on investment of R$26.9 million in 2003. Without giving effect to the proportional consolidation of our jointly controlled companies, non-operating expenses increased to R$29.2 million in 2004 compared to R$4.6 million in 2003.

*Income Tax and Social Contribution*

Income tax and social contribution decreased by 29.8% in 2004. This decrease resulted primarily from the increase in deferred income tax of R$25.6 million in 2003 to R$141.4 million in 2004, primarily as a result of a

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deferred income tax benefit that we recorded in 2004 in connection with our merger with Trikem. Without giving effect to the proportional consolidation of our jointly controlled companies, income tax and social contribution was a benefit of R$10.5 million in 2004 compared to an expense of R$91.8 million in 2003.

*Minority Interest*

Minority interest decreased by 89.1% in 2004, primarily as a result of elimination of the minority interest in Trikem as a result of our merger with Trikem in January 2004. Without giving effect to the proportional consolidation of our jointly controlled companies, minority interest also decreased by 89.1% in 2004.

*Net Income*

We recorded net income of R$687.1 million, or 5.5% of net sales revenue, in 2004 compared to net income of R$215.1 million, or 2.1% of net sales revenue, in 2003.

*Business Segment Results*

The following table sets forth consolidated financial information for our business segments for the years ended December 31, 2004 and 2003.

| | Year ended December 31, | |
|---|---|---|
| **(in millions of *reais*, except percentages)** | **2004** | **2003** |
| | **Consolidated** | |
| **Basic Petrochemicals** | | |
| Net sales revenue | R$ 6,480.0 | R$ 4,765.3 |
| Cost of sales and services rendered | (5,330.1) | (4,111.5) |
| Gross profit | 1,149.9 | 653.8 |
| Operating income(1) | 955.7 | 499.9 |
| Gross margin (%) | 17.7% | 13.7% |
| Operating margin (%) | 14.7% | 10.5% |
| **Polyolefins** | | |
| Net sales revenue | R$ 3,489.4 | R$ 3,386.8 |
| Cost of sales | (2,523.0) | (2,719.7) |
| Gross profit | 966.4 | 667.1 |
| Operating income(1) | 767.7 | 529.5 |
| Gross margin (%) | 27.7% | 19.7% |
| Operating margin (%) | 22.0% | 15.6% |
| **Vinyls** | | |
| Net sales revenue | R$ 1,858.8 | R$ 1,371.8 |

| | | |
|---|---|---|
| Cost of sales | (1,157.1) | (1,007.0) |
| Gross profit | 701.7 | 364.8 |
| Operating income(1) | 635.9 | 313.7 |
| Gross margin (%) | 37.8% | 26.6% |
| Operating margin (%) | 34.2% | 22.9% |
| **Business Development** | | |
| Net sales revenue | R$ 620.8 | R$ 455.3 |
| Cost of sales | (564.9) | (416.8) |
| Gross profit | 55.9 | 38.5 |
| Operating income(1) | 32.9 | 28.8 |
| Gross margin (%) | 9.0% | 8.5% |
| Operating margin (%) | 5.3% | 6.3% |

(1) Operating income does not include financial income, financial expense and investment in associated companies.

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*Basic Petrochemicals*

Net Sales Revenue. Net sales revenue of the Basic Petrochemicals segment increased by 36.0% in 2004. Significant factors contributing to this increase were:

- a R$617.5 million, or 60.9%, increase in net sales revenue generated by sales to our other business units (which net sales revenue is eliminated in preparation of our consolidated financial statements);
- a R$217.3 million, or 119.0%, increase in net sales revenue generated by export sales of benzene;
- a R$208.9 million, or 22.1%, increase in net sales revenue generated by domestic sales of ethylene to third parties;
- a R$142.0 million, or 23.8%, increase in net sales revenue generated by domestic sales of propylene to third parties; and
- a R$131.9 million, or 55.4%, increase in net sales revenue generated by domestic sales of benzene to third parties.

Net sales revenue generated by sales of basic petrochemicals by our Basic Petrochemicals segment to our other segments increased by 65.6% in 2004 to R$1,508.1 million from R$910.7 million in 2003, and net sales revenue generated by sales of utilities by our Basic Petrochemicals segment to our other segments increased by 19.4% in 2004 to R$123.9 million from R$103.8 million in 2003.

Net sales revenue generated by sales of utilities to third parties increased by 4.6% in 2004 to R$293.6 million from R$280.7 million in 2003. Net sales revenue generated by export sales of the Basic Petrochemicals segment increased by 52.9% in 2004 to R$946.1 million from R$618.8 million in 2003.

Export sales volume of benzene increased by 20.3% to approximately 169,500 tons in 2004 from approximately 140,900 tons in 2003, principally due to our strategic decision to increase our exports of benzene to take advantage of the high prices available in the international market. As a result, domestic sales volume of benzene to third parties declined by 2.2% to approximately 154,400 tons in 2004 from approximately 157,900 tons in 2003. Average export prices for benzene increased by 82.2% to R$2,359 per ton in 2004 from R$1,295 per ton in 2003, while average domestic prices for benzene increased by 58.9% to R$2,395 per ton in 2004 from R$1,507 per ton in 2003.

Domestic sales volume of ethylene to third parties increased by 0.5% to approximately 561,800 tons in 2004 from approximately 559,100 tons in 2003. Average domestic prices for ethylene increased by 21.4% to R$2,057 per ton in 2004 from R$1,694 per ton in 2003.

Domestic sales volume of propylene to third parties increased by 4.1% to approximately 415,600 tons in 2004 from approximately 399,200 tons in 2003, principally due to increased demand by other second generation producers of petrochemicals derived from propylene as a result of the economic recovery in Brazil. Average domestic prices for propylene increased by 18.9% to R$1,777 per ton in 2004 from R$1,495 per ton in 2003.

Cost of Sales and Services Rendered and Gross Profit. Cost of sales and services rendered of the Basic Petrochemicals segment increased by 29.6% in 2004. This increase was primarily attributable to the increase in the average cost of naphtha to R$1,077.2 per ton in 2004 from R$886.1 per ton in 2003 as well as the increase in sales volume in 2004. Naphtha accounted for 82.4% of the Basic Petrochemicals segment s cost of sales in 2004 and 84.6% in 2003.

Gross profit of the Basic Petrochemicals segment increased by 75.9% in 2004 and gross margin increased to 17.7% in 2004 compared to 13.7% in 2003.

Operating Income. Operating income of the Basic Petrochemicals segment (which excludes financial income, financial expense and results from investment in associated companies) increased by 91.2% in 2004, principally as a result of a R$496.1 million increase in gross profit. Operating margin of the Basic Petrochemicals segment in 2004 was 14.7% compared to 10.5% in 2003.

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*Polyolefins*

Net Sales Revenue. Net sales revenue of the Polyolefins segment increased by 3.0% in 2004. This increase was primarily attributable to:

- a 30.1% increase in net sales revenue generated by domestic sales of polyethylene, led by a 42.9% increase in domestic sales of LLDPE;
- a 31.0% increase in net sales revenue generated by domestic sales of polypropylene; and
- a 22.4% increase in net sales revenue generated by export sales of polyethylene.

The effects of these increases were substantially offset by the elimination of certain export transactions that were undertaken in 2003 to support export finance transactions and that were included in net sales revenue generated by export sales of this segment. Net sales revenue generated by export sales of the Polyolefins segment decreased by 45.0% to R$678.6 million 2004 from R$1,233.7 million in 2003.

Domestic sales volume of polyethylene increased by 11.8% to approximately 498,700 tons in 2004 from approximately 446,100 tons in 2003, principally due to increased sales of flexible packaging for food, particularly frozen meat for export, snacks and cookies, as well as long shelf-life beverages. Average domestic prices for polyethylene increased by 16.2% to R$2,984 per ton in 2004 from R$2,567 per ton in 2003.

Domestic sales volume of polypropylene increased by 11.6% to approximately 418,500 tons in 2004 from approximately 374,900 tons in 2003, principally due to the performance of the automotive and the electrical/electronic industries and agricultural sectors. Average domestic prices for polypropylene increased by 17.3% to R$3,155 per ton in 2004 from R$2,689 per ton in 2003.

Export sales volume of polyethylene decreased by 7.2% to approximately 205,900 tons in 2004 from approximately 221,900 tons in 2003, principally due to our decision to sell a greater volume of polyethylene products domestically in light of increased demand in the domestic market. Average export prices for polyethylene increased by 31.9% to R$2,733 per ton in 2004 from R$2,072 per ton in 2003.

Cost of Sales and Gross Profit. Cost of sales of the Polyolefins segment decreased by 7.2% in 2004 compared to 2003 despite the 5.1% increase in sales volume, primarily as a result of the cessation of purchases related to certain export transactions that were undertaken in 2003 to support export finance transactions. This effect was partially offset by a 22.5% increase in the cost of ethylene and a 13.7% increase in the cost of propylene.

Gross profit of the Polyolefins segment increased by 44.9% in 2004, while gross margin increased to 27.7% in 2004 compared to 19.7% in 2003.

Operating Income. Operating income of the Polyolefins segment (which excludes financial income, financial expense and results from investment in associated companies) increased by 45.0% in 2004, primarily as a result of a R$299.3 million increase in gross profit. This effect was partially offset by a R$59.8 million increase in selling, general and administrative expenses as a result of higher sales volumes of polyolefins in the domestic market and an increase in the provision for doubtful accounts of this segment. Operating margin of the Polyolefins segment increased to 22.0% in 2004 compared to 15.6% in 2003.

*Vinyls*

Net Sales Revenue. Net sales revenue of the Vinyls segment increased by 35.5% in 2004. This increase was primarily attributable to a 46.6% increase in net sales revenue generated by domestic sales of PVC, supplemented by a 61.9% increase in net sales revenue generated by export sales of EDC and a 17.8% increase in net sales revenue generated by domestic sales of caustic soda. Net sales revenue generated by export sales of this segment increased by 25.8% to R$256.2 million in 2004 from R$203.7 million in 2003.

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Domestic sales volume of PVC increased by 15.2% to approximately 394,400 tons in 2004 from approximately 342,400 tons in 2003, principally due to increased sales by the footwear, laminate and wire and cable industries, as well as by the commencement of a recovery of the construction sector. Average domestic prices for PVC increased by 27.3% to R$3,042 per ton in 2004 from R$2,390 per ton in 2003.

Export sales volume of EDC decreased by 1.6% to approximately 157,600 tons in 2004 from approximately 160,100 tons in 2003. Average export prices for EDC increased by 64.4% to R$1,118 per ton in 2004 from R$680 per ton in 2003.

Domestic sales volume of caustic soda increased by 4.1% to approximately 444,000 tons in 2004 from approximately 426,600 tons in 2003, principally due to the increased demand of our clients in the aluminum, paper and cellulose industries. Average domestic prices for caustic soda increased by 13.1% to R$770 per ton in 2004 from R$681 per ton in 2003.

Cost of Sales and Gross Profit. Cost of sales of the Vinyls segment increased by 14.9% in 2004 compared to 2003. This increase was primarily attributable to increases in some of our production costs, principally due to a 17.1% increase in the cost of ethylene, and an increase of 4.7% in the total sales volume of this segment.

Gross profit of the Vinyls segment increased by 92.4% in 2004, while gross margin increased to 37.8% in 2004 from 26.6% in 2003.

Operating Income. Operating income of the Vinyls segment (which excludes financial income, financial expense and results from investment in associated companies) increased by 102.7% in 2004, primarily as a result of a R$336.9 million increase in gross profit. This effect was partially offset by a R$25.3 million increase in selling, general and administrative expenses, primarily as a result of the increase of our domestic sales volume of vinyls and an increase in the provision for doubtful accounts of this segment. The operating margin of the Vinyls segment increased to 34.2% in 2004 from 22.9% in 2003.

*Business Development*

Net Sales Revenue. Net sales revenue of our Business Development segment increased by 36.3% in 2004. This increase was primarily attributable to a 41.7% increase in net sales revenue generated by domestic sales of PET during 2004, a 27.6% increase in net sales revenue generated by domestic sales of caprolactam during 2004 and an increase in net sales revenue generated by export sales of PET to R$26.2 million in 2004 compared to R$3.5 million in 2003. Net sales revenue generated by export sales of this segment increased to R$56.8 million in 2004 from R$34.4 million in 2003.

Domestic sales volume of PET increased by 20.1% to approximately 66,200 tons in 2004 from approximately 55,100 tons in 2003, primarily as a result of the increase in our PET plant s annual production capacity from 70,000 tons to 78,000 tons during 2004. Average domestic sales prices of PET increased by 18.0% to R$3,605 per ton in 2004 from R$3,056 per ton in 2003.

Domestic sales volume of caprolactam increased by 1.2% to approximately 43,000 tons in 2004 from approximately 42,500 tons in 2003. Average domestic sales prices of caprolactam increased by 26.2% to R$5,349 per ton in 2004 from R$4,237 per ton in 2003.

Export sales volume of PET was approximately 8,100 tons in 2004 compared to approximately 1,200 tons in 2003. Average export sales prices of PET increased by 12.0% to R$3,235 per ton in 2004 from R$2,888 per ton in 2003.

Cost of Sales and Gross Profit. Cost of sales of the Business Development segment increased by 35.5% in 2004, primarily reflecting increases in some of our production costs, primarily a 65.7% increase in the cost of benzene, and the effects of a 5.9% increase in sales volume of this segment.

Gross profit of the Business Development segment increased by 45.2% in 2004, resulting in a gross margin of 9.0% compared to 8.5% in 2003.

Operating Income. Operating income of the Business Development segment (which excludes financial income, financial expense and results from investment in associated companies) increased by 14.2% in 2004, principally as a result of a R$17.4 million increase in gross profit. Operating margin of the Business Development segment decreased to 5.3% in 2004 from 6.3% in 2003.

**Liquidity and Capital Resources**

Our principal cash requirements consist of the following:

- working capital requirements;
- the servicing of our indebtedness;
- capital expenditures related to investments in operations, maintenance and expansion of plant facilities;
- funds required for acquisitions of equity interests in other petrochemical producers; and
- dividends on our shares, including in the form of interest attributable to shareholders equity.

Our principal sources of liquidity have traditionally consisted of the following:

- cash flows from operating activities;
- short-term and long-term borrowings; and
- sales of debt securities in domestic and international capital markets.

During 2005, cash flow generated by operations was used primarily for investing activities, for working capital requirements and to service our outstanding debt obligations. At December 31, 2005, our consolidated cash and cash equivalents and other investments amounted to R$2,281.5 million, including R$178.3 million that has been included in our consolidated financial statements due to the effects of proportional consolidation and to which we do not generally have access because we jointly control our proportionally consolidated companies with third parties. At December 31, 2005, we had working capital of R$1,373.7 million. Without giving effect to the proportional consolidation of our jointly controlled companies, we had working capital of R$779.4 million at December 31, 2005.

***Projected Sources and Uses of Cash***

We anticipate that we will be required to spend approximately R$2,505.3 million to meet our short-term contractual obligations and commitments and budgeted capital expenditures in 2006, without giving effect to proportional consolidation. We expect that we will meet these cash requirements through a combination of cash generated from operating activities and cash generated by financing activities, including new debt financings and the refinancing of our existing short-term indebtedness as it becomes due.

We anticipate that we will be required to spend approximately R$7,788.9 million to meet our long-term contractual obligations and commitments and budgeted capital expenditures through 2008, without giving effect to proportional consolidation. We anticipate that we will meet these cash requirements through a combination of: (1) cash generated from operating activities; (2) cash generated by financing activities, including new debt financings and the refinancing of our indebtedness as it becomes due; and (3) dividends received from our subsidiaries and jointly controlled companies.

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We have commitments from several financial institutions to provide us with financing in the future, including:

- a commitment from an international financial institution to lend us an aggregate principal amount of up to US$300.0 million or its equivalent in other currencies for use in connection with our capital expenditure program;

- a commitment from BNDES to lend us an aggregate principal amount of R$48.4 million for use in connection with our capital expenditure program in addition to the remaining amounts to be disbursed under two credit facilities described under Liquidity and Capital Resources Indebtedness and Financing Strategy Long-Term Indebtedness; and

- a commitment from a local financial institution to lend us an aggregate principal amount of up to R$195.0 million for use in connection with the the production of goods and services for export and/or the payment of our obligations.

These commitments are subject to conditions precedent which we believe that we will be able to satisfy in connection with any amounts drawn under these facilities. We pay commitment fees to these financial institutions in connection with their commitments.

***Cash Flows***

*Cash Flows from Operating Activities*

Net cash provided by operating activities was R$1,719.4 million in 2005, R$1,916.0 million in 2004 and R$596.9 million in 2003. Without giving effect to the proportional consolidation of our jointly controlled companies, net cash provided by operating activities was R$2,109.1 million in 2005, R$1,662.0 million in 2004 and R$431.9 million in 2003.

The most significant factors in the generation of our consolidated cash flows from operating activities in 2005 were:

- our net income of R$625.8 million; and

- longer payment terms for imported raw materials under our raw material financing arrangements, resulting in a R$485.1 million increase in our liabilities to suppliers.

These positive factors contributing to our cash flows from operations were partially offset by the effects of a R$130.3 million increase in our taxes recoverable resulting primarily from our increased level of exports in 2005.

The most significant factors in the generation of our consolidated cash flows from operating activities in 2004 were:

our net income of R$687.1 million;

the R$1,152.1 million increase in our liabilities to suppliers, principally resulting from longer payment terms for imported raw materials; and

the R$289.4 million decrease in taxes recoverable as a result of our use of tax credits to offset R$174.3 million of federal taxes due in 2004.

These positive factors contributing to our cash flows from operations in 2004 were partially offset by the effects of:

a R$451.7 million increase in our trade accounts receivable resulting from higher prices for certain of our principal products due to the realignment of our prices with international market prices during 2004;

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- a R$389.6 million increase in inventories primarily as a result of (1) increased production of certain products at the end of 2004 to maintain capacity utilization rates in order to sustain better operational performance, and (2) increased prices for, and higher volumes of, certain of our principal raw materials; and

- a R$212.3 million decrease in advances from customers primarily as a result of faster delivery of products to our customers.

The significant factors that led to the generation of our consolidated cash flows from operating activities in 2003 included our net income of R$215.1 million, and a R$321.2 million decrease in our taxes recoverable primarily as a result of the use of our tax credits to offset R$364.9 million of our federal tax assessment in 2003. These positive factors contributing to our cash flows from operations in 2003 were partially offset by the effects of, among other factors:

- a R$612.2 million decrease in our accounts payable to suppliers as a result of our reduced reliance on this high-cost source of liquidity;

- a R$242.8 million increase in our trade accounts receivable resulting from higher prices for certain of our principal products due to our realignment of the prices of certain of our principal products with international market prices in 2003; and

- a R$197.7 million increase in inventories resulting from our increased production of certain products for inventory in late 2003 in anticipation of the shutdown of our Olefins 2 and Aromatics units for maintenance in early 2004.

*Cash Flows Used in Investing Activities*

Investing activities used net cash of R$1,048.0 million during 2005, R$1,014.4 million during 2004 and R$469.4 million in 2003. Without giving effect to the proportional consolidation of our jointly controlled companies, investing activities used net cash of R$973.5 million during 2005, R$815.9 million during 2004 and R$494.8 million in 2003.

During 2005, investing activities for which we used cash on a consolidated basis primarily consisted of additions to equipment related to the increase of our annual PVC production capacity at our Alagoas PVC plant by 50,000 tons, the increase of our annual polyethylene production capacity in the Northeastern Complex by 30,000 tons and capital expenditures that are expected to increase our annual polyethylene production capacity in the Northeastern Complex by 30,000 tons when completed in 2006. In addition, we used R$150.0 million to perform maintenance on our plants during scheduled shutdowns during 2005 and R$150.0 million in our safety, health and environmental programs.

During 2004, investing activities for which we used cash on a consolidated basis primarily consisted of additions to equipment related to the increase of our annual polypropylene production capacity in the Southern Complex by 100,000 tons, the increase of our annual paraxylene production capacity in the Northeastern Complex by 50,000 tons and capital expenditures related to the increase of our annual PVC production capacity at our Alagoas PVC plant by 50,000 tons. In addition, we used R$210.1 million to perform maintenance of our plants during scheduled shutdowns during 2004.

In 2003, investing activities for which we used cash on a consolidated basis primarily consisted of additions to property, plant and equipment related to upgrading, maintaining and modernizing the Olefins 1 unit of our Basic Petrochemicals Unit during a scheduled shutdown.

*Cash Flows from Financing Activities*

Financing activities used net cash of R$329.7 million during 2005 and provided net cash of R$166.0 million during 2004 and R$379.1 million in 2003. Without giving effect to the proportional consolidation of our jointly controlled companies, financing activities used net cash of R$754.4 million during 2005, and provided net cash of R$309.5 million during 2004 and R$481.9 million in 2003.

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During 2005, our principal sources of long-term borrowed funds consisted of:

- issuances of our 9.75% Perpetual Bonds in an aggregate principal amount of US$150.0 million, our 9.375% Senior Notes due 2015 in an aggregate principal amount of US$150.0 million, our 13th issue of debentures in an aggregate principal amount of R$300.0 million, and quotas (shares) by Chemical Credit Rights Investment Fund II in the aggregate amount of R$400.0 million; and

- loans of US$111.7 million under two syndicated credit agreements and US$45.0 million under a pre-export finance facility.

During 2005, we used cash to repay:

- R$2,338.8 million of our short-term debt, principally debt denominated in foreign currencies, including US$247.3 million under advances on export contracts (*Adiantamentos sobre Contratos de Exportação*), US$213.8 million under our export prepayment agreements, US$146.7 million under our raw materials financing arrangements, and US$65.0 million of 9.25% notes due 2005 issued under our medium-term note program; and

- R$617.2 million of our long-term debt, including US$150 million of our 9.375% Senior Notes due 2015 and US$100 million of our 10.625% Notes due 2007.

We also repaid R$124.7 million of borrowings under four loan agreements with Copesul Trading International Inc., a related party, during 2005.

During 2004, we recorded a capital increase of R$1,211.0 million as a result of our sale of 53,820,000 of our class A preferred shares in a global offering, principally conducted in the United States and Brazil. During 2004, our principal sources of long-term borrowed funds consisted of:

- issuances in an aggregate amount of US$250.0 million under our medium-term note program, R$1,200.0 million under our 11th issue of debentures, and R$300.0 million under our 12th issue of debentures; and

- loans of US$200.0 million under a syndicated secured export prepayment facility and US$50.0 million under an export prepayment facility.

During 2004, we used cash to repay:

- R$4,595.7 million of our short-term debt, including (1) the short-term portion of our 11th issue of debentures, (2) our 11.0% notes due 2004 at maturity and the first tranche of an export prepayment credit facility, and (3) the second tranche of an export prepayment credit facility; and

- R$991.6 million of our long-term debt, including the prepayment of the long-term portion of our 11th issue of debentures.

We also borrowed R$39.9 million on market terms from related parties, principally from Copesul Trading International Inc., to finance our working capital requirements during 2004 and repaid R$109.2 million of borrowings from Copesul Trading International Inc.

In 2003, our principal source of long-term borrowed funds consisted of issuances in an aggregate amount of US$461.0 million under our medium-term note program and US$30.0 million of proceeds of a syndicated, secured pre-export finance facility. We used cash in 2003 to repay R$389.3 million of our outstanding long-term debt and to repay R$1,259.4 million of our outstanding short-term debt as part of our strategy to increase the average maturity of our indebtedness. We borrowed R$833.6 million on market terms from related parties, principally from Copesul Trading International Inc. and Petroflex, to finance our working capital requirements during 2003 and repaid R$843.2 million to these related parties.

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Between May 20, 2002 and March 31, 2005, we did not have retained earnings (but rather had an accumulated deficit) and accordingly did not pay dividends or interest attributable to stockholders equity in 2003 or 2004. In December, 2004, we offset our accumulated deficit against our tax incentive reserve. On April 12, 2005, we paid a distribution of R$204.2 million, including R$170.0 million that was paid in the form of interest attributable to shareholders equity and R$34.2 million that was paid in the form of dividends.

On April 18, 2006, we paid a distribution of R$325.7 million, including R$270.0 million that was paid in the form of interest attributable to shareholders equity and R$55.7 million that was paid in the form of dividends.

Unless our board of directors deems it inconsistent with our financial position, payment of dividends is mandatory under our by-laws and also is required under agreements with two of our shareholders and, consequently, may give rise to a significant cash requirement in future periods. Without giving effect to the proportional consolidation of our jointly controlled companies, we recorded dividend payments and interest attributable to shareholders equity of R$209.3 million in 2005, R$4.2 million in 2004 and R$72.3 million in 2003 in our consolidated financial statements.

***Indebtedness and Financing Strategy***

At December 31, 2005, our total outstanding indebtedness on a consolidated basis, excluding related party debt, was R$5,361.1 million, consisting of R$904.3 million of short-term indebtedness, including current portion of long-term indebtedness (or 16.9% of our total indebtedness), and R$4,456.8 million of long-term indebtedness (or 83.1% of our total indebtedness). Without giving effect to the proportional consolidation of our jointly controlled companies, at December 31, 2005, our total outstanding indebtedness was R$5,003.8 million, consisting of R$620.2 million of short-term indebtedness, including current portion of long-term indebtedness, and R$4,383.6 million of long-term indebtedness.

On a consolidated basis, our *real*-denominated indebtedness at December 31, 2005 was R$2,614.5 million, and our foreign currency-denominated indebtedness was R$2,746.6 million. Without giving effect to the proportional consolidation of our jointly controlled companies, our *real*-denominated indebtedness at December 31, 2005 was R$2,329.9 million, and our foreign currency-denominated indebtedness was R$2,673.9 million. At December 31, 2005, our total outstanding indebtedness to related parties on a consolidated basis was R$6.1 million.

Our financing strategy has been to continue to extend the average maturity of our outstanding indebtedness, including by repaying short-term debt through longer-term borrowings and issuing longer-term debt securities, in order to increase our liquidity levels and improve our strategic, financial and operational flexibility. Our financing strategy over the next several years involves maintaining adequate liquidity and a debt maturity profile that is compatible with our anticipated cash flow generation. In addition, we do not expect our capital expenditures to adversely affect the quality of our debt leverage ratios or our disciplined approach to capital allocation.

*Short-Term Indebtedness*

Our consolidated short-term debt, including debentures and current portion of long-term debt, but excluding related party debt, decreased to R$904.3 million at December 31, 2005 from R$1,790.9 million at December 31, 2004. Without giving effect to the proportional consolidation of our jointly controlled companies, our short-term debt decreased to R$620.2 million at December 31, 2005, compared to R$1,522.1 million at

December 31, 2004.

We maintain short-term finance lines denominated in *reais* with a number of financial institutions in Brazil. Although we have no committed lines of credit with these financial institutions, we believe that we will continue to be able to obtain sufficient credit to finance our working capital needs based on current market conditions. At

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December 31, 2005, the consolidated outstanding balance under our working capital lines denominated in *reais* was R$73.8 million. Without giving effect to the proportional consolidation of our jointly controlled companies, we did not have an outstanding balance under our working capital lines denominated in *reais*.

We also obtain advances on certain export contracts from a variety of Brazilian financial institutions. These advances generally have a maturity of less than one year and relatively low interest rates. These advances on export contracts are generally secured by receivables to be generated from future export sales under those contracts. At December 31, 2005, our consolidated outstanding advances on export contracts totaled R$36.3 million (US$15.5 million). See note 15 to our consolidated financial statements included in this annual report. Without giving effect to the proportional consolidation of our jointly controlled companies, at December 31, 2005, we did not have any outstanding advances on export contracts.

In addition, we have incurred import financing for raw materials from various domestic and international institutions. These advances have a maturity of less than one year and bear interest at LIBOR plus a spread which varied between 0.45% and 2.50% during the year. These financings are generally evidenced by promissory notes. At December 31, 2005, our consolidated outstanding advances under our import financing arrangements totaled R$50.2 million (US$21.4 million). Without giving effect to the proportional consolidation of our jointly controlled companies, our outstanding advances under our import financing arrangements at December 31, 2005 were R$31.1 million (US$13.3 million).

*Long-Term Indebtedness*

The following table sets forth selected information with respect to certain of our principal outstanding long-term debt instruments at December 31, 2005.

| Instrument | Outstanding principal amount at December 31, 2005 | Final maturity | Principal covenants |
|---|---|---|---|
| Debentures: | | | |
| 13th Issue of Debentures | R$300.0 million | June 2010 | Financial ratios |
| 12th Issue of Debentures | R$300.0 million | June 2009 | Financial ratios, limitations on liens, dividends, asset sales and investments |
| Subordinated Convertible Debentures | R$855.8 million | July 2007 | Limitation on liens, indebtedness and investments |
| Medium-Term Notes: | | | |
| 12.50% Notes due 2008 | US$275.0 million | November 2008 | Limitations on liens, dividends, indebtedness, related party transactions, investments, and mergers |
| 11.75% Notes due 2014 | US$250.0 million | January 2014 | Limitations on liens, dividends, indebtedness, related party transactions, asset sales, and mergers |
| Other Fixed-Rate Notes: | | | |
| 9.0% Notes due 2007 | US$150.0 million | June 2007 | Limitations on liens |

| | | | |
|---|---|---|---|
| 9.375% Notes due 2015 | US$150.0 million | June 2015 | Limitations on liens, related party transactions and mergers |
| 9.75% Perpetual Bonds | US$150.0 million | | Limitations on liens, related party transactions and mergers |
| Bank Credit Facilities: | | | |
| Bank Loan (construction financing) | US$7.5 million | December 2007 | Limitations on liens and mergers |
| Secured Credit Agreement (construction financing) | R$60.3 million | June 2016 | Limitation on liens and asset sales |
| Syndicated Credit Agreement | US$44.5 million | March 2012 | Financial ratios, limitations on liens, related party transactions, mergers and asset sales |
| Syndicated Credit Agreement | US$56.2 million | June 2012 | Financial ratios, limitations on liens, related party transactions, mergers and asset sales |

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| Instrument | Outstanding principal amount at December 31, 2005 | Final maturity | Principal covenants |
|---|---|---|---|
| Acquisition Financing: | | | |
| BNDESPAR Loan | R$167.7 million | August 2006 | Limitation on share transfers |
| Export Finance Facilities: | | | |
| Customer Export Prepayment | US$15.9 million | June 2006 | Financial ratios, limitations on liens, dividends, indebtedness, investments, mergers, related party transactions and asset sales |
| Syndicated Secured Export Prepayment Facility | US$175.0 million | June 2009 | Financial ratios, limitations on liens, dividends, investments, indebtedness, asset sales, related party transactions and mergers |
| Export Prepayment Facility | US$20.0 million | October 2006 (repaid in January 2006) | Financial ratios, limitations on liens and asset sales |
| Pre-Export Finance Facility | US$36.8 million | January 2008 | |

Many of our debt instruments require that we comply with financial covenants that we must maintain, the most restrictive of which are as follows:

net debt to EBITDA less than or equal to 4.0 to 1.0 at the end of and for each fiscal quarter until maturity; and

EBITDA to net financial expenses greater than or equal to 3.5 to 1.0 at the end of and for each fiscal quarter until maturity.

We also are required to maintain a maximum ratio of short-term net debt to EBITDA for a particular fiscal quarter if our net debt to EBITDA ratio is greater than a specified level or our EBITDA to net financial expenses ratio is less than a specified level.

The definitions of EBITDA contained in these instruments vary. In the instruments containing the most restrictive financial ratios described above, EBITDA is calculated differently than under the medium-term note program and is generally defined, for purposes of the net debt to EBITDA ratio and the EBITDA to net financial expenses ratio, as operating income less financial expenses, taxes, depreciation and amortization, plus dividends and interest attributable to shareholders equity paid to us by our unconsolidated associated companies. In contrast to EBITDA as calculated under the medium-term note program covenant, the calculation of EBITDA under these instruments for purposes of these ratios does not eliminate the effect of proportional consolidation under Instruction 247. However, these instruments exclude the effect of proportional consolidation for purposes of calculating the short-term net debt to EBITDA ratio.

For the fiscal year ended December 31, 2005, we reported the following financial ratios to our creditors under the instruments containing our most restrictive debt covenants:

- net debt to EBITDA of 1.3 to 1.0; and

- EBITDA to net financial expenses of 6.1 to 1.0.

Accordingly, we were in compliance with these financial covenants at December 31, 2005, and we believe that we will be able to comply with these financial covenants for the foreseeable future. In addition, we believe that our compliance with these financial covenants will not adversely affect our ability to implement our financing plans.

Many of these instruments also contain other covenants that restrict, among other things, the ability of our company and most of our subsidiaries to:

- incur additional indebtedness;

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- incur liens;
- issue guarantees;
- issue or sell capital stock of subsidiaries;
- pay dividends or make certain other restricted payments;
- consummate certain asset sales;
- enter into certain transactions with affiliates; or
- merge or consolidate with any other person or sell or otherwise dispose of all or substantially all of our assets.

In addition, the instruments governing a substantial portion of our indebtedness contain cross-default or cross-acceleration clauses, such that the occurrence of an event of default under one of these instruments could trigger an event of default under other indebtedness or enable the creditors under other indebtedness to accelerate that indebtedness.

At December 31, 2005, R$566.2 million of our *real*-denominated debt and R$183.9 million of our foreign currency-denominated debt (in each case, excluding related party debt) was secured. In order to secure this debt, we have pledged (1) some shares owned by our company in subsidiaries and affiliates, including shares of Copesul and Politeno, (2) certain of our property and equipment and (3) certain of our accounts receivable. The security arrangements for our secured debt vary depending on the transaction.

The following discussion briefly describes certain of our significant financing transactions. We have assumed the obligations of predecessor companies, including, among others, OPP Química (and its predecessor OPP Petroquímica) and Trikem, under these financing transactions as a result of the mergers of these companies into our company.

*13th Issue of Debentures*. On June 1, 2005, we issued our 13th issue of unsecured non-convertible debentures in a single series of 30,000 debentures, each with a par value of R$10,000. The principal amount of these debentures is payable in full on June 1, 2010, and these debentures bear interest at a rate of 104.1% of the CDI rate per annum payable semi-annually in arrears in June and December of each year.

*12th Issue of Debentures*. On June 1, 2004, we issued our 12th issue of secured non-convertible debentures in a single series of 3,000 debentures, each with a par value of R$100,000. These debentures are secured by a pledge of one of our long-term customer contracts and a related collection account, which pledge may be replaced or supplemented by a pledge of some of our current and future customer receivables, as well as by certain of our cash and cash equivalents if the value of the original pledge falls below a certain specified minimum level. The principal amount of these debentures is payable in full on June 1, 2009, and these debentures bear interest at the rate of 117% of the CDI rate per annum, payable semi-annually. We have the right to redeem these debentures at any time on or after June 1, 2007.

*Subordinated Convertible Debentures.* On May 31, 2002, OPP Produtos Petroquímicos S.A., or OPP Produtos, issued subordinated convertible debentures. As a result of our merger with OPP Produtos on August 16, 2002, these debentures became our obligations. The original principal amount of these debentures was R$591.9 million. At December 31, 2005, the outstanding amount of these debentures was R$999.3 million (including interest). Interest and monetary adjustment on these debentures accrues at the TJLP plus 5.0% per annum and will be accreted until their maturity on July 31, 2007. ODBPAR Investments, as the holder of these debentures, has the option to convert the debentures into shares of our share capital at any time. The initial conversion price of these debentures was R$12.19 per class A preferred share, plus accrued interest. The conversion price increases at a rate equal to the TJLP less 6.0% per annum from the date of the issuance of these debentures. At March 31, 2006, the conversion price of these debentures was R$14.23 per class A preferred share. Upon conversion, we will issue class A preferred shares up to the legal limit for preferred shares of two-thirds of our total share capital. After this two-thirds limit is reached, we will issue any remaining shares to be converted in the following proportions: one-third in common shares; and two-thirds in class A preferred shares. If ODBPAR Investments had exercised its option to convert these debentures in full on May 31, 2006, ODBPAR Investments would have received 24,718,773 of our common shares and 49,437,545 of our class A preferred shares in exchange for these debentures.

*Medium-Term Note Program.* On July 16, 2003, we established a medium-term note program permitting us to issue up to US$500.0 million aggregate principal amount of notes with maturities of up to five years from date of issuance. On December 16, 2003, we amended our medium-term note program to increase the maximum aggregate principal amount that we are permitted to issue to US$1.0 billion and to extend the maximum maturity of the notes issued under the program to ten years from the date of issuance. We have two series of outstanding notes under the program.

Between November 5, 2003 and November 26, 2003, we issued and sold US$275.0 million aggregate principal amount of our 12.50% Notes due 2008. Interest on these notes is payable semi-annually in arrears in May and November of each year and these notes mature on November 5, 2008.

On January 22, 2004, we issued and sold US$250.0 million in aggregate principal amount of our 11.75% Notes due 2014 under the medium-term note program. Interest on these notes is payable semi-annually in arrears in January and July of each year and these notes mature on January 22, 2014.

*Fixed Rate Notes.* On June 25, 1997, we issued and sold US$150.0 million aggregate principal amount of our 9.0% Notes due 2007. Interest on these notes is payable semi-annually in arrears in June and December in each year, and these notes mature on June 25, 2007.

On July 24, 1997, Trikem issued and sold US$250.0 million aggregate principal amount of its 10.625% Notes due 2007. We assumed the obligations of Trikem under these notes as a result of the merger of Trikem with and into our company on January 15, 2004. On July 24, 2005, we repurchased these notes and amended and restated their terms. As amended and restated, these notes bear interest at the rate of 9.375% per annum, payable semi-annually in arrears in June and December in each year and mature on June 1, 2015. On August 24, 2005, we exchanged US$150.0 million aggregate principal amount of these notes for US$150.0 million aggregate principal amount of outstanding notes issued by one of subsidiaries on June 1, 2005 and guaranteed by our company.

On June 17, 2005, we issued and sold US$150.0 million aggregate principal amount of our 9.75% Perpetual Bonds. Interest on these bonds is payable quarterly in arrears in March, June, September and December in each year. We may, at our option, redeem these bonds, in whole but not in part, at 100% of their principal amount plus accrued interest and additional amounts, if any, on any interest payment date on or after June 17, 2010.

*Bank Credit Facilities.* In January 1998, several financial institutions granted a loan in the amount of US$30.0 million to Proppet to finance construction of its PET plant in Camaçari, Bahia. This loan has since been amended to, among other provisions, reflect the merger of Proppet with and into our company. ODBPAR Investments, Norquisa and Mitsubishi have guaranteed this loan. ODBPAR Investments and Norquisa have also agreed to reimburse Mitsubishi for any payments that it makes in respect of this guarantee if we default on our payment obligations under the loan. To guarantee their reimbursement obligations, Norquisa and ODBPAR Investments have caused our company to grant Mitsubishi a second mortgage on its DMT and PET plants and to pledge the equipment related to its DMT and PET production. The loan amortizes in equal semi-annual installments until its final maturity in December 2007. The loan bears interest at the rate of LIBOR plus

3.875% per annum, payable semi-annually in arrears in June and December of each year. Ninety-five percent of the principal and interest of this loan is supported by insurance from Nippon Export and Investment Insurance, and we pay annual premiums in yen for this insurance. At December 31, 2005, the outstanding principal amount of this loan was US$7.5 million.

On June 30, 2004, we entered into a secured credit agreement in the aggregate amount of R$152.7 million to finance capital expenditures in certain of our plants located in the Northeastern Complex and in Alagoas that we made in 2004 and 2005. The loans under this credit agreement are secured by a first mortgage on our PVC plant located in São Paulo and our chloro-soda plant located in the Northeastern Complex, as well as by a purchase-money security interest in machinery and equipment that we have and will purchase with the proceeds of this loan. Under this credit agreement, we are required to invest up to R$65.4 million of our own funds in accordance with an investment schedule as a condition precedent to disbursements of the loans. As of December 31, 2005, we have invested R$41.0 million on capital expenditures included on this investment schedule, including loans to our company in the aggregate principal amount of R$28.7 million disbursed by the lender. The loans under this credit agreement bear interest at the rate of 14.0% per annum, payable quarterly in arrears through June 30, 2008 and thereafter monthly in arrears through June 30, 2016. The lender under this credit agreement may modify the interest rate annually based on fluctuations in the TJLP during the preceding year and upon written notice to our company. The principal amount of these loans is payable in 96 equal monthly installments, commencing on July 30, 2008. At December 31, 2005, the outstanding principal amount under this credit agreement was R$60.3 million.

On March 24, 2005, we borrowed the Japanese yen equivalent of US$50 million under a syndicated credit agreement dated March 8, 2005. The proceeds of this loan were required to be used for capital expenditures related to our Braskem+ program. This loan bears interest at the rate of six-month Tokyo Inter-Bank Offered Rate plus 0.95% per annum, payable semi-annually in arrears. Principal on this loan is payable in 11 equal installments beginning in March 2007 with a final maturity date in March 2012. In connection with this loan, we entered into a swap contract in the total amount of this debt, which effectively modifies the interest rate to 101.59% of CDI. The maturities, currency, rates and amounts of the swap contract correspond to the terms of the loan. Ninety-five percent of the commercial risk of this loan and 97.5% of the political risk of this loan are supported by insurance from Nippon Export and Investment Insurance, for which we paid a lump-sum premium in yen. At December 31, 2005, the outstanding principal amount under this credit agreement was US$44.5 million.

On September 20, 2005, we borrowed the Japanese yen equivalent of US$60 million under a syndicated credit agreement dated June 30, 2005. The proceeds of this loan were required to be used for capital expenditures related to the Braskem+ program. This loan bears interest at the rate of six-month Tokyo Inter-Bank Offered Rate plus 0.95% per annum, payable semi-annually in arrears. Principal on this loan is payable in 11 equal installments beginning in June 2007 with a final maturity date in June 2012. In connection with this loan, we entered into a swap contract in the total amount of this debt, which effectively modifies the interest rate to 104.4% of CDI. The maturities, currency, rates and amounts of the swap contract correspond to the terms of the loan. Ninety-five percent of the commercial risk of this loan and 97.5% of the political risk of this loan are supported by insurance from Nippon Export and Investment Insurance, for which we paid a lump-sum premium in yen. At December 31, 2005, the outstanding principal amount under this credit agreement was US$56.2 million.

*Acquisition Financing.* In September 2001, BNDESPAR Participações S.A. BNDESPAR or BNDESPAR, sold 1,000,000,000 class B preferred shares of Nova Camaçari for a purchase price of R$163.9 million and, as part of this transaction, BNDESPAR extended a loan to Nova Camaçari in a principal amount equal to the purchase price. We acquired Nova Camaçari on July 25, 2001 and merged with Nova Camaçari in September 2001. This loan bears interest at the TJLP plus 4.0% per annum, payable annually each August 15, and matures on August 15, 2006. At December 31, 2005, the outstanding principal amount of this loan was R$167.7 million.

Subject to the preemptive rights of existing shareholders, BNDESPAR has the option to convert the principal amount of and accrued interest on this loan into our class A preferred shares at any time prior to the maturity of this loan. If this loan is converted in connection with a public offering, the conversion price will be the offering price. If this loan is converted other than in connection with a public offering, the conversion price will be the weighted average of the average daily prices for our class A preferred shares on the São Paulo Stock Exchange during the 60 days prior to the conversion, or, if greater, the offering price in our last public offering occurring within the nine months prior to the conversion, if any, monetarily restated by the IGP-M. At May 31, 2006, the conversion price would have been R$15.62 per share. If BNDESPAR had exercised its option to convert this loan in full on May 31, 2006, BNDESPAR would have been entitled to receive 11,864,558 of our class A preferred shares in exchange for this loan. Our bylaws require that no more than two-thirds of our total share capital be represented by preferred shares. In the event that at the time that BNDESPAR exercises its option we are unable to issue the number of shares of class A preferred shares to which BNDESPAR is then entitled, we expect that we and BNDESPAR will mutually agree on an alternative that will satisfy the provisions of our bylaws.

Upon conversion, we will issue class A preferred shares up to the legal limit for preferred shares of two-thirds of our total share capital. After this two-thirds limit is reached, we will issue any remaining shares to be converted in the following proportions: one-third in common shares; and two-thirds in class A preferred shares.

*Export Prepayment Facilities.* In December 2002, OPP Química entered into a prepayment advance for products to be exported to a foreign customer in the amount of US$97.2 million. This prepayment advance bore interest at the rate of six-month LIBOR plus 3.75% per annum until December 9, 2004. On December 9, 2004, this prepayment advance was amended to reduce the interest rate on this prepayment advance to the rate of six-month LIBOR plus 1.25% per annum. This prepayment advance will be paid through partial semi-annual shipments from December 2003 to June 2006. Our obligation to deliver export products is guaranteed by a surety bond. At December 31, 2005, the outstanding principal amount of this prepayment advance was US$15.9 million.

On June 7, 2004, Overseas III Export Ltd., a special purpose company created by QSPV Limited, entered into a US$200.0 million syndicated credit agreement. During June 2004, US$70.0 million was disbursed to Overseas III Export Ltd. and lent by Overseas III Export Ltd. to our company on identical terms and conditions as those contained in the syndicated credit agreement. During August 2004, the remaining US$130.0 million was disbursed to Overseas III Export Ltd. and lent by Overseas III Export Ltd. to our company on the identical terms and conditions as those contained in the syndicated credit agreement. The loan to Overseas III Export Ltd. has been guaranteed by our company and is secured by certain of our exports. The first tranche of this loan in the principal amount of US$145.0 million bore interest at the rate of six-month LIBOR plus 3.5% per annum, payable semi-annually in arrears, until June 30, 2005. The second tranche of this loan in the principal amount of US$55.0 million bore interest at the rate of six-month LIBOR plus 4.5% per annum, payable semi-annually in arrears, until June 30, 2005. On June 30, 2005, the syndicated credit agreement was amended to combine the two tranches into one and to reduce the interest rate on the outstanding principal amount of this loan to the rate of six-month LIBOR plus 1.45% per annum. Principal on this loan is payable in eight semi-annual installments beginning in December 2005. At December 31, 2005, the outstanding principal amount of this loan was US$175.0 million.

On July 21, 2004, we entered into an export prepayment facility in an aggregate amount of US$50.0 million. The loan under this facility is secured by certain of our export receivables and bears interest at a rate of three-month LIBOR plus 3.0% per annum, payable quarterly in arrears commencing on January 21, 2005. The principal amount of this facility is payable in eight equal quarterly installments beginning in January 2005. At December 31, 2005, the outstanding principal amount under this export prepayment facility was US$20.0 million. The outstanding principal amount of this facility was prepaid on January 21, 2006.

On January 19, 2005, we entered into a pre-export finance facility in an aggregate principal amount of US$45.0 million. The loans under this facility are secured by certain of our export receivables and bear interest at a rate of three-month LIBOR plus 1.00% per annum, payable quarterly in arrears commencing on April 30, 2005. The principal amount of this facility is payable in 11 equal quarterly installments beginning on July 31, 2005, with a final maturity date of January 31, 2008. At December 31, 2005, the outstanding principal amount under this facility was US$36.8 million.

*BNDES Development Loans.* We maintain credit facilities that are granted directly or indirectly by BNDES, the Brazilian federal government development bank, to fund general capital expenditures associated principally with the expansion of our production capacity, environmental projects and the development of operation control centers, laboratories and waste treatment station, of which R$189.1 million principal amount was outstanding at December 31, 2005. Amounts borrowed from BNDES are secured by a pledge of certain equipment and machinery owned by us. The interest rate on most of the amounts we borrowed from BNDES is based on the TJLP plus a margin of 2% to 5% per annum. Other amounts borrowed from BNDES bear interest at a government reference rate (the *Taxa Referencial*), plus a margin of 6.5%, or at a rate based on the Monetary Unit of BNDES (*Unidade Monetária do BNDES*, or UM), a BNDES rate based on a basket of currencies (which rate reflects the daily exchange rate fluctuations in the currencies in which BNDES borrows), plus a margin. The principal and interest on these credit facilities is payable monthly through July 2007.

On June 24, 2005, we entered into two credit facilities with BNDES under which BNDES will disburse loans in an aggregate principal amount of approximately R$336.2 million. The proceeds of the first credit facility are R$84.2 million, which we will use to finance capital expenditures related to (1) the 50,000 ton increase in the annual production capacity of our Alagoas PVC plant, and (2) a project to use polypropylene in the disposable plastics market. The proceeds of the second credit facility are R$252.0 million, which we will use to finance capital expenditures related to (1) the 100,000 ton increase in the annual production capacity of one of our polypropylene plants located in the Southern Complex, and (2) quality, productivity, environmental, health and safety projects at our plants. These credit facilities are secured by a letter of credit. This letter of credit may be substituted by (1) a mortgage on one of our plants located in the Southern Complex (including the land on which this plant is located, as well as certain of the equipment, machinery and improvements in this plant) and (2) a guarantee by Odebrecht. Amounts under the first credit facility will be disbursed in two tranches, and amounts under the second credit facility will be disbursed in three tranches. The first tranche of these credit facilities in an aggregate principal amount of R$12.6 million and R$37.8 million, respectively, bears interest at a rate based on the UM plus a margin of 4% per annum. The other tranches of these credit facilities bear interest at the TJLP plus a margin of 4% per annum. Interest is payable on the first credit facility quarterly from July 15, 2005 through July 15, 2007 and monthly thereafter through maturity. The outstanding principal amount of the first credit facility is payable in 48 equal, successive monthly installments beginning on August 15, 2007. Interest is payable on the first and second tranches of the second credit facility quarterly from July 15, 2005 through January 15, 2007 and monthly thereafter through maturity. The outstanding principal amount of the first and second tranches of the second credit facility is payable in 48 equal, successive monthly installments beginning on February 15, 2007. Interest is payable on the third tranche of the second credit facility quarterly from July 15, 2005 through July 15, 2008 and monthly thereafter through maturity. The outstanding principal amount of the third tranche of the second credit facility is payable in 42 equal, successive monthly installments beginning on August 15, 2008. At December 31, 2005, the outstanding principal amount under the first of these credit facilities was R$23.2 million and the outstanding principal amount under the second of these credit facilities was R$108.1 million.

*FINEP Credit Facility.* On March 8, 2005, we entered into a credit facility with *Financiadora de Estudos e Projetos*, or FINEP, a technology funding institution of the Ministry of Science and Technology of Brazil, in an aggregate principal amount of R$84.9 million, to be disbursed in eight quarterly installments, beginning on March 15, 2005, with the final disbursement on March 15, 2007. We are required to use the proceeds disbursed under this credit facility for capital expenditures at the Braskem Center for Innovation and Technology operated by our Polyolefins Unit, the research and development pilot plant of our Vinyls Unit, and the research center of our Vinyls Unit. Under this credit facility, we are required to invest at least R$9.4 million of our own funds in these projects. The loans bear interest at a rate of TJLP plus 5% per annum, payable quarterly in arrears commencing on June 15, 2005. However, we may be required to pay interest at only the TJLP, depending on the financial condition and liquidity of the National Scientific and Technological Development Fund (*Fundo Nacional de Desenvolvimento Científico e Tecnológico*) at any given time. The principal amount under this credit facility will be payable in 61 equal monthly installments beginning on March 15, 2007, with a final maturity date of March 15, 2012. At December 31, 2005, the outstanding principal amount under this credit facility was R$22.1 million. Our obligation to make payments under this credit facility is guaranteed by a surety bond.

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*Quotas (shares) subject to mandatory redemption.* We have retained an interest in subordinated quotas (shares) of two receivables securitization funds described below. The receivables securitization funds are consolidated under Brazilian GAAP to the extent that we retain the majority of the possible losses. We have entered into these arrangements in order to increase our liquidity, as it enables us to receive immediate payment for purchases of petrochemical products by clients to whom we provide short-term trade financing in the ordinary course of our business.

Beginning on January 1, 2005, pursuant to CVM Instruction 408, we are required to consolidate special purpose entities in our financial statements if specific criteria are met. See Introduction Financial Statements.

*Chemical Credit Rights Investment Fund.* On November 6, 2003, our company, Trikem and Polialden entered into a receivables purchase and sale agreement with a special purpose receivables investment fund under which our company, Trikem and Polialden agreed to sell to the fund from time to time, without recourse, certain trade receivables represented by negotiable invoices *(duplicatas)*. As a result of the merger of Trikem into our company in January 2004, we assumed Trikem s rights and obligations under this agreement. As a result of the merger of Polialden into our company on May 31, 2006, we assumed Polialden s rights under this agreement. Under this agreement, this fund may purchase these receivables using (1) the net proceeds that it obtains from the sale of interests, or senior quotas, in the fund to certain qualified investors in Brazil and (2) past due receivables that our company has previously sold to the fund and, although not obligated to do so, agreed to repurchase. The fund also may invest a portion of such net proceeds in cash and certain cash equivalents. The aggregate amount of the quotas of all series outstanding at any time may not exceed R$500.0 million. Each series of quotas will have a maturity of not less than 12 months from the date of issuance and will amortize on June 15 and December 15 of each year. The amortization payments will include amounts in respect of interest calculated as a multiple of the CDI rate.

The fund may cause the early amortization of quotas to the extent necessary to meet specified coverage ratios or to ensure that receivables constitute at least a specified percentage of the fund s net worth. We also agreed to purchase subordinated quotas from the fund to the extent necessary to enable the fund to meet specified coverage ratios, whether measured on periodic calculation dates or measured on a pro forma basis before the issuance of quotas to investors. In addition, we are required to maintain an insurance policy covering an aggregate amount of 20% of the value of any series of quotas issued by the fund, and the fund may demand payment under the insurance policy in the amount of the receivables under any negotiable invoice for which documents necessary to pursue a collection action against the applicable obligor are unavailable.

On December 15, 2003, the fund issued R$100.0 million in aggregate amount of quotas, and on January 9, 2004, the fund issued another R$100.0 million in aggregate amount of quotas. These quotas will mature on December 15, 2006. The first series of quotas consists of 8,000 quotas, each with a unit value of R$25,000. The quotas began amortizing on June 15, 2004, and the amortization payments include a targeted (but not guaranteed) amount of interest at a rate of 113.5% of the CDI rate based on market conditions. At December 31, 2005, we held R$26.4 million of subordinated quotas.

*Chemical Credit Rights Investment Fund II.* On November 30, 2005, our company and Polialden entered into a receivables purchase and sale agreement with a special purpose receivables investment fund under which our company and Polialden agreed to sell to the fund from time to time, without recourse, certain trade receivables represented by negotiable invoices *(duplicatas)*. As a result of the merger of Polialden into our company on May 31, 2006, we assumed Polialden s rights under this agreement. Under this agreement, this fund may purchase the receivables using (1) the net proceeds that it obtains from the sale of interests, or senior quotas, in the fund to certain qualified investors in Brazil and (2) past due receivables that our company has previously sold to the fund and, although not obligated to do so, agreed to repurchase. The fund also may invest a portion of such net proceeds in cash and certain cash equivalents. The aggregate principal amount of the quotas of all series outstanding at any time may not exceed R$800.0 million. Each series of quotas will have a maturity of not less

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than 12 months from the date of issuance and will amortize on June 15 and December 15 of each year. The amortization payments will include amounts in respect of interest calculated as a multiple of the CDI rate.

The fund may cause the early amortization of quotas to the extent necessary to meet specified coverage ratios or to ensure that receivables constitute at least a specified percentage of the fund s net worth. We also agreed to purchase subordinated quotas from the fund to the extent necessary to enable the fund to meet specified coverage ratios, whether measured on periodic calculation dates or measured on a pro forma basis before the issuance of quotas to investors.

On December 9, 2005, the fund issued R$400.0 million in aggregate amount of quotas, and on January 9, 2004, the fund issued another R$100.0 million in aggregate amount of quotas. These quotas will mature on December 15, 2008. The first series of quotas consists of 16,000 quotas, each with a unit value of R$25,000. The quotas began amortizing on June 15, 2006, and the amortization payments include a targeted (but not guaranteed) amount of interest at a rate of 103.75% of the CDI rate based on market conditions. At December 31, 2005, we held R$40.4 million of subordinated quotas.

**Off-balance sheet arrangements**

We do not currently have any transactions involving off-balance sheet arrangements.

**Contractual Commitments**

The following table summarizes significant contractual obligations and commitments at December 31, 2005 that have an impact on our liquidity:

| | **Payments due by period** | | | | |
|---|---|---|---|---|---|
| **(In millions of *reais*)** | **Less than one year** | **One to three years** | **Three to five years** | **More than five years** | **Total** |
| Loans and financings | R$ 895.0(1) | R$ 1,228.5 | R$ 243.5 | R$ 1,385.5 | R$ 3,752.5 |
| Debentures | 9.3(1) | 999.3 | 600.0 | | 1,608.6 |
| Interest on loans, financings and debentures(2) | 355.2 | 745.8 | 339.6 | 669.2 | 2,109.8 |
| Quotas (shares) subject to mandatory redemption | 225.4 | 404.1 | | | 629.5 |
| Interest on quotas subject to mandatory redemption(3) | 111.6 | 118.7 | | | 230.3 |
| Purchase obligations(4) | 6,247.8 | 8,616.5 | 1,177.1 | 1,569.4 | 17,610.8 |
| Pension plan contributions(5) | | 55.3 | | | 55.3 |
| Other long-term liabilities | | 128.5 | | | 128.5 |
| Total contractual obligations | 7,844.3 | 12,296.7 | 2,360.2 | 3,624.1 | 26,125.3 |
| Exclusion of proportional consolidation: | | | | | |
| Loans and financings | 284.1(1) | 53.6 | 17.5 | 2.1 | 357.3 |

| | | | | | |
|---|---|---|---|---|---|
| Interest on loans and financings(2) | 28.4 | 5.4 | 1.8 | 0.2 | 35.8 |
| Other long-term liabilities | | 36.4 | | | 36.4 |
| Total contractual obligations, excluding the effects of proportional consolidation | R$ 7,531.8 | R$ 12,201.3 | R$ 2,340.9 | R$ 3,621.8 | R$ 25,695.8 |

(1) Includes interest accrued at December 31, 2005.

(2) Consists of estimated future payments of interest on our loans, financings and debentures, calculated based on interest rates and foreign exchange rates applicable at December 31, 2005 and assuming (i) that all amortization payments and payments at maturity on our loans, financings and debentures will be made on their scheduled payment dates, and (ii) that our perpetual bonds are redeemed on the first permitted redemption date.

(3) Consists of estimated future payments of interest on quotas (shares) subject to mandatory redemption, calculated based on interest rates and foreign exchange rates applicable at December 31, 2005 and assuming that all amortization payments and payments at maturity on our quotas (shares) subject to mandatory redemption will be made on their scheduled payment dates.

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(4) Consists of purchase commitments for raw material and electric power pursuant to binding obligations which include all significant terms, including fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transaction. Based upon the applicable purchase prices at December 31, 2005.

(5) Consists of a final disbursement by our company to two defined benefit pension plans in an amount that we estimate will be assessed by the *Secretaria da Previdencia Complementar* (Secretariat for Complementary Pensions) based on projections which we have obtained from independent actuaries. In June 2005, we announced that we intend to withdraw as a sponsor of these two defined benefit pension plans.

We are also subject to contingencies with respect to tax, labor, distributors, and other claims and have made provisions for accrued liability for legal proceedings related to certain tax claims of R$1,370.4 million at December 31, 2005. The tax contingencies relate primarily to COFINS, PIS, IPI, federal income tax and the Social Contribution on Net Income. See Item 8. Financial Information Legal Proceedings and notes 17 and 18 to our consolidated financial statements.

**U.S. GAAP Reconciliation**

Our net income in accordance with Brazilian GAAP was R$625.8 million in 2005, R$687.1 million in 2004 and R$215.1 million in 2003. Under U.S. GAAP, we would have reported net income of R$737.1 million in 2005, R$887.8 million in 2004 and R$378.1 million in 2003.

Our shareholders equity in accordance with Brazilian GAAP was R$4,535.8 million at December 31, 2005 and R$4,183.7 million at December 31, 2004. Under U.S. GAAP, we would have reported shareholders equity of R$3,063.6 million at December 31, 2005 and R$2,588.9 million at December 31, 2004.

The principal differences between Brazilian GAAP and U.S. GAAP that affected our net income in 2005, 2004 and 2003, as well as shareholders equity at December 31, 2005 and 2004, are described in note 31 to our audited consolidated financial statements included elsewhere in this annual report. The major differences relate to the accounting treatment of the following items:

- supplementary inflation restatement of permanent assets and shareholders equity in 1996 and 1997;
- capitalized interest;
- deferred charges and other intangible assets;
- impairment;
- business combinations and goodwill;
- transactions giving rise to distributions to shareholders;

guarantees;

pension benefits;

earnings per share;

comprehensive income;

deferred taxes;

dividends

tax incentives;

revenue recognition;

consolidation of securitization fund;

proportional consolidation of jointly controlled entities;

classification of statement of operations and balance sheet items;

segment reporting;

derivatives;

U.S. GAAP adjustments on equity investee; and

capital issuance cost.

For a discussion of the principal differences between Brazilian GAAP and U.S. GAAP as they relate to our financial statements and a reconciliation of net income and shareholders equity, see note 31 to our audited consolidated financial statements included elsewhere in this annual report.

## ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

### Directors and Senior Management

Our board of directors (*conselho de administração*) and our board of executive officers (*diretoria*) are responsible for operating our business.

### Board of Directors of Braskem

Our by-laws provide for a board of directors of eleven members and eleven alternate members. During periods of absence or temporary unavailability of a regular member of our board of directors, the corresponding alternate member substitutes for the absent or unavailable regular member. Our board of directors is a decision-making body responsible for, among other things, determining policies and guidelines for our business and our wholly-owned subsidiaries and controlled companies. Our board of directors also supervises our board of executive officers and monitors its implementation of the policies and guidelines that are established from time to time by the board of directors. Under the Brazilian Corporation Law, our board of directors is also responsible for hiring an external independent registered public accounting firm.

The members of our board of directors are elected at general meetings of shareholders for two-year terms and are eligible for reelection. The terms of all current members expire at our annual shareholders meeting in 2008. Members of our board of directors are subject to removal at any time with or without cause at a general meeting of shareholders. Although our by-laws do not contain any citizenship or residency requirements for members of our board of directors, the members of our board of directors must be shareholders of our company. Our board of directors is presided over by the president of the board of directors, and, in his absence, the vice president of the board of directors. The president and the vice president of our board of directors are elected at a general meeting of shareholders from among the members of our board of directors, serve for one-year terms and are eligible for reelection.

Our board of directors ordinarily meets four times a year and extraordinarily when a meeting is called by the president, the vice president or any two other members of our board of directors. Decisions of our board of directors require a quorum of a majority of the directors and are taken by majority vote, subject to the veto rights of Petroquisa over resolutions of our board of directors relating to certain matters under the Petroquisa memorandum of understanding. See Item 7. Major Shareholders and Related Party Transactions Major Shareholders Shareholders Agreements.

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The following table sets forth certain information with respect to the current members of our board of directors and their alternates:

| Name | Member since | Position held | Age |
|---|---|---|---|
| Pedro Augusto Ribeiro Novis | Aug. 15, 2001 | President of the Board | 59 |
| Eliani Maria Borazo Rubira | April 7, 2006 | Alternate | 55 |
| Alvaro Fernandes da Cunha Filho | Nov. 6, 1997 | Vice President of the Board | 57 |
| Marcos Luiz Abreu de Lima | March 31, 2005 | Alternate | 63 |
| José de Freitas Mascarenhas | Aug. 15, 2001 | Board Member | 64 |
| Guilherme Simões de Abreu | March 4, 2002 | Alternate | 54 |
| Luiz Fernando Cirne Lima | Aug. 15, 2001 | Board Member | 73 |
| Hilberto Mascarenhas Alves da Silva Filho | April 29, 2003 | Alternate | 50 |
| Newton Sergio de Souza | Aug. 15, 2001 | Board Member | 53 |
| Cláudio Melo Filho | October 3, 2005 | Alternate | 38 |
| Alvaro Pereira Novis | Aug 15, 2001 | Board Member | 62 |
| Marcos Wilson Spyer Rezende | Sept. 29, 2002 | Alternate | 58 |
| Francisco Teixeira de Sá | May 24, 2001 | Board Member | 57 |
| Lúcio José Santos Júnior | Aug. 15, 2001 | Alternate | 40 |
| Maria das Graças Silva Foster | October 3, 2005 | Board Member | 52 |
| Edmundo José Correia Aires | April 29, 2003 | Alternate | 47 |
| Patrick Horbach Fairon | November 30, 2004 | Board Member | 50 |
| Rogério Gonçalves Mattos | Sept. 29, 2002 | Alternate | 50 |
| Ruy Lemos Sampaio | April 7, 2006 | Board Member | 56 |
| Rubio Fernal Ferreira e Sousa | April 7, 2006 | Alternate | 55 |
| Masatoshi Furuhashi | April 7, 2006 | Board Member | 57 |
| Yukihiro Funamoto | April 7, 2006 | Alternate | 34 |

The following is a summary of the business experience, areas of expertise and principal outside business interests of our current directors and their alternates. Except as otherwise set forth below, the business address of (1) each of our current directors is Avenida Nações Unidas, 4777, São Paulo, SP CEP 05477-000, Brazil and (2) each of our alternate directors is the same as the business address of the director for which he or she is an alternate.

***Directors***

*Pedro Augusto Ribeiro Novis*. Mr. Novis was elected to our board of directors as a nominee of Odebrecht. He has been a member of our board of directors since August 2001 and was elected president of our board of directors in March 2002. He has served as a member of the board of directors of Odebrecht since October 1997 and as the chief executive officer of Odebrecht since January 2002. In addition, Mr. Novis serves in various capacities with other companies in the Odebrecht Group. He has been with the Odebrecht Group since 1968. He holds a law degree from the Universidade Federal da Bahia. Mr. Novis is a cousin of Mr. Alvaro Pereira Novis.

*Alvaro Fernandes da Cunha Filho*. Mr. Cunha Filho was elected to our board of directors as a nominee of Odebrecht and has been a member of our board of directors since 1997. He is currently the vice president of our board of directors and the president of Valora Participações Ltda. Mr. Cunha Filho served as vice president of the board of directors of Norquisa from 1997 through 1999, and from 2001 through 2003 as a member of the board of directors of Norquisa. He has also occupied several executive positions in subsidiaries and affiliates of Odebrecht. Mr. Cunha Filho holds a bachelor s degree in civil engineering and a master s degree in economics from the Universidade Federal da Bahia.

*José de Freitas Mascarenhas*. Mr. Mascarenhas has been a member of our board of directors as a nominee of Odebrecht since 2001. He has been an executive officer of Odebrecht since September 2001 and serves in

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various capacities with other companies in the Odebrecht Group. He also has served as vice president of CNI Confederação Nacional das Indústrias since October 1985 and of the Brazilian Association of Chemical Industry and Derivative Products since May 1993. Mr. Mascarenhas holds a bachelor s degree in civil engineering from Universidade Federal da Bahia. Mr. Mascarenhas business address is Avenida Luiz Viana Filho, 2841, Salvador, BA CEP 41730-900, Brazil.

*Luiz Fernando Cirne Lima*. Mr. Lima has been a member of our board of directors as a nominee of Odebrecht since 2001. He is currently the superintendent executive officer of Copesul and a member of the board of directors of Banco Icatu S.A., a Brazilian bank. Mr. Lima has also served as the Brazilian Minister of Agriculture from 1969 through 1973. Mr. Lima holds a bachelor s degree in agronomical engineering from the Universidade Federal do Rio Grande do Sul. Mr. Lima s business address is Rua Dolores Alcaraz Caldas, 90, Porto Alegre, RS CEP 90110-180, Brazil.

*Newton Sergio de Souza*. Mr. Souza has been a member of our board of directors as a nominee of Odebrecht since 2001. He has been the general counsel and an executive officer of Odebrecht since May 1997, and the vice president of the board of directors and an executive officer of Norquisa since April 2003. He also serves in several executive positions in subsidiaries and affiliates of Odebrecht. Mr. Souza served as the president of the board of directors of Companhia de Concessões Rodoviárias CCR. He was also a visiting lawyer at the law firm Dechert, Price & Rhoads (Philadelphia), a senior lawyer at the law firm Pinheiro Neto Advogados from 1976 through 1982 and a senior counsel of Latin America and Caribbean Division of the World Bank (Washington D.C.) from 1982 through 1987. Mr. Souza holds a law degree from Pontifícia Universidade Católica do Rio de Janeiro and an LL.M. from the University of Pennsylvania.

*Alvaro Pereira Novis*. Mr. Novis has been a member of our board of directors as a nominee of Odebrecht since 2001. He has been the administrator of the board of directors of Odebrecht since December 2003, the chief financial officer and an executive officer of Odebrecht since July 1998, and serves in various capacities with other companies in the Odebrecht Group. In 1980, he was elected managing director of Banco Iochpe de Investimentos, where he became president in 1995 upon its association with Bankers Trust Company. Mr. Novis holds a bachelor s degree in economics from the Universidade do Rio de Janeiro and a master s degree in Public Administration from Fundação Getúlio Vargas. Mr. Novis is a cousin of Pedro Augusto Ribeiro Novis.

*Francisco Teixeira de Sá*. Mr. Sá has been a member of our board of directors as a nominee of the Mariani Group since 2001. He served as a member of the board of directors of Norquisa from April 2001 through April 2005 and served as president of the board of directors of Norquisa from April 2001 through April 2003. He is also president of Pronor. Mr. Sá served as engineering and production manager of Dow Química S.A. from 1973 through 1984. He holds a bachelor s degree in chemical engineering from the Universidade Federal da Bahia. Mr. Sá s business address is Quadra 3 do SESFI, Cia Sul, Simões Filho, BA CEP 43780-000, Brazil.

*Maria das Graças Silva Foster*. Mrs. Foster was elected to our board of directors as a nominee of Petroquisa and has been a member of our board of directors since October 3, 2005. Mrs. Foster has been the CEO of Petroquisa since September 2005. Mrs. Foster has served as Executive Manager of the supply area for Petrobras since September 2005 and has been responsible for investor relations at Petroquisa since September 2005. Prior to assuming these duties, Mrs. Foster served as Secretary of Oil, Natural Gas and Renewable Fuels under the Ministry of Energy from 2003 through 2005. Mrs. Foster also served as natural gas and energy technology manager of Petrobras and coordinator of RedeGasEnergia Excellence Natural Gas and Energy Distribution Network from 2000 to 2002. Mrs. Foster holds a bachelor s degree in chemical engineering from Universidade Federal Fluminense, a master´s degree in mechanical and nuclear engineering from Universidade Federal do Rio de Janeiro, and an MBA in economics from Fundação Getúlio Vargas.

*Patrick Horbach Fairon*. Mr. Fairon was elected to our board of directors as a nominee of Petroquisa and has been a member of our board of directors since November 30, 2004. Mr. Fairon has been the chief financial officer of Downstream Participações S.A. since October 2000. Mr. Fairon also served as general manager of

business development for Petrobras. Mr. Fairon holds a bachelor s degree in electrical engineering from the Universidade Federal do Rio de Janeiro UFRJ and an MBA from the Universidade Católica do Rio de Janeiro. Mr. Fairon s business address is Av. República do Chile, 500, 20 andar, Rio de Janeiro, RJ CEP 20031-170, Brazil.

*Ruy Lemos Sampaio*. Mr. Sampaio has been a member of our board of directors as a nominee of Odebrecht since April 7, 2006, and prior to that date, Mr. Sampaio served as an alternate member of our board of directors since September 27, 2002. He has been the investment officer of Odebrecht since August 2002. Previously, Mr. Sampaio occupied several executive positions within the Odebrecht Group beginning in 1985. Mr. Sampaio holds a bachelor s degree of business administration from the Universidade Federal da Bahia and an MBA degree from Michigan State University.

*Masatoshi Furuhashi*. Mr. Furuhashi has been a member of our board of directors since April 7, 2006. He has been managing director of Sojitz Corporation of America and president of Sojitz do Brasil S.A. since April 2004. From April 2001 to April 2004, he was senior vice president and managing director for the Mercosur region for Nissho Iwai American Corporation. From December 2000 to April 2001, he was general manager for southern South America and President of Nissho Iwai do Brasil S.A. From September 1995 to December 2000, he was director general and president of Nissho Iwai Mexicana S.A. Mr. Furuhashi holds a bachelor s degree in Spanish from Tokyo University of Foreign Studies. Mr. Furuhashi s business address is Avenida Paulista 1842 Torre Norte 21o andar, CEP: 01310-200 São Paulo-SP.

***Alternate Directors***

*Eliani Maria Borazo Rubira*. Ms . Rubira has been an alternate member of our board of directors as a nominee of Odebrecht since April 7, 2006. She has served as legal counsel for Odebrecht since 1999. Ms . Rubira holds a bachelor s degree in law from Faculdades Integradas de Guarulhos and completed post-graduate studies in corporate law at the Universidade Presbiteriana Mackenzie.

*Ruy Lemos Sampaio*. Mr. Sampaio has been an alternate member of our board of directors as a nominee of Odebrecht since September 27, 2002. He has been the investment officer of Odebrecht since August 2002. Previously, Mr. Sampaio occupied several executive positions within the Odebrecht Group beginning in 1985. Mr. Sampaio holds a bachelor s degree of business administration from the Universidade Federal da Bahia and a MBA degree from Michigan State University.

*Marcos Luiz Abreu de Lima*. Mr. Lima has been an alternate member of our board of directors as a nominee of Odebrecht since March 31, 2005. Mr. Lima has been an executive officer of Construtora Norberto Odebrecht since 1999, chief executive officer of Odebrecht Administradora e Corretora de Seguros Ltda. since 1980 and is a member of the fiscal council of Fundação Odebrecht. Mr. Lima holds bachelor s degrees in accounting, management and economics from the Universidade Católica de Belo Horizonte and a post-graduate degree in auditing and organization development, in addition to insurance and surety bonds. Mr. Lima s business address is Av. Luiz Viana Pinto, 2841, 1º andar Salvador, Bahia, Brazil.

*Guilherme Simões de Abreu*. Mr. Abreu has been an alternate member of our board of directors as a nominee of Odebrecht since March 4, 2002. He has been the assistant to the president of Odebrecht since 2002 and an officer of Odeprev Odebrecht Previdência since 1998. Previously, Mr. Abreu occupied several executive positions with Odebrecht beginning in 1986. Mr. Abreu holds a bachelor s degree in business administration from the Universidade Federal da Bahia.

*Hilberto Mascarenhas Alves da Silva Filho*. Mr. Silva has been an alternate member of our board of directors as a nominee of Odebrecht since April 29, 2003. He has been the assistant to the chief financial officer of Odebrecht since 1998. Previously, Mr. Silva occupied several executive positions with the Odebrecht Group beginning in 1978. He is also an officer of the Commercial Association of Bahia (Associação Comercial da

Bahia) and a member of the Financial Committee of the Brazilian Infrastructure and Basic Industry Association (ABDIB Associação Brasileira de Infra-Estrutura e Indústria de Base). Mr. Silva holds a bachelor s degree in business administration from the Universidade Federal da Bahia and attended a senior executive program at Columbia Business School and a financial planning and management course at Fundação Getúlio Vargas.

*Cláudio Melo Filho*. Mr. Melo has been an alternate member of our board of directors as a nominee of Odebrecht since October 3, 2005. He has been the new business, development and representation director of Odebrecht since 2004. Mr. Melo served as financial manager and contract manager in several projects in Brazil and Angola for Construtora Norberto Odebrecht from 1990 to 2004. Mr. Melo holds a bachelor degree in business administration from the Universidade de Brasilia and a post-graduate degree in financial administration from Fundação Getúlio Vargas.

*Marcos Wilson Spyer Rezende*. Mr. Rezende has been an alternate member of our board of directors as a nominee of Odebrecht since September 29, 2002. He has been the vice president of institutional relations of the Odebrecht Group since 2002. Mr. Rezende served as a journalist in various capacities for newspapers and television stations from 1972 through 2002. Mr. Rezende holds a bachelor s degree in sociology and politics from the Universidade Federal de Minas Gerais and in social communication from the Faculdade Casper Líbero/PUC São Paulo.

*Lúcio José Santos Júnior*. Mr. Santos has been an alternate member of our board of directors as a nominee of the Mariani Group since August 15, 2001. He has been the superintendent officer of Pronor since 2001 and a member of the board of directors of Pronor since 2002. Mr. Santos served as chief financial officer of Nitrocarbono from 1996 through 2002. Mr. Santos holds a bachelor s degree in economics from the Pontifícia Universidade Católica do Rio de Janeiro and a post graduate degree in finance from Ibemec Instituto Brasileiro de Mercado de Capitais.

*Edmundo Jose Correia Aires*. Mr. Aires has been an alternate member of our board of directors as a nominee of Petroquisa since August 15, 2001. He has been the partnership manager of Petroquisa since 2001. Previously, Mr. Aires occupied several executive positions with Petroquisa and Petrobras beginning in 1980. Mr. Aires holds a bachelor s degree in chemical engineering from the Universidade Federal do Rio de Janeiro.

*Rogério Gonçalves Mattos*. Mr. Mattos has been an alternate member of our board of directors as a nominee of Petroquisa since September 29, 2002. Mr. Mattos has occupied several executive positions with Petrobras since 1979. He has been the manager of business development for Petrobras since 1998 and a member of the fiscal council of the pension fund of Petrobras (PETROS Fundacão Petrobras de Seguridade Social), or PETROS, since 2003. He holds a bachelor s degree in chemical engineering from the Universidade Federal do Rio de Janeiro and a bachelor s degree in economics from the Universidade Estadual do Rio de Janeiro. Mr. Mattos also attended a senior executive program at the Harvard Business School.

*Rubio Fernal Ferreira e Sousa*. Mr. Ferreira e Sousa has been an alternate member of our board of directors as a nominee of Odebrecht since April 7, 2006. He has been a business development manager of Odebrecht since 1989. Mr. Ferreira e Sousa holds a bachelor s degree of engineering from Universidade Federal de Minas Gerais.

*Yukihiro Funamoto*. Mr. Funamoto has been an alternate member of our board of directors since April 7, 2006. He has been an executive officer of Sojitz do Brasil S.A. since June 2004. From September 2000 until June 2004, he worked in the energy and chemical project department of the investment group of Nissho Iwai Corporation. Mr. Funamoto began working for Nissho Iwai Corporation in April 1997. Mr. Funamoto holds a bachelor s degree of social sciences from Rikkyo University, Tokyo. Mr. Funamoto s business address is Avenida Paulista 1842 Torre Norte 21o andar, CEP: 01310-200 São Paulo-SP.

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**Board of Executive Officers of Braskem**

Our board of executive officers is our executive management body. Our executive officers are our legal representatives and are responsible for our internal organization and day-to-day operations and the implementation of the general policies and guidelines established from time to time by our board of directors.

Our by-laws require that the board of executive officers consist of a chief executive officer and between three and nine additional members, each responsible for business areas that our board of directors assigns to them. The members of our board of executive officers, other than our chief executive officer, have no formal titles (other than the title of executive officer or *director* ) but have the informal titles set forth in the table below.

The members of our board of executive officers are elected by our board of directors for two-year terms, corresponding to the terms of the members of our board of directors, and are eligible for reelection. The current term of all of our executive officers ends at our annual shareholders meeting in 2008. Our board of directors may remove any executive officer from office at any time with or without cause. According to the Brazilian Corporation Law, executive officers must be residents of Brazil but need not be shareholders of our company. Our board of executive officers holds meetings when called by our chief executive officer.

The following table lists the current members of our board of executive officers:

| Name | Year of appointment | Position held | Age |
|---|---|---|---|
| José Carlos Grubisich Filho | 2002 | Chief Executive Officer | 49 |
| Paul Elie Altit | 2002 | Vice President Executive Officer, Chief Financial Officer and Director of Investor Relations | 48 |
| Bernardo Afonso de Almeida Gradin | 2002 | Vice President Executive Officer | 41 |
| Luiz de Mendonça | 2002 | Vice President Executive Officer | 43 |
| Mauricio Roberto de Carvalho Ferro | 2002 | Vice President Executive Officer and General Counsel | 40 |
| Roberto Prisco Paraíso Ramos | 2002 | Vice President Executive Officer | 59 |
| Roberto Lopes Pontes Simões | 2004 | Vice President Executive Officer | 49 |

Summarized below is information regarding the business experience, areas of expertise and principal outside business interests of our current executive officers. The business address of each of our current executive officers is Avenida Nações Unidas, 4777, São Paulo, SP CEP 05477-000, Brazil.

*José Carlos Grubisich Filho.* Mr. Grubisich is currently our chief executive officer. He is also currently the president of the board of directors of Copesul. He was the chief executive officer of OPP Química and the president of the board of directors of OPP Química. From 2000 to 2001, Mr. Grubisich served as vice president of Rhodia Fine Organics worldwide and was a member of the executive committee of the Rhône Poulenc Group. Prior to 2000, he served as vice president of Rhodia S.A. (currently known as Rhodia Brasil Ltda., a member of the Rhône Poulenc Group) for Brazil and Latin America. Mr. Grubisich holds a bachelor s degree in chemical engineering from Escola Superior de Química Oswaldo Cruz and completed an Advanced Management Program at INSEAD France.

*Paul Elie Altit.* Mr. Altit is currently one of our vice president executive officers, our chief financial officer and director of investor relations. He is also a member of the board of directors of Copesul and a member of the board of directors of Politeno, and was a member of the board of directors of Polialden and the investor

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relations officer of Polialden until our merger with Polialden on May 31, 2006. Mr. Altit has also served in several executive positions at Construtora Norberto Odebrecht S.A., most recently as the chief financial officer and investor relations officer of Construtora Norberto Odebrecht S.A. from 1993 through 2002. He also served as assistant vice president of Odebrecht S.A. from 1989 to 1992. Mr. Altit holds a bachelor s degree in engineering from the Universidade Federal do Rio de Janeiro and a post-graduate degree in finance from the Pontifícia Universidade Católica do Rio de Janeiro.

*Bernardo Afonso de Almeida Gradin.* Mr. Gradin is currently one of our vice president executive officers and head of our Basic Petrochemicals Unit. He is also a member of the board of directors of Cetrel. Mr. Gradin was a member of the board of directors of OPP Química and Trikem and an executive officer of Trikem. Mr. Gradin holds a bachelor s degree in civil engineering from the Universidade Federal da Bahia, a master s degree in international politics from the University of Pennsylvania and an MBA degree from The Wharton School of Business.

*Luiz de Mendonça.* Mr. Mendonça is currently one of our vice president executive officers and head of our Polyolefins Unit. He was also an executive officer (Superintendent) of Polialden, a member of the board of directors of Polialden and an alternate member of the board of directors of Politeno until our merger with Polialden on May 31, 2006. Mr. Mendonça also worked for 15 years at Rhodia S.A., where he served as general manager of production, supply and finance and marketing, as an officer in the chemical division (Latin America) and as vice president of Rhodia U.S.A. Mr. Mendonça holds a bachelor s degree in production engineering from Escola Politécnica da Universidade de São Paulo and an MBA degree from INSEAD France.

*Mauricio Roberto de Carvalho Ferro.* Mr. Ferro is currently our vice president executive officer and general counsel, the vice president of the board of directors of Politeno and an alternate member of the board of directors of Petroflex. He was also a member of the board of directors of Polialden until our merger with Polialden on May 31, 2006. He served as a lawyer at the law firm of Carlos Eduardo Paladini Cardoso in 1989 and as a lawyer at the law firm of Bulhões Pedreira, Bulhões Carvalho e Advogados Associados from 1991 until 1995. Mr. Ferro holds a law degree from the Pontifícia Universidade Católica do Rio de Janeiro and an LL. M. degree from the University of London and from the London School of Economics.

*Roberto Prisco Paraíso Ramos.* Mr. Ramos is currently one of our vice president executive officers and head of business competitiveness. He is a member of the board of directors of Cetrel and Companhia Alagoas Industrial-Cinal, and the vice president of the board of directors of Petroflex. Mr. Ramos was a member of the board of directors of Trikem and served on the board of directors of several companies in the Odebrecht Group. Mr. Ramos holds a bachelor s degree in mechanical engineering from the Universidade Federal do Rio de Janeiro, a post-graduate degree in the Program for Management Development from Harvard Business School and a master s degree in finance from the University of Leicester, England.

*Roberto Lopes Pontes Simões.* Mr. Simões is currently one of our vice president executive officers and head of our Vinyls Unit. He was the president of IG Internet Group from 2002 to 2004, where he had served as the chief operational officer since 2000. He also was the president of Opportrans Concessão Metroviária Metrô Rio from 1999 to 2000 and an executive officer of Odebrecht Engenharia e Construções from 1994 to 1999. Mr. Simões holds a bachelor s degree in mechanical engineering from the Universidade Federal da Bahia and in maintenance engineering from CEMANT (a program developed by the Universidade Federal da Bahia and Petrobras/Petroquisa).

**Fiscal Council**

The Brazilian Corporation Law requires us to establish a permanent or non-permanent fiscal council *(conselho fiscal).* Our by-laws provide for a permanent fiscal council composed of five members and their respective alternate members. The fiscal council is a separate corporate body independent of our management and our external independent registered public accounting firm. The primary responsibility of the fiscal council is to review our management s activities and our financial statements and to report their findings to our shareholders.

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The members of our fiscal council are elected by our shareholders at the annual general shareholders meeting for one-year terms and are eligible for reelection. The terms of the members of our fiscal council expire at the next annual general shareholders meeting. Under the Brazilian Corporation Law, the fiscal council may not contain members who are members of our board of directors or our board of executive officers or are employees or spouses or relatives of any member of our management. To be eligible to serve on our fiscal council, a person must be a resident of Brazil and either be a university graduate or have been a company officer or fiscal council member of another Brazilian company for at least three years prior to election to our fiscal council.

Holders of preferred shares without voting rights and non-controlling common shareholders that together hold at least 10.0% of our voting share capital are each entitled to elect one member and his or her respective alternate to the fiscal council.

The following table lists the current members of our fiscal council and their alternates:

| Name | First year of appointment |
|---|---|
| Ismael Campos de Abreu | 2003 |
| Anna Cecília de M.C. Dutra da Silva (alternate) | 2003 |
| Manoel Mota Fonseca | 2002 |
| Maria Cláudia Freitas Sampaio (alternate) | 2002 |
| Walter Murilo Melo de Andrade | 2002 |
| Marcelo André Lajchter (alternate) | 2002 |
| Janildo Dantas de Souza | 2006 |
| José Easton Matos Neto (alternate) | 2006 |
| Marcos Antonio Silva Menezes | 2005 |
| Sergio José de Barros (alternate) | 2005 |

The following is a summary of the business experience, areas of expertise and principal outside business interests of the current members of our fiscal council and their alternates.

***Members of Fiscal Council***

*Ismael Campos de Abreu.* Mr. Abreu has been a member of our fiscal council as a nominee of Norquisa, Odebrecht and ODBPAR since 2003. Mr. Abreu has been the controller of Odebrecht since 1995, and previously served as manager of the tax consulting division of PricewaterhouseCoopers Auditores Independentes from 1978 to 1985, controller of Corrêa Ribeiro S.A. Comércio e Indústria from 1986 to 1988, manager of the consulting area of Arthur Andersen from 1989 to 1991, and a partner of Performance Auditoria e Consultoria from 1992 to 1995. He is currently a member of the fiscal council of Petroflex and was a member of the fiscal council of Polialden until our merger with Polialden on May 31, 2006. Mr. Abreu holds a bachelor s degree in accounting from Fundação Visconde de Cairú, and a post-graduate degree in economic engineering from Centro Interamericano de Desenvolvimento. Mr. Abreu s business address is Av. Luis Viana Filho, 2841, Salvador, BA CEP 41730-900, Brazil.

*Manoel Mota Fonseca.* Mr. Fonseca has been a member of our fiscal council as a nominee of Norquisa, Odebrecht and ODBPAR since 2002 and has served as president of our fiscal council since 2003. Mr. Fonseca has been a partner of the law firm Mota Fonseca e Advogados since

1990 and previously served as legal and tax counsel of Coopers & Lybrand, KPMG and PricewaterhouseCoopers Auditores Independentes.
Mr. Fonseca holds a law degree from the Universidade de São Paulo, and a post-graduate degree in tax law from Fundação Getúlio Vargas.
Mr. Fonseca s business address is Rua Frederico Simões, 85 Edifício Empresarial Simonsen, Sala 304 3° andar, Salvador, BA CEP 41820-020, Brazil.

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*Walter Murilo Melo de Andrade.* Mr. Andrade has been a member of our fiscal council as a nominee of Norquisa, Odebrecht and ODBPAR since 2002. Mr. Andrade has been a legal counsel of Engepack Embalagens S.A. , or Engepack, since 2002. Previously, he served as legal counsel of Nitrocarbono, Pronor and Proppet from 1998 to 2002. Mr. Andrade holds a law degree from the Universidade Católica de Salvador, with a specialization in civil law from Fundação Faculdade de Direito da Bahia and in corporate law from Escola de Magistratura do Estado do Rio de Janeiro. Mr. Andrade s business address is Quadra 03 do Sesfi, Cia. Sul, Simões Filho, BA CEP 42780-000, Brazil.

*Janildo Dantas de Souza.* Mr. Souza has been a member of our fiscal council as a nominee of PETROS, *Caixa de Previdência dos Funcionários do Banco do Brasil* PREVI, or PREVI, and Petroquisa since April 7, 2006. Mr. Souza has been a partner with Souza Mafra Consultoria since March 2001, president of the Union of Retail Optical Materials in the State of Rio Grande do Norte since October 2003 and president of the Assistance, Consulting and Support to Corporate Management Cooperative in the State of Rio Grande do Norte since April 1999. He is also director of the Commercial Federation of the State of Rio Grande do Norte and of the Retail Commerce Union of Rio Grande do Norte and serves as a member of the fiscal council of COSERN Companhia Energetica do Rio Grande do Norte. Mr. Souza holds a bachelor s degree in accounting from the Universidade Federal do Rio Grande do Norte. Mr. Souza s business address is Av. Senador Salgado Filho, 2190, Sala 130, Lagoa Nova, Natal, Rio Grande do Norte, 59075-000.

*Marcos Antonio Silva Menezes*. Mr. Menezes was elected a member of our fiscal council in 2005, as a nominee of Petroquisa. Mr. Menezes has been the director of Petrobras International Finance Company PIFCo since 2003 and chief accountant officer of Petrobras since 1998. He joined Petrobras in 1976 and served as Deputy Superintendent of the former Financial Services SEFIN from 1995 through 1998. He served as a member of the fiscal council of Companhia de Gás de Minas Gerais GASMIG from 2003 through 2005, as president of the fiscal council of PETROS and as a member of the fiscal council of Companhia de Gás da Bahia BAHIAGAS. Mr. Menezes has been the chairman of the fiscal council of Instituto Brasileiro de Petróleo e Gás IBP since 1998, and Organização Nacional das Indústras de Petróleo ONIP since 1999. He is also a director of the American Chamber of Commerce AMCHAM/RJ and a member of Associação Nacional dos Executivos de Finanças, Administração e Contabilidade ANEFAC and Associação Brasileira das Companhias Abertas ABRASCA and its Auditing and Accounting Rules Commission CANC. Mr. Menezes holds bachelor s degrees in accounting and in business management from Faculdade Moraes Júnior in Rio de Janeiro, a post-graduate degree in financial management from Fundação Getúlio Vargas, and completed an advanced management program PGA at Fundação Dom Cabral/INSEAD França. Mr. Menezes business address is Av. República do Chile, 65, Rio de Janeiro, RJ, Brazil.

***Alternate Members of Fiscal Council***

*Anna Cecília de M.C. Dutra da Silva.* Ms. Silva has been an alternate member of our fiscal council as a nominee of Norquisa, Odebrecht and ODBPAR since 2003. Ms. Silva has been an associate at the law firm of Barbosa, Müssnich & Aragão Advogados since 2001 and an alternate member of the fiscal council of Pronor since 2002 and of Cimento Tupi S.A. since 2003. She was also a member of the fiscal council of Polialden from 2003 until our merger with Polialden on May 31, 2006. She holds a law degree from the Pontifícia Universidade Católica do Rio de Janeiro. Mr. Silva s business address is Av. Pres. Juscelino Kubitschek, 50 4th Floor, São Paulo, SP CEP 04543-000, Brazil.

*Maria Cláudia Freitas Sampaio.* Ms. Sampaio has been an alternate member of our fiscal council as a nominee of Norquisa, Odebrecht and ODBPAR since 2002. Mrs. Sampaio has been a lawyer at the law firm Mota Fonseca e Advogados since 2001 and a member of the fiscal council of Norquisa since 1991. Previously, she served as an auditor of PricewaterhouseCoopers Auditores Independentes from 1986 to 1991. Ms. Sampaio holds a law degree and a bachelor s degree in business administration from the Universidade Católica de Salvador. Ms. Sampaio s business address is Rua Frederico Simões, 85 -Edifício Empresarial, Simonsen Sala 304 30 andar, Salvador, BA CEP 41820-020, Brazil.

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*Marcelo André Lajchter.* Mr. Lajchter has been an alternate member of our fiscal council as a nominee of Norquisa, Odebrecht and ODBPAR since 2002. Mr. Lajchter has been a partner of the law firm Barbosa, Müssnich & Aragão Advogados since 2000 and a professor at Fundação Getúlio Vargas since 2003. Previously, he served as a lawyer in the tax litigation area of PricewaterhouseCoopers Auditores Independentes from 1993 to 1995. Mr. Lajchter holds a law degree from the Universidade do Estado do Rio de Janeiro. Mr. Lajchter s business address is Av. Pres. Juscelino Kubitschek, 50 4th Floor, 04543-000, São Paulo, SP CEP 04543-000, Brazil.

*José Easton Matos Neto*. Mr. Neto has been an alternate member of our fiscal council as a nominee of PETROS, PREVI and Petroquisa since April 7, 2006. Mr. Neto worked for Banco do Brasil S.A. for 28 years, retiring in November 2004 as a bank manager. Mr. Neto holds a bachelor s degree in accounting from Faculdade de Tecnologia e Ciências de Feira de Santana and an MBA from the Universidade Federal da Bahia UFBA. Mr. Neto s business address is Rua Almirante Carlos Paraguaçu de Sá, 1, Sala 5A7, Pituba, Salvador, Bahia, 41810-660.

*Sergio José de Barros*. Mr. Barros has been an alternate member of our fiscal council as a nominee of Petroquisa since 2005. Mr. Barros has been the accounting manager of international businesses of Petrobrás since 2005, and served as the financial businesses manager of Petrobrás from 2002 through 2005. Prior to 2002, he served in various capacities in the finance and accounting areas of Petrobras since 1993. He has been a member of the fiscal council of Petrobras Gás S.A. GASPETRO. He also served as member of the Fiscal Council of Companhia de Gás do Ceará CEGÁS in 2003 and 2004, Gás de Alagoas ALGÁS in 2005, and Sergipe Gás SERGÁS in 2005. He also served as a supervisor at KPMG Peat Marwick Auditores Independentes and at Boucinhas, Campos e Claro Auditores Independentes. Mr. Barros holds bachelor s degrees in accounting and law, a post-graduate degree in business management from the Universidade Federal do Rio de Janeiro (UFRJ), and an MBA from IBMEC. Mr. Barros s business address is Av. República do Chile, 65, Rio de Janeiro, RJ, Brazil.

**Compensation**

According to our by-laws, our shareholders are responsible for establishing the aggregate compensation we pay to the members of our board of directors, our board of executive officers and our fiscal council. Our shareholders determine this aggregate compensation at the general shareholders meeting each year. Once aggregate compensation is established, the members of the board of directors are responsible for distributing such aggregate compensation individually to the members of our board of directors, our board of executive officers and our fiscal council in compliance with our bylaws. Our board of directors does not have a compensation committee.

***Compensation and Benefits***

The aggregate compensation paid by us to all members of our board of directors, board of executive officers and our fiscal council for services in all capacities was R$12.8 million in 2005. On April 7, 2006, our shareholders (acting in the annual general meeting) established the following compensation for the year 2006:

- board of directors: an aggregate limit of R$1.4 million;

- board of executive officers: a total amount of R$16.8 million; and fiscal council: the greater of (1) 10% of the average monthly compensation of the members of our board of executive officers to each regular member of our fiscal council, plus travel and lodging expenses (the statutory minimum set forth in the Brazilian Corporation Law and in our by-laws) and (2) R$4,433 per month.

We compensate our alternate directors for each meeting of our board of directors that they attend. We compensate alternate members of our fiscal council for each meeting of our fiscal council that they attend.

Our executive officers receive the same benefits generally provided to our employees, such as medical (including dental) assistance, private pension plan and meal vouchers. Like our employees, our executive officers also receive a yearly bonus equal to one-month s salary (known as the thirteenth (monthly) salary in Brazil), an additional one-third of one-month s salary for vacation, and contributions of 8.0% of their salary into a defined contribution pension fund known as the Guarantee Fund for Time of Service *(Fundo de Garantia por Tempo de Serviço).* Members of our board of directors and fiscal council are not entitled to these benefits. We made contributions into the Guarantee Fund for Time of Service for our executive officers in an aggregate amount of R$0.6 million during the year ended December 31, 2005.

Members of our board of directors, board of executive officers and fiscal council are not parties to contracts providing for benefits upon the termination of employment other than, in the case of executive officers, the benefits described above.

***Long-Term Incentive Plan***

On September 26, 2005, we adopted a long-term incentive plan. Under the terms of this plan, we may issue investment units, each of which has an economic value equivalent to the economic value of one class A preferred share of our company, to our executive officers, senior management and other employees involved in our strategic programs, which the plan refers to as our business partners. These investment units do not carry any voting rights and may not be transferred. Each year, our Chief Executive Officer will submit an annual program to our board of directors stating:

- the maximum number of investment units to be issued in that year;
- the business partners that will be offered investment units in that year;
- the purchase price of the investment units to be paid by the participating business partners;
- the projected allocation of the investment units among the business partners; and
- as an incentive to purchase investment units, the number of additional investment units that each business partner will receive in connection with the purchase of an investment unit.

Upon the purchase by a business partner of his allocation of investment units, the business partner will receive additional investment units as an incentive for the purchase of the purchased investment units. We refer to the purchased investment units as alpha units and the additional investment units as beta units. Each beta unit will automatically convert into an alpha unit ten years after the date of issue of the beta unit. Upon the payment by our company of dividends or interest attributable to shareholders equity to holders of our class A preferred shares, we will issue additional units, which we refer to as gamma units, with an aggregate value equivalent to the value of the dividends or interest attributable to shareholders equity attributed and paid to the holders of a class A preferred share.

Each year we will determine the unit value of the investment units applicable from April 1 of that year until March 31 of the following year calculated as the average closing price in *reais* of our class A preferred shares on the São Paulo Stock Exchange from October 1 of the preceding year through March 31 of the year in which the unit price is established. Following the fifth anniversary of the date on which any business partner first acquires investment units, we will redeem up to 20% of the investment units held by that business partner at the then-established unit price upon the request of that business partner made within 120 days following the delivery of an annual statement from us with respect to the investment units held by that business partner. After the first redemption, we will redeem up to 10% per year of the investment units held by that business partner at the then-established unit price upon the request of that business partner made in subsequent years. We will redeem any gamma unit at the then-established unit price upon the request of the holder made within 60 days following the issuance of that gamma unit. Any gamma unit not so redeemed will automatically convert into an alpha unit.

In the event that a business partner is dismissed without just cause or retires, we will redeem all of the investment units held by that business partner at the then-established unit price upon the request of that business partner. In the event that a business partner is dismissed for just cause or resigns, all of the beta units held by that

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business partner will be immediately extinguished, and we will redeem all of the alpha units held by that business partner at the then-established unit price upon the request of that business partner. Upon the death of a business partner, we will automatically redeem all of the investment units held by that business partner (for the benefit of the business partner s estate) at the then-established unit price.

Our board of directors has adopted an annual program for the 2005 fiscal year. Under this annual plan, certain executive officers are entitled to purchase up to an aggregate of 135,500 investment units and to receive up to an additional 135,500 investment units.

**Corporate Governance Practices**

The significant differences between our corporate governance practices and the New York Stock Exchange standards can be found on our website, *www.braskem.com.br*. The information found at this website is not incorporated by reference into this annual report.

**Employees**

The following table sets forth the number of our employees by main category of activity and location.

| | At December 31, | | |
|---|---|---|---|
| **Main category of activity** | **2005(1)** | **2004(2)** | **2003(3)** |
| Coordinators and operators | 1,589 | 1,563 | 1,494 |
| Engineers and other professionals | 695 | 521 | 491 |
| Administrative and support | 254 | 272 | 273 |
| Technicians | 283 | 226 | 223 |
| Maintenance | 243 | 224 | 206 |
| Managers and directors | 198 | 190 | 181 |
| Total | 3,262 | 2,996 | 2,868 |

(1) At December 31, 2005, 1,982 employees worked in the State of Bahia, 427 employees worked in the State of Alagoas, 415 employees worked in the State of Rio Grande do Sul, 413 employees worked in the State of São Paulo and 25 employees worked in other states in Brazil.

(2) At December 31, 2004, 1,818 employees worked in the State of Bahia, 397 employees worked in the State of Alagoas, 400 employees worked in the State of Rio Grande do Sul, 356 employees worked in the State of São Paulo and 25 employees worked in other states in Brazil.

(3) At December 31, 2003, 1,754 employees worked in the State of Bahia, 377 employees worked in the State of Alagoas, 372 employees worked in the State of Rio Grande do Sul, 341 employees worked in the State of São Paulo and 24 employees worked in other states in Brazil.

We do not employ a material number of temporary employees.

In Brazil, both employees and employers have the right to organize unions. Employees belonging to a specific professional category and employers constituting a specific economic category may each be represented by a single union in a particular geographic area. Individual unions generally belong to state-wide union federations, which in turn belong to nationwide union confederations. We are a member of the Petrochemicals and Synthetic Resins Industries Union of the States of Bahia, Alagoas and Rio Grande do Sul, and our employees belong to the Petrochemicals Industries Workers Unions in each of these states.

Approximately 33% of our non-management employees were union members at December 31, 2005. We believe that we have good ongoing relations with our employees and their unions. We have not experienced a strike since OPP Química was privatized in 1992 and Trikem was privatized in 1995. The current collective bargaining agreements with our unions have one-year terms and are subject to annual renegotiation. We have traditionally applied the terms of bargaining agreements entered into with the unions equally to unionized and non-unionized employees.

Since coming under the control of the Odebrecht Group, we have adopted and applied the personnel management philosophy of the Odebrecht Group, which emphasizes a performance-related pay structure and a decentralized management structure. Employees in each of our business units participate in setting and achieving their business unit s annual objectives. As a result, employees in those business units that meet or exceed their goals share in our financial performance through performance-based employee compensation plans. During 2005, we recorded an expense of R$91.1 million related to this program with respect to 2,971 employees. We paid an additional R$8.4 million to our executive officers under this program during 2005. The members of our board of directors do not participate in this program.

We seek to recruit top graduates from Brazilian technical schools and universities to work at each of our plants and offer career development training to employees to develop skills necessary to operate an internationally competitive, vertically integrated petrochemical company. We have invested in a series of training courses for our operating, laboratory and maintenance personnel through agreements with technical training organizations. During 2005, our total investment in education and training amounted to R$8.7 million for 317,730 hours of training, representing an average of 100 hours per employee.

We tailor career development programs to each employee s individual needs and abilities. We established this program with our own resources and technology, and it has become a Brazilian benchmark in human resources practices. In 2005, 51.3% of our employees received salary increases as a result of their participation in our career development programs.

Our employees and their dependents receive medical and dental assistance through a network of accredited doctors. We pay most of the costs for these services, with a small portion being paid by our employees. A small monthly fee is also charged to our employees to pay for more costly medical services. In 2005, we spent R$15.6 million on this assistance.

We pay part of the monthly payments made by our employees to three private pension funds: Odebrecht Pension Plan *(ODEPREV Odebrecht Previdência)*; PETROS and Previnor Pension Plan *(PREVINOR Associação de Previdência Privada)*. The majority of our employees participate in these pension funds. These pension funds pay supplementary pension and retirement amounts similar in amount to those paid by the Brazilian government s pension system and are intended to provide their members with income on retirement. In 2005, we paid R$12.0 million into these funds. The Odebrecht Pension Plan and the Previnor Pension Plan are defined contribution plans. The PETROS plan is a defined benefit plan. The present value of our obligations under the PETROS plan exceeded the value of the assets of that fund by R$58.6 million at December 31, 2005. See note 28 to our consolidated financial statements. In June 2005, we announced that we intend to withdraw as a sponsor of the Previnor Pension Plan and the PETROS plan.

**Share Ownership of Directors and Officers**

The total number of shares owned by members of Braskem s Board of Directors and Executive Officers as of June 22, 2006 represents less than 1% of Braskem s capital stock. Under our by-laws, each of our directors must also be a shareholder of our company. Accordingly, if a person is appointed to our board of directors and is not one of our shareholders at the time, the shareholder that designated such person to be one of our directors (in accordance with the terms of the relevant shareholders agreement) generally transfers one share to the newly appointed director at no cost. All other shares owned by our directors were purchased at market prices through the São Paulo Stock Exchange. As of the date hereof, none of our executive officers owns any of our shares.

**ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS**

**Major Shareholders**

At June 22, 2006, we had 123,492,142 outstanding common shares, 246,107,138 outstanding class A preferred shares and 803,066 outstanding class B preferred shares.

We have registered one class of ADSs, with the United States Securities and Exchange Commission, or the Commission, pursuant to the Securities Act. Each ADS is evidenced by American Depositary Receipts, or ADRs, representing two of our class A preferred shares. At June 22, 2006, we had approximately 18,333 shareholders, including one U.S. resident holder of our common shares, approximately 117 U.S. resident holders of our class A preferred shares (including The Bank of New York, as depositary) and no U.S. resident holders of our class B preferred shares.

The following table sets forth information concerning the ownership of our common shares and preferred shares at June 22, 2006, by each person whom we know to be the owner of more than 5.0% of our common shares and our class A preferred shares, and by all of our directors and executive officers as a group. Our principal shareholders have the same voting rights with respect to each class of our shares that they own as other holders of shares of that class.

| | Common Shares | | Class A Preferred Shares | | Class B Preferred Shares(1) | | Total | |
|---|---|---|---|---|---|---|---|---|
| | Number of Shares | % | Number of shares | % | Number of Shares | % | Number of shares | % |
| Odebrecht Group(2) | 92,153,272 | 74.6 | 53,763,411 | 21.8 | | | 145,916,683 | 39.4 |
| Petroquisa | 12,110,937 | 9.8 | 18,522,258 | 7.5 | | | 30,633,195 | 8.3 |
| BNDESPAR(3) | | | 13,649,731 | 5.5 | | | 13,649,731 | 3.7 |
| Alliance Capital Management L.P. (4) | | | 12,191,991 | 5.0 | | | 12,191,991 | 3.3 |
| Marcos Juliano Lucas Carvalho | 80 | * | 5,086 | * | 260,368 | 32.4 | 265,534 | * |
| Liane Maria Wolf | | | 15,900 | * | 54,400 | 6.8 | 70,300 | * |
| Beatriz Maria Wolf | | | | | 54,400 | 6.8 | 54,400 | * |
| Vera Maria Wolf | | | | | 50,700 | 6.8 | 50,700 | * |
| All directors, fiscal council members, their alternates and executive officers as a group (39 persons) | 7 | * | 74,998 | * | | | 74,998 | * |

* less than 1%

(1) Our Class B preferred shares may be converted at any time at the request of the holder into class A preferred shares at the ratio of two class B shares per class A share.

(2) Represents direct ownership of 26,781,079 common shares owned by Odebrecht, 33,939,508 common shares owned by ODBPAR Investments (a subsidiary of Odebrecht), 30,852,354 common shares owned by Norquisa (a subsidiary of Odebrecht and ODBPAR Investments), 580,331 common shares owned by Braskem Participações S.A., 49,101,180 class A preferred shares owned by Odebrecht, 2,207,091 class A preferred shares owned by Norquisa, 2,164,975 class A preferred shares owned by Politeno and 290,165 class A preferred shares owned by Braskem Participações S.A. The Odebrecht Group disclaims ownership of our shares owned by Norquisa other than with respect to its proportionate interest in these shares. Odebrecht also owns convertible debentures issued originally by OPP Produtos. These debentures may be converted into our shares at any time, at the discretion of the Odebrecht Group. If such right had been

exercised at May 31, 2006, 24,718,773 new common shares and 49,437,545 new class A preferred shares of our company would have been issued. These shares have not been included in the above table.

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(3) BNDESPAR is the lender under a loan agreement with our company which provides that BNDESPAR has the option to convert the principal amount of and accrued interest on this loan into our class A preferred shares at any time prior to the maturity of this loan. If this option had been exercised at May 31, 2006, BNDESPAR would have been entitled to receive 11,864,558 new class A preferred shares of our company. These shares have not been included in the above table. See Item 5. Operating and Financial Review and Prospects Liquidity and Capital Resources Indebtedness and Financing Strategy.

(4) Based on filing of Alliance Capital Management L.P with the São Paulo Stock Exchange on February 4, 2005 pursuant to CVM Instruction 358.

We currently have no management or employee option plans or management or employee options outstanding. See Item 6. Directors, Senior Management, and Employees Compensation Long-Term Incentive Plan.

***Changes in Ownership***

At January 1, 2005:

- Norquisa owned 9.1% of our total share capital, including 25.4% of our voting share capital;
- the Odebrecht Group owned 42.9% of Norquisa s total share capital, including 50.1% of its voting share capital;
- the Odebrecht Group including Norquisa, owned 41.9% of our total share capital, including 72.9% of our voting share capital; and
- Petroquisa owned 8.5% of our total share capital, including 10.0% of our voting share capital.

During 2005, some of the shareholders of our class B preferred shares exercised their rights to convert their class B preferred shares into class A preferred shares. As a result of these conversions, we issued 4,938,742 class A preferred shares in exchange for 9,877,484 class B preferred shares.

On March 22, 2005, Odebrecht transferred 2,784,799 class A preferred shares to BNDESPAR in exchange for non-voting shares of Norquisa representing 10.06% of the total share capital of Norquisa.

On April 28, 2005, Odebrecht transferred 2,044,990 class A preferred shares to EDN Distribuidora do Nordeste S.A. in exchange for shares of Norquisa representing 11.1% of the total share capital, including 12.5% of the voting share capital, of Norquisa.

On April 3, 2006, Odebrecht transferred 2,164,975 class A preferred shares to Politeno and 2,129,324 class A preferred shares to another shareholder of Norquisa in exchange for shares of Norquisa representing an aggregate of 22.0% of the total share capital, including 21.4% of the voting share capital, of Norquisa.

On May 31, 2006, we issued 7,878,825 of our class A preferred shares to the shareholders of Polialden, other than our company, in exchange for their share capital of Polialden. In addition, at an extraordinary general shareholders meeting held on May 31, 2006, Odebrecht and Norquisa converted 2,518,822 and 113,221 of their class A preferred shares, respectively, into the same number of common shares.

As a result of these transactions, at June 22, 2006.

- Norquisa owned 8.9% of our total share capital, including 25.0% of our voting share capital;

- the Odebrecht Group owned 86.1% of Norquisa s total share capital, including 83.9% of its voting share capital;

- the Odebrecht Group, including Norquisa, owned 39.4% of our total share capital, including 74.6% of our voting share capital; and

- Petroquisa owned 8.3% of our total share capital, including 9.8% of our voting share capital.

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***Shareholders Agreements***

*Petroquisa Memorandum of Understanding*

On July 3, 2001, Odebrecht, Odebrecht Química, Petroquisa and Petroquímica da Bahia S.A., or Petroquímica da Bahia entered into a Memorandum of Understanding regarding Shareholders Agreement, which was amended with respect to Odebrecht and Petroquisa, with Petroquímica da Bahia and Norquisa as consenting parties, on July 26, 2002. On April 29, 2005, Odebrecht, Petroquisa, ODBPAR and Norquisa entered into a further amendment to the Memorandum of Understanding regarding Shareholders Agreement, with Petrobras and our company as consenting parties, which revoked the initial amendment, and which, together with the Memorandum of Understanding regarding Shareholders Agreement, we refer to as the Petroquisa memorandum of understanding. The Petroquisa memorandum of understanding grants Petroquisa (1) an option to purchase additional shares from our company and from Odebrecht, ODBPAR and Norquisa, (2) the right to designate two members of our board of directors and their alternates, (3) veto rights over certain actions by the shareholders and the board of directors, and (4) tag-along rights. The Petroquisa memorandum of understanding also grants Petroquisa a right to include a right of first refusal in respect of our common or preferred shares in the final shareholders agreement. The Petroquisa memorandum of understanding terminates on July 25, 2021, unless a shareholders agreement including the terms set forth below is entered into prior to that date.

Under the Petroquisa memorandum of understanding, Odebrecht, ODBPAR and Norquisa granted to Petroquisa an option to purchase such number of our common shares as may be necessary for Petroquisa to own up to 30% of our voting share capital, which we refer to as the Petroquisa option. Under the Petroquisa memorandum of understanding, Petroquisa had the right to exercise the Petroquisa option in full on a single occasion on or prior to December 31, 2005. On September 29, 2005, we agreed with the other parties to the Petroquisa memorandum of understanding to extend the expiration of the Petroquisa option until March 31, 2006. On March 31, 2006, the Petroquisa option expired without being exercised.

Under the Petroquisa memorandum of understanding, Petroquisa has veto rights over the following matters at any general meeting of our shareholders:

- any modification of the rights conferred on our shares by our by-laws if that modification would adversely affect the value of our shares;
- any change, increase or reduction of the scope of our corporate purpose, except as necessary for us to operate as an integrated petrochemical company;
- any increase in the number of members of our board of directors;
- any decrease in the number of members of our board of directors to be nominated by Petroquisa;
- any capital increase by us paid in by tendering goods or rights, unless those goods or rights relate to our corporate purpose and a valuation of those goods or rights is performed by a first tier investment bank or independent auditing firm;
- any merger or spin-off of our company into another company or of another company into our company that could result in the unjustified dilution of the percentage ownership of Petroquisa except that the integration of the second generation petrochemical

producers controlled by the Odebrecht Group is expressly permitted; and

our dissolution or liquidation.

Under the Petroquisa memorandum of understanding, Petroquisa has veto rights over resolutions of our board of directors relating to the following matters:

acquisitions, sales or granting of liens against our fixed assets with values in excess of 30.0% of our net worth, if such acquisition, sale or grant of a lien is not related to, or is outside the scope of, our corporate purpose;

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transactions involving affiliates of the parties to the Petroquisa memorandum of understanding, other than transactions involving the integration of the second generation petrochemical producers controlled by the Odebrecht Group or the Mariani Group;

investments in other companies, unless they are in the same business as our company; and

any resolution that would cause us to fail to meet any of the following financial ratios, with any projections to determine compliance with this provision to be performed by an internationally recognized entity:

projected net debt to EBITDA;

EBITDA to interest expense; and

EBITDA to debt service (excluding trade finance).

Although the Petroquisa memorandum of understanding does not provide a definition of EBITDA, we calculate EBITDA for purposes of this agreement on the same basis as set forth in the most restrictive financial covenants in our debt instruments. See Item 5. Operating and Financial Review and Prospects Liquidity and Capital Resources Indebtedness and Financing Strategy. Petroquisa has the right to sell *a pro rata* portion of its shares of our company in connection with any direct or indirect sale of our common shares by the Odebrecht Group to a third party that involves a change of our control.

*Mariani Group Shareholders Agreement*

On July 27, 2001, Odebrecht Química and Petroquímica da Bahia entered into a shareholders agreement with respect to their shares of Norquisa and our company, which was amended on July 29, 2002 pursuant to the First Amendment to Shareholders Agreement among Odebrecht Química, Odebrecht, ODBPAR Investments and Petroquímica da Bahia. We refer to this agreement, as amended, as the Mariani Group Shareholders Agreement.

The Mariani Group Shareholders Agreement provides that:

The Odebrecht Group has the right to nominate a majority of Norquisa s board of directors and a majority of our board of directors;

The Mariani Group has the right to nominate at least one member of Norquisa s board of directors and at least one member of our board of directors;

The Odebrecht Group has the right to nominate all of the members of Norquisa s board of executive officers and our board of executive officers; however, if Norquisa s shareholders eliminate its board of directors (as shareholders of privately held companies, such as Norquisa, are permitted to do under the Brazilian Corporation Law), the Mariani Group will have the right to nominate at least one member of Norquisa s board of executive officers; and

Odebrecht, ODBPAR Investments and Petroquímica da Bahia will exercise their voting rights with respect to our company and Norquisa, and cause their representatives on the boards of directors of our company and Norquisa to vote, to implement the organizational restructuring of our company.

Under the Mariani Group Shareholders Agreement, Odebrecht, ODBPAR Investments and Petroquímica da Bahia will vote their shares as a block in each general shareholders meeting of Norquisa. Odebrecht, ODBPAR Investments and Petroquímica da Bahia will meet prior to each meeting to determine how to vote these shares with respect to matters to be submitted to the meeting. These determinations will be made by majority vote among these shareholders based on the number of Norquisa shares held by each of them. As a result, the Odebrecht Group may effectively determine the vote for all of these shareholders.

Under the Mariani Group Shareholders Agreement, Odebrecht and ODBPAR Investments, on the one hand, and Petroquímica da Bahia, on the other hand, granted to the other a right of first refusal in respect of sales

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transfers or encumbrances of common shares of Norquisa owned directly or indirectly by either of them. If the Odebrecht Group intends to sell any of its shares of Norquisa, Petroquímica da Bahia has the right to sell a *pro rata* portion of its shares of Norquisa on the terms and conditions under which the Odebrecht Group intends to sell its shares. If the Odebrecht Group intends to sell a sufficient number of its shares of Norquisa to result in a change of joint control of Norquisa, Petroquímica da Bahia has the right to sell all of its shares of Norquisa on the same terms and conditions under which the Odebrecht Group intends to sell its shares. If the Odebrecht Group sells or transfers direct or indirect control of our company to a third party, Petroquímica da Bahia also has the right to sell all of its shares of our company on the same terms offered by the third party acquiring control of our company from the Odebrecht Group.

On September 9, 2003, Odebrecht granted to Pronor, a company in the Mariani Group, an option to exchange all its shares of Norquisa, representing 13.8% of Norquisa s total share capital, including 16.1% of its voting share capital, for 1,454,424 of our class A preferred shares, representing 0.4% of our total share capital, owned directly or indirectly by Odebrecht. On December 26, 2003, Pronor exercised its option and is required to complete the exchange of shares between January 30, 2005 and January 30, 2009. As of June 22, 2006, Pronor owned 1.7% of our total share capital, including 2.8% of our voting share capital.

*Pension Funds Memorandum of Understanding*

On July 20, 2001, Odebrecht Química, Petroquímica da Bahia, PETROS and PREVI entered into a Memorandum of Understanding Regarding Shareholders Agreement, which we refer to as the Pension Funds memorandum of understanding. The Pension Funds memorandum of understanding grants certain preemptive and share transfer rights to PETROS and PREVI. The Pension Funds memorandum of understanding has a term of 20 years, unless a shareholders agreement containing the terms set out below is entered into prior to that date. Under the Pension Funds memorandum of understanding, the parties agreed to adopt the following basic principles for our management:

- our board of executive officers will be composed of competent professionals;
- our dividend policy will have as its objective the distribution of at least 50.0% of net income available during the relevant period, provided that all necessary reserves for the efficient operation and development of our business are established and maintained; and
- we will adopt a commercial policy that assures the regular and continuous supply of raw materials and utilities on a competitive basis and consistent with the domestic and international markets.

The Pension Funds memorandum of understanding contains the following liquidity provisions with respect to our shares owned by PETROS and PREVI:

- PETROS and PREVI have the right to sell our shares owned by each of them in connection with any sale of our shares by our controlling shareholders to a third party that involves a change of our control; and
- In order to transfer their veto rights under the Pension Funds memorandum of understanding, PETROS and PREVI must give our controlling shareholders a right of first refusal to purchase our shares owned by each of them in the event of a proposed sale except that our controlling shareholders will not have a right of first refusal if our shares are being sold to another private pension fund or to a company that does not compete with our controlling shareholders.

The Pension Funds memorandum of understanding granted certain voting rights to PETROS and PREVI, including veto rights to PETROS and PREVI over certain actions by our shareholders and our board of directors. These vero rights of PETROS and PREVI were valid so long as on a combined basis they owned, together with other private pension funds, at least 15.0% on August 16, 2002 as a result of our mergers with OPP Produtos and 52114 Participações S.A. The Pension Funds memorandum of understanding provided that these veto rights would remain in effect for three years after the date on which the percentage of voting capital owned by these pension funds fell below 15.0%, during which PETROS and PREVI could purchase more of our shares in order to maintain their veto rights beyond such three-year period. As of August 16, 2005, the percentage of voting capital owned by these pension funds did not equal or exceed 15.0% and, consequently, these veto rights expired.

*BNDESPAR Shareholders Agreement*

We, Odebrecht and BNDESPAR have entered into a shareholders agreement. This shareholders agreement provides that if BNDESPAR s ownership of our total share capital exceeds 5.0% on or prior to July 31, 2007, BNDESPAR will have the right to appoint one member of our board of directors. Until the earlier of the date on which BNDESPAR appoints a member of our board of directors and July 31, 2007, a representative of BNDESPAR may attend meetings of our board of directors, but is not allowed to participate or to vote in such meetings. If BNDESPAR s ownership of our total share capital exceeds 5.0% on or prior to July 31, 2007, this shareholders agreement will expire on the earlier of any date thereafter on which BNDESPAR ceases to own more than 5.0% of our total share capital, and August 24, 2011. This shareholders agreement also provides that BNDESPAR has the right to (1) require our company and Odebrecht to purchase the shares that it owns in our company if we do not comply with the terms of the shareholders agreement and do not cure any such non- compliance within a specified period, and (2) sell its shares in the event that Odebrecht sells its voting control of our company to a third party.

**Related Party Transactions**

The following summarizes the material transactions that we have engaged in with our principal shareholders and their affiliates since January 1, 2005.

We and our subsidiaries have engaged in extensive transactions with our principal shareholders and their affiliates and expect to do so in the future. We also have commercial relationships with some of our affiliates and, as a result, record trade accounts receivable and current and long-term liabilities mainly from purchases and sales of goods and services at prices and on terms equivalent to the average terms and prices of transactions that we enter into with third parties. In addition, we have entered into financial and other transactions with our principal shareholders and their affiliates, including, among others, as obligor on R$999.3 million, at December 31, 2005, of convertible subordinated debentures held by the Odebrecht Group and as a party to four shareholder s agreements or memoranda of understandings with shareholders of our company.

Under the Brazilian Corporation Law, each of our directors, their alternates and our executive officers cannot vote on any matter in which they have a conflict of interest and such transactions can only be approved on reasonable and fair terms and conditions that are no more favorable than the terms and conditions prevailing in the market or offered by third parties. However, if one of our directors is absent from a meeting of our board of directors, that director s alternate may vote even if that director has a conflict of interest, unless the alternate director shares that conflict of interest or has another conflict of interest.

***The Odebrecht Group***

On May 31, 2002, OPP Produtos issued subordinated convertible debentures to Odebrecht. These debentures became our obligations as a result of the merger of OPP Produtos into our company on August 16, 2002. Odebrecht has the option to convert these debentures into shares of our share capital at any time. See Item 5. Operating and Financial Review and Prospects Liquidity and Capital Resources Indebtedness and Financing

Strategy.

On December 4, 2004, we entered into an Alliance Agreement with CNO, under which we have appointed CNO as a non-exclusive preferred provider with respect to maintenance services and efficiency enhancement projects at each of our plants. This agreement was unanimously approved by our board of directors. Under this agreement, we are required to request bids from CNO for these services and projects. If CNO is retained for any specific service or project, we will pay CNO its costs related to the service or project plus 15%. In addition, we are required to pay any applicable taxes with respect to such fees. This agreement expires in December 2008. We purchased services under this agreement from CNO of R$109.5 million in 2005. We had accounts payable to CNO of R$12.3 million at December 31, 2005.

***Petrobras***

Petrobras is the controlling shareholder of Petroquisa, which owns 8.3% of our total share capital, including 9.8% of our voting share capital. We purchase naphtha from Petrobras, and we sell automotive gasoline and LPG to Petrobras Distribuidora S.A., a wholly-owned subsidiary of Petrobras.

On June 22, 1978, we entered into a 10-year renewable contract with Petrobras under which the prices paid by us to Petrobras for naphtha are established based on the Amsterdam-Rotterdam-Antwerp market price and are linked to fluctuations in the *real*/U.S. dollar exchange rate. This contract was amended and renewed in February 1993 and in February 2003.

We maintain a rotating naphtha supply line of credit with Petrobras that permits us to finance purchases of naphtha from Petrobras. We are permitted to maintain balances up to an aggregate of R$570.0 million under this line of credit. We pay interest on the outstanding balance under this line of credit at the monthly rate of 1.78%.

We purchased raw materials and utilities from Petrobras and Petrobras Distribuidora S.A. of R$5,311.4 million in 2005. We had accounts payable to Petrobras and Petrobras Distribuidora S.A. of R$103.1 million at December 31, 2005.

On February 21, 2005, we purchased (1) 15,390,139 common shares, 379,955 class B preferred shares and 7,695,071 class C preferred shares, representing 13.74% of the total share capital of Companhia Alagoas Industrial-Cinal, including 16.6% of its voting share capital, and (2) 1,669,518,451 quotas, representing 25% of the total capital of Alclor Química de Alagoas Ltda., from Petroquisa for R$7.7 million.

Petrobras subsidiary, Petroquisa, is a party to the Petroquisa memorandum of understanding with Odebrecht and Petroquímica da Bahia. This agreement grants certain voting and other rights in respect of our company to Petroquisa. See Major shareholders Shareholders Agreements Petroquisa Memorandum of Understanding.

On September 16, 2005, we and Petroquisa incorporated Paulínia, a joint venture for the construction and operation of a polypropylene plant to be located in Paulínia, in the State of São Paulo. We own 60.0% of the total and voting share capital of Paulínia and Petroquisa owns the remaining 40.0%. On September 16, 2005, (1) we entered into a shareholders agreement with Petroquisa with respect to the management of Paulínia and the transfer of its shares, (2) we contributed the process technology that will be used by this plant under an agreement with a 20-year term, and (3) Paulínia entered into a supply agreement with Petrobras with a 20-year term for the supply to Paulínia of polymer-grade propylene, the primary feedstock to be used in Paulínia s production processes, through Petrobras refineries in Paulínia and Henrique Lage.

***Our Subsidiaries, Jointly Controlled Companies and Associated Companies***

*Copesul*

Our Polyolefins Unit purchases ethylene and propylene from Copesul, in which we have a 29.5% interest. We have a long-term supply contract with Copesul that is described in Item 4. Information on the Company Polyolefins Unit Raw Materials of Our Polyolefins Unit. Our Polyolefins Unit also buys nitrogen on market terms from Copesul. We recorded purchases from Copesul of R$1,814.3 million in 2005. We had accounts payable to Copesul of R$353.2 million at December 31, 2005.

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*COPESUL International Trading Inc.*

COPESUL International Trading Inc. is a subsidiary of Copesul, in which we have a 29.5% interest. At December 31, 2004, one of our subsidiaries, Lantana Trading Company Inc., had four outstanding loans from COPESUL International Trading Inc. of R$145.8 million (R$102.9 million giving effect to proportional consolidation) at interest rates equivalent to the market rates. These loans were paid in full during the year ended December 31, 2005.

*Politeno*

At December 31, 2005, we owned 34.0% of the total share capital of Politeno, including 35.0% of its voting share capital. Our Basic Petrochemicals Unit supplies ethylene to Politeno. We recorded net sales to Politeno of R$696.0 million in 2005. We had accounts receivable from Politeno of R$18.5 million at December 31, 2005. As a result of the Politeno acquisition, we now own 96.2% of the total share capital of Politeno, including 100% of its voting share capital, and will fully consolidate Politeno in our consolidated financial statements at dates and for periods following this acquisition.

*Cetrel*

We own, directly and indirectly, 53.0% of the voting and total share capital of Cetrel. We purchase treatment services on market terms from Cetrel for the wastewater and organic residues generated by us in the Northeastern Complex. We recorded purchases from Cetrel of R$13.6 million in 2005. We had accounts payable to Cetrel of R$0.9 million at December 31, 2005.

*Petroflex*

We own 20.1% of the voting and total share capital of Petroflex. We sell butadiene-l to Petroflex on market terms under a long-term contract that is renewable automatically for ten-year periods. We recorded net sales to Petroflex of R$353.2 million in 2005. We had accounts receivable from Petroflex of R$41.4 million at December 31, 2005.

On June 11, 2004, Petroflex entered into a R$34.3 million secured credit agreement with BNDES to finance capital expenditures. In accordance with the terms of a shareholders agreement among our company and the other controlling shareholders of Petroflex, we have guaranteed severally, but not jointly, 40% of this loan, or approximately R$13.7 million of its aggregate principal amount. The first tranche of this loan in the principal amount of R$10.3 million bears interest at a rate based on the UM plus a margin of 5.125% per annum. The second and third tranches of this loan in the aggregate principal amount of R$24.0 million bear interest at the TJLP plus 5.125% per annum. As set forth in the shareholders agreement, we charge Petroflex a fee of 1.25% of the outstanding principal amount of this loan that we guarantee.

*Borealis Brasil S.A.*

We sell polypropylene and polyethylene to Borealis Brasil S.A. in which we have a 20.0% interest. We recorded net sales to Borealis of R$128.5 million in 2005. We had accounts receivable from Borealis of R$8.7 million at December 31, 2005.

***Other***

*Engepack*

We sell PET from time to time to Engepack, a packaging manufacturer. Francisco Teixeira de Sá, the chairman of the board of directors of Engepack, is a member of our board of directors. In addition, one of the alternate members of our board of directors, Lucio José Santos Junior, is an executive officer of Engepack, and one of the members of our fiscal council, Walter Murilo Melo de Andrade, is the internal counsel of Engepack. We recorded net sales to Engepack of R$25.5 million in 2005. Engepack purchases PET from a variety of second generation producers, including our company.

*Sojitz*

We sell PVC and EDC to, and we purchase raw materials, principally naphtha, from, Sojitz, a chemical trader. Masatoshi Furuhashi, the managing director of Sojitz Corporation of America and president of Sojitz do Brasil S.A., both subsidiaries of Sojitz, is a member of our board of directors. In addition, Yukihiro Funamoto, an executive officer of Sojitz do Brasil S.A., is an alternate member of our board of directors. At December 31, 2005, Sojitz owned 1.2% of our total share capital, including 3.6% of our voting share capital.

We have an ongoing obligation to export PVC and EDC under a supply agreement with Sojitz. Under this supply agreement, we have agreed to supply, and Sojitz has agreed to purchase, minimum annual volumes of 6,000 tons of PVC, and minimum annual volumes of EDC, which decline over time from 100,000 to 80,000 tons. We recorded net sales to Sojitz of R$93.5 million in 2005. In addition, we recorded purchases from Sojitz of R$827.6 million in 2005.

## ITEM 8. FINANCIAL INFORMATION

### Consolidated Statements and Other Financial Information

Reference is made to Item 19 for a list of all financial statements filed as part of this annual report.

### Legal Proceedings

***Tax Proceedings***

We are engaged in several legal proceedings with Brazilian tax authorities for which we have established provisions in an aggregate amount of R$1,370.4 million at December 31, 2005. In addition, there are currently certain legal proceedings pending in which we are involved for which we have not established provisions. If any of these legal proceedings is decided adversely to us, our results of operations or financial condition could be materially and adversely affected.

*IPI*

IPI Credits on Raw Materials Purchases. We pay IPI tax on industrial products that we manufacture. The regulations governing the IPI tax assess this tax on a non-cumulative basis, meaning that companies may offset their IPI tax obligations with the amount of IPI taxes paid by suppliers earlier in the production chain. The Brazilian federal tax authorities have asserted that the purchase of raw materials that are tax-exempt, non-taxable or taxed at a zero percent rate does not generate IPI tax credits, on the basis that there is no law or regulation that expressly authorizes these credits. We believe that this interpretation is contrary to Article 153, paragraph 3 of the Brazilian Constitution, which sets forth the principle of non-cumulative taxation and does not exclude purchases of raw materials that are tax-exempt, non-taxable or taxed at a zero percent rate.

In July 2000, OPP Química filed suit in the State of Rio Grande do Sul requesting the acknowledgement of IPI tax credits for its purchases of raw materials from our company and Copesul. The amount of credits claimed by OPP Química comprised the book value of those raw materials plus monetary adjustments. In December 2002, the Brazilian Federal Supreme Court held that OPP Química was entitled to IPI tax credits in an aggregate amount of R$1,030.1 million, including R$367.9 million attributable to monetary adjustments, for the ten-year period ended in 2002, calculated based on the price of the raw materials purchased during the ten-year period preceding the filing of the suit, plus monetary adjustments based on official indices.

The Brazilian government appealed the decision of the Brazilian Federal Supreme Court. As the appeal does not challenge the validity of IPI tax credits, but only the method of calculating monetary adjustments on those credits and the time period for appealing the decision of the Brazilian Federal Supreme Court has expired, we believe that (1) the decision acknowledging the validity of the IPI tax credits is no longer subject to appeal, and

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(2) it is reasonably possible that we could lose the appeal regarding the method of calculating monetary adjustments on those credits. If the Brazilian Government prevails in this appeal, we could lose all or part of the IPI tax credits attributable to monetary adjustments. We recognized IPI tax credits in an aggregate amount of R$1,030.1 million in December 2002. At December 31, 2005, we have used the full amount of the R$1,030.1 million IPI tax credit to offset our IPI and other federal tax obligations.

We have three other similar suits pending on behalf of OPP Química and Trikem (which have merged into our company) in federal courts in the States of Bahia, São Paulo and Alagoas. In two of these cases, we obtained preliminary injunctions that allowed these companies to use these credits to offset other IPI tax obligations. In the third case, we obtained a favorable decision in federal trial court that recognized our right to these credits for the ten-year period preceding the filing of this suit, which decision the Brazilian government appealed to the Superior Court of Justice and the Brazilian Federal Supreme Court in 2002. All three of these suits remain pending. Based on (1) these favorable lower court decisions, (2) the favorable decision of the Brazilian Federal Supreme Court relating to the validity of the IPI tax credits in OPP Química s suit in Rio Grande do Sul described above and (3) our assessment of the arguments made in a similar case involving a third party that is currently pending before the Brazilian Federal Supreme Court, we believe that it is reasonably possible that we will prevail in these suits. Accordingly, we have used R$203.7 million at December 31, 2005 of Trikem s and OPP Químicas IPI tax credits to offset our IPI and other federal tax obligations and have recorded a provision in the amount of R$308.7 million at December 31, 2005. We have not recognized any assets or gains in relation to these claims.

We also have a similar suit pending in federal court in the State of Bahia that was commenced by Poliaden prior to our merger with Polialden. Polialden won this suit in federal trial court, which ruled that Polialden was entitled to IPI tax credits for the ten-year period preceding the filing of this suit. However, the Brazilian government appealed this decision to the Federal Superior Court of Justice, which appeal remains pending. Based on (1) this favorable lower court decision, (2) the favorable decision of the Brazilian Federal Supreme Court relating to the validity of the IPI tax credits in OPP Química s suit in Rio Grande do Sul described above, and (3) our assessment of the arguments made in a similar case involving a third party that is currently pending before the Brazilian Federal Supreme Court, we believe that it is reasonably possible that we will prevail in this suit. Accordingly, Polialden used R$98.0 million at December 31, 2005 in IPI tax credits to offset its IPI and other federal tax obligations and recorded a provision in the amount of R$157.6 million at December 31, 2005. Polialden did not recognize any assets or gains in relation to these claims.

For further information on our accounting treatment of these IPI credits, see note 17 to our consolidated financial statements.

*IPI Export Credits.* Brazilian Decree Law No. 491/69 provides a tax credit to exporters of manufactured products to compensate them for taxes paid in Brazil prior to exporting their products. The regulations governing the IPI tax permit exporters to offset IPI taxes with IPI export credits and/or to transfer their IPI export credits to third parties. However, the Brazilian tax authorities issued a series of administrative rules that reduced, restricted and ultimately suspended the use of these credits based on Decree Law No. 1,724/79, which expressly delegated these powers to the Brazilian Ministry of Finance. We believe that this delegation of powers to the Ministry of Finance violated the distribution of functions among the executive branch, and that secondary administrative rules may not restrict or suspend a benefit created by a constitutionally superior norm. Accordingly, we believe that the administrative rules promulgated under the authority of Decree Law No. 1,724/79 have no legal effect. On these grounds, we and some of our subsidiaries filed suits against the Brazilian government challenging Decree Law No. 1,742/79 and these administrative rules and seeking to offset and transfer IPI export credits as provided under Decree Law No. 491/96.

We and our subsidiaries believe that we are entitled to more than R$794.6 million in IPI export credits. In one of these suits, the Regional Federal Court ruled against OPP Química, holding that it does not have the right to IPI export credits. OPP Química s appeals before the Superior Court of Justice and the Brazilian Federal

Supreme Court remain pending. Although our other suits also are pending, the Brazilian tax authorities have issued deficiency notices against us (1) attempting to collect amounts offset using these IPI export credits and (2) asserting their right to do so before the expiration of the applicable statute of limitations. We filed administrative appeals in respect of these deficiency notices, but we received unfavorable decisions in each of these appeals. We have appealed each of these unfavorable decisions to the taxpayers council (an administrative appeal board). However, based on recent Brazilian Federal Supreme Court and other jurisprudence holding that the sub-delegation by the Ministry of Finance of the authority to regulate IPI export credits under Decree Law No. 1,742/79 was unconstitutional and recognizing the right to offset IPI export credits as provided under Decree Law No. 491/96, we believe that it is reasonably possible that we will prevail in all of these judicial and administrative proceedings. We note that the Brazilian Federal Supreme Court rendered a decision in an unrelated proceeding involving a third party holding that this sub-delegation was constitutional. However, the Federal Senate issued Resolution No. 71 on December 27, 2005 confirming the unconstitutionality of this sub-delegation and ratifying the validity of IPI export credits. We are analyzing the potential consequences of this Resolution. We have used a portion of these credits to offset IPI and other federal taxes in the amount of R$391.0 million at December 31, 2005 and recorded a provision in the amount of R$550.3 million at December 31, 2005 because these suits remain pending. For further information on our accounting treatment of these IPI credits, see note 17 to our consolidated financial statements.

*IPI Credits Arising from the Acquisition of Fixed Assets and Materials Not Used in Production.* We are involved in four suits against the Brazilian government seeking the acknowledgment of IPI credits arising from the acquisition of fixed assets and materials not used by us in the production of our products. The regulations governing the IPI tax permit companies to offset against their IPI tax liability IPI credits arising from the acquisition of raw materials and other unfinished products only to the extent that they are used in production. We believe that this limitation imposed by the IPI regulations is unconstitutional. Article 153, paragraph 3 of the Brazilian Constitution sets forth a broad principle of non-cumulative taxation and does not limit the grant or use of IPI credits arising from the acquisition of fixed assets or in respect of materials not used in production.

We lost one of these suits in federal trial court and appealed this decision, which appeal remains pending. Although our three other suits also remain pending in federal court, the Brazilian tax authorities have issued deficiency notices against us attempting to collect amounts offset using these credits, asserting their right to do so before the expiration of the applicable statute of limitations. We appealed the issuance of these deficiency notices to the taxpayers council. We believe that it is reasonably possible for us to prevail in all of these judicial and administrative proceedings. We have used R$20.2 million at December 31, 2005 of these credits to offset IPI taxes and recorded a provision in the amount of R$37.7 million at December 31, 2005 because these suits remain pending. For further information on our accounting treatment of these IPI credits, see note 17 to our consolidated financial statements.

*Social Contribution on Net Income*

Law No. 7,689/88 created the Social Contribution on Net Income (CSLL), a tax similar to the corporate income tax. Under Article 146, item III of the Brazilian Constitution, the Social Contribution on Net Income should have been enacted as a supplementary law and not as an ordinary law. Under Brazilian law, supplementary laws must be approved by at least a majority of the members of each house of the Brazilian Congress, while an ordinary law may be approved by a simple majority of the members of Congress present at the relevant voting session. In addition, we believe that Social Contribution on Net Income violates Article 154, item II of the Brazilian Constitution, which provides that new taxes may not be assessed and calculated on the same basis as existing taxes. We believe the Social Contribution on Net Income is assessed and calculated on the same basis as the corporate income tax.

On these grounds, we and some of our subsidiaries filed suit challenging the constitutionality of the Social Contribution on Net Income. We received a final decision in our favor in 1992. However, in 1993, Brazilian tax authorities filed a rescission action (ação rescisória) against us in relation to all but one of these cases seeking to

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overrule this decision on the basis of a ruling by the Brazilian Federal Supreme Court in an unrelated case that recognized the constitutionality of the Social Contribution on Net Income. The Brazilian tax authorities prevailed in their rescission action both in the first instance and on appeal. We filed further appeals in respect of this decision with the Superior Court of Justice and the Brazilian Federal Supreme Court, which appeals remain pending. In the remaining case, we believe that it is reasonably possible that the final decision in our favor will remain in effect.

Brazilian tax authorities issued several deficiency notices against us and our subsidiaries attempting to collect Social Contribution on Net Income. We obtained suspensions of all deficiency notices that we have received to date based on a Brazilian civil procedure provision that states that a rescission action may take effect only after the court publishes a final decision.

We believe it is reasonably possible that we will lose our appeals. However, if we lose these suits, we believe that we would be required to pay Social Contribution on Net Income only from the date that a final decision is published. We note, however, that Brazilian law allows rescission actions to relate back to, and to take effect from, the date of the initial decision. Although this legislation does not involve tax proceedings and the Brazilian Federal Supreme Court has not ruled on this issue, the same line of reasoning has been adopted by the Brazilian tax authorities and may be adopted by the courts in our suit. Accordingly, we believe that it is reasonably possible that we will be required to pay these taxes retroactively.

If Social Contribution on Net Income is charged retroactively, then our total estimated exposure at December 31, 2005 would be R$651.7 million, including interest. This amount does not include approximately R$175.0 million in penalties at December 31, 2005, which we believe are not payable because we relied upon a judicial decision in not paying Social Contribution on Net Income. We believe that there is a possibility that we will be required to pay related interest and a remote possibility that we will be required to pay fines as a result of this tax litigation.

As we believe that Social Contribution on Net Income may not be payable for periods before the date the final decision is published in the rescission action, we have not made any provision in our consolidated financial statements for these contingencies. For further information on our accounting treatment of CSLL, see note 18(c) to our consolidated financial statements.

*PIS and COFINS*

The PIS and COFINS taxes are Brazilian federal taxes created to fund the government s unemployment payments, social security and other social programs. Prior to February 1999, PIS and COFINS were assessed on gross billings, that is, billings or invoices for sales of goods and services. Effective February 1999, Law No. 9,718/98 introduced significant changes in the assessment of PIS and COFINS, which changes have materially increased the tax burden of our company on a consolidated basis. Law No. 9,718/98 substantially broadened the concept of gross billings to include revenue generated from sources other than sales of goods and services, increasing the tax base upon which PIS and COFINS are assessed. At the same time, the rate of COFINS increased from 2% to 3%.

We believe that these changes were unconstitutional. The provisions of Law No. 9,718/98 that broadened the concept of gross billings in our view violated the original terms of Article 195 of the Brazilian Constitution, as well as Article 110 of the Brazilian tax code, which prohibits tax laws from changing the definition, content and reach of private law doctrines and concepts. In addition, although the Brazilian Congress enacted Constitutional Amendment No. 20 on December 15, 1998 to modify Article 195 of the Brazilian Constitution in order to validate the expanded calculation basis of PIS and COFINS as set forth in Law No. 9,718/98, we believe that this law cannot be validated by constitutional amendment for periods before the effectiveness of the constitutional amendment. On these grounds, we and our subsidiaries have filed suit against the Brazilian government seeking to pay PIS and COFINS in accordance with the rules prevailing prior to February 1999.

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We and some of our subsidiaries lost our suits challenging the change in the definition of gross billings and have appealed these decisions to the Brazilian Federal Supreme Court. On November 9, 2005, the full bench of the Brazilian Federal Supreme Court ruled that the increase in PIS and COFINS tax basis under Law No. 9,718/98 was unconstitutional. Following this decision, the previous unfavorable decisions against us and these subsidiaries were vacated, and we and these subsidiaries won most of our suits challenging the change in the definition of gross billings.

We and some of our subsidiaries lost suits challenging the increase in the COFINS tax rate and have appealed these decisions to the Brazilian Federal Supreme Court. Based on recent Brazilian Federal Supreme Court and Superior Court of Justice jurisprudence, we believe that our chances of success in these suits are remote. Two of our subsidiaries have voluntarily settled their COFINS liabilities under a special program created by Law No. 10,684/03, for which we have recorded a long-term liability in an aggregate amount of R$43.2 million at December 31, 2005. As of February 2004, we and our subsidiaries have been paying COFINS in accordance with Law 10,833/03, which introduced new criteria for calculating COFINS.

We recorded a provision in accordance with Law No. 9,718/98 in respect of the proceedings that were not settled in an aggregate amount of R$316.1 million at December 31, 2005 and have deposited R$39.1 million of this amount in court. For further information on our accounting treatment of these contingencies, see notes 10 and 17(iii) to our consolidated financial statements.

*Tax on Net Profits*

Law No. 7713/88 imposed an 8.0% income tax on equity holders, the tax on net profits, which was calculated on net profits recorded by companies in which such holders own equity and was assessed even when the net profits have not been distributed to those equity holders. We believe that Law No. 7713/88 violates Article 43 of the Brazilian tax code, which provides that income tax may be assessed only at the moment when the equity holder effectively receives or is entitled to receive income.

On these grounds, we filed a lawsuit in 1997 against the Brazilian government seeking a refund of, or the right to offset other taxes with, the tax on net profits that we overpaid with respect to the 1990 and 1991 tax years, which at December 31, 2005 totaled approximately R$73.2 million. We deposited a portion of this amount with the court and have used this amount to offset our PIS and COFINS liabilities. In March 2002, the Regional Federal Court recognized our right to use these overpaid amounts to offset other taxes, as adjusted for inflation and including interest accrued on these amounts at the SELIC rate. The Brazilian government filed a special appeal before the Superior Court of Justice, which decided the case in favor of our company. Based on the decision of the Superior Court of Justice, we have petitioned the Regional Federal Court, requesting the refund of our judicial deposits and the nullification of the deficiency notices issued by the tax authorities with respect to these amounts.

We brought suit for recovery of unduly paid tax on net profits in the 1989 and 1990 tax years. The Regional Federal Court issued a non-appealable order in our favor, and we requested that the Federal Revenue Office acknowledge that a tax credit be recognized and be available to offset against subsequent tax obligations. In November 2005, the Federal Revenue Office acknowledged our entitlement to a R$45.4 million tax credit, which we used to offset PIS and COFINS liabilities in 2005.

*Offset of Tax Credits*

From May through October 2000, OPP Química and Trikem offset their own federal tax obligations with IPI tax credits assigned by a third-party export trading company. In June 1999, the export trading company filed a motion for a writ of mandamus requiring the federal tax authority of the State of São Paulo to recognize these offsets, and in October 1999, the federal tax authority of the State of São Paulo issued offset support certificates in response to an injunction obtained by the export trading company. In September 1999, the export trading

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company filed a motion for a writ of mandamus requiring the federal tax authority of the State of Rio de Janeiro to recognize the recovery of IPI tax credits by the export trading company and the validity of their use in offsetting third-party tax obligations. In March 2001, the motion for a writ of mandamus filed by the export trading company in the State of São Paulo was dismissed without prejudice, confirming the administrative and jurisdictional authority of the State of Rio de Janeiro to rule on the export trading company s tax credits.

In June 2005, the federal tax authority of the State of São Paulo issued regulations canceling the offset support certificates. Based on these regulations, the Federal Revenue Office unit in Camaçari, Bahia sent collection letters to our company in June 2005. We presented notices of dispute against these collection letters, but the administrative authorities declined to process these notices.

On October 3, 2005, the Federal Supreme Court granted a non-appealable writ of mandamus to the export trading company, confirming the export trading company s right to use its IPI tax credits from all its exports and the availability of these IPI tax credits for offsetting third-party obligations. As a result, we believe that our use of the export trading company s IPI credits to offset our federal taxes has been confirmed and that the assessment made by the Federal Revenue Office unit in Camaçari, Bahia is not due. In addition and notwithstanding the writ of mandamus granted to the export trading company, we believe that the statue of limitations has expired with respect to the federal taxes offset against the IPI tax credits of the export trading company and can no longer be claimed by the tax authorities.

In December 2005, the Federal Revenue Office unit in Camaçari, Bahia assessed past-due federal tax liabilities of R$276.6 million against our company related to our alleged undue offset of federal taxes. In January 2006, we were ordered to post bond in aid of execution of the tax claim made by the Federal Revenue Office unit in Camaçari, Bahia, and we posted this bond in the form of an insurance policy.

We and the export trading company subsequently commenced judicial and administrative proceedings to defend the lawfulness and validity of those offsetting procedures. We believe that it is probable that we will prevail in these judicial and administrative proceedings in light of our view of the validity and liquidity of those credits as confirmed in a special audit conducted by the federal tax authority of the State of Rio de Janeiro. In the event that we are unsuccessful in all of these judicial and administrative proceedings, pursuant to the agreement under which the export trading company assigned the IPI tax credits to OPP Química and Trikem, we will be entitled to full recourse against the export trading company concerning all amounts we are required to pay to the National Treasury.

*Other Tax Proceedings*

We, our subsidiaries and our affiliates are involved in several other judicial and administrative proceedings regarding withholding taxes, corporate income taxes *(Imposto de Renda da Pessoa Jurídica),* the ICMS, the tax on financial transactions (*Imposto Sobre Operações Financeiras*), monetary adjustments, the Social Investment Fund (*Fundo de Investimento Social*), compulsory loans to Eletrobrás and other issues related to tax matters. Some of these disputes involve substantial amounts.

***Labor Proceedings***

*Clause Four   Cláusula Quarta*

Our company and other companies in the Northeastern Complex enter into annual collective bargaining agreements with the petrochemical workers union. The collective bargaining agreement that was valid between September 1989 and August 1990 required employers to pay workers monthly cost of living adjustments equal to 84.3% of the consumer price index (*Índice de Preços ao Consumidor*), or IPC, and prohibited the substitution of the IPC by another index with lower values.

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In March 1990, the Brazilian government introduced an economic plan known as the Collor Plan, named after the then-President of Brazil. The Collor Plan provided that cost of living adjustments in wages could be based on other indices but not on the IPC. Based on judicial precedent, we interpreted the Collor Plan as prohibiting wage increases based on the IPC, which interpretation was contrary to the terms of the collective bargaining agreements in effect at the time. The petrochemical employers union filed a lawsuit against the petrochemical workers union, seeking to confirm that the cost of living adjustment indices provided in the Collor Plan preempted the conflicting provisions in the collective bargaining agreements. The Regional Labor Court ruled in favor of the workers union, and the decision was later modified in part on appeal to the Superior Labor Court. In 1998, the employers union filed an extraordinary appeal to the Brazilian Federal Supreme Court.

The Brazilian Federal Supreme Court initially held in favor of the workers union, but reversed its decision in December 2002 and held that a private collective bargaining agreement cannot preempt federal law, particularly a law that related to Brazilian public policy. In 2003, the workers union requested reconsideration of this decision. The Brazilian Federal Supreme Court accepted the workers union s request for reconsideration, but on May 31, 2005, the Brazilian Federal Supreme Court unanimously reaffirmed its December 2002 decision and dismissed the workers union s appeal.

On October 24, 2005, the workers union filed a divergence appeal to the Brazilian Federal Supreme Court, requesting the resolution of conflict between the decisions given by the Brazilian Federal Supreme Court under this proceeding and prior decisions given by the another panel of the Brazilian Federal Supreme Court. The Brazilian Federal Supreme Court has agreed to consider this appeal, but has not yet issued a decision.

*Other*

We and our subsidiaries are involved in approximately 1,100 labor lawsuits that involve claims totaling R$223.4 million at December 31, 2005. We have deposited R$22.5 million of this amount in court and have established a provision for labor contingencies in an aggregate amount of R$12.3 million at December 31, 2005.

*Occupational Health and Safety Proceedings*

At December 31, 2005, we were party to 169 occupational health and safety proceedings as to which the total amount claimed was approximately R$147.4 million. As we believe that the risk of losing these proceedings is possible and not probable, we have not established a provision in respect of these proceedings and do not believe that these proceedings will have a material adverse effect on our business, financial condition or operations.

*Other Proceedings*

At December 31, 2005, we were a defendant in three civil suits filed by a former caustic soda distributor, its controlling shareholder and a former transporter for breach of a caustic soda distribution agreement. The damages claimed in these suits totaled R$132.6 million at December 31, 2005 (monetarily adjusted). We prevailed in one of these suits in trial court, which the plaintiff appealed. This appeal remains pending. On January 19, 2006, a lower court issued a non-appealable judgment in our favor in one or these suits in which the damages claimed were R$106.5 million. The remaining suit is pending. We believe that we will prevail in this suit and in the appeal.

We have also filed a claim in the amount of R$1.9 million against this distributor in its pending bankruptcy proceeding. The bankruptcy court has initially accepted our claim.

We are parties to certain proceedings brought by some preferred shareholders of our company and Polialden which we do not believe will have a material adverse effect on our business, financial condition or results of operations.

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**Dividends And Dividend Policy**

***Payment of Dividends***

Our dividend distribution policy has historically included the distribution of periodic dividends, based on annual balance sheets approved by our board of directors. When we pay dividends on an annual basis, they are declared at our annual shareholders meeting, which we are required by the Brazilian Corporation Law and our by-laws to hold by April 30 of each year. When we declare dividends, we are generally required to pay them within 60 days of declaring them unless the shareholders resolution establishes another payment date. In any event, if we declare dividends, we must pay them by the end of the fiscal year for which they are declared. Under Article 9 of Law 9,249/95 and our bylaws, we also may pay interest attributable to shareholders equity as an alternative form of dividends upon approval of our board of directors. For a more detailed description of interest attributable to shareholders equity, see Payment of Dividends and Interest Attributable to Shareholders Equity Interest Attributable to Shareholders Equity.

The following table sets forth the dividends and/or interest attributable to shareholders equity paid to holders of our common shares, class A preferred shares and class B preferred shares since 2001 in *reais* and in U.S. dollars translated from *reais* at the commercial market selling rate in effect as of the payment date.

| | | Nominal Brazilian Currency per | | | US$ equivalent per | | |
|---|---|---|---|---|---|---|---|
| **Year** | **Payment Date** | **Common shares** | **Class A Preferred Shares** | **Class B Preferred Shares** | **Common shares** | **Class A Preferred Shares** | **Class B Preferred Shares** |
| 2001 | February 20, 2001 | R$ 0.21 | R$ 0.21 | R$ | US$ 0.11 | US$ 0.11 | US$ |
| | May 20, 2001 | 0.14 | 0.14 | 0.14 | 0.06 | 0.06 | 0.06 |
| | August 20, 2001 | 0.14 | 0.14 | 0.14 | 0.06 | 0.06 | 0.06 |
| | November 20, 2001 | 0.14 | 0.14 | 0.14 | 0.06 | 0.06 | 0.06 |
| 2002 | February 25, 2002 | | 0.08 | 0.08 | | 0.04 | 0.04 |
| | May 20, 2002 | | 0.13 | 0.13 | | 0.05 | 0.05 |
| 2005 | April 12, 2005(1) | 0.56 | 0.56 | 0.56 | 0.22 | 0.22 | 0.22 |
| 2006 | April 18, 2006 | 0.90 | 0.90 | 0.56 | 0.42 | 0.42 | 0.26 |

(1) Represents interest attributable to shareholders equity of R$0.28 (US$0.11) per common share, R$0.56 (US$0.22) per class A preferred share and R$0.56 (US$0.22) per class B preferred share, plus dividends of R$0.28 (US$0.11) per common share.

(2) Represents interest attributable to shareholders equity of R$0.75 (US$0.35) per common share, R$0.75 (US$0.35) per class A preferred share and R$0.56 (US$0.26) per class B preferred share, plus dividends of R$0.15 (US$0.07) per common share and R$0.15 (US$0.07) per class A preferred share.

***Amounts Available for Distribution***

The following discussion summarizes the principal provisions of the Brazilian Corporation Law and our by-laws relating to the distribution of dividends, including interest attributable to shareholders equity.

***Calculation of Adjusted Net Profits***

At each annual shareholders meeting, our board of directors is required to recommend how to allocate our net profits for the preceding fiscal year, which recommendation our board of executive officers initially submits to our board of directors for approval. This allocation is subject to approval by our common shareholders. The Brazilian Corporation Law defines net profits for any fiscal year as our net income after income taxes for that fiscal year, net of any accumulated losses from prior fiscal years and any amounts allocated to employees participation in our net profits in that fiscal year. Under the Brazilian Corporation Law, our adjusted net profits available for distribution are equal to our net profits in any fiscal year, reduced by amounts allocated to our legal reserve and other applicable reserves, and increased by any reversals of reserves that we constituted in prior years.

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Our calculation of net profits and allocations to reserves for any fiscal year are determined on the basis of financial statements prepared in accordance with Brazilian GAAP.

***Reserve Accounts***

Under the Brazilian Corporation Law and our by-laws, we are required to maintain a legal reserve. In addition, we are permitted by the Brazilian Corporation Law to establish the following discretionary reserves:

- a contingency reserve for an anticipated loss that is deemed probable in future years. Any amount so allocated in a previous year must be reversed in the fiscal year in which the loss had been anticipated if the loss does not occur as projected or charged off in the event that the anticipated loss occurs;

- a reserve for investment projects, in an amount based on a capital expenditure budget approved by our shareholders;

- an unrealized income reserve described under Mandatory Distributions below; and

- a tax incentive investment reserve, included in our capital reserve accounts, in the amount of the reduction in our income tax obligations due to government tax incentive programs. See note 19(a) to our audited consolidated and combined financial statements.

Allocations to each of these reserves (other than the legal reserve) are subject to approval by our common shareholders voting at our annual shareholders meeting.

The Brazilian Corporation Law provides that the legal reserve and the tax incentive investment reserve may be credited to shareholders equity or used to absorb losses, but these reserves are unavailable for the payment of distributions in subsequent years. The amounts allocated to the other reserves may be credited to shareholders equity and used for the payment of distributions in subsequent years.

*Legal Reserve Account*

Under the Brazilian Corporation Law and our by-laws, we must allocate 5% of our net profits for each fiscal year to our legal reserve until the aggregate amount of our legal reserve equals 20% of our paid-in capital. However, we are not required to make any allocations to our legal reserve in a fiscal year in which our legal reserve, when added to our other reserves, exceeds 30% of our shareholders equity. At December 31, 2005, we had a balance of R$68.9 million in our legal reserve account.

*Capital Reserve Accounts*

Under the Brazilian Corporation Law, we are also permitted to record a capital reserve that may be used only (1) to absorb losses which exceed retained earning and profit reserves as defined in the Brazilian Corporation Law, and (2) to redeem or repurchase share capital and/or participation certificates, (3) to increase our capital, or (4) if specified in our by-laws (which currently do not so specify), to pay preferred share dividends. Amounts allocated to our capital reserves are unavailable for the payment of distributions and are not taken into consideration for purposes of determining the mandatory distributable amount. At December 31, 2005, we had a balance of R$396.8 million in our capital reserve accounts.

***Mandatory Distributions***

As permitted by the Brazilian Corporation Law, our by-laws specify that 25% of our adjusted net profits for each fiscal year must be distributed to shareholders as dividends or interest attributable to shareholders equity. We refer to this amount as the mandatory distributable amount.

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Under the Brazilian Corporation Law, the amount by which the mandatory distributable amount exceeds the realized portion of net income for any particular year may be allocated to the unrealized income reserve, and the mandatory distribution may be limited to the realized portion of net income. The realized portion of net income is the amount by which our net income exceeds the sum of (1) our net positive results, if any, from the equity method of accounting for earnings and losses of our subsidiaries and certain associated companies, and (2) the profits, gains or income obtained on transactions maturing after the end of the following fiscal year. As amounts allocated to the unrealized income reserve are realized in subsequent years, such amounts must be added to the dividend payment relating to the year of realization.

In addition to the mandatory distributable amount, our board of directors may recommend that holders of our common shares approve the payment of additional distributions from other funds legally available for distribution. Distributions made to holders of our class A preferred shares and our class B preferred shares are computed in determining whether we have paid the required mandatory distribution. We net any payment of interim distributions against the required mandatory distribution for that fiscal year.

As described under Item 7. Major Shareholders and Related Party Transactions Major Shareholders Shareholders Agreements, we have entered into an agreement with two of our shareholders that establishes as our dividend policy the distribution of at least 50% of our adjusted net profits during any relevant period, provided that we have established and maintained all necessary reserves for the efficient operation and development of our business.

Under our 10.625% Notes due 2007 and our 11.75% Notes due 2014, we may not pay dividends in excess of two times the minimum dividends or interest attributable to shareholders equity payable under our by-laws or under applicable Brazilian law.

The Brazilian Corporation Law permits us to suspend the mandatory distribution if our board of directors reports to our annual shareholders meeting that the distribution would be incompatible with our financial condition at that time. Our fiscal council must approve any suspension of the mandatory distribution. In addition, our management must report the reasons of any suspension of the mandatory distribution to the Brazilian Securities Commission. We must allocate net profits not distributed by our company as a result of a suspension to a special reserve and, if not absorbed by subsequent losses, we must distribute these amounts as soon as our financial condition permits. In case our profits reserves, as defined in the Brazilian Corporation Law, exceed our share capital, the excess must be credited to shareholders equity or used for the payment of distributions.

***Payment of Dividends and Interest Attributable to Shareholders Equity***

We may pay the mandatory distributable amount as dividends or as interest attributable to shareholders equity, which is similar to a dividend but is deductible in calculating our income tax obligations. There are no restrictions on our ability to distribute dividends that have been lawfully declared under Brazilian law. However, as with other types of remittances from Brazil, the Brazilian government may impose temporary restrictions on remittances to foreign investors of the proceeds of their investments in Brazil, as it did for approximately six months in 1989 and early 1999, and on the conversion of Brazilian currency into foreign currencies, which could hinder or prevent the depositary from converting dividends into U.S. dollars and remitting these U.S. dollars abroad. See Item 3. Key Information Risk Factors Risks Relating to Our Class A Preferred Shares and the ADSs.

*Dividends*

We are required by the Brazilian Corporation Law and by our by-laws to hold an annual shareholders meeting by April 30 of each year. At our annual shareholders meeting, our common shareholders may vote to declare an annual dividend. Our payment of annual dividends is based on our audited financial statements prepared for our preceding fiscal year.

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Any holder of record of shares at the time that a dividend is declared is entitled to receive dividends. Under the Brazilian Corporation Law, we are generally required to pay dividends within 60 days after declaring them, unless the shareholders resolution establishes another payment date, which, in any case, must occur prior to the end of the fiscal year in which the dividend is declared.

Our board of directors may declare interim dividends based on the accrued profits recorded or the realized profits in our annual or semi-annual financial statements approved by our common shareholders. In addition, we may pay dividends from net income based on our unaudited quarterly financial statements. These quarterly interim dividends may not exceed the amounts included in our capital reserve accounts. We may set off any payment of interim dividends against the amount of the mandatory distributable amount for the year in which the interim dividends were paid.

*Interest Attributable to Shareholders Equity*

Brazilian companies, including our company, are permitted to pay interest attributable to shareholders equity as an alternative form of payment of dividends to our shareholders. These payments may be deducted when calculating Brazilian income tax and social contribution tax. The interest rate applied to these distributions generally cannot exceed the Long-Term Interest Rate for the applicable period. The amount of interest paid that we can deduct for tax purposes cannot exceed the greater of:

- 50% of our net income (after the deduction of the provision for social contribution tax and before the deduction of the provision for corporate income tax) before taking into account any such distribution for the period for which the payment is made; and

- 50% of the sum of our retained earnings and profit reserves.

Any payment of interest attributable to shareholders equity to holders of common shares, preferred shares or ADSs, whether or not they are Brazilian residents, is subject to Brazilian withholding tax at the rate of 15%, except that a 25% withholding tax rate applies if the recipient is a resident of a tax haven jurisdiction. A tax haven jurisdiction is a country (1) that does not impose income tax or whose income tax rate is lower than 20% or (2) which does not permit disclosure of the identity of shareholders of entities organized under its jurisdiction. See Item 10. Additional Information Taxation Brazilian Tax Considerations. Under our by-laws, we may include the amount distributed as interest attributable to shareholders equity, net of any withholding tax, as part of the mandatory distributable amount.

*Prescription of Payments*

Our shareholders have three years to claim dividend distributions made with respect to their shares, as from the date that we distribute the dividends to our shareholders, after which any unclaimed dividend distributions legally revert to us. We are not required to adjust the amount of any distributions for inflation that occurs during the period from the date of declaration to the payment date.

***Dividend Preference of Preferred Shares***

Under our by-laws, our preferred shareholders are entitled to a minimum annual non-cumulative preferential dividend equal to 6% of their *pro rata* share of our capital before dividends may be paid to our common shareholders. If we declare a dividend in an amount that exceeds the preferential dividends due to our preferred shareholders, our common shareholders are then entitled to receive distributions equivalent, on a per share basis, to the preferential dividend payable to our preferred shareholders. If any additional dividend amounts remain, our common shareholders and our class A preferred shareholders are entitled to receive the same amount per share. Our class B preferred shareholders, however, are not entitled to receive any additional dividend amounts after they have received the preferential dividend.

**Significant Changes**

Other than as otherwise disclosed in this annual report, no significant change has occurred since the date of the audited consolidated financial statements included in the annual report.

## ITEM 9. THE OFFER AND LISTING

**Markets for Our Equity Securities**

The principal trading market for our common shares, class A preferred shares and class B preferred shares is the São Paulo Stock Exchange. Our common shares and class A preferred shares began trading on the São Paulo Stock Exchange on November 11, 1980, and our class B preferred shares began trading on the São Paulo Stock Exchange on August 19, 1983.

On December 21, 1998, ADSs representing our class A preferred shares began trading on The New York Stock Exchange. On December 31, 2005, there were 15,115,684 ADSs outstanding, representing 30,231,368 class A preferred shares, or 12.6% of our outstanding class A preferred shares.

On October 8, 2003, we listed our class A preferred shares on the LATIBEX, a stock market for Latin American issuers that is quoted in euros on the Madrid Stock Exchange, under the symbol XBRK. Our class A preferred shares are traded on the LATIBEX in lots of one share.

At June 22, 2006, we had approximately 18,333 shareholders, including one U.S. resident holder of our common shares, approximately 117 U.S. resident holders of our class A preferred shares (including The Bank of New York, as depositary) and no U.S. resident holders of our class B preferred shares. At June 22, 2006, there were 72,000 common shares, 50,729,756 class A preferred shares (including class A preferred shares represented by ADSs), and no class B preferred shares held by U.S. resident holders.

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**Price History of Our Class A Preferred Shares and the ADSs**

The tables below set forth the high and low closing sales prices for our class A preferred shares on the São Paulo Stock Exchange and the high and low closing sales prices for the ADSs on The New York Stock Exchange for the periods indicated.

| | São Paulo Stock Exchange | | New York Stock Exchange | |
|---|---|---|---|---|
| | ***Reais* per Class A Preferred Share** | | **U.S. dollars per ADS** | |
| | **High** | **Low** | **High** | **Low** |
| 2001 | R$ 7.25 | R$ 3.61 | US$ 8.94 | US$ 3.07 |
| 2002 | 6.84 | 2.24 | 6.38 | 1.29 |
| 2003 | 15.63 | 1.85 | 11.70 | 1.10 |
| 2004 | 31.68 | 9.36 | 25.48 | 6.18 |
| 2005 | 31.84 | 16.16 | 25.82 | 14.57 |

| | São Paulo Stock Exchange | | New York Stock Exchange | |
|---|---|---|---|---|
| | ***Reais* per Class A Preferred Share** | | **U.S. dollars per ADS** | |
| | **High** | **Low** | **High** | **Low** |
| **2004** | | | | |
| First Quarter | R$ 18.82 | R$ 14.73 | US$ 14.63 | US$ 10.75 |
| Second Quarter | 16.95 | 9.36 | 12.77 | 6.32 |
| Third Quarter | 22.26 | 13.30 | 16.54 | 9.12 |
| Fourth Quarter | 31.68 | 21.58 | 25.48 | 15.89 |
| **2005** | | | | |
| First Quarter | 31.84 | 25.04 | 25.82 | 19.42 |
| Second Quarter | 26.49 | 18.02 | 20.87 | 15.78 |
| Third Quarter | 24.45 | 16.16 | 22.45 | 14.57 |
| Fourth Quarter | 21.93 | 17.00 | 21.00 | 15.79 |
| **2006** | | | | |
| First Quarter | 18.95 | 15.84 | 18.24 | 14.37 |
| **Most Recent Six Months** | | | | |
| December 2005 | 19.11 | 17.64 | 18.26 | 15.85 |
| January 2006 | 18.70 | 16.65 | 16.62 | 14.95 |
| February 2006 | 18.95 | 16.72 | 18.24 | 15.35 |
| March 2006 | 18.13 | 15.84 | 17.45 | 14.37 |
| April 2006 | 15.96 | 14.43 | 14.95 | 13.66 |
| May 2006 | 15.55 | 13.85 | 15.05 | 11.94 |

*Source*: Economática Ltda.

On June 22, 2006, the closing sales price of:

our class A preferred shares on the São Paulo Stock Exchange was R$12.42 per share;

our class A preferred shares on the LATIBEX was 4.45 per share; and

the ADSs on The New York Stock Exchange was US$10.93 per ADS.

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The following table sets forth the average daily trading volume for our class A preferred shares on the São Paulo Stock Exchange and for the ADSs on The New York Stock Exchange for the periods indicated.

| | Average Daily Trading Volume | |
|---|---|---|
| | São Paulo Stock Exchange | New York Stock Exchange |
| | Class A Preferred Shares | ADSs |
| **2004** | | |
| First Quarter | 569,440 | 59,736 |
| Second Quarter | 613,548 | 50,120 |
| Third Quarter | 802,780 | 94,642 |
| Fourth Quarter | 777,788 | 178,366 |
| **2005** | | |
| First Quarter | 983,247 | 224,456 |
| Second Quarter | 1,023,416 | 207,602 |
| Third Quarter | 1,353,811 | 255,289 |
| Fourth Quarter | 1,277,477 | 222,679 |
| **2006** | | |
| First Quarter | 1,521,282 | 302,466 |

**Trading on the São Paulo Stock Exchange**

Settlement of transactions conducted on the São Paulo Stock Exchange is effected three business days after the trade date without any adjustment for inflation. Delivery of and payment for shares is made through the facilities of the the Brazilian Clearing System (*Companhia Brasileira de Liquidação e Custódia)*. The seller is ordinarily required to deliver the shares to the exchange on the second business day following the trade date.

The São Paulo Stock Exchange is significantly less liquid than The New York Stock Exchange and many other of the world s major stock exchanges. While all of the outstanding shares of a listed company may trade on the São Paulo Stock Exchange, in most cases fewer than half of the listed shares are actually available for trading by the public. The remaining shares are often held by a single or small group of controlling persons or by governmental entities.

Trading on the São Paulo Stock Exchange by a holder not deemed to be domiciled in Brazil for Brazilian tax and regulatory purposes, or a non-Brazilian holder, is subject to certain limitations under Brazilian foreign investment regulations. With limited exceptions, non-Brazilians holders may trade on the São Paulo Stock Exchange only in accordance with the requirements of Resolution No. 2,689 of January 26, 2000 of the National Monetary Council. Resolution No. 2,689 requires securities held by non-Brazilian holders to be maintained in the custody of, or in deposit accounts with, financial institutions that are authorized by the Central Bank and the Brazilian Securities Commission. In addition, Resolution No. 2,689 requires non-Brazilian holders to restrict their securities trading to transactions on the São Paulo Stock Exchange or organized over-the-counter markets. With limited exceptions, non-Brazilian holders may not transfer the ownership of investments made under Resolution No. 2,689 to other non-Brazilian holders through private transactions. See Item 10. Additional Information Regulation of Foreign Investment.

**Regulation of Brazilian Securities Markets**

The Brazilian securities markets are regulated by the Brazilian Securities Commission, which has authority over stock exchanges and the securities markets generally, by the National Monetary Council and by the Central Bank, which has, among other powers, licensing authority over brokerage firms and which regulates foreign investment and foreign exchange transactions. The Brazilian securities market is governed by Brazilian Law No. 6,385/76, as amended, and by the Brazilian Corporation Law and other Brazilian Securities Commission rulings and regulations.

Under the Brazilian Corporation Law, a company may be either public (*companhia aberta*), as we are, or closely held (*companhia fechada*). All public companies are registered with the Brazilian Securities Commission and are subject to periodic reporting requirements. A company registered with the Brazilian Securities Commission may have its securities traded on the Brazilian stock exchanges or in the Brazilian over-the-counter market. The shares of a listed company, like those of our company, also may be traded privately subject to certain limitations.

The Brazilian over-the-counter market consists of direct trades between persons in which a financial institution registered with the Brazilian Securities Commission serves as intermediary. No special application, other than registration with the Brazilian Securities Commission, is necessary for securities of a public company to be traded in this market. The Brazilian Securities Commission must receive notice of all trades carried out in the Brazilian over-the counter market by the respective intermediaries.

Trading of a company s securities on the São Paulo Stock Exchange may be suspended in anticipation of a material announcement. A company must also suspend trading of its securities on international stock exchanges on which its securities are traded. Trading may also be suspended by a Brazilian stock exchange or the Brazilian Securities Commission, among other reasons, based on or due to a belief that a company has provided inadequate information regarding a material event or has provided inadequate responses to an inquiry by the Brazilian Securities Commission or the relevant stock exchange.

Brazilian Law No. 6,385/76, as amended, the Brazilian Corporation Law and regulations issued by the Brazilian Securities Commission provide for, among other things, disclosure obligations, restrictions on insider trading and price manipulation and protections for minority shareholders. However, the Brazilian securities markets are not as highly regulated and supervised as securities markets in the United States and some other jurisdictions. In addition, rules and policies against self-dealing or for preserving shareholder interests may be less well-defined and enforced in Brazil than in the United States, which may put holders of our class A preferred shares and the ADSs at a disadvantage. Corporate disclosures also may be less complete than for public companies in the United States and certain other jurisdictions.

***São Paulo Stock Exchange Corporate Governance Standards***

On December 11, 2000, the São Paulo Stock Exchange launched three new listing segments:

- Corporate Governance Level 1;
- Corporate Governance Level 2; and
- The New Market (*Novo Mercado*) of the São Paulo Stock Exchange.

These new listing segments have been designed for the trading of shares issued by companies that voluntarily undertake to abide by corporate governance practices and disclosure requirements in addition to those already required under the Brazilian Corporation Law. The inclusion of a company in any of the new segments requires adherence to a series of corporate governance rules. These rules are designed to increase shareholders rights and enhance the quality of information provided by Brazilian corporations.

On February 13, 2003, we agreed to comply with Level 1. In becoming a Level 1 company, we agreed to:

- ensure that shares representing 25% of our total share capital are available for trading;
- adopt offering procedures that favor widespread ownership of shares whenever making a public offering;
- comply with minimum quarterly disclosure standards;
- follow stricter disclosure policies with respect to transactions involving our securities made by our controlling shareholder and our directors and executive officers;
- disclose any existing shareholders agreements and stock option plans; and
- make a schedule of corporate events available to our shareholders.

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To become a Level 2 company, a company must agree to the following additional provisions:

- have a board of directors consisting of at least five members; at least 20% of whom will be independent, as defined in the Level 2 regulations;

- confer upon preferred shares the right to vote on at least the following issues: (1) transformation, merger, consolidation or spin-off of the company; (2) approval of transactions between the company and its controlling shareholder and/or related parties, whenever such matter is subject to authorization at a general meeting of shareholders pursuant to law or under the company s by-laws; (3) appraisal of assets contributed to pay the company s capital increases; (4) selection of a specialized company in charge of determining the company s economic value for delisting purposes; and (5) amendment to or revocation of any provisions contained in the company s by-laws, whenever such acts alter or modify any requirements set forth in the São Paulo Stock Exchange regulations;

- offer tag-along rights to minority shareholders (meaning that upon the acquisition of a controlling interest, the purchaser must also agree to purchase the shares of the company s minority shareholders in an amount equivalent to 100% of the price paid for each share in the controlling stake, in the case of holders of common shares, and at least 80% of the price paid for each share in the controlling stake, in the case of holders of preferred shares);

- conduct a tender offer at fair market value in the event of a delisting of shares or termination of Level 2 registration;

- present an annual balance sheet prepared in accordance with, or reconciled to, U.S. GAAP or international financial reporting standards;

- establish a two-year term for all members of the board of directors; and

- resolve corporate conflicts with or among the company s shareholders through arbitration.

To be a company listed on the New Market, a company must have its share capital composed exclusively of common shares in addition to meeting the Level 1 and the Level 2 requirements. We have no current plans to propose to amend our share capital structure to provide solely for the issuance of common shares.

## ITEM 10. ADDITIONAL INFORMATION

### Description of Our Company s Bylaws

The following is a summary of the material provisions of our by-laws and of the Brazilian Corporation Law. In Brazil, a company s by-laws (e*statuto social*) is the principal governing document of a corporation (*sociedade anônima*).

### General

Our registered name is Braskem S.A., and our registered office is located in the Municipality of Camaçari, State of Bahia, Brazil. Our registration number with the Brazilian Commercial Registry is No. 29300006939. We have been duly registered with the Brazilian Securities Commission under No. 4820 since December 18, 1978. Our principal place of business is in the Municipality of Camaçari, State of Bahia, Brazil. Our company has a perpetual existence.

At June 22, 2006, we have outstanding share capital of R$3,508,271,820.78, equal to 370,402,346 total outstanding shares consisting of 123,492,142 outstanding common shares, 246,107,138 outstanding class A preferred shares and 803,066 outstanding class B preferred shares, including 4,470,947 class A preferred shares held in treasury. All of our outstanding share capital is fully paid. All of our shares are without par value. Under the Brazilian Corporation Law, the aggregate number of our non-voting and limited voting class A and class B preferred shares may not exceed two-thirds of our total outstanding share capital.

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**Corporate Purposes**

Article 2 of our by-laws establishes our corporate purposes to include:

the manufacture, trading, import and export of chemical and petrochemical products;

the production of utilities for use by component companies of the Northeastern Complex, including the supply of steam, water, compressed air, industrial gases, electric power, as well as the provision of various services to these companies;

the holdings of equity stakes (quotas or shares) in other companies; and

the manufacture, distribution, sale, import and export of gasoline, diesel oil, LPG and other oil derivatives.

**Board of Directors**

Under the Brazilian Corporation Law, any matters subject to the approval of our board of directors can be approved by a simple majority of votes of the members present at a duly convened meeting, unless our by-laws otherwise specify. Under our by-laws, our board of directors may only deliberate if a majority of its members are present at a duly convened meeting. Any resolutions of our board of directors may be approved by the affirmative vote of a majority of the members present at the meeting, subject to veto rights of Petroquisa, PETROS and PREVI over resolutions of our board of directors relating to certain matters under the Petroquisa memorandum of understanding and the Pension Funds memorandum of understanding. See Item 7. Major Shareholders and Related Party Transactions Major Shareholders Shareholders Agreements Petroquisa Memorandum of Understanding and Pension Funds Memorandum of Understanding.

***Election of Directors***

The majority of the members of our board of directors are elected by the Odebrecht Group. In addition, any director appointed by a shareholder pursuant to a shareholders agreement is bound by the terms of such agreement. See Item 7. Major Shareholders and Related Party Transactions Major Shareholders Shareholders Agreements.

The members of our board of directors are elected at general meetings of shareholders for concurrent two-year terms.

***Qualification of Directors***

The Brazilian Corporation Law requires members of our board of directors to own shares of our company. However, there is no minimum share ownership or residency requirement to q