RISK FACTORS

Risks relating to our business

A decline in demand for steel would adversely affect our business.

Demand for our most important products depends on global demand for steel. Iron ore and iron ore pellets, which together accounted for 44.2% of our 2007 gross revenues, are used to produce carbon steel. Nickel, which accounted for 30.3% of our 2007 gross revenues, is used mainly to produce stainless steel. Demand for steel depends heavily on global economic conditions, but it also depends on a variety of regional and sectoral factors, and demand for stainless steel is partly independent of demand for carbon steel. The prices of different steels and the performance of the global steel industry are highly cyclical, and these business cycles in the steel industry affect demand and prices for our products.

In recent years, growing worldwide demand for carbon steel has led to strong demand and rising prices for iron ore and iron ore pellets. However, in the event of a sustained decline in prices or sales volumes for iron ore and iron ore pellets would have a material adverse effect on our revenues and earnings. Consolidation in the steelmaking industry may lead to backward integration, which could reduce the global seaborne trade of iron ore.

Growing demand for stainless steel has contributed to strong demand and rising prices for nickel, leading to record-high nickel prices in the second quarter of 2007. In response to high prices, producers and consumers of stainless steel have been shifting to stainless steels with lower nickel content. A sustained decline in austenitic stainless steel production, which could potentially result from a technological development that reduces the amount of nickel required in stainless steel, would have a material adverse effect on our revenues from nickel.

Adverse economic developments in our principal markets, especially China, could reduce demand for our products, leading to lower revenues and profitability.

The global economy is the primary driver of demand in the global market for minerals and metals. In recent years, China has been the main driver of minerals and metals demand and of our sales increases. In 2007, China represented approximately 49% of the global demand for seaborne iron ore, 24.2% of global demand for nickel, 33% for aluminum and 26.3% for copper.

The percentage of our gross revenues attributable to sales to customers in China was 17.7% in 2007. The percentage of our gross revenues attributable to sales to customers from Asian countries other than China was 23.3% in 2007. The percentage of our gross revenues attributable to sales to European customers was 22.1% in 2007. A weakened global economy or a weakened economy in specific markets where we sell our products, such as China, could reduce demand for our products, leading to lower revenues and profitability.

The prices of nickel, aluminum and copper, which are actively traded on world commodity exchanges, are subject to significant volatility.

Nickel, aluminum and copper are sold in an active global market and traded on commodity exchanges, such as the London Metal Exchange and the New York Mercantile Exchange. Prices for these metals are subject to significant fluctuations and are affected by many factors, including actual and expected global macroeconomic and political conditions, levels of supply and demand, the availability and cost of substitutes, inventory, investments by commodity funds and others and actions of participants in the commodity markets. Prices for these metals are more volatile than contractual prices for products such as iron ore, iron ore pellets and metallurgical coal, because they respond more quickly to actual and expected changes in market conditions.

Increased substitution of primary nickel could adversely affect our nickel business.

Demand for primary nickel may be negatively impacted by the substitution of primary nickel with other materials in current applications. Scrap nickel competes directly with primary nickel as a source of nickel for use in the production of stainless steel, and the choice between them is largely driven by their relative prices and availability. In 2007, the stainless steel scrap ratio is estimated to have remained unchanged compared to 2006, at 48%. Nickel pig iron, a product developed by Chinese steel and alloy makers that utilizes low-grade lateritic nickel ores, competes with other nickel sources in the production of stainless steel. In 2007, nickel pig iron represented an estimated 6% of world primary nickel supply, compared to 2% in 2006.

A reduction of global demand for Brazilian steel or agriculture products could reduce the demand for our logistics services.

The Brazilian agriculture and steel industries are currently the primary drivers of demand for our logistics services to customers. The percentage of our logistics revenues attributable to these industries was 83.9% in 2007. A reduction in world demand for Brazilian steel or agricultural products could reduce demand for our logistics services and harm the profitability of our logistics business.

We may not be able to successfully integrate our acquired businesses.

We have grown our business in part through acquisitions, and some of our future growth may also stem from acquisitions. We may not be able to successfully integrate acquired businesses or generate the cost savings and synergies anticipated, which could negatively affect our financial condition and results of operations.

The mining industry is intensely competitive, and we may have difficulty effectively competing with other mining companies in the future.

Intense competition characterizes the global mining industry. We compete with a large number of mining companies. Some of them possess substantial mineral deposits at locations closer to our principal customers. Competition from other producers may result in our loss of market share and revenues.

Demand for our products in peak periods may outstrip our production capacity, rendering us unable to satisfy customer demand.

Our ability to rapidly increase production capacity to satisfy increases in demand for our products is limited. In periods when customer demand exceeds our production capacity, we may meet excess customer demand by reselling iron ore, iron ore pellets or nickel purchased from joint ventures or unrelated parties. If we are unable to satisfy excess customer demand in this way, we may lose customers. We may be unable to complete expansion and greenfield projects in time to take advantage of the current high levels of worldwide demand for iron ore and nickel.

We have been operating at or above full capacity in our iron ore systems since 2003. As a result, disruptions in operations in any part of our integrated systems, or maintenance programs that require more time than expected, could result in lower volumes and lower revenues. In addition, operating at or above full capacity may expose us to higher costs, including demurrage fees due to capacity restraints in our logistics systems.

Political, economic, regulatory and social conditions in the countries in which we operate or have projects could adversely impact our business and the market price of our securities.

Our financial performance may be negatively affected by general economic, political, regulatory and social conditions in countries in which we have significant operations or projects, particularly Brazil, Canada, Indonesia, Australia, New Caledonia and Mozambique. Actual or potential political changes and changes in economic policy may undermine investor confidence, result in economic slowdowns and otherwise adversely affect the economic and other conditions under which we operate in ways that could have a material adverse effect on our business. Governments in emerging economies such as Brazil, Indonesia and New Caledonia frequently intervene in the economy and occasionally make substantial changes in policy that could adversely affect exchange rates, inflation, interest rates, rates of taxes or royalties and the economic and regulatory environment in which we operate. In New Caledonia, a planned referendum in 2014 may result in New Caledonia becoming fully independent from France, which could result in significant political and economic changes in New Caledonia and may adversely affect our Goro project. See *Item 4. Information on the company—Regulatory matters—Mining regulation.*

Acts by protestors may hamper our mining and logistics operations and projects.

Protestors have taken actions to disrupt our operations and projects, and they may continue to do so in the future. For example, in New Caledonia, in the past protestors caused physical damage to our Goro project and have impeded the construction of the marine pipeline. Although we vigorously defend ourselves against illegal acts, while supporting the communities living near our operations, future attempts by protestors to harm our operations could adversely affect our business.

Our projects are subject to risks that may result in increased costs or delay or prevent their successful implementation.

We are investing heavily to further increase our production capacity, logistics capabilities and to expand the scope of minerals we produce. Our expansion and mining projects are subject to a number of risks that may adversely affect our growth prospects and profitability, including the following:

- We may encounter delays or higher than expected costs in obtaining the necessary equipment or services to build and operate a project.
- Our efforts to develop projects according to schedule may be hampered by a lack of infrastructure, including a reliable power supply.
- We may fail to obtain, or experience delays or higher than expected costs in obtaining, the required permits to build a project.
- Changes in market conditions or regulations may make a project less profitable than expected at the time we initiated work on it.
- Adverse mining conditions may delay and hamper our ability to produce the expected quantities of minerals.
- Some of our development projects are located in regions where tropical diseases, AIDS, malaria, yellow fever and other contagious diseases are a major public health issue and pose health and safety risks to our employees. If we are unable to ensure the health and safety of our employees, our business may be adversely affected.

Our principal shareholder has significant influence over our company.

At December 31, 2007, Valepar S.A. owned 53.3% of our outstanding common stock and 32.5% of our total outstanding capital. For a description of our ownership structure, see *Item 7. Major shareholders and related party transactions—Major shareholders—Principal shareholder*. As a result of its share ownership, Valepar can control the outcome of any action requiring shareholder approval, except for the appointment of certain directors and certain members of our fiscal council. Moreover, the Brazilian government owns 12 golden shares granting it limited veto power over certain actions that we could otherwise take. For a detailed description of the Brazilian government’s veto power by virtue of its ownership of these golden shares, see *Item 10. Additional information—Common shares and preferred shares—General*.

Our governance and compliance processes may fail to prevent regulatory penalties and reputational harm.

We operate in a global environment, and our activities straddle multiple jurisdictions and complex regulatory frameworks with increased enforcement activities worldwide. Our governance and compliance processes, which include the review of internal control over financial reporting, may not prevent future breaches of law, accounting or governance standards. We may be subject to breaches of our Code of Ethical Conduct, business conduct protocols and instances of fraudulent behavior and dishonesty by our employees, contractors or other agents. Our failure to comply with applicable laws and other standards could subject us to fines, loss of operating licenses and reputational harm.

Many of our operations depend on joint ventures or consortia, and our business could be adversely affected if our partners fail to observe their commitments.

We currently operate important parts of our pelletizing, nickel, bauxite, coal and steel businesses through joint ventures with other companies. Important parts of our electricity business are operated through consortia. Our forecasts and plans for these joint ventures and consortia assume that our partners will observe their obligations to make capital contributions, purchase products and, in some cases, provide managerial personnel. If any of our partners fails to observe its commitments, the affected joint venture or consortium may not be able to operate in accordance with its business plans, or we may have to increase the level of our investment to implement these plans. For more information about our joint ventures, see *Item 4. Information on the company—Lines of business*.

Our operations depend on authorizations from regulatory agencies in many jurisdictions, and changes in regulations could adversely affect our business.

Our operations depend on authorizations from and concessions by governmental regulatory agencies of the countries in which we operate, and we are subject to laws and regulations in many jurisdictions that can change at any time. Changes in laws and regulations may require modifications to our technologies and operations and result in unanticipated capital expenditures. For example, in Indonesia, the pending new mining legislation could have a material adverse effect on our PT Inco operations. For details about the authorizations and concessions upon which our operations activities depend, see *Item 4. Information on the company—Regulatory matters*.

Environmental, health and safety regulation may adversely affect our business.

Our operations often involve the use, handling, disposal and discharge of hazardous materials into the environment or the use of natural resources, and nearly all aspects of our operations and development projects around the world are subject to environmental, health and safety regulation. Such regulation requires us to obtain operating licenses, permits and other approvals and to conduct environmental assessments prior to initiating projects or undertaking significant changes to existing operations. Difficulties in obtaining licenses may lead to construction delays or cost increases, and in some cases may lead us to abandon a project. Environmental regulation also imposes standards and controls on activities relating to mining, exploration, development, production, reclamation, closure, and the refining, distribution and marketing of our products. Such regulation may give rise to significant costs and liabilities. In addition, community activist groups and other stakeholders may increase demands for environmentally-sustainable development, which could entail significant costs and reduce our profitability.

Environmental regulation in many countries in which we operate has become stricter in recent years, and it is possible that more regulation or more aggressive enforcement of existing regulations will adversely affect us by imposing restrictions on our activities, creating new requirements for the issuance or renewal of environmental licenses, raising our costs or requiring us to engage in expensive reclamation efforts. For example, in Brazil, environmental protection laws restrict our ability to expand operations without undertaking extensive conservation efforts. They also impose fees on development in protected areas, and many Brazilian states are considering implementing water usage fees, while one state, São Paulo, in which we do not have any operations is already charging water usage fees. In Canada, we may be required to conduct investigations or undertake remediation efforts in connection with elevated levels of metals in the soils near our Canadian facilities, which may involve significant expenditures. In addition, compliance with sulphur dioxide emissions limits could have an adverse impact on nickel production levels to the extent we are required to operate our facilities at reduced levels to comply with such limits or are unable to bank or trade sufficient emission allowances in emissions trading markets. For more information on environmental, health and safety regulation applicable to our operations, see *Item 4. Information on the company—Regulatory matters—Environmental regulation* and *Item 8. Financial information—Legal proceedings*.

Our reserve estimates may materially differ from mineral quantities that we may be able to actually recover; our estimates of mine life may prove inaccurate; and market price fluctuations and changes in operating and capital costs may render certain ore reserves uneconomical to mine.

Our reported ore reserves are estimated quantities of ore and minerals that we have determined can be economically mined and processed under present and anticipated conditions to extract their mineral content. There are numerous uncertainties inherent in estimating quantities of reserves and in projecting potential future rates of mineral production, including many factors beyond our control. Reserve engineering involves estimating deposits of minerals that cannot be measured in an exact manner, and the accuracy of any reserve estimate is a function of the quality of available data and engineering and geological interpretation and judgment. As a result, no assurance can be given that the indicated amount of ore will be recovered or that it will be recovered at the rates we anticipate. Estimates of different engineers may vary, and results of our mining and production subsequent to the date of an estimate may lead to revision of estimates. Reserve estimates and estimates of mine life may require revision based on actual production experience and other factors. For example, fluctuations in the market prices of minerals and metals, reduced recovery rates or increased operating and capital costs due to inflation, exchange rates or other factors may render proven and probable reserves uneconomic to exploit and may ultimately result in a restatement of reserves.

We may not be able to replenish our reserves, which could adversely affect our mining prospects.

We engage in mineral exploration, which is highly speculative in nature, involves many risks and frequently is nonproductive. Our exploration programs, which involve significant capital expenditures, may fail to result in the expansion or replacement of reserves depleted by current production. If we do not develop new reserves, we will not be able to sustain our current level of production beyond the remaining lives of our existing mines.

Even if we discover mineral deposits, we remain subject to drilling and production risks, which could adversely affect the mining process.

Once mineral deposits are discovered, it can take a number of years from the initial phases of drilling until production is possible, during which the economic feasibility of production may change. Substantial time and expenditures are required to:

- establish mineral reserves through drilling;
- determine appropriate mining and metallurgical processes for optimizing the recovery of metal contained in ore;
- obtain environmental and other licenses;
- construct mining, processing facilities and infrastructure required for greenfield properties; and
- obtain the ore or extract the metals from the ore.

If a project proves not to be economically feasible by the time we are able to exploit it, we may incur substantial write-offs. In addition, potential changes or complications involving metallurgical and other technological processes arising during the life of a project may result in cost overruns that may render the project not economically feasible.

We face rising extraction costs over time as reserves deplete.

Reserves are gradually depleted in the ordinary course of a given mining operation. As mining progresses, distances to the primary crusher and to waste deposits become longer, pits become steeper and underground operations become deeper. As a result, over time, we usually experience rising unit extraction costs with respect to each mine. Several of our mines have been operating for long periods, and we will likely experience rising extraction costs per unit in the future at these operations.

We face shortages of equipment, services and skilled personnel.

The mining industry faces worldwide shortages of mining and construction equipment, spare parts, contractors and other skilled personnel as a result of high demand for minerals and metals and the large number of projects under development. We are experiencing longer lead-times for mining equipment and problems with the quality of contracted engineering, construction and maintenance services. We are competing with other mining companies for highly skilled executives and staff with relevant industry and technical experience, and we may not be able to attract and retain such people. These shortages could negatively impact our operations, resulting in higher production costs, production interruptions, higher inventory costs, project delays and potentially lower production and revenues.

Labor disputes have disrupted our operations, and such disputes could recur.

A substantial number of our employees, and some of the employees of our subcontractors, are represented by labor unions and are covered by collective bargaining or other labor agreements, which are subject to periodic renegotiation. Renegotiation may become more difficult, as labor unions seek wage increases based on the higher prices and increased profits in the mining and metals industries. Strikes or work stoppages have occurred recently in Canada and Indonesia and could reoccur in connection with negotiations of new labor agreements or during other periods for other reasons. Moreover, we could be adversely affected by labor disruptions involving unrelated parties who may provide us with goods or services. Strikes and other labor disruptions at any of our operations could adversely affect the operation of facilities and the timing of completion and the cost of our capital projects.

Higher energy costs or energy shortages would adversely affect our business.

To fulfill our energy needs, we depend on oil by-products, which represented 49.4% of total energy needs in 2007 in TOE (tons of oil equivalent), natural gas (11.5% on the same basis), coal (3.8% on the same basis) and electricity (35.3% on the same basis). Fuel costs, which represented 8.5% of our cost of goods sold in 2007, are a major component of our total costs in our logistics, iron ore pellets and nickel businesses and indirectly affect numerous other areas of our business, including our mining and alumina businesses. Fuel prices increased by 17.9% in 2007. Increases in oil and gas prices adversely affect margins in our logistics, mining, iron ore pellets, finished nickel and alumina businesses.

Electricity costs are a significant component of the cost of our production, representing 5.3% of our total cost of goods sold in 2007. If we are unable to secure reliable access to electric energy at acceptable prices, we may be forced to curtail production or may experience higher production costs, either of which would adversely affect our results of operations. We currently generate 24.5% of our worldwide electricity needs from our own hydroelectric power plants and we are developing hydroelectric and thermal power plants and engaging in natural gas exploration programs in order to increase the amount of energy we produce and reduce our future exposure to price and supply volatility of energy.

Electricity shortages have occurred in Brazil in the past and could reoccur in the future, and there can be no assurance that the Brazilian government’s policies will succeed in encouraging growth in generation capacity. Future shortages, and government efforts to respond to or prevent shortages, may adversely impact the cost or supply of electricity for our Brazilian aluminum and ferroalloy operations. Changes in the laws, regulations or governmental policies regarding the power sector or concession requirements could reduce our expected returns from our investments in power generation. See *Item 4. Information on the company—Regulatory matters—Electric energy regulation.*

Through our subsidiary PT Inco in Indonesia, we process lateritic nickel ores, which is energy-intensive. Although PT Inco currently generates a majority of the electricity for its operations from its own hydroelectric power plants, hydrological factors, such as low rainfalls, could adversely affect electricity production at PT Inco’s plants in the future, which could significantly increase the risk of higher costs. For more information on the regulations governing energy production, see *Item 4. Information on the company—Regulatory matters—Electric energy regulation.*

Price volatility of the currencies in which we conduct operations relative to the U.S. dollar could adversely affect our financial condition and results of operations.

We are affected by fluctuations in the prices of the currencies in which we conduct operations relative to the U.S. dollar. A substantial portion of our revenues and debt is denominated in U.S. dollars, and changes in exchange rates may result in losses or gains on our net U.S. dollar-denominated indebtedness and accounts payable. In 2007, 2006 and 2005, changes in exchange rates produced net foreign exchange gains of US$1.639 billion, US$452 million and US$227 million, respectively. In addition, the price volatility of the Brazilian *real*, the Canadian dollar, the Indonesian rupiah and other currencies against the U.S. dollar affect our results since most of our costs of goods sold are denominated in currencies other than the U.S. dollar, principally the *real* (56.6% in 2007) and the Canadian dollar (23.3% in 2007), while our revenues are mostly U.S. dollar-denominated. Currency fluctuations are expected to continue to affect our financial income, expense and cash flow generation.

Significant volatility in currency prices may also result in disruption of countries’ foreign exchange markets and may limit our ability to transfer or to convert such currencies into U.S. dollars and other currencies for the purpose of making timely payments of interest and principal on our indebtedness. The governments of countries in which we operate may institute restrictive exchange rate policies in the future.

Investor perceptions of risk in Brazil and other emerging market economies may undermine our ability to finance our operations at an acceptable cost or reduce the trading price of our securities.

Although our acquisition of Inco in October 2006 significantly expanded the proportion of our non-Brazilian operations, our largest operations, corporate headquarters and senior management continue to be located in Brazil, which investors generally consider an emerging market. Economic crises in one or more emerging market countries may produce a contagion that reduces overall investor appetite for securities of emerging market issuers. Past economic crises in emerging markets, such as in Southeast Asia, Russia and Argentina, have resulted in significant outflows of U.S. dollars from Brazil and caused Brazilian companies to face higher costs for raising funds, both domestically and abroad, and have effectively impeded access to international capital markets for extended periods.

We cannot assure you that global capital markets will remain open to Brazilian companies or that prevailing interest rates in these markets will be advantageous to us. In addition, future financial crises in emerging market countries may have a negative impact on the Brazilian markets, which could adversely affect the trading price of our securities.

Our market risk management strategy may not be effective.

We are exposed to traditional market risks such as volatility in interest rates, exchange rates and commodity prices. We earn most of our revenues in U.S. dollars, but incur a substantial portion of our costs and expenses in currencies other than the U.S. dollar. The exchange rates for such currencies are very volatile. In order to manage market prices and rates exposure, our board of directors has established an enterprise risk management policy and a risk management committee. See *Item 11. Quantitative and qualitative disclosures about market risk*. Our strategy may not be successful in managing risk exposure, and we may fail to identify correlations between the various market risks to which we are subject. In addition, to the extent we choose to hedge our commodity price exposure, we may limit the upside benefits that we would otherwise experience if commodities prices were to increase.

We may not have adequate insurance coverage for some business risks.

Our businesses are generally subject to a number of risks and hazards, including:

- industrial accidents;
- railroad accidents;
- port accidents;
- labor disputes;
- slope or pit-wall failures, cave-ins or rock falls;
- environmental hazards;
- electricity stoppages;
- equipment or vessel failures;
- severe weather and other natural phenomena such as seismic events;
- unavailability or late delivery of materials, supplies or equipment;
- unexpected ground, grade or water conditions; and
- unusual or unexpected geological formations or pressures.

These occurrences could result in damage to, or destruction of, mineral properties, production facilities, logistics facilities, equipment or vessels. They could also result in personal injury or death, environmental damage, waste of resources or intermediate products, delays or interruption in mining, production or transportation activities, monetary losses and possible legal liability. The insurance we maintain against risks that are typical in our business may not provide adequate coverage. Insurance against some risks (including liabilities for environmental pollution or certain hazards or interruption of certain business activities) may not be available at a reasonable cost, or at all. As a result, accidents or other negative developments involving our mining, production or transportation facilities could have a material adverse effect on our operations.

Risks relating to the American Depositary Shares

If ADR holders exchange ADSs for the underlying shares, they risk losing the ability to remit foreign currency abroad and Brazilian tax advantages.

The Brazilian custodian for the shares underlying our ADSs will obtain an electronic registration from the Central Bank to entitle it to remit U.S. dollars abroad for payments of dividends and other distributions relating to the shares underlying our ADSs or upon the disposition of the underlying shares. If an ADR holder decides to exchange its ADRs for the underlying shares, it will be entitled to continue to rely, for five business days from the date of exchange, on the custodian’s electronic registration.