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Vale's performance in 1Q16

Vale reached several production records for a first quarter, as total iron ore production and Carajás iron ore production

Vale delivered a sound operational performance in 1Q16, reaching several production records for a first quarter, namely: (i) total iron ore production[1] of 77.5 Mt; (ii) Carajás iron ore production of 32.4 Mt; (iii) Tubarão pellet production of 7.2 Mt; (iv) nickel production of 73,500 t; and (v) copper production of 109,900 t.

Vale's CFO comments on 1Q16 financial results

Net revenues totaled US$ 5.719 billion in 1Q16, decreasing US$ 180 million vs. 4Q15 as a result of seasonally lower sales volumes of iron ore fines (US$ 612 million), base metals (US$ 107 million), and fertilizers (US$ 48 million), which were partly offset by higher sales prices for iron ore fines (US$ 584 million).

Costs and expenses, net of depreciation charges, totaled US$ 3.715 billion in 1Q16, decreasing by US$ 880 million vs. 4Q15. Costs decreased US$ 805 million (19%), mainly driven by lower sales volumes, and expenses decreased US$ 75 million (21%) as a result of lower SG&A, R&D and pre-operating and stoppage expenses.

SG&A[2] totaled US$ 96 million in 1Q16, decreasing US$ 33 million (26%) from the US$ 129 million recorded in 4Q15, with reductions in personnel, services, selling expenses and others. R&D[2] totaled US$ 60 million in 1Q16, decreasing US$ 59 million (50%) from the US$ 119 million recorded both in 4Q15 and in 1Q15, with reductions across all business segments. Pre-operating and stoppage expenses[2] totaled US$ 102 million in 1Q16, decreasing US$ 136 million (57%) from the US$ 238 million recorded in 4Q15, mainly due to the absence of pre-operating expenses for VNC and the Nacala Logistics Corridor in 1Q16.

Adjusted EBITDA was US$ 2.005 billion in 1Q16, 44% higher than in 4Q15 mainly as a result of the improvement in the EBITDA for Ferrous Minerals (US$ 329 million) and Base Metals (US$ 218 million). Adjusted EBITDA margin was 35.1% in 1Q16, increasing from the 23.6% recorded in 4Q15.

Capital expenditures totaled US$ 1.449 billion in 1Q16, decreasing by US$ 744 million vs. 4Q15. Investments in project execution totaled US$ 920 million in 1Q16, with expenditures associated with the S11D project accounting for 69% of this total. Sustaining capex totaled US$ 529 million in 1Q16, decreasing US$ 298 million from the US$ 827 million recorded in 4Q15.

Net income totaled US$ 1.776 billion in 1Q16 vs. a net loss of US$ 8.569 billion in 4Q15. The US$ 10.345 billion increase in net income was mostly driven by the higher EBITDA, the impairment charges recorded in 4Q15 and the positive effect on financial results of the 8.7% end-to-end appreciation of the BRL against the USD in 1Q16. Underlying earnings were positive US$ 514 million in 1Q16, against negative US$ 1.032 billion in 4Q15.

Free cash flow (FCF) was negative US$ 1.919 billion in 1Q16, despite the US$ 2.005 billion adjusted EBITDA in the quarter, being negatively impacted mainly by the settlement of derivatives in the quarter (US$ 510 million) and by the increase in working capital in 1Q16 vs. 4Q15 stemming mostly from higher accounts receivable (US$ 1.016 billion)[3] and lower supplier and contractor liabilities (US$ 383 million)[4]. Accounts receivable increased, mainly driven by the concentration of iron ore sales volumes (sales not yet collected) at higher provisional prices at the end of the quarter. Working capital changes should have a positive impact on cash flows in 2Q16 as sales collections increase throughout the quarter.

Gross debt totaled US$ 31.470 billion as of March 31st 2016, increasing US$ 2.617 billion vs. the US$ 28.853 billion as of December 31st 2015, mainly as a result of the: (i) net addition to loans and financing of US$ 2.042 billion and (ii) impact of the exchange rate on the translation of BRL denominated debt into USD[5].

Net debt totaled US$ 27.661 billion on March 31st, 2016 vs. US$ 25.234 billion as of December 31st, 2015, with a cash balance of US$ 3.809 billion. The increase in net debt was mainly driven by the: (i) impact of the exchange rate on the translation of BRL denominated debt into USD and (ii) negative free cash flow in 1Q16.

EBITDA from the Ferrous Minerals business segment increased 23% in 1Q16 driven by higher realized prices and lower landed cash cost in China, despite the effects of seasonally lower sales volumes

- Adjusted EBITDA for Ferrous Minerals was US$ 1.738 billion in 1Q16, US$ 329 million higher than the US$ 1.409 billion achieved in 4Q15, mainly as a result of higher realized sales prices (US$ 565 million) and lower costs[6] (US$ 244 million), which were partially offset by seasonally lower sales volumes (US$ 209 million) and the positive one-off effect of the Asset Retirement Obligation (ARO) recorded in 4Q15 (US$ 322 million).
- Cash flow generation, simply measured by adjusted EBITDA less sustaining and growth capex, was US$ 829 million in 1Q16, increasing by US$ 1.299 billion from the negative US$ 470 million recorded in 1Q15, despite the 23% drop in the Platts IODEX 62% reference price.
- CFR dmt reference price for iron ore fines (ex-ROM) increased by US$ 9.6/t from US$ 45.1/t in 4Q15 to US$ 54.7/t in 1Q16, equivalent to a price realization 13% higher than the average Platts IODEX 62% of US$ 48.3/t in 1Q16, whereas the CFR/FOB wmt price for iron ore fines (ex-ROM)[7] increased by US$ 9.3/t from US$ 37.2/t in 4Q15 to US$ 46.5/t in 1Q16.
- Average Fe content on iron ore fines decreased slightly from 63.7% in 4Q15 to 63.5% in 1Q16, driven mostly by mine plan adjustments in the Southern and Southeastern systems in response to market demand and better pricing for higher silica ores.
- C1 cash cost FOB port per metric ton for iron ore fines, ex-royalties, totaled US$ 12.3/t in 1Q16, remaining practically in line with the US$ 12.2/t[8] recorded in 4Q15, despite the reduced fixed costs dilution on seasonally lower production volumes.
- C1 Cash cost FOB port per metric ton of iron ore fines in Brazilian Reais was R$ 47.5/t in 1Q16, practically in line with the R$ 47.0/t[9] recorded in 4Q15, mainly due to increases in operational productivity and the ongoing cost-cutting initiatives, despite less fixed-costs dilution on seasonally lower production volumes and higher inflationary pressures in Brazil.
- Unit maritime freight cost of iron ore fines per metric ton was US$ 11.3/t in 1Q16, US$ 2.8/t lower than the US$ 14.1/t recorded in 4Q15[10].
- Iron ore and pellets EBITDA break-even, measured by unit cash costs and expenses on a landed-in-China basis (and adjusted for quality, pellets margins differential and moisture, excluding ROM), decreased from US$ 31.0/dmt in 4Q15 to US$ 28.0/dmt in 1Q16, mainly driven by the US$ 2.80/t reduction on maritime freight costs.
- Sustaining capex for iron ore fines and pellets totaled US$ 208 million in 1Q16, US$ 18 million higher than in 4Q15 mainly driven by the impact of carryover of payments of mining equipment acquired in 2015.
- Physical progress reached 85% at the S11D mine and plant, 64% at the S11D logistic sites, and 85% at the S11D railway spur.

EBITDA from the Base Metals business segment increased 196% despite lower nickel and copper LME prices

- Sales revenues totaled US$ 1.353 billion in 1Q16, US$ 105 million lower than in 4Q15 as a result of lower sales volumes (US$ 107 million) and lower nickel realized prices (US$ 42 million), which were partly offset by better copper realized prices (US$ 46 million).

- Nickel realized prices were favorably impacted by improving premiums over the LME, decreasing only 6% in 1Q16 vs. 4Q15 vs. the 10% reduction on LME nickel prices in the same period.
- Copper realized prices increased 13% in 1Q16 vs. 4Q15 vs. the 4% reduction on LME copper prices in the same period, mainly due to the positive impact of the provisional pricing system on sales revenues of US$ 14 million in 1Q16 vs. negative US$ 60 million in 4Q15.
- Adjusted EBITDA was US$ 329 million in 1Q16, US$ 218 million higher than in 4Q15, as a result of the reduction in costs and expenses throughout all operations, with the highlight for the improvements in VNC and Salobo.
- Adjusted EBITDA for VNC totaled negative US$ 48 million in 1Q16, increasing US$ 59 million (55%) from the negative US$ 107 million recorded in 4Q15, mainly as a result of the good operational performance which enabled a reduction in the unit costs and pre-operating expenses net of by-product credits from US$ 17,380/t in 4Q15 to US$ 12,711/t in 1Q16.
- Salobo´s EBITDA totaled US$ 131 million in 1Q16, increasing US$ 56 million (75%) from the US$ 75 million recorded in 4Q15, mainly driven by a 41% decrease in unit COGS[11] due to higher copper grades and higher by-product credits.
- Salobo achieved a monthly production record of 14,100 t of copper in concentrates in 1Q16 and is expected to reach its full production capacity in 2H16.

EBITDA from the Coal business segment improved by 38% as a result of lower costs

- Adjusted EBITDA was negative US$ 93 million in 1Q16, compared to negative US$ 149 million in 4Q15, mainly driven by lower costs.
- Costs in Mozambique[12] decreased US$ 45 million in 1Q16 vs. 4Q15, mainly as a result of the ramp-up of the Nacala Logistic Corridor, while costs decreased US$ 108 million in Australia[13] in 1Q16 vs. 4Q15 due to the good operational performance at Carborough Downs, after the longwall move in 4Q15.
- Ramp-up of the Nacala Logistics Corridor continued as planned, with 747,000 t being transported on the railway in 1Q16 vs. 241,000 t in 4Q15 and with thirteen shipments concluded in 1Q16 vs. one shipment concluded in 4Q15.

EBITDA from the Fertilizers business segment decreased, driven by lower market prices and seasonally lower volumes

- Adjusted EBITDA for the Fertilizer business segment decreased to US$ 70 million in 1Q16 from US$ 117 million in 4Q15, as a result of lower prices (US$ 48 million) and seasonally lower volumes (US$ 18 million), being partly offset by lower expenses (US$ 25 million).
- SG&A and other expenses, R&D and Pre-operating and stoppage expenses[14] decreased US$ 4 million, US$ 17 million and US$ 5 million, respectively, in 1Q16 vs. 4Q15.

We successfully reduced our costs and expenses in all business segments, despite the seasonally lower production and sales volumes, and progressed with the implementation of our most important projects in 1Q16.

We remain focused on maximizing our margins by leveraging our iron ore supply chain flexibility (22 mines, 11 pelletizing plants, 5 railways, 4 ports, 2 distribution centers etc.) to have a responsible and sustainable reaction to various market conditions.

Together with Samarco and BHP Billiton, we reached an agreement with the Brazilian authorities which provides a long-term remedial and compensation framework for responding to the impact of the Samarco dam failure and accelerates both the environmental remediation measures and the reparations for the people affected.

Finally, we acknowledge the recent improvement in iron ore prices but are cognizant of market volatility, thus remaining fully committed to strengthening our balance sheet through the reduction of our net debt as previously informed. We remain focused on our operating and capital allocation discipline and on progressing our divestment and asset optimization program.

[1] *Excluding Samarco's attributable production and including iron ore acquired from third parties.*
[2] *Net of depreciation charges.*
[3] *This figure represents the accounts receivable variation in 1Q16 vs. 4Q15.*
[4] *This figure represents the supplier and contractor liabilities variation in 1Q16 vs. 4Q15.*
[5] *In 1Q16, from end-to-end, the BRL appreciated 8.7% against the USD.*
[6] *Net effect on costs, after adjusting for volume and exchange rate impacts.*
[7] *After adjusting for moisture and the effect of the lower FOB sales prices on 35% of the total sales volumes.*
[8] *US$ 12.2/t is equivalent to the US$11.9/t reported in 4Q15 after adjusting for the new allocation criteria for ICMS (US$ 0.57/t) and Distribution Costs (-US$ 0.33/t) as described in the box "Managerial Allocation Changes" in pages 45-46 of the 4Q15 Earnings Release. Additional adjustment was made to include the cost of Third Party Ore Purchases to our C1 costs.*
[9] *R$ 47.0/t is equivalent to the R$45.5/t reported in 4Q15 after adjusting for the new allocation criteria for ICMS and Distribution Costs as described in the box "Managerial Allocation Changes" in pages 45-46 of the 4Q15 Earnings Release. Additional adjustment was made to include the cost of Third Party Ore Purchases (US$ 0.13/t) to our C1 costs.*
[10] *Excluding the negative impact of the bunker oil hedge in 4Q15.*
[11] *Net of depreciation charges and net of by-products credit.*
[12] *After adjusting for the effects of higher volumes.*
[13] *After adjusting for the effects of higher volumes and exchange rate.*
[14] *Net of depreciation charges.*

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