NATIONAL STEEL CO
Form 20-F
July 02, 2007

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
ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2006
OR
TRANSITION REPORT PURSUANT TO SECTION 13
OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _____ to _____

SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT
OF 1934
Comission file number: 1-14732

COMPANHIA SIDERÚRGICA NACIONAL

(Exact Name of Registrant as Specified in its Charter)

National Steel Company	**Federative Republic of Brazil**
(Translation of Registrant's Name into English)	(Jurisdiction of Incorporation or Organization)

Av. Brigadeiro Faria Lima, 3.400 - 20ºandar
04538-132 - São Paulo, SP, Brazil
Tel.: (55 11) 3049 7100
(Address of principal executive offices)

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

Title of Each Class	Name of Each Exchange on Which Registered
Common Shares, without par value	New York Stock Exchange*
American Depositary Shares (evidenced by American Depositary Receipts) each representing one common share of CSN	New York Stock Exchange

*

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

Securities registered or to be registered pursuant to Section 12(g) of the Act: None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: None

Indicate the number of outstanding shares of each of the issuer s classes of capital or common stock as of the period covered by the annual report: 272,067,946 common shares with no par value, including 14,654,500 shares held in treasury

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

Yes 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

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 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 Accelerated Filer Non-accelerated Filer

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

Item 17 Item 18

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

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INTRODUCTION

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

- we , us , our or CSN in this annual report are to Companhia Siderúrgica Nacional and its consolidated subsidiaries;
- "Brazilian government"are to the federal government of the Federative Republic of Brazil;
- "*real*", "*reais*"or "R$" are to Brazilian reais, the official currency of Brazil;
- "U.S. dollars", $ or "US$" are to United States dollars;
- "billions" means thousands of millions, "km" means kilometers, "tons" means metric tons and "MW" means megawatts;
- consolidated financial statements" are to the Consolidated Financial Statements of Companhia Siderúrgica Nacional as of December 31, 2005 and 2006 and, for the years ended December 31, 2004, 2005 and 2006, together with the corresponding Report of Independent Registered Public Accounting Firm;
- amounts in *reais* stated at a particular date and followed by U.S. dollar equivalents have been converted using the *reais* to U.S. dollars exchange rate in effect on such date; and
- parent company are to Companhia Siderúrgica Nacional.

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FORWARD-LOOKING STATEMENTS

This annual report includes forward-looking statements, within the meaning of Section 27A of the U.S. Securities Act of 1933, as amended, or the Securities Act, and Section 21E of the U.S. Securities Exchange Act of 1934, as amended, or the Exchange Act, principally in Items 3 through 5 and Item 11 of this annual report. We have based these forward-looking statements largely on our current expectations and projections about future events, industry and financial trends affecting our business. These forward-looking statements are subject to risks, uncertainties and assumptions, including, among other things:

- general economic, political and business conditions, both in Brazil and in our principal export markets,
- changes in competitive conditions and in the general level of demand for our products;
- management s expectations and estimates concerning our future financial performance, financing plans and programs, and the effects of competition;
- our level of debt;
- availability of raw materials;
- changes in international trade;
- protectionist measures imposed by Brazil and other steel-importing countries;
- anticipated trends in our industry;
- our expenditure plans;
- inflation, interest rate levels and fluctuations in exchange rates;
- our ability to develop and deliver our products on a timely basis;
- electricity shortages and government responses to them;
- existing and future governmental regulation; and
- other risk factors as set forth under Item 3D. Risk Factors.

The words believe, may, will, forecast, estimate, plan, continue, anticipate, intend, expect, li are intended to identify forward-looking statements. We undertake no obligation to update publicly or revise any forward-looking statements because of new information, future events or other factors. In light of these risks and uncertainties, the forward-looking events and circumstances discussed in this annual report might not occur. Our actual results and performance could differ substantially from those anticipated in our forward-looking statements. As a result of various factors such as those risks described in Item 3D. Risk Factors , undue reliance should not be placed on these forward-looking statements.

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PRESENTATION OF FINANCIAL AND OTHER INFORMATION

Our consolidated financial statements as of December 31, 2005 and 2006 and for each of the years ended December 31, 2004, 2005 and 2006 contained in Item 18. Financial Statements have been presented in U.S. dollars and prepared in accordance with accounting principles generally accepted in the United States of America, or U.S. GAAP. See Note 2(a) to our consolidated financial statements. For certain purposes, such as providing reports to our Brazilian shareholders, filing financial statements with the *Comissão de Valores Mobiliários*, the Brazilian securities commission, or CVM, and determining dividend payments and other distributions and tax liabilities in Brazil, we have prepared and will continue to be required to prepare financial statements in accordance with the accounting principles required by the Brazilian Corporate Law, specifically, Law No. 6,404 dated December 15, 1976, as amended, and the rules and regulations of the CVM, or Brazilian GAAP, which differ in certain significant respects from U.S. GAAP.

Because we operate in an industry that uses the U.S. dollar as its currency of reference, our management believes that it is appropriate to present our U.S. GAAP financial statements in U.S. dollars in our filings with the U.S. Securities and Exchange Commission, or SEC. Accordingly, as permitted by the rules of the SEC, we have adopted the U.S. dollar as our reporting currency for our U.S. GAAP financial statements contained in our annual reports that we file with the SEC.

As described more fully in Note 2(a) to our consolidated financial statements, the U.S. dollar amounts as of the dates and for the periods presented in our consolidated financial statements have been translated from the *real* amounts in accordance with the criteria set forth in the U.S. Financial Accounting Standards Board s Statement of Financial Accounting Standards no. 52, Foreign Currency Translation , at the period-end exchange rate (for balance sheet items) or the average exchange rate prevailing during the period (for income statement items). In this Annual report, we refer to a Statement of Financial Accounting Standards issued by the U.S. Financial Accounting Standards Board as an SFAS .

Unless the context otherwise indicates:

- historical data contained in this annual report that were not derived from our consolidated financial statements have been translated from *reais* on a basis similar to that used in our consolidated financial statements for the same periods or as of the same dates, except investment amounts that have been translated at the exchange rate in effect on the date the investment was made.

- forward-looking statements have been translated from *reais* at the exchange rate in effect at the time of the most recently budgeted amounts. We may not have adjusted all of the budgeted amounts to reflect all factors that could affect them. In addition, exceptionally we may have translated budgeted amount based on the exchange rate in effect on the date of the action, operation or document.

Some figures included in this annual report have been subject to rounding adjustments; accordingly, figures shown as totals in certain tables may not be an arithmetic aggregation of the figures which precede them.

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PART I

Item 1. Identity of Directors, Senior Management and Advisors

Not applicable.

Item 2. Offer Statistics and Expected Timetable

Not applicable.

Item 3. Key Information

3A. Selected Financial Data

Our consolidated financial statements have been prepared in accordance with U.S. GAAP. For certain purposes, such as providing reports to our Brazilian shareholders, filing financial statements with the CVM and determining dividend payments and other distributions and tax liabilities in Brazil, we have prepared and will continue to be required to prepare financial statements in accordance with Brazilian GAAP. Our financial statements prepared in accordance with Brazilian GAAP are not adjusted to account for the effects of inflation.

The following table presents our selected financial data as of the dates and for each of the years indicated, prepared in accordance with U.S. GAAP. Our U.S. GAAP consolidated financial statements as of December 31, 2005 and 2006 appear elsewhere herein, together with the reports of our Independent Registered Public Accounting Firm, Deloitte Touche Tohmatsu Auditores Independentes. The selected financial information at December 31, 2002, 2003 and 2004 have been derived from our U.S. GAAP consolidated financial statements in U.S. dollars, not included in this annual report. The selected financial data below should be read in conjunction with Item 5. Operating and Financial Review and Prospects .

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	Year Ended December 31,				
Income Statement Data:	**2002**	**2003**	**2004**	**2005**	**2006**
	(in millions of US$, except per share data)				
Operating revenues					
Domestic sales	1,570	1,843	2,895	3,449	3,550
Export sales	599	1,077	1,008	1,224	1,263
	2,169	**2,920**	**3,903**	**4,673**	**4,813**
Sales taxes	315	322	735	829	899
Discounts, returns and allowances	12	50	84	39	68
Net operating revenues[(1)]	**1,842**	**2,548**	**3,084**	**3,805**	**3,846**
Cost of products sold	994	1,457	1,407	1,837	2,102
Gross profit	**848**	**1,091**	**1,677**	**1,968**	**1,744**
Operating expenses					
Selling	127	176	156	186	167
General and administrative	110	96	109	108	148
Other	47	74	50	28	149
	284	346	315	322	464
Operating income	**564**	**745**	**1,362**	**1,646**	**1,280**
Non-operating income (expenses), net					
Financial income (expenses), net	247	(564)	(510)	(550)	(533)
Foreign exchange and monetary gain (loss),	(891)	325	153	183	218
Other	(30)	14	(6)	3	22
	(674)	(225)	(363)	(364)	(293)
Income (loss) before income taxes, equity in results of affiliated companies	**(110)**	**520**	**999**	**1,282**	**987**
Income tax expense (benefit)					
Current	7	152	289	458	198
Deferred	(190)	(88)	2	(31)	98
	(183)	64	291	427	296
Equity in results of affiliated companies	(71)	9	51	47	58
Net income	**2**	**465**	**759**	**902**	**749**
Basic and diluted earnings per common share	0.01	1.62	2.68	3.34	2,91
Weighted average number of common shares outstanding at end of period (in thousands)	286,917	286,917	283,476	270,275	257,434

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	At December 31,				
Balance Sheet Data:	**2002**	**2003**	**2004**	**2005**	**2006**
	(In millions of US$, except per share data)				
Current assets	1,590	2,310	2,907	3,330	3,962
Property, plant and equipment, net	1,527	1,874	2,143	2,547	3,211
Investments in affiliated companies and other investments (including goodwill)	8	85	233	312	375
Other assets	530	748	874	968	1,000
Total assets	3,655	5,017	6,157	7,157	8,548
Current liabilities	1,732	1,228	1,216	1,398	1,678
Long-term liabilities[2]	1,448	2,982	3,615	4,750	5,823
Stockholders equity	475	807	1,326	1,009	1,047
Total liabilities and stockholders equity	3,655	5,017	6,157	7,157	8,548

	At and for the year ended December 31,				
Other Data:	**2002**	**2003**	**2004**	**2005**	**2006**
Cash flows from operating activities	827	580	354	1,757	919
Cash flows used in investing activities	(340)	(259)	(365)	(593)	(839)
Cash flows from (used in) financing activities	(348)	495	(380)	(996)	(263)
Dividends declared and interest on stockholders equity[3]	143	258	253	969	914
Dividends declared and interest on stockholders equity per common share[3]	0.50	0.90	0.89	3.59	3.55

(1) Net operating revenues consist of operating revenues minus sales taxes, discounts, returns and allowances.
(2) Excluding the current portion of long-term debt.
(3) Amounts consist of dividends declared and interest on stockholders equity accrued, during the year. For a discussion of our dividend policy and dividend and interest payments made in 2006, see Item 8A. Consolidated Statements and Other Financial Information Dividend Policy.

Exchange Rates

Prior to March 4, 2005, there were two principal legal 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. These included the purchase or sale of shares or payment of dividends or interest with respect to shares. Foreign currencies could only be purchased in the commercial exchange market through a Brazilian bank authorized to buy and sell currency in these markets. In both markets, rates were freely negotiated.

Resolution No. 3,265 by the National Monetary Council, dated March 4, 2005, consolidated the foreign exchange markets into one single foreign exchange market, effective as of March 14, 2005. All foreign exchange transactions are now carried out through institutions authorized to operate in the consolidated market and are subject to registration with the electronic registration system of the Central Bank of Brazil, or Central Bank. Foreign exchange rates continue to be freely negotiated, but may be influenced by Central Bank intervention.

Since 1999, the Central Bank has allowed the *real*/U.S. dollar exchange rate to float freely, and during that period, the *real*/U.S. dollar exchange rate has fluctuated considerably. At June 29, 2007, the commercial selling rate for U.S. dollars was R$1.929 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 let the *real* float freely or will intervene in the exchange rate market through a currency band system or otherwise. The *real* may depreciate or appreciate against the U.S. dollar substantially in the future. See Item 3D. Risk Factors Risks Relating to Brazil.

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The following table sets forth the commercial selling rate, expressed in *reais* per U.S. dollar, for the periods indicated.

	Exchange Rate of *Reais* to US$1.00			
	Low	**High**	**Average (1)**	**Period-end**
Year ended December 31,				
2002	2.271	3.955	2.998	3.533
2003	2.822	3.662	3.060	2.889
2004	2.654	3.205	2.917	2.654
2005	2.163	2.762	2.413	2.341
2006	2.059	2.371	2.177	2.138
2007 (through June 29)	1.905	2.156	2.063	1.929

	Exchange Rate of *Reais* to US$1.00			
	Low	**High**	**Average (1)**	**Period-end**
Month ended				
December 31, 2006	2.138	2.169	2.154	2.138
January 31, 2007	2.125	2.156	2.140	2.125
February 28, 2007	2.077	2.118	2.097	2.118
March 31, 2007	2.050	2.139	2.081	2.050
April 30, 2007	2.023	2.048	2.036	2.037
May 31, 2007	1.929	2.031	1.982	1.929
June 30, 2007	1.905	1.964	1.932	1.929

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Source: Central Bank.

(1) Represents the monthly average exchange rate for the relevant periods.

We will pay any cash dividends and make any other cash distributions with respect to the common shares in Brazilian currency. Accordingly, exchange rate fluctuations may affect the U.S. dollar amounts received by the holders of ADSs on conversion by the depositary of such distributions into U.S. dollars for payment to holders of ADSs. Fluctuations in the exchange rate between the *real* and the U.S. dollar may also affect the U.S. dollar equivalent of the *real* price of the common shares on the São Paulo Stock Exchange (*Bolsa de Valores do Estado de São Paulo, or BOVESPA).*

3B. Capitalization and Indebtedness

Not applicable.

3C. Reasons for Offer and Use of Proceeds

Not applicable.

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3D. Risk Factors

An investor should consider carefully the risks described below before making an investment decision. If any of the following risks were to occur, our business, financial condition or results of operations could be harmed.

Risks Relating to the Steel Industry and CSN

We are exposed to substantial swings in the demand for our steel, which has a substantial impact in the prices for our steel.

The steel industry behaves in a highly cyclical manner both in Brazil and abroad. In addition, as the Brazilian steel industry produces substantially more steel than the domestic economy is able to consume, the Brazilian steel industry is heavily dependent on export markets. The demand for steel products and, thus, the financial condition and results of operations of companies in the steel industry, including us, are generally affected by macroeconomic fluctuations in the world economy and domestic economies of steel-producing countries, including trends in the automotive, construction, home appliances, packaging and distribution sectors. In recent years, the price of steel in world markets has been at historically high levels, but these price levels may not continue. Since 2003, demand for steel products from developing countries (particularly China), the strength of the Euro and overall worldwide economic growth have contributed to historically high prices for our steel products, but these relatively high prices may not continue. Any material decrease in demand for steel in domestic or export markets served by us could have a material adverse effect on our business, financial condition and results of operations.

We face significant competition, including price competition and competition from other producers, which may adversely affect our profitability and market share.

The steel industry is highly competitive with respect to price. Over the last decade, the world steel industry was adversely affected by excess worldwide production capacity, reflecting the decreasing demand for steel in Western industrial countries and significant increases in steel production capacity in countries outside the Organization for Economic Development, or OECD. Further, continuous advances in materials sciences and resulting technologies have given rise to products such as plastics, aluminum, ceramics and glass that compete with steel in various segments. Due to high start-up costs, the economics of operating a steelworks facility on a continuous basis may encourage mill operators to maintain high levels of output, even in times of low demand, which increases the pressure on industry profit margins. In addition, downward pressure on steel prices by our competitors may affect our profitability.

The steel industry is also highly competitive with respect to product quality and customer service, as well as technological advances that would allow a steel manufacturer to lower its costs of production. In addition, most markets are served by several suppliers, often from different countries. Competition from foreign steel producers is strong and may increase due to increases in foreign steel installed capacity, appreciation of the *real* against the U.S. dollar and the reduction of domestic steel demand in other markets.

In addition, many factors influence our competitive position, including efficiency and operating rates, and the availability, quality and cost of raw materials and labor. China has recently become a net exporter of steel and may become one of the main international exporters of steel in the future. If we are unable to remain competitive with China or other producers in the future, our market share and financial performance may be adversely affected.

Protectionist measures adopted by the governments in some of our main markets could adversely affect our export sales.

In response to the increased production and exports of steel in many countries, anti-dumping, countervailing duties and safeguard measures have been imposed by countries which represent some of the main markets for our exports. Those and similar measures could create an imbalance in the international steel market, which could adversely affect our exports. For example, in March 2002, the U.S. government imposed certain quotas and tariffs on imports of a range of steel products. Although the U.S. lifted those tariffs in December 2003, there can be no assurance that the U.S. or other countries will not impose other quotas or tariffs and, if that occurs, we cannot quantify the impact on our exports and results of operations.

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The availability or increases in prices of raw materials that we need to produce steel, particularly coal and coke, may adversely affect our results of operations.

In 2006, the parent company s costs of raw materials accounted for approximately 53.2% of our total production costs, including outsourced slabs. Our principal raw materials include iron ore, coal, coke (a portion of which we make from coal), limestone, dolomite, manganese, zinc, tin and aluminum. We are dependent on third parties for some of our raw materials requirements. In addition, all of the coal that we use to produce coke and approximately 10-15% of our coke requirements are imported. Currently there is a worldwide shortage of coke and coal, mainly as a result of the rapid growth in the demand for steel globally. In 2006, there was a sharp rise in the cost of a number of commodities essential for the process of steel-making. In particular, the prices of zinc and nickel rose substantially due to a worldwide stock shortage. Any prolonged interruption in the supply of raw materials or energy, or substantial increases in their costs, could adversely affect the business, financial condition or results of operations of steel companies, including us. The availability and prices of raw materials may be negatively affected by, among other factors, new laws or regulations, suppliers allocations to other purchasers, interruptions in production by suppliers, accidents or similar events at suppliers premises or along the supply chain, worldwide price fluctuations, and the availability and cost of transportation.

Global developments, particularly the dramatic increase in Chinese and Indian demand for materials and inputs used in steel manufacturing, may cause severe shortages and/or substantial price increases in key raw materials and ocean transportation capacity. Inability to pass those cost increases on to our customers or to cater to our customers demands because of non-availability of key raw materials or other inputs, may harm our business, financial condition or results of operations.

New or more stringent environmental and health regulations imposed on us may result in increased liabilities and increased capital expenditures.

Our steel making, mining and logistics facilities are subject to a broad range of laws, regulations and permit requirements in Brazil relating to the protection of human health and the environment. Brazilian pollution standards are expected to continue to change through 2007, including new liquid effluent and air emission standards and solid waste handling regulations. New or more stringent environmental and health standards imposed on us can require us to make increased capital expenditures. We could be exposed to civil penalties, criminal sanctions and closure orders for non-compliance with these regulations, which, among other things, limit or prohibit emissions or spills of toxic substances produced in connection with our operations. Current and past waste disposal and emissions practices may result in the need for us to clean up or retrofit our facilities at substantial costs and could result in substantial liabilities.

Interruptions in the supply of natural gas and power transmission over the government power grid may adversely affect our business, financial condition and results of operations.

We require significant amounts of energy, both in the form of natural gas and electricity, to power our plant and equipment. We purchase our natural gas needs through distributors which purchase natural gas from Petróleo Brasileiro S.A. - Petrobras (the sole producer and supplier of natural gas in Brazil). Petrobras, in turn, is significantly dependent upon the supply of natural gas from Bolivia. On May 1, 2006, the president of Bolivia announced the nationalization of the country s gas reserves. The effects of this measure on the supply of natural gas in Brazil are still uncertain. The events in Bolivia could result in the disruption of the natural gas supply to Petrobras or an increase in the prices of natural gas. Any resulting interruptions or reductions in the levels of supply of natural gas by Petrobras to the distributors from whom we purchase our natural gas or a significant price increase may affect our production and production costs and consequently, our business, financial condition and results of operations.

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In addition, we rely on the government power grid for transmission of the electricity we produce to our facilities. Our production could be adversely affected, as a consequence of an electricity supply failure due to problems in transmission lines.

Accidents or malfunctions in our critical equipment may decrease or interrupt production, reducing our revenues. The insurance policies we hold may not cover all liabilities arising from such decreases or interruptions in production.

The steel production process depends on certain critical equipment, such as blast furnaces, steel converters, and continuous casting machines. This equipment may encounter serious malfunctions or damages. Significant interruptions in our production process may adversely impact the amounts of our production and consequently decrease our revenues.

The insurance policies held by us for losses in connection with operational risks, covering damages to our facilities (including damage to equipment and blockage of port facilities) and business interruption, may not be sufficient to cover all liabilities arising from a decrease or interruption in the production of the Presidente Vargas steelworks, including those related to the failure to deliver orders to clients in a timely manner as a result of such events.

In addition, if in the future we are not able to contract insurance policies on comparable terms to those currently in effect, our results of operation and financial condition may be adversely affected if we incur liabilities which are not completely covered by our insurance policies.

We are subject to risks related to judicial and administrative proceedings.

We are involved in numerous legal and administrative proceedings, including proceedings related to tax liabilities, labor and civil disputes. As of December 31, 2006, we recorded provisions for these proceedings in the total amount of R$1,820 million and judicially deposited a total amount of R$301 million in escrow.

It is not possible to predict the outcome of these proceedings. In the event that a substantial portion of these proceedings or one or more of the proceedings involving a substantial amount are decided against us, and in the event that no provision has been recorded, our results of operations may be adversely affected. In addition, even if sufficient provisions have been recorded, our liquidity may be adversely affected.

Our activities depend on authorizations from regulatory agencies, and changes in regulations could adversely affect our business.

Our activities depend on authorizations from and concessions by governmental regulatory agencies of the countries in which we operate. Our mining, mineral processing and logistics activities are also subject to laws and regulations that can change at any time. If these laws and regulations change in the future, modifications to our technologies and operations could be required, and we could be required to make unexpected capital expenditures.

We have experienced labor disputes in the past that have disrupted operations, and such disputes could recur.

A substantial number of our employees and some of the employees of our subcontractors are represented by labor unions and are covered by collective bargaining or other labor agreements, which are subject to periodic renegotiation. Strikes and other labor disruptions at any of our facilities or labor disruptions involving third parties who may provide us with goods or services, could adversely affect the operation of facilities, or the timing of completion and the cost of our capital projects.

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Risks Relating to Brazil

The Brazilian government has exercised, and continues to exercise, significant influence over the Brazilian economy. Brazilian political and economic conditions have a direct impact on our business.

The Brazilian government frequently intervenes in the Brazilian economy and occasionally makes significant changes in policy and regulations. The Brazilian government s actions to control inflation and other policies and regulations have often involved, among other measures, increases in interest rates, changes in tax policies, price controls (such as those imposed on the steel sector prior to privatization), currency devaluations, capital controls and limits on imports. Our business, financial condition and results of operations may be adversely affected by changes in policy or regulations involving or affecting factors, such as:

- interest rates;
- exchange controls and restrictions on remittances abroad, such as those which were imposed in 1989 and early 1990;
- currency fluctuations;
- inflation;
- price instability;
- energy shortages and rationing programs (such as occurred in 2001);
- liquidity of domestic capital and lending markets;
- tax policies and rules; and
- other political, social and economic developments in or affecting Brazil.

Uncertainty over whether the Brazilian government will implement changes in policy or regulation affecting these or other factors in the future may contribute to economic uncertainty in Brazil and to heightened volatility in the Brazilian securities markets and in the securities issued abroad by Brazilian issuers.

In addition, in October 2006, elections were held in all states of Brazil and at the federal level, to elect state governors and the president. It is impossible to foresee how new policies that may be adopted by the re-elected president or by the state governors would affect the Brazilian economy or our business.

Historically, the political scenario in Brazil has influenced the performance of the Brazilian economy in the past; in particular, political crises have affected the confidence of investors and the public in general, which adversely affected the economic development in Brazil.

These and other future developments in the Brazilian economy and governmental policies may adversely affect us and our business and results of operations and may adversely affect the trading price of our common shares and ADSs.

Inflation and government efforts to combat inflation may contribute significantly to economic uncertainty in Brazil and to heightened volatility in the Brazilian securities markets and, consequently, may adversely affect the

market value of our common shares and ADSs.

Brazil has experienced extremely high rates of inflation in the past. More recently, Brazil s annual rate of inflation was 12.4% in 2004, 1.2% in 2005, and 3.8% in 2006, as measured by general market price index (*Índice Geral de Preços Mercado)*, or the IGP- M. Inflation, and certain government actions taken to combat inflation, have in the past had significant negative effects on the Brazilian economy. Actions taken to combat inflation, coupled with public speculation about possible future governmental actions, have contributed to economic uncertainty in Brazil and heightened volatility in the Brazilian securities markets.

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Future Brazilian government actions, including interest rate decreases, intervention in the foreign exchange market and actions to adjust or fix the value of the *real* may trigger increases in inflation. If Brazil experiences high inflation again in the future, our operating expenses and borrowing costs may increase, our operating and net margins may decrease and, if investor confidence decreases, the price of our common shares and ADSs may fall.

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

As a result of inflationary pressures, among other factors, the Brazilian currency has devalued periodically during the last four decades. Throughout this period, the Brazilian government has implemented various economic plans and utilized a number of exchange rate policies, including sudden devaluations, periodic mini-devaluations during which the frequency of adjustments has ranged from daily to monthly, floating exchange rate systems, exchange controls and dual exchange rate markets. Although over long periods depreciation of the Brazilian currency generally has correlated with the rate of inflation in Brazil, devaluation over shorter periods has resulted in significant fluctuations in the exchange rate between the Brazilian currency and the U.S. dollar and other currencies.

The *real* depreciated against the U.S. dollar by 9.3% in 2000 and 18.7% in 2001. In 2002, the *real* depreciated 52.3% against the U.S. dollar, due in part to political uncertainty surrounding the Brazilian political elections and the global economic slowdown. Although the *real* appreciated 8.1%, 11.8%, 8.7% and 4.1% against the U.S. dollar in 2004, 2005, 2006 and the first three months of 2007, respectively, no assurance can be given that the *real* will not depreciate or be devalued against the U.S. dollar again.

Historically, depreciations in the *real* relative to the U.S. dollar have also created additional inflationary pressures in Brazil by generally increasing the price of imported products and requiring recessionary government policies to curb aggregate demand. On the other hand, appreciation of the *real* against the U.S. dollar may lead to a deterioration of the current account and the balance of payments, as well as dampen export-driven growth. Depreciations generally curtail access to foreign financial markets and may prompt government intervention, including recessionary governmental policies. Depreciations of the *real* relative to the U.S. dollar would also reduce the U.S. dollar value of distributions and dividends on our ADSs and may also reduce the market value of our common shares and ADSs.

In the event the *real* devaluates in relation to the U.S. dollar, the cost in *reais* of our foreign currency-denominated borrowings and imports of raw materials, particularly coal and coke, will increase. To the extent that we do not succeed in promptly reinvesting the funds received from such borrowings in dollar-denominated assets, we are exposed to a mismatch between our foreign currency-denominated expenses and revenues. On the other hand, if the appreciation trend of the past few years continues, it will cause *real*-denominated production costs to increase as a percentage of total production costs.

Developments and perceptions of risk in other countries, especially emerging market countries, may adversely affect the trading price of Brazilian securities, including our common shares and ADSs.

The market value of securities of Brazilian issuers is affected to varying degrees by economic and market conditions in other countries, including other Latin American and emerging market countries. Although economic conditions in such countries may differ significantly from economic conditions in Brazil, the reaction of investors to developments in these other countries may have an adverse effect on the market value of securities of Brazilian issuers. Crises in other emerging market countries may diminish investor interest in securities of Brazilian issuers, including ours. This could adversely affect the trading price of our common shares and ADSs, and could also make it more difficult for us to access the capital markets and finance our operations in the future on acceptable terms or at all.

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Risks Relating to a Routine SEC Review

An ongoing SEC review of our registration statement on Form F-4, filed in connection with a proposed public debt exchange offer, may require us to further amend this annual report.

We are in the process of responding to comments made by the staff of the SEC regarding our registration statement on Form F-4, filed on September 19, 2005. That registration statement was filed in connection with a proposed public exchange offer of notes originally issued in a non-public transaction. Until our responses to the SEC s comments are finalized, our capital-raising activities will be limited to the U.S. non-public markets and the markets outside the United States.

Risks Relating to our Common Shares and ADSs

If holders of ADSs exchange the ADSs for common shares, they risk losing the ability to remit foreign currency abroad and Brazilian tax advantages.

The Brazilian custodian for the common shares has obtained an electronic certificate of registration from the Central Bank permitting it to remit foreign currency abroad for payments of dividends and other distributions relating to the common shares or upon the disposition of the common shares. If holders of ADSs decide to exchange their ADSs for the underlying common shares, they will be entitled to continue to rely on the custodian s electronic certificate of registration for five business days from the date of exchange. Thereafter, such holders of ADSs may not be able to obtain and remit foreign currency abroad upon the disposition of, or distributions relating to, the common shares unless they obtain their own electronic certificate of registration or register their investment in the common shares pursuant to Resolution No. 2,689, which entitles certain foreign investors to buy and sell securities on the São Paulo Stock. Holders who do not qualify under Resolution No. 2,689 will generally be subject to less favorable tax treatment on gains with respect to the common shares. If holders of ADSs attempt to obtain their own electronic certificate of registration, they may incur expenses or suffer delays in the application process, which could delay their ability to receive dividends or distributions relating to the common shares or delay the return of their capital in a timely manner. In addition, we cannot assure you that the custodian s electronic certificate of registration or any certificate of foreign capital registration obtained by a holder of ADSs will not be affected by future legislative or other regulatory changes, or that additional restrictions applicable to such holder, to the disposition of the underlying common shares or to the repatriation of the proceeds from such disposition will not be imposed in the future.

Holders of ADSs may not be able to exercise their voting rights.

Holder of ADSs may only exercise their voting rights with respect to the underlying common shares in accordance with the provisions of the deposit agreement. Under the deposit agreement, ADS holders must vote by giving voting instructions to the depositary. Upon receipt of the voting instructions of the ADS holder, the depositary will vote the underlying common shares in accordance with these instructions. Otherwise, ADS holders will not be able to exercise their right to vote unless they surrender the ADS for cancellation in exchange for the common shares. Pursuant to our bylaws, the first call for a shareholders meeting must be published at least 15 days in advance of the meeting, the second call must be published at least eight days in advance of the meeting. When a shareholders meeting is convened, holders of ADSs may not receive sufficient advance notice to surrender the ADS in exchange for the underlying common shares to allow them to vote with respect to any specific matter. If we ask for voting instructions, the depositary will notify ADS holders of the upcoming vote and will arrange to deliver the proxy card. We cannot assure that ADS holders will receive the proxy card in time to ensure that they can instruct the depositary to vote the shares. In addition, the depositary and its agents are not responsible for failing to carry out voting instructions or for the manner of carrying out voting instructions. As a result, holders of ADSs may not be able to exercise their voting rights.

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The relative volatility and illiquidity of the Brazilian securities markets may substantially limit the ability of holders of our common shares or ADSs to sell the common shares underlying the ADSs at the price and time they desire.

Investing in securities, such as the common shares or the ADSs, of issuers from emerging market countries, including Brazil, involves a higher degree of risk than investing in securities of issuers from more developed countries.

The Brazilian securities markets are substantially smaller, less liquid, more concentrated and more volatile than major securities markets in the United States and other jurisdictions, and are not as highly regulated or supervised as some of these other markets. The relatively small market capitalization and illiquidity of the Brazilian equity markets may substantially limit the ability of holders of our common shares or ADSs to sell the common shares or the ADSs at the price and time desired. There is also significantly greater concentration in the Brazilian securities markets than in major securities markets in the United States. See Item 9C. Markets Trading on the São Paulo Stock Exchange .

The sale of a substantial number of common shares, or the belief that this may occur, could decrease the trading price of the common shares and the ADSs; holders of our common shares and/or ADSs may not be able to sell their securities at or above the price they paid for them.

Holders of our ADSs might be unable to exercise preemptive rights with respect to the common shares.

Holders of our ADSs may not be able to exercise the preemptive rights relating to the common shares underlying their 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 or other securities relating to these preemptive rights and we cannot assure holders of our ADSs that we will file any such registration statement. Unless we file a registration statement or an exemption from registration applies, holders of our ADSs may receive only the net proceeds from the sale of their preemptive rights by the depositary or, if the preemptive rights cannot be sold, the rights will be allowed to lapse.

***Judgments of Brazilian courts with respect to our common shares will be payable only in* reais.**

If proceedings are brought in the courts of Brazil seeking to enforce our obligations in respect of the common shares, we will not be required to discharge our obligations in a currency other than *reais*. Under Brazilian exchange control limitations, an obligation in Brazil to pay amounts denominated in a currency other than *reais* may only be satisfied in Brazilian currency at the exchange rate, as determined by the Central Bank, in effect on the date the judgment is obtained, and such amounts are then adjusted to reflect exchange rate variations through the effective payment date. The then prevailing exchange rate may not afford non-Brazilian investors with full compensation for any claim arising out of or related to our obligations under the common shares or the ADSs.

Item 4. Information on the Company

4A. History and Development of the Company

General

We are the second largest fully integrated steel producer in Brazil and one of the largest in Latin America in terms of crude steel production. Our current annual crude steel capacity and rolled product capacity is 5.6 million and 5.1 million tons, respectively. Production of crude steel and rolled steel products decreased in 2006 to 3.5 million and 4.2 million tons, respectively.

Our fully-integrated manufacturing facilities produce a broad line of steel products, including slabs, hot- and cold-rolled, galvanized and tin mill products for the distribution, packaging, automotive, home appliance and construction industries. In 2006, we accounted for approximately 42.0% of the galvanized steel products sold in Brazil. We are also one of the world s leading producers of tin mill products for packaging containers. In 2006, we accounted for approximately 98% of the tin mill products sold in Brazil.

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Our production process is based on the integrated steelworks concept. Following is a brief summary of the steel making process at our Presidente Vargas steelworks, located in the city of Volta Redonda, Rio de Janeiro State:

- iron ore produced from our own mines is processed in continuous sintering machines to produce sinter;
- the sinter and lump ore direct charges are smelted with lump coke and injected powdered coal in blast furnaces to produce the molten iron formed during the first smelting of iron ore, or pig iron; and
- the pig iron is then refined into steel by means of basic oxygen converters.

In addition to owning our own source of iron ore, we also currently produce from our own mines our total requirements of limestone and dolomite and a portion of our tin requirements. Using imported coal, we produce approximately 75-80% of our coke requirements, at current production levels, in our own coke batteries at Volta Redonda. Imported coal is also pulverized and used directly in the pig iron production process. Zinc, manganese ore, aluminum and a portion of our tin requirements are purchased in local markets. Our steel production and distribution also require water, gases, electricity, rail and road transportation, and port facilities.

History

Companhia Siderúrgica Nacional is a Brazilian corporation (*sociedade por ações*) incorporated in 1941 pursuant to a decree of Brazilian President Getúlio Vargas. The Presidente Vargas steelworks, located at Volta Redonda, in Rio de Janeiro State, started production in 1946, initially producing coke, pig iron castings and long products.

Three major expansions were undertaken at the Presidente Vargas steelworks during the 1970s and 1980s. The first, completed in 1974, increased installed annual production capacity to 1.6 million tons of crude steel. The second, completed in 1977, raised capacity to 2.4 million tons of crude steel. The third, completed in 1989, increased capacity to 4.5 million tons of crude steel.

We were privatized through a series of auctions held in 1993 and early 1994, through which the Brazilian government sold its 91% interest in our company.

From 1993 through 2002, we implemented a capital improvement program aimed at increasing our annual production of crude steel, improving the productivity of our production units and the quality of our products and enhancing our environmental protection and cleanup programs. As part of the investments made under the capital improvement program, since February 1996, all our production has been based on the continuous casting process, rather than ingot casting, an alternative method that results in higher energy use and metal loss. From 1996 through 2002, we spent the equivalent of US$2.4 billion under the capital improvement program and for operational capacity maintenance, culminating with the revamping in 2001 of Blast Furnace No. 3 and Hot Strip Mill No. 2 at the Presidente Vargas steelworks that have increased our annual production capacity to 5.6 million tons of crude steel and 5.1 million tons of rolled products.

Additional projects completed under the capital improvement program include:

- the installation of a pulverized coal injection, or PCI, system;
- the start-up of a vacuum-degasser unit and a ladle furnace, to improve steel quality and allow us to supply high-end products to the more stringent automotive and packaging industries specifications;

- the start-up of continuous casting machine No. 4; and

- the start-up of a 238-MW thermoelectric co-generation power plant, designed to supply 60% of the Presidente Vargas steelworks current energy requirements, using as its primary fuel the waste gases generated by our coke ovens, blast furnaces and steel processing facilities. This power plant also produces steam for the steelworks rolling facilities and coking plant and blown air for their blast furnaces.

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Accident in Blast Furnace No. 3

In January 2006, we had an accident involving the gas cleaning system adjacent to Blast Furnace No. 3 at the President Vargas steelworks. The accident prevented us from operating the equipment for approximately six months, impacting our operating revenues, as a result of reduced sales volumes, cost of goods sold, as a result of having to purchase slabs from third-party sources, gross profit and operating income, as further explained in Item 5A. Operating Results Results of Operations 2006 Compared to 2006 . In order to meet our customers purchasing orders during the period in which Blast Furnace No. 3 was under repair, we purchased slabs and coils from third-party sources, therefore increasing our costs of goods sold in 2006.

Capital Expenditures

We invested US$178 million, US$290 million and US$706 million in 2004, 2005 and 2006 to further improve productivity levels and to maintain our operational capacity. The expenditures were for, among other things, equipment revamping, spare parts purchases, building repairs, equipment automation and information technology at our facilities.

We have also implemented our strategy of developing downstream opportunities, new products and market niches by creating or expanding capacity of galvanized products for the automotive sector and by investing in a galvanizing and pre-painting plant for supply to the construction and home appliance industry sectors, as described in Item 4B. Business Overview Facilities.

We also intend to control production costs and secure reliable sources of raw materials, energy and transportation in support of our steelmaking operations through a program of strategic investments. The principal strategic investments already implemented are set forth in Item 4B. Business Overview Facilities .

Acquisitions

In June 2004, we acquired the remaining 49% ownership interest in GalvaSud from our then partner Thyssen-Krupp Stahl AG., or TKS, for US$28.5 million, becoming the sole owner of GalvaSud, and repaid GalvaSud s project finance debt resulting for the formation of the joint venture in 1998, including the portion that had been guaranteed by TKS, which aggregated US$132 million. GalvaSud produces and sells galvanized steel *Galvanew*®, laser-welded and pre-stamped parts for the automotive industry.

In April 2005, we purchased from Brascan Brasil Ltda., 100% of the capital stock of Estanho de Rondônia S.A., or ERSA, and the assets of a tin mine and a smelter located in Rondônia state, Brazil, for US$38.8 million. The inventory of the geological reserves has been prepared from a review of the major reports from the Santa Barbara Mine Document Center. The majority of the deposits and/or target areas are within Mining Leases that have been consolidated into a Mining Group (*Grupamento Mineiro* No. 131/92). The reserves provided were recognized by DNPM, Brazil s competent authority for the reporting of ore reserves. The reserves and resources presented are *in situ* .

In May 2006, we entered into an agreement with Corus Group Plc, to purchase the remaining 50% of the capital stock of Lusosider Projectos Siderúrgicos S.A., or Lusosider for approximately US$31.9 million. This acquisition was duly approved by the Portuguese Competition Authority and further concluded on August 31, 2006. Lusosider produces approximately 240,000 tons of galvanized products, 50,000 tons of cold rolled and 60,000 tons of tin plate annually. Its main customers include service centers, food and general line can making and steel packaging industries.

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On June 5, 2006, we acquired 100% of the shares of Companhia Metalúrgica Prada, or Prada, from Kiskidee Investments Limited LLC, for a total of US$1.00. Prada is the largest steel can manufacturer in Brazil and produces more that one billion steel cans in its four production units located in São Paulo, Santa Catarina and Minas Gerais states, in the southeastern and southern regions of Brazil and, accordingly, is one of our major customers of tin mill products.

Planned Investments

Iron Ore Project (Casa De Pedra)

In January 2004, we announced the approval of investments of approximately US$1.5 billion to expand our iron ore production, which are currently being implemented. The investments will be financed by BNDES, which already approved credit lines of up to US$393.6 million indexed based on the long term reference interest rate, *Taxa de Juros a Longo Prazo*, or TJLP, by other export credit agencies, resources obtained in the capital markets in general and the use of free cash flow from our current operations. These investments comprise the expansion of our mining activities, our port facilities and the construction of pellet plants. We expect full capacity of the project to be achieved by July 2011. The main investments to be made are the following:

- expansion of the annual production of the Casa de Pedra iron ore mine from approximately 16 million tons to 53 million tons;
- expansion of the coal terminal adjacent to our Itaguaí Port facilities to enable annual exports of up to 40 million tons of iron ore; and
- construction of two pellet plants, each with capacity of three million tons per year.

Additionally, in 2006, pursuing our strategy to increase value for our shareholders and strengthen our position as a global player, our Board of Directors approved new investments of over US$4 billion over the next three years, comprised as follows:

Steelmaking (Slab Mills)

We plan to invest approximately US$3.6 billion to build greenfield slab mills, located in Itaguaí, State of Rio de Janeiro, close to CSN s port terminals, and/or in the State of Minas Gerais, that are expected to be concluded in October 2009. As part of our strategy to strengthen our position as a global player, we are seeking to take advantage of our existing competitive iron ore mine and integrated infra-structure to produce slabs that will feed downstream operations in the United States and/or Europe. We intend to finance these investments with BNDES, other export credit agencies and the use of free cash flow from our current operations.

Long Steel Production

We are also investing in the long steel segment, in order to be strategically positioned to take advantage of the current construction boom in Brazil. We have been taking advantage of our existing infrastructure in the Presidente Vargas steelworks by revamping a former foundry unit in Volta Redonda and plan to invest a total of approximately US$113 million in the necessary installations, including expanding and upgrading a 30-ton electric furnace. The new facility is expected to be concluded in December 2008 and to produce 500,000 tons of long steel per year from surplus pig iron and low added- value slabs. We intend to finance these investments with BNDES, other export credit agencies and the use of free cash flow from our current operations.

Cement Project

This project represents the entrance of CSN into the cement market, taking advantage of the slag generated by our blast furnaces and of our limestone reserves, located in Arcos, Minas Gerais. These two raw materials, slag and limestone, which is further transformed into clinker, account for approximately 95% of the production cost to produce cement. We are investing approximately US$185 million to build a greenfield grinding mill and clinker furnace, with capacity of 3 million tons and 825,000 tons, which we expect will be concluded in January and November 2008, respectively. These investments will be financed by BNDES, which has already approved a seven-year credit line of up to R$66.8 million indexed based on the TJLP, as well as the use of free cash flow from our current operations.

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Transnordestina

In August 2006, our Board of Directors approved a transaction to merge Transnordestina, an infrastructure project led by the Federal Government of Brazil, into Companhia Ferroviária do Nordeste CFN, which is a 30-year concession granted to CSN in 1998 to operate the Northeastern Railroad of the RFFSA with 4,238 km of railway track. Investments of approximately US$2,067.8 million were approved to revamp 800 km of an existing railway track and to build an additional 1,000 km of large gauge, world class railway track. The investments will allow the company to increase the transportation of various products, such as soy beans, cotton, sugar cane, fertilizers, oil and fuels, iron ore and limestone. The investments will be financed mainly with equity and debt from the Brazilian Federal Government through BNDES, FINOR Northeastern Investment Fund and FDNE Northeastern Development Investment Fund. We will invest up to R$1 billion to the extent required to complete the investments mentioned above and only after full disbursement of approximately R$3.5 billion by the Federal Government and its agencies and investment funds.

Additional Investments

In addition to the currently planned investments and maintenance capital expenditures, we continue to consider possible acquisitions, joint ventures and brownfield or greenfield projects to increase or complement our steel producing capabilities.

Other Information

CSN s legal and commercial name is Companhia Siderúrgica Nacional. CSN is organized for an unlimited period of time. Its head offices are located at Avenida Brigadeiro Faria Lima, 3,400, 20th floor, 04538-132, São Paulo, SP, Brazil and its telephone number is +55-11-3049-7100. CSN s agent for service of process in the United States is CT Corporation, with offices at 1633 Broadway, New York, NY 10019.

4B. Business Overview

Competitive Strengths

We believe that we have the following competitive advantages:

Fully integrated business model. We believe we are one of the mostly fully integrated steelmakers in the world. We have captive iron ore reserves, which differentiates us from our main competitors in Brazil that purchase their iron ore requirements from mining companies such as CVRD. We have recently audited our mineral deposits at our Casa de Pedra iron ore mine. The results confirmed mineral resources in excess of 8.3 billion tons, out of which 1.6 billion tons of proven and probable reserves with a grade of approximate 48%. In addition to our iron ore reserves, we have captive dolomite and limestone mines that supply our Presidente Vargas steelworks. Our steelworks is close to the main steel consumer centers in Brazil, with easy access to port facilities and railroads. Our operations are strongly integrated as a result of our captive sources of raw materials, such as iron ore and cole, and our access to owned infrastructure, such as railroads and deep- sea water port facilities.

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Thoroughly developed logistics infrastructure. We have a thoroughly developed logistics infrastructure, from our iron ore mine to our steel mill to, finally, our ports. The location of our steelworks facility is next to railroad systems and port facilities, facilitating the supply of raw material, the shipment of our production and easy access to our principal clients. The concession for the main railroad used by us is owned by MRS, a company in which we hold 32.9% of the voting capital. The railway system connects the Presidente Vargas steelworks to the container terminal at Itaguaí Port, which handles most of our steel exports. Since we obtained the concession to operate MRS railway in 1996, we have significantly improved its tracks and developed its business, with strong cash generation. We also own concessions to operate two deep-sea water terminals from which we export our products and also import coal and small amounts of coke, which are the only important raw materials that we need to purchase from third-party sources.

Self-sufficiency in energy generation. We are self-sufficient in energy, through our interests in the hydroelectric plants of Itá and Igarapava, and our own thermoelectric plant inside the Presidente Vargas steelworks. We also sell excess energy we generate into the energy market. Our 238 MW thermoelectric co-generation plant provides the Presidente Vargas steelworks with approximately 60% of its energy needs for its steel mills, using as its primary fuel the waste gases generated by our coke ovens, blast furnaces and steel processing facilities. We indirectly hold 60.5% of the Itá hydroelectric plant that has installed capacity of 1,450 MW, with a guaranteed output of 668 MW. In addition, the Igarapava hydroelectric, with 210 MW fully installed capacity, representing a guaranteed output of 126 MW, supplies energy mainly to the Casa de Pedra and Arcos mines.

Low cost structure. As a result of our fully integrated business model, our thoroughly developed logistics infrastructure and our self sufficiency in energy generation, we have been constantly and consistently presenting substantially high margins. Other factors that lead to our high margins are the strategic location of our steelworks facility, the use of state of the art technology and our qualified work force.

Diverse product portfolio and product mix. We believe we have one of the best product mixes in Latin America as a whole, especially considering our 98% dominance in steel tin mill products in Brazil. We produce all kinds of steel packaging produced in Brazil at our tin plate steel mill and 50% of the galvanized flat steel produced in Brazil. We also produce a diversified portfolio of products to meet a wide range of customer needs across all steel consuming industries. We focus on selling high margin products, such as tin plate, pre-painted, galvalume and galvanized products, in our product mix. Our GalvaSud product provides material for exposed auto parts, using hot-dip galvanized steel and laser-welded blanks, which is a trend in this industry. This, together with our hot-dip galvanizing process know-how, should allow us to increase our sales to the automotive segment. Our subsidiary CSN Paraná, gives us additional capacity to produce high-quality galvanized, galvalume and pre-painted steel products for the construction and home appliance industries. In addition, our subsidiary, INAL, the largest flat steel distributor in Brazil, is a strong sales channel in the domestic market, enabling us to meet smaller customer demands, and therefore, to have a strong presence in retail market. We believe we are well positioned strategically to develop new products such as long steel and cement that are very important for the civil construction industries.

Strong presence in domestic market and strategic international exposure. We have a strong presence in the domestic market for steel products, with a 98% dominance of the steel tin mill product industry in Brazil and a large market for galvanized flat steel. In addition, our subsidiaries CSN LLC and Lusosider constitute significant sales channels for our products in the United States and Europe, respectively.

Strategy

Our mission is to increase value for our shareholders, maintaining our position as one of the world s lowest-cost steel producers. With this in mind, we intend to strengthen our position as a global player, optimizing our infrastructure assets (our mines, ports and railways) and their competitive cost advantages.

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To achieve this goal, we have adopted strategies in each of our four business segments (where we already have assets, current operations or inherited competitive advantages) as described below.

Steel

Our strategy related to our steel business involves:

- implementing a carefully crafted globalization strategy that may include association with or the acquisition and/or construction of steel operations, steel-related businesses or distribution or service centers outside Brazil, which could further process low cost semi-finished products (slabs) from Brazil and improve our distribution channels abroad;
- emphasizing a wide range of value-added products, mostly galvanized, pre-painted and tin-coated;
- introducing new technologies and systems to enhance our understanding of customers, competitors and industry trends; and
- providing customer solutions supported by quality products and services.

For further information on our planned investments relating to our steel activities, see Item 4A. History and Development of the Company Planned Investments Steel Making (Slab Mills) and Item 4A. History and Development of the Company Planned Investments Long Steel Production .

Mining

In order to strengthen our position as a player in the iron ore market, we plan to expand our mining asset Casa de Pedra (iron ore) mine and search for investment opportunities, primarily in mining operations related to the steel business. For further information on our planned investments relating to our mining activities, see Item 4A. History and Development of the Company Planned Investments Iron Ore Project (Casa de Pedra).

In this regard, in November 2006 we incorporated a new subsidiary named Nacional Minérios S.A. to study the acquisition of other iron ore bodies and trade iron ore from other miners as well.

In 2007, we made our first entry into the international iron ore market. The first step towards this goal was taken in February 2007, with the completion of the first phase of the expansion our coal seaport terminal in Itaguaí (RJ) which enabled it to also to handle and export iron ore, and the loading from its facilities of the first shipment of iron ore products from our subsidiary Nacional Minérios S.A.

Logistics

We expect to take advantage of and expand our logistics capabilities, including our integrated infrastructure operations (our railways and ports).

We have substantially improved the infrastructure needed to support the President Vargas steelworks and our export and international strategies by making investments in projects such as power generation through hydroelectric power plants, railways and port facilities in order to increase our ability to control production costs and secure reliable sources of energy, raw materials and transportation.

Cement

Our strategy for our cement business includes the achievement of greater usage of by-products by constructing a clinker furnace and a grinding mill to produce 3.0 million tons of cement, using the slag generated by our blast furnaces, which we expect will become operational in January and November 2008, respectively. For further information on our planned investments relating to our cement activities, see Item 4A. History and Development of the Company Planned Investments Cement Project.

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Major Products

We produce carbon steel, which is the world s most widely produced type of steel, representing the vast bulk of global steel consumption. From carbon steel, we sell a variety of steel products, both domestically and abroad, to manufacturers in several industries.

The following chart reflects our production cycle in general terms.

Our Presidente Vargas steelworks produces flat steel products slabs, hot-rolled, cold-rolled, galvanized and tin mill products. For further information on our production process, see Process .

Slabs

Slabs are semi-finished products used for processing hot-rolled, cold-rolled or coated coils and sheet products. We are able to produce continuously cast slabs with a standard thickness of 250 millimeters, widths ranging from 830 to 1,600 millimeters and lengths ranging from 5,250 to 10,500 millimeters. We produce medium and low carbon slabs, as well as micro-alloyed, ultra-low-carbon and interstitial free slabs.

Hot-rolled Products

Hot-rolled products comprise heavy-gauge hot-rolled coils and sheets and light-gauge hot-rolled coils and sheets. A heavy gauge hot-rolled product, as defined by Brazilian standards, is a flat-rolled steel coil or sheet with a minimum thickness of five millimeters. We are able to provide coils of heavy gauge hot-rolled sheet having a maximum thickness of 12.7 millimeters and cut sheet having a maximum thickness of 6.3 millimeters. Heavy gauge sheet steel is used to manufacture automobile parts, pipes, mechanical construction and other products.

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Light gauge hot-rolled coils and sheets produced by us have a minimum thickness of 1.2 millimeters and are used for welded pipe and tubing, automobile parts, gas containers, compressor bodies and cold-formed light shapes, channels and profiles for the construction industry.

Cold-rolled Products

Cold-rolled products comprise cold-rolled coils and sheets. A cold-rolled product, as defined by Brazilian standards, is a flat cold-rolled steel coil or sheet with thickness ranging from 0.30 millimeters to 3.00 millimeters. Compared to hot-rolled products, cold-rolled products have more uniform thickness and better surface quality and are used in applications such as automotive bodies, home appliances and construction. In addition, cold-rolled products serve as a base steel for our galvanized and tin mill products. We supply cold-rolled coils in thickness from 0.30 millimeters to 2.65 millimeters.

Galvanized Products

Galvanized products comprise flat-rolled steel coated on one or both sides with zinc or a zinc-based alloy applied by either a hot-dip or an electrolytic process. We use the hot-dip process, which is approximately 20% less expensive than the electrolytic process. Galvanizing is one of the most effective and low-cost processes used to protect steel against corrosion caused by exposure to water and the atmosphere. Galvanized products are highly versatile and can be used to manufacture a broad range of products, such as:

- bodies for automobiles, trucks and buses;
- manufactured products for the construction industry, such as panels for roofing and siding, dry wall and roofing support frames, doors, windows, fences and light structural components;
- air ducts and parts for hot air, ventilation and cooling systems;
- culverts, garbage containers and other receptacles;
- storage tanks, grain bins and agricultural equipment;
- panels and sign panels; and
- pre-painted parts.

Galvanized sheets, both painted and bare, are also frequently used for gutters and downspouts, outdoor and indoor cabinets, all kinds of home appliances and several similar applications. We produce galvanized sheets and coils in continuous hot-dip processing lines, with thickness ranging from 0.30 millimeters to 2.70 millimeters. The continuous process results in products with highly adherent and uniform zinc coatings capable of being processed in nearly all kinds of bending and heavy machinery.

In addition to standard galvanized products, we produce *Galvanew*®, galvanized steel that is subject to a special annealing process following the hot-dip coating process. This annealing process causes iron to diffuse from the base steel into the zinc coating. The resulting iron- zinc alloy coating allows better welding and paint performance. The combination of these qualities makes our *Galvanew*® product particularly well suited for manufacturing automobile and home appliance parts including high gloss exposed parts.

At CSN Paraná, one of our subsidiaries, we produce galvalume, a cold-rolled material coated with a zinc-aluminum alloy. The production process is similar to hot-dip galvanized coating, and galvalume has at least twice the corrosion resistance of standard galvanized steel. Galvalume is primarily used in outdoor construction applications that may be exposed to severe acid corrosion environment like marine atmosphere.

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The added value from the galvanizing process permits us to price our galvanized products with a higher profit margin. Our management believes that our value-added galvanized products present one of our best opportunities for profitable growth because of the anticipated increase in Brazilian demand for such high margin products.

Through CSN Paraná, we also produce pre-painted flat steel, which is manufactured in a continuous coating line. In this production line, a layer of resin-based paint in a choice of colors is deposited over either cold-rolled or galvanized base materials. Pre-painted material is a high value-added product used primarily in the construction and home appliance markets.

Tin Mill Products

Tin mill products comprise flat-rolled low- carbon steel coils or sheets with, as defined by Brazilian standards, a maximum thickness of 0.49 millimeters, coated or uncoated. Coatings of tin and chromium can be applied by various electrolytic and hot-dip processes. Coating costs place tin mill products among the highest priced products that we sell. The added value from the coating process permits us to price our tin mill products with a higher profit margin. There are four types of tin mill products, all produced by us in coil and sheet forms:

- tin plate - coated on one or both faces with a thin metallic tin layer plus a chromium oxide layer, covered with a protective oil film;
- tin free steel - coated on both faces with a very thin metallic chromium layer plus a chromium oxide layer, covered with a protective oil film;
- low tin coated steel - coated on both faces with a thin metallic tin layer plus a thicker chromium oxide layer, covered with a protective oil film; and
- black plate - uncoated product used as the starting material for the coated tin mill products.

Tin mill products are primarily used to make cans and other containers. With six electrolytic coating lines, we are one of the biggest producers of tin mill products in the world and the sole producer of coated tin mill products in Brazil.

Production

Production Process

The principal raw materials for steel production in an integrated steelworks are iron ore, coal, coke, and fluxes like limestone and dolomite. The iron ore consumed at the Presidente Vargas steelworks is extracted, crushed, screened and transported by railway from our Casa de Pedra mine located in Congonhas, Minas Gerais State, 328 km from the Presidente Vargas steelworks. The high quality ores mined and sized at Casa de Pedra, with iron content of approximately 60%, and their low extraction costs are major contributors to our low steel production costs.

Because Brazil lacks quality coking coals, we import all the coal required for coke production. The coal is then charged in coke batteries to produce coke through a distillation process. See - Raw Materials and Energy Requirements . This coal distillation process also produces coke oven gas as a by-product, which we use as a main source of fuel for our thermoelectric co-generation power plant. After being screened, coke is transported to blast furnaces, where it is used as a combustion source and as a component for transforming iron ore into pig iron. In 2006, we produced about 75-80% of our coke needs and imported the balance. At sintering plants, fine-sized iron ore and coke or other fine-sized solid fuels are mixed with fluxes (limestone and dolomite) to produce sinter.

The sinter, lump iron ore, fluxing materials and coke are then loaded into our two operational blast furnaces for smelting. We operate a PCI facility, which injects low-cost pulverized coal directly into the blast furnaces as a substitute for approximately one-third of the coke otherwise required.

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The iron ore is reduced to pig iron through successive chemical reactions with carbon monoxide (from the coke and PCI) in two blast furnaces that operate 24 hours a day. The ore is gradually reduced, then melts and flows downward. Impurities are separated from the iron to form a liquid slag with the loaded fluxes (limestone and dolomite). From time to time, white- hot liquid iron and slag are drawn off from the bottom of the furnace. Slag (containing melted impurities) is granulated and sold to neighboring cement companies. Upon completion of our planned cement plant expected to occur by 2008, slag also will be used to produce cement.

The molten pig iron is transported to the steelmaking shop by 350-ton capacity torpedo cars and charged in basic oxygen furnaces together with scrap and fluxes. In the basic oxygen furnaces, oxygen is blown onto the liquid burden to oxidize its remaining impurities and to lower its carbon content, thus producing liquid steel. The molten steel is conveyed from the basic oxygen furnaces into the continuous casting machines from which crude steel (i.e., rectangular shaped slabs) is produced. A portion of the slab products is sold directly in the export market.

The hot-rolling, reheated slabs from the continuous casting machines are fed into hot strip mills to reduce the thickness of the slabs from 250 millimeters to a range between 1.2 and 12.7 millimeters. At the end of the hot strip mill, the long, thin steel strip from each slab is coiled and conveyed to a cooling yard. Some hot-rolled coils are dispatched directly to customers in the as-rolled condition. Others are further processed in the pickling line, in a hydrochloric bath, to remove surface oxides and improve surface quality. After pickling, the hot-rolled coils selected to produce thinner materials are sent to be rolled in cold strip mills. The better surface characteristics of cold-rolled products enhance their value to customers as compared to hot-rolled products. Additional processing related to cold-rolling may further improve surface quality. Following cold-rolling, coils may be annealed, coated (by a hot dip or electrolytic tinning process) and painted, to enhance medium-and long-term anti-corrosion performance and to add characteristics that will broaden the range of steel utilization. Coated steel products have higher profit margins than bare steel products. Of our coated steel products, tin mill and galvanized products are our highest margin products.

Steel plant equipment regularly undergo scheduled maintenance shutdowns. Typically the rolling mills and coating lines are maintained on a weekly or monthly basis whereas the blast furnaces and other special equipment are scheduled for routine maintenance on a semi-annual or annual basis.

Quality Management Program

We practice Total Quality Management, a set of techniques that have been adopted by many leading transnational companies. We also maintain a Quality Management System that has been certified to be in compliance with the ISO 9001 standards set forth by the International Standardization Organization, or ISO. In October 2003, we were awarded the ISO 9000: 2000 certificate for the design and manufacture of hot-rolled, pickled and oiled products, cold-rolled, galvanized and tin mill products, which replaced the ISO 9001 Certificate that we were awarded in December 1994. In October 2003, we were also awarded the automotive industry s Technical Specification - 16949: 2002, for the design and manufacture of hot-rolled, pickled and oiled, cold-rolled and galvanized products, which replaced the QS 9000 standards that we were awarded in 1997. Some important automotive companies, like Volkswagen, General Motors and Ford, require their suppliers to satisfy the QS 9000 standards.

Production Output

The following table sets forth, for the periods indicated, the annual production of crude steel within Brazil and by us and the percentage of Brazilian production attributable to us.

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CRUDE STEEL PRODUCTION
(In millions of metric tons)

	Brazil	CSN	CSN% of Brazil
2006	30.9	3.5 *	11.3%
2005	31.6	5.2	16.5%
2004	32.9	5.5	16.8%
2003	31.1	5.3	17.0%
2002	29.6	5.1	17.2%

Source: Instituto Brasileiro de Siderurgia IBS (Brazilian Steel Institute)
*Lower production due to accident at Blast Furnace No. 3 on January 22, 2006.

The following table contains some of our operating statistics for the periods indicated.

CERTAIN OPERATING STATISTICS
(In millions of metric tons)

	2004	2005	2006[1]
Production of:			
Iron Ore	15.5	13.7	13.1
Molten Steel	5.7	5.3	3.6
Crude Steel	5.5	5.2	3.5
Hot-rolled Coils and Sheets	5.1	4.8	4.1
Cold-rolled Coils and Sheets	2.8	2.6	2.3
Galvanized Products	1.3	1.0	1.1
Tin Mill Products	1.0	1.0	0.8
Consumption of Coal for Coke Batteries	2.3	2.3	2.0
Consumption of Coal for PCI[2]	0.9	0.8	0.5

(1) Lower production due to accident at Blast Furnace No. 3 on January 22. 2006.
(2) Pulverized coal injection

Raw Materials and Suppliers

The principal raw materials we use in our integrated steel mill include iron ore, coke, coal (from which we make coke), limestone, dolomite, aluminum, tin and zinc. In addition, our production operations consume water, gases, electricity and ancillary materials.

Raw Materials and Energy Requirements

Iron Ore. We obtain all of our iron ore requirements from our Casa de Pedra mine in Minas Gerais State, which has an installed mining capacity of 21.5 million tons annually (run-of-mine or ROM) with a processing ratio of 74.4%, resulting in a mining capacity of 16 million tons of processed iron ore per year. In 2006, the run-of-mine was 17.5 million tons, resulting in 13.1 million tons of processed iron ore per year. Of this total, 4.8 million tons were utilized

at the Presidente Vargas steelworks and 3.2 million tons were sold to third parties, consisting of 1.9 million tons of sinter-feed material, 0.4 million tons of pellet feed materials, 0.5 million tons of lump ore and 0.5 million tons of small lump ore. In addition, approximately 5.1 million tons of processed iron ore were kept in inventory in 2006.

We process the iron ore at the mine site prior to shipment by railway to the Presidente Vargas steelworks. See the map under Item 4D. Property, Plant and Equipment for the location of the Casa de Pedra mine in relation to the Presidente Vargas steelworks.

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Coal. In 2006, our coal consumption totaled 2.5 million tons and accounted for approximately 16% of our production cost. The 20% reduction compared to the 2005 consumption is due to the stoppage of Blast Furnace No. 3 in the first half of 2006, from January to June. Because of the cyclical nature of the coal industry, price and quantity terms contained in our coal supply contracts, which are denominated in U.S. dollars, are usually renegotiated annually. Thus, our coal costs can vary from year to year.

Coke. In 2006, in addition to the approximately 1.5 million metric tons of coke we produced, we also consumed 152,000 tons of coke bought from third parties in China and Colombia. The market for coke has been very tight since 2002, because China, a major player in the sea- borne trade, has increased its internal consumption and adopted restrictive export quotas.

We use a PCI system that allows us to use less coke in our blast furnaces, substituting a portion of the coke with lower grade coal. The PCI system has reduced our need for imported coal and imported coke, thereby reducing our production costs. In 2006, we used approximately 479,000 tons of imported PCI coal.

Limestone and Dolomite. We obtain limestone and dolomite from our Bocaina mine at Arcos in Minas Gerais State, which produces 1.6 million tons of limestone and 0.9 million tons of dolomite on an annual basis, more than 90% of which is used in the steelmaking process. See the map under Item 4D. Property, Plants and Equipment for the location of the Bocaina mine in relation to the Presidente Vargas steelworks.

Aluminum, Zinc and Tin. Aluminum is mostly used for steelmaking. Zinc and tin are important raw materials used in the production of certain higher-value steel products, such as galvanized and tin plate, respectively. We purchase aluminum, zinc and tin typically from third-party domestic suppliers under one- or two-year contracts. We maintain approximately a one-week reserve of such materials at the Presidente Vargas steelworks.

In April 2005, we acquired ERSA, a tin mine and smelter facility. This smelter was one of our main tin suppliers in 2004. We intend to increase production from 1,800 tons in 2005 to 3,800 tons in 2009, in order to achieve self-sufficiency of this raw material.

Other Raw Materials. In our production of steel, we also consume, on an annual basis, significant amounts of spare parts, refractory bricks and lubricants, which are generally purchased from domestic suppliers.

We also consume significant amounts of oxygen, nitrogen, hydrogen, argon and other gases at the Presidente Vargas steelworks. These gases are supplied by a third party under long-term contracts from its gas production facilities located on the Presidente Vargas steelworks site. In 2006 we used 575,00 tons of oxygen to produce 3.5 million tons of crude steel.

Water. Large amounts of water are also required in the production of steel. Water serves as a solvent, a catalyst and a cleaning agent. It is also used to cool, to carry away waste, to help produce and distribute heat and power and to dilute liquids. Our source of water is the Paraíba do Sul River, which runs through the city of Volta Redonda. Over 80% of the water used in the steelmaking process is recirculated and the balance, after processing, is returned to the Paraíba do Sul River. Since March 2003, the Brazilian government has imposed a monthly tax for our use of water from the Paraíba do Sul River, based on an annual fee of approximately US$0.8 million.

Electricity. Steelmaking also requires significant amounts of electricity to power rolling mills, production lines, hot metal processing, coking plants and auxiliary units. In 2005, the Presidente Vargas steelworks consumed approximately 3.0 million MWh of electric energy or 580 kilowatt hours per ton of crude steel. This consumption made us one of the largest consumers of electricity in Brazil, accounting for approximately 11.6% of the overall consumption of electricity in Rio de Janeiro State. Our current sources of electricity are our

238-MW thermoelectric co-generation power plant at the Presidente Vargas steelworks and the Itá and Igarapava hydroelectric facilities held by us, from which we receive 167 MW and 22 MW, respectively.

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Natural Gas. In addition to electricity, we consume natural gas, mainly in our hot-stripmill. *CEGRio S.A.*, which was privatized in 1997, is currently our sole source of natural gas. Variations in the supply of gas can affect the level of steel production. We have not experienced any significant stoppages of production due to a shortage of natural gas. We also purchase fuel oil from Petrobrás, the Brazilian national oil company. See Item 3D. Risk Factors Risks Relating to the Steel Industry and CSN Interruptions in the supply of natural gas and power transmission over the government power grid may adversely affect our business, financial condition and results of operations.

Suppliers

We acquire the inputs necessary for the production of our products in Brazil and abroad, with aluminum, zinc, tin, spare parts, refractory bricks, lubricants, oxygen, nitrogen, hydrogen and argon being the main inputs acquired in Brazil and coal and coke being the only inputs acquired abroad.

Our main raw materials suppliers are set forth below:

Main Suppliers	**Raw Material**
BHP Billiton, Jim Walter Resources and Alpha Coal PTY	Coal
Minmetals, Noble and Seatrade	Coke
Valesul, Nexans, Imbra and Alubar	Aluminum
Votorantim Metais	Zinc
ERSA, Glencore and Coppertrading	Tin
Engebasa, Tecnometal and Dedini	Spare parts
Magnesita, Saint Gobain and RHI	Refractory bricks
BR Distribuidora, Yushiro and Quaker	Lubricants

Logistics

Transportation costs are a significant component of our steel production costs and are a factor in our price-competitiveness in the export market. Railway transportation is the principal means by which we transport raw materials from our mines to the Presidente Vargas steelworks and steel products to ports for shipment overseas. Iron ore, limestone and dolomite from our two mines located in Minas Gerais State are transported by railroad to the Presidente Vargas steelworks for processing into steel. The distances from such mines to the Presidente Vargas steelworks are 328 km and 455 km. Imported coal and coke bought from foreign suppliers are unloaded at the port of Itaguaí, 90 km west of the City of Rio de Janeiro, and shipped 109 km by train to the Presidente Vargas steelworks. Our finished steel products are transported by train, truck and ships to our customers throughout Brazil and abroad. Our principal Brazilian markets are the cities of São Paulo (335 km from the Presidente Vargas steelworks), Rio de Janeiro (120 km) and Belo Horizonte (429 km).

Until recently, Brazil s railway system (including railcars and tracks) was principally government-owned and in need of repair, but has now been largely privatized. In an attempt to increase the reliability of our rail transportation, we indirectly hold concessions for the main railway systems we use.

We export mainly through the ports of Itaguaí and Rio de Janeiro, and import coal and coke through the Itaguaí Port, all in Rio de Janeiro State. The coal and container terminals have been operated by us since August 1997 and 1998, respectively.

Sales and Marketing

Our products are sold both domestically and abroad as a main raw material for several different manufacturing industries, including the automotive, home appliance, packaging, construction and steel processing industries.

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Marketing Organization and Strategy

Our sales approach is to establish a brand loyalty image and achieve a reputation for quality products by developing relationships with our clients and focusing on their specific needs. Our business encompasses operations and commercial activities. Our operations activities are undertaken by our production sector, which is composed of the following two units:

- the operations unit is responsible for steel production operations, repair shops, in-plant railroad, and process development at Volta Redonda; and

- the support unit is responsible for production planning, management of product stockyards, energy and utility facilities and work force safety assistance at the Presidente Vargas steelworks.

The production sector is also responsible for environment and quality consulting, new products development, capital investment implementation for steel production and processing, as well as the supervision of GalvaSud s and CSN Paraná s operations.

Our commercial sector is responsible for sales of all of our products. This sector is divided into two major sections, one focused on export sales and the other on domestic sales. The domestic market oriented sales section is divided, in turn, into five market segments: packaging, distribution, automotive, home appliances and original equipment manufacturer, or OEM, and construction. Each one of these segments has a specific strategic goal to provide tailor-made steel solutions that meet the specific needs of each of the segments they serve.

The distribution unit is responsible for supplying large steel processors and distributors, as well as some industries that produce small diameter pipe and light profiles. The packaging unit acts in an integrated way with suppliers, representatives of the canning industry and distributors to respond to customer needs for finished-products. The automotive unit markets GalvaSud products and a portion of the galvanized material produced at Presidente Vargas steelworks, using a combined sales strategy. The home appliance, OEM and construction units, in addition to being responsible for these segments, market the steel produced at CSN Paraná.

In 2006, approximately two thirds of our domestic sales were made through our own sales force directly to customers. The remainder was sold to distributors for subsequent resale to smaller clients.

Historically, our export sales were made primarily through international brokers. However, as part of our strategy to establish direct, longer-term relationships with end-users, we have decreased our reliance on such brokers. We have sought to orient our export sales to more profitable markets in order to maximize revenues and shareholder returns. Our strategy is to maintain Europe and North America as our main export markets, taking advantage of the commercial channels provided by our subsidiaries CSN LLC, in the United States and Lusosider, in Portugal.

All of our sales are on an order-by-order basis and have an average delivery time of 45 days. As a result, our production levels closely reflect our order log book status. We forecast sales trends in both the domestic and export markets based on the historical data available over the prior two-year period and the general economic outlook for the near future. We have our own data systems to remain informed of worldwide and Brazilian market developments. Further, our management believes that one of the keys to our success is maintaining a presence in the export market. Such presence gives us the flexibility to shift between domestic and export markets, thereby allowing us to maximize profitable capacity utilization.

Unlike classic commodity products, there is no exchange trading of steel, or uniform pricing, as wide differences exist in terms of size, chemical composition, quality and specifications. In general, export sales are priced based on

international spot prices of steel at the time of sale in U.S. dollars or Euros, depending on the export destination. To establish the domestic price, the corresponding international quotations are converted into *reais* and an additional amount is added to reflect, among other things, local demand and the transportation and tariff costs to import similar products. Sales are normally paid at sight, or within 15 or 30 days, and, in the case of exports, usually backed by a letter of credit and an insurance policy. Sales are made primarily on cost and freight terms.

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Steel Sales by Geographic Region

In 2006, we sold steel products to customers in Brazil and 60 other countries. The fluctuations in the portion of total sales attributable to domestic sales, which can be seen in the table below, reflect our ability to adjust sales in light of variations in the domestic and international economies, as well as steel demand and prices, domestically and abroad.

The three main export markets for our products are North America, Europe and Latin America, representing 47%, 36% and 9%, respectively, of our export sales volume in 2006. In addition to sale to end customers.

In North America, we take advantage of our subsidiary CSN LLC presence, which acts as a commercial channel for our products. In order to gain a cost advantage among our US competitors, CSN is able to export slab to CSN LLC which is processed at third parties into hot-rolled coil and then to be transformed into more added value products at CSN LLC s plant, such as cold-rolled coil and galvanized. Moreover, CSN is able to export cold-rolled coils which can be directly sold or processed by CSN LLC in order to manufacture galvanized products.

In Europe, CSN sells hot-rolled coil as raw material for Lusosider, our subsidiary located in Portugal.

The following table contains certain information relating to our sales of steel products by destination:

SALES OF STEEL PRODUCTS BY DESTINATION

(In thousands of metric tons and millions of US$)

	2004				**2005**				**2006**			
	Tons	% of Total	Gross Operating Revenues(2	% of Total	Tons	% of Total	Gross Operating Revenues(2)	% of Total	Tons	% of Total	Gross Operating Revenues(2)	% of Total
Brazil	3,298	70.5	2,699	73.0	2,875	59.6;	3,155	72.2	2,817	64.3	3,258	72.5
Export	1,383	29.5	997	27.0	1,945	40.4	1,214	27.8	1.567	35.7	1,235	27.5
Total	4,681	100.0	3,696	100.0	4,820	100.0	4,369	100.0	4,384	100.0	4,493	100.0
Exports by Region												
Asia	149	3.2	62	1.7	543	11.3	268	6.1	79	1.8	47	1.1
North America(1)	605	12.9	602	16.3	662	13.7	479	11.0	729	16.7	600	13.4
Latin America	136	2.9	77	2.1	146	3.0	101	2.3	142	3.2	92	2.0
Europe	447	9.5	228	6.2	510	10.6	298	6.8	563	12.8	455	10.1
All Others	46	1.0	27	0.7	84	1.7	68	1.6	54	1.2	41	0.9
Total Exports	1,383	29.5	997	27.0	1,945	40.4	1,214	27.8	1,567	35.7	1,235	27.5

(1) Sales to Mexico are included in North America
(2) Total gross operating revenues presented above differ from amounts in our U.S. GAAP financial statements because they do not include revenues from non-steel products, which in 2004 represented US$207, in 2005 represented US$304 and in 2006 represented US$320.

Sales by Steel Product

The following table sets forth our market shares for sales in Brazil of hot-rolled, cold-rolled, galvanized and tin mill products for the past three years according to the *Instituto Brasileiro de Siderurgia*, the Brazilian Steel Institute, or IBS.

DOMESTIC MARKET SHARE
(As a percentage of the market for each product)

	2004	**2005**	**2006**
Hot-rolled Products	29.0%	29.0%	25.0%
Cold-rolled Products	25.0%	19.0%	19.0%
Galvanized Products	49.0%	44.0%	42.0%
Tin Mill Products	98.0%	99.0%	98.0%

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Sales by Industrial Segment

We sell our products to manufacturers in several industries. Following is a breakdown of our domestic shipments by volume for the last three years among our market segments:

SALES BY INDUSTRIAL SEGMENT IN BRAZIL
(In percentages of total domestic volume shipped)

	2004	2005	2006
Distribution	32.3%	33.8%	38.0%
Packaging	19.8%	22.5%	21.9%
Home Appliances/OEM	17.4%	15.2%	15.4%
Automotive	20.0%	17.4%	14.6%
Construction	10.6%	11.0%	10.2%

We believe we have a particularly strong domestic and export position in the sale of tin mill products used for packaging. Our customers for these products include some of the world s most important food processing companies, as well as many small and medium-sized entities. We also maintain a strong position in the sale of galvanized products for use in the automobile manufacturing, construction and home appliance industries in Brazil and abroad, supplied by GalvaSud and CSN Paraná. No single customer accounts for more than 5% of our net operating revenues.

Seasonality

Sales by us are subject to seasonality. In the international and domestic steel market, demand is lower in the first six months of each year, which directly affects sales. On the other hand, demand normally increases in the third quarter. The sales force considers this seasonality in its planning while, at the same time, seeks to keep production stable by offsetting domestic market fluctuations with exports to other markets.

Facilities

Steel Mill

The Presidente Vargas steelworks, located in the city of Volta Redonda, Rio de Janeiro State, began operating in 1946. It is an integrated facility covering approximately 3.8 square km and containing five coke batteries (three of which are currently in operation), three sinter plants, two blast furnaces, a basic oxygen furnace steel shop, which is also referred to as a BOF shop, with three converters, three continuous casting units, one hot strip mill, three cold strip mills, two continuous pickling lines, one continuous annealing line, three continuous galvanizing lines, four continuous annealing lines exclusively for tin mill products and six electrolytic tinning lines.

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Our major operational units and corresponding effective capacities as of December 2006, including CSN LLC and Lusosider are set forth in the following chart:

EFFECTIVE CAPACITY

	Metric tons per year	Equipment in operation
Process:		
Coking plant	1,680,000	3 batteries
Sintering plant	6,930,000	3 machines
Blast furnace	5,380,000	2 furnaces
BOF shop	5,750,000	3 converters
Continuous casting	5,600,000	3 casters
Finished Products:		
Hot strip mill	5,100,000	1 mill
Cold strip mill	4,550,000	6 mills
Galvanizing line	2,095,000	7 lines
Electrolytic tinning line	1,190,000	7 lines

Downstream Facilities

GalvaSud. We currently hold 100% of GalvaSud, which produces and sells galvanized steel *Galvanew*®, laser-welded and pre-stamped parts for the automotive industry. GalvaSud has an annual capacity of 350,000 tons. For further information on the acquisition of GalvaSud, see Item 4A. History and Development of the Company Acquisitions .

CSN Paraná. Our subsidiary CSN Paraná, produces and supplies plain regular galvanized, Galvalume® and pre-painted steel products for the construction and home appliance industries. The plant has an annual capacity of 330,000 tons of galvanized products and Galvalume® products, 100,000 tons of pre-painted product, which can use cold-rolled or galvanized steel as substrate, and 220,000 tons of pickled hot-rolled coils in excess of the coils required for the coating process.

Metalic. We hold 100% of the shares of *Cia. Metalic Nordeste*, or Metalic. Metalic is the only two-piece steel can producer in all Americas. It has approximately 50% of the packaging market for carbonated drinks in the Northeastern regions of Brazil. Currently, we are the only supplier to Metalic of the steel used to make two-piece cans. The development of drawn-and-wall-ironed steel for the production of two-piece cans is an

important achievement in the production process at the Presidente Vargas steelworks.

Prada. We hold 100% of the shares of *Companhia Metalúrgica Prada*, or Prada. Prada is the largest steel can manufacturer in Brazil and produces more than one billion steel cans in its four production units located in São Paulo, Santa Catarina and Minas Gerais states, in the southeastern and southern regions of Brazil and, accordingly, is one of our major customers of tin mill products. Currently, we are the only Brazilian producer of tin-coated products, Prada´s principal raw material. Prada has important customers in the food and chemical segments, including seeds, dairy products, lubricants, varnish, resins and other business activities. For further information on the acquisition of Prada, see Item 4A. History and Development of the Company Acquisitions.

Heartland Steel. CSN LLC holds the assets of Heartland Steel, a flat-rolled steel processing facility in Terre Haute, Indiana. This facility has an annual production capacity of 800,000 tons of cold-rolled products and 315,000 tons of galvanized products. Currently, CSN LLC is obtaining hot coils by buying slabs from us and then having them converted into hot coils by American steel companies or buying hot rolled coils directly from mills in the United States. See Item 4B. Government Regulation and Other Legal Matters-Anti-Dumping Proceedings-United States for a discussion about anti-dumping issues on Brazilian hot coils exports to the United States.

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Lusosider. We hold 100% of Lusosider, a producer of hot-dip galvanized products, cold-rolled and tin plate located in Seixal, near Lisbon, Portugal. Lusosider produces approximately 240,000 tons of galvanized products, 50,000 tons of cold rolled and 60,000 tons of tin plate annually. Its main customers include service centers, food and general line can making and steel packaging industries. For further information on the acquisition of the remaining 50% of the capital stock of Lusosider, see Item 4A. History and Development of the Company Acquisitions.

INAL. INAL (Indústria Nacional de Aços Laminados S/A), is a very traditional distributor founded in 1957. Currently INAL is the number one in the Brazilian distribution market, with 730,000 tons/year of capacity. INAL has four steel service centers and five distribution centers strategically located in the Brazilian territory. Its main and biggest service center is located in Mogi das Cruzes between São Paulo and Rio de Janeiro. INAL has a dedicated service center for processing tin plate, located in Volta Redonda. Its product mix also includes sheets, slit coils, sections, tubes, roofing in standard or customized format, according to client s specifications. INAL processes all the range of products produced by CSN and services 4,000 clients annually in sectors, such as: civil construction, automotive, home appliances, among others.

Mines and Mineral Reserves

We have concessions to mine iron ore, limestone, dolomite and manganese. However, at the present time, we believe it is more cost efficient to purchase manganese on the local market. As a result, we do not currently operate any of the manganese concessions.

We have an 100% ownership interest in each of our mines. In addition, each mine is an open pit mine. See the map under Item 4D. Property, Plant and Equipment for the location of the mines in relation to the Presidente Vargas steelworks and for information on the reserves at our Casa de Pedra mine.

Iron Ore Mine. Our iron ore extraction, crushing and screening are done at our Casa de Pedra mine facilities located at Congonhas, Minas Gerais State, located 350 km from the Presidente Vargas steelworks. The current mine equipment fleet and treatment facilities have an installed annual run-of-mine capacity of approximately 60 and 21.5 million tons, respectively. Assuming current and future levels of production and quality, we assume that our proven and probable reserves will last for 28 years.

Until 2001, we held an interest in CVRD, Latin America s largest mining company and the largest producer and exporter of iron ore in the world, through Valepar. Pursuant to an agreement entered into on December 31, 2000, we sold our interest in Valepar to some companies and pension funds, including Bradespar S.A. and Litel Participações S.A. In connection with the sale of our then controlling stake at Valepar to Bradespar S.A. and Litel Participações S.A. and the subsequent sale of CVRD s 10.3% interest in 2003 in our company, CVRD obtained a 30-year right of first refusal to match all the conditions, including price, quality and tenor, obtained by us in contracts with third parties to purchase iron ore produced at Casa de Pedra in excess of our and our affiliates needs.

In connection with CVRD s right of first refusal, in March 2005, we and CVRD executed a purchase and sale agreement providing for our sale to CVRD of a total of 54.7 million tons of iron ore produced in the Casa de Pedra iron ore mine over the term of the agreement which expires in 2015. The pricing terms of the agreement are subject to prices charged by CVRD to its customers in the Asian market. This agreement is the first long-term sale of iron ore anticipated from the expansion of Casa de Pedra mine and it marks the beginning of the sales of our iron ore to third parties on a large scale. Currently, the place of delivery of the iron ore and its effects on certain commercial terms are under dispute by means of arbitration proceeding before the International Chamber of Commerce (ICC).

Additionally, in view of certain acquisitions made by CVRD in 1995, the *Conselho Administrativo de Defesa Econômica*, the Brazilian anti-trust agency, or CADE, issued a decision in August 2005 according to which CVRD would have to choose between its share participation in Ferteco Mineração S.A. (Ferteco) or its rights of first refusal mentioned above. Such decision is being challenged by CVRD before the Brazilian courts.

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Limestone and Dolomite Mine. Our extraction and preparation of limestone and dolomite is done at our Bocaina mining facility located at Arcos, Minas Gerais State. This mining facility has an installed annual production capacity of approximately 4.0 million tons. We believe this mining facility has sufficient limestone and dolomite reserves to adequately supply our steel production, at current levels, for more than 45 years. The mining facility is located 455 km from the Presidente Vargas steelworks.

Tin. We hold the assets of a tin mine and a smelter located in Rondônia state. The inventory of the geological reserves has been prepared from a review of the major reports from the Santa Barbara Mine Document Center. The majority of the deposits and/or target areas are within Mining Leases that have been consolidated into a Mining Group (*Grupamento Mineiro* n" 131/92). The reserves provided were recognized by DNPM, Brazil s competent authority for the reporting of ore reserves. The reserves and resources presented are in situ. For further information on this acquisition, see Item 4A. History and Development of the Company Acquisitions.

Electricity Distribution and Generation

Thermoelectric Co- Generation Power Plant. We completed construction of a 238 MW thermoelectric co-generation power plant at the Presidente Vargas steelworks in December 1999. Since October 2000, the plant has provided the Presidente Vargas steelworks with approximately 60% of its electric energy needs for its steel mills. Aside from operational improvements, the power plant supplies our strip mills with electric energy, process steam and blown air for the blast furnaces, benefiting the surrounding environment through the elimination of flares that burn steel-processing gases into the atmosphere. The plant was constructed in accordance with the most stringent international environmental standards, meeting and surpassing applicable Brazilian environmental standards.

Itá Hydroelectric Facility. We and *Tractebel Energia S.A.* Tractebel each own 48.75%, and *Companhia de Cimento Itambé* Itambé owns the remaining 2.5%, of *Itá Energética S.A.* ITASA, a special-purpose company formed for the purpose of implementing, and owning, under a 30-year concession, 60.5% of the Itá hydroelectric facility on the Uruguay river in southern Brazil. Tractebel directly owns the remaining 39.5% of the Itá hydroelectric facility. ITASA has been responsible for the construction of the Itá plant, while Tractebel has been responsible for environmental matters (such as property condemnations and resettlements). Tractebel is also responsible for the plant operation and maintenance.

The power facility was built under a project finance structure with an investment of approximately US$860 million. The long-term financing for the project was closed in March 2001 and consisted of US$78 million of debentures issued by ITASA, a US$144 million loan from private banks and US$116 million of direct financing from BNDES, all of which are due by 2013. The sponsors have invested approximately US$306 million in this project.

Itá has an installed capacity of 1,450 MW, with a firm guaranteed output of 668 MW and, became fully operational in February 2001.

We and the other shareholders of ITASA have the right to take our pro rata shares (based on our interests in the project) of Itá s output pursuant to 30-year power purchase agreements at a fixed price per megawatt hour, adjusted annually for inflation. Since October 2002, we have been using our entire Itá take internally.

Igarapava Hydroelectric Facility. We own 17.9% of a consortium that built and will operate for 30 years the Igarapava hydroelectric facility. Other consortium members are CVRD, *Companhia Mineira de Metais CMM, Mineração Morro Velho Ltda. MMV, and Companhia Energética de Minas Gerais CEMIG*. The plant attained its full installed capacity of 210 MW, corresponding to 126 MW of firm guaranteed output in September

1999. We have been using part of our 22 MW take from Igarapava to supply energy to the Casa de Pedra and Arcos mines. The balance is consumed by the Presidente Vargas steelworks or sold into the energy market.

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Railways

Southeastern Railway System. We own 32.93% (20% of the voting capital) of MRS Logística S.A., or MRS, which has a concession to operate, through the year 2026, the assets of Brazil s southeastern railway system. The southeastern railway system, covering 1,674 km of track, serves the São Paulo Rio de Janeiro Belo Horizonte industrial triangle in southeast Brazil, and links the mines of Minas Gerais State to the ports of São Paulo and Rio de Janeiro states and to the steel mills of CSN, Companhia Siderúrgica Paulista Cosipa and Gerdau Açominas. In addition to serving other customers, the line transports iron ore from our mines at Casa de Pedra in Minas Gerais State and coke and coal from the Itaguaí Port in Rio de Janeiro State to the Presidente Vargas steelworks and transports our exports to the ports of Itaguaí and Rio de Janeiro. The railway system connects the Presidente Vargas steelworks to the container terminal at Itaguaí Port, which handles most of our steel exports. Our transport volumes represent approximately 13% of the southeastern railway system s total volume. As of December 31, 2006, US$1,623 million remained payable over the remaining 20-year life of the concession, of which US$1,571 million are treated as an off-balance sheet item (See Item 5E. Off-Balance Sheet Arrangements). While we have joint and several liabilities with the other principal MRS shareholders for the full payment of the outstanding amount, we expect that MRS will make the lease payments through internally generated funds and proceeds from borrowings.

Northeastern Railway System. We and the Steinbruch family each hold 45.78% of the capital stock of Companhia Ferroviária do Nordeste, or CFN, which has a 30-year concession to operate the assets of Brazil s northeastern railway system. The northeastern railway system covers 4,238 km of track and operates in the states of Maranhão, Piauí, Ceará, Paraíba, Pernambuco, Alagoas and Rio Grande do Norte. It also connects with the region s leading ports, thereby offering an important competitive advantage through opportunities for intermodal transportation solutions and made-to-measure logistics projects. In 2006, CFN was authorized to absorb the Transnordestina, a large-gauge, high-performance rail project. As of December 31, 2006, US$15 million remained payable over the remaining 20-year life of the concession, of which US$14.9 million are treated as an Off-Balance sheet item (See Item 5E. Off-Balance Sheet Arrangements). We and the Steinbruch family have joint and several liabilities for the full payment of the outstanding amount.

Port Facilities

Coal Terminal. We own the concession to operate a coal terminal, one of four terminals that form the Itaguaí Port, located in Rio de Janeiro State, for a term expiring in 2022 that is renewable for another 25 years. Itaguaí Port, in turn, is connected to the Presidente Vargas steelworks by the southeastern railway system. Our imports of coal and coke are made through this terminal. Under the terms of the concession, we undertook to unload at least 3.4 million metric tons of coal and coke through the terminal annually, as well as shipments from third parties. Among the approved investments that we announced in January 2004 is the development and expansion of the coal terminal at Itaguaí to also handle up to 40 million tons of iron ore per year. For further information, see Item 4A. History and Development of the Company Planned Investments Iron Ore Project (Casa de Pedra).

Container Terminal. We own 100% of Sepetiba Tecon S.A., or TECON, which has a concession to operate, for a 25-year term that is renewable for another 25 years, the container terminal at Itaguaí Port. As of December 31, 2006, US$130 million of the cost of the concession remained payable over the next 20 years of the lease. TECON is expected to reach a nominal annual capacity of 600,000 containers by 2010. We intend to send all of our exports of steel products through this terminal. Approximately 60% of the steel products that we exported in 2006 were shipped through TECON.

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Insurance

In order to minimize the various risks resulting from our operations, we take several measures. Besides implementing different procedures for maintenance and risk control, which include, but are not limited to, the publication of safety policies for employees, accident simulation, among others, we contract various insurance policies to protect our assets and to comply with applicable law.

We maintain all risk insurance coverage against damage to our principal operating assets at the Presidente Vargas steelworks and our mining facilities and port operations, which we believe adequately covers the principal risks of operating such facilities. In addition, we maintain business interruption and transportation risk insurance, as well as general third-party liability insurance. We also insure our hydroelectric, electricity distribution, railways, coal and container terminal investments.

Our insurance policy gives us coverage for up to US$750 million on business interruption and damaged equipment. The insurance companies confirmed that the losses are covered by the terms of our insurance policy and that there are no restrictions on payments or reimbursement.

On January 22, 2006, there was an accident involving equipment adjacent to Blast Furnace No. 3, mainly affecting the powder collecting system. As a result of this accident the equipment production was interrupted until the end of the first semester of 2006. We have an insurance policy for loss of profits and equipment damages in the maximum amount of US$750 million, which our management deems to be sufficient to recover any losses derived from the accident. The cause of the accident was expressly covered by the insurance policy, and the calculation of our losses is being concluded.

The amount of losses subject to indemnification shown by regulating bodies up to the closing date of the our consolidated financial statements is US$445 million. Based on the insurance policy and confident as to the conclusion of studies about the loss, CSN requested and the insurance companies granted an advance of US$237 million (US$223 million in 2006 and US$14 million in 2007) that will be deducted from losses subject to indemnification, verified during the normal course of the regulatory process.

Based on reports issued by independent consultants and on the confirmation of the insurance coverage by the insurance company, we recognized up to December 31, 2006, the amount of US$342 million related to costs incurred to purchase slabs from third-party sources and fixed expenses as an offset to cost of sales and US$9 million as an offset to cost of sales corresponding to the income in the write-off of damaged assets (net book value of approximately R$81 million).

On December 31, 2006, we maintained a balance receivable from losses claimed in the amount of US$209 million. We do not identify any risk in such credit, taking into account the international reputation and prestige of the insurance and reinsurance companies and we consider this is a current asset of the Company based on the fact that we expect to receive such amount in the next 12 months.

Intellectual Property

We have entered into technical assistance contracts with a number of foreign steel companies and technical cooperation agreements with various universities and research institutes to provide us with assistance and advice from time to time related to specific products and processes. In addition, we have various patent applications pending before, and own various patents approved by, the Brazilian National Institute of Industrial Property. We also own licenses for patents relating to a number of our products and processes.

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Competition

Both the worldwide and the Brazilian steel markets are intensely competitive. The primary competitive factors in these markets include quality, price, payment terms and customer service. Moreover, continuous advances in materials sciences and resulting technologies have given rise to new products that pose competition for traditional steel products. These steel substitutes include plastics, aluminum, ceramics, glass and concrete, each one in a specific industrial segment.

Competition in the Brazilian Steel Industry

The primary competitive factors in the domestic market include quality, price, payment terms and customer service. Although we compete with other integrated Brazilian steel mills, we have not experienced significant import competition in Brazil from foreign steel companies. Several foreign steel companies, however, are significant investors in Brazilian steel mills.

The following table sets forth the production of crude steel by Brazilian companies for the years indicated:

	2004		**2005**		**2006**	
	Ranking	**Production**	**Ranking**	**Production**	**Ranking**	**Production**
		(In million tons)		*(In million tons)*		*(In million tons)*
Gerdau[1]	1	7.3	1	6.9	1	7.0
CSN[4]	2	5.5	2	5.2	6	3.5
CST[2]	3	5.0	3	4.8	2	5.1
Usiminas[3]	4	4.7	4	4.5	3	4.6
Cosipa	5	4.2	5	4.1	4	4.2
Belgo[2]	6	3.3	6	3.3	5	3.6
Others		2.9		2.8		2,9
TOTAL		32.9		31.6		30,9

Source: Brazilian Steel Institute

(1) Gerdau is partly integrated, but the bulk of Gerdau s steel production comes from non-integrated plants.

(2) In 2005, Arcelor S.A. accomplished a shareholder restructuring of its companies in Brazil, resulting in a consolidation of its stakes on CST, Belgo and Vega do Sul in a new company called Arcelor Brasil.

(3) Since 1999, Usiminas has had a majority stake in Cosipa, and the companies acted as a group. In 2005, Cosipa was merged into Usiminas.

(4) In 2006, CSN s production was negatively affected by an accident of its biggest blast furnace. Since the second half of the year, CSN has been operating at its full capacity.

Competitive Position Global

During 2006, Brazil retained its place as the largest producer of crude steel in the Latin America, with a production output of 30.9 million tons and a 2.5% share of total world production, according to *Instituto Brasileiro de Siderurgia*,

the Brazilian Steel Institute, or IBS. In 2006, Brazil was the tenth world s steel producer, accounting for approximately half of total production in Latin America, approximately twice the size of Mexico s and approximately one-third of U.S. steel production, also according to IBS. Brazilian exports in 2006 reached 12.5 million tons of finished and semi-finished steel products.

We compete on a global basis with the world s leading steel manufacturers. We have positioned ourselves in the world market with a product mix characterized by high margin and strong demand, such as, tin mill and galvanized. We have relatively low-cost and sufficient availability of labor and energy and own high-grade iron ore reserves that we believe more than meet our production needs. These global market advantages are partially offset by costs of transporting steel throughout the world, usually by ship. Shipping costs, while helping to protect our domestic market, put pressure on our export price. To maintain our position in the world steel market in light of the highly competitive international situation with respect to price, our product quality and customer service must be maintained at a high level. We have continually monitored the quality of our products by measuring customer satisfaction with our steel in Europe, Asia and the Americas. See "Item 4B. Business Overview-Government Regulation and Other Legal Matters-anti-dumping Proceedings" for a description of protectionist measures being taken by steel-importing countries that could negatively impact our competitive position.

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Competitive Advantages of the Brazilian Steel Industry

Brazil s principal competitive advantages are its abundant supply of low-cost, high-grade iron ore, low-cost labor and energy resources and good quality infrastructure (principally railways and ports). Brazil also benefits from a vast internal market with a large growth potential, a privatized industry making investments in plant and equipment, and deep water ports that allow the operation of large ships, which facilitates access to export markets. Nevertheless, Brazil s products have lost partially their competitiveness, mainly affected by the valuation of the *real* since the beginning of 2006, that resulted in the increase of the price of our products, and the sharp increase of China s exports, including steel products. Despite all these factors, we believe Brazil s average cost of steel production is one of the lowest in the world.

As in most domestic markets, the domestic price of steel in Brazil has historically been higher than its export price. This differential, however, is generally not large enough to compensate for the cost of importing steel to Brazil from producers in Asia, Europe and North America. The low production costs in Brazil are another barrier to foreign steel imports. Consequently, most of the steel sold in the Brazilian steel market is manufactured by Brazilian producers, and we do not believe that sales in Brazil by foreign producers will increase significantly or that steel prices in Brazil will decrease significantly because of competition from foreign steel producers.

Greenfield competition from new market entrants would be discouraged by existing participant s ties to sources of raw materials and well- established distribution networks. In the last years, several foreign competitors announced their intention to undertake greenfield projects in Brazil. To date, they are still determining the feasibility of such projects. The strategic goal of these projects, as announced by their participants, is to replace non-competitive slab production plants in Europe or to expand upon slab capacity production of Asian companies in order to service their home markets.

Government Regulation and Other Legal Matters

Promoting responsible environmental and social management is part of our business. We prioritize processes and equipments that offer the most modern and reliable technologies on environmental risks monitoring and control. We operate a corporate environmental department managed under an Environmental Management System ("EMS"), compliant with ISO 14001:2004 requirements. In addition, we have a factory committee for environmental management composed of professionals from all departments of CSN s main steelworks. This technical assembly usually meets every week to discuss eventual problems and to identify risks and aspects of the operations in which the group can act pro-actively, in order to prevent possible environmental damages and harm.

Environmental Regulation

We are subject to Brazilian federal, state and municipal environmental laws and regulations governing air emissions, waste water discharges, and solid and hazardous waste handling and disposal. We are committed to controlling the substantial environmental impact caused by our steelmaking, mining and logistics operations, in accordance with international standards and in compliance with environmental laws and regulations in Brazil. We believe we are currently in substantial compliance with applicable environmental requirements.

The Brazilian Federal Constitution gives both the federal and state governments power to enact environmental protection laws and issue regulations under such laws. In addition, we are subject to municipal environmental laws and regulations. While the Brazilian government has power to promulgate environmental regulations setting forth minimum standards of environmental protection, state governments have the power to enact more stringent environmental regulations. Most of the environmental regulations in Brazil are thus at the state and local level complemented by a current process of regulations reviews and new propositions at the federal level. The

environmental regulations of Rio de Janeiro State, in which the Presidente Vargas steelworks is located, are plant-specific. Thus, specific goals and standards are established in operating permits or environmental accords issued to each company or plant. These specific operation conditions complement the standards and regulations of general applicability and are required to be observed throughout the life of the permit or accord. The terms of such operating permits are subject to change and are likely to become stricter. All of our facilities currently have operating permits.

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In 2006, we requested several emissions permits and renewals of environmental permits, both for current operations and for the development of new projects regarding steel and cement manufacturing, iron ore andlimestone mining and logistics, including a new slab mill at Itaguaí; the expansion of TECAR, aiming at exports of iron ore; the expansion of the Casa de Pedra mine; the construction of a cement klinker plant at Arcos and of a cement mill at Volta Redonda; and the first part of Transnordestina Railway.

Environmental Expenditures and Claims

Since our privatization, we have invested heavily in environmental protection and remediation programs. We had environmental expenditures (capitalized and expensed) of US$54.4 million in 2004, US$94.1 million in 2005 and US$109.0 million in 2006.

Our investments in environmental projects during 2006 were related mainly to (1) operations and maintenance of environmental control equipments (2) development of environmental studies for permit applications (3) studies monitoring and remediation of environmental liabilities due to prior operations, mainly before our privatization and (4) conclusion of works and measures defined in the *Termo de Compromisso Ambiental*, an environmental accord related to TECAR Solid Bulks Terminal of Itaguaí Port, in Rio de Janeiro State, or TECAR. the US$109.0 million spent in 2006, US$26.9 million constituted capital expenditures and US$82.1 million constituted operational expenditures.

Our main environmental claims on December 31, 2006 are related to cleaning-up obligations at former coal mines decommissioned in 1989; legal environmental compensation projected for new projects at Minas Gerais and Rio de Janeiro states; and cleaning-up obligations due to former operations of Presidente Vargas steelworks. We did not include in the accruals any environmental liabilities related to ERSA, as they will be borne by its former owner (CESBRA/BRASCAN).

We reserve an accrual for remediation costs and environmental lawsuits when a loss is probable and the amount can be reasonably estimated. We record provisions for all environmental liabilities and obligations for which we are formally enforced by competent judicial and administrative authorities. As of December 31, 2006, we had provisions for environmental liabilities in the total amount of US$25.0 million (US$9 million as of December 31, 2005), which our management and legal advisors consider sufficient to cover all probable losses. For further information, see Note 19 to our consolidated financial statements included in Item 18. Financial Statements.

Mining Concessions

Our mining operations are governed by the Brazilian Federal Constitution and the Mining Code and are subject to the laws, rules and regulations promulgated pursuant thereto. Under the Brazilian Constitution, all mineral resources belong to Brazil. Our mining activities at the Casa de Pedra mine are performed based on a *Manifesto de Mina*, which gives us full ownership over the mineral deposits existing within our property limits. Our mining activities at the Bocaina mine are based on a concession which gives us the right to mine for as long as ore reserves exist. See Item 4D. Property, Plant and Equipment for further information on our reserves at the Casa de Pedra mine.

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The Mining Code and the Brazilian Federal Constitution impose on mining companies, such as us, requirements relating to, among other things, the manner in which mineral deposits are exploited, the health and safety of workers, the protection and restoration of the environment, the prevention of pollution and the promotion of the health and safety of local communities where the mines are located. The Mining Code also imposes certain notification and reporting requirements.

Antitrust Regulation

We are subject to various laws in Brazil which seek to maintain a competitive commercial environment in the Brazilian steel industry. For instance, under Law 8,884/94, the *Lei de Defesa da Concorrência,* or Competition Defense Law, the *Secretaria de Direito Econômico* of Brazil s Ministry of Justice has broad authority to promote economic competition among companies in Brazil, including the ability to suspend price increases and investigate collusive behavior between companies. In addition, if the *Conselho Administrativo de Defesa Econômica* CADE determines companies have acted collusively to raise prices, CADE has the authority to impose fines on the offending companies, prohibit them from receiving loans from Brazilian government sources and bar them from bidding on public works projects. In addition, CADE has the authority to dissolve mergers and to require a company to divest assets should it determine that the industry in which it operates is insufficiently competitive.

Anti- Dumping Proceedings

Over the past several years, exports of steel products from various countries and companies, including Brazil and us, have been the subject of anti-dumping, countervailing duty and other trade-related investigations from importing countries. Most of these investigations resulted in duties that limit the investigated companie s abilities to access these markets. To date, however, the investigations have not had a significant impact on our export volume, either because the quantities that we exported were small or because we were able to re-direct our exports from affected markets to other markets.

Following are summaries of the protectionist measures to which our exports are subject. The widespread adoption of protectionist measures, even if by countries that have not been important market for us, might nevertheless adversely impact the international markets for our products.

United States

Anti-dumping and Countervailing Duties. In September 1998, U.S. authorities initiated anti-dumping and countervailing duties investigations on hot-rolled steel sheet and coil imported from Brazil and other countries. In February 1999, the U.S. Department of Commerce, or DOC, reached a preliminary determination on the anti-dumping and countervailing duties margins. We were found to have preliminary margins of 50.7% for anti-dumping, and of 6.6% for countervailing duties. In July 1999, Brazil and the United States signed a five-year suspension agreement, suspending the anti-dumping investigation and establishing a minimum price of US$327 per ton (delivery duty paid), subject to quarterly review by the DOC. In February 2002, the U.S. government terminated the anti-dumping suspension agreement and reinstated the anti-dumping margin of 41.27% . Also in July 1999, the Brazilian and U.S. governments signed a suspension agreement related to the countervailing duties investigation, which limited exports of hot-rolled sheets and coils from Brazil to 295,000 tons per year. At the request of the Brazilian government, the agreement was terminated in September 2004. Upon the termination of this agreement, countervailing duties of 6.35% became effective in September 2004, to be applied to imports of hot-rolled products from Brazil. In April 2004, we requested the DOC to conduct an administrative review of the anti-dumping investigation. Through this review, in April 2005, we obtained a favorable preliminary determination of "zero" margins of dumping from the DOC. Final determination was issued in October 2005 and the "zero" margin of dumping found by the DOC was confirmed.

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Simultaneously to the administrative review, we participated in an anti-dumping and countervailing duties expiry review which involved the exports of hot-rolled sheet and coils to the U.S. The expiry review was jointly developed by the International Trade Commission and the DOC, through the Import Administration- I.A. that was initiated in May 2004. Final determination was rendered in April 2005, retaining the anti-dumping and countervailing duties orders in effect.

In October 2005, the DOC initiated an administrative review of the investigation of subsidies and countervailing duties involving hot-rolled products. As the petitioners give up on their participation in the review, it was terminated by the DOC in February 2006.

Canada

Anti-dumping. In January 2001, the Canadian government initiated an anti-dumping investigation process involving hot-rolled sheets and coils exported from Brazil. The investigation was concluded in August 2001, with the imposition by Canada of an anti-dumping tax of 26.3% on imports of those products from Brazil, with minimum prices to be observed. In August 2002, the Canada Border and Services Agency, or the CBSA, initiated a revision of the values previously established and, in March 2003, the revised values were issued. These values are adjusted whenever there is an adjustment of the Canadian domestic prices. In February 2005, the CBSA initiated a reinvestigation of hot-rolled sheets and coils. We did not participate in this investigation

In December 2005, the Canadian International Trade Tribunal CITT initiated an expiry review of hot-rolled products, in which we participated. A final determination was issued in August 2006, determining the continuation of the anti-dumping order for hot-rolled products. As a result, exports of our hot rolled products to Canada are subject to anti-dumping duties of 77%.

Argentina

Anti-dumping hot-rolled products. Argentina commenced an anti-dumping investigation of hot-rolled products from Brazil, Russia and Ukraine in October 1998. In April 1999, the Argentinean government applied a provisional anti-dumping order on Brazilian imports, fixing a minimum price of US$410 per ton FOB (free on board), for four months ending in August 1999.

In December 1999, the Argentine government accepted a suspension agreement of the anti-dumping measures, providing for quotas of 36,000 tons for the first year, 38,000 tons for the second and 39,000 tons for the third, fourth and fifth years, and minimum prices from US$325 to US$365 per ton CFR FO (cost, insurance and freight, free out), subject to quarterly adjustments based on the publication of the Argentine National Institute of Statistics and Census (INDEC).

In December 2004, exporters were notified of the revision of resolution No. 1,420/1999 from the Economic, Work and Public Services Ministry of Argentina relating to the export of Brazilian hot-rolled products. In January 2005, an expiry review of the anti-dumping process was initiated to analyze the maintenance, modification and/or derogation of the action of the administrative authority of the Argentinean government. We participated in this review.

In June 2006, Argentina published resolution 412/2006 terminating the anti-dumping investigation for hot-rolled products from Brazil, Russia and Ukraine. The margin determined to Brazil was 147,95%, but it wasn t applied due the acceptance of a price commitment proposed. This price commitment has the same terms of the prior commitment and will be in force for five years as of the date of execution.

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Anti-dumping cold-rolled products. An investigation on anti-dumping on cold-rolled products from Brazil was initiated by Argentina in September 1999. In January 2000, a suspension agreement established quotas of 36,000 tons for the first year, 38,000 tons for the second year and 39,000 tons for the third, fourth and fifth years and a minimum price of US$457 per ton CIF (cost, insurance and freight), subject to quarterly adjustments based on the publications of the INDEC.

In January 2001, the government of Argentina accepted the suspension agreement, maintaining the quotas and renegotiating the minimum price to US$420 per ton CIF (cost, insurance and freight) for five years, subject to quarterly updates.

In May 2006, an expiry review of the cold-rolled anti-dumping investigation was initiated to analyze the maintenance, modification and/or derogation of the action of the administrative authority of the Argentinean government. The review was concluded in June 2006, terminating the existing anti-dumping order.

Overview of Steel Industry

World Steel Industry

The worldwide steel industry comprises hundreds of steelmaking facilities divided into two major categories, integrated steelworks and non- integrated steelworks, characterized by the method used for producing steel. Integrated plants, which accounted for approximately 66% of worldwide crude steel production in 2006, typically produce steel by smelting in blast furnaces the iron oxide found in ore and refining the iron into steel, mainly through the use of basic oxygen furnaces or, more rarely, in electric arc furnaces. Non- integrated plants (sometimes referred to as mini-mills), which accounted for approximately 34% of worldwide crude steel production in 2006, produce steel by melting scrap metal, occasionally complemented with other metallic materials, such as direct reduction iron or hot-briquetted iron, in electric arc furnaces. Industry experts expect that a lack of a reliable and continuous supply of quality scrap metal, as well as the high cost of electricity, may restrict the growth of mini- mills.

Steel continues to be the material of choice in the automotive, construction, machinery and other industries. Notwithstanding potential threats from substitute materials such as plastics, aluminum, glass and ceramics, especially for the automotive industry, steel continues to demonstrate its economic advantage. From 1990 through 2004, total global crude steel production ranged between approximately 770 million and 1.07 billion tons per year. In 2006, it reached 1.22 billion tons, representing an 8,0% increase compared to 2005. In 2005 it reached 1.13 billion tons, representing a 6.1% increase compared to 2004. According to the International Iron and Steel Institute, or IISI, global finished steel demand is expected to reach 1.18 billion tons in 2007, representing an 8.5% increase from 2006.

Developing economies have been increasing their own production capacity. In 2006, China increased its crude steel production by approximately 19% when compared to the Chinese production in 2005. Excluding Chinese figures, the world s average increase is less than 5%.

As a traditional global exporter and with its large steel production capacity, Brazil has consistently exported a substantial portion of its production. In 2006, steel production totaled 30.0 million tons, from which 11.5 million tons were designated to exports, compared to a total production of 28.0 million tons and exports of 11.8 million tons in 2005. Domestic sales in 2006 and 2005 amounted to 18.5 million tons and 16.8 million tons, respectively.

Brazil has been playing an important role in the export market, primarily as an exporter of semi-finished products. The Brazilian steel industry has taken several steps towards expanding its capacity to produce value-added products. Brazil s exports of semi-finished steel products aggregated 6.0 million tons in 2005 and 5.7 million tons in 2006, which represented 48% and 45% of total steel exports for both periods, respectively.

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Brazilian Steel Industry

Since the 1940s, steel has been of vital importance to the Brazilian economy. During the 1970s, huge government investments were made to provide Brazil with a steel industry able to support the country s industrialization boom. After a decade of little to no investment in the sector in the 1980s, the government selected the steel sector as the first for privatization commencing in 1991, resulting in a more efficient group of companies operating today.

A Privatized Industry

During almost 50 years of state control, the Brazilian flat steel sector was coordinated on a national basis under the auspices of *Siderbrás*, the national steel monopoly. The state had far less involvement in the non-flat steel sector, which has traditionally been made up of smaller private sector companies. The larger integrated flat steel producers operated as semi autonomous companies under the control of Siderbrás and were each individually privatized between 1991 and 1993. We believe that the privatization of the steel sector in Brazil has resulted in improved financial performance, as a result of increased efficiencies, higher levels of productivity, lower operating costs, a decline in the labor force and a resumption of investment.

Domestic Demand

Historically, the Brazilian steel industry has been affected by substantial fluctuations in domestic demand for steel. Although national per capita consumption varies with gross domestic product, or GDP, fluctuations in steel consumption tend to be more pronounced than changes in economic activity. Per capita crude steel consumption in Brazil has increased from 95 kilograms per capita in 1999 to 110 kilograms in 2006, which is low when compared to levels in developed country such as the United States, where the per capita crude steel consumption in 2006 was of 444 kilograms, and Germany, where the consumption was of 607 kilograms.

In 2004, mainly driven by the export market, Brazilian GDP grew 4.9%, its largest increase in ten years. In 2005, despite a good global conjuncture, the Brazilian economy exhibited a modest growth of 2.3% . From 2004 to 2005, total domestic steel sales decreased 9.6%, from 17.8 to 16.1 million tons. Sales of flat steel products decreased 9.3% in 2005, from 10.8 to 9.8 million tons. In 2006, supported by a 3.7% increase in Brazilian GDP, the sales of flat steel products increased 8.4%, compared to 2005.

The Brazilian flat steel sector is shifting production to the higher value-added consumer durable sector, which is dependent on domestic consumer confidence, which, in turn, is linked to the economic and political record of the current government administration. The consumer durable goods sector increased by 20.5% in 2000, as the economy improved, but as a result of the energy crisis in Brazil, that sector only showed some recovery in 2002, with a 2.7% increase, later reduced by 0.5% in 2003. After three years of showing quite modest growth rates, the consumer durable goods sector increased 21.8% in 2004. Despite the moderate growth rate performed by Brazilian economy, the consumer durable goods sector exhibited a 12.2% and 6.0% increase in 2005 and 2006, respectively. Over the past years, General Motors, Ford and Volkswagen, automobile manufacturers already in Brazil, made significant investments. In addition, Renault, Honda, Daimler-Chrysler, Audi and Peugeot/Citroen built new facilities in Brazil. In 2005, 2.5 million vehicles were produced and in 2006 a total of 2.6 million vehicles were produced in Brazil, representing a 4% increase compared to 2005.

Market Participants

According to IBS associated companies, the Brazilian steel industry is composed of 13 producers, with an installed annual capacity of approximately 37 million tons, producing a full range of flat, long, carbon, stainless

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and specialty steel. For information on the production by the largest Brazilian steel companies for the years ended December 2004, 2004 and 2006, see "Item 4B. Business Overview Competition Competition in the Brazilian Steel Industry."

Capacity Utilization

Total Brazilian nominal capacity in 2006 was estimated at 37 million tons, compared to 36 million tons of capacity in 2005. The Brazilian steel industry operated at approximately 83% of nominal crude steel capacity during 2006, contrasting with 88% from the previous year.

Exports/Imports

In 2006, Brazilian steel exports totaled 12.5 million tons, representing 42% of total Brazilian steel sales (domestic plus exports), accounting for US$6.9 billion in export earnings for Brazil in 2006. Over the last 20 years, the Brazilian steel industry has been characterized by a structural need to export, which is demonstrated by the industry s supply demand curve. The Brazilian steel industry has experienced periods of overcapacity, cyclicality and intense competition during the past several years. Demand for finished steel products, as measured by domestic apparent consumption, has consistently fallen short of total supply (defined as total production plus imports). In 2006, supply totaled 30.0 million tons, compared to apparent consumption of 18.5 million tons.

Brazil also enjoys a diversified steel export market. In 2006, export sales were made to over 120 countries. North America and South America were Brazil s main export markets, accounting for 34% and 24%, respectively, of all Brazilian steel exports in such year. United States was the main destination, representing 22.5% of total exports. The European Union was responsible for 17% of the Brazilian steel exports in 2006. The next ten largest markets, taken together, accounted for 63.7% of Brazil s 2006 steel exports in 2006. See also "Item 4B. Business Overview Competition."

As a result, Brazil is a negligible importer of foreign steel products. Steel imports were 1.9 million tons, or 10.1% of apparent domestic consumption in 2006. Due to the accident of our Blast Furnace No. 3, we decided to import semi-finished steel products to maintain our downstream operations, and, therefore the Brazilian steel imports in 2006 were unusually affected, increasing by 148% over imports in 2005. According to the BSI, domestic apparent consumption equals domestic sales plus imports. In 2006, Brazil had a steel trade surplus of US$5.5 billion and an overall trade surplus of US$23.4 billion.

4C. Organizational Structure

We do business directly and through subsidiaries. None of our subsidiaries is significant as defined under Regulation S- X.

4D. Property, Plant and Equipment

Our principal executive offices are located in the city of São Paulo, São Paulo State at Avenida Faria Lima, 3400, 20º, andar (telephone number 5511- 3049- 7100), and our main production operations are located in the city of Volta Redonda, Rio de Janeiro State, located approximately 120 km from the city of Rio de Janeiro. Presidente Vargas steelworks, our steel mill, is an integrated facility covering approximately 3.8 square km and located in the city of Volta Redonda in Rio de Janeiro State. Our iron ore, limestone and dolomite mines are located in Minas Gerais State, which borders Rio de Janeiro State to the north. Each of these mines is within 500 km of, and is connected by rail and paved road to the city of Volta Redonda.

The table below sets forth some relevant information regarding our property as of December 31, 2006.

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Facility	Location	Size	Use	Productive Capacity	Title	Encumbrances
Presidente Vargas steelworks	Volta Redonda, Rio de Janeiro state	3.95 square km	steel mill	5.6 million tons per year (mtpy)	owned	none
GalvaSud	Porto Real, Rio de Janeiro state	0.27 square km	galvanized steel producer	350,000 tons per year	owned	mortgage[4][5]
CSN Paraná	Paraná state	0.98 square km	galvanized and pre-painted products	100,000 tons of pre-painted product and 220,000 tons of pickled hot-rolled coils	owned	none
Metalic	Ceará state	0.10 square km	steel can manufacturer	900 million cans per year	owned	mortgage[6]
Prada	São Paulo, Santa Catarina and Minas Gerais states	SP 0.14 square km MG 0.02 square km SC 0.008 square km	steel can manufacturer	1 billion cans per year	owned	none
Heartland Steel	Terre Haute, Indiana, USA	0.78 square km	cold-rolled and galvanized products	800,000 tons of cold-rolled products and 315,000 tons per year of galvanized products	owned	none
Lusosider	Seixal, Portugal	0.39 square km	hot-dip	240,000 tons of	owned	none

			galvanized, cold-rolled and tin products	galvanized products, 50,000 of cold rolled and 60,000 of tin plates per year		
INAL	Mogi das Cruzes, São Paulo state	0.20 square km	distributor	730,000 tons per year	owned	none
Casa de Pedra mine	Congonhas, Minas Gerais state	31.35 square km	iron ore mine	60.0 mtpy [3]	concession	none
Bocaina mine	Arcos, Minas Gerais state	4.11 square km	limestone and dolomite mines	4.0 mtpy	concession	none
ERSA mine	Rondônia state	0.015 square km	tin mine	1,800 tons	owned	none
Thermoelectric co-generation power plant	Volta Redonda, Rio de Janeiro state	0.04 square km	power plant	238 MW	owned	none
Itá	Uruguay River - Southern Brazil	9.87 square km	power plant	1,450 MW	concession	none
Igarapava	Minas Gerais state	5.19 square km	power plant	210 MW	owned	none
Southeastern Railway System [1]	Southern and southeastern regions of Brazil	1,674 km of tracks	railway	--	concession	none
Companhia Ferroviária do Nordeste [2]	Northern and northeastern regions of Brazil	4,238 km of tracks	railway	--	concession	none

TECAR at Itaguaí Port	Rio de Janeiro state	0.69 square km	raw materials	4 mtpy	concession	none
Container terminal - TECON at Itaguaí port	Rio de Janeiro state	0.44 square km	containers	2 mtpy	concession	none
Land	Rio de Janeiro state	31.02 square km	undeveloped	--	owned	pledge[7]/ mortgage[5]
Land	Santa Catarina state	6.22 square km	undeveloped	--	owned	pledge[7]/ mortgage[5]
Land	Minas Gerais state	29.09 square km	undeveloped	--	owned	none

Facility	Location	Size	Use	Productive Capacity	Title	Encumbrances

(1) We indirectly hold the concession through MRS.
(2) We indirectly hold the concession through CFN.
(3) For information on mineral resources at our Casa de Pedra mine, see table under Casa de Pedra Mine below.
(4) Pursuant to a loan agreement entered into by the Rio de Janeiro State, Galvasud and Banco do Brasil as of May 4, 2000.
(5) Pursuant to a loan agreement entered into by Kreditanstatt Für Wiederafbau, Galvasud and Unibanco as of August 23, 1999.
(6) Pursuant to an industrial letter of credit issued by Banco do Nordeste do Brasil to Metalic, as of June 5, 2001 with maturity on February 5, 2011.
(7) Pledged pursuant to various legal proceedings, mainly related to tax claims.

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For information on environmental issues with respect to some of the facilities described above, see Item 4B. Business Overview Government Regulation and Other Legal Matters Environmental Expenditures and Claims. In addition, for information on our plans to construct, expand and improve our facilities, see Item 4A. History and Development of the Company Planned Investments.

The following map shows the locations of the Presidente Vargas steelworks, the CSN Paraná, INAL, INAL Nordeste, GalvaSud, Metalic, Lusosider, ERSA and CSN LLC facilities, our iron ore, limestone and dolomite mines, the power generating facilities in which we have an interest, and the main port used by us to export steel products and import coal and coke, as well as the main railway connections.

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Reserves at Casa de Pedra mine

We have concluded an extensive, multi-year study of our iron ore reserves at our Casa de Pedra mine in Congonhas, Minas Gerais State. The study consisted of three phases. Phase one, which was completed during 1999, covered the ore bodies that are currently being mined or are close to the current operating open pits. Phase two, which was completed in early 2003, covered the other iron ore deposits at the Casa de Pedra site. Phase three started in 2005 and involved a complete revaluation of reserves.

CSN conducted extensive work throughout 2006 to document and classify all information related to both the current and future operations of the Casa de Pedra mine.

As required by applicable SEC rules, we hired Golder Associates S.A., or Golder, to undertake an audit of the Casa de Pedra iron ore reserves. Golder carried out a full analysis of all available information and has used checks and experience to independently validate that the reported reserves are available to CSN for mining.

Golder accepts as appropriate the estimates regarding proven and probable reserves made by CSN totaling 1,631 million tons of iron ore at a grade of 47.79% Fe and 26.63% SiO2. This new ore reserve represents a significant increase when compared to the last appraisal report prepared in 2003, which totaled 444 million tons.

Casa de Pedra mine reserves are sufficient for production of about 50 Mtpa and give CSN the opportunity to develop a new age in its mining business.

The following table sets forth our estimates of proven and probable reserves and other mineral deposits at our mines reflecting the results of reserve study. They have been calculated in accordance with the technical definitions contained in the SEC's Industry Guide 7, and estimates of mine life described herein are derived from such reserve estimates.

MINERAL RESOURCES

	Proven and Probable Reserves[1]					**Mineral Deposits Resources[2]**
Mine Name and Location	**Ore Tonnage[3] (millions of tons)**		**Grade[4]**	**Rock Type**	**Recoverable Product[5] (millions of tons)**	**Tonnage (millions of tons)**
	Proven[6]	**Probable[7]**				
Iron:						
Casa de Pedra (Congonhas, Minas Gerais)	1,117	514	47.79% Fe	Hematite (21%) Itabirite (79%)	976	8,386
Limestone and Dolomite:	**Proven[6]**	**Probable[7]**				

Bocaina (Arcos, Minas Gerais)	134.5	46.6	49.4%CaO 3.78%MgO	Limestone (86%) Dolomite (14%)	177.1	1,201
	Proven+Probable (Mm^3)				**(tons)**	**Resources (Mm^3)**
Tin						
(Itapoã do Oeste, Rondônia)		42.82		Paleo valley and	24,934	97.36

(1) Reserves means that part of a mineral deposit which could be economically and legally extracted or produced at the time of the reserve determination.
(2) Includes inferred tonnages.
(3) Represents run-of-mine material.
(4) Grade is the proportion of metal or mineral present in ore or any other host material.
(5) Represents total product tonnage after mining and processing losses.
(6) Means reserves for which: (i) quantity is computed from dimensions revealed in outcrops trenches, workings or drill holes; grade and/or quality are estimated from the results of detailed sampling; and (ii) the sites for inspection, sampling and measurement are spaced so closely and the geological character is so well defined that size, shape, depth and mineral content of reserves are well established.
(7) Means reserves for which quantity and grade and/or quality are computed from information similar to that used for proven reserves, but the sites for inspection, sampling and measurement are farther apart or are otherwise adequately spaced. The degree of assurance, although lower than that for proven reserves, is high enough to assume between points of observation.

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Item 4A. Unresolved Staff Comments

The SEC has advised us that it has reviewed our amended Annual report on Form 20-F/A for the fiscal year ended December 31, 2004 (the "2004 Form 20-F") and our consolidated financial statements as of and for the years ended December 31, 2002, 2003 and 2004 included therein, filed with the SEC on April 27, 2006. Based on its review of this document, the SEC provided us with comments and questions. The unresolved staff comments are related to the accounting treatment of our accruals for disputed taxes payable that relates to certain tax liabilities for which we are disputing payment and the use of certain tax credits to offset such tax liabilities. Discussions regarding the 2004 Form 20-F are ongoing and could result in modifications to that document or this Form 20-F with respect to those or other issues. The company will continue to work with the SEC to reach resolution of any outstanding issues and will provide updates if any material developments occur.

Item 5. Operating and Financial Review and Prospects

The following discussion should be read in conjunction with our consolidated financial statements at and for the years ended December 31, 2006, 2005 and 2004 included in Item 18. Financial Statements. Our consolidated financial statements were prepared in accordance with U.S. GAAP and are presented in U.S. dollars, as explained in Note 2(a) to our consolidated financial statements included in Item 18. Financial Statements.

5A. Operating Results

Overview

The primary factors affecting our results of operations include:

- the cyclical dynamics of supply and demand for steel products both inside and outside Brazil, including the prices for such products;
- the mix of products sold by us (between domestic and export sales and between lower value-added and higher value-added products);
- our production costs; and
- Brazilian economic conditions generally, including changes in the *real* exchange rate against other currencies, particularly the U.S. dollar.

Markets and Product Mix

Supply and Demand for Steel

Prices of steel are sensitive to changes in worldwide and local demand, which in turn are affected by worldwide and country-specific economic cycles, and to available production capacity. While the export price of steel (which is denominated in U.S. dollars or Euros, depending on the export destination) is the spot price, there is no exchange trading of steel or uniform pricing. Unlike other commodity products, steel is not completely fungible due to wide differences in terms of size, chemical composition, quality and specifications, all of which impact prices. Many companies (including us) discount their list prices for regular customers, making actual transaction prices difficult to determine.

Historically, export prices and margins have been lower than domestic prices and margins, because of the logistics costs, taxes and tariffs. The portion of production that is exported is affected by domestic demand, exchange rate fluctuations and the prices that can be charged in the international markets.

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The following table shows Brazilian steel production and apparent consumption (domestic sales plus imports) and global production and demand for the periods indicated:

	Year ended December 31,		
	2004	**2005**	**2006**
Brazilian Market (in thousands of tons)			
Total Flat and Long Steel			
Production[1]	23,368	22,579	23,504
Apparent Consumption	18,316	16,806	18,533
Hot-Rolled Coils and Sheets			
Production	4,230	4,249	4,074
Apparent Consumption	2,971	2,600	2,822
Cold-Rolled Coils and Sheets			
Production	3,208	3,206	3,227
Apparent Consumption[1]	2,610	2,253	2,526
Galvanized Sheets			
Production[1]	2,193	1,883	2,293
Apparent Consumption[1]	1,706	1,540	1,879
Tin Mill			
Production[1]	973	741	828
Apparent Consumption[1]	677	504	655
Global Market (in millions of tons)			
Crude Steel Production	1,035	1,132	1,244
Demand	957	1,013	1,113

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Source: Brazilian Steel Institute and IISI

(1) Information for 2005 does not include heavy and coiled plates.

Product Mix and Prices

We have a strategy of maintaining production at full capacity in order to spread fixed costs over a higher volume of products and to maintain flexibility. This allows us to change our product mix in response to changes in domestic and export demand brought about by domestic and international macroeconomic conditions. As a result of this strategy, production levels are maintained, notwithstanding a decrease in domestic demand. This strategy could, therefore, in any particular period, cause the percentage of sales attributable to export sales to increase and the percentage attributable to domestic sales to decrease. As discussed below, the percentage of sales made in domestic and export markets will impact revenues expressed in U.S. dollars. See Effects of Exchange Rate Fluctuations.

We also have a strategy of increasing the portion of our sales attributable to higher value- added coated products, particularly galvanized products. Galvanized products are directed at the automotive, construction and home appliance industries. Similar to its impact on the percentage of domestic sales, the full production strategy could, therefore, in any particular period, cause the percentage of sales attributable to coated products to decrease. In addition, the increased production capacity coming on stream could have a similar impact, because increased capacity results in an increase in slabs and hot-rolled products production before the production of downstream coated products increases.

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Sales Volume and Net Operating Revenues by Steel Products and Markets

The following table sets forth our steel product sales volume and net operating revenues by product and market.

	Sales Volume								
	Metric Tons			% of Sales Volume					
				In Market			Total		
	2004	2005	2006	2004	2005	2006	2004	2005	2006
	(In thousands of metric tons)			*(In percentages)*					
Domestic Sales									
Slabs	57	46	46	2	2	2	1	1	1
Hot-rolled	1,142	1,037	1,003	34	36	35	24	22	22
Cold-rolled	648	399	439	20	14	16	14	8	10
Galvanized	783	726	736	24	25	26	17	15	17
Tin Mill	668	667	594	20	23	21	14	14	14
Sub-total	3,298	2,875	2,818	100	100	100	70	60	64
Export sales									
Slabs	44	86	120	3	4	8	1	2	3
Hot-rolled	512	717	289	37	38	19	12	15	7
Cold-rolled	96	237	142	7	12	9	2	5	3
Galvanized	455	593	759	33	30	48	9	12	17
Tin Mill	276	312	256	20	16	16	6	6	6
Sub-total	1,383	1,945	1,566	100	100	100	30	40	36
Total	4,681	4,820	4,384				100	100	100
Total Sales									
Slabs	101	132	166				2	3	4
Hot-rolled	1,654	1,754	1,292				36	37	29
Cold-rolled	744	636	581				16	13	13
Galvanized	1,238	1,319	1,495				26	27	34
Tin Mill	944	979	850				20	20	20
Total	4,681	4,820	4,384				100	100	100

The following table sets forth our steel product net revenues by product and market.

Net Operating Revenues

	U.S. dollars			% of Net Operating Revenues					
				In Market			Total		
	2004	2005	2006	2004	2005	2006	2004	2005	2006
	(In millions of US$)			*(In percentages)*					
Domestic Sales									
Slabs	15	14	14	1	1	1	1	-	-
Hot-rolled	543	693	618	28	29	26	19	19	17
Cold-rolled	372	313	322	19	13	14	13	9	9
Galvanized	535	661	713	27	28	30	19	19	20
Tin Mill	482	669	716	25	28	29	17	19	20
Sub-total	1,947	2,350	2,383	100	100	100	68	65	66
Export sales									
Slabs	22	18	43	2	1	4	1	1	1
Hot-rolled	272	327	168	29	27	14	9	9	5
Cold-rolled	72	125	93	8	10	8	3	3	3
Galvanized	362	463	659	39	39	55	13	13	18
Tin Mill	202	275	243	22	23	19	7	8	7
Sub-total	930	1,208	1,206	100	100	100	32	34	34

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Net Operating Revenues

	U.S. dollars			% of Net Operating Revenues					
				In Market			Total		
	2004	2005	2006	2004	2005	2006	2004	2005	2006
	(In millions of US$)			*(In percentages)*					
Total	2,877	3,558	3,589				100	100	100
Total Sales									
Slabs	37	32	57				1	1	1
Hot-rolled	815	1,020	786				28	29	22
Cold-rolled	444	438	415				15	12	12
Galvanized	897	1,124	1,372				31	32	38
Tin Mill	684	944	959				24	27	27
Total	2,877	3,558	3,589				100	100	100

(1) Net operating revenues do not include revenues from non-steel products, principally by-products, services and electric energy, which amounted to US$207 million, US$247 million and US$257 million in 2004, 2005 and 2006. Net operating revenues attributed to each product class were obtained by multiplying the average price per ton of each class of product by the sales volume of such class.

Effects of Exchange Rate Fluctuations

Our financial statements included in this annual report are expressed in U.S. dollars. Our export revenues are substantially denominated in U.S. dollars. Our domestic revenues are denominated in Brazilian *reais* (although domestic sales prices reflect international prices with a time lag of some months).

A significant portion of our cost of products sold are commoditized raw materials, the prices of which are denominated in U.S. dollars. The balance of our cost of products sold and our cash operating expenses (i.e., operating expenses other than depreciation and amortization) are denominated in *reais*.

The appreciation of the U.S. dollar against the *real* has the following effects on our results of operations expressed in U.S. dollars:

- domestic revenues tend to be lower (in comparison with prior years) and to the extent we sell more products than usual in the domestic as opposed to the export markets, this effect is magnified;
- the impact of *real* denominated costs of products sold and operating costs tend to be lower; and
- financial expenses are increased to the extent the exposure to dollar-denominated debt is not protected.

The appreciation of the *real* against the U.S. dollar has the following effects on our results of operations expressed in US dollars:

- domestic revenues tend to be higher (in comparison with prior years) and this effect is magnified to the extent that we have sold more products than usual in the domestic markets;

- the impact of real-denominated costs of products sold and operating costs tends to be higher; and

- financial income is higher to the extent the exposure to dollar-denominated debt has not been protected.

The impact during the three years ending December 31, 2006 of fluctuations in the *real* exchange rate against other currencies on our results of operations can be seen in the "foreign exchange and monetary gain (loss), net" line in our income statement, although that amount is partially offset by the net financial income (or expense) attributable to the profit (or loss) on our derivative transaction of our foreign currency-denominated debt. In order to minimize the effects of the exchange rate fluctuations, we often engage in derivative transactions, including currency swap and foreign currency option agreements. The appreciation of the *real* against the U.S.

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dollar during 2005 and 2006 affected our net results because the positive effects of such appreciation were not entirely offset by losses on derivative transactions.

For a discussion of the possible impact of fluctuations in the foreign currency exchange and interest rates on our principal financial instruments and positions, see Item 11. Quantitative and Qualitative Disclosures About Market Risk.

Effects of Inflation

Inflation rates in Brazil have been significantly volatile in the past, although they have stabilized in recent years. Inflation rates remained relatively stable from 2003 to 2004 and decreased in 2005 and 2006. These decreases in inflation are largely a result of the government s restrictive monetary policy, including periodic changes in interest rates, and the appreciation of the *real* against the U.S. dollar during the past three years.

Inflation affects our financial performance by increasing some of our costs and expenses denominated in *reais* that are not linked to the U.S. dollar. Our cash costs and operating expenses are substantially denominated in *reais* and have tended to increase with Brazilian inflation because the our suppliers and service providers generally increase prices to reflect Brazilian inflation. In addition, some of our *real-denominated* debt is indexed to take into account the effects of inflation. Under this debt, the principal amount is generally adjusted with reference to inflation indexes, 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 based on the *Certificado de Depósito Interbancário*, or CDI, rate which is partially adjusted for inflation.

The table below shows the Brazilian general price inflation (according to the IGP- M) and the CDI for the periods shown.

	Year ended December 31,		
	2004	**2005**	**2006**
Inflation (IGP-M) [1]	12.4%	1.2%	3.8%
CDI [2]	16.3%	19.1%	15.1%

Source: Fundação Getúlio Vargas, or FGV, and Bloomberg.

(1) The IGP-M inflation is the general market price index measured by the FGV.

(2) The CDI rate is the average rate for interbank deposits made during the day in Brazil (accumulated for the month of the end of the period and annualized).

Critical Accounting Estimates

In preparing our financial statements, we make estimates concerning a variety of matters. Some of these matters are highly uncertain, and our estimates involve judgments we make based on the information available to us. In the discussion below, we have identified several of these matters for which our financial presentation would be materially affected if either (1) we used different estimates that we could reasonably have used or (2) in the future we change our estimates in response to changes that are reasonably likely to occur.

This discussion addresses only those estimates that we consider most important based on the degree of uncertainty and the likelihood of a material impact if we used a different estimate. There are many other areas in which we use estimates about uncertain matters, but the reasonably likely effect of changed or different estimates is not material to

our financial presentation.

Valuation of long- lived assets

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Under U.S. GAAP, in accordance with SFAS No. 144, long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to the estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized in the amount by which the carrying amount of the asset exceeds the fair value of the asset.

A determination of the fair value of an asset requires management to make certain assumptions and estimates with respect to projected cash inflows and outflows related to future revenues and expenditures and expenses. These assumptions and estimates can be influenced by different external and internal factors, such as economic and industry trends, interest rates and changes in the marketplace. A change in the assumptions and estimates that we use could change our estimate of the expected future net cash flows and lead to the recognition of an impairment charge in results of operations relating to our property, plant and equipment.

Depreciation and amortization

Adopted depreciation rates are based on estimated useful lives of the underlying assets, derived from historical information available to us, as well as known industry trends. Depreciation is computed on the straight-line basis at rates which take into consideration the useful lives of the related assets, as follows (average): buildings - 25 years; equipment - 15 years; furniture and fixtures - 10 years; hardware and vehicles - 5 years. The sensitivity of an impact in changes in the useful lives of property, plant and equipment was assessed by applying a hypothetical 10% increase in the depreciation rate existing at December 31, 2006. This hypothetical change would result in an incremental increase in the annual depreciation expense of US$21 million in the year of the change.

Financial instruments

SFAS 133, Accounting for Derivative Financial Instruments and Hedging Activities, as amended by SFAS 137, SFAS 138 and SFAS 149, requires that we recognize all derivative financial instruments as either assets or liabilities on our balance sheet and measure such instruments at fair value. Changes in the fair value of derivatives are recorded in each period in current earnings or in other comprehensive income (outside net income), in the latter case depending on whether a transaction is designated as an effective hedge. We have not designated any derivative financial instruments as hedges and the fair value adjustments to our derivatives were thus recorded in current net income. With respect to the fair value measurement, we must make assumptions such as to future foreign currency exchange and interest rates. For a discussion of the possible impact of fluctuations in the foreign currency exchange and interest rates on our principal f inancial instruments and positions, see Item 11. Quantitative and Qualitative Disclosures About Market Risk.

Pension plans

We sponsor defined benefit pension plans covering some of our retirees. We account for these benefits in accordance with SFAS No. 87, Employers Accounting for Pensions, and amendments.

The determination of the amount of our obligations for pension benefits depends on certain actuarial assumptions. These assumptions are described in Note 16 to our consolidated financial statements and include, among others, the expected long-term rate of return on plan assets and increases in salaries. In accordance with U.S. GAAP, actual results that differ from our assumptions are accumulated and amortized over future periods and generally affect our recognized expenses and recorded obligations in such future periods.

Deferred taxes

We compute and pay income taxes based on results of operations determined under Brazilian GAAP. We recognize deferred income tax assets and liabilities based on the differences between the financial statement carrying amounts and the tax bases of assets and liabilities. We regularly review the deferred income tax assets for recoverability and establish a valuation allowance if, under U.S. GAAP, it is more likely than not that the deferred income tax assets will not be realized, based on historical taxable income, projected future taxable income, and the expected timing of the reversals of existing temporary differences. A change in the assumptions and estimates with respect to our expected future taxable income could result in the recognition of a valuation allowance being charged to income. If we operate at a loss or are unable to generate sufficient future taxable income, or if there is a material change in the actual effective tax rates or discount rates, the time period over which the underlying temporary differences become taxable or deductible, or any change in its future projections, we could be required to establish a valuation allowance against all or a significant portion of our deferred tax assets, resulting in a substantial increase of our effective tax rate and a material adverse impact on operating results.

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Contingencies and disputed taxes

We record provisions for contingencies relating to legal proceedings with respect to which we deem the likelihood of an unfavorable outcome to be probable and the loss can be reasonably estimated. This determination is made based on the legal opinion of our internal and external legal counsel. We believe these contingencies are properly recognized in our financial statements in accordance with Statements of Financial Accounting Standards No. 5, or SFAS No. 5. 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 us. We believe that these proceedings will ultimately result in the realization of contingent tax credits or benefits that can be used to settle direct and indirect tax obligations owed to the Brazilian Federal or State Governments. We do not recognize these contingent tax credits or benef its in our financial statements until realization of such gain contingencies has been resolved. This occurs when a final irrevocable decision is rendered by the courts in Brazil. When we use contingent tax credits or benefits based on favorable temporary court decisions that are still subject to appeal to offset current direct or indirect tax obligations, we maintain the legal obligation accrued in our financial statements until a final irrevocable judicial decision on those contingent tax credits or benefits is rendered. The accrual for the legal obligation related to the current direct or indirect tax obligations offset is not reversed until such time as the utilization of the contingent tax credits or benefits is ultimately realized. This accounting is consistent with our analysis of a liability under FASB Concepts Statement No. 6. The accounting for the contingent tax credits is in accordance with accounting for contingent assets under SFAS No. 5. Our accruals include interest on the tax obligations that we may offset with contingent tax credits or benefits at the interest rate defined in the relevant tax law. The recorded accruals for these disputed taxes and other contingencies may change in the future due to new developments in each matter, such as changes in legislation, irrevocable, final judicial decisions specific to us, or changes in approach, such as a change in settlement strategy in dealing with these matters. See Item 5A. Operating Results Results of Operations 2006 Compared to 2005 Disputed Taxes Payable and Item 8A. Consolidated Statements and Other Financial Information Legal Proceedings for further information on the judicial and administrative proceedings in which we are involved.

Recently Issued Accounting Pronouncements

The following new accounting standards have been issued and were adopted by us as of December 31, 2006:

FSP No. FAS 115- 1 and 124- 1, "The Meaning of Other-Than-Temporary Impairment and its Application to Certain Investments" (FSP No. FAS 115- 1 and 124- 1). The FASB issued FSP No. FAS 115- 1 and 124- 1 in November 2005, which was effective for us beginning January 1, 2006. This FSP addresses the determination as to when an investment is considered impaired, whether that impairment is other than temporary, and the measurement of an impairment loss. This FSP also includes accounting considerations subsequent to the recognition of an other-than-temporary impairment and requires certain disclosures about unrealized losses that have not been recognized as other- than- temporary impairments. The guidance in this FSP amends SFAS No. 115, " Accounting for Certain Investments in Debt and Equity Securities,"and SFAS No. 124, " Accounting for Certain Investments Held by Not-for- Profit Organizations,"and APB Opinion No. 18. The adoption of FSP No. FAS 115- 1 and 124- 1 did not have a material impact on the our consolidated results of operations, cash flows or financial position.

SFAS No. 158, "Employer s Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106, and 132(R)" (SFAS No. 158). In September 2006, the FASB issued SFAS No. 158, which changes the recognition and disclosure provisions and measurement date requirements for an employer s accounting for defined benefit pension and other postretirement plans. The recognition and disclosure provisions require an employer to (1) recognize the funded status of a benefit plan-- measured as the difference between plan assets at fair value and the benefit obligation-- in its statement of financial position, (2) recognize as a component of OCI, net of tax, the gains or losses and prior service costs or credits that arise during the period but are

not recognized as components of net periodic benefit cost, and (3) disclose in the notes to financial statements certain additional information. SFAS No. 158 does not change the amounts recognized in the income statement as net

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periodic benefit cost. We are required to initially recognize the funded status of our defined benefit pension and other postretirement plans and to provide the required additional disclosures as of December 31, 2006. Retrospective application is not permitted. The adoption of SFAS No. 158 recognition and disclosure provisions are discussed in Note 16 to these consolidated financial statements.

SAB No. 108, "Considering the Effects of Prior Year Misstatements When Quantifying Misstatements in Current Year Financial Statements" (SAB No. 108). In September 2006 the SEC issued SAB No. 108, which provides interpretive guidance on how the effects of the carryover or reversal of prior year misstatements should be considered in quantifying a current year misstatement. Traditionally, there have been two widely-recognized approaches for quantifying the effects of financial statement misstatements. The income statement approach focuses primarily on the impact of a misstatement on the income statement-- including the reversing effect of prior year misstatements--but its use can lead to the accumulation of misstatements in the balance sheet. The balance sheet approach, on the other hand, focuses primarily on the effect of correcting the period-end balance sheet with less emphasis on the reversing effects of prior year errors on the income statement. The SEC staff believes that registrants should quantify errors using both a balance sheet and an income statement approach (a " dual approach") and evaluate whether either approach results in quantifying a misstatement that, when all relevant quantitative and qualitative factors are considered, is material.

SAB No. 108 was effective for our year ended December 31, 2006. SAB No. 108 permits existing public companies to initially apply its provisions either by (i) restating prior financial statements as if the "dual approach" had always been used or (ii), under certain circumstances, recording the cumulative effect of initially applying the "dual approach" as adjustments to the carrying values of assets and liabilities as of January 1, 2006 with an offsetting adjustment recorded to the opening balance of retained earnings. The adoption of SAB No. 108 did not have any material impact on our consolidated results of operations, cash flows or financial position.

The following new accounting standards have been issued, but have not yet been adopted by us as of December 31, 2006.

SFAS No. 155, "Accounting for Certain Hybrid Financial Instruments an amendment of FASB Statements No. 133 and 140" (SFAS No. 155). In February 2006, the FASB issued SFAS No. 155, which amends SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" and SFAS No. 140,"Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities." SFAS No. 155 allows financial instruments that have embedded derivatives to be accounted for at fair value at acquisition, at issuance, or when a previously recognized financial instrument is subject to a remeasurement (new basis) event, on an instrument- by-instrument basis, in cases in which a derivative would otherwise have to be bifurcated. SFAS No. 155 is effective for us for all financial instruments acquired, issued, or subject to remeasurement after January 1, 2007, and for certain hybrid financial instruments that have been bifurcated prior to the effective date, for which the effect is to be reported as a cumulative-effect adjustment to beginning retained earnings. We do not anticipate the adoption of SFAS No. 155 will have any material impact on our consolidated results of operations, cash flows or financial position.

SFAS No. 156, "Accounting for Servicing of Financial Assets-- an amendment of FASB Statement No. 140" (SFAS No. 156). In March 2006, the FASB issued SFAS No. 156, which amends SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities."SFAS No. 156 requires recognition of a servicing asset or liability when an entity enters into arrangements to service financial instruments in certain situations. Such servicing assets or servicing liabilities are required to be initially measured at fair value, if practicable. SFAS No. 156 also allows an entity to subsequently measure its servicing assets or servicing liabilities using either an amortization method or a fair value method. SFAS No. 156 is effective for us as of January 1, 2007, and must be applied prospectively, except that where an entity elects to remeasure separately recognized existing arrangements and reclassify certain available-for-sale securities to trading securities, any effects must be

reported as a cumulative- effect adjustment to retained earnings. We do not anticipate the adoption of SFAS No. 156 will have any material impact on our consolidated results of operations, cash flows or financial position.

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SFAS No. 157, "Fair Value Measurements" (SFAS No. 157). In September 2006, the FASB issued SFAS No. 157, which defines fair value, establishes a framework for measuring fair value in GAAP, and expands disclosures about fair value measurements. SFAS No. 157 does not require any new fair value measurements. For us, SFAS No. 157 is effective as of January 1, 2008 and must be applied prospectively except in certain cases. We are currently evaluating the impact of adopting SFAS No. 157, and believe that such standard will not generate a material impact on our consolidated results of operations, cash flows or financial position.

In June 2006, the FASB issued FIN 48 - "Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109", which clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No.109 - "Accounting for Income Taxes". This interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This Interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. This Interpretation is effective for fiscal years beginning after December 15, 2006. Earlier application is encouraged if the enterprise has not yet issued financial statements, including interim financial statements, in the period this Interpretation is adopted. We have not fini shed our work on evaluating the impacts of the adoption of such pronouncement.

SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" (SFAS No. 159). In February 2007, the FASB issued SFAS No. 159, which permits entities to choose to measure many financial instruments and certain other items at fair value. For us, SFAS No. 159 is effective as of January 1, 2008 and will have no impact on amounts presented for periods prior to the effective date. We cannot currently estimate the impact of SFAS No. 159 on our consolidated results of operations, cash flows or financial position and have not yet determined whether or not we will choose to measure items subject to SFAS No. 159 at fair value.

FSP No. AUG AIR- 1, "Accounting for Planned Major Maintenance Activities," (FSP No. AUG AIR- 1). In September 2006, the FASB Staff issued FSP No. AUG AIR- 1. This FSP prohibits the use of the accrue- in- advance method of accounting for planned major maintenance activities in annual and interim financial reporting periods, if no liability is required to be recorded for an asset retirement obligation based on a legal obligation for which the event obligating the entity has occurred. The FSP also requires disclosures regarding the method of accounting for planned major maintenance activities and the effects of implementing the FSP. The guidance in this FSP is effective for us as of January 1, 2007 and will be applied retrospectively for all financial statements presented. We do not anticipate the adoption of FSP No. AUG AIR-1 will have any material impact on our consolidated results of operations, cash flows or financial position, as we already apply the direct expensing method of accounting.

EITF Issue No. 06- 3, "How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That Is, Gross versus Net Presentation)" (EITF No. 06- 3). In June 2006, the EITF reached a consensus on EITF No. 06- 3 to address any tax assessed by a governmental authority that is directly imposed on a revenue- producing transaction between a seller and a customer and may include, but are not limited to, sales, use, value added, and some excise taxes. For taxes within the issue s scope, the consensus requires that entities present such taxes on either a gross (i.e. included in revenues and costs) or net (i.e. exclude from revenues) basis according to their accounting policies, which should be disclosed. If such taxes are reported gross and are significant, entities should disclose the amounts of those taxes. Disclosures may be made on an aggregate basis. The consensus is effective for us beginning January 1, 2007. We do not anticipate the adoption of EITF No. 06- 3 will have any material impact on our consolidated results of operations, cash flows or financial position. As discussed in Note 3 to our financial statements included in "Item 18. Financial Statements", our policy is and will continue to be to classify such taxes as a deduction from operating revenues.

EITF Issue No. 06- 6, "Debtor s Accounting for a Modification (or exchange) of Convertible Debt Instruments" (EITF No. 06- 6). In November 2006, the EITF reached a consensus on EITF No. 06- 6. EITF No. 06- 6 addresses how a modification of a debt instrument (or an exchange of debt instruments) that affects the terms of an embedded conversion option should be considered in the issuer s analysis of whether debt extinguishment accounting should be applied, and further addresses the accounting for a modification of a debt instrument (or an exchange of debt instruments) that affects the terms of an embedded conversion option when extinguishment accounting is not applied. EITF No. 06- 6 applies to modifications (or exchanges) occurring in interim or annual reporting periods beginning after November 29, 2006, regardless of when the instrument was originally issued. Early application is permitted for modifications (or exchanges) occurring in periods for which financial statements have not been issued. There were no modifications to, or exchanges of, any of our debt instruments within the scope of EITF No. 06- 6 in 2006. The impact to us of applying EITF No. 06- 6 in subsequent periods will be dependent upon the nature of any modifications to, or exchanges of, any debt instruments within the scope of EITF No. 06- 6.

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Results of Operations

For purposes of comparison, the following table presents the items indicated as percentages of net operating revenues for each of the years ended December 31, 2004, 2005 and 2006 and the percentage change in each of these items from 2004 to 2005 and from 2005 to 2006:

	Year Ended December 31,			Increase (Decrease)	
	2004	**2005**	**2006**	**2005/2004**	**2006/2005**
	%	%	%	%	%
Operating revenues					
Domestic sales	93.9	90.6	92.3	19.1	2.9
Export sales	32.7	32.2	32.8	21.4	3.2
	126.6	**122.8**	**125.1**	**19.7**	**3.0**
Sales Taxes	(23.8)	(21.8)	(23.4)	12.8	(8.4)
Discounts, returns and allowances	(2.7)	(1.0)	(1.7)	(53.6)	(74.4)
Net operating revenues	**100.0**	**100.0**	**100.0**	**23.4**	**1.1**
Cost of products sold	45.6	48.3	54.7	30.6	14.4
Gross profit	**54.4**	**51.7**	**45.3**	**17.4**	**(11.4)**
Operating expenses					
Selling	5.1	4.9	4.3	19.2	(10.2)
General and administrative	3.5	2.8	3.8	(0.9)	37.0
Others	1.6	0.7	3.9	(44.0)	432.1
Operating income	**44.2**	**43.3**	**33.3**	**20.9**	**(22.2)**
Non-operating income (expenses), net					
Financial income (expenses), net	(16.5)	(14.5)	(13.9)	7.8	3.1
FOREIGN EXCHANGE AND MONETARY GAIN					
(LOSS), NET	5.0	4.8	5.7	19.6	19.1
Others, net	(0.2)	0.1	0.6	(150.0)	633.3

Income before income taxes and equity in results of affiliated companies	**32.4**	**33.7**	**25.7**	**28.3**	**(23.0)**
Income tax expense (benefit)	9.4	11.2	7.7	46.7	(30.7)
Current	9.4	12.0	5.1	58.5	(56.8)
Deferred	0.1	(0.8)	2.5	(1,650.0)	416.1
Equity in results of affiliated companies	1.7	1.2	1.5	(7.8)	23.4
Net income	**24.6**	**23.7**	**19.5**	**18.8**	**(17.0)**

2006 Compared to 2005

Operating Revenues

Our results for the year ended December 31, 2006 were strongly affected by an accident involving the gas cleaning system adjacent to our Blast Furnace No. 3, on January 22, 2006. This accident prevented us from operating the equipment until the second half of the year, and impacted our operating revenues, gross profit and operating income, as a result of reduced sales volumes and higher cost of goods sold (because we had to purchase slabs from third-party sources), as explained below. The 17% reduction (US$153 million) in our net income to US$749 in 2006, from US$902 in 2005 was mainly due to the impact of the accident mentioned above, partially offset by the recognition of the insurance claim in the amount of US$351 million.

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Export Sales

The year 2006 was marked by adjustments between global supply and demand and price recoveries through localized production cutbacks and by exceptionally volatile prices for metals, with a direct effect on steel prices. International steel product prices were subject to swings, peaking in mid- July, 2006.

In addition, the international steel market continued with its consolidation process, with expansion projects concentrated in the low-cost production regions, notably in the BRIC nations (Brazil, India, Russia and China).

In the North American and European markets, the increase in consumption combined with the slowdown in supply growth (in the US, various blast furnace repairs led to delays in the production schedule) and higher import prices, were the key drivers in the price increases.

In the Chinese market, prices had been rising since the end of 2005, due to the reduction in output rates by the local steel mills.

Due to the accident described above and to the commercial strategy of prioritizing local sales, in 2006 CSN exported 1,566 million tons, 19% below the exported volume registered in 2005. CSN s average 2006 export prices increased at an average of 12.8% in U.S. dollars compared to 2005. In the export market, operating revenues increased 3% to US$1,263 million in 2006, from US$1,224 million in 2005

Domestic Sales

Brazil s GDP recorded growth of 3.7% in 2006, less than the global average of 5.1% and also lower than the 6.5% average registered by the emerging countries. In 2006 as a whole, Brazil s flat steel sales increased 7.3% over the previous year, led by the automotive (11.8%), distribution (12.0%), home appliance (9.9%) and OEM (19.7%) segments.

CSN s 2006 annual domestic sales volume (2,818 million tons) remained in line with the previous year, in accordance with the Company s strategy of prioritizing the Brazilian market, where the Company historically generates higher margins.

For the year as a whole, CSN recorded an average market share of 27%, remaining stable in comparison with the previous year. As for the product mix, once again high value- added products such as galvanized, galvalume and tin plate accounted for more than 53% of the market share for the coated products domestic market, at the same level as in 2005.

Domestic prices began to recover in the middle of the second quarter, in line with metal prices (copper, zinc, tin, aluminum, etc.) and with international prices. Domestic prices peaked in the third quarter, returning to their 2005 levels in the final quarter. For the year as a whole, CSN s average prices increased 2.4% in U.S. dollars.

In the domestic market, CSN s operating revenues increased by 3% to US$3,550 million in 2006, from US$3,449 million in 2005.

As a result of the combined effect of prices and volumes sold and the exchange rate appreciation, we recorded total operating revenues of US$4,813 million in 2006, representing a 3% (or US$140 million) increase from operating revenues of US$4,673 million in 2005.

These results are particularly important, given the accident described above which interrupted the production at Blast Furnace No. 3 at our Presidente Vargas steelworks, which is responsible for approximately 70% of the Company s crude steel output. Also, CSN took immediate steps to acquire appropriate volumes of steel slabs in order to ensure the delivery of end products to its clients and to keep its dominant market-shares.

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The Company immediately activated its pool of insurers, in order to guarantee compensation as quickly as possible, both for damaged equipment and margin lost, through the insurance policies duly taken out to cover such a contingency.

Net Operating Revenues

Net operating revenues increased by 1%, to US$3,846 in 2006, from US$3,805 million in 2005, mainly due to the 3% increase in operating revenues, whereas sales deductions experienced an increase of 11.0% . Sales deductions, as a percentage of operating revenues, were 19% in 2005 and 20% in 2006.

Cost of Goods Sold and Production Costs

Cost of goods sold increased by 14%, to US$2,102 million in 2006, from US$1,837 million in 2005, mainly as a result of the strengthening of the *real* against the U.S. dollar and the resulting effect on our *real-denominated* costs, the consumption of 957,000 tons of slabs and 63,000 tons of hot-rolled coils acquired from third parties after the accident on the gas cleaning system adjacent to Blast Furnace No. 3, to keep our rolling mills at full capacity, and the increase in international zinc prices, partially offset by the US$342 million provision for business interruption.

Production costs totaled US$2,062 million in 2006, representing a 13% increase (US$232 million) compared to US$1,830 of production costs in 2005. Expressed in *reais*, production costs were in line with the 2005 figure. There were, however, opposing factors among various lines , which ended up canceling each other out: the cost increase was from the consumption of slabs and coils acquired from third parties and the upturn in international zinc prices offset by reduced consumption of raw materials, such as coke, iron ore, tin, electric power and fuel costs.

As the parent company s production cost is a proxy to our cost of goods sold, we can analyze our changes in cost of goods sold based on the variations occurred in our production cost.

The following table sets forth for the parent company s production costs, the production costs per ton of crude steel and the portion of production costs attributable to the primary components of our costs of production. With the exception of coal and some coke, which we import, and some metals (such as zinc, aluminum and tin), whose domestic prices are linked to international prices, our costs of production, as well as our other operating expenses, are mostly denominated in *reais.* The devaluation of the Brazilian *real* causes U.S. dollar-denominated or U.S. dollar-linked production costs to increase as a percentage of total production costs. Conversely, appreciation of the *real* causes *real*-denominated production costs to increase as a percentage of total production costs.

	Year Ended December, 31								
	2004			**2005**			**2006**		
	US$ 000	**US$/ton**	**%**	**US$ 000**	**US$/ton**	**%**	**US$ 000**	**US$/ton**	**%**
Raw Materials									
Iron Ore	52,533	9.58	3.6	72,551	14.03	4.0	66,174	14.92	3.2
Coal	258,879	47.23	17.7	387,514	74.92	21.2	348,264	78.52	16.9
Coke	259,318	47.31	17.7	224,530	43.41	12.3	36,048	8.13	1.7
Metals	28,215	5.15	1.9	4,501	0.87	0.2	165,020	37.20	8.0
Outsourced Hot Coils	111,923	20.42	7.7	119,177	23.04	6.5	30,712	6.92	1.5

Outsourced Slabs	0	0	-	0	0	-	389,095	87.72	18.9
Other	113,213	20.66	7.7	148,418	28.70	8.1	136,206	30.71	6.6
	824,081	**150.35**	**56.4**	**956,690**	**184.97**	**52.3**	**1,171,519**	**264.12**	**56.8**
Energy/Fuel	159,631	29.12	10.9	191,568	37.04	10.5	169,349	38.18	8.2
Labor	106,566	19.44	7.3	157,899	30.53	8.6	175,651	39.60	8.5
Services and Maintenance	166,993	30.47	11.4	256,965	49.68	14.0	274,440	61.87	13.4
Tools and Supplies	77,683	14.17	5.3	105,272	20.35	5.7	100,752	22.71	4.9
Depreciation	111,765	20.39	7.6	142,219	27.50	7.8	165,813	37.38	8.0
Others	15,674	2.86	1.1	20,313	3.93	1.1	5,055	1.14	0.2
	1,462,392	**266.81**	**100.0**	**1,830,925**	**354.00**	**100.0**	**2,062,579**	**465.00**	**100.0**

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The comparative analysis of the average cost per ton of products, which increased 31% from US$354.00 in 2005 to US$465.00 in 2006, is also impacted by the use of slabs and coils acquired from third parties and the reduced consumption of raw materials and other items in 2006. The consumption of raw materials such as iron ore, coal, coke, aluminum and tin decreased by 35%, 18%, 70%, 7% and 20%, respectively. Prices per ton of iron ore, zinc and aluminum increased by 41%, 85%, and 13%, respectively.

There is a large difference between the costs of other items expressed in *reais* and that expressed in U.S. dollars, and a large proportion of these costs is denominated in *reais*. As a result, our labor costs in 2006 expressed in U.S. dollars increased 11%, while our labor costs expressed in *reais* increased 2% compared to 2005, mainly reflecting the annual Brazilian inflation rate and the annual wage increases in May 2006. For further information, see Selling, General and Administrative Expenses. In addition, our depreciation costs in 2006 expressed in U.S. dollars increased by 17%, while our depreciation costs expressed in Brazilian *reais* increased by 5%.

Gross Profit

Gross profit decreased by 11.4% to US$1,744 million in 2006, from US$1,968 million in 2005, mainly due to the US$265 million increase in cost of goods sold in 2006, due principally to the acquisition of slabs and coils from third-party sources at higher costs than our production costs (net of recorded insurance recoveries of US$351 million), and to higher zinc prices. As a result, our gross margin decreased from 42.1% in 2005 to 36.2% in 2006.

Selling, General and Administrative Expenses

In 2006, we recorded selling, general and administrative expenses of US$315 million, representing a 7.1% increase from the US$294 million recorded in 2005.

Selling expenses decreased by 10.2%, to US$167 million in 2006, from US$186 million in 2005, mainly due to lower freight costs as a result of a decrease in volume of exports, which decreased 19% to 1,566 million tons in 2006. As a percentage of net operating revenues, selling expenses decreased from 4.9% in 2005 to 4.3% 2006. Expressed in *reais*, these expenses decreased by 17.5% .

General and administrative expenses increased by US$40 million, or 37%, to US$148 million in 2006, from US$108 million in 2005, mainly due to increased labor expenses (wage increases in May 2006 pursuant to annual negotiations under our collective bargaining agreements), and external legal counsel and consultant expenses. Expressed in *reais*, these expenses increased by 16.7% .

Other Income (Expenses)

When compared to 2005, other expenses sharply increased by US$121 million to an expense of US$149 million in 2006 from an expense of US$28 million in 2005. The variation is basically due to the US$73 million (US$224 million in 2005) reversal of provisions motivated by the revision of the likelihood of success in many judicial disputes made by our internal and external legal advisors, as well as due to the recent favorable track record on related disputes for labor and civil contingencies.

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Operating Income

Operating income decreased by US$366 million, or 22.2%, to US$1,280 million in 2006, from US$1,646 million in 2005. This decrease was mainly due to the US$224 million decrease in gross profit.

Non-operating Expenses (Income), Net

Non-operating expenses net decreased by 19.5%, or US$71 million, to US$293 million in 2006, from US$364 million in 2005. Our non- operating expenses (income), net are comprised of financial expenses, net and foreign exchange and monetary gain, net.

Financial Expenses (Income), net

In 2006, our financial expenses, net decreased by 3%, or US$17 million, to US$533 million in 2006, from US$550 million in 2005, mainly due to the following items:

- US$24 million decrease in interest income;
- US$24 million increase in interest expense;
- US$27 million decrease in our expenses on derivative instruments; and
- US$38 million decrease in other financial income (expenses).

Interest income

Interest income decreased by 15.7%, or US$24 million, to US$129 million in 2006, from US$153 million in 2005, mainly due to lower interest rates in Brazil and a lower average amount of cash & cash equivalents and short-term investments.

Interest expense

Interest expense increased by 5.9%, or US$24 million, to US$431 million in 2006, from US$407 million in 2005 mainly due to the PIS and COFINS on the provision for insurance claim related to the accident with an equipment adjacent to Blast Furnace No.3.

Derivative Instruments

The expenses derived from our derivative instruments decreased by US$27 million to an expense of US$218 million in 2006, from an expense of US$245 million in 2005. Due to the strengthening of the *real* against the U.S. dollar, our expenses on foreign exchange derivative instruments increased by US$32 million, to US$328 million in 2006, and were partially offset by a US$59 million increase in gain on equity linked derivatives, to US$110 million in 2006, from US$51 million in 2005.

Other financial income (expense)

Other financial income (expense) decreased by US$64 million, to an income of US$13 million in 2006, from an expense of US$51 million in 2005, mainly due to the US$45 million reversal of the CPMF tax provision during 2006 and an additional US$7 million of capitalized interest, higher than in 2005.

Foreign exchange and monetary gain, net

Foreign exchange and monetary gain, net is mainly affected by fluctuations in the *real*/U.S. dollar foreign exchange rate and the impact of such fluctuations on the following:

- our U.S. dollar-denominated gross debt;

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- our U.S. dollar-denominated cash, cash equivalents and short term investments;
- our equity investments in offshore subsidiaries; and
- our trade accounts receivable and payable.

The 19.1%, or US$35 million increase in foreign exchange and monetary gain, to US$218 million in 2006, from US$183 million in 2005, was primarily due to the impact of lower inflation rates in Brazil on our inflation-indexed outstanding debt and the 8.7% appreciation of the *real* against the U.S. dollar on our higher average accounts payable denominated in U.S. dollars.

Income Taxes

We recorded an expense for income tax and social contribution of US$296 million in 2006, compared to US$427 million in 2005. The difference is due to decrease in income before taxes and equity in results of affiliated companies, to US$987 million in 2006, from US$1.282 million in 2005. Expressed as a percentage of pre-tax income, income tax expense decreased to 30% in 2006, from 33.3% in 2005. Income tax expense in Brazil refers to the collection of federal income tax and social contribution tax. The statutory rates for these taxes applicable to the periods presented herein were 25% for federal income tax and 9% for the social contribution. Therefore, the balances owed for these periods totaled US$436 million in 2005 and US$336 million in 2006 (34% of income before taxes and equity in affiliated companies). Adjustments are made to these rates in order to arrive at the actual tax expense for the years.

For the period ended December 31, 2006, adjustments totaled an income of US$40 million and were comprised of:

- a US$28 million benefit from interest on stockholder s equity;
- other permanent differences that represented a net tax credit of US$12 million. The reversal of tax payable under dispute in the amount of US$18 million was offset against foreign exchange loss on the net equity of our offshore subsidiaries, due to the appreciation of the *real* against the U.S. dollar, which was recorded in our results of operations for Brazilian GAAP purposes and represented a non-taxable item. Also, certain expenses such as fines, gifts and donations are included within these permanent differences.

For the period ended December, 31 2005, these adjustments totaled an expense of US$9 million and were comprised of:

- US$38 million benefit from interest on stockholder s equity, which is a deductible expense for tax purposes; and
- other permanent differences that represented tax expenses of US$29 million. Foreign exchange loss on the net equity of our offshore subsidiaries represented a significant permanent item this period due to the appreciation of the *real* against the U.S. dollar, which was recorded in our results of operations for Brazilian GAAP purposes and represented a non-taxable item. Also, certain expenses such as fines, gifts and donations are included within these permanent differences.

The effect regarding the reversal of income taxes provision, which was calculated based on tax loss carryforward compensated over the legal limit of 30%, in the amount of US$76 million, was offset against deferred income tax calculated at the same base.

Our taxable income, generated from our operations in Brazil and abroad, is comprised of the following:

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	Year Ended December 31,		
	2005	**2006**	**Changes**
	(In million of U.S. dollars)		
Taxable income generated in Brazil	1,231	944	(287)
Foreign taxable income	51	43	(8)

Our taxable income in Brazil was impacted by the decrease in sales as a result of the accident involving the gas cleaning system adjacent to Blast Furnace No. 3 in early 2006, which resulted in a lower taxable income in 2006 as compared to 2005, particularly sharpened by a net loss of US$81 million in the second quarter of 2006, period in which the effects of the interruption in activities of Blast Furnace No. 3 became stronger. The total decrease in taxable income in 2006 compared to 2005 totaled US$295 million. Expressed in *reais*, our taxable income decreased 23% in 2006 compared to 2005.

Our foreign taxable income in the years ended December 31, 2005 and 2006 decreased US$8 million.

It is not possible to predict the adjustments to the federal income tax and social contribution at statutory rates, as they depend on interest on stockholder s equity, non-taxable factors including income from offshore operations, and tax losses from offshore operations, especially when expressed as a percentage of income. Therefore, management cannot foresee the effective income tax rate in future periods.

Accruals for Disputed Taxes Payable

We record provisions for contingencies relating to legal proceedings with respect to which we deem the likelihood of an unfavorable outcome to be probable and the loss can be reasonably estimated. This determination is made based on the legal opinion of our internal and external legal counsel. We believe these contingencies are properly recognized in our financial statements in accordance with SFAS No. 5. 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 us. We believe that these proceedings will ultimately result in the realization of contingent tax credits or benefits that can be used to settle direct and indirect tax obligations owed to the Brazilian Federal or State Governments. We do not recognize these contingent tax credits or benefits in our financial statements until realization of such gain contingencies has been resolved. This occurs when a final irrevocable decision is rendered by the courts in Brazil. When we use contingent tax credits or benefits based on favorable temporary court decisions that are still subject to appeal to offset current direct or indirect tax obligations, we maintain the legal obligation accrued in our financial statements until a final irrevocable judicial decision on those contingent tax credits or benefits is rendered. The accrual for the legal obligation related to the current direct or indirect tax obligations offset is not reversed until such time as the utilization of the contingent tax credits or benefits is ultimately realized. This accounting is consistent with our analysis of a liability under FASB Concepts Statement No. 6. The accounting for the contingent tax credits is in accordance with accounting for contingent assets under SFAS No. 5. Our accruals include interest on the tax obligations that we may offset with contingent tax credits or benefits at the interest rate defined in the relevant tax law.

We classify an accrual as short-term when we expect the liability to be settled in 360 days or less. This usually occurs when a final and unappealable and irrevocable judgment has been rendered and the legal processes are in the execution phase. However, given the complexity of the Brazilian legal system and the intricacies of some claims, it is impracticable for Brazilian companies to predict the time period in which final

decisions will be reached for such claims. Consequently, these claims are classified as long-term liabilities.

A brief description of the major recent developments regarding our accruals for disputed taxes payable follows:

Disputed taxes payable

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- *Imposto sobre produtos industrializados* - IPI (Excise tax) presumed credit on inputs

We have accrued a liability for certain tax liabilities that were offset by credits related to IPI excise tax. The accrual is necessary to offset the contingent gain resulting from the use of IPI excise tax credits. The IPI excise tax credits are similar to value added tax credits related to the purchase of goods used in the production process. Brazilian law prevents companies from recognizing IPI excise tax credits on the acquisition of certain goods. We believe that this prohibition is unconstitutional since it is not consistent with general value added tax principles and we are challenging this prohibition in the Brazilian courts. In May 2003, we sought and obtained a favorable preliminary order from a Brazilian court authorizing us to compensate federal tax liabilities with IPI excise tax credits under dispute. We are awaiting the decision of a Brazilian court of first instance. After such a decision is rendered, we expect the decision will be subject to several stages of appellate review before a final unappealable judgment is obtained. The IPI excise tax credit accrual recorded by us represents our statutory obligation to pay taxes that were offset with IPI excise tax credits.

We have noted that several other Brazilian companies have challenged the same prohibition and these companies have received both favorable and unfavorable judgments at different stages of the judicial process. Recently, for example, the Federal Supreme Court issued a final, unappealable and irrevocable decision on June 25, 2007 against another taxpayer in a similar legal proceeding, denying the use of these credits.

As of December 31, 2006, the IPI excise tax credit accrual representing the accumulated IPI tax credits used was US$441 million (US$303 million as of December 31, 2005), as updated at the SELIC interest rate. This provision affects the sales taxes line-item of our income statement, and a reversal of this provision would affect the sales taxes and the financial income (expense), net line-items of our income statement.

- IPI premium credit over exports

We have accrued a liability for certain tax liabilities that were offset by IPI premium tax credits. The accrual is necessary to offset the contingent gain resulting from the use of IPI premium tax credits and represents the statutory obligation to pay taxes that were offset by these credits. The IPI premium tax credits relate to export sales made during 1992 to 2002. Tax legislation allowed Brazilian companies to recognize IPI premium tax credits until 1983, when an act of the executive branch of the Brazilian government cancelled such benefits and prohibited companies from recognizing these credits. CSN is challenging the constitutionality of the executive branch s action since only a law enacted by the Brazilian legislature can cancel or repeal benefits duly enacted by prior legislation. In August 2003, CSN sought and obtained a favorable decision from a Brazilian court of first instance that authorized the use of IPI premium tax credits.

The Brazilian National Treasury appealed such decision and got a favorable decision from the court of appeals. We filed appeals against such decision, to both the Superior Court of Justice and the Federal Supreme Court and are still awaiting the decisions from such courts. In September 2006, the National Treasury filed five tax foreclosures against us to require payments in the total amount of approximately R$1 billion referring to the collection of taxes which were offset by the use of IPI premium tax credits. One of the tax foreclosures is secured by judicial liens of (i) cash deposits in the amount of R$685 million; and (ii) treasury stock, in an amount equivalent to R$504 million (market value). Additionally, in view of such judicial decision, the payment of part of the dividends approved in the Annual Shareholders Meeting of April 30, 2007, is temporarily suspended. We are still awaiting decision from the court of appeals on this matter. For more information, see Item 8A. Consolidated Statements and Other Financial Information Dividend Policy General and Item 13. Dividends, Dividend Arrearages and Delinquencies.

As of December 31, 2006, the IPI premium credit accrual represented the accumulated IPI tax credits used of US$676 million (US$350 million as of December 31, 2005), already updated by the SELIC Brazilian base

interest rate.

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This provision affects the sales taxes line-item of our income statement, and a reversal of this provision would affect the sales taxes and the financial income (expense), net line-items of our income statement.

We have noted that several other Brazilian companies have challenged the same prohibition. Recent decisions from lower courts indicated that companies may be entitled to utilize these credits. However, on June 27, 2007, the Superior Court of Justice issued a decision against one taxpayer, denying the use of these credits. This decision is subject to review by the Federal Supreme Court, the highest court in this case.

- Income tax and social contribution

We claim recognition of the financial and tax effects on the calculation of income tax and social contribution on net income, related to Consumer Price Index IPC understated inflation, which occurred in January and February 1989, by a percentage of 51.87% (Plano Verão). In 2004, the proceeding was concluded and judgment was made final and unappealable, granting us the right to apply the index of 42.72% (Jan/89), of which the 12.15% already applied should be deducted. The application of 10.14% (Feb/89) was granted. The proceeding is now under accounting inspection.

On December 31, 2006, we recorded US$153 million (US$155 million in 2005) as judicial deposit and a provision of US$10 million (US$26 million in 2005), which represents the portion not recognized by the courts.

In February 2003, we were charged by tax authorities related to the calculation of income tax and social contribution of previous years in view of the fact that had tax losses carryforward above the 30% limit of taxable income, as provided for by laws.

On August 21, 2003, a decision was rendered by the second panel of the Judgment Federal Revenue Office in Rio de Janeiro related to the decision which made said tax deficiency notice null and void and a new Tax Deficiency Notice was issued about same matter in November 2003. We challenged such new Tax Deficiency Notice, which was rejected in administrative lower courts. An administrative appeal was brought against such decision, which was accepted in administrative appellate court on April 26, 2006, so that said Tax Deficiency Notice had favorable decision to us, on an irrevocable basis, and respective decision was published in November 2006.

We filed a lawsuit challenging the assessment of Social Contribution on Income on export revenues, based on Constitutional Amendment #33/01 and in March 2004, we obtained an initial decision authorizing the exclusion of these revenues from said calculation basis, as well as the offsetting of amounts paid as from 2001. The lower court decision was favorable and the proceeding is waiting for trial of the appeal filed by the Federal Government in the Regional Federal Court. On December 31, 2006, the amount of suspended liability and the offset credits based on the referred proceedings was US$368 million (US$234 million in 2005), already adjusted by the Selic - Brazilian base interest.

- PIS/COFINS Law No. 9,718/98

PIS and COFINS taxes are assessed on revenues. In 1998, new tax legislation was enacted which required Brazilian companies to pay PIS and COFINS taxes on revenues generated by financial investments. Prior to 1998, the Brazilian constitution dictated that Brazilian companies were only required to pay PIS and COFINS taxes on revenues generated by operating activities. We are challenging the constitutionality of the assessment of PIS and COFINS taxes on revenues generated by financial investments since, in order to expand the PIS and COFINS tax computation basis, the Brazilian legislature was required to observe a constitutionally mandated waiting period prior to enacting the legislation. In addition, at the time the new tax legislation was enacted, the Brazilian constitution did not allow such taxes to be assessed on revenues generated by financial investments. In

February 1999, a lower court confirmed we sought and obtained a favorable preliminary order in March 2000. In April 2000, the Brazilian tax authorities appealed to Brazilian court of appeals. On March 6, 2006, Brazilian court of appeals

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issued a decision against us. On March 10, 2006, we appealed such decision to both the Superior Court of Justice and the Federal Supreme Court. Until the resolution of these appeals, our rights under the initial favorable decision are in effect. The PIS/COFINS accrual represents our statutory obligation to pay PIS/COFINS taxes due. We have noted that some Brazilian companies obtained favorable final and unappealable judgments in 2005 regarding similar PIS/COFINS legal challenges. Those companies have accordingly reversed some or most of their related disputed tax payment provisions. However, one company did not obtain a favorable decision and was required to pay the related tax obligation. We have a reasonable expectation of success in the final resolution of this matter, though a final and unappealable decision may not be delivered for many years, due to the nature of the Brazilian legal system. It is unlikely that a final and unappealable decision would be delivered within the following year.

As of December 31, 2006, this accrual amounted to US$149 million (US$125 million as of December 31, 2005), which represents the PIS and COFINS incremental taxes statutorily due, as updated at the SELIC interest rate. This provision affects the financial income (expense), net line item of our income statement, and a reversal of this provision would affect the financial income (expense), net line item of our income statement.

- CPMF Provisional contribution on financial activities tax

CPMF tax is assessed on cash transactions, including movements of cash between bank accounts. CPMF taxes were created by a constitutional amendment 21 enacted in 1999. We have challenged the legality of the constitutional amendment that created the CPMF tax and despite of the fact that we obtained a favorable decision from a Brazilian lower court in August 1999, an unfavorable final and unappealable decision was rendered by the appropriate Brazilian court of appeals in June 2006. Consequently, we paid US$113 million and recognized a gain of US$45 million due to the expiration (statute of limitations based on which the tax authorities must challenge the tax treatment of the matter) of the accrual recorded up to June 2001. This provision affected the financial expenses line-item of our income statement when recorded, this gain also affected the same line item.

2005 Compared to 2004

Operating Revenues

The performance of the global steel market in 2005 was determined by two main factors: high inventories, which had been building up since the second half of 2004, and weaker-than-normal demand.

Given less buoyant final demand and overstocked service centers, demand for flat steel suffered, triggering a slide in international prices during the first half of 2005. In an unprecedented reaction, steel companies decided to cut back production to align output with the new scenario, thereby avoiding a further price slump. Prices only began to recover at the end of the third quarter, when inventories had fallen back to normal levels and final demand was beginning to pick up again, particularly in the United States steel markets.

On the domestic front, annual flat-steel demand fell 9% over the year before, mainly due to dwindling demand from the distribution and civil construction industries, which fell by 20% and 9% respectively. Although demand from the auto and packaging industrial segments edged up by 3% and 1% respectively, this was insufficient to offset the decline in the other two sectors. On the other hand, Brazilian steel market prices increased in 2005, compared on an average basis to 2004. The domestic market improvement was chiefly due to the fact that prices in 2004 took some time to react to the international upturn, only doing so at the end of the third quarter. This low comparative base, together with relative domestic price stability throughout 2005, explains the increase.

Regarding our results, total sales volume increased 3.0% from 4.68 million tons in 2004 to 4.82 million in 2005. The decline of 423,000 tons in domestic sales, compared to 2004, was more than offset by the 562,000 tons

increase in export sales. Thus, in 2005 a greater proportion of sales was made into the export market (40% of total sales volume) than in 2004 (30%). This increase resulted from weaker than expected flat steel demand in Brazil, reflecting unimpressive overall growth in the economy, as discussed above.

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In contrast, steel prices, when measured in U.S. dollars, increased significantly. Domestic steel prices increased 38% on average, more than offsetting an 8% decline in export prices, with the result that average steel prices charged in 2005 were 20% higher than in 2004. Measured in *reais,* steel prices charged to domestic customers increased 15%, while steel prices charged to international customers decreased 23%. The net effect was that total average prices remained flat.

As a result of the combined effect of price and volume increases and exchange rate appreciation, we recorded operating revenue of US$4,673 million in 2005, 20% (or US$770 million) higher than previous year operating revenue of US$3,903 million. In the domestic market, operating revenues increased by 19% to US$3,449 million in 2005, from US$2,895 million in 2004, as higher local average prices and the strengthening of the *real* more than offset the decrease in volume. In the export market, operating revenues increased 21% to US$1,224 million in 2005, from US$1,008 million in 2004, with higher volumes more than compensating for the decline in prices.

Net Operating Revenues

Net operating revenues increased by 23% to US$3,805 in 2005, from US$3,084 million in 2004, mainly due to the 20% increase in operating revenues, whereas sales deductions experienced an increase of 6.0% . Sales deductions, as a percentage of operating revenues, were 21.0% in 2004 and 18.6% in 2005, because revenues derived from exports, which are exempted from value added taxes such as IPI and ICMS, as well as PIS and COFINS contributions, increased its share to 26.2% in 2005 from 25.8% in 2004.

Cost of Goods Sold and Production Costs

Cost of goods sold increased by 31% to US$1,837 million in 2005, from US$1,407 million in 2004, as a result of the higher sales volume, the strengthening of the *real* and changes in production costs which are further explained below. Measured in *reais,* the cost of goods sold increased only 9%.

Production costs totaled US$1,831 million in 2005, which means an increase of US$369 million, or 25%, over the 2004 result. Expressed in *reais,* this increase is only 3%. As parent company production costs are a *proxy* to the cost of goods sold, we can analyze the changes in cost of goods sold going through the variations occurred in the production cost.

The following table sets forth for the parent company the production costs, the production costs per ton of crude steel and the portion of production costs attributable to the primary components of our costs of production. With the exception of coal and some coke, which we import, and some metals (such as zinc, aluminum and tin), whose domestic prices are linked to international prices, our costs of production, as well as our other operating expenses, are mostly denominated in *reais.* The devaluation of the *real* causes U.S. dollar-denominated or -linked production costs to increase as a percentage of total production costs. Conversely, appreciation of the *real* causes *real* denominated production costs to increase as a percentage of total production costs.

	Year Ended December 31,								
	2003			**2004**			**2005**		
	US$ 000	**US$/ton**	**%**	**US$ 000**	**US$/ton**	**%**	**US$ 000**	**US$/ton**	**%**

Raw Materials									
Iron Ore	45,665	8.68	4.4	52,533	9.58	3.6	72,551	14.03	4.0
Coal	180,566	34.30	17.3	258,879	47.23	17.7	387,514	74.92	21.2
Coke	82,667	15.70	7.9	259,318	47.31	17.7	224,530	43.41	12.3
Metals	60,658	11.52	5.8	28,215	5.15	1.9	4,501	0.87	0.2
Outsourced Hot Coils	75,242	14.29	7.2	111,923	20.42	7.7	119,177	23.04	6.5
Other [1]	77,391	14.70	7.4	113,213	20.66	7.7	148,418	28.70	8.1
	522,188	99.20	49.9	824,081	150.35	56.4	956,690	184.97	52.3
Energy/Fuel	118,707	22.55	11.3	159,631	29.12	10.9	191,568	37.04	10.5
Labor	124,732	23.70	11.9	106,566	19.44	7.3	157,899	30.53	8.6
Services and Maintenance	115,389	21.92	11.0	166,993	30.47	11.4	256,965	49.68	14.0
Tools and Supplies	62,627	11.90	6.0	77,683	14.17	5.3	105,272	20.35	5.7
Depreciation	87,992	16.72	8.4	111,765	20.39	7.6	142,219	27.50	7.8
Others	14,374	2.73	1.4	15,674	2.86	1.1	20,313	3.93	1.1
	1,046,010	198.71	100.0	1,462,392	266.81	100.0	1,830,925	354.00	100.0

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As shown in the table above, all cost items showed an increase in 2005, with emphasis on raw materials, which increased by US$133 million, and services and maintenance, which increased by US$90 million. Under raw materials, the increases were a) US$20 million in iron ore cost, reflecting the approximately 70% price increase in 2005, b) US$129 million in coking coal, explained by the 50% price increase, c) US$7 million in metals (zinc, aluminum and tin) as a result of higher international prices for each of these materials, and d) US$35 million in other raw materials. On other hand, these increased costs were partially offset by reductions of e) US$35 million of purchased coke, due to both lower prices of coke and lower usage as we adapted our blast furnaces to use natural gas; and f) US$24 million of outsourced hot coils, given that we almost ceased to use hot coils from third parties in 2005.

Regarding the other items, there is a huge difference on variations measured in *reais* and U.S. dollars, because a large proportion of these costs are *reais*- denominated. Thus a) labor costs increased by 48% measured in U.S. dollars and 8% expressed in *reais,* reflecting the wage increases in May (see Selling, General and Administrative Expenses below), b) services and maintenance showed changes of 54% and 26%, measured in both currencies respectively, mainly due to more maintenance activities accomplished during the year, c) tools and supplies increased 36% and 12%, respectively, reflecting increases on several miscellaneous items, and finally d) depreciation showed a positive change of US$17 million.

Gross Profit

Gross profit increased by 17% to US$1,968 million in 2005, from US$1,677 million in 2004, due to an increase of US$721 million of net operating revenues which was only partially offset by an increase of US$430 million in cost of goods sold. Even though we had a higher gross profit in 2005 as compared to 2004, our gross margin decreased from 54.4% to 51.7% as the percentage increase in net operating revenues was smaller than the percentage increase in cost of goods sold.

Selling, General and Administrative Expenses

In 2005, we recorded selling, general and administrative expenses of US$294 million, an 11% increase over the US$265 million reported in 2004. Expressed in *reais,* these expenses showed an 8% decline.

Selling expenses increased by US$30 million, or 19%, due to appreciation of the *real* and the increase in export volumes and related freight costs. However, as a percentage of net operating revenues, it remained stable: 5.1% in 2004 and 4.9% in 2005. Additionally, when measured in *reais,* these expenses remained virtually flat, showing a slight decrease of 0.8% .

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General and administrative expenses remained stable in 2005 as compared to 2004, recording a 0.9% or US$1 million decrease. When expressed in *reais,* these expenses showed a decrease of 18%, despite wage increases reflecting annual negotiations under our collective bargaining agreement.

Other Income (Expenses)

Other expenses were US$28 million in 2005 as compared to US$50 million in 2004, a US$22 million decrease mainly due to a reversal of provisions, motivated by the revision of the likelihood of success in many judicial disputes made by our internal and external legal advisors, as well as due to recent favorable track record on related disputes, for labor and civil contingencies in the amount of US$61 million which had been accrued in 2004, partially offset by a US$13 million accrual of tax contingencies and US$10 million of environmental remediation costs in Santa Catarina. (See Note 18 to the Company s Financial Statements Commitments and Contingencies). While the decline in dollars was 44%, measured in reais, other income (expenses) declined by 53%.

Operating Income

Our operating income increased by US$284 million, or 21%, to US$1,646 million in 2005, from US$1,362 million in 2004. This increase was essentially related to the increase of US$291 million in gross profit, which was partially offset by the US$7 million higher selling, general and administrative expenses and other income (expenses).

Non - operating Expenses (Income), Net

In 2005, our non- operating expenses, net were stable as compared to 2004 with a decrease of US$1 million (or 0.3%) to US$364 million, from US$363 million in 2004.

The foreign exchange and monetary gain (loss), net line-item is mainly impacted by the variation in the value of the *real* against the U.S. dollar and its impact on our U.S. dollar denominated gross debt, on denominated cash, cash equivalents and short term investments, on equity investments in offshore subsidiaries and on trade accounts receivable. The US$30 million increase in foreign exchange and monetary gains in 2005 was mainly due to the further appreciation of the *real* (12% in 2005 versus 8% in 2004) and to our higher US dollar denominated gross debt, which increased to US$ 2,886 million from US$ 2,362 million. As a percentage of total debt, the debt denominated in foreign currencies was 88% in 2005 against 85% in 2004. The financial income (expenses), net line comprises following sub- items: a) derivatives; b) interest income; c) interest expense, and d) other financial income (expenses). In the following paragraphs, we provide detailed explanation on each of them.

We use currency derivatives instruments to offset the impact of foreign exchange variation on the foreign exchange and monetary gain (loss), net accounting line. The net result of currency derivative transactions was an expense of US$296 million in 2005, a marginally poorer result (US$5 million) compared to the expenses of US$291 million in 2004. Our equity swap transactions yielded US$51 million in 2005 and US$57 million in 2004. Therefore, the total loss on derivatives was US$245 million in 2005 and US$234 million in 2005. Our equity swap transactions mainly are intended to enhance the return of our financial assets by adding exposure to equity securities that historically yield higher long-term returns than fixed- income assets.

We reported interest income of US$153 million in 2005, versus US$78 million in 2004, mainly due to higher cash, cash equivalents and short-term investments, from US$1,113 million in 2004 to US$1,582 million in 2005, and higher short-term interest rates in the United States.

We had interest expenses of US$407 million in 2005, compared to US$280 million in 2004, as a result of the increase in our gross debt from US$2,844 million in 2004 to US$3,365 million in 2005. As most of our foreign

(non-Brazilian *real* denominated) debt carries fixed interest rates, interest rate increases generally do not impact our interest expenses.

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Other financial income (expenses) improved by US$51 million to expense of US$27 million in 2005 versus expenses of US$74 million in 2004, mainly due to approximately US$30 million of financial expenses incurred during GalvaSud s acquisition in 2004, related to the repayment of its debt, including breakup costs, and higher financial income related to interest on accounts receivable and other minor income items in the amount of US$37 million in 2005 as compared to US$30 million in 2004.

Income Taxes

We recorded a provision for income tax and social contribution of US$427 million in 2005, compared to US$291 million in 2004. The difference is due to higher income before taxes and equity in results of affiliated companies in 2005 (US$1,282 million against US$999 million in 2004). Expressed as a percentage of pre- tax income, the income tax expense increased to 33.3% in 2005, from 29.1% in 2004.

Income tax expense in Brazil refers to the collection of two taxes, federal income tax and social contribution (which is an additional income tax). The statutory rates for these taxes applicable for 2004 and 2005 were 25% for federal income tax and 9% for the social contribution. Therefore, the balance owed according to the statute for these years amounts to US$340 million in 2004 and US$455 million in 2005 (34% of income before taxes and equity in affiliated companies). Adjustments are made to these rates, in order to arrive at the actual tax expense for the years.

In 2004, these adjustments totaled US$49 million and comprised:

- a US$31 million benefit from interest on stockholders equity, a deductible expense for tax purposes;
- a US$61 million benefit due to non-taxable income from operations outside Brazil;
- certain permanent differences amounting to US$43 million which partially offset the benefits mentioned above. This amount refers principally to the foreign exchange loss on the net equity of our subsidiaries offshore and to minor expenses such as fines, gifts and donations as these are non-deductible expenses.

In 2005, adjustments totaled an additional benefit of US$9 million, mainly due to:

- a US$38 million benefit from interest on stockholders equity, a deductible expense for tax purposes; and
- other permanent differences that represented tax expenses of US$29 million. Foreign exchange loss on the net equity of our offshore subsidiaries represented a significant permanent item this period due to the appreciation of the Brazilian real against the U.S. dollar, which was recorded in the results of operations for Brazilian GAAP purposes and represented a non-taxable item. Also, certain expenses such as fines, gifts and donations are included within these permanent differences.

Our taxable income, generated from our operations in Brazil and abroad, is comprised of the following:

	Year Ended December 31, 2006		
	2004	**2005**	**Changes**
	(In million of U.S. dollars)		

Taxable income in Brazil	999	1,231	232
Foreign taxable income	-	51	51

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Our taxable income in Brazil was impacted by lesser compensation of tax loss carryforwards in 2005 of approximately US$190 million, by an increase of US$140 million in non- deductible expenses and by the effect of the appreciation of the *real* against U.S. dollar of approximately US$150 million.

In December 2004, we transferred part of our foreign operations to Luxembourg and, as from that date those results became taxable in that country due to an agreement between Brazil and Luxembourg to avoid double taxation. Accordingly, the results generated in 2004 until the date of the transfer of our foreign operations were exempt from taxation in Luxembourg in conformity with the tax legislation of that country. In 2005 those foreign operations were fully taxable and amounted to US$51 million.

In 2005, we utilized US$33 million of income tax credits (or 2% of the income before taxes), compared to US$131 million for 2004 (13%).

It is impossible to predict the adjustments to the federal income tax and social contribution at statutory rates, as they depend on interest on stockholder s equity, non-taxable factors including income from offshore operations, and tax losses from offshore operations, especially when expressed as a percentage of income. Therefore, management cannot foresee the effective income tax rate in future periods.

Accruals for Disputed Taxes Payable

A brief description of the major recent developments regarding our accruals for disputed taxes payable follows:

IPI Excise Tax Credit Accrual

The US$72 million increase in the IPI excise tax credit accrual (from US$231 million in 2004 to US$303 million in 2005) is due to the effects of the appreciation of the Brazilian real against the U.S. dollar in the amount of US$31 million and the effects of the update at the SELIC interest rate in the amount of US$41 million. This provision affects the sales taxes line-item of our income statement, and a reversal of this provision would affect the sales taxes and the financial income (expense), net line-items of our income statement.

IPI Premium Tax Credit Accrual

In 2005, the Company compensated federal taxes due with the IPI premium credit resulting in an increase of US$313 million; accordingly, as of December 31, 2005, the IPI premium credit accrual representing the accumulated IPI tax credits used increased to US$350 million (US$37 million as of December 31, 2004), as updated at the SELIC interest rate. This provision affects the sales taxes line-item of our income statement, and a reversal of this provision would affect the sales taxes and the financial income (expense), net line-items of our income statement.

PIS/COFINS Accrual

The US$27 million increase in the PIS/COFINS accrual (from US$98 million in 2004 to US$125 million in 2005) is mainly due to the effects of the SELIC interest rate and the appreciation of the Brazilian real against the U.S. dollar. This provision, as well as a reversal of this provision, would affect the financial income (expense), net line item of our income statement.

Income Tax and Social Contribution (Plano Verão) Accrual

The US$3 million increase in the income tax and social contribution ("Plano Verão") accrual (from US$23 million in 2004 to US$26 million in 2005) is mainly due to the appreciation of the Brazilian real against the U.S. dollar (this provision is not updated by the SELIC interest rate). This provision affects the income tax expense line-item of our income statement, and a reversal of this provision would affect the income tax benefit and the financial income (expense), net line-items of our income statement.

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Income Tax and Social Contribution (Tax Loss Carryforwards) Accrual

The US$32 million increase in the income tax and social contribution (tax loss carryforwards) accrual (from US$144 million in 2004 to US$176 million in 2005) refers mainly to the appreciation of the Brazilian reais against the U.S. dollar and to the effects of the SELIC interest rate. This provision affects the income tax expense line-item of our income statement, and a reversal of this provision would affect the income tax benefit and the financial income (expense), net line-items of our income statement.

Social Contribution Tax on Export Revenues Accrual

The US$119 million increase in the social contribution accrual (from US$115 million in 2004 to US$234 million in 2005) is related to the social contribution tax due on our income from export revenues and to the effects of the SELIC interest rate and the appreciation of the Brazilian real against the U.S. dollar. This provision affects the income tax expense line-item of our income statement, and a reversal of this provision would affect the income tax benefit and the financial income (expense), net line-items of our income statement.

CPMF Accrual

The US$53 million increase in the CPMF accrual (from US$105 million in 2004 to US$158 million in 2005) is mainly due to the effects of the SELIC interest rate and the appreciation of the Brazilian real against the US dollar. This provision, as well as a reversal of this provision, would affect the financial income (expense), net line item of our income statement.

Equity in Results of Affiliated Companies

Equity results of affiliated companies were US$47 million in 2005, compared to US$51 million in 2004. MRS improved its performance, yielding US$61 million in 2005 as compared to US$46 million in 2004. This MRS s result was totally offset by deterioration of Lusosider s results, moving from a gain of US$1 million in 2004 to a US$10 million loss in 2005, by CFN s activities which in 2004 resulted in a US$10 million loss and in 2005 this loss worsened to US$12 million and by Ita s results, which recorded a US$8 million gain in 2005, less than the US$14 million gain reached in 2004.

5B. Liquidity and Capital Resources

Overview

Our main uses of funds are for capital expenditures, repayment of debt and dividend payments. We have historically met these requirements by using cash generated from operating activities and through the issuance of short-and long-term debt instruments. We expect to meet our cash needs for 2007 primarily through a combination of operating cash flow, cash and cash equivalents on hand and newly issued long-term debt instruments.

In addition, from time to time, we review acquisition and investment opportunities and will, if a suitable opportunity arises, make selected acquisitions and investments to implement our business strategy. We generally make investments directly or through subsidiaries, joint ventures or affiliated companies, and fund these investments through internally generated funds, the issuance of debt, or a combination of such methods.

Sources of Funds and Working Capital

Cash Flows

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Cash and cash equivalents as of the end of 2004, 2005 and 2006 totaled US$970 million, US$1,241 million, and US$959 million, respectively.

Cash Generated by Operating Activities

We generated cash from our operations in the total amount of US$354 million, US$1,757 million , and US$919 million in 2004, 2005 and 2006, respectively, providing us with a significant source of liquidity. The 47.7% or US$838 million decrease in cash flow from operating activities in 2006 compared to 2005 was mainly due to: (i) a US$326 million increase in inventories in 2006; (ii) the balance still to be collected from insurance companies of US$ 209 million on the accident of an equipment adjacent to Blast Furnace No. 3.

The 396%, or US$1,403 million increase in cash flow from operating activities in 2005 compared to 2004 was mainly due to an unrealized loss on derivatives of US$272 million in 2005 and to the US$493 million increase in inventory in 2004 and the subsequent decrease in inventory of US$177 million that took place in 2005.

Cash Used in Investing Activities

We used cash in our investing activities in the total amount of US$365 million, US$593 million and US$839 million in 2004, 2005 and 2006, respectively, mainly for capital expenditures and long-term investments in downstream opportunities (including acquisitions), new products and market niches, and infrastructure investments. For further information, see Item 4A. History and Development of the Company Acquisitions.

Cash Generated by Financing Activities

We generated cash from financing activities in the total amount of US$380 million, US$996 million and US$263 million in 2004, 2005 and 2006. The US$733 million decrease in cash from financing activities in 2006 compared to 2005 was mainly driven by (i) a significantly lower distribution of dividends and interest on stockholders equity of US$833 million in 2006 as compared to US$961 million in 2005, (ii) lower share buyback of US$17 million in 2006 as opposed to US$365 million in 2005, and (iii) new debt issuances and bilateral loans totaling US$2,082 million in 2006 against US$1,200 million in 2005.

Trade Accounts Receivable Turnover Ratio

Our receivable turnover ratio (the ratio between trade accounts receivable and net operating revenues), expressed in days of sales increased from 45 on December 31, 2005, to 52 on December 31, 2006, reflecting higher prices charged to our customers in 2005 and 2006 and its impact on the monetary value on accounts receivable, that has not ocurred in 2004.

Inventory Turnover Ratio

Our inventory turnover ratio (obtained by dividing inventories by annualized cost of goods sold), expressed in days of cost of goods sold, remained stable at 145 on December 31, 2005 and 149 in 2006. This variation is mainly reflected by increasing inventories cost, as a consequence of the accident in Blast Furnace No. 3.

Trade Accounts Payable Turnover Ratio

The accounts payable turnover ratio (obtained by dividing trade accounts payable by annualized cost of goods sold), expressed in days of cost of goods sold, increased to 73 on December 31, 2006 from 67 on December 31, 2005 as a consequence of CSN s financing of slab purchases, which were bought to supply the Company s

finishing lines due to the stoppage at Blast Furnace No. 3.

Short-Term Debt and Short-Term Investments

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Given the capital intensive and cyclical nature of our industrial segment, and the generally volatile economic environment in certain relevant emerging markets, we have retained a substantial amount of cash on hand to run our operations, to satisfy our financial obligations, and to be prepared for potential investment opportunities. As of December 31, 2006, cash and cash equivalent instruments equaled US$959 million.

We were also taking advantage of the then current liquidity conditions to extend the maturity profile of gross debt. Such activities are unrelated to the management of any interest rate, inflation and/or foreign exchange risk exposure. Given the lack of a liquid secondary market for our short term debt instruments, we have accumulated cash instead of prepaying our debt prior to final maturity. As of December 31, 2006, short-term and long-term indebtedness accounted for 11% and 89%, respectively, of our total debt, and the average life of our existing debt was equivalent to 11,75 years, considering 40 years-term for the perpetual bonds issued in July 2005.

In 2006, we had capital expenditures of US$706 million, primarily consisting of US$82 million for projects relating to the Itaguaí Port expansion, US$116 million for Casa de Pedra mine expansion and US$185 million for maintenance.

In 2007, we plan to make capital expenditures of approximately US$1,235 million, compared to US$706 million in 2006, US$290 million in 2005 and US$178 million in 2004.

We expect to meet our liquidity requirements from cash generated from operations, and, if needed, the issuance of debt securities.

Company Debt and Derivative Instruments

At December 31, 2005 and 2006, total debt (composed of current portion of long-term debt, accrued finance charges, negative mark-to-market adjustments on derivative instruments, and long-term debt and debentures) aggregated US$3,517 million and US$4,160 million, respectively, equal to 349% and 397% of the stockholders equity at December 31, 2005 and 2006, respectively. At December 31, 2006, our short-term debt (composed of current portion of long-term debt, negative mark-to-market adjustments on derivative instruments and accrued finance charges) totaled US$457 million and our long-term debt (composed of long-term debt and debentures) totaled US$3,703 million. The foregoing amounts do not include debt of others for which we are contingently liable. See "Item 5E. Off-Balance Sheet Arrangements."

At December 31, 2006, approximately 11% of our debt was denominated in *reais* and substantially all of the remaining balance was denominated in U.S. dollars. Our current policy is to protect ourselves against foreign exchange losses on our foreign currency-denominated debt and currently approximately 100% of our exposure are protected through foreign exchange derivative products, U.S. dollar-denominated fixed income investments and equity investments in offshore subsidiaries. We continue to review our foreign exchange exposure policy and there are no assurances that we will maintain our current level of protection against such exposure. For a description of our derivative instruments, see Note 22 to our consolidated financial statements contained in "Item 18. Financial Statements". Also see "Non-operating Expenses (Income), Net "under" Item 5A. Operating Results Results of Operations 2006 Compared to 2005 and 2005 Compared to 2004".

The major components of US$457 million of consolidated short-term loans and financing outstanding at December 31, 2006 were (amounts are reflected in current portion of long-term debt):

- US$114 million of trade-related transactions;

- US$79 million of Euronotes;
- US$101 million of negative marked-to-market value on foreign exchange or derivative instruments; and
- US$86 million of accrued interest.

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The major components of US$3,703 million of consolidated long-term loans and financing outstanding at December 31, 2006 were (amounts are reflected in long-term debt):

- US$420 million in local debentures;
- US$638 million of export pre-payments (of which US$461 million is part of our export receivables securitization program);
- US$300 million of revolving credit facilities;
- US$1,225 million of Eurodollar notes;
- US$140 million of trade-related transactions; and
- US$750 million in perpetual bonds.

The debentures are *real*-denominated debt instruments that were issued in December 2003 and April 2006, being one issuance of US$85.5 million five- year debentures, indexed to the *Índice Geral de Preços e Mercado* IGPM, a Brazilian price index, and bearing interest at 10% per annum coupon and another issuance of US$281 million six-year debentures bearing interest of 103.6% of CDI Brazilian Interbank Reference interest Rate.

Eurodollar and Euro notes issued in accordance with Rule 144A and Regulation S under the Securities Act reflect senior unsecured debt instruments issued by the parent company and its offshore subsidiaries over a period of time, including the issuance in 2005 of US$750 million, 9,5% per annum coupon perpetual notes. They also include (1) the US$275 million notes, 10,75% per annum coupon, issued in September and December 2003 with final maturity in 2008; (2) the US$550 million notes, 9,75% per annum coupon, issued in December 2003 and January 2004 with final maturity in 2013; and (3) the US$400 million notes, 10% per annum coupon, issued in September 2004 and January 2005 with final maturity in 2015.

Pre- export agreements include the four series of the export receivables securitization program launched in June 2003 as well as other trade- related transactions outside of the program. The first series, issued in June 2003 in the amount of US$142 million, has a seven-year maturity and bears interest at 7.28% per annum, with a two- years grace period for payment of principal. The second series, issued in August 2003 in the amount of US$125 million, has a three-year maturity and bears interest at Libor plus 1.55% per annum. The third series, issued in June 2004 in the amount of US$162 million, has an eight-year maturity and bears interest at 7.427% per annum with a three-year grace period. In May 2005, a fourth series was issued in the amount of US$250 million having a 10- year maturity and bearing interest at 6.148% per annum with a three- year grace period. A portion of the proceeds of the fourth series was used to repay the second series.

Maturity Profile

The following table sets forth the maturity profile of our long-term debt at December 31, 2006:

Maturity in	**Principal Amount**
	(In millions of US$)
2008	958
2009	144
2010	135

2011	239
2012 and thereafter	1,477
Perpetual securities	750
Total	3,703

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The foregoing amounts do not include debt of others which we have guaranteed. See "Item 5E. Off-Balance Sheet Arrangements".

5C. Research and Development, Patents and Licenses, etc.

Our research and development center works closely with customers. One of the features of this unit is the resident engineer concept, where key customers receive our engineers to help them make better use of our steel products. This unit works closely with the commercial sector, focusing on product improvements and developments that will meet our customers needs.

Another feature are the work shops focusing on products applications and simultaneous engineering for parameters adjustment of the CSN steel products and the customers final goods on the segments of white goods, packaging, automotive and civil construction.

Our investment for research and development projects and activities in 2004, 2005 and 2006 totaled US$8 million, US$10.1 million and US$20.9 million, respectively. New products developed under our research and development program include: Special Steel Grades for Tin Plate products for two pieces cans, Special Tin Plate for 3 pieces Shaped Expanded Cans, Pre-coated Steel for Civil Construction and White Goods, Electrical Steel as cold-rolled used for electric motors, High-Strength Low-Alloy hot-rolled steels used for pipes, structures, agricultural appliances, gas containers and automobile wheels, Special Bake Hardned Galvanized Steels used for automobiles, Galvalume for construction and home appliances and others.

5D. Trend Information

Other than discussed below, there are no recent significant developments that were not fully reflected in our results of operations for the twelve- month period ended December 31, 2006 or in our financial position as of December 31, 2006 and that could impact our future results of operations and financial position. No significant and unexpected changes in the currency rate, in interest rates and/or in inflation rates have occurred.

On November 10, 2006, Tata Steel UK Limited (Tata) posted an offer through the Panel of Takeovers and Mergers to Corus Group PLC (Corus) shareholders, to be implemented by way of a scheme of arrangement. On December 10, Tata announced a revision of its offer. Both Tata and CSN made offers, with Tata being the winner at the auction. Although CSN did not win the auction for Corus, CSN sold its stake of 34,072,613 shares of Corus for the reviewed final price offered by Tata of 608 pence for each common share of Corus, corresponding to a non-operating gain of US$89 million. This amount, net of taxes and expenses, was US$65 million, recorded in the first quarter of 2007.

In addition, as set forth in the agreement for implementation entered into between CSN Acquisitions and Corus on December 10, 2006, CSN Acquisitions received from Corus the Incentive Remuneration corresponding to 1% of the reviewed final price proposed by CSN Acquisitions for the acquisition of the Company of 603 pence for each common share of Corus in amount of US$115 million.

5E. Off- Balance Sheet Arrangements

In addition to the debt that is reflected on our balance sheet, we are contingently liable for the off-balance lease payments related to activities of MRS, CFN and TECON. The following table summarizes all of the off-balance sheet obligations for which we are contingently liable and which are not reflected under liabilities in our consolidated financial statements:

CONTINGENT LIABILITY WITH RESPECT TO NON- CONSOLIDATED ENTITIES AS OF DECEMBER 31, 2006

	Aggregate Amount	Maturity
	(In millions of US$)	
Guarantees of Debt:		
CFN	87.6	2007-2020
Contingent Liability for Concession Payments:[1]		
MRS	1,571	2026
CFN	14.9	2026
TOTAL	1,585.9	

(1) Other consortia members are also jointly and several liable for these payments.

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CFN

We guarantee, together with Taquari Participações S.A., the loans BNDES has granted to CFN in May and December 2005 and in January 2006, all of which mature by November 2020, adjusted based on TJLP plus 1.5% per annum. The total outstanding amount of the debt as of December 31, 2006 was US$87.6 million.

MRS s Concession Obligations

We assigned as negligible the likelihood of being responsible for the concession obligations of MRS because (1) MRS currently transports approximately 108 million tons of products (mainly steel, iron ore, coal and coke), and the average annual growth rate of the cargo transported by MRS over the last five years was approximately 10%, (2) MRS is expected to continue to report operating revenues, EBITDA and EBITDA margin above approximately US$500, US$200 million and 40%, respectively, in the following years, and (3) MRS will benefit from recently announced mining projects which are expected to support a further 10% annual increase of cargo transported over the next five years.

In addition to the very positive business outlook, MRS has a tariff model which aids its financial sustainability by determining ideal tariffs to be charged for its transportation services of captive cargo (which is cargo that cannot be transported in any way other than through MRS s rail). This tariff model provides that costs incurred by MRS with respect to captive cargo, including operational, fixed and variable costs, costs of remunerating MRS s own and third-party capital, concession costs, and leasing and investment costs aimed at maintaining the productive capacity of leased assets, are duly covered by the calculated tariffs. Clients that transport captive cargo account for roughly 69% of MRS s overall volume.

This tariff model also aids MRS s financial sustainability by defending MRS s margin as costs rise. Tariffs are fixed annually for clients that transport captive cargo based on MRS s budget for the relevant year. Tariffs are fixed for clients that transport cargo that is not captive through negotiated agreements with MRS.

5F. Tabular Disclosure of Contractual Obligations

The following table represents our long-term contractual obligations as of December 31, 2006:

		Payment due by period			
		(In millions of US$)			
Contractual obligations	**Total**	**Less than 1 year**	**1-3 years**	**3-5 years**	**More than 5 years**
Long-term accrued finance charges[1]	1,618	338	564	378	338
Pension plan	668	57	120	128	363
Long-term debt	3,703	-	1,102	374	2,227
Purchases:	2,261	1,270	193	157	641
Raw materials[2]	1,399	1,053	63	126	157
Maintenance[3]	39	39	-	-	-
Utilities/Fuel[4]	1,200	209	193	157	641

Total	8,627	1,696	2,177	1,403	3,351

(1) These accrued finance charges refer to the cash outflow related to the contractual interest expense of our long-term debt and were calculated using the contractual interest rates taken forward to the maturity dates of each contract.

(2) Refer mainly to purchases of coal, tin, aluminum and zinc, which comprise part of the raw materials for steel manufacturing and take-or-pay contracts. The use of these raw materials has a fast turnover and, consequently, the purchases fall within short-term obligations.

(3) We have outstanding contracts with several contractors in order to maintain our plants in good operation conditions; due to the strong demand for specialized maintenance service, the term of some contracts is for more than one year.

(4) Refer mainly to natural gas, power supply and cryogenics, which are provided by limited suppliers; with some of these suppliers we maintain long-term contracts.

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Item 6. Directors, Senior Management and Employees

6A. Directors and Senior Management

We are managed by our Board of Directors (*Conselho de Administração*), which consists of seven to eleven members, and our Board of Executive Officers (*Diretoria Executiva*), which consists of two to nine Executive Officers with no specific designation (one of which is the Chief Executive Officer). In accordance with our *Estatuto Social* (bylaws, each Director is elected for a term of one year by our stockholders at a stockholders meeting. Our Bylaws require our employees to be represented by one Director on the Board of Directors. The members of the Board of Executive Officers are appointed by the Board of Directors for a two-year term.

Our Board of Directors is responsible for the formulation of business plans and policies and our Board of Executive Officers is responsible for the implementation of specific operating decisions. As of December 31, 2006, our Board of Directors was comprised of one Chairman, one Vice Chairman and six members, and our Board of Executive Officers was comprised of our Chief Executive Officer, our Chief Financial Officer and six Executive Officers.

Our Directors and Executive Officers are as follows.

Name	**Position**
Board of Directors	
Benjamin Steinbruch	Chairman
Jacks Rabinovich	Vice Chairman
Mauro Molchansky	Member
Fernando Perrone	Member
Dionísio Dias Carneiro Netto	Member
Antonio Francisco dos Santos	Member
Darc Antonio da Luz Costa	Member
Yoshiaki Nakano	Member
Board of Executive Officers	
Benjamin Steinbruch	Chief Executive Officer
Otávio de Garcia Lazcano	Chief Financial Officer
Enéas Garcia Diniz	Executive Officer
Marcos Marinho Lutz [(1)]	Executive Officer
Pedro Felipe Borges Neto	Executive Officer
Isaac Popoutchi	Executive Officer
Juliano de Oliveira	Executive Officer
Juarez Saliba de Avelar	Executive Officer

(1) As of February 1, 2007, Mr. Lutz is no longer a member of our Board of Executive Officers.

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Board of Directors

Benjamin Steinbruch. Mr. Steinbruch was born on June 28, 1953 and has been Chairman of our Board of Directors since April 28, 1995 and Chief Executive Officer since April 30, 2002. Mr. Steinbruch is also Superintendent Officer of Vicunha Siderurgia, our controlling shareholder.

Jacks Rabinovich. Mr. Rabinovich was born on September 20, 1929 and has been a member of our Board of Directors since April 23, 1993 and Vice Chairman since April 24, 2001. He is also Chief Executive Officer of Vicunha Siderurgia.

Mauro Molchansky. Mr. Molchansky was born on September 11, 1950 and has been a member of our Board of Directors since April 24, 2001. He was Executive Officer of *Globo Comunicações e Participações S.A.* Globopar from August 1994 to March 2002. Before joining *Globo Comunicações e Participações S.A.* - Globopar in 1994, he was Financial Officer and Investor Relations Officer of *Aracruz Celulose S.A*. Under Mr. Molchansky s leadership, Aracruz Celulose S.A. was the first Brazilian company to issue American Depositary Shares (level 3) listed and traded on the NYSE, in 1992.

Fernando Perrone. Mr. Perrone was born on May 6, 1947 and elected a member of our Board of Directors on September 26, 2002. He was our Infrastructure and Energy Executive Officer from July 10, 2002 to October 2, 2002. Previously, Mr. Perrone occupied the position of Chief Executive Officer of *Empresa Brasileira de Infra-Estrutura Aeroportuária* INFRAERO and was an officer of BNDES.

Dionísio Dias Carneiro Netto. Mr. Carneiro Netto was born on September 23, 1945 and elected a member of our Board of Directors on April 30, 2002. He is a professor at Pontifícia Universidade Católica do Rio de Janeiro.

Antonio Francisco dos Santos. Mr. Santos was born on December 6, 1950 and has been a member of our Board of Directors since November 25, 1997. Since 1972, Mr. Santos has served internally in various positions of responsibility, including Coordinator of Industrial Engineering, Chief of Industrial Engineering and Chief of Production Planning. He is currently Chairman and Chief Executive Officer of the Board of the *Clube de Investimento CSN* (" CSN Employee Investment Club") and a member of the Board of Directors of *Caixa Beneficente dos Empregados* of CSN, or CBS, our pension plan.

Darc Antonio da Luz Costa. Mr. Costa was born on March 22, 1948 and has been a member of our Board of Directors since April 29, 2004. Since 1975, Mr. Costa has worked for the *Banco Nacional de Desenvolvimento Econômico e Social* BNDES. He was Vice-President of BNDES until November 2004.

Yoshiaki Nakano. Mr. Nakano was born on August 30, 1944 and has been a member of our Board of Directors since April 29, 2004. From 1995 to 2001 Mr. Nakano was Treasury Secretary of the State of São Paulo. Since 2001, he has been Chief of the Economics Department at *Fundação Getúlio Vargas* FGV/SP.

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Board of Executive Officers

In addition to Mr. Steinbruch, the following persons are members of our Board of Executive Officers as of December 31, 2006:

Otávio de Garcia Lazcano. Mr. Lazcano was born on June 9, 1969 and elected Chief Financial Officer on August 8, 2006. He has been serving the company since 1996, acting as Financial Manager and Financial Officer. Mr. Lazcano previously served as Financial Analyst of *Aracruz Celulose*.

Marcos Marinho Lutz. Mr. Lutz was born on December 30, 1969 and originally elected Executive Officer in charge of Infrastructure & Energy in June 24, 2003. Prior to joining CSN, Mr. Lutz served as Superintendent Officer at *Ultracargo S.A.*, a logistics arm of *Grupo Ultra*. As of February 1, 2007, Mr. Lutz is no longer a member of our Board of Executive Officers.

Enéas Garcia Diniz. Mr. Diniz was born on January 1, 1960 and originally elected Executive Officer in charge of Production in June 21, 2005. He has been serving the company since 1985, acting as General Manager of Hot Rolling, General Manager of Maintenance, Metallurgy Director and General Director of the Presidente Vargas steelworks.

Pedro Felipe Borges Neto. Mr. Borges Neto was born on September 27, 1951, and originally elected Executive Officer in charge of institutional matters on September 20, 2005. Prior to joining CSN, Mr. Borges Neto served as Superintendent Officer, Vice-President and Chief Executive Officer at *Vicunha Têxtil*. He is currently a member of the Board of Directors of Companhia Gás do Ceará and of Companhia Ferroviária do Nordeste- CFN.

Isaac Popoutchi. Mr. Popoutchi was born on August 21, 1949, and elected Executive Officer in March 27, 2006. Prior to joining CSN, Mr. Popoutchi served as Chief Executive Officer *of Coimex Trading*, of *Rede Ferroviária Federal* and of *CBTU Companhia Brasileira de Trens Urbanos*.

Juliano de Oliveira. Mr. Oliveira was born on January 28, 1955, and elected Executive Officer in March 27, 2006. Prior to joining CSN, Mr. Oliveira served as Chief Executive Officer of *Loma Negra Cimentos C.I.A.S.A.*, in Argentina, Superintendent Officer of *Camargo Corrêa Cimentos S.A.*, officer of the business unit of *Aços Villares S.A.* from Villares/Sidenor group.

Juarez Saliba de Avelar. Mr. Avelar was born on February 13, 1961 and elected Executive Officer in charge of mineral resources on September 26, 2006. He has been working with us since 2003, acting as Port and Railroads Officer and Mineral Resources Officer. Mr. Avelar served as President of *FERTECO Mineração* and as Officer of south and north unit of *Companhia Vale do Rio Doce.*

There are no family relationships between any of the persons named above. The address for all of our directors and executive officers is Av. Brigadeiro Faria Lima, 3400, 20° Andar, Itaim Bibi, São Paulo, São Paulo State, Brasil (telephone number 55-11-3049-7591).

Indemnification of Officers and Directors

There is no provision for or prohibition against the indemnification of officers and directors in Brazilian law or in our Bylaws. Officers are generally not individually liable for acts within the course of their duties. We either indemnify, or maintain directors and officers liability insurance insuring our Directors, our Chief Executive Officer, our Chief Financial Officer and our other Executive Officers and certain key employees against liabilities incurred in connection with their positions with us.

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6B.Compensation

For the year ended December 31, 2006, the aggregate compensation paid by the company to all members of our Board of Directors and the members of our Board of Executive Officers for services in all capacities was approximately US$7.1 million. In addition, the members of the Board of Directors and of the Board of Executive Officers may receive certain additional company benefits generally provided to company employees and their families, such as medical assistance and life insurance among others.

6C. Board Practices

Fiscal Committee and Audit Committee

Under Brazilian Corporate Law, shareholders may request the appointment of a *Conselho Fiscal* (a "Fiscal Committee"), which is a corporate body independent of management and our external auditors. The primary responsibility of the Fiscal Committee is to review management s activities and the financial statements, and report its findings to the shareholders. The shareholders did not request the installation of a Fiscal Committee at the General Shareholders Meeting held on April 30, 2007.

In June 2005 a *Comitê de Auditoria* (an "Audit Committee") was appointed in compliance with SEC s rules, which is composed of three independent members of our Board of Directors.

The Audit Committee is responsible for recommending to the Board of Directors the appointment of the independent auditors; reporting on our auditing policies and our annual auditing plan prepared by our internal auditing team, as well as monitoring and evaluating the activities of the external auditors and identifying, prioritizing and submitting actions to be implemented by the executive officers; and analyzing the annual report, and our financial statements and making recommendations to the Board of Directors.

The Audit Committee is currently composed of Messrs. Carneiro Netto, Nakano and Perrone. Since the creation of the Audit Committee, it is assisted by a consultant, who renders financial consultant services to the members of the Committee.

For information on the date of election and term of office of the members of our Board of Directors and Board of Executive Officers, see Item 6A. Directors and Senior Management.

Service Contracts

We do not have any agreements with our directors providing for benefits upon termination of employment.

6D. Employees

As of December 31, 2004, 2005 and 2006, we had 10,207, 12,936 and 13,659 employees. As of December 31, 2006 approximately 3,204 of our employees were members of the steelworkers union of Volta Redonda and region, which is affiliated with the *Central Única dos Trabalhadores*, or *CUT*, a national union. We believe we have a good relationship with CUT. We have collective bargaining agreements, renewable annually each May 1.

We are the principal sponsor of CBS, our employee pension plan. As a result of a general pay increase that we granted at the time of our privatization and a decline in the value of CBS s assets, CBS had substantial unfunded projected benefit obligations. Our unfunded pension benefit obligations totaled US$254 million as of December 31, 2006. The amount of the unfunded pension benefit obligations is affected by, among other things, fluctuations in the

value of CBS s assets, which totaled US$859 million as of December 31, 2006, 43% of which was attributed to our common shares held by CBS. See Note 16 to our consolidated financial statements contained in Item 18. Financial Statements.

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In March 1997, we established an employee profit sharing plan. All employees participate in the plan, and earn bonuses based on our reaching certain goals for each year, including a minimum EBITDA margin as well as goals based on measures including sales, cost control, productivity and inventory levels, appropriate to the nature of the different sectors.

In June 2000, we increased the average workshift at our Volta Redonda steel works from six to eight hours. This increase was implemented in our iron ore, limestone and dolomite mines during 1999. We have signed a collective bargaining agreement with our employees unions pursuant to which we have agreed not to dismiss employees in connection with this workshift increase. This eight- hour workshift improved productivity, quality and job safety as a result of fewer interruptions in the production process, which is continuous.

6E. Share Ownership

Besides the common shares issued by us that Mr. Steinbruch owns as a result of his ownership interest in Vicunha Siderurgia, our controlling shareholder, as of May 31, 2007 he directly held 255,216 of our common shares (0.09% of the outstanding common shares). Other executive officers and members of our Board of Directors held an aggregate of less than 0.001% of our outstanding common shares as of May 31, 2007.

Item 7. Major Shareholders and Related Party Transactions

7A. Major Shareholders

The following table sets forth, as of May 31, 2007, the number of our common shares owned by all persons known to us to own more than 5% of our outstanding common shares as of such date:

	Common Shares	
Name of Person or Group	**Shares Owned**	**Percent of Total**
	(in thousands)	
Vicunha Siderurgia S.A.[1]	116,286,665	42.74%
BNDESPAR	17,085,986	6.28%

(1) Owned indirectly by Benjamin Steinbruch, Chairman of our Board of Directors, and members of his family. Does not include the outstanding shares that are described under "Item 6E. Share Ownership", which are beneficially owned by Benjamin Steinbruch.

7B. Related Party Transactions

From time to time we conduct transactions with companies directly or indirectly owned by our principal shareholders or members of our Board of Directors. See "Acquisitions" and Planned Investments under "Item 4A. History and Development of the Company," Item 4B. Business Overview, "Item 6A. Directors and Senior Management" and "Item 7A. Major Shareholders" and Note 21 to the consolidated financial statements included in Item 18. Financial Statements.

During 2004 and 2005, we used Banco Fibra, or Fibra, a bank controlled by the Steinbruch family, in connection with the management of our exclusive investment funds, under circumstances where we were not exposed to Fibra s credit risk and where we paid investment fees not in excess of such fess we would expect to pay to a non-affiliated bank for such services. However, as of August 22, 2006, the management of our exclusive investment funds was

transferred to Bank UBS Pactual, under the same circumstances where we are not exposed to the bank s credit risk.

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Item 8. Financial Information

8A. Consolidated Statements and Other Financial Information

See "Item 18. Financial Statements" for our consolidated financial statements.

Legal Proceedings

We record provisions for contingencies relating to legal proceedings with respect to which we deem the likelihood of an unfavorable outcome to be probable and the loss can be reasonably estimated. This determination is made based on the legal opinion of our internal and external legal counsel. We believe these contingencies are properly recognized in our financial statements in accordance with SFAS No. 5. 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 us. We believe that these proceedings will ultimately result in the realization of contingent tax credits or benefits that can be used to settle direct and indirect tax obligations owed to the Brazilian Federal or State Governments. We do not recognize these contingent tax credits or benefits in our financial statements until realization of such gain contingencies has been resolved. This occurs when a final irrevocable decision is rendered by the courts in Brazil. When we use contingent tax credits or benefits based on favorable temporary court decisions that are still subject to appeal to offset current direct or indirect tax obligations, we maintain the legal obligation accrued in our financial statements until a final irrevocable judicial decision on those contingent tax credits or benefits is rendered. The accrual for the legal obligation related to the current direct or indirect tax obligations offset is not reversed until such time as the utilization of the contingent tax credits or benefits is ultimately realized. This accounting is consistent with our analysis of a liability under FASB Concepts Statement No. 6. The accounting for the contingent tax credits is in accordance with accounting for contingent assets under SFAS No. 5. Our accruals include interest on the tax obligations that we may offset with contingent tax credits or benefits at the interest rate defined in the relevant tax law.

We classify an accrual as short-term when it expects the liability to be settled in 360 days or less. As of December 31, 2006, US$25 million had been classified as short-term accrual for contingencies (US$19 million as of December 31, 2005). This usually occurs when a final, unappealable and irrevocable judgment has been rendered and the legal processes are in the execution phase. However, given the complexity of the Brazilian legal system and the intricacies of some claims, it is impracticable for Brazilian companies to predict the time period in which final decisions will be reached for such claims. Consequently, these claims are classified as long-term liabilities.

The deposits for contingencies and disputed taxes payable are generally based on (i) accruals recorded in connection with lawsuits, (ii) judicial orders issued in connection with lawsuits and (iii) guarantees in connection with judicial foreclosure proceedings. Such deposits are classified as long-term assets, and the release of such deposits is conditioned upon judicial order. When such a judicial order is granted in our favor, the deposit is forfeited and returned to us in cash and the deposit account is appropriately offset. When such a judicial order is granted in a manner unfavorable to us, the deposit is used to offset the related liability and the deposit account is appropriately offset.

We are party to a number of legal proceedings arising from our ordinary course of business, including tax, civil and labor claims. As of December 31, 2006, we recorded aggregate provisions of US$1,820 million relating to tax, civil and labor claims, for which we had deposited US$301 million in judicial escrow accounts. See Note 18 to our consolidated financial statements contained in Item 18. Financial Statements in this annual report.

Labor Contingencies

As of December 31, 2006, the amount of the accrual relating to probable losses for these contingencies were US$21 million (US$27 million in 2005). In 2006, the our legal counselors revised the claims and based on their judgment and the recent favorable track record on these disputes, management reversed certain labor claims which are currently considered as possible. Most of the lawsuits are related to alleged joint liability between us and our independent contractors, wage equalization, additional payments for unhealthy and hazardous activities, overtime and disagreement between employees and the Brazilian government over the amount of severance payable by us. The lawsuits related to the alleged joint liability between us and our independent contractors represent a large portion of the total labor lawsuits against us and are originated from by the independent contractors lack of payment of labor charges, resulting in our inclusion in the lawsuits.

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Civil Contingencies

These are mainly claims for indemnities within the civil judicial processes in which we are involved. Such proceedings, in general, are a result of occupational accidents and diseases related to our industrial activities. In 2006, our legal counselors revised the claims and based on their judgment and the recent favorable track record on these disputes, our management reversed certain civil claims which are currently considered as possible. As of December 31, 2006, the amount of the accrual relating to probable losses for these contingencies was US$9 million (US$6 million as of December 31, 2005).

Other Tax Contingencies

In addition to the tax contingencies described in Item 5A. Operating Results Results of Operations 2006 Compared to 2005 Disputed Taxes Payable, we are party to other judicial and administrative proceedings not described in the notes to our consolidated financial statements, involving a total of approximately US$286 million as of December 31, 2006 (US$428 million as of December 31, 2005). Our external legal counsel deemed that the risk of loss arising from these lawsuits are possible as opposed to probable. Therefore, we not recorded accruals with respect to these lawsuits.

Other taxes contingencies relate to a variety of disputes for which CSN has recorded provisions for probable losses. No single group of similar claims constitutes more than 5% of total contingencies.

Dividend Policy

General

Subject to certain exceptions set forth in the Brazilian Corporate Law, our bylaws require that we pay a yearly minimum dividend equal to 25% of adjusted net profits, calculated in accordance with Brazilian Corporate Law. Proposals to declare and pay dividends in excess of the statutory minimum are generally made at the recommendation of the Board of Directors and require approval by the vote of holders of common shares. Any such proposal will be dependent upon our results of operations, financial condition, cash requirements for our business, future prospects and other factors deemed relevant by the Board of Directors. Until December 2000, it had been our policy to pay dividends on our outstanding common shares not less than the amount of our required distributions for any particular fiscal year, subject to any determination by the Board of Directors that such distributions would be inadvisable in view of our financial condition. In December 2000, the Board of Directors decided to adopt a policy of paying dividends equal to all legally available net profits, after taking into consideration the following priorities: (i) our business strategy; (ii) the performance of our obligations; (iii) the accomplishment of our required investments, and (iv) the maintenance of our good financial status.

Pursuant to a change in Brazilian tax law effective January 1, 1996, Brazilian companies are also permitted to pay limited amounts of interest on stockholders equity to holders of equity securities and to treat these payments as an expense for Brazilian income tax purposes. These payments may be counted in determining if the statutory minimum dividend requirement has been met, subject to shareholder approval.

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For dividends declared during the past five years, see Item 3A. Selected Financial Data. At our Annual Shareholders Meeting of April 30, 2007, our shareholders approved the payment of dividends and interest on shareholders equity referred to 2006, in the total amount of US$682.1 million, out of which US$191.7 million and US$153.5 million were already paid on June 30, 2006 and August 8, 2006, respectively, as intermediary dividends, in accordance with the relevant resolutions of our Board of Directors. These amounts were translated into U.S. dollars based on the exchange rate in effect on the respective dates of payment. The outstanding balance of US$336.9 million (this amount was translated into U.S. dollars based on the exc