



China – Challenges and Opportunities

Murilo Ferreira, Vale CEO

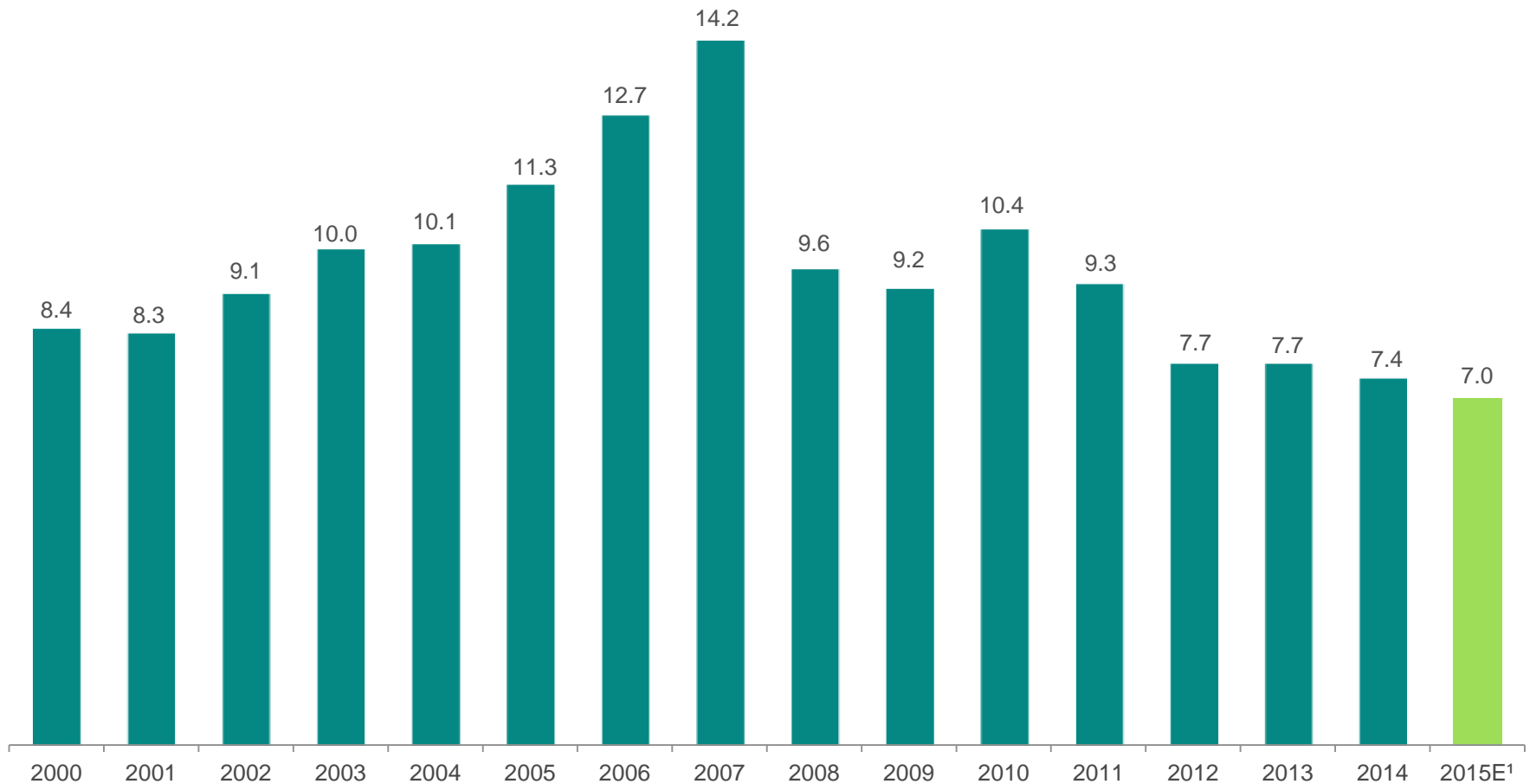
Rio de Janeiro, June 10, 2015

Main messages

- The Chinese economy has been slowing down albeit from a much larger GDP base
- The Chinese Government is taking support measures to achieve its economic growth targets and expand the country's global influence
- China will remain very important for the world economy and be an even more important trade partner for Brazil

China's GDP growth has been slowing down to what is now considered a "new normal"

GDP growth, %

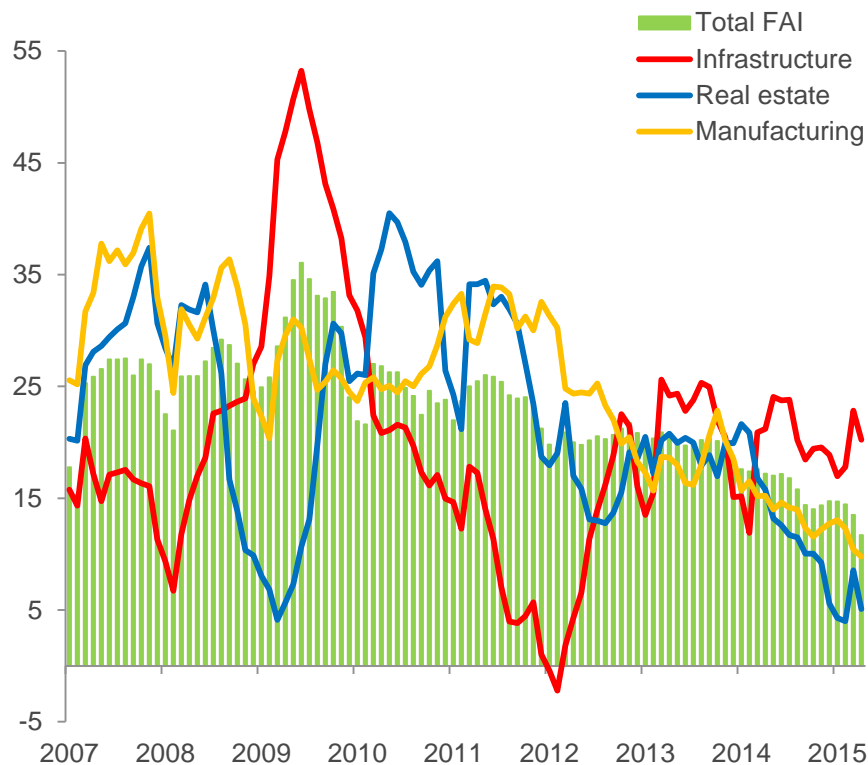


¹ Projection from Chinese Government.
Source: IMF

Fixed asset investments are growing at a lower pace

Fixed Assets Investments (FAI)

Growth rate (% y/y 3mma¹)



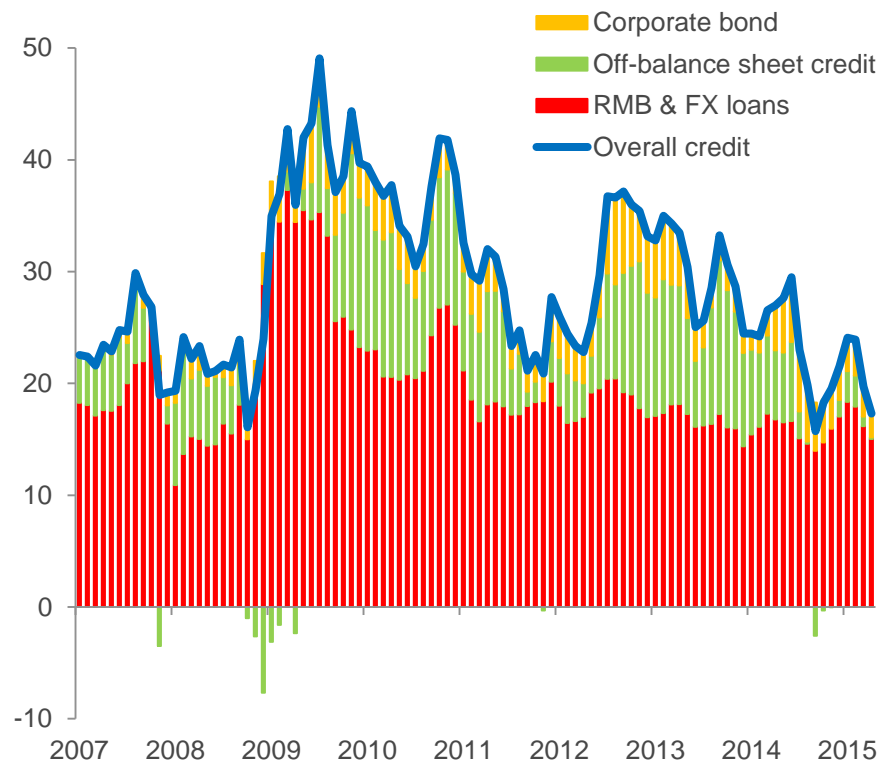
- Investments in real estate, infrastructure and manufacturing shrank significantly from 2013 to 2014 with reduction in investments in:
 - Real estate, from 19.8% to 10.5%
 - Industry from 18.5% to 13.5%
 - Infrastructure from 21.2% to 20.3%
- The main reason for the slowdown in the Chinese economy was the contraction of the real estate sector (2014 vs. 2013):
 - Real estate sales fell by 7.6%
 - Newbuild shrank by 10.7% (residential 14.4%)

¹ Three month moving average

Credit has tightened as shadow bank practically ceased

Monthly overall credit

Share in GDP (% , sa, 3mma¹)



- Overall credit as a percentage of GDP increased strongly after 2009, when the central government approved a package to stimulate investments as a response to the global financial crisis
 - Off-balance sheet credit was the main driver of credit growth after 2009
- Since 2013, the Central government has imposed restrictions to contain off-balance sheet credit, impacting the total availability of credit

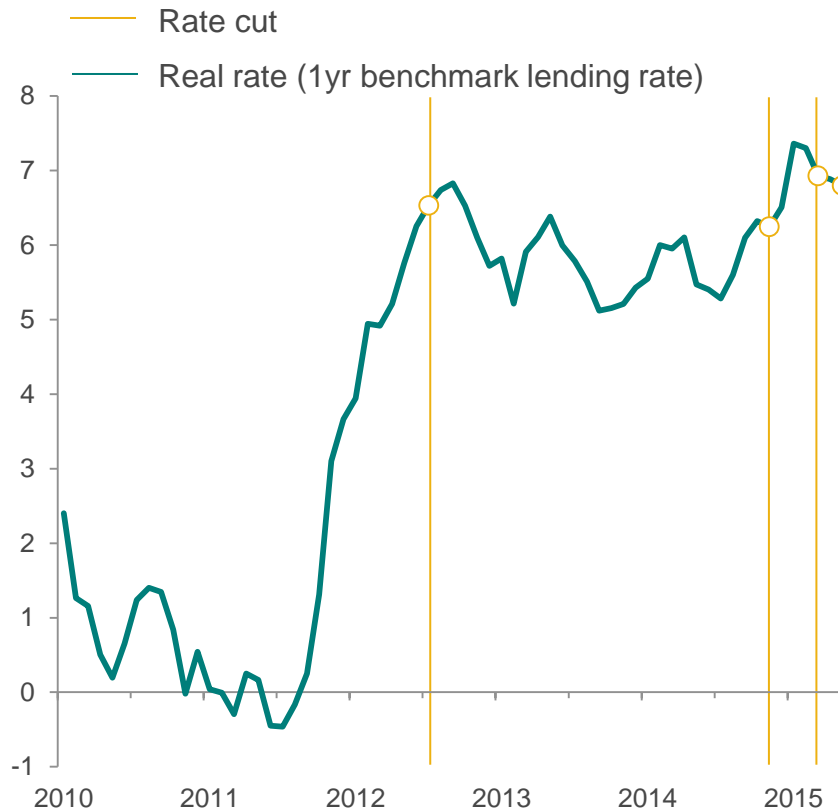
¹ Three month moving average

Source: CEIC, UBS estimates

Real interest rates remain at higher levels despite recent rate cuts

Real interest rate

% per annum, CPI & PPI average deflated



- The PBoC cut interest rates three times in the last six months to stimulate the economy
- Real interest rates have increased since 2010 and remain above the 2014 average given the PPI deflation

¹ The real interest rate is the nominal interest rate less inflation.

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The Chinese government is taking several initiatives to support GDP growth

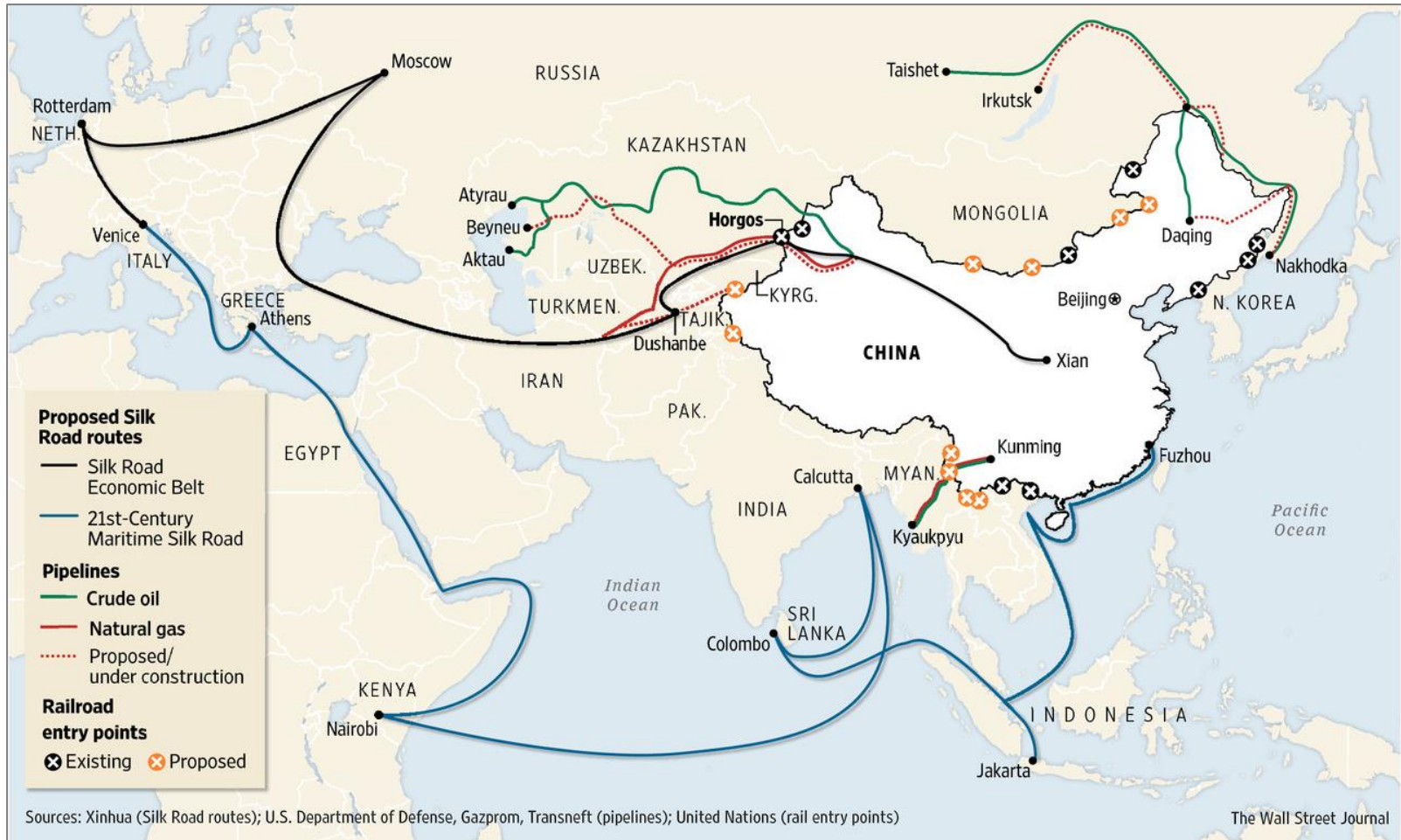
Several initiatives were taken by the Chinese government

Goals

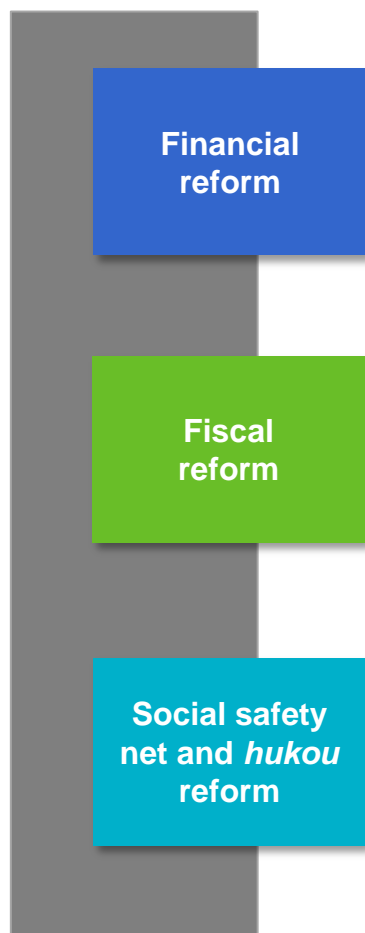
- Support investment in the real estate market
- Stimulate and direct local governments investments towards key infrastructure projects
- Reduce credit risk and increase liquidity in the financial system
- Create demand for Chinese products and services outside China

The new silk road economic belt will help the export of Chinese products and services

The new silk road | China assembling new trade routes, binding other regions closer to it



Meanwhile reforms which are more supportive of growth and help rebalance China's economic structure were prioritized



Current priorities

- Internationalization of the RMB through less capital control and interest rate liberalization
- Restructuring of local government's debt to contain financial risks and control credit growth
- Relaxation of the *hukou* policies in some small cities and implementation of pilot projects in others to encourage "urbanization" of rural migrants

With the reforms the RMB is expected to maintain its relative value against the USD



- Even after the depreciation of major currencies, the RMB has remained practically stable against the USD
- The Chinese government is expected to keep the RMB relatively stable against the USD despite the expected USD strengthening and the persistent net capital outflows since China is seeking the internationalization of the RMB
- China has a sizable and growing current account surplus, even after a continuing appreciation of the RMB started in 2011

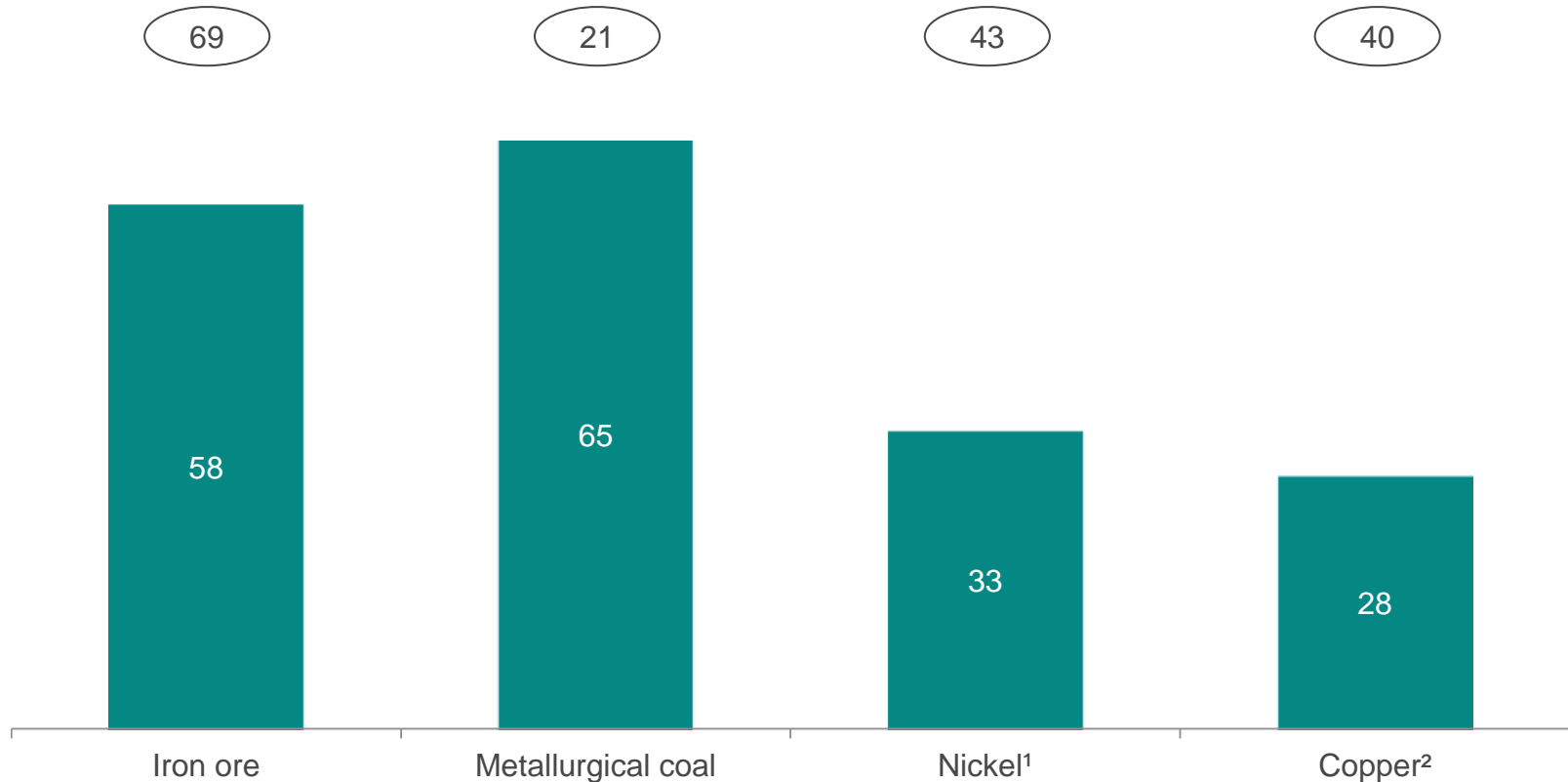
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China is very important for the mineral commodities market

Share of global demand in 2014 - %

○ Share of seaborne trade, %



¹ Based on the non-integrated seaborne market for nickel concentrate (not considering ore used in production of nickel pig iron from Indonesia, the Philippines, among others).

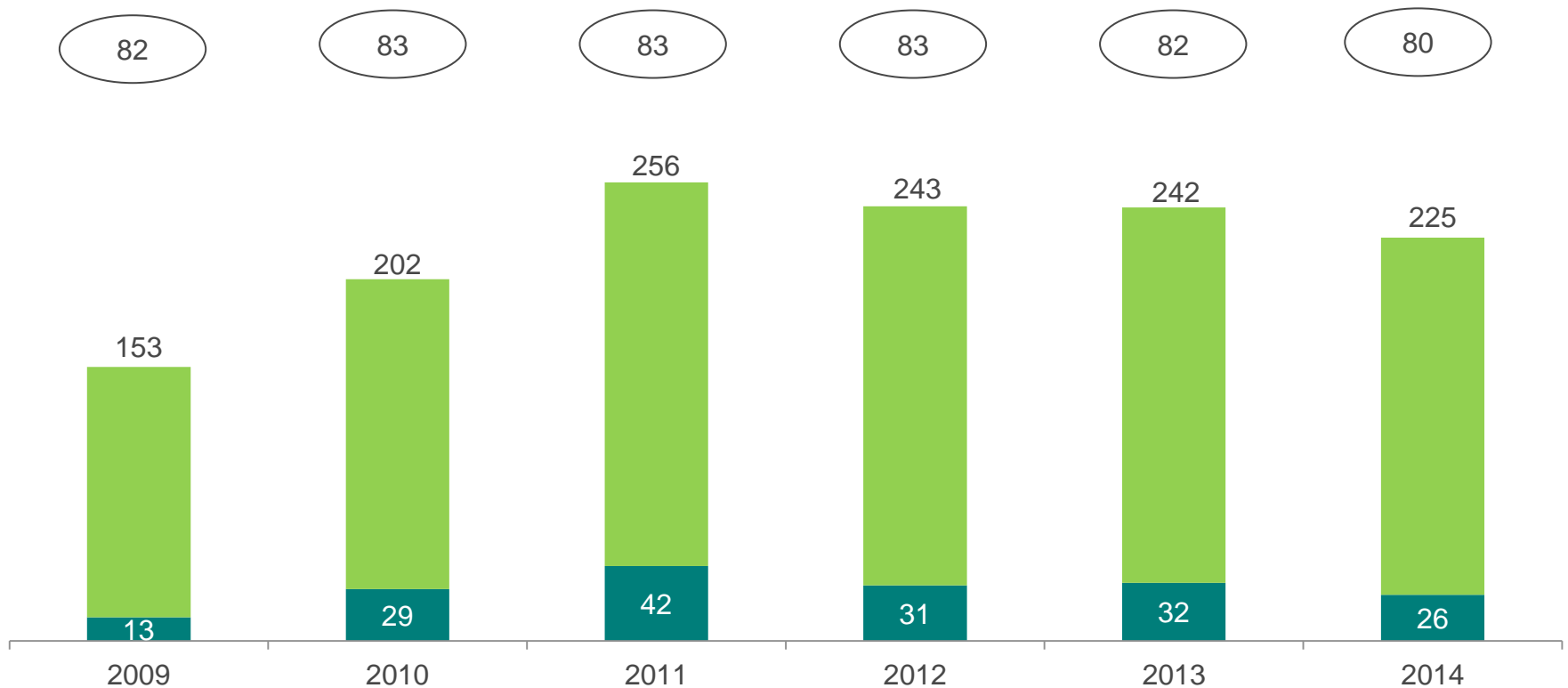
² Based on the non-integrated seaborne market for copper concentrate

Source: CRU, WoodMackenzie

Iron ore alone represents about 10% of the revenues from Brazilian exports

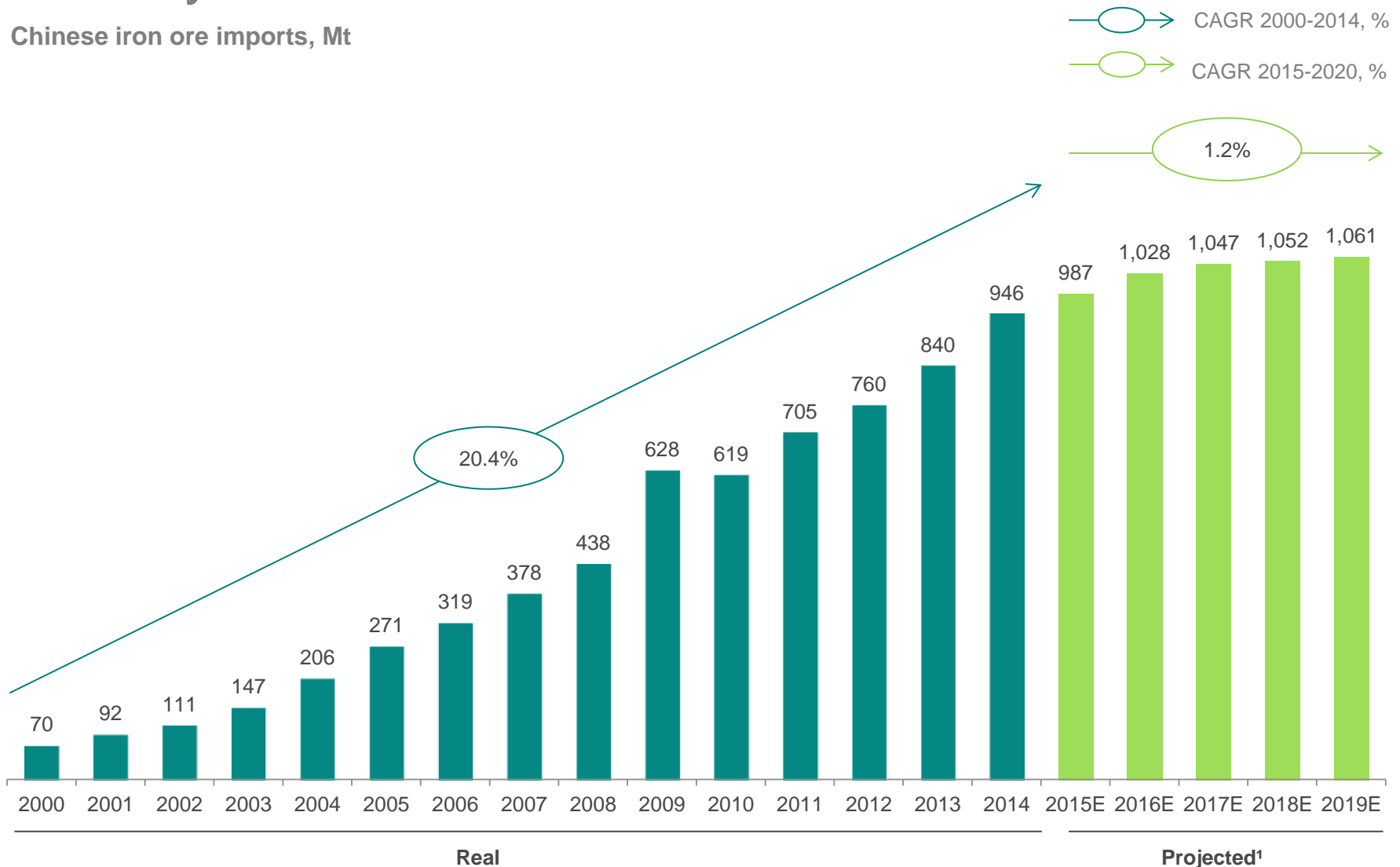
Brazilian exports in US\$ billions

○ Vale's share in iron ore exports, %
 ■ Iron ore exports in US\$ billions



China's iron ore imports are expected to grow only moderately in the next years under the "new normal"

Chinese iron ore imports, Mt



¹ Bank average (Macquarie, Citi, BTGPactual, UBS, Morgan Stanley, Clarkson) and research institutions (CRU)
Source: China Customs

But the opportunities go beyond the export of commodities



- During Premier Li Keqiang's visit to Brazil a few cooperation agreements were emphasized:
 - The construction of the railway line to connect the Atlantic to the Pacific ocean;
 - The set up of a Latin America Fund, investing USD30 billion to help with capacity cooperation
- Vale, in particular, signed MOUs with partners in the shipping business and with the Chinese Exim Bank

Final remarks

- Chinese GDP growth has been slowing down to a “new normal”
- However, the Chinese government is acting promptly to support the domestic market and to create demand for Chinese products and services outside China
- Meanwhile the Chinese government is progressing with the structural reforms and working to increase its political and financial influence in the international financial markets with the internationalization of the RMB
- In the case of Brazil, China currently is and will remain a very important business partner as new cooperation opportunities arise

