

(A free translation of the original in Portuguese)

Samarco Mineração S.A.

**Annual Report
on the Financial Statements
at December 31, 1997 and 1996**

(A free translation of the original in Portuguese)

1997 ANNUAL REPORT

To Our Stockholders,

1997 witnessed an important economic milestone for SAMARCO MINERAÇÃO S.A. The company celebrated 20 years of successful operations and completed an investment program started 3 years ago involving US\$ 500 million. The conclusion of this expansion project will optimize the return on investments now that the entire production line has started to operate at full capacity.

At the Germano/Alegria mine, the concentration plant has been amplified to increase annual production from 9.5 million to 13.3 million tons of iron ore concentrate.

The slurry pipeline, designed to move 12 million tons per year, is now operating at its full capacity of 13.3 million tons per year, with total reliability, a higher efficiency level and, consequently, reduced costs.

At Ponta Ubu, the second pelletizing plant has been constructed, with an annual production capacity of 6 million tons. This plant features the world's largest pelletizing furnace, with 744 square meters. The first pelletizing plant of SAMARCO features the second largest furnace.

The second plant started up on November 19, and by the end of December had reached 90% of capacity, yielding a product of the required quality.

SAMARCO has doubled its annual production capacity to 12 million tons of pellets, substantially increasing sales of products with a high added value. (Average FOB price of US\$ 37.00 per ton of pellets, as opposed to US\$ 16.00 per ton of pellet-feed)

SAMARCO maintains a longtime business relationship with top-line customers worldwide. These customers are located in several different regions of the world which provides the company with a proper balance of its sales in the overseas market.

With this new dimension, SAMARCO will jump from fourth to second place among the world's largest iron ore pellet exporters, increasing its overseas market share from 8% to 16%.

Pellet and pellet-feed sales in 1997 were slightly lower than in the previous year due to implementation of the expansion project at the Germano/Alegria plant. By the end of December, SAMARCO's production had already achieved projected capacity levels, i.e., 1.1 million tons per month.

In August, the Muniz Freire hydroelectric plant came onstream and in October the Guilman Amorim hydroelectric plant, a project carried out in association with Companhia Siderúrgica Belgo-Mineira, started operations. Both plants have been operating at full capacity since January 1998 generating 58% of the electric power demand at peak hours, contributing to a significant reduction in SAMARCO's operating costs.

In the environmental protection field, investments reached US\$ 40.3 million. A major investment was the installation of a modern cutting-edge electrostatic precipitator in Plant No. 2 to filter particulate material emissions. A similar precipitator is currently being installed at Plant No. 1, involving an investment of US\$ 24.1 million. This equipment is expected to be placed in operation in the first half of 1998.

A decisive contributing factor to success was the trust placed by the financial community in SAMARCO, which made the financing of all these investments feasible. Of special note is the participation of *the National Bank for Economic and Social Development - BNDES* and the *Government Agency for Machinery and Equipment Financing - FINAME*; International Finance Corporation - IFC; Export-Import Bank of the United States of America - Eximbank; Export Development Corporation of Canada - EDC; HERMES Kreditversicherungs-AG of Germany; institutional investors in the United States and Japan, and commercial banks which maintain business relationships with SAMARCO.

Among the events which have promoted the strengthening of SAMARCO's position as a modern mining company are the following:

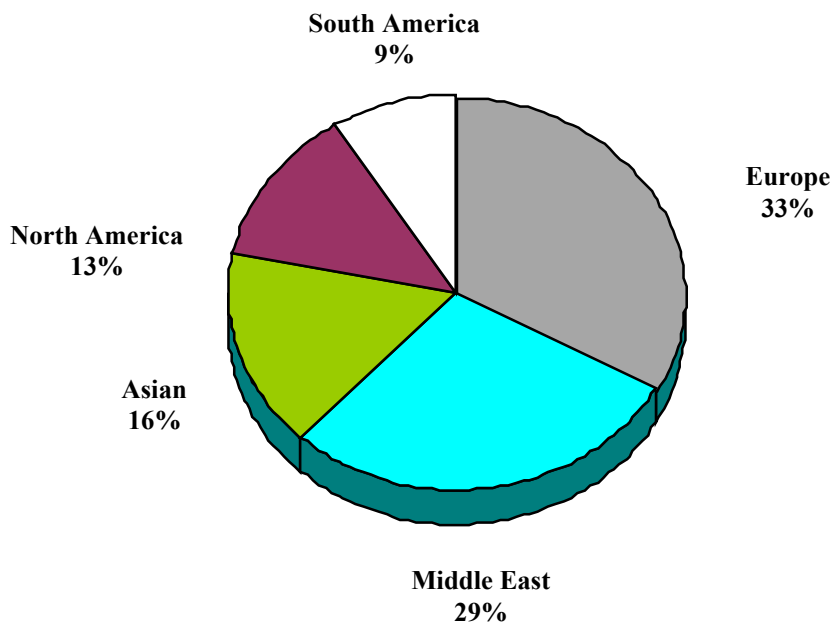
- SAMARCO was the first company in the State of Espírito Santo and in all of Brazil to undergo an environmental audit carried out in compliance with State laws. This audit not only addressed all technical aspects of environmental management, but was conducted with total transparency and merit through the joint efforts of both parties. The company intends to obtain the ISO 14000 Certification in the second half of 1998.
- The consulting firm Hay Mc Ber has once again selected SAMARCO as a Brazilian benchmark for the quality of its organizational environment.
- EXAME business magazine has included SAMARCO among the 30 best companies in Brazil to work for, according to a study performed by “The Great Places to Work Institute”.
- SAMARCO was chosen “The Mining Company of the Year”, at the end of 1997, by the highly respected *Brasil Mineral* magazine, and was awarded the prize during a ceremony in February this year. The company received this honor because of its significant investments over the past years, its policy of valuing its human resources, especially through team work and ongoing training activities promoting high workforce morale which today is an international benchmark, and an environmental protection policy which has been in place since the company began its activities.
- SAMARCO’s management approach is based on a model of maximization of employees’ values, aiming to maintain a motivated and participative staff, permanently up-to-date on technological advances. The company provided 118,944 hours of training in 1997, with an average of 81 hours per man year.
- Investments in the expansion project will reach about US\$ 336 million. Of these, US\$ 324.5 million has been spent through December 1997.
- Investments of US\$ 25.3 million were made in the construction of the Muniz Freire Hydroelectric Plant, in Espírito Santo, with a hydroelectric capacity of 25 MW. Of this amount, US\$ 7.6 million was spent in 1997.
- Investments in the Guilman Amorim Hydroelectric Plant, with a 140 MW capacity, are estimated at US\$ 152.5 million, of which US\$ 148.6 million has been spent through December. These investments are being made directly by Usina Hidrelétrica Guilman Amorim S.A., a company 51% owned by Companhia Siderúrgica Belgo-Mineira and 49% by SAMARCO.
- A further US\$ 28.9 million was spent in 1997 on various improvements aimed at maintaining production capacity.
- Gross sales and net profit in 1997 reached R\$ 276.2 million and R\$ 42.5 million, respectively. This represented a net margin of 15.4%, still with hardly any influence from the expansion project.

- The company's financial forecasts evidence an absolutely comfortable scenario for its administration, with an operating cash generation substantially higher than the debt service.
- The Asian crisis, which led the Brazilian government to implement emergency economic measures, will not affect the continuity of sales to customers in that region, which represent 16% of its total sales thanks to longtime business relations. SAMARCO's customers consist of solid, globally competitive and very well managed companies.

SAMARCO's sales in 1997 totaled 9.1 million tons of iron ore (5.7 million tons of pellets and 3.4 million tons of concentrates), which represent US\$ 255 million of billings. For 1998, billings are expected to reach US\$ 450 million.

Increasing sales reflect the perception of SAMARCO's quality products by its customers. These products are sold in all major markets worldwide, and distributed as follows:

Sales Breakdown by Region (NMT) - 1997



The Directors of SAMARCO are grateful for the support of all stockholders, employees, customers, sales agents, suppliers and financial institutions, and are confident of the commitment to maintain SAMARCO as a truly efficient company.

(A free translation of the original report in Portuguese on financial statements prepared in conformity with accounting principles determined by Brazilian corporate legislation)

Samarco Mineração S.A.

**Financial Statements at
December 31, 1997 and 1996
and Report of Independent Accountants**

Report of Independent Accountants

January 19, 1998

To the Board of Directors and Stockholders
Samarco Mineração S.A.

- 1 We have audited the accompanying balance sheets of Samarco Mineração S.A. as of December 31, 1997 and 1996 and the related statements of income, of changes in stockholders' equity and of changes in financial position for the years then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements.
- 2 We conducted our audits in accordance with approved auditing standards which require that we perform the audits to obtain reasonable assurance about whether the financial statements are fairly presented in all material respects. Accordingly, our work included, among other procedures: (a) planning our audits taking into consideration the significance of balances, the volume of transactions and the accounting and internal control systems of the company, (b) examining, on a test basis, evidence and records supporting the amounts and disclosures in the financial statements and (c) assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.
- 3 In our opinion, the financial statements audited by us present fairly, in all material respects, the financial position of Samarco Mineração S.A. at December 31, 1997 and 1996 and the results of operations, the changes in stockholders' equity and the changes in financial position for the years then ended, in conformity with accounting principles determined by Brazilian corporate legislation.

Price Waterhouse
Auditores Independentes
CRC-SP-160 "S" MG

Francisco J. P. Fagundes
Partner
Contador CRC-MG-54.755

Samarco Mineração S.A.

Balance Sheet at December 31 In thousands of reais

(A free translation of the original in Portuguese prepared in conformity with accounting principles determined by Brazilian corporate legislation)

| Assets | <u>1997</u> | <u>1996</u> | Liabilities and stockholders' equity | <u>1997</u> | <u>1996</u> |
|---|------------------|----------------|---|------------------|----------------|
| Current assets | | | Current liabilities | | |
| Cash and banks | 737 | 1,111 | Suppliers, including R\$ 3,648 (1996 - R\$ 6,728) from abroad | 17,389 | 18,046 |
| Mutual funds and fixed-yield investments | | 3,117 | Advances against export contracts | 128,756 | 37,068 |
| Short-term investments | 7,941 | 6,733 | Loans | 74,595 | 41,624 |
| Trade accounts receivable | 35,579 | 26,517 | Financial charges | 9,457 | 4,828 |
| Discounted foreign exchange contracts | (14,924) | (10,793) | Salaries and social charges | 7,648 | 7,227 |
| Receivables from stockholders and related companies | 13 | 1,612 | Provision for income tax | 25,815 | 17,994 |
| Other accounts receivable | 52,410 | 15,686 | Taxes other than on income | 915 | 484 |
| Inventories | 42,961 | 32,124 | Proposed dividends | | 20,788 |
| Prepaid expenses | <u>1,397</u> | <u>796</u> | Payable to stockholders and related companies | 192 | 7 |
| | | | Other accounts payable | <u>1,638</u> | <u>3,195</u> |
| | <u>126,114</u> | <u>76,903</u> | | <u>266,405</u> | <u>151,261</u> |
| Long-term receivables | | | Long-term liabilities | | |
| Judicial Escrow | 3,861 | 2,167 | Loans | 280,314 | 186,108 |
| Deferred income tax | 468 | 503 | Other | <u>3,720</u> | <u>12,327</u> |
| Compulsory loans and investments - ELETROBRÁS | 756 | 306 | | <u>284,034</u> | <u>198,435</u> |
| Receivables from stockholders and related companies | | 14,840 | Stockholders' equity | | |
| Other | <u>7,549</u> | <u>6,298</u> | Capital | 297,025 | 297,025 |
| | <u>12,634</u> | <u>24,114</u> | Capital reserves | 2,477 | 2,477 |
| Permanent assets | | | Revaluation reserve | 10,897 | 11,422 |
| Investments | 8,736 | 7,756 | Incentivated depletion reserve | 1,516 | 1,516 |
| Property, plant and equipment | 934,207 | 728,563 | Revenue reserves | 97,746 | 95,619 |
| Deferred charges | <u>2,866</u> | <u>3,930</u> | Retained earnings | <u>124,457</u> | <u>83,511</u> |
| | <u>945,809</u> | <u>740,249</u> | | <u>534,118</u> | <u>491,570</u> |
| | <u>1,084,557</u> | <u>841,266</u> | | <u>1,084,557</u> | <u>841,266</u> |

The accompanying notes are an integral part of these financial statements.

Samarco Mineração S.A.

Statement of Income Years Ended December 31 In thousands of reais

(A free translation of the original in Portuguese
prepared in conformity with accounting principles
determined by Brazilian corporate legislation)

| | <u>1997</u> | <u>1996</u> |
|---|------------------|------------------|
| Operating revenue | | |
| Sales | 276,161 | 267,796 |
| Taxes on sales | <u>(1,763)</u> | <u>(1,140)</u> |
| Net sales | 274,398 | 266,656 |
| Cost of sales | <u>(194,721)</u> | <u>(189,031)</u> |
| Gross profit | <u>79,677</u> | <u>77,625</u> |
| Operating expenses (income) | | |
| Selling | 26,229 | 25,744 |
| General and administrative | 14,268 | 12,636 |
| Management fees | 544 | 655 |
| Financial expenses | 11,658 | 7,832 |
| Financial income | (3,517) | (6,053) |
| Provision for losses on ELETROBRÁS investments | 681 | 270 |
| Other operating (income) expenses | <u>(27,892)</u> | <u>1,311</u> |
| | <u>21,971</u> | <u>42,395</u> |
| | <u>57,706</u> | <u>35,230</u> |
| Exchange differences and monetary correction | | |
| Income | 4,952 | 4,546 |
| Expenses | <u>(12,237)</u> | <u>(6,859)</u> |
| | <u>(7,285)</u> | <u>(2,313)</u> |
| Non-operating income (expense) | <u>61</u> | <u>(401)</u> |
| | <u>(7,224)</u> | <u>(2,714)</u> |
| Income before taxation | 50,482 | 32,516 |
| Income tax | <u>(4,014)</u> | <u>(5,203)</u> |
| Income before profit sharing | 46,468 | 27,313 |
| Employees' profit sharing | <u>(3,920)</u> | <u>(3,690)</u> |
| Net income for the year | <u>42,548</u> | <u>23,623</u> |
| Net income per thousand shares at the end of the year - R\$ | <u>8.11</u> | <u>4.51</u> |

The accompanying notes are an integral part of these financial statements.

Samarco Mineração S.A.

(A free translation of the original in Portuguese prepared in conformity with accounting principles determined by Brazilian corporate legislation)

Statement of Changes in Stockholders' Equity
In thousands of reais

| | <u>Capital reserves</u> | | | | | | <u>Revenue reserves</u> | | | <u>Total</u> | |
|--|-------------------------|-------------------------------|--|----------------------|-----------------------|----------------------------|---------------------------------------|---------------|-------------------------|----------------|--------------------------|
| | <u>Capital</u> | <u>Restatement of capital</u> | <u>Special restatement of fixed assets</u> | <u>Share premium</u> | <u>Tax incentives</u> | <u>Revaluation reserve</u> | <u>Incentivated depletion reserve</u> | <u>Legal</u> | <u>Retained profits</u> | | <u>Retained earnings</u> |
| At December 31, 1995 | 242,545 | 54,480 | 784 | 1,681 | 12 | 11,947 | 1,516 | 25,809 | 68,629 | 81,332 | 488,735 |
| Capitalization of reserve | 54,480 | (54,480) | | | | | | | | | |
| Revaluation reserve released to retained earnings | | | | | | (525) | | | | 525 | |
| Net income for the year | | | | | | | | | | 23,623 | 23,623 |
| Appropriation to reserve: | | | | | | | | 1,181 | | (1,181) | |
| Proposed dividends (R\$ 3.96 per thousand shares) | | | | | | | | | | (20,788) | (20,788) |
| At December 31, 1996 | 297,025 | | 784 | 1,681 | 12 | 11,422 | 1,516 | 26,990 | 68,629 | 83,511 | 491,570 |
| Revaluation reserve released to retained earnings | | | | | | (525) | | | | 525 | |
| Net income for the year | | | | | | | | | | 42,548 | 42,548 |
| Appropriation to reserve | | | | | | | | 2,127 | | (2,127) | |
| At December 31, 1997 | <u>297,025</u> | <u></u> | <u>784</u> | <u>1,681</u> | <u>12</u> | <u>10,897</u> | <u>1,516</u> | <u>29,117</u> | <u>68,629</u> | <u>124,457</u> | <u>534,118</u> |

The accompanying notes are an integral part of these financial statements.

Samarco Mineração S.A.

Statement of Changes in Financial Position Years Ended December 31 In thousands of reais

(A free translation of the original in Portuguese
prepared in conformity with accounting principles
determined by Brazilian corporate legislation)

| Financial resources were provided by: | <u>1997</u> | <u>1996</u> |
|---|-----------------------------|-------------------------|
| Operations | | |
| Net income for the year | 42,548 | 23,623 |
| Expenses not affecting working capital | | |
| Depreciation | 32,640 | 29,452 |
| Amortization of deferred charges | 1,064 | 1,330 |
| Residual value of property, plant and equipment disposals | 158 | 526 |
| Provision for losses on Eletrobrás investments | 681 | 270 |
| Exchange differences and monetary correction on long-term loans | <u>14,467</u> | <u>6,800</u> |
| | 91,558 | 62,001 |
| Third parties | | |
| Decrease in long-term receivables | 15,237 | 1,681 |
| Increase in long-term liabilities | <u>141,518</u> | <u>97,724</u> |
| Total funds provided | <u>248,313</u> | <u>161,406</u> |
| Financial resources were used for: | | |
| Long-term receivables | | |
| Deposits and compulsory loans | 1,696 | 1,261 |
| Receivables from stockholders and related companies | 10,557 | 15,815 |
| Other accounts receivable | 874 | 1,223 |
| Taxes recoverable | | 270 |
| Permanent assets | | |
| Property, plant and equipment | 238,442 | 230,302 |
| Investments | 980 | 7,516 |
| Transfer from long-term to current liabilities | 61,697 | 3,190 |
| Dividends | <u> </u> | <u>20,788</u> |
| Total funds used | <u>314,246</u> | <u>280,365</u> |
| Decrease in working capital | <u>(65,933)</u> | <u>(118,959)</u> |

Samarco Mineração S.A.

Statement of Changes in Financial Position Years Ended December 31

In thousands of reais

(continued)

| | <u>1997</u> | <u>1996</u> |
|------------------------------------|-----------------|------------------|
| Current assets | | |
| At the end of the year | 126,114 | 76,903 |
| At the beginning of the year | <u>76,903</u> | <u>127,150</u> |
| | <u>49,211</u> | <u>(50,247)</u> |
| Current liabilities | | |
| At the end of the year | 266,405 | 151,261 |
| At the beginning of the year | <u>151,261</u> | <u>82,549</u> |
| | <u>115,144</u> | <u>68,712</u> |
| Decrease in working capital | <u>(65,933)</u> | <u>(118,959)</u> |

The accompanying notes are an integral part of these financial statements.

(A free translation of the original notes in Portuguese to financial statements prepared in conformity with accounting principles determined by Brazilian corporate
Samarco Mineração S.A.

**Notes to the Financial Statements
at December 31, 1997 and 1996**

All amounts in thousands of reais unless otherwise indicated

1 Operations

The company operates an integrated iron ore pelletizing operation based on the mining and concentration of low grade iron ore (Germano/Alegria) and its transportation via a slurry pipeline system, pelletizing and subsequent export through its own maritime terminal (Ponta Ubu). Most of the production is exported.

The iron ore reserves ceded by the parent company and to which the company has the mining rights, are currently estimated at 5.6 billion metric tons. Production for the year ended December 31, 1997 was 9.6 million metric tons of pellets and pellet feed (9.1 million metric tons in 1996).

The second pelletizing plant started operations in the second half of November, 1997. This expansion project, which started in 1995, will double the productive capacity of pellets to 12 million tons a year. The investment in this project has amounted to US\$ 324.5 million. A further US\$ 11.5 million will be invested in 1998 to complete the project.

2 Presentation of Financial Statements

The financial statements as at December 31, 1997 and 1996 were prepared in conformity with the requirements of Brazilian corporate legislation and are presented in thousands of reais.

3 Significant Accounting Policies

(a) Determination of net income

Net income is determined on the accrual basis.

(b) Current assets and long-term receivables

Inventories are stated at the average cost of purchase or production, which is lower than replacement cost or net realizable value. Other assets are stated at realizable values and include accrued income and monetary correction, where applicable, except for prepaid expenses which are stated at cost.

Samarco Mineração S.A.

Notes to the Financial Statements at December 31, 1997 and 1996

All amounts in thousands of reais unless otherwise indicated

(c) Permanent assets

Permanent assets are stated at cost, including restatements up to December 31, 1995 based on official indices, and take the following matters into consideration:

- . Depreciation of property, plant and equipment is calculated on a straight-line basis at the rates, based on a technical appraisal, disclosed in Note 7.
- . Buildings, the slurry pipeline and related systems were revalued in 1980; the shipping terminal and stockpile equipment were revalued in 1986 (Note 7).
- . Deferred charges are amortized over periods of five and ten years as from the dates the benefits start to accrue.

(d) Current and long-term liabilities

Liabilities are stated at their known or estimated amounts, including accrued charges, monetary correction and exchange differences, where applicable, on a daily pro rata basis.

(e) Provision for income tax

The income tax provision is calculated at the reduced tax rate of 18% applicable to profits from exports.

4 Short-term Investments

These refer mainly to a deposit of US\$ 7.1 million (1996 - US\$ 6.4 million) in an "Escrow Account", subject to exchange differences plus variable interest of between 5.0% and 5.5% per annum.

Samarco Mineração S.A.

Notes to the Financial Statements at December 31, 1997 and 1996

All amounts in thousands of reais unless otherwise indicated

5 Other Accounts Receivable

| | <u>1997</u> | <u>1996</u> |
|---|---------------|---------------|
| Taxes and contributions recoverable | | |
| Value-added tax on sales and services (ICMS) | 25,484 | 6,504 |
| Income tax | 5,569 | 22 |
| Social integration program (PIS) | | 3,198 |
| Companhia Siderúrgica Belgo-Mineira | 11,012 | |
| Belgo-Mineira Participação Indústria e Comércio Ltda. | 5,810 | |
| Advances to employees | 1,717 | 1,466 |
| Advances for customs clearance | 183 | 2,777 |
| Other | <u>2,635</u> | <u>1,719</u> |
| | <u>52,410</u> | <u>15,686</u> |

6 Inventories

| | <u>1997</u> | <u>1996</u> |
|--------------------------------------|---------------|---------------|
| Finished products | 18,106 | 8,551 |
| Concentrate in process | 6,224 | 8,139 |
| Consumable materials and spare parts | 14,635 | 13,402 |
| Advances to suppliers | 3,080 | 1,845 |
| Other | <u>916</u> | <u>187</u> |
| | <u>42,961</u> | <u>32,124</u> |

Samarco Mineração S.A.

**Notes to the Financial Statements
at December 31, 1997 and 1996**

All amounts in thousands of reais unless otherwise indicated

7 Property, Plant and Equipment

| | | | <u>1997</u> | <u>1996</u> | <u>%</u> | |
|--|------------------|--------------------|-------------------------------------|----------------|----------------|--|
| | <u>Cost</u> | <u>Revaluation</u> | <u>Accumulated depreciation</u> | <u>Net</u> | <u>Net</u> | <u>Annual depreciation rates</u> |
| Land | 1,706 | | | 1,706 | 1,747 | |
| Working rights | 303 | | | 303 | 303 | |
| Transportation rights | 1,578 | | | 1,578 | 1,578 | |
| Mining rights | 12,763 | | 1,348 | 11,415 | 12,842 | 5,0 |
| Other rights | 695 | | 557 | 138 | 138 | 7,50 |
| Industrial facilities (buildings, machinery and equipment) | 920,840 | 8,227 | 226,613 | 702,454 | 261,437 | 3.03 to 10.0 |
| Slurry pipeline and systems | 253,419 | 36,923 | 148,373 | 141,969 | 105,659 | 3.09 to 5.26 |
| Stockpile equipment and shipping terminal | 114,383 | 20,707 | 73,115 | 61,975 | 65,793 | 3.47 to 4,21 |
| Furniture and fixtures | 4,782 | | 3,768 | 1,014 | 819 | 12.50 |
| Vessels | 1,847 | | 689 | 1,158 | 1,245 | 4.00 |
| Vehicles | 25,448 | | 14,951 | 10,497 | 12,534 | 14.29 to 20.00 |
| Construction in progress | | | | | 264,468 | |
| | <u>1,337,764</u> | <u>65,857</u> | <u>469,414</u> | <u>934,207</u> | <u>728,563</u> | |

The increase in property, plant and equipment accounts relates mainly to investments in the new pelletizing plant, as described in Note 1.

Samarco Mineração S.A.

Notes to the Financial Statements at December 31, 1997 and 1996

All amounts in thousands of reais unless otherwise indicated

8 Loans

| | <u>1997</u> | <u>1996</u> |
|--|-----------------|-------------------|
| Foreign currency - US\$ - 223.4 million (1996 - US\$ 144.1 million) | 249,422 | 149,811 |
| Local currency | <u>105,487</u> | <u>77,920</u> |
| | 354,909 | 227,731 |
| Current | <u>(74,595)</u> | <u>(41,623)</u> |
| Long-term | <u>280,314</u> | <u>186,108</u> |
| Long-term amounts fall due as follows: | | |
| | <u>1997</u> | <u>1996</u> |
| 1998 | | 45,735 |
| 1999 | 56,234 | 33,816 |
| 2000 | 64,039 | 30,981 |
| 2001 | 59,200 | 30,981 |
| 2002 | 47,797 | 24,298 |
| 2003 | 24,410 | 11,249 |
| 2004 | 20,039 | 9,048 |
| Other | <u>8,595</u> | <u> </u> |
| | <u>280,314</u> | <u>186,108</u> |

Foreign currency loans are subject to exchange differences and to interest of either LIBOR plus 0.5% p.a. or to a fixed interest rate of 10% p.a. These loans are secured by charges on machinery and equipment, the proceeds of exports and guarantees given by the shareholders.

Local currency loans are subject to the long-term interest rate (TJLP) and to a spread of 2.5% to 4% per annum. These loans are also secured by charges on machinery and equipment and guarantees given by the shareholders.

Samarco Mineração S.A.

Notes to the Financial Statements at December 31, 1997 and 1996

All amounts in thousands of reais unless otherwise indicated

9 Advances Against Export Contracts

The advances against export contracts were received to finance working capital and to serve as a bridging loan for the company's expansion projects. These advances are due to be repaid from January to September 1998, plus exchange differences and interest of 5% to 7% per annum.

10 Taxes and Contributions

(a) Income tax

To protect stockholders' interests, the company requested a court injunction to relieve it of the obligation to pay additional income tax on profits from exports sales in 1989, as a result of an increase in the tax rate introduced by Law 7988/89. This additional tax has not been provided for in the financial statements, but the full amount has been deposited with the courts. The restated balance at December 31, 1997 amounts to R\$ 4.7 million.

In 1991, the company filed a Declaratory Action against the Federal Government because it understood that it was not affected by the increase in income tax rates on profits from the export of services and manufactured products, introduced by Law No. 8034/90, and that it had not lost the tax incentives to which it was entitled by the terms of Decree Law 1.240/40 ("export of abundant minerals"). Corporate counsel believe that the company's chances of success in this case are very favorable. On November 18, 1997, the First Regional Court - Brasília ruled unanimously in the company's favour. As at December 31, 1997, the contingent liability in this respect amounts to approximately R\$ 52.3 million.

(b) Social contribution on net income

In December 1993, as it had been successful in its action against the Federal Government proving that it was not liable to pay the social contribution on net income, the amount deposited with the courts was returned to the company (approximately R\$ 28.2 million in terms of price-levels at December 31, 1997), at which time the provision for the payment of this contribution was reversed to the credit of income in 1993.

The Federal Government filed an action to have the court's decision annulled, claiming payment of the contribution as from 1989. A final decision in the company's favour was given on September 30, 1996.

Samarco Mineração S.A.

Notes to the Financial Statements at December 31, 1997 and 1996

All amounts in thousands of reais unless otherwise indicated

(c) Value-added tax on sales and services (ICMS)

Based on an interpretation of Complementary Law No. 65 of April 1991 and the opinion of its legal advisors, the company believes that it is not liable to pay ICMS on semi-finished products and makes no provision therefor in its financial statements. This matter is still being discussed in the lower courts.

11 Stockholders' Equity

- (a)** Capital comprises 5,243,308 thousand shares with no par value, of which 2,621,654 thousand are common shares and 2,621,654 thousand are preferred shares (Class A - 1,337,044 thousand; Class B - 1,284,610 thousand).

Preferred shares have no voting rights but have priority to the return of capital, without a premium, and participate equally with the common shares in the receipt of dividends.

(b) Dividends

Stockholders are entitled to a minimum annual dividend equal to 5% of net income as adjusted in accordance with the company's statutes and Brazilian corporate law. No provision has been made for the minimum dividend this year as the stockholders have declared that the whole of the net income for 1997 is to be retained to meet investments and commitments foreseen in the company's budget.

(c) Retained profits reserve

At December 31, 1995, based on a capital budget approved by the stockholders, a retained profits reserve in the amount of R\$ 68.6 million was created to finance future investments, in conformity with Article 196 of Corporate Law.

Samarco Mineração S.A.

Notes to the Financial Statements at December 31, 1997 and 1996

All amounts in thousands of reais unless otherwise indicated

12 Related Parties

The principal transactions and balances with stockholders and related companies included in the financial statements as at December 31, 1997 and 1996 (which were carried out at normal market prices and conditions) can be summarized as follows:

| | | | | | | <u>1997</u> | <u>1996</u> | |
|---|---|---------------------------------|-------------------------------------|--|---|--------------|--------------|--------------|
| Balance sheet | S.A. Mineração da Trindade - SAMITRI | BHP Brasil Ltda. | BHP Minerals Int Inc | Usina Hidrelétrica Guilman- Amorin S.A. | Companhia Siderurgia Belgo-Mineira | Other | Total | Total |
| Current assets | | | | | | | | |
| Trade accounts receivable | | | | | | | 20,454 | |
| Receivables from stockholders and related companies | | 8 | | | | 8 | 1,471 | |
| Inventories (advances to suppliers) | | | 250 | | | | 250 | |
| Other accounts receivable | | | | | 11,012 | 5,810 | 16,822 | |
| Long-term receivables | | | | | | | | |
| Receivables from stockholders and related companies | | | | | | | 14,840 | |
| Permanent assets | | | | | | | | |
| Investments | | | | 8,496 | | 129 | 8,625 | |
| Current liabilities | | | | | | | | |
| Suppliers | 965 | | 217 | | 22 | 21 | 1,225 | |
| Proposed dividends | | | | | | | 20,788 | |
| Other accounts payable | | | 523 | | | | 523 | |
| Long-term liabilities | | | | | | | | |
| Other | | | | | | | 10,161 | |

The associated company, Usina Hidrelétrica Guilman-Amorim S.A., received loans from the National Bank for Economic and Social Development (BNDES) and from Banco BBA Creditanstalt, in the amount of R\$ 120.9 million. The loans were backed by Samarco Mineração S.A. with guarantees from its major stockholder - S.A. Mineração da Trindade - SAMITRI.

Samarco Mineração S.A.

Notes to the Financial Statements at December 31, 1997 and 1996

All amounts in thousands of reais unless otherwise indicated

| | | | | | | <u>1997</u> | <u>1996</u> | |
|--|---|---------------------------------|-------------------------------------|--|---|--------------|--------------|--------------|
| | <u>S.A. Mineração da Trindade - SAMITRI</u> | <u>BHP Brasil Ltda.</u> | <u>BHP Minerals Int Inc</u> | <u>Usina Hidrelétrica Guilman- Amorin S.A.</u> | <u>Companhia Siderúrgica Belgo- Mineira</u> | <u>Other</u> | <u>Total</u> | <u>Total</u> |
| Statement of income | | | | | | | | |
| Operating revenue | 2,221 | | | | | 2,221 | 195,344 | |
| Cost of sales | 7,210 | | 2,277 | | 435 | 9,922 | 9,812 | |
| Selling expenses | | | 8,695 | | | 8,695 | 9,569 | |
| Monetary correction and exchange differences | | | | | | | | |
| . Expense | | | 26 | | | 26 | 138 | |
| . Income | | | | | | | 1,783 | |
| Financial expenses | 2,347 | | | | | 2,347 | 140 | |
| Financial income | | | | 420 | | 420 | 3,322 | |
| General and administrative expenses | | | | | | | 1,289 | |
| Other operating expenses | 841 | | | | | 841 | 782 | |

Samarco Mineração S.A.

Notes to the Financial Statements at December 31, 1997 and 1996

All amounts in thousands of reais unless otherwise indicated

13 Insurance Cover

The company maintains insurance cover in amounts considered sufficient to meet possible risks. The insurance cover for property, plant and equipment at December 31, 1997 amounted to R\$ 1,484 million (1996 - R\$ 1,078 million).

14 Financial Instruments

The company's financial instruments are recorded in asset and liability accounts at December 31, 1997 in amounts compatible with those practiced in the market. Management of these instruments is effected through operating controls and strategic policies, to assure liquidity, profitability and security.

The company does not invest in derivatives or similar risk assets.

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BOARD OF DIRECTORS

JOSÉ LUCIANO DUARTE PENIDO
Director-President

WALTER GONÇALVES TAVEIRA
Financial Director

RUBEN ELIAS BREÑA BREÑA
Industrial Director

CARLOS ALBERTO CÉZAR DE ANDRADE
Sales Director

ACCOUNTANT

PETRÔNIO LANARE DE PAULA
CRC-MG 31.972 "S" ES