SADIA S.A.
Form 20-F
June 30, 2006

U.S. SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 20-F

[ ] REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g)

OF THE SECURITIES EXCHANGE ACT OF 1934

OR

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15 (d)

OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2005

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d)

OF THE SECURITIES EXCHANGE ACT OF 1934

OR

[ ] SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15 (d)

OF THE SECURITIES EXCHANGE ACT OF 1934

Commission file number 1-15184

SADIA S.A.

(Exact Name of Registrant as Specified in its Charter)

Federative Republic of Brazil

(Jurisdiction of Incorporation or Organization)

N/A

(Translation of Registrant's name into English)

Rua Fortunato Ferraz, 365

Vila Anastácio, Sao Paulo, SP

05093-901, Brazil

(Address of principal executive offices)

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

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

Securities registered pursuant to Section 12(g) of the Act:

None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:

None

The total number of issued shares of each class of stock of SADIA S.A. as of December 31, 2005, was:

257,000,000 Common Shares, no par value per share

423,495,712 Preferred Shares, no par value per share

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

Yes X No __

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1034.

Yes __ No X

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes _X_ No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer.

(X) 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 _X_ .

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

Ross Kaufman, Greenberg Traurig, LLP

200 Park Avenue, New York, New York 10166

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GENERAL

Unless otherwise indicated, all references contained herein, to the "Company", to "Sadia", or to "Sadia Group" are references to Sadia S.A., a corporation organized under the laws of the Federative Republic of Brazil ("Brazil"), and its consolidated subsidiaries: Sadia International Ltd.; Sadia GmbH; Rezende Marketing e Comunicaçao Ltda., Rezende Óleo Ltda., and Concórdia S.A. Corretora de Valores Mobiliários, Câmbio e Commodities.

Presentation of Certain Financial Information

References to "preferred shares" and "common shares" refer to the Company's authorized and outstanding preferred stock and common stock, designated as "*açoes preferenciais*" and "*açoes ordinárias*", respectively, each without par value. All references herein to the *"real," "reais" or "R$"* are to the *real,* the official currency of Brazil since July 1, 1994. All references to (i) "U.S. dollars", "dollars" or "US$" refer to United States dollars, (ii) "km" to kilometers, and (iii) "tons" to metric tons.

Forward-Looking Statements

This annual report contains certain forward-looking statements as defined in Section 21E of the U.S. Securities Exchange Act of 1934 with respect to the financial condition, results of operations and business achievements/ performance of Sadia and certain of the plans and objectives of management of the Company with respect thereto. These statements may generally, but not always, be identified by the use of words such as "should", "expects", "estimates", "believes" or similar expressions. Such statements include, but are not limited to, statements under the following headings: (i) Item 4. Information on the Company; and (ii) Item 5. Operating and Financial Review and Prospects. This annual report also contains forward-looking statements attributed to certain third parties relating to their estimates regarding the growth of markets and demand for products. By their nature, forward-looking statements involve risk and uncertainty because they reflect the Company's current expectations and assumptions as to future events and circumstances that may not prove accurate: the factors discussed in Item 3. Key Information — Risk Factors, among others, could cause the Company's actual financial condition, results of operations and business achievements/ performance to differ materially from the estimates made or implied in such forward-looking statements.

PART I

ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not applicable.

ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

ITEM 3. KEY INFORMATION

A. Selected Financial Data

U.S. GAAP Presentation

The selected financial information for the Company included in the following table should be read in conjunction with, and is qualified in its entirety by reference to, the U.S. GAAP financial statements of the Company and "Operating and Financial Review and Prospects" appearing elsewhere herein. The consolidated financial data for the Company as of December 31, 2005, 2004, 2003, 2002, and 2001 are derived from the audited U.S. GAAP financial statements, which differ in certain respects from accounting practices adopted in

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Brazil (defined as Brazilian GAAP). Brazilian GAAP is determined by the requirements of Law No. 6,404, dated December 15, 1976, as amended (Brazilian corporate law), and the rules and regulations of the *Comissao de Valores Imobiliários*, or CVM, the Brazilian Securities Commission.

SADIA S.A.

SELECTED FINANCIAL DATA

Years ended December 31, 2005, 2004, 2003, 2002 and 2001 (In thousands of *reais* - R$, except numbers of shares and per share amounts)

	2005	**2004**	**2003**	**2002**	**2001**
Net Operating Revenue	7,317,842	6,109,225	5,081,717	4,139,070	3,602,470
Operating Income	680,903	635,029	401,009	345,322	487,853
Net income	603,268	489,501	473,268	284,262	203,484
Basic earnings per thousand shares in R$:					
Preferred	885.08	742.42	717.80	431.14	308.62
Common	885.08	674.93	652.54	391.94	280.56
Diluted earnings per thousand share in R$:					
Preferred	884.38	742.42	717.80	431.14	308.62
Common	884.38	674.93	652.54	391.94	280.56
Dividends paid per thousand shares in R$:					
Preferred	231.96	234.68	170.08	106.89	69.75
Common	210.87	213.34	154.61	97.18	63.41
Total Current Assets	4,588,176	3,944,802	3,645,379	2,759,217	1,562,713
Total Assets	6,707,284	5,830,973	6,149,453	4,975,627	3,325,305
Total Current Liabilities	2,625,812	2,766,719	2,969,833	2,591,383	1,335,176
Total Liabilities	4,081,472	3,064,254	3,179,620	2,384,244	1,990,129
Total Shareholders' Equity	2,228,117	1,838,364	1,521,585	1,057,759	967,181
Weighted average number of shares outstanding:					
Preferred	424,595,712	425,695,712	425,695,712	425,695,712	425,695,712
Common	257,000,000	257,000,000	257,000,000	257,000,000	257,000,000

The exchange rates of *real* amounts into U.S. dollars for the years ended December 31, 2001, 2002, 2003, 2004, 2005 and January 2006 through May 2006 are shown in the table below:

	Reais per U.S. Dollar			
Year Ended December 31,	**High**	**Low**	**Average**	**End of Period**
2001	2.8007	1.9353	2.3532	2.3204
2002	3.9552	2.2709	2.9983	3.5333
2003	3.6623	2.8219	3.0600	2.8892
2004	3.2051	2.6544	2.9171	2.6544
2005	2.7621	2.1633	2.4125	2.3407

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	Reais per U.S. Dollar	
Months Ended	**High**	**Low**
January 2006	2.3460	2.2116
February 2006	2.2217	2.1177
March 2006	2.2238	2.1067
April 2006	2.1542	2.0892
May 2006	2.3711	2.0586

B. Capitalization and Indebtedness

Not applicable

C. Reasons for the offer and use of proceeds

Not applicable

D. Risk Factors

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 the Company's business and the market price of the preferred shares.

The Brazilian economy has been characterized by frequent and occasionally extensive intervention by the Brazilian government. The Brazilian government has often changed monetary, taxation, credit, tariff and other policies to influence the course of Brazil's economy. The Brazilian government's actions to control inflation and implement other policies have involved interest rate increases, wage and price controls, currency devaluations, freezing of bank accounts, capital controls and limits on imports.

Sadia's results of operations and financial condition may be adversely affected by the following factors and governmental reaction to them:

- fluctuations in exchange rates;
- interest rates;
- inflation;
- tax policies;
- exchange controls;
- energy shortages;

- liquidity of domestic capital and lending markets; and
- other political, diplomatic, social and economic developments in or affecting Brazil.

Uncertainty over whether the Brazilian government will change policies or regulations affecting these or other factors may contribute to economic uncertainty in Brazil and to heightened volatility in the Brazilian capital markets. These and other developments in the Brazilian economy and governmental policies may adversely affect the Company and its business.

Inflation and government actions to combat inflation may contribute significantly to economic uncertainty in Brazil and could adversely affect the Company´s business.

Historically, Brazil has experienced high rates of inflation. Inflation, as well as certain government efforts to combat inflation, has had significant negative effects on the Brazilian economy. Inflation rates were 25.31% in 2002, 8.71% in 2003, 12.41% in 2004 and 1.21% in 2005, as measured by the *Índice Geral de Preços-Mercado*, or the IGP-M. The Brazilian government's measures to control inflation have often included maintaining a tight monetary policy with high interest rates, thereby restricting availability of credit and reducing economic growth. Inflation, actions to combat inflation and public speculation about possible additional actions also contributed materially to economic uncertainty in Brazil.

If Brazil experiences high levels of inflation in the future, the rate of growth of the Brazilian economy may be slowed, which would lead to reduced demand for the Company´s products in Brazil. Inflation also is likely to increase some of Sadia´s costs and expenses, which the Company may not be able to pass on to its customers and, as a result, may reduce profit margins and net income. In addition, high inflation generally leads to higher domestic interest rates, and, as a result, the costs of servicing its *real*-denominated debt may increase. Inflation may, in addition, hinder access to capital markets, which could adversely affect the Company´s ability to refinance its indebtedness. Inflationary pressures may also lead to the imposition of government policies to combat inflation that could adversely affect its business.

Fluctuations in the value of Brazil's currency against the value of the U.S. dollar may result in uncertainty in the Brazilian economy and the Brazilian securities market, which may adversely affect the Company's financial condition and results of operations and, consequently, the market value of the preferred shares and ADSs.

The Company's results of operations are affected by exchange-rate fluctuations between the Brazilian *real* and the U.S. dollar.

The *real* appreciated 22.3% in 2003, 8.9% in 2004 and 13.4% in 2005 against the dollar. On December 31, 2005, the U.S. dollar/*real* exchange rate was US$1.00 per R$2.3407.

Devaluation of the *real* relative to the U.S. dollar also could result in additional inflationary pressures in Brazil by generally increasing the price of imported products and services and requiring recessionary government policies to curb demand. In addition, a devaluation of the *real* could weaken investor confidence in Brazil. On the other hand, appreciation of the *real* against the U.S. dollar may lead to a deterioration of the country's current account and the balance of payments and may dampen export-driven growth. A significant devaluation of the *real* in relation to the U.S. dollar or other currencies could reduce the Company´s ability to meet debt service requirements of its foreign currency-denominated obligations.

Export revenues and the Company´s margins are also affected by the *real* fluctuations in relation to the U.S. dollar. Production costs are denominated in local currency but export sales are denominated in U.S. dollars or euros. Financial revenues generated by exports are reduced when they are translated to *reais* in the periods in which the Brazilian currency appreciates in relation to the U.S. currency.

In addition, fluctuations in the value of the *real* relative to the U.S. dollar can affect the market value of the ADSs. Devaluation of the *real* may reduce the U.S. dollar value of distributions and dividends on the ADSs and may also reduce the market value of the preferred shares and the ADSs.

Restrictions on the movement of capital out of Brazil may hinder investors' ability to receive dividends and other distributions as well as the proceeds of any sale of preferred shares.

The Brazilian government may impose temporary restrictions on the conversion of Brazilian currency into foreign currencies and on the remittance to foreign investors, of proceeds from investments in Brazil. Brazilian law permits the government to impose these restrictions whenever there is a serious imbalance in Brazil's balance of payments or reasons to foresee a serious imbalance.

Government restrictions on capital outflow may hinder or prevent the custodian in Brazil, or if investors have exchanged ADSs for the underlying preferred shares, from converting the proceeds relating to the preferred shares into U.S. dollars and remitting those proceeds abroad. Investors could be adversely affected by delays in obtaining any required governmental approval for conversion of Brazilian currency payments and remittances abroad in respect of the preferred shares underlying the ADSs. In addition, the Brazilian government may institute a more restrictive exchange control policy in the future.

Currently, in order to remit the proceeds of distributions on, and gains with respect to, the preferred shares to the U.S., the depositary must register with the Central Bank the amount invested by non-Brazilians in the preferred shares underlying the ADSs. The depositary will register its interest in the preferred shares as a foreign investment with the Central Bank. The Central Bank will issue a certificate of foreign capital registration in the name of the depositary, under which the custodian will, assuming the continued availability of foreign exchange, be able to convert dividends and other Brazilian currency-denominated distributions from the Company into U.S. dollars and remit such U.S. dollars abroad to the depositary for distribution to the foreign investor.

Developments in other emerging markets may adversely affect the market price of the preferred shares and ADSs

The market price or the preferred shares and ADSs may be adversely affected by declines in the international financial markets and world economic conditions. The Brazilian securities market is, to varying degrees, influenced by economic and market conditions in other emerging market countries, especially those in Latin America. Although economic conditions may differ in each country, investors’ reaction to developments in one country can have an effect on the securities markets and the securities of issuers in other countries, including Brazil.

Accordingly, adverse developments in emerging market countries could lead to a reduction in both demand and the market price for the preferred shares and ADSs. These events may discourage international investment in Brazil and, more directly, may hurt the market price of the Company’s preferred shares and ADSs.

Enforcement of civil liabilities may be difficult

The Company is organized under the laws of Brazil. All of the Company’s directors and officers and many of its advisors reside in Brazil and substantially all of the assets of these persons and of the Company are located in Brazil. As a result, it may not be possible to effect service of process upon these persons within the United States or other jurisdictions outside of Brazil. Similarly, it may not be possible to enforce, judgments of non-Brazilian courts, including judgments predicated on civil liability under the U.S. securities laws against the Company or its directors and officers.

Brazilian counsel has advised the Company that Brazilian courts will enforce judgments of U.S. courts for civil liabilities predicated on the U.S. securities laws only if the judgment satisfies certain requirements imposed by the Brazilian federal supreme court. The foreign judgment will be enforceable in Brazil if:

· It fulfills all formalities required for its enforceability under the laws of the country that granted the foreign judgment;

· It is for the payment of a certain sum of money;

· It was issued by a competent court after service of process was properly made on the Company in the jurisdiction where the judgment was awarded;

· It is not subject to appeal;

· It is authenticated by a Brazilian consular office in the country where it was issued and is accompanied by a sworn translation into Portuguese; and

· It is not contrary to Brazilian national sovereignty, public policy or good morals, and does not contain any provision that for any reason would not be upheld by the courts of Brazil.

Brazilian counsel has also advised the Company that:

· As a plaintiff, a holder may bring an original action predicated on the U.S. securities laws in Brazilian courts and that Brazilian courts may enforce liabilities in such actions against the Company, its directors, and certain of its officers and advisors;

· If a holder resides outside Brazil and owns no real property in Brazil, such holder must provide a bond to guarantee court costs and legal fees in connection with litigation in Brazil; and

· Brazilian law limits the ability of a judgment creditor of the Company to satisfy a judgment against the Company by attaching certain of its assets.

Risks Relating to the Company's Business

The business involves breeding of animals and meatprocessing

The Company's operations involve raising animals, which is subject to a variety of risks, including disease, contamination, consumer health concerns and adverse weather conditions. Meat is subject to contamination during processing and distribution. Contamination during processing could affect a large number of the Company's products and therefore could have a significant impact on its operations. The Company's sales are dependent on consumer preferences, and the loss of consumer confidence in the products sold by Brazilian producers because of disease or contamination could affect the Company's results of operations.

Grains are the most representative isolated component of COGS and are exposed to the volatility of the commodity markets

The Brazilian foodstuffs industry, like the processed feed industry in other countries, has been characterized by cyclical periods of higher prices and profitability, followed by overproduction, leading to periods of lower prices and lower profitability. The Company believes that domestic prices and export prices for its product line are likely to remain volatile and subject to cyclical variation. There can be no assurance that the Company's results will not be adversely affected by future downturns in market prices. The largest single component of the Company's cost of sales is the cost of ingredients used in the preparation of feed. The price of most of the Company's feed ingredients is subject to significant volatility resulting from weather, the size of harvests, transportation and storage costs, governmental agricultural policies, currency exchange rates and other factors.

Environmental issues and new regulation requirements can affect costs

Brazilian food producers, including the Company, are subject to stringent federal, state and local environmental laws and regulations concerning, among other things, human health, the handling and disposal of wastes and discharges of pollutants to the air and water. In view of the possibility of unanticipated regulatory or other developments, particularly as environmental laws become more stringent both in Brazil and worldwide, the amount and timing of future expenditures required to maintain compliance could vary substantially from their current levels and could adversely affect the availability of funds for other capital expenditures and other purposes.

Competition in both domestic and foreign livestock and food processing sector is very strong

The Company faces significant competition from other Brazilian producers in the domestic markets in which it sells its products, and from world producers in the export markets in which it sells its products. Other major vertically integrated Brazilian producers compete with the Company. To varying degrees, these companies have substantial financial resources and strengths in particular product lines and regions. The Company expects that it will continue to face strong competition in every market and that existing or new competitors are likely to broaden their product lines and to extend their geographic scope. Accordingly, there can be no assurance that the Company’s performance will not be adversely affected by increased competition.

Protectionist measures could restrict Company exports

Due to the growing share of the Brazilian livestock, pork and poultry sector in the international market, companies are increasingly being affected by measures taken by importing countries in order to protect local producers. Because of the competitiveness of Brazilian companies, certain countries have raised several restrictions to prevent the entrance of Brazilian livestock products. Outcomes such as quota restrictions or import suspensions in a certain country or region, can affect substantially the sector’s export volumes and consequently the Company’s export performance as well as the results of its operations.

FMD Cases in Brazil can indirectly affect pork sales and adversely impact the results of the Company

Although the detected Foot and Mouth Disease (FMD) cases in the northeast region of Brazil in the past have affected only cattle, hogs can also be contaminated. Cases of FMD were identified in the states of Mato Grosso and Paraná during the second half of 2005. The Company´s animal breeding facilities are located in the states of Santa Catarina and Minas Gerais, internationally recognized FMD free regions. No assurance can be given, however, that we will not be affected by FMD, either directly or through limitations on exports imposed by importing countries.

An outbreak of Avian Influenza could require the destruction of a significant portion of the Company´s flocks of fowl

Recent outbreaks of a strain of virus, H5N1, known as Avian Influenza (“AI”), have been reported in Europe and India. Earlier outbreaks were reported during late 2003 and early 2004 in eight countries in Asia. At that time, more than 100 million birds in the affected countries either died from the disease or were destroyed in order to try to control the outbreak. The virus, which is believed to be spread from region to region by infected wild birds, represents a significant risk to flocks of fowl, which if infected must be destroyed to assure containment of the virus. No AI has been detected in Brazil and climatic conditions and distance from previous outbreaks reduce the likelihood of any outbreak. In 2003, through a joint effort of the Brazilian Ministries of Agriculture, Health and Environment, Brazil implemented a program to monitor and test birds with potential to carry the Avian Influenza virus from the South Pole.

In addition to the animal health requirements, which are part of the Brazilian National Poultry Health Program, Brazil has adopted a range of measures intended to limit the possibility of an outbreak of AI, including: tightened controls at ports and airports for travelers arriving from Asia; a prohibition on the importation of paddy rice from Asia; restrictions on visits to Brazilian poultry farms by travelers from Asia; and restrictions on the importation of poultry genetics.

Additional preventative measures have been discussed and the Brazilian government has proposed and approved the adoption of a National Plan for the Prevention and Control of Newcastle Disease and the Prevention of Avian Influenza (*Plano Nacional de Controle e Prevençao da Doenca de Newcastle e de Prevençao de Influenza Aviária)* which will conform with OIE (World Organization for Animal Health) standards. These measures are intended to assure international markets that Brazil maintains sanitary barriers between states. Specific measures include regulation of animal transportation, traceability, blood tests, designated laboratories and other controls to monitor production conditions on a regional basis. These measures are intended to permit the early detection of contamination in one region and to prevent the spread

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of that contamination to other regions within Brazil. Because the virus that causes AI is destroyed by cooking, it is generally agreed that the consumption of contaminated poultry does not present a threat to human health.

Despite measures adopted by the Company, the Brazilian government, and other poultry producers, no assurance can be given that the Company will not be affected by AI, either directly or through limitations on exports imposed by importing countries.

Risks relating to Sadia S.A.

The Company is controlled by a Group of Shareholders and the interests of the controlling group may conflict with those of other shareholders

The Company is controlled by a group of shareholders under the Company's shareholders' agreement. The preferred shares and the ADSs are not entitled to vote at meetings of shareholders, except in limited circumstances. This means, among other things, that preferred shareholders are not entitled to vote on corporate transactions, including mergers or consolidations of the Company with other companies. In addition, the controlling shareholders have the ability to determine the outcome of any action requiring shareholder approval, including transactions such as corporate reorganizations, change of control transactions and the timing and payment of future dividends. For more information, see Item 7 – "Major shareholders and related party transactions".

If the Company loses any of its largest clients, or if they significantly reduce the amount they purchase from the Company, its revenue and operating income could be materially adversely affected

The Company´s ten largest customers in 2005 accounted for approximately 20% of total domestic sales and approximately 10% of total gross sales. While the Company has been developing new client-oriented policies to reduce the concentration of revenues, if it loses any of its ten largest customers or if they reduce significantly the amount they purchase from the Company, revenues and operating income could be materially adversely affected.

The Company's ability to export could be adversely affected by port labor disputes and disruptions and by import restrictions

The Company's ability to export is dependent, in part, on factors beyond its control, including the lack of transport facilities due to strikes or other causes, or the enactment of Brazilian laws or regulations restricting exports in general or its products in particular. Any of these could affect the Company's revenue and operating income.

ITEM 4. INFORMATION ON THE COMPANY

A. History and Development of the Company

Sadia is a public held company, incorporated in Brazil on June 7, 1944, and therefore is subject to the requirements of Law No. 6,404, dated December 15, 1976, as amended by Law 9.457/97 (Brazilian corporate law), and the rules and regulations of the *Comissao de Valores Imobiliários*, or CVM, the Brazilian Securities Commission.

Sadia is Brazil's leading refrigerated and frozen protein products company, operating in the processed product, poultry and pork segments. The Company believes that its brand name and distinctive logotype are among the most widely recognized and admired in Brazil and in the foreign markets in which it market its products, associated with quality, tradition and value. The Company's central administrative headquarters are located at Rua Fortunato Ferraz, 365, Vila Anastácio, Sao Paulo, state of Sao Paulo, Zip

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Code 05093-901, Brazil, telephone number (55 11) 2113-3465, and the Company's website is www.sadia.com.br or www.sadia.com and e-mail address is ri@sadia.com.br. Materials posted on the website are not deemed incorporated by reference into this annual report nor made a part hereof.

Sadia S.A. began in 1944, with the acquisition by Attilio Fontana of the meatpacker Concórdia Ltda., located in the municipality of the same name, in the Western part of the state of Santa Catarina, Brazil. At the time, the Company consisted of a wheat mill and an unfinished slaughterhouse for hogs.

Over the course of its 60-year history, the Company evolved based on two key strategies: the diversification of its portfolio of food products, and investment in quality.

At the end of the 1980s and the beginning of the 1990s, the Company's policy of expansion gave way to rationalization of management and cost structures through reduction by merger of a number of companies in the Sadia Group. Sadia began the 1990s having the controlling ownership in 21 companies, and began to concentrate its operations in the production of processed meat products.

From 1997 forward, management has continued the reorganization of the Sadia Group and has implemented the strategy of concentrating on higher value-added processed products.

In 1997, the Company sold its cattle slaughterhouse in Barra do Garças, state of Mato Grosso, four soybean processing facilities (crushing and refining), 12 purchasing and warehousing centers (for grains), and also transformed its Várzea Grande slaughterhouse, state of Mato Grosso, into a plant for the production of processed meat products. In addition, the transport of the products, which had been made by a fleet of owned vehicles, was outsourced to specialized transportation companies.

In July 1998, Sadia was merged with two of its subsidiaries, Sadia Frigobrás S.A. and Sadia Concórdia S.A., so that all of the activities of the Sadia Group were concentrated in a single listed company, Sadia S.A. This resulted from a gradual process of reorganization with a view to simplifying the Sadia Group structure, increasing visibility to capital markets, and achieving gains in scale through the reduction of general and administrative expenses and tax costs.

In December 1999, Sadia acquired the capital stock of Granja Rezende S.A. (primarily a producer and distributor of poultry and pork products) and its wholly owned subsidiaries Rezende Alimentos Ltda., Rezende Óleo Ltda. and Rezende Marketing Comunicaçoes Ltda.

Immediately following the acquisition of Granja Rezende, the Company decided to sell Granja Rezende's soybean crushing and oil manufacturing plant and administrative complex.

During 2000, the subsidiary Rezende Alimentos Ltda. was converted from a limited liability company into a corporation and the subsidiary's name was changed to Sadia Alimentos S.A. On December 29, 2000, the then parent was merged into Sadia Alimentos S.A., whose name was then changed to Sadia S.A. The purpose of the merger was to permit an operational and administrative rationalization, and the utilization of tax loss carry forwards. In August 2002, Granja Rezende S.A. was merged into Sadia, aiming at cost reduction both through standardization and through rationalization of the administrative and operational activities as well as by resulting reflections of financial and fiscal nature.

In April 2001, the Company listed its American Depositary Receipts (ADRs) program on the New York Stock Exchange, providing investors an alternate channel to buy its stocks. In June 2001, the Company adhered to the level one corporate governance with Bovespa, certifying its commitment to transparency and fair disclosure of information.

In the second half of 2001, Sadia and Sun Valley, U.K. based subsidiary of Cargill Foods, formed a partnership. This partnership gave rise to Concordia Foods Ltd., Worcester, UK. In January 2005, the partnership between Sadia and

Sun Valley was discontinued, the legal entity is being phased out. Sadia U.K. Ltd., assumed the operations once performed by Concordia Foods Ltd.

In August 2001, Sadia opened a distribution center (DC) in Jundiaí, Sao Paulo, to supply the Sao Paulo state region, considered the largest market in Brazil. The Jundiaí DC, is a technological milestone for the Company with 20,000 square meters of area. The Company invested R$ 23 million in facilities and IT structure.

In May 2002, Sadia GmbH and its subsidiary, Laxness F.C.P.A. Lda. (Laxness) were created, aiming to leverage exports to the European market. In February 2005, Laxness changed its name to Wellax Food Logistics C.P.A.S.U. Ltd (Wellax).

In November 2004, the Company opened a distribution center in Ponta Grossa, state of Paraná, giving the Company greater capacity and efficiency in its export processes.

In January 2005, Sadia acquired 100% of the ownership interest of Só Frango Produtos Alimenticios Ltda. (Só Frango), a company based in Brasilia with a total capacity for slaughtering 150,000 chickens per day (at the time of the acquisition). In April 2005, Só Frango was merged into Sadia.

In November 2005, Sadia decided to return to the beef segment due to the belief that it represents a complementary business to the Company’s activities. Sadia’s strategy in this segment is to concentrate sales towards the external market; for the domestic market the Company will focus its efforts on special beef cuts.

Reclassification

The Company reclassified the poultry and hog breeders, reclassifying them from inventories to property, plant and equipment, since breeders are generally accounted for as fixed assets and also because they contribute to the cost formation of the poultry and hogs raised for commercial purposes. The Company has not changed the breeders’ estimated useful life.

The breading stock (net of depreciation) in the amount of R$108,065 for the year ended December 31, 2004 has been reclassified from inventories to property, plant and equipment and its related depreciation in the amount of R$58,755 and R$50,837 for the years ended December 31, 2004 and 2003 respectively has been added to the depreciation and amortization line item under operating activities in the statements of cash flows for these respective years. Also, the amount of R$85,813 and R$73,594 has been added to the purchase of property, plant and equipment line item under the investing activities in the statements of cash flows for the years ended December 31, 2004 and 2003, respectively.

Investments

In the last years Sadia has continually increased its level of capital expenditures.

In 2005, an amount of R$ 742.4 million was invested, of which R$ 194.6 million (26.2%) was directed towards the processed products segment, R$ 372.8 million (50.2%) towards poultry, R$ 27.0 million (3.6%) to pork and the remaining R$148 million (20%) mainly to information technology. These investments were made in order to supply the growing demand in the domestic and external markets.

As part of the 2005 investment plan, in January 2005 Sadia acquired 100% of Só Frango Produtos Alimentícios Ltda. (“Só Frango”), for R$70.3 million. Só Frango was active in poultry slaughtering and processing as well as in the production of animal feed meal. Its product line ranges from whole chicken, special frozen and chilled cuts to sausages and cold cut meats. With 1,700 employees, Só Frango generated R$220 million in gross revenues in 2004 and had a slaughtering capacity of 150,000 chickens per day. In April 2005, Só Frango was merged into Sadia S.A.. Sadia intends to expand this capacity over the next five years to 400,000 chickens per day, which should generate 2,000 new direct jobs and around 12,000 indirect jobs. All operations with out growers and suppliers, as well as Só Frango’s job positions, have been maintained. Through this acquisition, the Company strengthened its presence in the central region of Brazil, close to raw material producers and to main centers of consumption.

As part of the 2005 and 2006 investment plan Sadia is undertaking a sizeable expansion at the Uberlândia Complex, which will require investments of over R$400 million intended to increase the capacity of all of its production lines. The Company will invest R$185 million, the integrated out growers will invest R$180 million, and R$36 million will be invested in logistics in 2006. The R$185 million investment will be distributed as follows: R$44 million to pork production, increasing the slaughter capacity from 700,000 heads to 1.6 million heads; chicken production will receive R$46 million to increase the slaughter capacity from 43 million heads to 88 million heads; the turkey line will receive R$35 million to increase its capacity of 7 million heads to 11 million heads. Sadia will also invest R$44 million in the construction of a new feed plant, R$7.5 million to expand the production of processed products and R$8 million in the storage of grains. The Uberlândia Complex will also house the Company's second margarine plant. This represents an investment of R$60 million and is expected to become operational in the second half of 2006.

In 2004, the amount invested was R$324.9 million, of which R$93.2 million (28.7%) was directed towards the processed products segment, R$146.6 million (45.1%) towards poultry, R$40.1 (12.3%) to pork. The remaining R$44.9 million (13.8%) was directed towards the Ponta Grossa distribution center located in the state of Paraná, and towards the upgrade of the management software, SAP.

In 2003 Sadia invested R$179.3 million.

Investment Plans

For 2006, the total expected investment is R$ 850 million, of which R$ 400 million will be directed towards the State of Mato Grosso units and the remaining towards new projects in Uberlândia (MG), Toledo and Ponta Grossa (PR), as well as expansions in units in the state of Santa Catarina. These investments are intended to ensure better service to Sadia's customers, both domestic and international. The Company expects to fund its investment plan with available cash flow generated from operations.

From 2006 to 2009, Sadia plans to invest R$1.5 billion in the state of Mato Grosso. The Company will be responsible for R$800 million, and the remainder will be invested by its outgrowers. The amount will be directed towards the construction of two poultry slaughter houses, one in the city of Lucas do Rio Verde, and the other in the city of Campo Verde. Each one of them will have the slaughter capacity of 500 thousand animals per day. As part of this investment, Sadia will also set up a slaughter and industrialization hog unit, with slaughter capacity of 5 thousand animals per day in the city of Lucas do Rio Verde, and a feed factory. The new units are expected to generate 8 thousand direct jobs and 24 thousand indirect ones.

Additional information on this investment plan are as follow:

• Sadia's R$800 million investment will be distributed as follows: 50% in 2006; 25% in 2007 and the remainder 25%, in 2008.

• From 2007 on, the poultry slaughter houses will operate with 20% of capacity. In 2008, it is expected that these units will operate with 85% of capacity, reaching their full capacity in 2009.

• The expected additional annual revenue for poultry is R$1.2 billion by 2009, and the expected additional revenue for the hog unit is R$400 million by 2009.

• The R$800 million investment does not contemplate additional working capital, which will add up to R$140 million in 2009, for the 3 units.

• The tax incentives will be similar to those obtained in other states in the Midwest and better than those obtained in the southern states of Brazil.

B. Business Overview

Sadia is the leader in all of the markets in which it operates within Brazil (see “Market Share”), with a product portfolio of over 1,000 products. According to the Brazilian Chicken Exports Association (ABEF), the Company is the largest Brazilian slaughterer and distributor of poultry and pork products, as well as the largest domestic exporter of poultry. Sadia is also the largest domestic distributor of frozen and refrigerated meat-based products (according to AC Nielsen), and leader in the Brazilian market for margarine. As of December 31, 2005, the Sadia Group had 45,537 employees, one of the largest employers in Brazil. During 2005 Sadia sold 950.7 thousand tons of poultry, 140.2 thousand tons of pork and 738.7 thousand tons of processed products, including frozen and refrigerated meat-based products and margarine, generating gross operating revenues of R$8.3 billion and net income of R$603.3 million.

The Company's high degree of vertical integration ensures control at all stages of production and distribution of products. Sadia's operations include breeding farms for poultry and hog grandparent and parent stock, hatcheries, pork breeding centers, slaughterhouses, processing units, animal feed production plants, representative offices and distribution centers. The Company pioneered the vertical integration of poultry and hog breeding in Brazil, initially in the state of Santa Catarina. Today, with the exception of beef, all operations employ a system of vertical integration, consisting of a partnership with rural producers, with a view to obtaining animals for slaughter, raised in highly productive breeding conditions and controlled hygienic-sanitary conditions. Sadia produces one-day chicks and piglets and supplies them to outgrowers, along with feed, transport, technical and veterinary assistance.

Sadia exports around 1,000 different products to approximately 100 countries. It currently produces a range of products that includes: frozen, refrigerated, salted and smoked pork cuts, lard, bacon, ingredients for "feijoada" (a Brazilian pork and bean stew); frozen and refrigerated pork and chicken giblets; whole frozen and seasoned chickens; frozen and refrigerated poultry cuts and parts; marinated and partially cooked chicken parts; whole frozen and seasoned turkeys; frozen and seasoned turkey cuts and parts; breaded chicken parts; raw, cooked and smoked hams; "tender" gammons, hams, cold cuts and related products; "Parma-type" hams; smoked chickens and turkeys; cooked and smoked turkey hams and turkey-based cold cuts; partially cooked and frozen products, such as beef, turkey and chicken meatballs; beef, turkey and chicken-based hamburgers; pork, turkey and chicken based frankfurters; sausages; bolognas; salamis; coppa; turkey-based hams; cold cuts in general; chicken, meat and pork-based patés; beef, poultry and fish-based frozen ready-made dishes and pasta; frozen ready-made foods for heating and serving as meals and snacks, such as breaded poultry, fish and appetizers, frozen pizzas and refrigerated fresh pasta; margarine and refrigerated desserts.

Sadia owns 13 plants within 7 different states in Brazil, and distributes its product line of over 1,000 items through distribution and sales centers located throughout Brazil, Latin America, the Middle East, Asia and Europe.

Business Strategy

Sadia's business strategy is designed to give continuity to the Company's growth and increase its profitability. The Company believes that with the recognition of its brand name as a symbol of quality, tradition and value—Sadia means "healthy" in Portuguese — an unequaled domestic distribution network supported by excellent logistics, attention to customer needs across the product line and in all distribution channels and highly favorable production economics in Brazil, the Company will be able to achieve both increased growth and increased profitability, while maintaining its commitment to its employees, outgrowers, suppliers and residents of the communities in which it does business. The principal elements of this strategy are as follows:

Increase domestic market penetration through expanded distribution. Sadia has an extensive distribution network, supported by an outsourced transportation fleet, superior knowledge of wholesale, retail and institutional sales channels, integrated logistics planning and strategically located distribution centers, trans-shipment points and facilities. The Company plans to continue to develop and improve its distribution network and systems in every product category.

Focus on retail sales, institutional and food service sales channels for domestic business. Sadia has increased, and plans to continue focusing on meeting the needs of retail sales outlets, institutional and food service sales channels, such as restaurants, rather than concentrating on wholesale outlets, such as large supermarkets and distributors. Between 2002 and 2005 the Company added more than 25,000 customers to its list.

Continue to increase service and market responsiveness. Sadia intends to remain the leader in Brazil in the markets that it serves by maintaining high standards of customer service and continuing to be responsive to the changing needs of varying market segments. As part of this strategy, it has structured its operations,distribution and logistics so that it can fill orders of varying sizes depending on the particular demands of the market segment. In export markets, the Company seeks to provide raw and processed products. It intends to remain close to its customer base, providing decentralized and rapid order fulfillment and personalized service, including attention to refrigeration quality in customers' facilities.

Maintain low-cost product and operating efficiency. The natural advantages of operating in Brazil—grains, labor, weather, out-grower and related costs—added to the Company's operating efficiency, permit it to compete in international markets. Sadia intends to continue to be amongst the lowest cost producers and distributors of protein products in the Brazilian and international markets. The Company's vertically integrated operations and attention to operating efficiencies, permit quality and cost control throughout the entire production process.

Continued brand differentiation. Sadia has developed its brand across the entire product line both in the domestic and international markets, and that is amongst its most valuable assets. The Company intends to continue to invest in the development of branded products, through shipping, packaging, advertising campaigns, with a view to continue to develop brand loyalty and the perception of premium quality that is associated with the Sadia products.

Increase production, through organic growth, investment in production capacity and acquisitions. Most recently, in January 2005, Sadia acquired 100% of Só Frango Produtos Alimentícios Ltda. ("Só Frango"), for US$26.5 million

Maintain exports and domestic sales volumes approximately equal. The competitiveness of the production of poultry and pork gives the Company access to international markets, economies of scale and low-cost export financing. Sadia has had success in increasing sales in foreign markets, such as Russia, where it previously did not have a presence, and increasing the number of markets in which the Company is present and the products that it sells. Sales to international markets and domestic markets, in substantially equal amounts, provides an important hedge against volatility in any particular market.

Invest in environmentally sound projects and initiatives. Sadia has been increasingly active in seeking to assure that its business is environmentally sound, beyond mere compliance with regulations, and it intends to invest significantly in this aspect of the business. Recently, Sadia concluded a borrowing of R$60 million from the Brazilian development bank, BNDES, in order to develop the "3S Program" - Sadia Sustainable Swine Production Program, which will consist in selling carbon certified emission reductions under the Clean Development Mechanism signed at the Kyoto Treaty to finance social initiatives in the outgrowers area.

Expand product portfolio, with emphasis on higher value-added processed products. Sadia believes that continuous product innovation is essential to meet the needs of customers and consumers. As the market for frozen ready to eat products has grown, both domestically and internationally, Sadia has sought to meet the challenge by increasing emphasis from poultry and pork production to production of processed food products, including a product portfolio that now numbers over 700 products. During the last three years, Sadia has introduced an average of 60 new products per year, after extensive product development and test marketing.

The Company's Operation

The Company's operations are organized into three segments: "processed products" (frozen and refrigerated products and margarines), "poultry" (chickens and turkeys) and "pork".

In 2005, 44% of total gross operating revenue was derived from the processed products segment, poultry 41%, pork 9%, and 5% from other activities. Of the Company's total gross operating revenue in 2004, 47% was derived from the processed products segment, poultry 41%, pork 8%, and 4% from other activities, such the grain and by-products segment, hog and poultry breeding, boiled beef, beef-parts and resale of products. In 2003 48% was derived from the processed products segment, poultry 38%, pork 10% and 4% from other activities.

Activities related to the grains and by-products currently consist of the crushing of soy to obtain the meal used as a raw material in the production of feed for the company's stock and that of the integrated producers.

The following tables present sales volumes and gross operating revenue (prepared and presented in accordance with US GAAP) for the years ended 2005, 2004 and 2003, as shown:

	Sales Volumes (ton)		
	2005	**2004**	**2003**
Domestic Market	**823,573**	**736,465**	**677,842**
Processed Products	647,062	581,213	529,663
Poultry	142,177	105,826	100,419
Pork	34,334	49,426	47,760
External Market	**1,006,047**	**855,303**	**668,044**
Processed Products	91,593	84,059	39,936
Poultry	808,636	692,192	524,419
Pork	105,818	79,052	103,689
Consolidated	**1,829,620**	**1,591,768**	**1,345,886**
Processed Products	738,655	665,272	569,599
Poultry	950,813	798,018	624,838
Pork	140,152	128,478	151,449

	Gross Operating Revenue (R$ Million)		
	2005	**2004**	**2003**
Domestic Market	**4,251.7**	**3,724.6**	**3,188.2**
Processed Products	3,289.1	2,946.4	2,523.7
Poultry	512.1	415.4	356.0
Pork	148.3	154.9	129.8
Other	302.2	207.9	178.7
External Market	**4,075.7**	**3,392.7**	**2,529.3**
Processed Products	412.3	405.6	284.9
Poultry	2,937.6	2,488.7	1,787.4
Pork	592.4	429.8	443.0
Other	133.4	68.6	14.0
Consolidated	**8,327.4**	**7,117.3**	**5,717.5**
Processed Products	3,701.4	3,352.0	2,808.6
Poultry	3,449.7	2,904.1	2,143.4

Pork	740.7	584.7	572.8
Other	435.6	276.5	192.7

(*) Other: Grains and by-products, beef parts, pig and chicken breeding and resale of products

The following table presents the breakdown of gross operating revenue in percentage terms by segment, for the years ended 2005, 2004 and 2003, as shown:

	Gross Operating Revenue by Segment (%)		
	2005	**2004**	**2003**
Processed Products	44	47	48
Poultry	41	41	38
Pork	9	8	10
Other	5	4	4

(*) Other: Grains and by-products, boiled beef parts, pig and chicken breeding and resale of products

The following information about segments is based upon information used by the Company's management to assess the performance of operating segments and decide on the allocation of resources and has been prepared and presented in accordance with Brazilian GAAP that is adjusted for US GAAP presentation. The Company has three identifiable reportable segments: Processed products, Poultry and Pork.

	2005	**2004**	**2003**
Net operating revenue			
Processed products	3,147,296	2,731,136	2,386,247
Poultry	3,199,246	2,951,897	2,250,189
Pork	732,710	586,595	554,698
Other	239,186	37,845	41,864
Adjustments for US GAAP presentation	(596)	(198,248)	(151,281)
Total net operating revenue	7,317,842	6,109,225	5,081,717

Other net operating revenue is primarily attributable to grain and by-products and beef products operations.

	2005	**2004**	**2003**
Depreciation expense			
Processed products	(60,863)	(48,708)	(54,069)
Poultry	(80,336)	(56,682)	(54,653)
Pork	(16,853)	(11,003)	(14,565)
Other	(7,294)	(973)	(961)
Total depreciation expense allocated to Segments	(165,346)	(176,134)	(169,672)
Depreciation allocated to administrative expenses	(12,829)	(13,461)	(18,227)
Adjustments for US GAAP presentation	(4,088)	31,774	37,801
Total depreciation expense	(182,263)	(157,821)	(150,098)

	2005	2004	2003
Segment operating income			
Processed products	273,684	274,197	194,188
Poultry	269,766	260,393	143,514
Pork	94,586	70,902	26,632
Other	2,798	(3,765)	5,548
Adjustments for US GAAP presentation	40,069	33,302	31,127
Total operating income	680,903	635,029	401,009
Interest expense	(324,231)	(413,461)	(449,408)
Interest income and other	248,203	309,454	481,609
Foreign currency exchange gain (loss), net	159,602	20,672	52,833
Adjustments for US GAAP presentation	(93,825)	35,428	(14,512)
Income before income taxes, equity income or loss of investees and minority interest	670,652	587,122	471,531
Segment assets			
Processed products	624,619	491,982	487,933
Poultry	750,504	459,035	377,799
Pork	147,724	137,798	118,985
Other	143,359	76,910	53,747
Adjustments for US GAAP presentation	(142,897)	(110,485)	(128,454)
Total property, plant and equipment	1,523,309	1,055,240	910,010
Reconciling items - corporate assets			
Cash and cash equivalents	2,663,689	2,406,125	2,610,961
Accounts and notes receivable, net	509,615	349,605	453,936
Inventories	992,490	1,064,671	839,557
Other corporate assets	690,825	739,691	616,095
Adjustments for US GAAP presentation	184,459	105,156	661,787
Total consolidated assets	6,707,284	5,830,973	6,149,453
Capital expenditures			
Processed products	194,587	93,220	45,056
Poultry	372,761	146,606	43,799
Pork	26,982	40,145	5,709
Other	91,662	52,286	15,656
Adjustments for US GAAP presentation	56,365	(7,340)	69,124
Total segment capital expenditures	742,357	324,917	179,344

Processed Products

As a result of the Company's strategy of concentrating on higher value-added, higher margin products, the processed products segment results increased significantly as from the second half of the 1990s. Average volumes sold increased 11.7% per year since 1998. Sales of processed products accounted for 44% of the Company´s gross operating revenues in 2005.

Sadia owns nine plants that manufacture processed products, eight of which are dedicated to meat processing and one to margarine production. These plants are located close to their suppliers of raw materials or to the main domestic centers of consumption.

The processed products segment comprises a wide range of products, including: frozen products (hamburgers, breaded products, ready-made dishes and pizzas), refrigerated products (hams, sausages,

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frankfurters, bolognas, salamis, cold cuts, product portions and refrigerated pasta) and margarine, the majority of which are sold under the Sadia brand.

Processed products in the domestic market, accounted for 88.9% of the total gross sales of this segment, with the remaining 11.1% directed towards exports. The total sales from this segment grew 10.4% as compared to 2004.

Most of the raw materials used derive from poultry and pork produced by the company. By contrast, selected suppliers, who are subject to inspection by the Federal Agriculture Ministry, produce all beef that is processed by the Company.

The Company believes that the use of chicken meat as a raw material for processed products should grow substantially for two reasons: (i) the increase in the range of chicken-based products such as breaded products, and (ii) an increasing share for this kind of meat in the composition of other processed products, such as sausages, frankfurters and bolognas. Moreover, the development of specialized products (boiled and roasted products) for the institutional and foreign markets should also contribute to the increase in chicken production.

The following table presents gross operating revenue from sales of processed products in 2005, 2004 and 2003:

	Gross Operating Revenue (R$ Million)		
	2005	**2004**	**2003**
Processed Products	**3,701.4**	**3,352.0**	**2,808.6**
Refrigerated	3,084.7	2,778.0	2,326.6
Frozen	616.7	574.0	482.0

Sadia is the Brazilian leader in frozen and refrigerated processed products according to AC Nielsen’s surveys. The Company’s market position is supported by significant investments in its brand, distribution channels and in quality control.

Brazilian Market Share (2005)

	Position	**Market Share by Revenue (%)**	**Period**
Frozen Processed Products	1st	45.70	October/November-05
Refrigerated Processed Products	1st	29.60	November/December-05
Margarine	1st	34.20	October/November-05

Source: AC Nielsen

In order to maintain market share, Sadia will continue to concentrate on launchings of higher value-added products. In 2005, the Company launched 76 products, against 57 products in 2004 and 53 products in 2003.

Poultry and Pork

In 2005, sales of non-processed products reached R$4,190.4 million, and accounted for 50.3% of the Company´s total gross operating revenue. In 2004, sales of non-processed products reached R$3,488.7 million, and accounted for 41.9% of Sadia´s total gross operating revenue. In 2003 sales of non-processed products reached R$2,716.2 million, and accounted for 32.6% of total gross operating revenue. Sadia exports significant amounts of fresh meat, which in 2005 accounted for approximately 86%. In 2005, poultry and pork sales accounted for approximately 86.6% of total export revenue, in 2004 for approximately 86% and in 2003, 88.2%.

Sadia owns eight chicken slaughterhouses, three turkey slaughterhouses, and four pork slaughterhouses. In addition, the Company has one beef slaughterhouse in the state of Mato Grosso, which became operational as of November 2005. The table below shows slaughtering volumes of the Company for the years ended December 31, 2005, 2004, and 2003, in millions of units:

	Slaughtering Volumes (Million Heads)		
	2005	**2004**	**2003**
Poultry	650.1	573.0	501.0
Hogs	3.8	3.5	3.9

The following table shows gross operating revenue from non-processed products, for the years of 2005, 2004 and 2003:

	Gross Operating Revenue (R$ Million)		
	2005	**2004**	**2003**
Poultry	**3,449.7**	**2,904.0**	**2,143.4**
Whole	1,492.9	1,206.9	740.8
Parts	1,811.0	1,583.9	1,298.5
By-products	145.8	113.2	104.1
Pork	**740.7**	**584.7**	**516.5**
Total	**4,190.4**	**3,488.7**	**2,659.9**

In 2005, Sadia had a 10.3% share of domestic chicken production, in terms of tons and a 25.8% share of the Brazilian poultry export market. This compares with results for 2004 and 2003, when the Company had a 13.6% and 12.9% share of domestic chicken production and a 27.9% and 23.0% share of the Brazilian poultry export market, respectively. Sadia introduced turkey production to the Brazilian market in 1973, when its consumption was virtually non-existent. Today the market is shared with other competitors, but the Company is still in the leadership position, with 65.6% of total sales in 2005, as compared with 66.2% of total sales in 2004 and 66.1% for 2003.

Approximately 70% of the Company’s pork production is used in its processed products segment. The remainder is sold as fresh meat cuts in the domestic and international markets. According to the Brazilian Pork Producers Association (ABIPECS), in 2005, Sadia had a 14.2 % share of domestic pork production, and a 14.2% share of the Brazilian pork export market. This compares with results for 2004 and 2003, when the Company had a 10.4% and 11.3% share of domestic pork production and a 19.7% and 21.3% share of the Brazilian pork export market, respectively.

Beef

In November 2005, Sadia decided to return to beef because it believes that it represents a complementary business to the Company’s activities. Sadia’s strategy in this sector is to concentrate sales towards the external market, for the domestic market the Company will focus its efforts on special beef cuts. In 2005, it accounted for less than 3% of total Gross Operating Revenues.

Production Process

Processed Products

The Company uses special cuts of pork, chicken and turkey, as well as selected and shaped fragments for the production of hams, sausages, frankfurters, bologna, hamburgers, pressed ham and related products. Seasonings and secondary raw materials are applied to each product type or line, according to established formulas, in order to ensure consistency, color, texture and flavor. The presentation of final products is achieved by shaping, casing, cooking and freezing in special machines. Products are then subjected to quality controls and distributed to the consumer market after having been packaged, labeled and boxed.

The raw material for margarine is crude soybean oil, which is subjected to refining and bleaching processes. Fats are obtained by hydrogenating bleached oil. Both of these materials are deodorized in order to prepare the “blend”. The process is completed by the preparation of an emulsion, the cooling and crystallization of the product, placing into containers, and the packing of these into boxes.

Poultry

The production process for poultry consists of four stages. The first two entail direct investment by the Company in grandparent and parent stock. The third relates to the commercial stock of birds, and involves the direct participation of integrated out-grower farmers, and the last is the slaughtering process.

The Company imports grandparent stock from the United States in the form of eggs that are hatched in its hatcheries and then raised on company-owned farms. These birds produce parent stock that are also raised on company-owned farms, and that in turn produce eggs. The operation involves eleven hatchery centers, eight of which produce “one-day-chicks” and three “one-day-turkeys”. The “one-day-chicks” are supplied to third-party outgrowers. Sadia operates a similar system for turkeys, importing eggs to produce grandparent stock that in turn produces parent stock that are raised on company-owned farms. The Company is not dependent on any foreign supplier for its genetic resources, nor does it face any barriers to their development.

The “one-day-chicks” produced by parent stock are supplied to integrated outgrowers who are responsible for raising the birds. Sadia has contracts with approximately 6,600 outgrowers, to which the Company provides feed, technical and veterinary assistance to allow such outgrowers the outgrowing process up to the time the birds reach slaughtering age, which for chickens is normally 40 days (at a weight of 2.0 kg). There are no employment agreements between the Company and the outgrowers, who generally carry out this activity in order to supplement their income. Most outgrowers farm on a small scale and raise six flocks per year (each flock consists of approximately 14,000 chickens). The Company remains the owner of the birds, and at the end of each production cycle, pays a commission fee based on a performance index that is calculated as a function of indicators such as bird mortality, feed to meat conversion ratio and average weight. The fee paid to the integrated farmers covers the outgrowing costs, raw materials, labor and their net profit.

Poultry are slaughtered through a process by which they are electrically stunned. They are then bled by puncturing of major blood vessels. After heating to a temperature of 55/60ºC, they are plucked and gutted by automatic machines. The gutting process is subject to health control and inspection. The carcasses are then moved for cooling or freezing at respective temperatures of 6ºC and –12/-18ºC, and are then packaged according to the required standards of the *Serviço de Inspeçao de Produtos Animais* (SIPA – Animal based Product Inspection Agency). At this stage, the whole birds are either distributed to the consumer market as fresh meat or used as raw material in processed products.

Pork

The Company produces grandparent, parent and piglet stock on its own farms, 90% of the parent stock produced by the company is supplied to integrated outgrowers who receive feed, medicine and technical assistance by way of support. These parent animals produce hogs that are sold to the Company for slaughter, after the fattening process is completed. The remainder of the parent stock produced by Sadia is sold to piglet producers, who also receive feed, medicine and technical assistance. The Company repurchases the piglets at market prices and distributes them to integrated outgrowers, who after the fattening process sell such pigs to Sadia for slaughtering.

The hogs are slaughtered through a process in which they are bled after being stunned electrically. After heating to a temperature of 60/64ºC, their bristles are removed by automatic machines. The animals are then dried, flamed, brushed and gutted, which process is subject to health inspection. After cooling to a temperature of 5ºC, the carcasses are cut up and processed.

Beef

Differently than poultry and pork, Sadia does not raise cattle. The Company purchases it in the spot market from one thousand selected producers. The slaughtering process is conducted by the Company in its facility in the state of Mato Grosso.

Principal markets where the Company competes

In 2005, Sadia had an average of 49% of its gross operating revenues provided from exports. This ratio was 48% and 44% for 2004 and 2003, respectively. The table set forth below presents the main regions of the world where the company has commercial relations and the discussion that follows describes the main trends and expectations for its markets. This information has been prepared and presented in accordance with Brazilian GAAP and is adjusted for U.S. GAAP. Refer to Note 20 of the consolidated financial statements for details on the primary differences between Brazilian GAAP and U.S. GAAP.

	Exports Gross Operating Revenues (Thousand R$)		
	2005	**2004**	**2003**
Europe	978,318	985,746	912,252
Middle East	1,047,615	802,935	632,991
Asia	635,907	602,202	353,731
South America	542,151	387,130	130,322
Emerging Markets (mainly Russia and other former Soviet Union countries	872,333	806,520	630,332
Adjustments to US GAAP presentation	(627)	(191,869)	(130,349)
Total	**4,075,697**	**3,392,664**	**2,529,279**

Revenues are attributed to regions based upon where the products are shipped. All long-lived operational assets are located in Brazil and assets located outside of Brazil consist of sales offices located in various countries.

Europe is a large purchaser of poultry cuts and processed products. Sadia maintains a traditional presence in the Middle East, with market leadership and a strong brand recognition. Middle Eastern countries primarily consume whole birds of low weight (up to 1.4 kilograms) and processed products. With respect to Eurasia, which comprises the Caucasus region and Russia, the Company exports mainly pork and poultry cuts. The main exports to Asia are special poultry cuts, pork carcasses and cuts. In the Americas, sales are concentrated primarily in processed products, poultry parts and whole birds. Secondary markets include regions with great potential for growth in the medium term.

Seventy nine percent of the Company’s exports in 2005 were to investment grade countries.

Market Overview – Domestic and International Markets

The growth potential of the Brazilian market for processed food, poultry and pork, and Brazil's low production costs are attractive to international competitors. The main barrier to such companies has nevertheless been the need to build a wide ranging refrigerated distribution chain, and a network of integrated producers. The prices of the sector's principal raw materials, corn and soybeans, are influenced principally by climate conditions.

The following analysis was prepared based on information mainly gathered from: The USDA (United States Department of Agriculture), FAO (Food and Agriculture Organization – United Nations), CONAB (Brazilian National Supply Company), ABEF (Brazilian Poultry Exporters Association) and ABIPECS (Brazilian Pork Meat Exporters Association) and AC Nielsen reports.

Brazilian Processed Products Market

Consumption of processed products is influenced by several factors, including the increase in consumer income, and efforts related to the development of products, with a view to meeting consumer demand for more sophisticated products.

The processed products segment is divided into three categories: frozen products, refrigerated products and margarines.

Frozen Processed Products

In 2005, the Brazilian market for frozen processed products accounted for sales of R$1,214.3 million. Approximately 85% of this total is attributable to the two largest companies, Sadia S.A. and Perdigao.

	2005	**2004**	**2003**
Sales (R$ million)	1,214.3	1,100.6	974.7
Change %	10.3%	12.9%	-
Volume (thousands of tons)	143.4	134.9	121.6
Change %	8.5%	10.9%	-

Source: AC Nielsen

Due to the characteristics of frozen processed products with production concentrated among a small number of companies, and supply aimed at a more restricted group of consumers, the Company believes that volume sales of frozen processed products will maintain their growth trend, although at rates below the 11.6% annual average registered between 2003 and 2005. In any case, since the market for frozen processed products is still far from mature in Brazil, Sadia believes that medium and long-term prospects for this segment are highly positive based on the trend over the preceding years.

Refrigerated Processed Products

In 2005, the Brazilian market for refrigerated processed products accounted for sales of R$5,094.9 million. The two largest companies in this market accounted for approximately 56% of the total share value of this market, according to AC Nielsen, with the remaining share being split among a large number of small companies.

	2005	**2004**	**2003**
Sales (R$ million)	5,094.9	4,383.1	3,656.5
Change %	16.2%	19.9%	-
Volume (thousands of tons)	744.0	675.5	616.7
Change %	10.2%	9.5%	-

Source: AC Nielsen

Margarine

In 2005, the Brazilian market for margarine accounted for sales of R$1,527.5 million. The three largest producers accounted for 85% of the market.

	2005	**2004**	**2003**
Value (R$ million)	1,527.5	1,501.2	1,485.3
Change %	1.8%	1.1%	
Volume (thousands of tons)	302.3	285.9	294.0
Change %	5.8%	2.9%	

Source: AC Nielsen

Poultry

Domestic Market

The Brazilian poultry market is a complex sector where a few large companies share the market with small producers. According to ABEF's 2005 annual report, the four largest chicken producers in Brazil accounted for 37.1% of Brazilian production in 2005. The low concentration in the market increases competitive pressure in the segment. Prices are subject to supply and demand imbalances.

Many of these small producers operate under low quality standards because of the large number of producers and government difficulties to inspect them on a regular basis. Additionally, there is a widespread belief that informal practices among these producers reduce their costs as compared to producers that comply with applicable regulations.

Growth in Brazilian per capita consumption of poultry over the last four years is expected to continue as the FAO forecast a 3.7% growth for 2005 as compared to 2004.

e= estimate / f= forecast

Source: FAO (Food and Agriculture Organization)

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In the local market, poultry export business in Brazil has grown more rapidly since the mid 1990s. This can be explained by the shift of large Brazilian company's exports, as well as by the competitiveness of Brazilian poultry. Recent sanitary problems in the main producing countries such as the Bovine Spongiform Encephalophy ("BSE") cases in Europe, Avian Influenza ("AI") problems in Thailand and both BSE and AI cases in the United States have changed the world broiler trade framework. The reduced competition from major exporting countries affected by sanitary issues and the competitive cost of Brazilian poultry favors Brazil as the most competitive exporter of quality poultry cuts and mechanically de-boned chicken meat. Additionally, several new markets in Europe, Africa and the Middle East have opened to Brazilian chicken, and the number of markets which Brazil has access to has risen from 134 to 142 in 2005, according to ABEF's 2005 annual report.

Brazilian Broiler Exports
Volume Destination (thousands of tons)

	2005		**2004**		**2005/04**
Middle East	843	31%	750	31%	12%
Asia	753	27%	629	26%	20%
EU	321	12%	278	11%	16%
Russia	254	9%	192	8%	33%
Africa	192	7%	181	7%	6%
South America	113	4%	81	3%	39%
Others	286	10%	314	13%	-9%
Total	**2,762**	**100%**	**2,425**	**100%**	**14%**

Source: ABEF

For 2006, the USDA has revised upwards the projected Brazilian broiler production to 10 million tons, 7% from the record production level of nearly 9.4 million tons last year. The projected increase in production reflects the firm domestic demand derived from higher employment rates and consumer purchasing power as the economy improves and continues to boost demand for animal proteins. Moreover, as 2006 is an election year, additional federal funding for social programs to fight hunger will help increase broiler demand. In addition to that, expansion in the export market will likely continue in view of the animal health (mostly Avian Influenza) problems faced by other countries.

According to the USDA's GAIN Report whole broiler exports in 2005 reached nearly 1.1 million tons, with an increase of 7% over 2004. The average export price for whole broilers in 2005 increased 26.6% over the previous year. Exports of broiler parts reached 1.7 million tons, up 18% over 2004. The average export price for broiler parts in 2005 increased 11.8% from the previous year. This confirms Brazilian broiler exporters' strategy to increase profitability by focusing on higher value products, such as broiler parts and further processed products which increased significantly in 2005 by 86% in volume, reaching 84,000 tons, valued at US$ 184 million, up 82% from 2004.

In 2005, Japan became the largest market for Brazil's broiler exports, mostly broiler parts. Exports to Japan increased by 24% in volume, and by 34% in value.

The European Union was the second largest market for Brazilian broiler exports, mostly broiler parts, with an increase of 24.9% in volume, and 34% in value. The increase in broiler exports to the European Union also reflects a significant increase in exports of processed broilers. The European Union market accounted for nearly 80% of all processed broiler exports from Brazil.

Saudi Arabia, traditionally Brazil’s largest single export market for poultry, now ranks third. In 2005, Saudi Arabia increased imports of Brazilian broilers, mostly for whole broilers, 14% in volume and 38% in value. Saudi Arabia also accounted for nearly 45% of all Brazilian broiler exports to the Middle East.

Russia remained as the 4th largest market for Brazilian broiler exports in 2005 despite quota restrictions. Shipments to Russia totaled 258,000 tons, up 34% from 2004. The value of broiler exports to Russia was significantly up in 2005 by 65%, reflecting a larger increase in broiler parts.

International Poultry Market

The prevalence of highly pathogenic avian influenza (“HPAI”), which is reportedly spreading from Asia to other countries, may impact the world broiler trade outlook in 2006. Despite the possible impacts on poultry consumption raised by concerns of HPAI, the USDA forecasts a 3.5% increase in the world poultry consumption in 2006.

According to the FAO, properly cooked poultry is safe to consume as conventional cooking (temperatures at or above 70°C in all parts of a food item) will inactivate the H5N1 virus. Moreover, there is no epidemiological evidence to indicate that people have been infected with the H5N1 virus following consumption of properly cooked poultry or eggs. It is expected, thus, that as consumers become more aware of the true dangers of HPAI, the level of poultry consumption will not be affected.

According to the USDA, world economic growth is expected to remain strong throughout 2006, although not at the same level of 2005. The forecasted positive economic environment will promote investment in meat production and processing capacity in many major livestock and poultry producing countries.

Moreover, increases in worldwide real per capita GDP in 2006 will continue to fuel rising livestock and poultry consumption and hence production. Asian economies particularly China, Hong Kong, Taiwan, and Thailand are forecast to experience strong growth, likely fostering meat consumption as consumers will have more disposable income.

According to the FAO, from 1999 to 2004 per capita consumption of poultry in developing countries grew at an annual rate of 2.8% compared with a 2.5% growth rate in developed countries. Many observers believe that the consumption of animal protein in developing countries will continue to grow at a faster rate than in developed countries, in part due to the rapid economic growth of many developing countries, such as China and India. Economic growth and increases in per capita income is tied to growth in meat demand as less expensive vegetable protein is substituted for animal protein sources. From 1999 to 2004, per capita poultry consumption in India grew at an annual rate of 12.7%, contrasted with a 0.3% decline in Japan for the same period.

According to the USDA, macroeconomic stability and growth in low and some middle-income countries results in higher consumption of red meat and poultry, providing new growth opportunities for domestic producers and world suppliers.

According to the FAO, per capita consumption of poultry in developed countries is more than three times that of developing countries. This difference is even more accentuated for certain countries. In 2005, for instance, while India is forecasted to consume 1.6kg poultry per capita, Japan will consume, 10 times that amount, with 16kg.

e= estimate / f= forecast

Source: FAO (Food and Agriculture Organization)

According to the USDA, broiler meat exports by major traders are forecasted to reach a record breaking 7.5 million tons in 2006. Poultry demand is expected to be strong due to the absence of the United States in major beef markets and constraints on growth in Brazilian beef exports. The 2006 increase of nearly 7% is the result of increased trade by a number of countries including Argentina, Brazil, China, Thailand, and the United States.

Thai broiler meat exports in 2006 are estimated to grow further by 30% over the 2005 level, mainly because of the market value of Thai cooked products and because of the ability of Thai producers to increase cooked product supplies quickly. It is expected that total exports will continue to be cooked products as import prohibitions on Thai uncooked chicken continue.

Thai domestic consumption in 2006 is forecasted to grow further by 7% due to increasing consumer confidence in the safety of cooked chicken meat among Thai consumers and relatively competitive prices of chicken meat against other meats. Broiler meat consumption in 2005 recovered from the 2004 level to 750,000 tons after a sharp drop in domestic consumption in 2004, and it is just bellow the 2003 record consumption of 775,000 tons. Improved disease controls have rebuilt consumer confidence in the safety of chicken meat.

According to the USDA, in 2005, Russian poultry production grew by 15% and is expected to increase by an additional 15% in 2006 as the sector continues to benefit from heavy investment. Despite these investments Russia will continue to be the worldwide leader in poultry imports with a forecasted 1.1 million tons for 2006. Poultry accounts for 35% of the total Russian meat market, of which 35% are whole birds, 37% are chicken leg quarters and 28% is deeply processed product.

Japan’s total broiler consumption in 2006 is projected to stay flat from the level achieved last year at 1.8 million tons. The USDA also expects a slight decrease of 2.1% in the Japanese poultry imports, as a consequence of the weaker outlook for food service demand, coupled with high year beginning stocks.

Saudi Arabia poultry imports for 2006 are expected to reach about 447,000 tons a 2.5% increase compared to the 2005. As stated in the USDA’s GAIN Report, according to local importers, Brazilian frozen broiler meat exports this year are expected to increase by at least 10% compared to the 2004 export level of 333,000 tons. France, the second largest broiler meat exporter to the Kingdom, is expected to lose significant market share to Brazil this year compared to last year.

The USDA projects that the European Union broiler meat consumption will have just a slight increase of 0.5%, reaching 7.3 million tons. Imports on the other hand, are expected to increase by 4.5%, to 460,000 tons in 2006.

In 2006, Chinese broiler meat imports are projected to reach 300,000 tons, a 20% increase from the previous year.

	World Broiler Balance (thousands of tons)					
	2005 (p)			**2006 (f)**		
	Production	**Consumption**	**Exports**	**Production**	**Consumption**	**Exports**
United States	15,792	13,363	2,464	16,300	13,769	2,538
China	10,200	10,150	300	10,500	10,440	360
Brazil	9,400	6,240	2,800	10,000	6,490	3,040
EU	7,670	7,330	780	7,690	7,370	780
Japan	1,130	1,820	-	1,125	1,810	-
Argentina	1,080	973	110	1,180	1,034	150
Canada	1,000	984	100	1,020	995	105
Thailand	950	750	300	1,120	803	400
Others	11,325	14,253	85	12,111	15,091	93
Total	**58,227**	**55,863**	**6,979**	**60,576**	**57,801**	**7,466**

Source: USDA

(p) preliminary (f) forecast

	World Broiler Imports (thousands of tons)			
	2005 (p)		**2006 (f)**	
Russia	1,040	23%	1,075	23%
Japan	695	15%	680	15%
EU	440	10%	460	10%
Saudi Arabia	436	10%	447	10%
Mexico	360	8%	378	8%
China	250	6%	300	6%
Hong Kong	230	5%	246	5%
South Africa	175	4%	190	4%
United Arab Emirates	160	4%	160	3%
Kuwait	130	3%	138	3%
United States	17	0%	16	0%
Others	580	13%	564	12%
Total	**4,513**	**100%**	**4,654**	**100%**

Source: USDA

(p) preliminary (f) forecast

Pork

Brazilian Pork Market

Processing companies are subject to the same problems as those in the poultry market, unfair competition with small and low quality producers. Although these problems influence product quality, there is still very low perception by part of the population of the risks involved and price dumping is widely practiced. According to ABIPECS 2005 annual report, the four largest pork producers in Brazil were responsible for 35.8% of Brazilian production in 2005.

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e= estimate / f= forecast

Source: FAO (Food and Agriculture Organization)

Brazilian pork breeding and slaughtering continues to increase its productivity efficiency. Measured by the average birth rate of piglets, productivity doubled since the 1970s, the birth rate reached 24 animals per female and at 160 days old, animals weigh 100 kg in average, ready to be slaughtered. Research has also contributed to reduce fat by 31%, cholesterol by 10% and calories by 14% in pork produced in Brazil. This enhancement allows for a better productivity of prime cuts, more meat per carcass as well as more nutritious and healthier meat.

Brazilian pork exports had an impressive expansion in 2005 increasing 22.5% in volume to 761,000 tons in 2005 from 510,000 tons in 2004. It had an even better performance in terms of market value, which grew to US$ 1.2 billion in 2005 from US$ 740 million in 2004 for an increase of 57.7%.

	Brazilian Pork Exports							
	Thousand Tons				**Million US$**			
	2005	**%**	**2004**	**%**	**2005**	**%**	**2004**	**%**
Russia	405	65%	288	57%	805	69%	449	58%
Hong Kong	61	10%	58	11%	84	7%	73	9%
Ukraine	22	4%	36	7%	34	3%	52	7%
South Africa	18	3%	12	2%	31	3%	18	2%
Argentina	17	3%	28	6%	33	3%	46	6%
Cingapore	17	3%	16	3%	34	3%	27	3%
Moldavia	8	1%	2	0%	15	1%	3	0%
Albania	8	1%	5	1%	14	1%	8	1%
Uruguay	7	1%	10	2%	12	1%	13	2%
Kasakistan	7	1%	2	0%	13	1%	3	0%
Others	55	9%	52	10%	93	8%	86	11%
Total	**625**	**100%**	**510**	**100%**	**1,168**	**100%**	**777**	**100%**

Source: ABIPECS

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In 2005, Brazilian pork exporters increased their shipments of pork cuts, which now account for more than 75% of all pork exports. This increase reflects the strategy of Brazilian exporters to increase profitability by exporting higher value products.

Russia remains the principal market for Brazilian pork exports. Russian market share of Brazilian pork imports in terms of volume increased from 57% in 2004 to 65% in 2005. Hong Kong is the second largest Brazilian market for pork exports with a 10% market share, followed by Ukraine, which is now the third largest market for Brazilian pork exports.

Pork production is expected to decline by 3.2% to 2.7 million tons in 2006. The decline in pork production is mostly attributed to lower expected exports to Russia. However, foreign and Brazilian companies estimate production to increase in the center-west region of Brazil as a result of maturing investments. Most of this production increase from the center-west will be absorbed by domestic demand, which is likely to be firm in 2006 due to lower consumer prices.

International Pork Market

Pork consumption continues to benefit from beef and poultry supply disruptions due to AI and BSE. Increases in pork production are substituting for reduced demand for beef and poultry in many countries. According to the USDA, global pork exports are forecasted to increase 2.5% in 2005 reaching a record high of 4.6 million tons.

Nevertheless, there is an increasing awareness that meat trade flows are becoming largely dictated by sanitary conditions and regulations. Exporters worry that market access, driven by trade policy, as well as veterinary and food safety controls, could become easily susceptible to non-tariff trade barriers, especially when those controls are not based on technical criteria. In this very uncertain environment, exporting countries are trying to maintain a competitive position in lucrative markets. At the same time, importing countries are seeking to ensure fairness for their domestic producers, while also safeguarding the health and economic needs of their consumers.

Pork consumption in the major consuming countries is expected to grow about 3% in 2006 and again China accounts for the largest portion (76%) of this forecasted growth.

Similar to poultry, in the next years, most of the growth in pork consumption will derive from the emerging economies. Not only are low and middle-income countries increasing their per capita consumption, but they are also gradually accounting for a greater share of world consumption. According to the USDA, China’s pork consumption accounted for 50% of pork consumption in major pork consuming countries in 2001 and is forecast to account for 53% in 2006. On the other hand, the EU’s share of pork consumption is forecast to decrease from 24% to 22% from 2001 to 2006.

e= estimate / f= forecast

Source: FAO (Food and Agriculture Organization)

EU pork production is expected to marginally increase in 2006 while exports will have a slight increase of 1% in 2006 to nearly 1.5 million tons. The European Union easily retains its position as the world's leading pork exporter and is forecast to account for 28% of pork exports by major traders.

The United States market is currently signaling producers to expand production. Production in recent years has been export driven. While only 8% of U.S. pork production was exported in 2001, 13% of American pork production is expected to be exported in both 2005 and 2006. In 2006, U.S. pork exports are forecast to reach 1.3 million tons.

In 2003, the Russian government published the resolutions that established poultry quota and beef and pork tariff rate quotas (“TRQ”). The Russian TRQ establishes country specific quotas for the EU, Paraguay, United States and a general quota for all other countries. As processed pork is not under the TRQ, imports of this kind of meat pork have increased.

Meat bans introduced by Russia at the end of 2005 (affecting Brazil and Poland) and in the beginning of 2006 (affecting Ukraine) created a state of uncertainty for importers looking to fill their TRQ allocations. According to the USDA, if the bans are not removed in the near future, it will be very difficult for importers to find adequate substitution. Brazilian meat imports entered Russia for only half a year in 2005. If the ban on Brazilian meat is lifted from two of Brazil’s most important meat-producing regions, then it is expected that importers will be able to fill their quotas.

One of the few countries in which a decline in consumption is anticipated in 2006 is Japan. While the decline in Japanese pork consumption is minor, less than 2%, it demonstrates the market is readjusting. In 2004, mainly due to import bans on U.S. beef due to BSE and Asian poultry due to AI, Japan experienced unusually high levels of demand for pork. As Japan adjusts to supply shocks to the beef and poultry sectors, pork consumption is forecast to return to more historic levels.

World Pork Balance (thousands of tons)

	2005 (p)			**2006 (f)**		
	Production	**Consumption**	**Exports**	**Production**	**Consumption**	**Exports**
China	48,900	48,570	400	50,900	50,535	415
EU	20,720	19,310	1,430	20,900	19,470	1,450
United States	9,402	8,619	1,229	9,591	8,763	1,263
Brazil	2,730	1,985	745	2,656	2,100	725
Canada	1,960	1,012	1,075	1,975	1,033	1,100
Russia	1,785	2,434	1	1,900	2,574	1
Japan	1,260	2,531	0	1,240	2,485	0
Mexico	1,175	1,615	55	1,200	1,640	65
Philippines	1,100	1,130	0	1,122	1,152	0
Korea South	1,050	1,328	5	1,010	1,351	10
Taiwan	910	950	0	935	965	0
Others	1,545	2,121	63	1,569	2,139	71
Total	**92,537**	**91,605**	**5,003**	**95,167**	**94,207**	**5,100**

Source: USDA

(p) preliminary (f) forecast

According to the USDA, Japan is expected to remain the world's largest pork importer in 2006, importing over 1,235 thousand tons, slightly below the previous year. In 2004, mainly due to the import ban on U.S. beef and broiler meat from key suppliers due to animal diseases, the Japanese pork market enjoyed an unusually high demand with record level imports, high levels of domestic pork production and high prices. In 2005, this heated situation started to cool, reflecting overall slow down in consumption, reduced imports and lower stocks compared to 2004.

World Pork Imports (thousands of tons)

	2005 (p)		**2006 (f)**	
	Volume	**%**	**Volume**	**%**
Japan	1,243	31%	1,235	30%
Russia	650	16%	675	16%
Mexico	495	12%	505	12%
Korea South	300	7%	351	9%
Hong Kong	250	6%	270	7%
Romania	185	5%	180	4%
Canada	135	3%	155	4%
Australia	90	2%	95	2%
Ukraine	75	2%	60	1%
China	70	2%	50	1%
Others	127	3%	118	3%
Total Foreign	3,620	89%	3,694	89%
United States	447	11%	435	11%
Total	**4,067**	100%	**4,129**	100%

Source: USDA

(p) preliminary (f) forecast

As a result of the substitution effect arising from the ban on chicken products from China and the U.S. in 2004, Hong Kong pork imports were higher than normal. When the substitution effect dissipated in

2005, Hong Kong pork imports dropped 24.7% . The USDA forecasts for 2006 a modest increase of 8% given the sporadic avian influenza cases in China. China is the largest supplier to Hong Kong followed by Brazil. According to the USDA, Brazilian pork are very price competitive and product specifications are good for Hong Kong’s retail.

Seasonal Nature of Business

Chicken and Pork

Not seasonal in nature.

Turkeys

Turkey production activities are seasonal in nature with respect to “whole turkeys”, whose production is concentrated in the second half of the year, with a higher volume of sales in the fourth quarter because of Christmas holidays.

Processed products

Processed products are seasonal only in the celebration products, with a higher volume of sales in the fourth quarter.

Raw Materials

Sadia owns nine animal feed plants with an installed capacity of 5.5 million tons per year, a volume sufficient to supply all the animal feed requirements of its breeding operations. The basic raw materials used in animal feed production are corn and soybeans, in a mix that contains preservatives and micronutrients. The Company supplies the basic animal feed to its outgrowers and sell the remainder on the spot market.

The Company purchases corn and soybeans from rural producers, small merchants, cooperatives, large scale traders and through auctions organized by the Brazilian government, as well as occasionally from Argentina. Most of the production of these raw materials is concentrated in the States of Santa Catarina, Paraná, Rio Grande do Sul, Goiás and Mato Grosso. Grains are received in sacks or in bulk, and are then weighed. A sample is taken to measure humidity and impurities in the grain. After approval, the grain is unloaded into a hopper for cleaning and drying. Grain is then sieved in order to eliminate the residues that accompany it. After selection and cleaning, the grain is milled and mixed with the other ingredients of the feed.

Sadia acquires beef for the production of frozen and refrigerated processed products, and boiled beef parts. Other inputs, such as prepared animal intestines (for casing), seasonings and other ingredients, cardboard boxes, plastic bags (for packaging and labels), and veterinary medicines (for poultry and hog breeding), are acquired from many different sources, both at home and abroad.

Costs and Operating Expenses

Sadia´s principal costs of production are incurred in *reais* and consist of grains, corn and soybeans, packaging, and labor. While input costs are *reais* denominated, the international commodity prices (grains and packaging) tend to follow international prices and are influenced by exchange rate fluctuations. The Company operates with an average idle capacity of 20% in processed product lines but can be at full capacity depending on the market demand. Due to the flexibility in production lines and to the diversity of the equipment present in its thirteen plants, production can be adapted and reformulated, depending on the Company´s needs to face a determined segment demand, night and weekend shifts as well as supply partnerships are broadly used to reduce bottlenecks during the production process.

Corn

Brazil's corn prices used to be determined only by domestic supply. Production was mainly on relatively small properties and had a low level of mechanization. However, during 2002, due to the *real* currency depreciation and the improvement of several local producers, part of their crop was shifted to the international market. Therefore, Brazilian corn prices went up to adjust to international prices.

In Brazil, there are some 20 different regions where buyers can bid for the product. Corn prices tend to be influenced by local supply, but international prices also influence local quotes, according to crop expectations among the main world producers (U.S.A., China and Argentina) and the level of international storage in the main consuming countries (Europe and Japan).

The following chart sets forth the Company’s average monthly buying price of corn for the period between January, 1995 and December 31, 2005:

According to CONAB’s May 2006 Report, it is expected that the 2005/06 Brazilian corn crop production will increase 16.6% compared to last year’s production, reaching approximately 40.8 million tons. This increase is mainly due to the need of crop rotation between corn and soy, the disappointing soybean prices and the better productivity in corn.

Soybean

Soybean producers in Brazil have been increasing their productivity during the last several years and Brazil has become the second largest producer in the world. Soybean production is substantially mechanized and grains are cultivated on large properties. Producers are well organized and production is oriented to the export market. Production is also spread over several regions among the southern, southeastern and central region of the country, and prices are regionally given by local supply. However, international prices tend to influence local prices when foreign demand and supply are unbalanced.

CONAB expects the Brazilian soybean planted area for 2005/06 to decrease around 4.7% in comparison to the last crop. This reduction is a result of the historical low soybean prices in the domestic and foreign markets, which leads to a reduction of soybean's profitability when compared to other agricultural products such as sugar cane and corn. In addition to that, there is a negative profit margin projection for the central states in Brazil.

Despite the reduction in planted area, CONAB forecasts that the production for 2005/06 crop will be equivalent to 55.2 million tons, a 7.3% increase as compared to the 2004/05 crop. This is due to an increase in productivity, especially in the southern region of Brazil

The following chart sets forth the Company's average monthly buying price of soybeans for the period between January 1995 and December 31, 2005.

Marketing

Sadia's brand name is considered one of the Company's most valuable assets. The Company maintains an active marketing program using both electronic and printed media.

The Company incurred advertising expenses of R$116.6 million, R$121.4 million, and R$96.8 million during the years ended December 31, 2005, 2004 and 2003, respectively.

Marketing expenses are related to investments in advertising of specific campaigns for the launch of higher value-added products and for the reinforcement of Sadia's brand name.

Logistics

The Company’s logistics system and distribution channels are two of its principal competitive advantages. Sadia has taken many initiatives to sustain its leadership, which includes partnerships, information technology investments and the development of new processes for optimization of logistics, both domestic and export-related.

Distribution

Within the Brazilian market, Sadia sells its finished products to wholesale and retail outlets, as well as to institutional clients. For the year ended December 31, 2005, the Company sold to approximately 94 thousand customers throughout Brazil. Sadia´s distribution strategy is based on the importance of direct sales to customers, thereby avoiding concentration among a few large customers.

Sadia maintains sales representation offices in Germany, England, Russia, Japan, China, the United Arab Emirates, Argentina, Uruguay, Chile, Panama and Turkey. In 2005, it sold to approximately 426 foreign clients.

In 2005, 60% of exports were sold to approximately 10 long-standing customers. All of these customers have imported increasing quantities of the Company´s products over the last ten years.

Transport

Transport

Sadia uses trucks as the primary method of distributing its products in Brazil. The Company’s distribution system is handled by a network of approximately 1,800 refrigerated hired vehicles for both long and short range deliveries, which service customers directly throughout Brazil.

Distribution by truck is made by refrigerated vehicles, given the perishable nature of the food products, whose shelf life varies from 12 days, refrigerated chicken to 540 days, frozen turkey . In the case of stoppage of transport by virtue of a general strike, the result would be a complete loss of the products in transit and lack of supply for the points of sale if the period of interruption is greater than 30 days, an outcome the Company considers remote. As an alternative to highway transport, supply could be effected by air, although this would increase the freight cost by more than 20 times. In the case of a sector strike, the impact would be minimized because the Company has manufacturing units producing the same products located in different regions of the country.

Shipment of Exports

The Company ships 45% of its exports through the port of Paranaguá, 15% through Antonina, both in the State of Paraná, 38% through the ports of Sao Francisco do Sul and Itajaí, in the state of Santa Catarina and the remaining 2% from other ports.

In the port of Paranaguá, the Company has two refrigerated warehouses, capable of receiving and expediting one thousand tons per day. These warehouses have a "drive in" storage system and only operate with palleted cargoes. Since one of the warehouses is located in the wharf area, the Company has priority in the mooring of ships arriving at the port of Paranaguá, thereby avoiding possible cost increases due to delays in loading its cargo.

The Company also has a warehouse in Ponta Grossa, in the state of Paraná, with storage capacity of 11 thousand tons, and is able to receive and expedite one thousand tons per day.

The Company ships its cargoes in "full container" or conventional "reefer" vessels for palleted cargo.

Sales

Sadia has adapted its sales structure and commercial policies to include the large chain, wholesale (cash and carry), regional mid-size clients, traditional retail (small retail), institutional and distributor channels. The Company sales force has been unified in a single management group, making it possible for the big retail chains to be serviced by an account manager, with the support of coordinators, promoters and re-stockers. For medium and small retailers, Sadia has instituted a telemarketing service, which complements the market work of the sales force and also relies to a limited extent on local distributors.

Brazilian Food Sector Regulation

The Brazilian Ministry of Agriculture, through the *Secretaria de Defesa Agropecuária* (SDA), Agricultural and Cattle Breeding Defense Secretary, under the Animal Products Inspection Department (DIPOA), regulates Sadia´s activities. The latter department is responsible for the issuance of regulations, conduct of inspections and legal support in respect to the livestock, animal breeding, food processing and any other activity involving animal related affairs in the Brazilian territory.

Sustainability and Environment

Brazilian environmental regulations have their principles established in the Federal Constitution, with concurrent jurisdiction among the Brazilian federal government, the states and the municipalities to regulate the subject. The public administration at each such level of government is responsible for the supervision and control of pollution in any form, as well as for the preservation of forests, hydraulic resources and the fauna and flora. The integration of all of the federal, state and municipal agencies responsible for the protection and improvement of environmental quality is undertaken by the National Environmental System (SISNAMA).

As a producer of foodstuffs using a wide range of industrial processes, especially its meat product lines which require slaughter of animals, Sadia is subject to compliance with all of the legal requirements, covering environmental risks that are customary in these processes, such as rules governing treatment of liquid effluents, solid organic waste, particle suspension and odors. The Company is careful to respect the environment at all stages of the production chain, including its activities in the field, the design of packaging (developed with a view to reducing the quantity of raw materials used) and adapting the same to recycling processes. In addition to simplify treating residues, Sadia invests in minimizing the generation of such residues by optimizing processes and adopting stringent procedures for controlling the emission of wastes and effluents. The Company's expenditures related to meeting environmental requirements and in process optimization amounted to approximately R$10.1 million in 2005, R$13.3 million in 2004 and R$15.8 million in 2003.

C. Organizational Structure

The Sadia Group is currently composed of seventeen companies, as shown in the chart above.

The Company concentrates all production, slaughtering, distribution and product sales activities within Brazil. Sadia International Ltd. is one of the company’s smaller vehicles for sales outside Brazil, and is a shareholder of the Churrascaria Beijing steakhouse, which was established in Beijing in partnership with Sky Dragon, a company linked to the Chinese Ministry of Agriculture. Rezende Óleo and Rezende Mkt. e Comunicaçoes Ltda. are non-operational. Sadia GmbH. is a holding that controls Wellax Food Logistics C.P.A.S.U. Lda., an offshore company responsible for the largest part of Sadia´s export operations. Sadia Alimentos is a subsidiary of Sadia International, established in 2003 aiming to develop commercial operations in the Argentine market. Sadia Uruguay and Sadia Chile are each responsible for the distribution and sales of the Company´s products in their respective countries. Nordfin Holding Limited owns 40% of Sadia Chile. Concórdia CVMCC is a brokerage firm authorized to operate in accordance with current Brazilian legislation. The assets of Empresa Matogrossense de Alimentos were acquired in September 2005, as part of the company's investment strategy in the state of Mato Grosso. The companies not mentioned above are representative offices.

D. Property, Plant and Equipment

In 2005, Sadia owns thirteen plants, including eight units for poultry production, four units for pork, one for beef, ten units for animal feed, two units for the crushing of soybeans and nine units for processed products. Some plants are multi-operational, including several integrated activities. Sadia owns seventeen distribution and commercial centers and eleven representative offices and distribution centers abroad.

Operating Units

The table below lists Sadia's operating units and their principal activities:

State	City	Principal activity
MG	Uberlândia	Raising and slaughtering chickens, turkeys and hogs, processed products and animal feed
MT	Várzea Grande	Raising and slaughtering chickens, processed products and animal feed. Beef slaughterhouse.
PR	Dois Vizinhos	Raising and slaughtering chickens; animal feed and crushing of soybean.
PR	Francisco Beltrao	Raising and slaughtering chickens and turkeys and animal feed
PR	Toledo	Raising and slaughtering chickens and hogs; processed products; animal feed and soy oil
PR	Ponta Grossa	Pizzas and pasta, Miss Daisy, processed products
PR	Paranáguá	Margarine
RJ	Duque de Caxias	Processed products
RS	Tres Passos	Raising and slaughtering hogs and animal feed
SC	Chapecó	Raising and slaughtering chickens and turkeys, animal feed and processed products
SC	Concórdia	Raising and slaughtering chickens and hogs, processed products and animal feed
MT	Campo Verde	Animal feed
DF	Brasília	Raising and slaughtering chicken, processed products and animal feed.

Leased Operating Units

The table below lists Sadia's leased operating units and their principal activities

State	City	Principal activity
RS	Lajeado	Raising and slaughtering poultry and animal feed
RS	Garibaldi	Raising and slaughtering poultry and animal feed

Distribution and Commercial Centers

The table below lists Sadia's distribution and commercial centers and the corresponding region of activity:

State	**City**	**Region of Activity**
AM	Manaus	North Region
BA	Salvador	Northeast Region
CE	Fortaleza	Northeast Region
DF	Brasília	Federal District
MG	Belo Horizonte	Southeast Region
MS	Campo Grande	Central region
MT	Várzea Grande	Central Region
PA	Belém	North Region
PE	Recife	Northeast Region
PR	Colombo	South Region
PR	Ponta Grossa	South Region
RJ	Rio de Janeiro	Southeast Region
RS	Porto Alegre	South Region
SC	Itajaí	South Region
SP	Sao Paulo	Southeast Region
SP	Jundiaí	Southeast Region and Sao Paulo State Region
ES	Vitória	Southeast Region

Production Capacity

Sadia's consolidated production capacity is as follow

	Production Capacity		
	2005 **Capacity**	**Production**	**2004** **Production**
Poultry Slaughtering (Million heads/year)	740.1	650.1	572.9
Hog Slaughtering (Million heads/year)	3.9	3.8	3.5
Processed Products (thousands of tons/year)	1,040.0	695.4	666.7
Animal Feed (thousands of tons/year)	**5,515.44**	4,647	4,169.1

Environmental issues affecting the Company's activities

As a poultry and hog livestock and slaughtering company, Sadia's activity impacts on environmental issues, especially related to water resources pollution, animal treatment and deforestation. However, the Company takes all measures to comply with the Brazilian environmental regulations.

As a way of ensuring the sustainability of its activities, Sadia has strict policies for reducing consumption of water and uses biomass to substitute fuel oil and gas to generate thermal energy. All its units have water resources treatment facilities to avoid the contamination of water tables and rivers near the units. The Company also strictly supervises the activities taken by the poultry and hog outgrowers.

The Company utilizes firewood in its productive process under the Brazilian environmental legal requirements and authorized by the IBAMA (Instituto Brasileiro do Meio Ambiente e dos Recursos Naturais Renovaveis), the Brazilian Environmental and Renewable Natural Resources Institute. This firewood comes from the Company's owned forest land and from third parties, and is used as fuel to warm up the boilers.

The only environmental requirement for Sadia related to its owned forest land is to maintain at least 20% of the Company's forest land as native forest. Sadia is in compliance with such requirement.

Moreover, the Company has a program for being self sufficient in firewood, maintaining forest land for all of its manufacturing units. These areas total 17 thousand hectares and supply 65% of the Company's current firewood requirements.

ITEM 4A. UNRESOLVED SEC STAFF COMMENTS

The Company has no unresolved comments from the staff of the U.S. Securities and Exchange Commission in respect of its periodic reports under the Exchange Act.

ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS

The following discussion should be read in conjunction with the Company's consolidated financial statements and notes thereto, and other financial information included elsewhere in this annual report.

Discussion on Critical Accounting Policies

Critical accounting policies are those that are considered important, complex or subjective by the Company's management to the understanding of the Company's financial condition and results, as well as estimates about the effect of matters that are uncertain.

Allowance for Doubtful Accounts

The collectibility of accounts receivable is based on a combination of factors. In circumstances where management is aware of a specific customer’s inability to meet its financial obligations, a specific allowance against amounts due is recorded to reduce the net recognized receivable to an amount that is likely to be collected. In addition, an allowance is recorded based on the length of time receivables are past due and historical experiences. In addition, Sadia records a provision in light of past collection and write-off experience, as well as when significant payment delays occur and the Company believes that it may not receive payment in full.

Given the assumptions involved, such as the financial situation of the Company’s debtors, commercial and economic trends, allowances for doubtful accounts are subject to uncertainty and may be revised upward or downward depending on the actual performance of an account receivable.

Depreciation and Amortization

Sadia recognizes expenses related to the depreciation and amortization of its property, plant and equipment and breeding stock based on the straight-line and estimated production cost methods, respectively. The useful life of assets and estimates for production is reviewed periodically based on existing facts and circumstances. The determination of useful lives and estimates for production requires considerable judgment and is inherently uncertain, due to changes in technology and industry competition, which could cause early obsolescence of the property, plant and equipment. If Sadia is required to materially change the assumptions used, its depreciation and amortization expense, obsolescence write-off and the net book value of property, plant and equipment could be materially different.

Impairment of Long-Lived Assets

Sadia periodically assesses the need to perform impairment tests of long-lived assets (or asset groups) based on various indicators such as the level of business profitability and technological developments. When necessary, upon the occurrence of any negative triggering event such as a significant loss in market value of a property, plant and equipment or significant adverse change in the extent or manner in which a long-lived asset is being used, cash flow studies are prepared to determine if the accounting value of the property, plant and equipment is recoverable through the profitability resulting from its business. In order to estimate future cash flows, Sadia makes various assumptions and estimates. These assumptions and estimates can be influenced by different external and internal factors, such as economic and industry trends, interest rates, foreign exchange rates, changes in the business strategies and in the type of products offered to the market.

Contingencies

Sadia establishes provision for contingencies on its balance sheet when it determines, taking into consideration the opinion of its legal advisors, that a loss is probable, in one of the labor, tax or civil cases to which the Company is party. Sadia continuously evaluates the estimates and assumptions used to establish the provision for contingencies based on relevant facts and circumstances that may have a material effect on the result of operations and stockholders' equity. Even though management believes that the provisions are presently adequate, the establishment of provisions for judicial proceedings involves estimates that can result in the final amount being different than the provisions as a result of uncertainties that are inherent to the establishment of the provision. In case the amount of provisions for contingencies is lower than the amount actually due, an increase in provisions would be necessary.

Deferred Tax Assets

Sadia recognizes deferred tax assets and liabilities which do not expire, arising from tax loss carry-forwards, temporary add-backs and other procedures. Sadia periodically reviews the deferred tax assets for recoverability and establishes a valuation allowance, as required, based on historical taxable income, projected future taxable income, and the expected timing of the reversals of existing temporary differences. In the event the Company or one of its subsidiaries operates 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 time period within which the underlying temporary differences become taxable or deductible, Sadia evaluates the need to establish a valuation allowance against all or a significant portion of the Company's deferred tax assets, resulting in an increase in the effective tax rate, thereby decreasing net income. If Sadia determines that it can realize a deferred tax in excess of its net recorded amount, it decreases the valuation allowance, thereby increasing net income. Significant management judgment is required in determining any valuation allowance. The principal uncertainty relates to the likelihood of future taxable income from the subsidiary that generated the deferred tax asset. A change in the Company's projections of profitability could result in the need to record a valuation allowance against deferred tax assets, resulting in a negative impact of future results.

Pension Benefits

Sadia accounts for its defined pension plan using actuarial models. These models use an attribution approach, which assumes employees render services over their service lives on a relatively smooth basis and also presumes that the income statement effects of pension benefit plans should follow the same pattern. Sadia accounts for its retirement plan based on actuarial recommendations following the applicable laws, income tax regulations, as well as in accordance with the plan's rules.

Net pension income or expense is determined using assumptions as of the beginning of each year. These assumptions are established at the end of the prior fiscal year and include expected long term return rates of the plan assets, discount rates and compensation rate increases. The actual future amounts and experience related to these assumptions will determine whether Sadia has created sufficient reserves for accrued pension costs.

Recently Issued Accounting Standards

In December 2004, the FASB issued FASB Statement No.151, Inventory Costs, which clarifies the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material (spoilage). Under this Statement, such items will be recognized as current-period charges. In addition, the Statement requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. The application of this Statement is required after January 1, 2006. The Company anticipates no significant impact on its financial statements by applying Statement 151.

In December 2004, the FASB issued FASB Statement No. 153, Exchanges of Nonmonetary Assets, which eliminates an exception in APB 29 for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. The application of this Statement is required after January 1, 2006. The Company anticipates no significant impact on its financial statements by applying Statement 153.

In May 2005, the FASB issued SFAS No.154, "Accounting Changes and Error Corrections" ("SFAS 154") which replaces Accounting Principles Board Opinions No. 20 "Accounting Changes" and SFAS No. 3, "Reporting Accounting Changes in Interim Financial Statements—An Amendment of APB Opinion No. 28." SFAS 154 provides guidance on the accounting for and reporting of accounting changes and error corrections. It establishes retrospective application, or the latest practicable date, as the required method for reporting a change in accounting principle and the reporting of a correction of an error. SFAS 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005.

In February 2006, the FASB issued SFAS No.155, “Accounting for Certain Hybrid Financial Instruments,” an amendment to SFAS No.133 and No.140. The primary objectives of this Statement with respect to SFAS No.133 are to simplify accounting for certain hybrid financial instruments by permitting fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation and eliminate the interim guidance in Statement No.133 Implementation Issue No D1, “Application of FAS No.133 to beneficial Interests in Securitized Financial Assets,” which provides that beneficial interests in securitized financial assets are not subject to the provisions of SFAS No.133. The primary objective of this Statement with respect to SFAS No.140 is to eliminate a restriction on the passive derivative instruments that a qualifying special-purpose entity (SPE) may hold. This Statement is effective for all financial instruments acquired or issued after the beginning of an entity’s first fiscal year that begins after September 15, 2006. Management does not expect the adoption of this Statement to have an impact on the Company’s consolidated financial statements.

Recently Adopted Accounting Standards

In December 2004, FASB issued the FASB Statement No.123 (revised 2004), Share-Based Payment, which addresses the accounting for transactions in which an entity exchanges its equity instruments for goods or services, with a primary focus on transactions in which an entity obtains employee services in share-based payment transactions. This Statement is a revision of the Statement 123 and supersedes APB Opinion No. 25, Accounting for Stock Issued to Employees, and it is related to the implementation guidance. This Statement was early adopted by the Company in 2005. (See note 15)

In March 2005, the FASB issued FIN 47, "Accounting for Conditional Asset Retirement Obligations, an interpretation of FASB Statement No.143" ("FIN 47"), which requires an entity to recognize a liability for the fair value of a conditional asset retirement obligation when incurred if the liability's fair value can be reasonably estimated. FIN 47 is effective for fiscal years ending after December 15, 2005. The Company did not have any impact on applying FIN 47.

Brazilian Economic Environment

The Company’s results of operations and financial condition are dependent on Brazil's general economic condition and particularly on (i) economic growth and inflation and their impact on people’s purchasing power, (ii) financing costs and the availability of financing, and (iii) exchange rates between Brazilian and foreign currencies. The following table sets forth Brazilian Gross Domestic Product (GDP) growth, inflation and the devaluation of Brazilian currency against the U.S. dollar and interest rate changes for the periods shown.

Brazilian Selected Economic Indicators

	2005	**2004**	**2003**	**2002**
Real GDP Growth(%)a	2.28	4.94	0.54	1.93
Inflation(%)?	1.21	12.41	8.71	25.31
US$ / R$ Exchange Ratel	2.3407	2.6544	2.8892	3.5333
TJLP(%)l	9.8	9.8	11.0	10.0

(1) Source:Ipeadata

(2) IGPM, source: Economática

(3) Long-Term Interest Rate

The Brazilian economy has been affected by interventions on the part of the government, which has made repeated changes in its monetary, credit, tariff and other policies, in order to influence the direction of the national economy. The changes in policies involving foreign exchange and tax rates could have a significant impact on the Company´s business and operating results, in the same way as inflation, currency devaluation, social instability and other political, economic and diplomatic issues, and the reaction of the Brazilian government to these issues.

Inflation and Real Plan Effects

Inflation has traditionally had a negative effect on the Brazilian economy in general in past years, and on the Company´s profitability and operating results in particular. In an attempt to control inflation, the government has at times imposed wage and price controls, and reduced its spending. Inflation and the measures adopted by the government, combined with public speculation about its future decisions, have also contributed to periods of uncertainty in the economy, as well as to increased volatility in the Brazilian securities markets. In addition, the government’s desire to control inflation and reduce budget deficits may cause it to take actions that slow Brazilian economic growth.

After the implementation of the *Real* Plan, which was based on an exchange rate anchor (*reais* x U.S. dollar), inflation rates declined and stabilized at low levels. This new economic environment increased the purchasing power of part of the population, which was accustomed to high inflation levels and did not have access to financial instruments to reduce their monetary losses due to high inflation. Incomes rose, credit availability increased and consumption of consumer goods grew. According to the IGP-M Brazilian inflation amounted to 868.30% in 1994, 15.25% in 1995, 9.20% in 1996, 7.74% in 1997, 1.78% in 1998, 20.1% in 1999, 9.95% in 2000, 10.38% in 2001, 25.31% in 2002 8.71% in 2003, 12.41% in 2004 and 1.21% in 2005.

Exchange Rate Effects

From March 1995 until January 1999, the Brazilian Central Bank managed a semi-fixed exchange rate policy based on the establishment of an annual exchange rate fluctuation target at the beginning of each year, setting both a wide limit or “band”, and a much narrower band, in order to effect a gradual devaluation by means of this exchange rate band system. The Central Bank bought or sold U.S. dollars in the market in order to ensure that the exchange rate remained within established limits.

In an attempt to stem the increasing capital outflows and concerns about the commitment of certain state governments to the fiscal austerity proposal, on January 13, 1999, Brazilian monetary authorities halted their intervention, abandoning the system of exchange rate bands, and allowed the *real*’s value to be determined by the foreign exchange markets, intervening only to limit wide swings in the value of the currency.

Since then, the exchange rate market has been operating under a floating rate regime and the Central Bank has implemented an inflation target policy, using local interest rates to adjust demand. A negative side-effect of this policy has been high interest rate levels, increasing cost of capital to the company and raising uncertainty in the financial markets about the capacity of Brazil to pay its debts, increasing the sovereign risk.

Although Sadia uses *reais* as its functional currency, a relevant portion of its assets, liabilities and revenues are dollar denominated. In December 2005, 49.5% of the Company´s gross revenues were mainly collected in foreign currency, coming from export proceeds, corresponding to R$4,076 million.

Considering that Sadia has subsidiaries abroad, the volatility of the *real* creates foreign exchange gains and losses, which are included in the Company’s foreign currency exchange gain (loss), net account in results of operations. In 2005, on a consolidated basis, the Company recorded foreign exchange gains (including gains from foreign currency swaps) of R$290.7 million compared to R$72.7 million in 2004.

A. Operating Results

The following table summarizes certain selected financial data derived from the Company´s statements of income, expressed as percentages of net operating revenue, for the periods indicated, as shown.

	Consolidated Income Statement Years Ended December 31, 2005, 2004 and 2003 (%)		
	2005	**2004**	**2003**
Net operating revenue	**100.0**	**100.0**	**100.0**
Cost of goods sold	(72.8)	(70.3)	(72.3)
Gross profit	**27.2**	**29.7**	**27.7**
Operating expenses:			
Selling	(17.0)	(18.7)	(18.0)
General and administrative	(1.1)	(0.9)	(1.1)
Other operating income (expenses), net	0.2	0.3	(0.7)
Total operating expenses	(17.9)	(19.3)	(19.8)
Operating income	**9.3**	**10.4**	**7.9**
Interest expense	(4.3)	(5.5)	(8.9)
Interest income and other, net	3.4	4.1	9.0
Foreign currency exchange gain, net	0.7	0.6	1.2
Income before income taxes, equity income of investees and minority interest	**9.2**	**9.6**	**9.3**
Income tax benefit (expense)			
Current benefit (expense)	(0.7)	(0.5)	(0.8)
Deferred tax benefit (expense)	(0.2)	(1.0)	0.8
Total income tax	**(0.9)**	**(1.6)**	**0.0**
Income before equity income of investees and minority interest	8.2	8.0	9.3
Net income	**8.2**	**8.0**	**9.3**

The following table sets forth components of Sadia´s cost of goods sold, expressed as a percentage of total cost of goods sold for 2005, 2004 and 2003:

	Composition of Cost of Goods Sold (%) December 31,

	2005	**2004**	**2003**
Raw Materials	76	78	78
Labor	12	12	11
Depreciation	3	2	3
Other	9	9	9
Total cost of goods sold	**100**	**100**	**100**

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Consolidated Income Statement
Years Ended December 31, 2005, 2004, 2003, 2002 and 2001
(R$ Million)

	2005	**2004**	**2003**	**2002**	**2001**
Gross operating revenue	**8,327.4**	**7,117.3**	**5,717.5**	**4,654.8**	**3,977.1**
Value-added tax on sales	(914.2)	(880.0)	(535.3)	(0.4)	(0.3)
Sales deductions	(95.3)	(128.1)	(100.5)	(98.4)	(81.4)
Net operating revenue	**7,317.8**	**6,109.2**	**5,081.7**	**4,139.1**	**3,602.5**
Cost of goods sold	(5,324.4)	(4,292.7)	(3,673.0)	(2,903.2)	(2,322.7)
Gross profit	**1,993.5**	**1,816.6**	**1,408.7**	**1,235.9**	**1,279.8**
Operating expenses:					
Selling	(1,245.9)	(1,144.5)	(916.7)	(828.7)	(720.8)
General and administrative	(81.0)	(52.5)	(54.2)	(49.1)	(54.0)
Other operating income (expenses), net	14.3	15.4	(36.8)	(12.8)	(17.1)
Total operating expenses	(1,312.6)	(1,181.5)	(1,007.7)	(890.6)	(791.9)
Operating income	**680.9**	**635.0**	**401.0**	**345.3**	**487.9**
Interest expense	(311.6)	(336.8)	(450.2)	(317.8)	(201.2)
Interest income and other, net	248.0	249.8	459.8	266.5	144.6
Foreign currency exchange gain, net	53.4	39.1	61.0	2.7	(171.4)
Income before income taxes, equity income of investees and minority interest	**670.7**	**587.1**	**471.5**	**296.7**	**259.9**
Income tax benefit (expense)					
Current benefit (expense)	(52.0)	(33.0)	(39.1)	34.6	(38.9)
Deferred tax benefit (expense)	(16.4)	(63.1)	40.1	(46.8)	(12.2)
Total income tax	**(68.4)**	**(96.1)**	**1.0**	**(12.2)**	**(51.1)**
Income before equity income of investees and minority interest	602.2	491.0	472.6	284.6	208.8
Equity income (loss) of investees	1.2	(1.4)	0.4	(0.7)	0.0
Minority interest	(0.2)	(0.1)	0.3	0.3	0.4
Income (loss) before cumulative effect of accounting change	603.3	489.5	473.3	284.3	209.3
Cumulative effect of accounting change, net of tax	-	-	-	-	(5.8)
Net income	**603.3**	**489.5**	**473.3**	**284.3**	**203.5**

SADIA S.A.

CONSOLIDATED BALANCE SHEET

Years ended December 31,2005, 2004, 2003, 2002, and 2001

(In thousands of *reais* - R$)

	2005	**2004**	**2003**	**2002**	**2001**
Cash and cash equivalents and investments in debt and held-to-maturity securities	2,574,996	1,917,192	1,957,753	1,249,783	346,354