

Mangels Industrial S.A. and Subsidiaries

**Consolidated Financial Statements at
31 December 2005
and Report of the Auditors**

Report of the Auditors

To the Shareholders and the Board of Directors
Mangels Industrial S.A.

We have audited the accompanying consolidated balance sheet of Mangels Industrial S.A. ("Mangels") and its subsidiaries (together, the "Group") as of 31 December 2005 and the related consolidated statements of income, cash flows and changes in shareholders' equity for the year then ended. These financial statements are the responsibility of Mangels' management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2005, and of the results of its operations and cash flows for the year then ended in accordance with International Financial Reporting Standards.

São Paulo, 1 June 2006

PricewaterhouseCoopers
Auditores Independentes
CRC 2SP000160/O-5

Paulo Cesar Estevão Netto
Contador CRC 1RJ026365/O-8 "T" SP

**Mangels Industrial S.A.
and Subsidiaries**

**Consolidated Balance Sheets
At 31 December
In thousands of reais**

Assets	Note	2005	2004
Non-current assets			
Property, plant and equipment	6	192,368	174,411
Intangible assets	7	3,299	892
Taxes recoverable	8	5,104	10,480
Judicial deposits	9	12,465	12,090
Notes receivable			1,189
		<u>213,236</u>	<u>199,062</u>
Current assets			
Taxes recoverable	8	24,940	23,233
Inventories	10	75,170	84,816
Notes receivable		206	1,729
Trade receivables	11	79,099	65,720
Cash and cash equivalents	12	57,319	63,170
Other		11,776	11,653
		<u>248,510</u>	<u>250,321</u>
Total assets		<u><u>461,746</u></u>	<u><u>449,383</u></u>

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

**Mangels Industrial S.A.
and Subsidiaries**

**Consolidated Balance Sheets
At 31 December
In thousands of Reais**

(continued)

Shareholders' equity	Note	2005	2004
Capital	13	79,360	79,360
Revenue reserves	13	<u>91,501</u>	<u>82,079</u>
Total shareholders' equity		<u>170,861</u>	<u>161,439</u>
Liabilities			
Non-current liabilities			
Borrowings	14	127,056	79,762
Taxes payable	15	20,241	18,818
Deferred taxes	16	8,664	8,624
Provisions for contingent liabilities	9	<u>24,890</u>	<u>29,735</u>
		<u>180,851</u>	<u>136,939</u>
Current liabilities			
Borrowings	14	55,199	69,312
Taxes payable	15	5,699	7,767
Trade and other payables	17	30,934	56,363
Salaries and payroll charges	18	7,836	7,555
Other		<u>10,366</u>	<u>10,008</u>
		<u>110,034</u>	<u>151,005</u>
Total liabilities		<u>290,885</u>	<u>287,944</u>
Total shareholders' equity and liabilities		<u><u>461,746</u></u>	<u><u>449,383</u></u>

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

**Mangels Industrial S.A.
and Subsidiaries**

**Consolidated Income Statements
Years Ended 31 December
In thousands of Reais**

	<u>Note</u>	<u>2005</u>	<u>2004</u>
Net sales		520,110	504,667
Cost of sales	19	<u>(410,354)</u>	<u>(367,063)</u>
Gross profit		<u>109,756</u>	<u>137,604</u>
Other operating income and expenses, net	20	6,504	6,821
Selling and marketing costs	19	(35,256)	(38,651)
Administrative expenses	19	(41,666)	(40,955)
Other operating expenses	19	<u>(104)</u>	<u>(8,645)</u>
Operating profit		<u>39,234</u>	<u>56,174</u>
Finance costs	21	<u>(22,559)</u>	<u>(30,912)</u>
Profit before income taxes		<u>16,675</u>	<u>25,262</u>
Income tax expense	16	<u>(4,272)</u>	<u>(6,942)</u>
Profit for the year		<u>12,403</u>	<u>18,320</u>
Attributable to			
Equity holders of Mangels		<u>12,403</u>	<u>18,320</u>
Earnings per share for profit attributable to the equity holders of Mangels during the year (expressed in R\$ per share - basic and diluted)	22	<u>1.26</u>	<u>1.86</u>

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

**Mangels Industrial S.A.
and Subsidiaries**

Consolidated Statements of Changes in Shareholders' Equity
In thousands of Reais

		<u>Revenue reserves</u>				
	<u>Note</u>	<u>Shared capital</u>	<u>Special reserve</u>	<u>Legal reserve</u>	<u>Retained earnings</u>	<u>Total equity</u>
At 1 January 2004		79,360	67,858	736		147,954
Increase of legal reserve				957	(957)	
Profit for the year					18,320	18,320
Dividend relating to 2004 (minimum mandatory dividend)	13				(4,835)	(4,835)
Transfer to special reserve	13		12,528		(12,528)	
At 31 December 2004		<u>79,360</u>	<u>80,386</u>	<u>1,693</u>		<u>161,439</u>
Adoption of IAS 32 and 39	5 (b)(v)				(26)	(26)
At 1 January 2005		<u>79,360</u>	<u>80,386</u>	<u>1,693</u>	(26)	161,413
Increase of legal reserve				603	(603)	
Profit for the year					12,403	12,403
Dividend relating to 2005 (minimum mandatory dividend)	13				(2,955)	(2,955)
Transfer to special reserve	13		8,819		(8,819)	
At 31 December 2005		<u>79,360</u>	<u>89,205</u>	<u>2,296</u>		<u>170,861</u>

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

**Mangels Industrial S.A.
and Subsidiaries**

Consolidated Statements of Cash Flows
Years Ended 31 December
In thousands of Reais

	<u>Note</u>	<u>2005</u>	<u>2004</u>
Cash flow from operating activities			
Cash generated from operations	23	(14,011)	19,111
Interest paid		(8,941)	(10,356)
Income tax paid		(4,111)	(7,363)
Net cash generated from/(used in) operating activities		<u>(27,063)</u>	<u>1,392</u>
Cash flows from investing activities			
Purchases of property, plant and equipment (PPE)	6	(32,473)	(16,467)
Purchases of intangible assets	7	(2,687)	
Net cash used in investing activities		<u>(35,160)</u>	<u>(16,467)</u>
Cash flows from financing activities			
Proceeds from borrowings		118,066	126,276
Repayments of borrowings		(63,261)	(102,596)
Dividends paid		(4,835)	(1,880)
Other long-term rights and obligations		6,470	3,469
Net cash generated from financing activities		<u>56,440</u>	<u>25,269</u>
Net (decrease)/increase in cash and cash equivalents		(5,783)	10,194
Cash and cash equivalents at beginning of the year		63,170	53,254
Exchange gains/(losses) on cash and cash equivalents		(68)	(278)
Cash, cash equivalents and bank overdrafts at end of the year	12	<u><u>57,319</u></u>	<u><u>63,170</u></u>

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

Mangels Industrial S.A. and Subsidiaries

Notes to the Consolidated Financial Statements at 31 December 2005 and 2004 In thousands of Reais

1 Operations

Mangels Industrial S.A. ("Mangels") and its subsidiaries (together the "Group") are engaged mainly in the production of steel strips and stamped steel pieces, liquid petroleum gas (LPG) containers and combustion air tanks for buses and trucks, steel and aluminum automotive wheels. They also render re-qualification services for LPG containers and galvanizing services on steel artifacts.

The Group's main office is located in São Paulo - Brazil.

These consolidated financial statements were approved for issue on 1 June 2006.

2 Summary of significant accounting policies

(a) Basis of preparation

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards - IFRS. These are the first IFRS financial statements prepared by the Group, which has applied IFRS 1, First-time Adoption of International Financial Reporting Standards.

The policies set out below have been consistently applied to all the years presented, except for those relating to the classification and measurement of financial instruments. The Group has made use of the exemption available under IFRS 1 to only apply IAS 32 and IAS 39 from 1 January 2005. The policies applied to financial instruments for 2004 and 2005 are disclosed separately below.

Mangels' consolidated financial statements prepared in accordance with the generally accepted accounting principles in Brazil ("BRGAAP") through 31 December 2004, BRGAAP differs in some aspects from IFRS.

In preparing these consolidated financial statements, management has amended certain accounting and valuation methods applied in the BRGAAP financial statements to comply with IFRS. The comparative figures in respect of 2004 were adjusted to reflect these accounting policies, except as described otherwise.

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Reconciliations and descriptions of the effect of the transition from BRGAAP to IFRS on the Group's equity and its profit are provided in Note 5.

These consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation at fair value of property, plant and equipment (Note 6), available for sale financial assets and financial assets and liabilities at fair value through the income statement (Note 2(h)).

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Group's accounting policies. The areas involving a higher degree of judgment or complexity, or where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4 (Accounting estimates and judgments).

(i) Standards, interpretations and amendments that are not yet effective

Certain new standards, amendments and interpretations to existing standards have been published that are mandatory for the Group's accounting periods beginning on or after 1 January 2006 or later periods, which the Group has not early adopted, as follows:

- **IAS 19 (Amendment), Employee Benefits (effective from 1 January 2006).** This amendment introduces the option of an alternative recognition approach for actuarial gains and losses. It may impose additional recognition requirements for multi-employer plans where insufficient information is available to apply defined benefit accounting. It also adds new disclosure requirements. The Group does not currently sponsor any post-retirement benefit plan to which this amended standard should be applied.
- **IAS 39 (Amendment), Cash Flow Hedge Accounting of Forecast Intragroup Transactions (effective from 1 January 2006).** The amendment allows the foreign currency risk of a highly probable forecast intragroup transaction to qualify as a hedged item in the consolidated financial statements, provided that: (a) the transaction is denominated in a currency other than the functional currency of the entity entering into that transaction; and (b) the foreign currency risk will affect the consolidated statement of income. This amendment is not relevant to the Group's consolidated financial statements, as the Group does not apply hedge accounting.

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- . **IAS 39 (Amendment), The Fair Value Option (effective from 1 January 2006).** This amendment changes the definition of financial instruments classified at fair value through the income statement and restricts the ability to designate financial instruments as part of this category. The Group believes that this amendment should not have a significant impact on the classification of financial instruments, as the Group should be able to comply with the amended criteria for the designation of financial instruments at fair value through the income statement. The Group does not, currently, designate any financial instrument as at fair value through the income statement. This amendment is not relevant to the Group's consolidated financial statements.

- . **IAS 39 and IFRS 4 (Amendment), Financial Guarantee Contracts (effective from 1 January 2006).** This amendment requires issued financial guarantees, other than those previously asserted by the entity to be insurance contracts, to be initially recognized at their fair value, and subsequently measured at the higher of (a) the unamortized balance of the related fees received and deferred, and (b) the expenditure required to settle the commitment at the balance sheet date. Management considered this amendment to IAS 39 and concluded that it is not relevant to the Group.

- . **IFRS 1 (Amendment), First-time Adoption of International Financial Reporting Standards and IFRS 6 (Amendment), Exploration for and Evaluation of Mineral Resources (effective from 1 January 2006).** These amendments are not relevant to the Group's operations, as the Group does not carry out exploration for and evaluation of mineral resources.

- . **IFRS 6, Exploration for and Evaluation of Mineral Resources (effective from 1 January 2006).** IFRS 6 is not relevant to the Group's operations.

- . **IFRS 7, Financial Instruments: Disclosures, and complementary amendment to IAS 1, Presentation of Financial Statements - Capital Disclosures (effective from 1 January 2007).** IFRS 7 introduces new disclosures to improve the information about financial instruments. It requires the disclosure of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk and market risk, including sensitivity analysis to market risk. It replaces IAS 30, Disclosures in the Financial Statements of Banks and Similar Financial Institutions, and disclosure requirements in IAS 32, Financial Instruments: Disclosure and Presentation. It is applicable to all entities that report under IFRS. The amendment to IAS 1 introduces disclosures about the level of an entity's capital and how it manages capital. The Group assessed the impact of IFRS 7 and the amendment to IAS 1 and concluded that the main additional disclosures will be the sensitivity analysis to market risk and the capital disclosures required by the amendment of IAS 1. The Group will apply IFRS 7 and the amendment to IAS 1 from annual periods beginning 1 January 2007.

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- . **IFRIC 4, Determining whether an Arrangement contains a Lease (effective from 1 January 2006).** IFRIC 4 requires the determination of whether an arrangement is or contains a lease to be based on the substance of the arrangement. It requires an assessment of whether: (a) fulfillment of the arrangement is dependent on the use of a specific asset or assets; and (b) the arrangement conveys a right to use the asset. Management is currently assessing the impact of IFRIC 4 on the Group's operations.

- . **IFRIC 5, Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds (effective from 1 January 2006).** Decommission, restoration and environmental rehabilitation funds are investment funds established to segregate assets to fund some or all of the costs of decommissioning plant or certain equipment, or in undertaking environmental rehabilitation. IFRIC 5 determines that assets arising from interests in these funds should be accounted for under IAS 27, IAS 28 or IAS 31 separately from the obligations to pay decommission costs, which should be accounted for under IAS 37. Management considered this interpretation and concluded that it is not relevant to the Group.

- . **IFRIC 6, Liabilities arising from Participating in a Specific Market - Waste Electrical and Electronic Equipment (effective from 1 December 2005).** IFRIC 6 is not relevant to the Group's operations.

(b) Foreign currency translation

(i) Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The consolidated financial statements are presented in Brazilian Reais, which is Mangels' functional and presentation currency.

(ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the statement of income.

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Notes to the Consolidated Financial Statements at 31 December 2005 and 2004 In thousands of Reais

(iii) Group companies

The results and financial position of all the group entities (none of which operating in a hyperinflationary economy) that have a functional currency different from the presentation currency, generally the local currency of the countries where Mangels' subsidiaries operate (which are: Brazilian Reais - R\$ and U.S. dollars - US\$), are translated into the presentation currency as follows:

- . Assets and liabilities are translated at the closing rate at each balance sheet date.
- . Income and expenses are translated at average exchange rates (unless the average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions).
- . Equity accounts have been translated into Reais at the closing rate at the balance sheet date.

Net translation gains or losses resulting from the translation are recorded directly in shareholders' equity under Cumulative Translation Adjustment - CTA.

On consolidation, exchange differences arising from the translation of the net investment in foreign operations, and of borrowings and other currency instruments designated as hedges of such investments, are taken to shareholders' equity. When a foreign operation is sold, exchange differences that were recorded in equity are recognized in the statement of income as part of the gain or loss on sale.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

The Group does not apply hedge accounting and has not recognized any amount of goodwill in connection with transactions it has entered into to date.

(c) Consolidation

Subsidiaries are all entities (including special purpose entities) over which the Group has the power to govern the financial and operating policies, generally involving a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that

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are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

Inter-company transactions, balances and unrealized gains on transactions between Group companies are eliminated. Unrealized losses are also eliminated unless the transaction provides evidence of impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

All of the subsidiaries included within these consolidated financial statements are wholly owned by the Group. The Group does not hold equity investment in any other entity.

(d) Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments.

(e) Property, plant and equipment

Property, plant and equipment are carried at fair value, less accumulated depreciation, which is computed on the straight-line method using rates based on the estimated useful lives of such assets. Fair value is determined on the basis of independent experts valuations carried out regularly.

Subsequent costs are included in the assets' carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the statement of income during the financial period in which they are incurred.

Depreciation is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, as follows:

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Notes to the Consolidated Financial Statements at 31 December 2005 and 2004 In thousands of Reais

	<u>Years</u>
Furniture, fittings and equipment	10
Vehicles	5
Buildings	25
Machinery	10-15

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 3(g)).

Gains and losses on disposals are determined by comparing the proceeds with the respective carrying amount. These are included in the income statement.

(f) Intangible assets - computer software

Acquired computer software licenses are capitalized on the basis of the costs incurred to acquire the specific software and bring it to use. These costs are amortized over their estimated useful lives (not exceeding five years).

Costs associated with developing or maintaining computer software programs are recognized as an expense as incurred. Mangels does not have internally developed software.

(g) Impairment of non-financial assets

Assets that have an indefinite useful life are not subject to amortization and are tested annually for impairment. Assets that are subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value, less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units).

Mangels Industrial S.A. and Subsidiaries

Notes to the Consolidated Financial Statements at 31 December 2005 and 2004 In thousands of Reais

(h) Financial assets

(i) From 1 January 2005

The Group classifies its financial assets in the following categories: at fair value through the income statement, loans and receivables, and available for sale. The classification depends on the purpose for which the financial assets were acquired and management's ability to keep the acquired assets. Management determines the classification of its financial assets at initial recognition and re-evaluates this designation at every reporting date.

(ii) From 1 January to 31 December 2004

Financial assets are carried at cost or amortized cost, net of impairment losses. Gains and losses are taken directly to the income statement.

Financial assets at fair value through the income statement

This category has two sub-categories: financial assets held for trading, and those designated at fair value through the income statement at inception. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management. Derivatives are also classified as held for trading, unless they are designated as hedges. Assets in this category are classified as current assets if they are either held for trading or are expected to be realized within twelve months of the balance sheet date.

The Group did not held derivatives during the financial years ended on 31 December 2005 and 2004.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than twelve months after the balance sheet date. These are classified as non-current assets. Loans and receivables are classified as "trade receivables" (Note 11) in the balance sheet.

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Notes to the Consolidated Financial Statements at 31 December 2005 and 2004 In thousands of Reais

Available-for-sale financial assets

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets, unless management intends to dispose of the investment within 12 months of the balance sheet date.

(i) Trade receivables

Trade receivables are initially recognized at fair value and subsequently measured at amortized cost, using the effective interest method, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables.

Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganization, and default or delinquency in payments are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the effective interest rate. The amount of the provision is recognized in the statement of operations within 'selling and marketing costs'.

(j) Cash and cash equivalents

Cash and cash equivalents include cash in hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities on the balance sheet.

(k) Share capital

Common and preferred shares that have no redeemable features are classified as equity. Incremental costs directly attributable to the issue of new shares or warrants are shown in equity as a deduction, net of tax, from the proceeds.

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Notes to the Consolidated Financial Statements at 31 December 2005 and 2004 In thousands of Reais

(l) Borrowings

Borrowings are recognized initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortized cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognized in the income statement over the period of the borrowings, using the effective interest method.

Borrowings are classified as current liabilities, unless the Group has an unconditional right to defer settlement of the liability for at least twelve months after the balance sheet date.

(m) Deferred income tax

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred income tax is not accounted for if it arises from the initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction does not affect either accounting or taxable income.

Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

Deferred income tax assets are recognized to the extent that it is probable that future taxable profit will be available against which the tax losses or temporary differences can be utilized.

(n) Provisions

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognized even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognized as interest expense.

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Notes to the Consolidated Financial Statements at 31 December 2005 and 2004 In thousands of Reais

(o) Revenue recognition

Revenue comprises the fair value of the consideration received or receivable for the sale of goods and services in the ordinary course of the Group's activities. Revenue is shown net of value-added tax, returns, rebates and discounts and after eliminated sales within the Group.

Revenue is recognized as follows:

(i) Sale of goods

Sales of goods are recognized when a Group entity sells a product to the customer.

It is the Group's policy to sell its products to the end customer with a right of return. Accumulated experience is used to estimate and provide for such returns at the time of sale.

(ii) Sale of services

Sales of services are recognized in the accounting period in which the services are rendered, by reference to completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided. When a specific act is much more significant than any other acts, the recognition of revenue is postponed until the significant act is executed.

(iii) Interest income

Interest income is recognized on a time-proportion basis, using the effective interest method and is presented as other operating income in the income statement. When a receivable is impaired, the Group reduces the carrying amount to its recoverable amount, being the estimated future cash flow, discounted at original effective interest rate of the instrument, and continues unwinding the discount as interest income. Interest income on impaired loans is recognized using the original effective interest rate.

(p) Dividend distribution

Dividend distribution to Mangels' shareholders is recognized as a liability in the Group's financial statements in the period in which the dividends are approved by Mangels' shareholders. At the end of each year a liability for the minimum mandatory dividends is recognized in the balance sheet.

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Notes to the Consolidated Financial Statements at 31 December 2005 and 2004 In thousands of Reais

(q) Risks and uncertainties

The operations of Mangels are subject to certain risks and uncertainties, including amongst others, those associated with: the ability to meet obligations; losses and negative cash flows; funding expansion; managing growth and expansion; suppliers; competition; technology trends and evolving industry standards.

(r) Advertising costs

Advertising costs are expensed as incurred. Advertising expenses amounted to R\$ 2,138 and R\$ 1,140 for the years ended 31 December 2005 and 2004, respectively.

3 Financial risk management

(a) Financial risk factors

The Group's activities expose it to a variety of financial risks: market risk (including currency risk, fair value interest rate risk and price risk), credit risk, liquidity risk and cash flow interest rate risk. The Group's overall risk management program focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the Group's financial performance. The Group rarely uses derivative financial instruments to hedge risk exposures.

Risk management is carried out by a central treasury department (Group Treasury), under policies approved by the Board of Directors. Group Treasury identifies, evaluates and hedges financial risks in close co-operation with the Group's operating units. The Board provides written principles for overall risk management, as well as written policies covering specific areas, such as foreign exchange risk, interest rate risk, credit risk, use of derivative financial instruments and non-derivative financial instruments, and investment of excess liquidity.

(i) Market risks

(i.1) Foreign exchange risk

The Group operates internationally and is exposed to foreign exchange risk arising from certain currency exposures, primarily with respect to the U.S. dollar and the Euro. Foreign exchange risk arises from future commercial transactions, recognized assets and liabilities and net investments in foreign operations.

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Notes to the Consolidated Financial Statements at 31 December 2005 and 2004 In thousands of Reais

Entities in the Group use export advances contracts to manage their foreign exchange risk arising from future commercial transactions, recognized assets and liabilities. Foreign exchange risk arises when future commercial transactions, recognized assets and liabilities are denominated in a currency that is not the entity's functional currency. Group Treasury is responsible for managing the net position in each foreign currency.

(i.2) Price risk

Mangels is exposed to commodity price risk related to the aluminum purchases.

(ii) Credit risk

The Group has no significant concentrations of credit risk. It has policies in place to ensure that sales of products are made to a large number of customers, internationally dispersed and who have an appropriate credit history. The Group has policies that limit the amount of credit exposure to any financial institution.

(iii) Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash and marketable securities, the availability of funding through an adequate amount of committed credit facilities and the ability to close out market positions. Due to the dynamic nature of the underlying businesses, Group Treasury aims to maintain flexibility in funding by keeping committed credit lines available.

(iv) Cash flow and fair value interest rate risk

The Group's income and operating cash flows are relatively independent of changes in market interest rates. The Group's fair value interest rate risk arises from long-term borrowings. Borrowings issued at variable rates expose the Group to cash flow interest rate risk. Borrowings issued at fixed rates expose the Group to fair value interest rate risk. Management determines and monitors position limits to manage these risks.

(b) Fair value estimation

The fair values of quoted financial instruments are based on current bid prices. The fair value of financial instruments that are not traded in an active market (Time Deposits) is determined by using valuation techniques. The Group uses a variety of methods and makes assumptions that

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are based on market conditions existing at each balance sheet date. Quoted market prices or dealer quotes for similar instruments are used for long-term debt. Other techniques, such as estimated discounted cash flows, are used to determine fair value for the remaining financial instruments.

The nominal value less impairment provision of trade receivables and payables are assumed to approximate their fair values. The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Group for similar financial instruments.

4 Accounting estimates and judgments

Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results.

5 Transition to IFRS

(a) Basis of transition to IFRS

(i) Application of IFRS 1

The Group has applied IFRS 1 in preparing these consolidated financial statements for the year ended 31 December 2005, which are the first annual financial statements that comply with IFRS.

Mangels' transition date is 1 January 2004. The Group prepared its opening IFRS balance sheet at that date. The Group's IFRS adoption date is 1 January 2005.

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In preparing these consolidated financial statements in accordance with IFRS 1, the Group has applied the mandatory exceptions and certain of the optional exemptions from full retrospective application of IFRS.

(ii) Exemption from full retrospective application elected by the Group

In determining the cost of property, plant and equipment for the IFRS opening balance sheet at 1 January 2004, Mangels applied the optional exemption allowed for in IFRS 1 from full retrospective application and adopted the revaluation amounts stated in the report issued by independent experts, dated 31 December 2003. Such amounts are also reflected in Mangels' statutory financial statements.

(iii) Exceptions from full retrospective application followed by the Group

The preparation of the consolidated IFRS financial statements fully complies with the requirements of IFRS 1 that sets forth the circumstances under which the retroactive application of the standards is not permitted.

(b) Reconciliations between IFRS and BRGAAP

The following reconciliations provide a quantification of the effects of the transition to IFRS and an overview of the impact on equity of the transition at 1 January 2004 and 31 December 2004, and, on the income and cash flows for the year ended 31 December 2004.

A reconciliation is also presented to provide quantification of the effect of the adoption of IAS 32 and IAS 39 on equity, at 1 January 2005.

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(i) Reconciliation of equity on 1 January 2004

Assets	Note	BR GAAP	Effect of transition to IFRS	IFRS
Non-current assets				
Property, plant and equipment		175,873		175,873
Intangibles assets		941		941
Deferred taxes	(c.iv)	13,900	157	14,057
Judicial deposits		11,566		11,566
Notes receivable		3,779		3,779
Other		1,783		1,783
		<u>207,842</u>	<u>157</u>	<u>207,999</u>
Current assets				
Taxes recoverable		20,715		20,715
Inventories	(c.ii)	50,698	(204)	50,494
Notes receivable		8,616		8,616
Trade receivables	(c.ii/vii)	38,873	12,162	51,035
Cash and cash equivalents		53,254		53,254
Other		1,854		1,854
		<u>174,010</u>	<u>11,958</u>	<u>185,968</u>
Total assets		<u><u>381,852</u></u>	<u><u>12,115</u></u>	<u><u>393,967</u></u>

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	<u>Note</u>	<u>BR GAAP</u>	<u>Effect of transition to IFRS</u>	<u>IFRS</u>
Shareholders' equity				
Capital		79,360		79,360
Revaluation reserve	(c.iii)	59,071	(59,071)	
Revenue reserves		<u>18,173</u>	<u>50,117</u>	<u>68,290</u>
Total shareholders' equity		<u>156,604</u>	<u>(8,954)</u>	<u>147,650</u>
Non-current liabilities				
Borrowings		54,086		54,086
Taxes payable		12,762		12,762
Deferred taxes	(c.iii)	18,231	8,650	26,881
Provision for contingent liabilities		<u>20,960</u>		<u>20,960</u>
		<u>106,039</u>	<u>8,650</u>	<u>114,689</u>
Current liabilities				
Borrowings	(c.vii)	64,697	12,623	77,320
Taxes payable		4,159		4,159
Trade and other payables	(c.ii)	36,931	(204)	36,727
Salaries and payroll charges		6,129		6,129
Other		<u>7,293</u>		<u>7,293</u>
		<u>119,209</u>	<u>12,419</u>	<u>131,628</u>
Total liabilities		<u>225,248</u>	<u>21,069</u>	<u>246,317</u>
Total shareholders' equity and liabilities		<u><u>381,852</u></u>	<u><u>12,115</u></u>	<u><u>393,967</u></u>

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(ii) Reconciliation of equity on 31 December 2005

	<u>Note</u>	<u>BR GAAP</u>	<u>Effect of transition to IFRS</u>	<u>IFRS</u>
Assets				
Non-current assets				
Property, plant and equipment		192,368		192,368
Intangible assets		3,299		3,299
Taxes recoverable		5,104		5,104
Deferred taxes	(c.iv/viii)	11,463	4,117	15,580
Judicial deposits		12,465		12,465
		<u>224,699</u>	<u>4,117</u>	<u>228,816</u>
Current assets				
Deferred taxes	(c.viii)	3,857	(3,857)	
Taxes recoverable		24,940		24,940
Inventories	(c.ii)	75,455	(285)	75,170
Notes receivable		206		206
Trade receivables	(c.ii/vii)	69,023	10,076	79,099
Cash and cash equivalents		57,389	(70)	57,319
Other		11,776		11,776
		<u>242,646</u>	<u>5,864</u>	<u>248,510</u>
Total assets		<u><u>467,345</u></u>	<u><u>9,981</u></u>	<u><u>477,326</u></u>

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	Note	BR GAAP	Effect of transition to IFRS	IFRS
Shareholders' equity				
Capital		79,360		79,360
Revaluation reserve		55,449	(55,449)	
Revenue reserves	(c.iii)	<u>45,208</u>	<u>46,293</u>	<u>91,501</u>
Total shareholders' equity		<u>180,017</u>	<u>(9,156)</u>	<u>170,861</u>
Non-current liabilities				
Borrowings		127,056		127,056
Taxes payable		20,241		20,241
Deferred taxes	(c.iii)	15,594	8,650	24,244
Provision for contingent liabilities		<u>24,890</u>		<u>24,890</u>
		<u>187,781</u>	<u>8,650</u>	<u>196,431</u>
Current liabilities				
Borrowings	(c.vii)	44,427	10,772	55,199
Taxes payable		5,699		5,699
Trade and other payables	(c.ii)	31,219	(285)	30,934
Salaries and payroll charges		7,836		7,836
Other		<u>10,366</u>		<u>10,366</u>
		<u>99,547</u>	<u>10,487</u>	<u>110,034</u>
Total liabilities		<u>287,328</u>	<u>19,137</u>	<u>306,465</u>
Total shareholders' equity and liabilities		<u><u>467,345</u></u>	<u><u>9,981</u></u>	<u><u>477,326</u></u>

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**(iii) Reconciliation of income statement for the year
ended 31 December 2005**

	<u>Note</u>	<u>BR GAAP</u>	<u>Effect of transition to IFRS</u>	<u>IFRS</u>
Sales	(c.ii)	520,806	(696)	520,110
Cost of sales		<u>(410,354)</u>		<u>(410,354)</u>
Gross profit		<u>110,452</u>	<u>(696)</u>	<u>109,756</u>
Other operating income, net	(c.ix/vi))		6,504	6,504
Selling and marketing costs		(35,256)		(35,256)
Administrative expenses		(41,666)		(41,666)
Other operating expenses		<u>(104)</u>		<u>(104)</u>
Operating profit		<u>33,426</u>	<u>5,808</u>	<u>39,234</u>
Finance costs	(c.ix)	(18,690)	(3,869)	(22,559)
Non-operating income	(c.vi)	<u>1,441</u>	<u>(1,441)</u>	
Profit before income taxes		<u>16,177</u>	<u>498</u>	<u>16,675</u>
Income tax expense	(c.iv)	<u>(4,111)</u>	<u>(161)</u>	<u>(4,272)</u>
Profit for the year		<u><u>12,066</u></u>	<u><u>337</u></u>	<u><u>12,403</u></u>

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**(iv) Reconciliation of cash flows for the year
ended 31 December 2005**

	<u>Note</u>	<u>BR GAAP</u>	<u>Effect of transition to IFRS</u>	<u>IFRS</u>
Cash flow from operating activities				
Cash generated from operations	(c)	(10,597)	(3,414)	(14,011)
Interest paid		(8,941)		(8,941)
Income tax paid		(4,111)		(4,111)
Net cash used in operating activities		<u>(23,649)</u>	<u>(3,414)</u>	<u>(27,063)</u>
Cash flows from investing activities				
Purchases of property, plant and equipment and intangible assets		<u>(35,160)</u>		<u>(35,160)</u>
Cash flows from financing activities				
Proceeds from borrowings		114,652	3,414	118,066
Repayments of borrowings		(63,261)		(63,261)
Dividends paid		(4,835)		(4,835)
Other long-term rights and obligations		6,470		6,470
Net cash generated by financing activities		<u>53,026</u>	<u>3,414</u>	<u>56,440</u>
Net increase in cash and cash equivalents		<u>(5,783)</u>		<u>(5,783)</u>
Cash and cash equivalents at beginning of the year		63,170		63,170
Exchange losses on cash and cash equivalents		<u>(68)</u>		<u>(68)</u>
Cash and cash equivalents at end of the year		<u><u>57,319</u></u>		<u><u>57,319</u></u>

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**(v) Reconciliation of equity on 1 January 2005
(relates to the effects of the adoption of
IAS 32/IAS39 as from 1 January 2005)**

	<u>Note</u>	<u>IFRS</u>	<u>Effect of adoption of IAS 32/39</u>	<u>IFRS (with the effects of IAS 32/39)</u>
Assets				
Non-current assets				
Property, plant and equipment		174,411		174,411
Intangible assets		892		892
Taxes recoverable		10,480		10,480
Deferred taxes	(c.iv)	16,916	14	16,930
Judicial deposits		12,090		12,090
Notes receivable		1,189		1,189
		<u>215,978</u>	<u>14</u>	<u>215,992</u>
Current assets				
Taxes recoverable		23,233		23,233
Inventories		84,816		84,816
Notes receivable		1,729		1,729
Trade receivable		65,720		65,720
Cash and cash equivalents	(c.i)	63,170	(40)	63,130
Other		11,653		11,653
		<u>250,321</u>	<u>(40)</u>	<u>250,281</u>
Total assets		<u><u>466,299</u></u>	<u><u>(26)</u></u>	<u><u>466,273</u></u>

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	<u>Note</u>	<u>IFRS</u>	<u>Effect of adoption of IAS 32/39</u>	<u>IFRS (with the effects of IAS 32/39)</u>
Shareholders' equity				
Capital		79,360		79,360
Revenue reserves		<u>82,079</u>	(26)	<u>82,053</u>
		<u>161,439</u>	(26)	<u>161,413</u>
Non-current liabilities				
Borrowings		79,762		79,762
Taxes payable		18,818		18,818
Deferred taxes		25,540		25,540
Contingencies		<u>29,735</u>		<u>29,735</u>
		<u>153,855</u>		<u>153,855</u>
Current liabilities				
Borrowings		69,312		69,312
Taxes payable		7,767		7,767
Trade and other payables		56,363		56,363
Salaries and social charges		7,555		7,555
Other		<u>10,008</u>		<u>10,008</u>
		<u>151,005</u>		<u>151,005</u>
Total liabilities		<u>304,860</u>		<u>304,860</u>
Total liabilities and shareholders' equity		<u>466,299</u>	(26)	<u>466,273</u>

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(c) Description of the differences between the accounting practices and related adjustments

(i) Adjustment of financial assets to fair value

Mangels has financial investments in time deposits, which bear fixed coupon plus exchange variation. Such financial instrument is recorded in the statutory financial statements at the original amount, plus the related contractual earnings. In accordance with IAS 39 ("Financial Instruments - Recognition and Valuation"), these instruments fall under the definition of "financial assets at fair value through profit and loss". The IFRS consolidated financial statements reflects the adjustment of time deposits to market value, determined on the basis of future interest information derived from official market quotations.

The contra entry to this adjustment was the "other operating income and expenses, net" line in the income statement for the year.

(ii) Adjustment to present value of accounts receivable and payable

Accounting practices adopted in Brazil do not require monetary items to be discounted to present value. Under IAS 18 ("Revenues"), whenever the nominal amount of accounts receivable from goods sold or services rendered significantly deviates from its cash basis, such discounting is required.

Mangels has trade accounts receivable from installment sales and renegotiations with customers, which are stated at face value in the statutory financial statements. For IFRS purposes, such balances have been discounted to their present value based on the interest rate usually adopted on longer term sales. Accounts payable were also discounted to present value.

The contra entry to the discount to present value of accounts receivable is sales revenues in the income statement, while the contra entry to the discount of accounts payable is the inventories account in the balance sheet, taking into account the inventory turnover.

(iii) Deferred income tax on revaluation of land

NPC 24, issued by the Brazilian Independent Auditors Institute ("IBRACON"), requires the recognition of deferred income tax and social contribution on the revaluation of assets only insofar as it is subject to depreciation, amortization or depletion, or when the assets are acquired or maintained for future sale. Accordingly, the statutory financial statements do not reflect the recognition of such taxes, which have been reflected in the IFRS financial statements, in compliance with IAS 12 ("Income Tax") and SIC 21 ("Income Tax - Recovery of Non Depreciable, Revalued Asset").

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(iv) Income tax

In accordance with IAS 12 ("Income Tax"), deferred income taxes have been recorded on all adjusted differences between the statutory balances and balances under IFRS, except for deferred income tax on the revaluation of land, as mentioned in item (iii).

(v) Reclassification of software to intangible assets

In order to comply with IAS 38 ("Intangible Assets"), software used by Mangels has been reclassified from deferred charges to intangible assets.

(vi) Reclassification of non-operating results

In accordance with IAS 1 ("Presentation of the Financial Statements"), non-operating results relating to gains on the sale of fixed assets and rental revenues were reclassified to other operating income and expenses, net.

(vii) Reclassification of Advances on Export Contracts ("ACEs")

Pursuant to IAS 32 ("Presentation and Disclosure of Financial Instruments"), the book value of ACEs was transferred from current assets (where it was offset against the accounts receivable balance) to financing, in current liabilities.

(viii) Reclassification of deferred income tax to long-term receivables

In compliance with IAS 12 ("Income Tax"), the short-term portion of deferred income tax credits was transferred to non-current assets.

(ix) Reclassification of financial income

In accordance with IAS 1 ("Presentation of the Financial Statements"), the book value of financial income was reclassified to "other operating income and expenses, net".

(x) Effects on cash flow statement

The combination of the adjustments referred to above resulted in a net effect on the cash flow generated from operations, as demonstrated in the reconciliation of cash flow.

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6 Property, plant and equipment

	<u>Land</u>	<u>Buildings</u>	<u>Machinery & equipment</u>	<u>Vehicles</u>	<u>Furniture & fittings</u>	<u>Assets in construction</u>	<u>Other</u>	<u>Total</u>
At 1 January 2004								
Cost	30,123	66,121	214,031	1,450	11,241	4,485	118	327,569
Accumulated depreciation		(18,217)	(124,699)	(737)	(8,043)			(151,696)
Net book amount	<u>30,123</u>	<u>47,904</u>	<u>89,332</u>	<u>713</u>	<u>3,198</u>	<u>4,485</u>	<u>118</u>	<u>175,873</u>
Year ended 31 December 2004								
Opening net book amount	30,123	47,904	89,332	713	3,198	4,485	118	175,873
Additions		1,465	5,880	31	1,396	7,695		16,467
Disposals	(2,924)	(1,650)	1,138	4	17			(3,415)
Depreciation charge (Note 19)		(2,029)	(11,515)	(253)	(717)			(14,514)
Closing net book amount	<u>27,199</u>	<u>45,690</u>	<u>84,835</u>	<u>495</u>	<u>3,894</u>	<u>12,180</u>	<u>118</u>	<u>174,411</u>
At 31 December 2004								
Cost	27,199	65,897	218,365	1,284	12,599	12,180	118	337,642
Accumulated depreciation		(20,207)	(133,530)	(789)	(8,705)			(163,231)
Net book amount	<u>27,199</u>	<u>45,690</u>	<u>84,835</u>	<u>495</u>	<u>3,894</u>	<u>12,180</u>	<u>118</u>	<u>174,411</u>

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	<u>Land</u>	<u>Buildings</u>	<u>Machinery & equipment</u>	<u>Vehicles</u>	<u>Furniture & fittings</u>	<u>Assets in construction</u>	<u>Other</u>	<u>Total</u>
Year ended 31 December 2005								
Opening net book amount	27,199	45,690	84,835	495	3,894	12,180	118	174,411
Exchange differences								
Additions		2,838	24,239	1,161	1,304	2,931		32,473
Disposals	(46)	3	38	(134)	(100)			(239)
Depreciation charge (Note 19)		(2,052)	(11,168)	(297)	(760)			(14,277)
Closing net book amount	<u>27,153</u>	<u>46,479</u>	<u>97,944</u>	<u>1,225</u>	<u>4,338</u>	<u>15,111</u>	<u>118</u>	<u>192,368</u>
At 31 December 2005								
Cost	27,153	68,735	242,541	2,016	13,903	15,111	118	369,577
Accumulated depreciation		(22,256)	(144,597)	(791)	(9,565)			(177,209)
Net book amount	<u>27,153</u>	<u>46,479</u>	<u>97,944</u>	<u>1,225</u>	<u>4,338</u>	<u>15,111</u>	<u>118</u>	<u>192,368</u>

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As described in Note 5(a)(ii), in determining the cost of property, plant and equipment for the IFRS opening balance sheet at 1 January 2004, Mangels applied the optional exemption allowed for the IFRS 1 from full retrospective application and adopted the revaluation amounts stated in the report issued by independent experts, dated 31 December 2003.

Depreciation expense of R\$ 11,768 (2004 - R\$ 11,859) has been charged to cost of sales, and R\$ 2,172 (2004 - R\$ 2,323) in administrative expenses.

7 Intangible assets

	<u>Software</u>	<u>Product development</u>	<u>Other</u>	<u>Total</u>
At 1 January 2004				
Cost	5,627	3,067	23,883	32,577
Accumulated amortization	<u>(4,865)</u>	<u>(3,054)</u>	<u>(23,717)</u>	<u>(31,636)</u>
Net book amount	<u>762</u>	<u>13</u>	<u>166</u>	<u>941</u>
Year ended 31 December 2004				
Opening net book amount	762	13	166	941
Additions	17		75	92
Amortization charge (Note 19)	<u>(55)</u>	<u>(5)</u>	<u>(81)</u>	<u>(141)</u>
Closing net book amount	<u>724</u>	<u>8</u>	<u>160</u>	<u>892</u>
At 31 December 2004				
Cost	5,644	3,067	23,958	32,669
Accumulated amortization	<u>(4,920)</u>	<u>(3,059)</u>	<u>(23,798)</u>	<u>(31,777)</u>
Net book amount	<u>724</u>	<u>8</u>	<u>160</u>	<u>892</u>
Year ended 31 December 2005				
Opening net book amount	724	8	160	892
Additions	2,647	40		2,687
Amortization charge (Note 19)	<u>(188)</u>	<u>(5)</u>	<u>(87)</u>	<u>(280)</u>
Closing net book amount	<u>3,183</u>	<u>43</u>	<u>73</u>	<u>3,299</u>

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8 Taxes recoverable

	<u>2005</u>	<u>2004</u>
Value-Added Tax on Sales and Services (ICMS) (i)	13,730	7,526
IPI presumed credit (ii)	5,104	6,818
Corporate Income Tax (IRPJ)	3,563	
Excise Tax (IPI)	3,272	11,898
Withholding Income Tax (IRRF)	1,810	852
Social Contribution on Net Income (CSLL)	1,329	
Social Contribution on Revenues (COFINS)	982	5,237
Social Integration Program (PIS)	254	1,382
	<u>30,044</u>	<u>33,713</u>
Non-current	<u>(5,104)</u>	<u>(10,480)</u>
Current	<u>24,940</u>	<u>23,233</u>

- (i) ICMS recoverable amounts arise essentially from credits on the purchase of inputs used in the production for export, as well as the acquisition of property, plant and equipment items, determined pursuant to Normative Decision CAT no. 1, of 25 April 2001, which are being used in 48 installments. As from 2006, this credit balance is expected to decrease as a result of increased internal sales from the Divisão Rodas aluminum re-smelting furnace on which Mangels has been investing.
- (ii) The IPI presumed credit refers to the reimbursement of PIS and COFINS contributions levied on inputs used for manufacturing products to be exported, calculated as prescribed by Law 10276/01 of September 2001.

9 Provisions for contingent liabilities

At the date of the financial statements, the provisions for contingent liabilities of probable negative outcome and related judicial deposits are as follows.

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	Judicial deposits		Provision for contingencies	
	2005	2004	2005	2004
Tax claims	7,024	6,612	16,727	23,571
Labor and social security claims	4,218	4,043	5,973	3,974
Others	1,223	1,435	2,190	2,190
	<u>12,465</u>	<u>12,090</u>	<u>24,890</u>	<u>29,735</u>

Mangels is party to various labor, tax and other disputes in progress and is discussing these issues at both the administrative and judicial levels, which, when applicable, are supported by judicial deposits. The provision for losses arising from these processes is estimated and updated by management, based on the opinion of its external legal advisors.

	Tax claims	Labor and social security claims	Others	Total
At 31 December 2004	23,571	3,974	2,190	29,735
Charged to the income statement				
Additional provisions		1,975		1,975
Discount unwinding and monetary variance	2,093	24		2,117
Used during the year	<u>(8,937)</u>			<u>(8,937)</u>
At 31 December 2005	<u>16,727</u>	<u>5,973</u>	<u>2,190</u>	<u>24,980</u>

The main tax contingencies are related to judicial claims concerning the extension of the calculation basis of Social Contribution on Revenues (COFINS), National Institute of Social Security (INSS) on 13th month salary, fines on Value Added Tax on Sales and Services (ICMS) installments and Income Tax and Social Contribution - Real Plan. In all cases, a negative outcome to Mangels has been assessed as probable by the legal advisors.

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10 Inventories

	<u>2005</u>	<u>2004</u>
Finished products	32,029	29,458
Work in process	20,563	18,928
Raw materials	16,197	27,514
Auxiliary materials	<u>6,381</u>	<u>8,916</u>
	<u>75,170</u>	<u>84,816</u>

11 Trade receivables

	<u>2005</u>	<u>2004</u>
Trade receivables	82,767	69,389
Less provision for impairment of receivables	<u>(3,668)</u>	<u>(3,669)</u>
Trade receivables - net	<u>79,099</u>	<u>65,720</u>
Non-current	<u> </u>	<u> </u>
Current	<u>79,099</u>	<u>65,720</u>

The Group recognized a loss of R\$ 3,668 (2004 - R\$ 3,669) arising on the impairment of its trade receivables during the year ended 31 December 2005. The related expense is included in 'selling and marketing costs' in the income statement.

12 Cash and cash equivalents

	<u>Interest rate</u>	<u>2005</u>	<u>2004</u>
Local currency			
Bank Deposit Certificates (CDB)	100% of CDI	29,280	29,117
Bank accounts and others		5,603	18,913
Impairment of financial assets		<u>(4,152)</u>	<u>(3,489)</u>
		<u>30,731</u>	<u>44,541</u>

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	<u>Interest rate</u>	<u>2005</u>	<u>2004</u>
Foreign currency			
Bank Deposit Certificates (CDB)	Foreign exchange variation + 4%	17,096	15,283
Bank accounts		<u>9,492</u>	<u>3,346</u>
		<u>26,588</u>	<u>18,629</u>
		<u>57,319</u>	<u>63,170</u>

An impairment loss was recognized in to relation time deposits held against a financial institution which is currently under liquidation.

13 Shareholders' equity

(a) Capital

Subscribed capital of Mangels comprises 9,239,019 shares with no par value, of which 3,100,865 are common and 6,138,154 are preferred shares with no voting rights.

(b) Special reserve

The special reserve is represented by the remaining balance of retained earnings, after establishing the legal reserve and the proposed dividends. This reserve is intended to ensure adequate operating conditions and is limited to 80% of restated capital, as prescribed in the by-laws (Article 32, paragraph one).

(c) Revaluation reserve

The revaluation reserve reflects valuation to fair value of property and equipment, net of deferred taxes. It is realized upon depreciation, impairment or sale of the respective revalued assets, when it is transferred to retained earnings.

(d) Proposed dividends

Under Mangels' by-laws, shareholders are assured a minimum mandatory dividend of 25% of the profit for the year, adjusted as required by the law.

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As from 1997, preferred stockholders receive dividends 10% higher than those of the common shareholders.

Management proposes the distribution of dividends on profit for the year, adjusted as required by the law, to be distributed on common and preferred shareholders, as follows:

	2005	2004
Profit for the year (under Brazilian GAAP)	12,066	19,137
(-) Legal reserve - 5%	<u>(603)</u>	<u>(957)</u>
Calculation basis	11,463	18,180
Proposed dividends - 25.8% (26.6% for 2004)	<u><u>2,955</u></u>	<u><u>4,835</u></u>

14 Borrowings

BNDES financings for property, plant and equipment purchase are collateralized by the assets financed.

Advances on Export Contracts (ACE) and prepayments of exports are collateralized by promissory notes and the exported products.

Working capital financing represent revolving credit lines, which are renewed annually and guaranteed by promissory notes.

The exposure of the Group's borrowings to interest rate changes and the contractual repricing dates at the balance sheet dates are as follows:

	2005	2004
6 months or less	<u>25,375</u>	<u>19,362</u>
6-12 months	29,824	49,950
1-5 years	127,056	71,176
Over 5 years	<u> </u>	<u>8,586</u>
	<u><u>182,255</u></u>	<u><u>149,074</u></u>

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The maturity of non-current borrowings is as follows:

	<u>2005</u>	<u>2004</u>
Between 1 and 2 years	27,875	35,656
Between 2 and 5 years	99,181	38,519
Over 5 years	<u> </u>	<u>5,587</u>
	<u>127,056</u>	<u>79,762</u>

The effective interest rates at the balance sheet date were as follows:

	<u>Average annual interest rate - %</u>
Local currency	
BNDES - FINAME - BDMG	Long Term Interest Rate ("TJLP") + 5.0
BNDES - PROGEREN	TJLP + 6.0
BNDES - EXIM BANK	TJLP + 4,0 to 4.8
Working capital	19.09
Foreign currency	
Advances on export contracts	Foreign exchange variation + 2,6 to 4.1
BNDES - BDMG	UMBNDDES + 5.0
Prepayments of exports	Foreign exchange variation + 6.7
Working capital	Foreign exchange variation + 6.7

The carrying amounts and fair value of the non-current borrowings are as follows:

	<u>Carrying amounts</u>		<u>Fair value</u>	
	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>
Local currency				
BNDES - FINAME -BDMG	9,354	14,283	9,354	14,283
BNDES - PROGEREN	10,286	10,045	10,286	10,045
BNDES - EXIM BANK	<u> </u>	8,270	<u> </u>	8,270
Working capital	<u>2,387</u>	<u>7,116</u>	<u>2,387</u>	<u>7,116</u>
	<u>22,027</u>	<u>39,714</u>	<u>22,027</u>	<u>39,714</u>

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	<u>Carrying amounts</u>		<u>Fair value</u>	
	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>
Foreign currency				
Advances on export contracts	12,713	28,363	12,713	28,363
BNDES - BDMG	1,999	3,173	1,999	3,173
Prepayments of exports	137,833	71,157	139,160	68,827
Working capital	7,683	6,667	7,621	6,667
	<u>160,228</u>	<u>109,360</u>	<u>160,953</u>	<u>107,030</u>
	<u>182,255</u>	<u>149,074</u>	<u>182,980</u>	<u>146,744</u>
Non-current	<u>127,056</u>	<u>79,762</u>		
Current	<u>55,199</u>	<u>69,312</u>		

The carrying amounts of short-term borrowings approximate their fair value.

In calculating fair value of the borrowings, the value of the risk-free rate added to the historic spread of the operation has been used in comparison with the contractual rate. The historic spread of the operation considers the additional value paid by the entity to the banks in the beginning of the operation, as compared to the risk-free rate.

The carrying amounts of the Group's borrowings are denominated in the following currencies:

	<u>2005</u>	<u>2004</u>
U.S. dollar	160,228	109,360
Real	<u>22,027</u>	<u>39,714</u>
	<u>182,255</u>	<u>149,074</u>

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15 Taxes payable

	<u>2005</u>	<u>2004</u>
Employees' Profit Participation Program/Taxes for Social Security Financing/Social Contribution on Net Income	23,150	22,043
Tax on financial operations	938	741
Withholding tax on interest on own capital	668	
Added value sales tax		2,508
Other taxes	<u>1,184</u>	<u>1,293</u>
	<u>25,940</u>	<u>26,585</u>
Non-current portion	<u>5,699</u>	<u>7,767</u>
Current portion	<u><u>20,241</u></u>	<u><u>18,818</u></u>

16 Deferred taxes

The deferred taxes balances are as follows:

	<u>2005</u>	<u>2004</u>
Deferred tax assets		
Deferred tax asset expected to be recovered in 12 months	3,857	3,825
Deferred tax asset expected to be recovered after 12 months	<u>11,723</u>	<u>13,091</u>
	<u>15,580</u>	<u>16,916</u>
Deferred tax liabilities		
Deferred tax liability expected to be settled after 12 months	<u>24,244</u>	<u>25,540</u>
Net deferred taxes	<u><u>8,664</u></u>	<u><u>8,624</u></u>

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the income tax relate to the same fiscal authority.

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The projections of the generation of future taxable income include various estimates relating to the performance of the Brazilian and worldwide economies, the selection of foreign exchange rates, volume of sales and sales prices, tax rates and other factors that may present variations in relation to the actual amounts.

As the income tax and social contribution bases result not only from the potential future profits, but also from Mangels' tax and corporate structure, the existence of non-taxable revenues, non-deductible expenses, tax exemptions and incentives, as well as several other variables, no immediate correlation exists between Mangels' profit and the income tax and social contribution results. Accordingly, the projection for the use of tax losses does not serve as a sole indication of future profits of Mangels and its subsidiaries.

Deferred income tax assets are recognized for tax loss carry-forwards to the extent that the realization of the related tax benefit through the future taxable profits is probable. Net deferred tax assets consists of 30% of the deferred tax liability recognized in Brazil on foreign exchange gains which are taxed on a cash basis at the option of Mangels.

As of 31 December 2005 and 2004, net operating loss carry-forwards relate only to the Brazilian Group companies.

Tax loss carry-forwards in Brazil have no expiration date and are available for offset against future taxable income. Tax regulations in Brazil impose certain conditions and limitations on the future availability of net operating loss and tax credit carry forwards, including restriction on the use of the carry-forwards in any particular year.

Income tax expense

	<u>2005</u>	<u>2004</u>
Current tax	(4,232)	(11,299)
Deferred tax	<u>(40)</u>	<u>4,357</u>
	<u>(4,272)</u>	<u>(6,942)</u>

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Deferred tax on the Group's income before tax differs from the theoretical amount that would arise using the weighted average tax rate applicable to income of the consolidated companies as follows:

	<u>2005</u>	<u>2004</u>
Profit before income taxes	16,675	25,262
Income tax expense at the nominal rate of 34%	5,670	8,589
Adjustments to obtain the effective rate:		
Realization of revaluation reserve	1,293	2,327
Other (additions) exclusions	(1,437)	5,386
Tax losses offset - deferred taxes not previously recognized	(1,646)	(4,210)
Temporary differences - deferred taxes not previously recognized	<u>392</u>	<u>(5,150)</u>
	<u>(1,398)</u>	<u>(1,647)</u>
Income tax expense	<u><u>4,272</u></u>	<u><u>6,942</u></u>

Income tax and social contribution are calculated according to the applicable legislation, using the rates effective on the balance sheet date, being 25% for income tax and 9% for the social contribution on profit. In accordance with IAS 12, deferred tax credits are recorded on income tax losses, negative social contribution bases and temporary differences.

17 Trade and other payables

	<u>2005</u>	<u>2004</u>
Suppliers	27,969	51,524
Dividends payable	<u>2,965</u>	<u>4,839</u>
	<u><u>30,934</u></u>	<u><u>56,363</u></u>

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18 Salaries and payroll charges

	<u>Brazil</u>		<u>United States</u>		<u>Total</u>	
	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>
Salaries payable	3,221	3,282	360	309	3,581	3,591
Provision for year-end extra salaries	<u>4,255</u>	<u>3,964</u>			<u>4,255</u>	<u>3,964</u>
	<u><u>7,476</u></u>	<u><u>7,246</u></u>	<u><u>360</u></u>	<u><u>309</u></u>	<u><u>7,836</u></u>	<u><u>7,555</u></u>

The Group does not sponsor, nor is obliged to sponsor, any postretirement benefit plan. It makes the legally required social security contributions to the social security plans managed by the governments in the countries where it has operations. The contributions owed by the Group to government-managed social security plans are incurred and paid on a monthly basis and generally calculated as a percentage of the salaries paid in each subsidiary with percentages varying from country to country.

The Group provides to its employees other benefits, such as health insurance, food and/or transport reimbursement, which are common practice in the countries where it carries out its activities. None of those benefits are provided after employment ceases.

19 Expenses by nature

	<u>2005</u>	<u>2004</u>
Depreciation, amortization and impairment charges (Notes 6 and 7)	14,556	14,514
Employee benefit expenses	64,131	53,166
Changes in inventories of finished goods and work in progress	58,968	59,869
Raw materials and consumables used	316,857	281,583
Transportation	13,075	16,535
Provision for impaired receivables - net	3,668	3,669
Advertising costs	2,288	1,267
Other expenses	<u>13,837</u>	<u>24,711</u>
	<u><u>487,380</u></u>	<u><u>455,314</u></u>

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	<u>2005</u>	<u>2004</u>
Classified as		
Cost of sales	410,354	367,063
Selling and marketing costs	35,256	38,651
Administrative expenses	41,666	40,955
Other operating expenses	<u>104</u>	<u>8,645</u>
	<u>487,380</u>	<u>455,314</u>
20 Other operating income		
	<u>2005</u>	<u>2004</u>
Interest income	5,063	6,563
Other	<u>1,441</u>	<u>258</u>
	<u>6,504</u>	<u>6,821</u>
21 Finance costs		
	<u>2005</u>	<u>2004</u>
Interest expense		
Bank borrowings	28,361	31,162
Bank fees and charges	<u>5,718</u>	<u>4,514</u>
Net foreign exchange transaction gains/(losses)	<u>11,520</u>	<u>4,764</u>
	<u>(22,559)</u>	<u>(30,912)</u>
22 Earnings per share		

Earnings per share are calculated by dividing the profit attributable to Mangels equity holders by the weighted average number of common and preferred shares in issue during the year. As no potential common shares were outstanding in 2005 or 2004, basic and diluted earnings per share are the same.

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	<u>2005</u>	<u>2004</u>
Profit for the year	12,403	18,320
Weighted average number of common shares in issue (thousands)	9,853	9,853
Earnings per share (R\$ per share)	<u>1.26</u>	<u>1.86</u>
23 Cash generated from operations		
	<u>2005</u>	<u>2004</u>
Cash flows from operating activities		
Profit for the year	12,403	18,320
Adjustment to reconcile profit to cash generated by operating activities		
Income tax and social contribution	4,272	6,942
Depreciation and amortization	14,557	14,655
Residual value of non current assets disposals	239	3,644
Provisions for contingent liabilities	(4,845)	8,783
Taxes payable - PAES	1,423	6,248
Accrued interest on financing	11,614	11,782
Foreign exchange variation on financing	<u>(19,488)</u>	<u>(5,096)</u>
	<u>20,175</u>	<u>65,278</u>
Changes in working capital accounts		
Trade accounts receivable	(13,379)	(14,685)
Inventories	9,646	(34,322)
Suppliers	(23,555)	16,677
Taxes recoverable	(1,707)	(12,998)
Other	<u>(5,191)</u>	<u>(839)</u>
	<u>(34,186)</u>	<u>(46,167)</u>
Net cash generated from (used in) operating activities	<u>(14,011)</u>	<u>19,111</u>

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24 Related-party transactions

	2005			
	<u>Mangels S.A.</u>	<u>Tecnopar S.A.</u>	<u>Shorewood S.A.</u>	<u>Total</u>
Balances				
Current liabilities				
Loans	105			<u>105</u>
Transactions				
Financial expenses				
Financial income	3	3	3	<u>9</u>
				2004
	<u>Mangels S.A.</u>	<u>Tecnopar S.A.</u>	<u>Shorewood S.A.</u>	<u>Total</u>
Balances				
Long-term receivables				
Loans			32	<u>32</u>
Transactions				
Financial expenses	90			<u>90</u>
Financial income		34	1	<u>35</u>

Intercompany transactions were carried out under normal market conditions and terms. The loan balances, arising from Mangels' centralized cash policy, bear market charges and these loans have no maturity date.

Key management compensation, including all related employee benefits, amounted to R\$ 5,600 and 4,294 in 2005 and 2004, respectively.

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25 Segment information

Primary reporting format - business segments

At 31 December 2005, the Group is organized into three main business segments: (1) Steel; (2) Wheels; and (3) Cylinders.

The segment results for the year ended 31 December 2004 are as follows:

	<u>Steel</u>	<u>Wheels</u>	<u>Cylinders</u>	<u>Unallocated</u>	<u>Group</u>
Total gross segment sales	297,125	134,759	72,783		504,667
Sales	<u>297,125</u>	<u>134,759</u>	<u>72,783</u>		<u>504,667</u>
Operating profit/Segment result	58,171	13,894	2,714	(18,605)	56,174
Finance costs - net (Note 21)					<u>(30,912)</u>
Profit before income tax					25,262
Deferred income tax					<u>(6,942)</u>
Profit for the year					<u><u>18,320</u></u>

The segment results for the year ended 31 December 2005 are as follows:

	<u>Steel</u>	<u>Wheels</u>	<u>Cylinders</u>	<u>Unallocated</u>	<u>Group</u>
Total gross segment sales	311,060	145,413	63,637		520,110
Sales	<u>311,060</u>	<u>145,413</u>	<u>63,637</u>		<u>520,110</u>
Operating profit/Segment result	43,000	12,487	(4,895)	(11,358)	39,234
Finance costs - net (Note 21)					<u>(22,559)</u>
Profit before income tax					16,675
Deferred income tax					<u>(4,272)</u>
Profit for the year					<u><u>12,403</u></u>

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Other segment items included in the income statement are as follows:

	<u>Year ended 31 December 2005</u>				<u>Year ended 31 December 2004</u>			
	<u>Steel</u>	<u>Wheels</u>	<u>Cylinders</u>	<u>Group</u>	<u>Steel</u>	<u>Wheels</u>	<u>Cylinders</u>	<u>Group</u>
Depreciation (Note 6)	5,411	5,356	3,510	14,277	5,180	5,465	3,869	14,514
Amortization (Note 7)	280			280	141			141
Reversal of inventory impairment	191	137	40	368				
Impairment of trade receivables (Note 11)	1,264	2,185	219	3,668	1,646	1,908	115	3,669

The segment assets and liabilities at 31 December 2004 for the year then ended are as follows:

	<u>Steel</u>	<u>Wheels</u>	<u>Cylinders</u>	<u>Unallocated</u>	<u>Group</u>
Total assets	301,830	70,858	70,876	22,735	466,299
Liabilities	16,281	13,876	5,876	268,827	304,860

The segment assets and liabilities at 31 December 2005 for the year then ended are as follows:

	<u>Steel</u>	<u>Wheels</u>	<u>Cylinders</u>	<u>Unallocated</u>	<u>Group</u>
Total assets	340,994	76,903	65,090	(5,661)	477,326
Liabilities	13,225	8,959	4,529	279,752	306,465

Segment assets consist primarily of property and equipment, intangible assets, receivables and operating cash.

Segment liabilities comprise operating liabilities. They exclude items such as taxation, and corporate borrowings.

Capital expenditure comprises additions to property and equipment (Note 6) and intangible assets (Note 7).

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Secondary reporting format - geographical segments

The Group's business segments operate in four main geographical areas, even though they are managed on a worldwide basis.

The areas of operation are principally:

	<u>2005</u>	<u>2004</u>
Sales		
Brazil	450,459	406,790
South America	32,348	40,312
Eurozone	23,511	33,436
US	11,737	22,106
Other countries	2,055	2,023

Sales are allocated based on the country in which the customer is located.

Total assets and capital expenditure are substantially located in Brazil.

* * *