Prumo Participações e Investimentos S.A. (A Privately Held Company)

Independent Auditors' Report
on the financial statements
December 31, 2017 and 2016
(A free translation of the original report in Portuguese containing financial statements prepared in accordance with accounting practices adopted in Brazil)

Contents

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Independent auditors' report on the financial statements

(A free translation of the original report in Portuguese containing financial statements prepared in accordance with accounting practices adopted in Brazil)

To the Managers and Shareholders of
Prumo Participações e Investimentos S.A.
Rio de Janeiro – RJ

Opinion
We have audited the financial statements of Prumo Participações e Investimentos S.A. ("the Company"), which comprise the balance sheet as at December 31, 2017, the statements of income and other comprehensive income, changes in shareholders´ equity and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Prumo Participações e Investimentos S.A. ("the Company") as at December 31, 2017, and of its financial performance and its cash flows for the year then ended in accordance with Accounting Practices Adopted in Brazil.

Basis for Opinion
We conducted our audit in accordance with Brazilian and International Standards on Auditing. Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Financial Statements section of our report. We are independent of the Company in accordance with the relevant ethical requirements included in the Accountant Professional Code of Ethics ("Código de Ética Profissional do Contador") and in the professional standards issued by the Brazilian Federal Accounting Council ("Conselho Federal de Contabilidade"), and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Responsibilities of Management and Those Charged with Governance for the Financial Statements
Management is responsible for the preparation and fair presentation of the financial statements in accordance with Accounting Practices Adopted in Brazil and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

Auditors' Responsibilities for the Audit of the Financial Statements
Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Brazilian and international standards on auditing will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Brazilian and international standards on auditing, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with management among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

Rio de Janeiro, March 29, 2018

KPMG Auditores Independentes
CRC SP-014428/O-6 F-RJ

Original in Portuguese signed by
Luis Claudio França de Araujo
Accountant CRC RJ-091559/O-4

Prumo Participações e Investimentos S.A.

Balance sheets as of December 31, 2017 and 2016

(In thousands of reais)

	Note	2017	2016
Assets			
Current			
Cash and cash equivalents	4	2,146	1,556
Recoverable taxes	5	4,294	9,114
Income taxes and social contribution recoverable	5	25,692	18,835
Loan with related parties	7	61,483	50,280
Other receivables		9	-
Total current assets		**93,624**	**79,785**
Non-current			
Escrow account	6	-	55,405
Recoverable taxes	5	2,713	10,654
Loans with related parties	7	738,405	844,668
Equity investment	8	333,297	295,326
Total noncurrent assets		**1,074,415**	**1,206,053**
Total assets		**1,168,039**	**1,285,838**

See the accompanying notes to the financial statements.

Prumo Participações e Investimentos S.A.

Balance sheets as of December 31, 2017 and 2016

(In thousands of reais)

	Note	2017	2016
Liabilities			
Current			
Trade payables		6	200
Loans and financing	9	16,807	30,746
Taxes payable	11	6,162	538
Income and social contribution taxes payable	11	2,561	20,217
Dividends payable		-	36,678
Other accounts payable		25	-
Total current liabilities		**25,561**	**88,379**
Non-current			
Loans and financing	9	322,191	422,210
Deferred taxes	10	32,610	35,785
Total noncurrent liabilities		**354,801**	**457,995**
Shareholders' equity	12		
Share capital		753,164	606,424
Capital reserve		14,285	14,310
Profit reserves		20,516	117,758
Equity appraisal adjustment		(288)	972
Total shareholders' equity		**787,677**	**739,464**
Total liabilities and shareholders' equity		**1,168,039**	**1,285,838**

See the accompanying notes to the financial statements.

Prumo Participações e Investimentos S.A.

Statements of income
Years ended December 31, 2017 and 2016
(In thousands of reais)

	Note	2017	2016
Operating expenses			
Administrative expenses		(269)	(253)
Financial income	13		
Financial income		147,673	244,711
Financial expenses		(117,333)	(77,193)
		30,340	**167,518**
Equity in income of associates	8	39,231	44,017
Net income before tax		**69,302**	**211,282**
Current income and social contribution taxes	11	(2,561)	(20,217)
Deferred income and social contribution taxes	11	3,174	(36,629)
Net income for the year		**69,915**	**154,436**

See the accompanying notes to the financial statements.

Prumo Participações e Investimentos S.A.

Statements of comprehensive income
Years ended December 31, 2017 and 2016
(In thousands of reais)

	2017	2016
Net income for the year	**69,915**	**154,436**
Items that can be subsequently reclassified to profit or loss		
Hedge Instrument, net of tax - accounting reflection	(1,260)	972
Total comprehensive income for the year	**68,655**	**155,408**

See the accompanying notes to the financial statements.

Prumo Participações e Investimentos S.A.

Statements of changes in shareholders' equity
Years ended December 31, 2017 and 2016
(In thousands of reais)

			Capital reserve						
	Capital	**Capital contribution (*)**	**Advance for future capital increase**	**Legal reserve**	**Retention reserve**	**Equity appraisal adjustment**	**Additional dividends proposed**	**Retained earnings**	**Total shareholders' equity**
Balance at January 1, 2016	**561,421**	**14,285**	**7,650**	**-**	**1,416**	**-**	**20,176**	**-**	**604,948**
Net income for the year	-	-	-	-	-	-	-	154,436	**154,436**
Advance for future capital increase	-	-	9,061	-	-	-	-	-	**9,061**
Capital increase through conversion of AFAC	16,686	-	(16,686)	-	-	-	-	-	-
Legal reserve	-	-	-	7,722	-	-	-	(7,722)	-
Minimum mandatory dividends	-	-	-	-	-	-	-	(36,678)	**(36,678)**
Additional dividends proposed	-	-	-	-	-	-	110,036	(110,036)	-
Capital increase with profits reserve	28,317	-	-	-	(1,416)	-	(20,176)	-	**6,725**
Financial instrument hedge - Ferroport	-	-	-	-	-	972	-	-	**972**
Balance at December 31, 2016	**606,424**	**14,285**	**25**	**7,722**	**-**	**972**	**110,036**	**-**	**739,464**
Net income for the year	-	-	-	-	-	-	-	69,915	**69,915**
Capital increase through conversion of AFAC	25	-	(25)	-	-	-	-	-	-
Capital increase through conversion of proposed dividends	110,036	-	-	-	-	-	(110,036)	-	-
Capital increase through conversion of dividends payable	36,679	-	-	-	-	-	-	-	**36,679**
Legal reserve	-	-	-	3,496	-	-	-	(3,496)	-
Profit reserves	-	-	-	-	9,298	-	-	(9,298)	-
Interim dividends	-	-	-	-	-	-	-	(25,318)	**(25,318)**
Interest on shareholders' equity	-	-	-	-	-	-	-	(31,803)	**(31,803)**
Financial instrument - Ferroport hedge	-	-	-	-	-	(1,260)	-	-	**(1,260)**
Balance at December 31, 2017	**753,164**	**14,285**	**-**	**11,218**	**9,298**	**(288)**	**-**	**-**	**787,677**

(*) Capital contribution in the amount of R$ 14,285 deriving from transfer of Ferroport shares held by Prumo.

See the accompanying notes to the financial statements.

Prumo Participações e Investimentos S.A.

Statements of cash flows
Financial years ended December 31, 2017 and 2016
(In thousands of reais)

	2017	**2016**
Cash flows from operating activities		
Net income before tax	69,302	211,282
Expenses (income) not affecting cash:		
Equity in income of associates	(39,231)	(44,017)
Monetary variance and interest	(55,719)	(190,077)
Amortization of transaction costs	10,319	10,321
	(15,329)	**(12,491)**
(Increase) decrease in assets and increase (decrease) in liabilities:		
Recoverable taxes	(4,467)	4,384
Income tax on loan	10,422	(33,923)
Escrow account	-	57,321
Trade payables	(194)	200
Taxes payable	(19,363)	(913)
Other assets and liabilities	16	-
Net cash provided by (used in) operating activities	**(28,915)**	**14,577**
Cash flows from investment activities		
Loans received from related parties	192,176	176,591
Net cash provided by investment activities	**192,176**	**176,591**
Cash flows from financing activities		
Advance for future capital increase	-	9,061
Dividends	(25,318)	-
Interest on shareholders' equity (“JCP")	(27,033)	-
Escrow account	57,926	-
Loans settled with third parties	(128,990)	(143,038)
Interest paid	(39,256)	(52,508)
Transaction cost – with third parties	-	(6,474)
Net cash used in financing activities	**(162,671)**	**(192,959)**
Increase (decrease) in cash and cash equivalents	**590**	**(1,791)**
Cash and cash equivalents at beginning of year	1,556	3,347
Cash and cash equivalents at end of year	2,146	1,556
Increase (decrease) in cash and cash equivalents	**590**	**(1,791)**

See the accompanying notes to the financial statements.

(In thousands of Reais, unless stated otherwise)

1. Reporting entity

Prumo Participações e Investimentos S.A. ("Prumo Participações" or "Company"), was incorporated on January 06, 2015 in order to acquire interests in other companies as a shareholder or partner, and to represent Brazilian and foreign companies regardless of their core activity. The Company carries out its operations via the joint venture Ferroport ("joint subsidiary") with Anglo American Participações Minério de Ferro Ltda. ("Anglo American").

Ferroport occupies a 300-hectare area at Porto do Açu to process, handle and store iron ore and is the co-owner of an offshore structure (T1) consisting of an access pier, approach channel, breakwater and two berths for loading iron ore. It began exporting on October 25, 2014, and in 2017 it shipped a total of 16,508 thousand tonnes of iron ore, in ninety-eight ships (95 Capesizes, 2 BabyCape and 1 Panamax).

2. Group companies

	Country	Equity interest 2017	Equity interest 2016
Direct joint subsidiary:			
Ferroport	Brazil	50.00%	50.00%

3. Basis of presentation, preparation of the financial statements and significant accounting practices

a) Statement of compliance

The financial statements were prepared in accordance with accounting practices adopted in Brazil (“BR GAAP”).

Authorization for the conclusion of the preparation of these financial statements was given by Management on March 29, 2018. These financial statements consider subsequent events to be events that could have an impact up to the reporting date.

The accounting policies described in detail below have been applied consistently to the financial statements of the Company's subsidiaries.

b) Basis of preparation

The financial statements have been prepared on the historical cost basis, except for certain financial instruments which have been measured at fair value through profit and loss.

c) Functional and presentation currency

These financial statements are reported in Reais, which is the Company’s functional currency.

d) Cash and Cash Equivalents

Cash equivalents are held for the purpose of meeting short-term cash commitments rather than for investment or other purposes. The Company classifies cash equivalents as short-term investments maturing within three months or less, and subject to an insignificant risk of impairment.

e) Financial instruments

(i) Financial assets

Financial assets are classified as financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, available-for-sale financial assets. The Group determines the classification of its financial assets at initial recognition, when it becomes a party to the contractual provisions of the financial instrument. The Company does not have financial assets classified as investments held-to-maturity or available-for-sale as of December 31, 2017.

3. Basis of presentation, preparation of the financial statements and significant accounting practices--Continued

e) Financial instruments--Continued

(i) Financial assets---Continued

Financial assets are recognized initially at fair value plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs.

Financial assets and liabilities are subsequently measured according to their classification, which can be as follows:

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, these financial assets are recorded at amortized cost at the effective interest method, minus any impairment. The amortized cost calculation takes into account any discounts or premiums upon acquisition, rates or other costs incurred. Amortization by the effective interest method is included in the financial revenue of the income statement. As of December 31, 2017, loans and receivables comprise loans and financing receivable from and payable to related-party and third parties.

Impairment of financial assets at amortized cost

Prumo Group first assesses whether evidence of impairment exists individually for each financial asset. If there is objective evidence of impairment, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding expected future credit losses that have not yet been incurred). The present value of estimated future cash flows is discounted at the financial asset's original effective interest rate.

Where applicable, the carrying amount of the asset is reduced by a provision and the amount of the loss is recognized in the statement of income. If, in a subsequent period, the estimated impairment loss increases or decreases due to an event occurring after the impairment was recognized, the previously recognized impairment loss is increased or decreased by adjusting an allowance account.

Derecognition of financial assets

A financial asset is derecognized where the contractual right to receive cash flows from the asset has expired and/or the Company has transferred its rights to receive the cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a "pass through" arrangement, and has transferred substantially all the risks and rewards of the asset.

3. Basis of presentation, preparation of the financial statements and significant accounting practices--Continued

e) Financial instruments--Continued

(i) Financial assets---Continued

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Company could be required to repay.

(ii) Financial liabilities

Financial liabilities are classified as "financial liabilities at fair value through profit or loss" or "other financial liabilities". The Company determines the classification of its financial liabilities at initial recognition. The Company does not have financial liabilities classified as financial liabilities at fair value through profit and loss as of December 31, 2017.

Such nonderivative financial liabilities are recognized initially at fair value less any directly attributable transaction costs. Subsequent to initial recognition, these financial liabilities are measured at amortized cost using the effective interest method.

A financial liability is derecognized when the obligation under the liability discharged, canceled or expires.

Derecognition of financial liabilities

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognized in profit or loss.

Financial assets and liabilities are offset and reported net in the balance sheet if, and only if, there is currently a legally enforceable right to set off the recognized amounts, and there is an intention to settle on a net basis, or to realize the asset and settle the liability simultaneously.

(iii) Fair value of financial instruments

The fair value of financial instruments actively traded in organized financial markets at the balance sheet date is based on quoted market prices or over-the-counter quotes, with no transaction cost deduction.

The fair value of financial instruments not traded in an active market is determined using appropriate valuation methods. Such methods may include using recent arm's length market transactions; reference to the current fair value of another similar instrument; discounted cash flow analysis or other valuation models.

3. Basis of presentation, preparation of the financial statements and significant accounting practices--Continued

f) Adjustment of assets and liabilities to present value

Long-term monetary assets and liabilities are monetarily restated and therefore adjusted to their present value. The adjustment to present value of short-term monetary assets and liabilities is calculated and only recorded if considered to have a material effect on the financial statements as a whole. Based on analyses conducted and Management's best estimates, the Company concluded that the adjustment to present value of monetary assets and liabilities is immaterial in relation to the financial statements, meaning no adjustments were made.

g) Financial income and financial expenses

Financial income and financial expenses include interest revenue, interest expenses, net foreign currency gain or loss on financial assets and financial liabilities. Interest income or expense is recognized using the effective interest method. The Company classifies interest earnings as cash flows from investment activities.

h) Income and social contribution taxes

Deferred income and social contribution taxes, when applicable, are recorded on tax losses and the negative basis of social contribution, and also on temporary differences between the tax bases of assets and liabilities and their respective carrying amounts. Deferred tax assets and liabilities are offset if there is a legal right to offset tax assets and liabilities, and they are related to income taxes levied by the same tax authority on the same entities subject to taxation. Deferred income and social contribution tax assets are reviewed annually and are reduced to the extent that realization is no longer probable, when applicable.

i) Other current and noncurrent assets and liabilities

An asset is recognized in the balance sheet when it is probable that its future economic benefits will be generated in favor of the Company and its cost or value can be reliably measured.

A liability is recognized in the statement of financial position when the Company has a present or constructive obligation as a result of a past event, and it is probable that an outflow of economic resources will be required in settlement. Provisions are recorded using best estimates of the risk involved. Long-term monetary assets and liabilities are adjusted to their present value and short-term items when the effect thereof on the financial statements as a whole is deemed material. The adjustment to present value is calculated based on the contractual cash flows and the explicit or, in certain cases, implicit interest rate on the relevant assets and liabilities.

j) Capital expenditure

The interest in the joint subsidiary is valued by the equity income method in the Company's financial statements.

Transfer of investment to Prumo Participações

The interest in the joint subsidiary Ferroport was transferred from Prumo Logística to Prumo Participações using the cost of the subsidiary's shareholders' equity on the transfer date, and does not include other adjustments.

3. Basis of presentation, preparation of the financial statements and significant accounting practices--Continued

k) Use of judgment and estimates

Judgments, estimates and assumptions are used to measure and recognize certain assets and liabilities in the Company's financial statements. These estimates took into account experience from past and current events, assumptions about future events and other objective and subjective factors.

Significant assets subject to these estimates include the impairment of deferred income and social contribution taxes. The future settlement of transactions involving these estimates may result in amounts different from those recorded in the financial statements due to the inaccuracies inherent to the determination process. The Company reviews its estimates and assumptions at least annually.

The accounting policies described in detail throughout these financial statements have been applied consistently and are being presented by the Company.

l) Pronouncements issued but not yet in force as of December 31, 2017.

Whilst encouraged by the IASB, the early adoption of standards in Brazil is not permitted by the Accounting Pronouncements Committee (CPC). The following new standards and interpretations have been issued by the IASB but are not in force for FY 2017.

IFRS 9 - Financial Instruments (CPC 48 – Financial Instruments):

CPC 48 was issued in December 2016, the equivalent of the standard IFRS 9. It replaces CPC 38 – Financial instruments: Recognition and Measurement (IAS 39) and introduces the following main changes: (i) impairment requirements for financial assets introducing the hybrid expected and incurred loss model instead of the current incurred loss model; (ii) new requirements for classifying and measuring financial assets; and (iii) an easing of hedge accounting requirements. CPC 48 is generally retrospectively applicable from January 01, 2018.

The Management of the Company and its subsidiaries have conducted a preliminary analysis of their financial assets and liabilities and did not identify any significant impacts from adopting the new standard as from January 01, 2018.

IFRS 15 - Revenue from contracts with customers (CPC 47 - Revenue from contracts with customers):

IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognized. It replaces existing revenue recognition guidance, including CPC 30 (IAS 18) Revenue, CPC 17 (IAS 11) Construction Contracts and CPC 30 Interpretation A (IFRIC 13) Customer Loyalty Programs. IFRS 15 is effective for annual periods beginning on or after 1 January 2018.

The Company made a preliminary analysis of the effects that this statement may have on the financial statements, and concluded that there will be no material changes. The Company is currently analising eventual impacts of this standard in the quarterly information.

3. Basis of presentation, preparation of the financial statements and significant accounting practices--Continued

l) Pronouncements issued but not yet in force as of December 31, 2017--Continued

IFRS 16 – Leases (no equivalent CPC has been issued yet):

IFRS 16 introduces a single, on-balance sheet lease accounting model for lessees. A lessee recognizes a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. There are optional exemptions for short-term leases and leases of low value items. Lessor accounting remains similar to the current standard – i.e. lessors continue to classify leases as finance or operating leases. IFRS 16 replaces existing leases guidance including CPC 06 (IAS 17) Leases and ICPC 03 (IFRIC 4, SIC 15 and SIC 27) additional matters regarding commercial leases. The standard is applicable from January 01, 2019.

The Company has not yet quantified the impact on its reported assets and liabilities of adoption of IFRS 16. The quantitative effect will depend on, inter alia, the transition method chosen, the extent to which the Company uses the practical expedients and recognition exemptions, and any additional leases that the Company enters into.

The new standards or modifications are not expected to have a material impact on the Prumo Group's individual and consolidated financial statements.

- Annual Improvements to IFRSs 2014-2016 Cycle – Amendments to IFRS 1 and IAS 28.
- Amendments to CPC 36 Consolidated Statements (IFRS 10) and CPC 18 Investments in Associates and Joint Ventures (IAS 28) in relation to the sale or contribution of assets between an investor and its associate or joint venture.
- ICPC 21 / IFRIC 22 Foreign Currency Transactions and Advance Consideration; and
- IFRIC 23 Uncertainty over Income Tax Treatments.

The Accounting Pronouncements Committee has not yet issued an accounting pronouncement or amended existing pronouncements related to all these new IFRS standards. As described earlier, early adoption of these IFRS is not therefore permitted for entities that disclose their financial statements in accordance with the accounting practices adopted in Brazil.

(In thousands of Reais, unless stated otherwise)

4. Cash and cash equivalents

	2017	2016
Cash and bank deposits	190	625
Cash equivalents		
CDBs	1,956	931
	2,146	**1,556**

The balance of cash and banks as of December 31, 2017 consists of current accounts and CBD investments, that are promptly convertible into a known cash amount and are subject to an insignificant risk of impairment.

5. Recoverable taxes

The recoverable taxes break down as follows:

	2017	2016
Income tax and social contribution (“IRPJ/CSLL”)	25,692	18,835
Income tax withheld at source (“IRRF”)	3,777	27
Income tax on loan (“IRPJ”)	3,230	19,741
	32,699	**38,603**
Current	29,986	27,949
Non-current	2,713	10,654

6. Escrow account

Due to the constant early amortizations through the cash rate mechanism, in June 2017 Prumo Participações received a waiver from the noteholders permitting the release of the escrow deposits for use by the company. As of December 31, 2017 there is therefore no balance of escrow deposits (R$ 55,405 as of December 31, 2016). These funds, held in US dollars in overseas accounts, were related to the financing operation conducted by the company, as described in Note 9 - Loans and Financing. The amount in cash refers to this operation and served as a guarantee for the future payment of interest and amortization of the debt. Payments were made in this period related to the principal and interest on the loan taken out by the Company.

(In thousands of Reais, unless stated otherwise)

7. Related-party transactions

Prumo group adopts practices of Corporate Governance and/or recommendations required by law, including those set down on the Regulations for the New Market (Novo Mercado). Furthermore, the Company´s Corporate Governance Policy establishes that the members of the Board of Directors must monitor and administrate any potential conflicts of interest among the executive officers, the members of the Board and the partners, in such a way as to avoid the inappropriate use of Company assets and, especially, abusive conduct in transactions between related parties.

In compliance with Corporation Law, all members of the Company's Board of Directors are prohibited from voting in any assembly or meeting of the Board, or from acting in any operation or business transaction in which there are interests in conflict with those of the Company.

The main balances of related-party assets and liabilities as of December 31, 2017 and 2016, as well as the related-party transactions that affected income for the year, are the result of transactions between the Company and its joint subsidiary, as follows:

	Accounts receivable	
	2017	**2016**
Loan with related parties		
Ferroport	799,888	894,948
	799,888	**894,948**
Current	61,483	50,280
Non-current	738,405	844,668

The table below denotes the effect on net income of the related-party transactions by company:

	Financial income	
	2017	**2016**
Loan interest		
Ferroport	97,915	138,483
	97,915	**138,483**

Company Management is compensated by the parent company Prumo.

Transactions not involving cash or cash equivalents

	Parent Company				
		Cash Flow	Transfers	Effect on P&L	
	2016	**Borrowing / Settlement**	**Other**	**Interest, restatement and exchange variance**	**2017**
Loan from Related Parties	894.948	(192.176)	(1.675)	98.792	799.888
	894.948	**(192.176)**	**(1.675)**	**98.792**	**799.888**

(In thousands of Reais, unless stated otherwise)

8. Investments

a) Equity interests

	2017									
Direct investee	**% interest**	**Number of shares/quotas (thousand)**	**Assets**	**Liabilities**	**Shareholders' equity**	**Capital**	**Capital reserve**	**Profit reserves**	**Gains (loss) on financial instruments**	**Retained earnings**
Ferroport	50%	1,080	2,673,106	2,006,511	666,595	414,397	94,589	67,483	(576)	90,702

	2016									
Direct investee	**% interest**	**Number of shares/quotas (thousand)**	**Assets**	**Liabilities**	**Shareholders' equity**	**Capital**	**Capital reserve**	**Profit reserves**	**Gains (loss) on financial instruments**	**Retained earnings**
Ferroport	50%	1,080	2,734,536	2,143,883	590,653	414,397	94,589	-	(1,944)	79,723

b) Changes

Direct investee	**2016**	**Equity in net income of subsidiaries**	**Equity Appraisal Adjustment**	**2017**
Ferroport	295,326	39,231	(1,260)	333,297
	295,326	**39,231**	**(1,260)**	**333,297**

Direct investee	**2015**	**Equity in net income of subsidiaries**	**Equity Appraisal Adjustment**	**2016**
Ferroport	250,337	44,017	972	295,326
	250,337	**44,017**	**972**	**295,326**

(In thousands of Reais, unless stated otherwise)

9. Loans and financing

			2017			2016
	Maturity	**Rates in %**	**Principal (*)**	**Interest and restatement (*)**	**Total**	**Total**
Institution						
Brookfield Asset Management	9/30/2022	**US Dollar + 8.50% p.a.**	388,872	-	388,872	513,148
(-) Transaction cost			(49,874)	-	(49,874)	(60,192)
			338,998	**-**	**338,998**	**452,956**
Current			16,807	-	16,807	30,746
Non-current			322,191	-	322,191	422,210

(*) The interest paid is being classified under financing in the cash flow statements.

On September 01, 2015 the Company concluded the issuance and placement of overseas securities amounting to USD 50 million (“Tranche One”), fully subscribed and paid in by Prumo Group's controlling shareholder EIG Global Energy Partners (“EIG”).

On October 07, 2015 the Company concluded a new overseas securities issuance and placement of USD 30 million (“Second Tranche”), with the second interest payment made on December 31, 2015.

On October 13, 2015 Brookfield Asset Management (“Brookfield”) acquired from an investment vehicle of EIG the debt securities issued by the Company referring to Tranches One and Two.

On October 14, 2015 the Company completed the issuance and placement of overseas debt in the amount of USD 120 million, fully subscribed and paid in by an associated company of Brookfield.

Following the acquisition of the Debt Securities (“Tranche Three” in conjunction with Tranche One, and Tranche Two), Brookfield's total investment in Prumo Participações amounts to USD 200 million.

The debt securities mature on September 30, 2022, incur interest of 8.50% p.a. and quarterly amortization of interest and principal payments. The first interest payment is on December 31, 2015 and the first principal payment on June 30, 2016.

After the forecast expenses and commission had been deducted, the net funding obtained by Prumo Participações under this issuance will be used in its entirety by Prumo Participações to acquire credits held by Prumo against the company Ferroport.

In 2016 Prumo Participações advanced the amortization of USD35.05 million of this financing via the contractual cash sweep mechanism. This mechanism was used in 2017 for the early amortization of US$8.87 million of this financing. These advances were made possible due to receipt of the Ferroport loan at amounts above the debt obligations.

(In thousands of Reais, unless stated otherwise)

9. Loans and financing --Continued

Debt amortization schedule

	2017	2016
2018	27,126	41,065
2019	55,574	26,725
2020	46,312	54,753
2021	79,392	45,627
from 2022 to 2033	180,468	344,978
	388,872	**513,148**

Guarantees provided

The guarantees submitted by the Company to Brookfield in relation to the debt securities are: (i) Statutory lien of the Ferroport shares for Prumo Participações; (ii) Statutory lien on the shares of Prumo Participações held by the parent company Prumo; (iii) Statutory lien on escrow accounts and (iv) Statutory lien of receivables from the Ferroport loan.

Transactions not involving cash or cash equivalents

		Cash Flow			Noncash effect		
	2016	Secured/Settled	Interest Paid	Addition of Transaction Costs	Interest, Monetary restatement and Exchange variance	Amortization of Transaction Cost	2017
Loans, financing, and debentures	452,956	(128,990)	(39,256)	-	43,969	10,319	338,998
	452,956	(128,990)	(39,256)	-	43,969	10,319	338,998

10. Deferred taxes

The Company records deferred income and social contribution tax assets and liabilities at the rate of 34%. Brazilian tax legislation allows tax losses to be offset against future taxable income for an indefinite term. However, this offsetting is limited to 30% of the taxable income in each accrual period.

The carrying amount of the deferred tax asset is revised and restated periodically, while the projections shall be restated annually, unless material factors occur that can modify them.

The origin of the deferred income and social contribution taxes is presented below:

	2017	2016
Deferred tax liability		
Temporary difference - Exchange variance	(32,610)	(35,785)
Total deferred tax liabilities	**(32,610)**	**(35,785)**
Total deferred taxes	**(32,610)**	**(35,785)**

(In thousands of Reais, unless stated otherwise)

11. Taxes and social contributions payable

	2017	2016
PIS/COFINS	263	538
IRRF and fines	5,899	-
IRPJ/CSLL	2,561	20,217
	8,723	**20,755**

The reconciliation between the tax expense as calculated by the combined statutory rates and the income and social contribution tax expense charged to net income is presented below:

	2017	2016
Profit before income and social contribution taxes	69,302	211,282
Income and social contribution taxes at the rate (34%)	(23,563)	(71,836)
Adjustment to determine the effective rate		
Interest on shareholders' equity	10,813	-
Equity in net income of subsidiaries	13,339	14,966
Tax credits are not recognized	24	24
Total income and social contribution taxes	**613**	**(56,846)**
Effective rate	(0.88%)	(26.91%)
Current	(2,561)	(20,217)
Deferred charges	3,174	(36,629)
Total income and social contribution taxes	**613**	**(56,846)**

12. Shareholders' equity

a) Share capital

The Company's ownership structure as of December 31, 2017 and 2016 is as follows:

	2017		2016	
Shareholders	**Number of common shares (thousand)**	**%**	**Number of common shares (thousand)**	**%**
Prumo	760,885	100.00	606,424	100.00
	760,885	**100.00**	**606,424**	**100.00**

As per the re-ratification of the Annual General Meeting (AGM) on April 29, 2016, the net income for FY 2015 of R$ 28,317 was allocated to the Company's share capital. 28,317 new common registered shares with no par value were accordingly issued at the issuance price of R$ 1.00 (one real) each, all of which were subscribed and paid in.

12. Shareholders' equity --Continued

On June 17, 2016 the parent company Prumo and paid in by converting the advance for future capital increase the amount of R$ 10,367 via the issuance of 10,367 new registered common shares with no par value, at the issuance price of R$ 1.00 each.

On March 29, 2017 the parent company Prumo and paid in by converting the advance for future capital increase the amount of R$ 25 via the issuance of 25 new registered common shares with no par value, at the issuance price of R$ 1.00 each.

As per the Annual and Extraordinary General Meeting (“AGOE") on April 27, 2017, the net income for FY 2016 of R$ 146,714 thousand was allocated to the Company’s share capital. 146,714 new common registered shares with no par value were accordingly issued at the issuance price of R$ 1.00 (one real) each, all of which were subscribed and paid in, with R$ 7,722 remaining in the legal reserve.

b) Capital reserve

Capital contribution in the amount of R$ 14,285 deriving from transfer of Ferroport shares held by Prumo.

c) Reserves

The Executive Board will present to the General Meeting for approval a proposal about the allocation of the net income that remains after the following deductions or increases have been made in this order:

i. 5% (five percent) to form the legal reserve, until it has reached 20% (twenty percent) of the share capital. Formation of the legal reserve may be waived in financial years where the balance of said reserve plus the capital reserves exceeds 30% (thirty percent) of the share capital.

ii. 25% (twenty-five percent) for payment of the minimum mandatory dividends to the shareholders.

(In thousands of Reais, unless stated otherwise)

12. Shareholders' equity --Continued

d) Dividends and interest on equity

	2017	2016
Net income for the year	69,915	154,436
Legal reserve - (5%)	(3,496)	(7,722)
Dividend calculation basis	**66,419**	**146,714**
Interim dividends	25,318	110,036
Interest on shareholders' equity (“JCP")	31,803	-

The EGM held July 3, 2017 resolved to pay out interim dividends on June 30, 2017 in the amount of R$ 52,350, where this was re-ratified, redistributing the interim dividend to R$ 25,318 and interest on shareholders' equity in the amount of R$ 27,032.

The corporate by-laws determine the distribution of a minimum compulsory dividend of 25% of the net income for the year, adjusted in accordance with article 202 of Law 6404/76. On July 3, 2017 the Company approved the advancement of dividends for FY 2017, pursuant to art. 204 (2) of Brazilian corporation law, which states the bylaws may authorize the Boards to declare the payment of interim dividends, from the retained earnings account or the profit reserves in the latest annual or semi-annual statement of financial position.

e) Other comprehensive income

On December 31, 2017 other comprehensive income was recognized derived from the loss on derivative financial instruments of the subsidiary Ferroport, in the amount of R$ (1,260), net of tax.

13. Financial income

	2017	2016
Financial income		
Loan interest	97,915	138,483
Interest on investments	264	116
Interest earned	1,112	863
Exchange variance	48,382	105,249
	147,673	**244,711**
Financial expenses		
Interest on loans	(38,820)	(53,002)
Exchange variance on loans	(51,019)	-
Commission and brokerage fees	(14,002)	(10,507)
Fine and interest	(1,128)	(297)
Taxes on financial revenue	(11,525)	(12,908)
Other	(839)	(479)
	(117,333)	**(77,193)**
	30,340	**167,518**

(In thousands of Reais, unless stated otherwise)

14. Financial instruments and risk management

The Company carries out transactions with financial instruments. These instruments are managed through operating strategies and internal controls, aimed at liquidity, profitability and security. Our control policy consists of periodically monitoring contract rates versus market rates. We do not invest in derivatives or any other risky assets on a speculative basis.

The estimated realization values of the Company's financial assets and liabilities were determined through information available in the market and appropriate valuation methodologies. However, considerable judgment was required in the interpretation of the market data to estimate the most adequate realization value. Consequently, the estimates below do not necessarily indicate the values that could be realized in the current exchange market.

The concept of fair value states that assets and liabilities should be valued at market prices, in the case of liquid assets, or by using mathematical pricing methods, in other cases. The hierarchy level of the fair value gives priority to unadjusted prices quoted on an active market. A part of the company's accounts has the fair value equal to book value, these accounts include cash equivalents, payables and receivables, bullet debts and short-term.

The table below demonstrates the book balances and respective fair values of the financial instruments and segregation of the hierarchal level, included in the balance sheet:

	2017			**2016**		
	Carrying amount	**Measurement**	**Hierarchical level (*)**	**Carrying amount**	**Measurement**	**Hierarchical level (*)**
Assets						
Cash and cash equivalents	2,146			1,556		
Escrow account	-	Amortized cost		55,405	Amortized cost	
Loan with related parties	799,888	Amortized cost		894,948	Amortized cost	
Other receivables	9			-		
	802,043			**951,909**		
Liabilities						
Trade payables	6	Amortized cost		200		
Loans and financing	338,998	Amortized cost	2	452,956	Amortized cost	2
Dividends payable	-	Amortized cost		36,679	Amortized cost	
Other accounts payable	25			-		
	339,029			**489,835**		

(*) Fair value hierarchy levels:

(Level 1) Prices traded (unadjusted) in active markets for identical assets or liabilities
(Level 2) Different inputs, except for traded prices in active markets included in Level 1 that are observable for the assets and liabilities, directly (as prices) or indirectly (derived from prices), and
(Level 3) Inputs for the asset or liability that are not based on observable market variables (unobservable inputs).

14. Financial instruments and risk management --Continued

As of December 31, 2017 loans and financing are measured at amortized cost. The fair value calculated by Management for reference purposes only is R$ 365,693.

The carrying amounts of financial instruments measured at amortized cost are classified as loans and receivables (assets) and other liabilities measured at amortized cost. The carrying amounts of these balances approximate fair value.

The Company's financial transactions are subject to the following risk factors:

(i) Market risk:

Exchange Risk

Risk of change in exchange rates which could be associated to the Company's assets and liabilities. The Company manages the exchange risk for its companies to detect and mitigate risks posed by changes in exchange rates underlying global assets and liabilities. The foreign-currency debt therefore exists on debt securities issued in US dollars by Prumo Participações. The cash flow intended to service the payment of this debt comes monthly from its subsidiary Ferroport, whose revenue is denominated in US dollars, where the fee for handling iron ore in force is restated annually by the PPI US inflation index.

Ferroport is in the unique situation where its cost structure is denominated in Brazilian Reais and its monthly revenue is indexed to the dollar. The operational income of the joint venture is therefore exposed to the risk of exchange variance due to a mismatch between revenue and cost currencies. The appreciation of the Brazilian real against the US dollar could diminish the operational margin and free cash flow of Ferroport. In respect of Prumo Participações' debt, in our opinion the fact that servicing the debt and the revenue of Ferroport are denominated in the same currency creates a natural hedge for this exposure.

The table below summarizes the current value of the debt in millions of reais, with a sensitivity scenario in the exchange rates (USD) suffering oscillations of 10% and 20%.

2017	**Real**	**USD +10%**	**USD +20%**
Institution			
Brookfield (vii)	388,872	427,759	466,646
Total	**388,872**	**427,759**	**466,646**

2016	**Real**	**USD +10%**	**USD +20%**
Institution			
Brookfield (vii)	513,149	564,464	615,779
Total	**513,149**	**564,464**	**615,779**

(In thousands of Reais, unless stated otherwise)

14. Financial instruments and risk management --Continued

(ii) Liquidity risk

The table below denotes the main financial liabilities of the Company as of December 31, 2017. These amounts are gross and are not discounted, and include payments of estimated interest.

	Up to 6 months	6 to 12 months	1 to 2 years	2 to 5 years	Total
Financial liabilities					
Loans and financing	29,946	29,369	84,466	360,616	504,397
Trade payables	-	6	-	-	6
Other accounts payable	-	-	25	-	25
Total by time range	**29,946**	**29,375**	**84,491**	**360,616**	**504,428**

(iii) Credit risk

This arises from the possibility of the Company suffering losses due to the default of its counterparties or of financial institutions where they have funds.

The Company also carries out a rating analysis of the financial institutions, through credit reports provided by the “Bank Risk Classification System” - Risk Bank, in order to classify and systematically follow up the risk and performance of each bank.

The balances exposed to credit risk are as follows:

	2017	2016
Financial instruments		
Cash and banks	2,146	1,556
Escrow account	-	55,405
Related-party loan	799,888	894,948
Other receivables	9	-
	802,043	**951,909**

(iv) Capital management

The Company's funds for developing its business plan were completely financed by capital contributions from shareholders and third-party loans. The Company's Treasury Department monitors the funds required for working capital and capital expenditure, which are provided by the shareholder every month.

Members of the Executive Board

Jose Magela Bernardes

Chief Executive Officer

Eugenio Leite de Figueiredo

Chief Financial Officer

Leonardo Fortuna Bernardo Ribeiro

Manager of the Controller's Department

Accountant CRC RJ 091,229/O-9