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***Banco de
Desenvolvimento de
Minas Gerais S.A. - BDMG***
***Financial statements at
December 31, 2016
and independent auditor's report***





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Independent auditor's report

To the Board of Directors and Stockholders
Banco de Desenvolvimento de Minas Gerais S.A. – BDMG

Opinion

We have audited the accompanying financial statements of Banco de Desenvolvimento de Minas Gerais S.A. - BDMG ("Bank"), which comprise the balance sheet as at December 31, 2016 and the statements of income, changes in equity and cash flows for the year and six-month period then ended, and notes to the financial statements, including a summary of significant accounting policies.

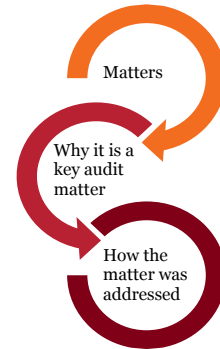
In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Banco de Desenvolvimento de Minas Gerais S.A. - BDMG as at December 31, 2016, and its financial performance and cash flows for the year and six-month period then ended, in accordance with accounting practices adopted in Brazil, applicable to institutions authorized to operate by the Brazilian Central Bank (BACEN).

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 "Auditor's responsibilities for the audit of the financial statements" section of our report. We are independent of the Bank in accordance with the ethical requirements established in the Code of Professional Ethics and Professional Standards issued by the Brazilian Federal Accounting Council, 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 audit opinion.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.



| Why it is a key audit matter | How the matter was addressed in the audit |
|-------------------------------------|--|
|-------------------------------------|--|

Provision for impairment of receivables (Notes 2.7 and 8)

The measurement of the provision for impairment of receivables takes into account the regulations of the Brazilian Central Bank, especially the National Monetary Council Resolution 2,682/99. In order to comply with these regulations, the Bank's management applies judgment and certain assumptions to measure the realizable value of the guarantees and to define the credit risk of the counterparties of the transactions.

Using incorrect judgments and assumptions or improperly applying the applicable regulation may result in a significantly different estimated provision for impairment of receivables.

We focused on this area in our audit because of the significance of the provision for impairment of receivables and of the matters disclosed above.

Our audit procedures included, among others, (a) obtaining an understanding of the calculation of the provision for impairment of receivables, and (b) testing of (i) the integrity of the credit operations database, (ii) the approval and monitoring of renegotiated transactions, (iii) compliance of the main assumptions adopted by management to measure the provision for impairment of receivables with the Brazilian Central Bank regulations, (iv) compliance with the internal rules related to the classification of risks of counterparties, as well as the approval of the corresponding risk levels established, (v) calculation of the amount of the provision, and (vi) reconciliation of the amount of the provision calculated for with the amounts recorded.

The results of these procedures provided appropriate and sufficient audit evidence in the context of the financial statements.



Banco de Desenvolvimento de Minas Gerais S.A. – BDMG

Information technology environment

The processing of the Bank's transactions, the development of its operations, and the continuity of its business depend on the Bank's technology infrastructure.

An inadequate technology environment can result in incorrect processing of critical information used by management, including that used to prepare the financial statements.

For this reason, we focused on the information technology environment in our audit work.

Our audit procedures included, among others, with the support of our systems specialists, obtaining an understanding of and testing the information technology general controls, which include information security, management and development of systemic changes, and the system processing.

We tested the automated or technology-dependent controls and the compensating controls related to the Bank's main business processes.

The information technology environment and the controls established by management provided a reasonable basis for the audit of the financial statements.

Post-employment benefit plans (Notes 2.16 and 28)

The Bank sponsors two pension plans of the defined benefit and variable contribution categories, which are managed by DESBAN – Fundação BDMG de Seguridade Social, a non-profit complementary pension entity.

The defined benefit plan showed an underfunded position and, for this reason, the Bank recognized an actuarial liability in order to comply with applicable accounting practice. Management applied judgment to determine the assumptions used to measure the actuarial liability of the post-employment benefit plan.

We focused on this area in our audit because changes in assumptions can significantly affect the amount of the Bank's actuarial liability.

As part of our audit procedures, we tested the Bank's actuarial calculations, with the support of our actuarial specialists.

These tests mainly included an analysis of the methodology and assumptions used to calculate the actuarial liability and comparison of the main assumptions used with market data and parameters.

We also confirmed the reasonableness of the related disclosures.

We consider that the criteria and assumptions adopted by management to determine the liability for the post-employment benefit plans are reasonable in the context of the financial statements.



Banco de Desenvolvimento de Minas Gerais S.A. – BDMG

Other information accompanying the financial statements and the independent auditor's report

The Company's management is responsible for the other information that comprises the Management Report.

Our opinion on the financial statements does not cover the Management Report, and we do not express any form of audit conclusion thereon.

Our responsibilities as auditors of the financial statements include reading the Management Report and, in doing so, considering whether this report is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement in the Management Report, we are required to report that fact. We have nothing to report in this regard.

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 applicable to institutions authorized to operate by the Brazilian Central Bank, 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 Bank'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 Bank or to cease operations, or has no realistic alternative but to do so. Those charged with governance are responsible for overseeing the Bank's financial reporting process.

Auditor's 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 auditor's 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.



Banco de Desenvolvimento de Minas Gerais S.A. – BDMG

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 controls.
- Obtain an understanding of internal controls 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 Bank's internal controls.
- 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 ability of the Bank to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's 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 auditor's report. However, future events or conditions may cause the Bank 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 governance (Management and Audit Committee) regarding, 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.

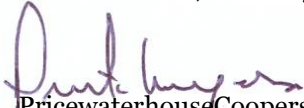
We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and have advised them of all relationships and other matters that may reasonably be thought to bear on our independence, and, where applicable, related safeguards.



Banco de Desenvolvimento de Minas Gerais S.A. – BDMG

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the Key Audit Matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Belo Horizonte, February 23, 2017


PricewaterhouseCoopers
Auditores Independentes
CRC 2SP000160/O-5 "F" MG


Carlos Augusto da Silva
Contador CRC 1SP197007/O-2 "S" MG

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BANCO DE DESENVOLVIMENTO DE MINAS GERAIS S.A. – BDMG

SUMMARY OF THE AUDIT COMMITTEE REPORT - DECEMBER 31, 2016

INTRODUCTION

The Audit Committee, a statutory body of Banco de Desenvolvimento de Minas Gerais S.A. - BDMG, assists the Bank's Board of Directors in the performance of its audit and inspection duties and, among other tasks established in its Internal Regulations, evaluates and provides opinions on: **(i)** the quality of the financial statements; **(ii)** the effectiveness of the internal control system; and **(iii)** the effectiveness of the internal and external (independent) audits. The evaluations of the Committee were based on information received from management, external and internal audit representatives, officers responsible for risk management and internal controls and its own evaluations arising from direct observation.

COMPOSITION

Until September 28, 2016, BDMG's Audit Committee was comprised of members Carlos Antônio Duarte and Jair Modesto da Costa. The Board of Directors met on August 18, 2016 and elected the Coordinator Adézio de Almeida Lima and the members Carlos Alberto de Carvalho Paiva e Pedro Carlos de Mello for participation into the Audit Committee, and they took office on September 29, 2016 for a five-year term. This was approved by the Brazilian Central Bank (BACEN) on September 13, 2016, in accordance with BACEN's Circular Letter 17,675/2016-BCB/Deorf/GTBHHO.

ACTIVITIES CONDUCTED IN THE PERFORMANCE OF ITS ATTRIBUTIONS DURING 2016

During 2016, the Committee held 36 meetings. At the beginning of the first half of 2017, the Committee participated in four meetings, including the Board of Directors' meetings. The Committee maintained permanent contact with the managers of the Bank's control areas in order to monitor the work carried out and obtain subsidies on which to base its assessments. The subjects discussed with the Controllershship, Internal Audit, Risk Management, Internal Controls and Ombudsman officers, according to their operational areas, related to the preparation of the financial statements and internal controls. Ten meetings were held with the external auditors, PricewaterhouseCoopers Auditores Independentes, to discuss the methodology, planning and results of the work in connection with the preparation of the financial statements at June 30, 2016 and December 31, 2016. The Committee met with the Bank's Executive Board to deal with subjects related to general management aspects of the Bank, especially those related to accounting, internal controls, internal audit, capital management, financial management and risk management. The Committee made recommendations for process improvements and monitored the implementation of improvements recommended by the internal and external (independent) audits, as reported during their work. The Committee held regular meetings with the Bank's Board of Directors, reporting on aspects related to its regulatory duties and providing information to the Board about its activities.

INTERNAL CONTROL AND RISK MANAGEMENT SYSTEMS

The Board maintained systematic monitoring of the work carried out by the Internal Control Management. The Audit Committee considers the activities of the Bank's management as positive to the extent it assures the effectiveness of the Bank's risk management and internal control systems.

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THE INTERNAL AUDIT

A number of meetings were held with the Internal Audit Manager to monitor the work carried out by that Unit. The Committee considers that the scope and quality of the audits carried out and the level of independence are positive. The internal audit work identified no failures in compliance with the pertinent legislation and internal policies that could put at risk the strength and continued operation of the Bank.

THE EXTERNAL (INDEPENDENT) AUDIT

The Committee met with the independent auditors in order to discuss the main aspects of the work carried out during the preparation of the financial statements at June 30, 2016 and December 31, 2016, as well as their assessment of the Bank's internal controls. The Committee considers as satisfactory the work carried out and identified no matters that could affect the external auditor's objectivity and independence.

THE FINANCIAL STATEMENTS

The Committee accompanied the preparation of the financial statements at June 30, 2016 and December 31, 2016 and analyzed trial balances, balance sheets, and related notes, and analyzed the financial statements, management reports, independent auditor's reports and other documents to be made public. It discussed the accounting practices adopted, the atypical occurrences and the related impacts on the Bank's financial position and results of operations at meetings held with those responsible for the preparation of these documents and with the external auditors. The Committee found that the accounting practices used in the preparation of the financial statements are in accordance with the generally accepted accounting principles, the Brazilian Corporate Law, and with the regulations of the National Monetary Council (CMN) and Brazilian Central Bank (BACEN) and that they fairly represent the Bank's financial position.

CONCLUSION

The Audit Committee did not receive, up to the date of this report, any reports of non-compliance, lack of controls or act or omission by the Bank's management evidencing the existence of fraud, failures or errors, which could affect the continuity of operations of the Bank or the fairness of its financial statements to risk. Based on the above, the Audit Committee, after considering its responsibilities and the natural limitations of its activities, recommends to the Board of Directors the approval of the financial statements of Banco de Desenvolvimento de Minas Gerais S.A. - BDMG at December 31, 2016.

Belo Horizonte, February 23, 2017

| | | |
|-------------------|----------------------------|-----------------|
| ADÉZIO DE ALMEIDA | CARLOS ALBERTO DE CARVALHO | PEDRO CARLOS DE |
| LIMA | PAIVA | MELLO |
| Coordinator | Member | Member |

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Opinion of the Statutory Fiscal Council

The Statutory Fiscal Council of Banco de Desenvolvimento de Minas Gerais S.A. - BDMG, in the performance of its legal and statutory duties, having analyzed the management report and the financial statements for 2016, at a meeting held on February 24, 2017, and considering the terms of the unqualified independent auditor's report issued by PricewaterhouseCoopers Auditores Independentes, dated February 23, 2017, considers that the aforementioned documents are in accordance with the accounting practices adopted in Brazil and fairly reflect the financial position of the Bank, and that they should be approved .x.x.x.x.x.x.x.x.x.x.x.x.x.x.x.x
Belo Horizonte, February 24, 2017

Dany Andrey Secco
Chairman
BDMG's Statutory Fiscal Council

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Management report

January to December 2016

1. Company

Banco de Desenvolvimento de Minas Gerais S.A. - BDMG is a financial institution established by State Law 2,607 of January 5, 1962, involved in the sustainable development of the State of Minas Gerais. It is part of the State economic development system, and is connected to the Science, Technology and Economic Development Secretariat of the State of Minas Gerais. The Bank's vision is "to be recognized as a strategic participant in the process of the economic and social development of Minas Gerais" and its mission is "to promote the sustainable and competitive economic and social development of Minas Gerais, generating more and better jobs and reducing social disparities".

In 2015, the Strategic Plan for 2016-2021 was prepared, defining as main guidelines more conscious actions, promoting support to projects that improve the competitiveness of Minas Gerais and its productive restructuring, fostering environmental sustainability and the regional and social development.

In this regard, a number of implemented actions in 2016 had been already planned and started in 2015, with the purpose of, at the same time, offering a portfolio of structured operations and products that would guarantee the Bank's sustainability, and allowing the Bank to become again a strategic player for the development of Minas Gerais.

The Government of Minas Gerais, despite the adverse financial situation, made a capital increase of R\$ 100 million in order to reinforce the Bank's strategic position, of which R\$ 50 million was paid up in August and the remaining is scheduled to be made in 2017, in accordance with the National Monetary Council (CMN) 394/1976.

2. Results of operations

In 2016, disbursements totaled R\$ 1,470.3 million, which represented a decrease of 26% in relation to 2015. Of the total disbursed, 77% represented onlendings (R\$ 1,083.7 million, divided among the National Bank for Economic and Social Development (BNDES), the Fund for the Defense of the Coffee Economy (FUNCAFÉ), the Fund for Financing of Studies and Projects (FINEP), the Foundation for Support of Research in the State of Minas Gerais (FAPEMIG), and the Federal Savings Bank (CEF)). Disbursements with own funds represented 24% of the total amount (R\$ 349.9 million), related to surety presented 2% of the total (R\$ 35.9 million) and the state fund disbursements amounted to R\$ 920 thousand (0.1 % of the total).

In sectorial terms, commerce and services had the greatest share, with R\$ 553 million (38%), followed by the manufacturing industry, with R\$ 529 million (36%), public utility services, with R\$ 194 million (13%), construction - R\$ 117 million (8%), farming, cattle-raising and forestry - R\$ 72 million (5%), and mineral extraction - R\$ 2 million (0.16%).

Considering the disbursement by company size, the large and medium companies were responsible for 69% of the total amount (R\$ 1,013.3 million), whereas micro and small companies represented 19% (R\$ 280.4 million). Financing to the public sector represented 11% of the disbursements (R\$ 167.6 million) and 1% (R\$ 9 million) was allocated to equity investment funds.

The portfolio of active customers totaled 22,546 customers, thus maintaining BDMG's presence in 89% of the municipalities of Minas Gerais (762 of 853).

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3. Business highlights

Innovation

Regarding the borrowing lines, BDMG make business with financial resources obtained from partnerships with FAPEMIG, BNDES, and FINEP. In 2016, more than R\$ 50 million was disbursed, which allowed the supporting of 41 new and innovative projects, thus representing an increase of 45% in relation to the prior year.

For indirect participations, BDMG became a quotaholder of two new Equity Investment Funds (FIPs): Criatec 3 and Venture Brasil Central. The first one, launched by BNDES in February, seeks to guarantee investments for small, technology-based companies, mainly operating in the nanotechnology, information technology, biotechnology, agribusiness, and new material industries. The second one seeks to invest in innovative Brazilian companies located in the central region of Brazil, from the Information and Communication Technology (ICT), Agribusiness, and Health Technology areas. In 2016, the capital committed to the seven FIPs already invested by the Bank totaled R\$ 48.2 million. Up to date, eleven companies from Minas Gerais have received these funds.

Regarding the participation, BDMG, through its subsidiary BDMGTEC has investments in the share capital of two companies, one from the semiconductor area and other from the biopharmaceutical area. At the end of 2016, the amounts paid up by BDMGTEC totaled R\$ 28 million in BIOMM, an insulin producer, and R\$ 48 million in Unitec Semicondutores.

Environmental sustainability

Borrowings to support the sustainable development totaled R\$ 140 million through disbursements made in sewage and waste treatment, forest production and conservation, atmospheric pollution reduction, and energy efficiency.

The Bank's disbursements to companies located in municipalities subject to natural disasters totaled R\$ 18 million and were made through the BDMG RIO DOCE and BNDES PER lines. The first had been effective up to June and offered working capital for the micro and small companies located in the 35 municipalities that were more affected by the Mariana environmental disaster. The BNDES Per (Emergency Program for the Reconstruction of Municipalities Affected By Natural Disasters) line was allocated to companies with a gross revenue between R\$ 30 million and R\$ 90 million per year and that are located in municipalities affected by natural disasters.

In-house actions were also developed involving the implementation of sustainable practices and environmental awareness programs targeting the natural resource preservation and cost reduction.

Regional and social development

In March, the Bank and the State Health Secretariat launched the Financing Program for Philanthropic Hospitals, which targets those institutions that (i) provide services to patients under the Public Integrated Health System (SUS), (ii) offer more than 100 beds, and (iii) have annual gross income of more than R\$ 10 million. For this purpose, R\$ 58.3 million was contracted and R\$ 30.7 million was disbursed during the year.

Also in March, the Geraminas Social project was launched to foster the regional development. The working capital borrowing line is for micro and small companies located in municipalities whose Municipal Human Development Index is below the average for the State. Companies from a total of 406 cities are eligible to receive these funds. In order to promote this financing line, campaigns were held in 44 cities with the purpose of obtaining a close awareness of the needs of local businesses. A total of R\$ 11.5 million was disbursed to companies of 133 municipalities.

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In September, the Minas Criativa credit product was launched, consisting of a working capital line for companies that produce cultural and artistic products, with creative content and economic value.

In October, the Geraminas Fidelidade product was launched with the purpose of offering better conditions to customers that are known for their good relationship and low risk profile. The benefit package includes lower rates, differentiated credit limit, less strict documentation requirement, and more agile analyses of requests. The reduced interest rate will be granted via "non-default bonus", which means that the customer will benefit from it only if all payments are made in due course. Disbursements for this program during the first quarter since its launch totaled R\$ 14 million.

In order to maintain the access to credit for micro and small companies, the Bank increased the product offerings through its web platform. In addition to the BDMG Geraminas, Geraminas Social, and BNDES Progeren products, which are related to working capital purposes, the Government Agency for Machinery and Equipment Financing (FINAME) was also offered for the segment as an incentive for fixed investments in machinery and equipment purchases. The Bank's partnerships with the bank correspondents continues, thus allowing it to offer credit throughout the State of Minas Gerais. Currently, the Bank has 214 active bank correspondents.

The amount disbursed for agribusiness totaled R\$ 222.9 million. We emphasize the Bank's partnership with the Ministry of Agriculture, which resulted in the offering of R\$ 170 million from the FUNCAFÉ (Coffee Economy Defense Fund) line for supporting companies and cooperatives of the coffee industry in the 2016/2017 season. The disbursement reached R\$ 126.5 million, thus representing an increase of 183% when compared to 2015, which consolidated this source of funds offered by the Bank.

Disbursements for the public sector were marked by the continuity of the actions from the Bid launched in 2015, in a partnership with the State Government. They totaled R\$ 167.6 million and were made to 219 municipalities. The borrowings targeted construction, renovation, and expansion of public buildings, water supply and sewage services, solid residue treatment, mobility, and urban drainage, as well as resources for machinery and equipment purchasing.

Public-Private Partnerships (PPP)

The Public-Private Partnerships (PPP) comprise one of the Bank's lines of operation regarding the infrastructure and innovation support, both in the structuring of concession operations and in the financing of projects. Highlights for 2016 are the PPPs with the Technology Complex BH-TEC and with the Minas Gerais Education Secretariat (SEE).

In the BH-TEC PPP, the Bank (i) coordinated the structuring project for the concession bid notice, (ii) executed the economic and financial front by integrating the legal and structural studies, and (iii) supported the BH-TEC in activities related to the concession project. Total investments amount to approximately R\$ 60 million.

In the education area, the Bank supported the SEE in conducting the Interest Manifestation Procedure (PMI) for making a PPP project feasible concerning the construction and operation of state schools, whose bidding is expected for the next semester, with estimated construction of up to 128 units.

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Funding and transfers

In November, the performance of many BNDES' agents for Automatic Products was disclosed. The Bank reached the first position in the state contracting ranking in the FINEM, BNDES Automatic, and PROGEREN lines. At the national level, BNDES was the third institution in the PROGEREN line and the fourth institution in BNDES Automatic in general.

In December, BDMG made its first issue of Agribusiness Letters of Credit (LCA). A total of R\$ 56 million was issued for a three-year period. LCAs are instruments that allow the funding with lower rates that are adherent to the Bank's products, which makes its initiative an essential feature for the Bank to be able to strengthen its business, expanding the credit offer to companies in Minas Gerais.

Credit, risk and guarantee policies

Within a context where the economy scenario demands that the financial institutions have a more strict approach to risk, BDMG reinforced its credit and risk policies in 2016. Improvements were made to the Capital and Risk Financial Management (FCR) and Credit Policy committees. The purpose of the FCR is to make a better use and to preserve the Bank's financial resources, financial health, and generation of value from the Bank's assets. The Credit Policy Committee aims at permanently reassessing the Bank's credit policy and making recommendations to the Bank's Executive Board regarding the Bank's strategy and risk appetite and the macro economic scenario.

The mapping of the Bank's operating and conformity risks was concluded. It resulted from the Bank's necessity of identifying, recording, and reporting its main operating and conformity risks as well as the controls already implemented for mitigating risks, in accordance with the National Monetary Council (CMN) Resolution 3,380.

The throughout review of the guarantee and asset policies was also concluded, and comprised the period from the assessment of the guarantee upon the borrowing negotiation up to the sale of the assets not for use. Its purpose was to align financial security with business feasibility, and the commercial practice with the financial sustainability.

Internal Control System

BDMG continued to make improvements in its Internal Control System in 2016 through policies and practices established to ensure conformity and maintenance of the operating risks within acceptable levels, thus allowing the Bank to efficiently and safely meet its objectives. This system depends on the commitment of the Bank as a whole, from Senior Management to service providers, with continuing acculturation, mainly through the strengthening of the management's role within this process. Among the improvement actions regarding the Internal Control System in 2016, the following stand out: (i) Operating Risk: conclusion of the operating risk mapping throughout the Bank; (ii) Monitoring: preparation of a new operating risk monitoring systematic, providing dynamism, automation, and feedback from the Operating Risk Mapping Matrix; (iii) Internal Normative Instructions: conclusion of the adjustments made to the Internal Normative Review Electronic Forms (FERNs) and preparation of internal reports and reporting of reviews and update of normative updates; and (iv) Conformity: creation of a system to launch, monitor, and report the external audit's and BACEN's observations, to be incorporated into the monitoring of the internal audit's and Audit Committee's observations.

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Credit management

The credit management was subject to a major remodeling in 2016, which involved the establishment of processes concerning the parametrized renegotiation and the specialized operation portfolio. The parametrized renegotiation includes less complex operations (amounts below R\$ 480 thousand) and is made via web platform within 15 days. There is an exclusive team working with the specialized portfolio, providing a differentiated treatment according to the customer's profile. This more strict approach to the credit renegotiation targets the preventive measures regarding the non-default situation with major customers.

BDMG Cultural

The BDMG Cultural Institute established its position in the cultural scenario of Minas Gerais in 2016, with an intense schedule in the fields of arts and knowledge. It maintained its activities in areas such as instrumental and classical music, audiovisual matters, visual arts, and theater. The theater and dance production circuit has reached 40 municipalities in the State, with the debut of artistic groups from the interior regions of Minas Gerais.

Together with the Liberdade Circuit, BDMG Cultural increased its participation in the areas of popular music, heritage, and literature, with emphasis on the Writing Arts Circuit, the most important literary event in Minas Gerais. Another initiative that has improved in the editorial area is the Mercado Gráfico Faisca, with monthly events that promoted the independent graphic production.

The Institute has incorporated into its cultural approach the awareness about critical reflection and the production of knowledge, with projects targeted at encouraging the critical thinking about culture, politics, economic, and the society. In this field, the BDMG Cultural promoted the Conversations on Development program, with a highlight on the Urbe Urge project, the latter targeting urban-related matters, in a partnership with the Piseograma Program. It also held the State Seminar on Creative Economy, whose purpose was to prepare a diagnosis that will serve as the basis for the research and systematization of the industry's data, in order to provide subsidies for collective actions in the creative economy area.

BDMG's Employee Citizenship Institute (INDEC)

In 2016, INDEC celebrated its 18th anniversary. The Projeto Vestibular Comunitário (Project that helps members of the community to enter university), which offers free lessons to low-income youths and adults was maintained. The institute also supports the development of the education of children and teenagers who live in the one of the Shelters of Associação Irmão Sol, in Belo Horizonte. It distributed the Pão Forte Educativo ("Educational Strong Bread") project, whose objective is to change health, hygiene and dietary habits and school attendance. The project provided resources to approximately 300 children per month.

4. Financial statements

At the end of 2016, BDMG's profit and equity amounted to R\$ 27 million and R\$ 1,681 million, respectively, which represents a stable result in relation to the balance at December 31, 2015 (R\$ 1,689 million).

The Bank's credit portfolio increased 1.2% in the period, from R\$ 5,893 million in 2015 to R\$ 5,964 million in 2016. The net portfolio of provision also had a positive variation of 2.6% in the period, from R\$ 5,504 million to R\$ 5,647 million.

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BDMG has securities classified as "held to maturity" that amounts to R\$ 131 million, and Management, in compliance with Circular 3,068/2001, declares that the Bank is financially able to hold them in its portfolio up to maturity.

On December 13, 2016, S&P Global Ratings reclassified BDMG's risk grading, following the risk grading provided to the State of Minas Gerais in the previous day, from "BB-" to "B-" in the global scale, and from "brA" to "brB" in the national scale, with negative perspective. Together with this, S&P Ratings confirmed the Bank's stand-alone credit profile (SACP) as "bb-", while making no changes to the Bank's standalone rating.

5. Acknowledgments

The management of BDMG would like to thank the support of all those who contributed to the results attained in 2016, specially the people of the State of Minas Gerais, who are the reason behind all efforts made by the Bank for the sustainable social and economic development of Minas Gerais.

Banco de Desenvolvimento de Minas Gerais S.A. – BDMG

Balance sheet at December 31

All amounts in thousands of reais

(A free translation of the original in Portuguese)

| | 2016 | 2015 Restated |
|--|------------------|------------------|
| Assets | | |
| Current assets | 1,786,786 | 1,839,947 |
| Cash (Note 4) | 2,192 | 4,817 |
| Short-term interbank investments (Note 5) | 159,715 | 351,063 |
| Open market investments | 124,620 | 351,063 |
| Investments in interbank deposits | 46,822 | 11,727 |
| (Provision for losses) | (11,727) | (11,727) |
| Marketable securities and derivative financial instruments (Notes 6-7) | 49,309 | 54,179 |
| Own portfolio | 46,939 | 44,575 |
| Derivative financial instruments (Note 7) | 2,370 | 9,604 |
| Credit operations (Note 8) | 1,370,868 | 1,332,247 |
| Credit operations | 1,469,909 | 1,555,515 |
| Public sector | 178,312 | 154,281 |
| Private sector | 1,291,597 | 1,401,234 |
| (Provision for impairment of receivables) | (99,041) | (223,268) |
| Other receivables (Note 9) | 204,491 | 97,455 |
| Income receivable | 2,654 | 1,954 |
| Sundry | 201,839 | 95,502 |
| (Provision for impairment of receivables) | (2) | (1) |
| Other assets (Note 10) | 211 | 186 |
| Other assets | 211 | 186 |
| Non-current assets | 5,828,536 | 5,460,704 |
| Long-term receivables | 5,711,919 | 5,351,761 |
| Short-term interbank investments (Note 5) | 10,353 | - |
| Investments in interbank deposits | 10,353 | - |
| Marketable securities and derivative financial instruments (Notes 6-7) | 1,048,796 | 768,814 |
| Own portfolio | 975,143 | 607,060 |
| Subject to guarantees | 11,268 | - |
| Derivative financial instruments (Note 7) | 62,385 | 161,754 |
| Credit operations (Note 8) | 4,274,275 | 4,170,070 |
| Credit operations | 4,492,476 | 4,335,924 |
| Public sector | 649,108 | 649,945 |
| Private sector | 3,843,368 | 3,685,979 |
| (Provision for impairment of receivables) | (218,201) | (165,854) |
| Other receivables (Note 9) | 323,705 | 392,771 |
| Income receivable | 1,115 | 1,843 |
| Specific receivables | 1,183 | 1,183 |
| Sundry | 333,714 | 402,047 |
| (Provision for impairment of other receivables) | (12,307) | (12,302) |
| Other assets (Note 10) | 54,790 | 20,106 |
| Temporary investments | 6 | - |
| Other assets | 57,415 | 22,180 |
| (Provision for losses) | (2,631) | (2,074) |
| Permanent assets (Note 11) | 116,617 | 108,943 |
| Investments | 84,802 | 78,683 |
| Domestic subsidiary and associated companies | 84,315 | 78,196 |
| Other investments | 1,324 | 1,324 |
| (Provision for losses) | (837) | (837) |
| Property and equipment in use | 20,479 | 21,958 |
| Real estate in use | 43,788 | 43,787 |
| Other property and equipment in use | 12,944 | 12,908 |
| (Accumulated depreciation) | (36,253) | (34,737) |
| Intangible assets | 11,336 | 8,302 |
| Intangible assets | 18,287 | 12,729 |
| (Accumulated amortization) | (6,951) | (4,427) |
| Deferred charges | - | - |
| Organization and expansion costs | 1,610 | 1,610 |
| (Accumulated amortization) | (1,610) | (1,610) |
| Total assets | 7,615,322 | 7,300,651 |

Banco de Desenvolvimento de Minas Gerais S.A. – BDMG

Balance sheet at December 31

All amounts in thousands of reais

(continued)

| | 2016 | 2015 Restated |
|---|------------------|------------------|
| Liabilities | | |
| Current liabilities | 1,781,501 | 1,055,237 |
| Deposits (Note 12(a)) | 6,358 | 137,501 |
| Interbank deposits | 6,358 | 137,501 |
| Funds from acceptance and issue of securities (Note 12 (b and c)) | 593,023 | 110,035 |
| Funds from financial bills, bills of credit and agribusiness | 593,023 | 110,035 |
| Borrowings (Note 13 (a)) | 159,956 | 76,722 |
| Foreign borrowings | 159,956 | 76,722 |
| Local onlendings - official institutions -Sundry (Note 13(b)) | 908,933 | 654,307 |
| National Treasury | 2,732 | 1,814 |
| National Bank for Economic and Social Development (BNDES) | 467,656 | 355,446 |
| CEF | 8 | - |
| Government Agency for Machinery and Equipment Financing (FINAME) | 271,758 | 240,414 |
| Other institutions | 166,779 | 56,633 |
| Other liabilities (Note 14) | 113,231 | 76,672 |
| Social and statutory | 14,770 | - |
| Collection of taxes and similar charges | 783 | 995 |
| Tax and social security | 44,971 | 36,978 |
| Financial and development funds | 1,401 | 1,222 |
| Sundry | 51,306 | 37,477 |
| Non-current liabilities | 4,111,878 | 4,551,599 |
| Deposits (Note 12(a)) | 322 | - |
| Interbank deposits | 322 | - |
| Funds from acceptance and issue of securities (Note 12 (b and c)) | 16,040 | 571,883 |
| Funds from financial bills, bills of credit and agribusiness | 16,040 | 571,883 |
| Borrowings (Note 13 (a)) | 392,652 | 751,341 |
| Foreign borrowings | 392,652 | 751,341 |
| Local onlendings - official institutions (Note 13(b)) | 3,099,436 | 2,780,149 |
| National Treasury | 9,754 | 10,694 |
| National Bank for Economic and Social Development (BNDES) | 1,800,428 | 1,463,319 |
| Caixa Econômica Federal (CEF) | 2,277 | - |
| Government Agency for Machinery and Equipment Financing (FINAME) | 1,190,959 | 1,246,570 |
| Other institutions | 96,018 | 59,566 |
| Derivative financial instruments | 15,600 | - |
| Derivative financial instruments (Note 7) | 15,600 | - |
| Other liabilities (Note 14) | 587,828 | 448,226 |
| Tax and social security | 190,575 | 175,864 |
| Financial and development funds | 68,745 | 12,617 |
| Sundry | 328,508 | 259,745 |
| Deferred income (Note 15) | 12,406 | 12,939 |
| Deferred income | 12,406 | 12,939 |
| Equity (Note 16) | 1,709,537 | 1,680,876 |
| Share capital: | | |
| Capital - local residents | 1,894,396 | 1,793,685 |
| Unpaid capital | (50,000) | - |
| Revenue reserves | 18,865 | 6,692 |
| Carrying value adjustments | (153,724) | (119,501) |
| Total liabilities | 7,615,322 | 7,300,651 |

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

Banco de Desenvolvimento de Minas Gerais S.A. – BDMG

Statement of operations at December 31

All amounts in thousands of reais unless otherwise stated

(A free translation of the original in Portuguese)

| | Second half | Years | |
|---|----------------|---------------|-----------------------------|
| | 2016 | 2016 | 2015 (Restated - Note 3) |
| Income from financial intermediation | 439,367 | 698,143 | 930,696 |
| Credit operations (Note 19) | 373,600 | 721,853 | 652,585 |
| Marketable security transactions (Note 20(a)) | 72,070 | 139,779 | 113,915 |
| Derivative financial instruments (Note 20(a)) | (6,311) | (163,234) | 131,291 |
| Foreign exchange transactions | 8 | (255) | 32,905 |
| Expenses with financial intermediation | (323,918) | (615,060) | (914,459) |
| Money market funding operations (Note 20 (b)) | (36,134) | (89,463) | (116,852) |
| Borrowings and onlendings (Note 20 (b)) | (190,409) | (352,791) | (511,728) |
| Provision for impairment of receivables (Note 8 (d)) | (97,375) | (172,806) | (285,879) |
| Gross profit from financial intermediation (Note 21) | 115,449 | 83,083 | 16,237 |
| Other operating income/expenses | (88,362) | (28,502) | (106,564) |
| Income from services rendered | 21,256 | 40,358 | 38,793 |
| Personnel expenses | (58,942) | (111,848) | (106,295) |
| Other administrative expenses (Note 22(a)) | (19,062) | (35,475) | (37,451) |
| Tax expenses (Note 22(b)) | (10,879) | (22,870) | (29,794) |
| Equity in the results of associates and subsidiaries | 43 | 43 | |
| Other operating income (Note 22 (c)) | 24,535 | 203,885 | 90,953 |
| Other operating expenses (Note 22 (d)) | (45,313) | (102,595) | (62,770) |
| Operating profit (loss) | 27,087 | 54,581 | (90,327) |
| Non-operating result | (78) | (211) | 1 |
| Profit (loss) before taxation and profit sharing | 27,009 | 54,370 | (90,326) |
| Income tax and social contribution (Note 23) | (6,246) | (23,130) | 60,368 |
| Provision for income tax | (17,951) | (27,032) | (29,637) |
| Provision for social contribution | (15,580) | (23,187) | (21,271) |
| Deferred tax assets | 27,285 | 27,089 | 111,276 |
| Statutory profit sharing | (3,379) | (4,067) | (1,371) |
| Employee profit sharing | (3,379) | (4,067) | (1,371) |
| Profit (loss) for the year | 17,384 | 27,173 | (31,329) |
| Interest on capital (R\$ 0.0002 per thousand shares) | (15,000) | (15,000) | |
| Earnings (loss) per share (thousand shares) - R\$ | 0.00027 | 0.00042 | (0.00051) |

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

Banco de Desenvolvimento de Minas Gerais S.A. - BDMG

Statement of changes in equity

All amounts in thousands of reais

(A free translation of the original in Portuguese)

| | Share capital | Capital increase | Unpaid capital | Revenue reserves | | Carrying value adjustments | Other carrying value adjustments | Retained earnings | Total |
|--|------------------|------------------|-----------------|------------------|---------------|----------------------------|----------------------------------|-------------------|------------------|
| | | | | Legal | Other | | | | |
| At December 31, 2014 | <u>1,771,693</u> | <u>3,530</u> | <u>-</u> | <u>38,021</u> | <u>18,462</u> | <u>(10,256)</u> | <u>(112,374)</u> | <u>-</u> | <u>1,709,076</u> |
| Approval of capital increase | 21,992 | 59,045 | - | - | (18,462) | - | - | - | 62,575 |
| Capital increase | - | (62,575) | - | - | - | - | - | - | (62,575) |
| Carrying value adjustments | - | - | - | - | - | (4,081) | 7,210 | - | 3,129 |
| Profit for the year | - | - | - | - | - | - | - | (31,329) | (31,329) |
| Allocations | - | - | - | - | - | - | - | - | - |
| Reserves | - | - | - | (31,329) | - | - | - | 31,329 | - |
| At December 31, 2015 (restated - Note 3) | <u>1,793,685</u> | <u>-</u> | <u>-</u> | <u>6,692</u> | <u>-</u> | <u>(14,337)</u> | <u>(105,164)</u> | <u>-</u> | <u>1,680,876</u> |
| Approval of capital increase | 100,711 | (100,711) | (50,000) | - | - | - | - | - | (50,000) |
| Capital increase | - | 100,711 | - | - | - | - | - | - | 100,711 |
| Carrying value adjustments | - | - | - | - | - | 7,042 | (41,265) | - | (34,223) |
| Profit for the year | - | - | - | - | - | - | - | 27,173 | 27,173 |
| Allocations | - | - | - | - | - | - | - | - | - |
| Reserves | - | - | - | 1,359 | 10,814 | - | - | (12,173) | - |
| Interest on capital (R\$ 0.0002 per thousand shares) | - | - | - | - | - | - | - | (15,000) | (15,000) |
| At December 31, 2016 | <u>1,894,396</u> | <u>-</u> | <u>(50,000)</u> | <u>8,051</u> | <u>10,814</u> | <u>(7,295)</u> | <u>(146,429)</u> | <u>-</u> | <u>1,709,537</u> |
| At June 30, 2016 | <u>1,793,685</u> | <u>-</u> | <u>-</u> | <u>7,182</u> | <u>-</u> | <u>(9,367)</u> | <u>(186,344)</u> | <u>9,299</u> | <u>1,614,455</u> |
| Approval of capital increase | 100,711 | (100,711) | (50,000) | - | - | - | - | - | (50,000) |
| Capital increase | - | 100,711 | - | - | - | - | - | - | 100,711 |
| Carrying value adjustments | - | - | - | - | - | 2,072 | 39,915 | - | 41,987 |
| Profit for the six-month period | - | - | - | - | - | - | - | 17,384 | 17,384 |
| Allocations | - | - | - | - | - | - | - | - | - |
| Reserves | - | - | - | 869 | 10,814 | - | - | (11,683) | - |
| Interest on capital (R\$ 0.0002 per thousand shares) | - | - | - | - | - | - | - | (15,000) | (15,000) |
| At December 31, 2016 | <u>1,894,396</u> | <u>-</u> | <u>(50,000)</u> | <u>8,051</u> | <u>10,814</u> | <u>(7,295)</u> | <u>(146,429)</u> | <u>-</u> | <u>1,709,537</u> |

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

Banco de Desenvolvimento de Minas Gerais S.A. - BDMG

Statement of cash flows at December 31

All amounts in thousands of reais

(A free translation of the original in Portuguese)

| | Second half | Years | |
|---|------------------|------------------|--------------------------------|
| | 2016 | 2016 | 2015 (Restated - Note 3) |
| Cash flows from operating activities | | | |
| Profit before taxation and profit sharing | 27,009 | 54,370 | (90,326) |
| Adjustments to profit | | | |
| Depreciation and amortization | 2,204 | 4,139 | 3,502 |
| Provisions and net liabilities | 36,990 | 62,867 | 46,825 |
| Provision for impairment of receivables, net of reversals | 97,375 | 172,806 | 285,879 |
| Provision (reversal) for losses | 22 | 498 | 115 |
| Gains on disposal of assets not for own use | - | - | 54 |
| Appropriation of deferred income | (12,200) | (22,210) | (13,547) |
| Net foreign exchange gains (losses) | 18,188 | (118,270) | 186,551 |
| Recovery of credit transactions written off as losses | (13,249) | (20,006) | (10,737) |
| Revenue from monetary restatement of long-term credit transactions | (5,288) | (17,917) | (23,513) |
| Equity in the results of the subsidiary | - | 24 | 58 |
| Adjustment to market value of derivative instruments and hedge transactions | 466 | (6,683) | 5,603 |
| Loss on available-for-sale financial assets | (47,423) | (84,251) | (72,234) |
| Loss on financial assets held to maturity | (7,604) | (18,262) | (13,686) |
| Adjusted profit | 96,490 | 7,105 | 304,544 |
| (Increase) in short-term interbank investments | (10,353) | (10,353) | - |
| Decrease (increase) in derivatives | (8,749) | 135,445 | (160,214) |
| (Increase) in credit operations | (245,436) | (277,702) | (568,047) |
| Increase in other receivables and other assets | (20,310) | (46,810) | (13,454) |
| Increase (decrease) in interbank deposits | (43,952) | (130,821) | 123,121 |
| Increase (decrease) in fundings from financial bills | (11,962) | (72,855) | (64,616) |
| Increase in borrowings and onlendings | 337,512 | 410,422 | 577,166 |
| Increase in deferred income | 12,301 | 21,677 | 13,338 |
| Increase (decrease) in other payables | 35,378 | 58,968 | (12,134) |
| Changes in assets and liabilities | 44,429 | 87,971 | (104,840) |
| Cash from operations | 140,919 | 95,076 | 199,704 |
| Income tax and social contribution paid | (21,240) | (44,137) | (66,260) |
| Net cash provided by operating activities | 119,679 | 50,939 | 133,444 |
| Cash flows from investing activities | | | |
| Purchase of permanent assets | (2,795) | (5,256) | (5,243) |
| Investment in subsidiary BDMGTEC | (6,600) | (6,600) | - |
| Purchases of available-for-sale financial assets | (422,878) | (455,013) | (121,764) |
| Proceeds from available-for-sale financial assets | 163,110 | 168,684 | 178,968 |
| Purchases of financial assets held to maturity | - | - | (142,028) |
| Receipts from financial assets held to maturity | 8,830 | 17,817 | 48,436 |
| Net cash used in investing activities | (260,333) | (280,368) | (41,631) |
| Cash flows from financing activities | | | |
| Capital increase | 50,711 | 50,711 | - |
| Interest on capital | (15,000) | (15,000) | - |
| Net cash provided by financing activities | 35,711 | 35,711 | - |
| Increase (decrease) in cash and cash equivalents | (104,943) | (193,718) | 91,813 |
| Cash and cash equivalents at the beginning of the year | 266,842 | 355,880 | 231,162 |
| Foreign exchange gains (losses) on cash | 8 | (255) | 32,905 |
| Cash and cash equivalents at the end of the year | 161,907 | 161,907 | 355,880 |

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

(A free translation of the original in Portuguese)

Banco de Desenvolvimento de Minas Gerais S.A. - BDMG

Notes to the financial statements at December 31, 2016

All amounts in thousands of reais unless otherwise stated

1 General information

Banco de Desenvolvimento de Minas Gerais S.A. - BDMG ("Bank") is a privately held corporation, controlled by the State of Minas Gerais, and is subject to the rules and regulations of Brazilian Corporate Law, the National Financial System and the applicable legislation of the Government of the State of Minas Gerais.

The objectives of the activities of BDMG are the economic and social development of the State of Minas Gerais. In this context, BDMG carries out development bank activities in accordance with the National Monetary Council (CMN) rules, and acts as a financial agent for the funds allocated by the State Government to finance programs and projects for the development of Minas Gerais. BDMG is also the financial agent and/or manager of other funds which do not pertain to the State Government, which finance projects in the State of Minas Gerais and, therefore, promote its development. The Bank also renders advisory and technical support services to the direct and indirect State Government administration, and creates opportunities for the implementation/expansion of companies with significant interest for the development of the State of Minas Gerais through its wholly-owned subsidiary BDMGTEC PARTICIPAÇÃO S.A., established in 2012.

The issue of these financial statements was authorized by the Company's Executive Board on February 21, 2017.

2 Summary of significant accounting policies

The financial statements have been prepared in accordance with the accounting practices adopted in Brazil, which include the accounting guidelines of Law 6,404/1976 and the changes introduced by Laws 11,638/2007 and 11,941/2009 to record the transactions, together with the rules and instructions of the National Monetary Council (CMN) and the Brazilian Central Bank (BACEN), and disclose all (and only) the applicable significant information related to the financial statements, which is consistent with the information utilized by management in the performance of its duties.

The Brazilian Accounting Pronouncements Committee (CPC) issued pronouncements related to the process of convergence with international accounting standards; however, not all of them were ratified by BACEN. Accordingly, the Bank, in the preparation of the financial statements, adopted the following pronouncements ratified by BACEN up to December 31, 2016:

CMN Resolution 3,566/2008 - CPC 01 (R1) - Impairment of Assets
CMN Resolution 3,604/2008 - CPC 03 (R2) - Statement of Cash Flows
CMN Resolution 3,750/2012 - CPC 05 (R1) - Disclosures on Related Parties
CMN Resolution 4,007/2011 - CPC 23 - Accounting Policies, Changes in Accounting Estimates and Correction of Errors
CMN Resolution 3,973/2011 - CPC 24 - Events after the Reporting Period
CMN Resolution 3,823/2012 - CPC 25 - Provisions, Contingent Liabilities and Contingent Assets
CMN Resolution 4,144/2012 - CPC 00 (R1) - Basic Conceptual Pronouncement
CMN Resolution 4,424/2015 - CPC 33 (R1) - Employee Benefits.

Banco de Desenvolvimento de Minas Gerais S.A. - BDMG

Notes to the financial statements at December 31, 2016

All amounts in thousands of reais unless otherwise stated

2.1 Basis of preparation

The preparation of financial statements requires the use of certain critical accounting estimates. It also requires management to exercise its judgment.

The Bank has an accounting technology structure based on a number of operating systems that are integrated to the accounting system. The major operating systems (that is, those related to the controls over credit operations, financial management, and equity) were developed internally and are responsible for the majority of the entries. In addition, the Bank contracts third-party operating systems that are necessary to perform and control additional activities.

The Bank adopts information security practices to guarantee the confidentiality, integrity, availability, and authenticity of the information necessary to the maintenance of its business.

2.2 Foreign currency translation

(a) Functional and presentation currency

Items included in the Bank's financial statements are measured using the currency of the primary economic environment in which the entity operates ("functional currency"). The financial statements are presented in Brazilian Reais, which is the Bank's functional and presentation currency.

(b) Transactions and balances

Foreign currency transactions are translated into the functional currency using the foreign exchange rates prevailing at the dates of the transactions or the dates of valuation when items are remeasured.

Foreign exchange gains and losses resulting from the settlement of these transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies, are recognized in the statement of operations.

Foreign exchange gains and losses that relate to borrowings and cash and cash equivalents are presented in the statement of operations as a subitem of financial intermediation, except for the debit balances arising from foreign exchange variations of credit operations, which are reclassified as other operating expenses, and the credit balances arising from foreign exchange variations of funding expenses and payables due to borrowings and onlendings, which are reclassified as other operating income.

The translation of asset and liability balances from operations involving foreign currencies are made into local currency (R\$) at the prevailing rate on the last day of the period. At December 31, 2016, the applicable foreign exchange rate was: US\$ 1.00 = R\$ 3.2591 (2015 - US\$ 1.00 = R\$ 3.9048) and € 1.00 = R\$ 3.4384 (12/31/2015 - € 1.00 = R\$ 4.2504).

2.3 Cash and cash equivalents

Cash and cash equivalents, according to CMN Resolution 3,604/2008, include cash, bank deposits both in Brazil and abroad and highly liquid short-term investments, without a significant risk of changes in the amount and limits, falling due within 90 days or less, at the acquisition date, which are used by the Bank to manage its short-term commitments (Note 4).

Banco de Desenvolvimento de Minas Gerais S.A. - BDMG

Notes to the financial statements at December 31, 2016

All amounts in thousands of reais unless otherwise stated

2.4 Short-term interbank investments

Unrestricted purchase and sale commitments are adjusted to market value. Other assets are stated at acquisition cost, plus income accrued up to the balance sheet date, net of a provision for devaluation, when applicable.

2.5 Marketable securities

In accordance with BACEN Circular 3,068/2001 and supplementary regulations, the marketable securities are classified, according to management's intentions, taking into consideration the following accounting criteria:

- (i) Trading securities - securities purchased in order to be frequently and actively traded. They are recorded at market value, and the realized and unrealized gains and losses are recorded in the statement of operations.
- (ii) Securities available for sale - marketable securities used as part of the cash flow management strategy. These securities are recorded at market value, the accrued income (yield curve) being recognized in the statement of operations for the year, and the unrealized gains and losses arising from market value variations, which have not yet been realized, are recorded in "Carrying value adjustments" within "Equity", net of the related tax effects. Gains and losses, when realized, are recorded in the statement of operations after being specifically identified on the trading date, with a corresponding entry to equity, net of the related tax effects.
- (iii) Securities held to maturity - securities for which the Bank has the intent and financial ability to hold to maturity, recorded at cost of purchase, plus accrued income which is recorded in the statement of operations. Financial capacity is defined based on cash flow projections, disregarding the possibility of the early redemption of these securities. Decreases in the market value of securities available for sale and held to maturity below their respective costs, for reasons not regarded as temporary, are recorded in the statement of operations as realized losses.

Management establishes guidelines for the classification of marketable securities within the categories defined in BACEN Circular 3,068/2001. The classifications of the securities in the portfolio, as well as those acquired during the period, are assessed on a periodical and systematic basis, according to these guidelines. As established in Article 5 of this Circular, the marketable security classification reassessment can only be made at the semi-annual trial balance sheet date. In addition, transfers from the "held to maturity" category can only be made due to an isolated, unusual, non-recurring and unpredicted event occurring after the date of classification.

2.6 Derivative financial instruments

In accordance with BACEN Circular 3,082/2002 and subsequent regulations, derivative financial instruments are classified based on management's intent to use them for hedge purposes or not.

As from October 2013, BDMG started to operate with derivative financial instruments of the swap type with the purpose of mitigating the risks arising from fluctuations in foreign currencies and interest rates on funds from borrowings contracted abroad.

As presented in Note 7, the derivatives are recorded, at fair value, as assets (when positive) and liabilities (when negative), and the changes in their fair values are recorded in the statement of operations.

Banco de Desenvolvimento de Minas Gerais S.A. - BDMG

Notes to the financial statements at December 31, 2016

All amounts in thousands of reais unless otherwise stated

At December 31, 2016, as presented in Note 7, the hedge operations were recorded as follows:

the operations that comply with the criteria defined in BACEN Circular 3,082/2002 are accounted for under the hedge accounting methodology and classified as market risk hedge, and both hedge instruments and the corresponding hedged items are adjusted to market value against income or expense accounts in the statement of operations for the year.

Derivative transactions that do not meet the conditions established by BACEN Circular Letter 3,082/2002 are accounted for at market value, and the objects of these hedges are accounted for at the curve value.

The management and monitoring of risks concerning transactions with derivative financial instruments are compliant with the Bank's policies and strategies.

2.7 Credit operations and provision for impairment of receivables

Credit operations are stated at realizable values including, when applicable, accrued income, on a daily pro rata basis, based on the index variation and contractual interest rate. The income accrued on overdue loans is recorded in income up to the 60th day and, after the 60th day, is no longer accrued and is recognized in income only when the installments are effectively received, as established by Article 9 of CMN Resolution 2,682/1999.

Renegotiated transactions are maintained, at least, at the same risk level in which they were classified before the renegotiation. However, when there are significant facts that justify a change in the risk level, the renegotiated transaction is reclassified to a lower risk rating. When renegotiated, credit operations that had already been written off against the provision and recorded in memorandum accounts remain classified in Level H, and may subsequently be reclassified to a lower-risk category due to a significant event. Any gains arising from the renegotiations are only recognized when they are received.

The provision for impairment of receivables is recorded based on the criteria applied to classify the credit risk of the customer and the operation, as defined by CMN Resolution 2,682/1999.

The criteria for classification are based on statistic techniques or models, as comprised of owned and distinct methodologies developed considering the size and type of customers, including economic and financial, industry-based, and registration aspects, as well as the characteristics of the guarantees.

The risk classifications for operations are made together with the credit concession and follow-up process, considering even the monthly review of default, in accordance with CMN Resolution 2682/1999.

The previous criteria is not applicable for the principal of the rural credit transactions renegotiated in compliance with CMN Resolution 2,471/1998, which is related to the Special Program of Asset Recovery (PESA), whose amount is guaranteed by National Treasury securities, and a supplementary provision is recorded as mentioned in Note 8 (c).

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2.8 Credit assignment

In accordance with the accounting practices established by the Brazilian Central Bank up to December 31, 2011, gains on credit assignments (with or without recourse) to other financial institutions and receivables funds recognized at the time of sale, and immediately recorded in the statement of operations, and the loan assignments with recourse were recorded in memorandum accounts.

On January 1, 2012, CMN Resolution 3,533/2008 (postponed by CMN Resolutions 3,673/2008 and 3,895/2010) became effective, changing the recording of credit assignments carried out as from 2012 and establishing new procedures for the classification and disclosure of financial asset sale or transfer transactions. Based on this Resolution, the maintenance or derecognition of the financial assets in the balance sheet depends on whether or not the risks and rewards of the assets are substantially retained.

For balances assigned before January 1, 2012, there were no retroactive changes in the criteria for the recording of credit assignments.

BDMG did not carry out any credit assignments as from 2012, therefore, these changes had no impacts on its financial statements.

2.9 Other current assets and long-term receivables

These assets are stated at realizable values including, when applicable, accrued income calculated on a daily pro rata basis, less the related unearned income.

2.10 Investments

The investment in the subsidiary BDMGETC is recorded on the equity method of accounting (Note 11 (a)). Other investments are recorded at cost and adjusted to market value through the recording of a provision for effective loss.

2.11 Property and equipment in use and intangible assets

Property and equipment in use, except purchases prior to 1995, which were price-level restated until 1996, according to the regulations effective at the time, and intangible assets are recorded at the cost of acquisition, net of the related accumulated depreciation and amortization, and adjusted for impairment if the impairment tests carried out annually indicate a loss on these assets.

Depreciation and amortization of these assets are calculated using the straight-line method to reduce their cost to their residual values over their estimated useful lives, as follows:

| | <u>Years</u> |
|-------------------------------------|--------------|
| Real estate | 20 |
| Facilities, furniture and equipment | 10 |
| Data processing system | 5 |
| Other | 10 |
| Software | 5 |

An asset's carrying amount is written down immediately to recoverable value when it exceeds its estimated recoverable value (Note 11 (b)).

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Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognized within "Non-operating income (expenses), net" in the statement of operations.

2.12 Impairment of permanent assets

Losses are recorded in the statement of operations if there is evidence that the assets are impaired.

At the end of each year, the Bank's property and equipment in use and intangible assets are subject to a technical assessment. This assessment considers the basis for the verification of the likelihood of impairment loss during the year.

The Bank's investment in the subsidiary BDMGTEC, which represents 99.4% of the Bank's total investments, is annually monitored in order to assess whether it is impaired.

2.13 Current and non-current liabilities

These liabilities are stated at known or estimated amounts including, when applicable, accrued charges calculated on a daily pro rata basis, less expenses to be appropriated.

2.14 Contingent assets and liabilities and legal obligations - taxes and social security

They are evaluated, recognized and disclosed in accordance with CMN Resolution 3,823, dated December 16, 2012, and BACEN Circular Letter 3,429, dated February 11, 2010, taking into account the Technical Pronouncement CPC 25, issued by the Brazilian Accounting Pronouncements Committee (CPC).

Contingent Assets – these are not recognized, except when management has total control over the situation or when there are real guarantees or favorable judicial decisions, in respect of which there can be no further appeals, thereby characterizing the gain as virtually certain, and with the confirmation of the capacity of its recovery by receipt or offset.

Contingent Liabilities - these are recognized in the financial statements when the risk of loss in a legal or administrative action is considered to be probable, with a probable outflow of resources to settle the obligations, based on the opinions of the legal advisors and management, in cases of similarities with previous processes and previous case law, and when the amounts involved can be measured with reasonable assurance. Contingent liabilities which are classified as involving possible losses are not recorded and are disclosed in the notes to the financial statements when the amounts involved are individually significant and when the contingent liabilities classified as remote are not provisioned nor disclosed (Note 14).

Legal obligations - tax and social security - derive from legal actions contesting the legality and constitutionality of the obligations and are fully recognized in the financial statements, regardless of the probability of favorable outcomes to the legal actions (Note 14).

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2.15 Current and deferred income tax and social contribution on net income

The provision for income tax is recorded at 15% of taxable income, plus an additional 10%. The provision for social contribution on adjusted profit had been recorded at the rate of 15% up to August 31, 2015 and at the rate of 20% as from September 1, 2015, as established by Provisional Measure 675/2015, as converted into Law 13,169/2015 (Note 23 (a)).

The tax credits on temporary differences and on income tax and social contribution losses are recorded at the rates considered for the income tax and social contribution provisions.

Tax credits related to income tax and social contribution are reviewed at each balance sheet date and are based on temporary additions and exclusions, as well as applicable legislation on the date of their recording. These tax credits will be realized upon the effective use and/or reversal of the amounts on which they have been based.

Deferred income tax and social contribution are recognized, using the liability method, on temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred income tax and social contribution are determined using tax rates that have been enacted or substantively enacted at the financial statement date and are expected to apply when the related deferred tax asset is realized or the deferred tax liability is settled.

Deferred tax assets are recognized only to the extent it is probable that future taxable profit will be available against which the temporary differences can be utilized.

Deferred income tax and social contribution assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred tax assets and liabilities relate to taxes levied by the same taxation authority on either the same taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

2.16 Employee benefits

The Bank offers to its active employees and retirees the following benefits:

- (i) Pension benefits - provides employees with supplementary retirement remuneration, to that guaranteed by the General Social Security Regime (RGPS). BDMG sponsors defined benefit pension plans (which were closed to new adhesions on November 10, 2011) and variable contribution pension plans.
- (ii) Healthcare and dental assistance benefits - this plan consists of coverage for medical and dental expenses of the plan members. BDMG funds this benefit through partial payments of the monthly contribution for the active participants and retirees who enrolled in the plan as active participants up to 10/10/2009. For employees who enrolled in the healthcare assistance plan as from 10/11/2009, the BDMG sponsorship is assured while they are active participants. When retired, these employees may continue to participate in the plan, being then responsible for the total contribution payable.
- (iii) Life insurance - BDMG offers this benefit through the payment of a part of the group life insurance policy premium, both for active members and retirees.
- (iv) Voluntary employment termination program - This program was implemented on December 14, 2011 and its purpose was to benefit employees who elected for retirement and who met the program's requirements, which terminated on January 29, 2016.

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- (v) Other benefits - In addition, the Bank offers to its active employees other benefits such as profit sharing and six-month maternity leave, and grants lifetime pension benefits to a retiree.

Except for "Other benefits" for active employees, all benefits granted by the Bank are accounted for in accordance with CPC 33 (R1), "Employee Benefits", as approved by CMN Resolution 4,424/2015.

The Bank complies with this standard when accounting for the benefits concerning the performance of the actuarial study on which the accounting records are based. The actuarial study used by the Bank is made annually at December 31 base date and adjusted on a six-month basis for the June 30 base date.

Information on the accounting for employee benefits from January 1, 2016 to December 31, 2016 is detailed in Note 28.

2.17 Profit sharing

Profit sharing is defined through a collective agreement and also as the fulfillment of the Goal Plan, and the related provision is recorded based on a percentage of the profit and adjusted at the end of the year after the profit for the year is established and the assessment of achievement of goals is carried out.

2.18 Share capital

The capital of BDMG, recorded in equity, is comprised of common shares with no par value.

2.19 Results of operations

The profit (loss) is determined on the accrual basis of accounting and is adjusted by income tax and social contribution on net income due on taxable income, and, when applicable, by deferred income tax and social contribution that will be recoverable or payable in future years, except in relation to gains on renegotiated credit operations, which are appropriated to profit (loss) on the cash basis, as established by CMN Resolution 2,682/1999.

2.20 Distribution of dividends and interest on capital

Stockholders are assured the payment of a minimum dividend of 1% of the profit for each year, adjusted in accordance with Brazilian Corporate Law and the Bank's bylaws.

Concerning the capital remuneration of its stockholders, BDMG distributes dividends or pays interest on capital according to the profit for each year.

2.21 Related parties

The disclosures on related parties included in the accompanying notes to the financial statements is in accordance with CMN Resolution 3,750/2009. According to this pronouncement, the Bank discloses its transactions with related parties which could affect its financial position and results of operations. Legal entities and individuals that meet the criteria of BDMG's internal Resolution 209/2009 are considered related parties. The related parties with whom the Bank carried out transactions during the year are disclosed in Note 24.

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3 Restatement of the financial statements for the year ended December 31, 2015

The Brazilian Internal Revenue Service (RFB), based on Law 13,169/2015, issued RFB Normative Instruction 1591 on November 5, 2015, which addresses the manner of calculation and the rate of the Social Contribution on Net Income (CSLL), which increased from 15% to 20%, applicable to taxable events occurring as from September 1, 2015 and effective up to December 31, 2018.

The Bank taxed the taxable result from January to August 2015 and from September to December 2015 at the rates of 15% and 20%, respectively, which resulted in an effective rate lower than 15% in the year since the Bank incurred a taxable profit from January to August 2015 and a tax loss from September to December 2015.

This situation was verified during the review of the "Tax and Accounting Records (ECF)" related to 2015, carried out during the procedures for the preparation of the financial information at June 30, 2016, and arose from a misinterpretation in the application of the Normative Instruction. Accordingly, the Bank had to make significant adjustments to the amounts recorded and paid of CSLL in that year since the correct procedure would be to apply the rule of proportionality based on the gross revenue in 2015, established by article 3 of the Instruction.

Moreover, this review also identified an error in the deductions of tax incentives for the purpose of calculation of the income tax liability. These adjustments are restricted to the current income tax and social contribution expenses and do not affect the deferred expenses.

The adjustments totaled R\$ 7,820 and arise from:

- Corporate Income Tax (IRPJ) expense overstated by R\$ 156, due to the mistake in the deductions of tax incentives.
- Social Contribution on Net Income (CSLL) expense understated by R\$ 7,976 due to the misinterpretation of RFB Normative Instruction 1,591, of November 5, 2015, which addresses the manner of calculation and rate for this tax, applicable to taxable events occurring as from September 1, 2015.

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Financial statements at December 31, 2015

Balance sheet

| | 12/31/2015 | | |
|--|---|-------------------|------------------------------|
| | Balances originally reported | Adjustment | Adjusted balances |
| Liabilities | | | |
| Current | 1,047,417 | 7,820 | 1,055,237 |
| Deposits | 137,501 | - | 137,501 |
| Funds from acceptances and issue of securities | 110,035 | - | 110,035 |
| Borrowings | 76,722 | - | 76,722 |
| Local onlendings - official institutions | 654,307 | - | 654,307 |
| Other liabilities | 68,852 | 7,820 | 76,672 |
| Long-term liabilities | 4,551,599 | - | 4,551,599 |
| Deferred income | 12,939 | - | 12,939 |
| Equity | 1,688,696 | (7,820) | 1,680,876 |
| Capital | 1,793,685 | - | 1,793,685 |
| Revenue reserves | 14,512 | (7,820) | 6,692 |
| Carrying value adjustments | (119,501) | - | (119,501) |
| Total liabilities and equity | 7,300,651 | - | 7,300,651 |

Statement of operations for the year

| | 12/31/2015 | | |
|---|--|-------------------|------------------------------|
| | Balance originally reported | Adjustment | Adjusted balances |
| Gross profit from financial intermediation | 16,237 | - | 16,237 |
| Operating loss | (90,327) | - | (90,327) |
| Loss before taxation and profit sharing | (90,326) | - | (90,326) |
| Income tax and social contribution (Note 22) | 68,188 | (7,820) | 60,368 |
| Provision for income tax | (29,793) | 156 | (29,637) |
| Provision for social contribution | (13,295) | (7,976) | (21,271) |
| Deferred tax assets | 111,276 | - | 111,276 |
| Statutory sharing of results | (1,371) | - | (1,371) |
| Loss | (23,509) | (7,820) | (31,329) |
| Loss per share | (0.0003863) | | (0.0005143) |

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Statement of cash flows

| | 2015 | | |
|---|---|-------------------|------------------------------|
| | Balances originally reported | Adjustment | Adjusted balances |
| Cash flows from operating activities | | | |
| Loss before taxation and profit sharing | (90,326) | (7,820) | (98,146) |
| Adjustments to loss | | | |
| Provisions and net liabilities | 46,825 | 7,820 | 54,645 |
| Other adjustments | 433,965 | - | 433,965 |
| Profit before taxation and profit sharing, adjusted | 390,464 | - | 390,464 |
| Changes in working capital | (227,148) | - | (227,148) |
| Cash from operations | 163,316 | - | 163,316 |
| Income tax and social contribution paid | (66,260) | - | (66,260) |
| Net cash provided by operating activities | 97,056 | - | 97,056 |
| Cash flows from investing activities | | | |
| Purchases of permanent assets | (5,243) | - | (5,243) |
| Net cash used in investing activities | (5,243) | - | (5,243) |
| Cash flows from financing activities | | | |
| Increase in cash and cash equivalents | 91,813 | - | 91,813 |

4 Cash and cash equivalents

| | 2016 | 2015 |
|----------------------------------|-------------|-------------|
| Available funds | 1,616 | 3,245 |
| Funds in foreign currency | 576 | 1,572 |
| Short-term interbank investments | 159,715 | 351,063 |
| | 161,907 | 355,880 |

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5 Short-term interbank investments

| | <u>2016</u> | <u>2015</u> |
|--|-----------------|-----------------|
| Investments in repurchase agreements - own portfolio | | |
| Financial Treasury Bills (LFT) | 124,620 | - |
| National Treasury Notes (NTN) | - | 213,919 |
| National Treasury Bills (LTN) | - | 137,144 |
| Investments in interbank deposits | 57,175 | 11,727 |
| Provision for loss in interbank deposits (i) | <u>(11,727)</u> | <u>(11,727)</u> |
| | <u>170,068</u> | <u>351,063</u> |
| Current | 159,715 | 351,063 |
| Non-current | 10,353 | |

- (i) The provision for loss was recorded because the investment was made in an interbank deposit issued by a financial institution which is currently undergoing bankruptcy proceedings. The due dates of the interbank investments are as follows:

| | <u>Overdue</u> | <u>Up to 30 days</u> | <u>360 days onwards</u> | <u>Total</u> |
|-------------------------------------|-----------------|--------------------------|-----------------------------|-----------------|
| LFT | - | 124,620 | - | 124,620 |
| Interbank Deposit Certificate (CDI) | 11,727 | 35,095 | 10,353 | 57,175 |
| Provision for loss | <u>(11,727)</u> | - | - | <u>(11,727)</u> |
| Total - 12/31/2016 | <u>-</u> | <u>159,715</u> | <u>10,353</u> | <u>170,068</u> |
| Total - 12/31/2015 | - | 351,063 | - | 351,063 |

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6 Marketable securities

(a) Portfolio

The marketable security portfolio is comprised as follows:

| | 2016 | | | 2015 | | |
|--|------------|-------------|--------------|------------|-------------|--------------|
| | Amount | Curve value | Market value | Amount | Curve value | Market value |
| Unrestricted securities | | | | | | |
| Financial Treasury Bills | 80,165 | 676,407 | 675,542 | 44,200 | 327,502 | 327,289 |
| National Treasury Notes | 94,900 | 290,006 | 288,834 | 102,900 | 293,293 | 280,767 |
| Debentures | 30 | 22,095 | 22,095 | 30 | 29,502 | 29,502 |
| Provision for debentures (i) | | - | (111) | | - | - |
| Fund quotas | | | | | | |
| Emerging Companies (Emerging Companies Investment Fund (FIEE)) | 125 | 1,404 | 1,404 | 125 | 1,791 | 1,791 |
| Fund for Investment in Equity Participation (FIP) | 15,344,237 | 12,906 | 12,906 | 13,317,452 | 11,609 | 11,609 |
| Fixed-income Investment Fund | 8,275,088 | 20,112 | 20,112 | | - | - |
| Investment Guarantor Fund (FGI) | 874,836 | 1,300 | 1,300 | 579,520 | 677 | 677 |
| Total unrestricted securities | | 1,024,230 | 1,022,082 | | 664,374 | 651,635 |
| Securities provided as guarantees (ii) | | | | | | |
| - Financial Treasury Bills | 1,335 | 11,280 | 11,268 | | - | - |
| | | 1,035,510 | 1,033,350 | | 664,374 | 651,635 |
| Current | | | 46,939 | | | 44,575 |
| Non-current | | | 986,411 | | | 607,060 |

- (i) In accordance with CMN Resolution 2,686/1999, the provision for debentures is based on the credit risk of the issuer because these securities are financial support, rather than a financial investment (Note 6 (b) (ii)).
- (ii) These securities refer to the guarantee for the differential margin payable on the swap contract.

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(b) Classification of marketable securities

Considering the Bank's intentions and financial capacity, the securities in the marketable security portfolio are classified as follows, as established by the BACEN Circular 3,068/2001:

| | 2016 | | 2015 | |
|--|------------------|------------------|----------------|----------------|
| | Curve value | Market value | Curve value | Market value |
| Available-for-sale securities (i) | 904,531 | 902,482 | 533,951 | 521,212 |
| LFT | 676,407 | 675,542 | 327,502 | 327,289 |
| More than 360 days | 676,407 | 675,542 | 327,502 | 327,289 |
| NTN | 181,122 | 179,950 | 192,372 | 179,846 |
| From 181 to 360 days | - | - | 22,528 | 22,671 |
| More than 360 days | 181,122 | 179,950 | 169,844 | 157,175 |
| Investment fund quotas | 35,722 | 35,722 | 14,077 | 14,077 |
| No stated maturity | 35,722 | 35,722 | 14,077 | 14,077 |
| LFT provided as guarantee | 11,280 | 11,268 | - | - |
| 360 days onwards | 11,280 | 11,268 | - | - |
| Securities held to maturity (ii) | 130,979 | 130,868 | 130,423 | 130,423 |
| NTN | 108,884 | 108,884 | 100,921 | 100,921 |
| More than 360 days | 108,884 | 108,884 | 100,921 | 100,921 |
| Debentures | 22,095 | 21,984 | 29,502 | 29,502 |
| Up to 30 days | 6,313 | 6,281 | 1,204 | 1,204 |
| From 31 to 60 days | 451 | 449 | 602 | 602 |
| From 61 to 90 days | 451 | 449 | 602 | 602 |
| From 91 to 180 days | 1,353 | 1,346 | 1,806 | 1,806 |
| From 181 to 360 days | 2,705 | 2,692 | 3,613 | 3,613 |
| More than 360 days | 10,822 | 10,767 | 21,675 | 21,675 |
| | <u>1,035,510</u> | <u>1,033,350</u> | <u>664,374</u> | <u>651,635</u> |
| Current | | 46,939 | | 44,575 |
| Non-current | | 986,411 | | 607,060 |

(i) Securities classified as available for sale

BDMG's marked-to-market government securities classified as available for sale consider the quotations disclosed by the Brazilian Association of Financial and Capital Market Entities (ANBIMA) for the secondary market of such securities.

(ii) Securities classified as held to maturity.

The securities classified in this category are as follows:

- Debentures

In January 2015, in a direct negotiation with the issuer, the Bank acquired 30 non-convertible debentures with maturities on December 22, 2019.

They are used for financial support, and not as a financial investment.

- National Treasury Notes (NTN)

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At June 30, 2015, the Bank reclassified the following securities from "available for sale" to "held to maturity":

| | <u>Amount</u> | <u>Maturity date</u> | <u>2016</u> | <u>2015</u> |
|--|---------------|----------------------|----------------------------|----------------------------|
| National Treasury Notes - Series B (NTN-B) | 21,000 | 8/15/2022 | 72,105 | 68,803 |
| National Treasury Notes - Series B (NTN-B) | 15,000 | 8/15/2018 | <u>47,624</u> | <u>45,852</u> |
| Adjustment to market value | | | 119,729 <u>(10,845)</u> | 114,655 <u>(13,734)</u> |
| Present value | | | <u>108,884</u> | <u>100,921</u> |

At the reclassification date, the balance of R\$ 15,178 was recorded as a separate component in equity as unrealized gains. Due to the reclassification, this amount must be appropriated to profit (loss) up to the maturity dates of the securities.

In 2016, R\$ 4,334 (2015 - R\$ 1,444) had been appropriated from the amount in equity.

(c) The marketable securities fall due as follows:

| | <u>No stated maturity</u> | <u>Up to 30 days</u> | <u>From 31 to 60 days</u> | <u>From 61 to 90 days</u> | <u>From 91 to 180 days</u> | <u>From 181 to 360 days</u> | <u>After 360 days</u> | <u>Total</u> |
|-------------------------------|-------------------------------|------------------------------|-----------------------------------|-----------------------------------|------------------------------------|-------------------------------------|---------------------------|------------------|
| Federal Government Securities | - | - | - | - | - | - | 975,644 | 975,644 |
| Debentures | - | 6,281 | 449 | 449 | 1,346 | 2,692 | 10,767 | 21,984 |
| Investment fund quotas | <u>35,722</u> | - | - | - | - | - | - | <u>35,722</u> |
| Total - 2016 | <u>35,722</u> | <u>6,281</u> | <u>449</u> | <u>449</u> | <u>1,346</u> | <u>2,692</u> | <u>986,411</u> | <u>1,033,350</u> |
| Total - 2015 | 14,077 | 1,204 | 602 | 602 | 1,806 | 26,284 | 607,060 | 651,635 |

(d) Carrying value adjustments of marketable securities

The changes during the year in the amounts recorded in equity under "Carrying value adjustments", which refer to the adjustments of the Bank securities classified as available for sale, were as follows:

| | <u>Unrealized gains (losses)</u> | <u>Tax effects</u> | <u>Adjustment to market value</u> |
|--------------------------|--------------------------------------|--------------------|---------------------------------------|
| In 2015 | <u>(26,473)</u> | <u>12,136</u> | <u>(14,337)</u> |
| Adjustment in the period | 13,578 | (6,536) | 7,042 |
| In 2016 | <u>(12,895)</u> | <u>5,600</u> | <u>(7,295)</u> |

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7 Derivative instruments

As a result of obtaining funds from overseas as from the second half of 2013, the Bank seeks protection against the risk of exposure to variations in foreign currencies and foreign interest rates established in the contracts. Risks are hedged through derivative financial instruments of the swap type, except with regard to transactions in which the external risks are transferred to the customers.

The outstanding derivative instruments were contracted exclusively as a hedge for risks associated with external funding and, for the contracting of such instruments, the Bank considers the risk control policy and the definition of hedge strategies, limits and manners to monitor these operations.

The contracted derivatives initially included the same terms as the funding transaction (similar beginning date, maturity and notional amount) and are in line with each settlement (interest or repayment + interest) specified for the released funds. In order to account for these transactions, the Bank used the hedge accounting method (market risk category) in order to neutralize the effects on its results of the volatility generated by the difference in the carrying amount of the products: borrowings recorded based on the amortized cost and market-to-market derivatives (MtM).

In accordance with BACEN Circular 3,082/2001, the Bank has documentation referring to the risk of the hedged items, which includes the management of these risks pursuant to risk control policies, the establishment of strategies, limits and manners to continuously monitor these items in order to verify the effectiveness of the hedge instrument.

The methodology used in establishing the market value of both asset and liability swap positions accounted for under the hedge accounting procedure considers the weighting factors calculated at the contracting date and which, at that date, were equal to the market value and operation curve value. The use of weighting factors aims at mitigating the credit risk spread distortion in the calculation of the market value.

BDMG performs effectiveness tests at the beginning of the operation, initial prospective test of the hedge structure and periodically assesses the effectiveness through prospective and retrospective tests, upon the preparation of the semi-annual and annual financial statements, through the calculation of the ratio of the market value variation of the hedge instrument asset position and the variation of the market value of the hedged item.

At December 31, 2016, the Bank's derivatives are classified as market risk hedges and recorded according to the hedge accounting procedure, since they all meet the condition of effectiveness of the hedge as established in BACEN Circular 3,082/2001.

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Because of the conditions established in the swap contracts, the Bank's positions at December 31, 2016 to meet the clauses related to the risk mitigation are as follows:

| | <u>2016</u> | <u>2015</u> |
|--|---------------|----------------|
| Investments in interbank deposits | 45,448 | - |
| Government securities linked as guarantee for the counterparty at the SELIC rate | 11,268 | - |
| Fundings in interbank deposits | 6,680 | 137,501 |
| | <u>63,396</u> | <u>137,501</u> |

SELIC – Special System for Settlement and Custody

In December 2016, the Bank suspended the hedge accounting for swap transactions contracted to hedge the first tranche of the funding with Corporación Andina de Fomento (CAF1) and the first tranche of the funding with the Bank of Tokyo (Tokyo-1) because of the mismatch of terms of funding contracts of the corresponding swaps, as disclosed in Note 29 - Events after the reporting period.

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The positions of the derivatives contracted by the Bank are detailed in the notes below:

(a) Foreign borrowings hedged by derivative instruments

| | Initial date | Final date | Index | Foreign currency loans | 2016 | | 2015 | |
|----------------------------|--------------|------------|---|------------------------------|----------------------------------|----------------|----------------------------------|----------------|
| | | | | | Balance (foreign currency) | Curve | Balance (foreign currency) | Curve |
| CAF 1 | 9/27/2013 | 9/27/2023 | Six-month Libor + 3.65% p.a. | US\$ 15,000 | US\$ 12,512 | 40,772 | US\$ 14,272 | 55,720 |
| CAF 2 | 10/21/2013 | 10/23/2023 | Six-month Libor + 3.65% p.a. | US\$ 30,000 | US\$ 24,945 | 81,283 | US\$ 28,467 | 111,142 |
| CAF3 | 12/19/2013 | 12/19/2023 | Six-month Libor + 3.65% p.a. | US\$ 30,000 | US\$ 24,747 | 80,638 | US\$ 28,270 | 110,372 |
| CAF4 | 10/23/2015 | 10/23/2018 | Six-month Libor + 2.40% p.a. | US\$ 23,500 | US\$ 23,662 | 77,104 | US\$ 23,632 | 92,263 |
| IDB | 8/4/2014 | 8/16/2021 | Six-month Libor + 2.25% p.a. | US\$ 50,000 | US\$ 46,056 | 150,075 | US\$ 50,523 | 197,252 |
| AFD | 8/5/2014 | 11/28/2025 | Six-month Euribor + 2% p.a. | € 5,000 | € 5,008 | 17,214 | € 5,008 | 21,277 |
| Bank of Tokyo 1 | 12/26/2014 | 12/27/2018 | Quarterly interest at the fixed rate of 3.09% p.a. and 3.19% p.a. after 12/31/2015. | US\$ 25,000 | US\$ 20,014 | 65,216 | US\$ 25,018 | 97,674 |
| Bank of Tokyo 2 (*) | 3/17/2015 | 3/13/2019 | Quarterly interest at the fixed rate of 2.68 % p.a. and 2.78% as from 03/14/2016. | US\$ 25,000 | - | - | US\$ 25,032 | 97,729 |
| | | | | | | 512,302 | | 783,429 |
| Adjustment to market value | | | | | | (1,477) | | (8,037) |
| Market value | | | | | | <u>510,825</u> | | <u>775,392</u> |

(*) The funding transaction Bank of Tokyo 2 and the corresponding hedge transaction were settled on April 1, 2016.

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(b) Swap amounts recorded

The derivative financial instruments at December 31 were as follows:

| | <u>2016</u> | | <u>2015</u> | |
|---------------------------------------|----------------|---------------|------------------|----------------|
| Notional value | - | Amount | Net effect | net effect |
| memorandum | - | receivable / | (statement | (statement |
| account | - | payable | of | of |
| | - | (balance | operations | operations |
| | - | sheet | account) | account) |
| | - | account) | - | - |
| (US\$+ Libor+ rate) x (BRL +%CDI) (1) | 258,358 | 52,118 | (71,806) | 89,612 |
| (EUR+Euribor+rate) x (BRL +%CDI) (1) | 15,210 | 1,294 | (4,933) | 1,903 |
| (US\$+rate) x BRL +%CDI (1) | 54,060 | 11,343 | (33,188) | 35,228 |
| (US\$+ Libor+ rate) x (BRL +%CDI) (2) | 172,163 | (15,600) | (53,307) | 4,547 |
| | <u>499,791</u> | <u>49,155</u> | <u>(163,234)</u> | <u>131,290</u> |

Notes:

(1) Differential receivable

(2) Differential payable

(c) Swaps, by index:

| | <u>2016</u> | <u>2015</u> |
|---|---------------|----------------|
| Asset position - differential receivable | | |
| Foreign currency | 64,755 | 171,358 |
| Interest | 64,705 | 172,819 |
| | 50 | (1,461) |
| Liability position - differential payable | (15,600) | - |
| Foreign currency | (15,600) | - |
| Net exposure | <u>49,155</u> | <u>171,358</u> |

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(d) Swaps, by maturity:

| | Up to 30 days | From 31 to 180 days | From 181 to 360 days | After 360 days | Total |
|--|------------------|------------------------|----------------------------|-------------------|-----------------|
| Asset position - differential receivable | | | | | |
| Foreign currency | 63,411 | - | - | 1,294 | 64,705 |
| Interest | - | - | - | 50 | 50 |
| Total - 12/31/2016 | <u>63,411</u> | <u>-</u> | <u>-</u> | <u>1,344</u> | <u>64,755</u> |
| Total - 12/31/2015 | - | 5,053 | 4,551 | 161,754 | 171,358 |
| Liability position - differential payable | | | | | |
| Foreign currency | - | - | - | (15,600) | (15,600) |
| Total - 12/31/2016 | <u>-</u> | <u>-</u> | <u>-</u> | <u>(15,600)</u> | <u>(15,600)</u> |
| Total - 12/31/2015 | - | - | - | - | - |
| Net exposure - 12/31/2016 | <u>63,411</u> | <u>-</u> | <u>-</u> | <u>(14,256)</u> | <u>49,155</u> |
| Net exposure - 12/31/2015 | - | 5,053 | 4,551 | 161,754 | 171,358 |

(e) Swaps, by index and notional amount:

| | Notional value | Curve value | Adjustment to market value | Market value |
|--|-------------------|-----------------|-------------------------------|-----------------|
| Asset position - differential receivable | | | | |
| (US\$+ Libor+ rate) x (BRL +%CDI) | 258,358 | 54,801 | (2,683) | 52,118 |
| (EUR+Euribor+rate) x (BRL +%CDI) | 15,210 | 1,806 | (512) | 1,294 |
| (US\$+ rate) x (BRL +%CDI) | 54,060 | 11,014 | 329 | 11,343 |
| Total - 12/31/2016 | <u>327,628</u> | <u>67,621</u> | <u>(2,866)</u> | <u>64,755</u> |
| Total - 12/31/2015 | 657,983 | 186,281 | (14,923) | 171,358 |
| Liability position - differential payable | | | | |
| (US\$+ Libor+ rate) x (BRL +%CDI) | 172,163 | (16,785) | 1,185 | (15,600) |
| Total - 12/31/2016 | <u>172,163</u> | <u>(16,785)</u> | <u>1,185</u> | <u>(15,600)</u> |
| Total - 12/31/2015 | - | - | - | - |
| Net exposure - 12/31/2016 | <u>499,791</u> | <u>50,836</u> | <u>(1,681)</u> | <u>49,155</u> |
| Net exposure - 12/31/2015 | 657,983 | 186,281 | (14,923) | 171,358 |

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8 Credit operations and receivables equated with credit operations

The Bank's credit portfolio is as follows:

| | <u>Total amount</u> | <u>Provision</u> | <u>Net amount</u> |
|--------------------------------------|---------------------|------------------|-------------------|
| Credit operations | 5,962,385 | (317,242) | 5,645,143 |
| Credits equated with loan operations | <u>1,418</u> | <u>(7)</u> | <u>1,411</u> |
| Total - 12/31/2016 | <u>5,963,803</u> | <u>(317,249)</u> | <u>5,646,554</u> |
| Total - 12/31/2015 | 5,893,114 | (389,122) | 5,503,992 |

The credit operations at December 31, 2016 totaled R\$ 5,963,803 (2015 - R\$ 5,893,114), of which R\$ 1,788,769 (2015 - R\$ 2,307,034) was granted with own resources and R\$ 4,175,034 (2015 - R\$ 3,586,080), originally, with funds onlent by other financial institutions.

The balance of the renegotiated operations at December 31, 2016 amounted to R\$ 818,732 (2015 - R\$ 694,738).

(a) Classification by product and by segment of activity

| | <u>2016</u> | <u>2015</u> |
|---|------------------|------------------|
| Loans | <u>1,276,627</u> | <u>1,477,698</u> |
| Industry | 756,846 | 681,027 |
| Commerce | 298,552 | 314,055 |
| Other services | 221,229 | 482,616 |
| Financing to the private sector | <u>3,858,338</u> | <u>3,609,515</u> |
| Manufacturing | 1,854,428 | 1,836,852 |
| Commerce | 222,729 | 204,209 |
| Other services | 991,863 | 918,105 |
| Rural and agribusiness | 774,790 | 628,295 |
| Financial intermediaries | 8,287 | 14,817 |
| Individuals | 6,241 | 7,237 |
| Financing to the public sector (municipal direct and indirect management) | 827,420 | 804,226 |
| Credits equated with credit operations | <u>1,418</u> | <u>1,675</u> |
| Subtotal | <u>5,963,803</u> | <u>5,893,114</u> |
| Provision for impairment of receivables | <u>(317,249)</u> | <u>(389,122)</u> |
| | <u>5,646,554</u> | <u>5,503,992</u> |
| Current | 1,371,268 | 1,332,614 |
| Non-current | 4,275,286 | 4,171,378 |

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(b) Classification by maturity and risk levels

| Risk level | 2016 | | | | | | | | | 2015 |
|------------|------------------|-------------------|---------------|----------------|-----------------------|------------------|-------------------|---------------------|---------------|------------------|
| | Total | Overdue (in days) | | | Falling due (in days) | | | | | Total |
| | | As from 15 | Up to 14 | Up to 90 | From 91 to 360 | From 361 to 1080 | From 1081 to 1800 | From 1,800 to 5,400 | Over 5400 | |
| AA | 1,982,240 | - | - | 109,629 | 275,167 | 700,558 | 371,881 | 523,972 | 1,033 | 1,840,617 |
| A | 998,977 | - | - | 63,146 | 165,066 | 335,146 | 189,553 | 228,343 | 17,723 | 1,123,740 |
| B | 1,278,229 | 2,462 | 239 | 88,724 | 275,272 | 504,631 | 244,483 | 162,418 | - | 1,148,876 |
| C | 1,041,914 | 3,852 | 31,439 | 73,208 | 185,789 | 366,322 | 183,263 | 198,041 | - | 1,059,330 |
| D | 259,584 | 6,858 | 826 | 15,421 | 42,342 | 90,835 | 56,747 | 46,555 | - | 398,276 |
| E | 278,142 | 4,933 | 254 | 15,783 | 43,654 | 120,739 | 65,499 | 27,280 | - | 56,717 |
| F | 16,621 | 3,402 | 91 | 1,086 | 2,917 | 4,308 | 1,920 | 2,897 | - | 53,032 |
| G | 14,411 | 2,522 | 137 | 632 | 6,793 | 3,265 | 725 | 337 | - | 14,555 |
| H | 93,685 | 28,763 | 419 | 5,615 | 13,869 | 21,848 | 11,353 | 11,818 | - | 197,971 |
| | <u>5,963,803</u> | <u>52,792</u> | <u>33,405</u> | <u>373,244</u> | <u>1,010,869</u> | <u>2,147,652</u> | <u>1,125,424</u> | <u>1,201,661</u> | <u>18,756</u> | <u>5,893,114</u> |

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(c) Classification by risk levels and provision

| | | <u>2016</u> | | | <u>2015</u> | |
|----------------|-----|------------------|--|--|------------------|----------------------------------|
| | | <u>Portfolio</u> | <u>Provision for credit risk based on minimum percentages required</u> | <u>Provision for impairment of receivables (i)</u> | <u>Portfolio</u> | <u>Impairment of receivables</u> |
| Level of risk: | % | | | | | |
| AA | 0 | 1,982,240 | | (46,730) | 1,840,617 | (48,716) |
| A | 0.5 | 998,977 | (4,996) | (4,996) | 1,123,740 | (5,619) |
| B | 1 | 1,278,229 | (12,782) | (12,782) | 1,148,876 | (11,489) |
| C | 3 | 1,041,914 | (31,257) | (31,257) | 1,059,330 | (31,780) |
| D | 10 | 259,584 | (25,958) | (25,958) | 398,276 | (39,828) |
| E | 30 | 278,142 | (83,443) | (83,443) | 56,717 | (17,015) |
| F | 50 | 16,621 | (8,311) | (8,311) | 53,032 | (26,516) |
| G | 70 | 14,411 | (10,087) | (10,087) | 14,555 | (10,188) |
| H | 100 | 93,685 | (93,685) | (93,685) | 197,971 | (197,971) |
| | | <u>5,963,803</u> | <u>(270,519)</u> | <u>(317,249)</u> | <u>5,893,114</u> | <u>(389,122)</u> |

(i) Until November 2005, the credit operations relating to the Special Program of Assets Recovery (PESA) (Rural Credit, under the terms of CMN/BACEN Resolution 2,471/1998) were classified in level H. As from that date, BDMG management reclassified them to level AA. This risk reclassification considered the characteristics of the transactions as regards the credit risk, mitigated through real guarantees represented by public securities. The Bank records a supplementary provision for credit transactions, which is calculated as the difference between the adjusted principal balance of the reclassified transactions and the present value of the securities which guarantee these transactions. At December 31, 2016, this additional provision amounted to R\$ 46,730 (2015 - R\$ 48,716).

Changes in the provision for impairment of receivables

| | <u>2016</u> | <u>2015</u> |
|--|------------------|------------------|
| Opening balance | 389,122 | 217,838 |
| Recording of provision, net of reversals | 172,806 | 285,879 |
| Credits written-off as losses | <u>(244,679)</u> | <u>(114,595)</u> |
| Closing balance | <u>317,249</u> | <u>389,122</u> |

(e) Credit assignments

The balance of operations assigned with co-obligation, according to the amounts shown below, refers to operations assigned up to December 31, 2011 (prior to CMN Resolution 3,533/2008):

| | <u>2016</u> | <u>2015</u> |
|--|---------------|---------------|
| Assignment prior to CMN Resolution 3,533/2008: | | |
| Recourses to be settled | 24,486 | 27,479 |
| Settled transactions to be transferred | <u>612</u> | <u>290</u> |
| | <u>25,098</u> | <u>27,769</u> |

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9 Other receivables

| | <u>2016</u> | <u>2015</u> |
|---|-----------------|-----------------|
| Tax credits (a) | 388,265 | 362,221 |
| Debtors for deposits in guarantee (b) | 117,418 | 110,155 |
| Notes and credits receivable (c) | 12,127 | 14,470 |
| Sundry debtors - local (d) | 13,948 | 7,520 |
| Income receivable (e) | 3,769 | 3,797 |
| Other | 4,978 | 4,366 |
| Provision for impairment of other receivables (f) | <u>(12,309)</u> | <u>(12,303)</u> |
| | <u>528,196</u> | <u>490,226</u> |
| Current | 204,491 | 97,455 |
| Non-current | 323,705 | 392,771 |

- (a) The tax credits for income tax and social contribution on net income were calculated and recorded based on the aspects disclosed in Note 23 (a).
- (b) The debtors for guarantee deposits mainly relate to legal disputes, especially those of a fiscal and tax nature, as described in Note 14 (a), which includes the relationship of the judicial deposits with the related legal cases.
- (c) The notes and credits receivable relate to: (i) income amounting to R\$ 11,119 (2015 - R\$ 11,119) due to the renegotiations based on laws related to rural credit transactions carried out with funds from the National Treasury Secretariat (STN), for which provisions were recorded as detailed in Note 9 (f); and (ii) income from the Fund for the Defense of the Coffee Economy (Funcafé) amounting to R\$ 1,007 (2015 - R\$ 20).
- (d) The balance of sundry debtors mainly comprises the receivable of R\$ 12,424 (2015 - R\$ 0) relating to guarantees received by the Bank as agreed-upon with creditor of the company under in-court reorganization and approved by the courts, and R\$ 1,319 (2015 - R\$ 7,448) relating to the non-default bonus granted by the Bank to customers of renegotiated rural operations according to the provisions of Law 9,138/1995 and its amendments.
- (e) Income receivable mainly comprises the remuneration receivable, net of the related provision, from credit operations carried out with resources of the development funds managed by BDMG, totaling R\$ 2,651 (2015 - R\$ 3,073). The income falls due based on the maturity dates of the contracted installments, and a provision is recorded based on the risk level in which the transaction generating the income is classified. This classification is a result of the policy adopted by the Bank referring to the transactions funded by resources from the managed funds, which are the same criteria established in CMN Resolution 2,682/1999 for the credit transactions of BDMG's own portfolio.
- (f) The provision for impairment of receivables of R\$ 12,309 (2015 - R\$ 12,303) mainly refers to credits without the characteristics of loan transactions comprised of amounts to be reimbursed by the National Treasury Secretariat (STN) and which were recorded based on the uncertainty regarding the period of realization of these receivables.

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10 Other assets

| | <u>2016</u> | <u>2015</u> |
|---------------------------------------|----------------|----------------|
| Assets not for own use | 57,415 | 22,180 |
| Equity investments | 6 | - |
| Other | 211 | 186 |
| Subtotal | <u>57,632</u> | <u>22,366</u> |
| Provisions for assets not for own use | <u>(2,631)</u> | <u>(2,074)</u> |
| | <u>55,001</u> | <u>20,292</u> |
| Current | 211 | 186 |
| Non-current | 54,790 | 20,106 |

11 Permanent assets

(a) Investments

| | <u>2016</u> | <u>2015</u> |
|---|---------------|---------------|
| BDMGTEC Participações S.A. (i) | 84,315 | 78,196 |
| Other | 1,324 | 1,324 |
| Provision for losses, shares and quotas | <u>(837)</u> | <u>(837)</u> |
| | <u>84,802</u> | <u>78,683</u> |

(i) The objective of BDMGTEC Participações S.A., a wholly-owned subsidiary of the Bank, established in March 2012, based on State Law 19,967/2011, is to invest in companies with significant interest to the State, in order to promote its development.

(b) Property and equipment in use

| | <u>2016</u> | | <u>2015</u> | |
|-------------------------------------|---------------|---------------------------------|-------------------|-------------------|
| | <u>Cost</u> | <u>Accumulated depreciation</u> | <u>Net amount</u> | <u>Net amount</u> |
| Real estate | 43,788 | (26,004) | 17,784 | 18,427 |
| Facilities, furniture and equipment | 6,115 | (5,224) | 891 | 1,094 |
| Data processing system | 6,079 | (4,491) | 1,588 | 2,065 |
| Other | 585 | (534) | 51 | 58 |
| Construction in progress | 165 | - | 165 | 314 |
| | <u>56,732</u> | <u>(36,253)</u> | <u>20,479</u> | <u>21,958</u> |

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(c) Intangible assets

| | <u>2016</u> | | <u>2015</u> |
|-------------------|---------------|-------------------------------------|-------------------|
| | <u>Cost</u> | <u>Accumulated amortization</u> | <u>Net amount</u> |
| Intangible assets | <u>18,288</u> | <u>(6,951)</u> | <u>11,337</u> |
| | <u>18,288</u> | <u>(6,951)</u> | <u>11,337</u> |
| | <u>18,288</u> | <u>(6,951)</u> | <u>11,337</u> |
| | <u>18,288</u> | <u>(6,951)</u> | <u>11,337</u> |

12 Deposits and funds from acceptances and issue of securities

The funds obtained in Brazil are as follows:

| | <u>2016</u> | <u>2015</u> |
|--|----------------|----------------|
| Interbank deposits (a) | 6,680 | 137,501 |
| Financial bills (b) | 593,023 | 681,918 |
| Agribusiness letters of credit (LCA) (c) | <u>16,040</u> | - |
| | <u>615,743</u> | <u>819,419</u> |
| Current | 599,381 | 247,536 |
| Non-current | 16,362 | 571,883 |

(a) Interbank deposits

At December 31, 2016, the balance of interbank deposits of R\$ 6,680 (2015 - R\$ 137,501) refers to the funds obtained to comply with the clause of credit risk mitigation included in derivative contracts, which requires that the party with a difference payable in excess of a certain amount maintain interbank deposits in the institution that is the counterparty of the transaction.

These deposits constitute a guarantee margin, have charges equal to the CDI interest rate and maturities varying in accordance with the amount adjusted for the coverage of the differential receivable from or payable for each one of the swaps contracted.

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(b) Financial bills

The funds obtained with the issue of financial bills were as follows:

| | | | <u>2016</u> | <u>2015</u> |
|----------------|-----------------|---------------|----------------|----------------|
| | <u>Maturity</u> | <u>Amount</u> | <u>Balance</u> | <u>Balance</u> |
| Type of issue: | | | | |
| Public | 3/14/2017 | 1,238 | 258,542 | 258,828 |
| Public | 12/17/2017 | 1,250 | 334,481 | 313,055 |
| Private | 5/9/2016 | 275 | - | 84,314 |
| Private | 12/23/2016 | 100 | - | 25,721 |
| | | <u>2,863</u> | <u>593,023</u> | <u>681,918</u> |
| Current | | | 593,023 | 110,035 |
| Non-current | | | - | 571,883 |

The issue of financial bills is supported by CMN Resolution 4,143/2012, which authorized the issue of such securities by development banks.

The Bank carried out two issues of financial bills with brAAA ratings, as attributed by Standard & Poor's Rating Services (S&P), which was the same long-term issuer credit rating attributed in Brazil National Scale to BDMG.

Despite the downgrading of the Bank's risk grades, as mentioned in Note 13 (a), there have been no consequences regarding the financial bills, since they were issued with the sole purpose of raising funds, and the downgrades require no condition of anticipated maturity, as disclosed in the following subjects included in the answer provided by BACEN to the survey made by BDMG:

- Ratification regarding the Bank's understanding that the initial downgrading of the bills issued does not trigger the prepayment of these securities, in accordance with article 38, IX, paragraph 5, and article 31, VI, of Law 12,249/2010 and CMN Resolution 4,132/12.

- The early maturity of financial bills can only be triggered according to Article 9 of Resolution 4,123, dated August 23, 2012, that is, when the security is used for the realization of related asset operations.

(c) Agribusiness letters of credit (LCA)

The Bank, backed by agribusiness credit transactions, started to issue LCAs as from December 2016. In compliance with the effective standards, the securities are held in custody in the Central System for Custody and Financial Settlement of Securities (CETIP) and are backed by the Credit Guarantor Fund.

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At December 31, 2016, the LCAs are as follows:

| <u>Date of issuance</u> | <u>Maturity</u> | <u>2016</u> | |
|-------------------------|-----------------|---------------|----------------|
| | | <u>Amount</u> | <u>Balance</u> |
| 12/21/2016 | 12/16/2019 | 1,000 | 1,003 |
| 12/23/2016 | 12/9/2019 | 15,000 | 15,037 |
| | | <u>16,000</u> | <u>16,040</u> |
| Current | | | - |
| Non-current | | | 16,040 |

13 Borrowings and onlendings

(a) Abroad

At December 31, 2016, the funds raised overseas by the Bank (with regard to all these fund raising operations) amounted, for all fundings, to R\$ 554,085 (2015 - R\$ 836,101) at the curve value and R\$ 552,608 (2015 - R\$ 828,063) at market value, which is only calculated for funding hedged by derivative instruments.

The external funding is as follows:

| | <u>2016</u> | | <u>2015</u> | |
|---------------|--------------|----------------|--------------|----------------|
| | <u>Curve</u> | <u>Market</u> | <u>Curve</u> | <u>Market</u> |
| Institution: | | | | |
| CAF | 283,711 | 284,087 | 375,360 | 373,201 |
| IDB | 150,075 | 148,781 | 197,252 | 192,656 |
| AFD | 55,083 | 54,523 | 68,086 | 66,790 |
| Bank of Tokyo | 65,216 | 65,216 | 195,403 | 195,416 |
| | | <u>552,608</u> | | <u>828,063</u> |
| Current | | 159,956 | | 76,722 |
| Non-current | | 392,652 | | 751,341 |

To hedge against the foreign exchange and foreign interest rate risks associated with foreign borrowings whose risks are not transferred to the borrower in the domestic market, the Bank uses derivative financial instruments, recorded according to hedge accounting principles. With regard to the hedged foreign borrowings, which are presented in Note 7, the market value adjustment is calculated for the use of that accounting procedure, except for the CAF-1 and the Bank of Tokyo transactions, for which this procedure was suspended in December 2016.

All contracts related to foreign funding and to the derivative instruments used to hedge these fundings have covenants. The Bank monitors and complies with these covenants, which can also be backed by additional agreements entered into by the parties.

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BDMG's risk rating, on a global scale, was reclassified on February 19, 2016, by the rating agency Standard & Poor's, from BB to BB-, with negative outlook, and, on February 25, 2016, by Moody's, from Ba1 to Ba3, with negative outlook. These reclassifications followed the downgrading of the State of Minas Gerais by the two rating agencies. The reclassification of the rating of Brazil is the main reason for the adjustment of the rating of the State government. On a local scale, BDMG's rating was reclassified from brA+ to brA by Standard & Poor's and from Aa2 to A2 by Moody's.

In July 2016, Moody's reclassified BDMG's risk grading as long-term domestic and global scale issuer from Ba3 to B1. On December 14, 2016, the Bank's risk rating granted by S&P Global Ratings changed from BB- to B- in the global scale, and from bra to brB- in the national scale. These reclassifications were in conformity with the same reclassifications granted to its controlling stockholder, the State of Minas Gerais, in the previous day. Together with this, S&P Ratings confirmed BDMG's stand-alone credit profile (SACP) as "bb-", while making no changes to the Bank's standalone rating.

The Bank assessed, for negotiations with counterparties whose contracts establish covenants related to credit risk ratings, the following conditions that can be adopted and that are more in consonance with its strategic planning: negotiation with creditors for obtaining waivers; replacement of counterparties, or early settlement of the contract.

However, even when the adoption of any of these occurrences is considered, Bank's internal studies prove that such events affect neither its liquidity nor the adequate progress of its businesses.

The funds raised by BMDG overseas are as follows:

I Corporación Andina de Fomento - CAF

The financing of US\$ 100 million, contracted with CAF, in August 2014, with interest of the six-month Libor plus up to 3.65% p.a. and maturity of up to 10 years, was released in tranches of different amounts, presented below::

| Tranches | Date of release | Final maturity | Release - US\$ (ooo) | 12/31/2016 | | 12/31/2015 | |
|----------|-----------------|----------------|----------------------|----------------|----------------|----------------|----------------|
| | | | | Curve - R\$ | Market - R\$ | Curve - R\$ | Market - R\$ |
| CAF 1 | 9/27/2013 | 9/27/2023 | 15,000 | 40,771 | 40,771 | 55,721 | 54,124 |
| CAF 2 | 10/21/2013 | 10/23/2023 | 30,000 | 81,283 | 80,451 | 111,142 | 108,572 |
| CAF 3 | 12/19/2013 | 12/19/2023 | 30,000 | 80,638 | 80,321 | 110,372 | 111,242 |
| CAF 4 | 10/23/2015 | 10/23/2018 | 23,500 | 77,104 | 78,629 | 92,263 | 93,401 |
| CAF 5 | 12/21/2015 | 12/21/2020 | 1,500 | 3,915 | 3,915 | 5,862 | 5,862 |
| | | | <u>100,000</u> | <u>283,711</u> | <u>284,087</u> | <u>375,360</u> | <u>373,201</u> |

BMDG opted to settle the swap transaction that hedged the funding of tranche CAF 1 in January 2017 and, then, to make a deposit in U.S. dollars equal to the amount of the debt at the same date of the settlement, for foreign exchange risk hedging purposes. As a result, the hedge accounting was suspended in December 2016 by reversing the adjustment to market value of the hedge object that generated an expense amounting to R\$ 654. As a result, the market value of this operation is equivalent to the curve value.

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The market value of the funding transaction of CAF 5 corresponds to the amortized cost, since it is a natural hedge for which the financial conditions related to the foreign funding have been transferred to the operations with credit-taking customers, plus the Bank's remuneration.

II French Agency for Development (or Agence Française de Développement - AFD)

In December 2013, the Bank entered into an agreement with the AFD amounting to € 50 million, bearing interest at the six-month Euro Interbank Offered Rate (Euribor) plus 2% p.a. and with maturity of 12 years, to be released through tranches in different amounts. The purpose of this transaction was the financing of municipal infrastructure projects related to climate issues and the expansion of basic services.

The released tranches are as follows:

| Tranches | Date of release | Final maturity | Release - € (ooo) | 2016 | | 2015 | |
|-------------|-----------------|----------------|-------------------|-------------|--------------|-------------|--------------|
| | | | | Curve - R\$ | Market - R\$ | Curve - R\$ | Market - R\$ |
| AFD 1 | 7/22/2014 | 5/30/2017 | 9,000 | 30,984 | 30,424 | 38,298 | 37,002 |
| 1st tranche | | | 4,000 | 13,770 | 13,770 | 17,021 | 17,021 |
| 2nd tranche | | | 5,000 | 17,214 | 16,654 | 21,277 | 19,981 |
| AFD 2 | 10/13/2014 | 5/30/2017 | 7,000 | 24,099 | 24,099 | 29,788 | 29,788 |
| | | | 16,000 | 55,083 | 54,523 | 68,086 | 66,790 |

III Inter-American Development Bank (IDB)

In June 2014, BDMG entered into a borrowing agreement with the IDB, of up to the limit of US\$ 150 million, through releases to be made in three tranches. This borrowing will bear a floating interest rate, to be paid on a six-monthly basis, at 2.25% plus the applicable semi-annual Libor rate, which may vary depending on the criteria established in the contract for each tranche.

The tranche already released is as follows:

| Tranches | Date of release | Final maturity | Release - US\$ (ooo) | 2016 | | 2015 | |
|----------|-----------------|----------------|----------------------|-------------|--------------|-------------|--------------|
| | | | | Curve - R\$ | Market - R\$ | Curve - R\$ | Market - R\$ |
| IDB | 8/4/2014 | 8/16/2021 | 50,000 | 150,075 | 148,781 | 197,252 | 192,656 |

IV Bank of Tokyo-Mitsubishi UFJ Ltd. (BTMU) - (Bank of Tokyo)

BDMG contracted, in December 2014, a bilateral borrowing amounting to US\$ 50 million with the Bank of Tokyo, which will be released through tranches with four-year maturities and financial charges of quarterly interest at the fixed rate of 3.09% p.a. up to December/2015 and of 3.19% p.a., after that date. The pro rata calculation of the interest is made according to the criterion established in the contract.

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The released tranches are as follows:

| Tranches | Date of release | Final maturity | Release - US\$ (000) | 2016 | | 2015 | |
|----------|-----------------|----------------|----------------------|-------------|--------------|-------------|--------------|
| | | | | Curve - R\$ | Market - R\$ | Curve - R\$ | Market - R\$ |
| Tokyo 1 | 12/26/2014 | 12/27/2018 | 25,000 | 65,216 | 65,216 | 97,674 | 97,329 |
| Tokyo 2 | 3/17/2015 | 3/13/2019 | 25,000 | - | - | 97,729 | 98,087 |
| | | | 50,000 | 65,216 | 65,216 | 195,403 | 195,416 |

The Bank settled tranche Tokyo 2 on April 1, 2016 and opted to settle Tokyo 1 in January 2017. With this option, there has been a mismatch of terms between the hedge and the hedge object, which led to the suspension of the hedge accounting in December, with a positive result in the statement of operations of R\$ 298.

(b) Official institutions

These obligations correspond to the balances of the resources obtained from official funds and programs onlent to finance projects in the State of Minas Gerais. The maturities of the principal and related charges are up to 2029, and the financial charges are defined in the operating policies of each agency or fund which is transferring the resources.

The balances of these obligations are summarized as follows:

| | 2016 | 2015 |
|--|------------------|------------------|
| BNDES (i) | 2,268,084 | 1,818,765 |
| FINAME | 1,462,717 | 1,486,984 |
| Bank of Northeast of Brazil (BNB) | 20,996 | 25,511 |
| National Treasury | 12,486 | 12,508 |
| Caixa Econômica Federal (CEF) | 2,285 | - |
| Fund for Financing of Studies and Projects (FINEP) | 67,194 | 34,918 |
| Funcafé | 174,607 | 55,770 |
| | <u>4,008,369</u> | <u>3,434,456</u> |
| Current | 908,933 | 654,307 |
| Non-current | 3,099,436 | 2,780,149 |

The National Bank for Economic and Social Development (BNDES)/Government Agency for Machinery and Equipment Financing (FINAME) System is the main source of funds for onlending from BDMG to its customers.

- (i) The funds from BNDES are mainly allocated to the financing of long-term investment projects.

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The funds transferred by BNDES arose mainly from the following credit lines:

| | <u>2016</u> | <u>2015</u> |
|------------------------------|------------------|------------------|
| BNDES Automático PROGEREN | 787,194 | 450,962 |
| BNDES FINEM | 343,915 | 251,403 |
| BNDES Automático TJLP | 138,756 | 163,209 |
| BNDES Automático | 225,448 | 146,789 |
| BNDES Automático PROCAP-AGRO | 45,271 | 100,920 |
| BNDES FINEM TJLP | 72,608 | 94,938 |
| BNDES Automático PRODECOOP | 90,031 | 84,042 |
| BNDES FINEM PSI | 66,119 | 75,998 |
| BNDES Automático TJ-462 | 41,352 | 54,118 |
| BNDES FINEM TJ-462 | 40,754 | 53,854 |
| Other | 416,636 | 342,532 |
| | <u>2,268,084</u> | <u>1,818,765</u> |

14 Other liabilities

| | <u>2016</u> | <u>2015</u> |
|---------------------------------|----------------|----------------|
| Taxes and social security (a) | 235,546 | 212,842 |
| Sundry (b) | 379,814 | 297,222 |
| Social and statutory | 14,770 | - |
| Financial and development funds | 70,146 | 13,839 |
| Collection of taxes | 783 | 995 |
| | <u>701,059</u> | <u>524,898</u> |
| Current | 113,231 | 76,672 |
| Non-current | 587,828 | 448,226 |

(a) Taxes and social security

| | <u>2016</u> | <u>2015</u> |
|--|----------------|----------------|
| Provision for tax obligations (i) and (ii) | 187,886 | 173,519 |
| Provision for deferred taxes and contributions | 12,627 | 12,839 |
| Provision for taxes and contributions | 27,941 | 14,451 |
| Taxes and contributions payable | 7,092 | 4,213 |
| | <u>235,546</u> | <u>218,842</u> |
| Current | 44,971 | 36,978 |
| Non-current | 190,575 | 175,864 |

- (i) The provision for tax obligations is comprised of the liabilities related to taxes, involving ongoing administrative proceedings and legal lawsuits with the Brazilian Federal Revenue Secretariat (SRF), which are adjusted by the Special System for Settlement and Custody (SELIC) interest rate on a monthly basis. The projection of results of BDMG consider the realization of the tax credits related to this provision over a period of 10 years.

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The changes in the provision for tax obligations in the year were as follows:

| | <u>2015</u> | <u>Provision</u> | <u>Adjustment</u> | <u>2016</u> |
|---|----------------|------------------|-------------------|----------------|
| Change in the Social Contribution on Revenues (COFINS) calculation basis - Law 9,718/1998 | 112,567 | - | 10,229 | 122,796 |
| Change in the Social Integration Program (PIS)/Public Service Employee Savings Program (PASEP) calculation basis - Law 9,718/1998 | 54,202 | - | 3,800 | 58,002 |
| Tax exemption for the Social Security Fund (FINSOCIAL) from December 1986 to March 1990 | 4,828 | - | 195 | 5,023 |
| Other contingencies and legal obligations | <u>1,922</u> | <u>12</u> | <u>131</u> | <u>2,065</u> |
| | <u>173,519</u> | <u>12</u> | <u>14,355</u> | <u>187,886</u> |

(ii) The Bank has judicial deposits in connection with the above tax obligations amounting to R\$ 114,122 (2015 - R\$ 106,487), which are included the balance of R\$ 117,418 (2015 - R\$ 110,155) of the account "Other receivables - Debtors for deposits in guarantee" (Note 9(b)).

The judicial deposits related to the ongoing tax proceedings are as follows:

| | <u>2016</u> | | <u>2015</u> | |
|---|------------------|-----------------|------------------|-----------------|
| | <u>Provision</u> | <u>Deposits</u> | <u>Provision</u> | <u>Deposits</u> |
| Change in the COFINS calculation basis - Law 9,718/1998 | 122,796 | 49,666 | 112,567 | 46,104 |
| Change in the PIS/PASEP calculation basis - Law 9,718/1998 | 58,002 | 58,002 | 54,202 | 54,202 |
| Tax exemption for the Social Security Fund (FINSOCIAL) from December 1986 to March 1990 | 5,023 | 5,023 | 4,828 | 4,828 |
| Other contingencies and legal obligations | <u>2,065</u> | <u>1,431</u> | <u>1,922</u> | <u>1,353</u> |
| | <u>187,886</u> | <u>114,122</u> | <u>173,519</u> | <u>106,487</u> |

In the judicial proceedings related to COFINS and to PIS/PASEP, the Bank seeks the suspension of the payment of these taxes, according to Law 9,718/1998. In addition to establishing the payment of COFINS by financial institutions, this Law also extended the calculation basis for the PIS/PASEP contribution by determining that revenue for this purpose considered both the gross operating and non-operating incomes. Because of the decisions already issued during the course of the proceedings, the Bank made judicial deposits up to December 2014 in order to cover the COFINS contribution on revenues from services rendered. As from January 2015, with the effectiveness of the amendments introduced by Law 12,973/2014, the Bank started to pay PIS/PASEP and COFINS normally on all of its revenues.

The tax and social security provisions recorded by the Bank follow BACEN Circular 3,429/2010, which requires the recognition, as liabilities of all tax obligations, even though there are current legal discussions about the constitutionality of the Laws that established such obligations, up to the effective termination of the corresponding lawsuits.

The contingent tax lawsuits whose likelihood of loss was considered as only possible are not accrued (Note 2.14) and are summarized as follows:

- Decision issued by the Federal Revenue Service on December 11, 2008 not accepting the income tax offsetting made in 2004 and 2005. The adjusted amount of the fine applied on the debits not offset is R\$ 569 (2015 - R\$ 569).

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- Tax assessment notice issued by the SRF in July 2010 related to the difference in the calculation of income tax and social contribution in the period from 2005 to 2007. The updated assessment notice amounts to R\$ 9,345 (2015 - R\$ 8,686).
- Assessment notice issued by the National Institute of Social Security (INSS) in 2006 related to events considered by the INSS as subject to social security contributions. This tax assessment notice, which was disclosed in the balance sheet at December 31, 2015 with the balance of R\$ 5,648, was assessed as having a remote likelihood of loss at December 31, 2016.

(b) Sundry

| | <u>2016</u> | <u>2015</u> |
|--|----------------|----------------|
| Provision for other obligations (i) | 75,197 | 59,186 |
| Provision for future payments (ii) | 16,432 | 12,557 |
| Actuarial liabilities (iii) | 282,703 | 215,245 |
| Contribution for capital increase (iv) | 49 | 594 |
| Sundry creditors - local (v) | <u>5,433</u> | <u>9,640</u> |
| | <u>379,814</u> | <u>297,222</u> |
| Current | 51,306 | 37,477 |
| Non-current | 328,508 | 259,745 |

(i) The provision for other obligations and the changes during the period are as follows:

| | <u>2015</u> | <u>New provisions</u> | <u>Restatements</u> | <u>Write-offs</u> | <u>2016</u> |
|--|---------------|-----------------------|---------------------|-------------------|---------------|
| Charges on the compulsory deposit in BACEN (i) | 36,016 | - | 5,049 | - | 41,065 |
| Coobligation assumed in loan transactions ceded to STN | 5,163 | 406 | - | (1,209) | 4,360 |
| Civil proceedings | 2,419 | 5,941 | 102 | (1,245) | 7,217 |
| Labor proceedings | 4,031 | 2,311 | 897 | (160) | 7,079 |
| Legal fees | 6,513 | 995 | 158 | (977) | 6,689 |
| Other | <u>5,044</u> | <u>15,263</u> | <u>-</u> | <u>(11,520)</u> | <u>8,787</u> |
| | <u>59,186</u> | <u>24,916</u> | <u>6,206</u> | <u>(15,111)</u> | <u>75,197</u> |

The Bank has R\$ 1,512 (2015 - R\$ 1,990) recorded in "Other receivables - Debtors for deposits in guarantee" in connection with the filing of appeals for labor proceedings, as well as R\$ 1,783 (2015 - R\$ 1,678) for coverage of risks with civil proceedings.

Labor and civil proceedings whose likelihood of loss was considered as possible and for which no provision has been recorded totaled R\$ 712 (2015 - R\$ 1,058) and R\$ 990 (2015 - R\$ 6,757), respectively, at December 31, 2016.

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(ii) The provision for future payments relates to the following commitments:

| | <u>2016</u> | <u>2015</u> |
|---|---------------|---------------|
| Vacation pay, 13th month salary and other charges | 13,060 | 11,884 |
| Employees' profit sharing program (PLR) | 2,576 | - |
| Compliance with State Law 11,050/93 and the BDMG bylaws | 195 | - |
| Other | 601 | 673 |
| | <u>16,432</u> | <u>12,557</u> |

(iii) The balance of the provision for actuarial liabilities, which are detailed in Note 28, relates to the following benefits provided by the Bank:

| | <u>2016</u> | <u>2015</u> |
|--|----------------|----------------|
| Actuarial liability related to the Pension Plan | 134,401 | 101,508 |
| Actuarial liability related to the medical and dental assistance plan - Health Promotion Program (PRÓ-SAÚDE). | 132,457 | 103,815 |
| Actuarial liability related to the life insurance | 15,845 | 9,922 |
| Bank's voluntary employment termination program effective from December 2011 to December 2015. | - | - |
| | <u>282,703</u> | <u>215,245</u> |

(iv) The balance of the "Contribution for capital increase" account refers to the percentage on returns of the borrowings contracted with the Social and Economic Development Fund (FUNDESE) for capital increase applicable to the Program for Popular Credit (CREDPOP), in accordance with State Law 13,667/2000.

(v) The balance of Domestic sundry creditors is mainly related to customer credits to be offset, totaling R\$ 3,306 (2015 - R\$ 2,838).

(c) Financial and development funds

The amount of R\$ 70,146 (2015 - R\$ 13,839) substantially relates to resources from funds managed by BDMG (private funds and those of government agencies), which were received from customers and that are yet to be transferred to the funds.

15 Deferred income

The balance of R\$ 12,406 (2015 - R\$ 12,939) relates to the net amount of commissions on credit operations received in advance and which are allocated during the periods established in the related contracts.

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16 Equity

(a) Share capital

The subscribed capital of BDMG is represented by 64,211,466,636 (2015 - 60,854,432,385) registered common shares with no par value, totaling R\$ 1,844,396 (2015 - R\$ 1,793,685). This balance includes the capital increase of R\$ 100,000 as approved by stockholders during the Extraordinary General Meeting held on August 11, 2016, fully subscribed by the State of Minas Gerais (a stockholder), which paid up, on that occasion, R\$ 50,000 and will pay the remaining balance up to August 2017.

At December 31, 2016, the Bank's stockholders were: (i) the State of Minas Gerais, which holds 90.29% of the Bank's share capital and, thus, is the controlling stockholder; (ii) Companhia de Desenvolvimento Econômico de Minas Gerais - CODEMIG, with 8.80% and which became a stockholder as from the last quarter of 2012; (iii) MGI - Minas Gerais Participações, which holds 0.90% and became a stockholder as from June 2016, through the acquisition of a portion of shares of CODEMIG; and (iv) the State Highway Authority of Minas Gerais (DER-MG), with 0.01% and which is a stockholder since 1990, when the Bank changed from an autonomous government agency to a corporation.

(b) Revenue reserve

The revenue reserve comprises the legal reserve amounting to R\$ 8,051 (2015 - R\$ 6,692), calculated based on 5% of the profit of each year, up to the limit of 20% of capital; and (ii) special revenue reserve related to the remaining profit for the year amounting to R\$ 10,814 (2015 - loss of R\$ 31,329).

The loss of R\$ 31,329 for 2015 was fully absorbed via the legal reserve balance recorded at December 31, 2015, pursuant to Article 189, sole paragraph, of Law 6,404/76.

(c) Carrying value adjustments

The adjustments recorded are as follows:

| | <u>2016</u> | <u>2015</u> |
|---------------------------------------|------------------|------------------|
| Adjustments to market value (i) | (7,295) | (14,337) |
| Other carrying value adjustments (ii) | <u>(146,429)</u> | <u>(105,164)</u> |
| Total | <u>(153,724)</u> | <u>(119,501)</u> |

- (i) The adjustments to market value, net of tax effects, refers to the adjustments of the securities classified as available for sale.
- (ii) Other adjustments refer to the recognition of costs inherent to obligations with employee benefits, which, as established by CPC 33 (R1), "Employee Benefits", effective as from January 2013, must be adjusted in equity, net of tax effects.

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(d) Dividends and interest on capital

Stockholders are assured the payment of a minimum dividend of 1% of the profit for each year, adjusted in accordance with Brazilian Corporate Law and the Bank's bylaws.

Concerning the capital remuneration of its stockholders, BDMG distributes dividends or pays interest on capital according to the result for the year.

17 Capital management

In compliance with CMN Resolution 3,988/2011, the Bank issued internal regulations, Resolution 213 and Instruction 239, which define the necessary structure and policy for the management of the Bank's capital. These regulations define guidelines for ensuring the maintenance of adequate capital, without failing to meet the regulatory requirements established, so as to permit the Bank to meet the goals of its strategic planning, even in different scenarios.

The scenarios considered take into account possible changes in market conditions, the Bank's different operating and administrative activities and its economic environment, as well as the risks to which the Bank is exposed.

Following these regulations and taking into account the strategic planning definitions, the assumptions for the proposed scenarios and the projected results of operations, the Bank prepared its capital plan for the period from 2017 to 2019. The "BDMG's Capital Management Structure Description Report" is available at: <http://www.bdmg.mg.gov.br/Transparencia/Paginas/demonstracao-financeira.aspx>.

The capital management structure comprises the Director assigned as responsible for the capital management and the Financial Management, Capital, and Risks Committee, as well as the following units of the Bank: (i) General Controllership Management area, responsible for the preparation of the capital plan and calculation of the capital required to cover the credit and operating risks and the consolidation of information referring to indicators and minimum capital requirements; (ii) General Risk Management area, responsible for the calculation of the capital required to cover the market risks and the preparation of stress tests for market risk; (iii) General Planning Management area, responsible for describing the Bank's strategy; (iv) General Financial Management area, responsible for the significant information on the sources of capital; and (v) the General Audit area, which should periodically assess the capital management process of the Bank

The Director responsible for the capital management deals with the procedures and controls related to the capital management and is part of the Financial, Capital, and Risks Management Committee. This Committee is responsible for assessing the main assumptions that may affect the capital plan and for suggesting changes in order to reach the desirable minimum capital levels and the respective indicators.

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18 Regulatory capital

The rules for measuring the regulatory capital determine the requirement for financial institutions to maintain equity compatible with the risk level of their assets, according to exposure-weighting factors, risk mitigation factors, and credit factors.

CMN Resolution 4,192/2013 and a new set of rules regulated in Brazil, as from 10/1/2013, the recommendations of the Basel Committee on Banking Supervision (BCBS) regarding the capital structure of financial institutions, known as Basel III. This new framework introduced the calculation methodology for the regulatory capital and for the capital maintenance requirement with minimum requirements regarding PR, Level-I PR and main capital.

The calculation of the Bank's capital ratios and regulatory capital is as follows:

| | <u>2016</u> | <u>2015</u> |
|--|------------------|------------------|
| Equity | 1,709,537 | 1,680,876 |
| Reference equity - level I or Main capital (CP) (a) | 1,704,325 | 1,678,671 |
| Capital for operations with public sector (b) | 700,000 | 700,000 |
| Reference equity (PR) (a-b) | 1,004,325 | 978,671 |
| Total risk weighted assets (RWA) | <u>6,768,722</u> | <u>6,492,994</u> |
| Credit risk (<i>RWAcpad</i>) | 5,762,076 | 5,582,321 |
| Market risk – (<i>RWAmpad</i>) | 569,890 | 494,516 |
| Operational risk (<i>RWAopad</i>) | 436,756 | 416,158 |
| Portion of capital for coverage of interest rate risk of the portfolio not subject to negotiation - (<i>RWA R_{BAN}</i>) | 30,020 | 30,383 |
| Minimum reference equity | 783,041 | 815,577 |
| Basel Index (PR/RWA) | 14.8% | 15.1% |
| Extended Basel Index (PR/(RWA + <i>RWA R_{BAN}</i>)) | 14.2% | 14.5% |

19 Income from credit operations

| | <u>2016</u> | <u>2015</u> |
|-------------------|--------------------------------|----------------|
| | <u>Second six-month period</u> | <u>Year</u> |
| | <u>Year</u> | <u>Year</u> |
| Income from loans | 336,001 | 675,046 |
| Credits recovered | 37,599 | 46,807 |
| | <u>373,600</u> | <u>721,853</u> |
| | <u>652,585</u> | <u>652,585</u> |

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20 Gains (losses) on marketable securities and derivative financial instruments and expenses on financial intermediation

(a) Result from marketable securities transactions and derivative financial instruments

| | 2016 | | 2015 | |
|--|-------------------------|-----------|------|---------|
| | Second six-month period | Year | Year | Year |
| Income from fixed-income securities | 54,411 | 101,224 | | 84,907 |
| Income from investments in repurchase transactions | 17,427 | 39,094 | | 27,372 |
| Income from investments in investment funds | (385) | (1,156) | | (431) |
| Interest on interbank deposits | 617 | 617 | | 1,981 |
| Results from swap transactions | (6,311) | (163,234) | | 131,291 |
| Other | - | - | | 86 |
| | 65,759 | (23,455) | | 245,206 |

(b) Expenses with financial intermediation

| | 2016 | | 2015 | |
|---|-------------------------|-----------|------|-----------|
| | Second six-month period | Year | Year | Year |
| Financial bill expenses | (34,996) | (81,673) | | (107,024) |
| Onlending expenses - BNDES/FINAME | (138,299) | (254,798) | | (189,026) |
| Onlending expenses - Other institutions | (10,752) | (14,187) | | (3,838) |
| Foreign borrowing expenses | (41,358) | (83,806) | | (318,864) |
| Interbank deposit and repurchase operation expenses | (1,138) | (7,790) | | (9,828) |
| | (226,543) | (442,254) | | (628,580) |

21 Gross income from financial intermediation after the reclassifications

Gross income from financial intermediation as stated in the statement of operations is prepared in compliance with BACEN normative guidelines related to the composition of income and expenses that comprise such result.

The following amounts, which result from financial intermediation transactions, are not considered in this composition:

- Receivables disclosed in debt accounts and that result from the recording of the foreign exchange variation on liability transactions with a foreign exchange adjustment clause (the balances are reclassified to other operating income, as established by Circular Letter 3105/2003);
- Payables disclosed in credit accounts and that result from the recording of the foreign exchange variation on asset transactions with a foreign exchange adjustment clause (the balances are reclassified to other operating income, as established by Circular Letter 3105/2003);

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- Income from adjustment to market value of hedged foreign borrowings that, due to the lack of a specific account, is accounted for in other operating income, when the contrary is applicable to expenses of the same nature, which are recorded in the specific borrowing and onlending expense account.

The balances of foreign exchange income and expenses reclassified to other operating income and to other operating expenses and from the income from adjustment to market value of the hedge object that were not disclosed in the gross income from financial intermediation presented in the statement of operations in the year were as follows:

| | <u>2nd half of 2016</u> | <u>12/31/2016</u> | <u>12/31/2015</u> |
|--|-------------------------|-------------------|-------------------|
| Other operating income | 12,627 | 189,889 | 79,823 |
| - Foreign exchange variation of borrowings and onlending | 6,619 | 152,249 | 3,435 |
| - Adjustment to market value of hedged items | 6,008 | 37,640 | 76,388 |
| Other operating expenses | (2,262) | (20,677) | (3,720) |
| - Foreign exchange variation of loan transactions | (2,262) | (20,677) | (3,720) |

The reclassified gross income from financial intermediation is as follows:

| | <u>Second half of 2016</u> | | |
|--|----------------------------|--------------------------|---------------------|
| | <u>Original balance</u> | <u>Reclassifications</u> | <u>Reclassified</u> |
| Revenues from financial intermediation | 439,359 | (2,262) | 437,097 |
| - Credit operations | 373,600 | (2,262) | 371,338 |
| - Gains on transactions with marketable securities | 72,070 | | 72,070 |
| - Gains (losses) on derivative financial instruments | (6,311) | | (6,311) |
| Financial intermediation expenses | (323,910) | 12,627 | (311,283) |
| - Funds obtained in the market | (36,134) | | (36,134) |
| - Borrowings and onlendings | (190,409) | 12,627 | (177,782) |
| - Foreign exchange transactions | 8 | | 8 |
| - Provision for impairment of receivables | (97,375) | | (97,375) |
| Gross income from financial intermediation after the reclassifications | <u>115,449</u> | <u>10,365</u> | <u>125,814</u> |
| | | | <u>12/31/2016</u> |
| | <u>Original balance</u> | <u>Reclassifications</u> | <u>Reclassified</u> |
| Revenues from financial intermediation | 698,398 | (20,677) | 677,721 |
| - Credit operations | 721,853 | (20,677) | 701,176 |
| - Gains on transactions with marketable securities | 139,779 | | 139,779 |
| - Gains (losses) on derivative financial instruments | (163,234) | | (163,234) |
| Financial intermediation expenses | (615,315) | 189,889 | (425,426) |
| - Funds obtained in the market | (89,463) | | (89,463) |
| - Borrowings and onlendings | (352,791) | 189,889 | (162,902) |
| - Foreign exchange transactions | (255) | | (255) |
| - Provision for impairment of receivables | (172,806) | | (172,806) |
| Gross income from financial intermediation after the reclassifications | <u>83,083</u> | <u>169,212</u> | <u>252,295</u> |

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| | <u>12/31/2015</u> | | |
|--|--------------------------------|--------------------------|---------------------|
| | <u>Original balance</u> | <u>Reclassifications</u> | <u>Reclassified</u> |
| Revenues from financial intermediation | 897,791 | (3,720) | 894,071 |
| - Loan transactions | 652,585 | (3,720) | 648,865 |
| - Gains on transactions with marketable securities | 113,915 | | 113,915 |
| - Gains on derivative financial instruments | 131,291 | | 131,291 |
| Financial intermediation expenses | (881,554) | 79,823 | (801,731) |
| - Funds obtained in the market | (116,852) | | (116,852) |
| - Borrowings and onlendings | (511,728) | 79,823 | (431,905) |
| - Foreign exchange transactions | 32,905 | | 32,905 |
| - Provision for impairment of receivables | (285,879) | | (285,879) |
| Gross income from financial intermediation after the reclassifications | <u>16,237</u> | <u>76,103</u> | <u>92,340</u> |
| 22 Other administrative expenses, tax expenses, other operating income and other operating expenses | | | |
| (a) Other administrative expenses | | 2016 | 2015 |
| | Second six-month period | Year | Year |
| Outsourced services and specialized personnel | (7,479) | (13,174) | (14,309) |
| Advertising and communication | (2,184) | (3,989) | (4,218) |
| Data processing | (1,596) | (3,089) | (3,715) |
| Depreciation and amortization | (2,204) | (4,139) | (3,502) |
| Maintenance and material | (1,540) | (2,922) | (3,029) |
| Travel and transportation | (960) | (2,171) | (2,308) |
| Rental and infrastructure | (612) | (1,268) | (1,318) |
| Other | (2,487) | (4,723) | (5,052) |
| | <u>(19,062)</u> | <u>(35,475)</u> | <u>(37,451)</u> |
| (b) Tax expenses | | 2016 | 2015 |
| | Second six-month period | Year | Year |
| PIS and COFINS | (9,715) | (19,616) | (26,129) |
| Services Tax (ISSQN) | (1,063) | (2,018) | (1,964) |
| Other | (101) | (1,236) | (1,701) |
| | <u>(10,879)</u> | <u>(22,870)</u> | <u>(29,794)</u> |

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(c) Other operating income

| | 2016 | | 2015 | |
|--|-------------|---------|------|--------|
| | Second half | Year | Year | Year |
| Foreign exchange variation gains | 6,619 | 152,249 | | 3,435 |
| Reversal of sundry provisions | 9,798 | 10,907 | | 5,841 |
| Gain from adjustment to market value of hedged items | 6,008 | 37,640 | | 76,388 |
| Equity in results of investees | - | - | | 180 |
| Other | 2,110 | 3,089 | | 5,109 |
| | 24,535 | 203,885 | | 90,953 |

(d) Other operating expenses

| | 2016 | | 2015 | |
|---|-------------|-----------|------|----------|
| | Second half | Year | Year | Year |
| Provisions for co-obligations in rural operations | (64) | (220) | | (3,223) |
| Provision for tax, labor and civil risks | (12,952) | (20,918) | | (12,640) |
| Expense with the INDI agreement | (1,269) | (2,726) | | (2,643) |
| Post-employment benefit - pension plan | (7,561) | (12,628) | | (8,723) |
| Post-employment benefit - health insurance and life insurance | (6,007) | (12,564) | | (11,609) |
| Other long-term benefits | (214) | (422) | | (104) |
| Expense with BDMG Cultural agreement | - | (772) | | (2,528) |
| Exchange variation | (2,262) | (20,678) | | (3,720) |
| Expense with bonus and discount on credit operations | (3,879) | (7,215) | | (6,295) |
| Expenses with discounts granted on renegotiation | (1,825) | (4,040) | | (2,585) |
| Expenses with guarantees provided | (5,052) | (12,065) | | (1,785) |
| Fees/commissions on foreign borrowings | (381) | (2,120) | | - |
| Other | (3,847) | (6,227) | | (6,915) |
| | (45,313) | (102,595) | | (62,770) |

23 Income tax and social contribution

(a) Deferred income tax and social contribution

Deferred tax credits are as follows:

| | 2016 | | 2015 | |
|--|------|---------|------|---------|
| Temporary additions (i) | | 382,263 | | 349,685 |
| Adjustment to market value (marketable securities) | | 5,993 | | 12,216 |
| PIS/COFINS credits | | 9 | | 320 |
| Total | | 388,265 | | 362,221 |

- (i) Because of Provisional Measure 675/2015, converted into Law 13,169/2015, which increased the rate of CSLL from 15% to 20% during the period from September 1, 2015 to December 31, 2018, it was necessary to adjust the amounts accounted for as CSLL tax credit in 2015.

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However, since the increase will be effective only during an established period of time, the rate increase of 5% was not accounted for on the total temporary differences for the period, but only on the balance to be realized, as projected up to December 31, 2018.

The tax credits from temporary additions as related to the provisions from which they resulted is as follows:

| | <u>2016</u> | <u>2015</u> |
|---|-----------------------|-----------------------|
| Impairment of receivables | 228,400 | 215,587 |
| COFINS - (change in the calculation basis of Law 9,718/1998) | 39,717 | 37,052 |
| Compulsory deposit with BACEN (financial charges on the deposit) | 16,426 | 14,406 |
| Civil, labor and tax contingencies | 9,438 | 6,385 |
| Change in the calculation basis of PIS/PASEP as established by Law 9,718/1998 | 10,203 | 10,203 |
| Post-employment benefits | 70,302 | 59,234 |
| Co-obligation with STN | 1,774 | 2,120 |
| Other | <u>6,003</u> | <u>4,698</u> |
| Total | <u><u>382,263</u></u> | <u><u>349,685</u></u> |

The changes in the tax credits during the period were as follows:

| | <u>Adjustments to market value</u> | <u>Temporary additions</u> | <u>PIS/COFINS credits</u> | <u>Total</u> |
|---------------|--|--------------------------------|-------------------------------|-----------------------|
| At 12/31/2015 | 12,216 | 349,685 | 320 | 362,221 |
| Recorded | - | 177,361 | - | 177,361 |
| Reversed | <u>(6,223)</u> | <u>(144,783)</u> | <u>(311)</u> | <u>(151,317)</u> |
| At 12/31/2016 | <u><u>5,993</u></u> | <u><u>382,263</u></u> | <u><u>9</u></u> | <u><u>388,265</u></u> |

The tax credits of BDMG recorded in conformity with CMN Resolution 3,059/2002 (as changed by Resolution 3,355/2007) consider the expected realization within 10 years, based on the taxable profit presented in the projections of results. These projections are subject to changes, since they are estimated using internal assumptions and future economic scenarios.

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The table below presents the probable recovery of the tax credits arising from temporary additions:

| | <u>Nominal value</u> | <u>Present value</u> |
|-------|--------------------------|--------------------------|
| Year: | | |
| 2017 | 74,886 | 69,704 |
| 2018 | 102,889 | 83,781 |
| 2019 | 85,733 | 61,071 |
| 2020 | 27,932 | 17,406 |
| 2021 | 25,595 | 13,953 |
| 2022 | 29,104 | 13,880 |
| 2023 | 11,258 | 4,697 |
| 2024 | 9,172 | 3,347 |
| 2025 | 7,971 | 2,545 |
| 2026 | <u>7,723</u> | <u>2,157</u> |
| Total | <u><u>382,263</u></u> | <u><u>272,541</u></u> |

The present value of the tax credits was obtained by discounting the future flow of realization at the average rate of the funding for onlending contracted by BDMG of 14.31 % p.a. (2015 – 14.56% p.a.).

At December 31, 2016, the Bank had remaining balances of tax credits from temporary differences of income tax and social contribution amounting to R\$ 27,912 (2015 - R\$ 18,474) and R\$ 16,747 (2015 - R\$ 11,084), respectively. These amounts are not accounted for because their estimated realization exceeds 10 years.

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(b) Reconciliation of income tax and social contribution recorded in the statement of operations

| | 2016 | | 2015 | |
|---|-------------|---------------------|-----------------|---------------------|
| | Second half | Year | Year (restated) | Year (restated) |
| | Income tax | Social contribution | Income tax | Social contribution |
| Profit before taxation | | | | |
| Interest on capital | 27,009 | 27,009 | 54,370 | 54,370 |
| Additions (deductions), net | (15,000) | (15,000) | (15,000) | (15,000) |
| Recording of provision for contingencies, net of reversals | 11,459 | 11,459 | 19,827 | 19,827 |
| Taxes with suspended payment | - | - | 12 | 12 |
| Recording of provision for impairment of receivables and recovery of credits written-off as losses, net | 62,514 | 62,514 | 130,133 | 130,133 |
| Effective credit losses | (16,545) | (16,545) | (91,433) | (91,433) |
| Recording of provision for post-employment benefits, net of reversals | 11,501 | 11,501 | 20,704 | 20,704 |
| Statutory profit sharing | (4,067) | (4,067) | (4,067) | (4,067) |
| Equity in the results of the subsidiary | (43) | (43) | (19) | (19) |
| Foreign exchange losses - accrual basis (i) | - | - | - | - |
| Other | 1,222 | 1,070 | 1,698 | 1,409 |
| Calculation basis | | | | |
| Tax, according to the standard rate | 78,050 | 77,898 | 116,225 | 115,936 |
| Additional income tax | (11,708) | (15,580) | (17,434) | (23,187) |
| Tax incentives | (7,793) | - | (11,599) | (13,698) |
| | 1,550 | - | 2,001 | 2,527 |
| Subtotal of income tax and social contribution payable | (17,951) | (15,580) | (27,032) | (23,187) |
| Provision for deferred taxes | - | - | - | 6,196 |
| Adjustment of amounts payable in prior years | - | - | - | (4,079) |
| Total of the provision for income tax and social contribution payable | (17,951) | (15,580) | (27,032) | (23,187) |
| Recording of deferred tax credits (net of reversals) on temporary differences | 18,223 | 9,062 | 18,609 | 8,480 |
| Income tax and social contribution in the statement of operations | 272 | (6,518) | (8,423) | (14,707) |
| | | | | 25,887 |
| | | | | 34,481 |

- (i) In 2016, the Bank considered the foreign exchange variations on the credit rights and obligations, on the calculation basis of federal taxes, under the accrual basis, in accordance with Article 30 of the Provisional Measure 2,158-35, dated August 24, 2001. For this reason, there are no additions/deductions of foreign exchange expense/income on the calculation of income tax and social contribution on net income for the current year.

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24 Related parties

The Bank carried out the following transactions with related parties during the year:

Legal entities

State of Minas Gerais and companies controlled both directly and indirectly:

- State of Minas Gerais - rendering of services acting as financial agent of the state funds. The commission received by the Bank is included in the financial charges on the loan contracts granted with the fund resources.
- Fundação João Pinheiro, a public institution linked to the Planning and Management State Secretariat. As established in its bylaws, and in accordance with the State Law 11,050/1993, the Bank is authorized to donate 5% of its profit for the year to the Foundation.

BDMG maintains, with cost, an employee assigned to the Foundation. The Bank's expenses with this assignment was R\$ 238 in the year (2015 - R\$ 108).

- (a) Institute of Integrated Development of Minas Gerais (INDI), a not-for-profit, private limited liability entity linked to the Economic Development State Secretariat and an associated company of the Bank. The effective State Law 22,287, of September 14, 2016, increased from 25% to 50% the Bank's interest in INDI as quotaholder. However, an agreement was made to maintain, for 2016, the condition of the Bank as the sponsor-partner of the company, with 25% of the capital quotas. This commitment is met through the assignment of employees and additional financial contributions. In 2016, the Bank's expenses with INDI totaled R\$ 2,725 (2015 - R\$ 2,643).
- (b) BDMGTEC Participações S.A., a wholly-owned subsidiary established by the Bank in 2012, whose purpose is to invest in companies with significant interest for the development of the State of Minas Gerais. At December 31, 2016, BDMGTEC's capital was R\$ 85,158 (2015 - R\$ 77,658). The Bank subscribed in the year a capital increase of the company amounting to R\$ 7,500 and paid up R\$ 6,100, with the remaining R\$ 1,400 to be paid.
- (c) BDMG Social Security Foundation (DESBAN), a not-for-profit supplementary pension plan entity sponsored by BDMG. As detailed in Note 28, BDMG made contributions to this Foundation to provide for social security and health benefits of its employees. The Bank assigned employees to work for DESBAN, the latter being responsible for the costs related to these employees;
- (d) The Banco de Desenvolvimento de Minas Gerais Cultural Institute (BDMG Cultural), a not-for-profit civil association, was established by BDMG together with the BDMG Employees Association (AFBDMG) as a space for the fostering of culture in the State of Minas Gerais. The Bank contributed to the maintenance of BDMG Cultural by assigning employees without charging the Institute, in addition to making contributions in 2016, which, in the first quarter, totaled R\$ 772 (2015 - R\$ 2,527).

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Individuals

The individuals who are related parties of the Bank are the key management represented by its Board of Directors, Executive Board and Managing Board who received the following compensation in the year:

| | <u>2016</u> | <u>2015</u> |
|---|--------------|--------------|
| Remuneration (including social charges and benefits) | 4,215 | 3,923 |
| Profit sharing | - | 43 |
| Contributions to the pension plans - post-employment benefits | 35 | 37 |
| Employment contract termination | | |
| Total | <u>4,250</u> | <u>4,003</u> |

25 Insurance (not audited)

In order to cover possible damages to its property and equipment, the Bank has insurance cover amounting to R\$ 51,700 (2015 - R\$ 62,250).

26 Risk management

Financial risk management policy

The Risk Management Policy, which is approved by the Senior Management, stipulates limits and guidelines to identify, measure, assess, monitoring, report, control, and mitigate the Bank's risks. The policy seeks to adopt methodologies and internal models consistent with the Basel Accords and to meet the guidelines of the Regulators, in accordance with the best practices of risk management.

The Bank's Risk Management focus on credit, market, liquidity, operating, and socio-environmental risks to optimize the operating effectiveness and the results. Accordingly, the Bank adopts risk management practices appropriate for the nature and specificities of the operations that it conducts.

The Bank adopted the credit, operating, market, liquidity, and socio-environmental risk management structure in compliance with CMN Resolutions 3,721 (April 30, 2012), 3,380 (June 29, 2006), 3,464 (June 26, 2007), 4,120 (May 24, 2012), and 4,327 (April 25, 2014), respectively.

The risk management structure involves the whole Bank and is organized as follows: Board of Directors, Audit Committee, Internal Audit, External (Independent) Audit, Executive Board, Risk and Corporate Management Board, General Risk Management (market, liquidity, credit, and socio-environmental risks and prevention of external fraud related to credit granting), Internal Control Management (operating risk, compliance, internal controls, prevention and fight against money laundering and financing terrorism and management of regulations), and other units (primary responsibility related to operating risks and implemented controls).

The descriptions of the management structures for these risks, as well as other information on management, are available at the BDMG website (<http://www.bdmg.mg.gov.br>).

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Operating risk

The operating and conformity risk management policy, pursuant to CMN Resolution 3,380/2006, establishes roles, responsibilities and a methodology for the managing such risks for the Bank, involving qualitative and quantitative analysis as well as monitoring.

Credit risk

The credit risk management policy establishes credit risk exposure limits per customer, economic group and credit portfolio quality monitoring, in addition to decision levels, credit analysis and monitoring criteria, seeking selectivity of the operations with the purpose of minimizing cases of default and the related consequences.

Liquidity risk

The liquidity risk management policy establishes roles and responsibilities, exposure limits and reporting levels with the purpose of preparing the Bank to support adverse scenarios, considering different time frames. It deals with the activation of the contingency plan, which includes the set of strategies and measures to be taken, with the purpose of recovering the limits established. This policy also establishes the monitoring of the action plans defined and the reporting of the results to the Senior Management.

Market risk

The Market Risk Management Policy establishes roles and responsibilities, operating limits, and reporting levels, as well as the means to minimize the effects of such risk on the Bank's financial statements, cash flows, and adjustment to the risk exposure limits.

Socio-environmental risk

The Socio-environmental risk policy establishes roles, responsibilities, own methodology for identification and assessment of socio-environmental risk, and criteria for analysis and monitoring of transactions.

27 Management of development funds (unaudited)

The Bank maintains a structure for the management of development funds. The balances related to the fund equities were as follows:

| | <u>2016</u> | <u>2015</u> |
|---------------|------------------|------------------|
| State funds | 3,780,328 | 3,733,278 |
| Private funds | 290 | 290 |
| Other funds | <u>60,706</u> | <u>32,706</u> |
| | <u>3,841,324</u> | <u>3,766,274</u> |

28 Employee benefits

As mentioned in Note 2.16, the Bank grants the following post-employment benefits to its employees: pension, healthcare and dental assistance, life insurance, and, before January 2016, voluntary employment termination benefits.

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The accounting for these benefits is in accordance with CPC 33 (R1), "Employee Benefits", which requires that an actuarial study be prepared as the basis for recording these obligations. The currently effective actuarial study was prepared for the base date December 31, 2016.

(a) Characteristics of the benefit plans

(i) Pension plans

BDMG is the sponsor of defined benefit and variable contribution pension plans, which are managed by BDMG Social Security Foundation (DESBAN), a not-for-profit supplementary pension plan entity. The purpose of both plans is to provide participating employees and their beneficiaries with a retirement income in addition to that paid by the Social Security General Regime (RGPS).

Defined benefit pension plan

The defined benefit pension plan, which has been closed to new participations since November 10, 2011, is based on a capitalization financial regime for the calculation and accrual of its reserves, which result from the participant's and sponsor's contributions. The sponsor's contributions is limited to the total of normal participant's contributions, taking into account the particularities of each plan, in conformity with the contributive parity determined in Constitutional Amendment 20/1998. Regarding this plan, it is also necessary to comply with Article 29 of the Board for Management of Supplementary Pension Funds (CGPC) No. 26, of September 29, 2008, which establishes the mandatory equation of the plan's deficit between the participants (active, assisted, and pensioners) and sponsors, taking into account the proportion of the normal contributions made in the year when the deficit occurs.

BDMG's defined benefit plan in 2015 had the following technical deficit to be subject to equation:

| | <u>Equation in 2015 - Desban</u> | <u>Equation in 2016 - Sponsor (*)</u> |
|-----------------------|--------------------------------------|---|
| Equation | R\$ 28,135.4 | R\$ 31,844.6 |
| Amount - sponsor | R\$ 14,067.7 | R\$ 15,922.3 |
| Amount - participants | R\$ 14,067.7 | R\$ 15,922.3 |
| Equation period | 20 years | 20 years |

(*) Equated amount defined according to the flow of liability discounted at present value, in accordance with the assumptions defined in BDMG's actuarial assessment of December 2016. The Bank, when considering the best estimate to be adopted for the accounting of the deficit equated amount, considered the legal and normative matters that are necessary for the calculation of the actuarial accounting liability of public entities that sponsor complementary pension plans. Therefore, it was established for the equation the equitable apportionment between the participants (50%) and the sponsors (50%). The actuarial deficit portion for which the Bank, as a sponsor, is responsible, is recorded in the Bank's liabilities.

This condition was accepted by DESBAN's Executive Board, as registered in the minutes of the 282th meeting, held on December 27, 2016: "equitable apportionment between the participants (50%) and the sponsors (50%) will be considered not only for the current Equation Plan, but also for other occasional deficit equation plans that may be required in the future, provided the same legal and regulatory basis remain effective".

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Variable contribution plan

The variable contribution pension plan, created on January 13, 2011, consists of a defined contribution plan in the savings structuring stage, becoming a defined benefit structure through the guarantee of a lifetime monthly income after concession.

The contribution of the Bank to this plan also is limited to the sum of the normal contributions of the participants, in conformity with the contributive parity determined in Constitutional Amendment 20/1998.

The number of BDMG participants in the pension plans is as follows:

| | <u>2016</u> | <u>2015</u> |
|--|-------------------|-------------------|
| Plans: | | |
| Defined benefit (BD) - Active participants | 246 | 250 |
| Defined benefit (BD) - Retirees | 525 | 525 |
| Variable contribution (CV) - Active participants | <u>73</u> | <u>75</u> |
| Total | <u><u>844</u></u> | <u><u>850</u></u> |

(ii) Health care and dental assistance benefit

DESBAN manages the Pró-Saúde Program (Health Promotion Program (PRÓ-SAÚDE)), which offers coverage for healthcare and dental expenses for active participants and their dependents (Note 2.16), and operates under the capitalization regime. The Bank also provides this benefit to the retirees who enrolled in the plan as active employees up to October 10, 2009.

(iii) Life insurance

BDMG sponsors a voluntary group life insurance for active employees and retirees. The Bank's contribution is equivalent to 50% of the premium paid.

(iv) Voluntary employment termination program

This Program, established by the Bank on December 14, 2011 and terminated on January 29, 2016, aimed to benefit employees who elected for retirement and who met the Program's requirements.

(b) BDMG's benefit plan commitments

In compliance with its benefit plan commitments, BDMG made the following contributions both for active employees and beneficiaries:

| | <u>2016</u> | <u>2015</u> |
|--|----------------------|----------------------|
| Pension Benefit Plan - (BD) | 9,874 | 9,023 |
| Pension Benefit Plan - (CV) | 523 | 469 |
| Healthcare Promotion Program- PRÓ-SAÚDE | 5,526 | 4,599 |
| Group life insurance | 914 | 919 |
| Voluntary employment termination program | <u>1,527</u> | <u>1,527</u> |
| Total | <u><u>16,837</u></u> | <u><u>16,537</u></u> |

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All amounts in thousands of reais unless otherwise stated

(i) Changes in the present value of the defined benefit obligation

At December 31, 2016, the net amounts of the obligations with the defined benefit plans, in accordance with CPC 33 (R1), resulted from the following changes in the period:

| | Social security benefit plan - DB | Health Promotion Program - PRO- SAÚDE | Group Life Insurance | Termination Program | Total |
|---|--------------------------------------|---|-------------------------|------------------------|-----------|
| Net (liability) at 12/31/2015 | (101,508) | (103,815) | (9,922) | - | (215,245) |
| Current service costs | (3,526) | (1,463) | (86) | | (5,075) |
| Interest costs, net | (15,066) | (12,890) | (1,176) | | (29,132) |
| Expected contributions to administrative expenses | - | (1,243) | - | | (1,243) |
| Sponsor contributions | 9,770 | 4,084 | 892 | | 14,746 |
| Remeasurements ⁽¹⁾ | | | | | - |
| Return on plan assets, excluding interest | 83,352 | 3,802 | | | 87,154 |
| Actuarial gain - Changes in assumptions (growth in salary and turnover) | 785 | | (71) | | 714 |
| Actuarial (loss) - Changes in assumptions (discount rate) | (150,373) | (29,448) | (1,669) | | (181,490) |
| Actuarial (loss) - Changes in assumptions (biometric tables) | | | | | - |
| Actuarial gain / (loss) - Experience adjustments | (19,802) | 8,517 | (3,813) | | (15,098) |
| Extraordinary contributions (active and assisted) | 15,922 | | | | 15,922 |
| Net (liability) at 12/31/2016 | (180,446) | (132,456) | (15,845) | - | (328,747) |
| Portion of participants in the surplus/deficit | 46,044 | | | | 46,044 |
| Net (liability) at 12/31/2016 ⁽¹⁾ | (134,402) | (132,456) | (15,845) | - | (282,703) |

(1) It refers to the portion of the sponsor's actuarial responsibility after the calculation of the effect of the sharing of risks between active and assisted participants.

The Social Security Benefit Plan's net liabilities for the defined benefit category in December 2016 were as follows:

Social security benefit plan - DB

| | |
|---|-----------|
| Sponsor's portion with future contributions | (72,435) |
| Sponsor's portion with equated deficit - 2015 | (15,922) |
| Sponsor's portion in the surplus/deficit | (46,044) |
| Net (liability) at 12/31/2016 ⁽¹⁾ | (134,402) |

(1) It refers to the portion of the sponsor's actuarial responsibility after the calculation of the effect of the sharing of risks between active and assisted participants.

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All amounts in thousands of reais unless otherwise stated

| | Social security benefit plan - DB | Health Promotion Program - PRO- SAÚDE | Group Life Insurance | Termination Program | Total |
|--|--------------------------------------|---|-------------------------|------------------------|-----------|
| Net (liability) at 12/31/2014 | (93,707) | (99,439) | (11,138) | (1,253) | (205,537) |
| Current service cost | (4,234) | (1,110) | (93) | (9) | (5,446) |
| Interest costs, net | (10,841) | (11,197) | (1,230) | | (23,268) |
| Past service cost | | | | (199) | (199) |
| Expected contributions to administrative expenses | | (1,823) | | | (1,823) |
| Sponsor contributions | 8,972 | 3,394 | 909 | 1,527 | 14,802 |
| Remeasurements (*) | | | | | |
| Return on plan assets, excluding interest | (58,359) | (781) | | | (59,140) |
| Actuarial gain - Changes in assumptions (growth in salary and turnover) | 5,556 | | 38 | | 5,594 |
| Actuarial gain - Changes in assumptions (discount rate) | 98,778 | 20,439 | 1,077 | | 120,294 |
| Actuarial (loss) - Changes in assumptions (biometric tables) | (14,368) | (4,352) | (241) | | (18,961) |
| Actuarial gain / (loss) - Experience adjustments | (33,305) | (8,946) | 756 | (66) | (41,561) |
| Net (liability) at 12/31/2015 | (101,508) | (103,815) | (9,922) | - | (215,245) |

(*) The remeasurements in employee benefit obligations are recorded in Other carrying value adjustments in equity, as disclosed in Note 16 (c) (ii).

(ii) Amounts recorded in the statement of operations

The expenses with the defined benefit plans are detailed below:

| | 2016 | | | | |
|--|---------------------------------|---|-------------------------|--------------------------------------|----------|
| | Pension benefit plan - DB | Healthcare Promotion Program - PRO-SAÚDE | Group life insurance | Employment termination program | Total |
| Current service cost | (3,526) | (1,463) | (86) | | (5,075) |
| Interest costs, net | (15,066) | (12,890) | (1,176) | | (29,132) |
| Expected contributions to administrative expenses | - | (1,243) | - | | (1,243) |
| (Expense) recognized in the statement of operations (*) | (18,592) | (15,596) | (1,262) | - | (35,450) |

Banco de Desenvolvimento de Minas Gerais S.A. - BDMG

Notes to the financial statements at December 31, 2016

All amounts in thousands of reais unless otherwise stated

2015

| | Pension benefit plan - DB | Healthcare Promotion Program - PRO-SAÚDE | Group life insurance | Employment termination program | Total |
|--|------------------------------|---|-------------------------|--------------------------------------|-----------------|
| Current service costs | (4,234) | (1,110) | (93) | (9) | (5,446) |
| Interest costs, net | (10,841) | (11,197) | (1,230) | | (23,268) |
| Past service cost | | | | (199) | (199) |
| Expected contributions to administrative expenses | | (1,823) | | | (1,823) |
| (Expense) recorded in the statement of operations (*) | <u>(15,075)</u> | <u>(14,130)</u> | <u>(1,323)</u> | <u>(208)</u> | <u>(30,736)</u> |

(i) The expenses were accounted for as follows: R\$ 10,258 (12/31/2015 - R\$ 10,404) in "Personnel" and R\$ 25,192 (12/31/2015 - R\$ 20,332) in "Other operating expenses".

The sponsor's monthly contributions for the Pension Benefit Plan - Variable Contribution in the period from January to December 2016 amounted to R\$ 523 (12/31/2015 - R\$ 469). These contributions are recognized monthly as personnel expenses.

(c) Actuarial studies

The actuarial liabilities were calculated by an independent actuary using the Projected Unit Credit method, and the studies prepared for December 31, 2016 are effective.

(i) Net amount recorded in the balance sheet

At 31 December, the net amounts of the obligations with the defined benefit plans, in accordance with CPC 33 (R1), were as follows:

2016

| | Pension benefit plan - DB | Healthcare Promotion Program - PRO-SAÚDE | Group life insurance | Employment termination program | Total |
|---|------------------------------|---|-------------------------|--------------------------------------|------------------|
| Defined benefit obligation | (1,016,272) | (155,096) | (15,845) | | (1,187,213) |
| Plan assets | 835,827 | 22,639 | | | 858,466 |
| Net actuarial liability | <u>(180,445)</u> | <u>(132,457)</u> | <u>(15,845)</u> | <u>-</u> | <u>(328,747)</u> |
| Sponsor's portion with future contributions | (72,435) | | | | (72,435) |
| Sponsor's portion with equated deficit - 2015 | (15,922) | | | | (15,922) |
| Sponsor's portion in the surplus/deficit | (46,044) | | | | (46,044) |
| Net (liability) at 12/31/2016 ⁽¹⁾ | <u>(134,401)</u> | <u>(132,457)</u> | <u>(15,845)</u> | <u>-</u> | <u>(282,703)</u> |

(1) It refers to the portion of the sponsor's actuarial responsibility after the calculation of the effect of the sharing of risks between active and assisted participants.

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| | 2015 | | | | |
|----------------------------------|--------------------------------------|---|---------------------------------|---|------------------|
| | Pension benefit plan - DB | Healthcare Promotion Program - PRO-SAÚDE | Group life insurance | Employment termination program | Total |
| Defined benefit obligation | (819,237) | (121,410) | (9,922) | | (950,569) |
| Assets of the plan | 717,729 | 17,595 | | | 735,324 |
| Net actuarial (liability) - 2015 | <u>(101,508)</u> | <u>(103,815)</u> | <u>(9,922)</u> | - | <u>(215,245)</u> |

(ii) Allocation of the fair value of plan assets

The plan assets at December 31, 2015 and December 31, 2016 are allocated into categories of assets as follows:

| | 2016 | | 2015 | |
|------------------------------|--------------------------------------|---|--------------------------------------|---|
| | Pension benefit plan - DB | Healthcare Promotion Program - PRO-SAÚDE | Pension benefit plan - DB | Healthcare Promotion Program - PRO-SAÚDE |
| Asset category: | | | | |
| Private Securities | 51.33% | 68.76% | 57.92% | 80.94% |
| Private credits and deposits | 3.45% | 16.15% | 2.85% | 9.09% |
| Linked investment funds | 0.00% | | 13.65% | |
| Shares and share funds | 3.73% | | 4.24% | |
| Real estate investments | 4.52% | | 5.74% | |
| Loans | 1.52% | | 1.71% | |
| Multimarket | 0.00% | | 1.04% | |
| Private equity funds | 5.16% | | 4.46% | |
| Fixed income | 18.85% | | 0.53% | |
| Other | 11.44% | 15.09% | 7.86% | 9.97% |

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All amounts in thousands of reais unless otherwise stated

(iii) Main assumptions used in the actuarial valuation

The actuarial studies presenting the obligations of BDMG in December 2016 and 2015 are based on the following assumptions:

| | 12/31/2016 | 12/31/2015 |
|--|---|---|
| Nominal discount rate for the actuarial liability | 10.528% | 12.59% |
| Expected annual nominal rate of return for investments | 10.528% | 12.59% |
| Estimated future annual inflation | 4.53% | 4.94% |
| Nominal rate of future salary growth: | | |
| BDMG (PCS) | 7.50% | 8.21% |
| BDMG (CC) | 5.02% | 6.38% |
| Annual real growth projection of medical expenses ⁽¹⁾ | 3.50% | 3.50% |
| Turnover: | | |
| Less than three years of service | | 7.31% |
| Over three years. | | 0.81% |
| After 39 years of age | 4.40% | |
| As from 39 years of age | 0.30% | |
| General Mortality Table | AT-2000 (Basic table reduced by 10%) - reduction of 10% and divided by gender. | AT-2000 (Basic table reduced by 10%) - reduction of 10% and divided by gender. |
| Disability Table | Álvaro Vindas - reduction of 70%. | Álvaro Vindas - reduction of 70%. |
| Disability Mortality Table | Winklevoss - reduction of 50%. | Winklevoss - reduction of 50%. |
| Composition of pensioners (families) | Active Employees: Standard family Beneficiary: Real family. | Active Employees: Standard family Beneficiary: Real family. |
| Life expectancy used in the definition of the social contribution factor applied in the calculation of state retirement benefit (in Brazil known as the "fator previdenciário"). | IBGE 2014 Table. | IBGE 2013 Table. |
| Other assumptions | All participants retire in the 1st eligibility - no salary growth for self-sponsored participants. | All participants retire in the 1st eligibility - no salary growth for self-sponsored participants. |
| Monetary restatement provision | Of salaries: 0.5208% (accumulated change in the Amplified Consumer Price Index (IPCA) of September to November 2016) - Base date for the readjustment - September. Of the benefits granted: 2.6377% (accumulated change in the IPCA of May to November 2016) - Base date for the readjustment - May. | Of salaries: 2.3882% (accumulated change in the Amplified Consumer Price Index (IPCA) of September to November 2015) - Base date for the readjustment - September. Of the benefits granted: 4.8354% (accumulated change in the IPCA of May to November 2015) - Base date for the readjustment - May. |

(1) Applicable only to healthcare assistance.

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(iv) Sensitivity of the defined benefit obligation

The changes in the assumptions on which the actuarial studies are based may have effects on the defined benefit obligation.

The following table presents the percentage of the increases in the defined benefit obligation arising from changes in the actuarial assumptions:

| | Changed assumptions | | | | | |
|--------------------------------------|--|--|--|--|---|---|
| | Increase of 0.5% p.a. in the discount rate | Decrease of 0.5% p.a. in the discount rate | Reduction of one year in the mortality table | Increase of 1% in the salary growth rate | Increase of 0.01% in the insurance premium rate | Increase of 1% in the medical cost trend rate |
| Pension benefit plan - DB | -5.20% | 5.90% | 2.00% | 1.40% | N/A | N/A |
| Health Promotion Program - PRO-SAÚDE | -7.00% | 7.90% | 3.60% | - | N/A | 28.30% |
| Group life insurance | -4.75% | 5.20% | 2.13% | - | 3.27% | N/A |
| Employment termination program | N/A | N/A | N/A | N/A | N/A | N/A |

(v) Projected cash flow

The actuarial studies made for December 2016 included the following estimates for the payment of benefits and contributions of the sponsor for 2016:

| | Pension benefit plan - DB | Pension benefit plan - CV | Healthcare Promotion Program - PRO-SAÚDE | Group life insurance | Employment termination program | Total |
|---------------------------------|---------------------------|---------------------------|--|----------------------|--------------------------------|--------|
| Expected benefit payments | 68,312 | | 7,058 | 1,154 | | 76,524 |
| Expected employer contributions | 11,574 | 544 | 4,419 | 1,154 | | 17,691 |

29 Events after the reporting period

In December 2016, BDMG's ratings were downgraded from BB- to B- (global scale) and from brA to brB- (Brazil scale). This resulted from the downgrade of the State of Minas Gerais, which is facing difficulties to settle its financial issues. This led to the breach of the covenants of the foreign funding contracts, as established during the initial act of the contract between the parties. Together with this, S&P Ratings confirmed BDMG's stand-alone credit profile (SACP) as "bb-", while making no changes to the Bank's standalone rating.

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Considering the covenant clauses related to the risk rating downgrade included in those contracts, after the downgrading, the Bank decided to settle in advance these contracts, which resulted in the suspension in December of the hedge accounting that had been used for these contracts. The Bank informed to the financial institutions affected by its decision that it will settle the contracts in advance in January 2017, because of the breach of the contractual covenant related to the downgrade of the risk rating.

Thus, in January 2017, the Bank settled in advance the foreign funding contracts held with Bank of Tokyo 1, BESI (purchased by Haitong Bank), Goldman (Goldman BID and Goldman CAF), and the derivative contracted used as hedge for this funding.

* * *

Board of Directors

| | |
|--------------------------------------|---------------|
| Helvécio Miranda Magalhães Júnior | Chairman |
| Marco Aurélio Crocco Afonso | Vice-chairman |
| Adézio de Almeida Lima | Member |
| Aluísio Eustáquio de Freitas Marques | Member |
| Ângelo Oswaldo de Araújo Santos | Member |
| Bernardo Gouthier Macedo | Member |
| César Cristiano de Lima | Member |

Executive Board

| | |
|---------------------------------|---------------|
| Marco Aurélio Crocco Afonso | Chairman |
| Luiz Guilherme Piva | Vice-chairman |
| Carolina Marinho do Vale Duarte | Director |
| Marcela Amorim Brant | Director |
| Rogério Sobreira Bezerra | Director |

Controllership Department

Giovani Rosemberg Ferreira Gomes - Accountant CRC-MG - 075701/O-5