

LABRADOR IRON ORE
ROYALTY CORPORATION

2017



**ANNUAL
REPORT**

80 YEARS IN LABRADOR WEST

■ Annual and Special Meeting

The Annual and Special Meeting of the holders of common shares of Labrador Iron Ore Royalty Corporation will be held:

Date Wednesday, May 16, 2018

Time 11:00 a.m.

Place Toronto Region Board of Trade
77 Adelaide Street West
First Canadian Place, Third Floor
Toronto, Ontario, Canada

The holders of common shares are encouraged to attend and those unable to do so should complete the Form of Proxy and forward it on or before May 15, 2018.

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Forward-Looking Statements

This report may contain "forward-looking" statements that involve risks, uncertainties and other factors that may cause the actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Words such as "may", "will", "expect", "believe", "plan", "intend", "should", "would", "anticipate" and other similar terminology are intended to identify forward-looking statements. These statements reflect current assumptions and expectations regarding future events and operating performance as of the date of this report. Forward-looking statements involve significant risks and uncertainties, should not be read as guarantees of future performance or results, and will not necessarily be accurate indications of whether or not such results will be achieved. A number of factors could cause actual results to vary significantly, including iron ore price and volume volatility, exchange rates, the performance of IOC, market conditions in the steel industry, mining risks and insurance, relationships with aboriginal groups, changes affecting IOC's customers, competition from other iron ore producers, estimates of reserves and resources and government regulation and taxation. A discussion of these factors is contained in LIORC's annual information form dated March 8, 2018 under the heading, "Risk Factors". Although the forward-looking statements contained in this report are based upon what management of LIORC believes are reasonable assumptions, LIORC cannot assure investors that actual results will be consistent with these forward-looking statements. These forward-looking statements are made as of the date of this report and LIORC assumes no obligation, except as required by law, to update any forward-looking statements to reflect new events or circumstances. This report should be viewed in conjunction with LIORC's other publicly available filings, copies of which can be obtained electronically on SEDAR at www.sedar.com.

■ Labrador Iron Ore Royalty Corporation

Labrador Iron Ore Royalty Corporation (“LIORC”), a Canadian corporation, owns interests in Iron Ore Company of Canada (“IOC”) which operates a major iron mine near Labrador City, Newfoundland and Labrador on lands leased from LIORC. Directly and through its wholly-owned subsidiary, Hollinger-Hanna Limited, LIORC owns a 15.10% equity interest in IOC and receives a 7% gross overriding royalty on all iron ore products produced from the leased lands, sold and shipped by IOC and a \$0.10 per tonne commission on sales of iron ore by IOC.

As at December 31, 2017, there were 64 million common shares issued and outstanding which are listed for trading on the Toronto Stock Exchange under the symbol LIF. Generally, LIORC pays cash dividends from its net income to the maximum extent possible, subject to the maintenance of appropriate levels of working capital. Currently, the holders of common shares receive quarterly dividends on the 25th day of the month following the end of each quarter. The common shares are qualified investments under the *Income Tax Act (Canada)* for deferred plans including registered retirement savings plans, registered retirement income funds and deferred profit sharing plans.

LIORC has a Board of eight Directors, an Audit Committee, a Compensation Committee and a Nominating Committee. Each Committee is composed of five independent Directors. Scotia Managed Companies Administration Inc., pursuant to an administration agreement, acts as the administrator of LIORC.

This information is prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”) and all amounts are shown in Canadian dollars unless otherwise indicated.



■ Shareholders' Investment Highlights

Years Ended December 31	2017	2016
	(\$ in millions except per share information)	
Revenue	158.6	115.1
Net Income	157.3	78.2
Cash Flow from Operations	167.0 ⁽¹⁾	63.5 ⁽²⁾
Net Income per Share	\$ 2.46	\$ 1.22
Cash Flow from Operations per Share	\$ 2.61 ⁽¹⁾	\$ 0.99 ⁽²⁾
Dividends Declared per Share	\$ 2.65	\$ 1.00

(1) Includes IOC dividends totaling \$76.7 million or \$1.20 per Share.

(2) Includes IOC dividend totaling \$15.1 million or \$0.23 per Share.

■ To the Holders of Common Shares of Labrador Iron Ore Royalty Corporation

The Directors of Labrador Iron Ore Royalty Corporation (“LIORC” or the “Corporation”) are pleased to present the Annual Report for the year ended December 31, 2017.

80 Years in Labrador West

Labrador Iron Ore Royalty Corporation has been involved in Labrador West for 80 years. Under a Statutory Agreement with Newfoundland made in 1938, a predecessor company, Labrador Mining and Exploration Limited, was granted extensive exploration and mining rights in Labrador West. LM&E found the iron ore bodies that now constitute the mine operated by Iron Ore Company of Canada. LM&E received grants of leases and licences under the Statutory Agreement. It also received a grant of surface rights to establish the town site that became Labrador City. LM&E sublet the leases to IOC and IOC, with major steel companies as original shareholders, built the infrastructure, mine, railway and port. Under the sublease, LIORC receives a 7% gross overriding royalty on iron ore products produced and sold by IOC.

Financial Performance

The Shareholders' cash flow from operations for the year ended December 31, 2017 was \$167.0 million or \$2.61 per share as compared to \$63.5 million or \$0.99 per share for 2016.

The Shareholders' consolidated net income for the year ended December 31, 2017 was \$157.3 million or \$2.46 per share compared to \$78.2 million or \$1.22 per share in 2016. Equity earnings from Iron Ore Company of Canada (“IOC”) amounted to \$74.3 million compared to \$24.7 million in 2016. LIORC received an IOC dividend in the fourth quarter of 2017 in the amount of \$19.3 million or \$0.30 per share compared to \$15.1 million or \$0.23 per share in the fourth quarter of 2016. IOC's 2017 iron ore sales for calculating the royalty to LIORC totaled 19.2 million tonnes compared to 18.2 million tonnes in 2016. Royalty revenue increased to \$156.4 million as compared to \$113.1 million in 2016.

The cash flow from operations, equity earnings and net income for the year were higher than last year mainly due to improved prices for concentrate, particularly in the first quarter of 2017, high premiums for concentrate and pellets, plus higher concentrate and pellet sales tonnages. Prices and premiums in 2017 were higher than most forecasts with the Chinese governments enacting and enforcing measures to reduce pollution; these measures favoured higher quality products such as the concentrate for sale (“CFS”) and pellets produced by IOC.

The average index price for 62% fines increased 22% year-on-year to US\$71 per tonne CFR China in 2017. The pellet premiums also increased year-on-year, particularly in the last few months of 2017, approaching approximately US\$60 per tonne in October and November. The average price realized by IOC for CFS and pellets, FOB Sept-Îles, was approximately C\$108 per tonne in 2017 compared to C\$80 per tonne in 2016, an increase of 35%. The higher premiums for 65% Fe concentrate and pellets were driven by the changes in environmental policy by the Chinese governments, which caused Chinese steel producers to increase the usage of higher value-in-use iron ore, such as the concentrate and pellets produced by IOC. With improving pellet premiums in 2017, IOC again focused on maximizing pellet production to the extent possible, given that two pellet lines were refurbished in 2017 with none in 2016. The sales tonnage of pellets in 2017, for calculating the royalty to LIORC, was 4% higher than in 2016. The CFS tonnages in 2017 were higher than in 2016 by 6%.

Iron Ore Company of Canada Operations Production

Total concentrate production of 20.2 million tonnes in 2017 was 5% higher as compared to 2016 of 19.2 million tonnes, but below the 22 million tonnes objective for 2017. In the fourth quarter of 2017, IOC experienced two site-wide power outages, weather conditions required the suspension of pit mining activities due to poor visibility, and the conveyor belt of the parallel ore delivery system split along several kilometers. The parallel ore delivery system was not operational for 21 days in December while repairs to the conveyor were undertaken. Quarterly concentrate production records were set in the first and third quarters of 2017 which drove the 5% improvement in concentrate production in 2017. Pellet production was 7% higher in 2017 as compared to 2016. While two pellet lines were down for several weeks for refurbishment, the annual pellet production improved with increased throughput being achieved in both lines once they returned to service.

REPORT TO SHAREHOLDERS

The cost per tonne of concentrate produced declined by 5% in 2017 as compared to 2016. The total cash cost in Canadian dollars was well controlled and increased by only 2.4%. The overall IOC employee productivity improved by 3% in 2017.

Sales as Reported for the LIORC Royalty

Total iron ore tonnage sold by IOC (CFS plus pellets) of 19.2 million tonnes was 5% above the total sales tonnage in 2016. The pellet sales tonnage was 4% higher and CFS sales tonnage was 6% higher than in 2016. The increase in the sales of both pellets and CFS was achieved despite the repair over a 34-day period in July and August on the dumper for the rail wagons that transport the iron ore products to the port at Sept Isles. IOC crews are to be commended for the dumper repair work and the reduction of the high concentrate inventories at Carol Lake at the end of the third quarter to normal levels by year end.

As noted above, pellet premiums were strong in 2017 and IOC maximized pellet production, while still meeting CFS sales commitments.

Capital Expenditures

Capital expenditure for IOC in 2017 was \$265 million in total as compared to \$99 million in 2016. The capital program for 2016 was set when the price outlook was poor and the expansion program had been largely completed. Therefore the capital budget was set for minimal sustaining capital. For 2017, the total capital budget was increased to \$245 million as the price outlook in December 2016 was much improved. The 2017 budget included some \$40 million as development capital for the Wabush 3 pit (total budget \$79 million in 2017 and 2018). The sustaining capital included the refurbishment of the No. 2 and 5 pellet lines, capital to improve air emissions from the pellet plant, the refurbishment of track and the remediation of high wall rock cuts along the route of the Quebec North Shore and Labrador Railway. The planned capital programs were executed largely on budget. In late 2017 IOC purchased some \$20 million of leased equipment to reduce future operating costs which added to the budget.

Outlook

Many forecasts for seaborne iron ore, 62% Fe, CFR China, are for the price to decline and average below US\$60 per tonne in 2018. Reportedly, the Office of the Chief Economist of Australia predicted in January 2018 that iron ore prices will average US\$53 per tonne (FOB Australia) in 2018, and US\$49 in 2019. Most forecasts note the anticipated increased supply, particularly from Vale's S11D mine in Brazil. It is also increasingly likely that the Samarco operation in Brazil could re-open in late 2018 or in 2019, which would likely adversely affect pellet premiums. However, some forecasts note the Chinese policies on pollution and the strong steel margins for Chinese producers as being supportive of iron ore prices and premiums for higher grade iron ore.

Rio Tinto has released guidance for 2018 of between 11.5 million to 12.5 million tonnes for their 58.7% share of IOC's saleable production (pellets and CFS tonnage). This would result in 19.6 million to 21.3 million tonnes of saleable production on a 100% basis. With the strong pellet premiums, IOC will continue to prioritize pellet production in 2018. The IOC objective is 22.2 million tonnes of concentrate production with sales of approximately 12.5 million tonnes of pellets and 8.4 million tonnes of CFS in 2018.

The capital expenditures for 2018 are expected to be \$220 million, lower than the \$265 million in 2017. The refurbishment of one induration machine in the pellet plant is planned for 2018. Production of ore from the Wabush 3 pit is on track as planned for July 2018. The six-year collective agreements with the United Steelworkers of America union employees expired on February 28, 2018. IOC expects to earn revenue from hauling product from the Bloom Lake mine of Quebec Iron Ore Inc., with mine production planned to start March 2018.

The price of iron ore early in 2018 has again exceeded forecasts. If the improved prices and premiums continue in 2018, IOC achieves the production guidance, and the Canadian dollar does not appreciate materially against the US dollar, the 2018 outlook for LIORC will be continued strong cash flows.

I would like to take this opportunity to thank our Shareholders for their interest and loyalty and my fellow Directors for their wisdom and support.

Respectfully submitted on behalf of the
Directors of the Corporation,



William H. McNeil
President and Chief Executive Officer
March 8, 2018

CORPORATE STRUCTURE

LIORC is a Canadian corporation resulting from the conversion of the Labrador Iron Ore Royalty Income Fund (the “Fund”) under an Arrangement effective on July 1, 2010. LIORC is also the successor by amalgamation under the Arrangement of Labrador Mining Company Limited, formerly a wholly-owned subsidiary of the Fund.

LIORC, directly and through its wholly-owned subsidiary Hollinger-Hanna Limited, holds a 15.10% equity interest in IOC and receives a 7% gross overriding royalty and a 10 cent per tonne commission on all iron ore products produced, sold and shipped by IOC. Generally, LIORC pays cash dividends from its net income to the maximum extent possible, subject to the maintenance of appropriate levels of working capital. The common shareholders receive quarterly dividends on the common shares on the 25th day of the month following the end of each quarter.

Eight Directors are responsible for the governance of the Corporation and also serve as directors of Hollinger-Hanna. The Directors, in addition to managing the affairs of the Corporation and Hollinger-Hanna, oversee the Corporation’s interests in IOC. Two of the eight Directors sit on the board of IOC and the five independent Directors serve as members of the Audit, Nominating and Compensation Committees. Scotia Managed Companies Administration Inc., pursuant to an administration agreement, acts as the administrator of the Corporation and Hollinger-Hanna.

Taxation

The Corporation is a taxable corporation. Dividend income received from IOC and Hollinger-Hanna is received tax free while royalty income is subject to income tax and Newfoundland royalty tax. Expenses of the Corporation include administrative expenses. Hollinger-Hanna is a taxable corporation.

Income Taxes

Dividends to a shareholder that are paid within a particular year are to be included in the calculation of the shareholder’s taxable income for that year. All dividends paid in 2017 were “eligible dividends” under the Income Tax Act.

REVIEW OF OPERATIONS

Iron Ore Company of Canada

The income of the Corporation is entirely dependent on IOC as the only assets of the Corporation and its subsidiary are related to IOC and its operations. IOC is one of Canada's largest iron ore producers, operating a mine, concentrator and pellet plant at Labrador City, Newfoundland and Labrador, and is among the top five producers of seaborne iron ore pellets in the world. It has been producing and processing iron ore concentrate and pellets since 1954. IOC is strategically situated to serve markets throughout the world from its year-round port facilities at Sept-Îles, Quebec.

IOC has ore reserves sufficient for approximately 25 years at current production rates with additional resources of a greater magnitude. It currently has the nominal capacity to extract around 55 million tonnes of crude ore annually. The crude ore is processed into iron ore concentrate and then either sold or converted into many different qualities of iron ore pellets to meet its customers' needs. The iron ore concentrate and pellets are transported to IOC's port facilities at Sept-Îles, Quebec via its wholly-owned Quebec North Shore and Labrador Railway, a 418 kilometer rail line which links the mine and the port. From there, the products are shipped to markets throughout North America, Europe, the Middle East and the Asia-Pacific region.

IOC's 2017 sales totaled 19.0 million tonnes, comprised of 10.4 million tonnes of iron ore pellets and 8.6 million tonnes of iron ore concentrate. Production in 2017 was 10.5 million tonnes of pellets and 8.5 million tonnes of CFS. IOC generated ore sales revenues (excluding third party ore sales) of \$2,249 million in 2017 (2016 – \$1,620 million).

Selected IOC Financial Information

	2017	2016	2015	2014	2013
			(\$ in millions)		
Operating Revenues	2,315	1,676	1,495	1,794	2,194
Cash Flow from					
Operating Activities	923	456	267	455	781
Net Income	499	170	21	273	549
Capital Expenditures	265	99	143	187	275

IOC Royalty

The Corporation holds certain leases and licenses covering approximately 18,200 hectares of land near Labrador City. IOC has leased certain portions of these lands from which it currently mines iron ore. In return, IOC pays the Corporation a 7% gross overriding royalty on all sales of iron ore products produced from these lands. A 20% tax on the royalty is payable to the Government of Newfoundland and Labrador. For the five years prior to 2017, the average royalty net of the 20% tax had been \$94.2 million per year and in 2017 the net royalty was \$125.1 million (2016 – \$90.5 million).

Because the royalty is “off-the-top”, it is not dependent on the profitability of IOC. However, it is affected by changes in sales volumes, iron ore prices and, because iron ore prices are denominated in US dollars, the United States–Canadian dollar exchange rate.

REVIEW OF OPERATIONS

IOC Equity

In addition to the royalty interest, the Corporation directly and through its wholly owned subsidiary, Hollinger-Hanna, owns a 15.10% equity interest in IOC. The other shareholders of IOC are Rio Tinto Limited with 58.72% and Mitsubishi Corporation with 26.18%.

IOC Commissions

Hollinger-Hanna has the right to receive a payment of 10 cents per tonne on the products produced and sold by IOC. Pursuant to an agreement, IOC is obligated to make the payment to Hollinger-Hanna so long as Hollinger-Hanna is in existence and solvent. In 2017, Hollinger-Hanna received a total of \$1.9 million in commissions from IOC (2016 – \$1.8 million).

Quarterly Dividends

Dividends of \$2.65 per share including special dividends of \$1.65 per share were declared in 2017 (2016 – dividends of \$1.00 per share). These dividends were allocated as follows:

Period Ended	Payment Date	Dividend Income per Share	Total Dividend (\$ Million)
Mar. 31, 2017	Apr. 25, 2017	\$ 0.25	\$ 16.0
Special Dividend	Apr. 25, 2017	0.25	16.0
Jun. 30, 2017	Jul. 25, 2017	0.25	16.0
Special Dividend	Jul. 25, 2017	0.35	22.4
Sep. 30, 2017	Oct. 25, 2017	0.25	16.0
Special Dividend	Oct. 25, 2017	0.75	48.0
Dec. 31, 2017	Jan. 25, 2018	0.25	16.0
Special Dividend	Jan. 25, 2018	0.30	19.2
Dividend to Shareholders – 2017		\$ 2.65	\$ 169.6
Mar. 31, 2016	Apr. 25, 2016	\$ 0.25	\$ 16.0
Jun. 30, 2016	Jul. 25, 2016	0.25	16.0
Sep. 30, 2016	Oct. 25, 2016	0.25	16.0
Dec. 31, 2016	Jan. 25, 2017	0.25	16.0
Dividend to Shareholders – 2016		\$ 1.00	\$ 64.0

The quarterly dividends are payable to all shareholders of record on the last day of each calendar quarter and are paid on the 25th day of the following month.

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following is a discussion of the consolidated financial condition and results of operations of the Corporation for the years ended December 31, 2017 and 2016. This discussion should be read in conjunction with the consolidated financial statements of the Corporation and notes thereto for the years ended December 31, 2017 and 2016. This information is prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and all amounts are shown in Canadian dollars unless otherwise indicated.

The Corporation is a Canadian corporation resulting from the conversion of the Fund under an Arrangement effective on July 1, 2010. LIORC is also the successor by amalgamation under the Arrangement of Labrador Mining Company Limited, formerly a wholly-owned subsidiary of the Fund.

General

The Corporation is dependent on the operations of IOC. IOC's earnings and cash flows are affected by the volume and mix of iron ore products produced and sold, costs of production and the prices received. Iron ore demand and prices fluctuate and are affected by numerous factors which include demand for steel and steel products, the relative exchange rate of the US dollar, global and regional demand and production, political and economic conditions and production costs in major producing areas.

Liquidity and Capital Resources

The Corporation had \$40.5 million (2016 – \$23.9 million) in cash as at December 31, 2017 with total current assets of \$82.6 million (2016 – \$62.9 million). The Corporation has working capital of \$33.1 million (2016 – \$38.8 million). The Corporation's cash flow from operations was \$167.0 million (2016 – \$63.5 million) and dividends paid during the year were \$150.4 million, resulting in cash balances increasing by \$16.6 million during 2017.

Cash balances consist of deposits in Canadian dollars and US dollars with Canadian chartered banks. Accounts receivable primarily consist of royalty payments from IOC. Royalty payments are received in US dollars and converted to Canadian dollars on receipt, usually 25 days after the quarter end. The Company does not normally attempt to hedge this short term foreign currency exposure.

Operating cash flow of the Corporation is sourced entirely from IOC through the Corporation's 7% royalty, 10 cents commission per tonne and dividends from its 15.10% equity interest in IOC. The Corporation intends to pay cash dividends of the net income derived from IOC to the maximum extent possible, subject to the maintenance of appropriate levels of working capital.

The Corporation has a \$50 million revolving credit facility with a term ending September 18, 2020 with provision for annual one-year extensions. No amount is currently drawn under this facility leaving \$50.0 million available to provide for any capital required by IOC or requirements of the Corporation.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Operating Results

The following table summarizes the Corporation's 2017 operating results as compared to 2016 results (in '000's).

Revenue	2017	2016
IOC royalties (<i>net of 20% Newfoundland royalty tax</i>)	\$ 125,094	\$ 90,465
IOC commissions	1,885	1,793
Other	374	233
	<u>127,353</u>	<u>92,491</u>
Expenses		
Administrative expenses	2,938	2,743
Income taxes expense – current	37,283	26,821
	<u>40,221</u>	<u>29,564</u>
Net income before undernoted items	<u>87,132</u>	<u>62,927</u>
Non cash revenue (expense)		
Equity earnings in IOC	74,300	24,723
Deferred income taxes	2,204	(4,343)
Amortization	(6,352)	(5,134)
	<u>70,152</u>	<u>15,246</u>
Net income for the year	<u>157,284</u>	<u>78,173</u>
Other comprehensive gain	2,060	699
Comprehensive income for the year	<u>\$ 159,344</u>	<u>\$ 78,872</u>

A summary of IOC's sales for calculating the royalty to LIORC in millions of tonnes is as follows:

	First Quarter 2017	Second Quarter 2017	Third Quarter 2017	Fourth Quarter 2017	Total Year 2017	Total Year 2016
Pellets	2.48	2.44	2.78	2.78	10.48	10.06
Concentrates ⁽¹⁾	2.19	1.60	2.23	2.66	8.67	8.17
Total	<u>4.67</u>	<u>4.04</u>	<u>5.00</u>	<u>5.44</u>	<u>19.15</u>	<u>18.23</u>

(1) Excludes third party ore sales.

(2) Totals may not add up due to rounding.

IOC's 2017 iron ore sales for calculating the royalty to LIORC, totaled 19.2 million tonnes compared to 18.2 million tonnes in 2016. Royalty revenue increased to \$156.4 million as compared to \$113.1 million in 2016. Equity earnings from IOC amounted to \$74.3 million compared to \$24.7 million in 2016. The higher royalty revenue and equity earnings achieved in 2017 as compared to 2016 was mainly due to improved prices for concentrate, particularly in the first quarter of 2017, high premiums for concentrate and pellets, plus higher concentrate and pellet sales tonnages. Prices and premiums were higher than most forecasts with the Chinese governments enacting and enforcing measures to reduce pollution, which favoured higher value-in-use products, such as the concentrates and pellets produced by IOC.

MANAGEMENT'S DISCUSSION AND ANALYSIS

The average index price for 62% fines increased 22% year-on-year to US\$71 per tonne CFR China in 2017. The pellet premiums also increased year-on-year, particularly in the last few months of 2017, approaching approximately US\$60 per tonne in October and November. The average price realized by IOC for CFS and pellets, FOB Sept-Îles, was approximately C\$108 per tonne in 2017 compared to C\$80 per tonne in 2016, an increase of 35%. The higher premiums for 65% Fe concentrate and pellets were driven by the changes in environmental policy by the Chinese governments, which caused Chinese steel producers to increase the usage of higher value-in-use iron ore, such as the concentrate and pellets produced by IOC. With improving pellet premiums in 2017, IOC again focused on maximizing pellet production to the extent possible, given that two pellet lines were refurbished in 2017 with none in 2016. The sales tonnage of pellets in 2017, for calculating the royalty to LIORC, was 4% higher than in 2016. The CFS tonnages in 2017 were higher than in 2016 by 6%.

Capital expenditure for IOC in 2017 was \$265 million in total as compared to \$99 million in 2016. The capital program for 2016 was set when the price outlook was poor and the expansion program had been largely completed. Therefore the capital budget was set for minimal sustaining capital. For 2017, the total capital budget was increased to \$245 million as the price outlook in December 2016 was much improved. The 2017 budget included some \$40 million as development capital for the Wabush 3 pit (total budget \$79 million in 2017 and 2018). The sustaining capital included the refurbishment of the No. 2 and 5 pellet lines, capital to improve air emissions from the pellet plant, the refurbishment of track and the remediation of high wall rock cuts along the route of the Quebec North Shore and Labrador Railway. The planned capital programs were executed largely on budget. In late 2017 IOC purchased some \$20 million of leased equipment to reduce future operating costs which added to the budget.

The Shareholders' consolidated net income for the year ended December 31, 2017 was \$157.3 million or \$2.46 per share compared to \$78.2 million or \$1.22 per share in 2016. Equity earnings from IOC amounted to \$74.3 million compared to \$24.7 million in 2016. The main cause of IOC's higher earnings for 2017 as compared to 2016 was the improved iron ore prices and premiums, and increased sales tonnages.

Administrative expenses for the year ended December 31, 2017 include a non-cash foreign exchange loss of \$0.3 million on the conversion of the dividend received from IOC in December 2016. Amortization expense for royalty and commission interests increased \$1.2 million for the year ended December 31, 2017 due to an increased amortization rate reflecting lower estimated total mineral resources over the prior year.

Fourth quarter 2017 CFS sales were much improved year-over-year, but pellet sales were lower as a result of the refurbishment of the No. 5 pellet line. However, the achieved sales prices of CFS and pellets were significantly improved, resulting in royalty income of \$40.0 million for the quarter as compared to \$38.0 million for the same period in 2016. Fourth quarter 2017 cash flow from operations was \$39.6 million or \$0.62 per share compared to 2016 of \$28.3 million or \$0.44 per share. LIORC received an IOC dividend in the fourth quarter of 2017 in the amount of \$19.3 million or \$0.30 per share (2016 – \$15.1 million or \$0.23 per share). Equity earnings from IOC amounted to \$16.6 million in the fourth quarter 2017 compared to \$18.0 million for the same period in 2016 in part as a result of a decline in the gross margin owing to higher product unit costs due to lower production overall for the quarter offset by higher iron ore prices and premiums achieved and increased sales tonnages.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Selected Consolidated Financial Information

The following table sets out financial data from a Shareholder's perspective for the three years ended December 31, 2017, 2016 and 2015.

Description	Years Ended December 31		
	2017	2016	2015
	(in millions except per share information)		
Revenue	\$ 158.6	\$ 115.1	\$ 101.7
Net Income	\$ 157.3	\$ 78.2	\$ 54.7
Net Income per Share	\$ 2.46	\$ 1.22	\$ 0.85
Cash Flow from Operations	\$ 167.0 ⁽¹⁾	\$ 63.5 ⁽²⁾	\$ 59.9
Cash Flow from Operations per Share	\$ 2.61 ⁽¹⁾	\$ 0.99 ⁽²⁾	\$ 0.94
Total Assets	\$ 750.0	\$ 737.0	\$ 714.1
Dividends Declared per Share	\$ 2.65	\$ 1.00	\$ 1.00
Number of Common Shares outstanding	64.0	64.0	64.0

(1) Includes IOC dividends totaling \$76.7 million or \$1.20 per Share.

(2) Includes IOC dividend totaling \$15.1 million or \$0.23 per Share.

The following table sets out quarterly revenue, net income, cash flow and dividend data for 2017 and 2016. Due to seasonal weather patterns the first and fourth quarters generally have lower production and sales. Royalty revenues and equity earnings in IOC track iron ore spot prices, which can be very volatile. Dividends, included in cash flow, are declared and paid by IOC irregularly according to the availability of cash.

	Revenue	Net Income	Net Income per Share	Cash Flow	Cash Flow from Operations per Share	Adjusted Cash Flow per Share ⁽¹⁾	Dividends Declared per Share
	(in millions except per share information)						
2017							
First Quarter	\$ 43.4	\$ 42.9	\$ 0.67	\$ 28.2 ⁽²⁾	\$ 0.44 ⁽²⁾	\$ 0.53 ⁽²⁾	\$ 0.50
Second Quarter	\$ 34.2	\$ 32.3	\$ 0.50	\$ 45.6 ⁽³⁾	\$ 0.71 ⁽³⁾	\$ 0.53 ⁽³⁾	\$ 0.60
Third Quarter	\$ 40.4	\$ 43.8	\$ 0.69	\$ 53.6 ⁽⁴⁾	\$ 0.84 ⁽⁴⁾	\$ 0.85 ⁽⁴⁾	\$ 1.00
Fourth Quarter	\$ 40.6	\$ 38.3	\$ 0.60	\$ 39.6 ⁽⁵⁾	\$ 0.62 ⁽⁵⁾	\$ 0.65 ⁽⁵⁾	\$ 0.55
2016							
First Quarter	\$ 22.3	\$ 11.0	\$ 0.17	\$ 12.5	\$ 0.19	\$ 0.19	\$ 0.25
Second Quarter	\$ 25.8	\$ 8.3	\$ 0.13	\$ 7.5	\$ 0.12	\$ 0.22	\$ 0.25
Third Quarter	\$ 28.4	\$ 21.2	\$ 0.33	\$ 15.2	\$ 0.24	\$ 0.24	\$ 0.25
Fourth Quarter	\$ 38.6	\$ 37.7	\$ 0.59	\$ 28.3 ⁽⁶⁾	\$ 0.44 ⁽⁶⁾	\$ 0.57 ⁽⁶⁾	\$ 0.25

(1) "Adjusted cash flow" (see below)

(2) Includes \$10.0 million IOC dividend.

(3) Includes \$15.2 million IOC dividend.

(4) Includes \$32.2 million IOC dividend.

(5) Includes \$19.3 million IOC dividend.

(6) Includes \$15.1 million IOC dividend.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Standardized Cash Flow and Adjusted Cash Flow

For the Corporation, standardized cash flow is the same as cash flow from operating activities as recorded in the Corporation's cash flow statements as the Corporation does not incur capital expenditures or have any restrictions on dividends. Standardized cash flow per share was \$2.61 for 2017 (2016 – \$0.99). Cumulative standardized cash flow from inception of the Corporation is \$25.15 per share and total cash distributions since inception are \$24.59 per share, for a payout ratio of 98%.

The Corporation also reports "Adjusted cash flow" which is defined as cash flow from operating activities after adjustments for changes in amounts receivable, accounts payable and income taxes recoverable and payable. It is not a recognized measure under IFRS. The Directors believe that adjusted cash flow is a useful analytical measure as it better reflects cash available for distributions to Shareholders.

The following reconciles standardized cash flow from operating activities to adjusted cash flow (in '000's).

	2017	2016
Standardized cash flow from operating activities	\$ 166,960	\$ 63,473
Changes in amounts receivable, accounts and interest payable and income taxes recoverable and payable	(3,116)	14,570
Adjusted cash flow	\$ 163,844	\$ 78,044
Adjusted cash flow per share	\$ 2.56	\$ 1.22

Disclosure Controls and Internal Control over Financial Reporting

The President and CEO and the CFO are responsible for establishing and maintaining disclosure controls and procedures and internal control over financial reporting for the Corporation. Two directors serve as directors of IOC and IOC provides monthly reports on its operations to them. The Corporation also relies on financial information provided by IOC, including its audited financial statements, and other material information provided to the President and CEO, the Executive Vice President and Secretary and the CFO by officers of IOC. IOC is a private corporation, and its financial statements are not publicly available.

The Directors are informed of all material information relating to the Corporation and its subsidiary by the officers of the Corporation on a timely basis and approve all core disclosure documents including the Management Information Circular, the annual and interim financial statements and related Management's Discussion and Analyses, the Annual Information Form, any prospectuses and all press releases. An evaluation of the design and operating effectiveness of the Corporation's disclosure controls and procedures was conducted under the supervision of the CEO and CFO. Based on their evaluation, they concluded that the Corporation's disclosure controls and procedures were effective in ensuring that all material information relating to the Corporation was accumulated and communicated for the year ended December 31, 2017.

The President and CEO and the CFO have designed internal control over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS. An evaluation of the design and operating effectiveness of the Corporation's internal control over financial reporting was conducted under the supervision of the CEO and CFO. Based on their evaluation, they concluded that the Corporation's internal control over financial reporting was effective and that there were no material weaknesses therein for the year ended December 31, 2017.

The preparation of financial statements requires the Corporation's management to make estimates and assumptions that affect the reported amounts of the assets, liabilities, revenue and expenses reported each period. Each of these estimates varies with respect to the level of judgment involved and the potential impact on the Corporation's reported financial results. Estimates are deemed critical when the Corporation's financial condition, change in financial condition or results of operations would be materially impacted by a different estimate or a change in estimate from period to period. By their nature, these estimates are subject to measurement uncertainty, and changes in these estimates may affect the consolidated financial statements of future periods.

No material change in the Corporation's internal control over financial reporting occurred during the year ended December 31, 2017.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Outlook

Many forecasts for seaborne iron ore, 62% Fe, CFR China, are for the price to decline and average below US\$60 per tonne in 2018. Reportedly, the Office of the Chief Economist of Australia predicted in January 2018 that iron ore prices will average US\$53 per tonne (FOB Australia) in 2018, and US\$49 in 2019. Most forecasts note the anticipated increased supply, particularly from Vale's S11D mine in Brazil. It is also increasingly likely that the Samarco operation in Brazil could re-open in late 2018 or in 2019, which would likely adversely affect pellet premiums. However, some forecasts note the Chinese policies on pollution and the strong steel margins for Chinese producers as being supportive of iron ore prices and premiums for higher grade iron ore.

Rio Tinto has released guidance for 2018 of between 11.5 million to 12.5 million tonnes for their 58.7% share of IOC's saleable production (pellets and CFS tonnage). This would result in 19.6 million to 21.3 million tonnes of saleable production on a 100% basis. With the strong pellet premiums, IOC will continue to prioritize pellet production in 2018. The IOC objective is 22.2 million tonnes of concentrate production with sales of approximately 12.5 million tonnes of pellets and 8.4 million tonnes of CFS in 2018.

The capital expenditures for 2018 are expected to be \$220 million, lower than the \$265 million in 2017. The refurbishment of one induration machine in the pellet plant is planned for 2018. Production of ore from the Wabush 3 pit is on track as planned for July 2018. The six-year collective agreements with the United Steelworkers of America union employees expired on February 28, 2018. IOC expects to earn revenue from hauling product from the Bloom Lake mine of Quebec Iron Ore Inc., with mine production planned to start March 2018.

The price of iron ore early in 2018 has again exceeded forecasts. If the improved prices and premiums continue in 2018, IOC achieves the production guidance, and the Canadian dollar does not appreciate materially against the US dollar, the 2018 outlook for LIORC will be continued strong cash flows.

Additional Information

Additional information relating to the Corporation, including the Annual Information Form, is on SEDAR at www.sedar.com. Additional information is also available on the Corporation's website at www.labradorironore.com.



William H. McNeil,
President and Chief Executive Officer

Toronto, Ontario
March 8, 2018

MANAGEMENT'S REPORT

The consolidated financial statements are the responsibility of the management of Labrador Iron Ore Royalty Corporation (the "Corporation"). They have been prepared in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board, using management's best estimates and judgements, where appropriate.

Management is responsible for the reliability and integrity of the consolidated financial statements, the notes to the consolidated financial statements and other financial information contained in this report. In the preparation of these consolidated financial statements, estimates are sometimes necessary because a precise determination of certain assets and liabilities is dependent on future events. Management believes such estimates have been based on careful judgements and have been properly reflected in the accompanying consolidated financial statements.

Management is also responsible for maintaining a system of internal controls designed to provide reasonable assurance that assets are safeguarded and that accounting systems provide timely, accurate and reliable financial information. The Directors are responsible for ensuring that management fulfills its responsibilities for financial reporting and internal control.

PricewaterhouseCoopers LLP, the independent auditors, have audited the Corporation's consolidated financial statements in accordance with Canadian generally accepted auditing standards and have provided an independent professional opinion.



William H. McNeil
President and Chief Executive Officer



Alan R. Thomas
Chief Financial Officer

Toronto, Ontario
March 8, 2018

INDEPENDENT AUDITOR'S REPORT

■ To the Shareholders of Labrador Iron Ore Royalty Corporation

We have audited the accompanying consolidated financial statements of Labrador Iron Ore Royalty Corporation and its subsidiary, which comprise the consolidated statements of financial position as at December 31, 2017 and 2016 and the consolidated statements of income and comprehensive income, statements of cash flows, and statements of changes in equity for the years then ended, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

Management's responsibility for the consolidated financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Labrador Iron Ore Royalty Corporation and its subsidiary as at December 31, 2017 and 2016 and their financial performance and their cash flows for the years then ended in accordance with International Financial Reporting Standards.

PricewaterhouseCoopers LLP

Chartered Professional Accountants, Licensed Public Accountants
Toronto, Ontario
March 8, 2018

LABRADOR IRON ORE ROYALTY CORPORATION

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

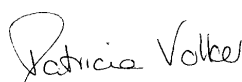
	As at December 31,	
	2017	2016
<i>(in thousands of Canadian dollars)</i>		
Assets		
Current Assets		
Cash	\$ 40,498	\$ 23,937
Amounts receivable (note 4)	42,092	38,487
Income taxes recoverable	—	490
Total Current Assets	82,590	62,914
Non-Current Assets		
Iron Ore Company of Canada (“IOC”) royalty and commission interests (note 5)	259,032	265,384
Investment in IOC (note 6)	408,691	408,680
Total Non-Current Assets	667,723	674,064
Total Assets	\$ 750,313	\$ 736,978
Liabilities and Shareholders' Equity		
Current Liabilities		
Accounts payable	\$ 8,601	\$ 8,073
Dividend payable (note 7)	35,200	16,000
Taxes payable	5,703	—
Total Current Liabilities	49,504	24,073
Non-Current Liabilities		
Deferred income taxes (note 9)	127,220	129,060
Total Liabilities	176,724	153,133
Shareholders' Equity		
Share capital (note 10)	317,708	317,708
Retained earnings	264,272	276,588
Accumulated other comprehensive loss (note 11)	(8,391)	(10,451)
	573,589	583,845
Total Liabilities and Shareholders' Equity	\$ 750,313	\$ 736,978

See accompanying notes to consolidated financial statements.

Approved by the Directors,



William H. McNeil
Director



Patricia M. Volker
Director

LABRADOR IRON ORE ROYALTY CORPORATION

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

(in thousands of Canadian dollars except for per share information)

	For the Year Ended December 31,	
	2017	2016
Revenue		
IOC royalties	\$ 156,367	\$ 113,081
IOC commissions	1,885	1,793
Interest and other income	374	233
	158,626	115,107
Expenses		
Newfoundland royalty taxes	31,273	22,616
Amortization of royalty and commission interests	6,352	5,134
Administrative expenses	2,938	2,743
	40,563	30,493
Income before equity earnings and income taxes	118,063	84,614
Equity earnings in IOC (note 6)	74,300	24,723
Income before income taxes	192,363	109,337
Provision for income taxes (note 9)		
Current	37,283	26,821
Deferred	(2,204)	4,343
	35,079	31,164
Net income for the year	157,284	78,173
Other comprehensive income		
Share of other comprehensive income of IOC that will not be reclassified subsequently to profit or loss (net of income taxes of 2017 – \$364; 2016 – \$47) (note 11)	2,060	699
Comprehensive income for the year	\$ 159,344	\$ 78,872
Net income per share (note 10)	\$ 2.46	\$ 1.22

See accompanying notes to consolidated financial statements.

LABRADOR IRON ORE ROYALTY CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands of Canadian dollars)

Net inflow (outflow) of cash related to the following activities

Operating

	2017	2016
Net income for the period	\$ 157,284	\$ 78,173
Items not affecting cash:		
Equity earnings in IOC	(74,300)	(24,723)
Current income taxes	37,283	26,821
Deferred income taxes	(2,204)	4,343
Amortization of royalty and commission interests	6,352	5,134
Common share dividend from IOC	76,713	15,117
Change in amounts receivable	(3,605)	(17,979)
Change in accounts payable	528	3,658
Income taxes paid	(31,090)	(27,071)
Cash flow from operating activities	166,961	63,473

Financing

Dividends paid to shareholders	(150,400)	(64,000)
Cash flow used in financing activities	(150,400)	(64,000)

Increase (decrease) in cash, during the year

	16,561	(527)
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Cash, beginning of year

	23,937	24,464
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Cash, end of year

	\$ 40,498	\$ 23,937
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See accompanying notes to consolidated financial statements.

LABRADOR IRON ORE ROYALTY CORPORATION

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(in thousands of Canadian dollars)

	Share capital	Retained earnings	Accumulated other comprehensive loss	Total
Balance as at December 31, 2015	\$ 317,708	\$ 262,415	\$ (11,150)	\$ 568,973
Net income for the year	—	78,173	—	78,173
Dividends declared to shareholders	—	(64,000)	—	(64,000)
Share of other comprehensive income from investment in IOC (net of taxes)	—	—	699	699
Balance as at December 31, 2016	\$ 317,708	\$ 276,588	\$ (10,451)	\$ 583,845
Balance as at December 31, 2016	\$ 317,708	\$ 276,588	\$ (10,451)	\$ 583,845
Net income for the year	—	157,284	—	157,284
Dividends declared to shareholders	—	(169,600)	—	(169,600)
Share of other comprehensive income from investment in IOC (net of taxes)	—	—	2,060	2,060
Balance as at December 31, 2017	\$ 317,708	\$ 264,272	\$ (8,391)	\$ 573,589

See accompanying notes to consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(in thousands of Canadian dollars)

1. Corporate Information

Labrador Iron Ore Royalty Corporation (the "Corporation") directly and through its wholly-owned subsidiary, Hollinger-Hanna Limited ("Hollinger-Hanna"), holds a 15.10% equity interest in Iron Ore Company of Canada ("IOC"), a 7% gross overriding royalty on all iron ore products produced, sold and shipped by IOC, a \$0.10 per tonne commission interest on sales of iron ore by IOC and certain lease interests and, accordingly, is economically dependent on IOC. The Corporation and Hollinger-Hanna were established under the Canada Business Corporations Act. The Corporation is listed on the Toronto Stock Exchange under the symbol LIF. The registered office of the Corporation is 235 Water Street, P.O. Box 610, St. John's, Newfoundland, A1C 5L3.

These consolidated financial statements were authorized for issuance by the Board of Directors of the Corporation on March 8, 2018.

2. Basis of Presentation

These consolidated financial statements of the Corporation have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). The consolidated financial statements are prepared on a going concern basis, under the historical cost convention. All financial information is presented in Canadian dollars, except as otherwise noted. The significant accounting policies described in Note 3 are consistently applied for all the years presented.

3. Summary of Significant Accounting Policies

(a) Basis of consolidation

These consolidated financial statements include the accounts of the Corporation and its wholly-owned subsidiary, Hollinger-Hanna. All inter-company transactions, balances, income and expenses are eliminated in full on consolidation.

(b) Investment in associate

The Corporation has a 15.1% equity and voting interest in its associate, IOC, and exercises significant influence over IOC through its direct ownership interest, combined with its representation on the board of directors, participation in policy-making and approval processes, and the mineral sublease under which IOC conducts its operations near Labrador City, Newfoundland and Labrador. This investment is accounted for using the equity method.

The Corporation recognizes its share of earnings (loss) net of tax in the consolidated statements of income and comprehensive income which is adjusted against the carrying amount of its investment in IOC.

Unrealized gains and losses on transactions between the Corporation and IOC are eliminated to the extent of the Corporation's interest in this entity. Unrealized losses are eliminated only to the extent that there is no evidence of impairment.

The excess of the cost of the investment in IOC over the underlying book value at the date of acquisition is amortized on the unit-of-production method based on actual production in the current year and estimated production of iron ore over the life of mine at IOC. The rate of amortization is based on estimates of total proven and probable reserves and a portion of mineral resources, which may differ from actual.

(c) Revenue recognition

Royalty and commission income are based on IOC sales, and are measured at the fair value of the consideration received or receivable. Royalty and commission income is recorded on an accrual basis in accordance with the substance of the mineral sublease provided that it is probable that the economic benefits will flow to the Corporation and the amount of revenue can be measured reliably and collectability is reasonably assured.

(d) IOC royalty and commission interests

The royalty and commission interests are carried at cost less accumulated amortization. Amortization is recognized on the unit-of-production method based on actual production in the current year and estimated production of iron ore over the life of

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

mine at IOC. The rate of amortization is based on estimates of total proven and probable reserves along with a portion of mineral resources, which may differ from actual.

(e) Asset impairment

At each balance sheet date the Corporation assesses whether for assets, including investments in associates, there is any indication that such assets are impaired. Impairment is recognized if the recoverable amount, determined as the higher of the estimated fair value less costs of disposal or the value in use, is less than its carrying value.

Fair value less costs of disposal is best evidenced if obtained from an active market or binding sale agreement. Where neither exists, the fair value is based on the best estimates available to reflect the amount that could be received from an arm's length transaction.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the relevant asset for which the estimates of future cash flows have not been adjusted. The projections of future cash flows take into account the relevant operating plans and management's best estimate of the most probable set of conditions anticipated to prevail.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the lesser of the revised estimate of recoverable amount and the carrying amount that would have been recorded had no impairment loss been recognized previously.

(f) Income taxes

The Corporation and Hollinger-Hanna are taxable corporations.

Current income taxes are measured at the amount expected to be paid to tax authorities, based on taxable profit for the period, net of recoveries using enacted tax rates at the balance sheet date. Taxable income differs from income as reported in the consolidated statements of income and comprehensive income because of items of income or expense that are taxable or deductible in other periods and items that are never taxable or deductible. Deferred income tax liabilities are recognized using the liability method on taxable temporary differences between the tax bases and carrying amounts of assets and liabilities. Deferred income tax assets are recognized for all deductible temporary differences to the extent that it is probable that deductions can be utilized. Deferred income tax assets and liabilities are measured at tax rates that are expected to apply to the year when the asset is realized or the liability settled, using enacted or substantively enacted tax rates at the statement of financial position date. Deferred income taxes are presented as non-current.

(g) Foreign currency transactions

The Canadian dollar is the functional and presentation currency of the Corporation and Hollinger-Hanna. Amounts receivable and payable denominated in U.S. dollars are translated at exchange rates in effect at the balance sheet date and revenues and expenses denominated in U.S. dollars are translated at exchange rates in effect at the transaction date.

(h) Financial instruments

Financial assets and financial liabilities are measured at fair value on initial recognition in the consolidated statements of financial position. Measurement subsequent to initial recognition depends on the financial instrument's classification which is determined by the purpose for which the instrument was acquired or issued, the instrument's characteristics and the Corporation's designation of the instrument. The Corporation's financial instruments are classified as loans and receivables or other financial liabilities. Financial instruments classified as loans and receivables and other financial liabilities are measured at amortized cost, net of associated transaction costs, using the effective interest method. Cash and amounts receivable are classified as loans and receivables measured at cost; accounts payable and dividend payable are financial liabilities measured at amortized cost.

(i) Financial liabilities and equity instruments

Debt and equity instruments issued by the Corporation are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangements and the definitions of a financial liability and an equity instrument.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(j) Segment reporting

The Corporation manages its business under a single operating segment, consisting of its investment in IOC and its IOC royalty and commission interests. All of the Corporation's assets and revenues are attributable to this single segment. The operating segment is reported in a manner consistent with the internal reporting provided to the President and Chief Executive Officer ("CEO") who fulfills the role of the chief operating decision-maker.

(k) Critical judgments and estimates

The preparation of financial statements requires the Corporation's management to make estimates and assumptions that affect the reported amounts of the assets, liabilities, revenue and expenses reported each period. Each of these estimates varies with respect to the level of judgment involved and the potential impact on the Corporation's reported financial results. Estimates are deemed critical when the Corporation's financial condition, change in financial condition or results of operations would be materially impacted by a different estimate or a change in estimate from period to period. By their nature, these estimates are subject to measurement uncertainty, and changes in these estimates may affect the consolidated financial statements of future periods.

Critical judgments in applying accounting policies

Determination of significant influence over investment in IOC

The Corporation owns 15.1% of IOC. Judgment is needed to assess whether this interest meets the definition of significant influence and should be accounted for under the equity method. Management makes this determination based on its legal ownership interest, board representation and through an analysis of the Corporation's participation in IOC's policy making process and mineral sub-lease agreements under which IOC conducts its operations.

Income taxes

The Corporation applies judgment in determining the tax rate to calculate deferred income taxes based upon temporary differences between the assets and liabilities that are reported in its consolidated financial statements and their tax bases as determined under applicable tax legislation. The Corporation records deferred income tax assets when it determines that it is probable that such assets will be realized. The future realization of deferred tax assets can be affected by many factors, including current and future economic conditions, expected royalties and commissions and can either be increased or decreased where, in the view of management, such change is warranted.

Critical accounting estimates and assumptions

Ore reserves and resources

Reserves are estimates of the amount of product that can be economically and legally extracted from IOC's mining properties. Reserve and resource estimates are an integral component in the determination of the commercial viability of the investment in IOC, the IOC royalty and commission interest, amortization calculations and impairment analyses. In calculating reserves and resources, estimates and assumptions are required about a range of geological, technical and economic factors, including quantities, grades, production techniques, production decline rates, recovery rates, production costs, commodity demand, commodity prices and exchange rates. In addition, future changes in regulatory environments, including government levies or changes in the Corporation's rights to exploit the resource imposed over the producing life of the reserves and resources may also significantly impact estimates.

Asset impairment

The Corporation's investment in IOC and the IOC royalty and commission interests are tested for impairment if there is an indicator of impairment. Where an indicator of impairment exists, a formal estimate of the recoverable amount, which is considered to be the higher of the fair value less costs of disposal and value in use, is made. These assessments require the use of estimates and assumptions such as long term commodity prices, discount rates, future capital requirements, and operating performance. Fair value is determined as the amount that would be obtained from the sale of the asset(s) in an arm's-length transaction between knowledgeable and willing parties. Value in use for mineral assets is generally determined as the present values of estimated future cash flows arising from the continued use of the assets. These cash flows are discounted by an appropriate pre-tax discount rate to determine the estimated value in use. Projections inherently require assumptions and

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

judgments to be made about each of the factors affecting future cash flows. Changes in any of these assumptions or judgments could result in a significant difference in the recoverable amount. Management considers the investment in IOC and the IOC royalty and commission interests to be a single combined cash generating unit.

(I) Future Accounting Policies

The Corporation has evaluated the impact of accounting policy changes effective January 1, 2017 and has determined that there are no policy changes that impact the consolidated financial statements for the year ended December 31, 2017. Future changes in accounting standards which may impact the consolidated financial statements for future periods pertain to adoption of IFRS 9 Financial Instruments and IFRS 15 Revenue from Contracts with Customers. The mandatory effective date of these standards is on or after January 1, 2018 and the Corporation will adopt the new standards on this date.

With respect to IFRS 9, the Corporation will be required to evaluate its financial assets for impairment based on an expected credit loss model. The Corporation's financial assets which are currently subject to credit risk are cash and amounts receivable. The Corporation does not expect that the standard will have a material impact on its consolidated financial statements because the Corporation's counterparties have strong credit ratings and there is no recent history of significant credit losses on the Corporation's financial assets. The expected credit loss on these financial assets would be nominal.

With respect to IFRS 15, the Corporation has conducted its assessment of the impact on royalty and commission revenue and net income from its equity interest in IOC. Based on work performed to date, the Corporation does not expect that the standard will have a material impact on its consolidated financial statements.

4. Amounts Receivable

Amounts receivable consist of the following:

	December 31	
	2017	2016
IOC royalties	\$ 41,834	\$ 38,334
IOC commissions	225	130
Other	33	23
	<u>\$ 42,092</u>	<u>\$ 38,487</u>

5. IOC Royalty and Commission Interests

	December 31	
	2017	2016
7% Overriding royalty interest, at cost	\$ 351,617	\$ 351,617
Commission interest, at cost	13,661	13,661
Accumulated amortization	(106,246)	(99,894)
	<u>\$ 259,032</u>	<u>\$ 265,384</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

6. Investment in IOC

The Corporation holds, directly and through Hollinger-Hanna, all of the Series B and Series C common shares of IOC, representing a 15.10% equity interest in the company as at December 31, 2017 and 2016. The Series B and Series C common shares have identical voting rights to all other issued and outstanding common shares of IOC.

	2017	2016
Investment in IOC, beginning of year	\$ 408,680	\$ 398,328
Equity earnings in IOC	74,300	24,723
Other comprehensive income (loss) of IOC	2,424	746
Common share dividend received	(76,713)	(15,117)
Investment in IOC, end of year	\$ 408,691	\$ 408,680

The Corporation's ability to exercise significant influence over IOC is achieved through its legal ownership interest, combined with its representation on the board of directors, participation in policy-making processes and in approval processes, and the mineral sublease agreement under which IOC conducts its operations near Labrador City, Newfoundland and Labrador.

The net excess of cost of the Investment in IOC over the net book value of underlying net assets amounts to \$44,303 (2016 – \$45,389) and is being amortized to net income on the units-of-production method based on actual production in the current year and estimated production of iron ore over the life of mine at IOC.

A summary of the financial information of IOC is as follows:

	2017	2016
Common share dividends received from IOC	\$ 76,713	\$ 15,117
Amounts per IOC's financial statements:		
Current assets	\$ 881,489	\$ 863,564
Non-current assets	3,015,042	2,915,942
Current liabilities	607,748	528,911
Non-current liabilities	892,007	860,817
Revenue	2,314,700	1,675,635
Net income	499,244	169,531
Other comprehensive income	16,055	4,939
Comprehensive income	515,299	174,470

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Reconciliation of IOC's net assets to LIORC's investment per Statements of Financial Position:

	2017	2016
IOC net assets, beginning of year	\$ 2,389,778	\$ 2,314,074
Net income of IOC	499,244	169,531
Share based transactions with other shareholders	(268)	1,346
Other comprehensive income of IOC	16,055	4,939
Common share dividends declared and paid	(508,033)	(100,112)
IOC net assets, end of year	2,396,776	2,389,778
Ownership interest	15.1%	15.1%
Share of net assets	361,913	360,856
Adjustments:		
Excess cost over net book value	44,303	45,389
Other	2,475	2,435
Carrying value – Investment in IOC	\$ 408,691	\$ 408,680

Commitments

LIORC has no commitments from its investment in IOC that would give rise to future outflow of cash.

Contingent Liability

IOC is the defendant in a lawsuit by two Quebec Innu communities, claiming damages of \$900,000 relating to aboriginal rights and titles on the land where IOC operates. At this stage, IOC's management does not consider the risk of a material financial impact of this action to be probable.

7. Dividends to Shareholders

A regular dividend of \$0.25 and a special dividend of \$0.30 per common share, being an aggregate dividend of \$35,200, was declared by the Directors of the Corporation payable to shareholders of record on December 31, 2017 and paid on January 25, 2018.

Total dividends to shareholders as declared by the Directors of the Corporation in 2017 were \$169,600 or \$2.65 per share (2016 – \$64,000 or \$1.00 per share).

On March 8, 2018 dividends of \$0.35 per common share, comprised of a regular dividend of \$0.25 and a special dividend of \$0.10 per common share, for a total of \$22,400 were declared by the Directors of the Corporation payable to shareholders of record at the close of business on March 31, 2018 and to be paid on April 25, 2018.

8. Debt

The Corporation has a \$50,000 revolving senior secured credit facility to September 18, 2020 with provision for annual one-year extensions. The credit facility provides for various forms of advances at the option of the Corporation. Various interest options are available for these revolving credits and a standby fee is payable on the unadvanced portion of the facility. The facility is secured by an assignment of the Corporation's and Hollinger-Hanna's interests in the IOC common shares, the IOC royalty and commission interests, and other assets of the Corporation and requires that the Corporation maintain certain financial ratios.

As at December 31, 2017, no amount was drawn on the credit facility (2016 – nil) leaving \$50,000 available to provide for any investment in IOC or other Corporation requirements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

9. Income Taxes

The provision for income taxes in the statements of income and comprehensive income differs from the amount computed by applying the combined Canadian federal and provincial tax rate to the Corporation's income before income taxes. The reasons for the difference and the related tax effects are as follows:

	2017	2016
Income before income taxes	\$ 192,363	\$ 109,337
Income taxes at combined federal and provincial statutory tax rates of 30.0%	57,709	32,801
Increase (decrease) in income taxes resulting from:		
Undistributed equity earnings in investment in IOC	(11,145)	(3,708)
Equity earnings distributed as dividends	(11,507)	(2,268)
Deferred taxes	—	4,294 ⁽¹⁾
Other	22	45
Income tax expense	\$ 35,079	\$ 31,164

(1) Adjustment for increase in Newfoundland and Labrador corporate income tax rate by 1%, effective January 1, 2016.

The impact of the change in corporate tax rate was adjusted prospectively in 2016.

The deferred tax liability is comprised of the following:

	Opening Balance	Recognized in net income	Recognized in other comprehensive loss	Closing Balance
December 31, 2016				
Difference in tax and book value of assets	\$ 125,453	\$ 4,294	\$ 47	\$ 129,794
Tax benefit of deductible temporary differences	(783)	49	—	(734)
Net deferred income tax liability	\$ 124,670	\$ 4,343	\$ 47	\$ 129,060
December 31, 2017				
Difference in tax and book value of assets	\$ 129,794	\$ (2,273)	\$ 364	\$ 127,885
Tax benefit of deductible temporary differences	(734)	69	—	(665)
Net deferred income tax liability	\$ 129,060	\$ (2,204)	\$ 364	\$ 127,220

The deferred tax liability attributable to the difference in tax and book value of the IOC royalty and commission interests is \$77,708 (2016 – \$79,615). The deferred tax liability attributable to the difference in tax and book value of the investment in IOC is \$50,177 (2016 – \$50,179).

10. Share Capital

The Corporation's authorized share capital includes an unlimited number of common shares (64 million common shares issued and outstanding) having no par value as at December 31, 2017 and 2016.

The Corporation's net income per share represents both basic and diluted.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

11. Accumulated Other Comprehensive Loss

	Net actuarial gain (loss) on IOC's defined benefit plans (net of tax)
Balance, January 1, 2016	\$ (11,150)
Other comprehensive income, net of income tax expense of \$47	699
Balance, December 31, 2016	\$ (10,451)
Balance, January 1, 2017	\$ (10,451)
Other comprehensive income, net of income tax expense of \$364	2,060
Balance, December 31, 2017	\$ (8,391)

12. Capital Management

The Corporation's capital consists of the shareholders' equity and the undrawn revolving senior secured credit facility. The Directors are responsible for managing the investments and affairs of the Corporation, which consist mainly of the receipt of revenues from IOC and the payment of dividends to the shareholders, in a manner that retains sufficient liquidity to provide funds to protect its investment in IOC. The Corporation pays cash dividends of the net income to the maximum extent possible, subject to the maintenance of appropriate levels of working capital.

13. Fair Value of Financial Instruments

Fair value is the amount that willing parties would accept to exchange a financial instrument based on the current market for instruments with the same risk, principal and remaining maturity. The fair value of interest bearing financial assets and liabilities is determined by discounting the contractual principal and interest payments at estimated current market interest rates for the instrument.

The carrying value of amounts of cash, amounts receivable, accounts payable and dividends payable to shareholders approximate their fair value because of the short-term nature of these items.

Such fair value estimates are not necessarily indicative of the amounts that would be realized upon disposition of the Corporation's financial instruments.

14. Financial Instrument Risk Management

Commodity price risk

The Corporation is dependent on royalty income, commissions and dividends received from IOC. IOC's earnings and cash flows are affected by the volume of iron ore products sold, the price of those products, operating costs, and currency movements. The demand for and price of iron ore fluctuate as a result of numerous factors outside the control of the Corporation and IOC. Such factors include, but are not limited to, the demand for steel and steel products, global and regional demand, political and economic conditions, and production conditions and costs in major producing regions.

Based on gross royalties for the year ended December 31, 2017, an increase or decrease in sale price of iron ore by 5% with all other variables held constant could have an unfavourable or favourable impact of approximately \$4,400 (2016 – \$3,200), respectively, on net income.

Currency risk

The Corporation derives dividends and royalty income from IOC denominated in US dollars. From time to time the Corporation may enter into financial agreements with banks and other financial institutions to reduce the underlying risks associated with this

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

foreign currency denominated income. As at December 31, 2017 and 2016, there were no foreign exchange contracts outstanding.

Based on financial instrument balances as at December 31, 2017, a strengthening or weakening of the Canadian dollar to the U.S. dollar by 1% with all other variables held constant could have an unfavourable or favourable impact of approximately \$240 (2016 – \$200), respectively, on net income.

Based on gross royalties for the year ended December 31, 2017, a strengthening or weakening of the Canadian dollar to the U.S. dollar by 1% with all other variables held constant could have an unfavourable or favourable impact of approximately \$860 (2016 – \$500), respectively, on net income.

Liquidity risk

Liquidity risk is the risk of loss from not having access to sufficient funds to meet both expected and unexpected cash demands. The Corporation manages its exposure to liquidity risk through prudent management of its statement of financial position, including maintaining sufficient cash balances and access to undrawn credit facilities. Management monitors and reviews both actual and forecasted cash-flows.

As at December 31, 2017 the Corporation held \$40,498 in cash (2016 – \$23,937). All of the Corporation's financial liabilities are due within one year.

Credit risk

The Corporation is exposed to credit risk with respect to amounts receivable from IOC, with whom there is no history of credit losses or uncollectability. The Corporation is economically dependent on IOC. The Corporation maintains all of its cash with financial institutions having a minimum debt rating of A.

15. Key Management Personnel Compensation

Key management personnel are the President and Chief Executive Officer, the Secretary and Executive Vice President, the Executive Vice President, the Chief Financial Officer and directors. Their remuneration for the year ended December 31, 2017 was comprised of salaries totaling \$1,101 (2016 – \$1,085).

CORPORATE INFORMATION

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President and Chief Executive Officer

William J. Corcoran⁽¹⁾

Company Director

Mark J. Fuller⁽¹⁾

President and CEO of
Ontario Pension Board

Duncan N.R. Jackman⁽¹⁾

Chairman, President and CEO of
E-L Financial Corporation Limited

James C. McCartney

Company Director
Retired Partner, McCarthy Tétrault LLP

Sandra L. Rosch

President, Stonecrest Capital Inc.

John F. Tuer⁽¹⁾

Company Director

Patricia M. Volker⁽¹⁾

Company Director

Officers

William J. Corcoran

Non-Executive Chairman of the Board

William H. McNeil

President and Chief Executive Officer

James C. McCartney

Executive Vice President and Secretary

Sandra L. Rosch

Executive Vice President

Alan R. Thomas

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⁽¹⁾ Member of Audit, Nominating and
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