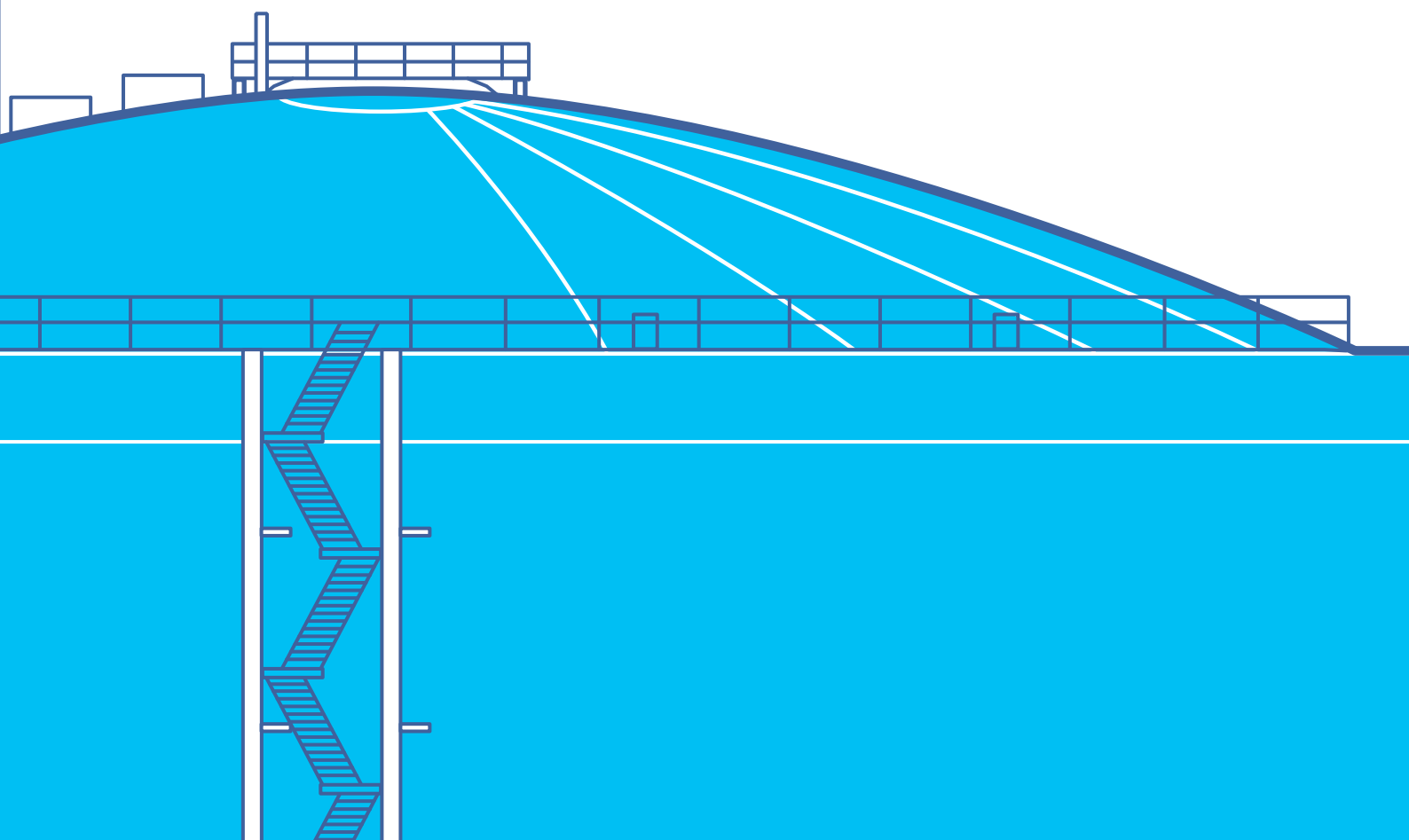


DELIVERING RESULTS 2016

Annual Report



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NOVATEK is one of the largest independent natural gas producers in Russia.

NOVATEK's main businesses are the exploration and production, processing, transportation and marketing of natural gas and liquid hydrocarbons.

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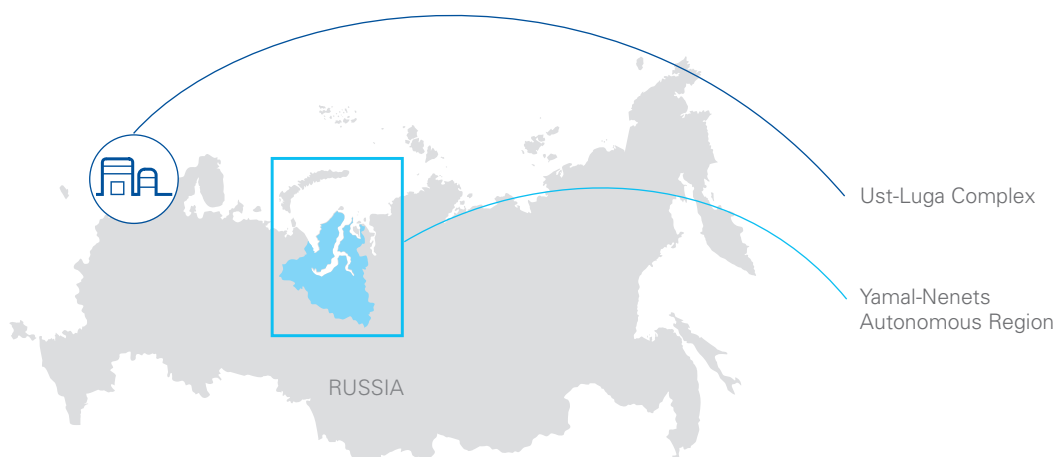
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Our production assets are located in the Yamal-Nenets Autonomous Region of the Russian Federation - one of the largest regions in the world in terms of gas reserves and production volumes.

We have a large conventional reserve base with high reserves concentration and high potential of new geological discoveries.

Our reserves allow us to maintain stable high growth rates of hydrocarbon production.



PRODUCTION

1. Yurkharovskoye field
2. East-Tarkosalinskoye field
3. Khancheyskoye field
4. Olimpiyskiy license area
5. Yumantilskiy license area
6. Samburgskiy license area
7. North-Urengoyenskoye field
8. North-Khancheyskoye field
9. Yaro-Yakhinskiy license area
10. Termokarstovoye field
11. Yarudeyskoye field

PROSPECTIVE FIELDS AND LICENSE AREAS

12. South-Tambeyskoye field
13. West-Yurkharovskoye field
14. Raduzhnoye field
15. West-Urengoyenskoye license area
16. North-Yubileynoye field
17. North-Russkiy license area
18. North-Russkoye field
19. Dorogovskoye field
20. Ukrainsko-Yubileynoye field
21. Malo-Yamalskoye field
22. West-Chaselskoye field
23. Yevo-Yakhinskoye field
24. North-Chaselskiy license area
25. Utrenneye field
26. Geofizicheskiy license area
27. North-Obskiy license area
28. East-Tambeyskiy license area
29. North-Tasiyskiy license area
30. East-Tazovskoye field
31. Trekhbugorniy license area
32. Nyakhartinskiy license area
33. Ladertoyskiy license area
34. Nyavuyahskiy license area
35. West-Solpatinskiy license area
36. North-Tanamskiy license area
37. Tanamskiy license area
38. Kharbeyskoye field
39. Syadorskiy license area



39

Fields and license areas



Purovsky Gas Condensate Processing Plant.
Key element in the production chain used for gas condensate stabilization.

— Gas condensate pipelines of NOVATEK.

LETTER TO SHAREHOLDERS



ALEXANDER NATALENKO
Chairman of NOVATEK's
Board of Directors



LEONID MIKHELSON
Chairman of NOVATEK's
Management Board



MARK GYETVAY
Deputy Chairman of NOVATEK's
Management Board

DELIVERING RESULTS UNDERSCORES OUR VALUE
CREATION MODEL TO OUR SHAREHOLDERS.
WE REACHED IMPORTANT MILESTONES
IN OUR FIRST INTERNATIONAL LNG PROJECT
AND CONTINUED DELIVERING POSITIVE
OPERATIONAL AND FINANCIAL RESULTS TO OUR
SHAREHOLDERS.

+37%

growth in liquid hydrocarbon
production

88%

completion rate on the first
LNG train

DEAR SHAREHOLDERS,

TWO THOUSAND AND SIXTEEN was another year of sustained growth in our operations and earnings despite the challenging macro-economic environment, the cyclicalities in global hydrocarbon prices and the high volatility in foreign exchange rates. We reached important milestones in our first international LNG project and continued delivering positive operational and financial results to our shareholders.

DELIVERING RESULTS underscores our value creation model to our shareholders. During the past year, total hydrocarbon production increased by 3% to 537 million barrels of oil equivalent (mmbbl), representing nine consecutive years of total hydrocarbon production growth. Driving this growth was the record level of liquids production of 12.4 million tons, an increase of 37%, allowing us to fully load our gas condensate processing facilities at Purovsky and Ust-Luga. The Yurdeyskoye crude oil field launched in the end of 2015 reached its full rated capacity and became the main source for NOVATEK's more than three-fold crude oil production growth for the year. We experienced a natural decline in our core gas production by 2.7%, but the next step forward in growing gas production is expected from the Yamal LNG project planned to come on stream in 2017.

YAMAL LNG REMAINS OUR FLAGSHIP PROJECT. At year-end 2016, construction of the plant's first LNG train was approximately 88% complete, which puts us on track to launch the project on schedule in 2017.

We have reached our main goal for 2016 - we successfully concluded the external financing package for Yamal LNG, achieving a very important milestone for the project. We spent a significant amount of time ensuring the timely completion of the external financing package and, accordingly, did not allow a single delay in financing and constructing the project. Loan agreements were signed with the Russian banks Sberbank and Gazprombank, China Development Bank and the Export-Import Bank of China, the Italian bank Intesa Sanpaolo with insurance coverage by the Italian export credit agency SACE and the French export credit agency COFACE, and with the Japan Bank for International Cooperation (JBIC). The

WE HAVE REACHED OUR MAIN GOAL FOR 2016 – WE SUCCESSFULLY CONCLUDED THE EXTERNAL FINANCING PACKAGE FOR YAMAL LNG, ACHIEVING A VERY IMPORTANT MILESTONE FOR THE PROJECT.

successful participation of international banks and export credit agencies demonstrates the global significance and world scale nature of the Yamal LNG project.

We also successfully closed the sale of a 9.9% equity stake in the Yamal LNG project to China's Silk Road Fund and reached the targeted shareholding structure with 50.1% stake owned by NOVATEK.

Significant progress was made in all areas of the project throughout the past year.

We continued our robust drilling at the South-Tambeyskoye field and completed 73 production wells, exceeding the well stock of 58 wells required for the plant's first LNG train. The main cryogenic heat exchanger for LNG train #1 was installed into the liquefaction module, and the remaining two other main cryogenic exchangers for LNG trains #2 and #3 were delivered to the construction site. All four cryogenic LNG tanks successfully passed hydro-testing, and the sea port ice protection barrier with the loading pipe rack and two shipping berths were under construction.

The first Arc7 ice-class vessel was put on water and fully equipped in 2016 and by year-end the LNG carrier successfully passed sea acceptance tests.

The growth in our liquids production remained the main driver of our financial results in 2016, as we increased the liquids share in our total production by 4 percentage points to 19%. The contribution from our liquid sales had a strong positive effect on our profitability. Our revenues increased by 13.1% to RR 537 bln and our normalized EBITDA increased by 13.2% to RR 242 bln. Based on the Company's financial results, the Board of Directors recommended to the General Meeting of Shareholders to approve dividends for 2016 at RR 13.9 per share, exceeding the dividend paid out for the previous year by 3%.



AT YEAR-END 2016, CONSTRUCTION OF THE PLANT'S FIRST LNG TRAIN WAS APPROXIMATELY 88% COMPLETE, WHICH PUTS US ON TRACK TO LAUNCH THE PROJECT ON SCHEDULE IN 2017.

As we delivered growth in our hydrocarbon production, we significantly decreased our capital expenditures, benefitting from the launches of several major fields in 2015. We increased our free cash flow by RR 57 bln, a record high for the Company, while our operating cash flow exceeded our capital expenditures by five times. The increased cash flow allows us to successfully repay outstanding debt, pay out dividends and invest into new prospective projects. In 2016, we fully repaid our five-year USD 600 million Eurobond at its maturity date.

We retained our core competitive advantage being ranked among the lowest cost hydrocarbon producers globally, and our lifting costs remained at a very low level of \$0.57 per BOE. We created shareholder value in a cyclical price environment whereas many international companies cut capital expenditures, laid off personnel and wrote down

significant oil and gas reserves. We remain fully committed to our strategy providing for strict cost control and conservative financial policies while maintaining the highest standards of corporate governance and sustainable development – DELIVERING RESULTS in challenging macro conditions.

For the past year, despite low hydrocarbon prices, we managed to achieve an organic reserve replacement ratio of 168% and recorded a reserve to production ratio of 24 years, a solid achievement among the global oil and gas companies. We are increasing our resource base having obtained the exploration rights for the Nyakhartinskiy, Ladertoyskiy, Nyavuyahskiy, West-Solpatinskiy, Syadorskiy, North-Tanamskiy and Tanamskiy license areas. The new license areas support our strategic objective aimed at expanding our resource base in the hydrocarbon rich Yamal and Gydan peninsulas as we actively study the region's geological potential for implementing future LNG projects. We also explore additional opportunities for supporting and expanding our hydrocarbons production in our current core production region.

We diversified our exploration activities in 2016 by signing a concession contract with

the Government of Montenegro for the exploration and production of hydrocarbons on four offshore blocks in the Adriatic Sea in partnership with Italian energy company, Eni.

Our prolific hydrocarbon resource base, the successful implementation of the Yamal LNG project and our experience in navigating the Northern Sea Route create a great platform for developing mutually beneficial cooperation in LNG projects. In 2016, we concluded Memorandums of Understanding with the Mitsubishi Corporation, Mitsui and Marubeni Corporation aimed at strategic cooperation for implementing LNG projects in Russia and supplying LNG and liquid hydrocarbons. We also signed a Memorandum of Understanding for Strategic Partnership with JBIC confirming the parties' intentions to cooperate in the implementation of NOVATEK's LNG projects, including financing and investment. We continue to consider opportunities of increasing our LNG production and supplying projects.

We successfully completed the first transformation stage of our business by evolving from a pure domestic gas business to production, processing and global marketing of liquid hydrocarbons. Now, we enter a new transformative stage with exciting prospects to grow the Company into a global player in the LNG market. We have achieved historically high growth rates and we aim to remain a growth company with the portfolio of exciting opportunities DELIVERING RESULTS and creating shareholder value.

Sustainable development practices remains at the forefront of our business. Our assets are located in the vulnerable and fragile environment of the Arctic region and we are strongly committed at preserving both the nature and traditional lifestyle of the indigenous minorities living in the areas where we operate. We also contribute to the development of the local societies by supporting education and sports programs as well as developing local infrastructure.

Environment protection and industrial safety remain our core focus helping us minimize environmental impact and achieve economic efficiencies by applying state-of-the art equipment and technologies.

One of our main sources of growth has always been and will always remain our highly qualified and dedicated team of professionals contributing their effort, know-how and energy into the implementation of our strategy to transform our business into a global LNG player. Our valued employees have a proven track record of DELIVERING RESULTS in a

ONE OF OUR MAIN SOURCES OF GROWTH HAS ALWAYS BEEN AND WILL ALWAYS REMAIN OUR HIGHLY QUALIFIED AND DEDICATED TEAM OF PROFESSIONALS CONTRIBUTING THEIR EFFORT, KNOW-HOW AND ENERGY INTO THE IMPLEMENTATION OF OUR STRATEGY TO TRANSFORM OUR BUSINESS INTO A GLOBAL LNG PLAYER.

sustainable manner despite challenging macro-economic environments. Their dedication and persistence is much appreciated.

On behalf of the Board of Directors and Management Board, we are pleased to present to our valued stakeholders the NOVATEK's 2016 Annual Report. We would like to thank everyone for your continued support, as we remain committed to growing our company in a new strategic direction while implementing best international practices and principles of sustainable development and corporate governance.

Kind regards,

ALEXANDER NATALENKO

Chairman of the Board of Directors



LEONID MIKHELSON

Chairman of the Management Board

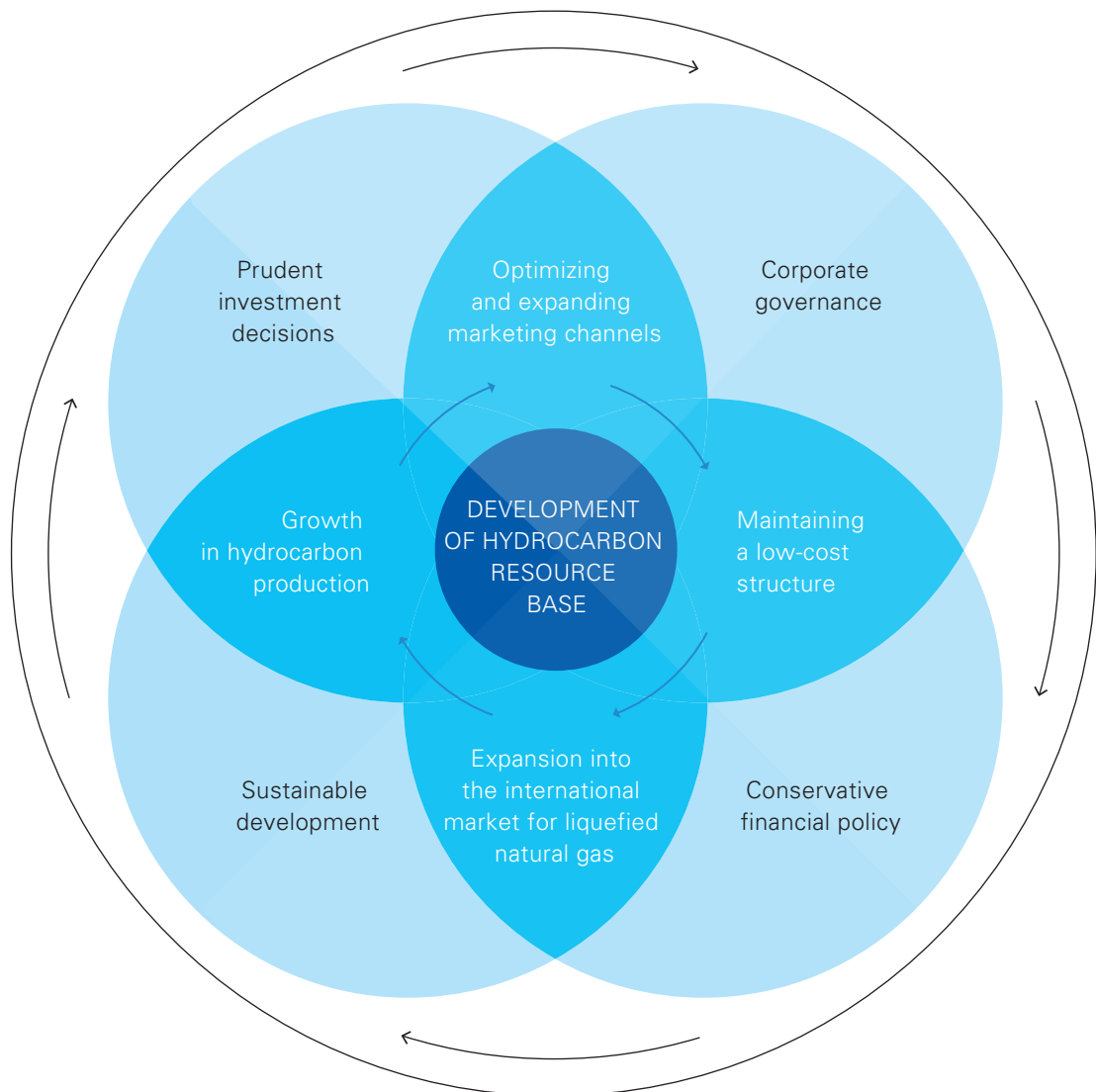


MARK GYETVAY

Deputy Chairman of the Management Board



STRATEGIC PRIORITIES



The Company has a number of key competitive advantages to successfully implement its strategy: the size and structure of its hydrocarbon resource base; the close proximity of existing infrastructure to core producing fields; a well-developed customer base for natural gas sales; its own facilities for gas condensate processing and product exports; and a well developed marketing channel for liquefied petroleum gas (LPG). Our high level of

operational flexibility and our consistent and efficient use of leading edge technologies in production and processing practices as well as our adherence to sound and prudent business management support our competitive position.

Our commitment to social responsibility and to observing the latest environmental, health and safety standards are integral parts of NOVATEK's development strategy.

KEY EVENTS AND ACHIEVEMENTS 2016

USD 19 bln



Finalization of external financing package for the Yamal LNG project for the total amount equivalent to USD 19 bln with participation of Russian and international banks, the National Welfare Fund of Russia and international export credit agencies.



Signing of Memorandums of Understanding with the Mitsubishi Corporation, Mitsui, Marubeni Corporation and PTT, and a Memorandum of Understanding for Strategic Partnership with the Japan Bank for International Cooperation (JBIC).

3.5 mmt



Obtaining the rights for the Nyakhartinskiy, Ladertoyskiy, Nyavuyahskiy, West-Solpatinskiy, Syadorskiy, North-Tanamskiy and Tanamskiy license areas as well as for the Kharbeyetskoye field.



Successfully reaching the Yarudeyskoye crude oil field's full production capacity of 3.5 mmt annualized and launching an associated petroleum gas treatment unit at the field.

9.9%



Closing of the sale of a 9.9% equity stake in the Yamal LNG project to China's Silk Road Fund.



Signing of a concession contract with the State of Montenegro for the exploration and production of hydrocarbons on four offshore blocks in the Adriatic.



Strategic partnership



LNG projects



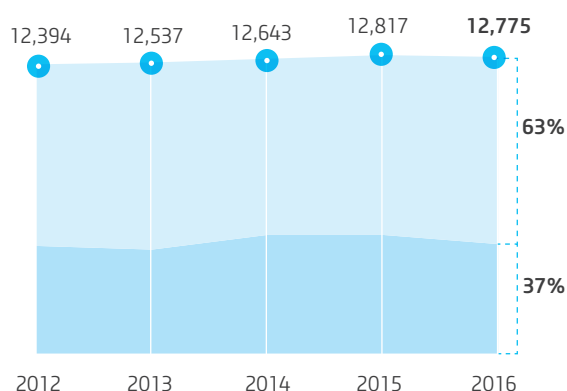
Development of the resource base and hydrocarbon production

KEY INDICATORS

	Unit	2015	2016	Change
FINANCIAL INDICATORS				
Total revenues	RR mln	475,325	537,472	13.1%
Normalized profit from operations ¹	RR mln	139,741	152,194	8.9%
Normalized EBITDA (including share in EBITDA of JVs) ¹	RR mln	214,189	242,407	13.2%
Profit attributable to shareholders of PAO NOVATEK	RR mln	74,396	257,795	246.5%
Earnings per share, basic and diluted	RR	24.63	85.41	246.8%
Net cash provided by operating activities	RR mln	132,864	173,791	30.8%
Net cash used for capital expenditures ²	RR mln	50,584	34,413	(32.0%)
Free cash flow	RR mln	82,280	139,378	69.4%
OPERATING INDICATORS				
Proved natural gas reserves (SEC)	bcm	1,775	1,755	(1.1%)
Proved liquid hydrocarbon reserves (SEC)	mmt	143	152	6.3%
Total hydrocarbon reserves (SEC)	mmboe	12,817	12,775	(0.3%)
Total hydrocarbon reserves excluding the effect of sale of 9.9% stake in Yamal LNG	mmboe	12,817	13,182	2.8%
Marketable production of natural gas	bcm	67.9	66.1	(2.7%)
Marketable production of liquid hydrocarbons	mt	9,094	12,441	36.8%
Total marketable production	mmboe	521.6	537.0	3.0%
POSITIONS IN RUSSIA				
Share in natural gas production	%	10.8%	10.5%	(0.3) p.p.
Share in liquid hydrocarbon production	%	1.7%	2.3%	0.6 p.p.

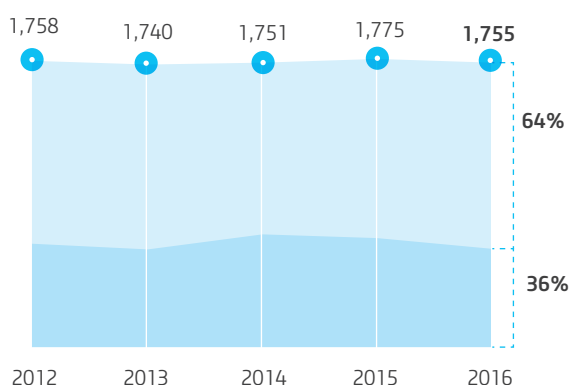
¹ Adjusted for the effect on disposal of interests in joint ventures.

² Cash used for capital expenditures represents purchases of property, plant and equipment, materials for construction and capitalized interest paid per Consolidated Statement of Cash Flows net of payments for mineral licenses and acquisition of subsidiaries.



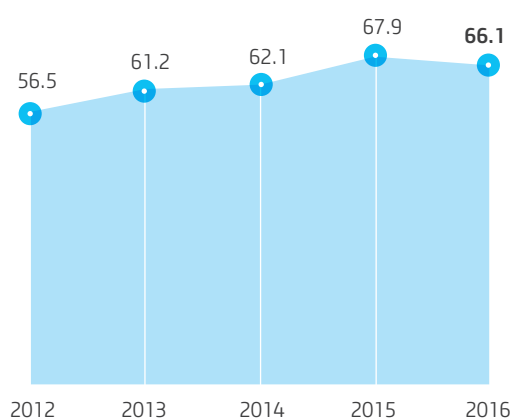
■ Proved developed
■ Proved undeveloped

↑ Total proved hydrocarbon reserves (SEC), mmbbl

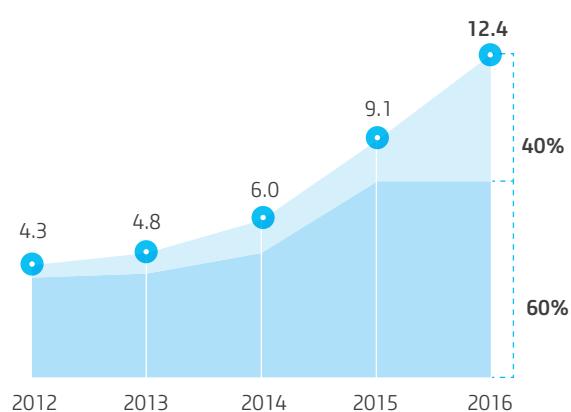


■ Proved developed
■ Proved undeveloped

↑ Proved natural gas reserves (SEC), bcm

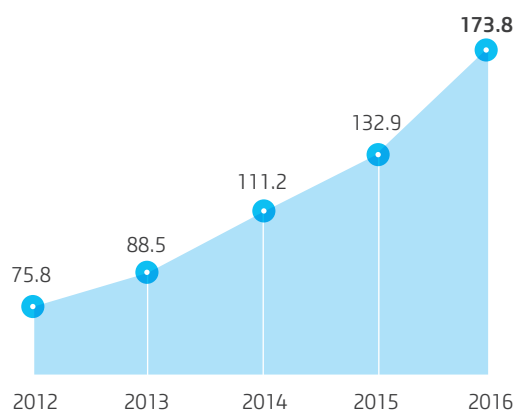


↑ Marketable natural gas production, bcm

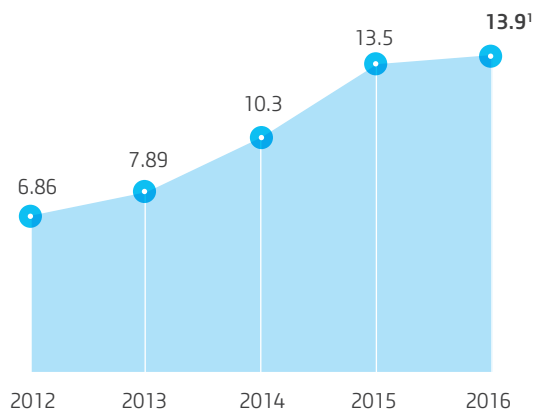


■ Crude oil
■ Gas condensate

↑ Marketable liquids production, mmt



↑ Operating cash flow, RUB bln



↑ Dividends per share, RUB

¹ Recommendation of the Board of Directors.

DELIVERING RESULTS

YAMAL LNG PROJECT

Photo: the LNG plant construction site.



88%
COMPLETION RATE
OF THE FIRST
LNG TRAIN AS
OF YEAR-END 2016



LNG MODULES INSTALLATION

In 2016 we significantly sped up the construction progress as the LNG modules constructed on contractor's shipyards were being delivered and installed.

78

 modules

All of the first train LNG modules were installed on the prepared foundations

22,000

workers on the construction site by year-end 2016

Photo: installation of the main cryogenic heat exchanger for train #1.





CONSTRUCTION OF THE SHIPMENT INFRASTRUCTURE

A two (2) km ice barrier was being constructed to protect the port harbor. LNG and stable gas condensate shipment pipe rack with shipping berths was being built at the ice barrier.

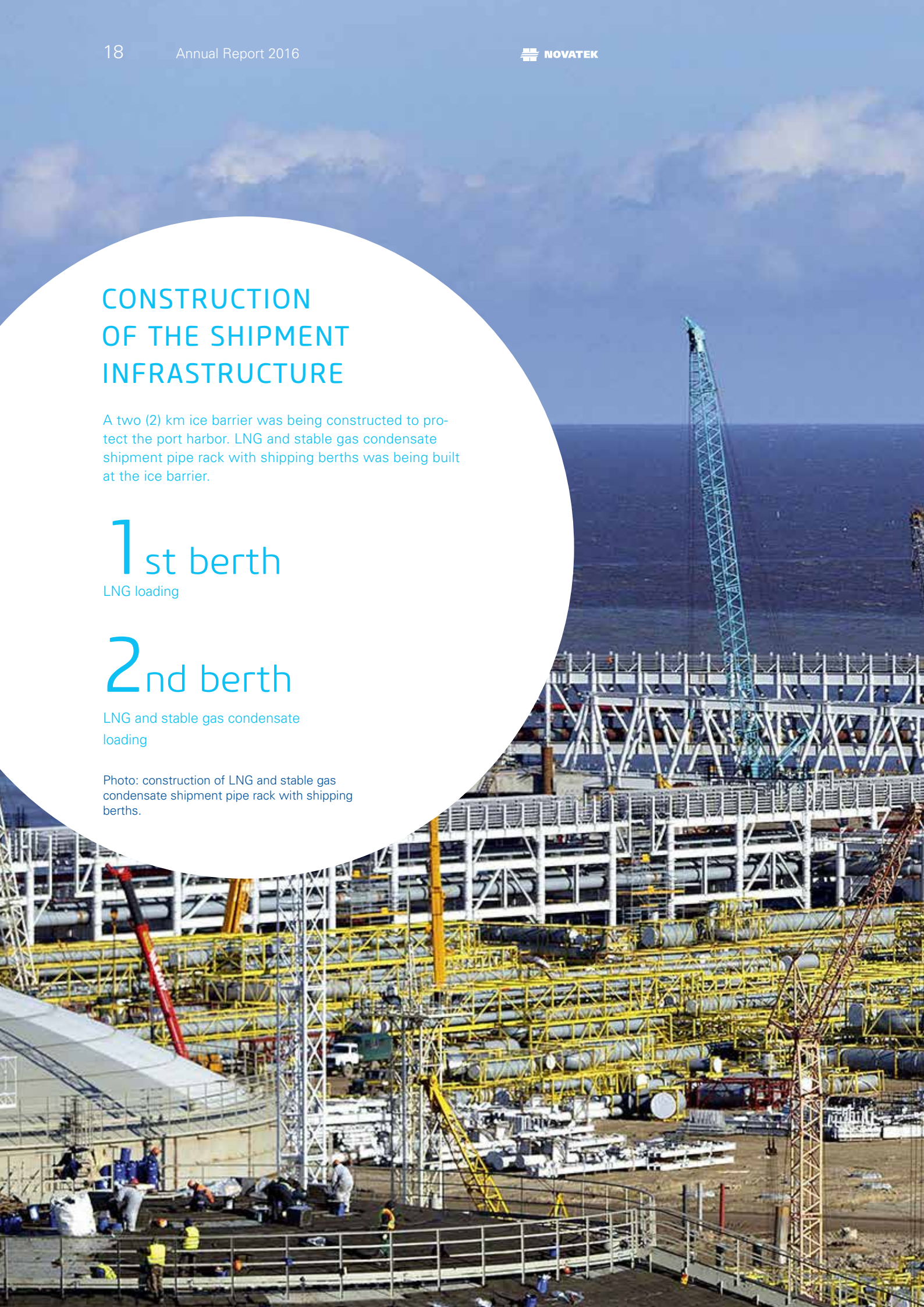
1st berth

LNG loading

2nd berth

LNG and stable gas condensate
loading

Photo: construction of LNG and stable gas
condensate shipment pipe rack with shipping
berths.





FIRST ARC7 LNG TANKER

The first Arc7 ice-class LNG carrier was placed from dry-dock into water and by year-end it successfully passed sea acceptance tests.

170,000 cm

the LNG tanker capacity

19.5 knots

The speed is 19.5 knots in open water and 7.2 knots in ice 1.5 m thick

Photo: the first Arc7 LNG tanker.





YAMAL LNG PROJECT

At year-end the construction progress on the first train was 88% and the construction progress of all three trains — 75%.

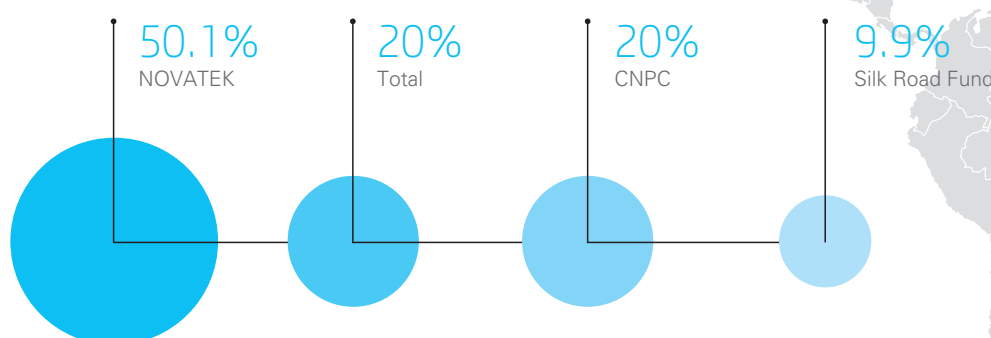
942 bcm

of natural gas

31 mmt

of liquid hydrocarbons

↑ Proved and probable reserves of the South-Tambeyskoye field under PRMS as of 31.12.16



↑ Shareholders of Yamal LNG as of 31.12.16

Yamal LNG is the flagship project in NOVATEK asset portfolio and is considered a transformational move for the Company into the international gas market. Yamal LNG envisages the construction of an LNG liquefaction plant with annual capacity of 16.5 million tons per annum, utilizing the prolific feedstock resources of the South-Tambeyskoye field located in the Northeast of the Yamal Peninsula. The launch of the first LNG train is planned for 2017.

As of 31 December 2016, the field was estimated to contain 607 bcm of proved natural gas reserves and 18 mmt of proved liquid

hydrocarbon reserves, under the SEC reserves methodology. In 2016 the production drilling results allowed us to increase the proved natural gas SEC reserves at the South-Tambeyskoye field by 85 bcm compared to year-end 2015. Based on total proved hydrocarbon reserves, the South-Tambeyskoye field is the largest field in NOVATEK reserves portfolio. According to the PRMS reserves standards, the proved and probable reserves of the South-Tambeyskoye field were appraised at 942 billion cubic meters of natural gas and 31 mmt of liquid hydrocarbons.



At year-end the construction progress on the first train was 88% and the construction progress of all three trains - 75%. The project's infrastructure includes the sea port, the international airport, automobile roads, power lines, gas gathering lines and the living quarters.

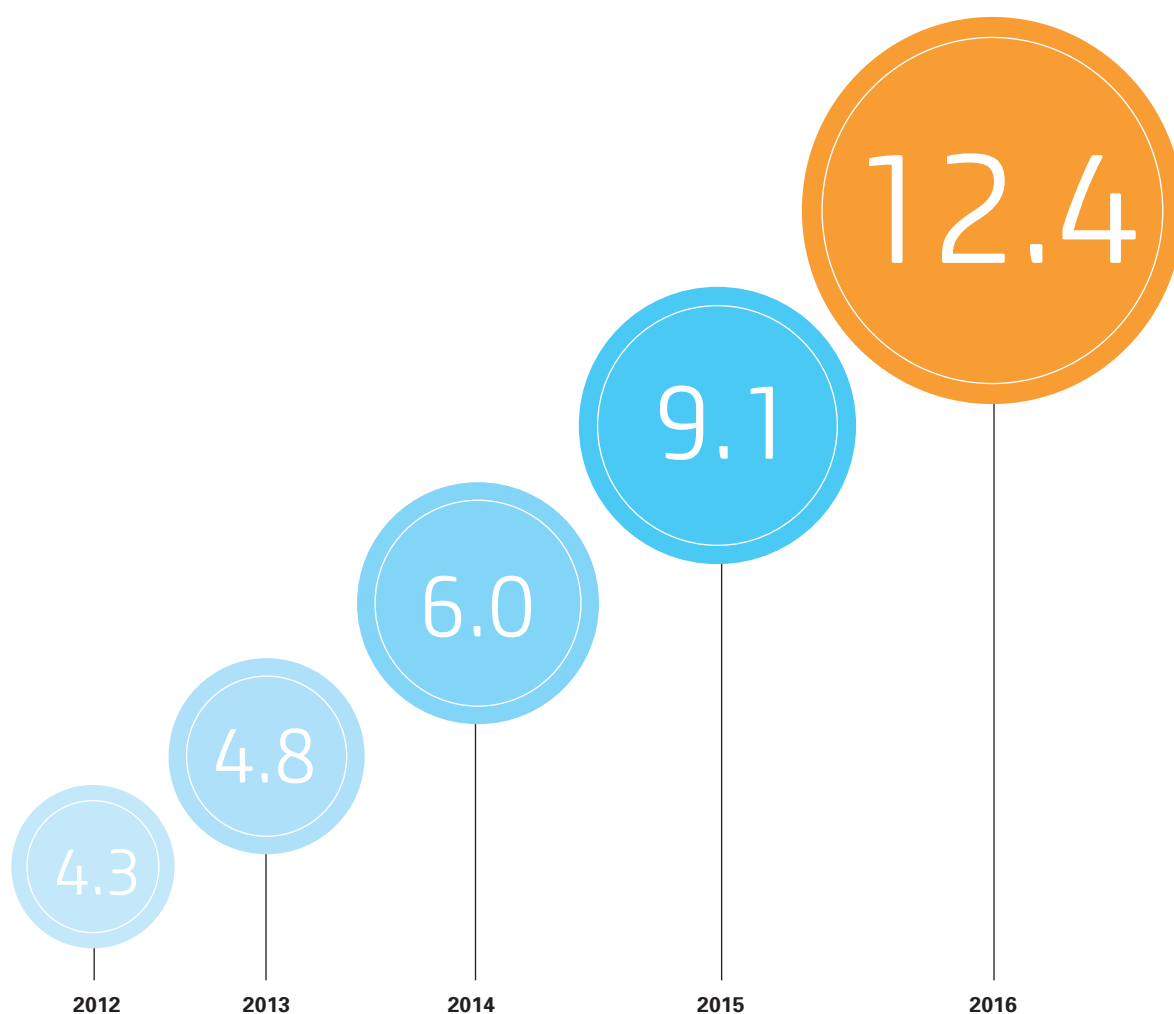
As of 31 December 2016, all the first train LNG modules were installed on the prepared foundations, and hook up was underway. The main cryogenic heat exchanger for LNG train #1 was installed into the liquefaction module. Compressor equipment for the first train and the backup heater were installed on the

foundations, as well as over 67,500 tons of steel work for pipe racks.

More than 95% of the LNG plant output has been contracted on a long-term basis. Specially designed Arc7 ice-class LNG carriers will be used for LNG transportation, and the first tanker was placed from dry-dock into water in early 2016, fully equipped and by year-end the LNG carrier successfully passed sea acceptance tests. As of year-end 2016, five (5) other LNG carriers and the two (2) Arc7 condensate tankers to be chartered by the project were under construction.

RECORD GROWTH OF LIQUID HYDROCARBON PRODUCTION

Marketable production of liquids increased by 37% as compared with 2015. Our growth in liquids production was mainly due to the launch of the Yarudeyskoye crude oil field ramped up to its full capacity of 3.5 mmt per annum.

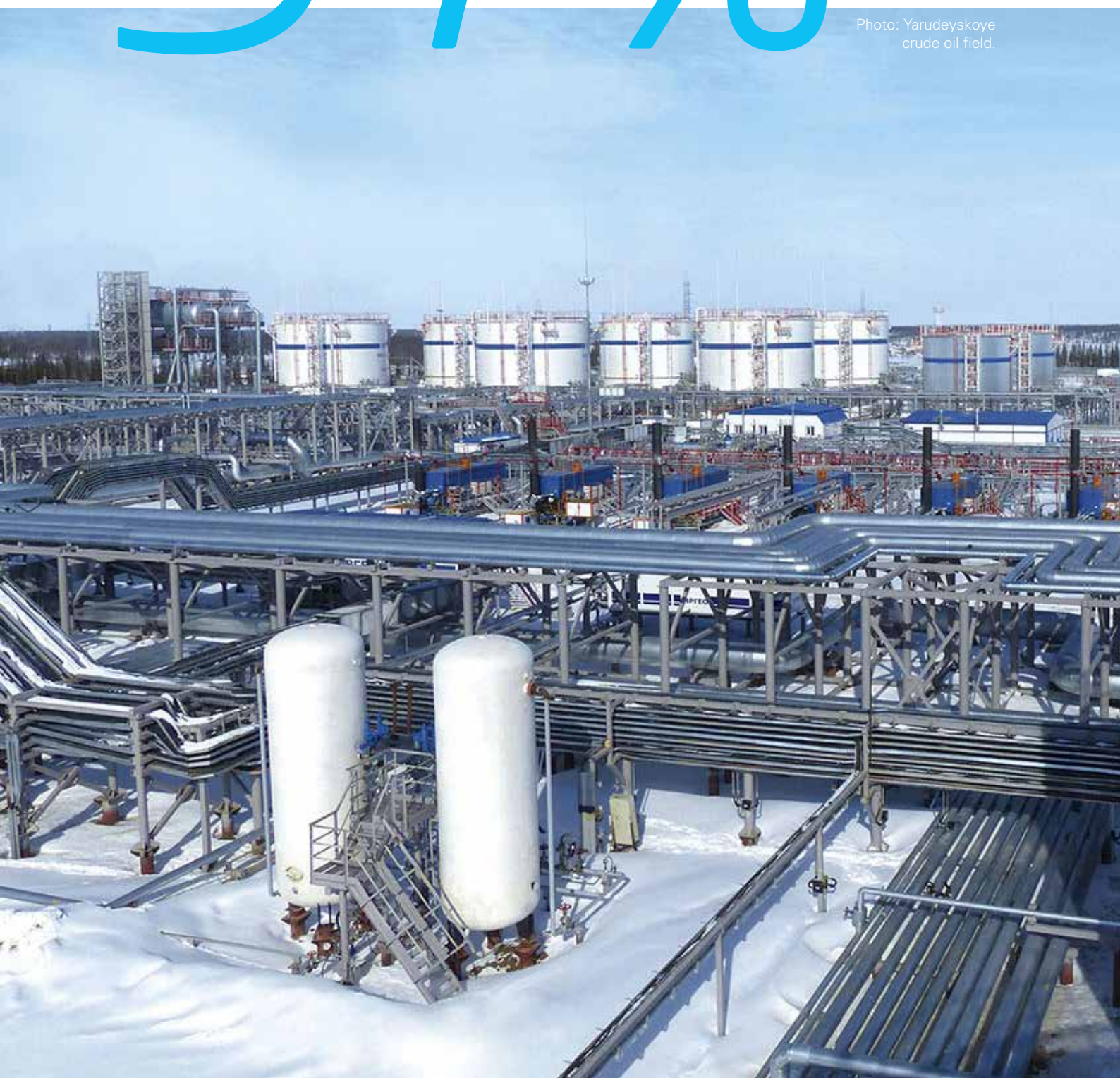


↑ Marketable production of liquid hydrocarbons, mmt

37%

MARKETABLE PRODUCTION
OF LIQUIDS INCREASED
BY 37% AS COMPARED
WITH 2015

Photo: Yarudeyskoye
crude oil field.





SUCCESSFUL GEOLOGICAL EXPLORATION

9 deposits

Nine (9) new gas condensate deposits were discovered at the Utrenneye, South-Tambeyskoye and Yevo-Yakhinskoye fields

10.2

thousand meters of exploration drilling

Photo: exploration well at the Utrenneye field on the Gydan Peninsula.

GEOLOGICAL EXPLORATION AND PRODUCTION

The Yamal-Nenets Autonomous District of Russia where our producing assets are located accounts for approximately 80% of Russian and 16% of global natural gas production.

As of 31 December 2016, NOVATEK's SEC proved reserves, including the Company's proportionate share in joint ventures, aggregated 12,775 million barrels of oil equivalent (boe), including 1,755 billion cubic meters (bcm) of natural gas and 152 million metric tons (mmt) of liquid hydrocarbons.

Excluding the decrease in the Company's proportional share in the Yamal LNG joint venture, total proved reserves increased by 2.8% year-on-year, with an organic reserve replacement rate of 168% due to successful exploration works and drilling, which amounted to reserves addition of 902 million boe, inclusive of 2016 production. The primary contributors to reserves additions were the Utrenneye, the South-Tambeyskoye, the Kharbeyskoye, the Dorogovskoye and the Yarudeyskoye fields.

At year-end 2016, the Company's reserve to production ratio (or R/P ratio) was 24 years.

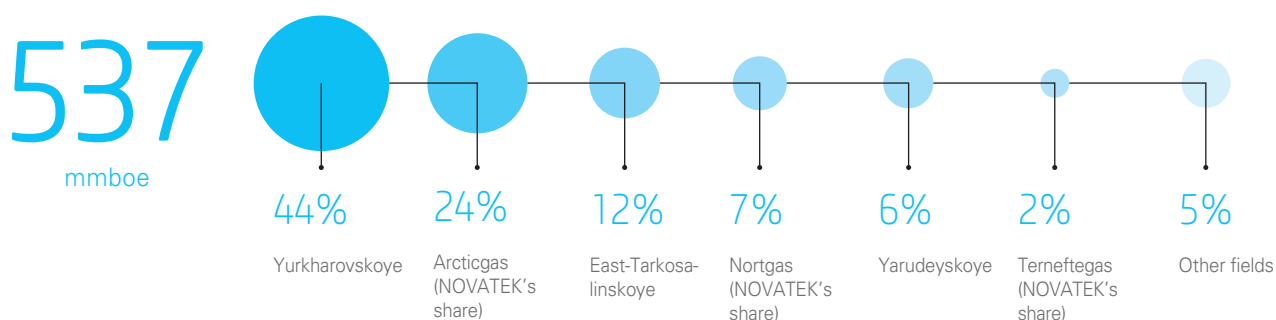
In 2016, we continued full-scale exploration works at our license areas located on the Gydan Peninsula and offshore in the Gulf of Ob to properly assess the resource potential of this strategically important region. We carried out three-dimensional (3D) seismic studies at the North-Obskiy offshore license area and also completed drilling of an exploration well at

the Utrenneye field. In total we have drilled five exploration wells at the Utrenneye field in 2014 to 2016, and the well testing results allowed us to increase the appraised reserves volumes and confirm higher well flows at the field.

Exploration activities also continued at the fields and license areas in the Nadym-Purtaz region. Seismic studies were done at the Yarudeyskoye field and the North-Russkiy and Dorogovskiy license areas while exploration drilling was performed at the Kharbeyskoye, West-Yurkharovskoye and Yevo-Yakhinskoye fields.

In 2016, NOVATEK carried out commercial hydrocarbon production at 13 fields. Marketable production from all fields (including the Company's share in production of joint ventures) amounted to 537.0 mmboe, representing an increase of 3.0% over the prior year.

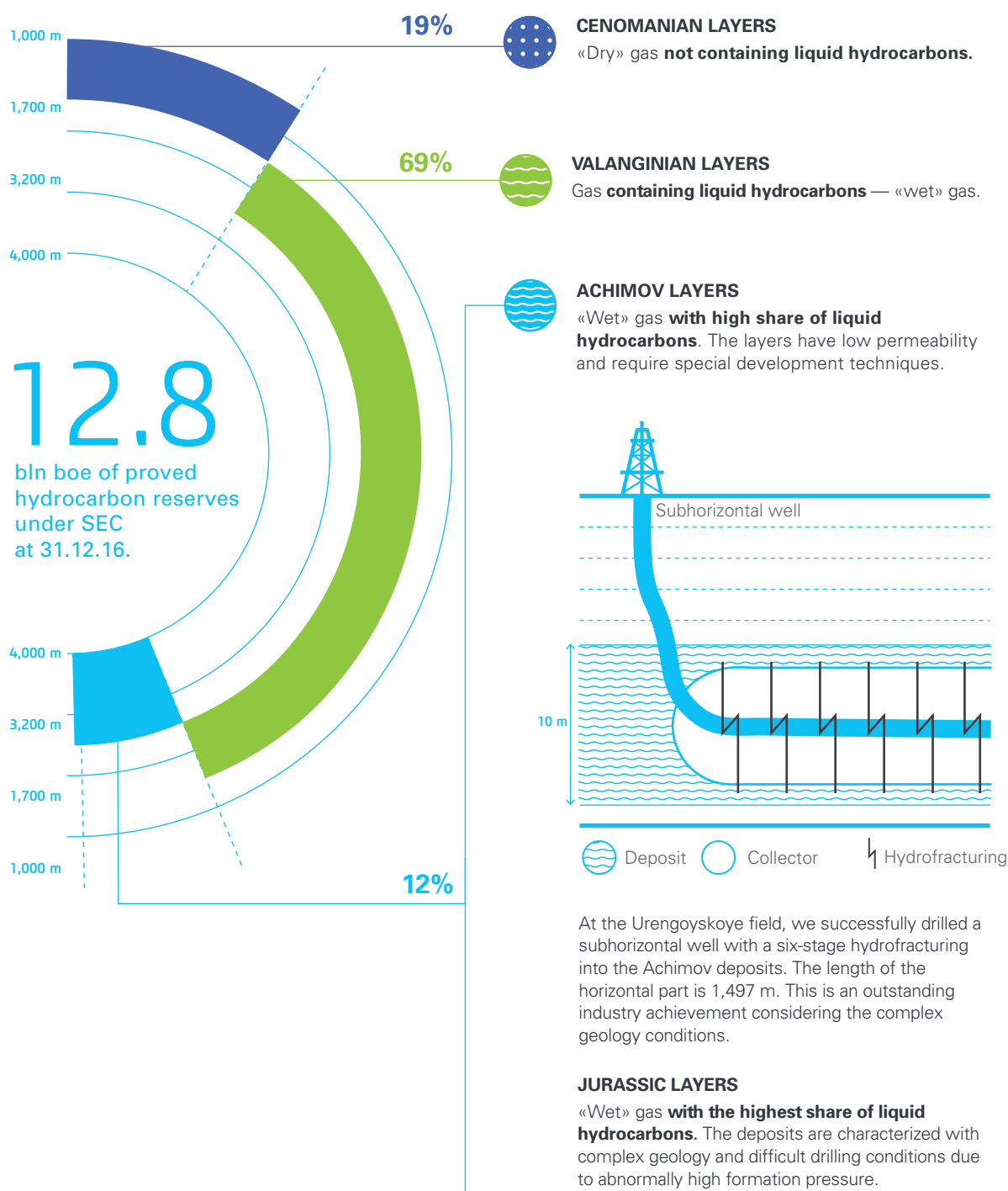
Total marketable production of natural gas including the Company's share in production of joint ventures aggregated 66.10 bcm, representing 80.5% of our total hydrocarbon output. Marketable production of liquid hydrocarbons including the Company's share in production of joint ventures totalled a record 12,441 thousand tons, of which 60.5% was unstable de-ethanized gas condensate and the remaining 39.5% consisted of crude oil.



USD 2.3 24

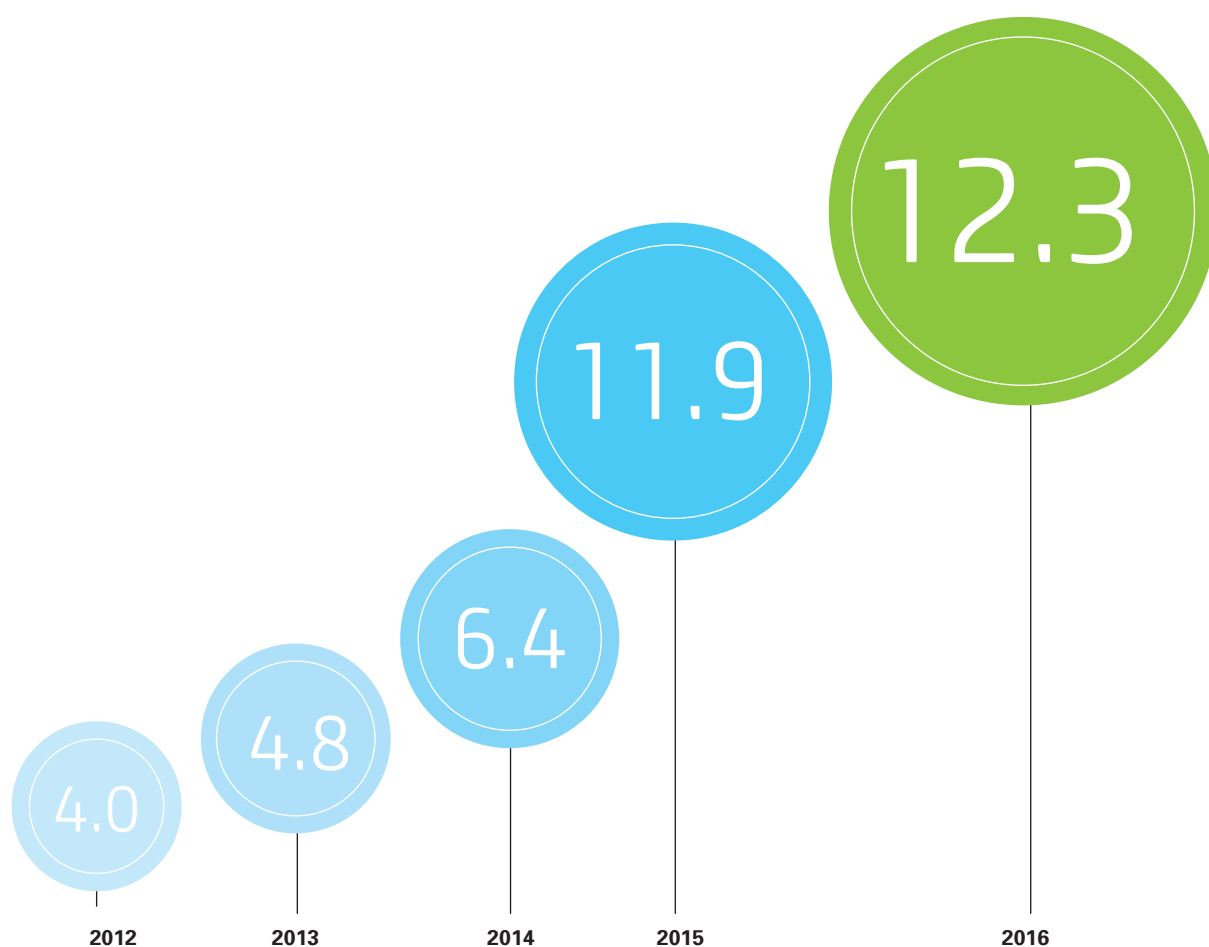
per boe — 2012-2016 reserve
replacement costs

years — reserve to production
ratio at year-end 2016



LOADING OUR PROCESSING CAPACITIES

Utilization of our integrated value-added chain for gas condensate allows us to maximize the economic effect for the Company and is one of our priorities. The Purovsky Plant's processing capacity matches the overall gas condensate production capacity of the Company's fields in operation.



↑ Output of the Purovsky Plant, mmt

12.3

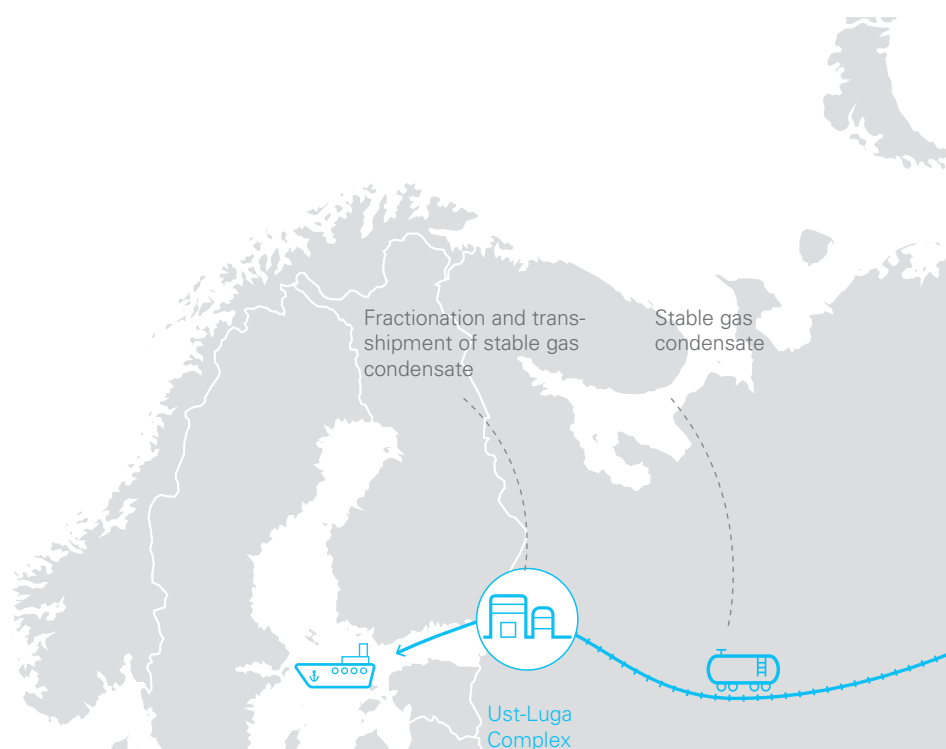
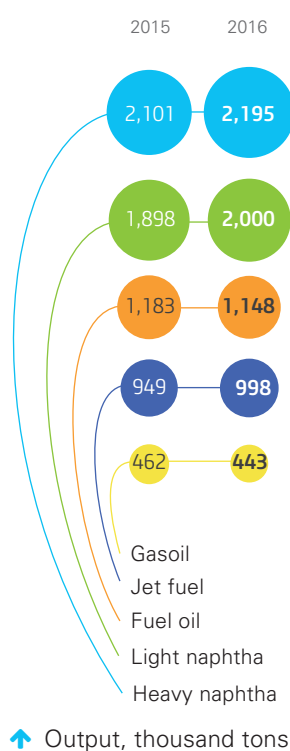
MILLION TONS —
OUTPUT OF THE
PUROVSKY PLANT
IN 2016

Photo: Purovsky Plant.



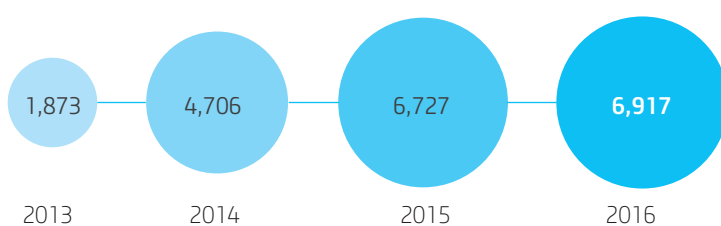
UST-LUGA COMPLEX

High value-added petroleum products produced at the Ust-Luga Complex have a significant positive impact on the profitability of our liquid hydrocarbon sales and the Company's cash flow generation.



The Gas Condensate Fractionation and Transshipment Complex located at the port of Ust-Luga on the Baltic Sea processes stable gas condensate into high value-added products like light and heavy naphtha, jet fuel, fuel oil and gasoil. Finished products are shipped to

international markets and stable gas condensate is transhipped to exports. The Complex expands our vertically integrated chain, positively impacts the unit profitability of our liquids sales, widens the variety of products and allows to diversify our customer base.

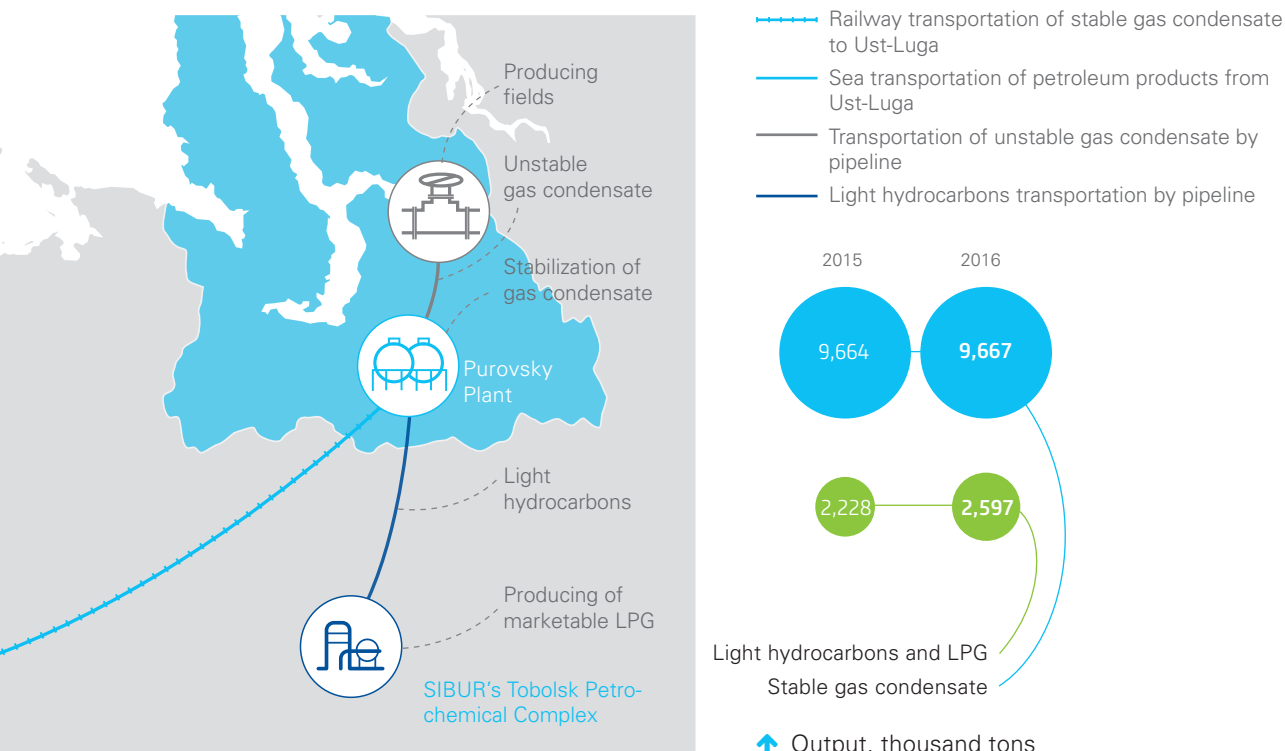


↑ Stable gas condensate processing volumes, thousand tons

+3%
stable gas condensate
processing volumes increase
in 2016

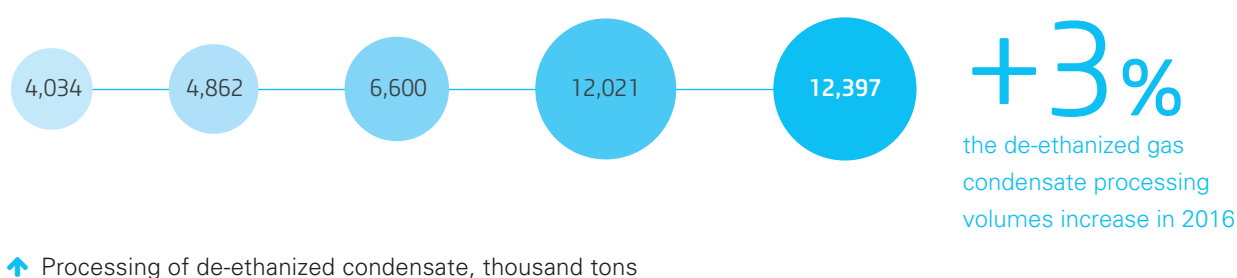
PUROVSKY PLANT

After being separated and de-ethanized at the field the unstable (de-ethanized) gas condensate is delivered via a system of condensate pipelines owned and operated by the Company for further stabilization at our Purovsky Plant.



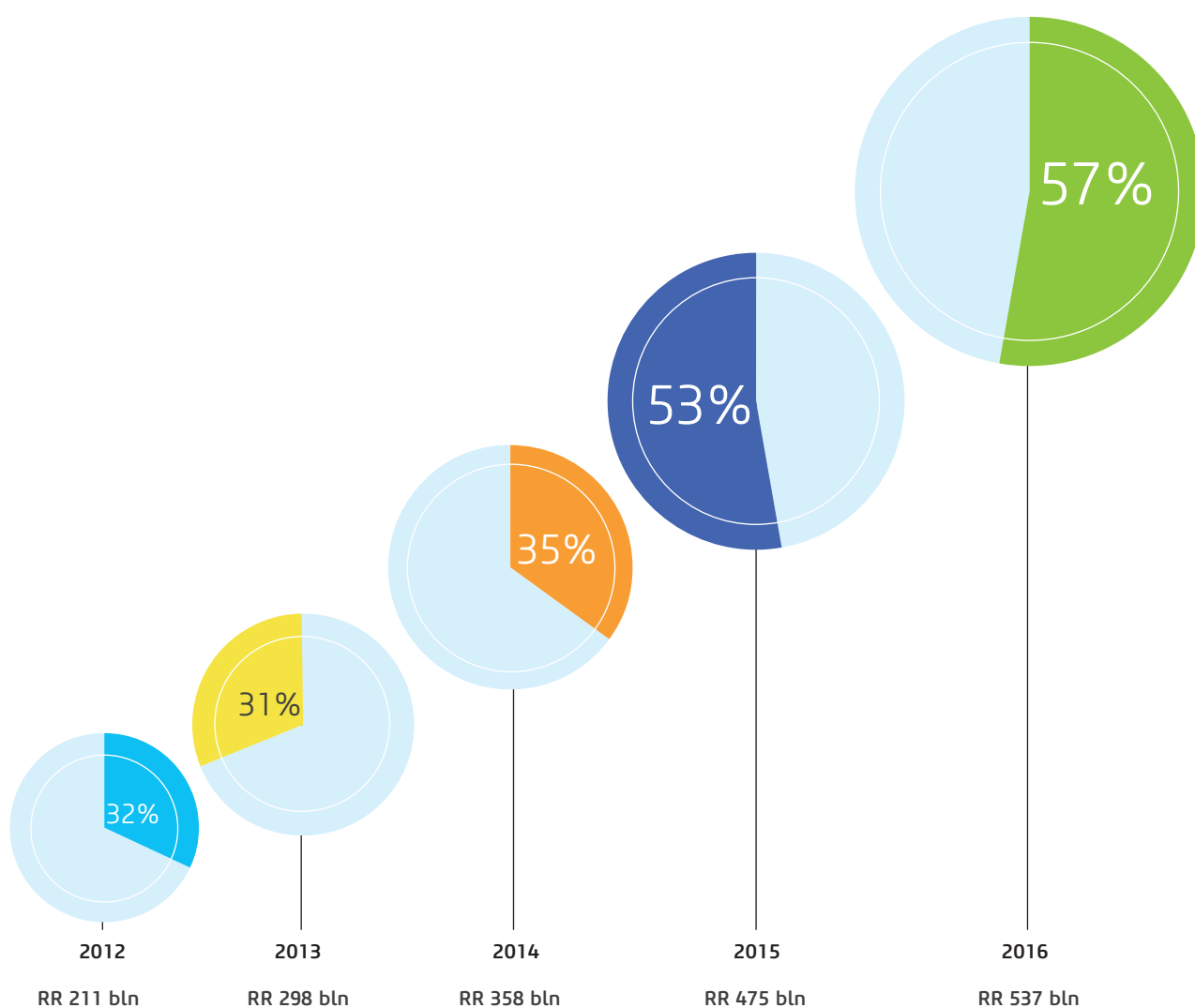
The Purovsky Plant is the integral element in our vertically-integrated production value chain that enables us to process all the volumes of de-ethanized gas condensate produced at our field into stable gas condensate and light hydrocarbons (feedstock for LPG production).

Most of the stable gas condensate volumes are delivered by rail to the Ust-Luga Complex for further processing, light hydrocarbons are delivered by pipeline to SIBUR's Tobolsk Petrochemical Complex for further processing.



GROWTH OF LIQUID HYDROCARBONS SHARE IN REVENUES

The share of liquid hydrocarbons in total production increased by 4 p.p. to 19%, while their share in total revenues increased to 57%, compared to 53% in 2015.



↑ Total revenues, including liquids share

31%

INCREASE OF LIQUIDS
SALES VOLUMES
IN 2016



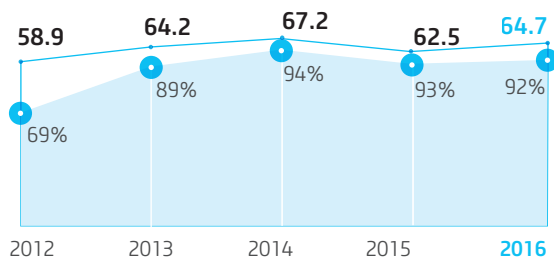
Photo: loading berth
at the Ust-Luga Complex.

NATURAL GAS SALES

NOVATEK plays an important role in ensuring supplies of natural gas to the Russian domestic market. During the past year, we supplied natural gas to 35 gas consuming regions of the Russian Federation.

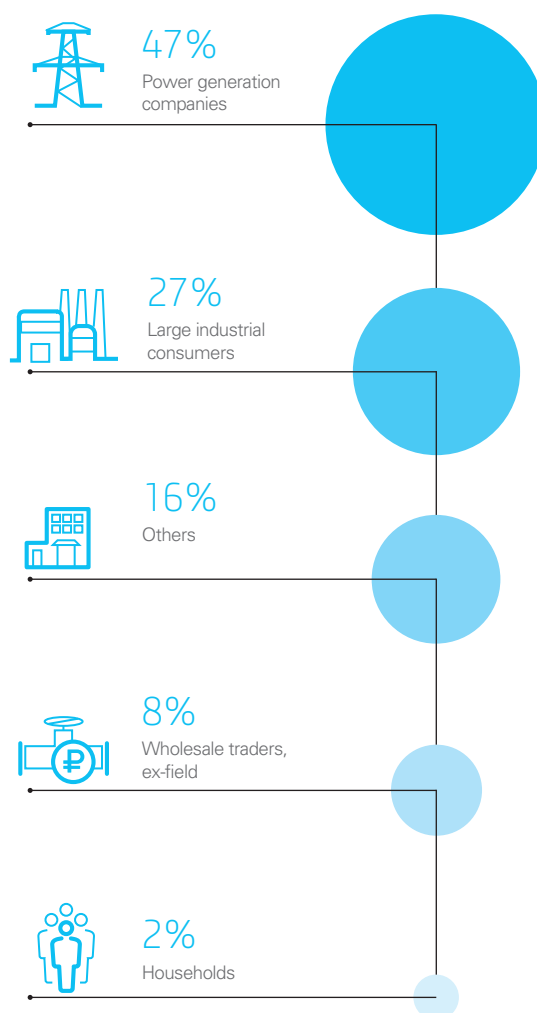
NOVATEK's 2016 natural gas sales volumes totalled 64.7 bcm, representing an increase of 3.6% as compared to 2015 sales volumes of 62.5 bcm. The sales volumes growth was a result of restoring sales to one of our major customers who did not take full contracted volumes in 2015 due to technical reasons, as well as sales of additional natural gas volumes to our end-customers and wholesale traders. The proportional share of natural gas sales to end-customers remained practically unchanged compared to 2015 and amounted to 92.2% of our total natural gas sales mix.

Our revenues from natural gas sales totalled RR 229.7 billion, which is 3.4% higher as compared to 2015. The sales volumes growth was the main driver for the growth in natural gas revenues.



■ Share of end customers

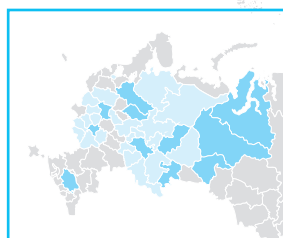
↑ Natural gas sales, bcm



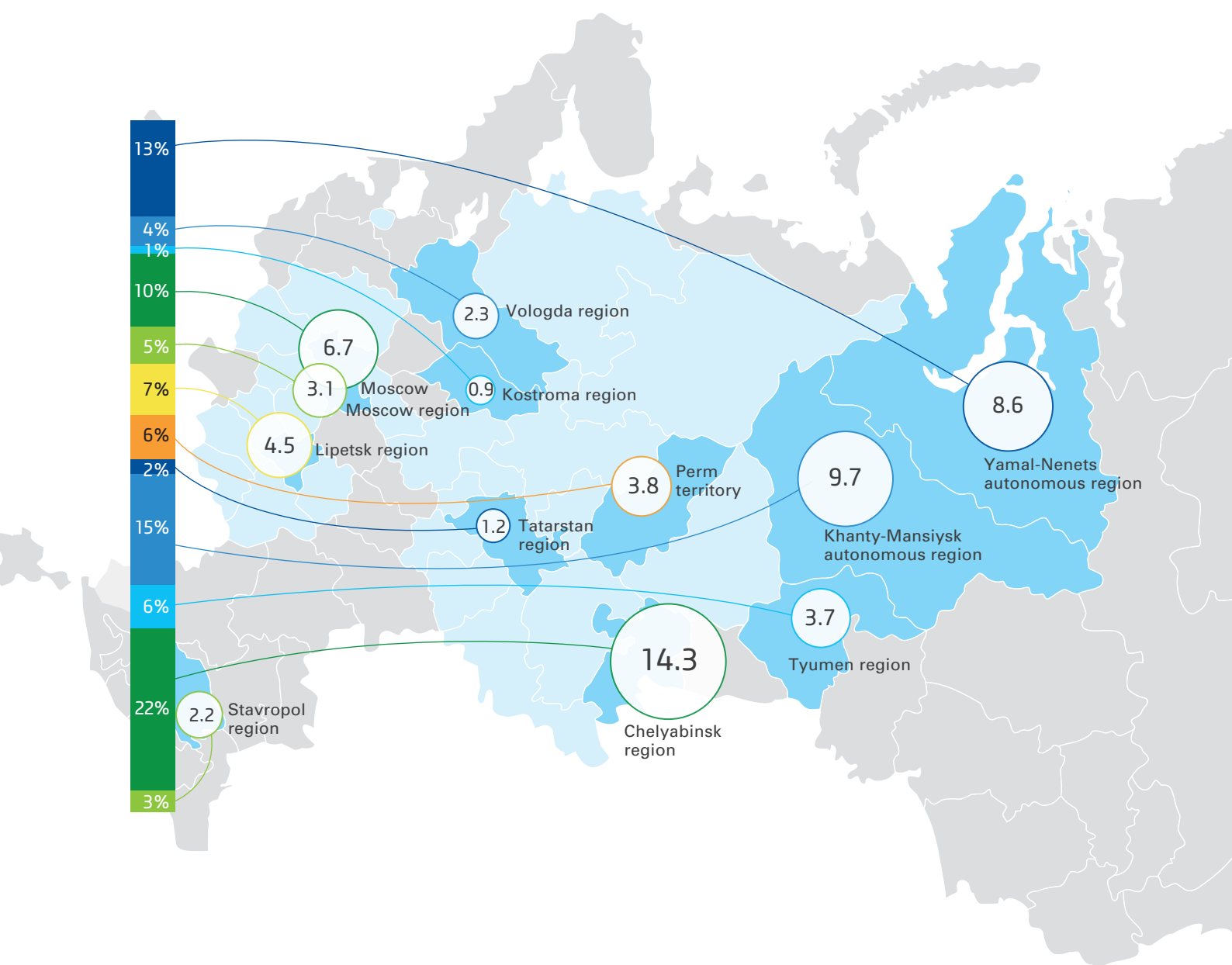
↑ Natural gas sales breakdown by customers in 2016

64.7 bcm

natural gas sales volumes in 2016



RUSSIA



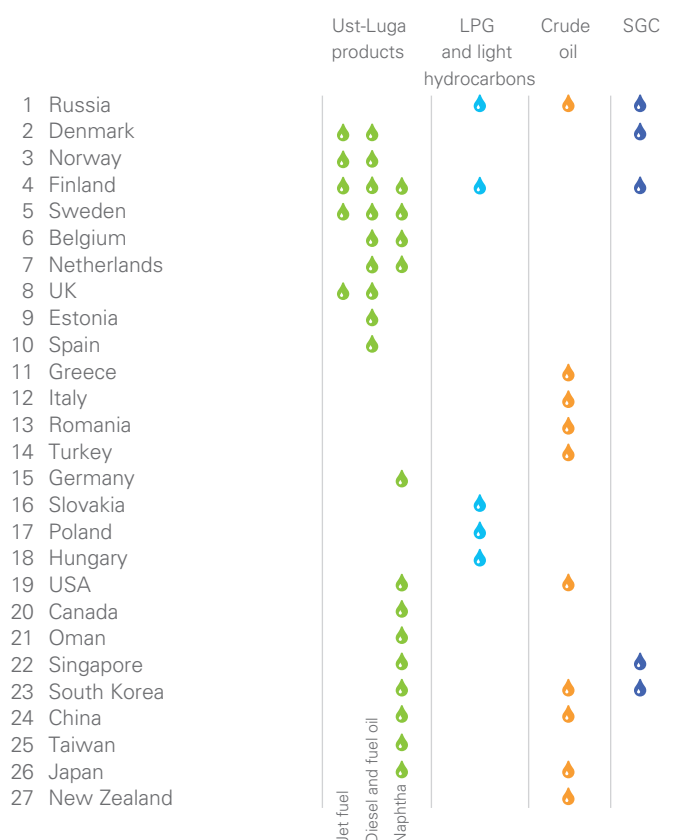
LIQUIDS SALES

NOVATEK sells liquid hydrocarbons (stable gas condensate, petroleum products, light hydrocarbons, LPG and crude oil) domestically and internationally.

Total sales volumes of liquid hydrocarbons in 2016 aggregated 16,850 thousand tons, representing a 30.7% increase over 2015 volumes. The growth is mainly due to increase in crude oil production. Our export sales of liquids grew by 9.6% year-on-year to 9,869 thousand tons.

High value-added petroleum products from the Ust-Luga Complex accounted for 40% share of our overall liquids sales volumes.

Export sales of stable gas condensate continued in 2016 as we reached full capacity utilization at the Ust-Luga Complex.

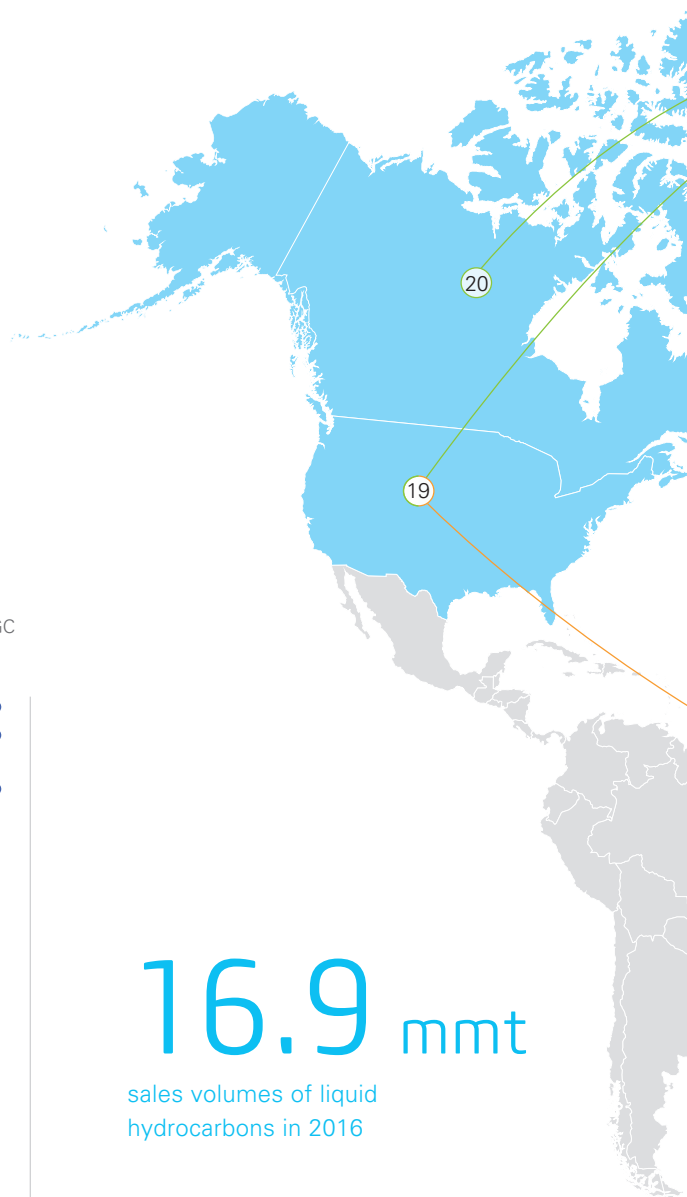


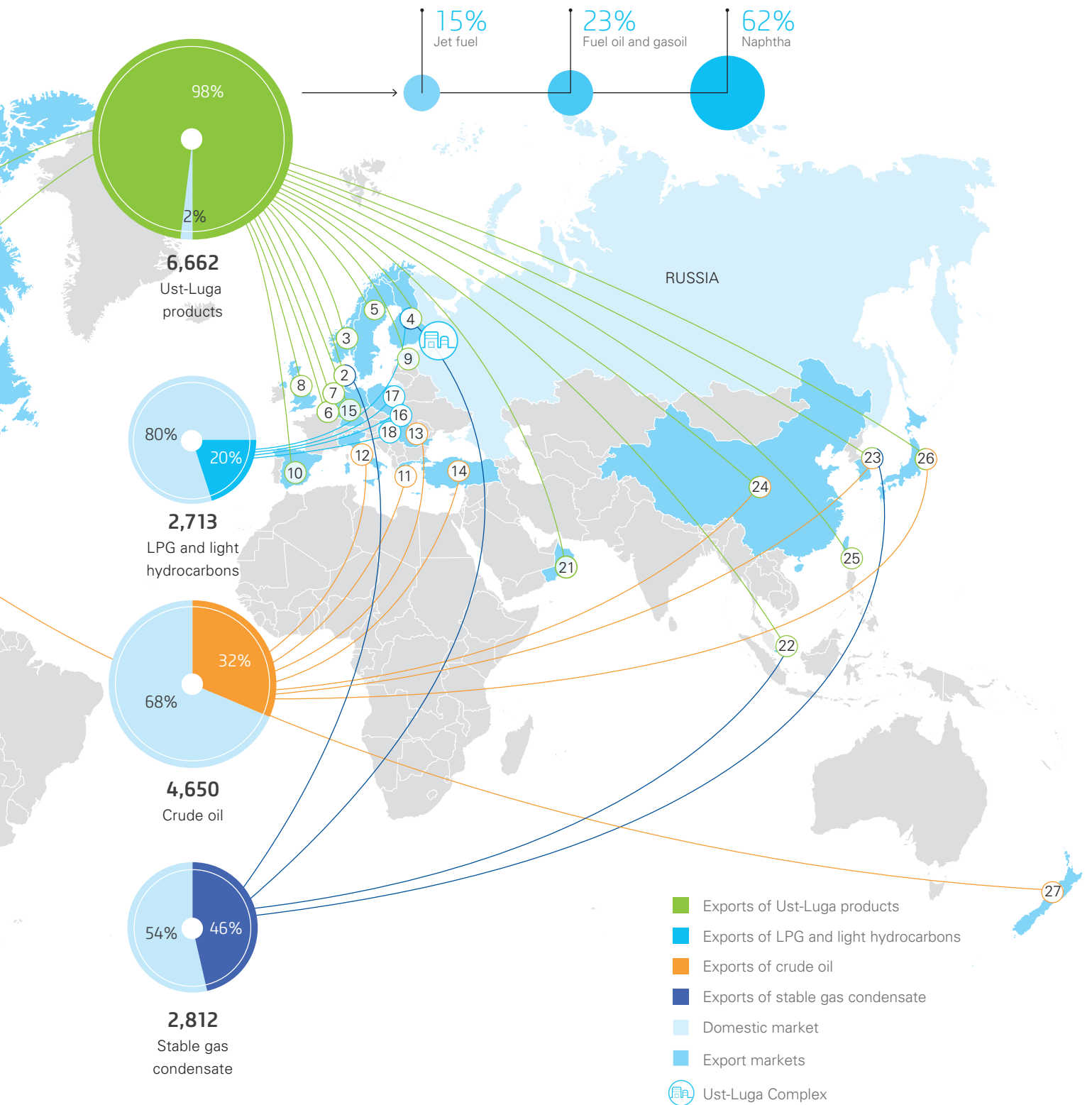
16.9 mmt

sales volumes of liquid hydrocarbons in 2016

RR 304 bln

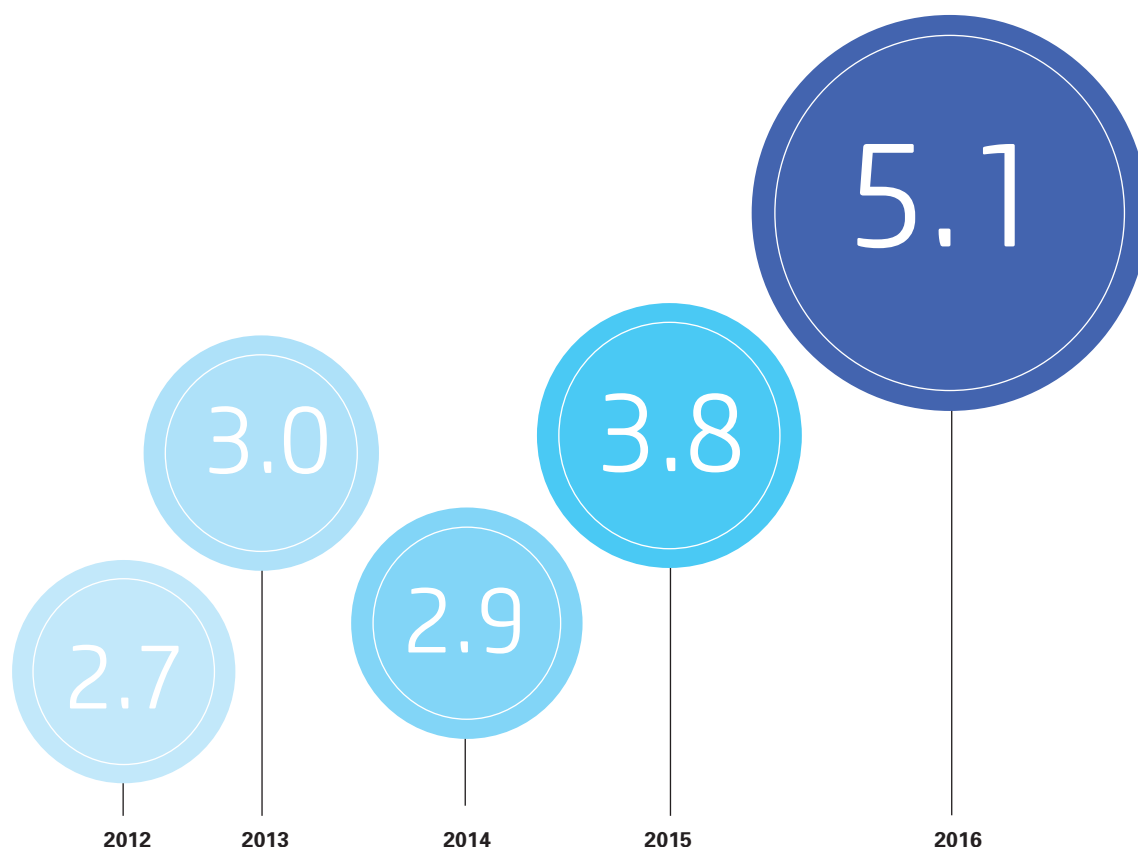
liquids sales revenues in 2016





HIGH LEVEL OF ENVIRONMENTAL AND SOCIAL RESPONSIBILITY

NOVATEK adheres to the highest standards of social responsibility and is committed to environmental integrity and industrial safety as well as supporting the regional development in the Far North of Russia, where Company's core operational assets are located.



↑ Social investments and expenses on HSE, RR bln

5.1

RR 5.1 BLN OF SOCIAL
INVESTMENTS AND
EXPENSES ON HSE
IN 2016

Photo: Purovsky Plant inventory tanks
equipped with state-of-the-art emergency
protection systems.



HSE AND SOCIAL RESPONSIBILITY

NOVATEK adheres to the principles of effective and responsible business conduct and considers the welfare of its employees and their families, environmental and industrial safety, the creation of a stable and beneficial social environment as well as contributing to Russia's overall economic development as priorities and responsibilities of the Company.

NOVATEK's core producing assets are located in the Far North, a harsh Arctic region with vast mineral resources and a fragile and vulnerable environment. The Company is committed to environmental protection in its operations. In 2016, the Company's overall expenses on environmental protection amounted to RUB 1,199 mln.

In 2016, a revised version of NOVATEK's Health, Safety and Environmental (HSE) Policy was approved, which included the Company's commitments consistent with the best Russian and international practices. Our key controlled entities are using an Integrated Management System for Environment Protection, Occupational Health and Safety (IMS) compliant with ISO 14001:2004 and OHSAS 18001:2007. In 2016, NOVATEK successfully passed the second follow-up IMS compliance audit.

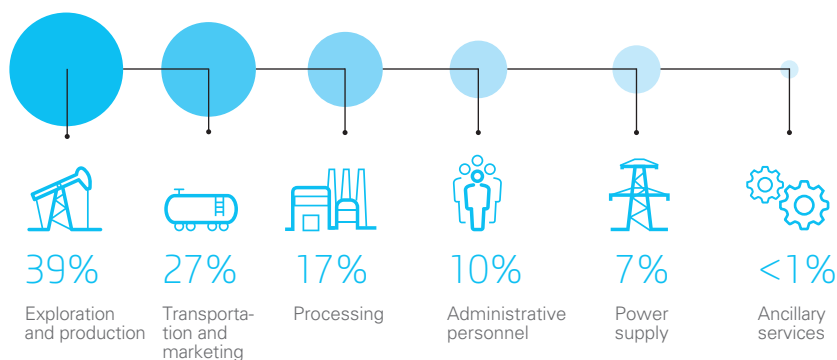
Special attention is paid to preventive measures in the area of environment protection. In particular, the environmental aspects are taken into account in designing new production facilities: modern technology and equipment is used to considerably reduce the adverse environmental impact and risk of environmental accidents.

Workplace certification includes evaluating measures to control the harmful impact of hazardous factors in the workplace. Measures to improve working conditions are developed based on the results of the certification process.

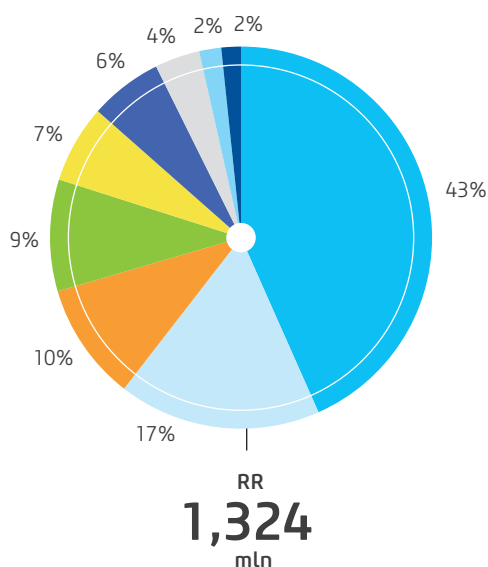
The Company's human resource management system is based on the principles of fairness, respect, equal opportunities for professional development, dialogue between management and employees, as well as continuous, comprehensive training and development opportunities for the Company's employees at all levels.

7,515

people – headcount of
NOVATEK and its subsidiaries
as of 31.12.16

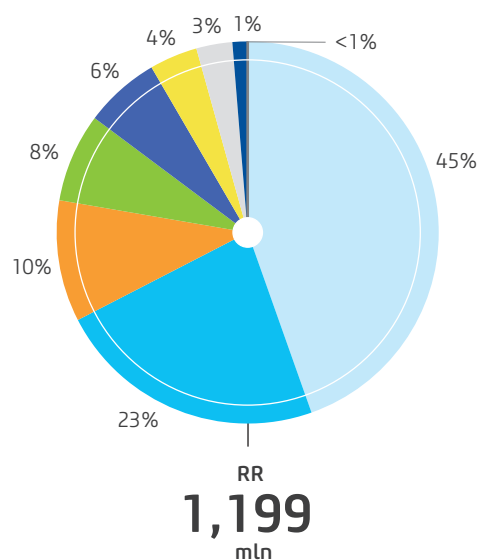


↑ NOVATEK's personnel structure as of 31.12.16



- Targeted Compensation and Socially Important Payments
- Repayable Financial Aid Program
- Health Resort Treatment and Rehabilitation
- Voluntary Medical Insurance
- State Guarantees Support Program
- Culture and sports
- Pension Program
- NOVATEK-Veteran Program
- Others

↑ Social Expenditures on employees in 2016

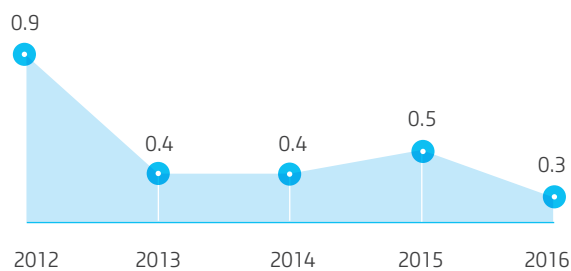


- Rational natural resources management
- Environmental protection against production and consumption waste
- Measures for the protection of flora and fauna and preservation of biodiversity
- Environmental monitoring and evaluation of the background
- Protection and use of water resources
- Soil protection
- Subsurface protection
- Atmospheric air protection
- Other

↑ Environmental Expenditures in 2016

RR 693 mln

expenses on Occupational Health and Safety in 2016



↑ Injury frequency rate (number of injuries per million working hours)

MANAGEMENT AND CORPORATE GOVERNANCE

THE BOARD OF DIRECTORS MEMBERSHIP AS OF 31 DECEMBER 2016

The Company has established an effective and transparent system of corporate governance complying with both Russian and international standards. NOVATEK's supreme governing body is the General Meeting of Shareholders. The corporate governance system comprises the Board of Directors, the Board Committees, and the Management Board, as well as internal control and audit bodies and the Corporate Secretary.

3

Independent Board Members¹



MR. ROBERT CASTAIGNE

Born in 1946
Independent Director
Member of the Audit Committee
Member of the Remuneration and Nomination Committee



MR. VICTOR P. ORLOV

Born in 1940
Independent Director
Chairman of the Remuneration and Nomination Committee
Member of the Audit Committee



MR. ANDREI V. SHARONOV

Born in 1964
Independent Director
Chairman of the Audit Committee
Member of the Remuneration and Nomination Committee

¹ Independent Director as of 31 December 2016 in accordance with the Corporate Governance Code recommended by the Central Bank of Russia and the UK Corporate Governance Code.



MR. ALEXANDER E. NATALENKO

Born in 1946

Chairman of the Board of Directors
Chairman of the Strategy
Committee



MR. LEONID V. MIKHELSON

Born in 1955

Chairman of the Management
Board



MR. ANDREI I. AKIMOV

Born in 1953

Member of the Strategy
Committee



DR. BURCKHARD BERGMANN

Born in 1943

Member of the Strategy
Committee



MR. MICHEAL BORRELL

Born in 1962

Member of the Strategy
Committee



MR. GENNADY N. TIMCHENKO

Born in 1952

Member of the Strategy
Committee

REVIEW OF OPERATING RESULTS

LICENSES

NOVATEK's core fields and license areas are located in, or in close proximity to, the Yamal-Nenets Autonomous District (YNAO) of the Russian Federation, which is one of the world's largest natural gas producing regions accounting for approximately 80% of Russian and 16% of global natural gas production. The concentration of the Company's fields in this prolific gas-producing region provides favorable opportunities for increasing NOVATEK's shareholder value with a minimum level of risks, low finding cost, and efficient replacement of reserves. With more than 20 years of operational experience in the region, NOVATEK is in a good position to efficiently monetize its resource base.

Exploration and production of hydrocarbons in Russia is subject to federal licensing regulations.

As of December 31, 2016, NOVATEK's subsidiaries and joint ventures held 39 subsoil licenses in Russia, five (5) of them are classified as exploration licenses. The duration of licenses for the Company's core fields exceeds 15 years. In particular, the license for the Yurkharovskoye field is valid until 2034, for the East-Tarkosalinskoye – until 2043, for the South-Tambeyskoye field – until 2045, and for the Samburgsky license area of Arcticgas – until 2034.

In 2016, NOVATEK significantly expanded its portfolio of licenses.

The Company's subsidiary, NOVATEK – YURKHAROVNEFTEGAS, obtained six (6) new licenses:

Following the results of an auction, NOVATEK – YURKHAROVNEFTEGAS obtained exploration and production licenses for the Nyakhartinsky, the Syadorsky and the Tanamsky license areas. The Nyakhartinsky license area is located in the YNAO in close proximity to the Yurkharovskoye field. Acquisition of licenses for the Syadorsky and the Tanamsky areas will enable the Company to enhance its resource base in the northern part of the Yamal Peninsula and in the Gydan Peninsula.

We obtained seven-year exploration licences for the West-Solpatinsky, North-Tanamsky and Nyavuyakhsky license areas. The license areas are located in the central part of the Gydan Peninsula.

In 2016, NOVATEK purchased Evrotek-Yuh, a company that holds an exploration and production license valid until 2032 for the Ladertoysky area containing the Ladertoyskoye gas condensate field. The license area is situated within the YNAO in the central part of the Gydan Peninsula in close vicinity to the new license areas.

In December 2016, upon the discovery of a new field, a subsoil exploration and production license valid until 2036 was obtained for the Kharbeyskoye field. The area is located in close proximity to the East-Tazovskoye, North-Russkoye and Dorogovskoye fields.

In September, 2016, NOVATEK and Eni, the Italian energy company, entered into a concessionary agreement with the State of Montenegro to explore and produce hydrocarbons on four offshore blocks in the Adriatic Sea. Each of the concessionaires holds 50% in the project, and Eni was designated as the concession operator. Participation in the concessionary agreement contributes to expanding the Company's potential to implement joint foreign projects.

NOVATEK strives to strictly observe and comply with all of its license obligations and conducts continuous monitoring of license tenders in order to expand its resource base in strategically important regions.

HYDROCARBON RESERVES

Most of the Company's reserves are located onshore or can be developed from onshore locations and are attributed to the conventional hydrocarbon categories (capable of being exploited using conventional technologies, in contrast to unconventional gas deposits such as shale gas or coal-bed methane).

The Company's reserves are appraised on an annual basis by independent petroleum engineers, "DeGolyer and MacNaughton" ("D&M"), under both the SEC and PRMS reserve reporting standards.

As of 31 December 2016, NOVATEK's SEC proved reserves, including the Company's proportionate share in joint ventures, aggregated 12,775 million barrels of oil equivalent (boe), including 1,755 billion cubic meters (bcm) of natural gas and 152 million metric tons (mmt) of liquid hydrocarbons.

Excluding the decrease in the Company's proportional share in the Yamal LNG joint venture, total proved reserves increased by 2.8% year-on-year, with an organic reserve replacement rate of 168% due to successful exploration works and drilling, which amounted to reserves addition of 902 million boe, inclusive of 2016 production. The primary contributors to reserves additions were the Utrenneye, the South-Tambeyskoye, the Kharbeyskoye, the Dorogovskoye and the Yarudeyskoye fields.

Total proved reserves dynamics during the reporting period was primarily affected by the decrease in the Company's proportional share in the Yamal LNG joint venture from 60% as at year-end 2015 to 50.1% as at 31 December 2016, resulting from the sale of a 9.9% equity stake in Yamal LNG to China's Silk Road Fund. Therefore including the decrease in the equity

stake and 2016 production, our total proved reserves decreased by 0.3%, representing a reserve replacement rate of 92% for the year. At year-end 2016, the Company's reserve to production ratio (or R/P ratio) was 24 years.

Under the PRMS reserves reporting methodology, the Company's total proved plus probable reserves, including the Company's proportionate share in joint ventures, aggregated 22,756 million boe, including 3,067 bcm of natural gas and 319 mmt of liquid hydrocarbons.

The high quality of our reserve base enables NOVATEK to maintain its competitive position as one of the lowest cost producers in the global oil and gas industry. Our average 2016 and five-year (2012-2016) reserve replacement costs amounted to RR 120 (USD 1.8) per boe and RR 88 (USD 2.3) per boe, respectively.

Proved reserves under the SEC standards as of 31 December 2016 (based on our equity ownership interest in the respective fields) and duration of licenses

Field / license area	Ownership	Duration of license	Gas reserves, bcm	Liquids reserves, mmt
TOTAL RESERVES	-	-	1,754.6	152.5
Yurkharovskoye	100%	2034	258.0	10.9
South-Tambeyskoye	50.1%	2045	304.1	8.9
Utrenneye	100%	2031	388.5	15.1
Urengoyevskoye ("Arcticgas")	53.3%	2034	184.0	43.7
East-Tarkosalinskoye	100%	2043	110.8	18.6
Geofizicheskoye	100%	2034	125.6	0.4
North-Urengoyevskoye	50%	2038	88.0	8.1
Yaro-Yakhinskoye	53.3%	2034	75.7	8.7
North-Russkoe	100%	2031	52.6	2.5
Samburgskoye	53.3%	2034	28.1	3.8
North-Chaselskoye	53.3%	the lifetime of the field	28.9	1.4
Khancheyevskoye	100%	2044	22.5	2.5
Olimpiyskiy license area	100%	2059	20.4	2.3
East-Tazovskoye	100%	2033	17.1	2.5
Kharbeyskoye	100%	2036	9.0	1.1
Dorogovskoye	100%	2033	7.0	-
Termokarstovoye	51%	2097	14.7	4.0
Yarudeyskoye	51% (100% of reserves)	2029	8.5	17.5
Other	-	-	11.1	0.5

GEOLOGICAL EXPLORATION

NOVATEK aims to expand its resource base through geological exploration at fields and license areas not only in close proximity to existing transportation and production infrastructure, but also in new potentially prospective hydrocarbon areas. The Company ensures the efficiency of geological exploration work by deploying state-of-the-art technologies and relying on the experience and expertise of the specialists in our geology department, and the Company's Scientific and Technical Center located in Tyumen.

The Company uses a systematic and comprehensive approach to exploration and development of its fields and license areas, beginning with the collection and interpretation of seismic data to the creation of dynamic field models for the placement of exploration and production wells. We employ modern geological and hydrodynamic modelling as well as new well drilling and completion techniques to maximize the ultimate recovery of hydrocarbons in a cost effective manner.

In 2016, we continued full-scale exploration works at our license areas located on the Gydan Peninsula and offshore in the Gulf of Ob to properly assess the resource potential of this strategically important region. We carried out three-dimensional (3D) seismic studies at the North-Obskiy offshore license area and also completed drilling of an exploration well at the Utrenneye field. In total we have drilled five (5)

exploration wells at the Utrenneye field in 2014 to 2016, and the well testing results allowed us to increase the appraised reserves volumes and confirm higher well flows at the field.

We also conducted 3D seismics in the Tazov bay within the Nyakhartinskiy license area in order to spot prospective targets for exploration drilling.

Exploration activities also continued at the fields and license areas in the Nadym-Pur-Taz region. Seismic studies were done at the Yarudeyskoye field and the North-Russkiy and Dorogovskiy license areas while exploration drilling was performed at the Kharbeyskoye, West-Yurkharovskoye and Yevo-Yakhinskoye fields.

In 2016, we completed 984 square km of 3D seismic works and drilled approximately 10.2 thousand meters of exploration drilling.

We successfully discovered one (1) new gas condensate deposit in the mid Jurassic layer at the Kharbeyskoye gas condensate field, and nine (9) new gas condensate deposits at the Utrenneye, South-Tambeyskoye and Yevo-Yakhinskoye fields. We managed to expand the gas condensate potential of the Achimov layer at Arcticgas's Urengoyevskoye field and confirmed the crude oil potential at the Yarudeyskoye and East-Tarkosalinskoye fields as well as confirmed the natural gas potential at the Malo-Yamalskoye field.

Based on the results of seismic works we have chosen a number of prospective structures for exploration drilling.

Exploration works

	Units	2015	2016	Change
3D SEISMIC	square km	1,004	984	(2%)
Subsidiaries	square km	1,004	984	(2%)
Joint ventures	square km	-	-	
EXPLORATION DRILLING	th. m	15.2	10.2	(33%)
Subsidiaries	th. m	9.6	10.2	6%
Joint ventures	th. m	5.6	-	(100%)

FIELD DEVELOPMENT

In 2016, NOVATEK continued investing capital in developing our producing and prospective fields. In the reporting year, the Company's subsidiaries invested RUB 23.6 billion in the resource base development.

Production drilling in 2016, including joint ventures, reached 235,000 m, which is 30% below the 2015 level. The decrease

in drilling activities is due to a successful completion of the main drilling program at the fields of Yurkharovneftegas, and the Arcticgas, and Yargeo joint ventures. The biggest drop in drilling activities was observed at the Yurkharovskoye, Urengoyevskoye, Yaro-Yakhinskoye, and Yarudeyskoye fields, whereas the drilling activities at the South-Tambeyskoye field increased during the year.

A total of 76 wells were put on production in 2016, including 41 gas and gas condensate wells and 35 crude oil wells.

New facilities commissioned at producing fields

In January, a month after it was commissioned, the Yarudeyskoye field, with 21 wells drilled and completed, reached its design production capacity of 3.5 mmt of crude oil per year. The field's infrastructure includes a central oil gathering facility, a gas treatment unit, a 350 km oil pipeline and a 149 km gas pipeline. Completion of water sourcing wells was finalized, as was commissioning of reservoir pressure maintenance systems.

As part of the Yurkharovskoye field development strategy, the Cenomanian production area achieved its design capacity with 18 wells in operation, the 48 MW Cenomanian gas booster compressor station was completed and launched. The 25 MW fourth phase of gas booster compressor station was commissioned bringing the station's aggregate capacity up to 300 MW.

The 10 MW third phase of the booster compressor station was launched at the Khancheyenskoye field increasing the total compressor equipment capacity to 40 MW.

Gas treatment plant and de-ethanizer unit reconstruction programs have been implemented at the East-Tarkosalinskoye field to enhance production quality and improve process equipment reliability.

A methanol production unit with a capacity of 50 mt per annum was launched at the Urengoyenskoye field resulting in a significant reduction of methanol purchasing costs.

HYDROCARBON PRODUCTION

In 2016, NOVATEK carried out commercial hydrocarbon production at 13 fields. Marketable

production from all fields (including the Company's share in production of joint ventures) amounted to 537.0 mmboe, representing an increase of 3.0% over the prior year.

Total marketable production of natural gas including the Company's share in production of joint ventures aggregated 66.10 bcm, representing 80.5% of our total hydrocarbon output. The share of gas produced from the gas condensate bearing layers (or "wet gas") in proportion to total gas production was 79.1%. Our marketable natural gas production decreased by 2.7% or by 1.8 bcm, as compared to 2015 volumes.

Volumes produced by our subsidiaries at mature fields decreased mainly due to natural declines in the reservoir pressure at the current gas producing horizons.

Marketable production of liquid hydrocarbons including the Company's share in production of joint ventures totalled a record 12,441 thousand tons, of which 60.5% was unstable de-ethanized gas condensate and the remaining 39.5% consisted of crude oil. Marketable production of liquids increased by 36.8%, or by 3,347 thousand tons as compared with 2015, with gas condensate production level almost unchanged at 7,526 thousand tons and crude oil production growing by more than three-fold to 4,915 thousand tons. Liquids production share in our overall production increased by four (4) percentage points to 19% as compared with 2015.

Our record growth in liquids production was mainly due to the launch of the Yarudeyskoye crude oil field in December 2015 and the Yaro-Yakhinskoye and the Termokarstovoye gas condensate fields in the first half 2015.

We continued to achieve some of the lowest lifting costs in the industry. The Company's lifting costs were RR 38.4 (USD 0.57) per boe in 2016.

Marketable hydrocarbon production (including share in production by joint ventures)

	Units	2015	2016	Change
TOTAL PRODUCTION	mmboe	521.6	537.0	3.0%
Gas	mmcm	67,905	66,103	(2.7%)
	mmboe	444.1	432.4	
Liquid hydrocarbons	mt	9,094	12,441	36.8%
	mmboe	77.5	104.6	

Marketable hydrocarbon production (including share in production by joint ventures)

	Gas, mmcm			Liquids, mt		
	2015	2016	Change	2015	2016	Change
TOTAL	67,905	66,103	(2.7)%	9,094	12,441	36.8%
Yurkharovskoye (100%)	35,979	33,766	(6.2%)	2,126	1,813	(14.7%)
Arcticgas fields (53.3%)	12,624	13,682	8.4%	4,016	4,300	7.1%
East-Tarkosalinskoye (100%)	9,075	8,015	(11.7%)	1,365	1,354	(0.8%)
North-Urengoyenskoye (50%)	5,395	5,023	(6.9%)	622	519	(16.6%)
Khancheyenskoye (100%)	2,510	2,473	(1.5%)	392	353	(9.9%)
Termokarstovoye (51%)	714	1,163	62.9%	258	428	65.9%
Yarudeyskoye (100%)	-	427	-	184	3,556	n/a
Other	1,608	1,554	(3.4%)	131	118	(9.9%)

YAMAL LNG PROJECT

Yamal LNG is the flagship project in NOVATEK asset portfolio and is considered a transformational move for the Company into the international gas market. Yamal LNG envisages the construction of an LNG liquefaction plant with annual capacity of 16.5 million tons per annum, utilizing the prolific feedstock resources of the South-Tambeyskoye field located in the Northeast of the Yamal Peninsula. The launch of the first LNG train is planned for 2017.

Yamal LNG is the operator of the project, the license holder and owner of all the assets. In March 2016 NOVATEK successfully closed the transaction of sale of a 9.9% equity stake in the Yamal LNG project to China's Silk Road Fund. At year-end, the shareholder structure comprised NOVATEK (50.1%), Total (20%), CNPC (20%) and Silk Road Fund (9.9%).

At year-end the construction progress on the first train was 88% and the construction progress of all three trains – 75%. The project's infrastructure includes the sea port, the international airport, automobile roads, power lines, gas gathering lines and the living quarters.

The South-Tambeyskoye field was discovered in 1974 and comprises 42 gas bearing layers with depths ranging from 900 to 3,730 meters and includes three domes. There are 112 Valanginian gas and gas condensate deposits, 10 Jurassic gas and gas condensate deposits, and two (2) Cenomanian dry gas deposits. The productive formations have a wide range of permeability and hydrostatic reservoir pressure. The field is being developed with horizontal wells with lengths up to 5,000 meters and horizontal parts up to 1,500 meters.

The license for exploration and production

at the South-Tambeyskoye field owned by Yamal LNG is valid until 2045.

As of 31 December 2016, the field was estimated to contain 607 bcm of proved natural gas reserves and 18 mmt of proved liquid hydrocarbon reserves, under the SEC reserves methodology. In 2016 the production drilling results allowed us to increase the proved natural gas SEC reserves at the South-Tambeyskoye field by 85 bcm compared to year-end 2015. Based on total proved hydrocarbon reserves, the South-Tambeyskoye field is the largest field in NOVATEK reserves portfolio. According to the PRMS reserves standards, the proved and probable reserves of the South-Tambeyskoye field were appraised at 942 billion cubic meters of natural gas and 31 mmt of liquid hydrocarbons.

The South-Tambeyskoye field has already been thoroughly studied with a complex suite of exploration activities, including running 3D seismic and exploration drilling, creation of the fields' geological model and annual reserves appraised by the independent petroleum engineers, D&M. The field development plan provides for the drilling of 208 wells on 19 well drilling pads, with production potential exceeding 27 bcm of natural gas and one (1) million tons of stable gas condensate per annum.

Natural gas produced at the field will be delivered to the international markets as liquefied natural gas, or LNG, which requires the construction of a liquefaction plant consisting of three (3) production trains of 5.5 mmt annual capacity each. The shipping infrastructure will include a jetty with two tanker-loading berths at the port of Sabetta.

At year-end 2016, 73 production wells were drilled at the South-Tambeyskoye field, exceeding the well stock required to launch the

first production train of the LNG plant (58 wells).

At year-end, there were more than 3,600 construction vehicles and 22,000 construction workers on site. The Sabetta international airport services regular flights from Novy Urengoy, Moscow and Samara, ensuring high efficiency of shift workers logistics. Regular flights served approximately 365,000 people in 2016.

To minimise on site construction activities due to challenging climate conditions, a modular approach to the LNG plant construction was selected. The LNG plant will consist of 142 large plant modules with weights ranging from 85 tons to 6,400 tons. The modules are built at contractor's yards and delivered to the Sabetta construction site by sea. Approximately 19,000 people were involved in modules fabrication for the Yamal LNG project at different construction yards.

At year-end 2016 all 78 modules of the first LNG train were delivered to the construction site. Ten (10) of the 64 modules necessary for the second and third LNG trains were in transit and three (3) were delivered on site. All three main cryogenic heat exchangers (key element of gas liquefaction technology) for trains #1, #2 and #3 were delivered to the construction site by year-end, as well as the full equipment package for compressor lines of the plant's first and second trains, boil-off gas compressors, a backup heater, packages of steel work pipe racks, power plant turbines and other equipment.

As of 31 December 2016, all the first train LNG modules were installed on the prepared foundations, and hook up was underway. The main cryogenic heat exchanger for LNG train #1 was installed into the liquefaction module. Compressor equipment for the first train and the backup heater were installed on the foundations, as well as over 67,500 tons of

steel work for pipe racks. By the end of 2016, over 37,000 foundation piles for the LNG plant were installed, about 3,900 pile caps were installed on the piles, and more than 53,000 cubic meters of concrete was poured for the foundation.

The project requires four (4) LNG tanks including two (2) LNG tanks for the first train. The outer walls of the tanks are made of concrete while the internal walls are multi-layer made of steel and insulating materials ensuring leak integrity and thermal insulation. All four (4) LNG tanks successfully passed hydro-testing in 2016.

In 2016, dredging was performed in the port harbor, approach and sea channels. Overall volumes of dredged sand totalled about 19 million cubic meters. The year-round use of the Sabetta port received more than six (6) million tons of cargoes (two-fold increase year-on-year), delivered by 259 marine ships and 304 river barges. A two (2) km Southeastern ice barrier was being constructed to protect the port harbor. LNG and stable gas condensate shipment pipe rack with shipping berths was being built at the ice barrier. During the reporting year two (2) new cargo berths for module and equipment unloading were added to the four (4) cargo berths built earlier. There are now six (6) cargo berths in full operations at the sea port area.

More than 95% of the LNG plant output has been contracted on a long-term basis. Specially designed Arc7 ice-class LNG carriers will be used for LNG transportation, and the first tanker was placed from dry-dock into water in early 2016, fully equipped and by year-end the LNG carrier successfully passed sea acceptance tests. As of year-end 2016, five (5) other LNG carriers and the two (2) Arc7 condensate tankers to be chartered by the project were under construction.

PROCESSING OF GAS CONDENSATE

Purovsky Plant

Our subsidiaries and joint ventures are producing wet gas – a mixture of natural gas and gas condensate. After being separated and de-ethanized at the field the unstable (de-ethanized) gas condensate is delivered via a system of condensate pipelines owned and operated by the Company for further stabilization at our Purovsky Plant located in the YNAO in close proximity to the East-Tarkosalinskoye field.

The Purovsky Plant is the central element in our production value chain that provides us complete operational control over our processing needs and access to higher yielding marketing channels for our stable gas condensate. The Purovsky Plant produces stable gas condensate and light hydrocarbons after processing our unstable gas condensate.

During the reporting year, the de-ethanized gas condensate processing volumes at the

Purovsky Plant increased by 3.1% to 12,397 mt. The Purovsky Plant's processing capacity matches the overall gas condensate production capacity of the Company's fields in operation. The structure of 2016 output included 9,667 mt of stable gas condensate, 2,597 mt of light hydrocarbons and LPG and 10 mt of regenerated methanol.

The Purovsky Plant is connected via its own railway line to the Russian rail network at the Limbey rail station. Subsequent to the launch of the Ust-Luga Complex in 2013, most of the stable gas condensate volumes produced at the Purovsky Plant are delivered by rail to Ust-Luga for further processing or transshipment to exports, with most of the remaining small volume of stable gas condensate sold directly from the plant to the domestic market. All of the light hydrocarbon volumes (feedstock for LPG production) produced at the plant are delivered by pipeline to SIBUR's Tobolsk Petrochemical Complex for further processing.

Processing volumes and output of the Purovsky Plant, thousand tons

	2015	2016	Change
PROCESSING OF DE-ETHANIZED CONDENSATE	12,021	12,397	3.1%
OUTPUT:			
Stable gas condensate	9,664	9,667	0.03%
Light hydrocarbons and LPG	2,228	2,597	16.6%
Methanol	11	10	(9.1%)

Ust-Luga Stable Gas Condensate Transshipment and Fractionation Complex

The Gas Condensate Fractionation and Transshipment Complex (the "Ust-Luga Complex") launched in 2013 is located at the all-season port of Ust-Luga on the Baltic Sea. The Ust-Luga Complex processes stable gas condensate into light and heavy naphtha, jet fuel, ship fuel component (fuel oil) and gasoil, and enables us to ship the value-added petroleum products to international markets. The Ust-Luga Complex also allows for transshipment of stable gas condensate to the export markets.

The Ust-Luga Complex processed 6,917 mt of stable gas condensate into 6,784 mt of end products, including 4,195 mt of light and heavy naphtha, 998 mt of jet fuel and 1,591 mt of ship fuel component (fuel oil) and gasoil.

High value-added petroleum products produced at the Ust-Luga Complex have a significant positive impact on the profitability of our liquid hydrocarbon sales and the Company's cash flow generation.

As the Ust-Luga Complex reached full processing capacity we transshipped stable gas condensate to the export markets by sea.

Processing volumes and output of the Ust-Luga Complex, thousand tons

	2015	2016	Change
STABLE GAS CONDENSATE PROCESSING	6,727	6,917	2.8%
OUTPUT:			
Heavy naphtha	2,101	2,195	4.5%
Light naphtha	1,898	2,000	5.4%
Ship fuel component (fuel oil)	1,183	1,148	(3.0%)
Jet fuel	949	998	5.2%
Gasoil	462	443	(4.1%)

NATURAL GAS SALES

NOVATEK plays an important role in ensuring supplies of natural gas to the Russian domestic market. During the past year, we supplied natural gas to 35 key consuming regions of the Russian Federation. Our customers were located primarily in the following: the Chelyabinsk, Lipetsk, Perm, Stavropol, Moscow, Kostroma, Vologda, and Tyumen regions, the Khanty-Mansiysk Autonomous Region, YNAO, the Republic of Tatarstan and the city of Moscow. The above-mentioned regions accounted for more than 94% of our total gas sales.

NOVATEK's 2016 natural gas sales volumes totalled 64.7 bcm, representing an increase of 3.6% as compared to 2015 sales volumes of 62.5 bcm. The sales volumes growth was a result of restoring sales to one of our major customers who did not take full contracted volumes in 2015 due to technical reasons, as well as sales of additional natural gas volumes to our end-customers and

wholesale traders. The proportional share of natural gas sales to end-customers remained practically unchanged compared to 2015 and amounted to 92.2% of our total natural gas sales mix.

Our revenues from natural gas sales totalled RR 229.7 billion, which is 3.4% higher as compared to 2015. The sales volumes growth was the main driver for the growth in natural gas revenues.

In order to maintain production levels during periods of seasonal demand NOVATEK has entered into an agreement with PAO Gazprom for underground storage services. Typically, natural gas inventories are accumulated during warmer periods when demand is lower and then used to meet increased demand during periods of colder weather. At year-end 2016, our inventories of natural gas in underground gas storage facilities and pipelines amounted to approximately 0.8 bcm.

As part of our international marketing strategy, we supplied our first LNG cargo sourced from the Trinidad & Tobago LNG plant to the port of Quintero, located in Chile.

Natural gas sales, mmcm

	2015	2016	Change
TOTAL GAS SALES, INCLUDING:	62,465	64,709	3.6%
End customers	58,054	59,646	2.7%
Traders	4,411	5,063	14.8%
Share of end-customers in total gas sales	92.9%	92.2%	(0.7) p.p.

LIQUID HYDROCARBON SALES

NOVATEK sells liquid hydrocarbons (stable gas condensate, petroleum products, light hydrocarbons, LPG and crude oil) domestically and internationally. We strive to respond quickly to changing market conditions by optimizing the customer base and supply geography, as well as developing and maintaining our own logistics infrastructure.

The logistical supply chain varies according to location and type of product - stable gas condensate and LPG are transported by rail, finished petroleum products produced at the Ust-Luga Complex are exported by sea, while crude oil produced from our fields is transported through the trunk pipelines owned and operated by PAO Transneft.

Total sales volumes of liquid hydrocarbons in 2016 aggregated 16,850 thousand tons,

representing a 30.7% increase over 2015 volumes. The growth is mainly due to increase in crude oil production. Our export sales of liquids grew by 9.6% year-on-year to 9,869 thousand tons.

Our liquids sales revenues increased to RR 304.1 billion, or by 21.7% as compared to 2015, mainly driven by higher sales volumes.

Petroleum products from the Ust-Luga Complex accounted for 40% share of our overall liquids sales volumes and amounted to 6,662 thousand tons. We sold 4,113 thousand tons of naphtha, 985.6 thousand tons of jet fuel and 1,563.7 thousand tons of fuel oil and gasoil. The main share of stable gas condensate processing products (98%) was sold for exports. Sales to the European markets accounted for 53% of total petroleum product sales volumes, 29% were sold to the Asian-Pacific region, 14% to North America and 4% to the Middle East. Naphtha was mainly exported to the Asian-Pacific countries, while jet fuel, fuel oil and gasoil was shipped to North-Western Europe.

Export sales of stable gas condensate continued in 2016 as we reached full capacity utilization at the Ust-Luga Complex. Total stable gas condensate sales volumes grew by 1% to 2,812 thousand tons compared to 2015.

A portion of light hydrocarbons produced at the Purovsky Plant is processed on tolling terms at SIBUR's Tobolsk Petrochemical Complex to commercial LPG, which is then delivered to

NOVATEK's customer base, while the rest of the light hydrocarbons volumes are sold to SIBUR. We sold 1,468 thousand tons of light hydrocarbons in 2016.

LPG sales volumes totaled 1,245 thousand tons in 2016, representing a 2.7% decrease compared to 2015. LPG export sales volumes amounted to 549 thousand tons or 44% of the total LPG sales volumes. Novatek Polska, our wholly owned LPG trading company in Poland, sold 507 thousand tons of LPG, representing 92% of our total LPG export sales. Other export markets for LPG were Finland, Hungary and Slovakia.

On the domestic market, our LPG is sold through large wholesale channels, as well as through our network of retail and small wholesale stations. In 2016, large wholesale supplies to the domestic market accounted for 560 thousand tons, representing 80% of commercial LPG domestic sales volumes. We also sold LPG via our network of 65 retail stations and seven (7) small wholesale stations in the Chelyabinsk, Volgograd, Rostov and Astrakhan regions. The total amount of LPG sold through our domestic network of retail and small wholesale stations amounted to 136 thousand tons.

Sales of crude oil in 2016 totaled 4,650 thousand tons, representing an increase by more than four-fold times over 2015 volumes. We sold 68% of our crude oil volumes on the domestic market with the remaining volumes supplied to export markets.

Liquid hydrocarbon sales, thousand tons

	2015	2016	Change
TOTAL	12,888	16,850	30.7%
Petroleum products (Ust-Luga)	6,693	6,662	(0.5%)
Crude oil	1,090	4,650	326.6%
Stable gas condensate	2,786	2,812	0.9%
Light hydrocarbons	1,026	1,468	43.1%
LPG	1,280	1,245	(2.7%)
Other	13	13	0.0%

ENVIRONMENTAL AND SOCIAL RESPONSIBILITY

NOVATEK adheres to the principles of effective and responsible business conduct and considers the welfare of its employees and their families, environmental and industrial safety, the creation of a stable and beneficial social environment as well as contributing to Russia's overall economic development as priorities and responsibilities of the Company.

ENVIRONMENTAL PROTECTION

NOVATEK's core producing assets are located in the Far North, a harsh Arctic region with vast mineral resources and a fragile and vulnerable environment. The Company is committed to environmental protection in its operations. In 2016, the Company's overall expenses on environment protection amounted to RUB 1,199 mln.

In 2016, a revised version of NOVATEK's Health, Safety and Environmental (HSE) Policy was approved, which included the Company's commitments consistent with the best Russian and international practices. Our key controlled entities are using an Integrated Management System for Environment Protection, Occupational Health and Safety (IMS) compliant with ISO 14001:2004 and OHSAS 18001:2007. In 2016, NOVATEK successfully passed the second follow-up IMS compliance audit.

Special attention is paid to preventive measures in the area of environment protection. In particular, the environmental aspects are taken into account in designing new production facilities: modern technology and equipment is used to considerably reduce the adverse environmental impact and risk of environmental accidents. The Company builds and rebuilds its waste disposal sites, equips its facilities with state-of-the-art oil sludge treatment units, new sewage treatment facilities are built and older ones are revamped.

Environmental monitoring was performed throughout the reporting year at all of the license areas and production facilities of the Company. During the monitoring process the

condition of the environment components is studied, soil, ground, snow cover, water and bed deposit samples are taken. Air contamination level is inspected. The status of fish stock and fodder resources in water areas is studied as are hydrologic and hydrochemical parameters. The samples taken are tested in certified laboratories. Based on the laboratory analysis the condition of the environment components is evaluated as well as its dynamic pattern over the year. The monitoring revealed that the condition of the environment components in the Company's production facility locations is evaluated as stable.

During 2016, NOVATEK rose by five positions in the oil and gas environmental responsibility rating under the Common Sense Project. Thus, it became an absolute leader in terms of annual dynamics. NOVATEK has eventually ranked seventh among 21 oil and gas companies in Russia. The project was implemented by the World Wildlife Fund (WWF) Russia and CREON Energy with the support of the Russian Ministry of Energy and Ministry of Natural Resources.

In the reporting year, the Company continued its participation in the Carbon Disclosure Project (CDP), whereby information on greenhouse gas emissions and operations energy efficiency is disclosed, as well as in the CDP Water Disclosure Project to disclose data on the use of water resources. By taking part in these projects the Company intends to achieve a balance between the climate change risks and efficiency of investment projects. The Company offers all stakeholders full access to its environmental information, including by publications in federal and local printed media, on its website, etc.

In 2016, the Company started developing its corporate Greenhouse Gas Emission Control System. This action became part of the Russian national set of actions delivered in the Year of Environment, and NOVATEK signed a relevant quadripartite agreement with the Russian Ministry of Natural Resources and Environment, YNAO Government, and the Federal Supervisory Natural Resources Management Service.

The Company together with NOVATEK Ust-Luga won the 2016 National Environmental Prize in the Innovative Eco-efficient Technologies for Industrial Application category (introduction of a smokeless flare technology in NOVATEK Ust-Luga). A total of 247 projects

from 50 constituent entities of the Russian Federation have submitted entries for the prize. The prize celebrates projects that offer practical solutions to energy- and resource saving, clean operations, preservation of a favorable environment, and environmental safety.

Key environmental indicators of NOVATEK, its subsidiaries and joint ventures

	Unit	2015	2016	Change
Water consumption	th. cubic meters	1,716	2,701 ¹	57%
Atmospheric emissions	th. tons	66.2	121.2 ²	83%

- 1 The increase in water consumption is due to the formation pressure maintenance program on the oil part of the East-Tarkosalinskoye field and increase in water production for industrial use from Aptian-Cenomanian wells for the pressure maintenance program.
- 2 Increase in atmospheric emissions is due to the Yarudeiskoye oil field achieving its designed capacity (oil production and treatment volume increased from 0.19 mmt in 2015 to 3.56 mmt in 2016) which led to a natural increase in associated gas production and flaring.

One of the Company's environmental priorities is the rational usage of resources, including energy resources. The table below sets out the physical volumes and the Russian rouble equivalent of energy resources consumed by the Company, its subsidiaries and joint ventures in 2016.

Energy resource consumption by NOVATEK, its subsidiaries and joint ventures

	Units	Volume	RR mln, net of VAT
Natural gas	mmcm	1,918	2,648.0
Electricity	MW*h	656,149	3,236.1
Heating energy	Gcal	272,663	509.3
Oil	tons	858	5.4
Motor gasoline	tons	882	35.8
Diesel fuel	tons	5,145	188.0
Other	tons	620	5.9

INDUSTRIAL SAFETY AND OCCUPATIONAL HEALTH

Our strategic goal is to achieve a leading position amongst oil and gas companies on all key indicators concerning Occupational Health and Safety. In order to accomplish this goal, the Company continually updates its IMS, improves employees' qualification and applies advanced technologies.

In accordance with the requirements of the Federal Law "On Industrial Safety of Hazardous Production Facilities" and the "Rules on the Organization and Implementation of Industrial Control over Compliance with Industrial Safety Requirements at Hazardous Production Facilities", all of our subsidiaries have adopted "Regulations on the Organization and Implementation of Industrial Compliance Control". As part of the monitoring and compliance process, we have established industrial control compliance commissions, who carry out regular audits of departments and production facilities to check adherence to health and safety requirements.

Workplace certification includes evaluating measures to control the harmful impact of hazardous factors in the workplace. Measures

to improve working conditions are developed based on the results of the certification process. In the reporting year, we certified 4,830 workplaces. There were no hazardous conditions found during the inspection.

In 2016, a NOVATEK commission continued comprehensive audits of NOVATEK subsidiaries for occupational health, industrial, fire and environmental safety requirements. In the reporting year, we conducted OHS due diligence checks on four subsidiaries and joint ventures. Based on their findings, relevant reports were produced, and remedial measures were developed.

All of NOVATEK's subsidiaries and joint ventures conduct periodic safety training and briefings; personnel training and development programs are offered, among others, by specialized training centers; knowledge assessment is implemented on a regular basis. During 2016, all entities undertook scheduled and unscheduled Health and Safety knowledge tests; within this period, 6,852 employees underwent occupational health training courses and certification, and 3,018 employees underwent safety training courses. In 2016, the financing of Occupational Health and Safety totaled approximately RR 693 million.

Key health and safety indicators of NOVATEK, its subsidiaries and joint ventures

	2015	2016	Change
Incident frequency rate (number of incidents per million working hours)	0.53	0.33	(38%)
Accidents at hazardous production facilities	0	0	0%
Incidents at hazardous production facilities	2	2	0%

HUMAN RESOURCES

Employees are NOVATEK's most valuable resource, allowing the Company to grow rapidly and effectively. The Company's human resource management system is based on the principles of fairness, respect, equal opportunities for professional development, dialogue between management and employees, as well as continuous, comprehensive training and development opportunities for the Company's employees at all levels.

As of the end of 2016, NOVATEK and its subsidiaries had 7,515 employees, 38.7% of whom work in exploration and production, 17.0% in processing, 26.9% in transportation and marketing, 6.8% in power supply and less than 1.0% in ancillary services. The remaining 9.7% are administrative personnel. The middle age

group (25 to 44 years old) is the predominate age range in our personnel composition. The average age of the Company's employees is 39 years.

Personnel Training and Development

Amid the rapid development of technologies and management systems, our multilevel training and professional development program enables our employees to contribute to making the Company more competitive. In 2016, the primary goals of training and professional development included:

- implementing an In-house Training program to improve the competences of the Company's employees;
- implementing the Steps in Discovering Talents program for young specialists targeted at training highly qualified personnel

- whose competence level fully meets business needs;
- developing and improving the Corporate System for the Evaluation of Technical Competencies; and
- engaging young specialists to take part in research-to-practice conferences.

To ensure targeted professional upgrade, an In-house Training program was launched in 2016 hosted by NOVATEK Scientific and Technical Center (NOVATEK STC). Its employees have developed courses and trained their colleagues on such topics as “Seismic Exploration Basics”, “Practical Aspects of Modelling Foundation: Theory and Practice”, “Integrated Engineering of Gas Condensate Fields”, “Geological 3D Modelling Basics”, “Complex Logging Methods to Address Geological Tasks: Basics of Log Interpretation”, “Hydrocarbon Fluid Properties for Modelling their Production, Treatment, and Transportation”, to name a few. A total of 147 employees of NOVATEK and the Company's subsidiaries received training under this program in 2016.

NOVATEK continued its efforts to advance the professional capabilities of its employees, improve working conditions and train its personnel on safe working practices at its production facilities. A total of 44.8 % of white- and blue-collar workers upgraded their skills. In 2016, the Corporate System for the Evaluation of Technical Competencies tested 613 employees across the Group, including 20 persons who were tested at recruitment and 91 persons – at promotion.

We had our fourth class of graduates under the Steps in Discovering Talents Program. Twenty young specialists graduated from the on-the-job adaptation and professional development program. By autumn 2016, another 32 young specialists joined the program.

Young specialists received the Mentoring Culture training courses together with their mentors. In total, 24 mentors attended the training.

To improve financial awareness of young specialists, a new unit on Value Creation Mindset was included in the program in 2016. The graduating young specialists participated in the new training course.

In November 2016, Tarko-Sale hosted the 2nd Interregional Professional Skills Contest among field workers. NOVATEK-TARKOSALENEFTGAS provided its facilities for the contest. The number of companies and participants in the contest doubled to 67 employees from eight NOVATEK Group companies

as compared to 2015. In addition to the four jobs, which participants competed in during the first contest, namely oil and gas production operator, process unit fitter, electrical equipment fitter, and instrument and automation fitter, this year's contest included two more professional categories: process unit operator and chemical analysis technician. All participants received valuable gifts and the winners in each professional category were awarded bonuses and personal salary allowances in recognition of their professional excellence.

In September 2016, Moscow hosted the 11th Interregional Research-to-Practice Conference for the Company's young specialists attended by 46 employees. Following the competition, all winners received bonuses, while seven of the most successful participants and the Best Implemented Project winner were also awarded a trip to petroleum training centers in Australia.

Social Programs

Employee relations primary focus is on implementing social programs, and according to the Core Concept of the Company's social policy which was adopted in 2006, the social benefits package for employees includes the following programs:

- voluntary medical insurance for employees;
- therapeutic resort treatment for employees and members of their families;
- provision of special-purpose short-term loans;
- special-purpose compensation and social support payments;
- provision of special-purpose interest-free loans to purchase housing, and
- pension program.

Along with providing an optimum social benefits package, the Company is also committed to creating opportunities for employees to play sports and get involved in sports and cultural events. In 2016, our employees and their family members visited exhibitions at Russia's national museums, classical music concerts, and attended sporting events like football (soccer) games and acrobatic rock'n'roll competition with the Company's assistance.

The Company publishes its corporate newsletter “NOVATEK” and corporate magazine “NOVATEK Plus” to inform employees, their family members, and third parties about the Company's activities, production results, cultural, sports, and charitable programs. The main events of NOVATEK are published in the Company's portal.

SOCIAL POLICY AND CHARITY

Social Policy and Charity make up an important part of NOVATEK's activities. In 2016, the Company continued to pay close attention to projects aimed at supporting the culture, preserving and revitalizing national values and spiritual legacy of Russia, promoting and integrating the Russian art into the international cultural space, and developing amateur and professional sports. NOVATEK entered into agreements with regional governments across the Company's footprint and implements programs to improve living standards and preserve the distinctive cultural identity of the indigenous peoples of the Far North.

In 2016, NOVATEK and its subsidiaries invested about RR 1,9 billion in projects and activities related to the support of indigenous peoples, charitable contributions, cultural and educational programs.

Cooperation with the regions

Within the framework of agreements signed with various regions, the Company made investments in the Yamal-Nenets Autonomous Area, and the Leningrad, Chelyabinsk, Tyumen, Samara and Kostroma Regions throughout 2016. The Company also financed the construction, repairs and upgrades of social infrastructure facilities as well as earmarked significant funds for implementing educational, cultural, children and youth programs and projects and was supporting low-income families, people with disabilities and the elderly.

Cooperation with Indigenous Peoples of the Far North

During 2016, NOVATEK provided financial support to the Yamal for Descendants Association of indigenous peoples and its district branches. We assisted indigenous peoples through financing the purchase of equipment and materials required for the work of fishermen and reindeer herders. NOVATEK financed fuel purchases for air delivery of the nomadic population and food to remote areas.

Educational Programs

NOVATEK continued to develop and support the Company's continuing education program, which provides opportunities to gifted students, from the regions where we operate, to further their education at top rated universities, participate in NOVATEK internships and, upon completion of their studies, possible employment with the Company.

Recruitment and career guidance for promising employees start with the "Gifted

Children" program implemented at School No. 8 in Novokuybyshevsk and School No. 2 in Tarko-Sale. In 2016, the "Gifted Children" class was opened in Tyumen vocational school №81. Special classes are formed on a competitive basis from the most talented grade 10 and 11 students with above-average test scores.

The Company also implemented two "Grants" programs for schoolchildren and teachers living in the Purovsky District of the YNAO.

The "Grants" program for schoolchildren is aimed at academic and creative development and encouraging a responsible attitude towards studies. Under the program, students in grades five (5) through 11 are awarded grants from the Company. In 2016, the Company awarded 36 grants to students under this program.

The "Grants" program for teachers is intended to raise the prestige of the teaching profession and create favorable conditions for developing new and talented teachers. In 2016, five (5) teachers from the Purovsky District received grants under this program.

In an effort to create conditions for more effective use of university and college resources in preparing students for future professional activities, the Company has developed and successfully implemented the NOVATEK-VUZ program. The program is an action plan for focused, high-quality training for specialists with higher education in key areas of expertise in order to grow the Company's business and meet its needs for young specialists. The program is based at the Saint-Petersburg University of Mines, the Gubkin Russian State University of Oil and Gas in Moscow and the Tyumen Industrial University.

Students, who have passed their exams with good and excellent results, receive additional monthly payments. During their studies, the students are offered paid field, engineering and directed internships. This experience allows them to apply the knowledge obtained at lectures and seminars to real-life situations and gain experience in the professions they have chosen, while the Company receives an opportunity to meet potential employees.

Preserving Cultural Heritage

In 2016, NOVATEK continued its cooperation with Russia's leading cultural and educational institutions, charity foundations, and creative groups. These include the Moscow Kremlin Museum, the Russian State Museum, the Moscow Museum of Modern Art, and the Multimedia Art Museum of Moscow.

The Moscow Kremlin Museum, with assistance from NOVATEK, prepared and hosted the exhibition titled “Elegance and Splendor of Art Deco. The Kyoto Costume Institute, Jewelry Houses Cartier and Van Cleef & Arpels”.

The Company supported the exhibition “Wassily Kandinsky and Russia” in the Russian State Museum to mark the 150th anniversary of the artist, one of the founders of the abstract art, and continued supporting the annual International Imperial Gardens of Russia Festival in St. Petersburg.

In partnership with NOVATEK, the Moscow Museum of Modern Art presented the exhibition “Little Golden America: based on a true story” devoted to Ilya Ilf’s and Evgeny Petrov’s travels as well as a solo exhibition of Stephan Balkenhol “Sculptures and Reliefs”.

Starting in late 2015, the education division of the Moscow Museum of Modern Art has been delivering a special course of lectures on the history of the 20th century Russian and foreign art, photography, architecture and cinema to the Company’s employees and their family members. To expand this activity, in 2016 the Company for the first time supported the educational program of the Fifth Moscow Biennale of Contemporary Art.

For several years, NOVATEK has been supporting the History of Russia in Photographs, a major program of the Multimedia Art Museum. In 2016, with the Company’s assistance, exhibitions “Sergey Shimansky. Leningrad” and “Alexander Rodchenko. Experiments for the Future” took place.

In 2016, NOVATEK traditionally cooperated as the General Partner with the Moscow Soloists Chamber Ensemble and acted as the General Partner of the tour across Russia and Europe of the Russian Youth Symphony Orchestra led by Yuri Bashmet.

Sports Projects

NOVATEK attaches great importance to programs for the development of amateur and professional sports. The Company, its subsidiaries

and joint ventures regularly hold tournaments in the most popular and wide-spread sports, such as football, volleyball, swimming, ski, etc.

The company supported the children and youth sports in the regions of its operations. The “NOVATEK – Step to Bigger Football” Indoor Football Cup among secondary school teams expanded its geographical presence in 2016. Besides the competition in the Chelyabinsk Region that were attended by several thousand boys and girls, the tournament was held in several cities and towns of the Kostroma Region and included more than one hundred teams.

The Company supported Figure Skating and Ice Hockey Federations of the Yamal-Nenets Autonomous Region, and Student Basketball Association with more than 800 teams and 10,000 boy and girls participating in competitions. The Russian Acrobatic Rock’n’roll Federation and the Company set up corporate acrobatic rock’n’roll clubs in the regions where the Company operates, and their students will take part in the Federation’s competitions as early as in the first half of 2017. In the reporting year, NOVATEK continued cooperation with the Football Union of Russia as the General Partner of the Russian National Football Team. The company supported woman’s volleyball club Dinamo and the NOVA Volleyball Club (Novokuybishevsk).

Charity

The Company has continued its cooperation with Chulpan Khamatova’s Gift of Life charitable foundation in 2016. The Company held two blood donor sessions for children from the Russian Children’s Clinical Hospital at its Moscow headquarters, in collaboration with the foundation.

The scope of activities undertaken by the All Together volunteer movement, which NOVATEK founded in 2008, expanded. Assistance to orphans and children with various illnesses, seniors, as well as support for the blood donor movement remained the main volunteer activities.

MANAGEMENT AND CORPORATE GOVERNANCE

CORPORATE GOVERNANCE SYSTEM

NOVATEK strives to commit to the highest standards of corporate governance. We believe that such standards are an essential prerequisite to business integrity and performance and provide a framework for socially responsible management of the Company's operations.

The Company has established an effective and transparent system of corporate governance complying with both Russian and international standards. NOVATEK's supreme governing body is the General Meeting of Shareholders. The corporate governance system comprises the Board of Directors, the Board Committees, and the Management Board, as well as internal control and audit bodies and the Corporate Secretary. The activity of all these bodies is governed by the applicable laws of the Russian Federation, NOVATEK's Charter and internal documents available on our website (www.novatek.ru).

NOVATEK strives to consider the principles of corporate governance outlined in the Corporate Governance Code recommended by the Central Bank of Russia (Information Letter № 06-52/2463 dated 10 April 2014). The Company follows the recommendations of the Code, as well as offering to our shareholders and investors other solutions that are intended to protect their rights and legitimate interests.

Since the Company's shares are listed on the London Stock Exchange in the form of depositary receipts, NOVATEK places great emphasis on the UK Corporate Governance Code and the Regulation of the European Parliament and of the Council on market abuse and follows their recommendations as far as practicable.

The Company adheres to the internal Corporate Governance Code approved by the Board of Directors in 2005 (Minutes No. 60 of 15 December 2005).

The Company also adheres to the internal Code of Business Ethics approved by the Board of Directors in 2011 (Minutes No. 133 of 24 March 2011). The Code establishes general norms and principles governing the conduct of members of the Board of Directors,

the Management Board and the Revision Commission, as well as NOVATEK's management and employees, which were drafted on the basis of moral and ethical values and professional standards. The Code also determines the rules governing mutual relationships inside the Company and NOVATEK's relationships with its subsidiaries and joint ventures, shareholders, investors, the government and public, consumers, suppliers, and other stakeholders.

In order to increase the effectiveness of the Company's corporate governance system and bring it into compliance with the current legislature, the Listing Rules of PAO Moscow Exchange and the requirements of the Corporate Governance Code, the following changes were made in the reporting year:

- the Board of Directors held on 5 February 2016 approved amendments to the Regulations on the Corporate Secretary;
- the Board of Directors held on 26 August 2016 approved NOVATEK's Internal Audit Policy, amendments to the Regulations on NOVATEK's Risk Management and Internal Control System and to the Regulations on NOVATEK's Board of Directors Remunerations and Nominations Committee;
- following the resolution of NOVATEK's General Meeting of Shareholders held on 30 September 2016 amendments were made to NOVATEK's Charter, the Regulations on the General Meeting of Shareholders of NOVATEK, the Regulations on the Board of Directors of NOVATEK, the Regulations on the Management Board of NOVATEK; and
- due to amendments to the Company's Charter, following the resolution of NOVATEK's General Meeting of Shareholders held on 30 September 2016 the company name OAO NOVATEK has changed to PAO NOVATEK.

NOVATEK's corporate governance practices make it possible for its executive bodies to effectively manage ongoing operations in a reasonable and good faith manner and solely to the benefit of the Company and its shareholders.

GENERAL MEETING OF SHAREHOLDERS

The General Meeting of Shareholders is NOVATEK's supreme governing body. The activity of the General Meeting of Shareholders is governed by the laws of the Russian Federation, the Company's Charter, and the Regulations on the General Meetings approved by NOVATEK's General Meeting of Shareholders in 2005 (Minutes No. 95 of 28 March 2005) with further alterations and amendments.

The General Meeting of Shareholders is responsible for the approval of annual reports, annual financial statements, the distribution of profit, including dividends payout, the election of the Board of Directors and the Revision Commission, approval of the Company's Auditor and other corporate and business matters.

On 22 April 2016, the Annual General Meeting of Shareholders approved the annual report, annual financial statements (in accordance with the Russian Accounting Standards), distribution of profit and the size of dividends based on the results of FY2015. The meeting also elected the Board of Directors and the Revision Commission, as well as approved remuneration to members of the Board of Directors, Revision Commission and the Company's external auditor for 2016 and approved interested-party transactions.

On 30 September 2016, the Extraordinary General Meeting of Shareholders approved the amount of interim dividend for the first half of 2016 and amendments to NOVATEK's Charter and internal documents regulating the activities of NOVATEK's bodies.

BOARD OF DIRECTORS

The Board of Directors (the Board) activity is governed by the laws of the Russian Federation, the Company's Charter and the Regulations on the Board of Directors approved by NOVATEK's General Meeting of Shareholders in 2005 (Minutes No. 96 of 17 June 2005) with further alterations and amendments.

The Board carries out the overall strategic management of the Company's activity on behalf of and in the interests of all its shareholders, and ensures the Company's efficient and effective performance in order to increase shareholder value in a prudent and responsible manner.

The Board determines the Company's strategy and priority lines of business, endorses long-term and annual business plans, reviews financial performance, internal control, risk management and other matters within its

competence, including optimization of corporate and capital structure, approval of major transactions, making decisions on investment projects and recommendations on the size of dividend per share and its payment procedure, and convening General Meeting of Shareholders. The General Meeting of Shareholders elects the members of the Board.

The current members of the Board were elected at the Annual General Meeting of Shareholders on 22 April 2016. The Board of Directors is comprised of nine (9) members, of which eight (8) are non-executive directors. Three (3) directors are considered to be independent in accordance with the Corporate Governance Code recommended by the Central Bank of Russia and the UK Corporate Governance Code. The Board Chairman is Alexander E. Natalenko. The Chairman is responsible for leading the Board and ensuring its effectiveness.

The members of NOVATEK's Board have a wide range of expertise as well as significant experience in strategic, operational, financial, commercial and oil and gas activities. The Board members hold regular meetings with NOVATEK's senior management to enable them to acquire a detailed understanding of NOVATEK's business activities and strategy and the key risks impacting the business. In addition to these formal processes, Directors have access to the Company's medium-level managers for both formal and informal discussions to ensure the regular exchange of information needed to participate in the Board meetings and make balanced decisions in a timely manner.

Efficient operation of the Board of Directors is supported by the Corporate Secretary, who has sufficient independence (appointed and dismissed by the Board of Directors) and endowed with the necessary powers and resources to carry out its tasks in accordance with the Regulations on the Corporate Secretary (Minutes No. 168 of 28 April 2014 with further alterations and amendments).

The Board of Directors membership as of 31 December 2016:

- Alexander E. Natalenko – Chairman of the Board
- Andrei I. Akimov
- Burckhard Bergmann
- Michael Borrell
- Robert Castaigne
- Leonid V. Mikhelson
- Victor P. Orlov
- Andrei V. Sharonov
- Gennady N. Timchenko

During 2016, there were no changes to the composition of NOVATEK's Board of Directors.

In accordance with the recommendations of the Corporate Governance Code and the Listing Rules of PAO Moscow Exchange, three (3) of the nine (9) elected members of the Board are considered independent directors.

Board activities during the 2016 corporate year¹

To ensure the Company's efficient performance, the Board meetings are convened on a regular basis at least once every two months. During 2016, the Board met 10 times, of which six (6) meetings were held in absentia. The following key issues were discussed and respective decision made:

- reviewed and approved the Company's 2016 full year operating and financial results;
- raised external financing for Yamal LNG;
- recommended an interim dividend for first half 2016, based on interim financial results for the period, and a full year dividend for 2016, based on full year financial results;
- reviewed and approved NOVATEK's business plan for 2017;
- submitted the following issues to the consideration of NOVATEK's Extraordinary General Meeting of Shareholders: amendments to NOVATEK's Charter and internal documents regulating the activities of NOVATEK's bodies; and
- approved NOVATEK's Internal Audit Policy.

Board and Committee meetings attendance in the 2016 corporate year

Member	Independence ²	Board of Directors	Audit Committee	Remuneration and Nomination Committee	Strategy Committee
Alexander E. Natalenko		10/10			4/4
Andrei I. Akimov		10/10			3/4
Burckhard Bergmann		10/10			4/4
Michael Borrell		10/10			4/4
Robert Castaigne	independent	10/10	4/4	4/4	
Leonid V. Mikhelson	executive	10/10			
Victor P. Orlov	independent	10/10	4/4	4/4	
Andrei V. Sharonov	independent	10/10	4/4	4/4	
Gennady N. Timchenko		10/10			4/4

BOARD COMMITTEES

The Company has three (3) Board Committees: the Audit Committee, the Strategy Committee and the Remuneration and Nomination Committee. The Committees' activities are governed by the specific Committee Regulations approved by the Board of Directors and are available on our website.

The Committees play a vital role in ensuring that the high standards of corporate governance are maintained throughout the Company and that specific decisions are analyzed and the

necessary recommendations are issued prior to general Board discussions. The minutes of the Committees meetings are circulated to the Board members and are accompanied by necessary materials and explanatory notes.

In order to carry out their duties, the Committees may request information or documents from members of the Company's executive bodies or heads of the Company's relevant departments. For the purpose of considering any issues being within their competence, the Committees may engage experts and advisers having necessary professional knowledge and skills.

¹ From the Annual General Meeting of Shareholders on 22 April 2016 until the Annual General Meeting of Shareholders on 21 April 2017.

² Independent Director as of 31 December 2016 in accordance with the Corporate Governance Code recommended by the Central Bank of Russia and the UK Corporate Governance Code.

Committees membership as of 31 December 2016

	Audit Committee	Strategy Committee	Remuneration and Nomination Committee
Chairman	Andrei V. Sharonov	Alexander E. Natalenko	Victor P. Orlov
Members	Robert Castaigne Victor P. Orlov	Andrei I. Akimov Burckhard Bergmann Michael Borrell Gennady N. Timchenko	Robert Castaigne Andrei V. Sharonov

Strategy Committee

The primary functions of the Strategy Committee are the determination of strategic objectives of the operations and control over the implementation of the strategy, as well as recommendations on the dividend policy.

In carrying out its responsibilities and assisting the members of the Board in discharging their duties, the Strategy Committee is responsible for but not limited to:

- evaluating the effectiveness of the Company's operations in the long-term;
- preliminarily reviewing and making recommendations on the Company's participation in other organizations;
- assessing voluntary and mandatory offers to acquire the Company's securities;
- considering the financial model and business valuation of the Company and its business segments in order to make recommendations to the Board of Directors in making decisions on the definition of business priorities of the Company;
- providing recommendations to the Board of Directors on transactions subject to approval by the Board of Directors; and
- providing recommendations to the Board of Directors with respect to the Company's policy on the use of its non-core assets.

In corporate year 2016, the Strategy Committee met four (4) times.

Remuneration and Nomination Committee

The primary functions of the Remuneration and Nomination Committee is the development of an efficient and transparent compensation practice of members of the Company's management, enhancement of the professional expertise and improvement of the Board of Directors' effectiveness.

In order to assist the Board, the Committee performs the following functions:

- develop and regularly review the Company's policy on remuneration of the members of the Board of Directors, members of the collective executive body and the sole

executive body of the Company, oversee its implementation and realization;

- preliminarily assess the work of the executive body of the Company for the year in accordance with the Company's remuneration policy;
- annual detailed and formalized performance self-appraisal or external appraisal of the Board of Directors and its members, as well as of BoD Committees, determination of the priority areas for reinforcing the Board of Director's composition;
- interaction with shareholders, which shall not be limited to major shareholders only, with a view to generate recommendations to the shareholders with respect to voting on the election of nominees to the Company's Board of Directors;
- plan appointments of members of the executive body and the sole executive body on the base of continuity principles; and
- supervision over disclosure of information on the Company's shares owned by the members of the Board of Directors and Management Board, and other key management employees.

In corporate year 2016, the Remuneration and Nomination Committee met four (4) times.

Audit Committee

The primary function of the Audit Committee is control over financial and operating activities of the Company. In order to assist the Board in performing control functions the Committee is responsible for but not limited to evaluating accuracy and completeness of the Company's full year financial statements, the candidature of the Company's external auditor and the auditor's report, and the efficiency of the Company's internal control procedures and risk management system.

The Audit Committee works actively with the Revision Commission, the external auditor and the Company's executive bodies, inviting NOVATEK's managers responsible for the preparation of the financial statements to attend the Committee meetings.

In corporate year 2016, the Audit Committee met four (4) times.

MANAGEMENT BOARD

NOVATEK's Management Board is a collegial executive body responsible for the day-to-day management of the Company's operations. The Management Board is governed by the laws of the Russian Federation, NOVATEK's Charter, decisions of the General Meetings of Shareholders and the Board of Directors and by other internal documents. More information regarding the Management Board's competence is provided in NOVATEK's Charter.

Members of the Management Board are elected by the Board of Directors from among the Company's key employees. The Management Board is subordinated to the Board of Directors and the General Meeting of Shareholders. The Chairman of the Management Board is responsible for leading the Board and ensuring its effectiveness as well as organizing the Management Board meetings and implementing decisions of the General Meeting of Shareholders and the Board of Directors. The Management Board acting as of 31 December 2016 is comprised of twelve (12) members elected by the Board of Directors on 30 August 2012 (Minutes No. 150 of 30 August 2012) and 12 March 2015 (Minutes No. 173 of 12 March 2015) and 10 March 2016 (Minutes No. 184 of 10 March 2016).

Management Board Members as of 31 December 2016:

- Leonid V. Mikhelson – Chairman
- Alexander M. Fridman – First Deputy Chairman
- Vladimir A. Baskov – Deputy Chairman
- Viktor N. Belyakov – Deputy Chairman of the Management Board for Economics and Finance
- Mark A. Gyetvay – Deputy Chairman
- Oleg V. Karpushin – Deputy Chairman of the Management Board - Operations Director
- Tatyana S. Kuznetsova – Deputy Chairman – Director of Legal Department
- Igor A. Plesovskikh – Deputy Chairman of the Management Board - Director for Geology
- Ilya V. Tafintsev – Director for Strategic Projects
- Lev V. Feodosyev – Deputy Chairman – Commercial Director
- Denis G. Khramov – Deputy Chairman
- Kirill N. Yanovskiy – Director for Finance

REMUNERATION TO MEMBERS OF THE BOARD OF DIRECTORS AND MANAGEMENT BOARD

The procedure for calculating the remuneration and compensations to members of NOVATEK's Board of Directors is governed by the Regulations on Remuneration and Compensations payable to members of NOVATEK's Board of Directors approved by the Annual General Meeting of Shareholders (Minutes No. 122 of 24 April 2015). According to the Regulations the remuneration consists of the following types:

- fixed part of remuneration;
- remuneration for attending the Board of Directors meetings; and
- remuneration for attending the meetings of the committees of the Board of Directors.

The fixed part of remuneration to a Board member constitutes RR 10 million per corporate year. The Chairman of the Board of Directors is paid a fixed remuneration for the performance of its functions in the amount of RR 20 million per corporate year. Members of the Board of Directors are also paid remuneration for attending the meetings of the Board of Directors in the maximum amount of RR 3 million per corporate year and remuneration for attending the meetings of the committees of the Board of Directors in the maximum amount of RR 2 million per corporate year. The Board members are also compensated for travel and lodging expenses related to implementation of their functions as NOVATEK Board of Directors members.

The procedure for and criteria of calculating remuneration to the Chairman and members of NOVATEK's Management Board, as well as the compensation of their expenses, are prescribed in the Regulations for the Management Board and the employment contracts they sign with the Company.

Information on remuneration of members of NOVATEK's Board of Directors and Management Board in 2016, RR mln

	Board of Directors³	Management Board
TOTAL PAID, INCLUDING:	133.38	1,996.5
Salaries	-	682.0
Bonuses	-	1,274.3
Fees	132.4	-
Other property advancements	0.98	40.2

INTERNAL CONTROL AND AUDIT

The Company has a system of internal control over financial and business operations in accordance with international best practices. The process of internal control is an integral part of the risk management process.

The system of internal control consists of the Board of Directors, the Audit Committee, the Chairman of the Management Board, the Management Board, the Revision Commission and the Internal Audit Division.

The primary objects of internal control are PAO NOVATEK, its subsidiaries and joint ventures, and their subdivisions, as well as their ongoing business processes.

In order to combat corruption, mitigate compliance, operational and reputation risks, the Company adopted the Anti-Corruption Policy and the Regulation on NOVATEK Risk Management and Internal Audit System approved by the Board of Directors on 1 September, 2014 (Minutes No. 170 of 1 September 2014).

Revision Commission

The Revision Commission consisting of four (4) members who are elected at the Annual General Meeting of Shareholders for a period of one year. The competence of the Revision Commission is governed by the Russian Federation Law On Joint Stock Companies No. 208-FZ dated 26 December 1995 as well as the Company's Charter and the Regulations on the Revision Commission approved by the General Meeting of Shareholders in 2005 (Minutes No. 95 of 25 March 2005).

The Revision Commission is an internal control body responsible for oversight of the

Company's financial and business activities. The Revision Commission performs audits of the Company's financial and business performance for the year, as well as any other period as may be decided by its members or other persons authorized in accordance with Russian Federation law and the Company's Charter. The results of these audits are presented in the form of findings by the Revision Commission.

In March 2017, the Revision Commission completed the on-site audit revision of financial and business activity of the Company for the year 2016. As a result, the conclusions about the reliability of the data contained in the Company's 2016 Financial Statements (under the Russian accounting standards) and Annual Report were prepared and submitted to the Annual General Meeting of Shareholders.

Internal Audit Division

In order to conduct a systematic, independent evaluation of the reliability and effectiveness of the risk management and internal control system as well as corporate governance practices the Company performs internal audits of the Company's operations. The internal audit function is implemented by the independent Internal Audit Division, which has operated continuously since 2005.

The Internal Audit Division is functionally subordinate to the Board of Directors and is guided by International professional internal audit standards of Institute of Internal Auditors. The Division also adheres to the principles and rules of conduct stated in internal auditor's Code of Business Conduct of the Institute of Internal Auditors. In 2016, the Board of Directors approved NOVATEK's Internal Audit Policy (Minutes No. 192 of 26 August 2016).

³ Some members of NOVATEK's Board of Directors are simultaneously members of the Management Board. Payments to such members in relation to their activities as members of the Management Board are included in the total payments to members of the Management Board.

The Division carries out its activities on the basis of an annual plan of inspections approved by the Audit Committee and uses a combination of risk-based and cyclic approaches. According to the results of inspections it develops measures to eliminate identified risks and optimize financial and business activities. Implementation of the measures is monitored on a regular basis.

The Internal Audit Division regularly interacts with the external auditor by exchanging information on action plans, audit results and other matters of significance to ensure the effective discharge of their responsibilities.

To improve the efficiency and optimize the costs the Internal Audit Division employees serve on the revision commissions of subsidiaries and joint ventures.

External Auditor

The Annual General Meeting of Shareholders appoints an external auditor to conduct independent review of NOVATEK's financial statements. The Audit Committee gives recommendations to the Company's Board of Directors regarding the candidatures of external auditors and the price of their services. Based on the Committee's recommendations, the Board proposes the auditor's candidature for the consideration and for approval by the Annual General Meeting of Shareholders.

AO PricewaterhouseCoopers Audit (an internationally recognized audit firm) was chosen as the Company's external auditor to conduct the audit of the annual financial statements for 2016 under RAS, as well as independent reviews of the Company's quarterly financial statements and audit of the annual financial statements under IFRS.

In selecting the auditor's candidature, attention is paid to level of their professional qualifications, independence, possible risk of any conflict of interest, terms of the contract, and

an amount of remuneration requested by the candidates.

The Audit Committee oversees the external auditor's independence and objectivity as well as the quality of the audit conducted. The Committee annually provides to the Board of Directors the results of review and evaluation of the audit opinion regarding the Company's financial statements. The Audit Committee meets with the auditor's representatives at least twice per year.

NOVATEK's management is aware of and accepts recommendations on the independence of the external auditor by restricting such auditor's involvement in providing non-audit services. Remuneration paid to the principle auditors for auditing and other services is specified in Note 24 to the consolidated financial statements prepared in accordance with IFRS standards for 2016.

SHARE CAPITAL

Our share capital is RR 303,630,600 and consists of 3,036,306,000 ordinary shares, each with a nominal value of RR 0.1. As of 31 December 2016, NOVATEK did not have preference shares.

Our shares are traded in Russian roubles on the Moscow Exchange and have a first grade listing (symbol: NVTK).

The Federal Financial Market Service issued to NOVATEK a permit for circulation of shares beyond the Russian Federation of 910,589,000 ordinary shares comprising 29.99% of the Company's share capital.

Our Global Depositary Receipts (GDR) are listed on the London Stock Exchange (symbol: NVTK), with each GDR representing 10 ordinary shares. As of 31 December 2016, NOVATEK's GDRs were issued on 910,574,600 ordinary shares comprising 29.99% of the Company's share capital.

Equity stakes in NOVATEK's share capital and the number of shares owned by members of the Board of Directors and Management Board⁴

	Equity stake as of 31 December 2016, %	Number of shares
Board of Directors		
Alexander E. Natalenko	-	-
Andrei I. Akimov	-	-
Burckhard Bergmann	-	-
Michael Borrell	-	-
Robert Castaigne	-	-
Leonid V. Mikhelson	0.7152	21,717,112
Victor P. Orlov	-	-
Andrei V. Sharonov	-	-
Gennady N. Timchenko	9.1583	278,073,034
Management Board		
Vladimir A. Baskov	0.0288	874,408
Viktor N. Belyakov	-	-
Mark A. Gyetvay	-	-
Oleg V. Karpushin	-	-
Tatyana S. Kuznetsova	0.1944	5,903,035
Igor A. Plesovskikh	-	-
Ilya V. Tafintsev	-	-
Lev V. Feodosyev	-	-
Alexander M. Fridman	0.0817	2,481,049
Denis G. Khramov	-	-
Kirill N. Yanovskiy	0.1051	3,192,530

In 2016, Gennady Timchenko, member of NOVATEK Board of Directors, made the following transactions with NOVATEK shares:

- transfer of 34,167,892 shares under a securities lending agreement (22 January 2016);
- transfer of 400,934,172 shares under a securities lending agreement (29 April 2016);
- receipt of 277,303,034 shares under a securities lending agreement (22 December 2016); and
- acquisition of 770,000 shares under a securities sales and purchase agreement (23 December 2016).

DIVIDENDS

The Company's Dividend Policy is regulated by the Regulations on Dividend Policy of PAO NOVATEK approved by the Board of Directors on 28 April 2014 (Minutes No. 168 of 28 April 2014). According to the regulations, consolidated net income under IFRS is applied for calculation of the dividend size.

NOVATEK's dividend policy is based on keeping the balance between the Company's business goals and shareholder's interests. A decision to pay dividends as well as the amount of the dividend, the payment deadline and form of the dividend is passed by the Annual General Meeting of Shareholders according to the recommendation

⁴ The equity stakes are given based on the records in the register of NOVATEK's shareholders and notification received from members of the Board of Directors and Management Board, in accordance with the Russian Federation laws.

of the Board of Directors. Dividends are paid twice a year. In determining the recommended amount of dividend payments to be distributed the Board of Directors consider the current competitive and financial position of the Company, as well as its development prospects, including operating cash flow and capital expenditure forecasts, financing requirements, debt servicing and other such factors as it may deem relevant to maintaining financial stability and flexible capital structure of the Company. NOVATEK is strongly committed to its dividend policy.

On 14 March 2017, the Board of Directors of PAO NOVATEK recommended to the Annual

General Meeting of Shareholders to pay dividends for FY 2016 in the amount of RR 7.0 per ordinary share or RR 70 per one Global Depositary Receipt (GDR), exclusive of RR 6.9 of interim dividends per ordinary share or RR 69 per one GDR paid for the first six months of 2016.

Thus, should the General Meeting of Shareholders approve the recommended dividend, the dividends for 2016 will total RR 13.9 per ordinary share (RR 139 per one GDR), and the total amount of dividends payable for 2016 will be RR 42,204,653,400. This will represent a 3.0% increase in dividend per share compared to 2015.

Accrued and paid dividends on NOVATEK shares for the period 2011 to 2016

Dividend accrual period	Amount of dividends, RR per share	Total amount of dividends accrued, RR	Total amount of dividends paid, RR
2011	6.00	18,217,836,000	18,217,661,018
2012	6.86	20,829,059,160	20,829,057,901
2013	7.89	23,956,454,340	23,956,346,951
2014	10.30	31,273,951,800	31,273,849,601
2015	13.50	40,990,131,000	40,989,939,487
First half 2016	6.90	20,950,511,400	20,950,494,606

The amount of paid dividends accrued for the years 2011 to 2015, and for the first six months 2016 is reported as of 31 December 2016. Partial payment of the accrued dividends was made due to provision by shareholders of incorrect postal and/or banking details and insufficient information regarding banking or postal details of shareholders.

INFORMATION TRANSPARENCY

NOVATEK is committed to providing objective, reliable, and consistent information about the Company and its activities to all stakeholders and also complies with best practices for information disclosure while adhering to a maximum level of transparency. The Regulations on Information Policy approved by the Board of Directors (Minutes No. 45 of 10 May 2005), define main principles for disclosing information and increasing information transparency.

Material information about the Company is disclosed in a timely manner in the form of press releases and material facts notifications through authorized disclosure in accordance with the applicable laws of Russian Federation

and United Kingdom. The Company discloses quarterly financial statements in accordance with the Russian ("RAS") and International Financial Reporting Standards ("IFRS"), Management's Discussion and Analysis of Financial Condition and Results of Operations as well as presentations for investors.

The Company's website provides detailed information on all aspects of its activities, including our Sustainability Report. We regularly participate in information disclosure on greenhouse gas emissions and energy efficiency of production – the Carbon Disclosure Project (CDP), and on the use of water resources – the CDP Water Disclosure Project, as well as other industry's publications and studies.

The Company maintains an ongoing dialogue with shareholders and investors in order to ensure full awareness of investment community about its activities. The main channels of communication with the investment community are through the Chairman of the Management Board, Deputy Chairman and the Investor Relations department. The Company's representatives meet on a regular base with key financial audiences to discuss issues of interest to them.

Pursuant to the uniform information policy principles, NOVATEK is actively involved in relations with federal, foreign and regional media. In 2016, the topics covered in mass media related to the Company's activities. As at the end of 2016, the number of publications on the Company's activities increased by 20%, and the number of TV spots on federal channels went up by 40%.

In 2016, the Public Relations Department hosted 10 meetings between the Company management and journalists of foreign and federal periodicals resulting in more than 25,000 publications. Among the topics covered were disposal and raising of LNG project-related investments, the Company's plans of business expansion, entering new markets and cooperation with European and Asian financial institutions.

Twelve tours were arranged for the Russian mass media journalists to visit the Company's regional production facilities and the areas involved in the Yamal LNG Project implementation.

The number of publications in foreign media increased, TV spots on the Yamal LNG Project implementation were issued on the TV channels

of France, Germany, Austria, Italy, Great Britain, China, Japan, and South Korea. More than four thousand publications were issued in foreign media in 2016. In May 2016, a dedicated press-tour was arranged for foreign journalists to visit the Yamal LNG site that was attended by 60 people from approximately 35 publications. Separate visits of camera units from Italy, Austria, Germany, France, United Kingdom and Japan to the company facilities Yamal LNG and NOVATEK-Yurkharovneftegas were arranged during the year.

NOVATEK takes active part in industrial exhibitions and conferences. In 2016, NOVATEK's managers and employees participated in more than 15 exhibitions, conferences and round tables. In 2016, the Company took part in the St. Petersburg International Economic Forum, Eastern Economic Forum, as well as governmental delegations within foreign business events. NOVATEK delegation also took part in the work of major international industry events – International Conference & Exhibition on Liquefied Natural Gas in Australia, V Eurasian Investment Forum in Verona, LNG Producer-Consumer Conference in Tokyo, etc.

ADDITIONAL INFORMATION

RISK MANAGEMENT SYSTEM

The Company's activities are subject to risks inherent only to the Company or associated with the Company's core business.

A multilevel system of risk management has been implemented at the Company. Powers, duties and responsibilities for specific risk management procedures are delegated to different governance levels of the Company depending on the assessment of financial impact of risk. The Company's risk management policy is laid out in the Regulations on OAO NOVATEK Risk Management and Internal Control System approved by the Board of Directors on 1 September 2014 (Minutes No. 170 of 1 September 2014) with amendments.

The Board of Directors' Audit Committee is responsible for the supervision over the reliability and efficiency of the risk management framework and review of the risk management policy. In the reporting year, the Audit Committee after careful review and analysis of the information provided, recognized NOVATEK's risk management activities as compliant with the risk management policy of the Company.

Below is the list of risks and approaches to risk management applied by the Company. The risks described herein are not exhaustive and reflect the opinion on the most material risks based on the estimates of the Company's management.

Risk	Risk description	Risk management approaches used by the Company
OPERATIONAL RISKS		
Risks of emergencies and incidents	The Company's subsidiaries and joint ventures are subject to the risks of emergencies and incidents at hazardous production facilities that may entail business interruption, hazardous emissions or spills, which in turn may have a negative effect on the Company's business reputation and financial performance.	The Company performs continuous monitoring of industrial safety compliance, develops and implements organizational and technical measures aimed at mitigating the risks of emergencies and incidents and reducing potential losses as part of its existing integrated industrial safety management system that is certified under the OHSAS 18001:2007 standard. The Company holds property and business interruption insurance policies. The Company adheres to the principle of responsible investments which implies that new design solutions, technologies and equipment installed help significantly mitigate accident risks. The Central Dispatch Office (CDO) operates in the Company, one of its function is to ensure prompt response to production incidents. Since 2017, the functionality of the CDO was expanded by adding centralized control of well construction and workover on top of the control of production, treatment and transportation processes.
Monopoly risks	The Company depends on monopoly suppliers of transport services (such as Gazprom, RZD, or Transneft). The Company has no influence on the capacity of transport facilities of the above monopolies and rates established by a Federal body.	The Company enters into long-term agreements and in a timely manner arranges for interaction with monopolies regarding hydrocarbon transportation by pipeline and railway transport. To reduce its dependency, the Company concludes agreements enabling it to use alternative methods of product transportation (an agreement with SIBUR for the supply of light hydrocarbons to Tobolsk Petrochemical Complex).

Competitive risks	<ul style="list-style-type: none"> • The Company operates in an environment of tough competition with Russian and international oil and gas companies in the following areas: • obtaining of subsoil licenses and acquisition of companies holding subsoil licenses • selling natural gas on the Russian market • selling liquid hydrocarbons in the Russian and global markets • acquisition of oil and gas equipment and services • access to transportation infrastructure, which has technological limitations • employment of highly qualified specialists to work for the Company and its subsidiaries and joint ventures. 	<p>The Company monitors commercially available assets with regard to the objectives of its long-term development strategy, enabling the Company to make an objective assessment of its competitive positions and to take the maximum benefit of its competitive advantages that include extensive regional work experience and synergy with the existing producing, transport, processing and distribution infrastructure.</p> <p>When acquiring equipment and services, the Company holds public tenders allowing it to diversify the suppliers and to ensure the best conditions. The Company works continuously to structure its relations with key service providers. Given the volatility in international relations with certain countries that are providers of sophisticated oil & gas equipment, the Company pursues import replacement policies where it is appropriate. The Company pursues an active marketing policy and takes efforts to expand its customer base, and to enter into long-term agreements with buyers. To diversify its natural gas marketing portfolio, throughout the reporting period the Company was engaged in trading in the Natural Gas Section of the St. Petersburg International Mercantile Exchange. The Company implements an active HR policy and applies efficient mechanisms of attracting and retaining highly qualified employees.</p>
Commodity price risks	<p>As an independent natural gas producer, NOVATEK is not subject to state regulation of natural gas prices. Nevertheless, the Company's prices are strongly influenced by the prices established by a Federal body. Moreover, the Company is exposed to the current pricing environment on the Russian and international liquid hydrocarbon markets as it has no power over the contracts' base prices. Reduction of prices for liquid hydrocarbons may have a negative effect on the Company's financial performance.</p>	<p>State regulation of gas prices significantly reduces the risk of price volatility on the Russian gas market. In view of the vertically integrated production chain for liquid hydrocarbons and taxation peculiarities, the Company does not use commodity derivative financial instruments to reduce the risk of price changes for such type of products.</p>
Geological risks	<p>Exploration drilling is associated with multiple risks, including the risk of non-discovery of commercial reserves. Information on the Company's reserves depends on a number of factors and assumptions. Actual production volumes at the fields, along with the cost-effectiveness of reserve development may deviate from estimates.</p>	<p>To minimize geological risks, the Company relies on the geological modeling and engages major contractors that apply state-of-the-art exploration technologies and methods.</p> <p>Since 2015, the Company has been employing foreign experts in geology and field development. Individual focused training programs have been implemented for the employees with due regard to periodic testing. The Company makes annual assessment and evaluation of its reserves based on the results of exploration and production drilling and other research information. An independent international adviser evaluates the Company's reserves according to international standards on annual basis.</p>
Risk of early termination, suspension or restriction of the right to use subsurface mineral resources	<p>Exploration and production of hydrocarbons in Russia is subject to licensing. The Company is thus exposed to the risk of early termination, suspension or restriction of its right to use subsurface mineral resources.</p>	<p>The Company strives to comply, and maintains a continuous monitoring of its compliance with the license agreements and the subsoil use laws, and submits timely requests for adjusting the terms of its license agreements.</p>

Environmental risks	<p>The Company is subject to the probability of events having adverse consequences for the environment and caused by a negative impact of its industrial and other activities, as well as natural and technology-related emergencies.</p>	<p>The Company and its key subsidiaries have an environmental management system according to ISO 14001:2004 standard to ensure rational use of resources and to minimize the adverse effect the Company's operation may have on the environment. The Company adheres to the principle of responsible investment in operations, which implies that new design solutions, technologies and equipment installed help minimize environmental impact.</p>
Project risks	<p>Volatile exchange rates of the national currency and unstable lending conditions, growing funding costs, drop in hydrocarbon prices, precarious financial position of contractors and oil and gas equipment suppliers may affect the Company's Investment Program leading to delays in project execution and/or rising project costs.</p>	<p>The Company implements expert review of projects at the project development stage. Investments are only channeled into the projects that are most likely to help the Company achieve its strategic objectives.</p> <p>The Regulation on Investment Projects Preparation, Coordination, Approval, Monitoring and Updating was approved in the Company in 2016. The project risks are evaluated at every stage.</p> <p>The Company has tightened its selection requirements for contractors and suppliers of oil and gas equipment. There is ongoing monitoring of their performance, including on-site visits to the oil and gas equipment plants involved in production and testing of the equipment for the Company.</p>
Ethical risks	<p>The Company is exposed to the risks of disturbed relationships within the Company and with its subsidiaries and joint ventures, shareholders, investors, the government, the public, consumers or suppliers or other corporate entities or individuals, including the risk of fraud, corruption, and conflict of interest.</p>	<p>In 2011 in order to minimize ethical risks, the Company introduced a Code of Business Conduct and Ethics.</p> <p>The Company is governed by the provisions of the internal Code of Business Conduct and Ethics and Code of Corporate Conduct, as well as the applicable Russian and English law in terms of public company regulation. This mitigates ethical risk to stakeholders and investors.</p> <p>To exclude ethical risks in its relations with third parties, the Company carries out tender procedures to select counterparties and has a well-established internal control and audit system.</p> <p>In 2014 the Board of Directors approved NOVATEK's Anti-Corruption Policy that established key principles and standards of anti-corruption practices for employees and includes a set of corruption prevention measures.</p> <p>As part of the Anti-Corruption Policy implementation a Security Hotline is in a 24/7 operation.</p> <p>In 2016, the Company established the procedure for notification and managing the conflicts of interest employees may come across in performing their job duties.</p>
Social risks	<ul style="list-style-type: none"> • The Company is subject to the following risks of a social nature: • internal risks associated with a possible incompliance of social programs implemented by the Company with the industry's average level that may lead to a higher labor turnover; • external risks associated with potential impediments in normal production activities caused by the public living in proximity to the production facilities 	<p>The Company strives to ensure compliance of its social programs with the industry's average level and uses the up-to-date mechanisms for attracting and retaining highly professional employees.</p> <p>The Company's production facilities are located outside densely populated territories, and the Company monitors compliance with the rules and regulations while operating its facilities. The risks related to possible military conflicts, announcement of a state of emergency, or strikes, are insignificant, as the Company operates in economically and socially stable regions.</p>

Terrorism risks	The Company is subject to a risk of terrorist threat.	The Company takes measures required to ensure strict compliance with Federal Law No. 256-FZ of 21 July 2011 concerning the Fuel and Energy Complex Security. A complex of organizational and practical measures is constantly in place to ensure security of facilities, including linear ones.
Country risk	NOVATEK is a Russian company operating in a number of Russian regions. Country risk is defined by the fact that Russia is still an emerging economy, the economic environment of which is not sufficiently stable. In 2015, a precipitous decline in crude oil prices and international sanctions caused volatility in foreign currencies, growing inflation rates, an increase in interest rates and an economic growth slowdown. The said factors have a negative impact on the Company's operational and financial performance.	Active marketing and financial policy enable the Company to mitigate the country risk. Moreover, the Company's management continuously analyzes the macro-economic environment and makes prompt decisions to mitigate potential risks.
Regional risk	The Company produces and processes hydrocarbons within Western Siberia, a region with a challenging climate.	The Company's vulnerability to region-specific impacts is insignificant and is entirely taken into account by the Company's management at the facilities design and operation stage.
Risks of information technology and information security (cyber-risks)	The Company is exposed to the risks in the area of information technologies and information security, such as unauthorized access and changing or destroying digital assets.	The Company uses a multilevel system for digital assets protection, namely: all information systems are classified, owners and terms for provision of access rights are defined in relation to each of them, information storage and archiving terms are regulated. The Company makes use of licensed software only. The information technology development strategy of NOVATEK has been developed and approved to ensure the Company's sustainable development.
FINANCIAL RISKS		
Credit risk	The Company is exposed to a risk of losses related to a failure by counterparties to perform their contractual financial obligations when due, and in particular depends on the reliability of banks in which the Company deposits its available cash.	When selling natural gas on the domestic market, the Company continuously monitors the financial soundness of its consumers and takes actions in case there are overdue payments. Most of NOVATEK's international liquid sales are made to major customers with independent ratings. Almost all domestic sales of liquid hydrocarbons are made on a 100 percent prepayment basis. When selecting banks, the Company is governed by the bank's reliability confirmed by international ratings.
Reinvestment risk	The Company's business requires substantial investments into field exploration and development, followed by the production, transportation, and processing of natural gas, oil, gas condensate and petroleum products. Insufficient funding for these and other expenditures may affect the Company's financial standing and performance.	The Company's capital investment plans are defined in its long-term development strategy, are revised on an annual basis and are generally in line with the Company's ability to generate cash flow from operations taking into account the need to pay dividend and service its debt.

Interest risks	As a major borrower, the Company is subject to risks associated with an increase in interest rates. Interest rates on some of the Company's loans may be linked to floating international and Russian base rates which dynamics are hard to predict. Volatile interest rates may restrict the use of borrowed capital as a financing source for the Company's investment activity and may increase interest rate expenses.	The Company pursues a balanced debt policy and strives to maximize the share of long-term liabilities with fixed rates in its debt portfolio. The Company strives to maintain flexibility in its investment program.
Currency risks	Part of the Company's liabilities is denominated in foreign currencies, which may lead to losses in the event of Russian rouble depreciation. On the other hand, part of the Company's proceeds is also denominated in foreign currencies, which may lead to losses in the event of Russian rouble appreciation.	The liabilities expressed in foreign currency on the one hand, and export proceeds on the other generally offset each other and serve as a natural mechanism to hedge currency risks.
Liquidity risk	Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due.	The Company's approach to managing liquidity risk is to ensure that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Company's reputation. In managing its liquidity risk, NOVATEK maintains an adequate ratio between cash reserves and debt, monitors forecast and actual cash flows and matches the financial assets and liabilities maturity profiles. The Company uses various short-term borrowings. The Company may use credit facilities and bank overdrafts to satisfy its short-term finance needs. To satisfy its needs for cash on a more permanent basis, the Company will normally raise long-term loans in the available markets.
Inflation risk	Changes in the consumer price index have an impact on NOVATEK's profitability and, as a consequence, its financial standing. The significant currency depreciation in 2015 caused a surge in inflation rates, which are impossible to accurately predict.	NOVATEK may not be able to predict the inflation level, since, apart from the consumer price level, it is necessary to take into account the change in the real purchasing power of the Russian rouble, the pricing conditions in liquid hydrocarbon export markets, and government policy in relation to tariffs for natural gas. NOVATEK monitors the consumer price index and accordingly acts to mitigate its costs.

LEGAL RISKS

Risk of law changes	<ul style="list-style-type: none"> • The Company is subject to a risk of facing consequences of changes in Russian laws in the following areas: • currency laws (in areas concerning export/import and borrowing operations) • tax laws (in areas regulating taxation systems and rates applicable to companies in general, and to companies producing and marketing natural gas and liquid hydrocarbons, specifically) • customs laws (in areas concerning the export of liquid hydrocarbons, including petroleum products); and • licensing requirements for natural resource extraction. 	The Company is constantly monitoring draft laws enabling it to evaluate the consequences of such changes and to take them into account in its plans.
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Litigation risks	The Company may be involved as a defendant or plaintiff in a number of proceedings arising in the normal course of its business.	When conducting its business, the Company adheres to the principle of prudence. Due to this fact, as of the approval date of the Annual Report, the Company was not involved in any material litigation and the associated risks are insignificant.
Risk of sanctions	In 2014, the Company was included into the US sectoral sanctions list whereby the US persons are prohibited to participate in providing financing to the Company for more than 90 days. The sanctions imposed restrict the Company's ability to refinance its debt. Furthermore, there is a risk of tougher US sanctions and risk of including the Company into other countries' sanctions lists, which may undermine the Company performance.	The Company follows a balanced financial policy enabling it to minimize its fundraising needs. Moreover, the Company still has a full access to the Russian capital market and a limited access to the international market. In case the US sanctions are toughened and the Company is included in other countries' sanctions lists, the Company management will make every possible effort to minimize the negative impact on the Company's business operations and financial standing.

Risk Insurance

Risk insurance is an integral part of NOVATEK's risk management system. In 2016, the insurance coverage guaranteed adequate protection against the risks of damage to the business of the Company or its subsidiaries and joint ventures. Insurance is provided by reputable insurance companies that have high ratings by leading rating agencies (Standard & Poor's, Expert RA, A.M. Best) with partial reinsurance of risks by major international insurance and reinsurance companies.

Obligatory Risk Insurance

The Company and its subsidiaries and joint ventures fully meet the requirements of the applicable laws for maintaining obligatory insurance, such as civil liability insurance of:

- owners of hazardous production facilities; and
- owners of transport vehicles.

Optional Risk Insurance

To reduce the risk of financial losses, the Company and its subsidiaries and affiliates maintain the following types of optional insurance:

- Insurance of the risk of property damage/loss, including the risk of mechanical failures;
- Insurance of the risk of damage from business interruption;
- Insurance of risks related to prospecting, exploration and production (risk of loss of control over a well); and
- Management liability insurance.

Since 2013, the Company implemented a comprehensive program of property and business risk insurance with respect to its and its subsidiaries' and joint venture's key assets. The cumulative insured amount for the risks of property damage and business interruption as at the

end 2016 was RR 512 billion. The implemented program is viewed by the Company's management as an efficient measure for mitigating the consequences of potential accidents and provides additional guarantees for the attainment of the expected net profit and key indicators of the Company's performance.

In the reporting year, no insured major accidents or incidents occurred.

At the end of 2016, one of NOVATEK's subsidiaries entered into a one-year contract for insurance of receivables of an approved natural gas consumer list with a view to assess how efficiently this instrument is used to manage risks.

For more than 11 years the Company has maintained a management liability insurance for the top management of the Company and its subsidiaries against possible third-party claims for any losses incurred through any wrong action (or decision) made by its management bodies. The overall limit of all insurance coverage is Euro 120 mln.

INFORMATION ON MEMBERS OF NOVATEK'S BOARD OF DIRECTORS

MR. ALEXANDER E. NATALENKO

- Chairman of NOVATEK's Board of Directors and Chairman of its Strategy Committee
- Born in 1946

Mr. Natalenko completed his studies at the Irkutsk State University in 1969 with a primary focus in Geological Engineering. Subsequently, he worked with the Yagodinskaya, Bagdarinskaya, Berelekhskaya, Anadirskaya and East-Chukotskaya geological expeditions. In 1986, Mr. Natalenko headed the North-East Industrial and Geological Association

and, in 1992, he was elected president of AO "Magadan Gold & Silver Company". He subsequently held various executive positions in Russian and foreign geological organizations. From 1996 to 2001, Mr. Natalenko held the position of Deputy Minister of Natural Resources of the Russian Federation. From 2013 to 2015 he was a member of the Board of Directors of AO Rosgeologia. From 2004 to present he is the Chairman of NOVATEK's Board of Directors.

Mr. Natalenko is the recipient of the State Prize of the Russian Federation and an Honored Geologist of Russia.

MR. ANDREI I. AKIMOV

- Member of NOVATEK's Board of Directors and Member of its Strategy Committee
- Born in 1953

Mr. Akimov graduated from the Moscow Financial Institute in 1975 where he specialized in international economics. Between 1974 and 1987, Mr. Akimov held various executive positions in the Bank for Foreign Trade of the USSR. From 1985 to 1987 he served as Deputy Chief General Manager of the Bank for Foreign Trade branch in Zurich (Switzerland) and between 1987 and 1990, Mr. Akimov was the Chairman of the Management Board of Donau Bank in Vienna (Austria). From February 1991 to January 2003 he was Managing Director of financial company, IMAG Investment Management & Advisory Group AG (Austria). Since 2003, Mr. Akimov has been the Chairman of the Management Board, the Deputy Chairman of the Board of Directors of Gazprombank (OAO). He is a member of Board of Directors of PAO Gazprom, Gazprombank (AO), PAO Rosneft, AO Rosneftegaz, OOO Gazprom gas motor fuel, Bank GPB International S.A. and other.

DR. BURCKHARD BERGMANN

- Member of NOVATEK's Board of Directors, and Member of its Strategy Committee
- Born in 1943

Dr. Bergmann studied physics at the Freiburg and Aachen Universities from 1962 to 1968 and was awarded a Doctorate in Engineering by Aachen University of Technology in 1970. From 1968 to 1969, Dr. Bergmann worked at the German Federal Ministry for Research and Technology and from 1969 to 1972 – at the Jülich Nuclear Research Center. In 1972, Dr. Bergmann joined Ruhrgas AG (from 1 July 2004 – E.ON Ruhrgas AG), heading the LNG Purchasing Department. In 1978, he became Head of the Gas Purchasing Division

responsible for gas purchasing, commercial aspects of gas transmission and storage. In 1980, he was elected as a member of the Management Board of E.ON Ruhrgas AG, serving from June 1996 as its Vice-Chairman and from June 2001 to February 2008 as its Chairman. From March 2003 to February 2008 he was also a member of the Management Board of E.ON AG.

Till 2013 Dr. Bergmann was a member of the Boards of Directors (Supervisory Boards) of: Allianz Lebensversicherungs-AG, Commerzbank AG, Contilia GmbH. At present, he is a Chairman of the Supervisory Board of Accumulatoren-werke Hoppecke GmbH, a member of the Advisory Boards of Contilia GmbH and Dana Gas and a member of the Board of Trustees of RAG Stiftung.

Dr. Bergmann holds the following distinctions: Commander of the Royal Norwegian Order of Merit (1997); Honorary Consul of the Russian Federation in the State of North Rhine-Westphalia; a Foreign Member of the Academy of Technological Sciences of the Russian Federation (2003); Order of Merit of the State of North Rhine-Westphalia (2004) as well as a winner of Director of the Year, Moscow (2007); Officer's Cross of the Order of Merit of the Federal Republic of Germany (2008). In June 2011, by means of presidential Decree he became a recipient of the Order of the Friendship of Peoples award for significant contribution in development of the Russian-German relations.

MR. MICHAEL BORRELL

- Member of NOVATEK's Board of Directors and Member of its Strategy Committee
- Born in 1962

Mr. Borrell graduated from the University of Cambridge with a degree in Chemical and Mechanical Engineering (Master of Science – 1993, Bachelor – 1984). He joined TOTAL in 1985. Mr. Borrell worked with the affiliated companies of the concern; from 1995 he held a number of senior management positions in TOTAL. From 2003, he worked at the position of Vice-President for Corporate Planning and Business Development in Total E&P Indonesia. In July 2006, he was appointed President and CEO of TOTAL E&P Canada in Calgary. From September 2009 to June 2010, he was Vice President of the Caspian Area and Central Asia for TOTAL Exploration and Production. From July 2010, he worked as First Vice President of Continental Europe and Central Asia. Since 1 January 2015, he has been appointed Senior Vice-President of Europe and Central Asia.

MR. ROBERT CASTAIGNE

- Independent member of NOVATEK's Board of Directors
- Member of the Remuneration and Nomination Committee of NOVATEK's Board of Directors
- Member of the Audit Committee of NOVATEK's Board of Directors
- Born in 1946

Mr Castaigne graduated from the Ecole Centrale de Lille in 1968 and the Ecole nationale supérieure du pétrole et des moteurs, he holds a doctorate in economics. He has spent his whole career at TOTAL SA, first as an engineer, then in various positions. From 1994 to 2008, he was Member of the Executive Committee, Executive Vice-President and Chief Financial Officer of TOTAL SA. He is Member of SANOFI's Board of Directors and Chairman of its Audit Committee, Member of VINCI's Board of Directors and its Audit and Remuneration Committees, Member of Societe Generale's Board of Directors and its Risk, Audit and Internal Control Committees. He is Chevalier of the National Order of the Legion of Honour.

MR. LEONID V. MIKHELSON

- Member of NOVATEK's Board of Directors
- Chairman of NOVATEK's Management Board
- Born in 1955

Mr. Mikhelson received his primary degree from the Samara Institute of Civil Engineering in 1977, where he specialized in Industrial Civil Engineering. That same year, Mr. Mikhelson began his career as foreman of a construction and assembling company in Surgut, Tyumen region, where he worked on the construction of the first section of Urengoi-Chelyabinsk gas pipeline. In 1985, Mr. Mikhelson was appointed Chief Engineer of Ryazantruboprovodstroy. In 1987, he became General Director of Kuibishevtruboprovodstroy, which in 1991, was the first company in the region to sell its shares and became private company, AO SNP NOVA. Mr. Mikhelson remained SNP NOVA's Managing Director from 1987 through 1994. Subsequently, he became a General Director of the management company "Novafininvest".

Since 2003, Mr. Mikhelson has served as a member of the Board of Directors and Chairman of the Management Board of NOVATEK. From March 2008 to December 2010, he has been a member of the Board of Directors and the Chairman of the Board of Directors of AO Stroytransgas. From 2009 to 2010 he was the Chairman of the Board of

Directors of OAO Yamal LNG and from 2008 to 2011 he was a member of the Board of Directors of OOO Art Finance. From 2011 he is the Chairman of the Board of Directors of PAO SIBUR Holding and from 2011 to 2013 he was a member of the Supervisory Board of the OAO Russian Regional Development Bank. Mr. Mikhelson is the recipient of the Russian Federation's Order of the Badge of Honor, the Order of Merit for the Fatherland 2 degree and the title of honor "Honored man of the gas industry".

MR. VICTOR P. ORLOV

- Independent member of NOVATEK's Board of Directors
- Chairman of NOVATEK's Remuneration and Nomination Committee
- Member of NOVATEK's Audit Committee
- Born in 1940

In 1968, Mr. Orlov graduated from the Tomsk State University as a geological engineer with a degree in "Geological survey and exploration of mineral deposits", and in 1986 from the Academy of National Economy under the USSR Council of Ministers, with a specialty in "Economics and Management of a National Economy".

From 1957 to 1963, he worked at coal mine and served in the Soviet Army. From 1968 to 1975, he was head of a geological survey, prospecting and exploration works in the geological organizations of Western Siberia, held positions of the geologist, chief geologist, chief of geological exploration crew. 1975-1978 - Consultant on geological exploration works in Iran. 1979-1981 - Deputy Head of the Geological Division of the Production Geological Association of central areas of Russia (Tsentrgeologiya). 1981-1986 - Deputy Head of Geology and Production departments of the Ministry of Geology of the RSFSR. 1986-1990 - CEO of Tsentrgeologiya. 1990-1992 - Deputy Minister of Geology of the USSR, First Deputy Chairman of the RSFSR State Committee for Geology and Use of Energy and Mineral Resources. 1992-1996 - Chairman of the Russian Federation Committee on Geology and Mineral Resources. 1996-1999 - Minister of Natural Resources of the Russian Federation. 2001-2012 - Member of the Federation Council of the Federal Assembly of the Russian Federation. 2001-2004 - First Deputy Chairman of the Federation Council Committee on Natural Resources and Environmental Protection. 2004-2011 - Chairman of the Federation Council Committee on Natural Resources and Environmental

Protection. From 1998 to present - President of "Russian Geological Society" public organization. Author and co-author of over 300 scientific publications.

Professor, Doctor of Economics (1991), Candidate of geological-mineralogical sciences (1974), an Honored Geologist of Russia. Laureate of the State Prize of the Russian Federation in the field of science and technology. He was awarded the Order of Merit for the Fatherland 4 degree (2001), the Order of Honor (2015), 18 non-governmental awards, including 3 appreciation letters of the President of the Russian Federation, 2 Certificates of Merit of the Government of the Russian Federation.

MR. ANDREI V. SHARONOV

- Independent member of NOVATEK's Board of Directors
- Chairman of NOVATEK's Audit Committee
- Member of NOVATEK's Remuneration and Nomination Committee
- Born in 1964

Mr. Sharonov graduated from the Ufa Aviation Institute and the Russian Academy of State Service at the President of the Russian Federation.

1989-1991 - Member of the USSR Parliament, until 1996 he headed the Committee for Matters Concerning Young Persons of the Russian Federation. From 1996 to 2007 - Head of Department, Deputy Minister, State Secretary in the Ministry of Economic Development and Trade of the Russian Federation. From 2007 to 2010 - Managing Director and Chairman of the Board of Directors of ZAO Investment Company Troika Dialog, head of the investment banking sector. From 2010 to 2013 - Deputy Mayor of Moscow for economic policy, was responsible for budgeting, procurement, industrial policy and business support, regulated market of trade and services. Served as a Chairman of the Regional Energy Commission. From September 2013 - President of the Moscow School of Management SKOLKOVO and Adviser to the Mayor of Moscow.

From 2011 to 2015 at various times he was a member of ALROSA's Supervisory Board (PAO); member of the Board of Directors of OAO Bank of Moscow and of "National Research University "Higher School of Economics".

He is currently a member of the Board of Directors of PAO Sovcomflot; Chairman of the Board of Directors, an Independent member of the Board of Directors of OOO Management Company NefteTransService; Chairman of the Board of Directors of PAO Management

Company Eko-sistema; a member of the Board of Directors of AO Rosgeologia, a member of the Supervisory Board of the Bank VTB (PAO).

Candidate of sociological sciences, an Honored Economist of the Russian Federation. He is the recipient of the "Aristos" Award in the "Independent Director" category in 2009, the National Award "Director of the Year – 2009" in the "Independent Director" category and the International Award "Person of the Year – 2012" in the "Business reputation" category. He was awarded the Order of Honor of the Russian Federation.

MR. GENNADY N. TIMCHENKO

- Member of NOVATEK's Board of Directors
- Member of NOVATEK's Strategy Committee
- Born in 1952

In 1976, Mr. Timchenko graduated with a Master's of Science from the Mechanical University in Leningrad. He began his career at the Izjorskii Factory in Leningrad, an industrial plant which made components for the energy industry. Between 1982 and 1988, he was a Senior Engineer at the Ministry of Foreign Trade. Mr. Timchenko has more than 20 years of experience in Russian and International energy sectors and he has built interests in trading, logistics and transportation related companies.

In 1988, Mr. Timchenko became a vice president of Kirishineftekhimexport, the export and trading arm of the Kirishi refinery. In 1991, he worked for Urals Finland which specialized in oil and petrochemical trading. Between 1994 and 2001, Mr. Timchenko was managing Director of IPP OY Finland and IPP AB Sweden. Between 1997 and 2014, he co-founded Gunvor, a leading independent oil-trading company. Mr. Timchenko was a member of the Board of Directors of OOO Transoil and OOO BalttransService, and Airfix Aviation OY. Since 2009, he is a member of the Board of Directors of PAO NOVATEK. He is a member of the Board of Directors of PAO SIBUR Holding, the Chairman of the Board of Directors, President of the Ice Hockey Club SKA St-Petersburg, as well as the Chairman of the Board of Directors of OOO Kontinental Hockey League, a member of the Board of Trustees of the All-Russian public organization Russian Geographical Society, the Chairman of the Russian Council of the NPO Russian Chinese Business Council, the Chairman of the Board to promote OCD, Vice-President of the Olympic Committee of the Russian Federation, the Chairman of the Economic Council of the Franco-Russian Chamber of Commerce (CCIFR).

INFORMATION ON MEMBERS OF NOVATEK'S MANAGEMENT BOARD

MR. LEONID V. MIKHELSON

- Chairman of NOVATEK's Management Board
- Member of NOVATEK's Board of Directors
- Born in 1955

Details on Mr. Leonid V. Mikhelson are available in the "Information on Members of NOVATEK's Board of Directors" section.

MR. VLADIMIR A. BASKOV

- Deputy Chairman of NOVATEK's Management Board
- Born in 1960

In 1986, Mr. Baskov graduated from the Moscow Higher Police School of the USSR. In 2000, he completed courses at the Management Academy at the Russian Ministry for Internal Affairs. From 1981 to 2003, he served in various departments within the Russian Ministry for Internal Affairs. From 1991 to 2003, Mr. Baskov held managerial positions within the aforementioned Ministry's organizational structures. In 2003 he was appointed Director of the Business Support Department for NOVATEK. In 2005 he was appointed Deputy Chairman of NOVATEK's Management Board and in 2007 he became a member of NOVATEK's Management Board. Candidate of legal Sciences. He was awarded the Order For Personal Courage, the Russian Federation's Order of the Badge of Honor and other state and departmental awards: Honorary Diplomas of the President of the Russian Federation, the Minister of Internal Affairs, the Governor of the Moscow Region. He also has the awards of the Russian Orthodox Church (Order of Holy Prince Daniel of Moscow and a medal of St. Sergius).

MR. VIKTOR N. BELYAKOV

- Deputy Chairman of the Management Board for Economics and Finance
- Born in 1973

Mr. Belyakov graduated from Tver State Technical University majoring in Automated Data Processing and Management Systems (1995) and in Information Systems in Economics (1997). In 2000, he completed an MBA degree program with Kingstone University (UK). A holder of CMA (Certified Management Accountant).

From 2004 till 2014 Mr. Belyakov worked for PAO Uralkali, where he successively held

the positions of Head of Division, Deputy Chief Financial Officer, Chief Financial Officer, Vice President for Finance, Deputy General Director, Executive Director. In 2015 he was appointed Vice President for Economics and Finance of PAO Far East Shipping Company (FESCO group). In February 2016, Viktor Belyakov joined PAO NOVATEK in the position of Deputy Chairman of the Management Board for Economics and Finance.

MR. MARK A. GYETVAY

- Deputy Chairman of NOVATEK's Management Board
- Born in 1957

Mr. Gyetvay studied at Arizona State University (Bachelor of Science, Accounting, 1981) and later at Pace University, New York (Graduate Studies in Strategic Management, 1995). After graduation, Mr. Gyetvay worked in various capacities at a number of independent oil and gas companies (Champlin Petroleum Co., Texas, Ensource Inc. and MAG Enterprises, Colorado, and Amerada Hess Corporation, New Jersey) where he specialized in financial and economic analysis for both upstream and downstream segments of the petroleum industry.

In 1994, Mr. Gyetvay began his work at Coopers and Lybrand, as Director, Strategic Energy Advisory Services. He subsequently moved to Moscow in 1995 with Coopers & Lybrand to lead the oil and gas practice. He was admitted as a partner of PricewaterhouseCoopers Global Energy where he assumed the role of client service engagement partner, Utilities and Mining practice, based in Russia (Moscow office). Mr. Gyetvay was an engagement partner on various energy and mining clients providing overall project management, financial and operational expertise, maintaining and supporting client service relationships as well as serving as concurring partner on transaction services to the petroleum sector.

Mr. Gyetvay is a Certified Public Accountant (inactive status), a member of the American Institute of Certified Public Accountants and an associate member of the Society of Petroleum Engineers. He is a recognized expert in the oil and gas industry, a frequent speaker at various industry and investor conferences, has published numerous articles on various oil and gas industry topics and was a former member of PwC's Petroleum Thought Leadership team. He has been recognized by Investor Relations Magazine as one of the best CFO's in Russia and the CIS,

and more recently by Institutional Investor magazine as one of the Top Five CFO's in Europe's Oil and Gas sector. Finance Monthly magazine recently named Mark Gyetvay the Best CFO in Russia for the years 2015 and 2016.

From 2003 to 2014, Mr. Gyetvay was a member of NOVATEK's Board of Directors and served on the Investment and Strategy Committee. In 2003-2014, he has been Chief Financial Officer and, in August 2007, Mr. Gyetvay was elected to NOVATEK's Management Board. In July 2010, he became Deputy Chairman of NOVATEK's Management Board.

MR. OLEG V. KARPUSHIN

- Deputy Chairman of the Management Board - Operations Director
- Born in 1968

In 1993, graduated from Moscow University of Oil and Gas named after I.M. Gubkin with distinction majoring in Oil and Gas Fields Exploration and Development. In 2013, received an MBA degree from the Duke University (USA).

In 1993, he started his career as a Field Engineer with Schlumberger, worked as well cementing technical instructor in the Kellyville Training Centre (USA), HSE Manager and Fracturing Field Service Manager in the Western Siberia, Business Development Manager in Central Asia, GeoMarket Operations Manager for Russia and Belarus for fracturing, cementing and coiled tubing services. In 2004, he joined Shell Corporation and commenced working in its joint venture Sakhalin Energy Investment Company Ltd. where he worked as Astokh field Operations Manager and then as Offshore Asset Manager responsible for offshore oil and gas production. In 2010, he moved to the position of Asset Manager for Shell Petroleum Development Company of Nigeria Ltd responsible for oil and gas production in its western division. In 2013, he became Chief Executive Officer at Salym Petroleum Development N.V.

In September 2015, he joined PAO NOVATEK in the position of Deputy Chairman of the Management Board — Director for Operations.

MS. TATYANA S. KUZNETSOVA

- Deputy Chairman of NOVATEK's Management Board
- Director of NOVATEK's Legal Department
- Born in 1960

Ms. Kuznetsova graduated from the Far East State University with a degree in Law.

From 1986, she was Senior Legal Advisor for a legal bureau. In 1993, Ms. Kuznetsova became Deputy General Director for Legal Issues and from 1996, Marketing Director for OAO Purneftegasseologiya. In 1998, she was appointed Deputy General Director of OAO Nordpipes. Since 2002, she has been Director of the Legal Department for NOVATEK. Since 2005, she has been the Deputy Chairman of NOVATEK's Management Board - Director of NOVATEK's Legal Department and in August 2007, she became a member of NOVATEK's Management Board. Ms. Kuznetsova has the title "Honored employee of PAO NOVATEK", and is awarded the Order of Merit for the Fatherland 2 degree.

MR. IGOR A. PLESOVSKIKH

- Deputy Chairman of the Management Board - Director for Geology
- Born in 1970

In 1993, Mr. Plesovskikh graduated from Tyumen Industrial Institute specialising in Oil and Gas Geology.

He has over 20 years of experience in the oil and gas industry. He started his career as Assistant Driller at Noyabrskneftegaz, subsequently holding the positions of General Director at Urengoyneftegazgeologia, General Director at YARGEO, Deputy General Director — Chief Geologist at NOVATEK-TARKOSALENEFTEGAZ, Deputy General Manager of the Federal Agency for Subsoil Use Rosnedra and Deputy General Director — Chief Geologist at ITERA Oil & Gas Company.

In December 2015, he joined PAO NOVATEK in the capacity of Deputy Chairman of the Management Board – Director for Geology.

Igor Plesovskikh has been awarded the Certificate of Merit of the Ministry of Natural Resources and Environment of the Russian Federation.

MR. ILYA V. TAFINTSEV

- Member of the Management Board - Director for Strategic Projects
- Born in 1985

In 2006 Mr. Tafintsev obtained a BA in Economics from the Higher School of Economics in Moscow. In 2007 graduated from University of London, where he majored in Investment and Finance. From 2007 to 2011 Mr. Tafintsev held the position of Deputy Head of PAO NOVATEK's Representative Office in London. In 2011-2014, he was a Finance & Investment Advisor with United Bureau of Consultants Limited.

Since 2013 he has served as a Strategic Projects Director of PAO NOVATEK, a member of the Board of Directors at SIBUR Holding. From 2014 to 2016 he was Chairman of the Board of Directors of OAO Yamal LNG. In December 2015, Mr. Tafintsev was appointed Member of the Management Board — Director for Strategic Projects of PAO NOVATEK.

MR. LEV V. FEODOSYEV

- Deputy Chairman of NOVATEK's Management Board – Commercial Director
- Born in 1979

In 2002, Mr. Feodosyev graduated from the Bauman Moscow State Technical University with a degree in Machinery and Foundry Engineering Technologies. In 2002, Mr. Feodosyev was appointed lead specialist at the Ministry of Energy of the Russian Federation. From 2003, he has served as lead specialist, senior specialist, adviser, deputy head of section, Deputy Director of Department at the Ministry of Economic Development and Trade of the Russian Federation. From October 2007, Mr. Feodosyev worked in NOVATEK as Director of the Strategic Planning and Development Department. From 2011, he was appointed as Deputy Commercial Director, Director of the Marketing and Gas Sales Department of NOVATEK. Since February 2015, he has been appointed Commercial Director, Deputy Chairman of the Management Board of NOVATEK.

In 2014, Mr. Feodosyev was awarded NOVATEK's Honorary Certificate.

MR. ALEXANDER M. FRIDMAN

- First Deputy Chairman of NOVATEK's Management Board
- Born in 1951

In 1973, Mr. Fridman graduated from the Gubkin Institute of Oil and Gas in Moscow, with a degree in Oil and Gas Fields Development and Exploitation. Since 1973, he was employed by various Gazprom companies: as Chief Engineer of Nadymgazprom, Head of the Production and Technical Department of the Industrial Association, and Chief Engineer of Mostransgaz's Kaluga Department for Gas Transportation and Underground Storage. From 1992 to 2003, he was Technical Director, First Deputy General Director of a joint venture established by PAO Gazprom and DKG-EAST (Hungary). Since 2003 Mr. Fridman was the Deputy General Director of Novafininvest. In 2004, Mr. Fridman was elected Deputy

Chairman of the Management Board of PAO NOVATEK. In August 2007, he was appointed a member of NOVATEK's Management Board. From February 2015 First Deputy Chairman of the Management Board of PAO NOVATEK. Mr. Fridman is the recipient of the title of honor "Honored man of the oil and gas industry".

MR. DENIS G. KHRAMOV

- Deputy Chairman of the Management Board
- Born in 1975

Graduated in 1997 from the Urals State Law Academy with a degree in Law. In 1999 completed a master's course in Private Law with the Russian School of Private Law. In 2004, he obtained his candidate degree in Law.

From 1995 he was an in-house counsel at Transneftgaz CJSC. In 1997, he joined the Legal Center for Northern Territories as a lawyer and was subsequently appointed Chief Specialist and Deputy Head of Department with the Russian Ministry of Fuel and Energy in 1999.

In 2001, he was appointed Deputy Head of Department and Head of Department with the Russian Ministry of Economic Development and Trade.

In 2002, he joined Zarubezhneft JSC as Deputy Head of Division with the responsibility of supervising subsoil use, economic and financial affairs. In 2007 he became Senior Lawyer at LeBoeuf, Lamb, Greene & MacRae LLP.

From 2008 he held a number of positions with the Ministry of Natural Resources and Environment of the Russian Federation, including Chief Officer for State Policy and Regulation in Geology and Subsoil Use and Deputy Minister of Natural Resources and Environment of the Russian Federation, and was appointed First Deputy Minister of Natural Resources and Environment of the Russian Federation in 2014. During his service with the Russian Ministry of Natural Resources and Environment, he was in charge of economic and financial affairs, geology and subsoil use.

His outstanding service was recognized with awards at different levels.

In December 2015, he was appointed Deputy Chairman of the Management Board at PAO NOVATEK.

MR. KIRILL N. YANOVSKIY

- Member of NOVATEK's Management Board
- Director for Finance
- Born in 1967

In 1991, Mr. Yanovskiy graduated from the Gubkin Institute of Oil and Gas in Moscow. From 1992, he headed a department of the

Yugorsky Joint-Stock Bank. From 1995, he headed the Securities Department at the Neftek Joint-Stock Commercial Bank. Since 2002, he has been Director of NOVATEK's Financial Planning, Analysis and Control Department. In August 2007, Mr. Yanovskiy was elected to NOVATEK's Management Board and in 2007 was appointed Deputy Director for Finance and Strategy. Since May 2011 he has been Director for Finance and Strategy, since February 2015 he is Director for Finance of PAO NOVATEK.

REPORT ON MAJOR, AND INTERESTED-PARTY TRANSACTIONS THAT THE COMPANY DID IN THE REPORTING YEAR

I. Transaction type: a major interested-party transaction.

Type and subject matter of the transaction: Debt Service Undertaking and interrelated transactions – Guarantee Agreement, Subordination Deed and Transfer Restrictions Agreement.

Subject matter of the transaction, including civil rights and obligations, which the transaction was intended to establish, modify or terminate:

Debt Service Undertaking (the "Debt Service Undertaking") between:

- (1) OAO NOVATEK, Total S.A., and China National Oil & Gas Exploration and Development Corporation ("CNODC") as sponsors (the "Sponsors");
- (2) OAO Yamal LNG as borrower (hereinafter the "Borrower");
- (3) Lenders' agents, including the Intercreditor Agent ("the Intercreditor Agent"), the Offshore Security Agent, the Joint and Several Creditor, the Credit Agents of CDB and CEXIM (if applicable), in which capacities one of the Lenders may act, and other persons nominated by the Lenders as well as, if applicable, Gazprombank and the Gazprombank and Sberbank Facility Agent and the EXIAR Facility Agent (hereinafter collectively referred to as the "Agents");
- (4) Other persons that may become party to it according to the Debt Service Undertaking, on the following material terms and conditions related to NOVATEK's obligations:
 - (a) If the Borrower fails to pay any amount payable to the Lenders under the Secured Obligations (as defined below), OAO NOVATEK undertakes to pay the Lenders represented by the Intercreditor Agent such a part of the Borrower's debt under the Secured Obligations (as defined below), the

maximum size of which in percentage shall correspond to the aggregate interest of OAO NOVATEK and Yarm Limited (and their subsidiaries) in OAO Yamal LNG share capital as of the Debt Service Undertaking signing date (unless this part has been increased on the initiative of OAO NOVATEK and with the Intercreditor Agent consent) on the terms and conditions stipulated by the Debt Service Undertaking;

- (b) In any OAO NOVATEK default event listed in the Debt Service Undertaking, OAO NOVATEK undertakes to pay the Lenders represented by the Intercreditor Agent such a part of the Borrower's debt under the Secured Obligations the maximum size of which in percentage shall correspond to the aggregate interest of OAO NOVATEK and Yarm Limited (and their subsidiaries) in OAO Yamal LNG share capital as of the Debt Service Undertaking signing date (unless this part has been increased on the initiative of OAO NOVATEK and with the Intercreditor Agent consent), regardless of whether the performance of Secured Obligations by the Borrowers is due or not, on the terms and conditions stipulated by the Debt Service Undertaking
- (c) If taxes need to be withheld from the amounts payable to the Lenders and (or) the Agents and (or) another person in line with the Debt Service Undertaking, the amount of OAO NOVATEK payment shall be increased so that the Lenders receive the full amount due under the Debt Service Undertaking on the terms and conditions stipulated by the Debt Service Undertaking;
- (d) OAO NOVATEK shall compensate the Lenders and (or) the Agents for their expenses connected with making claims to OAO NOVATEK or maintaining the rights related to OAO NOVATEK obligations under the Debt Service Undertaking on the terms and conditions stipulated by the Debt Service Undertaking;
- (e) OAO NOVATEK's obligations to pay the Lenders and (or) Agents and (or) other persons in line with the Debt Service Undertaking any amounts under the Debt Service Undertaking terminate when the conditions provided for by the Debt Service Undertaking occur;
- (f) the Debt Service Undertaking secures the Borrower's obligations under the International Financing (the "Secured Obligations") that arise, among others, under the following documents:

- (l) Common Terms Agreement (the "Common Terms Agreement") entered into on the following material terms and conditions:
 - (a) Parties: (1) Borrower as the borrower; (2) Yamal Trade Pte. Ltd. (the "Yamal Trade") and OOO Sabetta International Airport (the "Airport") as Permitted Subsidiaries and Guarantors of the Borrower's obligations; (3) the Lenders; (4) the Agents; (5) other persons specified in the Common Terms Agreement as well as persons that may become party thereto according to the Common Terms Agreement.
 - (b) The Common Terms Agreement provides for the key terms and conditions of International Financing, including the provisions that stipulate the parties' key obligations, default events, warranties and representations and others. At the same time, specific financing conditions, including the amount of financing, maximum tenor, repayment of loans extended under the financing arrangements, payment of interest, interest rates, the amount and procedure for payment of fees and other commissions, reimbursable expenses and other amounts payable by the Borrower (and, if applicable, its subsidiaries) shall be determined in accordance with the terms of the agreements and other documents listed in clauses (II) to (IX) below.
- (II) CDB Term Loan Facilities Agreement (the "CDB Facility Agreement") and CEXIM Term Loan Facilities Agreement (the "CEXIM Facility Agreement") executed on 29 April 2016, hereinafter referred to as the "Chinese Banks Facility Agreements" (as these may be amended, modified and re-stated) on the following material terms and conditions:
 - (a) Parties: (1) Borrower as the borrower; (2) Yamal Trade and Airport as the Permitted Subsidiaries and Guarantors of the Borrower's obligations; (3) CDB as the Senior Lender under the CDB Facility Agreement; (4) CEXIM as the Senior Lender under the CEXIM Facility Agreement; and (5) other persons that may become party to the Chinese Banks Facility Agreement, including Agents or any of them.
 - (b) Amount of the facilities:
 - under the CDB Facility Agreement: not more than Five billion fifty-seven million eight hundred thousand (5,057,800,000) euro and not more than Five billion two hundred eighty-six million (5,286,000,000) RMB;
 - under the CEXIM Facility Agreement: not more than Four billion two hundred seventy-nine million seven hundred thousand (4,279,700,000) euro and not more than Four billion four hundred seventy-two million five hundred thousand (4,472,500,000) RMB.
 - (c) Maximum loan term: Until 15 June 2031.
 - (d) Facility repayment: (1) euro facility - in semi-annual installments starting on 15 December 2019, (2) RMB facility - in semi-annual installments starting on 15 December 2019. Options of mandatory and voluntary prepayment are provided for.
 - (e) Interest payment: In semi-annual installments with the last interest payment to be made on the final repayment date.
 - (f) Interest rate:
 - (1) Under the euro facilities: Interest rate on each of the euro facilities under the Chinese Banks Facility Agreements is equal to the aggregate of:
 - (i) A EURIBOR margin; and
 - (ii) EURIBOR (to be determined in line with the Chinese Banks Facility Agreement).
 The EURIBOR margin equals:
 - (i) in relation to any part or any Interest Period before the Debt Service Undertaking Release Date – 3.30% per annum; and
 - (ii) in relation to any part or any Interest Period as of the Debt Service Undertaking Release Date and after such date – 3.55% per annum.
 - (2) Under the RMB facilities: Interest rate on each of the RMB facilities under the Chinese Banks Facility Agreements is equal to the aggregate of:
 - (i) A SHIBOR margin; and
 - (ii) SHIBOR (to be determined in line with the Chinese Banks Facility Agreement).
 A SHIBOR margin equals:
 - (i) in relation to any part or any Interest Period before the Debt Service Undertaking Release Date – 3.30% per annum; and
 - (ii) in relation to any part or any Interest Period as of the Debt Service Undertaking Release Date and after such date – 3.55% per annum.
 - (g) Default interest payable by the Borrower under the Chinese Banks Facility Agreements in case of overdue debt and incurred on the overdue amount: not more than 1.5% per annum over the facilities' interest rate;
 - (h) Upfront fee (or similar fee): equals 2% of the loans provided in euro and 2% of the loans provided in RMB and is payable according to the CDB Upfront Fee Letter and the CEXIM Upfront Fee Letter.
 - (i) The Commitment Fee (or a similar fee) under the Chinese Banks Facility Agreements

- payable semi-annually on 15 June and 15 December after 15 December 2016 during the Funds Availability Period under the Chinese Banks Facility Agreements and on the last day of the Funds Availability Period under the Chinese Banks Facility Agreements (the first accrued payment for utilizing the limit under the Chinese Banks Facility Agreements shall be paid on 15 December 2016); in the amount of 1.5% per annum of the total amount of non-utilized funds in euro under the Chinese Banks Facility Agreements and 1.5% per annum of the total amount of non-utilized facility funds in RMB under the Chinese Banks Facility Agreements.
- (j) Expenses: expenses incurred by the Parties in connection with entering into the Chinese Banks Facility Agreements and/or any other agreement to be entered into in connection with the Chinese Banks Facility Agreements or otherwise in respect thereof shall be reimbursed by the Borrower.
 - (k) Other amounts: Other amounts, including the prepayment fee, shall be payable by the Borrowers and other persons in the events and on the terms and conditions provided for by the Chinese Banks Facility Agreements and other financing documents related thereto.
- (III) Facility Agreement executed on 11 April 2016 (as amended by the Amendment dated 29 April 2016) between, among others, Sberbank and Gazprombank as lenders and the Borrower, the materials terms and conditions of which were approved by NOVATEK Annual General Meeting of Shareholders dated 22 April 2016 in Minutes No. 124 ("Minutes No. 124"), as further on amended and modified and restated as of 24 June 2016 in connection with the International Financing (the "Russian Banks Facility Agreement") on the following material terms and conditions:
- (a) Parties: (1) Borrower; (2) Yamal Trade and Airport as the Permitted Subsidiaries and Guarantors of the Borrower's obligations; (3) Sberbank and Gazprombank as lenders and arrangers; (4) Gazprombank as the facility agent and EXIAR facility agent; (5) the Agents or any one of them; (6) other persons specified in the Russian Banks Facility Agreement as well as other persons that may become party thereto according to the Russian Banks Facility Agreement.
 - (b) Loan amount: Not more than Three billion six hundred million (3,600,000,000) euro.
 - (c) Maximum loan term: Not more than 16 years from the date when the conditions precedent for the first drawdown are fulfilled.
 - (d) Loan repayment: In semi-annual installments starting on December 15, 2019. Options of mandatory and voluntary prepayment are provided for.
 - (e) Interest payment: In semi-annual installments with the last interest payment to be made on the final repayment date.
 - (f) Interest rate: EURIBOR 6M (indicative interest rate for six-month loans) provided that if EURIBOR rate is negative it shall be deemed to be zero, plus a margin of not more than 4,7 percent per annum.
 - (g) Default interest payable by the Borrower in case of overdue debt and incurred on the overdue amount: Not more than 1.5% per annum over the loan interest rate.
 - (h) Credit account upfront and maintenance fee (or similar fee): Not more than 1.5% of the total loan amount.
 - (i) Commitment fee payable on interest payment dates: Not more than 1% per annum of the total amount of non-utilized facility funds.
 - (j) Expenses: Expenses incurred by the financing parties shall be reimbursed by the Borrower.
 - (k) Other amounts: Other amounts, including the prepayment fee, shall be payable by the Borrower and other persons in the events and on the terms and conditions provided for by the Russian Banks Facility Agreement and other financing documents related thereto.
- (IV) Commission and fee letter and agreements entered into by the Borrower and the Agents in connection with the International Financing, including (but not limited to) the Intercreditor Agent Fee Letter, the Offshore Security Agent Fee Letter, the Joint and Several Creditor Fee Letter, the CDB and CEXIM Facility Agents Fee Letter, the Gazprombank as Gazprombank and Sberbank Agent Fee Letter, the EXIAR Facility Agent Fee Letter, and other letters and agreements on fees to any other Agent, account bank and (or) other fees payable under the Common Terms Agreement and other documents under the International Financing.
- (V) Accounts Agreement (the "Accounts Agreement") entered into or, if applicable, restated on the following main terms and conditions:

- (a) Borrower as the borrower, Airport and Yamal Trade as the Permitted Subsidiaries and Guarantors of the Borrower's obligations, Lenders as the lenders, account banks, Agents and/or in other capacities provided for by the Accounts Agreement as well as other persons specified in the Accounts Agreement and persons that may become party thereto according to the Accounts Agreement; and
 - (b) The Borrower, the Airport and Yamal Trade shall open and maintain specific bank accounts in the account banks that will be specified in the Accounts Agreement and use them in accordance with the terms and priority of payments set out in the Accounts Agreement.
- (VI) Any facility agreement that is to be entered into in the future within the International Financing (the "Future Facility Agreement") on the following materials terms and conditions:
- (a) Parties (in respect of each party – if applicable in line with each Future Facility Agreement): (1) Borrower; (2) Yamal Trade; (3) Airport; (4) banks and (or) other financial institutions; and (4) other persons that may become party to each Future Facility Agreement, including the Agents or anyone of them – each in the capacity(-ies) provided for by each Future Facility Agreement.
 - (b) Loan amount: to be determined in line with each Future Facility Agreement but not more than an equivalent to Six hundred million (600,000,000) U.S. dollars. At the same time, the total amount of financing available under the CDB Facility Agreement, CEXIM Facility Agreement, Russian Banks Facility Agreement, and Future Facility Agreements will not exceed a 19 billion USD equivalent.
 - (c) The maximum term will be stipulated by each Future Facility Agreement but in any case will not exceed 15 years after the first drawdown date under each of the Future Facility Agreements.
 - (d) The loan repayment and interest payment procedure will be stipulated by each Future Facility Agreement.
 - (e) The interest rate (including, if applicable, the possibility of changing it) will be stipulated by each Future Facility Agreement but in case will exceed EURIBOR 6M (the indicative interest rate for 6 month euro loans) plus not more than 3.55%.
 - (f) Default interest payable by the Borrower in case of overdue debt and incurred on the overdue amount: shall be determined in accordance with terms and conditions of each Future Facility Agreement but in any case it will not exceed 1.5% per annum over the loan interest rate.
 - (g) The amount and procedure for payment of fees and other commissions shall be determined in accordance with the terms of each Future Facility Agreement and/or fee letter (or other similar agreements) to be entered into by virtue of and/or under each Future Facility Agreement.
 - (h) Expenses: expenses incurred by the Parties in connection with entering into each Future Facility Agreement and/or any other agreement to be entered into in relation to each Future Facility Agreement or otherwise in respect thereof, including lenders' expenses for ECAs premium payment, shall be reimbursed by the Borrower and/or by another entity specified in such an agreement.
 - (i) Other amounts: other amounts, including any commissions, the prepayment fee (if applicable), shall be payable by the Borrower and other persons in the events and on the terms and conditions provided for by each Future Facility Agreement and other financing documents related thereto.
- (VII) Any Secured Hedging Agreement entered into between the Borrower and/or Yamal Trade, including for the purposes of interest rate-related risks, currency risks and risks associated with changes in the goods cost, and as it is further detailed in the Common Terms Agreement (the "Secured Hedging Agreement").
- (VIII) Any Additional Term Loan Facility Agreement, Project Bond Documents and other Additional Debt Finance Documents to be entered into by the Borrower or the Project Bonds Issuer in order to raise Additional Debt covered under the Debt Service Undertaking as established by and in accordance with the terms set out in the Common Terms Agreement.
- (IX) Other agreements and documents entered into (signed) based on the contracts (agreements) specified in this item 1 in connection or in accordance therewith.
- Guarantee Agreement between:**
- (1) Bank for Development and Foreign Economic Affairs, a State Corporation (Vnesheconombank) (the "Guarantor") and
 - (2) OAO NOVATEK (the "Principal") (hereinafter referred to as the "Guarantee Agreement") in respect of the Principal's obligations under the

Debt Service Undertaking on the following material terms and conditions:

- in respect of the guarantee:
 - (i) Guarantee amount: a USD 3 billion equivalent;
 - (ii) Term of the Guarantee: Until 15 December 2025 with an automatic renewal in case NOVATEK obligations under the Debt Service Undertaking are renewed; and
 - (iii) Guarantee fee: 0.75 % per annum of the Guarantee amount, but not less than USD 1,000 from the Guarantee effective date. The rate may be increased by 0.5% in the event the Principal fails to perform its obligations to agree the following amendments with the Guarantor:
 - (a) the definition of fundamental event of default and Sponsor's event of default;
 - (b) amendments envisaging the increase of the Principal's share under the Debt Service Undertaking above 59.973% and/or the overall amount of International Financing exceeding the equivalent of 20 billion USD, if such amendments increase the Guarantor's liability and significantly increase the probability of initiating claims under the guarantee;
 - (iv) penalty in the event the Principal fails to perform its payment obligations – in the amount specified by the Guarantee Agreement.
- in relation to recourse under the Guarantee:
 - (i) in the event it is impossible for the Guarantor to have recourse to the Principal, such recourse shall be novated as the Principal's commitment to the Guarantor;
 - (ii) Loan amount: the Guarantor's debt amount resulting from the performance of the Guarantor's obligations under the guarantee calculated under the formula specified by the Guarantee Agreement;
 - (iii) Loan currency: Euro;
 - (iv) Loan interest: cost of Vnesheconombank long-term unsecured financial borrowing in euro determined in line with the Guarantee Agreement increased by 0.75% per annum;
 - (v) Term of the loan: not more than 10 years.
 - (vi) Interest payment: on a quarterly basis, with a possible partial capitalization in line with the Guarantee Agreement;
 - (vii) Loan repayment: The loan is to be repaid with a lump sum on the earlier of the following dates: (1) 10 years after the Guarantor makes a payment under the guarantee, and (2) on the date when the Principal's obligations under the Debt Service Undertaking terminate;

(viii) penalty in the event the Principal fails to perform its payment obligations – in the amount specified by the Guarantee Agreement.

Term for the discharge of obligations under the transaction:

Debt Service Undertaking; approximately 7 years.

Guarantee Agreement: 10 years after the Guarantor makes a payment under the guarantee, should there be such a payment.

The size of the transaction is comprised of the amount of Secured Obligations and exceeds 50% of NOVATEK assets value as of 31 March 2016.

Value of the issuer's assets as of the last day of the last full reporting period preceding the transaction (agreement execution): RUR 568,315,453,000 as of 31 March 2016.

Transaction date (date of the Agreement): 24 June 2016.

Last name, first name, and patronymic (if any) of the individual who is deemed interested in the issuer making the transaction according to the Russian Federation legislation; the reason (reasons) why the individual is deemed interested in the transaction; the interested individual's share in the authorized share (joint-stock) capital (the portion of shares held by the interested individual) of the issuer and the legal entity that is party to the transaction:

The transactions are interested-party transactions as Andrei I. Akimov, member of NOVATEK Board of Directors is also Chairman of the Management Board and member of the Board of Directors of Gazprombank (Joint-Stock Company) that is party to and (or) beneficiary under the Agreements To Be Approved. Andrei I. Akimov holds no shares in the issuer of entities that are party to the transaction.

Information on the transaction approval: NOVATEK Extraordinary General Meeting of Shareholders approved the transaction on 20 June 2016 (Minutes No. 125 dated 20 June 2016).

Subordination Deed (the "Subordination Deed") between:

- (a) (1) Borrower, (2) Airport and Yamal Trade, (3) Sponsors; (4) OAO NOVATEK, Total E&P Yamal, CNODC and Yaym Limited as shareholders (the "Shareholders"); (5) Polyshine Holding B.V., Total E&P Yamal, Novatek Equity (Cyprus) Limited, and (or) other persons that have extended subordinated loans to OAO Yamal LNG as subordinated lenders (the "Subordinated Lenders"), (6) the Agents; and (7) other persons stipulated in the Subordination Deed, as well as persons that may become party thereto under the Subordination Deed.

- (b) OAO NOVATEK's claims to the Borrower, the Airport, Yamal Trade and other OAO Yamal LNG subsidiaries (the "Project Obligors") shall be subordinated vis-a-vis the claims of the Lenders on the terms and conditions set out in the Subordination Deed.
- (c) The Project Obligors are entitled to make payments in relation to the subordinated loans and other subordinated debt only in the events and in the form and manner set out in the Subordination Agreement; should the Project Obligors be in breach of these obligations, OAO NOVATEK undertakes to pay the Intercreditor Agent, at the latter's demand, the respective amount (which may not exceed the amount of Secured Obligations) it received from the Project Obligors.
- (d) In the event of enforcement by Lenders of shares or equity interest in Project Obligors, such Project Obligors shall be released from a number of obligations in respect of OAO NOVATEK set out in the Subordination Deed.
- (e) OAO NOVATEK shall also assume other obligations in line with the terms and conditions of the Subordination Deed.
- (f) Term: OAO NOVATEK obligations shall remain in force as long as the Secured Obligations remain outstanding and/or there are Lenders' obligations to provide loan moneys to the Borrower.

Transaction date (date of the Deed): 24 June 2016.

Last name, first name, and patronymic (if any) of the individual who is deemed interested in the issuer making the transaction according to the Russian Federation legislation; the reason (reasons) why the individual is deemed interested in the transaction; the interested individual's share in the authorized share (joint-stock) capital (the portion of shares held by the interested individual) of the issuer and the legal entity that is party to the transaction:

These transactions are considered to be interested-party transactions as Andrei I. Akimov, member of NOVATEK Board of Directors is also Chairman of the Management Board and member of the Board of Directors of Gazprombank (Joint-Stock Company) that is party to and (or) beneficiary under the Agreements To Be Approved. Andrei I. Akimov holds no shares in the issuer of entities that are party to the transaction.

Information on the transaction approval: NOVATEK Extraordinary General Meeting of Shareholders approved the transaction on 20 June 2016 (Minutes No. 125 dated 20 June 2016).

Transfer Restrictions Agreement (the "Transfer Restrictions Agreement") between:

(1) Borrower; (2) Agents; (3) China National Petroleum Corporation; (4) PetroChina Company Limited; (5) Sponsor; (6) Shareholders (except for Yaym Limited),

on the following material terms and conditions related to OAO NOVATEK's obligations:

- (a) OAO NOVATEK undertakes to directly or indirectly hold at least 50% plus one share of OAO Yamal LNG;
- (b) Restrictions are put in place in respect of the transfer of, and creation of security in relation to, the OAO Yamal LNG shares held by OAO NOVATEK as well as a procedure is established for application of funds received by OAO NOVATEK as compensation from the Russian Federation or a Russian Federation government body in relation to nationalization, confiscation, expropriation or compulsory acquisition of the shares of OAO Yamal LNG (if applicable);
- (c) OAO NOVATEK shall also assume other obligations in accordance with the terms and conditions of the Transfer Restrictions Agreement;
- (d) Term: OAO NOVATEK obligations shall remain in force as long as the Secured Obligations remain outstanding and/or there are Lenders' obligations to provide loan moneys to the Borrower.

Transaction date (date of the Deed): 24 June 2016.

Last name, first name, and patronymic (if any) of the individual who is deemed interested in the issuer making the transaction according to the Russian Federation legislation; the reason (reasons) why the individual is deemed interested in the transaction; the interested individual's share in the authorized share (joint-stock) capital (the portion of shares held by the interested individual) of the issuer and the legal entity that is party to the transaction:

These transactions are considered to be interested-party transactions as Andrei I. Akimov, member of NOVATEK Board of Directors is also Chairman of the Management Board and member of the Board of Directors of Gazprombank (Joint-Stock Company) that is party to and (or) beneficiary under the Agreements To Be Approved. Andrei I. Akimov holds no shares in the issuer of entities that are party to the transaction.

Information on the transaction approval: NOVATEK Extraordinary General Meeting of Shareholders approved the transaction on 20 June 2016 (Minutes No. 125 dated 20 June 2016).

II. Transaction type: an interested-party transaction.

Type and subject matter of the transaction: suretyship.

Subject matter of the transaction, including civil rights and obligations, which the transaction was intended to establish, modify or terminate:

Suretyship towards the Guarantor for the Principal's obligations arising from bank guarantees provided by the Guarantor on behalf of the Principal.

Fee rates for issuing, increasing and renewing the Guarantees shall not exceed 1.5% per annum from the amount of each Guarantee, but shall not be less than USD 100.

Guarantee limit: Forty billion (40,000,000,000) Russian rubles.

Term of the suretyship: Until 31 August 2021.

Term for the discharge of obligations under the transaction: Until 31 August 2021.

Parties:

Surety: OAO NOVATEK; Guarantor: VTB Bank (PAO); Principal: NOVATEK – Ust-Luga

The size of the transaction is comprised of the amount of the Principal's obligations arising from bank guarantees provided by the Guarantor on behalf of the Principal and exceeds 1% of NOVATEK assets value as of 30 June 2016.

Value of the issuer's assets as of the last day of the last full reporting period preceding the transaction (agreement execution): 573,092,345,000 Russian rubles as of 30 June 2016.

Transaction date (date of the Agreement): 5 August 2016

Last name, first name, and patronymic (if any) of the individual who is deemed interested in the issuer making the transaction according to the Russian Federation legislation; the reason (reasons) why the individual is deemed

interested in the transaction; the interested individual's share in the authorized share (joint-stock) capital (the portion of shares held by the interested individual) of the issuer and the legal entity that is party to the transaction:

These transactions are considered to be interested-party transactions as Andrei V. Sharonov, member of NOVATEK Board of Directors is a member of the Supervisory Board of VTB Bank (PAO), a party to the transaction. Mr. Andrei V. Sharonov owns no equity interests in the authorized share capital or shares in the issuer and persons that are a party to the transaction.

Information on the transaction approval: NOVATEK Annual General Meeting of Shareholders approved the transaction on 22 April 2016 (Minutes No. 124 dated 22 April 2016)

Corporate Governance Code Compliance Report

This Corporate Governance Code Compliance Report was reviewed at the meeting of PAO NOVATEK's Board of Directors on 14 March 2017 (Minutes No. 195).

The Board of Directors certifies that data in this Report contain full and reliable information on compliance by the Company with the principles and recommendations of the Corporate Governance Code for 2016.

When assessing our compliance with corporate governance principles as set out in the Code we were guided by the Guidelines for Reporting on Compliance with the Corporate Governance Code recommended by the Bank of Russia in its Letter No. IN-06-52/8 dated 17 February 2016.

An overview of the most relevant aspects of the corporate governance model and practices in the Company is presented in the Corporate Governance section of this Annual Report.

CORPORATE GOVERNANCE CODE COMPLIANCE REPORT

This Corporate Governance Code Compliance Report was reviewed at the meeting of PAO NOVATEK's Board of Directors on 14 March 2017 (Minutes No. 195).

The Board of Directors certifies that data in this Report contain full and reliable information on compliance by the Company with the principles and recommendations of the Corporate Governance Code for 2016.

When assessing our compliance with

corporate governance principles as set out in the Code we were guided by the Guidelines for Reporting on Compliance with the Corporate Governance Code recommended by the Bank of Russia in its Letter No. IN-06-52/8 dated 17 February 2016.

An overview of the most relevant aspects of the corporate governance model and practices in the Company is presented in the Corporate Governance section of this Annual Report.

No.	Corporate governance principles	Compliance criteria	Compliance status	Reasons for non-compliance
1.1.	THE COMPANY ENSURES FAIR AND EQUITABLE TREATMENT OF ALL SHAREHOLDERS IN EXERCISING THEIR CORPORATE GOVERNANCE RIGHT.			
1.1.1	The company ensures the most favorable conditions for its shareholders to participate in the general meeting, develop an informed position on agenda items of the general meeting, coordinate their actions, and voice their opinions on items considered.	1. The company's internal document approved by the general meeting of shareholders and governing the procedures for holding the general meeting is publicly available. 2. The company provides accessible means of communication via hotline, e-mail or an online forum for shareholders to voice their opinions and submit questions on the agenda in preparing for the general meeting. The company performed the above actions in advance of each general meeting held in the reporting period.	Full	In preparing for the General Meeting of shareholders the Company posts a dedicated e-mail address on its website for shareholders to submit their opinions and questions on the agenda. Historically, when preparing for General Meetings, shareholders have no or few questions on the agenda of a forthcoming General Meeting. Should the Company's shareholders need communication means other than those specified in the Code, the Company is prepared to provide such means as necessary.
1.1.2	The procedure for giving notice of, and providing relevant materials for, the general meeting enables shareholders to properly prepare for attending the general meeting.	1. The notice of an upcoming general meeting of shareholders is posted (published) online at least 30 days prior to the date of the general meeting. 2. The notice of an upcoming meeting specifies the meeting venue and documents required for admission. 3. Shareholders were given access to the information on who proposed the agenda items and who proposed nominees to the company's board of directors and the revision commission.	Full	—

1.1.3	In preparing for, and holding of, the general meeting, shareholders were able to receive clear and timely information on the meeting and related materials, put questions to the company's executive bodies and the board of directors, and to communicate with each other.	1. In the reporting period, shareholders were able to put questions to members of executive bodies and members of the board of directors before and during the annual general meeting.	Full	–
		2. The position of the board of directors (including dissenting opinions entered into the minutes) on each agenda item of general meetings held in the reporting period was included in the materials to the general meeting of shareholders.	Partial	When convening General Meetings of Shareholders, the Board of Directors reviews all agenda items of the relevant meeting and presents them to the Meeting for consideration or provides necessary advice. Materials to the General Meeting of Shareholders include recommendations of the Board of Directors as required by law. In other cases, the position of the Board of Directors is not included in the Meeting materials to avoid any influence on shareholders' voting.
		3. The company gave duly authorised shareholders access to the list of persons entitled to attend the general meeting, as from the date of its receipt by the company, for all general meetings held in the reporting period.	Full	–
1.1.4	There were no unjustified difficulties preventing shareholders from exercising their right to request that a general meeting be convened, to propose nominees to the company's governing bodies, and to make proposals for the agenda of the general meeting.	1. In the reporting period, shareholders were able to submit, within at least 60 days after the end of the relevant calendar year, proposals for the agenda of the annual general meeting. 2. In the reporting period, the company did not reject any proposals for the agenda or nominees to the company's governing bodies due to misprints or other insignificant flaws in the shareholder's proposal.	Partial	In the reporting period, shareholders were not able to submit, within at least 60 days after the end of the relevant calendar year, proposals for the agenda of the Annual General Meeting, since the Company's Charter valid until 12 October 2016 provided for such items to be submitted within 30 days after the end of the financial year. The Extraordinary General Meeting of the issuer's shareholders that was held on 30 September 2016 approved amendments to the issuer's Charter on extending the deadline for shareholders to submit proposals for the agenda of the Annual General Meeting to 60 days after the end of the relevant calendar year; these amendments were registered on 12 October 2016.
1.1.5	Each shareholder was able to freely exercise their voting right in the simplest and most convenient way.	1. An internal document (internal policy) of the company provides that each participant of the general meeting may request a copy of the ballot filled out by them and certified by the counting commission before the end of the relevant meeting.	Full	–

1.1.6	The procedure for holding a general meeting set by the company provides equal opportunities for all persons attending the meeting to voice their opinions and asks questions.	1. General meetings of shareholders held in the reporting period in the form of a meeting (i.e. joint presence of shareholders) provided for sufficient time for making reports on and for discussing agenda items.	Full	–
		2. Nominees to the Company's governing and control bodies were available to answer questions of shareholders at the meeting at which their nominations were put to vote.	Full	–
		3. When passing resolutions on preparing and holding general meetings of shareholders, the board of directors considered using telecommunication means for remote access of shareholders to general meetings in the reporting period.	None	When passing resolutions on preparing and holding general meetings of shareholders, the Board of Directors did not consider using telecommunication means for remote access of shareholders to general meetings in the reporting period, since the Company had no reasons to believe that many shareholders would be interested in this service. The non-compliance with this provision of the Code is temporary. The Company intends to achieve compliance with this Code provision in 2017. The Extraordinary General Meeting of Shareholders of the issuer held on 30 September 2016 added a provision to the issuer's Charter authorising the Board of Directors to adopt resolutions on using telecommunication means to enable remote access of shareholders to general meetings; these amendments were registered on 12 October 2016.
1.2 SHAREHOLDERS ARE GIVEN EQUAL AND FAIR OPPORTUNITIES TO SHARE PROFITS OF THE COMPANY IN THE FORM OF DIVIDENDS.				
1.2.1	The company has designed and put in place a transparent and clear mechanism to determine the dividend amount and payout procedure.	1. The company has drafted and disclosed a dividend policy approved by the board of directors. 2. If the company's dividend policy uses reporting figures to determine the dividend amount, then relevant provisions of the dividend policy take into account the consolidated financial statements.	Full	–
1.2.2	The company does not resolve to pay out dividends if such payout, while formally compliant with law, is economically unjustified and may lead to a false representation of the company's performance.	1. The company's dividend policy clearly identifies financial / economic circumstances under which the company shall not pay out dividends.	Full	–

1.2.3	The company does not allow for dividend rights of its existing shareholders to be impaired.	1. In the reporting period, the company did not take any actions that would lead to the impairment of the dividend rights of its existing shareholders.	Full	–
1.2.4	The company makes every effort to prevent its shareholders from using other means to profit (gain) from the company other than dividends and liquidation value.	1. To prevent shareholders from using other means to profit (gain) from the company other than dividends and liquidation value, the company's internal documents provide for controls to timely identify and approve deals with affiliates (associates) of the company's substantial shareholders (persons entitled to use votes attached to voting shares) where the law does not formally recognize such deals as related-party transactions.	None	This principle is not complied with as the Company believes that statutory controls are sufficient for relevant purposes. The Company does not transact with persons under control by substantial shareholders, which prevents substantial shareholders from profiting (gaining) from the Company.
1.3	THE CORPORATE GOVERNANCE FRAMEWORK AND PRACTICES ENSURE EQUAL CONDITIONS FOR ALL SHAREHOLDERS OWNING THE SAME TYPE (CLASS) OF SHARES, INCLUDING MINORITY AND NON-RESIDENT SHAREHOLDERS, AND THEIR EQUAL TREATMENT BY THE COMPANY.			
1.3.1	The company has created conditions for fair treatment of each shareholder by the company's governing and control bodies, including conditions that rule out abuse by major shareholders against minority shareholders.	1. In the reporting period, procedures for management of potential conflicts of interest among substantial shareholders were efficient, while the board of directors paid due attention to conflicts, if any, between shareholders.	Full	–
1.3.2	The company does not take any actions that lead or may lead to artificial redistribution of corporate control.	1. No quasi-treasury shares were issued or used to vote in the reporting period.	Full	–
1.4	SHAREHOLDERS ARE PROVIDED WITH RELIABLE AND EFFICIENT MEANS OF RECORDING THEIR RIGHTS TO SHARES AND ARE ABLE TO FREELY DISPOSE OF THEIR SHARES WITHOUT ANY HINDRANCE.			
1.4	Shareholders are provided with reliable and efficient means of recording their rights to shares and are able to freely dispose of their shares without any hindrance.	1. The company's registrar maintains the share register in an efficient and reliable way that meets the needs of the company and its shareholders.	Full	–
2.1	THE BOARD OF DIRECTORS PROVIDES STRATEGIC MANAGEMENT OF THE COMPANY, DETERMINES KEY PRINCIPLES OF, AND APPROACHES TO, SETTING UP A CORPORATE RISK MANAGEMENT AND INTERNAL CONTROL FRAMEWORK, MONITORS PERFORMANCE BY THE COMPANY'S EXECUTIVE BODIES, AND PERFORMS OTHER KEY FUNCTIONS.			
2.1.1	The board of directors is responsible for appointing and dismissing executive bodies, including for improper performance of their duties. The board of directors also ensures that the company's executive bodies act in accordance with the company's approved development strategy and core lines of business.	1. The board of directors has the authority stipulated in the charter to appoint and remove members of executive bodies and to set out the terms and conditions of their contracts.	Partial	The authority of the Board of Directors under the Company's Charter does not include the right to set out the terms and condition of contracts with members of the Company's Management Board.
		2. The board of directors reviewed the report(s) by the sole executive body or members of the collective executive body on the implementation of the company's strategy.	Full	

2.1.2	The board of directors sets key long-term targets for the company, assesses and approves its key performance indicators and key business goals, as well as the strategy and business plans for the company's core lines of business.	1. At its meetings in the reporting period, the board of directors reviewed strategy implementation and updates, approval of the company's financial and business plan (budget), and criteria and performance (including interim) of the company's strategy and business plans.	Full	
2.1.3	The board of directors defines the company's principles and approaches to risk management and internal controls.	1. The board of directors defined the company's principles and approaches to risk management and internal controls. 2. The board of directors assessed the company's risk management and internal controls in the reporting period.	Full	
2.1.4	The board of directors determines the company's remuneration and reimbursement (compensation) policy for its directors, members of executive bodies and other key executives.	1. The company developed and put in place a remuneration and reimbursement (compensation) policy (policies), approved by the board of directors, for its directors, members of executive bodies and other key executives. 2. At its meetings in the reporting period, the board of directors discussed matters related to such policy (policies).	Partial	The Company did not put in place any remuneration and reimbursement (compensation) policy for the Company's directors, members of executive bodies and other key executives.
2.1.5	The board of directors plays a key role in preventing, identifying and resolving internal conflicts between the company's bodies, shareholders and employees.	1. The board of directors plays a key role in preventing, identifying and resolving internal conflicts. 2. The company set up mechanisms to identify transactions leading to a conflict of interest and to resolve such conflicts.	Full	–
2.1.6	The board of directors plays a key role in ensuring that the company is transparent, timely and fully discloses its information, and provides its shareholders with unhindered access to the company's documents.	1. The board of directors approved the company's information policy regulations. 2. The company identified persons responsible for implementing the information policy.	Full	–
2.1.7	The board of directors controls the company's corporate governance practices and plays a key role in material corporate events of the company.	1. In the reporting period, the board of directors reviewed the company's corporate governance practices.	None	In the reporting period, the Board of Directors did not review the Company's corporate governance practices at its meetings. The non-compliance with this provision of the Code is temporary. The Company intends to achieve compliance with this Code provision in 2017. The Board of Directors intends to discuss this matter in 2017.

2.2 THE BOARD OF DIRECTORS IS ACCOUNTABLE TO THE COMPANY'S SHAREHOLDERS.

2.2.1	Performance of the board of directors is disclosed and made available to the shareholders.	1. The company's annual report for the reporting period includes the information on individual attendance at board of directors and committee meetings. 2. The annual report discloses key performance assessment results of the board of directors in the reporting period.	Full	
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2.2.2	The chairman of the board of directors is available to communicate with the company's shareholders.	1. The company has in place a transparent procedure enabling shareholders to forward questions and express their position on such questions to the chairman of the board of directors.	Full	In preparing for the General Meeting, the Company posts a dedicated e-mail address on its website for shareholders to submit their opinions and questions on the agenda. Besides, at General Meetings of Shareholders held in person, shareholders may personally ask questions of the Chairman of the Board of Directors.
2.3 THE BOARD OF DIRECTORS MANAGES THE COMPANY IN AN EFFICIENT AND PROFESSIONAL MANNER AND IS CAPABLE OF MAKING FAIR AND INDEPENDENT JUDGEMENTS AND ADOPTING RESOLUTIONS IN THE BEST INTERESTS OF THE COMPANY AND ITS SHAREHOLDERS.				
2.3.1	Only persons of impeccable business and personal reputation who have knowledge, expertise and experience required to make decisions within the authority of the board of directors and essential to perform its functions in an efficient way are elected to the board of directors.	1. The procedure for assessing the board of directors' performance established in the company includes, inter alia, assessment of professional qualifications of the board members. 2. In the reporting period, the board of directors (or its nomination committee) assessed nominees to the board of directors for required experience, knowledge, business reputation, absence of conflicts of interest, etc.	Partial	The Company did not assess the performance of the Board of Directors. The Remuneration and Nomination Committee advises the Board of Directors on nominees proposed by shareholders to the Board of Directors based on such criteria as the nominee's independence and professional qualifications, and also appraises such nominees for having required experience, expertise, business reputation and absence of conflicts of interest.
2.3.2	The company's directors are elected via a transparent procedure that enables shareholders to obtain information on nominees sufficient to judge on their personal and professional qualities.	1. Whenever the agenda of the general meeting of shareholders included election of the board of directors, the company provided to shareholders the biographical details of all nominees to the board of directors, the results of their assessment carried out by the board of directors (or its nomination committee), and the information on whether the nominee meets the independence criteria set forth in Recommendations 102–107 of the Code, as well as the nominees' written consent to be elected to the board of directors.	Partial	In preparing and holding General Meetings of Shareholders in the reporting period, the Company did not provide shareholders with nominee assessment results obtained by the Board of Directors (or its Nomination Committee). The Company intends to achieve compliance with this principle in 2017.
2.3.3	The board of directors has a balanced membership, including in terms of directors' qualifications, experience, expertise and business qualities, and enjoys its shareholders' trust.	1. As part of assessment of the board of directors' performance run in the reporting period, the board of directors reviewed its requirements to professional qualifications, experience and business skills.	None	The Company did not run any assessment of the Board of Directors' performance in the reporting period. The Company believes that such assessment is unnecessary as the Company's directors are highly skilled experts with long track records, including in management.

2.3.4	The company has a sufficient number of directors to organize the board of directors' activities in the most efficient way, including ability to set up committees of the board of directors and enable the company's substantial minority shareholders to elect a nominee to the board of directors for whom they vote.	1. As part of assessment of the board of directors' performance run in the reporting period, the board of directors considered whether the number of directors met the company's needs and shareholders' interests.	None	The Company did not run any assessment of the Board of Directors' performance in the reporting period. The Company believes that the current number of Directors (nine) is optimal and enables representing all shareholders, including minority shareholders, in the Board of Directors with the necessary number of Independent Directors.
2.4 THE BOARD OF DIRECTORS INCLUDES A SUFFICIENT NUMBER OF INDEPENDENT DIRECTORS.				
2.4.1	An independent director is a person who is sufficiently professional, experienced and independent to develop their own position, and capable of making unbiased judgements in good faith, free of influence by the company's executive bodies, individual groups of shareholders or other stakeholders. It should be noted that a nominee (elected director) who is related to the company, its substantial shareholder, substantial counterparty or competitor of the company, or related to the government, may not be considered as independent under normal circumstances.	1. In the reporting period, all independent directors met all independence criteria set out in Recommendations 102–107 of the Code or were deemed independent by the board of directors.	Full	-
2.4.2	The company assesses compliance of nominees to the board of directors and reviews compliance of independent directors with independence criteria on a regular basis. In such assessment, substance should prevail over form.	1. In the reporting period, the board of directors (or its nomination committee) made a judgement on independence of each nominee to the board of directors and provided its opinion to shareholders. 2. In the reporting period, the board of directors (or its nomination committee) reviewed, at least once, the independence of incumbent directors listed by the company as independent directors in its annual report. 3. The company has in place procedures defining the actions to be taken by a member of the board of directors if they cease to be independent, including the obligation to timely notify the board of directors thereof.	Full	-
2.4.3	Independent directors make up at least one third of the elected board members.	1. Independent directors make up at least one third of directors.	Full	-
2.4.4	Independent directors play a key role in preventing internal conflicts in the company and in ensuring that the company performs material corporate actions.	1. Independent directors (with no conflicts of interest) run a preliminary assessment of material corporate actions implying a potential conflict of interests and submit the results to the board of directors.	None	The Company intends to achieve compliance with this principle in 2017

2.5 THE CHAIRMAN OF THE BOARD OF DIRECTORS ENSURES THAT THE BOARD OF DIRECTORS DISCHARGES ITS DUTIES IN THE MOST EFFICIENT WAY.

2.5.1	The board of directors is chaired by an independent director, or a senior independent director supervising the activities of other independent directors and interacting with the chairman of the board of directors is chosen from among the elected independent directors.	1. The board of directors is chaired by an independent director, or a senior independent director is appointed from among the independent directors. 2. The role, rights and duties of the chairman of the board of directors (and, if applicable, of the senior independent director) are duly set out in the company's internal documents.	Partial	Formally, the Chairman of the Board of Directors is not an Independent Director. However, the Chairman of the Board of Directors meets all independence criteria, except for his tenure on the Board of Directors. For chairmanship purposes, the directors elected the most experienced director who is not an Independent Director. No senior independent director was elected from among independent directors.
2.5.2	The chairman of the board of directors maintains a constructive environment at meetings, enables free discussion of agenda items, and supervises the execution of resolutions passed by the board of directors.	1. Performance of the chairman of the board of directors was assessed as part of assessment of the board of directors' performance in the reporting period.	None	The Company did not run any assessment of the Board of Directors' performance in the reporting period.
2.5.3	The chairman of the board of directors takes all steps necessary for the timely provision to members of the board of directors of information required to pass resolutions on agenda items.	1. The company's internal documents set out the duty of the chairman of the board of directors to take all steps necessary for the timely provision to members of the board of directors with materials on agenda items of the board meeting.	Full	–

2.6 DIRECTORS ACT REASONABLY AND IN GOOD FAITH IN THE BEST INTERESTS OF THE COMPANY AND ITS SHAREHOLDERS, ON A FULLY INFORMED BASIS AND WITH DUE CARE AND DILIGENCE.

2.6.1	Directors pass resolutions on a fully informed basis, with no conflict of interest, subject to equal treatment of the company's shareholders, and assuming normal business risks.	1. The company's internal documents provide that a director should notify the board of directors of any existing conflict of interest as to any agenda item of the meeting of the board of directors or its committee, prior to discussion of the relevant agenda item. 2. The company's internal documents provide that a director should abstain from voting on any item in connection with which they have a conflict of interest. 3. The company has in place a procedure enabling the board of directors to get professional advice on matters within its remit at the expense of the company.	Full	–
2.6.2	The rights and duties of directors are clearly stated and incorporated in the company's internal documents.	1. The company adopted and published an internal document that clearly defines the rights and duties of directors.	Full	–

2.6.3	Directors have sufficient time to perform their duties.	<p>1. Individual attendance at board and committee meetings, as well as time devoted to preparation for attending meetings, was recorded as part of the procedure for assessing the board of directors in the reporting period.</p> <p>2. Under the company's internal documents, directors notify the board of directors of their intentions to be elected to governing bodies in other entities (apart from the entities controlled by, or affiliated to, the company), and of their election to such bodies.</p>	Partial	The Company did not run any assessment of the Board of Directors' performance in the reporting period
2.6.4	All directors shall have equal access to the company's documents and information. Newly elected directors are furnished with sufficient information about the company and performance of the board of directors as soon as possible.	<p>1. Under the company's internal documents, directors are entitled to access documents and make requests on the company and its controlled entities, while executive bodies of the company should furnish all relevant information and documents.</p> <p>2. The Company has in place a formalized onboarding program for newly elected Directors.</p>	None	The Company intends to formalize its onboarding procedure for newly elected Directors in 2017.
2.7 MEETINGS OF THE BOARD OF DIRECTORS, PREPARATION FOR SUCH MEETINGS AND PARTICIPATION OF BOARD MEMBERS THEREIN ENSURE EFFICIENT PERFORMANCE BY THE BOARD OF DIRECTORS.				
2.7.1	Board meetings are held as needed, taking into account the scale of operations and goals of the company at a particular time.	1. The board of directors held at least six meetings in the reporting year.	Full	–
2.7.2	Internal regulations of the company provide a procedure for the preparation and holding of the board meetings, enabling members of the board of directors to prepare for such meetings in a proper manner.	1. The company has an approved internal document that describes the procedure for arranging and holding meetings of the board of directors and sets out, in particular, that the notice of the meeting shall be given, as a rule, at least five days prior to such meeting.	Full	–
2.7.3	The format of the meeting of the board of directors is determined taking into account the importance of items on the agenda. The most important matters are dealt with at meetings of the board of directors held in person.	1. The company's charter or internal document provides for the most important matters (as per the list set out in Recommendation 168 of the Code) to be passed at in-person meetings of the board of directors.	Partial	The list of matters to be resolved at the Board's in-person meetings does not fully match the list specified in Recommendation 168 of the Code.
2.7.4	Resolutions on most important matters relating to the company's operations are passed at a meeting of the board of directors by a qualified majority or by a majority of all elected board members.	1. The company's charter provides for the most important matters set out in Recommendation 170 of the Code to be passed at a meeting of the board of directors by a qualified majority of at least three quarters or by a majority of all elected board members.	Partial	<p>The Company's Charter does not provide for resolutions of the Board to be passed by qualified majority on the following matters:</p> <ul style="list-style-type: none"> – submission to the General Meeting of matters relating to the Company's liquidation – submission to the General Meeting of matters relating to amendments to the Company's Charter – review of material issues relating to operations of legal entities controlled by the Company

2.8 THE BOARD OF DIRECTORS SETS UP COMMITTEES FOR PRELIMINARY CONSIDERATION OF THE MOST IMPORTANT ISSUES RELATED TO THE BUSINESS OF THE COMPANY.

2.8.1	To preview matters related to controlling the company's financial and business activities, it is recommended to set up an audit committee comprised of independent directors.	<p>1. The board of directors has set up an audit committee comprised solely of independent directors.</p> <p>2. The company's internal documents set out the tasks of the audit committee, including those listed in Recommendation 172 of the Code.</p> <p>3. At least one member of the audit committee represented by an independent director has experience and knowledge of preparing, analysing, assessing and auditing accounting (financial) statements.</p> <p>4. Meetings of the audit committee were held at least once a quarter during the reporting period.</p>	Full	–
2.8.2	To preview matters related to adopting an efficient and transparent remuneration scheme, a remuneration committee is set up, comprised of independent directors and headed by an independent director who is not the chairman of the board of directors.	<p>1. The board of directors has set up a remuneration committee comprised solely of independent directors.</p> <p>2. The remuneration committee is headed by an independent director who is not the chairman of the board of directors.</p> <p>3. The company's internal documents set out the tasks of the remuneration committee, including those listed in Recommendation 180 of the Code.</p>	Full	–
2.8.3	To preview matters related to talent management (succession planning), professional composition and efficiency of the board of directors, a nomination (HR) committee is set up, predominantly comprised of independent directors.	<p>1. The board of directors has set up a nomination committee (its tasks listed in Recommendation 186 of the Code are fulfilled by another committee, the Remuneration and Nomination Committee) predominantly comprised of independent directors.</p> <p>2. The company's internal documents set out the tasks of the nomination committee (or the tasks of the committee with combined functions), including those listed in Recommendation 186 of the Code.</p>	Full	–
2.8.4	Taking into account the company's scope of business and level of risks, the company's board of directors made sure that the composition of its committees is fully in line with company's business goals. Additional committees were either set up or not deemed necessary (strategy committee, corporate governance committee, ethics committee, risk management committee, budget committee, health, safety and environment committee, etc.).	1. In the reporting period, the board of directors considered whether the composition of its committees was in line with the board's tasks and the company's business goals. Additional committees were either set up or not deemed necessary.	None	In 2005, the Board of Directors set up an additional committee, the Strategy Committee. Each newly elected Board of Directors forms this Committee in accordance with the Regulations on the Strategy Committee of the Company's Board of Directors.

2.8.5	Committees are composed so as to enable comprehensive discussions of matters under preview, taking into account the diversity of opinions.	1. Committees of the board of directors are headed by independent directors. 2. The company's internal documents (policies) include provisions stipulating that persons who are not members of the audit committee, the nomination committee and the remuneration committee may attend committee meetings only by invitation of the chairman of the respective committee.	Partial	The Strategy Committee is headed by a director who is not an independent director.
2.8.6	Committee chairmen inform the board of directors and its chairman on the work of their committees on a regular basis.	1. During the reporting period, committee chairmen reported to the board of directors on the work of committees on a regular basis.	Full	–
2.9 THE BOARD OF DIRECTORS ENSURES PERFORMANCE ASSESSMENT OF THE BOARD OF DIRECTORS, ITS COMMITTEES AND MEMBERS OF THE BOARD OF DIRECTORS.				
2.9.1	The board of directors' performance assessment is aimed at determining the efficiency of the board of directors, its committees and members, consistency of their work with the company's development requirements, as well as bolstering the work of the board of directors and identifying areas for improvement.	1. Self-assessment or external assessment of the board of directors' performance carried out in the reporting period included performance assessment of committees, individual members of the board of directors and the board of directors in general. 2. Results of self-assessment or external assessment of the board of directors' performance carried out in the reporting period were reviewed at the in-person meeting of the board.	None	The Board's performance was not assessed during the reporting period.
2.9.2	Performance of the board of directors, its committees and directors is assessed on a regular basis at least once a year. An external advisor is engaged at least once in three years to conduct an independent assessment of the board of directors' performance.	1. The company engaged an external advisor to conduct an independent assessment of the board of directors' performance at least once over the last three reporting periods.	None	Over the past three reporting periods the Company has not engaged an external entity (advisor) to conduct an independent assessment of the Board of Directors' performance.
3.1 THE COMPANY'S CORPORATE SECRETARY ENSURES EFFICIENT ONGOING INTERACTION WITH SHAREHOLDERS, COORDINATES THE COMPANY'S EFFORTS TO PROTECT SHAREHOLDER RIGHTS AND INTERESTS AND SUPPORTS THE ACTIVITIES OF THE BOARD OF DIRECTORS.				
3.1.1	The corporate secretary has the knowledge, experience and qualifications sufficient to perform his/her duties, as well as an impeccable reputation and the trust of shareholders.	1. The company has adopted and published an internal document – regulations on the corporate secretary. 2. The biographical data of the corporate secretary are published on the corporate website and in the company's annual report with the same level of detail as for members of the board of directors and the company's executives.	Partial	Neither the Company's website nor the annual report contains biographical data of the corporate secretary.
3.1.2	The corporate secretary is sufficiently independent of the company's executive bodies and has the powers and resources required to perform his/her tasks.	1. The board of directors approves the appointment, removal and additional remuneration of the corporate secretary.	Full	–

4.1 REMUNERATION PAYABLE BY THE COMPANY IS SUFFICIENT TO ATTRACT, MOTIVATE, AND RETAIN PEOPLE WITH COMPETENCIES AND QUALIFICATIONS REQUIRED BY THE COMPANY. REMUNERATION PAYABLE TO THE MEMBERS OF THE BOARD OF DIRECTORS, EXECUTIVE BODIES AND OTHER KEY EXECUTIVE OFFICERS OF THE COMPANY IS IN COMPLIANCE WITH THE APPROVED REMUNERATION POLICY OF THE COMPANY.

4.1.1	The amount of remuneration paid by the company to members of the board of directors, executive bodies and other key executives creates sufficient incentives for them to work efficiently, while enabling the company to engage and retain competent and qualified specialists. At the same time, the company avoids unnecessarily high remuneration, as well as unjustifiably large gaps between remunerations of the above persons and the company's employees.	1. The company has in place an internal document (internal documents) – the policy (policies) on remuneration of members of the board of directors, executive bodies and other key executives, which clearly defines (define) the approaches to remuneration of the above persons.	Partial	The Company does not have in place a policy (policies) on remuneration of executives and other key managers.
4.1.2	The company's remuneration policy is developed by the remuneration committee and approved by the board of directors. The board of directors, assisted by the remuneration committee, ensures control over the introduction and implementation of the company's remuneration policy, revising and amending it as required.	1. During the reporting period, the remuneration committee considered the remuneration policy (policies) and the practical aspects of its (their) introduction and presented relevant recommendation to the board of directors as required.	Full	–
4.1.3	The company's remuneration policy includes transparent mechanisms for determining the amount of remuneration due to members of the board of directors, executive bodies and other key executives of the company, and regulates all types of expenses, benefits and privileges provided to such persons.	1. The company's remuneration policy (policies) includes (include) transparent mechanisms for determining the amount of remuneration due to members of the board of directors, executive bodies and other key executives of the company, and regulates (regulate) all types of expenses, benefits and privileges provided to such persons.	Partial	The Company does not have in place a policy (policies) on remuneration of executives and other key managers.
4.1.4	The company defines a policy on reimbursement (compensation) of costs detailing a list of reimbursable expenses and specifying service levels that members of the board of directors, executive bodies and other key executives of the company can claim. Such policy can make part of the company's remuneration policy.	1. The remuneration policy (policies) defines (define) the rules for reimbursement of costs incurred by members of the board of directors, executive bodies and other key executives of the company.	Full	–

4.2 REMUNERATION SYSTEM OF MEMBERS OF THE BOARD OF DIRECTORS ENSURES ALIGNMENT OF FINANCIAL INTERESTS OF THE DIRECTORS WITH LONG-TERM FINANCIAL INTERESTS OF SHAREHOLDERS.

4.2.1	<p>The company pays fixed annual remuneration to members of the board of directors.</p> <p>The company does not pay remuneration for attending particular meetings of the board of directors or its committees.</p> <p>The company does not apply any form of short-term motivation or additional financial incentive for members of the board of directors.</p>	<p>1. Fixed annual remuneration was the only form of monetary remuneration payable to members of the board of directors for their service on the board of directors during the reporting period.</p>	Full	–
4.2.2	<p>Long-term ownership of the company's shares helps align the financial interests of members of the board of directors with long-term interests of shareholders to the utmost. At the same time, the company does not link the right to dispose of shares to performance targets, and members of the board of directors do not participate in stock option plans.</p>	<p>1. If the company's internal document(s) – the remuneration policy (policies) stipulates (stipulate) provision of the company's shares to members of the board of directors, clear rules for share ownership by board members are defined and disclosed, aimed at stimulating long-term ownership of such shares.</p>	Not applicable, since the Regulations on Remuneration and Compensations Payable to Members of PAO NOVATEK Board of Directors does not provide for remuneration of the directors with company shares.	–
4.2.3	<p>The company does not provide for any extra payments or compensations in the event of early termination of office of members of the board of directors resulting from the change of control or any other reasons whatsoever.</p>	<p>1. The company does not provide for any extra payments or compensations in the event of early termination of office of members of the board of directors resulting from the change of control or any other reasons whatsoever.</p>	Full	–

4.3 THE COMPANY CONSIDERS ITS PERFORMANCE AND THE PERSONAL CONTRIBUTION OF EACH EXECUTIVE TO THE ACHIEVEMENT OF SUCH PERFORMANCE, WHEN DETERMINING THE AMOUNT OF REMUNERATION PAYABLE TO MEMBERS OF THE EXECUTIVE BODIES AND OTHER KEY EXECUTIVES OF THE COMPANY.

4.3.1	<p>Remuneration due to members of executive bodies and other key executives of the company is determined in a manner providing for reasonable and justified ratio of the fixed and variable parts of remuneration, depending on the company's performance and the employee's personal contribution.</p>	<p>1. In the reporting period, annual performance results approved by the board of directors were used to determine the amount of the variable part of remuneration due to members of executive bodies and other key executives of the company.</p> <p>2. During the latest assessment of the system of remuneration for members of executive bodies and other key executives of the company, the board of directors (remuneration committee) made sure that the company applies efficient ratio of the fixed and variable parts of remuneration.</p> <p>3. The company has in place a procedure that guarantees return to the company of bonus payments illegally received by members of executive bodies and other key executives of the company.</p>	None	–
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4.3.2	The company put in place a long-term incentive programme for members of executive bodies and other key executives of the company with the use of the company's shares (options and other derivative instruments where the company's shares are the underlying asset).	1. The company has in place a long-term incentive programme for members of executive bodies and other key executives of the company with the use of the company's shares (financial instruments based on the company's shares). 2. The long-term incentive programme for members of executive bodies and other key executives of the company implies that the right to dispose of shares and other financial instruments used in this programme takes effect at least three years after such shares or other financial instruments are granted. The right to dispose of such shares or other financial instruments is linked to the company's performance targets.	None	–
4.3.3	The compensation (golden parachute) payable by the company in case of early termination of powers of members of executive bodies or key executives at the company's initiative, provided that there have been no actions in bad faith on their part, does not exceed the double amount of the fixed part of their annual remuneration.	1. In the reporting period, the compensation (golden parachute) payable by the company in case of early termination of the powers of executive bodies or key executives at the company's initiative, provided that there have been no actions in bad faith on their part, did not exceed the double amount of the fixed part of their annual remuneration.	Full	–
5.1 THE COMPANY PUT IN PLACE EFFECTIVE RISK MANAGEMENT AND INTERNAL CONTROLS FRAMEWORK PROVIDING REASONABLE ASSURANCE IN THE ACHIEVEMENT OF THE COMPANY'S GOALS.				
5.1.1	The board of directors has determined the principles of, and approaches to, risk management and internal controls in the company.	1. Functions of different management bodies and divisions of the company in the risk management and internal controls are clearly defined in the company's internal documents /relevant policy approved by the board of directors.	Full	–
5.1.2	The company's executive bodies ensure establishment and continuous operation of efficient risk management and internal controls in the company.	1. The company's executive bodies ensured the distribution of functions and powers related to risk management and internal controls between the heads (managers) of divisions and departments accountable to them.	Full	–
5.1.3	The company's risk management and internal controls ensure an objective, fair and clear view of the current state and future prospects of the company, the integrity and transparency of the company's reporting, as well as reasonable and acceptable risk exposure.	1. The company has in place an approved anti-corruption policy. 2. The company established an accessible method of notifying the board of directors or the board's audit committee of breaches of any violations of the law, the company's internal procedures and code of ethics.	Full	–

5.1.4	The company's board of directors shall take necessary measures to make sure that the company's risk management and internal controls are consistent with the principles of, and approaches to, its setup determined by the board of directors, and that the system is functioning efficiently.	1. In the reporting period, the board of directors or the board's audit committee assessed the efficiency of the company's risk management and internal controls. Key results of this assessment are included in the company's annual report.	Full	–
5.2 THE COMPANY PERFORMS INTERNAL AUDIT FOR REGULAR INDEPENDENT ASSESSMENT OF THE RELIABILITY AND EFFICIENCY OF THE RISK MANAGEMENT AND INTERNAL CONTROLS AND THE CORPORATE GOVERNANCE PRACTICE.				
5.2.1	The company set up a separate business unit or engaged an independent external organization to carry out internal audits. Functional and administrative reporting lines of the internal audit department are delineated. The internal audit unit functionally reports to the board of directors.	1. To perform internal audits, the company set up a separate business unit – internal audit division, functionally reporting to the board of directors or to the audit committee, or engaged an independent external organization with the same line of reporting.	Full	–
5.2.2	The internal audit division assesses the performance of the internal controls, risk management, and corporate governance. The company applies generally accepted standards of internal audit.	1. In the reporting period, the performance of the internal controls and risk management was assessed as part of the internal audit procedure. 2. The company applies generally accepted approaches to internal audit and risk management.	Full	–
6.1 THE COMPANY AND ITS OPERATIONS ARE TRANSPARENT FOR ITS SHAREHOLDERS, INVESTORS AND OTHER STAKEHOLDERS.				
6.1.1	The company has developed and implemented an information policy ensuring an efficient exchange of information by the company, its shareholders, investors, and other stakeholders.	1. The company's board of directors approved an information policy developed in accordance with the Code's recommendations. 2. The board of directors (or its committee) reviewed the company's compliance with its information policy at least once in the reporting period.	Partial	The Board of Directors or its Committees did not review the Company's compliance with its Information Policy in the reporting period.
6.1.2	The company discloses information on its corporate governance and practice, including detailed information on compliance with the principles and recommendations of the Code.	1. The company discloses information on its corporate governance and general principles of corporate governance, including disclosure on its website. 2. The company discloses information on the membership of its executive bodies and board of directors, independence of the directors and their membership in the board's committees (as defined by the Code). 3. If the company has a controlling person, the company publishes a memorandum of the controlling person setting out this person's plans for the company's corporate governance.	Full	–

6.2 THE COMPANY MAKES TIMELY DISCLOSURES OF COMPLETE, UPDATED AND RELIABLE INFORMATION TO ALLOW SHAREHOLDERS AND INVESTORS TO MAKE INFORMED DECISIONS.

6.2.1	The company discloses information based on the principles of regularity, consistency and promptness, as well as availability, reliability, completeness and comparability of disclosed data.	<p>1. The company's information policy sets out approaches to, and criteria for, identifying information that can have a material impact on the company's evaluation and the price of its securities, as well as procedures ensuring timely disclosure of such information.</p> <p>2. If the company's securities are traded on foreign organized markets, the company ensured concerted and equivalent disclosure of material information in the Russian Federation and in the said markets in the reporting year.</p> <p>3. If foreign shareholders hold a material portion of the company's shares, information was disclosed both in the Russian language and one of the most widely used foreign languages in the reporting period.</p>	Full	–
6.2.2	The company avoids a formalistic approach to information disclosure and discloses material information on its operations, even if disclosure of such information is not required by law.	<p>1. In the reporting period, the company disclosed annual and 6M financial statements prepared under the IFRS. The company's annual report for the reporting period included annual financial statements prepared under the IFRS, along with the auditor's report.</p> <p>2. The company discloses full information on its capital structure in accordance with Recommendation 290 of the Code both in the annual report and on the company's website.</p>	Partial	<p>The Company's annual report for the reporting period did not include annual financial statements prepared under the IFRS or the auditor's report. These statements are disclosed on the Company's official website earlier than the annual report is prepared (in February of the year following the reporting year).</p> <p>The Company discloses its capital structure to the extent required by the applicable laws.</p>
6.2.3	The company's annual report, as one of the most important tools of its information exchange with shareholders and other interested parties, contains information enabling assessment of the company's annual performance results.	<p>1. The company's annual report contains information on the key aspects of its operating and financial performance.</p> <p>2. The company's annual report contains information on the environmental and social aspects of the company's operations.</p>	Full	–

6.3 THE COMPANY PROVIDES INFORMATION AND DOCUMENTS REQUESTED BY ITS SHAREHOLDERS IN ACCORDANCE WITH PRINCIPLES OF FAIRNESS AND EASE OF ACCESS.

6.3.1	The company provides information and documents requested by its shareholders in accordance with principles of fairness and ease of access.	1. The company's information policy establishes the procedure for providing shareholders with easy access to information, including information on legal entities controlled by the company, as requested by shareholders.	None	Access to information and copies of documents are provided to the shareholders at their request in the manner set out in the Federal Law on Joint-Stock Companies.
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6.3.2	When providing information to shareholders, the company shall ensure reasonable balance between the interests of particular shareholders and its own interests consisting in preserving the confidentiality of important commercial information which may materially affect its competitiveness.	1. In the reporting period, the company did not refuse any shareholder requests for information, or such refusals were justified. 2. In cases defined by the information policy, shareholders are warned of the confidential nature of the information and undertake to maintain its confidentiality.	Full	–
7.1 ACTIONS THAT MATERIALLY AFFECT OR MAY AFFECT THE COMPANY'S SHARE CAPITAL STRUCTURE AND ITS FINANCIAL POSITION AND ACCORDINGLY THE POSITION OF ITS SHAREHOLDERS ("MATERIAL CORPORATE ACTIONS") ARE TAKEN ON FAIR TERMS ENSURING THAT THE RIGHTS AND INTERESTS OF THE SHAREHOLDERS AND OTHER STAKEHOLDERS ARE OBSERVED.				
7.1.1	Material corporate actions include restructuring of the company, acquisition of 30% or more of the company's voting shares (takeover), execution by the company of major transactions, increase or decrease of the company's authorised capital, listing or de-listing of the company's shares, as well as other actions which may lead to material changes in the rights of shareholders or violation of their interests. The company's charter provides a list (criteria) of transactions or other actions classified as material corporate actions within the authority of the company's board of directors.	1. The company's charter includes a list of transactions or other actions deemed to be material corporate actions, and their identification criteria. Resolutions on material corporate actions are referred to the jurisdiction of the board of directors. When execution of such corporate actions is expressly referred by law to the jurisdiction of the general shareholders meeting, the board of directors presents relevant recommendations to shareholders. 2. According to the company's charter, material corporate actions include at least: company reorganization, acquisition of 30% or more of the company's voting shares (in case of takeover), entering in major transactions, increase or decrease of the company's charter capital, listing or de-listing of the company's shares.	Partial	The Company's Charter does not contain a specific list of corporate actions; however, matters classified as material corporate actions fall within the competence of the Board of Directors.
7.1.2	The board of directors plays a key role in passing resolutions or making recommendations on material corporate actions, relying on the opinions of the company's independent directors.	1. The company has in place a procedure enabling independent directors to express their opinions on material corporate actions prior to approval thereof.	None	The Company does not have in place a formal procedure enabling independent directors to express their opinions on material corporate actions prior to approval thereof, however independent directors take an active part in discussions on material corporate actions and within such discussions express their position on them.

7.1.3	When taking material corporate actions which would affect rights or legitimate interests of shareholders, equal terms and conditions are guaranteed for all shareholders; if the statutory procedure designed to protect shareholders' rights proves insufficient, additional measures are taken to protect their rights and legitimate interests. In doing so, the company is guided by the corporate governance principles set forth in the Code, as well as by formal statutory requirements.	<p>1. Due to specifics of the company's operations, the company's charter contains less stringent criteria for material corporate actions than required by law.</p> <p>2. All material corporate actions in the reporting period were duly approved before they were taken.</p>	Partial	Not all material corporate actions in the reporting period were duly approved before they were taken.
7.2 THE COMPANY PERFORMS MATERIAL CORPORATE ACTIONS IN SUCH A WAY AS TO ENSURE THAT SHAREHOLDERS TIMELY RECEIVE COMPLETE INFORMATION ABOUT SUCH ACTIONS, ALLOWING THEM TO INFLUENCE SUCH ACTIONS AND GUARANTEEING ADEQUATE PROTECTION OF THEIR RIGHTS WHEN PERFORMING SUCH ACTIONS.				
7.1.2	Information about material corporate actions is disclosed with explanations of the grounds, circumstances and consequences.	1. In the reporting period, the company disclosed information about its material corporate actions in due time and in detail, including the grounds for, and timelines of, such actions.	Full	–
7.2.2	Rules and procedures related to material corporate actions taken by the company are set out in the company's internal documents.	<p>1. The company's internal documents set out a procedure for engaging an independent appraiser to estimate the value of assets either disposed of or acquired in a major transaction or a related-party transaction.</p> <p>2. The company's internal documents set out a procedure for engaging an independent appraiser to estimate the value of shares acquired and redeemed by the company.</p> <p>3. The company's internal documents provide for an expanded list of grounds on which the company's directors and other persons as per the applicable law are deemed to be related parties to the company's transactions.</p>	None	The company's internal documents do not set out a procedure for engaging an independent appraiser to estimate the value of assets either disposed of or acquired in a major transaction or a related-party transaction because the need to engage an independent appraiser is stipulated by the Federal Law on Joint-Stock Companies.

FORWARD—LOOKING STATEMENTS

This Annual Review includes ‘forward-looking information’ within the meaning of Section 27A of the US Securities Act of 1933, as amended, and Section 21E of the US Securities Exchange Act of 1934, as amended. Certain statements included in this Annual Report and Accounts, including, without limitation, statements concerning plans, objectives, goals, strategies, future events or performance, and underlying assumptions and other statements, which are other than statements of historical facts. The words “believe,” “expect,” “anticipate,” “intends,” “estimate,” “forecast,” “project,” “will,” “may,” “should” and similar expressions identify forward-looking statements. Forward-looking statements include statements regarding: strategies, outlook and growth prospects; future plans and potential for future growth; liquidity, capital resources and capital expenditures; growth in demand for our products; economic outlook and industry trends; developments of our markets; the impact of regulatory initiatives; and the strength of our competitors. The forward-looking statements in this Annual Review are based upon various assumptions, many of which are based, in turn, upon further assumptions, including without limitation, management’s examination of historical operating trends, data contained in our records and other data available from third parties. Although we believe that these assumptions were reasonable when made, these assumptions are inherently subject to significant uncertainties and contingencies, which are difficult or impossible to predict and are beyond our control. As a result, we may not achieve or accomplish these expectations, beliefs or projections. In addition, important factors that, in our view, could cause actual results to differ materially from those discussed in the forward-looking statements include:

- changes in the balance of oil and gas supply and demand in Russia and Europe;
- the effects of domestic and international oil and gas price volatility and changes in regulatory conditions, including prices and taxes;
- the effects of competition in the domestic and export oil and gas markets;
- our ability to successfully implement any of our business strategies;

- the impact of our expansion on our revenue potential, cost basis and margins;
- our ability to produce target volumes in the event, among other factors, of restrictions on our access to transportation infrastructure;
- the effects of changes to our capital expenditure projections on the growth of our production;
- potentially lower production levels in the future than currently estimated by our management and/or independent petroleum reservoir engineers;
- inherent uncertainties in interpreting geophysical data;
- changes to project schedules and estimated completion dates;
- our success in identifying and managing risks to our businesses;
- the effects of changes to the Russian legal framework concerning currently held and any newly acquired oil and gas production licenses;
- changes in political, social, legal or economic conditions in Russia and the CIS;
- the effects of technological changes;
- the effects of changes in accounting standards or practices.

This list of important factors is not exhaustive. When relying on forward-looking statements, one should carefully consider the foregoing factors and other uncertainties and events, especially in light of the political, economic, social and legal environment in which we operate. Such forward looking statements speak only as of the date on which they are made. Accordingly, we do not undertake any obligation to update or revise any of them, whether as a result of new information, future events or otherwise. We do not make any representation, warranty or prediction that the results anticipated by such forward-looking statements will be achieved, and such forward-looking statements represent, in each case, only one of many possible scenarios and should not be viewed as the most likely or standard scenario. The information and opinions contained in this document are provided as at the date of this review and are subject to change without notice.

TERMS AND ABBREVIATIONS

Mentions in this Annual Report of "PAO NOVATEK", "NOVATEK", "the Company", "we" and "our" refer to PAO NOVATEK and/or its subsidiaries (according to IFRS methodology) and/or joint ventures (accounted for on an equity basis according to IFRS standards), depending upon the context, in which the terms are used.

barrel	one stock tank barrel, or 42 US gallons of liquid volume
bcm	billion cubic meters
boe	barrels of oil equivalent
km	kilometer(s)
mboe	thousand boe
mcm	thousand cubic meters
mt	thousand metric tons
mmboe	million boe
mmcm	million cubic meters
mmt	million metric tons
ton	metric ton
SEC	United States Securities and Exchange Commission
PRMS	Petroleum Resources Management System
YNAO	Yamal-Nenets Autonomous Region
RR	Russian rouble
LPG	liquified petroleum gases
LNG	liquified natural gas

CONVERSION FACTORS

1000 cubic meters of gas = 6.54 boe.

To convert crude oil and gas condensate reserves from tons to barrels we used various coefficients depending on the liquids density at each field.

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PAO NOVATEK

IFRS CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2016

AND INDEPENDENT AUDITOR'S REPORT

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Independent Auditor's Report

To the Shareholders and Board of Directors of PAO NOVATEK:

Our opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of PAO NOVATEK and its subsidiaries (together – the “Group”) as at 31 December 2016, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

What we have audited

The Group's consolidated financial statements comprise:

- the consolidated statement of financial position as at 31 December 2016;
- the consolidated statement of income for the year then ended;
- the consolidated statement of comprehensive income for the year then ended;
- the consolidated statement of cash flows for the year then ended;
- the consolidated statement of changes in equity for the year ended; and
- the notes to the consolidated financial statements, which include summary of significant accounting policies and other explanatory information.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report.

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

Independence

We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements of the Auditor's Professional Ethics Code and Auditor's Independence Rules that are relevant to our audit of the consolidated financial statements in the Russian Federation. We have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code.

Our audit approach

Overview

Materiality

Overall group materiality: 7,000 million Russian Roubles (“RUB”) which represents 4% of adjusted profit before tax excluding currency exchange differences, net gain on disposal of interests in joint ventures and the Group's share of joint ventures' currency exchange differences net of income tax.

Audit scope

- We conducted audit work covering all significant components and balances in Russia, Switzerland, Singapore and Republic of Cyprus.
- The group engagement team visited all significant locations in Russia and Switzerland.
- Our audit scope addressed more than 99% of the Group's revenues and more than 99% of the Group's absolute value of underlying profit before tax.

Key audit matters

- Impairment of production assets and investments in joint ventures;
- Accounting for trading activities in Europe;
- Valuation of non-commodity financial derivatives.

We designed our audit by determining materiality and assessing the risks of material misstatement in the consolidated financial statements. In particular, we considered where management made subjective judgements; for example, in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. We also addressed the risk of management override of internal controls, including among other matters consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

Materiality

The scope of our audit was influenced by our application of materiality. An audit is designed to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the consolidated financial statements.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall group materiality for the consolidated financial statements as a whole as set out in the table below. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, if any, both individually and in aggregate on the financial statements as a whole.

<i>Overall group materiality</i>	RUB 7,000 million
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<i>How we determined it</i>	4% of adjusted profit before tax excluding currency differences, net gain on disposal of interests in joint ventures and share of joint ventures' currency differences net of income tax.
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<i>Rationale for the materiality benchmark applied</i>	We chose profit before tax as the benchmark because, in our view, it is the benchmark against which the performance of the Group is most commonly measured by users, and is a generally accepted benchmark. The use of adjusted profit before tax mitigates the effect of volatility (that could be material) caused by non-recurring factors such as gains on disposals of assets and foreign exchange differences that can be material and provides a more stable basis for determining materiality, focusing on the underlying profitability of the Group.
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We chose 4% which is consistent with quantitative materiality thresholds used for profit-oriented companies in this sector which resulted in an increase in materiality of RUB 500 million or 7.7% as compared to the prior year that is consistent with the increase in operational performance.

Key audit matters

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

Key audit matter

How our audit addressed the Key audit matter

Impairment of production assets and investments in joint ventures

Due to the current economic environment in Russia and high volatility of prices for oil and oil products there is a possibility that property, plant and equipment, as well as investments in joint ventures may not be recoverable.

We focused on this area due to the significant carrying values of property, plant and equipment of the Group and investments in joint ventures and the nature of the judgements and assumptions management are required to make in determining whether there are any impairment triggers or impairments.

We analyzed management's assessment of impairment triggers and did not identify any further triggers, which had not been considered by management.

We critically evaluated the appropriateness and consistency of key assumptions of the impairment test models to ensure that the results of the performed tests are reasonable.

Specific work that we performed over the impairment analysis included:

- comparing the assumptions used within the impairment review model to approved budgets and business plans and other evidence of future intentions for individual properties, which we found to be consistent;
- benchmarking of key assumptions including commodity prices and discount rates and inflation rates against generally accepted forecasts which we found to be consistent;
- performing sensitivity analysis over key assumptions in the model in order to assess the potential impact of a range of possible outcomes; and
- challenged management on the inclusion of all appropriate assets and liabilities in the cash-generating units and in particular, given that the recoverable amount is determined based on value in use, the inclusion or exclusion of certain tax related balances and agreed that all relevant balances had been included.

Key audit matter

How our audit addressed the Key audit matter

None of the items noted above revealed an impairment charge.

Accounting for trading activities in Europe

The Group conducts natural gas foreign trading in active markets under long-term and short-term purchase and sales contracts. The Group also purchases and sells various derivative instruments (with reference of the delivery points to the European natural gas hubs) in order to increase delivery optimization and decrease exposure to the risk of negative changes in natural gas prices.

The fair value of long-term natural gas derivative contracts involving the physical delivery of natural gas is determined using internal models and other valuation techniques (the mark-to-market and mark-to-model analysis) due to the absence of quoted prices or other observable, market-corroborated data, for the duration of the contracts.

We focused on this area because of the complexity of the models and because model parameters are inherently subject to judgement applied by management.

We critically evaluated the appropriateness and consistency of key valuation assumptions used for the measurement of the contracts to ensure that the resulting valuation is reasonable.

We tested material valuations in detail and sought additional external evidence. We assessed the methodologies used, and the judgements and assumptions made. We identified the market data input used by the Group and tested them against independent data.

We tested the appropriateness of the valuation methodology applied and the integrity of the models used, and noted no material issues. We also tested the accuracy of the contractual inputs and the appropriateness of key valuation inputs including price and discount rates, and noted no material issues.

Where the Group entered into new significant contracts in the year, we tested the contracts and assumptions used to assess whether the accounting treatment adopted is in accordance with International Accounting Standard 39.

We also gained an understanding of the controls that are in place for these trading activities.

We identified no material issues.

Valuation of non-commodity financial derivatives

Certain shareholders' loans provided by the Group to its joint ventures include embedded derivatives that modify the cash flows of the loans based on financial and non-financial variables. The terms and conditions of each of these loans related to those variables were defined as a single compound embedded derivative. The Group designated these loans as financial assets at fair value through profit or loss. In accordance with IFRS, such loans are measured at fair value at each reporting date.

We focused on this area because of the significant impact of the valuation results on the financial

We evaluated the appropriateness and consistency of key valuation assumptions (such as expected free cash flows of the joint ventures, production volumes, and discount rates used) to ensure that the resulting valuation of the financial instruments is reasonable. Those assumptions mainly referred to the Group's projections of future expected free cash flows to be generated by the joint ventures and estimates of market interest rates applied in the valuation. We also tested the accuracy of the contractual inputs and analyzed the appropriateness of the valuation methodology.

Key audit matter

How our audit addressed the Key audit matter

statements of the Group and the fact that the measurement of the fair value of these loans is based on judgement and estimates applied by management which can be highly subjective.

We identified no material issues.

How we tailored our group audit scope

We tailored the scope of our audit in order to perform sufficient work to be able to give an opinion on the consolidated financial statements as a whole, taking into account the geographic and management structure of the Group, the accounting processes and controls and the industry in which the Group operates.

In establishing the overall group audit strategy and plan, we determined the type of work that needed to be performed at the reporting units by the group engagement team and by the component auditors from other PwC network firms. For each reporting unit we issued specific instructions to the audit teams of the component auditors within our audit scope. We determined the level of our and component auditors involvement we needed to be involved in the audit process at those reporting units so as to be able to conclude whether sufficient appropriate audit evidence had been obtained as a basis for our opinion on the consolidated financial statements as a whole. We determined whether we required an audit of full scope of financial information or whether a defined scope of specified procedures was sufficient.

The group consolidation, financial statements disclosures and a number of complex items are audited directly by the PAO NOVATEK audit engagement team. These items include the assessment of accounting estimates performed by management in respect of fair values and classification of financial assets and liabilities, deferred income tax asset recognition, estimation of oil and gas reserves, impairment of financial and non-financial assets, impairment provision for trade receivables, pension obligations, asset retirement obligations and assessment of joint arrangements.

By performing the procedures described above at the individual component level, combined with the additional procedures performed at the group level, we have obtained sufficient and appropriate audit evidence regarding the financial information of the Group to provide a basis for our opinion on the consolidated financial statements.

Other information

Management is responsible for the other information. The other information comprises report “Management’s discussion and analysis of financial condition and results of operations of PAO NOVATEK for the years ended 31 December 2016 and 2015” (but does not include the consolidated financial statements and our auditor’s report thereon), which we obtained prior to the date of this auditor’s report, and “Quarterly Issuer’s Report of PAO NOVATEK for the first quarter of 2017” as well as “Annual Report Review of PAO NOVATEK for 2016”, which are expected to be made available to us after that date.

Our opinion on the consolidated financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information that we obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, 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 consolidated financial statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS, 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.

In preparing the consolidated financial statements, management is responsible for assessing the Group'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 Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated 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 ISAs 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 consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- identify and assess the risks of material misstatement of the consolidated 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 control;
- obtain an understanding of internal control 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 Group's internal control;
- 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 Group's ability 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 consolidated 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 Group to cease to continue as a going concern;
- evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation;

- obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance 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.

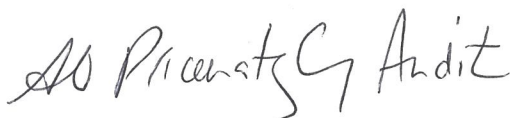
We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated 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.

The certified auditor on the audit resulting in this independent auditor's report is A.G. Yashkov.

21 February 2017

Moscow, Russian Federation



Wardell Jason Edward, Partner, for AO PricewaterhouseCoopers Audit



A.G. Yashkov, certified auditor (licence no. № 01-001391), AO PricewaterhouseCoopers Audit

Audited entity: PAO NOVATEK

State registration certificate №1461/94, issued by the administration of Oktyabrskiy district of Samara on 16 August 1994.

Certificate of inclusion in the Unified State Register of Legal Entities regarding the legal entity registered before 1 July 2002 No. 1026303117642 issued by the Inspectorate of the Russian Ministry of Taxes and Levies of Novokuybyshevsk, Samara Region on 20 August 2002.

Location of the Company according to the Charter: Russian Federation, Yamalo-Nenetski state, Purovsky region, Tarko-Sale

Mailing address: 629850, Yamalo-Nenetski state, Purovsky region, Tarko-Sale, Pobedi str., 22 "a".

Independent auditor: AO PricewaterhouseCoopers Audit

State registration certificate № 008.890, issued by the Moscow Registration Chamber on 28 February 1992

Certificate of inclusion in the Unified State Register of Legal Entities issued on 22 August 2002 under registration № 1027700148431

Member of Self-regulated organization of auditors «Russian Union of auditors» (Association)

ORNZ 11603050547 in the register of auditors and audit organizations

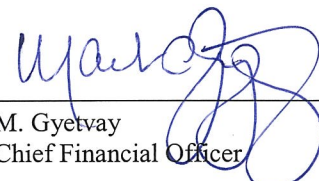
PAO NOVATEK
Consolidated Statement of Financial Position
(in millions of Russian roubles)

	Notes	At 31 December 2016	At 31 December 2015
ASSETS			
Non-current assets			
Property, plant and equipment	6	331,795	331,712
Investments in joint ventures	7	259,650	154,725
Long-term loans and receivables	8	209,145	230,799
Other non-current assets	9	30,484	34,316
Total non-current assets		831,074	751,552
Current assets			
Inventories	10	9,044	8,226
Current income tax prepayments		581	84
Trade and other receivables	11	41,586	37,564
Prepayments and other current assets	12	33,248	45,424
Cash and cash equivalents	13	48,301	29,187
Total current assets		132,760	120,485
Assets held for sale	5	-	7,987
Total assets		963,834	880,024
LIABILITIES AND EQUITY			
Non-current liabilities			
Long-term debt	14	161,296	252,050
Deferred income tax liabilities	26	24,656	23,706
Asset retirement obligations		7,605	4,149
Other non-current liabilities		3,766	2,273
Total non-current liabilities		197,323	282,178
Current liabilities			
Short-term debt and current portion of long-term debt	15	55,469	106,655
Trade payables and accrued liabilities	17	38,462	48,535
Current income tax payable		747	3,165
Other taxes payable		14,113	11,320
Total current liabilities		108,791	169,675
Total liabilities		306,114	451,853
Equity attributable to PAO NOVATEK shareholders			
Ordinary share capital		393	393
Treasury shares		(6,913)	(5,997)
Additional paid-in capital		31,297	31,297
Currency translation differences		(724)	(5,092)
Asset revaluation surplus on acquisitions		5,617	5,617
Retained earnings		618,680	399,861
Total equity attributable to PAO NOVATEK shareholders	18	648,350	426,079
Non-controlling interest		9,370	2,092
Total equity		657,720	428,171
Total liabilities and equity		963,834	880,024

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


L. Mikhelson
Chairman of the Management Committee

21 February 2017


M. Gyetvay
Chief Financial Officer

PAO NOVATEK
Consolidated Statement of Income

(in millions of Russian roubles, except for share and per share amounts)

	Notes	Year ended 31 December:	
		2016	2015
Revenues			
Oil and gas sales	19	533,857	472,007
Other revenues		3,615	3,318
Total revenues		537,472	475,325
Operating expenses			
Purchases of natural gas and liquid hydrocarbons	20	(134,268)	(120,504)
Transportation expenses	21	(133,462)	(130,229)
Taxes other than income tax	22	(44,053)	(36,630)
Depreciation, depletion and amortization	6	(34,631)	(19,980)
Materials, services and other	23	(19,133)	(14,551)
General and administrative expenses	24	(18,126)	(14,356)
Exploration expenses	6	(2,087)	(1,109)
Net impairment (expenses) reversals		(178)	204
Change in natural gas, liquid hydrocarbons and work-in-progress		439	2,113
Total operating expenses		(385,499)	(335,042)
Net gain on disposal of interests in joint ventures	5	73,072	989
Other operating income (loss), net		221	(542)
Profit from operations		225,266	140,730
Finance income (expense)			
Interest expense	25	(11,570)	(8,792)
Interest income	25	18,732	12,622
Change in fair value of non-commodity financial instruments	27	10,387	(10,505)
Foreign exchange gain (loss), net	25	(25,490)	(9,507)
Total finance income (expense)		(7,941)	(16,182)
Share of profit (loss) of joint ventures, net of income tax	7	90,839	(31,607)
Profit before income tax		308,164	92,941
Income tax expense			
Current income tax expense		(35,577)	(22,780)
Net deferred income tax benefit (expense)		(7,514)	3,958
Total income tax expense	26	(43,091)	(18,822)
Profit		265,073	74,119
Profit (loss) attributable to:			
Non-controlling interest		7,278	(277)
Shareholders of PAO NOVATEK		257,795	74,396
Basic and diluted earnings per share (in Russian roubles)		85.41	24.63
Weighted average number of shares outstanding (in millions)		3,018.5	3,020.3

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

PAO NOVATEK
Consolidated Statement of Comprehensive Income
(in millions of Russian roubles)

	Notes	Year ended 31 December:	
		2016	2015
Profit		265,073	74,119
Other comprehensive income (loss) that will not be reclassified subsequently to profit (loss):			
Remeasurement of pension obligations	16	(121)	(642)
Share of remeasurement of pension obligations of joint ventures		(21)	-
Total other comprehensive income (loss) that will not be reclassified subsequently to profit (loss)		(142)	(642)
Other comprehensive income (loss) that may be reclassified subsequently to profit (loss), net of income tax:			
Currency translation differences		4,368	(5,300)
Other comprehensive income (loss)		4,226	(5,942)
Total comprehensive income		269,299	68,177
Total comprehensive income (loss) attributable to:			
Non-controlling interest		7,278	(277)
Shareholders of PAO NOVATEK		262,021	68,454

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

PAO NOVATEK
Consolidated Statement of Cash Flows

(in millions of Russian roubles)

	Notes	Year ended 31 December:	
		2016	2015
Profit before income tax		308,164	92,941
Adjustments to profit before income tax:			
Depreciation, depletion and amortization		34,631	19,980
Impairment expenses (reversals), net		178	(204)
Foreign exchange loss (gain), net		25,490	9,507
Loss (gain) on disposal of assets, net		(73,072)	(941)
Interest expense		11,570	8,792
Interest income		(18,732)	(12,622)
Share of loss (profit) in joint ventures, net of income tax	7	(90,839)	31,607
Change in fair value of			
non-commodity financial instruments		(10,387)	10,505
Revaluation of commodity derivatives through loss (profit)		1,778	1,006
Increase in long-term advances given		(3,331)	(9,352)
Other adjustments		152	(10)
Working capital changes			
Decrease (increase) in trade and other receivables,			
prepayments and other current assets		2,592	(4,537)
Decrease (increase) in inventories		(861)	(2,280)
Increase (decrease) in trade payables and accrued liabilities,			
excluding interest and dividends payable		9,953	(310)
Increase (decrease) in taxes payable, other than income tax		2,836	2,009
Total effect of working capital changes		14,520	(5,118)
Dividends received from joint ventures		-	1,850
Interest received		1,983	1,454
Income taxes paid excluding actual payments			
relating to disposal of stakes in joint ventures		(28,314)	(16,531)
Net cash provided by operating activities		173,791	132,864
Cash flows from investing activities			
Purchases of property, plant and equipment		(28,170)	(42,224)
Payments for mineral licenses		(1,928)	-
Purchases of materials for construction		(929)	(2,313)
Payments for acquisition of subsidiaries net of cash acquired	5, 17	(2,961)	(3,630)
Additional capital contributions to joint ventures	7	(19,565)	-
Proceeds from disposal of stakes in joint ventures	5	84,978	-
Costs to sell stakes in joint ventures	5	(2,634)	-
Actual income tax payments			
relating to disposal of stakes in joint ventures		(9,932)	-
Interest paid and capitalized		(5,314)	(6,047)
Guarantee fees paid		(1,061)	-
Loans provided to joint ventures	8	(6,645)	(108,570)
Repayments of loans provided to joint ventures	8	6,038	3,710
Net cash provided by (used for) investing activities		11,877	(159,074)

PAO NOVATEK**Consolidated Statement of Cash Flows**

(in millions of Russian roubles)

	Notes	Year ended 31 December:	
		2016	2015
Cash flows from financing activities			
Proceeds from long-term debt		6,373	71,345
Repayments of long-term debt		(82,753)	(42,240)
Proceeds from short-term debt			
with original maturity more than three months		-	21,300
Repayments of short-term debt			
with original maturity more than three months		(21,300)	-
Net increase (decrease) in short-term debt			
with original maturity three months or less		(5,040)	5,880
Interest paid		(11,423)	(7,149)
Dividends paid	18	(41,653)	(35,640)
Purchase of treasury shares	18	(916)	(782)
Net cash provided by (used for) financing activities		(156,712)	12,714
Net effect of exchange rate changes on cash and cash equivalents		(9,842)	1,365
Net increase (decrease) in cash and cash equivalents		19,114	(12,131)
Cash and cash equivalents at the beginning of the period		29,187	41,318
Cash and cash equivalents at the end of the period		48,301	29,187

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

PAO NOVATEK
Consolidated Statement of Changes in Equity

(in millions of Russian roubles, except for number of shares)

<i>For the year ended 31 December 2015</i>	<i>Number of ordinary shares (in millions)</i>	Ordinary share capital	Treasury shares	Additional paid-in capital	Currency translation differences	Asset revaluation surplus on acquisitions	Retained earnings	Equity attributable to PAO NOVATEK shareholders	Non- controlling interest	Total equity
1 January 2015	3,020.4	393	(5,222)	31,297	208	5,617	352,462	384,755	2,369	387,124
Profit (loss)	-	-	-	-	-	-	74,396	74,396	(277)	74,119
Other comprehensive income (loss)	-	-	-	-	(5,300)	-	(642)	(5,942)	-	(5,942)
Total comprehensive income (loss)	-	-	-	-	(5,300)	-	73,754	68,454	(277)	68,177
Dividends (Note 18)	-	-	-	-	-	-	(35,640)	(35,640)	-	(35,640)
Effect from other changes in joint ventures' net assets (Note 7)	-	-	-	-	-	-	9,285	9,285	-	9,285
Purchase of treasury shares (Note 18)	(1.3)	-	(775)	-	-	-	-	(775)	-	(775)
31 December 2015	3,019.1	393	(5,997)	31,297	(5,092)	5,617	399,861	426,079	2,092	428,171

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

PAO NOVATEK
Consolidated Statement of Changes in Equity

(in millions of Russian roubles, except for number of shares)

<i>For the year ended 31 December 2016</i>	<i>Number of ordinary shares (in millions)</i>	Ordinary share capital	Treasury shares	Additional paid-in capital	Currency translation differences	Asset revaluation surplus on acquisitions	Retained earnings	Equity attributable to PAO NOVATEK shareholders	Non- controlling interest	Total equity
1 January 2016	3,019.1	393	(5,997)	31,297	(5,092)	5,617	399,861	426,079	2,092	428,171
Profit (loss)	-	-	-	-	-	-	257,795	257,795	7,278	265,073
Other comprehensive income (loss)	-	-	-	-	4,368	-	(142)	4,226	-	4,226
Total comprehensive income (loss)	-	-	-	-	4,368	-	257,653	262,021	7,278	269,299
Dividends (Note 18)	-	-	-	-	-	-	(41,653)	(41,653)	-	(41,653)
Effect from other changes in joint ventures' net assets (Note 7)	-	-	-	-	-	-	2,819	2,819	-	2,819
Purchase of treasury shares (Note 18)	(1.4)	-	(916)	-	-	-	-	(916)	-	(916)
31 December 2016	3,017.7	393	(6,913)	31,297	(724)	5,617	618,680	648,350	9,370	657,720

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

1 ORGANIZATION AND PRINCIPAL ACTIVITIES

PAO NOVATEK (hereinafter referred to as “NOVATEK” or the “Company”) and its subsidiaries (hereinafter jointly referred to as the “Group”) is an independent oil and gas company engaged in the acquisition, exploration, development, production, processing, and marketing of hydrocarbons with its oil and gas operations located mainly in the Yamal-Nenets Autonomous Region (“YNAO”) of the Russian Federation. The Group delivers its natural gas on the Russian Federation’s domestic market and liquid hydrocarbons on both the Russian domestic and international markets.

The Group sells its natural gas on the Russian domestic market at unregulated market prices (except for deliveries to residential customers); however, the majority of natural gas sold on the Russian domestic market by all producers is sold at prices regulated by the governmental agency of the Russian Federation that carries out state regulation of prices and tariffs for goods and services of natural monopolies in energy, utilities and transportation. The Group’s natural gas sales volumes fluctuate on a seasonal basis mostly due to Russian weather conditions, with sales peaking in the winter months of December and January and troughing in the summer months of July and August.

The Group processes unstable gas condensate at its Purovsky Gas Condensate Processing Plant located in close proximity to its fields into stable gas condensate and liquefied petroleum gas. The majority of stable gas condensate is further processed at the Group’s Gas Condensate Fractionation and Transshipment Complex located at the port of Ust-Luga on the Baltic Sea into higher-value refined products (naphtha, jet fuel, gasoil and fuel oil). The remaining stable gas condensate volumes are sold on domestic and international markets. The Group sells its liquid hydrocarbons at prices that are subject to fluctuations in underlying benchmark crude oil, naphtha and other gas condensate refined products prices. The Group’s liquids sales volumes are not subject to significant seasonal fluctuations.

The Group also purchases and sells natural gas on the European market under long-term and short-term supply contracts to carry out its foreign commercial trading activities.

In March 2016, the Group closed the transaction on the disposal of a 9.9 percent equity stake in OAO Yamal LNG, the Group’s joint venture, to China’s investment fund Silk Road Fund Co. Ltd. (see Note 5).

In September 2016, the Group and Eni S.p.A. (hereinafter referred to as the “Concessionaries”), through their wholly owned subsidiaries NOVATEK Montenegro B.V. and Eni Montenegro B.V., entered into a Concession Contract with the State of Montenegro for the exploration and production of hydrocarbons on four offshore blocks located in the Adriatic Sea (hereinafter referred to as the “Concession Contract”). The Concession Contract stipulates that the Concessionaries are assigned a 50 percent participating interest each and are committed to undertake specified joint upstream activities during the exploration phase within seven years (see Note 28). The Group considers that the Concession Contract constitutes a joint arrangement and classifies it as a joint operation in accordance with IFRS 11, *Joint Arrangements*.

On 12 October 2016, an amended version of NOVATEK’s Charter was registered, according to which the Company’s name was changed to PAO NOVATEK (former name – OAO NOVATEK). The Company’s name was changed to comply with the current provisions of the Part 1 Chapter 4 of the Civil Code of the Russian Federation.

2 BASIS OF PREPARATION

The accompanying consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) under the historical cost convention, as modified by the initial recognition of financial instruments based on fair value, and by the revaluation of available-for-sale financial assets and financial instruments categorised at fair value through profit or loss. In the absence of specific IFRS guidance for oil and gas producing companies, the Group has developed accounting policies in accordance with other generally accepted accounting principles for oil and gas producing companies, mainly US GAAP, insofar as they do not conflict with IFRS principles.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise judgment in the process of applying the Group’s accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4.

2 BASIS OF PREPARATION (CONTINUED)

Most of the Group entities prepare their statutory financial statements in accordance with the Regulations on Accounting and Reporting of the Russian Federation. The Group's consolidated financial statements are based on the statutory records with adjustments and reclassifications recorded in the consolidated financial statements for the fair presentation in accordance with IFRS. The principal adjustments primarily relate to: (a) depreciation, depletion and amortization, and valuation of property, plant and equipment; (b) consolidation of subsidiaries; (c) business combinations; (d) accounting for income taxes; (e) revaluation of shareholders' loans provided by the Group to its joint ventures to fair value; and (f) valuation of unrecoverable assets, expense recognition and other provisions.

Functional and presentation currency. The consolidated financial statements are presented in Russian roubles, the Group's reporting (presentation) currency and the functional currency for the majority of the Group's entities. The assets and liabilities (both monetary and non-monetary) of the Group entities whose functional currency is not the Russian rouble are translated into Russian roubles at the closing exchange rate at each balance sheet date. All items included in the shareholders' equity, other than profit or loss, are translated at historical exchange rates. The financial results of these entities are translated into Russian roubles using average exchange rates for each reporting period. Exchange adjustments arising on the opening net assets and the profits for the reporting period are taken to other comprehensive income before the disposal of the foreign operation and reported as currency translation differences in the consolidated statement of changes in equity and the consolidated statement of comprehensive income.

Exchange rates for foreign currencies in which the Group conducted significant transactions or had significant monetary assets and/or liabilities in the reporting period were as follows:

Russian roubles to one currency unit	At 31 December 2016	At 31 December 2015	Average rate for the year ended 31 December:	
			2016	2015
US dollar (USD)	60.66	72.88	67.03	60.96
Euro (EUR)	63.81	79.70	74.23	67.78
Polish zloty (PLN)	14.44	18.79	17.03	16.18

Exchange rates and restrictions. The Russian rouble is not a fully convertible currency outside the Russian Federation and, accordingly, any remeasurement of Russian rouble amounts to US dollars or any other currency should not be construed as a representation that such Russian rouble amounts have been, could be, or will in the future be converted into other currencies at these exchange rates.

Reclassifications. Certain reclassifications have been made to the comparative figures to conform to the current period presentation with no effect on profit for the period or shareholder's equity. Insurance expenses relating to production assets and major part of expenses of the Group's research and development center are presented in these consolidated financial statements within materials, services and other expenses and exploration expenses depending on their function, which were previously disclosed within general and administrative expenses. Accordingly, expenses in the amount of RR 807 million were reclassified from general and administrative expenses to materials, services and other expenses and exploration expenses in the amount of RR 465 million and RR 342 million, respectively, for the year ended 31 December 2015.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Adoption of new and amended standards and interpretations. In 2016, the Group adopted all IFRS, amendments and interpretations which are effective 1 January 2016 and relevant to its operations. None of them had material impact on the Group's consolidated financial statements.

Principles of consolidation. Subsidiaries are all entities (including structured entities) over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvements with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are consolidated from the date on which control is transferred to the Group (acquisition date) and are deconsolidated from the date that control ceases.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Intercompany transactions, balances and unrealized gains on transactions between group companies are eliminated. The Group and all of its subsidiaries use uniform accounting policies consistent with the Group's policies.

Non-controlling interest is that part of the net results and of the equity of a subsidiary attributable to interests which are not owned, directly or indirectly, by the Group. Non-controlling interest forms a separate component of the Group's equity. Changes in the Group's ownership interest in a subsidiary that do not result in the loss of control are accounted for as equity transactions.

Business combinations. The acquisition method of accounting is used to account for acquisitions of subsidiaries. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured at their fair values at the acquisition date, irrespective of the extent of any non-controlling interest.

The Group measures non-controlling interest on an acquisition-by-acquisition basis, either at: (a) fair value, or (b) the non-controlling interest's proportionate share of net assets of the acquiree.

Goodwill is measured by deducting the net assets of the acquiree from the aggregate of the consideration transferred for the acquiree, the amount of non-controlling interest in the acquiree and fair value of an interest in the acquiree held immediately before the acquisition date. Any negative amount ("negative goodwill") is recognized in profit or loss, after management reassesses whether it identified all the assets acquired and all liabilities and contingent liabilities assumed and reviews appropriateness of their measurement.

The consideration transferred for the acquiree is measured at the fair value of the assets transferred, equity instruments issued and liabilities incurred or assumed, including fair value of assets or liabilities from contingent consideration arrangements but excludes acquisition related costs such as advisory, legal, valuation and similar professional services. Transaction costs incurred for issuing equity instruments are deducted from equity; transaction costs incurred for issuing debt are deducted from its carrying amount and all other transaction costs associated with the acquisition are expensed.

Joint arrangements. Investments in joint arrangements are classified as either joint ventures or joint operations depending on the contractual rights and obligations each investor has rather than the legal structure of the joint arrangement.

The Group's investments in joint ventures are accounted for using the equity method. Under the equity method, an investment in a joint venture is initially recognized at cost. The difference between the cost of an acquisition and the share of the fair value of the joint venture's identifiable net assets represents goodwill upon acquiring the joint venture.

Post-acquisition changes in the Group's share of net assets of a joint venture are recognized as follows: (a) the Group's share of profits or losses is recorded in the consolidated profit or loss for the year as share of financial result of joint ventures; (b) the Group's share of other comprehensive income or loss is recognized in other comprehensive income or loss and presented separately; (c) dividends received or receivable from a joint venture are recognized as a reduction in the carrying amount of the investment; (d) all other changes in the Group's share of the carrying value of net assets of joint ventures are recognized within retained earnings in the consolidated statement of changes in equity.

After application of the equity method, including recognizing the joint venture's losses, the entire carrying amount of the investment is tested for impairment as a single asset whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

When the Group's share of losses in a joint venture equals or exceeds its interest in the joint venture, the Group does not recognize further losses, unless it has incurred obligations or made payments on behalf of the joint ventures. The interest in a joint venture is the carrying amount of the investment in the joint venture together with any long-term interests that, in substance, form part of the Group's net investment in the joint venture, including receivables and loans for which settlement is neither planned nor likely to occur in the foreseeable future.

Unrealized gains on transactions between the Group and its joint ventures are eliminated to the extent of the Group's interest in joint ventures; unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Accounting policies of joint ventures have been changed where necessary to ensure consistency with the policies adopted by the Group.

The Group recognizes on a line-by-line basis in the consolidated financial statements its share of assets, liabilities, revenues and expenses of its joint operations in accordance with the provisions of the respective joint operation agreements.

Disposals of subsidiaries, associates or joint ventures. When the Group ceases to consolidate a subsidiary or account for an investment using the equity method because of a loss of control, joint control or significant influence, any retained interest in the entity is remeasured to its fair value, with the change in carrying amount recognized in profit or loss. The fair value is the initial carrying amount for the purposes of subsequently accounting for the retained interest as an associate, joint venture or financial asset. In addition, any amounts previously recognized in other comprehensive income in respect of that entity are accounted for as if the Group had directly disposed of the related assets or liabilities. This may mean that amounts previously recognized in other comprehensive income are recycled to profit or loss.

If the ownership interest in a joint venture is reduced but joint control is retained or replaced with significant influence, the Group continues to apply the equity method and does not remeasure the retained interest; only a proportionate share of the amounts previously recognized in other comprehensive income are reclassified to profit or loss where appropriate.

Foreign currency transactions. Transactions denominated in foreign currencies are converted into the functional currency of each entity of the Group at the exchange rates prevailing on the date of transactions. Exchange gains and losses resulting from foreign currency remeasurement into the functional currency are included in the determination of profit (loss) for the reporting period.

Monetary assets and liabilities denominated in foreign currencies are converted into the functional currency of each entity of the Group by applying the year end exchange rate and the effect is stated in the consolidated statement of income. Non-monetary assets and liabilities denominated in foreign currencies valued at cost are converted into the functional currency of each entity of the Group at the initial exchange rate. Non-monetary assets that are remeasured to fair value, recoverable amount or realizable value, are translated at the exchange rate applicable to the date of remeasurement.

Extractive activities. The Group follows the successful efforts method of accounting for its oil and gas properties and equipment whereby property acquisitions and development costs are capitalized, and exploration costs (geological and geophysical expenditures, expenditures associated with the maintenance of non-proven reserves and other expenditures relating to exploration activity), excluding exploratory drilling expenditures and exploration license acquisition costs, are recognized within operating expenses in the consolidated statement of income as incurred.

Exploration license acquisition costs and exploratory drilling costs are recognized as exploration assets in line “property, plant and equipment” until it is determined whether proved reserves justifying their commercial development have been found. If no proved reserves are found, the relevant costs are charged to the consolidated statement of income. When proved reserves are determined, exploration license acquisition costs are reclassified to proved properties acquisition costs and exploratory drilling costs are reclassified to development expenditure categories within “property, plant and equipment”. Exploration license acquisition costs and exploratory drilling costs recognized as exploration assets are reviewed for impairment on an annual basis.

The cost of 3-D seismic surveys used to assist production, increase total recoverability and determine the desirability of drilling additional development wells within proved reservoirs are capitalized as development costs. All other seismic costs are expensed as incurred.

Production costs and overheads are charged to expense as incurred.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Property, plant and equipment. Property, plant and equipment are carried at historical cost of acquisition or construction and adjusted for accumulated depreciation, depletion, amortization and impairment.

The cost of self-constructed assets includes the cost of direct materials, direct employee related costs, a pro-rata portion of depreciation of assets used for construction and an allocation of the Group's overhead costs.

The present value of the estimated costs of dismantling oil and gas production facilities, including abandonment and site restoration costs, are recognized when the obligation is incurred and are included within the carrying value of property, plant and equipment, subject to depletion using the unit-of-production method.

Depreciation, depletion and amortization of oil and gas properties and equipment is calculated using the unit-of-production method for each field based upon total proved reserves for costs associated with acquisitions of proved properties and common infrastructure facilities, and proved developed reserves for other development costs, including wells.

The Group's principal oil and gas reserves have been independently estimated by internationally recognized petroleum engineers whereas other oil and gas reserves of the Group have been determined based on estimates of mineral reserves prepared by the Group's management in accordance with internationally recognized definitions.

A portion of the reserves used for depreciation, depletion and amortization calculations include reserves expected to be produced beyond license expiry dates. The Group's management believes that there is requisite legislation and past experience to extend mineral licenses at the initiative of the Group and, as such, intends to extend its licenses for properties expected to produce beyond the current license expiry dates.

Where unit-of-production method does not reflect useful life and pattern of consumption of particular oil and gas assets, such as processing facilities serving several properties, those assets are depreciated on a straight-line basis.

Property, plant and equipment, other than oil and gas properties and equipment, are depreciated on a straight-line basis over their estimated useful lives. Land and assets under construction are not depreciated.

The estimated useful lives of the Group's property, plant and equipment, other than oil and gas properties and equipment, are as follows:

	<u>Years</u>
Machinery and equipment	5-15
Processing facilities	20-30
Buildings	25-50

Costs of minor repairs and maintenance are expensed when incurred. Cost of replacing major parts or components that extend the life of property, plant and equipment items are capitalized and depreciated over the estimated remaining life of the major part or component. All components that are replaced are written off.

At each reporting date management assesses whether there is any indication of impairment in respect of property, plant and equipment. If any such indication exists, management estimates the recoverable amount, which is determined as the higher of an asset's fair value less selling costs and its value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows which are largely independent of the cash inflows from other assets or groups of assets (cash generating units). The carrying amount is reduced to the recoverable amount and the impairment loss is recognized in profit or loss for the respective period. An impairment loss recognized for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset's recoverable amount.

Gains and losses on disposals of property, plant and equipment are determined by comparing proceeds with the carrying amount. Gains and losses are recognized within other operating profit (loss) in the consolidated statement of income.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Borrowing costs. Interest costs on borrowings and exchange differences arising from foreign currency borrowings (to the extent that they are regarded as an adjustment to interest costs) used to finance the construction of property, plant and equipment are capitalized during the period of time that is required to complete and prepare the asset for its intended use. All other borrowing costs are recognized in the consolidated statement of income.

Intangible assets. Intangible assets that have a finite useful life are amortized using the straight-line method over the period of their useful life. There were no intangible assets with indefinite useful lives held by the Group at the reporting dates.

Non-current assets held for sale. Non-current assets are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use and a sale is considered highly probable. They are measured at the lower of their carrying amount and fair value less costs to sell.

The Group ceases to use the equity method of accounting in relation to the interest in a joint venture or an associate classified as an asset held for sale.

Inventories. Natural gas, gas condensate, crude oil and gas condensate refined products are valued at the lower of cost or net realizable value. The cost of inventories includes direct cost of materials, direct operating costs, and related production overhead expenses and is recorded on a first-in-first-out (“FIFO”) basis. Net realizable value is the estimate of the selling price in the ordinary course of business, less selling expenses.

Materials and supplies are carried at amounts which do not exceed their respective recoverable amounts in the normal course of business.

Effective interest method. The effective interest method is a method of calculating the carrying value of a financial asset or a financial liability held at amortized cost and of allocating the interest income or interest expense over the relevant period.

The effective interest rate is the rate that exactly discounts future cash payments and receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying value of the financial asset or financial liability.

Derivatives. Derivative instruments are contracts: (a) whose value changes in response to the change in one or more observable variables; (b) that do not require any material initial net investment; and (c) that are settled at a future date. Derivative financial instruments are carried as financial assets when fair value is positive and as financial liabilities when fair value is negative. Gains or losses arising from changes in the fair value of derivative instruments are included in the consolidated statement of income. The Group does not apply hedge accounting.

Contracts to buy or sell a non-financial item that can be settled net in cash or another financial instrument, or by exchanging financial instruments with the exception of contracts that were entered into and continue to be held for the purpose of the receipt or delivery of a non-financial item in accordance with the Group’s expected purchase, sale or usage requirements, are accounted for as derivatives. Gains or losses arising from changes in the fair value of commodity derivatives are recognized within other operating income (loss) in the consolidated statement of income.

Derivatives embedded in other non-derivative financial instruments or in non-financial host contracts are recognized as separate derivatives when their risks and economic characteristics are not closely related to those of the host contracts, and the host contracts are not carried at fair value.

Where there is an active market for a commodity or other non-financial item subject of a purchase or sale contract, a pricing formula will, for instance, be considered to be closely related to the host purchase or sales contract if the price formula is related to the market for such host contracts. A price formula with indexation to other markets or products will however result in the recognition of a separate derivative. Where there is no active market for the commodity or other non-financial item in question, the Group assesses the characteristics of such a price related embedded derivative to be closely related to the host contract if the price formula is based on relevant indexations commonly used by other market participants. Contracts are assessed for embedded derivatives when the Group becomes a party to them, including at the date of a business combination.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Certain shareholders' loans provided by the Group to its joint ventures include embedded derivatives that modify cash flows of the loans based on financial (market interest rates) and non-financial (interest rate on borrowings of the lender and free cash flows of the borrower) variables. The risks relating to these variables are interrelated; therefore, terms and conditions of each of these loans related to those variables were defined as a single compound embedded derivative. The Group designated these loans as financial assets at fair value through profit or loss (see Note 27).

In accordance with IAS 39, *Financial instruments: recognition and measurement*, such loans are initially measured at fair value based on future expected cash flows discounted at benchmark interest rates adjusted for the borrower credit risk (Level 3 in the fair value measurement hierarchy described in Note 27). The difference between the loan proceeds and the initial fair value is recorded as the Group's investment in the joint ventures. Subsequently, the loans are measured at fair value at each reporting date with recognition of the revaluation through profit or loss. Interest income and foreign exchanges differences (calculated using the effective interest method), and remaining effect from fair value remeasurement are disclosed separately in the consolidated statement of income.

Non-derivative financial instruments. Non-derivative financial assets include cash and cash equivalents, trade receivables, other financial receivables, some of loans issued, and other investments. The Group classifies its non-derivative financial assets as loans and receivables.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Financial assets classified as loans and receivables are recognized initially at fair value, normally being the transaction price, plus directly attributable transaction costs, and subsequently carried at amortized cost using the effective interest method. Gains and losses are recognized in the consolidated statement of income when the loans and receivables are derecognized or impaired, as well as through the amortization process.

Loans and receivables are included in current assets, except for maturities greater than 12 months after the balance sheet date which are classified as non-current assets.

Loans and receivables are analyzed for impairment on a debtor by debtor basis. A provision for impairment of loans and receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to their original terms. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The amount of the provision is recognized within operating expenses in the consolidated statement of income. Subsequent recoveries of amounts previously written off are credited against the amount of the provision in the consolidated statement of income.

The Group's non-derivative financial liabilities are classified as financial liabilities measured at amortized cost.

Financial liabilities included in this category are initially recognized at fair value less directly attributable transaction costs. For interest-bearing debt, the liability is recognized at the fair value of the proceeds received net of associated issue costs. After initial recognition, financial liabilities included in this category are measured at amortized cost using the effective interest method. This category of financial liabilities includes trade and other payables and debt in the consolidated statement of financial position.

Offsetting financial instruments. Financial assets and liabilities are offset and the net amount reported in the statement of financial position only when there is a legally enforceable right to offset the recognized amounts, and there is an intention to either settle on a net basis, or to realize the asset and settle the liability simultaneously. Such a right of set off (a) must not be contingent on a future event and (b) must be legally enforceable in all of the following circumstances: (i) in the normal course of business, (ii) in the event of default and (iii) in the event of insolvency or bankruptcy.

Financial guarantee contracts. Financial guarantee contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument. Financial guarantee contracts are recognized initially as a liability at fair value, adjusted for transaction costs that are directly attributable to the issuance of the guarantee. Subsequently, the liability is measured at the higher of the best estimate of the expenditure required to settle the present obligation at the reporting date and the amount recognized less cumulative amortization, if applicable.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Provisions for liabilities and charges. Provisions are recognized when the Group has a present legal or constructive obligation as a result of past events; when it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and a reliable estimate of the amount of the obligation can be made.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognized even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be low.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. Provisions are reassessed at each reporting date and changes in the provisions resulting from the passage of time are recognized in the consolidated statement of income as interest expense. Where the Group expects a provision to be reimbursed, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain.

Asset retirement obligations. An asset retirement obligation is recognized when the Group has a present legal or constructive obligation to dismantle, remove and restore items of property, plant and equipment whose construction is substantially completed. The amount of the obligation is the present value of the estimated expenditures expected to be required to settle the obligation, determined using discount rates reflecting adjustments for risks specific to the obligation. Changes in the obligation resulting from the passage of time are recognized in the consolidated statement of income as interest expense. Changes in the obligation, reassessed at each balance sheet date, related to a change in the expected pattern of settlement of the obligation, or in the estimated amount of the obligation or in the discount rates, are treated as a change in an accounting estimate in the current period. Such changes are reflected as adjustments to the carrying value of property, plant and equipment and the corresponding liability.

The Group's exploration, development and production activities involve the use of wells, related equipment and operating sites, oil and gas gathering and treatment facilities and in-field pipelines. Generally, licenses and other regulatory acts require that such assets be decommissioned upon the completion of production, i.e. the Group is obliged to decommission wells, dismantle equipment, restore the sites and perform other related activities. The Group's estimates of these obligations are based on current regulatory or license requirements, as well as actual dismantling and related costs.

The Group's management believes that due to the limited history of gas condensate processing plants activities, the useful lives of these assets are indeterminable (while certain of the operating components and equipment have definite useful lives). Because of these reasons, and the lack of clear legal requirements as to the recognition of obligations, the present value of an asset retirement obligation for such processing facilities cannot be reasonably estimated and, therefore, legal or contractual asset retirement obligations related to these assets are not recognized.

Due to continuous changes in the Russian regulatory and legal environment, there could be future changes to the requirements and contingencies associated with the retirement of long-lived assets.

Pension obligations. The Group contributes to the Pension Fund of the Russian Federation on behalf of its employees based on gross salary payments. Mandatory contributions to the Pension Fund of the Russian Federation, which is a defined contribution plan, are expensed when incurred and are included in the employee compensation in the consolidated statement of income.

The Group also operates a non-contributory post-employment defined benefit plan based on employees' years of service and average salary (see Note 16).

The liability recognized in the consolidated statement of financial position in respect of the defined benefit pension plan is the present value of the defined benefit obligations at the balance sheet date. The present value of the pension obligations are determined by discounting the estimated future cash outflows and then attributing such present value to years of service of the respective employees. The defined benefit obligations are calculated annually by independent actuaries using the projected unit credit method. The discount rate was determined by reference to Russian rouble denominated bonds issued by the Government of the Russian Federation chosen to match the duration of the post-employment benefit obligations.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Actuarial gains and losses on assets and liabilities arising from experience adjustments and changes in actuarial assumptions are charged or credited to other comprehensive income in the period in which they arise. They are not reclassified to profit or loss in subsequent periods. Past-service costs are recognized in profit or loss in the period when a plan is amended, and curtailment gains and losses are accounted for as a past-service cost.

Non-financial guarantees. The Group issued a number of parent company guarantees that provide compensation to third parties if a joint venture fails to perform a contractual obligation. Such guarantees meet the definition of insurance contracts and are accounted for under IFRS 4, *Insurance contracts*. Liabilities for non-financial guarantee are recognized when an outflow of resources embodying economic benefits required to settle the obligation is probable. The liabilities are recognized in the amount of best estimates of such an outflow.

Income taxes. The income tax charge or benefit comprises current tax and deferred tax and is recognized in the consolidated statement of income unless it relates to transactions that are recognized, in the same or a different period, in other comprehensive income or directly in equity.

Current tax is the amount expected to be paid to or recovered from the tax authorities in respect of taxable profits or losses for the current and prior periods. Russian tax legislation contains an option to prepare and file a single, consolidated income tax declaration by the taxpayers' group comprised of a holding company and any number of entities with at least 90 percent ownership in each (direct or indirect). Eligible taxpayers' group must be registered with tax authorities and meet certain conditions and criteria. The tax declaration can be submitted then by any member of the group. The Group's management has chosen to adopt this option.

Deferred tax assets and liabilities are recognized in full for the estimated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax base. In accordance with the initial recognition exemption, deferred taxes are not recorded for temporary differences on initial recognition of an asset or a liability in a transaction other than a business combination if the transaction, when initially recorded, affects neither accounting nor taxable profit. Deferred tax balances are measured at tax rates enacted or substantively enacted at the balance sheet date which are expected to apply to the period when the temporary differences will reverse or when the tax loss carry forwards will be utilized. Deferred tax assets for deductible temporary differences and tax loss carry forwards are recorded only to the extent that it is probable that future taxable profit will be available against which the deductions can be utilized.

Deferred income tax 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 income taxes balances relate to the same taxation authority and the same taxable entity, consolidated tax group of entities or different taxable entities where there is an intention to settle the balances on a net basis. Deferred tax assets and liabilities are netted only with respect to individual companies of the Group (for companies outside the consolidated tax group of companies) and within the consolidated tax payers' group of companies.

The Group controls the reversal of temporary differences relating to taxes chargeable on dividends from subsidiaries or on gains upon their disposal. The Group does not recognize deferred tax liabilities on such temporary differences except to the extent that management expects the temporary differences to reverse in the foreseeable future.

Treasury shares. Where any Group company purchases PAO NOVATEK's equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to PAO NOVATEK shareholders until the shares are cancelled or reissued or disposed. Where such shares are subsequently reissued or disposed, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to PAO NOVATEK shareholders. Treasury shares are recorded at weighted average cost. Gains or losses resulting from subsequent sales of shares are recorded in the consolidated statement of changes in equity, net of associated costs including taxation.

Dividends. Dividends are recognized as a liability and deducted from shareholders' equity at the balance sheet date only if they are declared before or on the balance sheet date. Dividends are disclosed when they are proposed or declared after the balance sheet date but before the consolidated financial statements are authorized for issue.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Revenue recognition. Revenues represent the fair value of consideration received or receivable for the sale of goods and services in the normal course of business, net of discounts, export duties, value-added tax, excise and fuel taxes.

Revenues from oil and gas sales are recognized when such products are shipped or delivered to customers in accordance with the contract terms, the price is fixed or determinable, and the title has transferred. Revenues from services are recognized in the period in which the services are rendered.

Interest income is recognized as the interest accrues based on the net carrying amount of the financial asset using the effective interest method and presented within finance income in the consolidated statement of income.

General and administrative expenses. General and administrative expenses represent overall corporate management and other expenses related to the general management and administration of the business unit as a whole. They include management and administrative compensation, legal and other advisory expenses, insurance of administrative buildings, social expenses and compensatory payments of general nature not directly linked to the Group's oil and gas activities, charity and other expenses necessary for the administration of the Group.

Earnings per share. Earnings per share are determined by dividing the profit or loss attributable to PAO NOVATEK shareholders by the weighted average number of shares outstanding during the reporting period.

Consolidated statement of cash flows. Cash and cash equivalents comprises cash on hand, cash deposits held with banks and short-term highly liquid investments which are readily convertible to known amounts of cash and which are not subject to significant risk of change in value and have an original maturity of three months or less.

For the purposes of presentation of the consolidated statement of cash flows bank overdrafts are deducted from cash and cash equivalents. Bank overdrafts are shown within short-term debt in current liabilities in the consolidated statement of financial position.

The Group reports cash receipts and the repayments of short-term borrowings which have a maturity of three months or less on a net basis in the consolidated statement of cash flows.

Segment reporting. Operating segments are defined as components of the Group where separate financial information is available and reported regularly to the Group's chief operating decision maker (hereinafter referred to as "CODM", represented by the Management Committee of PAO NOVATEK). Segments whose revenues, results or assets are ten percent or more of the total segments are reported separately.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

Consolidated financial statements prepared in accordance with IFRS require management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period.

Management reviews these estimates and assumptions on a continuous basis, by reference to past experience and other factors considered as reasonable which form the basis for assessing the book values of assets and liabilities. Adjustments to accounting estimates and assumptions are recognized in the period in which the estimate is revised if the change affects only that period or in the period of the revision and subsequent periods, if both are affected. Management also makes certain judgments, apart from those involving estimations, in the process of applying the Group's accounting policies. Actual results may differ from such estimates if different assumptions or circumstances apply.

Judgments and estimates that have the most significant effect on the amounts reported in these consolidated financial statements and have a significant risk of causing a material adjustment to the carrying amount of assets and liabilities within the next financial year are described below.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS (CONTINUED)

Fair values of financial assets and liabilities. The fair value of financial assets and liabilities, other than financial instruments that are traded in active markets, is determined by applying various valuation methodologies. Management uses its judgment to make assumptions primarily based on market conditions existing at each reporting date.

Discounted cash flow analysis is used for loans and receivables as well as debt instruments that are not traded in active markets. The effective interest rate is determined by reference to the interest rates of financial instruments available to the Group in active markets. In the absence of such instruments, the effective interest rate is determined by reference to the interest rates of active market financial instruments available adjusted for the Group's specific risk premium estimated by management.

For commodity derivative contracts where observable information is not available, fair value estimations are determined using mark-to-market analysis and other acceptable valuation methods, for which the key inputs include future prices, volatility, price correlation, counterparty credit risk and market liquidity. Fair values of the Group's commodity derivative contracts and sensitivities are presented in Note 27.

Fair value estimation of shareholders' loans to joint ventures is determined using benchmark interest rates adjusted for the borrower credit risk and free cash flows from the borrower's strategic plans approved by the shareholders of the joint ventures. Fair values of the shareholders' loans to joint ventures and sensitivities are presented in Note 27.

Deferred income tax asset recognition. Management assesses deferred income tax assets at each reporting date and determines the amount recorded to the extent that realization of the related tax benefit is probable. In determining future taxable profits and the amount of tax benefits that are probable in the future management makes judgments and applies estimations based on prior years taxable profits and expectations of future income that are believed to be reasonable under the circumstances.

Estimation of oil and gas reserves. Oil and gas reserves have a direct impact on certain amounts reported in the consolidated financial statements, most notably depreciation, depletion and amortization, as well as impairment expenses and asset retirement obligations. Depreciation rates on oil and gas assets using the unit-of-production method are based on proved developed reserves and total proved reserves estimated by the Group in accordance with rules promulgated by the Securities and Exchange Commission (SEC) for proved reserves. Assuming all variables are held constant, an increase in proved developed reserves for each field decreases depreciation, depletion and amortization expenses. Conversely, a decrease in the estimated proved developed reserves increases depreciation, depletion and amortization expenses. Estimated proved, probable and possible reserves are also used to calculate future cash flows from oil and gas properties, which serve as an indicator in determining their economic lives and whether or not property impairment is present.

Proved reserves are defined as the estimated quantities of oil and gas which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic conditions. Proved reserves are estimated by reference to available reservoir and well information, including production and pressure trends for producing reservoirs. Furthermore, estimates of proved reserves only include volumes for which access to market is assured with reasonable certainty. In some cases, substantial new investment in additional wells and related support facilities and equipment will be required to recover such proved reserves. Due to the inherent uncertainties and the limited nature of reservoir data, estimates of underground reserves are subject to change over time as additional information becomes available, such as from development drilling and production activities or from changes in economic factors, including product prices, contract terms or development plans.

In general, estimates of reserves for undeveloped or partially developed fields are subject to greater uncertainty over their future life than estimates of reserves for fields that are substantially developed and depleted. As those fields are further developed, new information may lead to further revisions in reserve estimates.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS (CONTINUED)

Although the possibility exists for changes or revisions in estimated reserves to have a critical effect on depreciation, depletion and amortization expenses and, therefore, reported profit for the year, it is expected that in the normal course of business the diversity of the Group's asset portfolio will mitigate the likelihood of this occurring.

Impairment of investments in joint ventures and property, plant and equipment. Management assesses whether there are any indicators of possible impairment of investments in joint ventures and property, plant and equipment at each reporting date based on events or circumstances that indicate that the carrying value of assets may not be recoverable. Such indicators include changes in the Group's business plans, changes in commodity prices leading to unprofitable performances, changes in product mixes, and for oil and gas properties, significant downward revisions of estimated proved reserves.

When value in use calculations are undertaken, management estimates the expected future cash flows from the asset or cash generating unit and chooses a suitable discount rate in order to calculate the present value of those cash flows.

Information about the carrying amounts of property, plant and equipment and long-term investments is presented in Notes 6 and 7.

Impairment provision for trade receivables. The impairment provision for trade receivables is based on management's assessment of the probability of collection of individual customer accounts receivable. Significant financial difficulties of the customer, probability that the customer will enter bankruptcy or financial reorganization, and default or delinquency in payments are considered indicators to determine that the receivables are potentially impaired. Actual results could differ from these estimates if there is deterioration in a major customer's creditworthiness or actual defaults are higher than the estimates.

When there is no expectation of recovering additional cash for an amount receivable, it is written off against the associated provision.

Future cash flows of trade receivables that are evaluated for impairment are estimated on the basis of the contractual cash flows of the assets and the experience of management in respect of the extent to which amounts will become overdue as a result of past loss events and the success of recovery of overdue amounts. Past experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect past periods and to remove the effects of past conditions that do not exist currently.

Pension obligations. The costs of defined benefit pension plans and related current service costs are determined using actuarial valuations. The actuarial valuations involve making demographic assumptions (mortality rates, age of retirement, employee turnover and disability) as well as financial assumptions (discount rates, expected rates of return on assets, future salary and pension increases). Due to the long-term nature of these plans, such estimates are subject to significant uncertainty.

Asset retirement obligations. Management makes provision for the future costs of decommissioning oil and gas production facilities, pipelines and related support equipment based on the best estimates of future cost and economic lives of those assets. In accordance with the guidelines of IFRIC 1, *Changes in Existing Decommissioning, Restoration and Similar Liabilities*, the amount recognized as a provision is the best estimate of the expenditures required to settle the present obligation at the reporting date based on current legislation where the Group's respective operating assets are located, and is also subject to change because of modifications, revisions and changes in laws and regulations and their interpretation thereof. Estimating future asset retirement obligations is complex and requires management to make estimates and judgments with respect to removal obligations that will occur many years in the future.

Changes in the measurement of existing obligations can result from changes in estimated timing, future costs or discount rates used in valuation.

5 ACQUISITIONS AND DISPOSALS

Acquisition of Blue Gaz Sp. z o.o.

In December 2016, in order to expand activities on Polish market, the Group acquired a 100 percent participation interest in Blue Gaz Sp. z o.o., a company owning of a regasification station in Poland, for total cash consideration of RR 26 million (PLN 2 million), which was paid by the end of 2016. The financial and operational activities of Blue Gaz Sp. z o.o. would not have had a material impact on the Group's revenues and results for the year ended 31 December 2016 if the acquisition had occurred in January 2016.

Acquisition of OOO Evrotek-Yuh

In April 2016, the Group acquired a 100 percent participation interest equity stake in OOO Evrotek-Yuh for RR 6 million. Evrotek-Yuh is a holder of the license for exploration and production of hydrocarbons within Ladertoyskiy license area located on the Gydan peninsula in YNAO. Evrotek-Yuh had no notable operating activities up to and as at the acquisition date and accordingly, this acquisition is outside the definition of "business" as defined in IFRS 3, *Business Combinations*. The acquisition cost has been fully allocated to the cost of the license.

Disposal of an ownership interest in OAO Yamal LNG

In December 2015, the Group and China's investment fund Silk Road Fund Co. Ltd., signed the Share Purchase Agreement on the disposal of a 9.9 percent equity stake in Yamal LNG, the Group's joint venture, to the fund. The transaction contained a set of conditions precedent and, in accordance with IFRS 5, *Non-current assets held for sale and discontinued operations*, the Group's 9.9 percent share in Yamal LNG has been classified as an asset held for sale at 31 December 2015. The asset's carrying amount of RR 7,987 million was determined based on the net assets of Yamal LNG on the date of the agreement.

In March 2016, the transaction was closed upon the completion of the conditions precedent, and the Group recognized the disposal of the 9.9 percent stake in Yamal LNG. The transaction included a cash payment and the provision of a 15-year tenor loan to the Group for the purpose of financing the Yamal LNG project (see Note 14). Concurrently, the Group has committed to provide cash contributions to the capital of Yamal LNG with regard to the interest disposed on the same terms that were previously applied upon the entrance of TOTAL S.A. and China National Petroleum Corporation into the project.

The following table summarizes the consideration details and shows the gain on the sale of the ownership interest in Yamal LNG:

	RR million
Cash payment received (EUR 1,087 million at exchange rate of 78.18 to EUR 1.00)	84,978
Adjustment to fair value at initial recognition of the loan from Silk Road Fund, previously recorded as deferred income (see Note 14)	9,173
Less: 49.9 percent share in the Group's liability in relation to capital contributions to Yamal LNG ^(*) (USD 149 million at exchange rate of 70.15 to USD 1.00)	(10,458)
Less: carrying amount of the Group's disposed 9.9 percent interest in the equity investment previously classified as held for sale	(7,987)
Costs to sell	(2,634)
Gain on the sale of ownership interest before income tax	73,072

^(*) – excluding the Group's 50.1 percent share in Yamal LNG's capital increase as a result of these contributions.

Consequently, the Group recognized a gain on the transaction of RR 57,677 million, net of associated income tax of RR 15,395 million.

As a result of this transaction, the Group's interest in Yamal LNG is 50.1 percent. The Group continues to exercise joint control over Yamal LNG and recognizes it as a joint venture, and, accordingly, accounts for this investment under the equity method.

PAO NOVATEK**Notes to the Consolidated Financial Statements**

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

5 ACQUISITIONS AND DISPOSALS (CONTINUED)***Disposal of ownership interest in Artic Russia B.V.***

In 2014, NOVATEK and PAO Gazprom Neft agreed in principle to conduct a series of transactions to achieve parity shareholdings in OOO SeverEnergiya. As part of such agreement, in August 2015, NOVATEK contributed its 6.4 percent ownership interest in Artic Russia to the capital of OOO Yamal Development. Simultaneously, the Group and Gazprom Neft made contributions to the capital of Yamal Development by converting their loans and accrued interest in the amount of RR 2,512 million and RR 14,922 million, respectively. As a result of these transactions, the Group's effective participation interest in SeverEnergiya decreased from 54.9 percent to 53.3 percent.

The gain on the disposal of the 6.4 percent ownership interest in Artic Russia is detailed below:

	RR million
The Group's share in the fair value of contributions to the capital of Yamal Development	14,922
Less: carrying amount of 6.4 percent ownership interest in Artic Russia contributed by the Group	(10,432)
Less: carrying amount of loan and accrued interest converted by the Group	(2,512)
Less: the Group's unrealized gain on the disposal	(989)
Gain on the disposal recognized	
in the consolidated statement of income before income tax	989

As a result of the aforementioned transactions, in August 2015, NOVATEK recognized a gain in the amount of RR 1,978 million. Due to the fact that NOVATEK contributed the equity stake in Artic Russia to the capital of Yamal Development, the Group's joint venture, in which it holds a 50 percent participation interest, the Group eliminated an unrealized gain on the disposal on the consolidation level in the amount of RR 989 million.

The Group's management expects that further steps to achieve parity shareholdings in SeverEnergiya will be undertaken in the foreseeable future.

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6 PROPERTY, PLANT AND EQUIPMENT

Movements in property, plant and equipment, for the reporting periods are as follows:

	Oil and gas properties and equipment	Assets under construction and advances for construction	Other	Total
Cost	291,212	63,162	14,422	368,796
Accumulated depreciation, depletion and amortization	(74,962)	-	(2,108)	(77,070)
Net book value at 31 December 2014	216,250	63,162	12,314	291,726
Additions	1,558	55,695	306	57,559
Transfers	53,366	(53,882)	516	-
Changes in asset retirement costs	2,410	-	-	2,410
Depreciation, depletion and amortization	(19,009)	-	(552)	(19,561)
Disposals, net	(193)	(197)	(32)	(422)
Cost	348,268	64,778	15,195	428,241
Accumulated depreciation, depletion and amortization	(93,886)	-	(2,643)	(96,529)
Net book value at 31 December 2015	254,382	64,778	12,552	331,712
Additions	3,099	29,191	26	32,316
Transfers	58,674	(59,001)	327	-
Acquisition of subsidiaries	53	-	-	53
Changes in asset retirement costs	2,990	-	-	2,990
Depreciation, depletion and amortization	(33,836)	-	(522)	(34,358)
Disposals, net	(645)	(192)	(81)	(918)
Cost	412,352	34,776	15,402	462,530
Accumulated depreciation, depletion and amortization	(127,635)	-	(3,100)	(130,735)
Net book value at 31 December 2016	284,717	34,776	12,302	331,795

Included in additions to property, plant and equipment for the years ended 31 December 2016 and 2015 are capitalized interest and foreign exchange differences of RR 5,314 million and RR 8,515 million, respectively.

Included within assets under construction and advances for construction are advances to suppliers for construction and equipment of RR 1,438 million and RR 2,719 million at 31 December 2016 and 2015, respectively.

In 2016, the Group purchased through auctions oil and gas exploration and production licenses for the Nyakhartinsky and Syadorsky license areas located in the YNAO and Tanamskiy license area located in Krasnoyarsk Territory for the total amount of RR 1,928 million, which were included in additions to oil and gas properties and equipment.

During 2016, the major transfers to oil and gas properties and equipment related to the Yarudeyskoye and East-Tarkosalinskoye fields in the amount of RR 21,631 million and RR 11,524 million, respectively.

During 2015, the major transfers to oil and gas properties and equipment in the amount of RR 26,408 million related to the launch of commercial production at the Yarudeyskoye oil field.

PAO NOVATEK**Notes to the Consolidated Financial Statements**

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6 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

The table below summarizes the Group's carrying values of total acquisition costs of proved and unproved properties included in oil and gas properties and equipment:

	At 31 December 2016	At 31 December 2015
Proved properties acquisition costs	47,243	46,343
Less: accumulated depreciation, depletion and amortization of proved properties acquisition costs	(16,782)	(15,540)
Unproved properties acquisition costs	10,069	7,874
Total acquisition costs	40,530	38,677

The Group's management believes these costs are recoverable as the Group has plans to explore and develop the respective fields.

Reconciliation of depreciation, depletion and amortization (DDA):

	Year ended 31 December:	
	2016	2015
Depreciation, depletion and amortization of property, plant and equipment	34,358	19,561
Add: DDA of intangible assets	554	566
Less: DDA capitalized in the course of intra-group construction services	(281)	(147)
DDA as presented in the consolidated statement of income	34,631	19,980

At 31 December 2016 and 2015, no property, plant and equipment were pledged as security for the Group's borrowings. No impairment was recognized in respect of oil and gas properties and equipment for the years ended 31 December 2016 and 2015.

Capital commitments are disclosed in Note 28.

Exploration for and evaluation of mineral resources. The amounts of assets, liabilities, expense and cash flows arising from the exploration and evaluation of mineral resources comprise the following:

	Year ended 31 December:	
	2016	2015
Net book value of assets value at 1 January	14,744	12,726
Additions	5,297	5,141
Expensed	(3)	(21)
Acquisition of subsidiaries	7	-
Reclassification to proved properties and development expenditures	(4,573)	(3,102)
Net book value of assets at 31 December	15,472	14,744
Liabilities	384	330
Cash flows used for operating activities	1,891	1,020
Cash flows used for investing activities	4,085	2,769

For the years ended 31 December 2016 and 2015, within operating expenses the Group has recognized exploration expenses in the amount of RR 2,087 million and RR 1,109 million, respectively. These expenses included employee compensations in the amount of RR 300 million and RR 263 million, respectively.

PAO NOVATEK**Notes to the Consolidated Financial Statements**

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7 INVESTMENTS IN JOINT VENTURES

	At 31 December 2016	At 31 December 2015
<i>Joint ventures:</i>		
OAO Yamal LNG	126,688	38,798
OOO Yamal Development	55,228	43,551
ZAO Nortgas	51,222	50,298
Artic Russia B.V.	24,449	22,078
ZAO Terneftegas	2,063	-
Total investments in joint ventures	259,650	154,725

The Group considers that Yamal LNG, Yamal Development, Nortgas, Artic Russia and Terneftegas constitute jointly controlled entities on the basis of the existing contractual arrangements. The Charters and Shareholders' agreements of these entities stipulate that strategic and/or key decisions of a financial, operating and capital nature require effectively the unanimous approval by all shareholders or by a group of shareholders. The Group accounts for its shares in joint ventures under the equity method.

OAO Yamal LNG. The Group holds a 50.1 percent ownership in Yamal LNG, along with TOTAL S.A. (20 percent), China National Petroleum Corporation ("CNPC", 20 percent) and Silk Road Fund Co. Ltd. (9.9 percent). At 31 December 2015, the Group held a 60 percent ownership in the joint venture, including a 9.9 percent share classified as an asset held for sale, which was sold to Silk Road Fund Co. Ltd. in March 2016 (see Note 5). The joint venture is responsible for implementing the Yamal LNG project including the construction of production facilities for natural gas, gas condensate and liquefied natural gas ("LNG") based on the resources of the South-Tambeyskoye field, located on the Yamal peninsula in the YNAO. Yamal LNG is the holder of the LNG export license.

In 2016, Yamal LNG has signed agreements with a number of Russian and foreign banks to raise project financing in the form of credit lines for the total amount of EUR 13.9 billion and CNY 7.6 billion with a repayment period from December 2019 to June 2031. At 31 December 2016, the Group's 50.1 percent ownership in Yamal LNG was pledged in connection with these facility agreements.

ZAO Nortgas. The Group holds a 50 percent ownership in Nortgas, its joint venture with PAO Gazprom Neft. Nortgas operates the North-Urengoykoye field, located in the YNAO.

Artic Russia B.V. The Group holds a direct 13.6 percent participation interest in Artic Russia, domiciled in the Netherlands. Artic Russia holds a 49 percent participation interest in OOO SeverEnergiya.

OOO Yamal Development. The Group holds a 50 percent participation interest in Yamal Development, its joint venture with PAO Gazprom Neft (50 percent). Yamal Development holds a 51 percent participation interest in SeverEnergiya and an 86.4 percent ownership interest in Artic Russia.

OOO SeverEnergiya. The Group holds an effective 53.3 percent participation interest in SeverEnergiya through two of the Group's other joint ventures, Yamal Development and Artic Russia. SeverEnergiya through its wholly owned subsidiary OAO Arcticgas operates the Samburgskoye, Urengoykoye and Yaro-Yakhinskoye fields, located in the YNAO.

ZAO Terneftegas. The Group holds a 51 percent ownership in Terneftegas, its joint venture with TOTAL S.A. (49 percent). Terneftegas operates the Termokarstovoye field, located in the YNAO.

The Group's investment in Terneftegas at 31 December 2015 was valued at RR nil in the consolidated statement of financial position due to the Group's proportionate share of accumulated losses exceeding the Group's cost of investment. The unrecognized share of accumulated losses of Terneftegas at 31 December 2015 was RR 1,409 million. During 2016, the Group's proportionate share of profit of Terneftegas exceeded the Group's share of previously unrecognized accumulated losses, thereafter the Group resumed recognizing its share of profits of Terneftegas.

PAO NOVATEK**Notes to the Consolidated Financial Statements**

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

7 INVESTMENTS IN JOINT VENTURES (CONTINUED)

The table below summarizes the movements in the carrying amounts of the Group's joint ventures:

	Year ended 31 December:	
	2016	2015
At 1 January	154,725	166,231
Share of profit from operations	33,655	32,052
Share of finance income (expense)	74,236	(68,821)
Share of total income tax benefit (expense)	(17,052)	5,162
Share of profit (loss) of joint ventures, net of income tax	90,839	(31,607)
Share of other comprehensive loss of joint ventures	(21)	-
Effect from initial measurement of loans provided by the Group to joint ventures (see Note 27)	836	14,185
Contributions to equity	9,802	14,922
Disposal of stakes in joint ventures	-	(11,421)
Effect from other changes in joint ventures' net assets	2,819	9,285
Group's costs capitalized in investments	753	-
Elimination of the Group's share in profits of joint ventures from hydrocarbons balances purchased by the Group from joint ventures and not sold at the reporting date	(103)	1,117
Reclassification to assets held for sale	-	(7,987)
At 31 December	259,650	154,725

In September 2016, the capital of Yamal LNG was increased through a cash contribution made by the Group as a result of the disposal of the 9.9 percent stake in Yamal LNG (see Note 5) in the amount of RR 19,565 million. The Group's 50.1 percent share in Yamal LNG's capital increase was recorded in the Group's investment in Yamal LNG in the amount of RR 9,802 million. The Group's shareholding in Yamal LNG did not change notably as a result of this capital contribution.

In August 2015, the Group disposed of its 6.4 percent ownership interest in Artic Russia at cost of RR 11,421 million, including an unrealized gain on disposal. Simultaneously, the equity of Yamal Development was increased through proportional contributions by its participants totalling RR 29,844 million, of which RR 14,922 million was contributed by NOVATEK (see Note 5).

For the years ended 31 December 2016 and 2015, the Group recorded an increase in equity in the amount of RR 2,819 million and RR 3,329 million, respectively, from the initial measurement of the disproportional loans provided to Yamal LNG by other shareholders.

In December 2015, the capital of Yamal LNG was increased by RR 21,256 million through the conversions of loans obtained by the joint venture from TOTAL S.A. and CNPC. These capital contributions were made by TOTAL S.A. and CNPC as a settlement of the third tranche (USD 143 million each) representing a part of the consideration for the acquisition of the 20 percent interests in Yamal LNG by each of the companies in 2011 and 2013, respectively. The Group's share (50.1 percent ownership excluding the share classified as held for sale) in the increase of the capital of Yamal LNG amounted to RR 10,649 million. The excess of the Group's share in the contributions over the amount of the third tranche previously recognized within the investment in Yamal LNG amounted to RR 5,956 million and was recorded as an increase in the investment in Yamal LNG, with the corresponding effect recognized in the consolidated statement of changes in equity in accordance with the Group's accounting policy. The Group's shareholding in Yamal LNG did not change notably as a result of this transaction.

For the year ended 31 December 2016, the Group recorded commission fees in the amount of 753 million for the guarantee received from the State corporation "Bank for Development and Foreign Economic Affairs (Vnesheconombank)" (see Note 28) as an increase to the investment in Yamal LNG.

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7 INVESTMENTS IN JOINT VENTURES (CONTINUED)

The Group eliminates its share in profits of joint ventures from natural gas and liquid hydrocarbons balances purchased by the Group from its joint ventures and not sold at the reporting date.

The summarized statements of financial position for the Group's principal joint ventures are as follows:

<i>At 31 December 2016</i>	Yamal LNG	SeverEnergia	Nortgas
Property, plant and equipment and materials for construction	1,265,939	385,404	138,768
Other non-current non-financial assets	273	278	47
Non-current financial assets	6,061	120,655	11,213
Total non-current assets	1,272,273	506,337	150,028
Cash and cash equivalents	12,842	13,517	277
Other current financial assets	23,211	15,520	2,639
Current non-financial assets	14,314	1,013	631
Total current assets	50,367	30,050	3,547
Non-current financial liabilities	(1,016,196)	(130,872)	(24,795)
Non-current non-financial liabilities	(35,798)	(57,555)	(23,544)
Total non-current liabilities	(1,051,994)	(188,427)	(48,339)
Trade payables and accrued liabilities	(17,628)	(14,308)	(1,302)
Other current financial liabilities	-	(29,355)	-
Current non-financial liabilities	(148)	(11,669)	(1,490)
Total current liabilities	(17,776)	(55,332)	(2,792)
Net assets	252,870	292,628	102,444
<i>At 31 December 2015</i>			
Property, plant and equipment and materials for construction	752,387	396,185	141,615
Other non-current non-financial assets	1	351	30
Non-current financial assets	135	96,221	10,204
Total non-current assets	752,523	492,757	151,849
Cash and cash equivalents	64,813	13,801	2,160
Other current financial assets	6,390	12,592	2,674
Current non-financial assets	22,811	1,849	468
Total current assets	94,014	28,242	5,302
Non-current financial liabilities	(753,099)	(161,051)	(24,841)
Non-current non-financial liabilities	(3,488)	(54,853)	(23,540)
Total non-current liabilities	(756,587)	(215,904)	(48,381)
Trade payables and accrued liabilities	(11,994)	(14,234)	(241)
Other current financial liabilities	-	(28,976)	(5,908)
Current non-financial liabilities	(514)	(9,110)	(2,025)
Total current liabilities	(12,508)	(52,320)	(8,174)
Net assets	77,442	252,775	100,596

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7 INVESTMENTS IN JOINT VENTURES (CONTINUED)

The summarized statements of comprehensive income of the Group's principal joint ventures are presented below:

<i>For the year ended 31 December 2016</i>	Yamal LNG	SeverEnergia	Nortgas
Revenue	2,722	133,229	25,697
Depreciation, depletion and amortization	(650)	(26,451)	(7,749)
Profit from operations	670	55,585	4,368
Change in fair value of non-commodity financial instruments	(25,223)	-	-
Foreign exchange gain (loss), net	200,485	25	-
Profit before income tax	176,043	47,806	2,436
Income tax expense	(28,952)	(7,930)	(574)
Profit, net of income tax	147,091	39,876	1,862
Other comprehensive loss	(27)	(23)	(14)
Total comprehensive income	147,064	39,853	1,848
<i>For the year ended 31 December 2015</i>			
Revenue	2,606	126,129	28,893
Depreciation, depletion and amortization	(814)	(28,944)	(8,205)
Profit (loss) from operations	(1,829)	53,858	9,287
Change in fair value of non-commodity financial instruments	19,036	-	-
Foreign exchange gain (loss), net	(102,084)	(15)	-
Profit (loss) before income tax	(84,962)	47,049	5,793
Income tax benefit (expense)	13,655	(8,697)	(1,192)
Total comprehensive income (loss)	(71,307)	38,352	4,601

The information above reflects the amounts presented in the financial statements of the joint ventures adjusted for differences in accounting policies between the Group and the joint ventures.

PAO NOVATEK**Notes to the Consolidated Financial Statements**

(in Russian roubles [tabular amounts in millions], unless otherwise stated)

7 INVESTMENTS IN JOINT VENTURES (CONTINUED)

Reconciliation of the summarized financial information presented to the Group's share in net assets of the joint ventures:

<i>As at and for the year ended 31 December 2016</i>	Yamal LNG	SeverEnergia	Nortgas
Net assets at 1 January 2016	77,442	252,775	100,596
Profit (loss), net of income tax	147,091	39,876	1,862
Other comprehensive loss	(27)	(23)	(14)
Other equity movements	28,364	-	-
Net assets at 31 December 2016	252,870	292,628	102,444
Ownership	50.1%	53.3%	50%
Group's share in net assets	126,688	156,059	51,222
<i>As at and for the year ended 31 December 2015</i>			
Net assets at 1 January 2015	96,936	216,534	95,995
Profit (loss), net of income tax	(71,307)	38,352	4,601
Other equity movements	51,813	-	-
Disposal of stakes in joint ventures	-	(2,111)	-
Net assets at 31 December 2015	77,442	252,775	100,596
Ownership excluding interests classified as held for sale	50.1%	53.3%	50%
Group's share in net assets	38,798	134,729	50,298

At 31 December 2016 and 2015, the Group's cumulative investments in Artic Russia and Yamal Development totaled RR 79,677 million and RR 65,629 million, respectively, which differed from the Group's share in the net assets of SeverEnergia. The differences of RR 76,382 million and RR 69,100 million mainly relate to the Group's interest in debt liabilities of Yamal Development and goodwill relating to acquisition of Arctic Russia, through which entities the Group holds the investments in SeverEnergia.

8 LONG-TERM LOANS AND RECEIVABLES

	At 31 December 2016	At 31 December 2015
Long-term loans	184,621	214,051
Long-term interest receivable	24,390	16,190
Other long-term receivables	442	558
Total	209,453	230,799
Less: current portion of long-term loans	(308)	-
Total long-term loans and receivables	209,145	230,799

8 LONG-TERM LOANS AND RECEIVABLES (CONTINUED)

The Group's long-term loans by borrowers are as follows:

	At 31 December 2016	At 31 December 2015
OAQ Yamal LNG	173,845	196,533
OOO Yamal Development	7,575	13,105
ZAO Terneftegas	3,201	4,413
Total long-term loans	184,621	214,051

OAQ Yamal LNG. In accordance with the Shareholders' agreement, the Group provided US dollar and Euro credit line facilities to Yamal LNG, the Group's joint venture. Under the terms of these credit line facilities, the Group provided loans to Yamal LNG prior to obtaining external project financing. During 2016 and 2015, the Group provided RR 6,645 million and RR 104,076 million, respectively, under these credit line facilities.

The loans interest rate in 2016 and 2015 was ranging from 4.29 to 4.46 percent per annum. The interest rate can be adjusted during subsequent periods subject to certain conditions. The repayment schedule is linked to free cash flows of the joint venture.

OOO Yamal Development. The Group provided Russian rouble denominated loans under agreed credit line facilities to Yamal Development, the Group's joint venture. The loans are repayable not later than 2021 and bear interest rates ranging from 9.25 to 10.90 percent per annum.

During 2015, the Group provided RR 4,494 million under these credit line facilities. In August 2015, the Group made a contribution to the capital of Yamal Development by converting a part of the loans in the amount of RR 2,200 million (see Note 5), and in December 2015, Yamal Development repaid a part of the loans to the Group in the amount of RR 2,550 million ahead of the maturity schedule.

During 2016, Yamal Development repaid to the Group a part of the loans in the total amount of RR 5,530 million ahead of the maturity schedule.

ZAO Terneftegas. In accordance with the Shareholders' agreement, the Group provided US dollar denominated loans to Terneftegas, the Group's joint venture.

For the year ended 31 December 2016, Terneftegas repaid to the Group a part of the loans and accrued interest in the total amount of RR 1,298 million. For the year ended 31 December 2015, Terneftegas repaid to the Group a part of the loans in the amount of RR 1,160 million.

The loans interest rate in 2016 and 2015 was ranging from 4.47 to 4.60 percent per annum. The interest rate can be adjusted during subsequent periods subject to certain conditions. The repayment schedule is linked to free cash flows of the joint venture.

No provisions for impairment of long-term loans and receivables were recognized at 31 December 2016 and 2015. The carrying values of long-term loans and receivables approximate their respective fair values.

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9 OTHER NON-CURRENT ASSETS

	At 31 December 2016	At 31 December 2015
<i>Financial assets</i>		
Commodity derivatives	1,172	1,511
Other financial assets	157	10
<i>Non-financial assets</i>		
Long-term advances	20,882	17,551
Deferred income tax assets	4,671	11,183
Materials for construction	2,004	2,407
Intangible assets, net	1,510	1,567
Other non-financial assets	88	87
Total other non-current assets	30,484	34,316

At 31 December 2016 and 2015, the long-term advances represented advances to OAO Russian Railways. The advances were paid in accordance with the Strategic Partnership Agreement signed with Russian Railways in 2012.

10 INVENTORIES

	At 31 December 2016	At 31 December 2015
Natural gas and liquid hydrocarbons	6,765	6,462
Materials and supplies (net of provision of RR 4 million at 31 December 2016 and 2015)	2,247	1,745
Other inventories	32	19
Total inventories	9,044	8,226

No inventories were pledged as security for the Group's borrowings or payables at both dates.

11 TRADE AND OTHER RECEIVABLES

	At 31 December 2016	At 31 December 2015
Trade receivables (net of provision of RR 196 million and RR 95 million at 31 December 2016 and 2015, respectively)	40,606	35,221
Other receivables (net of provision of RR 22 million and RR 18 million at 31 December 2016 and 2015, respectively)	980	2,343
Total trade and other receivables	41,586	37,564

Trade receivables in the amount of RR 5,362 million at 31 December 2016 are secured by letters of credit, issued by banks with investment grade rating. The Group does not hold any other collateral as security for trade and other receivables (see Note 27 for credit risk disclosures).

The carrying values of trade and other receivables approximate their respective fair values. Trade and other receivables were categorized as Level 3 in the fair value measurement hierarchy described in Note 27.

Trade and other receivables that are less than three months past due are generally not considered for impairment unless other indicators of impairment exist. Trade and other receivables of RR 4,269 million and RR 4,998 million at 31 December 2016 and 2015, respectively, were past due but not impaired. The Group has assessed the payment history of these accounts and recognized impairment where deemed necessary.

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11 TRADE AND OTHER RECEIVABLES (CONTINUED)

The ageing analysis of these past due but not impaired trade and other receivables is as follows:

	At 31 December 2016	At 31 December 2015
Up to 90 days past-due	3,628	3,624
91 to 360 days past-due	561	1,225
Over 360 days past-due	80	149
Total past due but not impaired	4,269	4,998
Not past due and not impaired	37,317	32,566
Total trade and other receivables	41,586	37,564

Movements in the Group provision for impairment of trade and other receivables are as follows:

	Year ended 31 December:	
	2016	2015
At 1 January	113	317
Additional provision recorded	269	79
Receivables written off as uncollectible	(68)	(58)
Provision reversed	(96)	(225)
At 31 December	218	113

The provision for impaired trade and other receivables has been included in the consolidated statement of income in impairment reversals (expenses), net.

12 PREPAYMENTS AND OTHER CURRENT ASSETS

	At 31 December 2016	At 31 December 2015
Financial assets		
Commodity derivatives	2,920	5,039
Current portion of long-term loans receivable (see Note 8)	308	-
Cash on special accounts	-	6,477
Non-financial assets		
Value-added tax receivable	10,456	13,437
Prepayments and advances to suppliers	5,998	5,304
Recoverable value-added tax	5,736	7,554
Deferred transportation expenses for liquid hydrocarbons	1,903	1,720
Deferred transportation expenses for natural gas	1,901	2,955
Prepaid customs duties	1,756	559
Deferred export duties for liquid hydrocarbons	1,643	2,251
Other non-financial assets	627	128
Total prepayments and other current assets	33,248	45,424

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13 CASH AND CASH EQUIVALENTS

	At 31 December 2016	At 31 December 2015
Cash at current bank accounts	31,525	11,243
Bank deposits with original maturity of three months or less	16,776	17,944
Total cash and cash equivalents	48,301	29,187

All deposits are readily convertible to known amounts of cash and are not subject to significant risk of change in value (see Note 27 for credit risk disclosures).

14 LONG-TERM DEBT

	At 31 December 2016	At 31 December 2015
Corporate bonds		
Eurobonds – Ten-Year Tenor (par value USD 1 billion, repayable in 2022)	60,503	72,662
Eurobonds – Ten-Year Tenor (par value USD 650 million, repayable in 2021)	39,318	47,207
Eurobonds – Four-Year Tenor (par value RR 14 billion, repayable in 2017)	13,996	13,977
Eurobonds – Five-Year Tenor (par value USD 600 million, repayable in 2016)	-	43,725
Bank loans		
Syndicated term credit line facility	41,906	83,861
Other bank loans	6,381	-
Other borrowings		
Loan from Silk Road Fund	41,125	48,619
Other loans	13,536	19,268
Total	216,765	329,319
Less: current portion of long-term debt	(55,469)	(77,269)
Total long-term debt	161,296	252,050

Eurobonds. In December 2012, the Group issued US dollar denominated Eurobonds in the amount of USD 1 billion. The US dollar denominated Eurobonds were issued with an annual coupon rate of 4.422 percent, payable semi-annually. The Eurobonds have a ten-year tenor and are repayable in December 2022.

In February 2011, the Group issued US dollar denominated Eurobonds in an aggregate amount of USD 1,250 million. The US dollar denominated Eurobonds were issued at par in two tranches, a ten-year USD 650 million Eurobond with an annual coupon rate of 6.604 percent and a five-year USD 600 million Eurobond with an annual coupon rate of 5.326 percent. The coupons are payable semi-annually. The ten-year USD 650 million Eurobond is repayable in February 2021. The five-year USD 600 million Eurobond was fully repaid at its maturity date in February 2016.

In February 2013, the Group issued four-year tenor Russian rouble denominated Eurobonds in the amount of RR 14 billion. The Russian rouble denominated Eurobonds were issued with an annual coupon rate of 7.75 percent, payable semi-annually. Subsequent to the balance sheet date, in February 2017, the four-year RR 14 billion Eurobond was fully repaid at its maturity date.

14 LONG-TERM DEBT (CONTINUED)

Syndicated term credit line facility. In June 2013, the Group obtained a USD 1.5 billion unsecured syndicated term credit line facility from a range of international banks and withdrew the full amount under the facility by June 2014. The loan is repayable until July 2018 by quarterly installments starting from June 2015. The facility includes the maintenance of certain restrictive financial covenants.

Other bank loans. In December 2016, the Group obtained a EUR 100 million loan from a Russian subsidiary of a foreign bank. The loan is repayable in December 2019. The facility includes the maintenance of certain restrictive financial covenants.

Loan from Silk Road Fund. As part of the transaction for the sale of the Group's 9.9 percent equity stake in OAO Yamal LNG, in December 2015, the Group obtained a loan from Silk Road Fund for financing of the Yamal LNG project (see Note 5).

In accordance with IAS 39, *Financial instruments: recognition and measurement*, the loan was recorded at fair value at initial recognition with the difference of RR 9,173 million between the fair value of the loan and cash received recognized as deferred income (see Note 17). In March 2016, the deferred income was included in the financial result on disposal of the 9.9 percent equity stake in Yamal LNG upon completion of the transaction (see Note 5).

The loan is repayable until December 2030 by semi-annual installments starting from December 2019 and includes the maintenance of certain restrictive financial covenants.

Other loans. At 31 December 2016 and 2015, other loans represented Russian rouble denominated loans, which were provided to one of the Group's subsidiaries by its non-controlling shareholder. The loans are repayable until the end of 2017. During the year ended 31 December 2016, a portion of the loans and accrued interest in the amount of RR 8,673 million was repaid ahead of maturity schedule.

The fair value of long-term debt including its current portion was RR 224,183 million and RR 319,191 million at 31 December 2016 and 2015, respectively. The fair value of the corporate bonds was determined based on market quote prices (Level 1 in the fair value measurement hierarchy described in Note 27). The fair value of other long-term loans was determined based on future cash flows discounted at the estimated risk-adjusted discount rate (Level 3 in the fair value measurement hierarchy described in Note 27).

Scheduled maturities of long-term debt at the reporting date were as follows:

<i>Maturity period:</i>	At 31 December 2016
1 January 2018 to 31 December 2018	13,968
1 January 2019 to 31 December 2019	8,169
1 January 2020 to 31 December 2020	3,576
1 January 2021 to 31 December 2021	42,894
After 31 December 2021	92,689
Total long-term debt	161,296

Available credit line facilities. At 31 December 2016, the Group had available long-term credit line facilities from Russian banks with credit limits in the amount of RR 50 billion and the equivalent of USD 750 million. The facilities include the maintenance of certain restrictive financial covenants.

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15 SHORT-TERM DEBT AND CURRENT PORTION OF LONG-TERM DEBT

	At 31 December 2016	At 31 December 2015
Loans with original maturity more than three months	-	21,300
Loans with original maturity three months or less	-	8,086
Total short-term debt	-	29,386
Add: current portion of long-term debt	55,469	77,269
Total short-term debt and current portion of long-term debt	55,469	106,655

Loans with original maturity more than three months. At 31 December 2015, short-term debt included a loan obtained by the Group under a non-revolving credit line facility from a Russian bank in the amount of RR 20 billion. In 2016, the loan was fully repaid.

At 31 December 2015, short-term debt also included loans obtained by one of the Group's subsidiaries from its non-controlling shareholder in the amount of RR 1,300 million. In 2016, these loans were fully repaid.

Loans with original maturity three months or less. In 2015 and 2016, the Group had available revolving credit line facilities under which obtained loans with original maturities three months or less to finance trade activities secured by cash revenues from specifically determined liquid hydrocarbons export sales contracts. At 31 December 2016, these loans were repaid.

Available credit line facilities. At 31 December 2016, the Group had available revolving credit line facilities from Russian banks, with total credit limits in the amount of RR 70 billion.

16 PENSION OBLIGATIONS

Defined contribution plan. For the years ended 31 December 2016 and 2015, total amounts recognized as an expense in respect of payments made by employer on behalf of employees to the Pension Fund of the Russian Federation were RR 1,853 million and RR 1,803 million, respectively.

Defined benefit plan. The Group operates a post-employment benefit program for its retired employees. Under the current terms of pension program, employees who are employed by the Group for more than five years and retire from the Group on or after the statutory retirement age will receive lump sum retirement benefit and monthly payments from NOVATEK for life unless they are actively employed. The amounts of payments to be disbursed depend on the employee's average salary, duration and location of employment.

The program represents an unfunded defined benefit plan and is accounted for as such under provisions of IAS 19, *Employee Benefits*. The present value of the defined benefit obligation is included in other non-current liabilities in the consolidated statement of financial position. The impact of the program on the consolidated financial statements is disclosed below.

16 PENSION OBLIGATIONS (CONTINUED)

The movements in the present value of the defined benefit obligation are as follows:

	Year ended 31 December:	
	2016	2015
At 1 January	1,905	1,167
Interest cost	201	152
Current service cost	126	83
Benefits paid	(105)	(88)
Pension plan revision	-	(51)
Actuarial remeasurement arising from:		
- changes in financial assumptions	110	595
- changes in demographic assumptions	(24)	37
- experience adjustment	36	10
At 31 December	2,249	1,905
<i>Defined benefit plan (benefits) costs were recognized in:</i>		
Materials, services and other (as employee compensation)	184	107
General and administrative expenses (as employee compensation)	143	128
Other comprehensive (income) loss	122	642

The principal actuarial assumptions used are as follows:

	At 31 December 2016	At 31 December 2015
Weighted average discount rate	8.3%	10.0%
Projected annual increase in employee compensation	5.0%	5.6%
Expected increases to pension benefits	6.5%	5.6%

The assumed average salary and pension payment increases for Group employees have been calculated on the basis of inflation forecasts, analysis of increases of past salaries and the general salary policy of the Group. Inflation forecasts have been estimated to reduce from 5.4 percent in 2017 to 4.3 percent in 2022 and subsequent years.

Mortality assumptions are based on the Russian mortality tables published by the State Statistics Committee of the Russian Federation from the year 2010 adjusted for estimates of mortality improvements in the future periods, which management believes are the most conservative and prudent Russian whole-population mortality tables available.

Management has assessed that reasonable changes in the principal significant actuarial assumptions will not have a significant impact on the consolidated statement of income or the consolidated statement of comprehensive income or the liability recognized in the consolidated statement of financial position.

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17 TRADE PAYABLES AND ACCRUED LIABILITIES

	At 31 December 2016	At 31 December 2015
Financial liabilities		
Trade payables	25,828	23,989
Commodity derivatives	2,754	2,355
Interest payable	1,821	3,100
Other payables	463	3,401
Non-financial liabilities		
Advances from customers	2,483	4,099
Salary payables	338	494
Deferred income	-	9,173
Other liabilities and accruals	4,775	1,924
Total trade payables and accrued liabilities	38,462	48,535

At 31 December 2015, other payables included outstanding liability related to the acquisition of AO Office in August 2014 which was paid during 2016 in the amount of RR 2,929 million (USD 39 million). During 2015, the Group paid RR 3,630 million (USD 62 million) under this transaction.

The carrying values of trade payables and accrued liabilities approximate their respective fair values. Trade and other payables were categorized as Level 3 in the fair value measurement hierarchy described in Note 27.

18 SHAREHOLDERS' EQUITY

Ordinary share capital. Share capital issued and paid in consisted of 3,036,306,000 ordinary shares with a par value of RR 0.1 each at 31 December 2016 and 2015. The total authorized number of ordinary shares was 10,593,682,000 shares at both dates.

Treasury shares. In accordance with the *Share Buyback Programs* authorized by the Board of Directors, the Group's wholly owned subsidiary, Novatek Equity (Cyprus) Limited, purchases ordinary shares of PAO NOVATEK in the form of Global Depositary Receipts (GDRs) on the London Stock Exchange (LSE) and ordinary shares on the Moscow Exchange through the use of independent brokers. NOVATEK also purchases its ordinary shares from shareholders where required by Russian legislation.

During the years ended 31 December 2016 and 2015, the Group purchased 1.4 million and 1.3 million ordinary shares (both ordinary shares and GDRs) at a total cost of RR 916 million and RR 775 million, respectively. At 31 December 2016 and 2015, the Group held in total (both ordinary shares and GDRs) 18.6 million and 17.2 million ordinary shares at a total cost of RR 6,913 million and RR 5,997 million, respectively. The Group has decided that these shares do not vote.

Dividends. Dividends (including tax on dividends) declared and paid were as follows:

	Year ended 31 December:	
	2016	2015
Dividends payable at 1 January	1	1
Dividends declared (*)	41,653	35,640
Dividends paid (*)	(41,653)	(35,640)
Dividends payable at 31 December	1	1
Dividends per share declared during the year (in Russian roubles)	13.80	11.80
Dividends per GDR declared during the year (in Russian roubles)	138.0	118.0

(*) – excluding treasury shares.

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18 SHAREHOLDERS' EQUITY (CONTINUED)

The Group declares and pays dividends in Russian roubles. Dividends declared in 2016 and 2015 were as follows:

Final for 2015: RR 6.90 per share or RR 69.0 per GDR declared in April 2016	20,951
Interim for 2016: RR 6.90 per share or RR 69.0 per GDR declared in September 2016	20,951

Total dividends declared in 2016	41,902
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Final for 2014: RR 5.20 per share or RR 52.0 per GDR declared in April 2015	15,789
Interim for 2015: RR 6.60 per share or RR 66.0 per GDR declared in September 2015	20,040

Total dividends declared in 2015	35,829
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Distributable retained earnings. The basis for distribution of profits of a company to shareholders is defined by Russian legislation as net profit presented in its statutory financial statements prepared in accordance with the Regulations on Accounting and Reporting of the Russian Federation, which may differ significantly from amounts calculated on the basis of IFRS. At 31 December 2016 and 2015, NOVATEK's closing balances of the accumulated profit including the respective year's net statutory profit totalled RR 366,928 million and RR 260,842 million, respectively.

19 OIL AND GAS SALES

	Year ended 31 December:	
	2016	2015
Natural gas	229,716	222,180
Naphtha	103,103	95,588
Crude oil	64,952	14,873
Other gas and gas condensate refined products	57,163	61,902
Stable gas condensate	47,271	43,997
Liquefied petroleum gas	31,652	33,467
Total oil and gas sales	533,857	472,007

20 PURCHASES OF NATURAL GAS AND LIQUID HYDROCARBONS

	Year ended 31 December:	
	2016	2015
Unstable gas condensate	93,854	91,078
Natural gas	38,119	27,715
Other liquid hydrocarbons	2,295	1,711
Total purchases of natural gas and liquid hydrocarbons	134,268	120,504

The Group purchases 50 percent of the natural gas volumes produced by its joint venture ZAO Nortgas, some volumes of natural gas produced by its joint venture OOO SeverEnergiya (through its wholly owned subsidiary, OAO Arcticgas) and, commencing May 2015, all volumes of natural gas produced by its joint venture ZAO Terneftegas (see Note 30).

The Group purchases all volumes of unstable gas condensate produced by its joint ventures Nortgas, SeverEnergiya (through its wholly owned subsidiary, Arcticgas) and Terneftegas (from May 2015) at ex-field prices based on benchmark crude oil prices (see Note 30).

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21 TRANSPORTATION EXPENSES

	Year ended 31 December:	
	2016	2015
Natural gas transportation		
by trunk and low-pressure pipelines	84,808	86,025
Stable gas condensate and		
liquefied petroleum gas transportation by rail	31,838	29,273
Gas condensate refined products,		
stable gas condensate and crude oil transportation by tankers	9,997	13,378
Crude oil transportation by trunk pipelines	6,654	1,476
Other	165	77
Total transportation expenses	133,462	130,229

22 TAXES OTHER THAN INCOME TAX

The Group is subject to a number of taxes other than income tax, which are detailed as follows:

	Year ended 31 December:	
	2016	2015
Unified natural resources production tax	40,997	33,656
Property tax	2,793	2,603
Other taxes	263	371
Total taxes other than income tax	44,053	36,630

23 MATERIALS, SERVICES AND OTHER

	Year ended 31 December:	
	2016	2015
Employee compensation	7,558	6,004
Repair and maintenance	3,026	1,959
Complex of services for preparation,		
transportation and processing of hydrocarbons	2,062	1,756
Materials and supplies	1,838	1,305
Electricity and fuel	1,101	938
Liquefied petroleum gas volumes reservation expenses	1,017	768
Security services	660	470
Transportation services	641	452
Insurance expenses	372	267
Rent expenses	257	59
Other	601	573
Total materials, services and other	19,133	14,551

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24 GENERAL AND ADMINISTRATIVE EXPENSES

	Year ended 31 December:	
	2016	2015
Employee compensation	12,327	9,364
Social expenses and compensatory payments	2,184	1,347
Legal, audit, and consulting services	1,019	1,036
Business travel expense	624	634
Fire safety and security expenses	387	313
Advertising expenses	370	253
Rent expenses	214	196
Repair and maintenance expenses	200	458
Other	801	755
Total general and administrative expenses	18,126	14,356

Auditor's fees. AO PricewaterhouseCoopers Audit has served as the independent external auditor of PAO NOVATEK for each of the reported financial years. The independent external auditor is subject to appointment at the Annual General Meeting of shareholders based on the recommendations from the Board of Directors. The aggregate fees for audit and other services rendered by PricewaterhouseCoopers Audit to the parent company of the Group included within legal, audit, and consulting services are as follows:

	Year ended 31 December:	
	2016	2015
Audits of PAO NOVATEK (audit of the Group's consolidated financial statements and audit of statutory financial statements of PAO NOVATEK)	34	31
Other services	9	10
Total auditor's fees and services	43	41

25 FINANCE INCOME (EXPENSE)

	Year ended 31 December:	
	2016	2015
<i>Interest expense (including transaction costs)</i>		
Interest expense on fixed rate debt	11,469	11,110
Interest expense on variable rate debt	4,828	3,439
Subtotal	16,297	14,549
Less: capitalized interest	(5,314)	(6,047)
Interest expense on debt	10,983	8,502
Provisions for asset retirement obligations: effect of the present value discount unwinding	587	290
Total interest expense	11,570	8,792
<i>Interest income</i>		
Interest income on loans receivable	17,597	11,206
Interest income on cash, cash equivalents and deposits	1,135	1,416
Total interest income	18,732	12,622

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25 FINANCE INCOME (EXPENSE) (CONTINUED)

<i>Foreign exchange gain (loss), net</i>	Year ended 31 December:	
	2016	2015
Gains	41,124	72,303
Losses	(66,614)	(81,810)
Total foreign exchange gain (loss), net	(25,490)	(9,507)

26 INCOME TAX

Reconciliation of income tax. The table below reconciles actual income tax expense and theoretical income tax, determined by applying the statutory tax rate to profit before income tax.

	Year ended 31 December:	
	2016	2015
Profit before income tax	308,164	92,941
Theoretical income tax expense at statutory rate of 20 percent	61,633	18,588
Increase (decrease) due to:		
Non-deductible (non-taxable) differences in respect of the Group's share of loss (profit) joint ventures	(18,147)	6,098
Non-deductible (non-taxable) differences in respect of net gain on disposal of interests in joint ventures	781	(396)
Deferred taxes relating to assets held for sale	-	(4,316)
Tax benefits relating to priority investment projects	(1,540)	(1,333)
Other differences	364	181
Total income tax expense	43,091	18,822

A number of the Group's investment projects were included by the government authorities in the list of priority projects, in respect of them the Group was able to apply a reduced income tax rate of 15.5 percent.

Domestic and foreign components of current income tax expense were:

	Year ended 31 December:	
	2016	2015
Russian Federation income tax	35,025	21,837
Foreign income tax	552	943
Total current income tax expense	35,577	22,780

Effective income tax rate. The Group's Russian statutory income tax rate for 2016 and 2015 was 20 percent. For the years ended 31 December 2016 and 2015, the consolidated Group's effective income tax rate was 14.0 percent and 20.3 percent, respectively.

The Group recognizes in profit before income tax its share of net profit (loss) from joint ventures, which influences the consolidated profit of the Group but does not result in additional income tax expense (benefit) at the Group's level. Net profit (loss) of joint ventures was recorded in their financial statements on an after-tax basis. The Group holds at least a 50 percent interest in each of its joint ventures, and dividend income from these joint ventures is subject to a zero withholding tax rate according to the Russian tax legislation. In addition, during the year ended 31 December 2015, the Group recognized a deferred tax asset of RR 4,316 million related to expected disposal of 9.9 percent participation interest in OAO Yamal LNG.

PAO NOVATEK

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26 INCOME TAX (CONTINUED)

Without the effect of net profit (loss) and dividends from joint ventures, and the deferred tax asset relating to the 9.9 percent interest in Yamal LNG classified as held for sale, the effective income tax rate for the years ended 31 December 2016 and 2015 was 19.8 percent and 18.7 percent, respectively.

In respect of PAO NOVATEK and majority of its Russian subsidiaries, the Group submits a single consolidated income tax return in accordance with Russian tax legislation (See Note 3).

Deferred income tax. Differences between IFRS and Russian statutory tax regulations give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and for income tax purposes.

Deferred income tax balances are presented in the consolidated statement of financial position as follows:

	At 31 December 2016	At 31 December 2015
Long-term deferred income tax asset (other non-current assets)	4,671	11,183
Long-term deferred income tax liability	(24,656)	(23,706)
Net deferred income tax liability	(19,985)	(12,523)

Deferred income tax assets expected to be realized within twelve months as of 31 December 2016 and 2015 were RR 1,556 million and RR 5,193 million, respectively. Deferred tax liabilities expected to be reversed within twelve months of 31 December 2016 and 2015 were RR 131 million and RR 212 million, respectively.

Movements in deferred income tax assets and liabilities during the years ended 31 December 2016 and 2015 are as follows:

	At 31 December 2016	Statement of Income effect	Statement of Comprehensive Income effect	At 31 December 2015
Property, plant and equipment	(26,805)	(1,521)	2	(25,286)
Intangible assets	(313)	66	-	(379)
Other	(676)	1,411	(14)	(2,073)
Deferred income tax liabilities	(27,794)	(44)	(12)	(27,738)
<i>Less: deferred tax assets offset</i>	<i>3,138</i>	<i>(894)</i>	<i>-</i>	<i>4,032</i>
Total deferred income tax liabilities	(24,656)	(938)	(12)	(23,706)
Tax losses carried forward	2,542	(616)	(2)	3,160
Loans receivable	1,975	(2,261)	-	4,236
Inventories	1,029	485	(1)	545
Assets held for sale	-	(4,316)	-	4,316
Asset retirement obligations	1,464	634	-	830
Trade payables and accrued liabilities	558	(1,445)	59	1,944
Other	241	49	8	184
Deferred income tax assets	7,809	(7,470)	64	15,215
<i>Less: deferred tax liabilities offset</i>	<i>(3,138)</i>	<i>894</i>	<i>-</i>	<i>(4,032)</i>
Total deferred income tax assets	4,671	(6,576)	64	11,183
Net deferred income tax liabilities	(19,985)	(7,514)	52	(12,523)

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26 INCOME TAX (CONTINUED)

	At 31 December 2015	Statement of Income effect	Statement of Comprehensive Income effect	At 31 December 2014
Property, plant and equipment	(25,286)	(3,341)	(2)	(21,943)
Intangible assets	(379)	(126)	-	(253)
Other	(2,073)	(1,220)	(16)	(837)
Deferred income tax liabilities	(27,738)	(4,687)	(18)	(23,033)
<i>Less: deferred tax assets offset</i>	<i>4,032</i>	<i>2,062</i>	<i>-</i>	<i>1,970</i>
Total deferred income tax liabilities	(23,706)	(2,625)	(18)	(21,063)
Tax losses carried forward	3,160	1,346	4	1,810
Loans receivable	4,236	1,293	-	2,943
Inventories	545	(172)	(2)	719
Assets held for sale	4,316	4,316	-	-
Asset retirement obligations	830	532	-	298
Trade payables and accrued liabilities	1,944	1,347	(67)	664
Other	184	(17)	14	187
Deferred income tax assets	15,215	8,645	(51)	6,621
<i>Less: deferred tax liabilities offset</i>	<i>(4,032)</i>	<i>(2,062)</i>	<i>-</i>	<i>(1,970)</i>
Total deferred income tax assets	11,183	6,583	(51)	4,651
Net deferred income tax liabilities	(12,523)	3,958	(69)	(16,412)

At 31 December 2016, the Group had recognized deferred income tax assets of RR 2,542 million (31 December 2015: RR 3,160 million) in respect of unused tax loss carry forwards of RR 13,102 million (31 December 2015: RR 17,400 million). In accordance with tax legislation of Russian Federation effective 1 January 2017, taxable profits can be reduced for the amount of tax losses carried forward during an unlimited period of time, and in 2017-2020 tax losses carried forward cannot be offset by more than 50 percent of taxable profits. Until 2017, tax legislation set limitation for the period of tax losses be carried forward for relief against taxable profits for ten years after they were incurred. In determining future taxable profits and the amount of tax benefits that are probable in the future management makes judgments including expectations regarding the Group's ability to generate sufficient future taxable income and the projected time period over which deferred tax benefits will be realized.

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27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS

The accounting policies and disclosure requirements for financial instruments have been applied to the line items below:

<i>Financial assets</i>	At 31 December 2016		At 31 December 2015	
	Non-current	Current	Non-current	Current
<i>Loans and receivables</i>				
Loans receivable	7,575	-	13,105	-
Trade and other receivables	24,832	41,586	16,748	37,564
Cash on special accounts	-	-	-	6,477
Cash and cash equivalents	-	48,301	-	29,187
Other	157	-	10	-
<i>At fair value through profit or loss</i>				
Loans receivable	176,738	308	200,946	-
Commodity derivatives	1,172	2,920	1,511	5,039
Total financial assets	210,474	93,115	232,320	78,267
<i>Financial liabilities</i>				
<i>At amortized cost</i>				
Long-term debt	161,296	55,469	252,050	77,269
Short-term debt	-	-	-	29,386
Trade and other payables	-	28,112	-	30,490
<i>At fair value through profit or loss</i>				
Commodity derivatives	1,517	2,754	368	2,355
Total financial liabilities	162,813	86,335	252,418	139,500

Fair value measurement. The Group evaluates the quality and reliability of the assumptions and data used to measure fair value in accordance with IFRS 13, *Fair Value Measurement*, in the three hierarchy levels as follows:

- quoted prices in active markets (Level 1);
- inputs other than quoted prices included in Level 1 that are directly or indirectly observable in the market (externally verifiable inputs) (Level 2);
- inputs that are not based on observable market data (unobservable inputs) (Level 3).

Commodity derivative instruments. The Group conducts natural gas foreign trading in active markets under long-term and short-term purchase and sales contracts, as well as purchases and sells various derivative instruments (with reference to the European natural gas hubs) for delivery optimization and to decrease exposure to the risk of negative changes in natural gas world prices.

These contracts include pricing terms that are based on a variety of commodities and indices, and/or volume flexibility options that collectively qualify them under the scope of IAS 39, *Financial instruments: recognition and measurement*, although the activity surrounding certain contracts involves the physical delivery of natural gas. All contracts mentioned above are recognized in the consolidated statement of financial position at fair value with movements in fair value recognized in the consolidated statement of income.

The fair value of long-term natural gas derivative contracts involving the physical delivery of natural gas is determined using internal models and other valuation techniques (the mark-to-market and mark-to-model analysis) due to the absence of quoted prices or other observable, market-corroborated data, for the duration of the contracts. Due to the assumptions underlying their fair value, the gas contracts are categorized as Level 3 in the fair value hierarchy, described above.

The fair value of short-term natural gas derivative contracts involving the physical delivery of natural gas and likewise contracts used for the price risk management and delivery optimization is determined based on available futures quotes in the active market (mark-to-market analysis) (Level 1).

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27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

The amounts recognized by the Group in respect of the natural gas derivative contracts measured in accordance with IAS 39, *Financial instruments: recognition and measurement*, are as follows:

<i>Commodity derivatives</i>	At 31 December 2016	At 31 December 2015
Within other non-current and current assets	4,092	6,550
Within other non-current and current liabilities	(4,271)	(2,723)

	Year ended 31 December:	
<i>Included in other operating income (loss)</i>	2016	2015
Operating income from natural gas foreign trading	1,970	206
Change in fair value	(1,778)	(1,006)

The table below represents the effect on the fair value estimation of natural gas derivative contracts that would occur from price changes by ten percent by one megawatt-hour in 12 months after the reporting date:

	Year ended 31 December:	
<i>Effect on the fair value (RR million)</i>	2016	2015
Increase by ten percent	(1,673)	(1,678)
Decrease by ten percent	1,673	1,678

Recognition and remeasurement of the shareholders' loans to joint ventures. Terms and conditions of the shareholders' loans provided by the Group to its joint ventures OAO Yamal LNG and ZAO Terneftegas contain certain financial (benchmark interest rates adjusted for the borrower credit risk) and non-financial (actual interest rates on the borrowings of shareholders, expected free cash flows of the borrower and expected maturities) variables and in accordance with the Group's accounting policy were classified as financial assets at fair value through profit or loss.

The following table summarizes the movements in the carrying amounts of shareholders' loans provided to Yamal LNG and Terneftegas and related interest receivable:

	Year ended 31 December:	
	2016	2015
At 1 January	216,136	88,726
Loans provided	6,645	104,076
Repayment of the loans and accrued interest	(1,298)	(1,160)
Initial measurement at fair value allocated to increase the Group's investments in joint ventures (see Note 7)	(836)	(14,185)
Subsequent remeasurement at fair value recognized in profit (loss) as follows:		
– Interest income (using the effective interest rate method)	16,248	9,596
– Foreign exchange gain (loss), net	(48,828)	39,588
– Remaining effect from changes in fair value (attributable to free cash flows of the borrowers and interest rates)	10,387	(10,505)
At 31 December	198,454	216,136

Fair value measurement of shareholders' loans to joint ventures is determined using benchmark interest rates adjusted for the borrower credit risk and free cash flows models based on the borrower's strategic plans approved by the shareholders of the joint ventures. Due to the assumptions underlying fair value estimation, shareholders' loans are categorized as Level 3 in the fair value hierarchy, described above.

27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

The fair value of the shareholders' loans is sensitive to benchmark interest rates changes. The table below represents the effect on fair value of the shareholders' loans that would occur from one percent changes in the benchmark interest rates.

<i>Effect on the fair value (RR million)</i>	Year ended 31 December:	
	2016	2015
Increase by one percent	(13,038)	(12,034)
Decrease by one percent	14,272	12,924

Financial risk management objectives and policies. In the ordinary course of business, the Group is exposed to market risks from fluctuating prices on commodities purchased and sold, prices of other raw materials, currency exchange rates and interest rates. Depending on the degree of price volatility, such fluctuations in market prices may create volatility in the Group's financial results. To effectively manage the variety of exposures that may impact financial results, the Group's overriding strategy is to maintain a strong financial position.

The Group's principal risk management policies are established to identify and analyze the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to these limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities.

Market risk. Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates, commodity prices and equity prices, will affect the Group's financial results or the value of its holdings of financial instruments. The primary objective of mitigating these market risks is to manage and control market risk exposures, while optimizing the return on risk.

The Group is exposed to market price movements relating to changes in commodity prices such as crude oil, oil and gas condensate refined products and natural gas (commodity price risk), foreign currency exchange rates, interest rates, equity prices and other indices that could adversely affect the value of the Group's financial assets, liabilities or expected future cash flows.

(a) Foreign exchange risk

The Group is exposed to foreign exchange risk arising from various exposures in the normal course of business, primarily with respect to the US dollar and Euro. Foreign exchange risk arises primarily from future commercial transactions, recognized assets and liabilities when assets and liabilities are denominated in a currency other than the functional currency.

The Group's overall strategy is to have no significant net exposure in currencies other than the Russian rouble, the US dollar and Euro. The Group may utilize foreign currency derivative instruments to manage the risk exposures associated with fluctuations on certain firm commitments for sales and purchases, debt instruments and other transactions that are denominated in currencies other than the Russian rouble, and certain non-Russian rouble assets and liabilities.

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27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

The carrying amounts of the Group's financial instruments are denominated in the following currencies:

<i>At 31 December 2016</i>	Russian rouble	US dollar	Euro	Other	Total
<i>Financial assets</i>					
<i>Non-current</i>					
Long-term loans receivable	7,575	79,484	97,254	-	184,313
Trade and other receivables	3,530	13,815	7,487	-	24,832
Commodity derivatives	-	-	1,172	-	1,172
Other	-	-	-	157	157
<i>Current</i>					
Trade and other receivables	23,525	15,297	1,841	923	41,586
Current portion of long-term loans receivable	-	308	-	-	308
Commodity derivatives	-	-	2,920	-	2,920
Cash and cash equivalents	10,346	18,116	19,544	295	48,301
<i>Financial liabilities</i>					
<i>Non-current</i>					
Long-term debt	-	(154,915)	(6,381)	-	(161,296)
Commodity derivatives	-	-	(1,517)	-	(1,517)
<i>Current</i>					
Current portion of long-term debt	(27,532)	(27,937)	-	-	(55,469)
Trade and other payables	(23,593)	(2,319)	(2,064)	(136)	(28,112)
Commodity derivatives	-	-	(2,754)	-	(2,754)
Net exposure	(6,149)	(58,151)	117,502	1,239	54,441

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27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

<i>At 31 December 2015</i>	Russian rouble	US dollar	Euro	Other	Total
Financial assets					
<i>Non-current</i>					
Long-term loans receivable	13,105	90,650	110,296	-	214,051
Trade and other receivables	2,341	11,515	2,862	30	16,748
Commodity derivatives	-	-	1,511	-	1,511
Other	-	-	-	10	10
<i>Current</i>					
Trade and other receivables	19,160	14,665	3,058	681	37,564
Commodity derivatives	-	-	5,039	-	5,039
Cash on special accounts	-	-	6,477	-	6,477
Cash and cash equivalents	10,171	7,223	11,499	294	29,187
Financial liabilities					
<i>Non-current</i>					
Long-term debt	(33,246)	(218,804)	-	-	(252,050)
Commodity derivatives	-	-	(368)	-	(368)
<i>Current</i>					
Current portion of long-term debt	-	(77,269)	-	-	(77,269)
Short-term debt	(21,300)	-	(8,086)	-	(29,386)
Trade and other payables	(20,243)	(7,653)	(2,373)	(221)	(30,490)
Commodity derivatives	-	-	(2,355)	-	(2,355)
Net exposure	(30,012)	(179,673)	127,560	794	(81,331)

The Group chooses to provide information about market risk and potential exposure to hypothetical loss from its use of financial instruments through sensitivity analysis disclosures in accordance with IFRS requirements.

The sensitivity analysis depicted in the table below reflects the hypothetical loss that would occur assuming a 10 percent increase in exchange rates and no changes in the portfolio of instruments and other variables at 31 December 2016 and 2015, respectively:

<i>Effect on profit before income tax</i>	Increase in exchange rate	Year ended 31 December:	
		2016	2015
RUB / USD	10%	(5,815)	(17,967)
RUB / EUR	10%	11,750	12,756

The effect of a corresponding 10 percent decrease in exchange rate is approximately equal and opposite.

(b) Commodity price risk

The Group's overall commercial trading strategy in natural gas and liquid hydrocarbons is centrally managed. Changes in commodity prices could negatively or positively affect the Group's results of operations. The Group manages the exposure to commodity price risk by optimizing its core activities to achieve stable price margins.

Natural gas supplies on the Russian domestic market. As an independent natural gas producer, the Group is not subject to the government's regulation of natural gas prices, except for those volumes sold to residential customers. Nevertheless, the Group's prices for natural gas sold are strongly influenced by the prices regulated by the governmental agency of the Russian Federation that carries out state regulation of prices and tariffs for goods and services of natural monopolies in energy, utilities and transportation.

There were no changes in regulated natural gas prices on the domestic market (excluding residential customers) from 1 January 2014 until 30 June 2015. Effective from 1 July 2015, natural gas prices were increased on average by 7.5 percent and remained unchanged through the end of 2016.

27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

Management believes it has limited downside commodity price risk for natural gas in the Russian Federation and does not use commodity derivative instruments for trading purposes. All of the Group's natural gas purchase and sales contracts in the domestic market are entered to meet supply requirements to fulfil contract obligations or for own consumption and are not within the scope of IAS 39, *Financial instruments: recognition and measurement*. However, to effectively manage the margins achieved through its natural gas trading activities, management has established targets for volumes sold to wholesale traders, end-customers and to the natural gas exchange.

Natural gas trading activities on the European and other foreign markets. The Group purchases and sells natural gas on the European and other foreign markets under long-term and short-term supply contracts, as well as purchases and sells different derivative instruments based on formulas with reference to benchmark natural gas prices quoted for the North-Western European natural gas hubs, crude oil and oil products prices and/or a combination thereof. Therefore, the Group's results from natural gas foreign trading and derivative instruments foreign trading are subject to commodity price volatility based on fluctuations or changes in the respective benchmark reference prices.

Natural gas foreign trading activities and respective foreign derivative instruments are executed by Novatek Gas & Power GmbH, the Group's wholly owned subsidiary, and are managed within the Group's integrated trading function.

Liquid hydrocarbons. The Group sells its crude oil, stable gas condensate and gas condensate refined products under spot contracts. Naphtha and stable gas condensate volumes sold to the Asian-Pacific Region, European and North American markets are based on benchmark reference crude oil prices of Brent IPE and Dubai and/or naphtha prices, mainly of Naphtha Japan and Naphtha CIF NWE or a combination thereof, plus a margin or discount, depending on current market situation. Other gas condensate refined products volumes sold mainly to the European market are based on benchmark reference jet fuel prices of Jet CIF NWE and gasoil prices of Gasoil 0.1 percent CIF NWE plus a margin or discount, depending on current market situation. Crude oil sold internationally is based on benchmark reference crude oil prices of Brent dated, minus a discount, or Dubai, plus a premium, and on a transaction-by-transaction basis for volumes sold domestically.

As a result, the Group's revenues from the sales of liquid hydrocarbons are subject to fluctuations in the crude oil and gas condensate refined products benchmark reference prices. All of the Group's liquid hydrocarbons purchase and sales contracts are entered to meet supply requirements to fulfill contract obligations or for own consumption and are not within the scope of IAS 39, *Financial instruments: recognition and measurement*.

(c) Cash flow and fair value interest rate risk

The Group is subject to interest rate risk on financial liabilities with variable interest rates. Changes in interest rates impact primarily debt by changing either their fair value (fixed rate debt) or their future cash flows (variable rate debt). To mitigate this risk, the Group's treasury function performs periodic analysis of the current interest rate environment and depending on that analysis management makes decisions whether it would be more beneficial to obtain financing on a fixed-rate or variable-rate basis. In cases where the change in the current market fixed or variable interest rates is considered significant management may consider refinancing a particular debt on more favorable interest rate terms.

The interest rate profiles of the Group's interest-bearing financial instruments were as follows:

	At 31 December 2016		At 31 December 2015	
	RR million	Percent	RR million	Percent
At fixed rate	161,323	74%	254,276	71%
At variable rate	55,442	26%	104,429	29%
Total debt	216,765	100%	358,705	100%

27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

The Group centralizes the cash requirements and surpluses of controlled subsidiaries and the majority of their external financing requirements, and applies, on its consolidated net debt position, a funding policy to optimize its financing costs and manage the impact of interest rate changes on its financial results in line with market conditions. In this way, the Group is able to ensure that the balance between the floating rate portion of its debt and its cash surpluses has a low level of exposure to any change in interest rates over the short term. This policy makes it possible to significantly limit the Group's sensitivity to interest rate volatility.

The Group's financial results are sensitive to changes in interest rates on the floating rate portion of the Group's debt portfolio. If the interest rates applicable to floating rate debt were to increase by 100 basis points (one percent) at the reporting dates, assuming all other variables remain constant, it is estimated that the Group's profit before taxation would decrease by the amounts shown below:

<i>Effect on profit before income tax</i>	Year ended 31 December:	
	2016	2015
Increase by 100 basis points	554	1,044

The effect of a corresponding 100 basis points decrease in interest rate is approximately equal and opposite.

The Group is examining various ways to manage its cash flow interest rate risk by using a combination of floating and fixed interest rates. No swaps or other similar instruments were in place at 31 December 2016 and 2015, or during the years then ended.

Credit risk. Credit risk refers to the risk exposure that a potential financial loss to the Group may occur if a counterparty defaults on its contractual obligations.

Credit risk is managed on a Group level and arises from cash and cash equivalents, including short-term deposits with banks, as well as credit exposures to customers, including outstanding trade receivables and committed transactions. Cash and cash equivalents are deposited only with banks that are considered by the Group during the whole deposit period to have minimal risk of default.

The Group's trade and other receivables consist of a large number of customers, spread across diverse industries and geographical areas. The Group has developed standard credit payment terms and constantly monitors the status of trade and other receivables and the creditworthiness of the customers.

Most of the Group's international liquid hydrocarbons sales are made to customers with independent external ratings; however, if the customer has a credit rating below BBB, the Group requires the collateral for the trade receivable to be in the form of letters of credit from banks with an investment grade rating. Most of domestic sales of liquid hydrocarbons are made on a 100 percent prepayment basis.

As a result of the domestic regional natural gas trading activities, the Group is exposed to the risk of payment defaults of small and medium-sized industrial users and individuals. To minimize credit risk the Group monitors the recoverability of these debtors by analyzing ageing of receivables by type of customers and their respective prior payment history.

The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the consolidated statement of financial position.

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27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

The table below highlights the Group's trade and other receivables to published credit ratings of its counterparties and/or their parent companies:

<i>Moody's, Fitch and/or Standard & Poor's</i>	At 31 December 2016	At 31 December 2015
Investment grade rating	12,913	13,143
Non-investment grade rating	5,062	8,880
No external rating	23,611	15,541
Total trade and other receivables	41,586	37,564

The table below highlights the Group's cash and cash equivalents balances to published credit ratings of its banks and/or their parent companies:

<i>Moody's, Fitch and/or Standard & Poor's</i>	At 31 December 2016	At 31 December 2015
Investment grade rating	38,087	24,542
Non-investment grade rating	10,194	4,627
No external rating	20	18
Total cash and cash equivalents	48,301	29,187

Investment grade ratings classification referred to as Aaa to Baa3 for Moody's Investors Service, and as AAA to BBB- for Fitch Ratings and Standard & Poor's.

In addition, the Group provides long-term loans to its joint ventures for development, construction and acquisitions of oil and gas assets. Required amount of loans and their maturity schedules are based on the budgets and strategic plans approved by the shareholders of the joint ventures.

Liquidity risk. Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity is to ensure that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation. In managing its liquidity risk, the Group maintains adequate cash reserves and debt facilities, continuously monitors forecast and actual cash flows and matches the maturity profiles of financial assets and liabilities.

The Group prepares various financial plans (monthly, quarterly and annually) which ensures that the Group has sufficient cash on demand to meet expected operational expenses, financial obligations and investing activities for a period of 30 days or more. The Group has entered into a number of short-term credit facilities. Such credit lines and overdraft facilities can be drawn down to meet short-term financing needs. To fund cash requirements of a more permanent nature, the Group will normally raise long-term debt in available international and domestic markets.

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27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

The following tables summarize the maturity profile of the Group's financial liabilities, except of natural gas derivative contracts, based on contractual undiscounted payments, including interest payments:

<i>At 31 December 2016</i>	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	More than 5 years	Total
Debt at fixed rate					
<i>Principal</i>	14,000	-	56,358	98,633	168,991
<i>Interest</i>	8,179	7,636	20,823	10,841	47,479
Debt at variable rate					
<i>Principal</i>	41,532	13,998	-	-	55,530
<i>Interest</i>	866	144	-	-	1,010
Trade and other payables	28,112	-	-	-	28,112
Total financial liabilities	92,689	21,778	77,181	109,474	301,122
<i>At 31 December 2015</i>					
Debt at fixed rate					
<i>Principal</i>	71,816	14,000	7,605	170,958	264,379
<i>Interest</i>	11,288	9,531	26,798	20,049	67,666
Debt at variable rate					
<i>Principal</i>	34,938	52,906	16,819	-	104,663
<i>Interest</i>	1,644	867	144	-	2,655
Trade and other payables	30,490	-	-	-	30,490
Total financial liabilities	150,176	77,304	51,366	191,007	469,853

The following table represents the maturity profile of the Group's derivative commodity contracts based on undiscounted cash flows:

<i>At 31 December 2016</i>	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	More than 5 years	Total
Cash inflow	39,310	25,336	57,713	13,704	136,063
Cash outflow	(39,144)	(25,871)	(57,570)	(13,655)	(136,240)
Net cash flows	166	(535)	143	49	(177)
<i>At 31 December 2015</i>					
Cash inflow	36,518	27,380	65,825	37,164	166,887
Cash outflow	(33,838)	(26,067)	(65,889)	(37,278)	(163,072)
Net cash flows	2,680	1,313	(64)	(114)	3,815

Capital management. The primary objectives of the Group's capital management policy are to ensure a strong capital base to fund and sustain its business operations through prudent investment decisions and to maintain investor, market and creditor confidence to support its business activities.

27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

Prior to 2015, the Group had investment grade credit ratings of Baa3 by Moody's Investors Service, BBB- by Fitch Ratings, and BBB- by Standard & Poor's. In February 2015, following the decrease of the sovereign credit rating of the Russian Federation by both Standard & Poor's and Moody's Investors Service, the Group's investment grade credit rating was also downgraded to noninvestment level BB+ and Ba1, respectively. In November 2016, the Group's credit rating was upgraded to investment level BBB- by Standard & Poor's. The Group has established certain financial targets and coverage ratios that it monitors on a quarterly and annual basis to maintain its credit ratings.

The Group manages its capital on a corporate-wide basis to ensure adequate funding to sufficiently meet the Group's operational requirements. The majority of external debts raised to finance NOVATEK's wholly owned subsidiaries are centralized at the parent level, and financing to Group entities is facilitated through inter-company loan arrangements or additional contributions to share capital.

The Group has a stated dividend policy that distributes not less than 30 percent of the Group's consolidated net profit determined according to IFRS, adjusted for one-off profits (losses). The dividend payment for a specific year is determined after taking into consideration future earnings, capital expenditure requirements, future business opportunities and the Group current financial position. Dividends are recommended by the Board of Directors of NOVATEK and approved by the NOVATEK's shareholders.

The Group defines the term "capital" as equity attributable to PAO NOVATEK shareholders plus net debt (total debt less cash and cash equivalents). There were no changes to the Group's approach to capital management during 2016. At 31 December 2016 and 2015, the Group's capital totaled RR 816,814 million and RR 755,597 million, respectively.

28 CONTINGENCIES AND COMMITMENTS

Operating environment. The Russian Federation continues to display some characteristics of an emerging market. These characteristics include, but are not limited to, the existence of a currency that is in practice not convertible in most countries outside of the Russian Federation, and relatively high inflation. In addition, the Russian economy is particularly sensitive to world oil and gas prices; therefore, significant prolonged declines in world oil prices have a negative impact on the Russian economy. The tax, currency and customs legislation is subject to varying interpretations, frequent changes and other legal and fiscal impediments contribute to the challenges faced by entities currently operating in the Russian Federation. The future economic direction of the Russian Federation is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the Government, together with tax, legal, regulatory, and political developments.

The Group's business operations are primarily located in the Russian Federation and are thus exposed to the economic and financial markets of the Russian Federation.

Developments in Ukraine during 2014 and 2015 and the subsequent negative reaction of the world community have had and may continue to have a negative impact on the Russian economy, including difficulties in obtaining international funding, devaluation of national currency and high inflation. These and other events, in case of escalation, may have a significant negative impact on the operating environment in the Russian Federation.

Sectoral sanctions imposed by the U.S. government. On 16 July 2014, the Office of Foreign Assets Control (OFAC) of the U.S. Treasury included PAO NOVATEK on the Sectoral Sanctions Identification List (the "List"), which prohibits U.S. persons or persons within the United States from providing new financing to the Group for longer than 90 days, whereas all other transactions, including financial, carried out by U.S. persons or within the United States with the Group are permitted. The inclusion on the List has not impacted the Group's business activities, in any jurisdiction, nor does it affect the Group's assets, listed shares and debt.

Management has reviewed the Group's capital expenditure programs and existing debt portfolio and has concluded that the Group has sufficient liquidity, through internally generated (operating) cash flows, to adequately fund its core oil and gas business operations including finance of planned capital expenditure programs of its subsidiaries, as well as to repay and service all Group's short-term and long-term debt existing at the current reporting date and, therefore, inclusion on the List does not adversely impact the Group's operational activities.

28 CONTINGENCIES AND COMMITMENTS (CONTINUED)

The Group together with its foreign partners currently raises necessary financing for our joint ventures from non-US debt markets and lenders.

Contractual commitments. At 31 December 2016, the Group had contractual capital expenditures commitments aggregating approximately RR 13 billion (at 31 December 2015: RR 23 billion) mainly for development at the Yardeyskoye (through 2017), the Salmanovskoye (Utrenneye) (through 2018), the East-Tarkosalinskoye (through 2019) and the Yurkharovskoye (through 2018) fields all in accordance with duly signed agreements.

The Group's commitments with regard to its joint operation in Montenegro relate to performance obligations of the Concessionaries to conduct mandatory work program exploration activities as stipulated by the Concession Contract (see Note 1). The maximum amount to be paid to the State of Montenegro by the Group in case of non-performance during the first exploration period of up to four years ending in 2020 is EUR 42.5 million. The outflow of resources embodying economic benefits required to settle this contingent liability is not probable; therefore, no provision for this liability was recognized in the consolidated financial statements.

The Group has entered into a number of agreements, maturing after the twelve months from the reporting date, relating to time chartering of marine tankers with service terms up to six years for transportation of liquid hydrocarbons. At 31 December 2016, the future minimum payments under these time charter agreements amounted to RR 11.5 billion (at 31 December 2015: RR 10.3 billion).

Non-financial guarantees. The aggregated amount of non-financial guarantees in respect of the Yamal LNG project issued by the Group to a number of third parties (the Ministry of Finance of the Russian Federation, Russian and foreign banks, LNG plant constructors, LNG-vessels owners, LNG-terminal owners) in favor of the Group's joint venture OAO Yamal LNG and its subsidiary totaled USD 3.0 billion and EUR 3.1 billion at 31 December 2016 (at 31 December 2015: USD 3.6 billion and EUR 0.1 billion). These non-financial guarantees have various terms depending mostly on the successful project completion (finalization of the LNG plant construction and achievement of its full production capacity). For certain factors as stipulated in the project financing agreements, the Group plans to issue in the future non-financial guarantees covering the project post-completion period.

With regard to the Group's obligations under the non-financial guarantee issued to the banks providing project financing to Yamal LNG, the State Corporation "Bank for Development and Foreign Economic Affairs (Vnesheconombank)" issued in favor of the banks a counter guarantee for the amount not exceeding the equivalent of USD 3 billion.

The outflow of resources embodying economic benefits required to settle the obligations under these non-financial guarantees issued by the Group is not probable; therefore, no provision for these liabilities was recognized in the consolidated financial statements.

Taxation. Russian tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Correspondingly, the relevant regional and federal tax authorities may periodically challenge management's interpretation of such taxation legislation as applied to the Group's transactions and activities. Furthermore, events within the Russian Federation suggest that the tax authorities may be taking a more assertive position in its interpretation of the legislation and assessments, and it is possible that transactions and activities that have not been challenged in the past may be challenged. As a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

Management believes that its interpretation of the relevant legislation is appropriate and that it is probable that the Group's tax, currency and customs positions will be sustained. Where management believes it is probable that a position cannot be sustained, an appropriate amount has been accrued in the consolidated financial statements.

Mineral licenses. The Group is subject to periodic reviews of its activities by governmental authorities with respect to the requirements of its mineral licenses. Management cooperates with governmental authorities to agree on remedial actions necessary to resolve any findings resulting from these reviews. Failure to comply with the terms of a license could result in fines, penalties or license limitation, suspension or revocation. The Group's management believes any issues of non-compliance will be resolved through negotiations or corrective actions without any material adverse effect on the Group's financial position, results of operations or cash flows.

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28 CONTINGENCIES AND COMMITMENTS (CONTINUED)

The major of the Group's oil and gas fields and license areas are located in the YNAO. Licenses are issued by the Federal Agency for the Use of Natural Resources of the Russian Federation and the Group pays unified natural resources production tax to produce crude oil, natural gas and unstable gas condensate from these fields and contributions for exploration of license areas. The principal licenses of the Group and its joint ventures and their expiry dates are:

Field	License holder	License expiry date
<i>Subsidiaries:</i>		
Salmanovskoye (Utrenneye)	OOO Arctic LNG 2	2031
Yurkharovskoye	OOO NOVATEK-Yurkharovneftegas	2034
Geofizicheskoye	OOO Arctic LNG 1	2034
East-Tarkosalinskoye	OOO NOVATEK-Tarkosaleneftgas	2043
North-Russkoye	OOO NOVATEK-Tarkosaleneftgas	2031
Khancheyevskoye	OOO NOVATEK-Tarkosaleneftgas	2044
Urengoyevskoye (within the Olimpiyskiy license area)	OOO NOVATEK-Tarkosaleneftgas	2059
Dobrovolskoye (within the Olimpiyskiy license area)	OOO NOVATEK-Tarkosaleneftgas	2059
East-Tazovskoye	OOO NOVATEK-Tarkosaleneftgas	2033
Kharbeyevskoye	OOO NOVATEK-Tarkosaleneftgas	2036
North-Khancheyevskoye + Khadyryakhinskoye	OOO NOVATEK-Tarkosaleneftgas	2029
Dorogovskoye	OOO NOVATEK-Tarkosaleneftgas	2033
Yarudeyskoye	OOO Yargeo	2029
Malo-Yamalskoye	OOO NOVATEK-Yarsaleneftgas	2034
<i>Joint ventures:</i>		
South-Tambeyskoye	OAo Yamal LNG	2045
Urengoyevskoye (within the Samburskiy and Yevo-Yakhinskiy license areas)	OAo Arcticgas ^(*)	2034
Yaro-Yakhinskoye	OAo Arcticgas	2034
Samburskoye	OAo Arcticgas	2034
North-Chaselskoye	OAo Arcticgas	Life of field
Yevo-Yakhinskoye	OAo Arcticgas	2034
North-Urengoyevskoye	ZAO Nortgas	2038
Termokarstovoye	ZAO Terneftgas	2097

^(*) Subsidiary of OOO SeverEnergiya

Management believes the Group has the right to extend its licenses beyond the initial expiration date under the existing legislation and intends to exercise this right on all of its fields.

Environmental liabilities. The Group operates in the oil and gas industry in the Russian Federation and abroad. The enforcement of environmental regulation in the Russian Federation and other countries of operation is evolving and the enforcement posture of government authorities is continually being reconsidered. The Group periodically evaluates its obligations under environmental regulations and, as obligations are determined, they are recognized as an expense immediately if no future benefit is discernible. Potential liabilities arising as a result of a change in interpretation of existing regulations, civil litigation or changes in legislation cannot be estimated. Under existing legislation, management believes that there are no probable liabilities, which will have a material adverse effect on the Group's financial position, results of operations or cash flows.

Legal contingencies. The Group is subject of, or party to a number of court proceedings (both as a plaintiff and a defendant) arising in the ordinary course of business. In the opinion of management, there are no current legal proceedings or other claims outstanding, which could have a material effect on the result of operations or financial position of the Group and which have not been accrued or disclosed in the consolidated financial statements.

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29 PRINCIPAL SUBSIDIARIES AND JOINT VENTURES

The principal subsidiaries and joint ventures of the Group and respective effective ownership in the ordinary share capital at 31 December 2016 and 2015 are set out below:

	Ownership percent at 31 December:		Country of incorporation	Principal activities
	2016	2015		
Subsidiaries:				
OOO NOVATEK-Yurkharovneftegas	100	100	Russia	Exploration and production
OOO NOVATEK-Tarkosaleneftegase	100	100	Russia	Exploration and production
OOO Yargeo	51	51	Russia	Exploration, development and production
OOO NOVATEK-Purovsky ZPK	100	100	Russia	Gas Condensate Processing Plant
OOO NOVATEK-Transervice	100	100	Russia	Transportation services
OOO NOVATEK-Ust-Luga	100	100	Russia	Fractionation and Transshipment Complex
OOO NOVATEK-AZK	100	100	Russia	Wholesale and retail trading
OOO NOVATEK-Chelyabinsk	100	100	Russia	Trading and marketing
OOO NOVATEK-Kostroma	100	100	Russia	Trading and marketing
OOO NOVATEK-Perm	100	100	Russia	Trading and marketing
OOO NOVATEK Moscow Region	100	100	Russia	Trading and marketing
Novatek Gas & Power GmbH	100	100	Switzerland	Trading and marketing
Novatek Gas & Power Asia PTE. Ltd	100	100	Singapore	Trading and marketing
Novatek Polska Sp. z o.o.	100	100	Poland	Trading and marketing
Joint ventures:				
OA O Yamal LNG	50,1	60(*)	Russia	Exploration and development, construction of LNG plant
ZAO Terneftegas	51	51	Russia	Exploration and production
ZAO Nortgas	50	50	Russia	Exploration and production
OOO Yamal Development	50	50	Russia	Holding company
Artic Russia B.V.	56,8	56,8	Netherlands	Holding company
OOO SeverEnergia (includes a producing subsidiary, see Note 7)	53,3	53,3	Russia	Holding company

(*) Includes a 9.9 percent ownership classified as an asset held for sale (see Note 5)

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30 RELATED PARTY TRANSACTIONS

Transactions between NOVATEK and its subsidiaries, which are related parties of NOVATEK, have been eliminated on consolidation and are not disclosed in this Note.

For the purposes of these consolidated financial statements, parties are generally considered to be related if one party has the ability to control the other party, is under common control, or can exercise significant influence or joint control over the other party in making financial and operational decisions. Management has used reasonable judgments in considering each possible related party relationship with attention directed to the substance of the relationship, not merely the legal form. Related parties may enter into transactions, which unrelated parties might not, and transactions between related parties may not be affected on the same terms, conditions and amounts as transactions between unrelated parties.

<i>Related parties – joint ventures</i>	Year ended 31 December:	
	2016	2015
Transactions		
OOO SeverEnergiya and its subsidiary:		
Purchases of natural gas and liquid hydrocarbons	(82,420)	(75,412)
Other revenues	195	182
OOO Yamal Development:		
Interest income on loans issued	1,275	1,517
ZAO Nortgas:		
Purchases of natural gas and liquid hydrocarbons	(17,180)	(20,064)
Other revenues	60	84
ZAO Terneftegas:		
Purchases of natural gas and liquid hydrocarbons	(12,898)	(7,922)
Interest income on loans issued	173	262
Other revenues	90	86
OAQ Yamal LNG:		
Interest income on loans issued	16,075	9,334
Other revenues	498	356
Materials, services and other	(77)	(11)

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30 RELATED PARTY TRANSACTIONS (CONTINUED)

<i>Related parties – joint ventures</i>	At 31 December 2016	At 31 December 2015
Balances		
OOO SeverEnergiya and its subsidiary:		
Trade payables and accrued liabilities	11,986	6,733
OOO Yamal Development:		
Long-term loans receivable	7,575	13,105
Interest on long-term loans receivable	3,088	1,813
ZAO Nortgas:		
Trade payables and accrued liabilities	1,829	1,751
ZAO Terneftegas:		
Long-term loans receivable	2,893	4,413
Current portion of long-term loans receivable	308	-
Interest on long-term loans receivable	106	813
Trade payables and accrued liabilities	1,589	1,133
PAO Yamal LNG:		
Long-term loans receivable	173,845	196,533
Interest on long-term loans receivable	21,302	14,377
Trade receivables	245	134

The terms and conditions of the loans receivable from the joint ventures are disclosed in Note 8.

The Group issued non-financial guarantees in favor of its joint ventures as described in Note 28.

<i>Related parties – parties under control of key management personnel</i>	Year ended 31 December:	
	2016	2015
Transactions		
OOO Transoil:		
Liquid hydrocarbons transportation by rail	(9,405)	(8,907)
OOO Nova:		
Purchases of construction services (capitalized within property, plant and equipment)	(530)	(2,626)
Materials, services and other	(72)	(75)
PAO SIBUR Holding and its subsidiaries (under control until December 2015):		
Sales of natural gas and liquid hydrocarbons	-	19,052
Purchases of natural gas and liquid hydrocarbons	-	(15,501)
Liquid hydrocarbons transportation by rail	-	(3,747)
Materials, services and other	-	(1,868)
PAO Pervobank (under control until November 2015):		
Interest income	-	431

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30 RELATED PARTY TRANSACTIONS (CONTINUED)*Related parties – parties under control
of key management personnel***At 31 December 2016 At 31 December 2015****Balances****OOO Transoil:**

Prepayments and other current assets	478	412
Trade payables and accrued liabilities	263	316

OOO Nova:

Advances for construction	23	75
Trade payables and accrued liabilities	8	262

In December 2015, following the change in the ownership structure and corporate governance in PAO SIBUR Holding, the Chairman of the Management Committee of NOVATEK ceased to be its controlling shareholder, and as the result, SIBUR Holding ceased to be a related party of the Group.

In November 2015, the Chairman of the Management Committee of NOVATEK sold a controlling stake in PAO Pervobank to a third party, and as the result, Pervobank ceased to be a related party of the Group.

Transactions with related parties also included loans which were provided to one of the Group's subsidiaries by its non-controlling shareholder (see Notes 14, 15).

Key management personnel compensation. The Group paid to key management personnel (members of the Board of Directors and the Management Committee) short-term compensation, including salary, bonuses, and excluding dividends the following amounts:

<i>Related parties – members of the key management personnel</i>	Year ended 31 December:	
	2016	2015
Board of Directors	132	147
Management Committee	1,956	2,042
Total compensation	2,088	2,189

Such amounts include personal income tax and are net of payments to non-budget funds made by the employer. Some members of key management personnel have direct and/or indirect interests in the Group and receive dividends under general conditions based on their respective shareholdings. The Board of Directors consists of nine members. Starting from March 2016, the Management Committee consists of twelve members (earlier – nine members).

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31 SEGMENT INFORMATION

The Group's activities are considered by the chief operating decision maker (hereinafter referred to as "CODM", represented by the Management Committee of NOVATEK) to comprise one operating segment: "exploration, production and marketing".

Segment information is provided to the CODM in accordance with Regulations on Accounting and Reporting of the Russian Federation ("RAR") with reconciling items largely representing adjustments and reclassifications recorded in the consolidated financial statements for the fair presentation in accordance with IFRS.

The CODM assesses reporting segment performance based on profit before income tax, since income tax is not allocated. No business segment assets or liabilities (except for capital expenditures for the period) are provided to the CODM for decision-making.

Segment information for the year ended 31 December 2016 is as follows:

<i>For the year ended 31 December 2016</i>	References	Exploration, production and marketing	Segment information as reported to CODM	Reconciling items	Total per consolidated financial statements
External revenues		537,461	537,461	11	537,472
Operating expenses	<i>a, b, h</i>	(380,448)	(380,448)	(5,051)	(385,499)
Other operating income (loss)	<i>c, d, h</i>	54,287	54,287	19,006	73,293
Interest expense	<i>e, h</i>	(15,921)	(15,921)	4,351	(11,570)
Interest income	<i>f</i>	13,317	13,317	5,415	18,732
Change in fair value of non-commodity financial instruments	<i>g</i>	-	-	10,387	10,387
Foreign exchange gain (loss), net	<i>c</i>	(26,177)	(26,177)	687	(25,490)
Segment result		182,519	182,519	34,806	217,325
Share of profit (loss) of joint ventures, net of income tax					90,839
Profit before income tax					308,164
Depreciation, depletion and amortization	<i>a</i>	32,554	32,554	2,077	34,631
Capital expenditures	<i>e</i>	32,367	32,367	2,992	35,359

Reconciling items mainly related to:

- different methodology in calculating depreciation, depletion and amortization for intangible assets and for oil and gas properties between IFRS (units of production method) and management accounting (straight-line method), which resulted in additional recognition of operating expenses of RR 2,077 million under IFRS;
- different methodology in accounting for exploration costs between IFRS and management accounting, which resulted in additional recognition of operating expenses of RR 1,293 million under IFRS;
- different methodology in calculating gain on disposal of a 9.9 percent equity stake in OAO Yamal LNG, the Group's joint venture, between IFRS and management accounting, which resulted in additional recognition of other operating income of RR 20,041 million and foreign exchange gain of RR 695 million under IFRS;
- different methodology in valuation of commodity derivatives under IFRS and management accounting, which resulted in additional recognition of other operating loss of RR 1,778 million under IFRS;
- different methodology in borrowing costs capitalization policy and certain recognition policy differences in capital expenditures between IFRS and management accounting, which resulted in additional recognition of capital expenditures of RR 2,992 million under IFRS;

31 SEGMENT INFORMATION (CONTINUED)

- f. different methodology in recognizing effect of the present value discount unwinding of long-term financial assets under IFRS and management accounting, which requires additional recognition of interest income of RR 5,354 million under IFRS;
- g. different methodology in valuation of shareholders' loans provided by the Group to its joint ventures classified as financial assets at fair value through profit or loss between IFRS and management accounting, which requires additional gain recognition of RR 10,387 million under IFRS; and
- h. other differences relating to recognition of natural gas storage expenses, employee compensation, bad debt provisions, exploration expenses, valuation of inventory balances, effect of the present value discount unwinding of asset retirement obligations.

Segment information for the year ended 31 December 2015 is as follows:

<i>For the year ended 31 December 2015</i>	References	Exploration, production and marketing	Segment information as reported to CODM	Reconciling items	Total per consolidated financial statements
External revenues		475,356	475,356	(31)	475,325
Operating expenses	<i>a, f</i>	(338,518)	(338,518)	3,476	(335,042)
Other operating income (loss)	<i>b, f</i>	1,091	1,091	(644)	447
Interest expense	<i>c, f</i>	(9,670)	(9,670)	878	(8,792)
Interest income	<i>d</i>	9,612	9,612	3,010	12,622
Change in fair value of non-commodity financial instruments	<i>e</i>	-	-	(10,505)	(10,505)
Foreign exchange gain (loss), net	<i>c</i>	(12,065)	(12,065)	2,558	(9,507)
Segment result		125,806	125,806	(1,258)	124,548
Share of profit (loss) of joint ventures, net of income tax					(31,607)
Profit before income tax					92,941
Depreciation, depletion and amortization	<i>a</i>	24,124	24,124	(4,144)	19,980
Capital expenditures	<i>c</i>	54,904	54,904	5,065	59,969

Reconciling items mainly related to:

- a. different methodology in calculating depreciation, depletion and amortization for intangible assets and for oil and gas properties between IFRS (units of production method) and management accounting (straight-line method), which resulted in reversal of RR 4,442 million in operating expenses under IFRS;
- b. different methodology in valuation of commodity derivatives under IFRS and management accounting, which requires additional recognition of other operating loss of RR 1,006 million under IFRS;
- c. different methodology in borrowing costs capitalization policy and certain recognition policy differences in capital expenditures between IFRS and management accounting, which resulted in additional recognition of capital expenditures of RR 5,065 million under IFRS, including capitalized interest of RR 856 million;
- d. different methodology in recognizing effect of the present value discount unwinding of long-term financial assets under IFRS and management accounting, which requires additional recognition of interest income of RR 2,934 million under IFRS;

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31 SEGMENT INFORMATION (CONTINUED)

- e. different methodology in valuation of shareholders' loans provided by the Group to its joint ventures classified as financial assets at fair value through profit or loss between IFRS and management accounting, which requires additional loss recognition of RR 10,505 million under IFRS; and
- f. other differences relating to recognition of natural gas storage expenses, employee compensation, bad debt provisions, exploration expenses, valuation of inventory balances, effect of the present value discount unwinding of asset retirement obligations.

Geographical information. The Group operates in the following geographical areas:

- *Russian Federation* – exploration, development, production and processing of hydrocarbons, and sales of natural gas, stable gas condensate, liquefied petroleum gas, crude oil and gas condensate refined products;
- *Countries of Europe (primarily, Denmark, Belgium, the Netherlands, Finland, Poland and Montenegro)* – exploration activities within joint operations, sales of naphtha, stable gas condensate, gas condensate refined products, crude oil and liquefied petroleum gas;
- *Countries of the Asia-Pacific region (primarily, China, Taiwan, South Korea and Japan)* – sales of naphtha, stable gas condensate and crude oil;
- *Countries of the Middle East (primarily, Oman) and North America (primarily, the USA)* – sales of naphtha and crude oil.

Geographical information for the year ended 31 December 2016 and 2015 is as follows:

<i>For the year ended 31 December 2016</i>	Natural gas	Stable gas condensate and naphtha	Crude oil	Other gas and gas condensate refined products	Liquefied petroleum gas	Total oil and gas sales
Russia	229,716	21,920	42,754	2,655	18,811	315,856
Europe	-	44,989	13,902	61,122	12,841	132,854
The Asia-Pacific region	-	71,752	13,184	-	-	84,936
North America	-	24,757	1,295	-	-	26,052
The Middle East	-	6,469	947	-	-	7,416
Less: export duties	-	(19,513)	(7,130)	(6,614)	-	(33,257)
Total outside Russia	-	128,454	22,198	54,508	12,841	218,001
Total	229,716	150,374	64,952	57,163	31,652	533,857

<i>For the year ended 31 December 2015</i>	Natural gas	Stable gas condensate and naphtha	Crude oil	Other gas and gas condensate refined products	Liquefied petroleum gas	Total oil and gas sales
Russia	222,180	19,110	9,244	2,235	20,543	273,312
Europe	-	51,580	7,913	70,512	12,891	142,896
The Asia-Pacific region	-	90,616	-	-	-	90,616
North America	-	14,662	-	-	-	14,662
The Middle East	-	1,712	423	-	322	2,457
Less: export duties	-	(38,095)	(2,707)	(10,845)	(289)	(51,936)
Total outside Russia	-	120,475	5,629	59,667	12,924	198,695
Total	222,180	139,585	14,873	61,902	33,467	472,007

31 SEGMENT INFORMATION (CONTINUED)

Revenues are based on the geographical location of customers even though all revenues are generated from assets located in the Russian Federation. Substantially all of the Group's operating assets are located in the Russian Federation.

Major customers. For the year ended 31 December 2016, the Group had one major customer to whom individual revenue exceeded 10 percent of total external revenues, which represented 18 percent (RR 97.7 billion) of total external revenues. For the year ended 31 December 2015, the Group had two major customers to whom individual revenue exceeded 10 percent of total external revenues, which on an individual basis represented 13 percent and 10 percent (RR 61.2 billion and RR 47.2 billion) of total external revenues, respectively. All of the Group's major customers reside within the Russian Federation.

32 NEW ACCOUNTING PRONOUNCEMENTS

The following amended standards and interpretations became effective for the Group from 1 January 2016:

Amendments to IAS 1, *Presentation of Financial Statements* (issued in December 2014 and effective for annual periods on or after 1 January 2016). The Standard was amended to clarify the concept of materiality and explains that an entity does need not to provide a specific disclosure required by an IFRS if the information resulting from that disclosure is not material, even if the IFRS contains a list of specific requirements or describes them as minimum requirements. The Standard also provides new guidance on subtotals in financial statements. The adoption of the amendments had no material impact on the Group's consolidated financial statements.

The following new standards have been issued that the Group has decided to early adopt starting from the annual period beginning on 1 January 2017:

IFRS 15, *Revenue from Contracts with Customers* (issued in May 2014, further amended in April 2016 and effective for annual periods beginning on or after 1 January 2018, early adoption is permitted). The new standard introduces the core principle that revenue must be recognized when the goods or services are transferred to the customer, at the transaction price. Any discounts on the contract price must generally be allocated to the separate elements of contracts with customers. When the consideration varies for any reason, minimum amounts must be recognized if they are not at significant risk of reversal. Costs incurred to secure contracts with customers have to be capitalized and amortized over the period when the benefits of the contract are consumed. The Group assesses that the adoption of this standard did not have a material impact on the Group's consolidated financial position as of the date of transition.

IFRS 16, *Leases* (issued in January 2016 and effective for annual periods beginning on or after 1 January 2019, early application is permitted, provided the new revenue standard, IFRS 15, *Revenue from Contracts with Customers*, has been applied, or is applied at the same date as IFRS 16). The standard requires lessees to recognize assets and liabilities for most leases. For lessors, there is a minor change to the existing accounting treatment in IAS 17, *Leases*. The Group assesses that the adoption of this standard did not have a material impact on the Group's consolidated financial position as of the date of transition.

Certain new standards and interpretations have been issued that are mandatory for the annual periods beginning on or after 1 January 2017, and which the Group has not early adopted:

Amendments to IAS 7, *Statement of Cash Flows* (issued in January 2016 and effective for annual periods on or after 1 January 2017, early adoption is permitted). The amended IAS 7 will require disclosure of a reconciliation of movements in liabilities arising from financing activities.

32 NEW ACCOUNTING PRONOUNCEMENTS (CONTINUED)

Amendments to IFRS 10, *Consolidated financial statements*, and IAS 28, *Investments in associates and joint ventures* (issued in September 2014, in November 2015 the effective date was postponed indefinitely). These amendments address an inconsistency between the requirements in IFRS 10 and those in IAS 28 in dealing with the sale or contribution of assets between an investor and its associate or joint venture. The amendments stipulate that a full gain or loss is recognized when a transaction involves a business. A partial gain or loss is recognized when a transaction involves assets that do not constitute a business, even if these assets are held by a subsidiary. The Group is considering the implications of these amendments for the Group's consolidated financial statements, and the timing of their adoption by the Group.

IFRS 9, *Financial Instruments: Classification and Measurement* (issued in July 2014 and effective for annual periods beginning on or after 1 January 2018, early adoption is permitted). The standard introduces new requirements for classification and measurement of financial instruments, impairment, and hedge accounting. The Group is considering the implications of this standard for the Group's consolidated financial statements, and the timing of its adoption by the Group.

UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES

The accompanying consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”). In the absence of specific IFRS guidance for the oil and gas industry, the Group has reverted to other relevant disclosure standards, mainly US GAAP, that are consistent with norms established for companies in the oil and gas industry. While not required under IFRS, this section provides unaudited supplemental information on oil and gas exploration and production activities but excludes disclosures regarding the standardized measures of discounted cash flows related to oil and gas activities.

The Group’s exploration and production activities are mainly within the Russian Federation; therefore, majority of the information provided in this section pertains to this country. The Group operates through various oil and gas production subsidiaries, and also has an interest in oil and gas companies that are accounted for under the equity method.

Oil and Gas Exploration and Development Costs

The following tables set forth information regarding oil and gas acquisition, exploration and development activities. The amounts reported as costs incurred include both capitalized costs and costs charged to expense, these costs do not include LNG liquefaction and transportation operations (amounts in millions of Russian roubles).

	Year ended 31 December:	
	2016	2015
Costs incurred in exploration and development activities		
Acquisition of unproved properties	1,928	-
Exploration costs	4,828	4,357
Development costs	23,550	53,427
Total costs incurred in exploration and development activities	30,306	57,784
The Group’s share in joint ventures’ cost incurred in exploration and development activities	71,408	39,899
	At 31 December 2016	At 31 December 2015
Capitalized costs relating to oil and gas producing activities		
Wells, related equipment and facilities	293,449	252,716
Support equipment and facilities	88,202	68,895
Uncompleted wells, related equipment and facilities	30,138	61,745
Total capitalized costs relating to oil and gas producing activities	411,789	383,356
Less: accumulated depreciation, depletion and amortization	(119,674)	(88,103)
Net capitalized costs relating to oil and gas producing activities	292,115	295,253
The Group’s share in joint ventures’ capitalized costs relating to oil and gas producing activities	343,096	285,445

UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)

Results of Operations for Oil and Gas Producing Activities

The Group's results of operations for oil and gas producing activities are shown below. The results of operations for oil and gas producing activities do not include general corporate overhead or its associated tax effects. Income tax is based on statutory rates. In the following table, revenues from oil and gas sales are comprised of the sale of hydrocarbons produced by the Group's subsidiaries and include processing costs, related to processing facilities of the Group's subsidiaries as well as transportation expenses to customers (amounts in millions of Russian roubles).

	Year ended 31 December:	
	2016	2015
Revenues from oil and gas sales	276,037	248,673
Lifting costs	(14,233)	(10,102)
Transportation expenses	(76,356)	(83,574)
Taxes other than income tax	(43,844)	(36,296)
Depreciation, depletion and amortization	(32,049)	(17,522)
Exploration expenses	(2,087)	(1,109)
Total production costs	(168,569)	(148,603)
Results of operations for oil and gas producing activities before income tax	107,468	100,070
Less: related income tax expenses	(21,494)	(20,014)
Results of operations for oil and gas producing activities of the Group's subsidiaries	85,974	80,056
Share of profit (loss) of joint ventures	29,821	28,957
Total results of operations for oil and gas producing activities	115,795	109,013

Proved Oil and Gas Reserves

The Group's oil and gas reserves estimation and reporting process involves an annual independent third party reserve appraisal as well as internal technical appraisals of reserves. The Group maintains its own internal reserve estimates that are calculated by qualified engineers and technical staff working directly with the oil and gas properties. The Group's technical staff periodically updates reserve estimates during the year based on evaluations of new wells, performance reviews, new technical information and other studies.

The Group estimates its oil and gas reserves in accordance with rules promulgated by the Securities and Exchange Commission (SEC) for proved reserves.

The oil and gas reserve estimates reported below are determined by the Group's independent petroleum reservoir engineers, DeGolyer and MacNaughton ("D&M"). The Group provides D&M annually with engineering, geological and geophysical data, actual production histories and other information necessary for the reserve determination. The Group's and D&M's technical staffs meet to review and discuss the information provided, and upon completion of this process, senior management reviews and approves the final reserve estimates issued by D&M.

The following reserve estimates were prepared using standard geological and engineering methods generally accepted by the petroleum industry. The method or combination of methods used in the analysis of each reservoir is tempered by experience with similar reservoirs, stages of development, quality and completeness of basic data, and production history.

UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)

The following information presents the quantities of proved oil and gas reserves and changes thereto as at and for the years ended 31 December 2016 and 2015.

Extensions of production licenses are assumed to be at the discretion of the Group. Management believes that proved reserves should include quantities which are expected to be produced after the expiry dates of the Group's production licenses. The principal licenses of the Group for exploration and production expire between 2029 and 2059, with the most significant licenses for Yurkharovskoye and East-Tarkosalinskoye fields, expiring in 2034 and 2043, respectively. Legislation of the Russian Federation states that, upon expiration, a license is subject to renewal at the initiative of the license holder provided that further exploration, appraisal, production or remediation activities are necessary and provided that the license holder has not violated the terms of the license. Management intends to extend its licenses for properties expected to produce beyond the license expiry dates.

Proved reserves are defined as the estimated quantities of oil and gas which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic conditions. In some cases, substantial new investment in additional wells and related support facilities and equipment will be required to recover such proved reserves. Due to the inherent uncertainties and the limited nature of reservoir data, estimates of underground reserves are subject to change over time as additional information becomes available.

Proved developed reserves are those reserves which are expected to be recovered through existing wells with existing equipment and operating methods. Undeveloped reserves are those reserves which are expected to be recovered as a result of future investments to drill new wells, to re-complete existing wells and/or install facilities to collect and deliver the production.

Net reserves exclude quantities due to others when produced.

The reserve quantities below include 100 percent of the net proved reserve quantities attributable to the Group's consolidated subsidiaries and the Group's ownership percentage of the net proved reserves quantities of the joint ventures. A portion of the Group's total proved reserves are classified as either developed non-producing or undeveloped. Of the non-producing reserves, a portion represents existing wells which are to be returned to production at a future date.

For convenience, reserves estimates are provided both in English and Metric units.

UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)

Net proved reserves of natural gas are presented below.

	Net proved reserves		Group's share in joint ventures		Total net proved reserves	
	<i>Billions of cubic feet</i>	<i>Billions of cubic meters</i>	<i>Billions of cubic feet</i>	<i>Billions of cubic meters</i>	<i>Billions of cubic feet</i>	<i>Billions of cubic meters</i>
Reserves at 31 December 2014	35,956	1,018	25,879	733	61,835	1,751
Changes attributable to:						
Revisions of previous estimates	1,035	30	1,210	34	2,245	64
Extension and discoveries	1,247	35	68	2	1,315	37
Disposals ⁽¹⁾	-	-	(325)	(9)	(325)	(9)
Production	(1,735)	(49)	(662)	(19)	(2,397)	(68)
Reserves at 31 December 2015 ⁽²⁾	36,503	1,034	26,170	741	62,673	1,775
Changes attributable to:						
Revisions of previous estimates	824	23	1,630	47	2,454	70
Extension and discoveries	633	18	360	10	993	28
Disposals ⁽²⁾	-	-	(1,823)	(52)	(1,823)	(52)
Production	(1,631)	(46)	(703)	(20)	(2,334)	(66)
Reserves at 31 December 2016	36,329	1,029	25,634	726	61,963	1,755
Net proved developed reserves (included above)						
At 31 December 2014	17,039	482	8,086	229	25,125	711
At 31 December 2015	16,598	470	7,785	220	24,383	690
At 31 December 2016	13,994	396	8,241	233	22,235	629
Net proved undeveloped reserves (included above)						
At 31 December 2014	18,917	536	17,793	504	36,710	1,040
At 31 December 2015	19,905	564	18,385	521	38,290	1,085
At 31 December 2016	22,335	633	17,393	493	39,728	1,126

⁽¹⁾ In August 2015, the Group contributed a 6.4 percent interest in Artic Russia to Yamal Development. As a result, the Group's effective participation interest in SeverEnergiya decreased from 54.9 percent to 53.3 percent.

⁽²⁾ At 31 December 2015, the Group's share in proved reserves of natural gas of joint ventures included reserves attributable to 9.9 percent interest in OAO Yamal LNG classified as asset held for sale of 1,823 billion of cubic feet or 52 billion of cubic meters. In March 2016, the Group recognized the disposal of the 9.9 percent stake in Yamal LNG. As a result, the Group's interest in Yamal LNG decreased from 60.0 percent to 50.1 percent.

The net proved reserves reported in the table above included reserves of natural gas attributable to non-controlling interest of 147 billion of cubic feet (four billion cubic meters) and 112 billion of cubic feet (three billion cubic meters) at 31 December 2016 and 2015, respectively.

UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)

Net proved reserves of crude oil, gas condensate and natural gas liquids are presented below.

	Net proved reserves		Group's share in joint ventures		Total net proved reserves	
	<i>Millions of barrels</i>	<i>Millions of metric tons</i>	<i>Millions of barrels</i>	<i>Millions of metric tons</i>	<i>Millions of barrels</i>	<i>Millions of metric tons</i>
Reserves at 31 December 2014	512	62	680	78	1,192	140
Changes attributable to:						
Revisions of previous estimates	14	2	34	3	48	5
Extension and discoveries	59	8	3	1	62	9
Disposals ⁽¹⁾	-	-	(14)	(2)	(14)	(2)
Production	(34)	(4)	(43)	(5)	(77)	(9)
Reserves at 31 December 2015 ⁽²⁾	551	68	660	75	1,211	143
Changes attributable to:						
Revisions of previous estimates	116	11	58	8	174	19
Extension and discoveries	15	1	18	3	33	4
Disposals ⁽²⁾	-	-	(13)	(2)	(13)	(2)
Production	(59)	(7)	(46)	(5)	(105)	(12)
Reserves at 31 December 2016	623	73	677	79	1,300	152
Net proved developed reserves (included above)						
At 31 December 2014	216	26	271	31	487	57
At 31 December 2015	305	38	302	34	607	72
At 31 December 2016	275	33	326	37	601	70
Net proved undeveloped reserves (included above)						
At 31 December 2014	296	36	409	47	705	83
At 31 December 2015	246	30	358	41	604	71
At 31 December 2016	348	40	351	42	699	82

⁽¹⁾ In August 2015, the Group contributed a 6.4 percent interest in Artic Russia to Yamal Development. As a result, the Group's effective participation interest in SeverEnergiya decreased from 54.9 percent to 53.3 percent.

⁽²⁾ At 31 December 2015, the Group's share in proved reserves of crude oil, gas condensate and natural gas liquids of joint ventures included reserves attributable to 9.9 percent interest in OAO Yamal LNG classified as asset held for sale of 13 million of barrels or two million of metric tons. In March 2016, the Group recognized the disposal of the 9.9 percent stake in Yamal LNG. As a result, the Group's interest in Yamal LNG decreased from 60.0 percent to 50.1 percent.

The net proved reserves reported in the table above included reserves of crude oil, gas condensate and natural gas liquids attributable to non-controlling interest of 66 million of barrels (nine million metric tons) and 49 million of barrels (six million metric tons) at 31 December 2016 and 2015, respectively.

PAO NOVATEK
Contact Information

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PAO NOVATEK

**MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION
AND RESULTS OF OPERATIONS**

**FOR THE YEARS ENDED
31 DECEMBER 2016 AND 2015**

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GENERAL PROVISIONS

You should read the following discussion and analysis of our financial condition and results of operations as of 31 December 2016 and for the year then ended in conjunction with our audited consolidated financial statements as of and for the years ended 31 December 2016 and 2015. The consolidated financial statements and the related notes thereto have been prepared in accordance with International Financial Reporting Standards (IFRS).

The financial and operating information contained in this "Management's Discussion and Analysis of Financial Condition and Results of Operations" comprises information of PAO NOVATEK, its consolidated subsidiaries and joint ventures (hereinafter jointly referred to as "we" or the "Group").

This report includes forward-looking statements concerned future possible events that can impact operational and financial results of the Group. Forward-looking statements can be identified by words such as "believes", "anticipates", "expects", "estimates", "intends", "plans" and similar expressions. Forward-looking statements are made based on the current situation with definite and indefinite risks and uncertainties. Actual future results could differ materially from those discussed in the forward-looking statements as they are dependent on various factors beyond and under the control of management.

OVERVIEW

We are one of the Russia's largest natural gas producers and leaders in terms of proved natural gas reserves in the Russian Federation under the Petroleum Resources Management System ("PRMS") and the Security and Exchange Commission ("SEC") reserve reporting methodologies.

Our exploration and development, production and processing of natural gas, gas condensate and crude oil are conducted mainly within the Russian Federation.

In accordance with Russian law, we currently sell all of our produced natural gas volumes exclusively in the Russian domestic market.

Several wholly owned subsidiaries of the Group (OOO Arctic LNG 1, OOO Arctic LNG 2, and OOO Arctic LNG 3) and the Group's joint venture OAO Yamal LNG are the holders of liquefied natural gas ("LNG") export licenses. The aforementioned subsidiaries hold licenses for exploration and production on the Salmanovskoye (Utrenneye) and Geofizicheskoye fields, and the North-Obskiy and Trekhbugorniy license areas located on the Gydan peninsula and the Gulf of Ob. Yamal LNG holds the exploration and production license for the South-Tambeyskoye field located in the north-eastern part of the Yamal peninsula in the Yamal-Nenets Autonomous Region ("YNAO").

We deliver our extracted unstable gas condensate through our own pipelines to our Purovsky Gas Condensate Plant (the "Purovsky Plant") for processing into stable gas condensate and liquefied petroleum gas ("LPG"). The Purovsky Plant allows us to process more than 12 million tons of unstable gas condensate per annum.

Most of our stable gas condensate is sent for further processing to our Gas Condensate Fractionation and Transshipment Complex located at the port of Ust-Luga on the Baltic Sea (the "Ust-Luga Complex"). The Ust-Luga Complex processes our stable gas condensate into light and heavy naphtha, jet fuel, gasoil and fuel oil, nearly all of which we sell to the international markets allowing us to increase the added value of our liquid hydrocarbons sales. The Ust-Luga Complex allows us to process about seven million tons of stable gas condensate annually.

The excess volumes of stable gas condensate received from the processing at the Purovsky Plant over volumes sent for further processing to the Ust-Luga Complex are sold on both the domestic and international markets (from the port of Ust-Luga on the Baltic Sea by tankers and to European markets by rail).

A significant part of our LPG produced at the Purovsky Plant is dispatched via pipeline for refining by OOO SIBUR Tobolsk at its refining facility (the "Tobolsk Refining Facilities"). The remaining volumes are sold directly from the Purovsky Plant without incurring additional transportation expenses. After processing at the Tobolsk Refining Facilities we receive LPG with higher added value, the majority of which are transported by rail to our end-customers in the domestic and international markets with the remaining portion sold directly from the Tobolsk Refining Facilities without incurring additional transportation expenses.

We deliver our crude oil to both domestic and international markets.

The Group, jointly with our international partners TOTAL S.A., China National Petroleum Corporation and China's Silk Road Fund Co. Ltd., through our joint venture OAO Yamal LNG, undertakes a large-scale project on constructing a liquefied natural gas plant with an annual capacity of 16.5 million tons based on the feedstock resources of the South-Tambeyskoye field (the "Yamal LNG project"). The Yamal LNG project also requires the construction of transportation infrastructure, including the seaport and the international airport. The launch of the first train of the LNG plant and start of liquefied natural gas shipments is planned in 2017. It is expected that the produced LNG will be sold mainly to the Asian-Pacific Region ("APR") and to the European market. The Yamal LNG project has now concluded the sale of more than 95% of LNG volumes produced under long-term contractual agreements.

RECENT DEVELOPMENTS

Increasing our production and utilization of refining capacity

At the end of 2014 and in the first half of 2015, OOO SeverEnergiya, the Group's joint venture with PAO Gazprom Neft, and ZAO Terneftegas, the Group's joint venture with TOTAL S.A., launched additional production facilities. As a result, the Group's gas condensate production has increased significantly enabling us to fill the capacity of processing facilities of our Ust-Luga Complex (effective January 2015) and our Purovsky Plant (effective May 2015).

In December 2015, we commenced commercial production at the Yarudeyskoye oil field and at the end of the month we reached the nameplate production capacity of approximately 3.5 million tons of crude oil per annum. The successful launch and production ramp-up of the Yarudeyskoye field allowed us to significantly increase our production of crude oil and represented the majority of liquids production growth in 2016.

Implementing our Yamal LNG project

Currently, the Yamal LNG project is in the final stage of preparation for the launch of the first train of the LNG plant and the start of liquefied natural gas shipments planned in 2017. Most of the infrastructure required for the launch is now completed, including the sea port and the international airport, production wells drilled, and all of the modules for the first LNG train have been delivered and installed. More than 95% of LNG volumes produced within the project have been contracted under long-term agreements and we have signed long-term agreements for time chartering of LNG ice class carriers to ensure future LNG deliveries.

In 2015, the Ministry of Finance subscribed for and purchased two tranches of Yamal LNG's bonds in the aggregate amount of RR 150 billion (nominal amount of USD 2.36 billion) allocated from the National Wealth Fund. The bonds will be repaid in equal installments from 2022 to 2030 in Russian roubles at the US dollar exchange rate at the date of payment. Interest is paid semi-annually starting from September 2015.

In 2016, Yamal LNG also signed credit line facility agreements to raise project financing for the total amount of approximately EUR 13.9 billion and CNY 7.6 billion, with the repayment period commencing from December 2019 through June 2031:

- in April 2016 – with PAO Sberbank and AO Gazprombank (with insurance coverage by the Russian Agency for Export Credit and Investment Insurance), the Export-Import Bank of China, and the China Development Bank;
- in December 2016 – with the Italian bank Intesa Sanpaolo (with insurance coverage by the Italian export-credit agency SACE and the French export-credit agency COFACE), and the Japan Bank for International Cooperation.

Signing of these credit agreements and the bonds placement completely cover the project's external finance needs and contribute to its further successful realization.

In December 2015, NOVATEK and China's Silk Road Fund Co. Ltd. signed an agreement on the acquisition of a 9.9% equity stake in Yamal LNG by the fund. In March 2016, the transaction was closed upon the completion of the conditions precedent. As a result of this transaction, the Group's interest in Yamal LNG was reduced from 60% to 50.1%. The Group continues to exercise joint control over Yamal LNG and, accordingly, recognizes the project as a joint venture. The entrance of Silk Road Fund Co. Ltd. to the Yamal LNG project is an important step in the execution of our long-term development strategy for this project.

Development of our operations at Gydan peninsula and the Gulf of Ob

The Group's wholly owned subsidiaries OOO Arctic LNG 1, OOO Arctic LNG 2, and OOO Arctic LNG 3 have significant hydrocarbon resources on the Gydan peninsula and the Gulf of Ob and are the holders of the liquefied natural gas export licenses. The aforementioned subsidiaries hold exploration and production licenses for the Salmanovskoye (Utrenneye) and Geofizicheskoye fields as well as the North-Obskiy and Trekhbugorniy license areas.

In 2016, we continued full-scale exploration activities in this region, conducted processing and interpretation of new and existing seismic data, drilled several exploration wells for the purpose of delineating the resource base and defining a plan to develop these fields.

The estimated aggregate proved, probable and possible reserves of the Salmanovskoye (Utrenneye) and Geofizicheskoye fields appraised under the PRMS reserve methodology as of 31 December 2016 totaled 1.24 trillion cubic meters of natural gas and 53.7 million tons of liquid hydrocarbons. The resources of the North-Obskiy license area according to the Russian reserve classification C3+D1L as of 31 December 2016 totaled 1.1 trillion cubic meters of natural gas and 71 million tons of liquid hydrocarbons. The resources of the Trekhbugorniy license area according to the Russian reserve classification C3+D as of 31 December 2016 amounted to approximately 1.0 trillion of cubic meters of natural gas and 92 million tons of liquid hydrocarbons.

In addition, we significantly expanded our resource base on the Gydan peninsula in 2016 and obtained the rights for the usage of five new license areas.

- In October 2016, based on results of auction held by the Federal Agency for the Use of Natural Resources of the Russian Federation, the Group won the right for geological research works, exploration and production of hydrocarbons at the Tanamskiy license area. The license area is located on the Gydan peninsula in the Krasnoyarsk region in close proximity to other license areas of the Group on the peninsula. As of 31 December 2016, the field's recoverable hydrocarbon resources according to the Russian reserve classification C3+D totaled approximately 1.2 billion barrels of oil equivalent. The payment for the license amounted to RR 467 million.
- In June 2016, the Group obtained mineral licenses for exploration works at the West-Solpatinskiy and Nyavuyahskiy license areas adjacent to the Ladertoyskiy license area, and the North-Tanamskiy license area located in the YNAO. As of 31 December 2016, the aggregate recoverable resources of these three new license areas according to the Russian reserve classification C3+D totaled approximately 560 billion cubic meters ("bcm") of natural gas and approximately 57 million tons of liquid hydrocarbons.
- In April 2016, the Group acquired a 100% equity stake in OOO Evrotek-Yuh for RR six million. Evrotek-Yuh is a holder of the license for geological research works, exploration and production of hydrocarbons within Ladertoyskiy license area located in the YNAO. As of 31 December 2016, the license area's reserves and recoverable resources according to the Russian reserve classification ABC1+C2+C3 totaled approximately 39 bcm of natural gas and approximately six million tons of liquid hydrocarbons.

The Group considers the Gydan peninsula and the Gulf of Ob as one of the most important regions for implementing our future strategic projects. We are studying different alternatives for developing and monetizing our hydrocarbon resources in this region and are presently conducting feasibility studies for a new LNG plant construction based on the resources of the Salmanovskoye (Utrenneye) field. It is contemplated to build the plant on gravity-based platforms which will be constructed, jointly with other major units for the plant, at our own center for construction of large-scale offshore structures located in Murmansk region. In the end of 2016, we acquired several properties for the construction of the project infrastructure, including a berth with an access road, and currently we are preparing project documentation for the plant and infrastructure construction.

Increasing our resource base in YNAO

In addition to obtaining the aforementioned five new license areas on the Gydan peninsula in 2016, the Group, based on auction results held by the Federal Agency for the Use of Natural Resources of the Russian Federation, won the right for the usage of two additional license areas in YNAO.

- In September 2016, the Group obtained the right for geological research works, exploration and production of hydrocarbons at the Syadorskiy license area. The acquisition of the new license area located in the northern part of the Yamal peninsula in YNAO expands the Group's resource base for implementing our future projects in this region. As of 31 December 2016, the field's natural gas reserves according to the Russian reserve classification C1 amounted to approximately 25 bcm, and recoverable resources according to the Russian reserve classification C3+D totaled approximately 63 bcm of natural gas and approximately 19 million tons of liquid hydrocarbons. The payment for the license amounted to RR 404 million.
- In April 2016, the Group obtained the right for geological research works, exploration and production of hydrocarbons at the Nyakhartinskiy license area. The license area is located in the YNAO in close proximity to our Yurkharovskoye field, which will allow us to develop the new area using the existing well-developed infrastructure of one of our core production assets. As of 31 December 2016, the field's recoverable resources according to the Russian reserve classification C3+D totaled 215 bcm of natural gas and more than 70 million tons of liquid hydrocarbons. The payment for the license amounted to RR 1,057 million.

International oil and gas projects

In September 2016, the Group and the Italian energy company Eni (the "Concessionaries") through their wholly owned subsidiaries entered into a concession contract with the State of Montenegro for the exploration and production of hydrocarbons on four offshore blocks located in the Adriatic Sea (the "Concession Contract"). The participation interest of each Concessioner is 50%, and Eni was appointed as the operator.

According to the Concession Contract, the Concessionaries are committed to perform 3D-seismic exploratory works and to drill several exploration wells during the exploration phase of up to seven years. The Concessionaries are currently preparing for performing exploration works that are planned to commence in early 2017.

The participation in the Concession Contract contributes to the Group's ability to realize future international joint projects, as well as enables the Group to gain experience working in offshore projects.

LNG market development

In July 2016, NOVATEK through its wholly owned subsidiary Novatek Gas and Power GmbH performed its first trading operation for the purchase and sale of liquefied natural gas on the spot market. The first LNG cargo was purchased in Trinidad and Tobago and supplied to Chile. This operation allowed the Group to gain experience in LNG trading and will contribute to our successful entry to the global LNG market. The financial result from the LNG trading activity was recorded in "Other operating income (loss)".

In December 2016, we acquired a 100% participation interest in a company Blue Gaz Sp. z o.o. for total cash consideration of RR 26 million (PLN two million) to expand the Groups' activities in Poland. The company purchases liquefied natural gas in Poland, regasifies it at its own regasification station and sells natural gas to customers in Poland.

Change in the participation interest in SeverEnergia

In August 2015, as part of the next stage of restructuring procedures, NOVATEK contributed a 6.4% ownership interest in Artic Russia B.V. to the capital of Yamal Development. Simultaneously, the Group and Gazprom Neft made contributions to the capital of Yamal Development by converting loans (including accrued interest) in the amount of RR 2.5 billion and RR 14.9 billion, respectively. As a result of these transactions the Group's effective participation interest in SeverEnergia decreased from 54.9% to 53.3%. It is expected that further procedures towards achieving parity shareholdings in SeverEnergia will be completed in the foreseeable future.

Extension and conclusion of new natural gas supply contracts

In 2015 and 2016, we continued forming and optimizing our natural gas supply agreements portfolio. The Group concluded and extended a number of large natural gas supply contracts:

- concluded a contract with PAO Enel Russia for the supply of approximately 2.0 bcm of natural gas per annum starting from January 2016 until the end of 2018;
- concluded a number of contracts with the companies of the Novolipetsk Steel Group for the supply of 2.8 bcm of natural gas per annum starting from January 2016 until 2020 which were subsequently extended to 2025; and
- extended the natural gas supply contract with PAO Mosenergo for an additional four years until the end of 2019, with annual supply volumes of approximately 9.1 bcm.

Contract extensions and concluding new major agreements are important steps for maintaining and increasing our client base.

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millions of Russian roubles except as stated	Year ended 31 December:		Change %
	2016	2015	
Financial results			
Total revenues ⁽¹⁾	537,472	475,325	13.1%
Operating expenses	(385,499)	(335,042)	15.1%
Normalized EBITDA ^{(2),(3)}	242,407	214,189	13.2%
Normalized profit attributable to shareholders of PAO NOVATEK ⁽³⁾	200,118	73,407	172.6%
Normalized profit attributable to shareholders of PAO NOVATEK ⁽³⁾ , excluding the effect of foreign exchange gains (losses)	133,759	132,509	0.9%
Normalized earnings per share ⁽³⁾ (in Russian roubles)	66.30	24.30	172.8%
Normalized earnings per share ⁽³⁾ , excluding the effect of foreign exchange gains (losses) (in Russian roubles)	44.31	43.87	1.0%
Net debt ⁽⁴⁾	168,464	329,518	(48.9%)
Production volumes ⁽⁵⁾			
Hydrocarbons production (million barrels of oil equivalent)	537.0	521.6	3.0%
Daily production (million barrels of oil equivalent per day)	1.47	1.43	3.0%
Sales volumes			
Natural gas sales volumes (million cubic meters)	64,709	62,465	3.6%
Crude oil sales volumes (thousand tons)	4,650	1,090	326.6%
Naphtha sales volumes (thousand tons)	4,113	4,120	(0.2%)
Stable gas condensate sales volumes (thousand tons)	2,812	2,786	0.9%
Liquefied petroleum gas sales volumes (thousand tons)	2,713	2,306	17.6%
Other gas condensate refined products (thousand tons) ⁽⁶⁾	2,549	2,573	(0.9%)
Oil and gas SEC reserves ⁽⁷⁾			
Total proved reserves (billion barrels of oil equivalent)	12.8	12.8	(0.3%)
Total natural gas proved reserves (trillion cubic meters)	1.75	1.77	(1.1%)
Total liquids proved reserves (million tons)	152	143	6.3%
Cash flow results			
Net cash provided by operating activities	173,791	132,864	30.8%
Cash used for capital expenditures ⁽⁸⁾	34,413	50,584	(32.0%)
Free cash flow ⁽⁹⁾	139,378	82,280	69.4%

⁽¹⁾ Net of VAT, export duties, excise and fuel taxes.

⁽²⁾ EBITDA represents profit (loss) adjusted for the add-back of depreciation, depletion and amortization, net impairment expenses (reversals), finance income (expense), income tax expense, as well as income (loss) from changes in fair value of derivative financial instruments. EBITDA includes EBITDA from subsidiaries and our proportionate share in the EBITDA of our joint ventures.

⁽³⁾ Excluding the effect from the disposal of interests in joint ventures.

⁽⁴⁾ Net Debt represents our total debt net of cash and cash equivalents.

⁽⁵⁾ Hydrocarbons production and daily production are calculated based on 100% of net production of our subsidiaries and our proportionate share in the production of our joint ventures.

⁽⁶⁾ Other gas condensate refined products include jet fuel, gasoil and fuel oil.

⁽⁷⁾ Oil and gas reserves are presented under SEC reserve classification and include 100% of reserves attributable to all consolidated subsidiaries and our proportionate share in the reserves of our joint ventures.

⁽⁸⁾ Cash used for capital expenditures represents purchases of property, plant and equipment, materials for construction and capitalized interest paid per Consolidated Statement of Cash Flows net of payments for mineral licenses and acquisition of subsidiaries.

⁽⁹⁾ Free cash flow represents the difference between Net cash provided by operating activities and Cash used for capital expenditures.

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Our financial results fluctuate period-on-period due to the recognition of non-cash foreign exchange gains (losses) resulting from the Russian rouble appreciation/depreciation relative to the foreign currencies.

In 2016, the Russian rouble appreciated relative to the US dollar and Euro by 17% and 20%, respectively, whereas in 2015, the Russian rouble depreciated relative to the US dollar and Euro by 30% and 17%, respectively. As a result, we recognized significant non-cash foreign exchange gains in 2016 compared to significant non-cash foreign exchange losses in 2015. These foreign exchange gains (losses) primarily related to the US dollar- and Euro-denominated borrowings of Yamal LNG, our joint venture. We believe that the risk of currency movements arising in relation to the debt portfolio of Yamal LNG will be fully mitigated due to its revenues denominated in foreign currency as all liquefied natural gas volumes will be delivered to and sold in international markets once commercial production commences.

Excluding the one-off effect from the disposal of interests in joint ventures and the effect of foreign exchange gains and losses, the Group's profit attributable to shareholders of PAO NOVATEK was relatively flat and amounted to RR 133,759 million compared to 132,509 million in 2015.

Reconciliation of EBITDA and normalized EBITDA is as follows:

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2016	2015	
Profit	265,073	74,119	257.6%
Depreciation, depletion and amortization	34,631	19,980	73.3%
Impairment expenses (reversals), net	178	(204)	n/a
Loss (income) from changes in fair value of derivative financial instruments	1,778	1,006	76.7%
Total finance expense (income)	7,941	16,182	(50.9%)
Total income tax expense	43,091	18,822	128.9%
Share of loss (profit) of joint ventures, net of income tax	(90,839)	31,607	n/a
EBITDA from subsidiaries	261,853	161,512	62.1%
Share in EBITDA of joint ventures	53,626	53,666	(0.1%)
EBITDA	315,479	215,178	46.6%
Net gain on disposal of interests in joint ventures	(73,072)	(989)	n/a
Normalized EBITDA	242,407	214,189	13.2%
Normalized EBITDA from subsidiaries	188,781	160,523	17.6%

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Exchange rate, RR for one foreign currency unit ⁽¹⁾	1Q		2Q		3Q		4Q		Year		Change Y-o-Y, %
	2016	2015	2016	2015	2016	2015	2016	2015	2016	2015	
US dollar (USD)											
Average for the period	74.63	62.19	65.89	52.65	64.62	62.98	63.07	65.94	67.03	60.96	10.0%
At the beginning of the period	72.88	56.26	67.61	58.46	64.26	55.52	63.16	66.24	72.88	56.26	29.5%
At the end of the period	67.61	58.46	64.26	55.52	63.16	66.24	60.66	72.88	60.66	72.88	(16.8%)
Depreciation (appreciation) of RR to US dollar	(7.2%)	3.9%	(5.0%)	(5.0%)	(1.7%)	19.3%	(4.0%)	10.0%	(16.8%)	29.5%	n/a
Euro											
Average for the period	82.34	70.43	74.40	58.24	72.15	70.11	68.13	72.27	74.23	67.78	9.5%
At the beginning of the period	79.70	68.34	76.54	63.37	71.21	61.52	70.88	74.58	79.70	68.34	16.6%
At the end of the period	76.54	63.37	71.21	61.52	70.88	74.58	63.81	79.70	63.81	79.70	(19.9%)
Depreciation (appreciation) of RR to euro	(4.0%)	(7.3%)	(7.0%)	(2.9%)	(0.5%)	21.2%	(10.0%)	6.9%	(19.9%)	16.6%	n/a

⁽¹⁾ Based on the data from the Central Bank of Russian Federation (CBR). The average rates for the period are calculated as the average of the daily exchange rates on each business day (rate is announced by the CBR) and on each non-business day (rate is equal to the exchange rate on the previous business day).

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Average for the period	1Q		2Q		3Q		4Q		Year		Change
	2016	2015	2016	2015	2016	2015	2016	2015	2016	2015	Y-o-Y, %
Benchmark crude oil prices ⁽²⁾											
Brent, USD per barrel	33.9	53.9	45.6	61.9	45.9	50.5	49.3	43.8	43.7	52.4	(16.6%)
Urals, USD per barrel	32.2	52.9	43.8	61.7	44.0	49.6	48.1	42.0	42.1	51.4	(18.1%)
Urals, RR per barrel	2,403	3,290	2,886	3,249	2,843	3,124	3,034	2,769	2,822	3,133	(9.9%)
Benchmark crude oil prices excluding export duties ⁽³⁾											
Urals, USD per barrel	24.7	35.1	34.6	43.8	31.8	32.0	35.5	29.4	31.7	34.9	(9.2%)
Urals, RR per barrel	1,843	2,183	2,280	2,306	2,055	2,015	2,239	1,939	2,125	2,128	(0.1%)
World market prices for oil products ⁽⁴⁾ and liquefied petroleum gas ⁽⁵⁾ , USD per ton											
Naphtha Japan	345	493	411	563	389	462	450	444	399	490	(18.6%)
Naphtha CIF NWE	320	468	400	538	382	431	440	413	386	461	(16.3%)
Jet fuel	342	565	437	603	437	503	484	439	425	526	(19.2%)
Gasoil	310	519	410	574	409	480	453	405	396	493	(19.7%)
Fuel oil	147	292	215	338	249	253	288	202	225	270	(16.7%)
Liquefied petroleum gas	232	316	225	364	326	352	403	367	299	350	(14.6%)
Export duties, USD per ton ⁽⁶⁾											
Crude oil, stable gas condensate	54.9	129.6	67.2	130.6	88.7	128.5	91.7	92.3	75.6	120.3	(37.2%)
Liquefied petroleum gas	0.0	16.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	4.0	n/a
Naphtha	39.0	110.1	47.6	110.9	62.9	109.2	65.0	78.4	53.6	102.2	(47.6%)
Jet fuel	22.0	62.1	26.8	62.6	35.4	61.6	36.6	44.3	30.2	57.7	(47.7%)
Gasoil	22.0	62.1	26.8	62.6	35.4	61.6	36.6	44.3	30.2	57.7	(47.7%)
Fuel oil	45.0	98.5	55.0	99.2	72.7	97.6	75.1	70.1	62.0	91.3	(32.1%)

⁽²⁾ Based on Brent (dtd) and Russian Urals CIF Rotterdam spot assessments prices as provided by Platts.

⁽³⁾ Export duties per barrel were calculated based on export duties per ton divided by the coefficient 7.3.

⁽⁴⁾ Based on Naphtha C+F (cost plus freight) Japan, Naphtha CIF NWE, Jet CIF NWE, Gasoil 0.1% CIF NWE, Fuel Oil 1.0% CIF NWE prices provided by Platts.

⁽⁵⁾ Based on spot prices for propane-butane mix at the Belarusian-Polish border (DAF, Brest) as provided by Argus.

⁽⁶⁾ Export duties are determined by the Russian Federation government in US dollars and are paid in Russian roubles (see "Our tax burden and obligatory payments" below).

CERTAIN FACTORS AFFECTING OUR RESULTS OF OPERATIONS**Current economic conditions**

Since 2014, the Russian economy has experienced weakening macro-economic conditions which became especially apparent during the fourth quarter of 2014 with the severe devaluation of the Russian rouble, the contraction of the Country's gross domestic product, a significant increase in the Central Bank's lending rates, increased inflation and other factors. The domestic economic situation was further exasperated by the rapid commodity price decline in global oil markets. As a result, in January and February 2015, both Standard & Poor's (S&P) and Moody's downgraded the Russian sovereign rating to below investment rating status as well as made the corresponding downward adjustments to Russian issuers, including NOVATEK. We strongly disagree with such assessment of our credit rating because our operating results and cash flow generating capabilities to support our liquidity position remain strong.

In 2015 and 2016, the Central Bank's lending rates gradually decreased, whereas the Russian rouble exchange rates relative to world currencies and benchmark commodity prices in international markets remained volatile. Commodity price volatility continues to exert significant influence on financial and operations results in the global oil and gas industry. Our financial results are obviously impacted by these global developments as our export sales are linked to the specific underlying benchmark commodity prices but we believe our business model, representing one of the lowest cost producers in the world, insulates us from severe financial and operational stress. In each quarter of 2015 and 2016, the Group achieved strong operating results and remained free cash flow positive. In November 2016, S&P restored our credit rating to investment grade after the downgrade in January 2015.

Management continues to closely monitor the economic and political environment in Russia and abroad, including the domestic and international capital markets, to determine if any further corrective and/or preventive measures are required to sustain and grow our business. We also closely monitor the present commodity price environment and its impact on our business operations. We do not expect any asset impairments or write-offs resulting from a lower commodity price environment.

We conduct regular reviews of our capital expenditure program and existing debt obligations. In our opinion, the Group's financial position is stable and expected operating cash flows are sufficient to service and repay our debt, as well as to execute our planned capital expenditure programs.

Political events in Ukraine in the beginning of 2014 have prompted a negative reaction by the world community, including economic sanctions levied by the United States of America, Canada and the European Union against certain Russian individuals and legal entities. In July 2014, NOVATEK was included on the OFAC's Sectoral Sanctions Identification List (the "List"), which imposed sanctions that prohibit individuals or legal entities registered or working on the territory of the United States from providing new credit facilities to the Group for longer than 90 days. Despite the inclusion on the List, the Group may conduct any other activities, including financial transactions, with U.S. investors and partners. NOVATEK was included on the List even though the Group does not conduct any business activities in Ukraine, nor does it have any impact on the political and economic processes taking place in this country. Management has assessed the impact of the sanctions described above on the Group's activities taking into consideration the current state of the world economy, the condition of domestic and international capital markets, the Group's business, and long-term projects with foreign partners. We have concluded that the inclusion on the List does not significantly impede the Group's operations and business activities in any jurisdiction, nor does it affect the Group's assets and exchange listed shares and debt, and does not have a material effect on the Group's financial position.

We together with our international partners are undertaking all necessary actions to implement the joint investment projects on time as planned, including, but not limited to, attracting financing from domestic and non-US capital markets.

Natural gas prices

The Group's natural gas prices on the domestic market are strongly influenced by the prices set by a federal executive agency of the Russian Federation that carries out governmental regulation of prices and tariffs for products and services of natural monopolies in energy, utilities and transportation (the "Regulator"), as well as present market conditions. During the first half of 2015, the Federal Tariffs Service ("FTS") fulfilled the Regulator's role. In July 2015, a Decree of the President of the Russian Federation became effective abolishing the FTS and transferring its functions to the Federal Anti-Monopoly Service.

In 2015, wholesale natural gas prices for sales to all customer categories (excluding residential customers) on the domestic market were increased by the Regulator effective 1 July by 7.5% and remained unchanged through the end of 2016.

In November 2016, the Ministry of Economic Development of the Russian Federation published the "Forecast of Socio-economic Development of the Russian Federation for 2017 and planned period 2018 and 2019" stating that wholesale natural gas prices for sales to all customer categories (excluding residential customers) will be increased from 1 July 2017, 2018 and 2019 by an average of 3.9%, 3.4% and 3.1%, respectively. The Russian Federation government continues to discuss various concepts relating to the natural gas industry development, including natural gas prices and transportation tariffs growth rates on the domestic market.

The specific terms for delivery of natural gas affect our average realized prices. The majority of our natural gas volumes are sold directly to end-customers in the regions of natural gas consumption, so transportation tariff to the end customer's location is included in the contract sales price. The remaining volumes of natural gas are sold "ex-field" to wholesale gas traders, in which case the buyer is responsible for the payment of further gas transportation tariff. Sales to wholesale gas traders allow us to diversify our natural gas sales without incurring additional commercial expenses.

We deliver natural gas to residential customers in the Chelyabinsk and Kostroma regions of the Russian Federation at regulated prices through our subsidiaries OOO NOVATEK-Chelyabinsk and OOO NOVATEK-Kostroma, respectively. We disclose such residential sales within our end-customers category.

In addition, we periodically sell natural gas at the Saint-Petersburg International Mercantile Exchange based on market conditions. We disclose such sales within our sales to end-customers category.

In 2016, our average natural gas price on end-customers sales was relatively flat due to an increase in the proportion of sales to our end-customers located closer to our production fields in 2016 as compared to 2015, on one hand, and an increase in wholesale natural gas prices by 7.5% effective 1 July 2015, on the other hand. The change in the sales geography also reduced our average transportation expense per mcm by 4.0%, despite an average 2.0% increase in the natural gas regulated transportation tariff effective 1 July 2015 (see "Transportation tariffs" below). As a result, the average natural gas price on end-customers sales excluding transportation expenses increased by 2.7%.

The following table shows our average realized natural gas sales prices (excluding VAT):

<i>Russian roubles per mcm</i>	Year ended 31 December:		Change %
	2016	2015	
Average natural gas price to end-customers ⁽¹⁾	3,677	3,678	(0.0%)
Average natural gas transportation expense for sales to end-customers	(1,423)	(1,483)	(4.0%)
Average natural gas price on end-customer sales excluding transportation expense	2,255	2,196	2.7%
Average natural gas price ex-field (wholesale traders)	2,051	1,965	4.4%
Total average natural gas price excluding transportation expense	2,239	2,180	2.7%

⁽¹⁾ Includes cost of transportation.

Stable gas condensate and refined products, crude oil and liquefied petroleum gas prices

Crude oil, stable gas condensate, LPG and oil products prices on international markets have historically been volatile depending on, among other things, the balance between supply and demand fundamentals, the ability and willingness of oil producing countries to sustain or change production levels to meet changes in global demand and potential disruptions in global crude oil supplies due to war, geopolitical developments, terrorist activities or natural disasters.

The actual prices we receive for our liquid hydrocarbons on both the domestic and international markets are dependent on many external factors beyond the control of management. Among many other factors volatile movements in benchmark crude oil and oil products prices can have a positive and/or negative impact on the contract prices we receive for our liquids sales volumes.

In addition, our actual realized net export prices for crude oil, stable gas condensate and its refined products are affected by the so-called "export duty lag effect". This effect is due to the differences between actual crude oil prices for a certain period and crude oil prices based on which export duty rate is calculated for the same period (see "Our tax burden and obligatory payments" below). In periods when crude oil prices are rising, the duty lag effect normally has a positive impact on the Group's financial results, as the export duty rates are set on the basis of lower crude oil prices compared to the actual prices. Conversely, in periods of crude oil prices decline, the export duty rate is calculated based on higher prices compared to the actual prices, which results in a negative financial impact.

Most of our liquid hydrocarbons sales prices on both the international and domestic markets include transportation expenses in accordance with the specific terms of delivery. The remaining portion of our liquids volumes is sold without additional transportation expenses (ex-works sales of liquefied petroleum gas from the Purovsky Plant and the Tobolsk Refining Facilities, as well as certain other types of sales).

We commonly sell our stable gas condensate and refined products, as well as liquefied petroleum gas to the international markets with a premium to the respective international benchmark reference products prices. Our crude oil sold to the international markets is commonly traded with a discount to the benchmark Brent crude oil in case of SILCO grade sales (low-sulfur "Siberian Light Crude Oil") and with a premium to the benchmark Dubai crude oil in case of ESPO grade sales (crude oil delivered by the pipeline "East Siberia – Pacific ocean").

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The following table shows our average realized stable gas condensate and refined products, crude oil and LPG sales prices. Average realized net prices are shown net of VAT, export duties, excise and fuel taxes expense, where applicable:

Russian roubles or US dollars per ton	Year ended 31 December:		Change %
	2016	2015	
Stable gas condensate			
Export contract price, USD per ton	358	394	(9.1%)
Net export price, USD per ton	286	282	1.4%
Net export price, RR per ton	19,430	16,842	15.4%
Domestic price, RR per ton	14,550	14,601	(0.3%)
Naphtha			
Export contract price, USD per ton	424	494	(14.2%)
Net export price, USD per ton	373	390	(4.4%)
Net export price, RR per ton	25,067	23,203	8.0%
Other gas condensate refined products			
Export contract price, USD per ton	377	473	(20.3%)
Net export price, USD per ton	335	401	(16.5%)
Net export price, RR per ton	22,432	24,064	(6.8%)
Domestic price, RR per ton	18,328	19,320	(5.1%)
Crude oil			
Export contract price, USD per ton	303	371	(18.3%)
Net export price, USD per ton	229	250	(8.4%)
Net export price, RR per ton	15,084	14,922	1.1%
Domestic price, RR per ton	13,451	12,967	3.7%
LPG			
Export contract price, USD per ton ⁽¹⁾	488	506	(3.6%)
Net export price, USD per ton ⁽¹⁾	349	385	(9.4%)
Net export price, RR per ton	23,407	23,457	(0.2%)
Domestic price, RR per ton	8,693	11,707	(25.7%)

⁽¹⁾ For operations in Polish zloty price in US dollars was translated from Russian roubles using the average exchange rate for the period.

Crude oil, stable gas condensate and gas condensate refined products

In 2016, our average realized export contract prices for stable gas condensate, gas condensate refined products and crude oil decreased compared to 2015 primarily due to decreases in the underlying respective product prices on the international markets (see "Selected macro-economic data" above). Our weighted-average stable gas condensate export contract price decreased to a lesser extent as a result of uneven distribution of sales volumes within periods, changes in the geography of shipments and significant volatility of benchmark crude oil prices on international markets.

A significant decrease in average export duties for liquid hydrocarbons sales (see "Selected macro-economic data" above), as well as an average 10.0% appreciation of the US dollar relative to the Russian rouble in 2016 compared to 2015 had a positive impact on our average realized net export prices. As a result, our average realized net export prices in Russian roubles terms increased for stable gas condensate, naphtha and crude oil. Our average realized net export prices for other gas condensate refined products in Russian rouble terms decreased but were also in line with the benchmark crude oil prices movements for these products net of the respective export duties.

In 2016, our average realized domestic prices for crude oil, stable gas condensate and its refined products changed marginally compared to 2015 as a result of the respective changes in benchmark crude oil prices excluding export duties in Russian roubles terms, and specifics of pricing mechanism for each particular product on the domestic market (such as time lag of international benchmark crude oil prices and export duty rates used in price calculation, price setting on an individual transaction basis for some deliveries and others).

Liquefied petroleum gas

In 2016, our average realized LPG export contract price decreased compared to 2015 due to a decrease in the underlying benchmark prices for LPG on international markets used in price calculation (see "Selected macro-economic data" above), which was partially offset by changes in sales geography (increase in the share of sales to Poland where the contract price is higher than prices for sales to other countries according to the delivery terms). Our average realized LPG net export price in Russian roubles terms stayed relatively flat as a result of a 10.0% appreciation of the average exchange rate of the US dollar relative to the Russian rouble in 2016 compared to 2015.

In 2016, our average realized LPG domestic price decreased compared to 2015 mainly due to a decrease in the underlying benchmark prices for LPG on international markets and increased transportation tariffs as these figures form the basis for the price setting of some LPG deliveries.

Transportation tariffs*Natural gas*

We transport our natural gas through our own pipelines into the Unified Gas Supply System ("UGSS"), which is owned and operated by PAO Gazprom, a Russian Federation government controlled monopoly. Transportation tariffs charged to independent producers for the use of the Gas Transmission System ("GTS"), as part of the UGSS, are set by the Regulator (see "Terms and abbreviations" below).

In accordance with the existing methodology of calculating transportation tariffs for natural gas produced in the Russian Federation for shipments to consumers located within the customs territory of the Russian Federation and the member states of the Customs Union Agreement (Belarus, Kazakhstan, Kyrgyzstan and Tajikistan), the transportation tariff consists of two parts: a rate for the utilization of the trunk pipeline and a transportation rate per mcm per 100 kilometers (km). The rate for utilization of the trunk pipeline is based on an "input/output" function, which is determined by where natural gas enters and exits the trunk pipeline and includes a constant rate for end-customers using Gazprom's gas distribution systems. The constant rate is deducted from the utilization rate for end-customers using non-Gazprom gas distribution systems.

In the first half of 2015, the transportation rate was set at RR 12.79 per mcm per 100 km (excluding VAT), and the rate for utilization of the trunk pipeline was set in the range from RR 57.18 to RR 2,048.11 per mcm (excluding VAT).

Effective 1 July 2015, the average tariff for natural gas transportation through the trunk pipeline was increased by 2.0% and remained unchanged through the end of 2016. The transportation rate amounted to RR 13.04 per mcm per 100 km (excluding VAT), and the rate for utilization of the trunk pipeline was set in the range from RR 62.57 to RR 2,014.16 per mcm (excluding VAT).

According to the Forecast of the Ministry of Economic Development of the Russian Federation published in November 2016, the increase in tariffs for natural gas transportation through the trunk pipeline in 2017 to 2019 will not exceed the growth rate for wholesale natural gas prices (see "Natural gas prices" above). The Russian Federation government continues to discuss various concepts relating to the natural gas industry development, including natural gas prices and transportation tariffs growth on the domestic market.

Stable gas condensate and LPG by rail

We transport stable gas condensate and LPG (excluding volumes sold ex-works from the Purovsky Plant and the Tobolsk Refining Facilities) by rail owned by Russia's state-owned monopoly railway operator – OAO Russian Railways ("RZD").

The railroad transportation tariffs are set by the Regulator and vary depending on the type of a product, direction and the length of the transport route. In addition, the Regulator sets the range of railroad tariffs as a percentage of the regulated tariff within which RZD may vary railroad transportation tariffs within the Russian Federation territory based on the type of product, direction and length of the transportation route taking into account current railroad transportation and market conditions.

During 2015, railroad freight transportation tariffs for all types of hydrocarbons did not change. Effective 3 January 2016, railroad freight transportation tariffs for all types of hydrocarbons were increased by 9% relative to the 2015 tariffs and did not change until the end of 2016. In January 2017, the Regulator increased the aforementioned tariffs by 6.1% relative to the 2016 tariffs.

In 2015 and 2016, we applied the discount coefficient of 0.94 to the existing railroad transportation tariffs for stable gas condensate deliveries from the Limbey rail station to the port of Ust-Luga and to end-customers on the domestic and export (only in 2016) markets. In December 2016, the discount co-efficient was extended until the end of 2017. The discount coefficient is set by the decision of the Management Board of RZD as part of the Strategic Partnership Agreement between the Group and RZD.

Stable gas condensate and refined products by tankers

We deliver part of our stable gas condensate and substantially all stable gas condensate refined products to international markets by chartered tankers via the port of Ust-Luga on the Baltic Sea. The tanker transportation cost is determined by standard shipping terms, the distance to the final port of destination, tanker availability and seasonality of deliveries.

Crude oil

We transport nearly all of our crude oil through the pipeline network owned by PAO Transneft, Russia's state-owned monopoly crude oil pipeline operator. The Regulator sets tariffs for transportation of crude oil through Transneft's pipeline network, which includes transport, dispatch, pumping, loading, charge-discharge, transshipment and other related services. The Regulator sets tariffs for each separate route of the pipeline network, so the overall expense for the transport of crude oil depends on the length of the transport route from the producing fields to the ultimate destination, transportation direction and other factors.

During 2015, crude oil transportation tariffs within the Russian Federation territory through the pipeline network did not change. Effective 1 January 2016, crude oil transportation tariffs were increased by an average of 5.76% relative to the 2015 tariffs and remained unchanged until the end of 2016. Effective 1 January 2017, crude oil transportation tariffs were increased by an average of 3.6% compared to 2016 tariffs.

Our tax burden and obligatory payments

We are subject to a wide range of taxes imposed at the federal, regional, and local levels, many of which are based on revenue or volumetric measures. In addition to income tax, significant taxes and obligatory payments to which we are subject include VAT, unified natural resources production tax ("UPT", commonly referred as "MET" – mineral extraction tax), export duties, property tax and social contributions to non-budget funds.

In practice, Russian tax authorities often have their own interpretation of tax laws that rarely favors taxpayers, who have to resort to court proceedings to defend their position against the tax authorities. Differing interpretations of tax regulations exist both among and within government ministries and organizations at the federal, regional and local levels, creating uncertainties and inconsistent enforcement. Tax declarations, together with related documentation such as customs declarations, are subject to review and investigation by a number of authorities, each of which may impose fines, penalties and interest charges. Generally, taxpayers are subject to an inspection of their activities for a period of three calendar years immediately preceding the year in which the audit is conducted. Previous audits do not completely exclude subsequent claims relating to the audited period. In addition, in some instances, new tax regulations may have a retroactive effect.

We have not employed any tax minimization schemes using offshore or domestic tax zones in the Russian Federation.

The tax maneuver in the oil and gas industry

In November 2014, as part of the tax maneuver in the oil and gas industry, a federal law №366-FZ "Concerning introducing changes to the second part of the Tax Code of the Russian Federation and certain legislative acts of the Russian Federation" was adopted which envisages the increase in national budgetary income as a result of the phased (during three years) increases in UPT rates with a simultaneous decrease in excise taxes and export duties (see below).

UPT – natural gas and gas condensate

In accordance with the Tax Code of the Russian Federation, the UPT rates for natural gas and gas condensate are calculated monthly according to a formula based on which the set base UPT rate is multiplied by the base value of a standard fuel equivalent and a coefficient characterizing the difficulty of extracting natural gas and gas condensate from each particular field. In addition, the formula for gas condensate UPT rate is multiplied by an adjusting coefficient, and the UPT rate for natural gas also takes into account a parameter characterizing natural gas transportation costs (the latter was set at zero for 2015 and 2016 and did not affect the UPT rate).

The base UPT rate is set at RR 35 per one thousand cubic meters of extracted natural gas and at RR 42 per one ton of extracted gas condensate. The base value of a standard fuel equivalent is calculated monthly and depends primarily on natural gas prices, Urals crude oil prices and crude oil export duty rate.

A coefficient characterizing the difficulty of extracting natural gas and gas condensate is defined as a minimum value from the coefficients characterizing either the reserves' depletion, the field's geographical location, the deposit's (or reservoir's) depth, assignment of the field to the regional gas supply chain or particular features of certain field deposits development.

In 2015, the adjusting coefficient for gas condensate UPT rate calculation was set at 4.4 and was increased to 5.5, or 25.0%, from 1 January 2016. Effective 1 January 2017, the adjusting coefficient for the Group was set at 6.5 (increased by 18.2% in relation to 2016).

UPT – crude oil

In both reporting periods, the UPT rate for crude oil was calculated as the base UPT rate multiplied by a coefficient characterizing the dynamics of world crude oil prices, and the resulting product was further decreased by a parameter characterizing crude oil production peculiarities. The base crude oil UPT rate in 2015 was set at RR 766 per ton and was increased to RR 857 per ton effective 1 January 2016. Effective 1 January 2017, the base UPT rate was set at RR 919 per ton.

In 2015 and 2016, in accordance with the Tax Code of the Russian Federation, we applied a reduced UPT rate for crude oil produced at our Yurkharovskoye, East-Tarkosalinskoye, Khancheykoye and Yarudeyskoye fields since these fields are located fully or partially to the north of the 65th degree of the northern latitude fully or partially in the YNAO. In 2016, the UPT rate for crude oil produced at the aforementioned fields was calculated using an effective rate of RR 298 per ton (increased by 26.3% compared to 2015) multiplied by a coefficient characterizing the dynamics of world crude oil prices. From 1 January 2017, the effective rate was set at RR 360 per ton. In November 2016, amendments were made to the Tax Code of the Russian Federation that envisage additional increase in the overall crude oil UPT rates calculated using a formula described above in 2017 to 2019 by RR 306, RR 357 and RR 428 per ton, respectively.

Export duties and excise taxes

According to the Law of the Russian Federation "On Customs Tariff" we are subject to export duties on our exports of liquid hydrocarbons (stable gas condensate and refined products, LPG and crude oil). Formulas for export duty rates calculation are set by the Russian Federation government. Based on the set formulas the Ministry of Economic Development calculates and publishes export duty rates on a monthly basis (see "Selected macro-economic data" above).

The export duty rate for stable gas condensate and crude oil for the next calendar month is calculated based on the average Urals crude oil price for the period from the 15th calendar day in the previous month to the 14th calendar day of the current month. In 2015, the calculation of the export duty rate in US dollars per ton when the average Urals crude oil price is more than USD 182.5 per ton (or USD 25 per barrel) was set as follows: USD 29.2 plus 42% of the difference between the average Urals crude oil price and USD 182.5 per ton. As part of the tax maneuver in the oil and gas industry (see above), effective 1 January 2016, the set percentage should have been decreased to 36%. However, in order to increase state budget income in 2016 in the anticipation of a lower crude oil price environment, in November 2015, the Russian Federation government made a decision not to adjust the formula for crude oil export duty rate calculation in 2016 and to keep a set percentage at the 2015 level of 42%. Effective 1 January 2017, the set percentage was reduced to 30%.

The export duty rates for oil products is calculated based on the export duty rate for crude oil which is adjusted by a coefficient set for each category of oil products. The export duty rates for our exported gas condensate refined products as a percentage of the crude oil export duty rate are presented below:

<i>% from the crude oil export duty rate</i>	2015	2016	2017 and further
Naphtha	85%	71%	55%
Jet fuel	48%	40%	30%
Gasoil	48%	40%	30%
Fuel oil	76%	82%	100%

The phased decrease in export duty rates for oil products (except fuel oil) is also implemented as part of the tax maneuver in the oil industry with a simultaneous increase in the UPT rates for gas condensate and crude oil (see above).

The export duty rate for LPG for the next calendar month is calculated based on the average LPG price at the Polish border (DAF, Brest) for the period from the 15th calendar day in the previous month to the 14th calendar day of the current month. The formula for LPG export duty rate calculation is presented in the table below:

<i>Average LPG price, USD per ton (P)</i>	Formula for export duty rate calculation
less 490 (inclusive)	Zero rate
between 490 and 640 (inclusive)	$0.5 \times (P - 490)$
between 640 and 740 (inclusive)	$75 + 0.6 \times (P - 640)$
above 740	$135 + 0.7 \times (P - 740)$

As the average LPG price for the export duty rate calculation was below USD 490 per ton, in 2015 and 2016 (except for January 2015), we applied a zero export duty rate in respect of our LPG export sales.

In accordance with the Tax Code of the Russian Federation, producers of excisable goods (petrol, diesel fuel, medium distillates and others) that sell those goods on the domestic market are subject to excise tax payments. The Group does not sell excisable goods of own production on the domestic market and, therefore, does not pay excise taxes in Russia.

Most of our LPG sales in Poland are subject to excise and fuel taxes in accordance with the local legislation. The amount of excise and fuel tax payments depends on the volume of excisable goods sold and the respective tax rates (the excise and fuel tax rates in 2015 and 2016 did not change and amounted to 670 and 159.71 Polish zloty per ton, respectively).

Social contributions

In 2015 and 2016, the rates for social contributions to the Pension Fund of the Russian Federation, the Federal Compulsory Medical Insurance Fund and the Social Insurance Fund of the Russian Federation paid by the employer on behalf of employees did not change and were set at 22.0%, 5.1% and 2.9%, respectively (cumulatively 30.0%).

The employer applies the aforementioned rates for social contributions to the Pension Fund of the Russian Federation and the Social Insurance Fund of the Russian Federation until the annual income of an employee exceeds the maximum taxable base set by the Russian Federation government. For the portion of the annual income exceeding the maximum base the reduced rates are applied: 10.0% for the Pension Fund of the Russian Federation and nil for the Social Insurance Fund of the Russian Federation.

The rate for social contributions to the Federal Compulsory Medical Insurance Fund does not vary with the employee's annual income.

The table below provides for the rates and maximum taxable bases set by the Russian Federation government for social contributions in 2015, 2016 and 2017:

	2015		2016		2017	
	Base, RR thousand	Rate, %	Base, RR thousand	Rate, %	Base, RR thousand	Rate, %
Pension Fund of the Russian Federation	less 711 above 711	22.0% 10.0%	less 796 above 796	22.0% 10.0%	less 876 above 876	22.0% 10.0%
Federal Compulsory Medical Insurance Fund	No limit	5.1%	No limit	5.1%	No limit	5.1%
Social Insurance Fund of the Russian Federation	less 670 above 670	2.9% 0.0%	less 718 above 718	2.9% 0.0%	less 755 above 755	2.9% 0.0%

OIL AND GAS RESERVES

We do not file with the Securities and Exchange Commission ("SEC") nor are obliged to report our reserves in compliance with these standards. However, we have consistently disclosed proved oil and gas reserves as unaudited supplemental information in the Group's IFRS audited consolidated financial statements. The Group's total proved reserves, comprised of proved developed and proved undeveloped reserves, as of 31 December 2016 and 2015, are provided using the SEC reserves reporting classification. We also provide additional information about our hydrocarbon reserves based on the widely-industry accepted PRMS reserves reporting classification, which in addition to total proved reserves discloses information on our probable and possible reserves.

The Group's reserves are located in the Russian Federation, primarily in the Yamal-Nenets Autonomous Region (Western Siberia), thereby representing one geographical area.

The Group's oil and gas estimation and reporting process involves an annual independent external appraisal, as well as internal technical appraisals of reserves. The internal technical appraisals of reserves are performed by the Group's qualified technical staff working directly with the oil and gas reserves and are periodically updated during the year based on evaluations of new wells, performance reviews, new technical information and other studies.

The annual independent external appraisal of our reserves is performed by independent petroleum engineers, DeGolyer and MacNaughton ("D&M"). The Group provides D&M annually with engineering, geological and geophysical data, actual production histories and other information necessary for reserves appraisal. The method or combination of methods used in the analysis of each reservoir is tempered by experience with similar reservoirs, stages of development, quality and completeness of basic data, and production history. Our reserves estimates were prepared using standard geological and engineering methods generally accepted in the oil and gas industry. The Group and D&M's technical staffs meet to review and discuss the information provided, and upon completion of the process, senior management reviews and approves the final reserves estimates issued by D&M.

The Reserves Management and Assessment Group ("RMAG") is comprised of qualified technical staff from various departments – geological and geophysical, gas and liquids commercial operations, engineering and capital construction, production, long-term financing planning and includes representatives from the Group's subsidiaries, which are the principal holders of the mineral licenses for geological research works, exploration and production of hydrocarbons. The person responsible for overseeing the work of the RMAG is a member of the Management Board.

The approval of the final reserve estimates is the sole responsibility of the Group's senior management.

The information below provides for our oil and gas reserves under SEC and PRMS reserve classifications including 100% of reserves attributable to all consolidated subsidiaries (whether or not wholly owned), as well as our proportionate share of reserves in companies accounted for by the equity method based on our equity ownership interest.

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The table below provides proved oil and gas reserves under SEC reserve classification in Metric units and on a total barrel of oil equivalent basis:

	As of and for the years ended 31 December:		Change %
	2016	2015	
Natural gas, billions of cubic meters	1,755	1,775	(1.1%)
Subsidiaries	1,029	1,034	(0.5%)
Share in joint ventures	726	741	(2.0%)
Liquids, millions of metric tons	152	143	6.3%
Subsidiaries	73	68	7.4%
Share in joint ventures	79	75	5.3%
Combined reserves, millions of boe	12,775	12,817	(0.3%)
Production, millions of boe	537	522	3.0%
Disposals ⁽¹⁾ , millions of boe	351	74	n/a
Reserves replacement ratio ⁽²⁾, %	92%	133%	
Normalized reserves replacement ratio ⁽³⁾, %	168%	148%	

⁽¹⁾ Represent reserves attributable to the disposal of a 9.9% participation interest in Yamal LNG in March 2016 and to the disposal of a 1.6% effective ownership interest in SeverEnergiya in August 2015.

⁽²⁾ The reserves replacement ratio is calculated as the difference between the reserves at the end of the year and the reserves at the beginning of the year plus production for the year and dividing the sum by production for the year.

⁽³⁾ Excluding the effect of the disposal of a 9.9% participation interest in Yamal LNG in March 2016 and the disposal of a 1.6% effective ownership interest in SeverEnergiya in August 2015.

Excluding the effect from the disposal of a 9.9% participation interest in Yamal LNG, our total proved reserves under SEC reserve classification increased by 2.8% and we effectively replaced 168% of our production as calculated under the normalized reserves replacement ratio. Additions to our natural gas proved reserves were primarily due to revisions of previous estimates at our Salmanovskoye (Utrenneye) field and at the South-Tambayskoye field of our joint venture Yamal LNG, as well as reserves added due to successful exploration works at our Kharbeykoye and Dorogovskoye fields discovered in June 2013 and August 2014, respectively. Additions to our liquid hydrocarbons proved reserves mainly related to revisions of previous estimates and extensions of the reserves at our Yarudeyskoye and Salmanovskoye (Utrenneye) fields. The launch of additional production facilities at our subsidiaries and joint ventures during 2015 allowed us to increase overall production of natural gas and liquid hydrocarbons in 2016 by 15 million boe, or 3.0% (see "Recent developments" above).

The following table provides for the Group's PRMS proved, probable and possible reserves in Metric units and on a total barrel of oil equivalent basis:

	Natural gas, billions of cubic meters		Liquid hydrocarbons, millions of metric tons		Combined reserves, millions of boe	
	31 December 2016	31 December 2015 ⁽¹⁾	31 December 2016	31 December 2015 ⁽¹⁾	31 December 2016	31 December 2015 ⁽¹⁾
Proved reserves	1,987	2,118	181	177	14,530	15,344
Probable reserves	1,080	1,034	138	121	8,226	7,773
Proved and probable	3,067	3,152	319	298	22,756	23,117
Possible reserves	594	662	122	110	4,874	5,230
Proved, probable and possible	3,661	3,814	441	408	27,630	28,347

⁽¹⁾ At 31 December 2015, the Group's share in reserves of joint ventures included reserves attributable to the 9.9% interest in Yamal LNG classified as held for sale (the transaction was completed in March 2016).

As we continue to invest capital into the development of our fields, we anticipate that we will increase our resource base as well as migrate reserves among the reserve categories.

The below table contains information about reserve to production ratios as of 31 December 2016 and 2015 under both reserves reporting methodologies:

<i>Number of years</i>	SEC		PRMS	
	At 31 December: 2016	2015	At 31 December: 2016	2015
Total proved reserves to production	24	25	27	29
Total proved and probable reserves to production	-	-	42	44
Total proved, probable and possible reserves to production	-	-	51	54

OPERATIONAL HIGHLIGHTS

Oil and Gas Production Costs

Oil and gas production costs are derived from our results of operations for oil and gas producing activities as reported in the "Unaudited Supplemental Oil and Gas Disclosures" in our consolidated financial statements and relate to the fields of our consolidated subsidiaries. Oil and gas production costs do not include general corporate overheads or their associated tax effects. The following tables set forth certain operating information with respect to our oil and gas production costs during the years presented in millions of Russian roubles and on a barrel of oil equivalent (boe) basis in Russian roubles and US dollars:

<i>millions of Russian roubles</i>	Year ended 31 December:		Change
	2016	2015	%
Production costs:			
Lifting costs	13,865	10,705	29.5%
Taxes other than income tax	43,844	36,296	20.8%
Transportation expenses	76,356	83,574	(8.6%)
Total production costs before DDA	134,065	130,575	2.7%
Depreciation, depletion and amortization ("DDA")	32,049	17,522	82.9%
Total production costs	166,114	148,097	12.2%
<i>RR per boe</i>	Year ended 31 December:		Change
	2016	2015	%
Production costs:			
Lifting costs	38.4	30.1	27.6%
Taxes other than income tax	121.4	102.1	18.9%
Transportation expenses	211.3	235.1	(10.1%)
Total production costs before DDA	371.1	367.3	1.0%
Depreciation, depletion and amortization	88.7	49.3	79.9%
Total production costs	459.8	416.6	10.4%
<i>USD per boe ⁽¹⁾</i>	Year ended 31 December:		Change
	2016	2015	%
Production costs:			
Lifting costs	0.57	0.49	16.3%
Taxes other than income tax	1.81	1.67	8.4%
Transportation expenses	3.16	3.87	(18.3%)
Total production costs before DDA	5.54	6.03	(8.1%)
Depreciation, depletion and amortization	1.32	0.80	65.0%
Total production costs	6.86	6.83	0.4%

⁽¹⁾ Production costs in US dollars per boe were translated from Russian roubles per boe using the average exchange rate for the period (see "Selected macro-economic data" above).

Oil and gas production costs represent the amounts directly related to the extraction of natural gas, gas condensate and crude oil from the reservoir and other related costs; including lifting costs, taxes other than income tax (unified natural resources production tax, property tax and other taxes), insurance expenses and shipping, transportation and handling costs to end-customers. The average production cost on a barrel of oil equivalent basis is calculated by dividing the applicable costs by the respective barrel of oil equivalent of our hydrocarbons produced during the year. Natural gas, gas condensate and crude oil volumes produced at our fields are converted to a barrel of oil equivalent based on the relative energy content of each fields' hydrocarbons.

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Our lifting costs, as presented in the tables above, differ from lifting costs as reflected in the "Unaudited Supplemental Oil and Gas Disclosures", in that the lifting costs as presented in the Group's IFRS consolidated financial statements include changes in balances of natural gas and liquid hydrocarbons to more appropriately match costs incurred to revenues under the IFRS matching principles. A reconciliation of lifting costs as reflected in the "Unaudited Supplemental Oil and Gas Disclosures" is set forth below:

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2016	2015	
Lifting costs presented in "Oil and Gas Production Costs" above	13,865	10,705	29.5%
Change in balances of natural gas and hydrocarbon liquids stated at cost in the Group's Consolidated Statement of Financial Position	368	(603)	n/a
Lifting costs per "Unaudited Supplemental Oil and Gas Disclosures"	14,233	10,102	40.9%

Hydrocarbon production and sales volumes

In 2016, our total natural gas sales volumes increased by 2,244 mmcm, or 3.6%, as a result of sales of additional natural gas volumes to our end-customers and wholesale traders, as well as restoring sales to one of our major customers who did not take full contracted volumes in 2015 due to technical reasons. Natural gas volumes produced at mature fields of our subsidiaries decreased, but were offset to a significant extent by an increase in the production of our joint ventures.

In 2016, our liquids sales volumes increased significantly by 3,962 thousand tons, or 30.7%, primarily due to the commencement of crude oil commercial production at the Yarudeyskoye field in December 2015.

Natural gas production volumes

In 2016, our total natural gas production (including our proportionate share in the production of joint ventures) decreased by 1,802 mmcm, or 2.7%, to 66,103 mmcm from 67,905 mmcm in 2015.

<i>millions of cubic meters</i>	Year ended 31 December:		Change %
	2016	2015	
Production by subsidiaries from:			
Yurkharovskoye field	33,766	35,979	(6.2%)
East-Tarkosalinskoye field	8,015	9,075	(11.7%)
Khancheyevskoye field	2,473	2,510	(1.5%)
Other fields	1,981	1,608	23.2%
Total natural gas production by subsidiaries	46,235	49,172	(6.0%)
Group's proportionate share in the production of joint ventures:			
SeverEnergiya (Arcticgas)	13,682	12,624	8.4%
Nortgas	5,023	5,395	(6.9%)
Terneftegas	1,163	714	62.9%
Total Group's proportionate share in the natural gas production of joint ventures	19,868	18,733	6.1%
Total natural gas production including proportionate share in the production of joint ventures	66,103	67,905	(2.7%)

In 2016, total natural gas volumes produced by our subsidiaries decreased by 2,937 mmcm, or 6.0%, to 46,235 mmcm from 49,172 mmcm in 2015 due to natural declines in the reservoir pressure at the current gas producing horizons at our mature fields (Yurkharovskoye, East-Tarkosalinskoye and Khancheyevskoye). The decrease was partially offset by the launch of the Yarudeyskoye field in December 2015.

In 2016, our proportionate share in the production of our joint ventures increased by 1,135 mmcm, or 6.1%, to 19,868 mmcm from 18,733 mmcm in 2015 primarily as a result of the production growth in SeverEnergiya. The production of SeverEnergiya increased due to reaching the nameplate production capacity of the second phase of the Urengoyevskoye field in February 2015, as well as the launch of the Yaro-Yakhinskoye field in April 2015, the nameplate production capacity of which was reached in June 2015. In addition, effective May 2015, our joint venture Terneftegas commenced production at the Termokarstovoye field and reached the nameplate production capacity in June 2015. The production at the mature field of Nortgas decreased due to natural declines in the reservoir pressure at the current gas producing horizons.

Natural gas sales volumes

In 2016, our total natural gas sales volumes increased by 2,244 mmcm, or 3.6%, to 64,709 mmcm from 62,465 mmcm in 2015.

<i>millions of cubic meters</i>	Year ended 31 December:		Change %
	2016	2015	
Production by subsidiaries	46,235	49,172	(6.0%)
Purchases from the Group's joint ventures	10,058	7,152	40.6%
Other purchases	8,108	6,626	22.4%
Total production and purchases	64,401	62,950	2.3%
Own usage ⁽¹⁾	(185)	(207)	(10.6%)
Decrease (increase) in GTS, UGSF and own pipeline infrastructure	493	(278)	n/a
Total natural gas sales volumes	64,709	62,465	3.6%
<i>Sold to end-customers</i>	<i>59,646</i>	<i>58,054</i>	<i>2.7%</i>
<i>Sold ex-field</i>	<i>5,063</i>	<i>4,411</i>	<i>14.8%</i>

⁽¹⁾ Own usage associated primarily with the maintaining of refining process at the Purovsky Plant, as well as heat and electric energy generation in some of our subsidiaries.

In 2016, natural gas purchases from our joint ventures increased by 2,906 mmcm, or 40.6%, to 10,058 mmcm from 7,152 mmcm in 2015 primarily due to an increase in purchases from SeverEnergia (through its wholly owned subsidiary, OAO Arcticgas) and the commencement of purchases from Terneftegas as a result of the launch of the Termokarstovoye field in May 2015, the nameplate production capacity of which was reached in June 2015.

Other natural gas purchases increased by 1,482 mmcm, or 22.4%, to 8,108 mmcm from 6,626 mmcm in 2015, and are included in our natural gas volumes for sale, which allows us to coordinate sales across geographic regions as well as to optimize end-customers portfolios.

As of 31 December 2016, our natural gas inventory balance in the GTS, the UGSF and our own pipeline infrastructure aggregated 834 mmcm and decreased by 493 mmcm during the year as compared to an increase by 278 mmcm in 2015.

Liquids production volumes

In 2016, our total liquids production (including our proportionate share in the production of joint ventures) increased by 3,347 thousand tons, or 36.8%, to 12,441 thousand tons from 9,094 thousand tons in 2015.

thousands of tons	Year ended 31 December:		Change %
	2016	2015	
Production by subsidiaries from:			
Yarudeyskoye field	3,556	184	n/a
Yurkharovskoye field	1,813	2,126	(14.7%)
East-Tarkosalinskoye field	1,354	1,365	(0.8%)
Khancheyskoye field	353	392	(9.9%)
Other fields	118	131	(9.9%)
Total liquids production by subsidiaries			
	7,194	4,198	71.4%
<i>including crude oil</i>	<i>4,784</i>	<i>1,434</i>	<i>233.6%</i>
<i>including gas condensate</i>	<i>2,410</i>	<i>2,764</i>	<i>(12.8%)</i>
Group's proportionate share in the production of joint ventures:			
SeverEnergia (Arcticgas)	4,300	4,016	7.1%
Nortgas	519	622	(16.6%)
Terneftegas	428	258	65.9%
Total Group's proportionate share in the liquids production of joint ventures			
	5,247	4,896	7.2%
Total liquids production including proportionate share in the production of joint ventures			
	12,441	9,094	36.8%

In 2016, the volumes of liquids produced by our subsidiaries significantly increased by 2,996 thousand tons, or 71.4%, primarily due to the commencement of crude oil commercial production at the Yarudeyskoye field in December 2015 and reaching the nameplate production capacity by the end of the month (see "Recent developments" above). At the same time gas condensate production decreased due to the natural declines in the concentration of gas condensate at our mature fields (Yurkharovskoye, East-Tarkosalinskoye and Khancheyskoye) as a result of decreasing reservoir pressure at the current gas condensate producing horizons.

In 2016, our proportionate share in liquids production of joint ventures increased by 351 thousand tons, or 7.2%, to 5,247 thousand tons from 4,896 thousand tons in 2015 mainly as a result of production growth at SeverEnergia. The production of SeverEnergia increased due to reaching the nameplate production capacity of the second phases of the Urengoyevskoye field in February 2015, as well as the launch of the Yaro-Yakhinskoye field in April 2015, the nameplate production capacity of which was reached in June 2015. In addition, our joint venture Terneftegas commenced production at the Termokarstovoye field in May 2015 and reached the nameplate production capacity in June 2015. The production at the mature field of Nortgas decreased due to natural declines in the concentration of gas condensate as a result of decreasing reservoir pressure at the current gas condensate producing horizons.

Liquids sales volumes

In 2016, our total liquids sales volumes increased by 3,962 thousand tons, or 30.7%, to 16,850 thousand tons from 12,888 thousand tons in 2015 mainly due to an increase in the production of crude oil in our subsidiaries, as well as an increase in gas condensate production of our joint ventures.

<i>thousands of tons</i>	Year ended 31 December:		Change %
	2016	2015	
Production by subsidiaries	7,194	4,198	71.4%
Purchases from the Group's joint ventures	9,809	9,045	8.4%
Other purchases	124	94	31.9%
Total production and purchases	17,127	13,337	28.4%
Losses ⁽¹⁾ and own usage ⁽²⁾	(284)	(278)	2.2%
Filling the system of processing facilities and pipelines at the Yarudeyskoye field	-	(36)	n/a
Decreases (increases) in liquids inventory balances	7	(135)	n/a
Total liquids sales volumes	16,850	12,888	30.7%
<i>Naphtha export</i>	<i>4,113</i>	<i>4,120</i>	<i>(0.2%)</i>
<i>Other gas condensate refined products export</i>	<i>2,430</i>	<i>2,479</i>	<i>(2.0%)</i>
<i>Other gas condensate refined products domestic</i>	<i>119</i>	<i>94</i>	<i>26.6%</i>
<i>Subtotal gas condensate refined products</i>	<i>6,662</i>	<i>6,693</i>	<i>(0.5%)</i>
<i>Crude oil export</i>	<i>1,472</i>	<i>377</i>	<i>290.5%</i>
<i>Crude oil domestic</i>	<i>3,178</i>	<i>713</i>	<i>345.7%</i>
<i>Subtotal crude oil</i>	<i>4,650</i>	<i>1,090</i>	<i>326.6%</i>
<i>Stable gas condensate export</i>	<i>1,305</i>	<i>1,477</i>	<i>(11.6%)</i>
<i>Stable gas condensate domestic</i>	<i>1,507</i>	<i>1,309</i>	<i>15.1%</i>
<i>Subtotal stable gas condensate</i>	<i>2,812</i>	<i>2,786</i>	<i>0.9%</i>
<i>LPG export</i>	<i>549</i>	<i>551</i>	<i>(0.4%)</i>
<i>LPG domestic</i>	<i>2,164</i>	<i>1,755</i>	<i>23.3%</i>
<i>Subtotal LPG</i>	<i>2,713</i>	<i>2,306</i>	<i>17.6%</i>
<i>Other oil products domestic</i>	<i>13</i>	<i>13</i>	<i>0.0%</i>
<i>Subtotal other oil products</i>	<i>13</i>	<i>13</i>	<i>0.0%</i>

⁽¹⁾ Losses associated with processing at the Purovsky Plant, the Ust-Luga Complex and the Tobolsk Refining Facilities, as well as during railroad, trunk pipeline and tanker transportation.

⁽²⁾ Own usage associated primarily with the maintaining of refining process at the Ust-Luga Complex, as well as bunkering of chartered tankers.

In 2016, our purchases of liquid hydrocarbons from joint ventures increased by 764 thousand tons, or 8.4%, due to an increase in purchases of gas condensate from SeverEnergiya and Terneftegas resulting from the launch of production facilities (see "Liquids production volumes" above).

Sales volumes of jet fuel, gasoil and fuel oil received from the processing of stable gas condensate are disclosed in lines "Other gas condensate refined products export" and "Other gas condensate refined products domestic".

In 2016, our liquids inventory balances slightly decreased by seven thousand tons to 903 thousand tons as of 31 December 2016 as compared to an increase in inventory balances by 171 thousand tons to 910 thousand tons in 2015. Our liquids inventory balances may vary period-to-period depending on shipping schedules and final destinations of stable gas condensate and its refined products shipments (see "Changes in natural gas, liquid hydrocarbons and work-in-progress" below).

PAO NOVATEK**Management's Discussion and Analysis of Financial Condition and Results of Operations
for the years ended 31 December 2016 and 2015****RESULTS OF OPERATIONS FOR THE YEAR ENDED 31 DECEMBER 2016
COMPARED TO THE YEAR ENDED 31 DECEMBER 2015**

The following table and discussion is a summary of our consolidated results of operations for the years ended 31 December 2016 and 2015. Each line item is also shown as a percentage of our total revenues.

<i>millions of Russian roubles</i>	Year ended 31 December:			
	2016	% of total revenues	2015	% of total revenues
Total revenues ⁽¹⁾	537,472	100.0%	475,325	100.0%
<i>including:</i>				
natural gas sales	229,716	42.7%	222,180	46.7%
liquids' sales	304,141	56.6%	249,827	52.6%
Operating expenses	(385,499)	(71.7%)	(335,042)	(70.5%)
Other operating income (loss)	221	0.0%	(542)	(0.1%)
Profit from operations before disposals of interests in joint ventures	152,194	28.3%	139,741	29.4%
Net gain on disposal of interests in joint ventures	73,072	13.6%	989	0.2%
Profit from operations	225,266	41.9%	140,730	29.6%
Finance income (expense)	(7,941)	(1.5%)	(16,182)	(3.4%)
Share of profit (loss) of joint ventures, net of income tax	90,839	16.9%	(31,607)	(6.6%)
Profit before income tax	308,164	57.3%	92,941	19.6%
Total income tax expense	(43,091)	(8.0%)	(18,822)	(4.0%)
Profit	265,073	49.3%	74,119	15.6%
Less: profit (loss) attributable to non-controlling interest	(7,278)	(1.3%)	277	0.1%
Profit attributable to shareholders of PAO NOVATEK	257,795	48.0%	74,396	15.7%
Normalized profit attributable to shareholders of PAO NOVATEK, excluding the effect of foreign exchange gains (losses)	133,759	24.9%	132,509	27.9%

⁽¹⁾ Net of VAT, export and import duties, excise and fuel taxes expense, where applicable.

Total revenues

The following table sets forth our sales (excluding VAT, export duties, excise and fuel taxes expense, where applicable) for the years ended 31 December 2016 and 2015:

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %	Change ⁽¹⁾		
	2016	2015		Total	Due to volume ⁽²⁾	Due to price ⁽³⁾
Natural gas sales	229,716	222,180	3.4%	7,536	7,137	399
End-customers	219,333	213,513	2.7%	5,820	5,857	(37)
Ex-field sales	10,383	8,667	19.8%	1,716	1,280	436
Gas condensate refined products sales	159,799	157,066	1.7%	2,733	(154)	2,887
Export – naphtha	103,103	95,588	7.9%	7,515	(150)	7,665
Export – other refined products	54,508	59,667	(8.6%)	(5,159)	(499)	(4,660)
Domestic – other refined products	2,188	1,811	20.8%	377	495	(118)
Crude oil sales	64,952	14,873	336.7%	50,079	48,303	1,776
Export	22,198	5,629	294.4%	16,569	16,332	237
Domestic	42,754	9,244	n/a	33,510	31,971	1,539
Stable gas condensate sales	47,271	43,997	7.4%	3,274	(22)	3,296
Export	25,351	24,887	1.9%	464	(2,911)	3,375
Domestic	21,920	19,110	14.7%	2,810	2,889	(79)
Liquefied petroleum gas sales	31,652	33,467	(5.4%)	(1,815)	4,735	(6,550)
Export	12,841	12,924	(0.6%)	(83)	(55)	(28)
Domestic	18,811	20,543	(8.4%)	(1,732)	4,790	(6,522)
Other products sales	467	424	10.1%	43	n/a	n/a
Domestic	467	424	10.1%	43	n/a	n/a
Total oil and gas sales	533,857	472,007	13.1%	61,850	n/a	n/a
Other revenues	3,615	3,318	9.0%	297	n/a	n/a
Total revenues	537,472	475,325	13.1%	62,147	n/a	n/a

⁽¹⁾ The figures reflect the impact of sales volumes and average realized prices factors on the change in total revenues from hydrocarbons sales in millions of Russian roubles for the respective periods.

⁽²⁾ The amount of the change in total revenues due to sales volumes is calculated for each product and selling destination as a product of the average realized price for the previous reporting period and the change in sales volumes.

⁽³⁾ The amount of the change in total revenues due to average realized prices is calculated for each product and selling destination as a product of the volume sold in the current reporting period and the change in average realized prices.

Natural gas sales

Our revenues from natural gas sales increased by RR 7,536 million, or 3.4%, compared to 2015 due to an increase in volumes sold by 3.6%, while our average sales prices stayed flat. The increase in our total sales volumes was due to sales of additional natural gas volumes to our end-customers and wholesale traders, as well as restoring sales to one of our major customers who did not take full contracted volumes in 2015 due to technical reasons. Our average sales prices changed insignificantly (decreased by 0.2%) due to an increase in the proportion of sales to our end-customers located closer to our production fields in 2016 compared to 2015, as well as an increase from 7.1% to 7.8% in the proportion of natural gas sold to wholesale traders with lower average sales prices compared to end-customer sales, on one hand, and an increase in wholesale natural gas prices by 7.5% effective 1 July 2015, on the other hand (see “Natural gas prices” above).

Gas condensate refined products sales

Gas condensate refined products sales represent revenues from sales of naphtha, jet fuel, gasoil and fuel oil produced from our stable gas condensate at the Ust-Luga Complex.

In 2016, our revenues from sales of gas condensate refined products increased by RR 2,733 million, or 1.7%, as compared to 2015 primarily due to an increase in average realized net export prices for naphtha in Russian roubles terms which was partially offset by a decrease in average realized net export prices for jet fuel, gasoil and fuel oil.

In 2016, our revenues from sales of naphtha increased by RR 7,515 million, or 7.9%, as compared to 2015 due to an increase in average realized net export prices in Russian roubles terms while sales volumes changed insignificantly. In the years ended 31 December 2016 and 2015, we exported 4,113 thousand and 4,120 thousand tons of naphtha, respectively. Nearly all our naphtha volumes were sold to the APR, and the European and North America markets. Our average realized net export price, excluding export duties, increased by RR 1,864 per ton, or 8.0%, to RR 25,067 per ton (CFR, CIF, DES and FOB) from RR 23,203 per ton (CIF, CFR, DES, DAP and FOB) in 2015 (see "Stable gas condensate and refined products, liquefied petroleum gas and crude oil prices" above).

In 2016, our revenues from sales of jet fuel, gasoil and fuel oil on the domestic and export markets decreased by RR 4,782 million, or 7.8%, as compared to 2015 primarily due to a decrease in average realized net export prices in Russian roubles terms. In the years ended 31 December 2016 and 2015, we exported in aggregate 2,430 thousand and 2,479 thousand tons of these products to the European markets, or 95.3% and 96.3% of total sales volumes (on the domestic and export markets), respectively. Our average realized net export price, excluding export duties, decreased by RR 1,632 per ton, or 6.8%, to RR 22,432 per ton (CIF, DES, FOB and DAP) from RR 24,064 per ton (CIF, DES, FOB and DAP) in 2015 (see "Stable gas condensate and refined products, liquefied petroleum gas and crude oil prices" above).

Crude oil sales

In 2016, revenues from crude oil sales increased significantly by RR 50,079 million, or 4.4 times, compared to 2015 due to a significant increase in sales volumes. Our crude oil sales volumes increased by 3,560 thousand tons, or 4.4 times, to 4,650 thousand tons from 1,090 thousand tons in 2015 mainly due to the commencement of crude oil commercial production at the Yarudeyskoye field in December 2015 and reaching the nameplate production capacity by the end of the month.

In 2016, we sold 3,178 thousand tons, or 68.3% of our total crude oil sales volumes, domestically at an average price of RR 13,451 per ton (excluding VAT), representing an increase of RR 484 per ton, or 3.7%, as compared to 2015.

The remaining 1,472 thousand tons, or 31.7% of our total sales volumes, were sold primarily to the APR, and the European and the North America markets at an average net export price of RR 15,084 per ton (FOB, excluding export duties) representing an increase of RR 162 per ton, or 1.1%, as compared to 2015 (see "Stable gas condensate and refined products, liquefied petroleum gas and crude oil prices" above).

Stable gas condensate sales

In 2016, our revenues from sales of stable gas condensate increased by RR 3,274 million, or 7.4%, compared to 2015 primarily due to an increase in average realized net export prices.

In 2016, we sold 1,305 thousand tons of stable gas condensate, or 46.4% of our total sales volumes, compared to 1,477 thousand tons, or 53.0%, in 2015 to the APR and the European markets. Our average realized stable gas condensate net export price, excluding export duties, increased by RR 2,588 per ton, or 15.4%, to RR 19,430 per ton from RR 16,842 per ton (CFR, DAP, CIF and DES in both reporting periods) (see "Stable gas condensate and refined products, liquefied petroleum gas and crude oil prices" above).

In 2016, we sold 1,507 thousand tons of stable gas condensate, or 53.6% of our total sales volumes, on the domestic market compared to 1,309 thousand tons, or 47.0%, in 2015. Our average realized price remained relatively flat compared to 2015 (see "Stable gas condensate and refined products, liquefied petroleum gas and crude oil prices" above).

Liquefied petroleum gas sales

In 2016, our revenues from sales of LPG decreased by RR 1,815 million, or 5.4%, compared to 2015 due to a decrease in average realized domestic prices (see "Stable gas condensate and refined products, liquefied petroleum gas and crude oil prices" above) which was largely offset by an increase in total sales volumes.

In 2016, we sold 549 thousand tons of LPG, or 20.2% of our total LPG sales volumes, to export markets as compared to sales of 551 thousand tons, or 23.9%, in 2015. Our average realized LPG net export price, excluding export duties, excise and fuel taxes expense, changed insignificantly (decreased by RR 50 per ton, or 0.2%).

In 2015 and 2016, our LPG export delivery terms were DAP at the border of the customer's country or free carrier (FCA) at terminal points in Poland. In 2015, we also sold our LPG under carriage paid to (CPT) the Port of Temryuk (southern Russia) delivery terms. We sold most of our LPG export sales volumes to Poland in both reporting periods.

In 2016, we sold 2,164 thousand tons of LPG, or 79.8% of our total LPG sales volumes, on the domestic market compared to sales of 1,755 thousand tons, or 76.1%, in 2015. Our average realized LPG domestic price in 2016, was RR 8,693 per ton representing a decrease of RR 3,014 per ton, or 25.7%, compared to 2015 (see "Stable gas condensate and refined products, liquefied petroleum gas and crude oil prices" above).

Other products sales

Other products sales represent our revenues from the domestic sales of purchased oil products (diesel fuel and petrol) through our retail stations, sales of other purchased liquid hydrocarbons, and sales of our produced methanol. In 2016, our revenues from other products sales increased by RR 43 million, or 10.1%, to RR 467 million from RR 424 million in 2015.

Other revenues

Other revenues include revenue from transportation, geological and geophysical research services, repair and maintenance of energy equipment services, and other services. In 2016, other revenues increased by RR 297 million, or 9.0%, to RR 3,615 million from RR 3,318 million in 2015 primarily due to a RR 297 million increase in revenues from repair and maintenance of energy equipment services provided by our subsidiary NOVATEK-Energo by RR 297 million. At the same time, other revenues increased by RR 170 million in 2016 due to an increase in revenues from services for preparation of third party hydrocarbons for transportation and decreased by RR 188 million due to a decrease in revenues from tankers transporting third party goods.

Operating expenses

In 2016, our total operating expenses increased by RR 50,457 million, or 15.1%, to RR 385,499 million compared to RR 335,042 million in 2015 mainly due to the launch of the Yarudeyskoye field in December 2015 and the respective increase of certain items in transportation, taxes other than income tax expenses, depreciation, depletion and amortization, and materials, services and other expenses. Our total operating expenses as a percentage of total revenues changed insignificantly (increased to 71.7% from 70.5%).

<i>millions of Russian roubles</i>	Year ended 31 December:			
	2016	% of total revenues	2015 ⁽¹⁾	% of total revenues
Purchases of natural gas and liquid hydrocarbons	134,268	25.0%	120,504	25.4%
Transportation expenses	133,462	24.8%	130,229	27.4%
Taxes other than income tax	44,053	8.2%	36,630	7.7%
Depreciation, depletion and amortization	34,631	6.4%	19,980	4.2%
Materials, services and other	19,133	3.6%	14,551	3.1%
General and administrative expenses	18,126	3.4%	14,356	3.0%
Exploration expenses	2,087	0.4%	1,109	0.2%
Impairment expenses (reversals), net	178	n/a	(204)	n/a
Changes in natural gas, liquid hydrocarbons and work-in-progress	(439)	n/a	(2,113)	n/a
Total operating expenses	385,499	71.7%	335,042	70.5%

⁽¹⁾ Certain reclassifications have been made to the 2015 figures to conform to the current reporting period presentation with no effect on profit for the period or shareholder's equity. Insurance expenses relating to production assets and major part of expenses of the Group's research and development center are presented in this report within Materials, services and other expenses and Exploration expenses depending on their function, which were previously disclosed within General and administrative expenses. Accordingly, expenses in the amount of RR 807 million were reclassified from General and administrative expenses to "Materials, services and other expenses and Exploration expenses in the amount of RR 465 million and RR 342 million, respectively, for the year ended 31 December 2015.

Purchases of natural gas and liquid hydrocarbons

In 2016, our purchases of natural gas and liquid hydrocarbons increased by RR 13,764 million, or 11.4%, to RR 134,268 million from RR 120,504 million in 2015.

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2016	2015	
Unstable gas condensate	93,854	91,078	3.0%
Natural gas	38,119	27,715	37.5%
Other liquid hydrocarbons	2,295	1,711	34.1%
Total purchases of natural gas and liquid hydrocarbons	134,268	120,504	11.4%

In 2016, our purchases of unstable gas condensate from our joint ventures increased by RR 2,776 million, or 3.0%, as compared to 2015, due to an increase in purchases from SeverEnergiya (through its wholly owned subsidiary, OAO Arcticgas) as a result of the launch of additional production capacities in the first half of 2015 (see "Liquids production volumes" above), as well as the commencement of purchases from Terneftegas effective May 2015.

In 2016, our purchases of natural gas increased by RR 10,404 million, or 37.5%, as compared to 2015 as a result of an increase in purchases from SeverEnergiya and third parties, as well as the commencement of purchases from Terneftegas since May 2015 (see "Natural gas production volumes" above). In addition, purchase prices increased due to an increase in the average regulated price by 7.5% effective 1 July 2015.

Other liquid hydrocarbons purchases represent our purchases of oil products and LPG for subsequent resale depending on the demand for these types of products. In 2016, our purchases of other liquid hydrocarbons increased by RR 584 million, or 34.1%, as compared to 2015.

Transportation expenses

In 2016, our total transportation expenses increased by RR 3,233 million, or 2.5%, to RR 133,462 million as compared to RR 130,229 million in 2015.

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2016	2015	
Natural gas transportation			
by trunk and low-pressure pipelines	84,808	86,025	(1.4%)
Stable gas condensate and			
liquefied petroleum gas transportation by rail	31,838	29,273	8.8%
Gas condensate refined products,			
stable gas condensate and crude oil transportation by tankers	9,997	13,378	(25.3%)
Crude oil transportation by trunk pipelines	6,654	1,476	350.8%
Other	165	77	114.3%
Total transportation expenses	133,462	130,229	2.5%

In 2016, despite an average 2.0% increase in the natural gas regulated transportation tariff effective 1 July 2015 (see "Transportation tariffs" above), our expenses for natural gas transportation decreased by RR 1,217 million, or 1.4%, to RR 84,808 million from RR 86,025 million in 2015, due to an increase in the proportion of sales to our end-customers located closer to our production fields in the current year as compared to the previous year.

In 2016, our total expenses for stable gas condensate and LPG transportation by rail increased by RR 2,565 million, or 8.8%, to RR 31,838 million from RR 29,273 million in 2015. The increase was due to a 9.0% increase in our weighted average transportation cost per unit mainly resulted from an increase in the regulated railroad transportation tariffs effective January 2016 (see "Transportation tariffs" above). Volumes of liquids sold and transported via rail remained relatively flat between reporting periods (decreased by 0.3%).

In 2016, our total transportation expenses for liquids delivered by tankers to international markets decreased by RR 3,381 million, or 25.3%, to RR 9,997 million from RR 13,378 million in 2015 as a result of a decrease in average freight rates which fluctuate period-on-period depending on worldwide demand for tankers transportation, as well as a decrease in volumes of liquids sold and transported via tankers by 6.7%.

In 2016, our expenses for crude oil transportation to customers by trunk pipeline significantly increased by RR 5,178 million, or 4.5 times, to RR 6,654 million from RR 1,476 million in 2015, due to a significant 4.3 times increase in volumes transported as a result of the commencement of crude oil commercial production at the Yarudeyskoye field in December 2015.

Taxes other than income tax

In 2016, taxes other than income tax increased by RR 7,423 million, or 20.3%, to RR 44,053 million from RR 36,630 million in 2015 primarily due to an increase in the unified natural resources production tax expense.

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2016	2015	
Unified natural resources production tax (UPT)	40,997	33,656	21.8%
Property tax	2,793	2,603	7.3%
Other taxes	263	371	(29.1%)
Total taxes other than income tax	44,053	36,630	20.3%

In 2016, our unified natural resources production tax expense increased by RR 7,341 million, or 21.8%, to RR 40,997 million from RR 33,656 million in 2015 primarily due to a significant increase in crude oil production as a result of the commercial production commencement at the Yarudeyskoye field in December 2015. In addition, as a part of the tax maneuver in the oil and gas industry (see "Our tax burden and obligatory payments" above), the adjusting coefficient that is applied in the calculation of the UPT rate for gas condensate was increased by 25.0% from 1 January 2016 in relation to 2015, thus also leading to an increase in our UPT expense.

In 2016, our property tax expense increased by RR 190 million, or 7.3%, to RR 2,793 million from RR 2,603 million in 2015 mainly due to the launch of the Yarudeyskoye field in December 2015, as well as additions to property, plant and equipment at our other production subsidiaries.

Depreciation, depletion and amortization

In 2016, our depreciation, depletion and amortization ("DDA") expense increased by RR 14,651 million, or 73.3%, to RR 34,631 million from RR 19,980 million in 2015 mainly due to the launch of the Yarudeyskoye field in December 2015, as well as additions of property, plant and equipment at our production subsidiaries.

We accrue depreciation and depletion on oil and gas assets using the "units-of-production" method and straight-line method for other facilities. Our reserve base is only appraised on an annual basis as of 31 December and does not fluctuate during the year until the subsequent appraisal, whereas our depletable cost base does change each quarter due to the ongoing capitalization of our costs throughout the year.

Materials, services and other

In 2016, our materials, services and other expenses increased by RR 4,582 million, or 31.5%, to RR 19,133 million compared to RR 14,551 million in 2015 primarily due to the launch of the Yarudeyskoye field in December 2015.

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2016	2015	
Employee compensation	7,558	6,004	25.9%
Repair and maintenance	3,026	1,959	54.5%
Complex of services for preparation, transportation and processing of hydrocarbons	2,062	1,756	17.4%
Materials and supplies	1,838	1,305	40.8%
Electricity and fuel	1,101	938	17.4%
Liquefied petroleum gas volumes reservation expenses	1,017	768	32.4%
Security services	660	470	40.4%
Transportation services	641	452	41.8%
Insurance expense	372	267	39.3%
Rent expenses	257	59	n/a
Other	601	573	4.9%
Total materials, services and other	19,133	14,551	31.5%

Operating employee compensation increased by RR 1,554 million, or 25.9%, to RR 7,558 million compared to RR 6,004 million in 2015. The increase was due to an increase in the average number of employees as a result of the launch of the Yarudeyskoye field in December 2015, an indexation of base salaries effective from 1 July 2016 and the related increase in social contributions for medical and social insurance and to the Pension Fund.

Repair and maintenance services expenses, materials and supplies, electricity and fuel, security services and transportation increased mainly due to the launch of the Yarudeyskoye field in December 2015.

Complex of services for preparation, transportation and processing of hydrocarbons expenses mainly relate to transportation of our LPG produced at the Purovsky Plant for further processing at the Tobolsk Refining Facilities. These expenses increased by RR 306 million, or 17.4%, to RR 2,062 million in 2016 compared to RR 1,756 million in 2015 primarily due to an increase in the contract rate for services at the Tobolsk Refining Facilities at the end of 2015, as well as additional expenses for preparation of crude oil for transportation by trunk pipeline resulted from the commencement of crude oil commercial production at the Yarudeyskoye field in December 2015.

In 2016, liquefied petroleum gas volumes reservation costs increased by RR 249 million, or 32.4%, to RR 1,017 million from RR 768 million in 2015 primarily due to an increase in LPG volumes sold through our subsidiary in Poland, as well as an increase in the average exchange rate of the Polish zloty to the Russian rouble, since this expense is denominated in Polish zloty. The reservation of LPG is required in order to maintain the necessary strategic reserve in Poland in accordance with local regulation.

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Insurance expense increased by RR 105 million, or 39.3%, to RR 372 million in 2016 from RR 267 million in 2015 due to an increase in insurable property valuation and the number of items of insured property, plant and equipment in our major subsidiaries.

Rent expenses increased by RR 198 million, or 4.4 times, to RR 257 million from RR 59 million in 2015 primarily due to rent of additional equipment used for stimulation of hydrocarbons production at some of our fields.

General and administrative expenses

In 2016, our general and administrative expenses increased by RR 3,770 million, or 26.3%, to RR 18,126 million compared to RR 14,356 million in 2015. The main components of these expenses were employee compensation, social expenses and compensatory payments, as well as legal, audit and consulting services, which, on aggregate, comprised 85.7% and 81.8% of total general and administrative expenses in the years ended 31 December 2016 and 2015, respectively.

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2016	2015	
Employee compensation	12,327	9,364	31.6%
Social expenses and compensatory payments	2,184	1,347	62.1%
Legal, audit and consulting services	1,019	1,036	(1.6%)
Business travel expense	624	634	(1.6%)
Fire safety and security expenses	387	313	23.6%
Advertising expenses	370	253	46.2%
Rent expense	214	196	9.2%
Repair and maintenance expenses	200	458	(56.3%)
Other	801	755	6.1%
Total general and administrative expenses	18,126	14,356	26.3%

Employee compensation relating to administrative personnel increased by RR 2,963 million, or 31.6%, to RR 12,327 million in 2016 from RR 9,364 million in 2015. The increase was due to an increase in the average number of employees, an indexation of base personnel salaries effective 1 July 2016, as well as an increase in bonuses accrued to key management and the related increase in social contributions for medical and social insurance and to the Pension Fund.

In 2016, our social expenses and compensatory payments increased by RR 837 million, or 62.1%, to RR 2,184 million compared to RR 1,347 million in 2015 mainly due to increase in compensatory payments. These payments mainly related to the development of Yarudeyskoye, Salmanovskoye and Geofizicheskoye fields and were RR 1,029 million in 2016 compared to RR 362 million in 2015. In addition, social expenses increased due to continued support of charities and social programs in the regions where we operate. Social expenses and compensatory payments fluctuate period-on-period depending on the implementation schedules of specific programs we support.

Fire safety and security expenses increased by RR 74 million, or 23.6%, to RR 387 million in 2016 from RR 313 million in 2015 primarily due to an increase in rates charged for security services starting from January 2016.

Advertising expenses increased by RR 117 million, or 46.2%, to RR 370 million in 2016 from RR 253 million in 2015 mainly due to the conclusion of a corporate sponsorship contract for the Group's advertising during sporting events at the end of 2015.

Repair and maintenance expenses decreased by RR 258 million, or 56.3%, to RR 200 million in 2016 from RR 458 million in 2015 mainly due to repair works performed at the Group's Moscow head office building in 2015 (absent in 2016).

Other items of our general and administrative expenses changed marginally.

Exploration expenses

In 2016, our exploration expenses increased by RR 978 million, or 88.2%, to RR 2,087 million from RR 1,109 million in 2015 and related in both reporting periods to exploration works performed at North-Obskiy license area, and in 2016 also to exploration works performed at the Nyakhartinskiy and Trekhbugorniy license areas. Exploration expenses include geological and geophysical research services expenditures, expenditures associated with the maintenance of license areas with non-proven reserves and other expenditures relating to exploration activity, as well as expenses of our research and development center associated with the exploration activities at our fields. The exploration expenses fluctuate period-to-period in accordance with the approved working schedule of exploration works at our production subsidiaries.

Impairment expenses (reversals)

In 2016, we recognized a net impairment expense of RR 178 million related primarily to trade accounts receivable. In 2015, we reversed a portion of previously accrued provisions in the total amount of RR 204 million as a result of revising management's estimates on the probability of recovering trade accounts receivable.

Changes in natural gas, liquid hydrocarbons and work-in-progress

In 2016, we recorded a reversal of RR 439 million to changes in inventory expense due to an increase in our gas condensate refined products inventory balances as of 31 December compared to 1 January, as well as an increase in the cost of inventories. In 2015, an increase in our natural gas and most of liquid hydrocarbons inventory balances as of 31 December compared to 1 January resulted in a reversal of RR 2,113 million to changes in inventory expense.

In 2016, our cumulative natural gas inventory balance in the Underground Gas Storage Facilities ("UGSF"), the GTS and own pipeline infrastructure decreased by 493 mmcm as compared to an increase of 278 mmcm in 2015. In 2016, we withdrew considerably more volumes of natural gas from inventory with relatively flat volumes injected into the UGSF due to higher demand for natural gas from end-customers (our total natural gas sales volumes increased by 3.6% (see "Natural gas sales volumes" above)).

In 2016, our cumulative liquid hydrocarbons inventory balances, recognized as inventory in transit or in storage, changed marginally (decreased by seven thousand tons), whereas in 2015, our cumulative inventory balances increased by 171 thousand tons. The increase in inventory balances in 2015 was mainly due to an increase in inventory balance of stable gas condensate in rail cars and tankers in transit and not realized at the reporting date, as well as an increase in inventory balance of crude oil due to the launch of the Yarudeyskoye field in December 2015. Inventory balances of stable gas condensate and refined products tend to fluctuate period-to-period depending on shipment schedules and final destination of our shipments.

The following table highlights movements in our hydrocarbons inventory balances:

<i>Inventory balances in transit or in storage</i>	2016			2015		
	At 31 December	At 1 January	Increase / (decrease)	At 31 December	At 1 January	Increase / (decrease)
Natural gas (millions of cubic meters)	834	1,327	(493)	1,327	1,049	278
<i>including Gazprom's UGSF</i>	787	1,245	(458)	1,245	1,016	229
Liquid hydrocarbons (thousand tons)	903	910	(7)	910	739	171
<i>including naphtha</i>	267	184	83	184	305	(121)
<i>stable gas condensate</i>	307	369	(62)	369	219	150
<i>crude oil</i>	105	157	(52)	157	29	128

Other operating income (loss)

Other operating income (loss) includes realized income (loss) from hydrocarbons trading on the international markets, income (loss) from the change in the fair value of the aforementioned contracts, as well as other income (loss) relating to penalty charges, disposal of materials, fixed assets and other transactions. In 2016, we recognized other operating income of RR 221 million compared to other operating loss of RR 542 million in 2015.

In 2016, within our trading activities we purchased and sold approximately 3.4 bcm of natural gas, as well as various derivative commodity instruments, and recognized the aggregate realized income from trading activities of RR 1,970 million as compared to RR 206 million of income in 2015. At the same time, we recognized a non-cash loss of RR 1,778 million in 2016 as a result of a decrease in the fair value of aforementioned contracts as compared to RR 1,006 million non-cash loss in 2015.

In addition, we recorded other operating income of RR 29 million and RR 258 million in 2016 and 2015, respectively, which in both periods primarily related to the penalties charges received from our suppliers due to non-compliance of their contractual obligations, profit (loss) on disposal of materials and fixed assets, as well as other similar transactions.

Net gain on disposal of interests in joint ventures

In December 2015, the Group and China's Silk Road Fund Co. Ltd. signed an agreement on the acquisition of a 9.9% equity stake in Yamal LNG by the fund. In March 2016, the transaction was closed upon the completion of the conditions precedent and we recognized a gain on the disposal in the amount of RR 73,072 million.

In August 2015, as part of the restructuring procedures intended to achieve parity shareholdings in SeverEnergia, we contributed a 6.4% ownership interest in joint venture Artic Russia B.V. to the capital of Yamal Development. As a result, taking into account the 50% participation interest of NOVATEK in joint venture Yamal Development, in the three months ended 30 September 2015, we recognized a gain on the disposal in the amount of RR 989 million.

Profit from operations and EBITDA

Our profit from operations significantly increased by RR 84,536 million, or 60.1%, to RR 225,266 million in 2016, as compared to RR 140,730 million in 2015. Our profit from operations before disposals of interests in joint ventures increased by RR 12,453 million, or 8.9%, to RR 152,194 million in 2016, as compared to RR 139,741 million in 2015 mainly due to a significant increase in crude oil sales volumes resulted from the commencement of commercial production at the Yarudeyskoye field in December 2015 and reaching the nameplate production capacity by the end of the month. At the same time our share in the profit from operations of our joint ventures increased by RR 1,603 million, or 5.0%, to RR 33,655 million compared to RR 32,052 million in 2015 (see "Share of profit (loss) of joint ventures, net of income tax" below).

Our EBITDA, normalized for the effect of the disposal of interests in joint ventures, increased by RR 28,218 million, or 13.2%, to RR 242,407 million in 2016 from RR 214,189 million in 2015 also mainly due to a significant increase in crude oil sales volumes.

Finance income (expense)

In 2016, we recorded a net finance expense of RR 7,941 million compared to a net finance expense of RR 16,182 million in 2015 due to the recognition of a non-cash foreign exchange loss in both reporting periods, as well as due to the recognition in 2015 of a non-cash loss from the remeasurement of the shareholders' loans issued to our joint ventures.

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2016	2015	
Accrued interest expense on loans received	(16,297)	(14,549)	12.0%
Less: capitalized interest	5,314	6,047	(12.1%)
Provisions for asset retirement obligations: effect of the present value discount unwinding	(587)	(290)	102.4%
Interest expense	(11,570)	(8,792)	31.6%
Interest income	18,732	12,622	48.4%
Change in fair value of non-commodity financial instruments	10,387	(10,505)	n/a
Foreign exchange gain (loss), net	(25,490)	(9,507)	168.1%
Total finance income (expense)	(7,941)	(16,182)	(50.9%)

In 2016, our interest expense increased by RR 2,778 million, or 31.6%, to RR 11,570 million primarily due to depreciation of the Russian rouble relative to the US dollar and Euro (most of our long-term borrowings are denominated in foreign currencies), as well as a decrease in the base used for interest capitalization as a result of additions to property, plant and equipment at Yarudeyskoye field after its launch in December 2015. The impact of these factors was reduced by repayments of a part of the Group's borrowings.

Interest income increased by RR 6,110 million, or 48.4%, to RR 18,732 million in 2016 from RR 12,622 million in 2015 due to an increase in loans provided to our joint ventures for the development and expansion of their activities, as well as a result of the average Russian rouble depreciation relative to the US dollar and Euro in 2016 compared to the average exchange rate in 2015.

In 2016, we recognized a non-cash gain of RR 10,387 million compared to a non-cash loss of RR 10,505 million in 2015 due to the remeasurement of the shareholders' loans issued by the Group to our joint ventures in accordance with IAS 39 "*Financial instruments: recognition and measurement*". The effect of the fair value remeasurement of shareholders' loans may change period-to-period due to the change in market interest rates and other macroeconomic parameters and does not affect real future cash flows of loans repayments.

The Group continues to record non-cash foreign exchange gains and losses each reporting period due to movements between currency exchange rates. In 2016, we recorded a net foreign exchange loss of RR 25,490 million compared to a net loss of RR 9,507 million in 2015 primarily due to the revaluation of our foreign currency denominated borrowings and loans provided, as well as cash balances in foreign currency.

Share of profit (loss) of joint ventures, net of income tax

In 2016, the Group's proportionate share of profit of joint ventures amounted to RR 90,839 million as compared to the share of loss of joint ventures in the amount of RR 31,607 million in 2015.

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2016	2015	
Share in profit from operations	33,655	32,052	5.0%
Share in finance income (expense)			
Share in interest income (expense), net	(15,250)	(17,160)	(11.1%)
Share in foreign exchange gain (loss), net	102,922	(61,200)	n/a
Share in change in fair value of non-commodity financial instruments	(13,436)	9,539	n/a
Total share in finance income (expense)	74,236	(68,821)	n/a
Share in total income tax benefit (expense)	(17,052)	5,162	n/a
Total share of profit (loss) of joint ventures, net of income tax	90,839	(31,607)	n/a

Our proportionate share in the profit from operations of our joint ventures increased by RR 1,603 million, or 5.0%, primarily due to higher operating results of SeverEnergy (as a result of the launch of additional production capacities in the first half of 2015) and Terneftegas (as a result of the launch of the Termokarstovoye field in May 2015 and reaching the nameplate production capacity in June 2015). The impact of these factors was partially offset by lower operating results of Nortgas (due to natural decline in gas and gas condensate production), as well as an increase in the unified natural resources production tax expense (see "Our tax burden and obligatory payments" above).

In 2016, our proportionate share in the finance income of our joint ventures amounted to RR 74,236 million compared to the share in the finance expense of RR 68,821 million in 2015. The change in our share in finance income (expense) was primarily due to a recognition in 2016 of a significant non-cash foreign exchange gain on foreign currency denominated loans at our joint ventures Yamal LNG and Terneftegas (our share amounted to RR 102.9 billion) as compared to a significant non-cash loss (our share amounted to RR 61.2 billion) in 2015. The impact of foreign exchange gain (loss) effect was partially offset by a recognition of a non-cash loss from the remeasurement of the fair value of shareholders' loans in Yamal LNG and Terneftegas in 2016 (our share amounted to RR 13.4 billion) compared to a recognition of a non-cash gain (our share amounted to RR 9.5 billion) in 2015. The remaining changes in both reporting periods primarily related to our share in interest expense of our joint ventures.

Income tax expense

The Russian statutory income tax rate for both reporting periods was 20%.

The Group recognizes in profit before income tax its share of net profit (loss) from joint ventures, which influences the consolidated profit of the Group but does not result in additional income tax expense (benefit) at the Group's level. Net profit (loss) of joint ventures was recorded in their financial statements on an after-tax basis. The Group's dividend income from its joint ventures is subject to a zero withholding tax rate according to the Russian tax legislation as the Group holds at least a 50% interest in each of its joint ventures, and also does not result in a tax charge. In addition, during the year ended 31 December 2015, the Group recognized a deferred tax asset of RR 4,316 million related to expected disposal of 9.9% participation interest in Yamal LNG.

Without the effect of net profit (loss) and dividends from joint ventures, and the deferred tax asset relating to the 9.9% interest in Yamal LNG classified as held for sale, the effective income tax rate (total income tax expense calculated as a percentage of profit before income tax) in 2016 and 2015, was 19.8% and 18.7%, respectively.

PAO NOVATEK**Management's Discussion and Analysis of Financial Condition and Results of Operations
for the years ended 31 December 2016 and 2015****Profit attributable to shareholders and earnings per share**

As a result of the factors discussed in the respective sections above, profit attributable to shareholders of PAO NOVATEK increased by RR 183,399 million, or 246.5%, to RR 257,795 million in 2016 compared to RR 74,396 million in 2015.

The major factors that had an effect on the Group's financial result were the recognition of significant non-cash foreign exchange gains (losses) on foreign currency denominated loans of the Group and its joint ventures in both reporting periods, as well as the recognition of a gain on the disposal of interests in joint ventures in 2016. Excluding the one-time effect from the disposal of interests in joint ventures and the effect of foreign exchange gains and losses, our profit attributable to shareholders of PAO NOVATEK changed insignificantly and amounted to RR 133,759 million in 2016 compared to RR 132,509 million in 2015 (see the table below):

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2016	2015	
Profit attributable to shareholders of PAO NOVATEK	257,795	74,396	246.5%
Net gain on disposal of interests in joint ventures	(73,072)	(989)	n/a
Income tax expense relating to the disposal of interests in joint ventures	15,395	-	n/a
Normalized profit attributable to shareholders of PAO NOVATEK	200,118	73,407	172.6%
Foreign exchange (gains) losses	25,490	9,507	168.1%
Income tax expense (benefit) relating to foreign exchange (gains) losses	(5,098)	(1,901)	168.2%
Share of foreign exchange (gains) losses of joint ventures	(102,922)	61,200	n/a
Share of income tax expense (benefit) relating to foreign exchange (gains) losses of joint ventures	16,171	(9,704)	n/a
Normalized profit attributable to shareholders of PAO NOVATEK, excluding the effect of foreign exchange gains (losses)	133,759	132,509	0.9%

Our weighted average basic and diluted earnings per share, calculated from the profit attributable to shareholders of PAO NOVATEK increased by RR 60.78 per share, or 246.7%, to RR 85.41 per share in 2016 from RR 24.63 per share in 2015. Excluding the effects of the disposals of interests in joint ventures and foreign exchange gains and losses, our weighted average basic and diluted earnings per share changed insignificantly and amounted to RR 44.31 per share in 2016 compared to RR 43.87 per share in 2015.

LIQUIDITY AND CAPITAL RESOURCES

Cash flows

The following table shows our net cash flows from operating, investing and financing activities for the years ended 31 December 2016 and 2015:

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2016	2015	
Net cash provided by operating activities	173,791	132,864	30.8%
Net cash provided by (used for) investing activities	11,877	(159,074)	n/a
Net cash provided by (used for) financing activities	(156,712)	12,714	n/a

Net cash provided by operating activities

Our net cash provided by operating activities increased by RR 40,927 million, or 30.8%, to RR 173,791 million compared to RR 132,864 million in 2015. The increase was due to higher profit from operations adjusted for non-cash items, as well as changes in working capital and long-term advances given, that was partially offset by an increase in income tax payments.

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2016	2015	
Profit from operations before disposals of interests in joint ventures	152,194	139,741	8.9%
Non-cash adjustments ⁽¹⁾	36,739	20,820	76.5%
Changes in working capital and long-term advances given	11,189	(14,470)	n/a
Interest received	1,983	1,454	36.4%
Dividends received from joint ventures	-	1,850	n/a
Income taxes paid	(28,314)	(16,531)	71.3%
Total net cash provided by operating activities	173,791	132,864	30.8%

⁽¹⁾ Include adjustments for depreciation, depletion and amortization, net impairment expenses (reversals), change in fair value of non-commodity financial instruments and some other adjustments.

The profit from operations adjusted for non-cash items increased mainly due to a significant increase in crude oil sales volumes as a result of the commencement of commercial production at the Yarudeyskoye field in December 2015 (see "Profit from operations and EBITDA" above).

Working capital balances fluctuate from period-on-period depending on various factors. The changes in long-term advances given were mainly due to a decrease in long-term advances payments to RZD in 2016 compared to 2015, which were provided in accordance with the Strategic Partnership Agreement's installment schedule (see "Transportation tariffs" above).

The increase in income tax payments in 2016 was mainly due to an increase in the taxable profit resulted from the Group's higher operating results, as well as income tax prepayments at the beginning of 2015.

The remaining cash proceeds in both reporting periods related to interest received, as well as RR 1,850 million of dividends received from our joint venture Nortgas in 2015.

Net cash provided by (used for) investing activities

In 2016, our net cash provided by investing activities amounted to RR 11,877 million compared to RR 159,074 million used for investing activities in 2015.

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2016	2015	
Cash used for capital expenditures	(34,413)	(50,584)	(32.0%)
Payments for mineral licenses	(1,928)	-	n/a
Proceeds from disposal of stakes in joint ventures			
net of costs to sell and income tax paid, net	72,412	-	n/a
Additional capital contributions to joint ventures	(19,565)	-	n/a
Loans provided to joint ventures	(6,645)	(108,570)	(93.9%)
Repayments of loans provided to joint ventures	6,038	3,710	62.7%
Payments for acquisition of subsidiaries net of cash acquired	(2,961)	(3,630)	(18.4%)
Other	(1,061)	-	n/a
Net cash provided by (used for) investing activities	11,877	(159,074)	n/a

Cash used for capital expenditures decreased by RR 16,171 million, or 32.0%, as compared to 2015. In 2016, cash was mainly used for the development of the Yarudeyskoye and East-Tarkosalinskoye field's crude oil deposits, maintenance of production at our Yurkharovskoye field and the development of the Salmanovskoye (Utrenneye) field. In addition, we purchased a land plot in the northern part of the Ust-Luga port, bordering with the territory of our Ust-Luga Complex, for implementing Group's future projects.

In 2016, we made a payment in the amount of RR 1,928 million for the acquisition of exploration and production licenses for the Nyakhartinskiy, Syadorskiy and Tanamskiy license areas (see "Recent developments" above).

In 2016, we received RR 72,412 million (net of costs to sell and income tax paid) for the sale of the 9.9% equity stake in Yamal LNG in March 2016.

In September 2016, we made capital contributions to Yamal LNG in the amount of RR 19,565 million as part of the financing commitment by the Group as a result of the disposal of the 9.9% equity stake in Yamal LNG to China's Silk Road Fund Co. Ltd. on the same terms that were previously applied upon the entrance of TOTAL S.A. and China National Petroleum Corporation into the Yamal LNG project.

In 2016, we provided loans to our joint venture Yamal LNG in the amount of RR 6,645 million as compared to RR 108,570 million provided to Yamal LNG and Yamal Development in 2015. At the same time, in 2016 and 2015, we received RR 6,038 million and RR 3,710 million, respectively, due to a partial repayment of the loans provided to Terneftegas and Yamal Development.

In 2016 and 2015, we paid RR 2,929 million (USD 39 million) and RR 3,630 million (USD 62 million), respectively, for 100% equity stake in AO Office acquired in August 2014. In addition, in April and December 2016, the Group acquired companies OOO Evrotek-Yuh and Blue Gaz Sp. z o.o. for RR six million and RR 26 million, respectively (see "Recent developments" above).

Net cash provided by (used for) financing activities

In 2016, our net cash used for financing activities amounted to RR 156,712 million as compared to RR 12,714 million provided by financing activities in 2015.

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2016	2015	
Proceeds from (repayments of) long-term debt, net	(76,380)	29,105	n/a
Proceeds from (repayments of) short-term debt, net	(26,340)	27,180	n/a
Dividends paid	(41,653)	(35,640)	16.9%
Interest paid	(11,423)	(7,149)	59.8%
Purchase of treasury shares	(916)	(782)	17.1%
Net cash provided by (used for) financing activities	(156,712)	12,714	n/a

In 2016, we obtained a long-term loan from a Russian subsidiary of a foreign bank in the amount of RR 6,373 million (EUR 100 million). At the same time, the Group fully repaid five-year US dollar denominated Eurobonds in the amount of RR 46,756 million (USD 600 million) and partially repaid a loan obtained under our syndicated credit line facility in the amount of RR 30,265 million (USD 462 million) according to the loan's maturity schedule, as well as partially repaid a loan obtained by a Group subsidiary from its non-controlling shareholder.

In 2015, we received funds under the loan agreement with China's Silk Road Fund in the amount of RR 55,215 million (EUR 0.73 billion) for financing of the Yamal LNG project as part of the transaction for the sale of the Group's 9.9% equity stake in Yamal LNG, and also one of the Group's subsidiaries obtained long-term loans from its non-controlling shareholder in the amount of RR 16,130 million. At the same time, the Group fully repaid three-year tenor non-convertible Russian rouble denominated exchange-traded bonds in the amount of RR 20 billion, as well as partially repaid a loan obtained under our syndicated credit line facility in the amount of RR 22,240 million (USD 346 million) according to the loan's maturity schedule.

During 2016, we repaid short-term loans from a Russian bank in the amount of RR 20,000 million and from the non-controlling shareholder of our subsidiary in the amount of RR 1,300 million obtained in 2015. In addition, in both reporting periods, we obtained short-term loans to finance trade activities. In the current reporting period net repayments from these loans amounted to RR 5,040 million, while in 2015 net proceeds amounted to RR 5,880 million.

The remaining change primarily related to an increase in dividends paid and interest paid on borrowings and loans.

Liquidity and working capital

The following table shows our liquidity and credit measures as of 31 December 2016 and 2015:

	31 December 2016	31 December 2015	Change, %
Absolute amounts, RR million			
Net debt ⁽¹⁾	168,464	329,518	(48.9%)
Net working capital position ⁽²⁾	23,969	(41,203)	n/a
Liquidity and credit ratios			
Current ratio ⁽³⁾	1.22	0.76	60.5%
Total debt to total equity	0.33	0.84	(60.7%)
Long-term debt to long-term debt and total equity	0.20	0.37	(45.9%)
Net debt to total capitalization ⁽⁴⁾	0.19	0.41	(53.7%)
Net debt to normalized EBITDA from subsidiaries ⁽⁵⁾	0.89	2.05	(56.6%)
Interest coverage ratio ⁽⁶⁾	12	11	9.1%

⁽¹⁾ Net debt represents total debt less cash and cash equivalents.

⁽²⁾ Net working capital position represents current assets plus assets held for sale less current liabilities.

⁽³⁾ Current ratio is calculated as current assets plus assets held for sale divided by current liabilities.

⁽⁴⁾ Total capitalization represents total debt, total equity and deferred income tax liability.

⁽⁵⁾ Net debt to normalized EBITDA from subsidiaries ratio is calculated as Net debt divided by EBITDA from subsidiaries excluding the effect from the disposal of interests in joint ventures for the last twelve months.

⁽⁶⁾ Interest coverage ratio is calculated as normalized EBITDA from subsidiaries divided by accrued interest on debt, including capitalized interest.

In 2016, we repaid short- and long-term debt in the aggregate amount of approximately RR 142 billion. As a result, the Group's net debt decreased significantly by 48.9% and net working capital position amounted to RR 24.0 billion as of 31 December 2016.

In each quarter of 2015 and 2016, the Group achieved strong operating results and retained positive free cash flow. The Group's management believes that it presently has and will continue to have the ability to generate sufficient cash flows (from operating and financing activities) to repay all its current liabilities as they become due and to finance the Group's capital construction programs.

Capital expenditures

In 2015 and 2016, our capital expenditures represent our investments primarily relating to developing our oil and gas properties. The following table shows capital expenditures at our main fields, processing facilities and other assets:

<i>millions of Russian roubles</i>	Year ended 31 December:	
	2016	2015
Yarudeyskoye field	8,677	25,826
East-Tarkosalinskoye field	4,393	8,745
Yurkharovskoye field	3,480	7,562
Salmanovskoye (Utrennee) field	2,682	6,165
Khancheyevskoye field	1,845	1,480
Infrastructure for future LNG projects	1,342	409
North-Russkoye field	1,131	1,124
North-Khancheyevskoye + Khadyryakhinskoye field	74	1,422
Other	6,764	4,826
Capital expenditures	30,388	57,559

Total capital expenditures on property, plant and equipment in 2016 decreased by RR 27,171 million, or 47.2%, to RR 30,388 million from RR 57,559 million in 2015. In both reporting periods, our main capital expenditures related to the development of the Yarudeyskoye and East-Tarkosalinskoye field's crude oil deposits, Yurkharovskoye field's production maintenance, as well as the development of the Salmanovskoye (Utrenneye) field. In addition, the Group is performing feasibility studies for our future LNG projects and invested in the development of a project for construction of our own center in Murmansk region which will build large-scale offshore structures (see "Recent Developments" above).

The "Other" line in the table above represents our capital expenditures related to other fields and processing facilities of the Group, as well as unallocated capital expenditures as of the reporting date. The allocation of capital expenditures by fields takes place upon the completion of the fixed assets construction stages and depends on the approved fixed assets launch schedule. At the end of 2016, we purchased for RR 3,990 million a land plot with other immovable items in the northern part of the Ust-Luga port, adjacent to the territory of our Ust-Luga Complex, for implementing Group's future projects (expenditures are included in the line "Other" in the table above).

The following table presents the reconciliation of our capital expenditures and additions to property, plant and equipment per Note "Property, plant and equipment" in the Group's IFRS Consolidated Financial Statements, and cash used for capital investments:

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2016	2015	
Total additions to property, plant and equipment per Note "Property, plant and equipment" in the Group's IFRS Consolidated Financial Statements	32,316	57,559	(43.9%)
Less: acquisition of mineral licenses	(1,928)	-	n/a
Capital expenditures	30,388	57,559	(47.2%)
Add (less): capitalized foreign exchange differences, change in accounts payable and other non-cash adjustments	4,025	(6,975)	n/a
Cash used for capital expenditures ⁽¹⁾	34,413	50,584	(32.0%)

⁽¹⁾ Represents purchases of property, plant and equipment, materials for construction and capitalized interest paid per Consolidated Statement of Cash Flows net of payments for mineral licenses and acquisition of subsidiaries.

QUALITATIVE AND QUANTITATIVE DISCLOSURES AND MARKET RISKS

We are exposed to market risk from changes in commodity prices, foreign currency exchange rates and interest rates. We are exposed to commodity price risk as our prices for crude oil, stable gas condensate and refined products destined for export sales are linked to international crude oil prices and other benchmark price references. We are exposed to foreign exchange risk to the extent that a portion of our sales, costs, receivables, loans and debt are denominated in currencies other than Russian roubles. We are subject to market risk from changes in interest rates that may affect the cost of our financing. From time to time we may use derivative instruments, such as commodity forward contracts, commodity price swaps, commodity options, foreign exchange forward contracts, foreign currency options, interest rate swaps and forward rate agreements, to manage these market risks, and we may hold or issue derivative or other financial instruments for trading purposes.

Foreign currency risk

Our principal exchange rate risk involves changes in the value of the Russian rouble relative to the US dollar. As of 31 December 2016, the total amount of our long-term debt denominated in US dollars was RR 154,915 million, or 71.5% of our total borrowings at that date. Changes in the value of the Russian rouble relative to foreign currencies will impact our foreign currency-denominated costs and expenses, our debt service obligations for foreign currency-denominated borrowings, as well as receivables at our foreign subsidiaries in Russian rouble terms. We believe that the risks associated with our foreign currency exposure are partially mitigated by the fact that a portion of our total revenues, 40.9% in 2016, was denominated in foreign currencies.

In addition, our share of profit (loss) of joint ventures is also exposed to foreign currency exchange rate movements due to the significant amount of foreign currency-denominated borrowings in our joint ventures, mostly in Yamal LNG. We expect that once commercial production commences, foreign currency risk relating to the debt portfolio of Yamal LNG will be mitigated by the fact that all of its products will be delivered to international markets and its revenues will be denominated in foreign currencies.

As of 31 December 2016, the Russian rouble appreciated by 16.8% and 19.9% against the US dollar and the Euro, respectively, compared to 31 December 2015 (see "Selected macro-economic data" above).

Commodity risk

Substantially all of our stable gas condensate and refined products, LPG and crude oil export sales are sold under spot market contracts. Our export prices are primarily linked to international crude oil and oil products prices. External factors such as geopolitical developments, natural disasters and the actions of the Organization of Petroleum Exporting Countries affect crude oil prices and thus our export prices.

The weather is another factor affecting demand for natural gas. Changes in weather conditions from year to year can influence demand for natural gas and to some extent gas condensate and refined products.

From time to time we may employ derivative instruments to mitigate the price risk of our sales activities. In our consolidated financial statements all derivative instruments are recognized at their fair values. Unrealized gains or losses on derivative instruments are recognized within other operating income (loss), unless the underlying arrangement qualifies as a hedge.

The Group purchases and sells natural gas on the European market under long-term contracts based on formulas with reference to benchmark natural gas prices quoted for the North-Western European natural gas hubs, crude oil and oil products prices and/or a combination thereof. Therefore, the Group's financial results from natural gas foreign trading activities are subject to commodity price volatility based on fluctuations or changes in the respective benchmark reference prices.

Pipeline access

We transport substantially all of our natural gas through the Gas Transmission System ("GTS") owned and operated by PAO Gazprom, which is responsible for gathering, transporting, dispatching and delivering substantially all natural gas supplies in Russia. Under existing legislation, Gazprom must provide access to the GTS to all independent suppliers on a non-discriminatory basis provided there is capacity available that is not being used by Gazprom. In practice, Gazprom exercises considerable discretion over access to the GTS because it is the sole owner of information relating to capacity. There can be no assurance that Gazprom will continue to provide us with access to the GTS; however, we have not been denied access in prior periods.

Ability to reinvest

Our business requires significant ongoing capital expenditures in order to grow our production and meet our strategic plans. An extended period of reduced demand for our hydrocarbons available for sale and the corresponding revenues generated from these sales would limit our ability to maintain an adequate level of capital expenditures, which in turn could limit our ability to increase or maintain current levels of production and deliveries of natural gas, gas condensate, crude oil and other associated products; thereby, adversely affecting our financial and operating results.

Off balance sheet activities

As of 31 December 2016, we did not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which are typically established for the purpose of facilitating off-balance sheet arrangements.

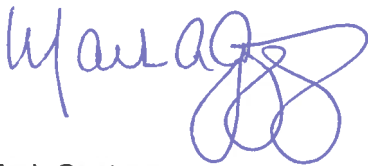
TERMS AND ABBREVIATIONS

APR	Asian-Pacific Region
bbl	barrel
bcm	billion cubic meters
boe	barrels of oil equivalent
CBR	Central Bank of Russian Federation
CFR	"Cost and freight"
CIF	"Cost, insurance and freight"
CNY	Chinese Yuan
DAP	"Delivery at point of destination"
DDA	depreciation, depletion and amortization
DES	"Delivery to the port of destination ex-ship"
FCA	"Free carrier"
FOB	"Free on board"
Forecast of the Ministry of Economic Development	The document " <i>Forecast of Socio-economic Development of the Russian Federation for 2015 and planned period 2016 and 2017</i> " prepared by the Ministry of Economic Development of the Russian Federation or the similar document prepared for another period
FTS	Federal Tariffs Service
GTS	Gas Transmission System part of the UGSS
IFRS	International Financial Reporting Standards
List	the OFAC's Sectoral Sanctions Identification List
LNG	liquefied natural gas
LPG	liquefied petroleum gas
mcm	thousand cubic meters
MET	mineral extraction tax
OFAC	Office of Foreign Assets Control
PRMS	Petroleum Resources Management System
Purovsky Plant	Purovsky Gas Condensate Plant
Regulator	A federal executive agency of the Russian Federation that carries out governmental regulation of prices and tariffs for products and services of natural monopolies in energy, utilities and transportation. During the first half of 2015, the Federal Tariffs Service fulfilled the Regulator's role. In July 2015, a Decree of the President of the Russian Federation became effective abolishing the FTS and transferring its functions to the Federal Anti-Monopoly Service
RR	Russian rouble(s)
RZD	OAo Russian Railways, Russia's state-owned monopoly railway operator
S&P	Standard & Poor's
SEC	Securities and Exchange Commission
Tobolsk Refining Facilities	Refining facilities of OOO SIBUR Tobolsk
UGSF	Underground Gas Storage Facilities
UGSS	Unified Gas Supply System owned and operated by PAO Gazprom
UPT	unified natural resources production tax
USD, US dollar	United States Dollar
Ust-Luga Complex	Gas Condensate Fractionation and Transshipment Complex located at the port of Ust-Luga on the Baltic Sea
VAT	value added tax
Yamal LNG project	A large-scale project on constructing a liquefied natural gas plant with an annual capacity of 16.5 million tons based on the feedstock resources of the South-Tambeyskoye field located at the northeast of the Yamal Peninsula that Group undertakes jointly with TOTAL S.A., China National Petroleum Corporation and China's Silk Road Fund Co. Ltd., through its joint venture OAo Yamal LNG
YNAO	Yamal-Nenets Autonomous Region

RESPONSIBILITY STATEMENT

I hereby confirm that to the best of my knowledge:

- (a) the set of financial statements, which has been prepared in accordance with International Accounting Standards, gives a true and fair view of the assets, liabilities, financial position and profit or loss of the undertakings included in the consolidation as a whole as required by the Disclosure and Transparency Rule (DTR) 4.1.6R,
- (b) the management report includes a fair review of the information required by DTR 4.1.9R-4.1.11R, being a balanced and comprehensive analysis of development and performance of the business and the position of the company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that the company faces.



Mark Gyetvay,

Deputy Chairman of the Management Board