commercial market may be carried out only through banks authorized to buy and sell currency in that market. In both markets, rates are freely negotiated but may be strongly influenced by Central Bank intervention

Between March 1995 and January 1999, the Brazilian Central Bank permitted the gradual devaluation of the *real* against the U.S. dollar pursuant to an exchange rate policy that established a band within which the *real*/U.S. dollar exchange rate could float.

Responding to pressure on the *real*, on January 13, 1999, the Brazilian Central Bank widened the foreign exchange band and, on January 15, 1999, allowed the *real* to float. As of June 16, 2003, the commercial market rate for purchasing U.S. dollars was R$2.8508 to U.S.$1.00. See “Item 5.A—Operating and Financial Review and Prospects—Operating Results—Overview—Brazilian Economic Environment.”

The following tables show, for the periods and date indicated, certain information regarding the *real*/U.S. dollar commercial exchange rate.

	Exchange Rate of R$ per U.S.$			
	Low	**High**	**Average(1)**	**Year-End**
Year ended December 31,				
1998	1.1165	1.2087	1.1611	1.2087
1999	1.2078	2.1647	1.8158	1.7890
2000	1.7234	1.9847	1.8295	1.9554
2001	1.9357	2.8007	2.3522	2.3204
2002	2.2709	3.9552	2.9309	3.5333

Source: Central Bank.
(1) Represents the average of the exchange rates on the last day of each month during the relevant period.

	Exchange Rate of R$ per U.S.$	
	High	**Low**
Month		
December 2002	3.7980	3.4278
January 2003	3.6623	3.2758
February 2003	3.6580	3.4930
March 2003	3.5637	3.3531
April 2003	3.3359	2.8898
May 2003	3.0277	2.8653

Source: Central Bank.

C. Capitalization and Indebtedness

Not applicable.

D. Reasons for the Offer and Use of Proceeds

Not applicable.

E. Risk Factors

This section is intended to be a summary of more detailed discussions contained elsewhere in this annual report. The risks described below are not the only ones we face. Additional risks may impair our business operations. Our business, results of operations or financial condition could be harmed if any of these risks materializes and, as a result, the trading price of the ADSs could decline.

Risks Relating to Brazil

The Brazilian government has exercised, and continues to exercise, significant influence over the Brazilian economy. Brazilian political and economic conditions have a direct impact on our business, operations and the market price of our preferred shares and our ADSs.

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

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

At the end of 2002, Brazil elected a new president from the Workers Party, Luís Inácio Lula da Silva, known as Lula. In the period leading up to, and subsequent to, his election there was substantial uncertainty relating to the policies that the new government might pursue, including the potential implementation of macroeconomic policies that could differ significantly from those of the prior administration. This uncertainty resulted in a loss of confidence in the Brazilian capital markets, including the steady devaluation of the *real* against the U.S. dollar in that period. Although the new government has not departed in any material way from previous policy, it may be premature to evaluate the way in which investors and the capital markets will react, whether these policies will continue and whether they will be effective. Any substantial negative reaction to the policies of the Brazilian government could adversely affect our business, operations and the market price of our preferred shares and ADSs.

Inflation and certain government measures to curb inflation may have adverse effects on the Brazilian economy, the Brazilian securities market and/or our business and operations.

Brazil has historically experienced extremely high rates of inflation. Inflation and certain of the government's measures taken in the attempt to curb inflation have had significant negative effects on the Brazilian economy. Since 1994, Brazil's inflation rate has been substantially lower than in previous periods. However, inflationary pressures persist, and actions taken in an effort to curb inflation, coupled with public speculation about possible future governmental actions, have contributed to economic uncertainty in Brazil and heightened volatility in the Brazilian securities market. Brazil's general price index, or the IGP-DI, reflected inflation rates of 26.4% in 2002, 10.4% in 2001 and 9.9% in 2000. If Brazil experiences significant inflation rates, we may be unable to increase service tariffs and prices charged to our customers in amounts that are sufficient to cover our increasing operating costs, and our business may be adversely affected as a consequence.

Fluctuations in the value of the real against the value of the U.S. dollar may adversely affect our ability to pay U.S. dollar-denominated or U.S. dollar-linked obligations and could lower the market value of our preferred shares and ADSs.

The Brazilian currencies have historically experienced frequent devaluations. The *real* devalued against the U.S. dollar by 9.3% in 2000 and by 18.7% in 2001. During 2002, the *real* continued to undergo significant devaluation due in part to the political uncertainty in connection with the elections and the global economic slowdown. In 2002, the *real* devalued against the U.S. dollar by 52.3%. See “Item 3.A—Selected Financial Data—Exchange Rates” for more information on exchange rates.

As of December 31, 2002, we had R$4.6 billion in total debt, of which R$4.2 billion was denominated in foreign currencies, especially in U.S. dollars. As of December 31, 2002, we had currency hedges in place to cover 100% of our foreign currency denominated debt. Significant costs relating to our network infrastructure are payable or linked to payment by us in U.S. dollars. However, other than income derived from hedging transactions, all of our revenues are generated in *reais*. To the extent that the value of the *real* decreases relative to the U.S. dollar, our debt becomes more expensive to service and it becomes more costly for us to import the technology and the goods that are necessary to operate our business.

Deterioration in economic and market conditions in other countries, especially emerging market countries, may adversely affect the Brazilian economy and our business.

The market for securities issued by Brazilian companies is influenced by economic and market conditions in Brazil and, to varying degrees, market conditions in other Latin American and emerging market countries. Although economic conditions are different in each country, the reaction of investors to developments in one country may cause the capital markets in other countries to float. Developments or conditions in other emerging market countries have at times significantly affected the availability of credit in the Brazilian economy and resulted in considerable outflows of funds and declines in the amount of foreign currency invested in Brazil.

For example, in 2001, after prolonged periods of recession followed by political instability, Argentina announced that it would no longer continue to service its public debt. In order to address the deteriorating economic and social crisis, the Argentine government abandoned its decade-old fixed dollar-*peso* exchange rate, allowing the *peso* to float to market rate levels. In 2002, the Argentine *peso* experienced a 236% devaluation against the U.S. dollar. The situation in Argentina may have negatively affected investors’ perceptions towards Brazilian securities.

The recent political crisis in Venezuela may also influence investors’ perception of risk in Brazil. Although market concerns that similar crises would ensue in Brazil have not become a reality, the volatility in market prices for Brazilian securities increased in 2001 and 2002. If market conditions in Argentina and Venezuela continue to deteriorate, they may adversely affect our ability to borrow funds at an acceptable interest rate or to raise equity capital, when and if there is a need. Accordingly, adverse developments in Argentina, Venezuela or in other emerging market countries could lead to a reduction in both demand for, and the market price for the preferred shares and ADSs.

Risks Relating to the Brazilian Telecommunications Industry and Us

Extensive government regulation of the telecommunications industry and our concession may limit our flexibility in responding to market conditions, competition and changes in our cost structure or impact our tariffs.

Our business is subject to extensive government regulation. Anatel, which is the primary telecommunications industry regulator in Brazil, regulates, among other things:

- regulations;
- licensing and concessions;
- tariffs;
- competition;
- telecommunications resource allocation;

- service standards;
- technical standards;
- quality standards;
- interconnection and settlement arrangements; and
- universal service obligations.

The initial monthly fees and usage fee tariffs for our services were initially determined in our concession agreement which also sets the annual price adjustment. We derive a substantial portion of our revenues from services subject to this price adjustment. The method of price adjustment is basically a price cap. Anatel applies annually a price index correction that reflects the inflation index of the period (in accordance with the concession agreement) and a productivity factor (in accordance with the concession agreement) to our local and long distance tariffs. Anatel has complied with the tariff range set by the concession agreement. However, we cannot assure you that our business or results of operations will not be adversely affected by any government-mandated tariff adjustments in the future.

We operate our business under a concession from the Brazilian government. According to the terms of the concession, we are obligated to meet certain requirements and to maintain minimum quality and service standards. Failure by us to comply with the requirements of our concession may result in the imposition of fines or other government actions, including the termination of our concession. Any partial or total revocation of our concession would have a material adverse effect on our financial condition and results of operations.

We face substantial competition that may reduce our market share and harm our financial performance.

There is substantial competition in the telecommunications industry. We compete not only with fixed-line telecommunications companies, but also with companies that provide wireless telecommunications services and Internet access services.

We expect competition to intensify as a result of the entrance of new competitors and the rapid development of new technologies, products and services. We cannot predict which of many possible future technologies, products or services will be significant to the maintenance of our competitive position or what expenditures will be required to develop and provide these technologies, products or services. Our ability to compete successfully will depend on marketing as well as on our ability to anticipate and respond to various competitive factors affecting the industry, including new services that may be introduced, changes in consumer preferences, demographic trends, economic conditions and discount pricing strategies by our competitors. Recently, the entry of new competitors in our concession region, together with an uncertain regulatory scenario resulting from controversies in the interpretation of certain interconnection rules, may generate imbalances in traffic and may negatively impact our interconnection revenues. To the extent that we do not keep pace with technological advances or fail to timely respond to changes in competitive factors in our industry, we could lose market share or experience a decline in our revenue and net income.

The industry in which we conduct our business is subject to rapid technological changes and these changes could have a material adverse effect on our ability to provide competitive services.

The telecommunications industry is subject to rapid and significant technological changes. Our future success depends, in part, on our ability to anticipate and adapt in a timely manner to technological changes. We expect that new products and technologies will emerge and that existing products and technologies will be further developed.

The advent of new products and technologies could have a variety of consequences for us. These new products and technologies may reduce the price of our services by providing lower-cost alternatives, or they may