



# EXPANDING OUR GLOBAL LNG FOOTPRINT

ANNUAL REPORT 2018



# NOVATEK at a Glance 2018

PAO NOVATEK is one of the largest independent producers of natural gas in Russia. The Company is engaged in the exploration, production, processing and sale of natural gas and liquid hydrocarbons and has almost twenty-five years of experience in the Russian oil and gas industry. The Company entered the international gas market in December 2017 with the start of LNG production at the Yamal LNG Project.



## HYDROCARBON RESERVES



**1.22** BLN  
BOE

Total proved hydrocarbon reserves addition (SEC), including production



**15.79** BLN  
BOE

Total proved hydrocarbon reserves (SEC)

**56**

Fields and license areas



## PRODUCTION



**549** MLN  
BOE

Hydrocarbon production



**9%**

Share of natural gas production in Russia



**+8.5%**

Natural gas production increase



**11.8** MMT

Liquid hydrocarbons production





## SALES



**66** <sup>BCM</sup>

Natural gas sales  
in Russia



**6** <sup>BCM</sup>

LNG sales on  
international markets



**15.8** <sup>MMT</sup>

Liquid hydrocarbons  
sales volume



**832** <sup>RR  
BLN</sup>

Total revenues

**415** <sup>RR  
BLN</sup>

Normalized EBITDA

**51.9** <sup>USD  
BLN</sup>

Market capitalization as of 31.12.2018 (LSE)

**26.06** <sup>RR</sup>

Recommended dividend per share



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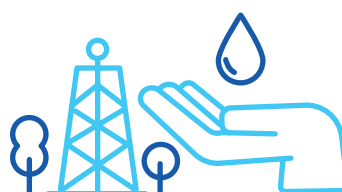


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# Letter to Shareholders



**ALEXANDER  
NATALENKO**

Chairman of the Board  
of Directors



**LEONID  
MIKHELSON**

Chairman of the  
Management Board



**MARK  
GYETVAY**

Deputy Chairman  
of the Management  
Board

## Dear Shareholders,

**TWO THOUSAND AND EIGHTEEN** was an incredible year for NOVATEK culminating with the successful launch of our flagship Yamal LNG project and reaching the facilities' full design capacity in record time. It marked a year of exceptional achievements and **EXPANDING OUR GLOBAL LNG FOOTPRINT** with shipments to customers around the globe.

Yamal LNG was launched in record time and on budget with the commissioning of the second and third LNG trains accomplished ahead of schedule by six months and more than a year, respectively. Yamal LNG established a new benchmark in the industry known for numerous budget overruns and delays in project implementation. The successful launch of all three liquefaction trains confirms that Yamal LNG is a unique project in the fastest-growing segment of the natural gas industry, enabling us to emerge as one of the major players in the global LNG market.

With a nameplate capacity of 16.5 million tons per annum (mmtpa) with the launch of three LNG trains, Yamal LNG's natural gas feedstock is based on reserves of the South-Tambeyskoye field on the coast of the Ob Bay, located on the hydrocarbon-rich Yamal Peninsula. We will build the fourth LNG train with a planned capacity of 0.9 mmtpa based on NOVATEK's patented proprietary liquefaction technology called "Arctic Cascade" using equipment produced and manufactured domestically in Russia. Combined, the project should reach a nameplate capacity of 17.4 mmtpa.

Yamal LNG is an integrated project encompassing natural gas production, liquefaction and marketing, with its key advantages of a prolific conventional reserve base, proven development technologies, very low lifting costs, advantageous geographical location and colder ambient temperatures. These strategic favorable operating conditions further support our future LNG projects on the Yamal and Gydan peninsulas, thus making our overall LNG platform extremely attractive based on lower capital intensity per ton of LNG produced, and optional transport routes to East and West natural gas consuming markets.

Yamal LNG is currently the largest LNG project in Russia with an aggregate share of about 5% of the global LNG market and represents a unique benchmark for the global oil and gas industry. We have something to be proud of, as we have consistently demonstrated our ability to develop our asset base and competitively produce natural gas and LNG in Russia's Arctic zone. We have gained invaluable experience in implementing a large-scale LNG project in the Arctic region where,



**Total hydrocarbons production**  
**7% growth as compared with 2017**

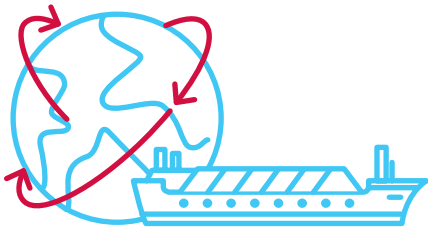
despite the harsh climatic conditions, the colder ambient temperature provides us with a competitive advantage to lower the cost of liquefaction.

Many industry commentators consider natural gas as a "transition" or "bridge" fuel. We disagree with this characterization. Natural gas is a clean burning fossil fuel and will play a major role in the future energy mix as a key contributor to meet climate change and de-carbonization goals. We are very optimistic about our future LNG projects given forecasted LNG and natural gas demand scenarios, and the transition from coal to natural gas in the primary energy mix to support sustainable development principles.

We officially opened the summer navigation period via the Northern Sea Route when we delivered the first commercial LNG shipments to China from Yamal LNG using the newly designed Arc7 ice-class tankers. These shipments were made possible due to the exceptional characteristics of our brand new, fully dedicated fleet of ice-class LNG carriers to serve our Arctic projects. These unique ice-class LNG carriers enable year-round navigation without icebreaker support along westbound navigation routes and, eastbound during the Arctic zones seasonal navigation period, along the Northern Sea Route.

During 2018, we delivered LNG cargos to Asia, India, South America, the Middle East and Europe, representing 113 cargos, or 8.4 million tons. This demonstrates the commercial viability of delivering competitively priced LNG from the Arctic region of Russia to all major consuming regions of the world.

We also optimized our transport costs by decreasing the travel distance of the Arc7 ice-class tankers to ensure



**113 LNG cargos or 8.4 mln tons of LNG offloaded in 2018 from Yamal LNG**



**The successful launch of all three liquefaction trains confirms that Yamal LNG is a unique project in the fastest-growing segment of the natural gas industry, enabling us to emerge as one of the major players in the global LNG market**



**Arctic LNG 2, based on the prolific hydrocarbon resources of the Utrenneye field located on the Gydan Peninsula, envisages for the construction of three LNG trains for a combined total of 19.8 mmtpa**

the timely loading and offloading of LNG produced from the Yamal LNG project. In November 2018, Yamal LNG successfully completed the first ship-to-ship LNG transshipment in the area near the port of Honningsvåg in northern Norway. The operational experience gained from this process will be used at our future large-scale LNG transshipment projects in Kamchatka and the Murmansk Region, according us the opportunity to build an efficient logistics chain for our LNG projects.

## Arc 7

**We officially opened the summer navigation period via the Northern Sea Route when we delivered the first commercial LNG shipments to China from Yamal LNG using the newly designed Arc7 ice-class tankers**

Our LNG strategy also provides for medium-tonnage and low-tonnage projects, enabling us to build effective distribution channels to target niche markets and customer segments. In the reporting year, we completed the construction and began commissioning of Cryogas-Vysotsk, a medium-tonnage LNG plant located on the Baltic Sea. In 2018, we established a joint venture with Fluxys to build a medium-tonnage transshipment LNG terminal in Rostock in Germany, which will receive LNG carriers from the Cryogas-Vysotsk liquefaction facility.

In order to manage our transportation costs and build up the unique competencies of Arctic navigation, in May 2018, we created a wholly owned transport subsidiary called Maritime Arctic Transport. Establishing an efficient Northern Sea Route shipping model is one of our key priorities to realize our long-term strategy and improve the competitiveness of NOVATEK's Arctic projects.

The successful launch of our flagship LNG project demonstrated our ability to contribute in a meaningful way to the next wave of LNG projects delivering cost competitive LNG to the international markets. This year, we are ready to move forward with implementing our next LNG project, Arctic LNG 2, and this past May, we agreed in principle with our long-term partner TOTAL to enter the project and in March 2019, the deal was closed. The intention of our respected partner to enter into the Arctic LNG 2 project at an early stage confirms the outstanding economic attractiveness and huge perspectives of future LNG projects on the Yamal and Gydan peninsulas.

Arctic LNG 2 is based on the prolific hydrocarbon resources of the Utrenneye field located on the Gydan peninsula. The project provides for the construction of three LNG trains at 6.6 mmtpa each, for a combined total of 19.8 mmtpa. Through innovation and technology, our goal for Arctic LNG 2 is to significantly reduce



**Our large, high-quality, low-cost resource base in the hydrocarbon-rich Yamal and Gydan peninsulas underlies our ambitious growth strategy**



**Nyakhartinskoye field**



**North-Obskoye field**



**Utrenneye field**

the liquefaction capital costs by using gravity-based structures (GBS) as the project's platform. In late 2018, we completed the front end engineering and design work, or FEED, confirming the commercial viability of the project's concept and estimated capital costs. Correspondingly, Arctic LNG 2 signed contracts on the design and construction of GBS, and the supply of turbo machinery equipment. In parallel, during 2018, we made ongoing construction progress at the LNG construction yard in the Murmansk Region, which will serve as the center for fabrication and construction of GBS platforms.

We can substantially facilitate global LNG trade and decrease the travel distance of the Arc7 ice-class tankers by constructing our transshipment facilities in the Murmansk Region (westbound cargos) and at Kamchatka (eastbound cargos). This provides our commercial trading group with various options to trade LNG cargos to maximize netback margins based on trading spreads between the Pacific and Atlantic LNG trades. Moreover, we signed an agreement during the past year with the Ministry of the Russian Federation for the Development of the Far East and the Government of the Kamchatka Territory on the construction of a marine LNG transshipment complex in the Kamchatka region. It is paramount that we optimize our LNG logistical model to ensure the most effective and efficient year-round transport scheme.

NOVATEK plans to significantly increase production of natural gas and LNG, and we are interested in developing the whole natural gas value chain to enhance the competitive advantages of our scalable low-cost LNG projects. In 2018, we concluded several Memorandums of Understanding in relation to the Company's current and future LNG projects.

Our large, high-quality, low-cost resource base in the hydrocarbon-rich Yamal and Gydan peninsulas underlies our ambitious growth strategy. In 2018, we successfully expanded our resource base through exploration works as well as obtaining new mineral licenses on the Yamal and Gydan peninsulas. Over the past several years we have managed to acquire through tenders and auctions very enviable license areas to support our future LNG growth ambitions. We will continue to deploy capital to our exploratory activities to prepare these license areas for future LNG projects.

Our first exploration well testing the North-Obskiy license area located in the shallow waters of the Ob Bay yielded a new field discovery called the North-Obskoye field. The North-Obskoye field was the single standalone largest gas discovery in the world in 2018 with natural gas reserves attributable to the first exploration well amounting to 322 billion cubic meters (bcm) according to the Russian reserve classification methodology.

In 2018, significant reserve growth was also confirmed at the Utrenneye field with the discovery of two new



hydrocarbon deposits increasing the field's natural gas reserves up to about 2 trillion cubic meters. The new deposits expand the field's reserve potential and open additional opportunities for implementing the Arctic LNG 2 project.

Our exploration success was not only confined to the Yamal and Gydan peninsulas. We discovered the Nyakhartinskoye field, located in close proximity to the Company's Yurkharovskoye field. This represents a very important reserve discovery to maintain NOVATEK's natural gas production output in the area of the Unified Gas Supply system.

The Company's reserves were also positively impacted by successful exploration works at the Utrenneye, Urengoyevskoye (Samburgskiy license area) and Yarudeyskoye fields, as well as production drilling at the South-Tambeyskoye, North-Russkoye and Yaro-Yakhinskoye fields.

We obtained the following new licenses: the South-Leskinskiy, Payutskiy, Palkurtoiskiy, Centralno-Nadoyakhskiy, Beregovoy, Ust-Yamsoveyskiy and Chernichniy license areas.

Our total SEC proved reserves, including the Company's proportionate share in joint ventures, aggregated 15,789 million barrels of oil equivalent (boe), including 2,177 bcm of natural gas and 181 million metric tons (mmt) of liquid hydrocarbons. At year-end 2018, our total proved reserves increased by 4% compared to year-end 2017, representing a reserve replacement rate of 222% for the year, the addition of 1,218 million boe, inclusive of 2018 production. We retained our core competitive advantage by being ranked among the lowest cost hydrocarbon producers globally, and our lifting costs remained at a very low level of \$0.6 per boe. We are fully committed to our strategy providing for strict cost control and conservative financial policies.



**Natural gas sales volumes, including volumes of LNG sold, 11% growth as compared with 2017**

During the past year, NOVATEK's hydrocarbon production totaled 549.1 million boe, including 68.8 bcm of natural gas and 11,800 thousand tons of liquids (gas condensate and crude oil), representing an increase in total hydrocarbons produced by 35.8 million boe, or by 7.0%, as compared with 2017. The positive factors contributing to our production growth were mainly attributable to



**The Company built a new residential school for 800 schoolchildren in the Gyda settlement located on the Gydan Peninsula. It is crucial that we give back to society and develop the future generation of Russia.**

the launch of the three trains at Yamal LNG and the acquisition of new assets at the end of 2017 and first quarter 2018.

We had a very successful year marketing natural gas to both the domestic and international markets. Our natural gas sales volumes, including LNG volumes sold, aggregated 72.1 bcm, representing an increase of 11.0% as compared with 2017. Volumes of natural gas sold in the Russian domestic market in 2018 were 66.1 bcm, whereas LNG volumes sold on international markets amounted to 6.1 bcm or 57 cargoes of LNG. Sales volumes of LNG in 2017 were 0.1 bcm as Yamal LNG commenced LNG shipments on 8 December 2017.

Our current business generates sufficient operating cash flows to internally fund our operations, service our debt and liabilities, and distribute cash to our shareholders in the form of dividends. Our strong cash flow generated from our core domestic business has allowed us to significantly reduce our long-term debt portfolio and maintain strong credit metrics. In 2018, our revenues increased by 43% to RR 832 bln and our normalized EBITDA increased by 62% to RR 415 bln while our normalized profit increased 49% to RR 233 bln.

Based on the Company's financial results, the Board of Directors recommended to the General Meeting of Shareholders to approve dividends for 2018 at RR 26.06 per share, exceeding the dividend paid out for the previous year by 74.3%.

TWO THOUSAND AND EIGHTEEN began the transformation of NOVATEK into a global gas company. We will play a major role in the global LNG markets and our ambitious strategic goal to be one of the largest single LNG producers in the world is supported by our unique resource potential, professional competences, exceptional experience gained with the launch of Yamal LNG, a balanced investment portfolio, keen focus on cost control and adherence to strict financial policies. These characteristics are the hallmark of a successful company but they alone are not sufficient to attain the status of a truly great company. We must take a responsible approach to our business conduct. NOVATEK seeks to



### Increase of normalized EBITDA to RR 415 bln

comply with the best sustainability principles taking into consideration the interests of all stakeholders when making decisions. We see sustainable development as one of the cornerstones of our future growth and key to EXPANDING OUR GLOBAL LNG FOOTPRINT.

YNAO is the principal home of our major oil and gas operations. Social commitments are often overlooked in the grander scheme of our development activities and lofty LNG ambitions but it is crucial that we give back to society and develop the future generation of Russia. We are very proud to have built a new residential school for 800 schoolchildren in the Gyda settlement located on the Gydan peninsula. This past year began the first academic year for students in a new school. We also launched the "Health Territory" charity project assisting children with medical care and targeted aid in the Yamal Nenets Autonomous Region (YNAO).

We were recognized for our efforts in environmental protection, social responsibility and corporate governance by the global community. In 2018, NOVATEK remained a constituent of the FTSE4Good Emerging Index of FTSE Russell Ratings. We became the winner of the 2018 National Environmental Award named after Vladimir Vernadskiy in the nomination "Innovative Eco-efficient Technologies in Industry and Energy" with our "Arctic Cascade" liquefaction technology; and the winner of the "Change Management. Visionaries." award with our Sustainability Report in the category "Disclosure of Information on Social Impact".

We would not be here today if it were not for the thousands of dedicated employees working at NOVATEK and our joint ventures. Human capital is mission critical to develop a world-class company based on innovation and technology to drive our next wave of LNG projects

and maintain our commitment to our core domestic business. We thank all of our employees for their commitment and dedication as we continue our journey of transforming NOVATEK into a global gas company.

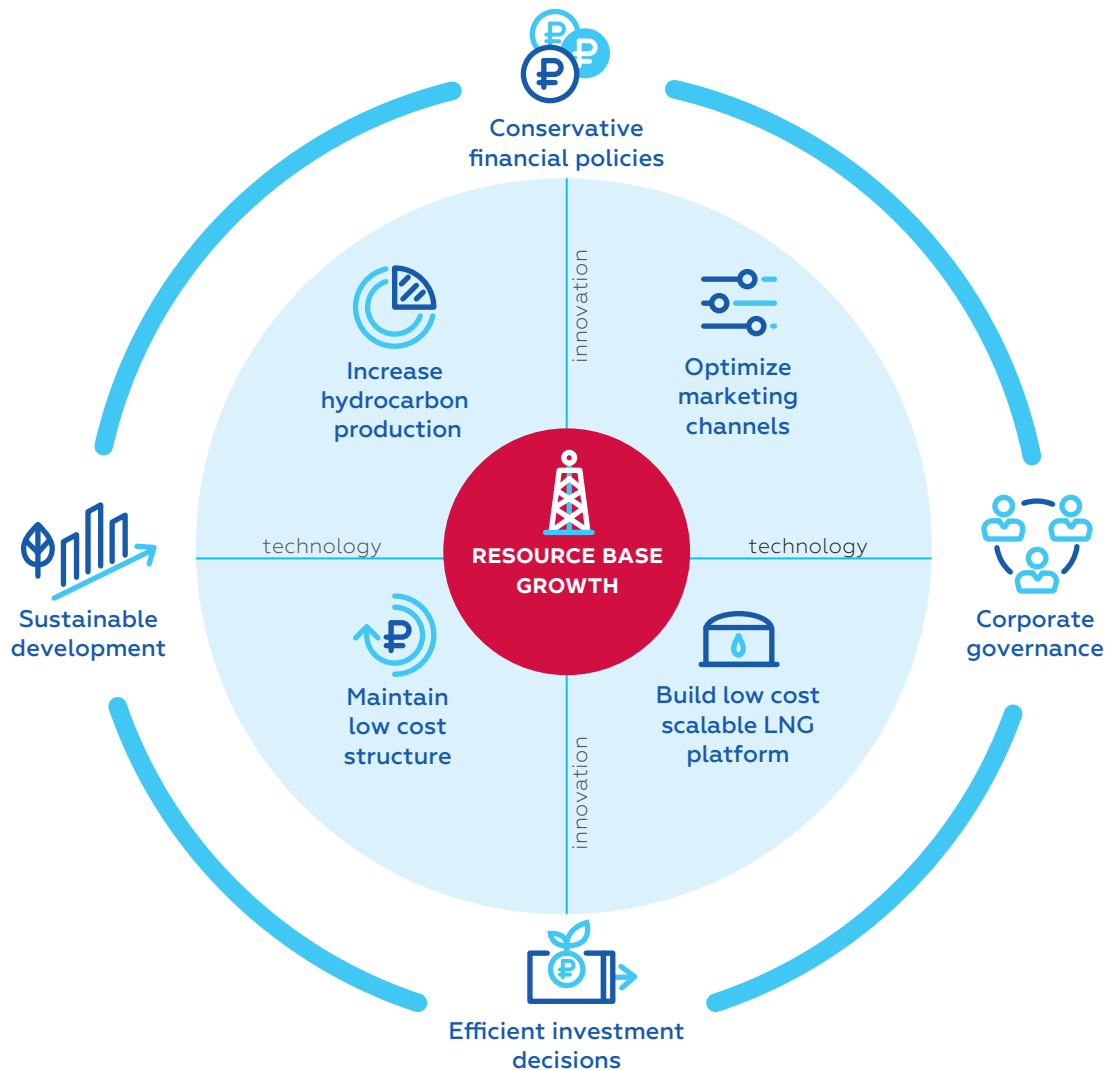
On behalf of the Board of Directors and Management Board, we are pleased to present to all our valued stakeholders the Company's 2018 Annual Report. We would like to thank everyone for your continued support, as we remain committed to growing NOVATEK and EXPANDING OUR GLOBAL LNG FOOTPRINT while implementing the best international practices and principles of sustainable development.

**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



## Resource base growth

- Organic resource growth from exploration and development activities on the Yamal and Gydan peninsulas
- Strategic acquisitions and active participation in license tenders

## Increase hydrocarbon production

- Increase gas production through development of projects within the UGSS and LNG projects in the Arctic
- Development of deeper Jurassic and Achimov layers
- Fully utilize processing capacity of Ust-Luga complex

## Maintain low cost structure

- Remain one of the lowest cost hydrocarbon producers in the global oil & gas industry
- Optimize cost structure through strategic investment of capital
- Develop low cost LNG value chain

## Optimize marketing channels

- Maximize use of Northern Sea Route and develop key transshipment points
- Build diversified LNG trading portfolio
- Develop strategic partnerships with industry partners in key markets

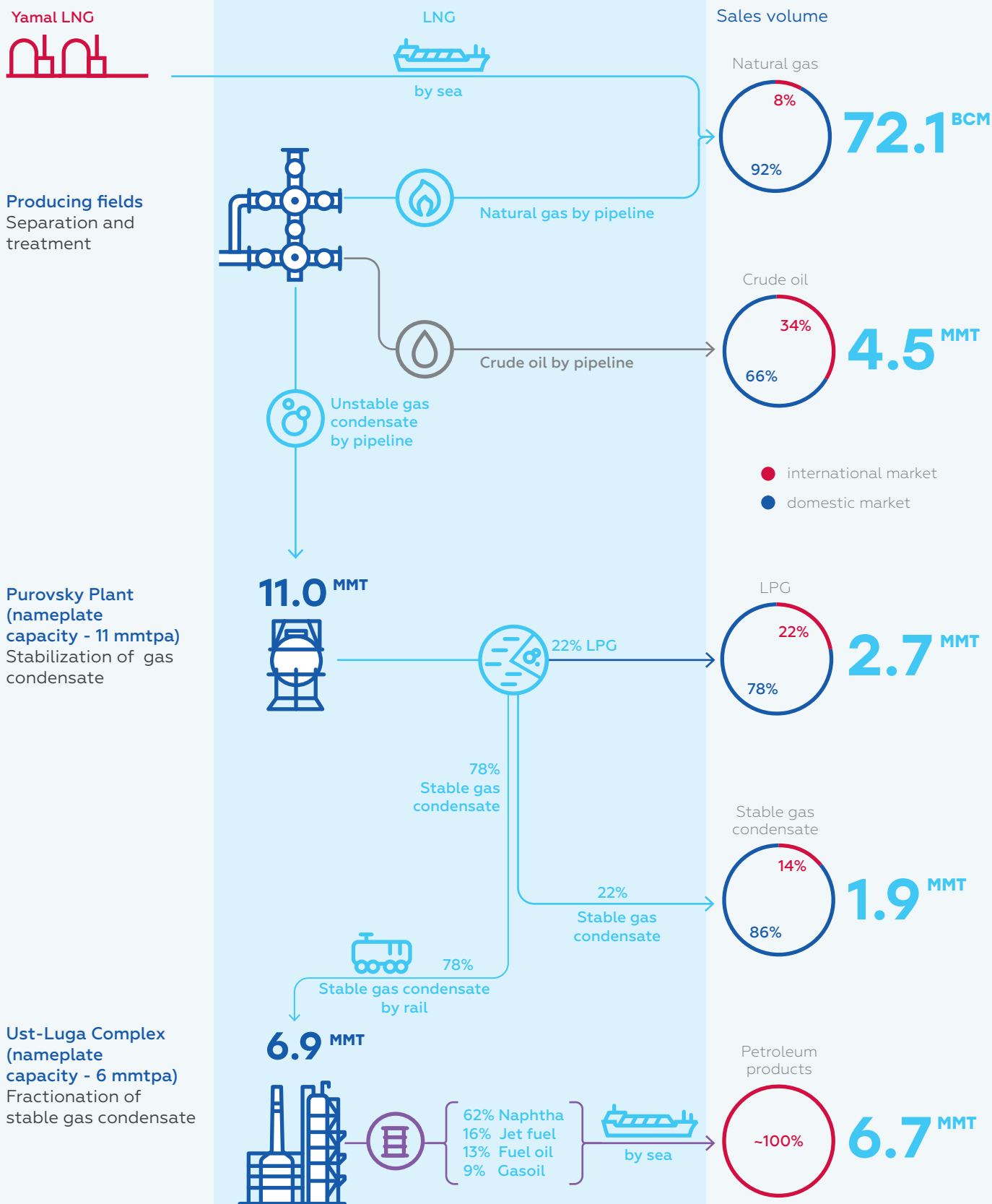
## Build low cost scalable LNG platform

- Increase production through development of scalable LNG projects
- Development of proprietary LNG technologies
- Integrated projects for production and liquefaction of natural gas

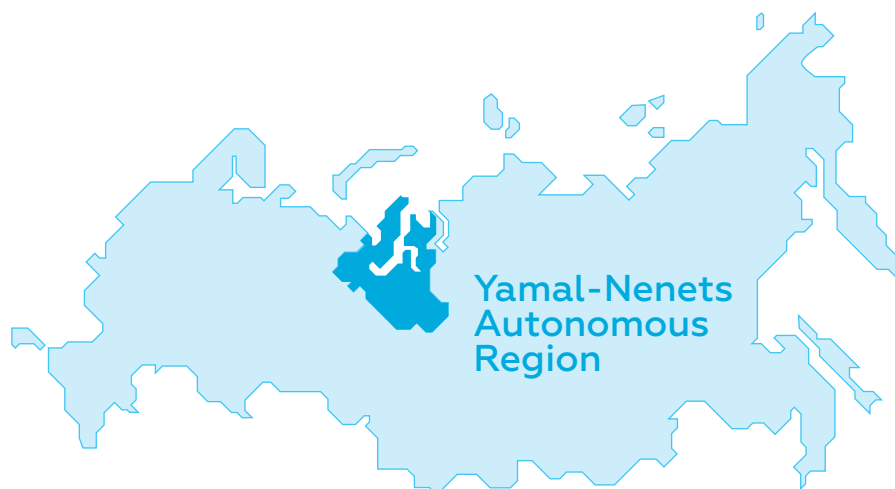
## Sustainable development

- Reduce and prevent negative environmental impact
- Increase the efficiency and rational use of natural resources, energy efficiency

# Business Model



# Hydrocarbon Reserves



**15.79** BLN  
BOE  
Total proved  
hydrocarbon reserves  
(SEC)

**222 %**  
Reserve replacement  
rate



Yamal LNG



Arctic LNG 2



Purovsky Gas Condensate Processing Plant



Gas condensate pipelines of NOVATEK

**56**

fields and license areas



Producing Fields



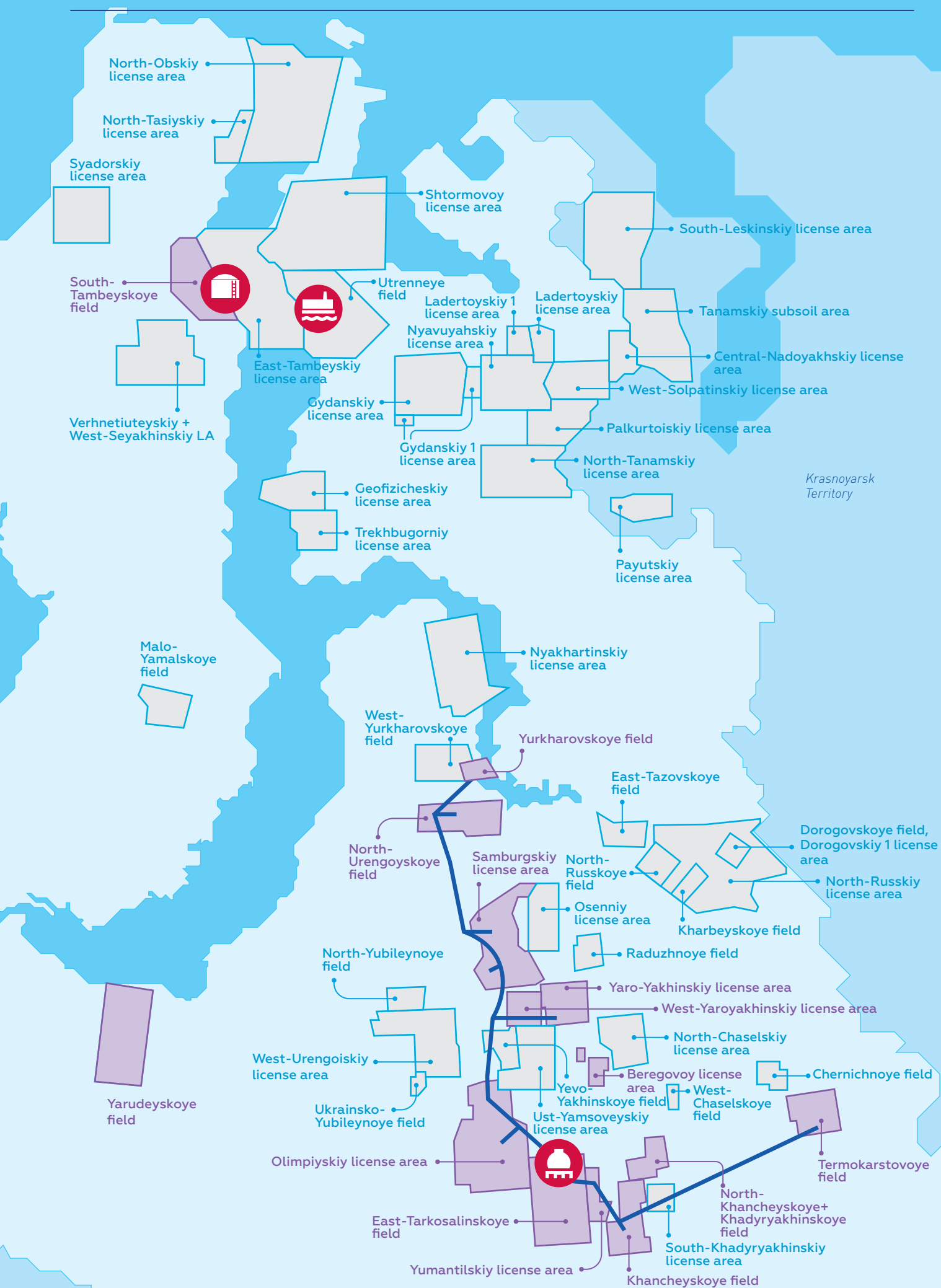
Prospective Fields and  
License Areas



Yamal-Nenets  
Autonomous Region

↓ Syskonsynynskiy LA  
(located in KMAO)





# Yamal LNG

YAMAL LNG

UNIQUE integrated project for production, liquefaction and sale of natural gas. In 2018, three LNG trains reached full capacity.

# No. 1

Yamal LNG is the largest LNG project in Russia

## TRAINS LAUNCH

3

➤ **12** months ahead of schedule

2

**6** months ahead of schedule

1

on schedule



# 5.5

MMTPA

Nameplate capacity of each of the three trains in operation



THE PROJECT WAS  
CONSTRUCTED AND  
COMMISSIONED  
**ON BUDGET**

# Arc7



The project is supported by a fleet of Arc7 ice-class tankers supplemented by lower ice-class designated tankers to transport LNG cargos



# 17.4<sup>MMTPA</sup>

LNG liquefaction capacity after Train 4 launch



## ARCTIC CASCADE

NOVATEK's patented proprietary liquefaction technology will be utilized for construction of Train 4

# 113

LNG cargos offloaded from Yamal LNG in 2018



# 0.9<sup>MMTPA</sup>

Nameplate capacity of Train 4



# 8.6<sup>MMT OF LNG</sup>

LNG production at Yamal LNG in 2018



# Arctic LNG 2

Arctic LNG 2 is the second LNG project of NOVATEK which includes the construction of three LNG trains, with a total design capacity of 19.8 mmtpa



The Utrenneye field is the resource base for the Project



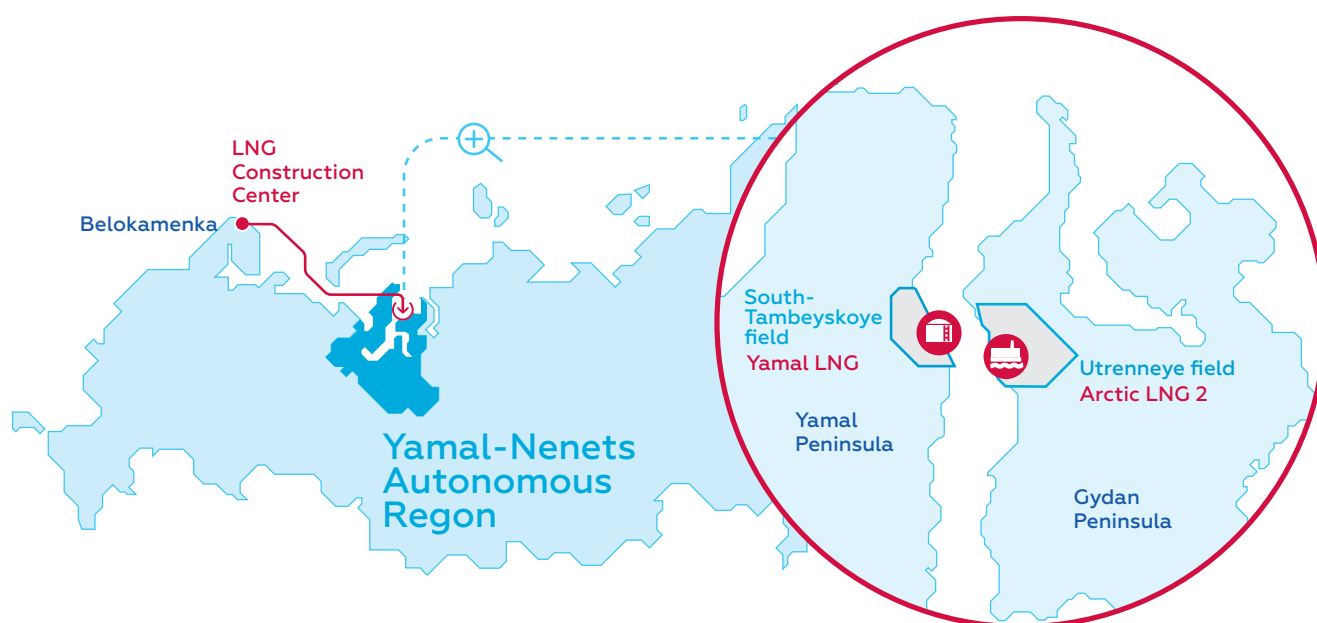
Innovative construction concept using gravity-based structures (GBS)



LNG trains will be fabricated at NOVATEK's LNG Construction Center



Three LNG trains at 6.6 mmtpa each



Exploration drilling at the Utrenneye field



## LNG CONSTRUCTION CENTER

LNG construction center is the world's first complex to build GBS-based LNG trains.

The LNG Construction Center will comprise two dry docks to build GBS and facilities to manufacture topside modules. This new facility will establish a state-of-the-art LNG platform in Russia, create new jobs in engineering and production, and also contribute to regional economic development

## Utrenneye field's reserves under PRMS as of 31.12.2018

# 1,138

BCM OF  
NATURAL  
GAS

# 57

MMT OF LIQUID  
HYDROCARBONS

## CONCEPT



In 2018:

Completed the front end engineering and design work (FEED)

**Contracted more than 50% of the equipment for the Project**



Started site preparation, construction of early phase power supply facilities, production wells drilling and berth construction



Signed a contract on the design and construction of GBS

Signed an agreement for the supply of turbo machinery equipment, including the supply of gas turbine compressors and gas turbine generators for the three liquefaction trains



NOVATEK and TOTAL agreed in principle on the entry into the Arctic LNG 2 providing for a purchase by TOTAL of a 10% participating interest in the project. The deal was closed in 2019

## KEY ADVANTAGES

- Optimize and reduce CAPEX per ton of LNG liquefaction
- Low cost, onshore conventional natural gas
- Reduce construction and logistical costs as main LNG equipment is built and installed at the LNG construction center
- High local content
- Minimize scope of work in the Arctic area
- Minimize environmental impact

## Total area over 150 Ha



Accommodation camp up to 15,000 people



Concrete batch plant 180,000 cubic meters per annum



Reinforced concrete structures fabrication shops



Process module fabrication shops (up to 100,000 tons per annum)



# Cryogas-Vysotsk

**CRYOGAS**  
**VYSOTSK**

Cryogas-Vysotsk is our first medium-scale LNG project on the Baltic Sea



LNG production facility is located in the port of Vysotsk, the Leningrad Region

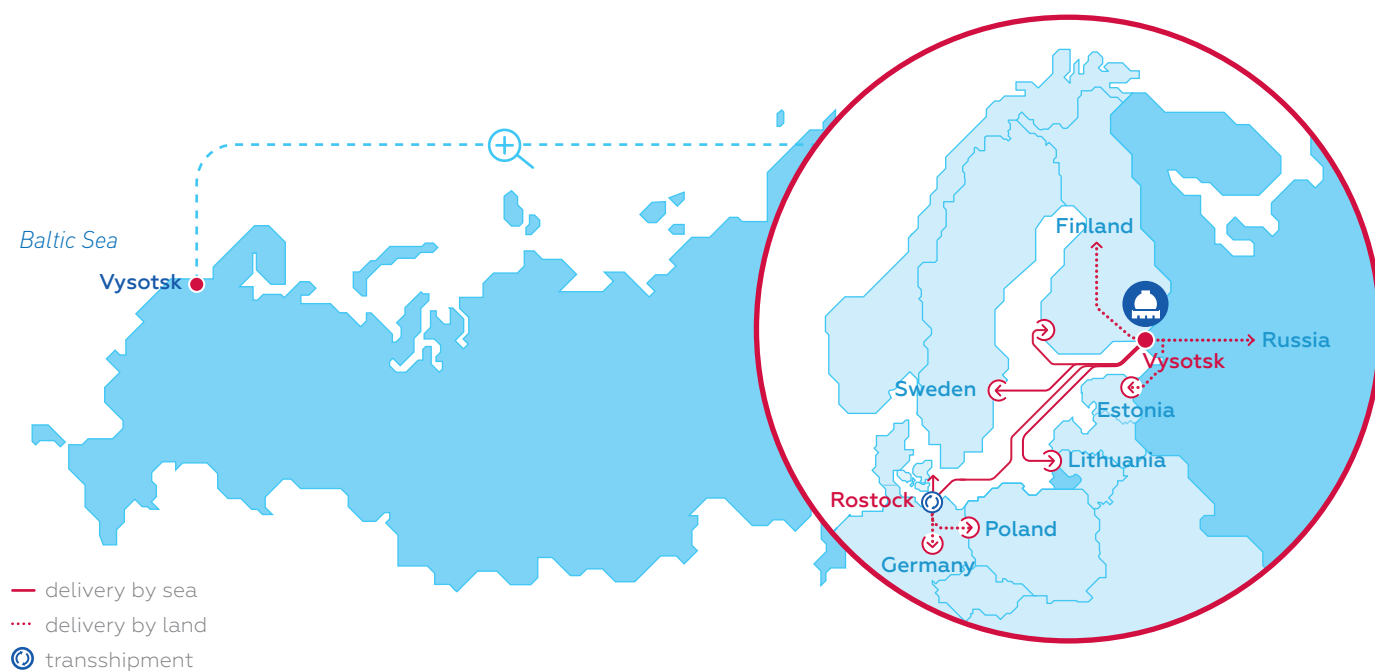


Sales:

- Domestic market
- Baltic, Scandinavian and North-Western European markets
- Refueling of bunkering vessels and sales of LNG as a motor fuel



The project infrastructure includes two LNG trains with a capacity of 330 mtpa each, a 42 mcm LNG storage tank and an offloading terminal



**We see vast prospects in using LNG as marine fuel and motor fuel to substitute for diesel and fuel oil, that will contribute to decreasing emissions and improving the environment.**

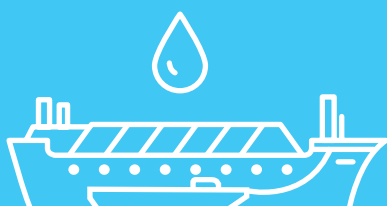
NOVATEK and Fluxys established a joint venture to design, build, finance, own and operate a medium-scale LNG transshipment terminal with a capacity of about 300 mtpa in the port of Rostock, Germany.

The transshipment terminal will receive LNG carriers from the Cryogas-Vysotsk liquefaction facility and further LNG deliveries to the consumer market will be made via trucks. It will also have an option of bunkering and loading of bunkering vessels.

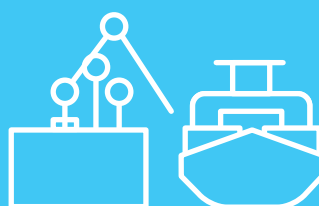
# 660

MTPA OF  
LNG

Initial design capacity



Bunkering



Shipping berth designed to handle up to 30 mcm  
capacity LNG tankers

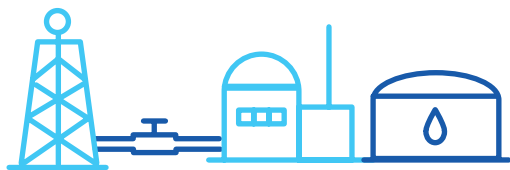


# Key Events and Achievements 2018



## YAMAL LNG

- The Yamal LNG project reached its full capacity more than a year ahead of the initial schedule. **First LNG cargos** were shipped to Europe, the Asian Pacific region and Latin America. Yamal LNG carried out **the first ship-to-ship LNG transshipment**.



## "ARCTIC CASCADE"

- We patented the "Arctic Cascade" **proprietary liquefaction technology** for use at Train 4 of Yamal LNG.
- NOVATEK was recognized by **the National Environmental Award** named after Vladimir Vernadskiy in the nomination category of "Innovative Eco-efficient Technologies in Industry and Energy" for its Arctic Cascade natural gas liquefaction process.



## LARGE GEOLOGICAL DISCOVERIES

- We discovered the **North-Obskoye field** through our successful exploration efforts, which was named the **world's largest standalone gas field discovery** in 2018. A new field called **Nyakhartinskoye** was also discovered. While testing a prospecting well at the Utrenneye field, we discovered new gas condensate deposits and confirmed the commercial productivity of the field's Middle Jurassic layer.
- We **acquired mineral licenses** for the Beregovoy, Ust-Yamsoveyskiy, Payutskiy, Palkurtoiskiy, Central-Nadoyakhskiy, South-Leskinskiy and Chernichniy license areas.
- The Company commissioned the oil deposits at the **Yaro-Yakhinskoye** oil, gas and condensate field (Arcticgas).



## DEVELOPMENT OF LNG BUSINESS

- NOVATEK and TOTAL agreed in principle on TOTAL's entry into **Arctic LNG 2**. The deal was closed in 2019.
- We **signed contracts** with SAREN on the design and construction of gravity-based structures (GBS) and Nuovo Pignone on the supply of turbo machinery equipment for **the Arctic LNG 2 project**.
- An agreement was signed with the Ministry for the Development of the Russian Far East and with the Government of the Kamchatka Region for the **construction of an offshore LNG transshipment terminal**.
- We signed **strategic cooperation agreements** on LNG projects with Sovcomflot, Rosatom, Siemens, and SACE, the Italian export and credit agency.
- **Memorandums of Understanding** were signed with Saudi Aramco, KOGAS, the Japan Oil, Gas and Metals National Corporation (JOGMEC) and Japan's Saibu Gas.



- We created a joint venture with Fluxys for the construction of a mid-scale LNG transshipment terminal in **the port of Rostock** in Germany.



- NOVATEK incorporated the **Maritime Arctic Transport LLC**, a wholly owned subsidiary to manage and optimize shipping costs, and to build unique competencies in Arctic navigation.



## SUSTAINABLE DEVELOPMENT

- NOVATEK remained a constituent in the FTSE4Good Emerging Index published by FTSE Russell Ratings. For its Sustainability Report, the company received the **"Change Management. Visionaries." Award** in the Social Impact Disclosure category.
- A new **"Health Territory" charity project** was launched aimed at providing medical aid to children from the regions where we operate.
- A new **boarding school** for 800 children was built in **Cyda village** on the Gydan peninsula, in one of the most remote settlements of the Yamal-Nenets Autonomous Region.



# Key Indicators

	Unit	2017	2018	Change
<b>Financial indicators</b>				
Total revenues	RR mln	583,186	831,758	42.6%
Normalized profit from operations <sup>1</sup>	RR mln	163,751	225,539	37.7%
Normalized EBITDA (including share in EBITDA of JVs) <sup>1</sup>	RR mln	256,464	415,296	61.9%
Normalized profit attributable to shareholders of PAO NOVATEK <sup>2</sup>	RR mln	156,166	232,930	49.2%
Normalized earnings per share, basic and diluted <sup>2</sup>	RR	51.78	77.29	49.3%
Net cash provided by operating activities	RR mln	180,399	216,349	19.9%
Cash used for capital expenditures <sup>3</sup>	RR mln	29,871	94,038	214.8%
Free cash flow	RR mln	150,528	122,311	(18.7%)
<b>Operating indicators</b>				
Proved natural gas reserves (SEC)	bcm	2,098	2,177	3.8%
Proved liquid hydrocarbon reserves (SEC)	mmt	164	181	10.4%
Total hydrocarbon reserves (SEC)	mmboe	15,120	15,789	4.4%
Natural gas production	bcm	63.4	68.8	8.5%
Liquid hydrocarbons production	mt	11,774	11,800	0.2%
Proportionate share in LNG production of JVs <sup>4</sup>	mt	162	5,152	n/a
Total production	mmboe	513.3	549.1	7.0%
Daily production	mmboe/day	1.41	1.50	7.0%
<b>Positions in Russia</b>				
Share in natural gas production <sup>5</sup>	%	9.1	9.3	0.2 p.p.
Share in liquid hydrocarbons production <sup>5</sup>	%	2.2	2.1	(0.1 p.p.)

1. Excluding the effect from disposal of interests in joint ventures.

2. Excluding the effects from the disposal of interests in joint ventures, as well as foreign exchange gains (losses).

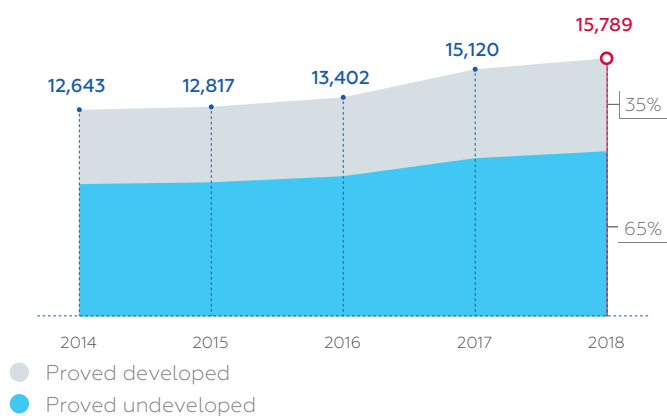
3. Cash used for capital expenditures represents purchases of property, plant and equipment, materials for construction and capitalized interest paid per Consolidated Statement of Cash Flows net of payments for mineral licenses and acquisition of subsidiaries.

4. Natural gas and LNG production at Yamal LNG are reported at 60%.

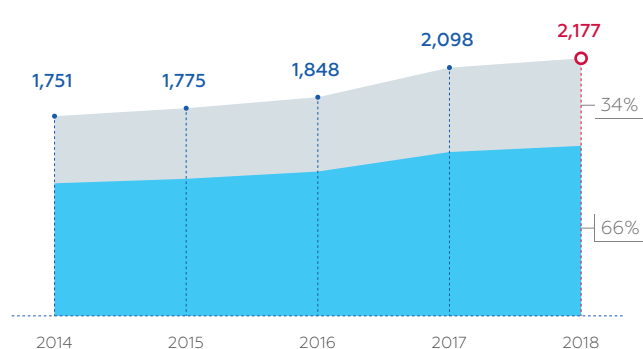
5. According to CDU TEK information.



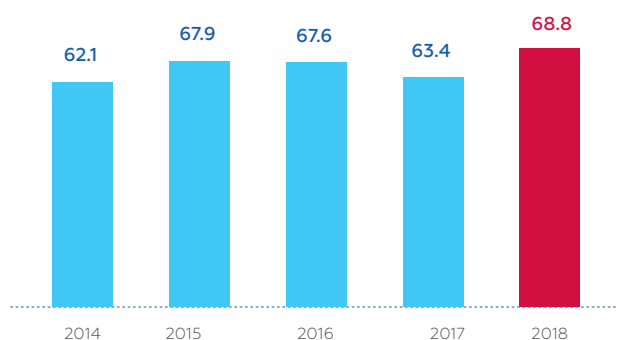
Total proved hydrocarbon reserves (SEC), mmboe



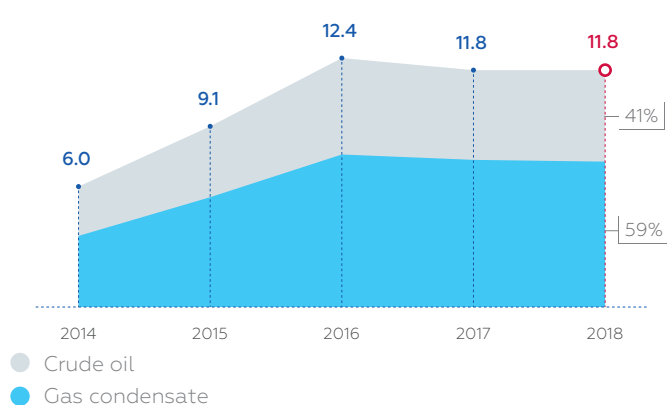
Proved natural gas reserves (SEC), bcm



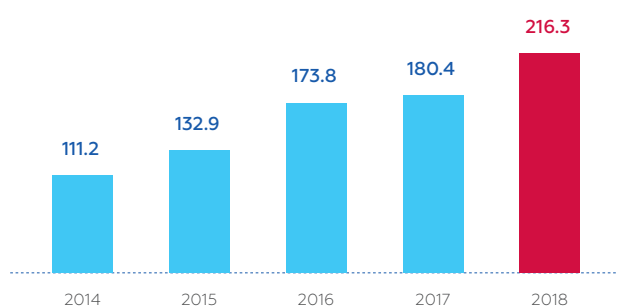
Natural gas production, bcm



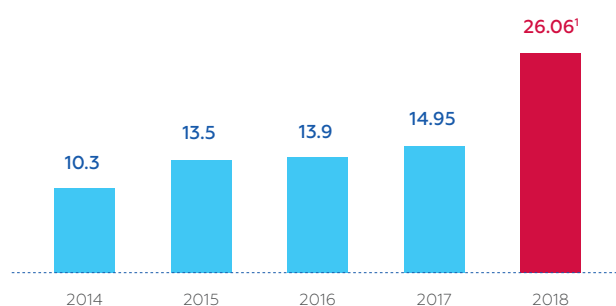
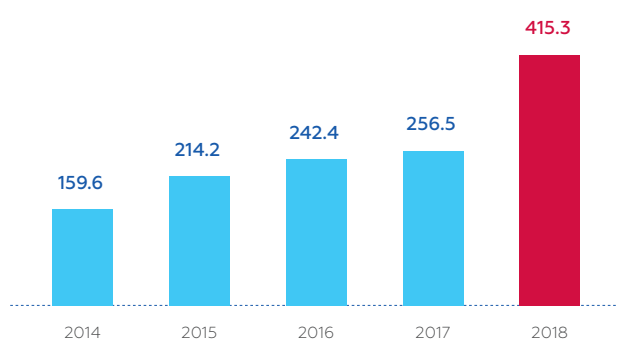
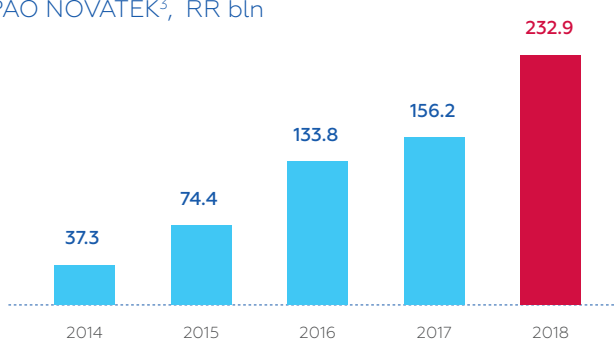
Liquids production, mmt



Operating cash flow, RR bln



Dividends per share, RR

Normalized EBITDA<sup>2</sup>, RR blnNormalized profit attributable to shareholders of PAO NOVATEK<sup>3</sup>, RR bln

1. Recommendation of the Board of Directors.

2. Including share in EBITDA of JVs. Excluding the effect from disposal of interests in JVs.

3. Excluding the effects from the disposal of interests in JVs, as well as foreign exchange gains (losses).

# Geological Exploration and Production

We continued to achieve some of the lowest lifting costs in the industry. In 2018, NOVATEK produced commercial hydrocarbons at 18 fields.

**68.8** <sup>BCM</sup>

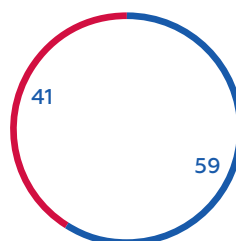
Total natural gas production  
8.5% growth as compared with 2017

**11.8** <sup>MMT</sup>

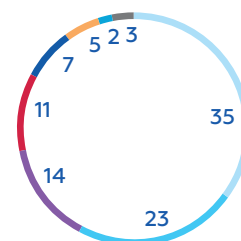
Total liquid hydrocarbons production

**549** <sup>MLN BOE</sup>

Total hydrocarbon production  
7% growth as compared with 2017



Liquid hydrocarbons production breakdown, %:  
 ● gas condensate  
 ● crude oil



Hydrocarbon production breakdown, %:  
 ● NOVATEK-Yurkharovneftegas' fields  
 ● Arcticgas' fields  
 ● NOVATEK-Tarkosaleftegas' fields  
 ● South-Tambeyskoye  
 ● Yarudeyskoye  
 ● North-Urengoyevskoye  
 ● Termokarstovoye  
 ● Others

**54**

years — proved and probable reserve to production ratio (PRMS)



**1.5** <sup>USD</sup>

per boe — 2014–2018 reserve replacement cost



**47.6** <sup>RR BLN</sup>

invested in resource base development

# Processing of Gas Condensate

## 11,017<sup>MT</sup>

Processing of de-ethanized condensate

Total output of the Purovsky Plant in 2018, mt



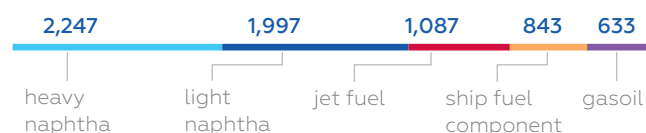
### PUROVSKY PLANT

The Purovsky Plant is the central element in our vertically integrated 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 processes unstable gas condensate into stable gas condensate and natural gas liquids (NGL).

## 6,949<sup>MT</sup>

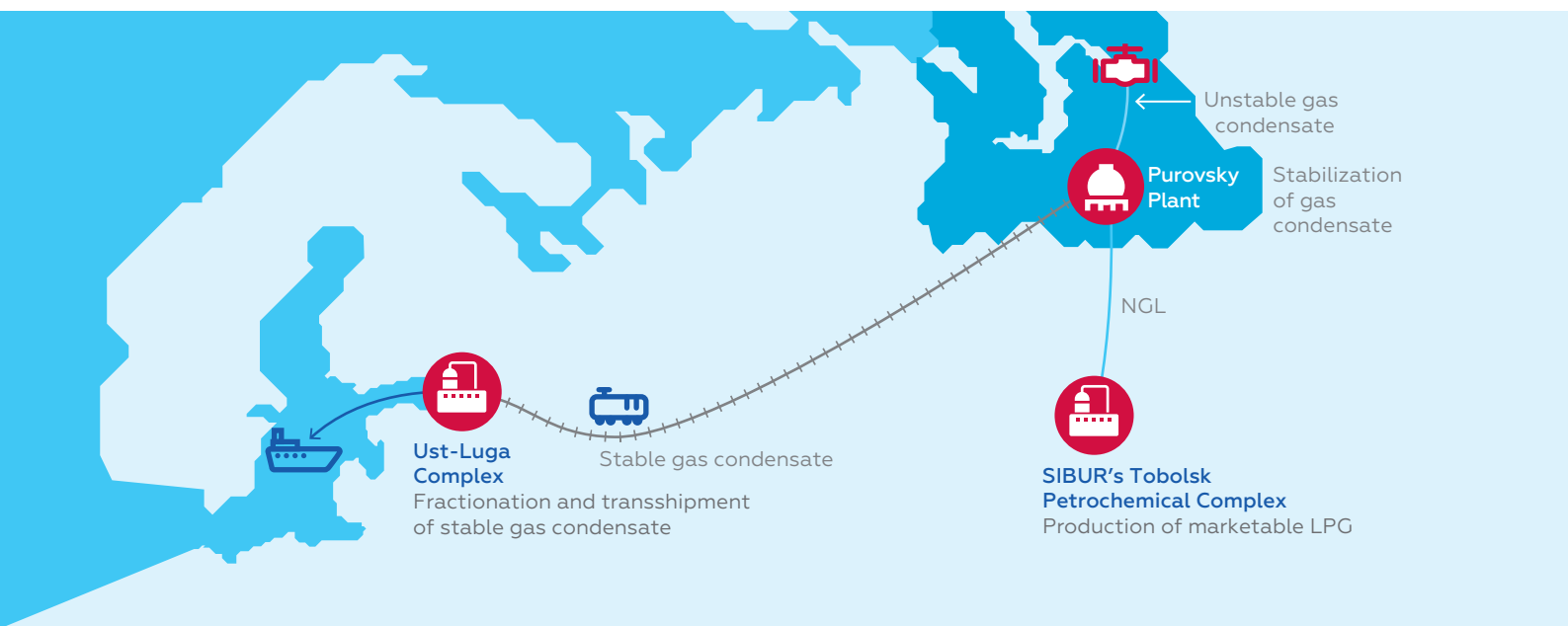
Processing of stable gas condensate

Total output of the Ust-Luga Complex in 2018, mt



### UST-LUGA COMPLEX

The Gas Condensate Fractionation and Transshipment Complex 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.



# Natural Gas Sales

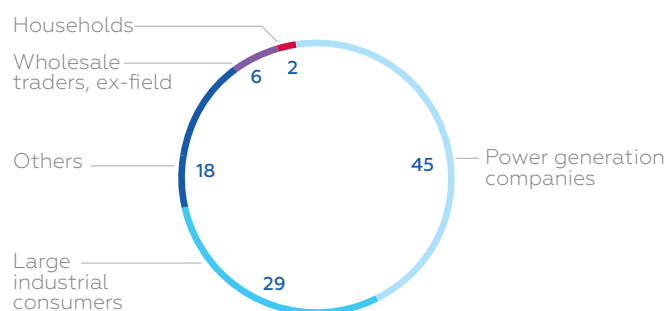
In 2018, natural gas sales volumes, including volumes of LNG sold, aggregated 72.1 bcm, representing an increase of 11% as compared with 2017



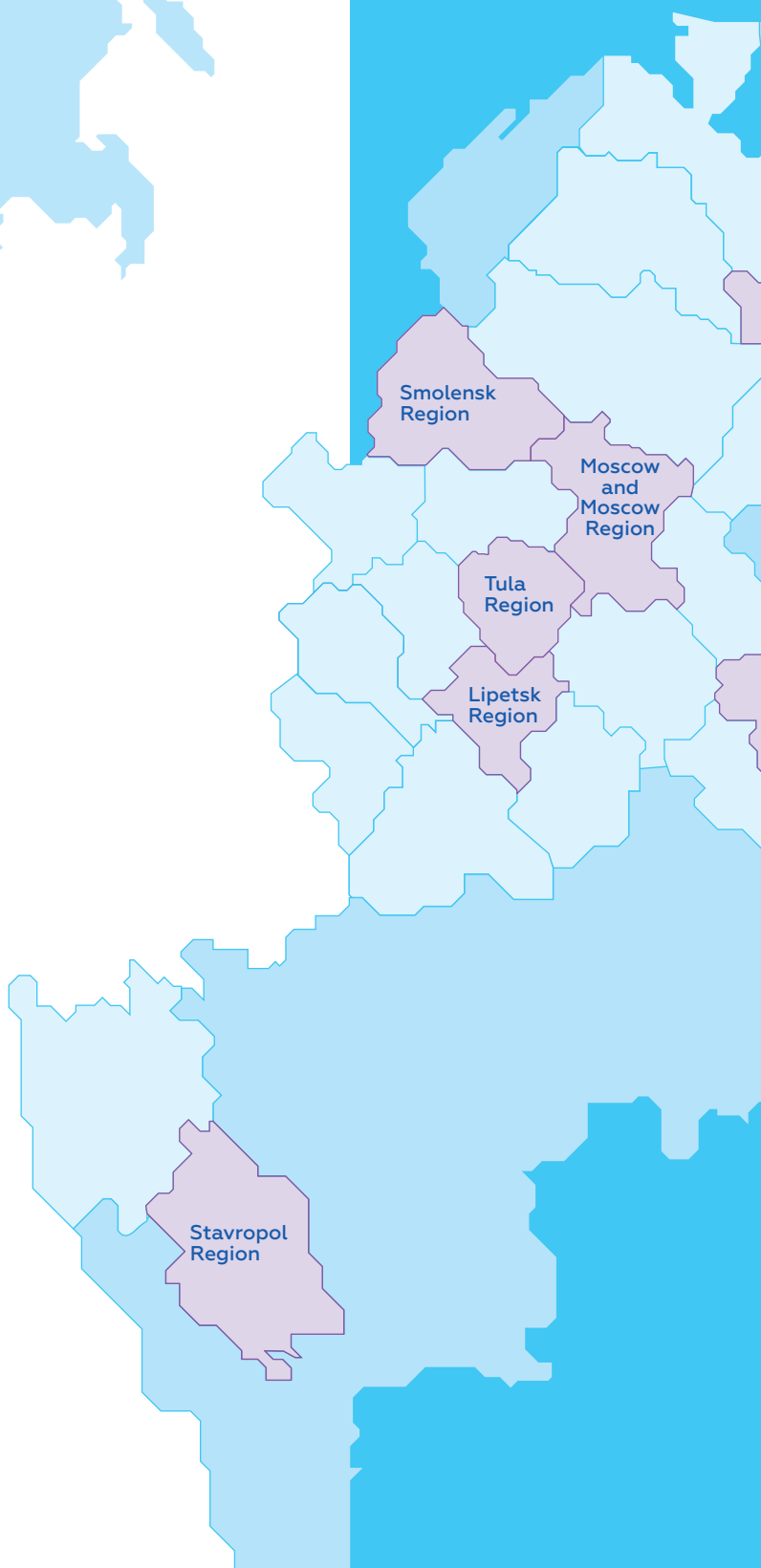
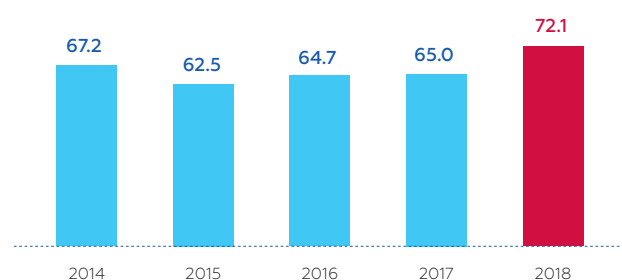
NOVATEK plays an important role in ensuring supplies of natural gas to the domestic market. During 2018, the Company supplied natural gas to 40 regions of Russia.

Revenues from natural gas sales amounted to RR 375.2 billion, representing a 51.5% increase compared to 2017. The revenue increase was mainly driven by start of LNG deliveries from the Yamal LNG project and an increase in sales prices and volumes in the Russian domestic market.

Natural gas sales breakdown on the Russian domestic market by customers in 2018, %



Natural gas sales, bcm

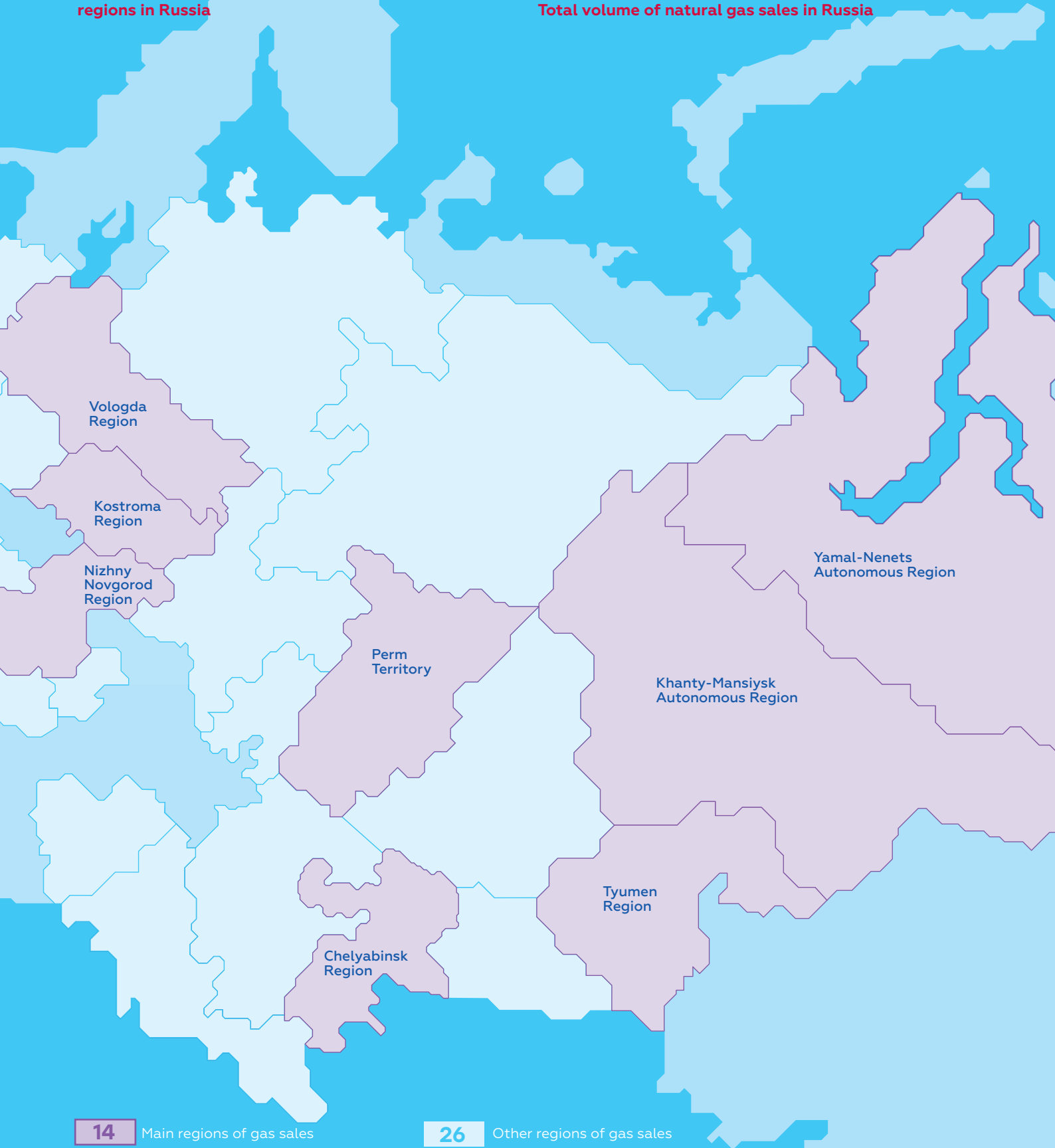


40

regions in Russia

66.1<sup>BCM</sup>

Total volume of natural gas sales in Russia



14

Main regions of gas sales

26

Other regions of gas sales



# LNG Sales

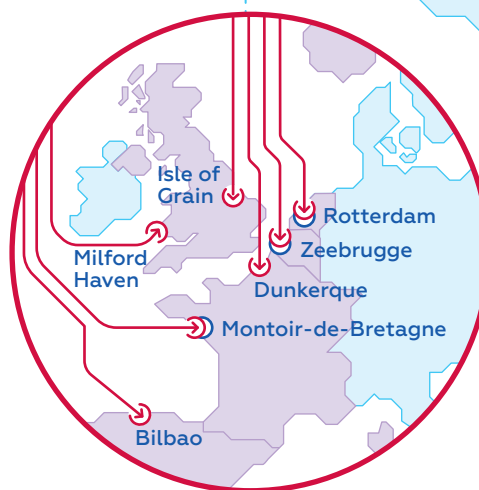
One of our core commercial marketing priorities is to expand our supply geography and grow our presence in the key consuming markets. In 2018, we shipped LNG cargos to Europe, the Asian-Pacific region and Latin America, thus demonstrating the commercial viability of delivering cost-competitive LNG around the globe

## LNG TRANSPORTATION

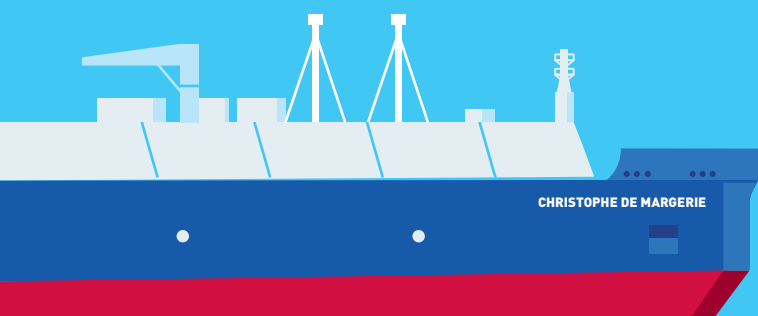
The Arc7 ice-class carriers, designed specifically for NOVATEK's Arctic projects, enable year-round navigation without icebreaker support along westbound navigation routes and, eastbound during the Arctic zones seasonal navigation period, along the Northern Sea Route

**57** LNG CARGOS

sold by NOVATEK in 2018



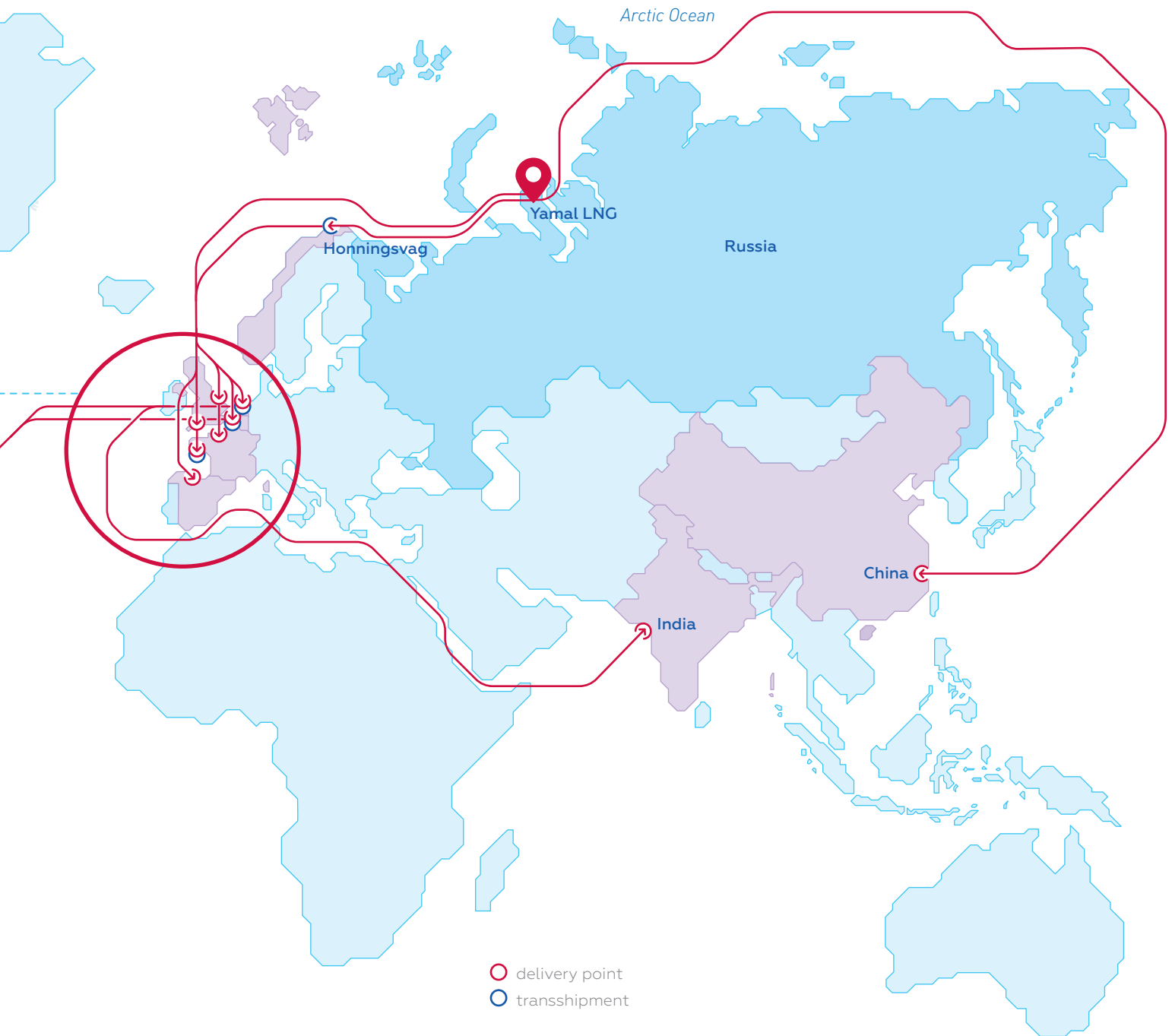
## ARC7 SPECIFICATIONS



**170** MCM  
LNG tanker capacity



**45** MWt  
Vessel power



**19.5** KNOTS

Speed in open water



**5.5** KNOTS

Speed in ice 1.5 m thick



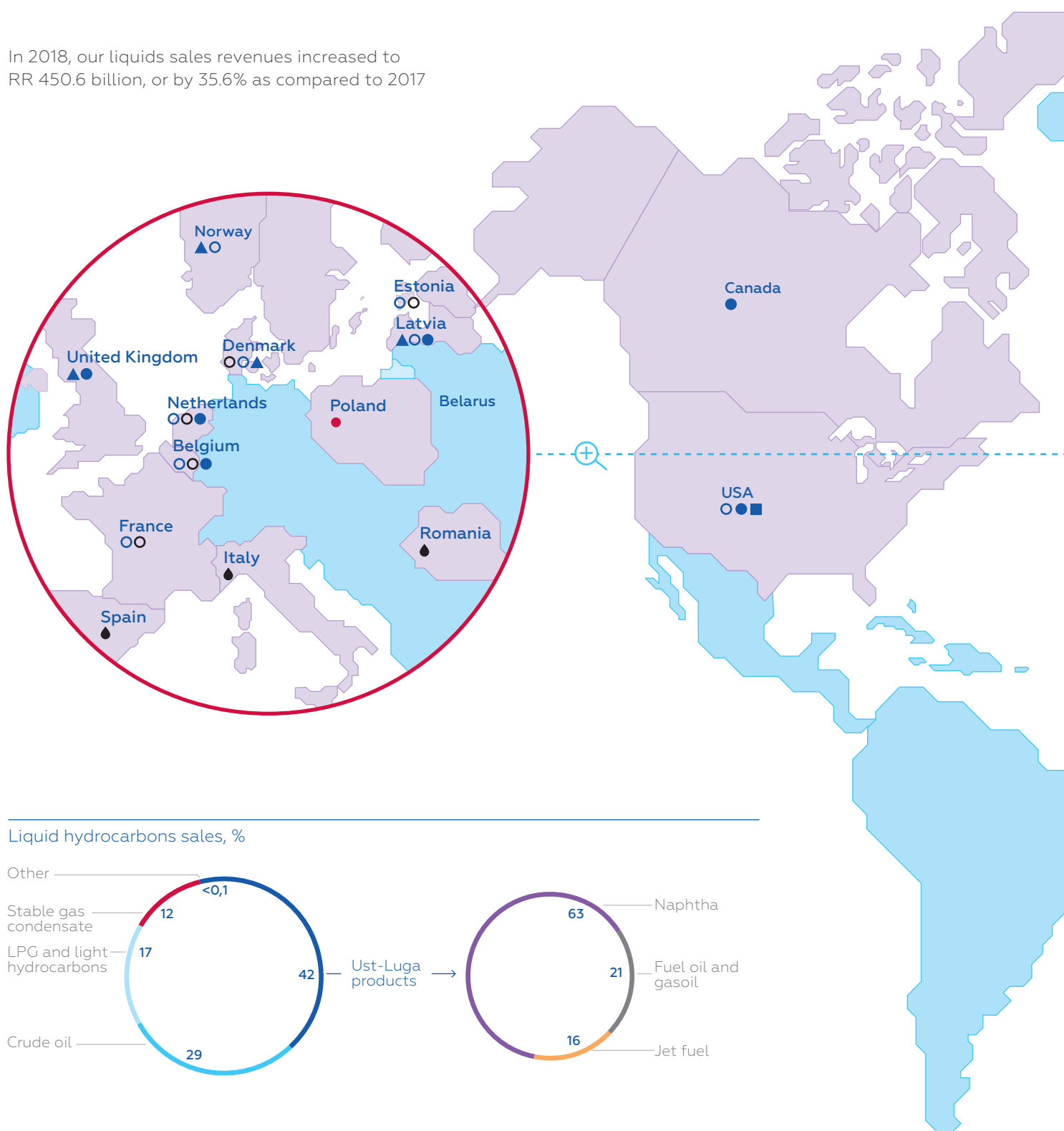
**19** DAYS

The first LNG tanker voyage from the port of Sabetta to China was completed in 19 days as compared to 35 days for the conventional route via the Suez Canal

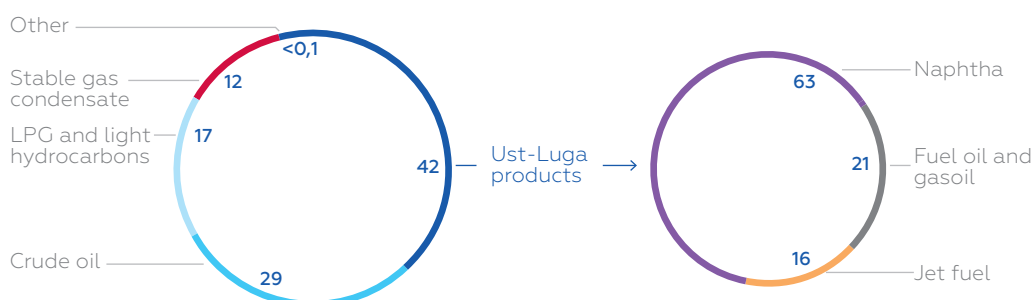
# Liquid Hydrocarbons Sales

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

In 2018, our liquids sales revenues increased to RR 450.6 billion, or by 35.6% as compared to 2017



Liquid hydrocarbons sales, %



15.8<sup>MMT</sup>

Liquid hydrocarbons sales volume

451<sup>RR BLN</sup>

Liquid hydrocarbons sales revenues

- LPG
- Stable gas condensate
- Jet fuel
- Gasoil
- Heavy naphtha
- Light naphtha
- Crude oil
- Fuel oil
- Ust-Luga Complex
- Purovsky Plant
- Export markets





# Environmental and Social Responsibility

## 38%

Reduction of injury frequency rate



### BIODIVERSITY

In 2018, at Yamal LNG we carried out a study of marine mammals' migration routes and an assessment of LNG shipping impact on their population in the northern part of the Ob Bay.

## 11,119 EMPLOYEES

completed OHS training and certification



### ACHIEVEMENTS

NOVATEK's Arctic Cascade liquefaction technology was recognized by the Vernadsky National Environmental Award in the Innovative Eco-Effective Industrial and Energy Technologies category.

## 97.1%

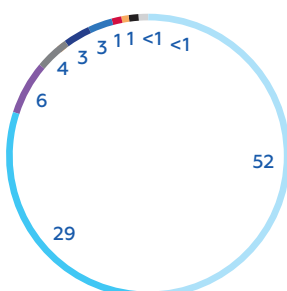
APG utilization rate



### ENVIRONMENTAL PROTECTION

NOVATEK, through its subsidiary NOVATEK-AZK, is implementing a pilot project for the sale of LNG as a motor fuel. Converting a vehicle to LNG enables a significant reduction of soot and carbon monoxide emissions compared to conventional fuels.

Environmental expenses in 2018, %



- Protection and use of water resources
- Environmental protection against production and consumption waste
- Environmental monitoring and evaluation of the background
- Soil protection
- Measures for the protection of flora and fauna and preservation of biodiversity

- Atmospheric air protection and climate change
- Subsurface protection
- Environmental management
- Environmental damage compensation
- Other



# 23%

Reduction of atmospheric emissions

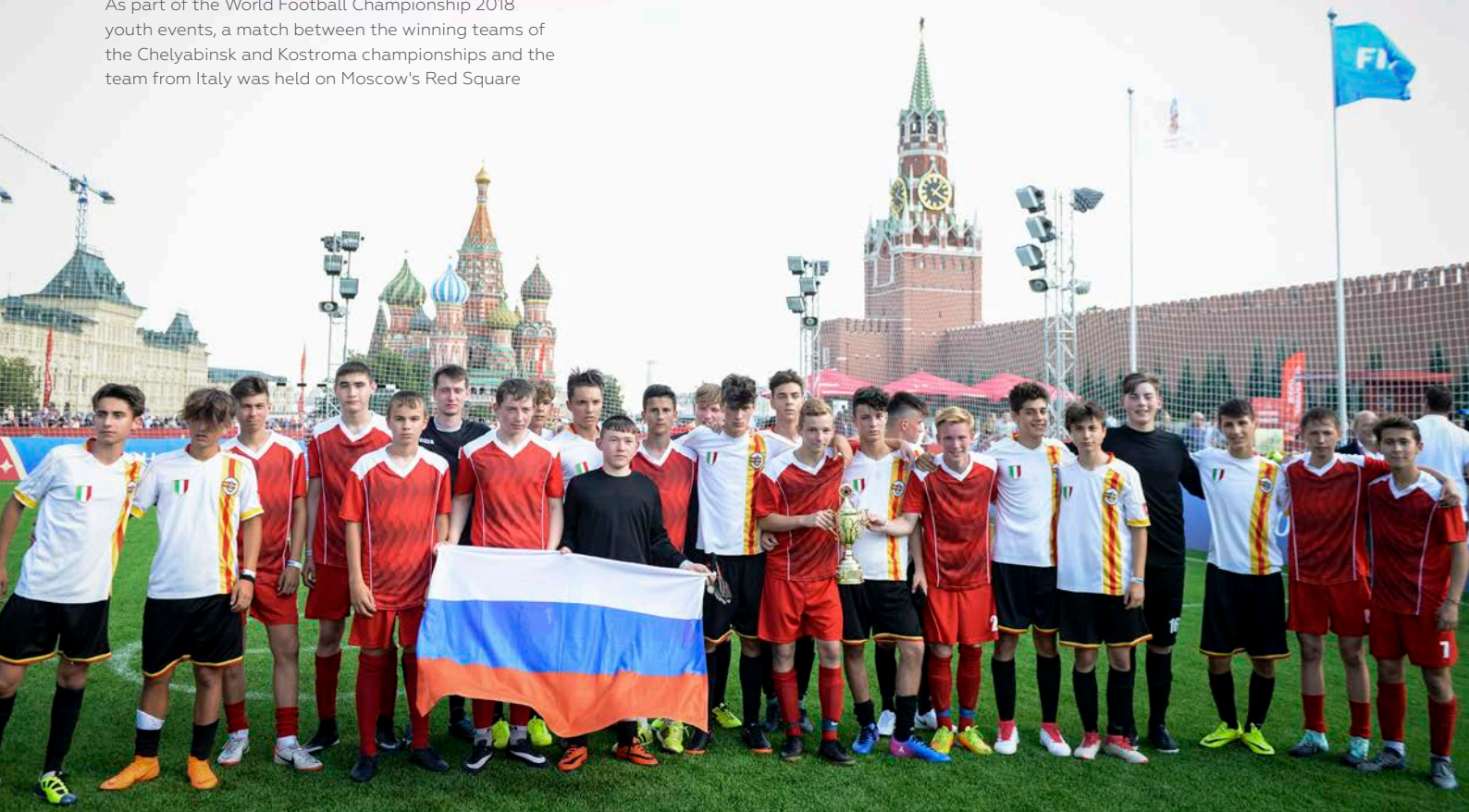
# 2,384<sup>RR</sup><sub>MLN</sub>

Expenses on environment protection and sustainable nature management





As part of the World Football Championship 2018 youth events, a match between the winning teams of the Chelyabinsk and Kostroma championships and the team from Italy was held on Moscow's Red Square



A total of 40.5% of white- and blue-collar workers **upgraded their skills** in 2018.

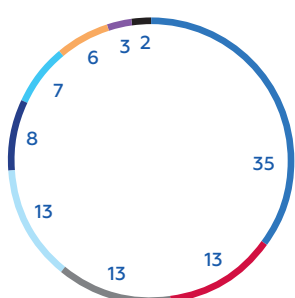


112 young specialists participated in **the Steps in Discovering Talents Program**. We had our sixth class.



In September 2018, Moscow hosted the **13th Interregional Research-to-Practice Conference** for the Company's young specialists attended by 93 employees.

#### Social expenses for employees, %



- Targeted Compensation and Socially Important Payments
- Health Resort Treatment and Rehabilitation
- Pension Program
- Voluntary Medical Insurance
- Culture and sports

- State Guarantees Support Program
- NOVATEK-Veteran Program
- Repayable Financial Aid Program
- Others

# 13,694

employees at NOVATEK, its subsidiaries and joint ventures as of 31 December 2018

# 1,431

RR  
MLN

Social program expenses for employees

## EDUCATIONAL PROGRAMS

For many years, NOVATEK has been developing a continuing education program set to bring professionals to the Company, which provides opportunities to gifted students from the regions where we operate.

"Gifted Children" program implemented at School No. 8 in Novokuybyshevsk, school No. 2 in Tarko-Sale, school No. 81 in Tyumen and in 2018, school No. 2 in Salekhard joined the program.

Two **Grants programs** for schoolchildren and teachers from the Purovsky District: in 2018, the Company awarded 39 grants to students and 4 teachers received grants under this program.

In 2018, a new boarding school for 800 children was built in Gyda village on the Gydan Peninsula, in one of the most remote settlements of the Yamal-Nenets Autonomous Region.



In October 2018, 77 employees participated in the **4th Professional Skills Contest** among field workers of the NOVATEK Group.



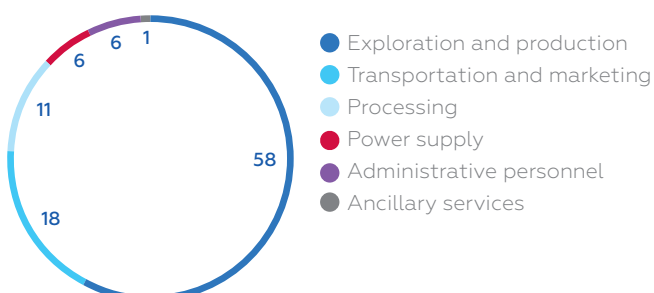
### The Innovator Corporate Idea

Management System focuses on improving business operations, reduction of production costs and implementation of new work methods. In 2017 and 2018, **more than 500 ideas** were submitted, of which 40 were approved for implementation and 24 ideas were implemented. They generated an economic effect of RR 104.7 bln.

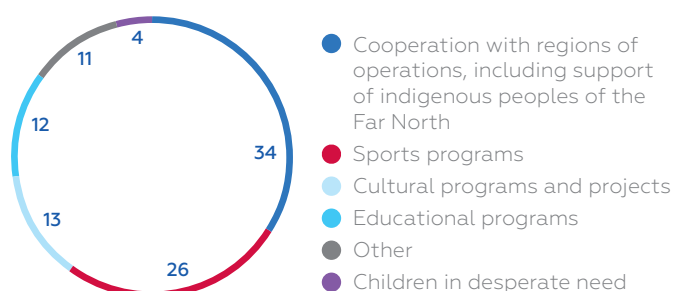


In 2018, NOVATEK and its subsidiaries invested **RR 2,047 million** in projects and activities related to the support of indigenous peoples, charitable contributions, cultural and educational programs.

NOVATEK's personnel structure as of 31.12.18, %



Projects and activities related to the support of indigenous peoples, charitable contributions, cultural and educational programs, %





# Corporate Governance

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 Board of Directors Membership



**MR. ALEXANDER  
E. NATALENKO**

Born in 1946  
Chairman of the Board  
of Directors  
Member of the Strategy  
Committee



**MR. ANDREI  
I. AKIMOV**

Born in 1953  
Member of the Strategy  
Committee



**MR. MICHAEL  
BORRELL**

Born in 1962  
Member of the Strategy  
Committee

## Independent Board Members



**DR. BURCKHARD  
BERGMANN**

Born in 1943  
Independent Director  
Chairman of the Strategy  
Committee  
Member of the Audit Committee  
Member of the Remuneration and  
Nomination Committee



**MR. ROBERT  
CASTAIGNE**

Born in 1946  
Independent Director  
Chairman 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. LEONID  
V. MIKHELSON**

Born in 1955  
Chairman of the Management  
Board



**MR. GENNADY  
N. TIMCHENKO**

Born in 1952  
Member of the Strategy  
Committee



**MR. ARNAUD  
LE FOLL**

(from 18.01.2019)  
Born in 1978  
Member of the Strategy  
Committee

# Review of Operating Results

## Licenses

NOVATEK's core fields and license areas are located in the Yamal-Nenets Autonomous Region. In 2018, we expanded the Company's operational footprint and obtained new licenses in Russia's Krasnoyarsk Territory, the Gydan Peninsula in close proximity to existing license areas of the Company as well as offshore licenses located in Montenegro and Lebanon.

The Yamal-Nenets Autonomous Region (YNAO) is one of the world's largest natural gas producing regions and accounts for approximately 80% of Russian natural gas production and 15% 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 31 December 2018, NOVATEK subsidiaries and joint ventures held 56 licenses for subsoil use. NOVATEK also entered into agreements on exploration and production of hydrocarbons on four offshore blocks in Montenegro and on two offshore blocks in Lebanon.

The duration of licenses for the Company's core fields exceeds 15 years. In particular, the license for the South-Tambeyskoye field is valid until 2045, for the Utrenneye field – until 2120, for the East-Tarkosalinskoye field – until 2043, for the Yurkharovskoye field – until 2034, and for the Samburgskiy license area of Arcticgas – until 2034.

In the reporting year, NOVATEK significantly expanded its portfolio of licenses.

In February 2018, NOVATEK won the ALROSA public auction, obtaining the subsoil licenses for the Beregovoy and Ust-Yamsoveyskiy license area. As of 31 December 2018, the two license areas had a total of 1,217 mmboe of Russian hydrocarbon reserves or 871 mmboe of PRMS reserves.

Our subsidiary NOVATEK-Yurkharovneftegas won the auctions for hydrocarbon exploration and production licenses for the Payutskiy and South-Leskinskiy license areas. The licenses were issued for a term of 27 years. The Payutskiy and South-Leskinskiy areas are located within the Krasnoyarsk Territory in the vicinity of NOVATEK assets, namely the West-Solpatinskiy, North-Tanamskiy, Nyavuyakhskiy and Tanamskiy areas in the Gydan Peninsula.

The Company's subsidiaries obtained five geological study licenses in 2018, which include prospecting and field appraisal, in particular, for the geological study of the Palkurtoiskiy and Central-Nadoyakhskiy areas and flanks of fields being explored, including the Gydanskiy 1, Lader-toyskiy 1, and Dorogovskiy 1.

The new acquisitions are estimated to hold a total resource potential of 19,872 mmboe.

The Company already holds a vast resource base in the Gydan Peninsula, including the Utrenneye, Geofizicheskoye, and Gydanskoye fields and a set of prospective license areas. With new licenses, NOVATEK is accumulating its vast hydrocarbon resource base in the peninsula and, accordingly is in a position to consider significant long-term projects to increase its hydrocarbon production output.

NOVATEK strives to strictly observe 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).

DeGolyer and MacNaughton, an independent petroleum engineers firm, estimates the Company's reserves on an annual basis under both the SEC and PRMS reserves reporting standards.

As of 31 December 2018, NOVATEK's SEC proved reserves, including the Company's proportionate share in joint ventures, aggregated 15,789 million barrels of oil equivalent (mmboe), including 2,177 bcm of natural gas and 181 mmt of liquid hydrocarbons. The Company's proved reserves grew by 4%, and the reserve replacement ratio stood at 222%. At year-end 2018, the Company's reserve to production ratio (or R/P ratio) was 29 years.

As of 31 December 2018, the Company's total PRMS proved and probable reserves, including the Company's proportionate share in joint ventures, aggregated 29,619 mmboe, including 4,021 bcm of natural gas and 387 mmt of liquid hydrocarbons, with a total R/P ratio of 54 years.

The Company's reserves trend in 2018 was positively impacted by successful exploration at the Utrenneye, Urengoykoye (Samburgskiy license area) and Yaredeyskoye fields, production drilling at the South-Tambeyskoye, North-Russkoye and Yaro-Yakhinskoye fields, as well as the acquisition of new assets (Beregovoye field and Ust-Yamsoveyskiy license area). Excluding the effect of obtaining new licenses, the organic reserve replacement rate was 121% due to successful exploration and field development.

The high quality of the reserve base enables NOVATEK to maintain its position as one of the lowest cost producers in the global oil and gas industry. Our average 2018 and five-year (2014-2018) proved reserve replacement costs amounted to RR 87 (USD 1.4) per boe and RR 83 (USD 1.5) per boe, respectively.

## 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 its 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, from the collection and interpretation of seismic data to the creation of dynamic field models for the placement of exploration and production

SEC proved reserves as of 31 December 2018 (based on the Company's equity ownership interest in joint ventures) and duration of licenses

Field / license area	Ownership	Duration of license	Natural gas reserves, bcm	Liquids reserves, mmt
<b>Total reserves</b>	<b>—</b>	<b>—</b>	<b>2,177</b>	<b>181</b>
South-Tambeyskoye	50.1% (59.97% of reserves)	2045	424	14
Utrenneye	100%	2120	417	15
Yurkharovskoye	100%	2034	192	7
Urengoykoye (Arcticgas)	50%	2034	183	45
Verkhnetiuteyskoye + West-Seyakhinskoye	100%	2044	157	2
Geofizicheskoye	100%	2034	129	0.4
East-Tarkosalinskoye	100%	2043	93	22
Yaro-Yakhinskoye	50%	2034	72	13
North-Urengoykoye	50%	2038	64	5
North-Russkoe	100%	2031	60	3
Urengoykoye (Ust-Yamsoveyskiy LA)	100%	2024	52	5
Beregovoy	100%	2070	43	3
Kharbeykoye	100%	2036	42	6



Table continued

Field / license area	Ownership	Duration of license	Natural gas reserves, bcm	Liquids reserves, mmt
Gydanskiy	100%	2044	39	-
North-Chaselskoye	50% lifetime of the field		27	1
Olimpiyskiy	100%	2059	26	2
West-Yaroyakhinskiy	100%	2025	24	3
Samburgskoye	50%	2034	22	2
East-Tazovskoye	100%	2033	18	3
Termokarstovoye	51%	2097	16	4
Khancheykoye	100%	2044	15	1
Yarudeyskoye	51% (100% of reserves)	2029	14	21
Others	-	-	48	4

wells. We employ modern geological and hydrodynamic modeling as well as new well drilling and completion techniques to maximize the ultimate recovery of hydrocarbons in a cost effective and environmentally prudent manner.

In 2018, NOVATEK continued exploration on the Yamal and Gydan peninsulas to expand the resource base of LNG projects.

With a prospecting well drilled in the shallow waters of the Ob Bay we discovered the North-Obskoye field. This discovery represented the world's largest standalone gas condensate field find in 2018\*. Aggregate reserves of natural gas and condensate approved by the State Reserves Commission according to the Russian reserves classification amounted to 322 bcm and 16 mmt, respectively.

With the testing of a prospecting well at the Utrenneye field, we discovered two new gas condensate deposits and confirmed the commercial productivity of the field's Middle Jurassic layers. Total natural gas reserves in the newly discovered deposits within the Utrenniy license area held by Arctic LNG 2 amounted to 405 bcm of natural gas and 40 mmt of gas condensate. Taking into account these new deposits, the field's total reserves amount to around 2 trillion cubic meters of natural gas and 105 mmt of liquids. The reserves were approved by the State Reserves Commission. By adding new deposits we improve the field's resource potential and open up additional prospects in the execution of Arctic LNG 2.

An exploration well drilled to the Jurassic layers at the South-Tambeyskoye field showed a significant flow with

430 mcm/day of gas and 81 tons/day (743 barrels/day) of stable condensate. The estimated reserves based on the Jurassic layers will be submitted to the State Reserves Commission for a formal expert review in 2019.

A prospecting well in the Nyakhartinskiy license area tested a commercial flow with 160 mcm/day of gas and 109 tons/day (938 barrels/day) of gas condensate. This field is geographically next to the well-developed infrastructure of the Yurkharovskoye field and is an important discovery for NOVATEK to maintain its production levels within the UGSS. The reserves will be submitted for expert review by the State Reserves Commission in 2019.

We have commenced an active exploration program at the Gydanskoye field. An initial prospecting well discovered significant oil and gas potential in the Achimov deposits.

In 2018, we continued 3D seismic exploration at the Gydanskiy, North-Obskiy, West-Solpatinskiy, Verkhne-teuteyskiy, and West-Seyakhinskiy license areas located on the Yamal and Gydan peninsulas.

In order to maintain pipeline gas production levels and unstable gas condensate volumes sent to the Purovsky Plant, we continued exploration in the fields and license areas within the Nadym-Pur-Taz district located in the YNAO.

At the Yurkharovskoye field, a well was drilled to further explore lower Jurassic deposits, which confirmed the commercial productivity of the Jurassic gas condensate formations. We are preparing to test the well in 2019.

\* Data provided by international energy research firms Wood Mackenzie, Rystad Energy.

## Geological Exploration

	Units	2017	2018	Change
<b>2D seismic</b>	<b>linear km</b>	<b>-</b>	<b>2,926</b>	<b>n/a</b>
Subsidiaries	linear km	-	2,926	n/a
Joint ventures	linear km	-	-	
<b>3D seismic</b>	<b>square km</b>	<b>1,465</b>	<b>4,759</b>	<b>225%</b>
Subsidiaries	square km	1,215	4,412	263%
Joint ventures	square km	250	347	39%
<b>Exploration drilling</b>	<b>'000 m</b>	<b>24.5</b>	<b>36.1</b>	<b>47%</b>
Subsidiaries	'000 m	16.2	24.3	50%
Joint ventures	'000 m	8.3	11.8	42%

In the North-Russkoye, Kharbeyskoye and Dorogovskoye license areas (collectively referred to as the "North-Russkoye cluster"), three prospecting wells were drilled to confirm oil and gas potential and to define commercial productivity, a prerequisite required to prepare the fields for development.

In the Samburgskiy license area, the successful exploratory drilling confirmed productivity of the Achimov layers, where a commercial flow of gas condensate at testing of wells was received. Seismic data and drilling results indicated the prospects for new discoveries in the drilled layers as well as deeper horizons.

The well testing for the Jurassic layers at the Yarudeyskoye field showed a commercial flow with 206 mcm/day of gas and 19 tons/day (162 barrels/day) of gas condensate.

In the reporting year, we shot 2,926 linear km of 2D seismic and 4,759 square km of 3D seismic works, as well as drilled a total of 36,100 meters of prospecting and exploration wells.

The successful exploration works contributed 989 bcm of gas and 61 mmt of liquids to NOVATEK's reserves under the Russian reserves classification, as well as 164 bcm of gas and 34 mmt of liquids to our PRMS reserves.

## Field Development

In 2018, NOVATEK continued development activities at our producing and prospective fields. In the reporting

year, the Company's subsidiaries invested RR 47.6 bln in resource base development.

Production drilling in 2018, including production drilling at our joint ventures, reached 446,000 meters, representing a 70% increase over 2017. Our drilling activities were mainly driven by the development of the Yaro-Yakhinskoye, North-Obsskoye, East-Tarkosalinskoye, North-Uren-goyskoye, East-Tazovskoye and Samburgskoye fields.

A total of 67 production wells, including 40 natural gas and gas condensate and 27 oil wells, were completed and commissioned during the year.

### NEW FACILITIES COMMISSIONED AT PRODUCING FIELDS

In 2018, at the North-Russkoye field, we continued the construction of gas and condensate pipeline links with diameters of 820 mm and 273 mm, and started the construction of the pipeline crossing under the Taz river. Construction activities were ongoing on the gas treatment facility, booster compressor station, auxiliary buildings and living camp.

On the crude oil part of the Yaro-Yakhinskoye field, an oil treatment facility with a capacity of 1.4 mmtpa with a oil delivery point, an external crude oil pipeline 57 km long, well pads and oil and gas gathering systems were built and commissioned into operation.

Ten new well pads have been put into operation at the Yarudeyskoye field. Construction has been completed and a 40-km road from the Nadym-Salekhard Federal road to the Yarudeyskoye field has been put into operation.

## Hydrocarbon production (including share in production by joint ventures)

	Units	2017	2018	Change
<b>Total</b>	<b>mmboe</b>	<b>513.3</b>	<b>549.1</b>	<b>7.0%</b>
Gas	mmcm	63,399	68,806	8.5%
	mmboe	414.6	450.0	
Liquid hydrocarbons	mt	11,774	11,800	0.2%
	mmboe	98.7	99.1	

## Hydrocarbon production (including share in production by joint ventures)

	Gas, mmcm		Change	Liquids, mt		Change
	2017	2018		2017	2018	
<b>Total</b>	<b>63,399</b>	<b>68,806</b>	<b>8.5%</b>	<b>11,774</b>	<b>11,800</b>	<b>0.2%</b>
NOVATEK-Yurkharovneftegas' fields (100%)	30,540	27,745	(9.2%)	1,489	1,264	(15.1%)
NOVATEK-Tarkosaleneftegas' fields (100%)	11,082	10,069	(9.1%)	1,665	1,661	(0.2%)
Arcticgas' fields (50%, before 21.03.2018 - 53.3%)	13,964	13,698	(1.9%)	4,190	3,999	(4.6%)
South-Tambeyskoye (59.97%)	776	8,213	n/a	25	542	n/a
North-Urengoykoye (50%)	4,291	3,789	(11.7%)	379	310	(18.2%)
Termokarstovoye (51%)	1,255	1,246	(0.7%)	421	403	(4.3%)
Yarudeyskoye (100%)	1,362	1,500	10.1%	3,596	3,439	(4.4%)
Others	129	2,546	n/a	9	182	n/a

## Hydrocarbon Production

In 2018, NOVATEK produced commercial hydrocarbons at 18 fields. The Company's production (including attributable share in the production of JV's) amounted to 549.1 mmboe, up 7.0% compared with 2017. The production increase was due to LNG production growth at the Yamal LNG, as well as the acquisition of new production fields at the end of 2017 and in the first quarter of 2018 (Beregovoy, West-Yaroyakhinskiy and Syskonsynynskiy license areas). The production volumes at mature fields of our subsidiaries and joint ventures decreased mainly due to natural declines in the reservoir pressure at the current gas-producing horizons.

Total natural gas production including the Company's share in production of joint ventures aggregated 68.81 bcm, representing approximately 82.0% 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 77.6%. Production of natural gas increased by 8.5% as compared to 2017 volumes.

Production of liquid hydrocarbons including the Company's share in production of joint ventures totaled 11,800 thousand tons, of which 59.3% was gas condensate and the remaining 40.7% consisted of crude oil. Production of liquid hydrocarbons increased by 0.2% as compared to 2017, with gas condensate production amounting to 7,001 thousand tons and crude oil production coming to 4,799 thousand tons.

In 2018, we continued to achieve some of the lowest lifting costs in the industry. The Company's lifting costs were RR 38.5 (USD 0.61) per boe in 2018.

## LNG Projects

### YAMAL LNG PROJECT

Yamal LNG is an integrated project for the extraction, liquefaction and sale of natural gas. OAO Yamal LNG is the operator and the owner of all the assets. As of the end of 2018, the shareholder structure of Yamal LNG was



Yamal LNG project. Loading of LNG tanker

as follows: NOVATEK – 50.1%, TOTAL – 20%, CNPC – 20%, and the Silk Road Fund – 9.9%.

Yamal LNG was constructed and commissioned ahead of schedule and on budget, an unprecedented accomplishment in the global oil and gas industry. The commissioning of the second and third LNG trains were executed ahead of the initial schedule by 6 months and by more than a year, respectively. The first liquefaction train started production in 4Q 2017, whereas LNG trains 2 and 3 became operational in July and November 2018, respectively, and the Yamal LNG project reached its full operational capacity as early as December 2018.

The aggregate design capacity of the three LNG trains amounted to 16.5 mmtpa of LNG, or 5.5 mmtpa per train. We plan to construct a fourth LNG train with the design capacity of 0.9 mmtpa, utilizing the Arctic Cascade liquefaction technology patented by NOVATEK.

In 2018, Yamal LNG shipped 113 LNG cargos (8.4 mmt) and 30 cargos of stable gas condensate (717 mt).

The South-Tambeyskoye field located in the North-East of the Yamal Peninsula is the resource base of the Project. The field is being developed with horizontal wells with total drilled lengths up to 5,000 meters and horizontal sections of up to 1,500 meters.

The license for exploration and production of hydrocarbons at the South-Tambeyskoye field held by Yamal LNG is valid until 2045.

As of 31 December 2018, the field's SEC proved reserves amounted to 707 bcm of natural gas and 24 mmt of liquid hydrocarbons. In terms of proved reserves, the South-Tambeyskoye field is the largest field in NOVATEK's portfolio. In 2018, the production drilling results increased the proved reserves at the field by 38 bcm of natural gas and 4 mmt of liquid hydrocarbons under the SEC reserves methodology, including production. According to the PRMS standards, the proved and probable reserves of the South-Tambeyskoye field as of the end of 2018 amounted to 1,002 bcm of natural gas and 37 mmt of liquid hydrocarbons.

The field's production capacity exceeds 27 bcm of natural gas and 1 mmt of stable gas condensate per annum.

A new fleet of LNG tankers designated as Arc7 ice class LNG carriers were specifically designed for the Yamal LNG project capable of navigating the Northern Sea Route (NSR) without icebreaker support all year round (westbound) and throughout the summer-autumn navigation period (eastbound). As of the end of 2018, eight of the fifteen Arc7 ice-class carriers were in operation.

# 113

LNG CARGOS

and 30 cargos of stable gas condensate were shipped from Yamal LNG in 2018

In November 2018, we started ship-to-ship LNG transshipment operations in the vicinity of the port of Honningsvåg in northern Norway in order to optimize transportation costs, shorten the travel distance for the Arc7 ice-class carriers and ensure timely loading and offtake of LNG production. The LNG is transshipped from the Arc7 ice class carriers to conventional LNG carriers delivering the cargos to the customers.

Yamal LNG inaugurated the 2018 summer navigation period along the NSR by delivering the first LNG cargos destined to China. These voyages represented the first shipment of Russian LNG along the NSR without icebreaker support. Moreover, they marked the start of regular LNG shipments via the NSR, which were only made possible by the unique ice-breaking characteristics of Arc7 carriers. The inaugural voyage from the port of Sabetta through the NSR to the destination port was completed in 19 days as compared to 35 days for the conventional route via the Suez Canal.

## ARCTIC LNG 2 PROJECT

Arctic LNG 2 is the second LNG project of NOVATEK. The project includes the construction of three LNG trains, with a design capacity of 6.6 mmtpa of LNG each, or a total of 19.8 mmtpa, and at least 1.6 mmtpa of stable gas condensate. The project employs an innovative construction concept using gravity-based structures (GBS). OOO Arctic LNG 2 is the operator and owner of all the assets.

The Utrenneye field is the resource base for Arctic LNG 2. The field is located on the Gydan Peninsula in YNAO approximately 70 km across the Ob Bay from Yamal LNG. In 2018, the boundaries of the license area were expanded, and gas condensate deposits of the field's southern flank were included in the area. The license term was extended until 2120.

In 2018, the Utrenneye field exploration drilling discovered two new deposits and confirmed the commercial productivity of the Middle Jurassic layers. The discovered deposits hold total reserves of 405 bcm of natural gas and 40 mmt of gas condensate under the Russian reserves classification. As of 31 December 2018, the Utrenneye field's reserves under the Russian reserves classification totaled 1,978 bcm of natural gas and 105 mmt of liquids. OOO Arctic LNG 2 holds the LNG export license.

# 19.8

MMTPA

Total design capacity of three LNG trains of Arctic LNG 2

In 2018, we completed the front end engineering design (FEED) and started site preparation, construction of early phase power supply facilities, production wells drilling and berth construction.

The GBS design concept as well as extensive localization of equipment and materials manufacturing in Russia will considerably decrease the capital cost per ton of LNG produced, ensuring the project's low cost structure and increasing its competitive advantages.

NOVATEK will build the LNG Construction Center in Belokamenka near Murmansk to provide fabrication of the GBS, assembly and installation of topside modules. The LNG Construction Center will comprise two dry docks to build GBS and facilities to manufacture topside modules. This new facility will establish a state-of-the-art LNG platform in Russia, create new jobs in engineering and production, and also contribute to regional economic development as well as manufacturing and equipment orders throughout Russia.

In December 2018, Arctic LNG 2 signed an agreement on the design and construction of three GBS platforms, with the Russian company SAREN, a joint venture of Renaissance Heavy Industries Russia (RHI Russia B.V.) and SAIPEM S.p.A of Italy.

In December, a contract was also signed with Nuovo Pignone (Italy) for the supply of gas turbine compressors and gas turbine power generators for three liquefaction trains.

In May 2018, NOVATEK and TOTAL agreed in principle on the entry into the Arctic LNG 2 providing for a purchase by TOTAL of a 10% participating interest in the project. The deal was closed in March 2019.

## CRYOGAS-VYSOTSK PROJECT

One of our LNG strategic initiatives is to develop small-to medium-scale LNG projects. This approach allows us to build effective marketing channels to sell our products on different markets. We see vast prospects in using LNG as marine fuel and motor fuel to substitute for diesel and fuel oil, that will contribute to decreasing emissions and improving the environment.



# 1,978

BCM

**of natural gas and 105 mmt of liquids -  
the Utrenneye field's reserves under the Russian  
reserves classification as of 31 December 2018**

In July 2017, NOVATEK acquired a 51% participation interest in the Cryogas-Vysotsk project including construction of an LNG production facility and a transshipment terminal.

Cryogas-Vysotsk, located in the port of Vysotsk, the Leningrad Region, is our first medium-scale LNG project with an initial design capacity of 660 mtpa. As of year-end 2018, most of the plant construction works were completed and equipment commissioning was in progress.

The project infrastructure includes two LNG trains with a capacity of 330 mtpa each, a 42-mcm LNG storage tank and an offloading terminal designed to handle LNG carriers with a capacity of up to 30 mcm.

In 2018, NOVATEK and Fluxys established a joint venture to design, build, finance, own and operate a medium-scale LNG transshipment terminal with a capacity of about 300 mtpa in the port of Rostock, Germany. The transshipment terminal will receive LNG carriers from the Cryogas-Vysotsk liquefaction facility and further LNG deliveries to the consumer market will be made via trucks. It will also have an option of bunkering and loading of bunkering vessels.

## 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 main part of 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 vertically integrated 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 processes unstable gas condensate into stable gas condensate and natural gas liquids (NGL).

# 660

MTPA

**Initial design capacity of Cryogas-Vysotsk,  
our first medium-scale LNG project**

In the reporting period, the Purovsky Plant processed 11,018 mt of de-ethanized gas condensate, representing a 3.7% decrease compared to 2017. The processing capacity of the Purovsky Plant is in line with the total production capacity of NOVATEK and its joint ventures' fields. The 2018 output mix included 8,501 mt of stable gas condensate, 2,452 mt of NGL and LPG and 15.0 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 the remaining volume of stable gas condensate sold directly from the plant to the domestic market.

All of the NGL volumes (feedstock for LPG production) produced at the plant are delivered by pipeline to SIBUR's Tobolsk Petrochemical Complex for further processing.

### UST-LUGA COMPLEX

The Gas Condensate Fractionation and Transshipment Complex (the "Ust-Luga Complex") 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. After launching in 2013, the complex also allowed us to improve logistics and reduce transportation costs due to a more favorable geographical location of Ust-Luga compared to the port of Vitino, through which we had previously exported our stable gas condensate.

In the reporting year, the Ust-Luga Complex processed 6,949 mt of stable gas condensate into 6,807 mt of end products, including 4,244 mt of light and heavy naphtha, 1,087 mt of jet fuel and 1,476 mt of ship fuel component (fuel oil) and gasoil. The Ust-Luga Complex will commence constructing a hydrocracker unit in 2019 that will eventually reduce the fuel oil and gasoil component

into higher grade petroleum products. We expect this new upgrading unit will be commissioned in 2020.

High value-added petroleum products produced at the Ust-Luga Complex have a significant positive impact on the profitability of our liquid hydrocarbons 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.

## Natural Gas Sales

NOVATEK sells natural gas within the Russian Federation as well as exports natural gas in the form of LNG. The Company started exporting LNG in December 2017 when the first train at the Yamal LNG project started production. In addition, on the European market we sell regasified liquefied natural gas arising during the transshipment of LNG (boil-off gas), as well as during the regasification of purchased LNG at our own regasification stations in Poland.

In 2018, natural gas sales volumes, including volumes of LNG sold, aggregated 72.13 bcm, representing an increase of 11% as compared with 2017. Revenues from natural gas sales amounted to RR 375.2 billion, representing a 51.5% increase compared to 2017. The revenue

increase was mainly driven by the start of LNG deliveries from the Yamal LNG project and an increase in sales prices and volumes in the Russian domestic market.

### SALES IN THE RUSSIAN FEDERATION

In 2018, the total volume of natural gas sales in the Russian Federation amounted to 66.07 bcm, increasing by 1.8% compared to the previous year.

NOVATEK plays an important role in ensuring supplies of natural gas to the domestic market. During 2018, the Company supplied natural gas to 40 regions of the Russian Federation. Our end customers and traders were located primarily in the following regions: the Chelyabinsk Region, the Khanty-Mansiysk Autonomous Region, Moscow and Moscow region, YNAO, Lipetsk, Tyumen, Vologda, Stavropol, Nizhny Novgorod, Smolensk, Tula and Kostroma regions and Perm Territory. The above regions accounted for more than 92% of our total gas sales in the Russian Federation.

In order to manage seasonal gas demand, NOVATEK has entered into an agreement with Gazprom for underground storage services. 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 2018, our inventories of natural gas, including LNG, amounted to approximately 2.2 bcm.

#### Processing volumes and output of the Purovsky Plant, mt

	2017	2018	Change
<b>Processing of de-ethanized condensate</b>	<b>11,445</b>	<b>11,017</b>	<b>(3.7%)</b>
<b>Output</b>			
Stable gas condensate	8,853	8,501	(4.0%)
NGL and LPG	2,493	2,452	(1.6%)
Regenerated methanol	16.5	15.0	(9.1%)

#### Processing volumes and output of the Ust-Luga Complex, mt

	2017	2018	Change
<b>Stable gas condensate processing</b>	<b>6,961</b>	<b>6,949</b>	<b>(0.2%)</b>
<b>Output</b>			
Heavy naphtha	2,261	2,247	(0.6%)
Light naphtha	1,962	1,997	1.8%
Jet fuel	1,072	1,087	1.4%
Ship fuel component (fuel oil)	967	843	(12.8%)
Gasoil	564	633	12.2%

NOVATEK, through its subsidiary NOVATEK-AZK, is implementing a pilot project for the sale of LNG as a motor fuel.

Together with industrial and commercial enterprises of the Chelyabinsk region, we have converted a number of pilot automotive vehicles (haul trucks and highway trucks) to the dual-fuel mode (LNG + diesel). In 2018, the preliminary testing results of these vehicle types were positive. Together with Chelyabinsk transport companies, we started trial operation of buses using LNG as a motor fuel. Two mobile refueling units were launched to refuel haul trucks, highway trucks and public transport in the Chelyabinsk region.

## SALES ON INTERNATIONAL MARKETS

The successful start of LNG sales on international markets confirms NOVATEK's transformation into a global gas company. Yamal LNG is currently the largest LNG project in Russia with an aggregate share of about five percent of the global LNG market.

In 2018, we sold 6.06 bcm of LNG (4.0 mmt) or 57 cargos. In 2017, LNG sales amounted to 0.1 bcm due to the start of LNG shipments from the Yamal LNG project on 8 December 2017.

One of our core commercial marketing priorities is to expand our supply geography and grow our presence in the key consuming markets. In the reporting year, we shipped LNG cargos to Europe, the Asia-Pacific region and Latin America, thus demonstrating the commercial viability of delivering cost-competitive LNG around the globe.

In June 2018, Yamal LNG shipped the first cargo of LNG under a long-term offtake agreement with Gas Natural Fenosa, a Spanish company. This represented the first Russian gas delivered under a long-term contract to Spain, where Russian pipeline gas is not supplied.

In July, we shipped our first cargos to China via the NSR in just 19 days (one way) compared to 35 days

of delivery via the traditional eastern route via the Suez Canal. NOVATEK began using the NSR in 2010, by successfully supplying large-capacity tankers with liquid hydrocarbons to the Asia-Pacific region. The Company has now become a pioneer in supplying Russian LNG along this important navigational route. This first LNG shipment opened a new era in the supply of Russian LNG to the growing energy consuming markets of the Asia-Pacific region. The NSR ensures shorter transportation time and lower costs, playing a key role in developing our hydrocarbon fields on the Yamal and Gydan peninsulas.

## Liquid Hydrocarbons Sales

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

In 2018, the liquids sales volume reached 15,822 mt, or 0.7% less than in 2017. In 2018, export sales decreased by 0.3% as compared to 2017 and amounted to 8,997 mt.

In 2018, our liquids sales revenues increased to RR 450.6 billion, or by 35.6% as compared to 2017, mainly driven by higher global benchmark prices.

High-value added petroleum products from the Ust-Luga Complex accounted for a 42% share of our overall liquids sales volumes. We sold a total of 6,683 mt of stable gas condensate products, including 4,185 mt of naphtha, 1,082 mt of jet fuel and 1,416 mt of fuel oil and gasoil. The majority of petroleum products (98%) were exported. Export volumes were distributed as follows: Europe – 55.1%, Asia-Pacific – 32.2%, North America – 10.4% and the Middle East – 2.3%. Most of our heavy naphtha was exported to Asia-Pacific, light naphtha – to Northwest Europe and North America, jet fuel, gasoil and fuel oil – to Northwest Europe.

### Natural gas sales, mmcm

	2017	2018	Change
<b>Total gas sales</b>	<b>65,004</b>	<b>72,134</b>	<b>11.0%</b>
International sales	106	6,061	n/a
Sales within the Russian Federation, including:	64,898	66,073	1.8%
• End customers	61,560	61,901	0.6%
• Traders	3,338	4,172	25.0%
Share of end customers in domestic gas sales	94.9%	93.7%	(1.2 p.p.)

# 6.1

BCM

of LNG sold in 2018

Export and domestic sales of stable gas condensate continued in 2018. Condensate was sold to international markets, including purchased volumes from Yamal LNG. Total stable gas condensate sales volumes amounted to 1,908 mt, representing a 0.5% decrease compared to 2017.

A portion of light hydrocarbons produced at the Purovsky Plant is processed on tolling terms at SIBUR's Tobolsk Petrochemical Complex into marketable LPG, which is then delivered to NOVATEK's customer base, while the rest of the light hydrocarbons volumes are sold to SIBUR. We sold 1,248 mt of light hydrocarbons in 2018.

Marketable LPG sales volumes totaled 1,428 mt in 2018, representing a 5% increase compared to 2017. LPG export sales volumes amounted to 593 mt or 42% of the total LPG sales volumes. Novatek Polska, our wholly owned

# 375.2

RR  
BLN

Natural gas sales revenues, 51.5% growth as compared with 2017

LPG trading company in Poland, sold all of our LPG export volumes.

In the domestic market, our LPG is sold through large wholesale channels as well as through our retail network and small wholesale stations. In 2018, large wholesale supplies to the domestic market stood at 688 mt, representing 82% of domestic LPG sales. We also sold LPG via our retail network of 68 stations and seven small wholesale stations in the Chelyabinsk, Volgograd, Rostov and Astrakhan regions. The combined sales from our retail and wholesale stations totaled 146 mt.

Sales of crude oil in 2018 totaled 4,542 mt, which is 1.6% lower compared with 2017. We sold 66% of our crude oil volumes in the domestic market, with the remaining volumes exported to international markets.

## Liquid hydrocarbons sales, mt

	2017	2018	Change
<b>Total</b>	<b>15,939</b>	<b>15,822</b>	<b>(0.7%)</b>
Petroleum products (Ust-Luga)	6,743	6,683	(0.9%)
Crude oil	4,616	4,542	(1.6%)
Stable gas condensate	1,918	1,908	(0.5%)
Light hydrocarbons	1,288	1,248	(3.1%)
LPG	1,360	1,428	5.0%
Other	14	13	(7.1%)



# 450.6<sup>RR BLN</sup> 15.8<sup>MMT</sup>

Liquids sales revenues,  
35.6% growth as compared with 2017

Liquids sales volume



Yamal LNG



# 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 2018, the Company's overall expenses on environmental protection and sustainable nature management amounted to RR 2.4 bln.

We would like to highlight the most significant actions in environmental protection and sustainable management in 2018.

The Company built a sewage and water-methanol mixture thermal disinfection unit at the Purovsky Condensate Processing Plant. In terms of pollutants content in effluents, this unit uses state-of-the-art technologies and meets the stringent Russian requirements for air protection.

The Yamal LNG plant completed and commissioned the treatment facilities for stormwater and residential sewage. The wastewater is treated to meet regulatory statutory norms and then once treated is discharged into the Ob Bay basin. The treatment process employs mechanical, biological, physical and chemical methods. Treated wastewater is disinfected with ultraviolet irradiation. Chemically and oil contaminated industrial effluents are treated in the treatment plant that brings it in line with quality standards thus enabling injecting them into absorbing formations. Before being injected, the wastewater undergoes separation, two-stage flotation and post-treatment in a pressure sand filter.

NOVATEK is an active contributor to the national objective of converting vehicles to using natural gas as fuel. The Company is developing the market segment for natural gas as a motor fuel by expanding the network of its natural gas retail stations in various Russian

regions. We launched a new business area, namely the construction of LNG retail stations and the subsequent use of LNG as an environmentally friendly motor fuel. Converting a vehicle to LNG enables the reduction of soot and carbon monoxide emissions by more than three times compared to conventional fuels (gasoline and diesel).

We drilled our first offshore prospecting well in shallow waters strictly adhering to the stringent environmental standards for activities within the Russian Federation inland seas. We developed an Accidental Spill Response Plan and an environmental monitoring program for the North-Obskiy license area. Regular water monitoring in the Ob Bay of the Kara Sea demonstrated that its hydrochemical and organoleptic properties are in line with the statutory standards. Environmental safety was ensured by multi-purpose emergency response and rescue vessels. Drill cuttings were transported to the port of Sabetta to be further disposed of in an eco-friendly manner.

In Yamal LNG, we carried out a study of marine mammals' migration routes and an assessment of LNG shipping impact on their population in the northern part of the Ob Bay and in the southern part of the Kara Sea, including aerial monitoring of their headcount and analysis of seal distribution on ice in the northern part of the Ob Bay (estimated headcount ranges between 3,639 and 5,433 individuals). Baseline data were collected prior to the start of active ice navigation in order to assess and supervise its impact on ringed seals during the ice period, and to develop mitigation measures. One of the tasks that the crews of chartered vessels sailing through the Ob Bay and the Kara Sea should address is to monitor encounters with marine mammals, record the coordinates and distances as well as the numbers and species of animals encountered. In case of dangerous proximity, a vessel must take measures to avoid troubling animals (slow down or divert).



Photography of a participant of photo contest "See and Preserve!"

#### Key Environmental Indicators of NOVATEK (including joint ventures)

	Unit	2017	2018	Change
Water consumption	mcm	2,779	2,993	7.7%*
Atmospheric emissions	mt	108.9	84.3	(22.6%)

One of the Company's 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 in 2018.

#### Energy Resource Consumption by NOVATEK in 2018 (including joint ventures)

	Units	Volume	RR mln, net of VAT
Natural gas	mmcm	2,185	2,667.0
Electricity	MWh	1,907,769	8,106.0
Heating energy	Gcal	899,752	661.5
Crude oil	tons	1,478	11.2
Motor gasoline	tons	1,246	58.9
Diesel fuel	tons	5,499	264.6
Butane	tons	97,786	n/a
Other	tons	1,177	6.6

\* The increase in water consumption is associated with water intake during the operation of a marine self-lifting drilling rig to ensure the cooling of technological equipment.

# 2.4 <sup>RR BLN</sup>

## Expenses on environmental protection and sustainable nature management

To encourage NOVATEK employees and residents of the Purovsky district of the YNAO to preserve the Far North environment and foster environmental awareness, an environment-related photo contest “See and Preserve!” was held. A total of 32 participants from among residents of the Purovsky District, YNAO, and NOVATEK employees submitted 198 works for the contest. A jury consisting of district administration representatives and professional photographers defined the best pictures. In each of the five categories, three winners were announced who received valuable gifts.

In 2018, more than 1,500 employees from the regions where the Company operates took part in “Green Spring 2018”, a Russian national environmental campaign.

Following a re-certification audit by Bureau Veritas Certification Rus, the NOVATEK HSE Management System was confirmed to be in compliance with OHSAS 18001 and a new version of the international standard ISO 14001 Environmental Management System.

The Company’s Arctic Cascade liquefaction technology was recognized by the Vernadsky National Environmental Award in the Innovative Eco-Effective Industrial and Energy Technologies category. This event is an annual competition aiming to discover and promote projects in the area of environmental protection and safety. Arctic Cascade, a prospective natural gas liquefaction technology developed and patented by NOVATEK, ensures enhanced performance with lower power consumption and reduced equipment costs. The technology is designed to use equipment from Russian manufacturers.

Environmental monitoring was performed throughout the reporting year at all of the Company’s license areas and production facilities. During the monitoring process the condition of the environmental components is studied, soil, ground, snow cover, water and bed 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 environmental components in the Company’s production facility locations is evaluated as stable.

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. 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, and other disclosure means.

## Industrial Safety and Occupational Health

NOVATEK is fully committed to putting the life and health of its employees above operational results, and is aware of its responsibility for ensuring accident-free operations and safe labor conditions for its employees, as well as protecting the health of the population in the areas in which it operates.

NOVATEK has in place an occupational health and safety management system which is part of a wider management system and ensures risk management based on the key principle of prioritizing prevention over incident containment and response.

The Company is engaged in exploration, production, processing and sales of natural gas and liquid hydrocarbons, which implies setting up complex technological processes for operating fire and explosion hazardous facilities. Operation of fire and explosion hazardous facilities requires that work and services at hazardous production facilities be performed in strict compliance with industrial safety laws.

To prevent accidents and incidents, and ensure accident containment and response at Class 1 and 2 hazardous production facilities, a unified industrial safety management system and industrial safety declaration were developed providing estimates and specifying activities for:

- identification, assessment and forecasting of accident risks;

# 23%

## Reduction of atmospheric emissions

- planning and implementation of accident risk mitigation measures;
- coordination of activities to prevent accidents and incidents;
- industrial control procedure; and
- employees' participation in the development and implementation of accident risk mitigation measures.

To compensate for the damage inflicted to third parties and the environment as a result of an accident at a hazardous industrial facility, all hazardous industrial facilities are insured in accordance with Federal Law No. 225-FZ On Mandatory Insurance of Civil Liability of Owners of Hazardous Facilities for Damages Inflicted by Emergencies at Hazardous Facilities.

Executives and specialists of subsidiaries and joint ventures supervised by Rostekhnadzor have been qualified for compliance with industrial security and safety rules in territorial bodies of Rostekhnadzor. From among these employees, the Company set up industrial safety assessment commissions to evaluate staff that operate technical devices at hazardous production facilities.

Occupational health training is mandatory for all categories of employees and is offered in all controlled entities. Structural unit leaders, including top managers, take courses in training centers, while specialists are offered in-house training opportunities. For that, training programs were developed, and occupational health knowledge testing commissions were set up. In-house occupational health training and knowledge testing not only enable significant cost optimization but also save man-hours as such training and tests take place on the job.

In 2018, 11,119 employees completed occupational health training and safety certification in line with the approved training plan.

In 2018, 365 industrial safety and occupational safety compliance checks were carried out by commissions of subsidiaries and joint ventures with results documented in industrial control reports. Employees in charge submit monthly reports to their respective health and safety

units specifying remedial actions. All violations are remedied within defined timeframes.

In 2018, NOVATEK ran programs of integrated and targeted audits of controlled entities for compliance with occupational health, industrial, fire and environmental safety requirements by NOVATEK's committee. In the reporting year, the Company conducted integrated audits of four (4) Company entities, and targeted audits of eight (8) entities. Based on their findings, relevant reports were produced, and remedial measures were developed.

At the Company level, data are collected and analyzed regarding remediation of all findings of both scheduled and unscheduled audits carried out by the state supervisory authorities and integrated and targeted audits of the Company's committee.

To prevent accidents and incidents, each year the Company develops and consistently implements technical inspection, certification and test schedules for various types of technical equipment (external and internal inspection, hydrostatic and pneumatic tests, and industrial safety audits). In 2018, the Company performed industrial safety audits of 534 equipment items and extended their safe operating life.

To protect the rights of employees to an occupational health-compliant workplace, special assessments of working conditions were performed to cover all workplaces. When workplaces with harmful working conditions are identified, a range of measures is first implemented to eliminate adverse factors. If these prove impossible to eliminate, the time of exposure to harmful conditions is then restricted while the affected employee is granted all guarantees and compensations for operating in harmful working conditions. In the reporting year, 7,050 workplaces were certified. A special workplace certification process found 5,950 (86.4%) workplaces to have permissible conditions. No workplaces with hazardous working conditions were identified.

The Company also arranged for preliminary health screening and regular medical examinations for timely detection of contraindications and signs of occupational diseases. No occupational diseases were identified for the reporting period.

## Key Health and Safety Indicators of NOVATEK (including joint ventures)

	2017	2018	Change
Accidents at hazardous production facilities	0	0	–
Incidents at hazardous production facilities	2	1	(50%)
Injury frequency rate	1.27	0.79	(38%)

Workers engaged in certain high-hazard operations and exposed to high-hazard production environments (operation and maintenance of hazardous industrial facilities) undergo mandatory mental health evaluation.

The Company actively exercises its right to receive a 20% refund of the mandatory social insurance payment that is duly transferred to the Social Insurance Fund of the Russian Federation to cover occupational accidents and diseases. These funds are mainly used to finance procurement of protective clothing and workplace certifications.

## 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 2018, NOVATEK and its subsidiaries had 13,694 employees, 57.9% of whom work in exploration and production, 11.3% in processing, 17.8% in transportation and marketing, 5.4% in power supply, 6.4% are administrative personnel and 1.2% are engaged in ancillary services. The predominant age of the personnel is between 30 and 50. The average age of the Company's employees is 40 years.

### PERSONNEL TRAINING AND DEVELOPMENT

Amid the rapid development of technologies and management systems, our multilevel training and professional development program enable our employees to contribute to raising the Company's competitiveness. In 2018, the primary activities 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 and practice conferences;

NOVATEK Scientific and Technical Center (NOVATEK STC) has hosted an In-House Training Program since 2016. In 2018, NOVATEK STC experts developed and delivered training courses on the following subjects: "Lithofacies Analyses. Depositional Environment. Theory and Practice"; "Dynamic Simulation of Multiphase Streams in Pipelines and Wells using OLGA Software: Principal Tasks and Examples of their Solution"; "Complexing Logging Methods to Address Geological Tasks. Basics of Log Interpretation and Practical Application (in NOVATEK Group projects)"; "Basics of Geological 3D Modelling"; "Basics of Intra- and Inter-Field Hydrocarbons Transportation Engineering and Operation"; and Application of Petroleum System Studies (Basin Analysis) during Exploration. A total of 34 of the Company's employees received training under this program in 2018.

In 2018, 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 40.5 % of white- and blue-collar workers upgraded their skills. In 2018, the Corporate System for the Evaluation of Technical Competencies tested 274 employees across the Group, including 49 persons who were tested at recruitment and 156 persons – at promotion.

In 2018, 112 young specialists participated in the Steps in Discovering Talents Program. We had our sixth class and 28 specialists graduated from the on-the-job adaptation and professional development program while 30 young specialists guided by 22 mentors completed the first step of the program. In autumn 2018, another 54 young specialists and 48 mentors assigned to them joined the program. Young specialists received the Mentoring Culture training courses together with their mentors. In total, 34 mentors attended the training. In 2018, the number of companies participating in the program increased to ten.



# 13,694

**employees at NOVATEK, its subsidiaries and joint ventures**

In September 2018, Moscow hosted the 13th Interregional Research-to-Practice Conference for the Company's young specialists attended by 93 employees. Based on the results of the competition, all the winners received cash prizes, while fifteen (15) of the first place winners were also awarded a trip to petroleum training centers in Japan.

In October 2018, the 4th Professional Skills Contest among field workers of the NOVATEK Group took place. A total of 77 participants from 9 entities took part in the event. The Contest was hosted by NOVATEK-Purovsky Plant and included two stages, a theoretical and a practical part with results of both defining the winners.

In 2017, the Innovator Corporate Idea Management System, an automated framework to collect and process employees' proposals on improving and developing business including labor-saving proposals, was launched in NOVATEK and its 14 subsidiaries. More than 230 ideas on improving business operations, reduction of production costs and implementation of new work methods were submitted by the employees in 2018. More than 500 ideas have been submitted over the two years, of which 40 were approved for implementation and 24 ideas were implemented. They generated an economic effect of RUB 104.7 bln.

## **SOCIAL PROGRAMS**

The focus in employee relations is on implementing social programs. 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**

The program includes full outpatient care, dental care, and emergency and scheduled hospitalization.

### **Therapeutic resort treatment**

Employees and their families can purchase health resort vouchers at a discount. Under this program, NOVATEK's employees may spend their vacations in 44 health resorts located in Russia's most picturesque settings.

### **Repayable Financial Aid Program**

The special-purpose loans program has two focus areas:

- short-term special-purpose loans intended for employees who experience economic hardship;
- special-purpose interest-free home loans to employees residing in Tarko-Sale, Novy Urengoy, Moscow, Nadym, Sosnovy Bor and Tyumen.

### **Targeted compensation and social support payments**

This program provides targeted free support to the Company's employees in specific life circumstances, including childbirth, the event of natural disasters or fire, compensation for care of a child up to 3 years of age, financial aid for care of disabled children, financial aid for burial, compensation for sports and recreation classes for employees, as well as on the occasion of the jubilee.

### **Pension Program**

Since 2007, NOVATEK has offered its retired employees supplementary benefits in line with the Regulations on Social Benefits for Retired NOVATEK Group Employees. Employees with an employment track record of at least five years with the Company who resign at the full retirement age are entitled to monthly benefit payments from the Company (suspendable in case the retiree gets a job). The benefit amount is subject to the employee's average salary, employment track record and geographical location.

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 2017, 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 and roll competitions with the Company's assistance.

## **Social Policy and Charity**

Social Policy and Charity make up an important part of NOVATEK's activities. In 2018, the Company continued

# 2.0 RR BLN

## Expenses on support of indigenous peoples, charitable contributions, cultural and educational programs

to pay close attention to projects aimed at supporting the culture, preserving and revitalizing national values and spiritual legacy of Russia, promoting and integrating Russian art into the international cultural space, and developing mass and high-performance sports. NOVATEK enters into agreements with regional governments across the Company's geographical footprint and implements programs improve living standards and preserve the distinctive cultural identity of the indigenous peoples of the Far North.

In 2018, NOVATEK and its subsidiaries invested RR 2.0 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 was investing in YNAO and KhMAO, the Leningrad, Murmansk, Chelyabinsk, Tyumen, and Kostroma regions throughout 2018. The Company also financed the construction, repairs and upgrades of social infrastructure facilities, earmarked significant funds for implementing educational, cultural, children and youth programs and projects, and supported low-income families, people with disabilities, the elderly and veterans.

NOVATEK is annually providing assistance to various regions by helping with settlement development, construction and renovation of accommodation, educational facilities and advancing local healthcare.

The Company is directly involved in funding the construction of important social infrastructure facilities across the YNAO.

In September 2018, NOVATEK together with the YNAO Government opened an 800-student boarding school in the village of Gyda in the YNAO. The project was fully funded by NOVATEK.

The new school will become an important educational and cultural centre of the Gydan Peninsula. It is equipped with modern equipment to ensure a proper



The opening of a new residential school in the Gyda: settlement, YNAO

educational process and carry out cultural and sports-related activities. The school facilities include a canteen, a medical facility, workshops, a language laboratory, a reading room, a conference hall, a museum and a projection room, where students can develop their creativity and get involved in the arts.

Construction of a new modern boarding school in one of the most remote settlements of the YNAO is a project aimed at improving the living standards of the Far North indigenous and minority groups. Education is a base for development of young people's vast capacities and human resources in the region in particular and in the country in general. Our contribution to the social and economic development creates better understanding and ensures that the cultural heritage is preserved in the Company's core regions.

### COOPERATION WITH INDIGENOUS PEOPLES OF THE FAR NORTH

During the reporting year, 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. Portacabins were purchased for the needs of the tundra population. NOVATEK financed fuel purchases for air delivery of the nomadic population and food to remote areas. Assistance was provided to people in financial distress. One particular area of support is taking part in organizing and staging ethnic festivals of indigenous peoples as well as provision of funding for environmental programs.

### EDUCATIONAL PROGRAMS

NOVATEK continued to develop 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.



Class-room in a new residential school in the Gyda: settlement, YNAO

Recruitment and career guidance for promising employees start with the “Gifted Children” program implemented at School No. 8 in Novokuybyshevsk, school No. 2 in Tarko-Sale, school No. 81 in Tyumen and in 2018, school No. 2 in Salekhard joined the program. Special classes are formed on a competitive basis from the most talented grade 10 and 11 students with above-average test scores. The Company has 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 eleven (11) are awarded grants from the Company. In 2018, the Company awarded 39 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 2018, four 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-University 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 2018, NOVATEK continued its cooperation with Russia’s leading museums including the State Tretyakov Gallery, the Russian State Museum, and the Moscow Museum of Modern Art, and supported the most important art and music projects.

In 2018, NOVATEK was involved in the implementation of the “Ilya and Emilia Kabakov. Not Everyone Will Be Taken Into the Future” international project. A large-scale retrospective exhibition of Ilya and Emilia Kabakov’s works was publicly available in the Tate Modern museum (United Kingdom, London), the State Hermitage (Russia, Saint Petersburg), and in the State Tretyakov Gallery (Russia, Moscow).

The Company supported exhibitions “Nikolai Kulbin” and “Lazar Khidekel” in the Russian State Museum. In 2018,

# 39 GRANTS

**awarded to schoolchildren under the program aimed at academic and creative development**

the main theme of the exhibitions was avant-garde art. NOVATEK also supported the annual Imperial Gardens of Russia international festival of garden and park art titled "Flower Assembly". In the year of the 315th anniversary of the founding of Saint Petersburg and the 120th anniversary of the opening of the State Russian Museum, the Imperial Gardens of Russia festival was for the first time held in the Summer Garden.

"Russian Museum. Common Stories", a book by Vladimir Gusev, the State Russian Museum director, was published with the support of the Company.

In partnership with NOVATEK, the Moscow Museum of Modern Art (MMOMA) presented the exhibition of the local nonconformist "Vladimir Yankilevsky. Mystery of Being" coinciding with the artist's 80th birthday anniversary. In 2018, NOVATEK continued supporting the MMOMA Education Center. In addition, MMOMA delivered a course of lectures on the history of Russian and foreign fine arts, fashion, design and architecture at the office of NOVATEK to the Company's employees and their families.

The Sixth Moscow International Biennale of Contemporary Art was held with the support of the Company.

NOVATEK is a permanent partner of the international festival-school of contemporary art TERRITORIYA. In 2018, the festival presented Russian and foreign plays and dance programs and organized an educational program.

The Company continued supporting the activities of the Gogol-center.

In 2018, NOVATEK remained a General Partner of the Moscow Soloists Chamber Ensemble under the direction of Yuri Bashmet. The Company acted as General Partner of the first Asian tour of the Russian Youth Symphony

# 10 YEARS

**of the "All Together" volunteer movement**

Orchestra led by Yuri Bashmet. The tour included concerts in Moscow, Vladivostok, Singapore, Shanghai, Beijing and Seoul.

## SPORTS PROJECTS

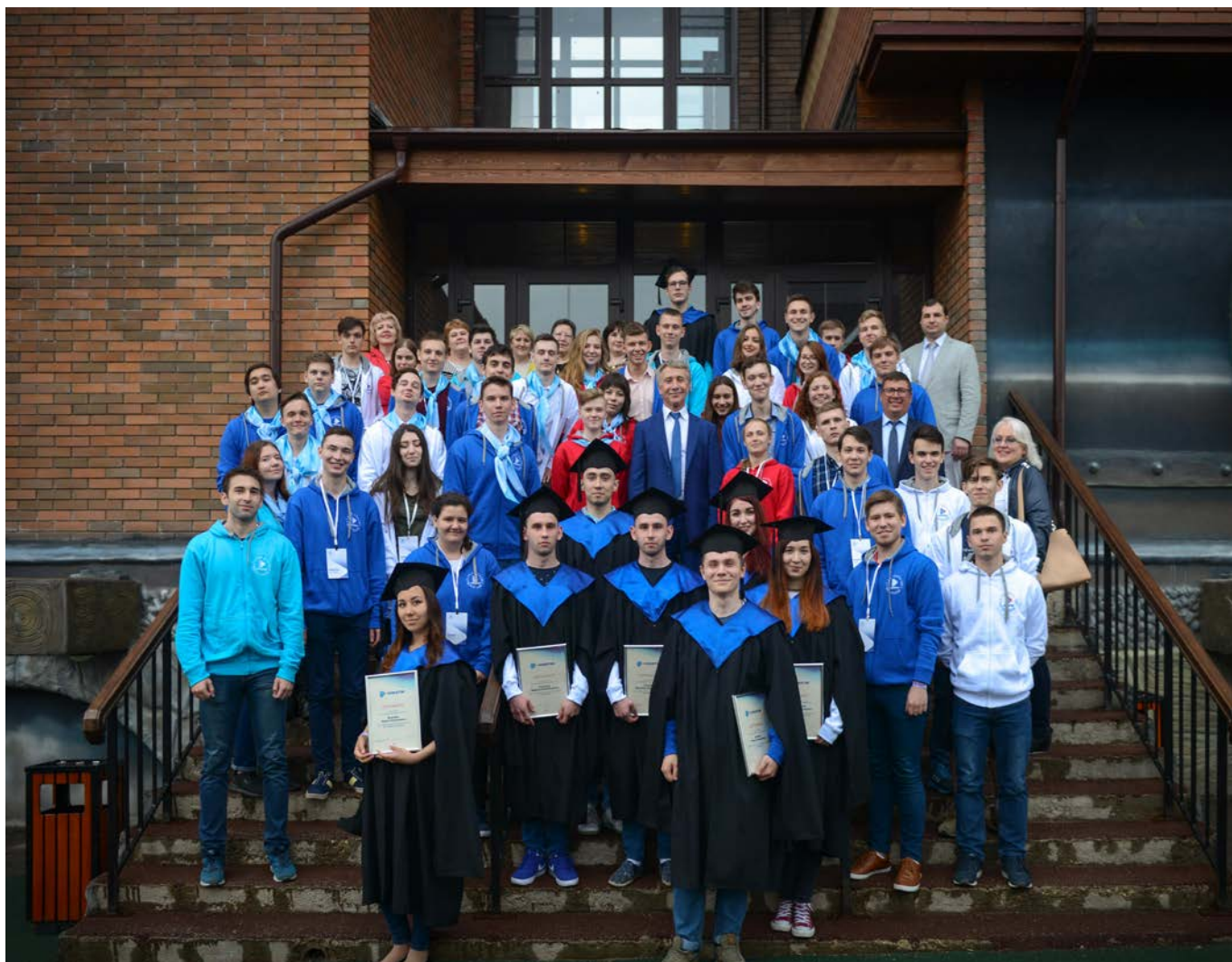
NOVATEK attaches great importance to programs for the development of mass and high-performance sports. The Company, its subsidiaries and joint ventures regularly hold tournaments in the most popular and wide-spread sports: football, volleyball, swimming, skiing, to name a few.

The Company supported the children and youth sports in the regions of its operations. In 2018, the "NOVATEK – Step to Bigger Football" Indoor Football Cups among secondary school teams were held in the Chelyabinsk and Kostroma regions. More than eleven thousand boys and girls took part in the competitions. As part of the World Football Championship 2018 youth events, a match of the winning teams of the Chelyabinsk and Kostroma championships was held on Moscow's Red Square.

The Company supported the Figure Skating and Ice Hockey Federations of the Yamal-Nenets Autonomous Region, and Student Basketball Association with more than 800 teams and 10,000 boys and girls participating in competitions. The Russian Federation of Dance Sports and Acrobatic Rock'n'Roll and the Company support corporate dance sport and acrobatic rock'n'roll clubs in the regions where the Company operates. In April 2018, members of the corporate acrobatic rock'n'roll clubs participated in the 3rd Russia-wide acrobatic rock'n'roll competition Rock'n'Roll & Co.

In the reporting year, NOVATEK continued cooperation with the Football Union of Russia as the General Partner of the Russian National Football Teams. The Company supported women's volleyball club Dinamo and the NOVA Volleyball Club (Novokuybishevsk).





Student Council meeting in 2018

## CHARITY

In 2017, NOVATEK adopted its Charity Policy, which provides for supporting children in desperate need of medical care residing in the regions where we operate.

In 2018, the Company kicked off execution of the new charity project titled "Health Territory". As part of this project, lead specialists of the Russian Children's Clinical Hospital visited children of the YNAO, Murmansk and Kostroma.

In the reporting year, the Company procured equipment for regional healthcare facilities and financed treatment and rehabilitation programs for prematurely-born and partially sighted children. The Company provided targeted assistance to children with severe conditions. In addition to its charity policy, the Company implemented

cultural programs for handicapped children and children from low-income and large families.

In 2018, the "All Together" volunteer movement celebrated its 10-year anniversary. Over the past ten years the charity's geography has expanded significantly, while it has remained focused on supporting orphans, children with various diseases, seniors and World War II veterans as its primary activity. In the reporting year, the first charity campaign aimed at providing help for animals was organized.



# 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 Articles of association and internal documents available on our website ([www.novatek.ru](http://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 No. 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.

The Company monitors changes of the current legislature and the Listing Rules of PAO Moscow Exchange and harmonizes its internal documents according to the changes. NOVATEK's Regulations on the Corporate Secretary, the Internal Audit Policy, Regulations on Risk Management and Internal Control System and other regulations on the Company's corporate bodies are current and do not require any amendments, corrections and/or changes.

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 to the benefit of the Company and its stakeholders.

## 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 Articles of association, 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 20 April 2018, 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 FY2017. 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 2018.

On 28 September 2018, the Extraordinary General Meeting of Shareholders approved the amount of interim dividend for the first half of 2018.

Following a request made by one of our shareholders to convene the meeting of shareholders with a view to re-electing the Board of Directors, on 18 January 2019, the Extraordinary General Meeting of Shareholders was held where a new composition of NOVATEK's Board of Directors was elected.

## Board of Directors

The Board of Directors (the Board) activity is governed by the laws of the Russian Federation, the Company's Articles of association 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 stakeholders, and ensures the Company's efficient and effective performance with the aim of increasing shareholder value in a prudent and responsible manner.

The Board determines the Company 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 the General Meeting of Shareholders. The General Meeting of Shareholders elects the members of the Board of Directors.

The current members of the Board of Directors were elected at the Annual General Meeting of Shareholders on 20 April 2018 and with further amendments made on 18 January 2019 at the Extraordinary General Meeting of Shareholders. The Board of Directors is comprised of nine (9) members, of which eight (8) are non-executive directors, including three (3) directors who are considered to be independent. The Chairman of the Board is Alexander 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 (elected at the Annual General Meeting of Shareholders on 20 April 2018):**

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

### **The Board of Directors membership (elected at the Extraordinary General Meeting of Shareholders on 18 January 2019):**

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

## BOARD ACTIVITIES DURING THE 2018 CORPORATE YEAR\*

To ensure the Company's efficient performance, the Board meetings are convened on a regular basis at least once every two months. During corporate year 2018, the Board of Directors (BoD) met 15 times, of which five meetings were held in the form of joint attendance. The following key issues were discussed and respective decisions made:

- reviewed and approved the Company's 2018 full year operating and financial results;
- recommended an interim dividend payment for first half 2018, based on interim financial results for the period, and a full year dividend payment for 2018, based on full year financial results;
- made decisions to convene an Extraordinary and Annual General Meetings of shareholders. During the meetings in 2018, telecommunications facilities were used to provide shareholders with remote access to participate and to fill out an electronic ballot form;
- reviewed and approved NOVATEK's business plan for 2019;
- passed a number of decisions on changing and increasing the number of members in NOVATEK Management Board up to thirteen persons;
- passed a resolution for NOVATEK to acquire 100% interest in OOO Maritime Arctic Transport;
- NOVATEK and Fluxys signed an agreement on joint development, design, construction, financing, ownership and operation of a mid-scale LNG transshipment terminal in the port of Rostock. In this connection, the BoD passed a resolution for NOVATEK to acquire a 49% stake in the authorized capital of ROSTOCK LNG GmbH;
- Based on the estimation by the Remuneration and Nomination Committee of NOVATEK's Board of Directors for the compliance with Independence Criteria established by the Moscow Exchange Listing Rules, the BoD acknowledged Burckhard Bergmann as an independent BoD member despite the fact that his membership in the Board of Directors is more than 7 years (but less than 12 years);
- The Company carried out a preliminary internal assessment of the internal audit activities resulting in submitting of the revised version of the Internal Audit Policy for the Board of Directors consideration. The Policy was aligned with the International Standards for the Professional Practice of Internal Auditing and the amended Law On Joint Stock Companies.

In order to improve efficiency of corporate governance, the Company carried out an external assessment of the BoD and the BoD Committees activities.

### Board and Committee Meetings Attendance in the 2018 Corporate Year

Member	Independence	Board of Directors	Audit Committee	Remuneration and Nomination Committee	Strategy Committee
Alexander E. Natalenko		15/15			5/5
Andrei I. Akimov		15/15			5/5
Burckhard Bergmann** independent		15/15	1/1	1/1	5/5
Michael Borrell		15/15			5/5
Robert Castaigne independent		15/15	5/5	6/6	
Arnaud Le Foll (from 18.01.2019)		6/6			1/1
Leonid V. Mikhelson executive		15/15			
Victor P. Orlov independent		15/15	5/5	6/6	
Andrei V. Sharonov independent (up to 18.01.2019)		9/9	4/4	5/5	
Gennady N. Timchenko		15/15			5/5

\* From the Annual General Meeting of Shareholders on 20 April 2018 until the Annual General Meeting of Shareholders on 23 April 2019.

\*\* Elected as a member of the Audit Committee and Remuneration and Nomination Committee on 18 January 2019.

During corporate year 2018, an external assessment of the BoD activities was performed in accordance with the recommendations of the Russian Corporate Governance Code. Following the review process headed by the Chairman of the BoD and the Remuneration and Nomination Committee, the Independent Directors Association was chosen as the external appraiser, which is a recognized Russian institution in the area of corporate governance and board of directors assessment, representing Russia in the Global Network of Director Institutes.

Assessment of the BoD activity had several stages, including a questionnaire, individual interviews with directors, as well as analysis of internal documents regulating the corporate governance issues.

During the appraisal process, the key areas of the BoD and the Committees activities were analyzed, including the formation of strategy, supervisory and control functions, effectiveness of interaction with the top management, risk management, remuneration, succession and development of key managers.

Based on the external evaluation, we determined directions for increasing the Board of Directors performance efficiency. The Board Committees conduct annual updates of NOVATEK Group's Risk Map and determine the acceptable risk level in the Company, annual reviews of the Company's Information Policy compliance report, the report on compliance with

Anti-corruption Policy, the Sustainable Development Report, the HSE performance report, and the report on the Company's social activity in the regions where the Company operates.

## Board Committees

The Company has three (3) Board Committees: the Audit Committee, the Remuneration and Nomination Committee and the Strategy 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.

### Committees membership from 20 April 2018 to 18 January 2019:

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

### Committees membership from 18 January 2019:

	Audit Committee	Strategy Committee	Remuneration and Nomination Committee
<b>Chairman</b>	Robert Castaigne	Burckhard Bergmann	Victor P. Orlov
<b>Members</b>	Burckhard Bergmann Victor P. Orlov	Andrei I. Akimov Arnaud Le Foll Michael Borrell Alexander E. Natalenko Gennady N. Timchenko	Burckhard Bergmann Robert Castaigne

## 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 the 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 2018, the Audit Committee met five (5) times, including three meetings in presentia.

## REMUNERATION AND NOMINATION COMMITTEE

The primary functions of the Remuneration and Nomination Committee are 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 generating 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 basis 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 2018, the Remuneration and Nomination Committee met six (6) times, including three meetings in presentia.

## 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 2018, the Strategy Committee met five (5) times, including four meetings in presentia.

## 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 Articles of Association, resolutions 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 Articles of Association.

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 was elected by the Board of Directors on 25 August 2017 (Minutes No. 198 of 25 August 2017) with further amendments by resolution of the Board of Directors on 12 July 2018, 21 September 2018, 14 November 2018, 14 December 2018, including with regard to the quantitative composition (increased up to thirteen members).

#### **Management Board Members from 1st January 2018 to 31 December 2018:**

- **Leonid V. Mikhelson** – Chairman
- **Alexander M. Fridman** – First Deputy Chairman
- **Lev V. Feodosyev** – First Deputy Chairman
- **Vladimir A. Baskov** – Deputy Chairman
- **Viktor N. Belyakov** – Deputy Chairman of the Management Board for Economics and Finance
- **Eduard S. Gudkov** – Deputy Chairman of the Management Board (elected on 21 September 2018)
- **Mark A. Gyetvay** – Deputy Chairman
- **Evgeny A. Kot** – Deputy Chairman of the Management Board - LNG Director (elected on 14 December 2018 and started acting from 14 January 2019)
- **Tatyana S. Kuznetsova** – Deputy Chairman - Director of Legal Department
- **Denis B. Solovyev** – Deputy Chairman of the Management Board - Director of Communications Development Department (elected on 21 September 2018)
- **Ilya V. Tafintsev** – Deputy Chairman of the Management Board
- **Sergey V. Vasyunin** – Deputy Chairman of the Management Board - Operations Director
- **Denis G. Khramov** – Deputy Chairman (the authorities were terminated on 12 July 2018)
- **Igor A. Plesovskikh** – Deputy Chairman of the Management Board - Director for Geology (the authorities were terminated on 14 November 2018)

## **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's 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.

## **Internal Control and Audit**

NOVATEK has a system of internal controls over financial and business operations organized taking into account the applicable requirements of the Russian Federation legislation and best international practices. The internal control system is an integral part of the risk management

Information on remuneration of members of NOVATEK's Board of Directors and Management Board in 2018, RR mln

	Board of Directors*	Management Board
<b>Total paid, including:</b>	<b>129.7</b>	<b>3,208.7</b>
Salaries	-	805.5
Bonuses	-	2,346.0
Fees	127.8	-
Other property advancements	1.9	57.2

system and is in line with the relevant risks and strategic objectives of NOVATEK.

The primary objectives of the internal control system are ensuring the implementation of the NOVATEK strategy, protecting the interests of the shareholders, safeguarding the assets, ensuring the efficiency of the financial and business operations, and compliance with the applicable requirements of the law and the Group's internal regulations.

The internal control system is implemented on a constant basis and covers all areas of activities of the Company and business processes at all management levels.

Defining the principles and approaches to organizing the internal control system is vested in the Board of Directors. The Chairman of the Management Board ensures the efficient functioning of the internal control system. The Internal Audit Division evaluates the risk management, internal control and corporate governance system efficiency.

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 affiliates, 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 approved by the Board of Directors on 1 September, 2014 (Minutes No. 170 of 1 September, 2014) 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) with further alterations and amendments.

## REVISION COMMISSION

The Revision Commission consisting of four members is 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 PAO NOVATEK Articles of Association and the Regulations on the Revision Commission Procedures approved by the General Meeting of Shareholders in 2005 (Minutes No. 95 of 25 March 2005) for the matters which are not set out in the aforementioned law.

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 Articles of Association. The results are presented in the form of findings by the Revision Commission.

In March 2019, the Revision Commission completed the on-site audit revision of financial and business activities of the Company for the year 2018. As a result, the conclusions about the reliability of the data contained in the Company's 2018 Financial Statements (under the Russian accounting standards), 2018 Annual Report and Report on interested-party transactions 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 system, as well as corporate governance practices, the Company and its subsidiaries and affiliates perform internal audits of their operations.

\* 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.

Performing audits in subsidiaries and affiliates is centralized and performed by the NOVATEK Internal Audit Division. The Internal Audit Division is functionally subordinated to the Board of Directors and administratively subordinated to the Chairman of the Management Board.

In its activity the Internal Audit Division is guided by International Standards for the Professional Practice of Internal Auditing. The NOVATEK Internal Audit Policy is approved by the Board of Directors (Minutes No.192 dated August 26, 2016) as amended and supplemented, approved by the Board of Directors (Minutes No. 212 dated December 14, 2018).

The Division carries out its activities on the basis of an annual plan of inspections prepared with the use of a risk-oriented approach mainly. According to the results audit 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 Quality Assurance and Improvement Program is developed and implemented in the Internal Audit Division. In accordance with this program, the Internal Audit Division Self-Assessment is carried out annually and the results are reported to the Audit Committee. In 2018, the Division initiated the external assessment recommended by the International Institute of Internal Auditors to be carried out every five years. To render external appraisal services, the Audit Committee selected Ernst and Young – Appraisal and Consulting Services Ltd. [The assessment identified the compliance of the NOVATEK Internal Audit Division activities with International Standards for the Professional Practice of Internal Auditing].

The Internal Audit Division interacts with an external auditor: in sharing information related to working plans, inspection results and other matters of relevance to the parties.

To improve the efficiency and optimize the costs, the Internal Audit Division employees serve on the revision commissions of the Company affiliates.

## EXTERNAL AUDITOR

The Annual General Meeting of Shareholders approved an external auditor to conduct an 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 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 2018 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 the level of their professional qualifications, independence, possible risk of any conflict of interest, terms of the contract, and the 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 2018.

In accordance with auditing standards, in order to maintain independence, the Company's External Auditor regularly rotates its key audit partner, at least once every seven years. The last time the Auditor's partner was rotated was in 2018.

## 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 2018, 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).

### Auditor's fees in 2018, RR mln

Audits of PAO NOVATEK (audit of the Group's consolidated financial statements and audit of statutory financial statements of PAO NOVATEK)	34
Other services	8
<b>Total auditor's fees and services</b>	<b>42</b>

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 2018, NOVATEK's GDRs were issued on 599,549,590 ordinary shares comprising 19.75% of the Company's share capital.

In 2018, Leonid V. Mikhelson, member of NOVATEK's Board of Directors, made transactions with NOVATEK's shares:

- acquisition of 16,000 GDRs under a securities sales and purchase agreement (10 April 2018);
- acquisition of 4,010 GDRs under a securities sales and purchase agreement (11 April 2018);
- acquisition of 12,360 GDRs under a securities sales and purchase agreement (12 April 2018).

## 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 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 considers 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 the financial stability and flexible capital structure of the Company. NOVATEK is strongly committed to its dividend policy.

On 19 March 2019, the Board of Directors of PAO NOVATEK recommended to the Annual General Meeting of Shareholders to pay dividends for FY 2018 in the amount of RR 16.81 per ordinary share or RR 168.1 per one Global Depositary Receipt (GDR), exclusive of RR 9.25 of interim dividends per ordinary share or RR 92.50 per one GDR paid for the first six months of 2018.

Thus, should the General Meeting of Shareholders approve the recommended dividend, the dividends for 2018 will total RR 26.06 per ordinary share (RR 260.6 per

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

	As of	Equity stake	Number of ordinary shares, including GDRs certifying rights of ordinary shares
<b>Board of Directors</b>			
Alexander E. Natalenko	31.12.2018	-	-
Andrei I. Akimov	31.12.2018	-	-
Burckhard Bergmann	31.12.2018	-	-
Michael Borrell	31.12.2018	-	-
Robert Castaigne	31.12.2018	-	-
Leonid V. Mikhelson	31.12.2018	0.7288	22,127,032
Victor P. Orlov	31.12.2018	-	-
Gennady N. Timchenko	31.12.2018	-	-
Andrei V. Sharonov	31.12.2018	-	-
Arnaud Le Foll	18.01.2019	-	-

\* 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.

	As of	Equity stake	Number of ordinary shares, including GDRs certifying rights of ordinary shares
<b>Management Board</b>			
Vladimir A. Baskov	31.12.2018	0.0288	874,408
Viktor N. Belyakov	31.12.2018	-	-
Lev V. Feodosyev	31.12.2018	-	-
Alexander M. Fridman	31.12.2018	0.0817	2,481,049
Mark A. Gyetvay	31.12.2018	-	-
Eduard S. Gudkov	31.12.2018	-	-
Evgeny A. Kot	14.01.2019	-	-
Denis G. Khramov	31.12.2018	-	-
Tatyana S. Kuznetsova	31.12.2018	0.1944	5,903,035
Igor A. Plesovskikh	31.12.2018	-	-
Denis B. Solovyov	31.12.2018	-	-
Ilya V. Tafintsev	14.11.2018	-	-
Sergey V. Vasyunin	12.07.2018	0.0003	9,320

one GDR), and the total amount of dividends payable for 2018 will be RR 79,126,134,360. This will represent a 74.3% increase in dividend per share compared to 2017.

The amount of paid dividends accrued for the years 2013 to 2017, and for the first six months 2018 is reported as of 31 December 2018. 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 complies with the best practices for information disclosure while adhering to a maximum level of information transparency. The Regulations on Information Policy approved by the Board of Directors as amended and

restated in 2017 (Minutes No. 198 of 25 August, 2017), 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 services in accordance with the Russian and foreign applicable laws. 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. The Company regularly participates in information disclosure on greenhouse gas emissions and energy efficiency of production – the Carbon Disclosure Project

### Accrued and paid dividends on NOVATEK shares for the period 2013 to 2018

Dividend Accrual Period	Amount of dividends, RR per share	Total amount of dividends accrued, RR	Total amount of dividends paid, RR
2013	7.89	23,956,454,340	23,956,386,795
2014	10.30	31,273,951,800	31,273,942,156
2015	13.50	40,990,131,000	40,990,062,712
2016	13.90	42,204,653,400	42,204,605,985
2017	14.95	45,392,774,700	45,392,718,222
First half 2018	9.25	28,085,830,500	28,085,776,082



(CDP), and on the use of water resources – the CDP Water Disclosure Project, as well as other industry publications and studies.

The Company maintains an ongoing dialog with shareholders and investors in order to ensure full awareness of the 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 basis 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 2018, the Public Relations Department hosted 24 meetings between the Company management and journalists of foreign and federal periodicals and organized 18 trips to visit the Company's regional production facilities involved in the implementation of the NOVATEK projects.

In 2018, the number of publications on the Company's activities increased by 34% compared to the previous year, the growth of TV stories on Federal channels and references on radio broadcasting stations amounted to 37%. At the end of the reporting year, there were more than 89,000 publications about the Company. Among the topics covered were the successful and ahead-of-schedule launch of Train 2 and Train 3 of the Yamal LNG Project, the plant ramp-up, LNG production and delivery ramp-up, entering new sales markets, the Company's prospective projects, local manufacturing content and supporting Russian manufacturers of LNG plant equipment, the active involvement of the Company in the development of the Arctic and implementation of the May Russian President decree on increasing the goods traffic via NSR to 80 mln t until 2024, and the Company's position on the global LNG market as one of its major players.

The number of publications in 2018 in foreign media exceeded 10,000, thus it increased by 55% compared with the year 2017. The main topics for foreign media were the Yamal LNG Project implementation, prospective projects of the Company, relations with foreign partners, increase in supply volumes and new sales markets.

Regular press tours were organized for Russian and foreign journalists to Sabetta. In addition, major federal and regional media covered two meetings in Chelyabinsk and Nizhny Novgorod on the subject of engaging Russian industry in the Company's LNG projects involving representatives of Russian enterprises.

NOVATEK takes active part in industrial exhibitions and conferences. In 2018, NOVATEK's managers and employees participated in more than 20 industry exhibitions, conferences and round tables. In 2018, the Company took part in the St. Petersburg International Economic Forum,

Eastern Economic Forum, and Russian Energy Week. NOVATEK delegations also took part in the work of major international business and industry events: the World Economic Forum in Davos, Conference on Natural Gas, LNG and associated gas, Gastech-2018 in Barcelona.

The following corporate periodicals are published to inform the Company's employees, their family members, and third parties of the Company's activities: the NOVATEK newspaper and the NOVATEK PLUS magazine, containing materials on production plans and results as well as on cultural, sports and charity programs and projects.

The main events of NOVATEK are published on the Company's official website and intranet portal. For interaction with the public, NOVATEK makes use of up-to-date channels of information dissemination through social media. The Company keeps its accounts in English and Russian on Facebook, VKontakte, Twitter, Instagram, and YouTube, where the channel subscribers stay updated with the Company's activities. There were 120 publications in the Company's social media in 2018. The number of subscribers increased by a factor of 2.5 as compared to 2017 and amounted to more than 7,000 people.

# 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 of the reliability and efficiency of the risk management framework and review of the risk management policy. In the reporting year, the Audit Committee paid great attention to risk management in the Company and during the meetings, after careful review and analysis of the information provided, it 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.	<p>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.</p> <p>The Company adheres to the principle of responsible investments which implies that new design solutions, technologies and equipment installed help significantly mitigate accident risks.</p> <p>The Central Dispatch Office (CDO) operates in the Company, one of its functions is to ensure prompt response to production incidents. 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.</p> <p>A Digital Field Production Management System was commissioned in three entities to ensure production management and prompt response to process incidents. It enables promptly calculating the optimum process mode in a semi-automatic way, identifying deviations and planning field operations.</p>

Risk	Risk description	Risk management approaches used by the Company
Monopoly risks	<p>The Company depends on monopoly suppliers of transport services (such as Gazprom, RZD, and Transneft). The Company has no influence on the capacity of transport facilities of the above monopolies and rates established by a Federal body.</p>	<p>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.</p> <p>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).</p>
Competitive risks	<p>The Company operates in an environment of tough competition with Russian and international oil and gas companies in the following areas:</p> <ul style="list-style-type: none"> <li>• obtaining of subsoil licenses and acquisition of companies holding subsoil licenses</li> <li>• selling gas in the Russian and global markets</li> <li>• selling liquid hydrocarbons in the Russian and global markets</li> <li>• selling liquefied natural gas in the Russian and global markets</li> <li>• access to transportation infrastructure, which has technological limitations</li> <li>• employment of highly qualified specialists to work for the Company, its subsidiaries and joint ventures</li> </ul>	<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>The Company pursues an active marketing policy and takes efforts to monitor, expand and balance its customer base, and strives to enter into long-term agreements with buyers.</p> <p>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.</p> <p>The Company expands its footprint in the global LNG market, increases its customer base and makes spot, mid-term and long-term sale and purchase agreements, which enables mitigating risks associated with a specific market or counterparty.</p> <p>The Company implements an active HR policy and applies efficient mechanisms of attracting and retaining highly qualified employees.</p>
Risks in Procurement of Materials, Works and Services	<p>Failure to perform their obligations by the counterparties (quality and timeline of procurement, works and services).</p> <p>Procurement of materials, works and services at prices higher than the market</p>	<p>The Company has put in place internal regulations and introduced a procedure to qualify counterparties and control performance of obligations. The Company has continuously encouraged its counterparties to improve their production capabilities, while making long-term agreements with the strategic counterparties.</p> <p>In 2018, the Company introduced a set of measures to optimize procurement activities, aiming to enhance control over the efficiency of spending on investment and operations, as well as to shorten counterparty selection procedures, and to ensure completeness and quality of procurement documentation, enabling prompt and efficient decisions.</p> <p>Counterparties are as far as possible selected on a competitive basis. Strategic approaches ensuring maximum procurement efficiency are defined for the most critical and expensive procurement items and timely satisfaction of needs.</p>

Risk	Risk description	Risk management approaches used by the Company
	Reputational risks deriving from competition restriction and malpractice by employees	<p>Procedures are developed within the Company that provide for an objective, timely and transparent process of counterparty qualification and selection. There is no discrimination and unwarranted restriction of competition in the Company when developing qualification and technical requirements to counterparties and to the subject of procurement as part of design and qualification as well as at the stage of counterparty selection. The internal regulations in place provide for a maximum transparency procedure of counterparty selection with an adequate system of control over the actions of employees. Open ways to select counterparties are mostly used.</p> <p>Given the volatility in international relations with the countries providing sophisticated oil &amp; gas equipment, the Company pursues import replacement policies where it is appropriate.</p>
Commodity price risks	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.	State regulation of gas prices significantly reduces the risk of price volatility on the Russian gas market.
	Moreover, the Company is exposed to the current pricing environment on the Russian and international liquid hydrocarbon and LNG markets as it has no power over the contracts' base prices. Reduction of prices for liquid hydrocarbons and LNG may have a negative effect on the Company's financial performance.	<p>The Company monitors changes in the global gas and LNG price environments and negotiates with LNG buyers striving to make efficient sale and purchase agreements.</p> <p>In view of the vertically integrated production chain for liquid hydrocarbons and LNG, the Company does not use commodity derivative financial instruments to reduce the risk of price changes for such type of products.</p>
Geological risks	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>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.</p> <p>The Company makes an 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	Exploration and production of hydrocarbons in Russia is subject to licensing.	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.
	The Company is thus exposed to the risk of early termination, suspension or restriction of its right to use subsurface mineral resources.	



Risk	Risk description	Risk management approaches used by the Company
Environmental risks	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>The Company has an environmental management system according to ISO 14001 standard to ensure rational use of resources and to minimize the adverse effect the Company's operation may have on the environment.</p> <p>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	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>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>
Strategic risks	There is a risk that the Company will fail to meet its strategic goals and objectives due to significant changes in external environment, realization of individual, or a group of, operational, financial and legal risks.	The Company strives to prudently accomplish strategic goals and objectives and applies the approaches described in this section to manage each of the risks. In order to efficiently manage its project portfolio and to ensure sustainable development, the Company regularly monitors market trends as well as takes into account risks and opportunities of the current and anticipated external environment. The decision-making process in strategic management includes, inter alia, an assessment of project execution risks and evaluation of resources required for their successful execution, including an analysis if financial, material and human resources employed are sufficient and/or if use of additional resources is justified.
Ethical risks	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>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 operation 24/7.</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>

Risk	Risk description	Risk management approaches used by the Company
Social risks	<p>The Company is subject to the following risks of a social nature:</p> <ul style="list-style-type: none"> <li>• 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;</li> <li>• external risks associated with potential impediments in normal production activities caused by the public living in proximity to the production facilities</li> </ul>	<p>The Company strives to ensure compliance of its social programs with the industry's average level and uses 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	<p>The Company is subject to risks of unlawful interference acts and terrorist threat concerning operation of fuel and energy facilities, transport and other facilities (areas).</p>	<p>The Company implements all necessary measures to fully comply with legislative requirements in the area of security and counter-terrorism measures at fuel and energy facilities, transport and other facilities (areas).</p>
Country risk	<p>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.</p> <p>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.</p> <p>These factors have a negative impact on the Company's operational and financial performance.</p> <p>The Company is involved in foreign projects related to LNG transportation and sales, and in projects aimed at enlarging its geographic footprint in hydrocarbon exploration, production and transportation. Legislative and political changes in the countries where the Company operates may affect financial performance and the cost of such projects.</p>	<p>Active marketing and financial policies enable the Company to mitigate the country risk.</p> <p>Moreover, the Company's management continuously analyzes the macro-economic environment and makes prompt decisions to mitigate potential risks.</p> <p>The Company continuously monitors legislative changes in the countries where it operates, analyzes the political situation, takes part in negotiations and builds up long-term partner relations with state authorities and various stakeholders.</p>

Risk	Risk description	Risk management approaches used by the Company
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 taken into account by the Company's management at the onshore production and processing facilities design and operation stage.
	In 2018, the Company started geological exploration works in the Ob Bay. Due to severe climatic conditions, there are risks of natural and man-induced emergencies when drilling offshore exploration wells.	<p>The Company implements a range of measures to prevent natural climatic conditions and man-caused factors from impacting offshore wells construction, such as:</p> <ul style="list-style-type: none"> <li>• construction is ongoing only during guaranteed ice-free season</li> <li>• continuous meteorological and ice monitoring is in place</li> <li>• all the required manpower and craft are continuously in place to implement an emergency response plan in the offshore and onshore operations area</li> <li>• comprehensive emergency drills are carried out in the course of construction involving rescue vessels with necessary equipment and specialized trained personnel on board.</li> </ul>
	The Company uses the Northern Sea Route (NSR) for LNG and gas condensate shipping. Severe weather and ice conditions in vessel voyage areas, ports, and cargo transshipment points may lead to longer vessel return voyages, a disruption of marketable products offtake, and tank tops, as well as may result in default on timely delivery obligations to buyers.	<p>To mitigate such risks, the Company implements the following measures:</p> <ul style="list-style-type: none"> <li>• coordinates day-to-day tanker management with structural units in charge of fleet planning and positioning, operations and sales, and adjusts production and supply schedules where necessary;</li> <li>• cooperates with Atomflot, Rosmorport, Northern Sea Route Administration and government authorities to ensure necessary icebreaker support along the NSR;</li> <li>• incorporates requirements in all time charter parties that the vessel's officers have necessary experience in ice navigation and that the crews take special training courses and programs with regards to ice navigation;</li> <li>• engages ice pilots and representatives of special institutions and companies when passing difficult ice areas.</li> </ul>
Risks of information technology and information security (cyber-risks)	<p>The Company is exposed to the risks in the area of information technology and information security, such as</p> <ul style="list-style-type: none"> <li>• the risk of confidential information leaks;</li> <li>• the risk of business interruption and the risk of an emergency situation as a result of computer-generated incidents.</li> </ul>	<p>All information processed within the Company's corporate information system is classified, and owners of information resources are defined as are terms for granting access thereto.</p> <p>Pursuant to Federal Law No. 187-FZ dated July 26, 2017, the Critical Infrastructure Categorization Plan is approved in the Company.</p> <p>The information technology development strategy of the NOVATEK Group was developed and approved to ensure the Group's sustainable development.</p>
<b>Financial Risks</b>		
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.

Risk	Risk description	Risk management approaches used by the Company
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, the dynamics of which 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.	<p>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.</p> <p>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.</p>
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 can cause a surge in inflation rates, which are impossible to accurately predict.	<p>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 and LNG export markets, and government policy in relation to tariffs for natural gas.</p> <p>NOVATEK monitors the consumer price index and accordingly acts to mitigate its costs.</p>



Risk	Risk description	Risk management approaches used by the Company
<b>Legal Risks</b>		
Risk of law changes	<p>The Company is subject to a risk of facing consequences of changes in Russian laws in the following areas:</p> <ul style="list-style-type: none"> <li>• currency laws (in areas concerning export/import and borrowing operations)</li> <li>• 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)</li> <li>• customs laws (in areas concerning the export of liquid hydrocarbons, including petroleum products); and</li> <li>• licensing requirements for natural resource extraction.</li> <li>• competition laws (in areas regulating natural gas sales market).</li> </ul>	<p>The Company is constantly monitoring draft laws, elaborates its proposals and takes part in the drafting of laws and incorporation of provisions that are in line with the Company's interests, all enabling it to evaluate the consequences of such changes and to take them into account in its plans.</p>
Litigation risks	<p>The Company may be involved as a defendant or plaintiff in a number of proceedings arising in the normal course of its business.</p>	<p>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.</p>
Risk of sanctions	<p>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 60 days. The sanctions imposed restrict the Company's ability to refinance its debt.</p> <p>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's performance.</p>	<p>The Company follows a balanced financial policy enabling it to minimize its fundraising needs. Moreover, the Company still has full access to the Russian capital market and limited access to the international market.</p> <p>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.</p>

## Risk Insurance

Risk insurance is an integral part of NOVATEK's risk management system. In 2018, 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 the leading rating agencies (Standard & Poor's, Fitch Ratings, 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;
- Construction risk insurance;
- 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 has 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 of 2017 was RR 772 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.

For more than 13 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**

**Member of NOVATEK's Strategy Committee**

Born in 1946

Mr. Natalenko completed his studies at the Irkutsk State University in 1969 with a primary focus on 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 ZAO '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**

**Member of NOVATEK's 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 1991 to 2002, 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 the Board of Directors of PAO Gazprom, Gazprombank (AO), AO Rosneftegaz, OOO Gazprom gas motor fuel and others.

**DR. BURCKHARD BERGMANN****Independent member of NOVATEK's Board of Directors****Chairman of NOVATEK's Strategy Committee****Member of NOVATEK's Audit Committee****Member of NOVATEK's Remuneration and Nomination Committee**

Born in 1943

Dr. Bergmann, born in Sendenhorst (Germany), studied physics at 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, he worked at the German Federal Ministry for Research and Technology and from 1969 to 1972 at the Jülich Nuclear Research Centre. 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, as well as gas billing. In January 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 Board of Management of E. ON AG.

Dr. Bergmann is a Chairman of the Supervisory Board of Accumulatoren-Werke Hoppecke GmbH and a member of the Advisory Boards for Dana Gas, Dubai. Since October 2012, he is a member of the board of trustees of RAG Stiftung. Between 1998 and 2000, Dr. Bergmann held the position of President of Eurogas (the European Union of the Natural Gas Industry) and between 2000 and 2010 he was Vice-Chairman of the Board of the German East-West Trade Committee. Dr. Bergmann was a member of the Board of OAO Gazprom from 2000 to 2011.

Dr. Bergmann holds the following distinctions: Commander of the Royal Norwegian Order of Merit (1997), Foreign Member of the Academy of Technological Sciences of the Russian Federation (2003), Order of Merit of the State of North Rhine-Westphalia (2004), Director of the Year, Moscow (2007), Officer's Cross of the Order of Merit of the Federal Republic of Germany (2008) and the Russian Order of Friendship (2011).

**MR. MICHAEL BORRELL****Member of NOVATEK's Board of Directors****Member of NOVATEK's 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 served as First Vice President of Continental Europe and Central Asia. From January 2015 to September 2017, he worked as Senior Vice-President of Europe and Central Asia. In September 2017, he has been appointed Senior Vice President North Sea and Russia, which comprises the United Kingdom, Norway, Denmark, the Netherlands and Russia.

**MR. ROBERT CASTAIGNE****Independent member of NOVATEK's Board of Directors****Chairman of NOVATEK's Audit Committee****Member of NOVATEK's Remuneration and Nomination Committee**

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 VINCI's Board of Directors and its Audit and Remuneration Committees. He is Chevalier of the National Order of the Legion of Honour.

**MR. ARNAUD LE FOLL****(since 18.01.2019)****Member of NOVATEK's Board of Directors****Member of NOVATEK's Strategy Committee**

Born in 1978

Graduate of "École polytechnique" and "École des mines de Paris" (France) Arnaud Le Foll began his professional career in French ministries and administrations. Between 2003 and 2006 he was Head of Regional Industrial Environment Inspectorate, Rhône-Alpes (Lyons, France), then he moved to a position of Auditor at General Inspectorate of Finance, Ministry of Finance, where he served from 2006 to 2007. In 2007, he became an Advisor on matters related to environment, energy and industry in the offices of C. Lagarde, Minister of Economy, and L. Chatel, Secretary of State in charge of Industry.

Arnaud Le Foll joined Total in 2010, as Analyst Strategy, Total Holding. In 2010 he was promoted to a position of Vice-president strategy and business development Asia-Pacific, Total Marketing & Services (Singapore). From 2013 to 2016, he headed Total Maroc affiliate as Managing Director.

In 2016, Arnaud Le Foll moved from the Marketing & Services branch of Total to Exploration & Production, and was appointed Strategy and Portfolio Management Director, Total E&P Angola.

On January 1, 2018, Arnaud Le Fall became Total Country Chair Russia and General Director, Total E&P Russie.

**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 the 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 a private company, AO SNP NOVA. Mr. Mikhelson remained AO 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. Since 2011, he has been 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, 2nd Degree Order of Merit for the Fatherland 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 a 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, and held positions of 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 4th 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****(up to 18.01.2019)****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 under 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. Mr. Sharonov is a Deputy Head of the Executive Committee of the Moscow Urban Forum. From 2013 to 2016 –Dean of SKOLKOVO Business School and in September 2016 he was elected President of the Business School.

He is currently Chairman of the Board of Directors, an Independent member of the Board of Directors of OOO Management Company NefteTransService; a member of the Boards of Directors of PAO Sovcomflot and PAO PhosAgro, 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, special award for personal contribution to the development of corporate management in 2016 from the Independent Directors Association and the Russian Union of Industrialists and Entrepreneurs. 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 the 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 has been 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, and the Chairman of the Economic Council of the Franco-Russian Chamber of Commerce (CCIFR).

#### **ZULMIRA A. RAZAKOVA**

**NOVATEK's Corporate Secretary**

Ms. Razakova holds a higher legal education degree and began working for NOVATEK in 2004. Between 2007 and 2012, Ms. Razakova held the position of lead specialist of the Management Board and Board of Directors staff. In April 2012, Ms. Razakova was elected as Secretary of the Board of Directors. Since 2014, Ms. Razakova has been NOVATEK's Corporate Secretary.

## **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, Mr. Baskov was appointed Deputy Chairman of NOVATEK's Management Board and in 2007, he became a member of NOVATEK's Management Board.

Mr. Baskov has a PhD in Law. 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. Mr. Baskov also has awards of the Russian Orthodox Church (Order of Holy Prince Daniel of Moscow, Order of Saint Seraphim of Sarov and a medal of St. Sergius).



**MR. VIKTOR N. BELYAKOV****Deputy Chairman of NOVATEK's 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 U. S. independent oil and gas companies 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 by Institutional Investor magazine as one of the Top Five CFO's in Europe's Oil and Gas sector. Institutional Investor voted him as the Best CFO in the EMEA Oil and Gas category for 2017. Finance Monthly magazine named Mark Gyetvay the Best CFO in Russia for the consecutive years of 2015 to 2018, and he received the Game Changer 2017 and 2018 Award for Russia.

From 2003 to 2014, Mr. Gyetvay was a member of NOVATEK's Board of Directors and served on the Investment and Strategy Committee. From 2003 to 2014, he was Chief 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. SERGEY V. VASYUNIN****Deputy Chairman of NOVATEK's Management Board – Operations Director**

Born in 1967

In 1993, Sergey Vasyunin graduated from the Ufa Oil Institute, specializing in the Development and Operation of Oil and Gas Fields. Between 1993 and 1997, Mr. Vasyunin was employed with Condor as deputy director, Stroykomplekt as head of sales department, and with OAO Spetsnefteenergmontazhavtomatika –as marketing engineer. From 1998, he worked in the Urengoygazprom industrial association of OAO Gazprom where he served in the capacity of an oil, gas and condensate production foreman. Between 2002 and 2017, Mr. Vasyunin was employed in the positions of Gas Condensate Production Shop Manager, Deputy General Director for operations, and First Deputy General Director –Chief Engineer of OOO NOVATEK-YURKHAROVNEFTEGAS. In April 2017, he was appointed Deputy Chairman of the Management Board – Director for Operations of NOVATEK.

In 2005, the Russian Ministry of Industry and Energy issued a commendation to Sergey Vasyunin. He holds the Honored Employee of NOVATEK title.

**MR. EDUARD S. GUDKOV****Deputy Chairman of NOVATEK's Management Board**

Born in: 1980

In 2002, Mr. Gudkov graduated from the Penza State University where he specialized in law. In 2006, he received a PhD in Law.

Between 1999 and 2003, Mr. Gudkov worked in the Russian Ministry for Antitrust Policy and Support of Entrepreneurship. In 2003, he joined the Russian Supreme Arbitrazh Court where he held the position of Assistant to the First Deputy Chairman. From 2012, Mr. Gudkov worked at the Executive Office of the Russian Federation Government. In 2013, he was appointed Assistant to the Deputy Prime Minister of the Russian Federation – Head of the Executive Office of the Russian Federation Government.

Since September 2018, Mr. Gudkov has been Deputy Chairman of NOVATEK's Management Board. In 2018, Mr. Gudkov was awarded the Medal of the 2nd Degree Order for Merits and Dedicated Service to the Country.

#### **MR. EVGENY A. KOT**

**Deputy Chairman of NOVATEK's Management Board – Director for LNG**

Born in: 1974

Mr. Kot graduated from the Tyumen State Academy of Architecture and Civil Engineering where he specialized in Economics and Company Management. He received a PhD in Economics from the Saint Petersburg State University of Engineering and Economics.

Between 1997 and 2001, Mr. Kot worked in the Tyumen branch of Gazprombank. From 2001 to 2002, he was employed by OAO SNP NOVA and OAO Oil and Gas Company ITERA.

In 2002, Mr. Kot joined NOVATEK. Between 2009 and 2011, he held the position of Deputy Chairman of the Management Board – Director of LNG Business Development of NOVATEK. Between 2010 and 2014, he was Chairman of the Board of Directors of Yamal LNG. From 2014 to 2018, Mr. Kot was General Director of Yamal LNG.

In December 2018, he was appointed Deputy Chairman of the Management Board – Director for LNG of NOVATEK.

#### **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 Purneftegasegeologiya. In 1998, she was appointed Deputy General Director of OAO Nordpipes. Since 2002, she has been Director of the Legal Department at 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 2nd Degree Order of Merit for the Fatherland.

#### **MR. DENIS B. SOLOVYEV**

**Deputy Chairman of NOVATEK's Management Board – Director of Corporate Communications Department**

Born in: 1977

In 2000, Mr. Solovyev graduated from the Lomonosov Moscow State University with a degree in Political Science. In 2003, he completed postgraduate studies at the Lomonosov Moscow State University with a degree in History. In 2000, he was appointed Deputy General Director of Senat PR LLC. In 2004, Denis Solovyev assumed the role of an adviser to the Krasnoyarsk Territory Deputy Governor and Assistant First Deputy Governor at the Krasnoyarsk Territory Board of Administration. Between 2006 and 2008, he headed an election projects group of the United Russia Central Electoral Commission Directorate.

Mr. Solovyev has been working for NOVATEK since 2008: in the capacity of Public Relations Director (until 2014), and Communications Director – Director of Public Relations Department (from January 2014.).

In September 2018, Mr. Solovyev was appointed Deputy Chairman of NOVATEK's Management Board and Director of Corporate Communications Department.

Mr. Solovyev has received several letters of recognition, honorable mentions from the Russian Ministry of Natural Resources and the Environment as well as from the Parliament of the Khanty-Mansy Autonomous Region. In 2018, he received an award from the Russian Ministry of Energy and an honorable mention from the Governor of the Yamal-Nenets Autonomous Region.

#### **MR. ILYA V. TAFINTSEV**

**Deputy Chairman of NOVATEK's Management Board**

Born in 1985

In 2006, Mr. Tafintsev obtained a BA in Economics from the Higher School of Economics in Moscow. In 2007, he graduated from the University of London (UK), where he majored in investment and finance.

From 2007 to 2011, Mr. Tafintsev held the position of Deputy Director of NOVATEK's Representative Office in London. Between 2011 and 2014, he was a Finance and Investment Advisor with United Bureau of Consultants Limited.

From 2013 to 2015, he served as Strategic Projects Director of NOVATEK. From 2013 to 2018, Mr. Tafintsev was Member of the Board of Directors of SIBUR Holding. Between 2014 and 2016, he held the position of Chairman of the Board of Directors of Yamal LNG. In December 2015, Mr. Tafintsev was appointed Member of the Management Board – Director for Strategic Projects of NOVATEK.

Since September 2018, he has been Deputy Chairman of NOVATEK's Management Board.

**MR. LEV V. FEODOSYEV**

**First Deputy Chairman of NOVATEK's Management Board**

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. Since 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. Since October 2007, Lev Feodosyev has worked for NOVATEK. Before 2011, he worked at 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, Mr. Feodosyev has been Deputy Chairman of the Management Board, Commercial Director of NOVATEK.

In February 2018, he was appointed First Deputy Chairman of NOVATEK's Management Board. 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. From 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 and First Deputy General Director of a joint venture established by PAO Gazprom and DKG-EAST (Hungary). Since 2003, Fridman has been the Deputy General Director of Novafininvest. In 2004, Alexander Fridman was elected Deputy Chairman of the Management Board of NOVATEK. In August 2007, he was elected a member of NOVATEK's Management Board. Since February 2015, he has been First Deputy Chairman of the Management Board of NOVATEK. Mr. Fridman is the recipient of the title of honor "Honored Man of the Oil and Gas Industry".

## Report on major, and interested-party transactions that the Company did in the reporting year

Information in this section of the Annual Report 2018 is not provided pursuant to the Order of the Government of the Russian Federation No. 10 dated 15 January 2018.

## Corporate Governance Code Compliance Report

This Corporate Governance Code Compliance Report (hereinafter "the Report") was reviewed at the meeting of PAO NOVATEK's Board of Directors on 19 March 2019 (Minutes No. 218).

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 2018.

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.

Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
1.1	<b>The Company should ensure equitable and fair treatment of every shareholder exercising their right to take part in managing the Company.</b>			
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.	<p>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.</p> <p>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.</p>	This principle is complied with.	–
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.	<p>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.</p> <p>2. The notice of an upcoming meeting specifies the meeting venue and documents required for admission.</p> <p>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.</p>	This principle is complied with.	–
1.1.3	In preparing for, and holding 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.	This principle is complied with.	–

Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
		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.	This principle is not fully complied with.	<p>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.</p> <p>Materials to the General Meeting of Shareholders include recommendations of the board of directors as required by law.</p> <p>In accordance with paragraph 1 of Art. 54 of the Russian Federal Law "On Joint Stock Companies", the list of information (materials) provided to shareholders in preparation for the General Meeting of Shareholders is determined by the Board of Directors. Accordingly, the Board of Directors, if it deems it necessary, to include its position on the issues on the agenda of the general meeting of shareholders.</p> <p>The Company considers the established procedure to be balanced, not bearing any risks for the Company and its shareholders, and does not plan to change the existing approach.</p>
		3. The Company gave duly authorized 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.	This principle is complied with.	–
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.	<p>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.</p> <p>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.</p>	This principle is complied with.	–



Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
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.	This principle is complied with.	–
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 ask 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.	This principle is complied with.	–
		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.	This principle is complied with.	–
		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.	This principle is complied with.	–
<b>1.2</b>	<b>Shareholders are given equal and fair opportunities to share profits of the Company in the form of dividends.</b>			
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.	This principle is complied with.	–
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.	This principle is complied with.	–
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.	This principle is complied with.	–

Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
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.	This principle is not complied with.	<p>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.</p> <p>The Company does not see any risks in the established practice, as the system of procurement procedures introduced in the Company ensures the conclusion of contracts on market terms.</p>
<b>1.3</b>	<b>Corporate governance framework and practices should ensure equality for the shareholders owning the same type (class) of shares, including minority and non-resident shareholders, and their equitable treatment by the Company.</b>			
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.	This principle is complied with.	–
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.	This principle is complied with.	–
<b>1.4</b>	<b>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.</b>			
1.4.1	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.	This principle is complied with.	–
<b>2.1</b>	<b>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.</b>			
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 Articles of Association to appoint and remove members of executive bodies and to set out the terms and conditions of their contracts.	This principle is not fully complied with.	The issue of determining the amount of remuneration paid to the Chairman of the Management Board based on the results of the work for the year, falls within the authority of the Board of Directors.

Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
				<p>In accordance with the Company's Articles of Association, the members of the Management Board are elected by the Board of Directors from among the Company's employees, solely on the recommendation of the Chairman of the Management Board. The amounts of official salaries and other terms of employment contracts with the Company's employees, including members of the Management Board, are determined by the Chairman of the Management Board taking into account the parameters of the Company's business plan approved by the Board of Directors.</p> <p>The Company considers the established procedure to be effective, balanced, not bearing any risks for the Company and its shareholders, and does not plan to change the existing approach.</p>
		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.	This principle is complied with.	–
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.	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.	This principle is complied with.	–
2.1.3	The Board of Directors defines the Company's risk management and internal control principles and approaches.	<p>1. The Board of Directors defined the Company's risk management and internal control principles and approaches.</p> <p>2. The Board of Directors assessed the Company's risk management and internal control system in the reporting period.</p>	This principle is complied with.	–

Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
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.	<p>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.</p> <p>2. At its meetings in the reporting period, the Board of Directors discussed matters related to such policy (policies).</p>	This principle is not fully complied with.	<p>The costs of the Management Board members and other key executives of the Company shall be reimbursed (compensated) under the applicable legislation.</p> <p>Remuneration of members of the Management Board and other key employees of the Company shall be effected upon the decision of the Chairman of the Management Board within the amount determined with consideration of the parameters of the Company's business plan approved by the Board of Directors.</p> <p>The Board of Directors also determines the remuneration of the Chairman of the Management Board based on the performance of the Company in the reporting year.</p> <p>The Company considers the established procedure to be balanced, not bearing any risks for the Company and its shareholders, and does not plan to change the existing approach.</p>
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.	<p>1. The board of directors plays a key role in preventing, identifying and resolving internal conflicts.</p> <p>2. The company set up mechanisms to identify transactions leading to a conflict of interest and to resolve such conflicts.</p>	This principle is complied with.	–
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.	<p>1. The board of directors approved the Company's information policy regulations.</p> <p>2. The company identified persons responsible for implementing the information policy.</p>	This principle is complied with.	–
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.	This principle is complied with.	–

Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
<b>2.2</b>	<b>The board of directors is accountable to the Company's shareholders.</b>			
2.2.1	Performance of the board of directors is disclosed and made available to the shareholders.	<p>1. The Company's annual report for the reporting period includes the information on individual attendance at board of directors and committee meetings.</p> <p>2. The annual report discloses key performance assessment results of the board of directors in the reporting period.</p>	This principle is complied with.	–
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.	This principle is complied with.	–
<b>2.3</b>	<b>The board of directors manages the company in an efficient and competent manner and make fair and independent judgments and decisions in line with the best interests of the company and its shareholders.</b>			
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.	<p>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.</p> <p>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.</p>	This principle is complied with.	–
2.3.2	The Company's directors are elected via a transparent procedure that enables shareholders to obtain information on nominees sufficient to judge their personal 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.	This principle is complied with.	–
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 for professional qualifications, experience and business skills.	This principle is complied with.	–



Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
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.	This principle is complied with.	–
<b>2.4</b>	<b>The board of directors includes a sufficient number of independent directors.</b>			
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.	This principle is complied with.	–
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.	<p>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.</p> <p>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.</p> <p>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.</p>	This principle is complied with.	–
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 the board members.	This principle is complied with.	–

Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
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.	This principle is not fully complied with.	<p>In accordance with the Company's Articles of Association, the Regulations on the Board of Directors and the Regulations on the Committees of the Board of Directors, a large block of issues related to significant corporate actions is preliminarily considered by the Audit Committee and the Remuneration Committee consisting of independent directors. In addition, most of such decisions shall be approved by the Board of Directors, if 8 out of 9 directors voted for the corresponding decision. Thus, any two independent directors may block the adoption of an undesirable decision in their opinion.</p> <p>The Company believes that independent directors have sufficient capacity to assess significant corporate actions.</p>
<b>2.5</b>	<b>The chairperson of the board ensures that the board of directors discharges its duties in the most effective and efficient way.</b>			
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.	<p>1. The board of directors is chaired by an independent director, or a senior independent director is appointed from among the independent directors.</p> <p>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.</p>	This principle is not fully complied with.	<p>The role of independent directors on the Company's Board of Directors is very important, since the Audit Committee and the Remuneration and Nomination Committee of the Board of Directors are comprised of independent directors only. 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 of the Board members who is not an independent director.</p> <p>The Company considers the established procedure to be balanced and does not plan to change the existing approach.</p>

Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
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.	This principle is complied with.	–
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.	This principle is complied with.	–
<b>2.6</b>	<b>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.</b>			
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.	<p>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.</p> <p>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.</p> <p>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.</p>	This principle is complied with.	–
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.	This principle is complied with.	–
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>	This principle is complied with.	–

Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
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>	This principle is complied with.	–
<b>2.7</b>	<b>Meetings of the board of directors, preparation for such meetings and participation of board members therein ensure efficient performance by the board of directors.</b>			
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.	This principle is complied with.	–
2.7.2	The Company's internal regulations stipulate the procedure to prepare for and hold the board's meetings, enabling the directors to make proper preparations for them:	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.	This principle is complied with.	–
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.	This principle is complied with.	–
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.	This principle is not fully complied with.	<p>The Company's Articles of Association do not provide for resolutions of the Board to be passed by qualified majority on the following matters:</p> <ul style="list-style-type: none"> <li>• submission to the General Meeting of matters relating to the Company's liquidation</li> <li>• submission to the General Meeting of matters relating to amendments to the Company's Articles of Association</li> <li>• review of material issues relating to operations of legal entities controlled by the Company.</li> </ul>

Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
				<p>The Company deems sufficient the existing norm stipulated in the legislation and the Articles of Association according to which decisions on amendments and additions in the Company's Articles of Association, including approval of the latter in a new wording, as well as on Company's liquidation, appointment of a winding up commission and approval of the interim and final liquidation balance shall be made by the general shareholders meeting by the three-fourths majority of the votes of shareholders holding the voting shares and taking part in the general shareholders meeting.</p> <p>The Company considers the established procedure to be balanced, not bearing any risks, and does not plan to change the existing approach.</p>
<b>2.8</b>	<b>The board of directors sets up committees for preliminary consideration of the most important issues related to the business of the company.</b>			
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, analyzing, 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>	This principle is complied with.	–



Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
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>	This principle is complied with.	–
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>	This principle is complied with.	–
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.	This principle is complied with.	–

Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
2.8.5	Committees are composed so as to enable comprehensive discussions of matters under preview, taking into account the diversity of opinions.	<p>1. Committees of the board of directors are headed by independent directors.</p> <p>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.</p>	This principle is not fully complied with.	<p>The Board of Directors' audit committee and remuneration and nomination committee are not only headed by but also fully consist of independent directors.</p> <p>Formally, the director heading an additional committee, the Strategy Committee, is not an independent director. However, he meets all independence criteria, except for his tenure on the Board of Directors.</p> <p>The Company does not see any risks in this.</p>
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.	This principle is complied with.	–
<b>2.9</b>	<b>The board of directors ensures performance assessment of the board of directors, its committees and members of the board of directors.</b>			
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.	<p>1. Self-assessment or external assessment of the board of directors' performance carried out in the reporting period included performance assessment of the committees, individual members of the board of directors and the board of directors in general.</p> <p>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.</p>	This principle is complied with.	–
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 organization (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.	This principle is complied with.	–

Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
<b>3.1</b>	<b>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.</b>			
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.	<p>1. The company has adopted and published an internal document – regulations on the corporate secretary.</p> <p>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.</p>	This principle is complied with.	–
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.	The board of directors approves the appointment, removal and additional remuneration of the corporate secretary.	This principle is complied with.	–
<b>4.1</b>	<b>Remuneration paid by the company is sufficient to attract, motivate and retain persons who have competencies and qualifications required by the company. Directors, executive body members and other key managers are remunerated as per the Company's remuneration policy.</b>			
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.	This principle is not fully complied with.	Relevant comments are provided in items 2.1.1. and 2.1.4 hereof.
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 recommendations to the board of directors as required.	This principle is complied with.	–

Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
<b>4.2</b>	<b>Directors' remuneration ensures that their financial interests are aligned with long-term financial interests of shareholders.</b>			
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>	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.	This principle is complied with.	–
4.2.2	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.	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.	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	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.	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.	This principle is complied with.	–
<b>4.3</b>	<b>Remuneration of executive body members and other key managers is linked to the Company's results and their personal contribution thereto.</b>			
4.3.1	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>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 an efficient ratio of the fixed and variable parts of remuneration.</p>	This principle is not fully complied with.	<p>The procedure for defining and payment of bonuses to members of the Management Board and other key executives existing in the Company does not allow illegal receipt of bonus payments by the persons named.</p> <p>The Company believes the executive bodies' members' civil liability norms set out in the applicable law to be sufficient.</p>

Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
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.	This principle is not fully complied with.	Relevant comments are provided in items 2.1.1. and 2.1.4 hereof.
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.  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.	This principle is complied with.	–
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 program 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 program 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 program 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.	This principle is not complied with.	Currently, the Company does not consider necessary implementing a long-term incentive program for members of executive bodies and other key executives of the company with the use of the Company shares (financial instruments based on the Company's shares).



Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
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.	This principle is complied with.	–
<b>5.1</b>	<b>The company put in place an effective risk management and internal control system to guarantee, in a reasonable manner, fulfillment of the Company's goals.</b>			
5.1.1	The board of directors of the Company has defined the Company's risk management and internal control principles and approaches.	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.	This principle is complied with.	–
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.	This principle is complied with.	–
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.	This principle is complied with.	–
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.	This principle is complied with.	–
<b>5.2</b>	<b>The company arranges for an internal audit, to assess reliability and performance of the risk management and internal control system on a regular and independent basis.</b>			

Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
5.2.1	<p>The company set up a separate business unit or engaged an independent external organization to carry out internal audits.</p> <p>Functional and administrative reporting lines of the internal audit department are delineated. The internal audit unit functionally reports to the board of directors.</p>	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.	This principle is complied with.	–
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.	<p>1. In the reporting period, the performance of the internal controls and risk management was assessed as part of the internal audit procedure.</p> <p>2. The company applies generally accepted approaches to internal audit and risk management.</p>	This principle is complied with.	–
<b>6.1</b>	<b>The company and its operations are transparent for its shareholders, investors and other stakeholders.</b>			
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.	<p>1. The Company's board of directors approved an information policy developed in accordance with the Code's recommendations.</p> <p>2. The board of directors (or its committee) reviewed the Company's compliance with its information policy at least once in the reporting period.</p>	This principle is complied with.	–
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.	<p>1. The company discloses information on its corporate governance and general principles of corporate governance, including disclosure on its website.</p> <p>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).</p> <p>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.</p>	This principle is complied with.	–
<b>6.2</b>	<b>The company discloses up-to-date, complete and reliable information on its operations in due time, to enable its shareholders and investors to make informed decisions.</b>			

Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
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>	This principle is complied with.	–
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>	This principle is not fully complied with.	The Company discloses its capital structure to the extent required by the applicable laws.
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>	This principle is complied with.	–

Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
<b>6.3</b>	<b>The company provides information and documents requested by its shareholders in accordance with principles of fairness and ease of access.</b>			
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.	This principle is not fully complied with.	The Company's Information Policy determines an easy procedure for providing shareholders with access to information, with the exception of information on legal entities controlled by the Company, the provision of which is not prescribed for by law.
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.	This principle is complied with.	–
<b>7.1</b>	<b>Actions which will or may materially 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.</b>			
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.	This principle is not fully complied with.	The Company's Articles of Association do not contain a separate section with a list of significant corporate actions. At the same time, decision-making on issues related to significant corporate actions falls within the authority of the Board of Directors.  The Company does not see any risks in this.

Item No.	Corporate Governance Principles	Compliance criteria	Compliance status	Reasons for non-compliance
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.	This principle is not fully complied with.	Relevant comments are provided in items 2.4.4. and 2.5.1 hereof.
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 the 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>	This principle is complied with.	–
<b>7.2</b>	<b>The company provides a procedure for taking material corporate actions that would enable its shareholders to receive full information about such actions in due time and influence them, and also guarantee that the shareholder rights are observed and duly protected when such actions are taken.</b>			
7.2.1	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.	This principle is complied with.	–
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>	This principle is not complied with.	The need to involve an appraiser for the valuation of the purchase price of the Company's shares is provided by the current legislation. There is no need to duplicate this requirement in the internal documents of the Company.



## 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.

## 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.

## 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
mmtpa	million metric tons per annum
mtpa	thousand metric tons per annum
ton	metric ton
SEC	United States Securities and Exchange Commission
PRMS	Petroleum Resources Management System
NSR	Northern Sea Route
YNAO	Yamal-Nenets Autonomous Region
RR	Russian rouble
LPG	liquified petroleum gases
LNG	liquified natural gas

**PAO NOVATEK**

**IFRS Consolidated  
Financial Statements  
for the Year Ended  
31 December 2018**

**and Independent  
Auditor's Report**

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## *Independent Auditor's Report*

To the Shareholders and Board of Directors of PAO NOVATEK:

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### *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 2018, 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 2018;
- 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 then ended; and
- the notes to the consolidated financial statements, which include significant accounting policies and other explanatory information.

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### *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.

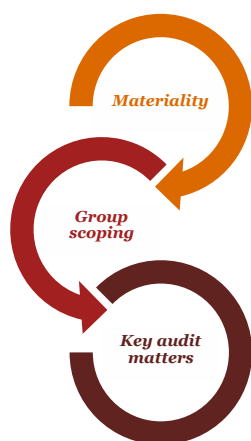
We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### **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



Overall group materiality: 11,000 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.

- 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 absolute value of income and expenses, forming the Group’s underlying profit before tax.
- Acquisition of AO Geotransgas and OOO Urengoyskaya gasovaya kompaniya.

As part of designing our audit, we determined materiality and assessed 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. As in all of our audits, 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 consolidated financial statements as a whole.



<b>Overall Group materiality</b>	RUB 11,000 million
<b>How we determined it</b>	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.
<b>Rationale for the materiality benchmark applied</b>	<p>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 and provides a more stable basis for determining materiality, focusing on the underlying profitability of the Group.</p> <p>We chose 4% which is consistent with quantitative materiality thresholds used for profit-oriented companies in this industry and prior year approach.</p>

## 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
<p><b>Acquisition of AO Geotransgas and OOO Urengoyanskaya gasovaya kompaniya</b></p> <p>In February 2018, upon the results of an auction held by AK ALROSA (PAO), the Group acquired 100 percent participation interests in Maretiom Investments Limited and Velarion Investments Limited for total cash consideration of RR 30.3 billion. These companies owned 100 percent participation interests in AO Geotransgas (renamed to AO NOVATEK-Pur in November 2018) and OOO Urengoyanskaya gasovaya kompaniya (reorganized by merging with OOO NOVATEK-Yurkharovneftegaz in January 2019), which held the licenses for exploration and production of hydrocarbons within the Beregovoy and Ust-Yamsoveyskiy license areas located in Yamalo-Nenetskiy state, respectively.</p>	<p>Our audit procedures included, among others, reconciliation of the purchase price consideration to the share purchase agreement and the amount of actual cash paid as per bank orders.</p> <p>We have evaluated the management's assessment that the acquisition should be accounted for as a business combination in accordance with IFRS 3.</p> <p>We have performed audit procedures to assess the appropriateness of the identification of assets and liabilities assumed at acquisition date.</p> <p>We assessed final purchase price allocation, including an assessment of the fair values of acquired assets and liabilities and the assumptions and methodology used by the Group's management for the fair value measurement of the assets and liabilities acquired.</p>

Key audit matter	How our audit addressed the key audit matter
<p>Management assessed that the acquisition qualifies as a business combination and applied IFRS 3 “Business Combinations”. In accordance with IFRS 3, the Group assessed fair values of the identified assets and liabilities of the acquired companies at the acquisition date.</p> <p>This was a significant focus area for our audit due to the significance of management’s judgements and estimates involved in accounting for this acquisition. The key judgement related to assessment of identifiable assets and liabilities fair values and the allocation of the purchase price to the assets and liabilities acquired.</p>	<p>We have not identified any significant issues in determination of the fair values.</p> <p>We evaluated the completeness of the disclosures made in Note 5 of the financial statements to comply with the requirements of IFRS 3 “Business Combinations”.</p> <p>No significant exceptions were noted in the accounting and consolidated financial statement disclosures for this acquisition.</p>

### How we tailored our Group audit scope

We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the consolidated financial statements as a whole, taking into account the 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 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.



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### *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 2018 and 2017” (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 2019” as well as “Annual Report Review of PAO NOVATEK for 2018”, 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.

When we read “Annual Report Review of PAO NOVATEK for 2018” and “Quarterly Issuer’s Report of PAO NOVATEK for the first quarter of 2019”, if we conclude that there is a material misstatement therein, we are required to communicate the matter to those charged with governance.

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### *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.



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### *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 responsible for the audit resulting in this independent auditor's report is Maxim E. Timchenko.

*AO PricewaterhouseCoopers Audit*

19 February 2019

Moscow, Russian Federation



M.E. Timchenko, certified auditor (licence no. 01-000267), AO PricewaterhouseCoopers Audit

Audited entity: PAO NOVATEK

Record made 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: 2, Udaltsova street, Moscow, 119415, Russian Federation.

Independent auditor: AO PricewaterhouseCoopers Audit

Registered by the Government Agency Moscow Registration Chamber on 28 February 1992 under No. 008.890

Record made in the Unified State Register of Legal Entities on 22 August 2002 under State Registration Number 1027700148431

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

Principal Registration Number of the Record in the Register of Auditors and Audit Organizations – 11603050547



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

	Notes	At 31 December 2018	At 31 December 2017
<b>ASSETS</b>			
<b>Non-current assets</b>			
Property, plant and equipment	6	408,201	360,051
Investments in joint ventures	7	244,500	285,326
Long-term loans and receivables	8	232,922	211,901
Other non-current assets	9	37,427	33,448
<b>Total non-current assets</b>		<b>923,050</b>	<b>890,726</b>
<b>Current assets</b>			
Inventories	10	17,251	11,084
Current income tax prepayments		1,311	43
Trade and other receivables	11	54,433	44,503
Prepayments and other current assets	12	89,645	31,863
Short-term bank deposits			
with original maturity more than three months		27,788	-
Cash and cash equivalents	13	41,472	65,943
Assets held for sale	5	61,420	-
<b>Total current assets</b>		<b>293,320</b>	<b>153,436</b>
<b>Total assets</b>		<b>1,216,370</b>	<b>1,044,162</b>
<b>LIABILITIES AND EQUITY</b>			
<b>Non-current liabilities</b>			
Long-term debt	14	170,043	141,448
Long-term lease liabilities	27	7,473	5,776
Deferred income tax liabilities	26	29,927	26,167
Asset retirement obligations		8,730	7,303
Other non-current liabilities		6,579	3,851
<b>Total non-current liabilities</b>		<b>222,752</b>	<b>184,545</b>
<b>Current liabilities</b>			
Short-term debt and current portion of long-term debt	15	2,120	14,302
Current portion of long-term lease liabilities	27	2,325	1,520
Trade payables and accrued liabilities	17	79,241	49,001
Current income tax payable		1,633	2,846
Other taxes payable		16,823	16,289
Liabilities associated with assets held for sale	5	4,881	-
<b>Total current liabilities</b>		<b>107,023</b>	<b>83,958</b>
<b>Total liabilities</b>		<b>329,775</b>	<b>268,503</b>
<b>Equity attributable to PAO NOVATEK shareholders</b>			
Ordinary share capital		393	393
Treasury shares		(10,445)	(8,353)
Additional paid-in capital		31,297	31,297
Currency translation differences		(1,702)	(3,283)
Asset revaluation surplus on acquisitions		5,617	5,617
Retained earnings		843,094	732,168
<b>Total equity attributable to PAO NOVATEK shareholders</b>	18	<b>868,254</b>	<b>757,839</b>
<b>Non-controlling interest</b>		<b>18,341</b>	<b>17,820</b>
<b>Total equity</b>		<b>886,595</b>	<b>775,659</b>
<b>Total liabilities and equity</b>		<b>1,216,370</b>	<b>1,044,162</b>

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

  
L. Mikhelson  
Chairman of the Management Committee

  
M. Gyetvay  
Chief Financial Officer

19 February 2019



**PAO NOVATEK**
**Consolidated Statement of Income**

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

	Notes	Year ended 31 December:	
		2018	2017
<b>Revenues</b>			
Oil and gas sales	19	825,761	579,819
Other revenues		5,997	3,367
<b>Total revenues</b>		<b>831,758</b>	<b>583,186</b>
<b>Operating expenses</b>			
Purchases of natural gas and liquid hydrocarbons	20	(319,990)	(161,443)
Transportation expenses	21	(145,664)	(137,192)
Taxes other than income tax	22	(58,768)	(49,494)
Depreciation, depletion and amortization	6	(33,094)	(34,523)
Materials, services and other	23	(22,675)	(20,768)
General and administrative expenses	24	(22,282)	(17,170)
Exploration expenses	6	(7,012)	(1,819)
Impairment (expenses) reversals, net		(287)	(52)
Change in natural gas, liquid hydrocarbons and work-in-progress		5,860	2,602
<b>Total operating expenses</b>		<b>(603,912)</b>	<b>(419,859)</b>
Net gain on disposal of interests in joint ventures	5	1,645	-
Other operating income (loss), net		(2,307)	424
<b>Profit from operations</b>		<b>227,184</b>	<b>163,751</b>
<b>Finance income (expense)</b>			
Interest expense	25	(4,746)	(7,712)
Interest income	25	14,003	15,872
Change in fair value of non-commodity financial instruments	27	3,492	(7,178)
Foreign exchange gain (loss), net	25	25,859	13,676
<b>Total finance income (expense)</b>		<b>38,608</b>	<b>14,658</b>
Share of profit (loss) of joint ventures, net of income tax	7	(37,258)	22,430
<b>Profit before income tax</b>		<b>228,534</b>	<b>200,839</b>
<b>Income tax expense</b>			
Current income tax expense		(44,543)	(35,227)
Deferred income tax benefit (expense), net		(1,044)	858
<b>Total income tax expense</b>	26	<b>(45,587)</b>	<b>(34,369)</b>
<b>Profit</b>		<b>182,947</b>	<b>166,470</b>
Profit attributable to:			
Non-controlling interest		19,205	10,083
Shareholders of PAO NOVATEK		163,742	156,387
Basic and diluted earnings per share (in Russian roubles)		54.33	51.85
Weighted average number of shares outstanding (in millions)		3,013.8	3,016.2

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:	
		2018	2017
<b>Profit</b>		<b>182,947</b>	<b>166,470</b>
<b>Other comprehensive income (loss)</b>			
<b>Items that will not be reclassified subsequently to profit (loss)</b>			
Remeasurement of pension obligations	16	(725)	(724)
Share of remeasurement of pension obligations of joint ventures		(112)	(100)
		<b>(837)</b>	<b>(824)</b>
<b>Items that may be reclassified subsequently to profit (loss)</b>			
Currency translation differences		1,934	(2,580)
Share of currency translation differences of joint ventures		(353)	21
		<b>1,581</b>	<b>(2,559)</b>
<b>Other comprehensive income (loss)</b>		<b>744</b>	<b>(3,383)</b>
<b>Total comprehensive income</b>		<b>183,691</b>	<b>163,087</b>
Total comprehensive income attributable to:			
Non-controlling interest		19,205	10,083
Shareholders of PAO NOVATEK		164,486	153,004

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:	
		2018	2017
<b>Profit before income tax</b>		<b>228,534</b>	<b>200,839</b>
<b>Adjustments to profit before income tax:</b>			
Depreciation, depletion and amortization		33,094	34,523
Impairment expenses (reversals), net		287	52
Foreign exchange loss (gain), net		(25,859)	(13,676)
Loss (gain) on disposal of assets, net	5	(1,645)	305
Interest expense		4,746	7,712
Interest income		(14,003)	(15,872)
Share of loss (profit) of joint ventures, net of income tax	7	37,258	(22,430)
Change in fair value of non-commodity financial instruments		(3,492)	7,178
Revaluation of commodity derivatives through profit or loss		450	9
Other adjustments		749	240
Decrease (increase) in long-term advances given		4,939	655
<b>Working capital changes</b>			
Decrease (increase) in trade and other receivables, prepayments and other current assets		(13,598)	(786)
Decrease (increase) in inventories		(9,137)	(2,607)
Increase (decrease) in trade payables and accrued liabilities, excluding interest and dividends payable		10,750	6,592
Increase (decrease) in taxes payable, other than income tax		592	1,962
<b>Total effect of working capital changes</b>		<b>(11,393)</b>	<b>5,161</b>
Dividends received from joint ventures		8,500	2,383
Interest received		1,311	5,949
Income taxes paid		(47,127)	(32,629)
<b>Net cash provided by operating activities</b>		<b>216,349</b>	<b>180,399</b>
<b>Cash flows from investing activities</b>			
Purchases of property, plant and equipment	6	(73,564)	(24,783)
Payments for mineral licenses	6	(327)	(9,786)
Purchases of materials for construction		(15,442)	(1,697)
Purchases of intangible assets		(872)	(780)
Proceeds from disposals of property, plant and equipment and materials for construction		2,133	-
Acquisition of joint ventures	5	(2)	(1,583)
Additional capital contributions to joint ventures	7	-	(2,269)
Payments for acquisition of subsidiaries, net of cash acquired	5	(30,492)	(15,706)
Interest paid and capitalized	6	(5,032)	(3,391)
Net decrease (increase) in bank deposits with original maturity more than three months		(26,161)	-
Guarantee fees paid		(1,431)	(1,315)
Loans provided to joint ventures	8	(3,429)	(5,211)
Repayments of loans provided to joint ventures	8	1,573	8,246
<b>Net cash used for investing activities</b>		<b>(153,046)</b>	<b>(58,275)</b>

**PAO NOVATEK**  
**Consolidated Statement of Cash Flows**  
(in millions of Russian roubles)

		<b>Year ended 31 December:</b>	
	<b>Notes</b>	<b>2018</b>	<b>2017</b>
<b>Cash flows from financing activities</b>			
Proceeds from long-term debt		7,928	-
Repayments of long-term debt		(22,035)	(53,035)
Repayments of short-term debt			
with original maturity more than three months		-	(136)
Proceeds from (repayments of) short-term debt			
with original maturity three months or less, net		(150)	(56)
Interest on debt paid		(3,024)	(6,526)
Dividends paid to shareholders of PAO NOVATEK	18	(51,980)	(42,075)
Dividends paid to non-controlling interest		(20,068)	-
Payments of lease liabilities		(2,192)	(567)
Purchases of treasury shares	18	(2,137)	(1,442)
<b>Net cash used for financing activities</b>		<b>(93,658)</b>	<b>(103,837)</b>
Net effect of exchange rate changes on cash and cash equivalents		5,884	(645)
<b>Net increase (decrease) in cash and cash equivalents</b>		<b>(24,471)</b>	<b>17,642</b>
Cash and cash equivalents at the beginning of the period		65,943	48,301
<b>Cash and cash equivalents at the end of the period</b>		<b>41,472</b>	<b>65,943</b>

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>Number of ordinary shares (in millions)</i>	<b>Ordinary share capital</b>	<b>Treasury shares</b>	<b>Additional paid-in capital</b>	<b>Currency translation differences</b>	<b>Asset revaluation surplus on acquisitions</b>	<b>Retained earnings</b>	<b>Equity attributable to PAO NOVATEK shareholders</b>	<b>Non- controlling interest</b>	<b>Total equity</b>
<b>At 1 January 2017</b>	<b>3,017.7</b>	<b>393</b>	<b>(6,913)</b>	<b>31,297</b>	<b>(724)</b>	<b>5,617</b>	<b>618,680</b>	<b>648,350</b>	<b>9,370</b>	<b>657,720</b>
Profit	-	-	-	-	-	-	156,387	156,387	10,083	166,470
Other comprehensive loss	-	-	-	-	(2,559)	-	(824)	(3,383)	-	(3,383)
<b>Total comprehensive income (loss)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>(2,559)</b>	<b>-</b>	<b>155,563</b>	<b>153,004</b>	<b>10,083</b>	<b>163,087</b>
Dividends (Note 18)	-	-	-	-	-	-	(42,075)	(42,075)	(1,633)	(43,708)
Purchase of treasury shares (Note 18)	(2.1)	-	(1,440)	-	-	-	-	(1,440)	-	(1,440)
<b>At 31 December 2017</b>	<b>3,015.6</b>	<b>393</b>	<b>(8,353)</b>	<b>31,297</b>	<b>(3,283)</b>	<b>5,617</b>	<b>732,168</b>	<b>757,839</b>	<b>17,820</b>	<b>775,659</b>
Profit	-	-	-	-	-	-	163,742	163,742	19,205	182,947
Other comprehensive income (loss)	-	-	-	-	1,581	-	(837)	744	-	744
<b>Total comprehensive income (loss)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>1,581</b>	<b>-</b>	<b>162,905</b>	<b>164,486</b>	<b>19,205</b>	<b>183,691</b>
Dividends (Note 18)	-	-	-	-	-	-	(51,979)	(51,979)	(18,684)	(70,663)
Purchase of treasury shares (Note 18)	(2.7)	-	(2,092)	-	-	-	-	(2,092)	-	(2,092)
<b>At 31 December 2018</b>	<b>3,012.9</b>	<b>393</b>	<b>(10,445)</b>	<b>31,297</b>	<b>(1,702)</b>	<b>5,617</b>	<b>843,094</b>	<b>868,254</b>	<b>18,341</b>	<b>886,595</b>

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 (hereinafter referred to as “YNAO”) of the Russian Federation. The Group delivers its natural gas and its 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 on the domestic market 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.

In the fourth quarter of 2017, the Group’s joint venture OAO Yamal LNG started production at the first train of its natural gas liquefaction plant (hereinafter referred to as the “LNG Plant”) based on the hydrocarbon resources of the South-Tambeyskoye field, located in the YNAO. In the third quarter of 2018, the second LNG train was launched, six months ahead of its original schedule, and in the fourth quarter of 2018, the third LNG train was launched, more than a year ahead of its original schedule. Annual capacity of the LNG Plant after launching the four LNG trains will aggregate 17.4 million tons of liquefied natural gas (5.5 million tons for each of the first three LNG trains and 0.9 million tons for the fourth LNG train) and up to 1.2 million tons of stable gas condensate. The Group purchases a portion of the liquefied natural gas (“LNG”) produced by Yamal LNG and sells it on the international markets. The Group’s LNG sales volumes are not subject to significant seasonal fluctuations.

The Group also purchases and sells natural gas on the European market under long- and short-term supply contracts to carry out its foreign commercial trading activities, as well as conducts LNG regasification in Poland.

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.

In October 2018, the Group and the company Fluxys Germany Holding GmbH arranged a joint venture, Rostock LNG GmbH, with 49 percent and 51 percent participation interests, respectively, to undertake a project to construct and operate a mid-scale LNG transshipment terminal with throughput capacity of approximately 300 thousand tons per annum located in the port of Rostock in Germany.

In May 2018, NOVATEK and TOTAL S.A. agreed in principle on the acquisition by TOTAL of a 10 percent participation interest in the Arctic LNG 2 project. The transaction is expected to close no later than 31 March 2019.

In February 2018, upon the results of an auction held by AK ALROSA (PAO), the Group acquired 100 percent participation interests in Maretim Investments Limited and Velarion Investments Limited for RR 30.3 billion. These companies were the owners of 100 percent participation interests in AO Geotransgas (renamed to AO NOVATEK-Pur in November 2018) and OOO Urengoyaskaya gasovaya kompaniya (merged into OOO NOVATEK-Yurkharovneftegas in January 2019), which held the licenses for exploration and production of hydrocarbons within the Beregovoy and Ust-Yamsoveyskiy license areas located in YNAO, respectively.

In January 2018, the Group acquired a 100 percent participation interest in OOO Chernichnoye for RR 616 million. OOO Chernichnoye is a holder of the license for exploration and production of hydrocarbons within the Chernichny license area located in YNAO.



**1 ORGANIZATION AND PRINCIPAL ACTIVITIES (CONTINUED)**

In January 2018, the Group, TOTAL S.A. and Eni S.p.A., through their subsidiaries NOVATEK Lebanon SAL, Total E&P Liban SAL and Eni Lebanon B.V. (hereinafter referred to as the “Right holders”), entered into Exploration and Production Agreements for Petroleum Activities with the Republic of Lebanon for the exploration and production of hydrocarbons on two offshore blocks located in the Eastern Mediterranean (hereinafter referred to as the “Exploration and Production Agreements”). The Exploration and Production Agreements stipulate that the Group is assigned a 20 percent participating interest and the Right holders are committed to undertake specified joint upstream activities during the exploration phase within five years. The Group considers that the Exploration and Production Agreements constitute a joint arrangement classified as a joint operation in accordance with IFRS 11, *Joint Arrangements*.

**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 financial instruments categorised at fair value through profit or loss or other comprehensive income. 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.

**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 Company and the majority of the Group’s subsidiaries.

Transactions denominated in foreign currencies are converted into the functional currency of each entity at the exchange rates prevailing on the date of transactions. Monetary assets and liabilities denominated in foreign currencies are converted into the functional currency of each entity by applying the year end exchange rate. Non-monetary assets and liabilities denominated in foreign currencies valued at cost are converted into the functional currency of each entity at the historical exchange rate. Non-monetary assets that are remeasured to fair value, recoverable amount or realizable value, are converted at the exchange rate applicable to the date of remeasurement. Exchange gains and losses resulting from foreign currency remeasurement into the functional currency are included in profit (loss) for the reporting period.

On consolidation 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 exchange rates at the dates of the transactions or the average exchange rate for the period when this is a reasonable approximation. Exchange adjustments arising on the opening net assets and the profits for the reporting period are taken to other comprehensive income 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 assets and/or liabilities in the reporting period were as follows:

Russian roubles to one currency unit	At 31 December 2018	At 31 December 2017	Average rate for the year ended 31 December:	
			2018	2017
US dollar (USD)	69.47	57.60	62.71	58.35
Euro (EUR)	79.46	68.87	73.95	65.90
Polish zloty (PLN)	18.48	16.51	17.36	15.48

## 2 BASIS OF PREPARATION (CONTINUED)

**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.

## 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Adoption of new and amended standards and interpretations.** In 2018, the Group adopted all IFRS, amendments and interpretations which are effective 1 January 2018 and relevant to its operations. None of them had material impact on the Group's consolidated financial statements. In particular, the following new standard was adopted by the Group starting from the annual period beginning on 1 January 2018:

**IFRS 9, Financial instruments.** The standard introduces new requirements for classification and measurement of financial instruments, impairment, and hedge accounting.

In accordance with the transition provisions in IFRS 9, the Group applied the new rules retrospectively, except for the items that have already been derecognized at the date of initial application, which is 1 January 2018. The Group also used an exemption in IFRS 9 allowing not to restate prior periods presented as a result of adoption of the new classification and measurement requirements, but rather recognize any differences in the opening retained earnings as at 1 January 2018. The initial application of the standard did not result in any reclassifications of the Group's financial instruments or any material changes in their measurement, therefore, the opening retained earnings were not restated.

**Principles of consolidation.** These consolidated financial statements present the assets, liabilities, equity, income, expenses and cash flows of PAO "NOVATEK" and its subsidiaries as those of a single economic entity. 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.

Intercompany transactions, balances and unrealized gains on transactions between group companies are eliminated. Accounting policies of the Group's subsidiaries have been changed where necessary to ensure consistency with the Group's policies.

**Joint arrangements.** The Group undertakes a number of business activities through joint arrangements, which exist when two or more parties have joint control. Joint arrangements are classified as either joint operations or joint ventures, based on the contractual rights and obligations between the parties to the arrangement.

Interests in joint ventures are accounted for using the equity method. With regard to joint operations, the Group records its share of assets, liabilities, revenues and expenses of its joint operations in the consolidated financial statements on a line-by-line basis.

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.

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**3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

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.

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

**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.

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.

**Disposals of joint ventures.** 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.

**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 within 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.

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. 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 depreciated on a straight-line basis are as follows:

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

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.

**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.

**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 obligation is recognized when incurred at the present value of the estimated costs of dismantling the assets, including abandonment and site restoration costs, and are included within the carrying value of property, plant and equipment.

Changes in the asset retirement obligation relating 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. Changes in the obligation resulting from the passage of time are recognized in the consolidated statement of income as interest expense.

**Leases.** A contract is (or contains) a lease if it conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

### 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Right-of-use assets are initially measured at cost and depreciated by the earlier of the end of the useful life of the right-of-use asset or the end of the lease term. The cost of right-of-use assets comprises of initial measurement of the lease liability, any lease payments made before or at the commencement date and initial direct costs. After the commencement date, the right-of-use assets are carried at cost less accumulated depreciation and impairment losses in accordance with IAS 16, *Property, plant and equipment*.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date and subsequently measured at amortized cost with the interest expense recognized within finance income (expense) in the consolidated statement of income.

In accordance with IFRS 16, *Leases*, the Group elected not to apply accounting requirements under this standard to short-term leases.

**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 the sale within a year from the date of classification is highly probable. They are measured at the lower of their carrying amount and fair value less costs to sell.

Property, plant and equipment are not depreciated once classified as held for sale.

The Group ceases to use the equity method of accounting in relation to an 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 natural gas and liquid hydrocarbons includes direct cost of materials, direct operating costs, and related production overhead expenses and is recorded on weighted average cost 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.

**Financial instruments.** Prior to 1 January 2018, the Group applied IAS 32, *Financial instruments: Presentation*, and IAS 39, *Financial instruments: recognition and measurement*, for accounting for its financial instruments. According to IAS 39, the Group's financial instruments were classified into the following measurement categories:

- Loans and receivables recognized initially at fair value plus directly attributable transaction costs and subsequently measured at amortised cost using the effective interest method. This category included the Group's loans provided and receivables with fixed or determinable payments that were not quoted in an active market.
- Financial liabilities recognized initially at fair value less directly attributable transaction costs and subsequently measured at amortised cost using the effective interest method. This category included the Group's debt, trade payables and other non-derivative liabilities.
- Financial instruments measured at fair value through profit or loss. This category included the Group's derivatives relating to certain shareholders' loans provided by the Group its joint ventures and certain commodity contracts (see Note 27).

Starting from 1 January 2018, the Group adopted IFRS 9, *Financial instruments*, according to which the financial assets are classified in the following measurement categories: those to be measured subsequently at amortised cost, those to be measured at fair value through profit or loss, and those to be measured at fair value through other comprehensive income. The classification depends on the Group's business model for managing the financial assets and the contractual terms of the cash flows. If a hybrid contract contains a host that is a financial asset, the classification requirements apply to the entire hybrid contract.

**3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

Under IFRS 9, financial assets are classified as at amortised cost only if both of the following criteria are met: the asset is held within a business model with the objective of collecting the contractual cash flows, and the contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal outstanding.

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 classified these loans as financial assets at fair value through profit or loss (see Note 27).

The difference between the loan proceeds and the fair at initial recognition 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 the remaining effect from fair value remeasurement of such loans are disclosed separately in the consolidated statement of income.

Other shareholders' loans provided by the Group, trade and other financial receivables, and cash and cash equivalents, are classified as at amortised cost. The Group does not have financial assets classified as at fair value through other comprehensive income.

In accordance with IFRS 9, the Group's non-derivative financial liabilities are measured at amortised cost. Derivatives are classified as at fair value through profit or loss. The Group does not apply hedge accounting.

Where there is an active market for a commodity, commodity contracts are accounted for as derivatives except for contracts that were entered into and continue to be held for the purpose of the receipt or delivery of a commodity in accordance with the Group's expected purchase, sale or usage requirements. 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 (see Note 27).

Overall, the Group's financial assets and liabilities that were measured at amortised cost or at fair value through profit and loss under IAS 39 continue to be measured at amortised cost or at fair value through profit and loss, respectively, in accordance with IFRS 9.

IFRS 9 replaced the "incurred loss" impairment model used in IAS 39, *Financial instruments: recognition and measurement*, with a new "expected credit loss" ("ECL") model that requires a more timely recognition of expected credit losses. An allowance for expected credit losses shall be recorded for financial assets classified as at amortised cost.

Under IFRS 9, loss allowances are measured on either of the following bases: 12-month ECLs that result from possible default events within the 12 months after the reporting date; and lifetime ECLs that result from all possible default events over the expected life of a financial instrument. For trade receivables, the Group measures loss allowances applying a simplified approach at an amount equal to lifetime ECLs. To measure the expected credit losses, expected loss rates are applied to trade receivables grouped based on the days past due. For other financial assets classified as at amortised cost, including some shareholders' loans provided, loss allowances are measured as 12-month ECLs unless there has been a significant increase in credit risk since origination, in which case the allowance is based on the lifetime ECLs.

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.

Financial assets and liabilities are offset and the net amount reported in the consolidated 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.



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**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.

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 those 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.

**Pension obligations.** The Group performs mandatory contributions to the Pension Fund of the Russian Federation on behalf of its employees based on gross salary payments. These contributions represent 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 defined benefit obligations are calculated annually by independent actuaries using the projected unit credit method.

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 or curtailed.

**Non-financial guarantees.** The Group issued a number of shareholder 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 a 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 allows 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 prepares a consolidated tax return for the taxpayers' group including the Company and majority of its subsidiaries in Russia.

Deferred tax assets and liabilities are recognized on temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax base. 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. The Group applies a net-basis accounting in respect of temporary differences arising from right-of-use assets and long-term lease liabilities. 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.

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**3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

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.

**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 control over such products has transferred to a customer, which refers to ability to direct the use of, and obtain substantially all of the remaining benefits from the products. The Group considers indicators of the transfer of control, which include, but are not limited to the following: the Group has a present right to payment for the products; the Group has transferred physical possession of the products; the customer has legal title to the products; the customer has the significant risks and rewards of ownership of the products; the customer has accepted the products. Not all of the indicators have to be met for management to conclude that control has transferred and revenue could be recognized. Management uses judgment to determine whether factors collectively indicate that the customer has obtained control over the products. Revenues from services are recognized in the period in which the services are rendered.

When the consideration includes a variable amount, minimum amounts must be recognized that are not at significant risk of reversal. If sales contract includes the variability associated with market price it represents a separated embedded derivative that is treated as part of revenue. Accordingly, at the date of sale the sales price is determined on a provisional basis, and the fair value of the final sales price adjustment is re-estimated continuously with changes in fair value recognized as an adjustment to revenue.

Trade receivables are recognized when the goods are transferred as this is the point in time that the consideration is unconditional and only the passage of time is required before the payment is due. No significant element of financing is deemed present as the sales are made with short-term credit terms consistent with market practice.

**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.

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### 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

**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.

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.

### 4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

Consolidated financial statements prepared in accordance with IFRS require management to make estimates which management reviews on a continuous basis, by reference to past experience and other factors considered as reasonable. 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.

Judgments and estimates that have the most significant effect on the amounts reported in these consolidated financial statements are described below.

**Fair value of financial instruments.** 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.

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.

In some cases, judgment is required to determine whether contracts to buy or sell commodities meet the definition of a derivative. Contracts to buy or sell LNG are not considered to meet the definition of a derivative, as they are not considered capable of being net settled. Therefore, such contracts are not within the scope of IFRS 9, *Financial Instruments*, and are accounted for on an accruals basis.

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.

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.

**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. 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 hydrocarbon reserves prepared by the Group's management in accordance with internationally recognized definitions.

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**4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS (CONTINUED)**

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. The Group also uses estimated probable and possible reserves 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.

A portion of the reserves estimated by the Group includes 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.

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.

**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.

**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.** 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 and 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.

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 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.

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

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

**5 ACQUISITIONS AND DISPOSALS*****Assets held for sale***

In May 2018, NOVATEK and TOTAL S.A. agreed in principle on the acquisition by TOTAL of a 10 percent participation interest in the Arctic LNG 2 project. The transaction is expected to close no later than 31 March 2019. In July 2018, the NOVATEK's Board of Directors approved the sale of a 10 percent participation interest in OOO Arctic LNG 2 to TOTAL.

It is expected that with a new participant added, key financial and operational decisions regarding the Arctic LNG 2 project will be subject to unanimous approval by both participants and none of the participants will have a preferential voting right. Management believes that upon closing this transaction, the Group will exercise joint control over OOO Arctic LNG 2.

At 31 December 2018, in accordance with IFRS 5, *Non-current assets held for sale and discontinued operations*, the conditions for recognition of an asset held for sale have been met. Therefore, assets and liabilities related to Arctic LNG 2 project, excluding intercompany balances, have been classified as assets and liabilities held for sale. No impairment of assets was identified as a result of the decision to sell an interest in this entity.

Below is a breakdown of major classes of assets and liabilities for assets classified as held for sale:

	<b>At 31 December 2018</b>
Property, plant and equipment	53,955
Other non-current assets	3,829
Prepayments and other current assets	3,636
<b>Total assets classified as held for sale</b>	<b>61,420</b>
Non-current liabilities	3,539
Current liabilities	1,342
<b>Total liabilities associated with assets held for sale</b>	<b>4,881</b>

***Acquisition of AO Geotransgas and OOO Urengoyskaya gasovaya kompaniya***

In February 2018, upon the results of an auction held by AK ALROSA (PAO), the Group acquired 100 percent participation interests in Maretom Investments Limited and Velarion Investments Limited for total cash consideration of RR 30.3 billion. These companies owned 100 percent participation interests in AO Geotransgas (renamed to AO NOVATEK-Pur in November 2018) and OOO Urengoyskaya gasovaya kompaniya (merged into OOO NOVATEK-Yurkharovneftegas in January 2019), which held the licenses for exploration and production of hydrocarbons within the Beregovoy and Ust-Yamsoveyskiy license areas located in YNAO, respectively.

In accordance with IFRS 3, *Business Combinations*, the Group assessed fair values of the identified assets and liabilities of the acquired companies at the acquisition date.

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

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

**5 ACQUISITIONS AND DISPOSALS (CONTINUED)**

The following table represents the net fair values comprising 100 percent of the assets and liabilities of the acquired companies:

	Fair values at the acquisition date
Property, plant and equipment	36,274
Other non-current assets	220
Other current assets	195
Cash and cash equivalents	424
Deferred income tax liabilities	(4,531)
Long-term debt	(1,007)
Other non-current liabilities	(417)
Trade payables and accrued liabilities	(858)
<b>Total identifiable net assets</b>	<b>30,300</b>
Purchase consideration	(30,300)
<b>Goodwill</b>	<b>-</b>

For the period from the date of acquisition to 31 December 2018, the acquired companies contributed RR 4.2 billion to the Group's revenues. The financial and operational activities of the acquired companies would have increased the Group's revenues for 2018 by an additional RR 0.8 billion, if the acquisition had occurred in January 2018.

***Acquisition of OOO Chernichnoye***

In January 2018, the Group acquired a 100 percent participation interest in OOO Chernichnoye for RR 616 million. OOO Chernichnoye is a holder of the license for exploration and production of hydrocarbons within the Chernichniy license area located in YNAO. OOO Chernichnoye had no notable operating activities at and before the acquisition date and, accordingly, this acquisition is outside the definition of business as defined in IFRS 3, *Business Combinations*. The cost of the acquisition has been allocated to property, plant and equipment, primarily to the license cost.

***Disposal of an ownership interest in AO Arcticgas***

At 31 December 2017, the Group held an effective 53.3 percent participation interest in AO Arcticgas through two of the Group's other joint ventures, OOO SeverEnergia and OOO Yamal Development. SeverEnergia was owned by the Group (a 6.7 percent participation interest) and Yamal Development (a 93.3 percent participation interest). Yamal Development was a joint venture of the Group and PAO Gazprom Neft with a 50 percent participation interest held by each investor. Arcticgas was a wholly owned subsidiary of SeverEnergia.

In the first quarter of 2018, the Group and Gazprom Neft completed the final stage of the previously commenced restructuring procedures to achieve parity shareholdings in Arcticgas. In January 2018, Yamal Development and SeverEnergia were merged with Arcticgas. As a result, the Group and Gazprom Neft obtained direct participation interests in Arcticgas of 53.3 percent and 46.7 percent, respectively. Subsequently, in March 2018, Gazprom Neft subscribed to Arcticgas's additional share emission for a total cash consideration of RR 32,098 million. As a result of the aforementioned transactions, the Group's participation interest in Arcticgas decreased from 53.3 to 50 percent and the Group recognised a gain on the disposal of the 3.3 percent ownership interest in Arcticgas in the amount of RR 1,645 million.

The Group continues to exercise joint control over Arcticgas 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)*****Acquisition of AO Eurotek and AO South-Khadyryakhinskoye***

In December 2017, the Group acquired for total cash consideration of RR 5,412 million 100 percent ownership interests in AO Eurotek and AO South-Khadyryakhinskoye (merged into OOO NOVATEK-Tarkosalenftegas in May 2018), which held licenses for exploration and production of hydrocarbons within the Syskonsyninskiy license area located in Khanty-Mansiysk Autonomous Region and the South-Khadyryakhinskiy license area located in YNAO, respectively.

In accordance with IFRS 3, *Business Combinations*, the Group assessed fair values of the identified assets and liabilities of acquired companies at the acquisition date:

	Fair values at the acquisition date
Property, plant and equipment	2,466
Deferred income tax assets	680
Cash and cash equivalents	2,701
Other current assets	101
Non-current liabilities	(375)
Trade payables and accrued liabilities	(161)
<b>Total identifiable net assets</b>	<b>5,412</b>
Purchase consideration	(5,412)
<b>Goodwill</b>	<b>-</b>

The financial and operational activities of the acquired companies would not have had a material impact on the Group's revenues for 2017, if the acquisition had occurred in January 2017. The financial results of these companies after the acquisition date did not have a material impact on the Group's revenues and results for the year ended 31 December 2017.

***Acquisition of OOO Severneft-Urengoy***

In November 2017, the Group acquired for a cash consideration of RR 13,062 million a 100 percent ownership interest in OOO Severneft-Urengoy (merged into OOO NOVATEK-Yurkharovneftegas in January 2019), which held a license for exploration and production of hydrocarbons within the West-Yaroyakhinsky license area, located in YNAO.

In accordance with IFRS 3, *Business Combinations*, the Group assessed fair values of the identified assets and liabilities of OOO Severneft-Urengoy at the acquisition date:

	Fair values at the acquisition date
Property, plant and equipment	14,252
Other non-current assets	140
Cash and cash equivalents	67
Other current assets	208
Deferred income tax liabilities	(858)
Other non-current liabilities	(145)
Current liabilities	(602)
<b>Total identifiable net assets</b>	<b>13,062</b>
Purchase consideration	(13,062)
<b>Goodwill</b>	<b>-</b>

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

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

**5 ACQUISITIONS AND DISPOSALS (CONTINUED)**

The financial and operational activities of Severneft-Urengoy would have increased the Group's revenues for 2017 by an additional RR 6.3 billion, if the acquisition had occurred in January 2017. The financial results of this company after the acquisition date did not have a material impact on the Group's revenues and results for the year ended 31 December 2017.

***Acquisition of a participation interest in OOO Cryogas-Vysotsk***

In July 2017, NOVATEK acquired a 51 percent ownership interest in OOO Cryogas-Vysotsk for a cash consideration of RR 1,583 million. Cryogas-Vysotsk undertakes a project to construct the first train of a medium-scale plant to liquefy natural gas with annual capacity of 660 thousand tons, located at the port of Vysotsk on the Baltic Sea.

The Charter of Cryogas-Vysotsk stipulates that key financial and operating decisions regarding its business activities are subject to unanimous approval by the Board of Directors. Consequently, the voting mechanism effectively establishes joint control over Cryogas-Vysotsk and the Group accounts for the investment under the equity method.

In accordance with IFRS 11, *Joint Arrangements*, the Group assessed fair values of the identified assets and liabilities of Cryogas-Vysotsk at the acquisition date:

	Fair values at the acquisition date
Property, plant and equipment	15,804
Deferred income tax assets	111
Prepayments and other current assets	1,393
Cash and cash equivalents	447
Short-term debt	(13,199)
Other current liabilities	(1,453)
<b>Total identifiable net assets</b>	<b>3,103</b>
Purchase consideration	1,583
Fair value of the Group's interest in net assets (RR 3,103 million at 51 percent ownership)	(1,583)
<b>Goodwill</b>	<b>-</b>

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

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

**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	412,368	34,776	15,642	462,786
Accumulated depreciation, depletion and amortization	(127,635)	-	(3,100)	(130,735)
<b>Net book value at 1 January 2017</b>	<b>284,733</b>	<b>34,776</b>	<b>12,542</b>	<b>332,051</b>
Additions	1,797	46,238	29	48,064
Transfers	42,740	(43,640)	900	-
Acquisition of subsidiaries (see Note 5)	14,873	1,756	89	16,718
Changes in asset retirement costs	(1,486)	-	-	(1,486)
Depreciation, depletion and amortization	(33,943)	-	(668)	(34,611)
Disposals, net	(371)	(207)	(27)	(605)
Currency translation differences	(99)	3	16	(80)
Cost	479,569	38,926	16,709	535,204
Accumulated depreciation, depletion and amortization	(171,325)	-	(3,828)	(175,153)
<b>Net book value at 31 December 2017</b>	<b>308,244</b>	<b>38,926</b>	<b>12,881</b>	<b>360,051</b>
Additions	3,671	94,813	-	98,484
Transfers	21,451	(23,104)	1,653	-
Acquisition of subsidiaries (see Note 5)	31,878	4,827	215	36,920
Changes in asset retirement costs	1,375	-	-	1,375
Depreciation, depletion and amortization	(32,307)	-	(886)	(33,193)
Reclassification to assets held for sale (see Note 5)	(18,469)	(35,431)	(55)	(53,955)
Disposals, net	(697)	(2,109)	(504)	(3,310)
Currency translation differences	1,764	31	34	1,829
Cost	525,089	77,953	17,949	620,991
Accumulated depreciation, depletion and amortization	(208,179)	-	(4,611)	(212,790)
<b>Net book value at 31 December 2018</b>	<b>316,910</b>	<b>77,953</b>	<b>13,338</b>	<b>408,201</b>

Included in additions to property, plant and equipment for the years ended 31 December 2018 and 2017 are capitalized interest and foreign exchange differences of RR 7,395 million and RR 3,827 million, respectively.

Included in additions to property, plant and equipment for the years ended 31 December 2018 and 2017 are RR 22,896 million and RR 8,593 million, respectively, related to the Arctic LNG 2 project, which assets were classified as assets held for sale at 31 December 2018.

Included within assets under construction and advances for construction are advances to suppliers for construction and equipment of RR 15,526 million and RR 6,554 million at 31 December 2018 and 2017, respectively.

In November 2018, the Group won an auction for an oil and gas exploration and production license for the South-Leskinskiy license area located on the Gydan peninsula in the YNAO for the total amount of RR 2,041 million, of which RR 35 million were paid at the reporting date as the auction's participation fee and included within assets under construction and advances for construction. The remaining amount of RR 2,006 million was paid after the state registration of the license in January 2019.

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**6 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)**

In March 2018, the Group won an auction for an oil and gas exploration and production license for the Payutskiy license area located in Krasnoyarsk Territory for a payment of RR 66 million, which was included within oil and gas properties and equipment.

In 2017, the Group purchased through auctions oil and gas exploration and production licenses for the Shtormovoy, the Gydanskiy, the Upper-Tiuteyskiy and the West-Seyakhinskiy license areas located in the YNAO for the total amount of RR 9,727 million, which were included in additions to oil and gas properties and equipment.

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 2018	At 31 December 2017
Proved properties acquisition costs	71,087	58,951
Less accumulated depletion of proved properties acquisition costs	(19,197)	(18,001)
Unproved properties acquisition costs	11,947	11,376
<b>Total acquisition costs</b>	<b>63,837</b>	<b>52,326</b>

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

Reconciliation of depreciation, depletion and amortization (DDA):

	Year ended 31 December:	
	2018	2017
Depreciation, depletion and amortization of property, plant and equipment	33,193	34,611
Add: DDA of intangible assets	622	639
Less: DDA capitalized in the course of intra-group construction services	(721)	(727)
<b>DDA as presented in the consolidated statement of income</b>	<b>33,094</b>	<b>34,523</b>

At 31 December 2018 and 2017, 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 2018 and 2017.

Capital commitments are disclosed in Note 28.

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

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

**6 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)**

**Leases.** Included in property, plant and equipment at 31 December 2018 and 2017 are the right-of-use assets primarily related to long-term agreements on time chartering of marine tankers. Movements in the carrying amounts of the right-of-use assets are as follows:

	Oil and gas properties and equipment	Other	Total
<b>Net book value at 1 January 2017</b>	<b>16</b>	<b>240</b>	<b>256</b>
Additions	7,123	500	7,623
Depreciation, depletion and amortization	(375)	(129)	(504)
Other movements	(130)	-	(130)
<b>Net book value at 31 December 2017</b>	<b>6,634</b>	<b>611</b>	<b>7,245</b>
Additions	2,308	172	2,480
Depreciation, depletion and amortization	(1,677)	(219)	(1,896)
Reclassification to assets held for sale	-	(15)	(15)
Other movements	1,731	25	1,756
<b>Net book value at 31 December 2018</b>	<b>8,996</b>	<b>574</b>	<b>9,570</b>

The maturity analysis of lease liabilities is disclosed in Note 27.

**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:	
	2018	2017
<b>Net book value of assets at 1 January</b>	<b>17,805</b>	<b>15,472</b>
Additions	5,417	6,345
Acquisition of subsidiaries	14	834
Reclassification to proved properties and development expenditures	(3,685)	(4,846)
Reclassification to assets held for sale	(240)	-
<b>Net book value of assets at 31 December</b>	<b>19,311</b>	<b>17,805</b>
Liabilities	1,938	689
Cash flows used for operating activities	7,012	1,819
Cash flows used for investing activities	4,463	5,749

For the years ended 31 December 2018 and 2017, the Group has recognized exploration expenses within operating expenses in the amount of RR 7,012 million and RR 1,819 million, respectively. These expenses included employee compensations in the amount of RR 207 million and RR 301 million, respectively.

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**7 INVESTMENTS IN JOINT VENTURES**

	At 31 December 2018	At 31 December 2017
<b>Joint ventures:</b>		
AO Arcticgas (combined investments in OOO SeverEnergiya and OOO Yamal Development at 31 December 2017)	146,631	101,539
OOO Yamal LNG	48,378	126,377
ZAO Nortgas	44,064	50,519
OOO Cryogas-Vysotsk	2,991	3,841
ZAO Terneftegas	2,434	3,050
Rostock LNG GmbH	2	-
<b>Total investments in joint ventures</b>	<b>244,500</b>	<b>285,326</b>

The Group considers that Arcticgas, Yamal LNG, Nortgas, Cryogas-Vysotsk, Terneftegas and Rostock LNG GmbH 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 participants or by a group of participants. The Group accounts for its shares in joint ventures under the equity method.

**AO Arcticgas.** Arcticgas operates the Samburgskoye, Urengoykoye and Yaro-Yakhinskoye fields, located in the YNAO.

At 31 December 2017, the Group held an effective 53.3 percent participation interest in Arcticgas through SeverEnergiya and Yamal Development, the Group's joint ventures with PAO Gazprom Neft. In the first quarter of the 2018, the Group and Gazprom Neft completed the final stage of the previously commenced restructuring procedures to achieve parity shareholdings in Arcticgas. As a result, Yamal Development and SeverEnergiya were merged with Arcticgas, and the Group's participation ownership in Arcticgas was reduced to 50 percent (see Note 5).

**OOO 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). The joint venture is responsible for implementing an integrated project on natural gas production, liquefaction and shipping. The project envisages the production of liquefied natural gas at the plant with an annual capacity of 17.4 million tons, including 5.5 million tons for each of the first three LNG trains and 0.9 million tons for the fourth LNG train, based on the feedstock resources of the South-Tambeyskoye field located on the Yamal peninsula in YNAO. Yamal LNG is the holder of the LNG export license.

At 31 December 2018 and 2017, the Group's 50.1 percent ownership in Yamal LNG was pledged in connection with credit line facility agreements signed by Yamal LNG with a number of Russian and foreign banks to obtain external project financing.

In accordance with the equity method of accounting, investment in Yamal LNG at 31 December 2018 was reduced for the Group's share of loss of the joint venture for the year ended 31 December 2018 in the amount of RR 78,978 million, of which RR 108,285 million were attributable to the Group's share of net foreign exchange loss of the joint venture.

**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.

In accordance with the equity method of accounting, investment in Nortgas at 31 December 2018 was reduced for the Group's share in dividends declared by the joint venture during 2018 in the amount of RR 8,500 million.

**OOO Cryogas-Vysotsk.** The Group holds a 51 percent ownership interest in Cryogas-Vysotsk acquired in July 2017 (see Note 5). Cryogas-Vysotsk is a joint venture with AO Gazprombank group. Cryogas-Vysotsk is undertaking a project to construct the first train of a medium-scale LNG plant with annual capacity of 660 thousand tons, located at the port of Vysotsk on the Baltic Sea.



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**7 INVESTMENTS IN JOINT VENTURES (CONTINUED)**

At 31 December 2018 and 2017, the Group's 51 percent ownership interest in Cryogas-Vysotsk was pledged in connection with credit line facility agreements signed by the joint venture with a Russian bank to obtain external project financing.

**ZAO Terneftegas.** The Group holds a 51 percent ownership in Terneftegas, its joint venture with TOTAL S.A.. Terneftegas operates the Termokarstovoye field, located in the YNAO.

**Rostock LNG GmbH.** The Group holds a 49 percent ownership interest in Rostock LNG GmbH since October 2018. Rostock LNG GmbH is a joint venture with the company Fluxys Germany Holding GmbH. The joint venture is undertaking a project to construct and operate a mid-scale LNG transshipment terminal with capacity of approximately 300 thousand tons per annum located in the port of Rostock in Germany.

The table below summarizes the movements in the carrying amounts of the Group's joint ventures:

	Year ended 31 December:	
	2018	2017
<b>At 1 January</b>	<b>285,326</b>	<b>259,650</b>
Share of profit from operations	124,211	39,854
Share of finance income (expense)	(160,836)	(10,297)
Share of total income tax benefit (expense)	(633)	(7,127)
<b>Share of profit (loss) of joint ventures, net of income tax</b>	<b>(37,258)</b>	<b>22,430</b>
Share of other comprehensive income (loss) of joint ventures	(465)	(79)
Group's costs capitalized in investments	1,378	1,328
Gain on disposal of interests in joint ventures (see Note 5)	1,645	-
Acquisitions of joint ventures (see Note 5)	2	1,583
Contributions to equity	-	2,269
Dividends received from joint ventures	(8,500)	(2,383)
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	2,372	528
<b>At 31 December</b>	<b>244,500</b>	<b>285,326</b>

For the years ended 31 December 2018 and 2017, the Group recorded commission fees in the amount of RR 1,378 million and RR 1,328 million, respectively, 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.

In October 2017, the capital of Cryogas-Vysotsk was increased through proportional contributions by its participants totalling RR 4,449 million, of which RR 2,269 million was contributed by NOVATEK.

In 2018 and 2017, Nortgas declared dividends in the total amount of RR 17,001 million and RR 4,766 million, respectively, of which RR 8,500 million and RR 2,383 million, respectively, were attributable to NOVATEK.

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.

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**Notes to the Consolidated Financial Statements**

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**7 INVESTMENTS IN JOINT VENTURES (CONTINUED)**

The summarized statements of financial position for the Group's principal joint ventures are as follows:

<i>At 31 December 2018</i>	<i>Arcticgas<sup>(*)</sup></i>	<i>Yamal LNG</i>	<i>Nortgas</i>
Property, plant and equipment and materials for construction	400,606	2,155,305	130,956
Other non-current non-financial assets	13	828	36
Non-current financial assets	70	-	9
<b>Total non-current assets</b>	<b>400,689</b>	<b>2,156,133</b>	<b>131,001</b>
Cash and cash equivalents	27,139	8,407	1,151
Other current financial assets	27,595	37,685	2,053
Current non-financial assets	2,117	32,213	444
<b>Total current assets</b>	<b>56,851</b>	<b>78,305</b>	<b>3,648</b>
Non-current financial liabilities	(65,160)	(1,832,224)	(15,435)
Non-current non-financial liabilities	(46,800)	(24,312)	(23,504)
<b>Total non-current liabilities</b>	<b>(111,960)</b>	<b>(1,856,536)</b>	<b>(38,939)</b>
Trade payables and accrued liabilities	(12,868)	(36,558)	(468)
Other current financial liabilities	(28,615)	(244,567)	(5,587)
Current non-financial liabilities	(10,834)	(163)	(1,527)
<b>Total current liabilities</b>	<b>(52,317)</b>	<b>(281,288)</b>	<b>(7,582)</b>
<b>Net assets</b>	<b>293,263</b>	<b>96,614</b>	<b>88,128</b>
<i>At 31 December 2017</i>			
Property, plant and equipment and materials for construction	388,589	1,741,465	135,180
Other non-current non-financial assets	276	391	44
Non-current financial assets	68	-	12,226
<b>Total non-current assets</b>	<b>388,933</b>	<b>1,741,856</b>	<b>147,450</b>
Cash and cash equivalents	8,660	29,297	1,409
Other current financial assets	17,484	19,793	2,550
Current non-financial assets	948	16,994	321
<b>Total current assets</b>	<b>27,092</b>	<b>66,084</b>	<b>4,280</b>
Non-current financial liabilities	(125,663)	(1,484,498)	(20,970)
Non-current non-financial liabilities	(42,218)	(38,705)	(23,149)
<b>Total non-current liabilities</b>	<b>(167,881)</b>	<b>(1,523,203)</b>	<b>(44,119)</b>
Trade payables and accrued liabilities	(24,919)	(26,946)	(693)
Other current financial liabilities	(29,647)	(5,294)	(3,881)
Current non-financial liabilities	(12,948)	(112)	(2,000)
<b>Total current liabilities</b>	<b>(67,514)</b>	<b>(32,352)</b>	<b>(6,574)</b>
<b>Net assets</b>	<b>180,630</b>	<b>252,385</b>	<b>101,037</b>

(\*) – at 31 December 2017, combined data for the Group's joint ventures Arcticgas, SeverEnergiya and Yamal Development after mutual balances elimination.

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**Notes to the Consolidated Financial Statements**

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**7 INVESTMENTS IN JOINT VENTURES (CONTINUED)**

The summarized statements of comprehensive income (loss) of the Group's principal joint ventures are presented below:

<i>For the year ended 31 December 2018</i>	<i>Arcticgas<sup>(*)</sup></i>	<i>Yamal LNG</i>	<i>Nortgas</i>
Revenues	195,066	181,835	23,339
Depreciation, depletion and amortization	(21,219)	(31,253)	(7,288)
Profit from operations	108,904	129,722	6,623
Change in fair value of non-commodity financial instruments	-	(24,624)	-
Foreign exchange gain (loss), net	(7)	(216,255)	-
Profit (loss) before income tax	102,971	(174,202)	5,162
Income tax benefit (expense)	(17,056)	16,477	(1,059)
<b>Profit (loss), net of income tax</b>	<b>85,915</b>	<b>(157,725)</b>	<b>4,103</b>
Other comprehensive loss	(95)	(798)	(11)
<b>Total comprehensive income (loss)</b>	<b>85,820</b>	<b>(158,523)</b>	<b>4,092</b>
<i>For the year ended 31 December 2017</i>			
Revenues	147,207	3,613	23,087
Depreciation, depletion and amortization	(22,903)	(895)	(6,914)
Profit from operations	66,724	528	5,581
Change in fair value of non-commodity financial instruments	-	27,110	-
Foreign exchange gain (loss), net	1	(26,089)	-
Profit before income tax	47,557	1,505	4,400
Income tax expense	(7,348)	(4,589)	(950)
<b>Profit (loss), net of income tax</b>	<b>40,209</b>	<b>(3,084)</b>	<b>3,450</b>
Other comprehensive loss	(66)	(94)	(91)
<b>Total comprehensive income (loss)</b>	<b>40,143</b>	<b>(3,178)</b>	<b>3,359</b>

(\*) – for the year ended 31 December 2017, combined data for the Group's joint ventures Arcticgas, SeverEnergy and Yamal Development after mutual transactions elimination.

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.

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 2018</i>	<i>Arcticgas</i>	<i>Yamal LNG</i>	<i>Nortgas</i>
<b>Net assets at 1 January 2018</b>	<b>180,630</b>	<b>252,385</b>	<b>101,037</b>
Profit (loss), net of income tax	85,915	(157,725)	4,103
Other comprehensive loss	(95)	(798)	(11)
Restructuring (see Note 5)	26,813	-	-
Other equity movements	-	2,752	-
Dividends	-	-	(17,001)
<b>Net assets at 31 December 2018</b>	<b>293,263</b>	<b>96,614</b>	<b>88,128</b>
Ownership	50%	50.1%	50%
<b>Group's share in net assets</b>	<b>146,631</b>	<b>48,378</b>	<b>44,064</b>

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**7 INVESTMENTS IN JOINT VENTURES (CONTINUED)**

<i>As at and for the year ended 31 December 2017</i>	<b>Arcticgas</b>	<b>Yamal LNG</b>	<b>Nortgas</b>
<b>Net assets at 1 January 2017</b>	<b>140,487</b>	<b>252,870</b>	<b>102,444</b>
Profit (loss), net of income tax	40,209	(3,084)	3,450
Other comprehensive loss	(66)	(94)	(91)
Other equity movements	-	2,693	-
Dividends	-	-	(4,766)
<b>Net assets at 31 December 2017</b>	<b>180,630</b>	<b>252,385</b>	<b>101,037</b>
Ownership	53.3%, 50%	50.1%	50%
<b>Group's share in net assets</b>	<b>101,539</b>	<b>126,377</b>	<b>50,519</b>

**8 LONG-TERM LOANS AND RECEIVABLES**

The following table presents long-term loans (including interest accrued) and receivables:

	<b>At 31 December 2018</b>	<b>At 31 December 2017</b>
Long-term loans receivable	272,901	212,363
Other long-term receivables	407	429
<b>Total</b>	<b>273,308</b>	<b>212,792</b>
Less: current portion of long-term loans receivable	(40,386)	(891)
<b>Total long-term loans and receivables</b>	<b>232,922</b>	<b>211,901</b>

The Group's long-term loans receivable by borrowers are as follows:

	<b>At 31 December 2018</b>	<b>At 31 December 2017</b>
OAo Yamal LNG	265,606	204,596
OOO Cryogas-Vysotsk	6,012	5,313
ZAO Terneftegas	1,283	2,454
<b>Total long-term loans receivable</b>	<b>272,901</b>	<b>212,363</b>

**OAo Yamal LNG.** In accordance with the Shareholders' agreement, in prior years the Group provided US dollar and Euro credit line facilities to Yamal LNG, the Group's joint venture. In 2018, the shareholders opened additional credit line facilities denominated in Euros to finance construction of the fourth train of the LNG Plant. The loans interest rates are set based on market interest rates, interest rates on borrowings of shareholders and/or combination thereof. The repayment schedules are linked to free cash flows of the joint venture.

**OOO Cryogas-Vysotsk.** The Group provided Russian rouble denominated loans under agreed credit line facilities to Cryogas-Vysotsk, the Group's joint venture. The loans are repayable not later than 2033 and bear variable interest rates.

**ZAO Terneftegas.** In accordance with the Shareholders' agreement, the Group provided US dollar denominated loans to Terneftegas, the Group's joint venture. The loans interest rate is set based on market interest rates and interest rates on borrowings of shareholders. The repayment schedule is linked to free cash flows of the joint venture.

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**8 LONG-TERM LOANS AND RECEIVABLES (CONTINUED)**

For the years ended 31 December 2018 and 2017, Terneftegas repaid to the Group a part of the loans and accrued interest in the total amount of RR 1,673 million and RR 910 million, respectively.

No provisions for impairment of long-term loans and receivables were recognized at 31 December 2018 and 2017. The carrying values of long-term loans and receivables approximate their respective fair values.

**9 OTHER NON-CURRENT ASSETS**

	At 31 December 2018	At 31 December 2017
<i>Financial assets</i>		
Commodity derivatives	2,397	1,705
Other financial assets	7	10
<i>Non-financial assets</i>		
Long-term advances	15,289	20,228
Materials for construction	10,852	2,694
Deferred income tax assets	6,486	6,898
Intangible assets, net	2,119	1,665
Other non-financial assets	277	248
<b>Total other non-current assets</b>	<b>37,427</b>	<b>33,448</b>

At 31 December 2018 and 2017, 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 2018	At 31 December 2017
Natural gas and liquid hydrocarbons	14,465	8,711
Materials and supplies (net of provision of RR 4 million at 31 December 2018 and 2017)	2,760	2,337
Other inventories	26	36
<b>Total inventories</b>	<b>17,251</b>	<b>11,084</b>

No inventories were pledged as security for the Group's borrowings or payables at both dates.

**11 TRADE AND OTHER RECEIVABLES**

	At 31 December 2018	At 31 December 2017
Trade receivables (net of provision of RR 349 million and RR 284 million at 31 December 2018 and 2017, respectively)	52,882	43,387
Other receivables (net of provision of RR 323 million and RR 19 million at 31 December 2018 and 2017, respectively)	1,551	1,116
<b>Total trade and other receivables</b>	<b>54,433</b>	<b>44,503</b>

Trade receivables in the amount RR 12,413 million and RR 8,921 million at 31 December 2018 and 2017, respectively, 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).

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**11 TRADE AND OTHER RECEIVABLES (CONTINUED)**

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.

Movements in the Group's provision for impairment of trade receivables are as follows:

	Year ended 31 December:	
	2018	2017
<b>At 1 January</b>	<b>284</b>	<b>196</b>
Additional provision recorded	42	55
Acquisition of subsidiaries	107	55
Receivables written off as uncollectible	(26)	(15)
Provision reversed	(58)	(7)
<b>At 31 December</b>	<b>349</b>	<b>284</b>

The provision for impaired trade and other receivables has been included in the consolidated statement of income in net impairment expenses.

**12 PREPAYMENTS AND OTHER CURRENT ASSETS**

	At 31 December 2018	At 31 December 2017
<i><b>Financial assets</b></i>		
Current portion of long-term loans receivable (see Note 8)	40,386	891
Commodity derivatives	9,313	2,117
<i><b>Non-financial assets</b></i>		
Value-added tax receivable	12,646	8,057
Recoverable value-added tax	8,467	7,284
Prepayments and advances to suppliers	7,066	6,326
Deferred transportation expenses for natural gas	3,963	1,965
Deferred export duties for liquid hydrocarbons	3,210	1,829
Deferred transportation expenses for liquid hydrocarbons	3,100	2,140
Prepaid customs duties	604	561
Other non-financial assets	890	693
<b>Total prepayments and other current assets</b>	<b>89,645</b>	<b>31,863</b>

**13 CASH AND CASH EQUIVALENTS**

	At 31 December 2018	At 31 December 2017
Cash at current bank accounts	30,196	28,994
Bank deposits with original maturity of three months or less	11,276	36,949
<b>Total cash and cash equivalents</b>	<b>41,472</b>	<b>65,943</b>

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).



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

**14 LONG-TERM DEBT**

	<u>At 31 December 2018</u>	<u>At 31 December 2017</u>
<b><i>Corporate bonds</i></b>		
Eurobonds – Ten-Year Tenor (par value USD 1 billion, repayable in 2022)	69,359	57,481
Eurobonds – Ten-Year Tenor (par value USD 650 million, repayable in 2021)	45,094	37,364
<b><i>Bank loans</i></b>		
Syndicated term credit line facility	-	13,280
Other bank loans	8,953	6,887
<b><i>Other borrowings</i></b>		
Loan from Silk Road Fund	48,757	39,716
Other loans	-	1,022
<b>Total</b>	<b>172,163</b>	<b>155,750</b>
Less: current portion of long-term debt	(2,120)	(14,302)
<b>Total long-term debt</b>	<b>170,043</b>	<b>141,448</b>

***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 the amount of USD 650 million. The US dollar denominated Eurobonds were issued with an annual coupon rate of 6.604 percent, payable semi-annually. The Eurobonds have a ten-year tenor and are repayable in February 2021.

***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 was repayable until July 2018 by quarterly equal installments starting from June 2015. The facility included the maintenance of certain restrictive financial covenants. In February 2018, the credit line facility was fully repaid ahead of its maturity schedule.

***Other bank loans.*** In December 2016, the Group obtained EUR 100 million under a revolving credit line facility from the Russian subsidiary of a foreign bank. The loan is repayable in April 2020 and includes the maintenance of certain restrictive financial covenants.

In February 2018, the Group acquired a 100 percent participation interest in AO Geotransgas (see Note 5) and consolidated RUR 1,007 million credit line facility obtained by AO Geotransgas from a Russian bank repayable in December 2020.

***Loan from Silk Road Fund.*** In December 2015, the Group obtained a loan from China's investment fund Silk Road Fund which is repayable until December 2030 by semi-annual equal installments starting from December 2019 and includes the maintenance of certain restrictive financial covenants.

***Other loans.*** At 31 December 2017, other loans represented Russian rouble denominated loans, which were provided to one of the Group's subsidiaries by its non-controlling shareholder. The loans were initially repayable until the end of 2017, which was subsequently extended to the end of 2018. In July 2018, the loans were fully repaid.

The fair value of long-term debt including its current portion was RR 176,984 million and RR 167,760 million at 31 December 2018 and 2017, 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).

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**14 LONG-TERM DEBT (CONTINUED)**

Scheduled maturities of long-term debt at the reporting date were as follows:

<i>Maturity period:</i>	<b>At 31 December 2018</b>
1 January 2020 to 31 December 2020	13,193
1 January 2021 to 31 December 2021	49,334
1 January 2022 to 31 December 2022	73,599
1 January 2023 to 31 December 2023	4,240
After 31 December 2023	29,677
<b>Total long-term debt</b>	<b>170,043</b>

**Available credit line facilities.** In addition to disclosed above, at 31 December 2018, the Group had available long-term credit line facilities from banks with credit limits in the amounts of RR 50 billion, the equivalent of USD 750 million, and EUR 50 million. The facilities include the maintenance of certain restrictive financial covenants.

**15 SHORT-TERM DEBT AND CURRENT PORTION OF LONG-TERM DEBT**

At 31 December 2018 and 2017, short-term debt and current portion of long-term debt consisted only of current portion of long-term debt in the amount of RR 2,120 million and RR 14,302 million, respectively.

**Loans with original maturity three months or less.** During 2018 and 2017, the Group had available revolving credit line facilities under which the obtained loans with original maturities of three months or less to finance trade activities were secured by cash revenues from specifically determined liquid hydrocarbons export sales contracts. At 31 December 2018 and 2017, these loans were repaid.

**Available credit line facilities.** At 31 December 2018, the Group had available short-term revolving credit line facilities from Russian banks, with credit limits in the total amount of RR 70 billion. Subsequent to the balance sheet date, in February 2019, the Group extended one of its short-term revolving credit line facilities in the amount of RR 50 billion to 2022.

**16 PENSION OBLIGATIONS**

**Defined contribution plan.** For the years ended 31 December 2018 and 2017, 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 2,608 million and RR 2,111 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 a 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:	
	2018	2017
<b>At 1 January</b>	<b>3,198</b>	<b>2,249</b>
Interest cost	217	197
Current service cost	254	181
Past service cost	(80)	(35)
Benefits paid	(138)	(118)
Actuarial gains (losses) arising from:		
- changes in financial assumptions	180	345
- changes in demographic assumptions	(15)	122
- experience adjustments	560	257
Reclassification to liabilities associated with assets held for sale	(2)	-
<b>At 31 December</b>	<b>4,174</b>	<b>3,198</b>
<i>Defined benefit plan (benefits) costs were recognized in:</i>		
Materials, services and other (as employee compensation)	206	225
General and administrative expenses (as employee compensation)	185	153
Other operating income (loss)	-	(35)
Other comprehensive loss	725	724

The principal actuarial assumptions used are as follows:

	At 31 December 2018	At 31 December 2017
Weighted average discount rate	7.7%	6.9%
Projected annual increase in employee compensation	5.0%	4.0%
Expected increases to pension benefits	5.0%	4.3%

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.

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.

Mortality assumptions are based on the Russian mortality tables published by the Federal State Statistics Service from the year 2014 adjusted for estimates of mortality improvements in the future periods.

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 2018	At 31 December 2017
<b>Financial liabilities</b>		
Trade payables	52,314	30,936
Commodity derivatives	8,492	3,333
Interest payable	1,451	1,221
Dividends payable to non-controlling interest	-	1,633
Other payables	2,017	775
<b>Non-financial liabilities</b>		
Advances from customers	5,447	4,474
Salary payables	837	472
Other liabilities and accruals	8,683	6,157
<b>Total trade payables and accrued liabilities</b>	<b>79,241</b>	<b>49,001</b>

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.

During the years ended 31 December 2018 and 2017, advances from customers in the amount of RR 4,394 million and RR 2,422 million, respectively, remained at the beginning of the respective period were recognized as revenue.

**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 2018 and 2017. 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 2018 and 2017, the Group purchased 2.7 million and 2.1 million ordinary shares at a total cost of RR 2,092 million and RR 1,440 million, respectively. At 31 December 2018 and 2017, the Group held in total 23.4 million and 20.7 million ordinary shares at a total cost of RR 10,445 million and RR 8,353 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:	
	2018	2017
Dividends payable at 1 January	1	1
Dividends declared (*)	51,979	42,075
Dividends paid (*)	(51,980)	(42,075)
<b>Dividends payable at 31 December</b>	<b>-</b>	<b>1</b>
Dividends per share declared during the year (in Russian roubles)	17.25	13.95
Dividends per GDR declared during the year (in Russian roubles)	172.50	139.50

(\*) – excluding treasury shares.

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**18 SHAREHOLDERS' EQUITY (CONTINUED)**

The Group declares and pays dividends in Russian roubles. Dividends declared in 2018 and 2017 were as follows:

Final for 2017: RR 8.00 per share or RR 80.00 per GDR declared in April 2018	24,291
Interim for 2018: RR 9.25 per share or RR 92.50 per GDR declared in September 2018	28,086

<b>Total dividends declared in 2018</b>	<b>52,377</b>
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Final for 2016: RR 7.00 per share or RR 70.00 per GDR declared in April 2017	21,254
Interim for 2017: RR 6.95 per share or RR 69.50 per GDR declared in September 2017	21,102

<b>Total dividends declared in 2017</b>	<b>42,356</b>
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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 2018 and 2017, NOVATEK's closing balances of the accumulated profit including the respective year's net statutory profit totaled RR 551,913 million and RR 445,104 million, respectively.

**19 OIL AND GAS SALES**

	Year ended 31 December:	
	2018	2017
Natural gas	375,198	247,663
Naphtha	149,770	111,979
Crude oil	106,257	77,102
Other gas and gas condensate refined products	89,686	69,066
Liquefied petroleum gas	56,243	40,016
Stable gas condensate	48,607	33,993
<b>Total oil and gas sales</b>	<b>825,761</b>	<b>579,819</b>

**20 PURCHASES OF NATURAL GAS AND LIQUID HYDROCARBONS**

	Year ended 31 December:	
	2018	2017
Unstable gas condensate	155,360	107,082
Natural gas	150,811	51,053
Other liquid hydrocarbons	13,819	3,308
<b>Total purchases of natural gas and liquid hydrocarbons</b>	<b>319,990</b>	<b>161,443</b>

The Group purchases not less than 50 percent of the natural gas volumes produced by its joint venture ZAO Nortgas, some volumes of natural gas produced by its joint venture AO Arcticgas, all volumes of natural gas produced by its joint venture ZAO Terneftegas and, commencing December 2017, some volumes of liquefied natural gas produced by its joint venture OAO Yamal LNG (see Note 30).

The Group purchases all volumes of unstable gas condensate produced by its joint ventures Nortgas, Arcticgas and Terneftegas at ex-field prices based on benchmark reference crude oil prices, as well as some volumes of stable gas condensate produced by its joint venture OAO Yamal LNG (see Note 30).

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**21 TRANSPORTATION EXPENSES**

	Year ended 31 December:	
	2018	2017
Natural gas transportation by trunk and low-pressure pipelines	96,146	93,686
Stable gas condensate and liquefied petroleum gas transportation by rail	30,643	29,832
Stable gas condensate and refined products, crude oil and liquefied natural gas transportation by tankers	10,145	5,980
Crude oil transportation by trunk pipelines	8,557	7,622
Other	173	72
<b>Total transportation expenses</b>	<b>145,664</b>	<b>137,192</b>

**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:	
	2018	2017
Unified natural resources production tax	54,644	45,459
Property tax	3,595	3,673
Other taxes	529	362
<b>Total taxes other than income tax</b>	<b>58,768</b>	<b>49,494</b>

**23 MATERIALS, SERVICES AND OTHER**

	Year ended 31 December:	
	2018	2017
Employee compensation	9,815	9,032
Repair and maintenance	2,948	2,853
Complex of services for preparation, transportation and processing of hydrocarbons	2,009	1,914
Materials and supplies	1,963	1,966
Electricity and fuel	1,311	1,221
Liquefied petroleum gas volumes reservation expenses	1,155	918
Fire safety and security expenses	976	749
Transportation services	822	727
Rent expenses	416	308
Insurance expenses	340	307
Other	920	773
<b>Total materials, services and other</b>	<b>22,675</b>	<b>20,768</b>

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**24 GENERAL AND ADMINISTRATIVE EXPENSES**

	Year ended 31 December:	
	2018	2017
Employee compensation	15,807	11,065
Social expenses and compensatory payments	2,484	2,735
Legal, audit, and consulting services	1,122	839
Business travel expense	621	560
Fire safety and security expenses	471	419
Advertising expenses	465	410
Repair and maintenance expenses	229	231
Rent expenses	176	90
Other	907	821
<b>Total general and administrative expenses</b>	<b>22,282</b>	<b>17,170</b>

**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:	
	2018	2017
Audits of PAO NOVATEK (audit of the Group's consolidated financial statements and audit of statutory financial statements of PAO NOVATEK)	34	34
Other services	8	9
<b>Total auditor's fees and services</b>	<b>42</b>	<b>43</b>

**25 FINANCE INCOME (EXPENSE)**

	Year ended 31 December:	
	2018	2017
<i>Interest expense (including transaction costs)</i>		
Interest expense on fixed rate debt	8,615	8,234
Interest expense on variable rate debt	87	2,001
<b>Subtotal</b>	<b>8,702</b>	<b>10,235</b>
Less: capitalized interest	(5,032)	(3,391)
<b>Interest expense on debt</b>	<b>3,670</b>	<b>6,844</b>
Provisions for asset retirement obligations:		
effect of the present value discount unwinding	602	749
Interest expense on lease liabilities	474	119
<b>Total interest expense</b>	<b>4,746</b>	<b>7,712</b>



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**25 FINANCE INCOME (EXPENSE) (CONTINUED)**

<i>Interest income</i>	<b>Year ended 31 December:</b>	
	<b>2018</b>	<b>2017</b>
Interest income on loans receivable classified as at amortised cost	653	641
Interest income on loans receivable classified as at fair value through profit or loss	11,940	13,106
Interest income on cash, cash equivalents and deposits	1,410	2,125
<b>Total interest income</b>	<b>14,003</b>	<b>15,872</b>

<i>Foreign exchange gains (losses)</i>	<b>Year ended 31 December:</b>	
	<b>2018</b>	<b>2017</b>
Gains	70,704	48,322
Losses	(44,845)	(34,646)
<b>Total foreign exchange gain (loss), net</b>	<b>25,859</b>	<b>13,676</b>

**26 INCOME TAX**

**Reconciliation of income tax.** The table below reconciles actual income tax expense and theoretical income tax, determined based on the applicable rates for each of the Group's entities and their accounting profit before income tax.

	<b>Year ended 31 December:</b>	
	<b>2018</b>	<b>2017</b>
Profit before income tax	228,534	200,839
Theoretical income tax expense at applicable rates of the Group's entities	38,878	38,056
Increase (decrease) due to:		
Non-deductible differences in respect of the Group's share of loss (profit) of joint ventures	6,977	(4,592)
Non-deductible differences in respect of net gain on disposal of interests in joint ventures	(329)	-
Other differences	61	905
<b>Total income tax expense</b>	<b>45,587</b>	<b>34,369</b>

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**26 INCOME TAX (CONTINUED)**

Domestic and foreign components of current income tax expense were:

	Year ended 31 December:	
	2018	2017
Russian Federation income tax	42,968	34,811
Foreign income tax	1,575	416
<b>Total current income tax expense</b>	<b>44,543</b>	<b>35,227</b>

**Effective income tax rate.** The Russian statutory income tax rate for 2018 and 2017 was 20 percent. 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. Profits of the Group's foreign subsidiaries are taxed at rates applicable in accordance with legislation of the respective jurisdiction.

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 dividend income received from the joint ventures in which the Group holds at least a 50 percent interest is subject to a zero withholding tax rate according to the Russian tax legislation.

Without the effect of net profit (loss) and dividends from joint ventures the effective income tax rate for the years ended 31 December 2018 and 2017 was 17.3 percent and 19.3 percent, respectively.

In respect of PAO NOVATEK and the 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 2018	At 31 December 2017
Long-term deferred income tax asset (other non-current assets)	6,486	6,898
Long-term deferred income tax liability	(29,927)	(26,167)
<b>Net deferred income tax liability</b>	<b>(23,441)</b>	<b>(19,269)</b>

Deferred income tax assets expected to be realized within twelve months as of 31 December 2018 and 2017 were RR 3,768 million and RR 3,902 million, respectively. Deferred tax liabilities expected to be reversed within twelve months of 31 December 2018 and 2017 were RR 1,113 million and RR 936 million, respectively.

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**26 INCOME TAX (CONTINUED)**

Movements in deferred income tax assets and liabilities during the years ended 31 December 2018 and 2017 are as follows:

	At 31 December 2017	Statement of Income effect	Statement of Comprehensive Income effect	Acquisition of subsidiaries	Reclassification to assets and liabilities held for sale	At 31 December 2018
Property, plant and equipment	(31,983)	(2,550)	(2)	(5,210)	2,850	(36,895)
Intangible assets	(346)	(24)	-	-	-	(370)
Inventories	(297)	(32)	-	(3)	-	(332)
Other	(639)	(149)	22	-	(15)	(781)
<b>Deferred income tax liabilities</b>	<b>(33,265)</b>	<b>(2,755)</b>	<b>20</b>	<b>(5,213)</b>	<b>2,835</b>	<b>(38,378)</b>
<i>Less: deferred tax assets offset</i>	<i>7,098</i>	<i>669</i>	<i>-</i>	<i>684</i>	<i>-</i>	<i>8,451</i>
<b>Total deferred income tax liabilities</b>	<b>(26,167)</b>	<b>(2,086)</b>	<b>20</b>	<b>(4,529)</b>	<b>2,835</b>	<b>(29,927)</b>
Tax losses carried forward	3,607	2,253	-	23	(940)	4,943
Property, plant and equipment	3,102	754	-	27	(374)	3,509
Inventories	2,438	(648)	(2)	516	-	2,304
Asset retirement obligations	1,389	351	-	110	(142)	1,708
Trade payables and accrued liabilities	1,237	(2)	9	-	(10)	1,234
Loans receivable	1,996	(987)	-	-	-	1,009
Other	227	(10)	7	6	-	230
<b>Deferred income tax assets</b>	<b>13,996</b>	<b>1,711</b>	<b>14</b>	<b>682</b>	<b>(1,466)</b>	<b>14,937</b>
<i>Less: deferred tax liabilities offset</i>	<i>(7,098)</i>	<i>(669)</i>	<i>-</i>	<i>(684)</i>	<i>-</i>	<i>(8,451)</i>
<b>Total deferred income tax assets</b>	<b>6,898</b>	<b>1,042</b>	<b>14</b>	<b>(2)</b>	<b>(1,466)</b>	<b>6,486</b>
<b>Net deferred income tax liabilities</b>	<b>(19,269)</b>	<b>(1,044)</b>	<b>34</b>	<b>(4,531)</b>	<b>1,369</b>	<b>(23,441)</b>

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**26 INCOME TAX (CONTINUED)**

	At 31 December 2016	Statement of Income effect	Statement of Comprehensive Income effect	Acquisition of subsidiaries	At 31 December 2017
Property, plant and equipment	(28,747)	(1,614)	15	(1,637)	(31,983)
Intangible assets	(313)	62	2	(97)	(346)
Inventories	(250)	(23)	(17)	(7)	(297)
Other	(451)	(212)	24	-	(639)
<b>Deferred income tax liabilities</b>	<b>(29,761)</b>	<b>(1,787)</b>	<b>24</b>	<b>(1,741)</b>	<b>(33,265)</b>
<i>Less: deferred tax assets offset</i>	<i>5,105</i>	<i>1,110</i>	<i>-</i>	<i>883</i>	<i>7,098</i>
<b>Total deferred income tax liabilities</b>	<b>(24,656)</b>	<b>(677)</b>	<b>24</b>	<b>(858)</b>	<b>(26,167)</b>
Tax losses carried forward	2,542	504	12	549	3,607
Property, plant and equipment	1,068	1,085	-	949	3,102
Inventories	2,153	279	6	-	2,438
Loans receivable	1,346	650	-	-	1,996
Asset retirement obligations	1,464	(122)	(5)	52	1,389
Trade payables and accrued liabilities	913	318	6	-	1,237
Other	290	(69)	(7)	13	227
<b>Deferred income tax assets</b>	<b>9,776</b>	<b>2,645</b>	<b>12</b>	<b>1,563</b>	<b>13,996</b>
<i>Less: deferred tax liabilities offset</i>	<i>(5,105)</i>	<i>(1,110)</i>	<i>-</i>	<i>(883)</i>	<i>(7,098)</i>
<b>Total deferred income tax assets</b>	<b>4,671</b>	<b>1,535</b>	<b>12</b>	<b>680</b>	<b>6,898</b>
<b>Net deferred income tax liabilities</b>	<b>(19,985)</b>	<b>858</b>	<b>36</b>	<b>(178)</b>	<b>(19,269)</b>

At 31 December 2018, the Group had recognized deferred income tax assets of RR 4,943 million (31 December 2017: RR 3,607 million) in respect of unused tax loss carry forwards of RR 25,029 million (31 December 2017: RR 18,373 million). In accordance with tax legislation of Russian Federation effective 1 January 2017, taxable profits can be reduced in the amount of tax losses carried forward for relief during unlimited period of time, at the same time in 2017 to 2020 tax losses carried forward cannot exceed 50 percent of taxable profits. In determining future taxable profits and the amount of tax benefits that are probable in the future, the Group's 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 2018		At 31 December 2017	
	Non-current	Current	Non-current	Current
<i>At amortised cost</i>				
Long-term loans receivable	9,556	-	5,313	-
Trade and other receivables	407	54,433	429	44,503
Short-term bank deposits				
with original maturity more than three months	-	27,788	-	-
Cash and cash equivalents	-	41,472	-	65,943
Other	7	-	10	-
<i>At fair value through profit or loss</i>				
Long-term loans receivable	222,959	40,386	206,159	891
Commodity derivatives	2,397	9,313	1,705	2,117
<b>Total financial assets</b>	<b>235,326</b>	<b>173,392</b>	<b>213,616</b>	<b>113,454</b>
<i>Financial liabilities</i>				
<i>At amortised cost</i>				
Long-term debt	170,043	2,120	141,448	14,302
Long-term lease liabilities	7,473	2,325	5,776	1,520
Trade and other payables	-	55,782	-	32,932
Dividends payable to non-controlling interest	-	-	-	1,633
<i>At fair value through profit or loss</i>				
Commodity derivatives	2,403	8,492	649	3,333
<b>Total financial liabilities</b>	<b>179,919</b>	<b>68,719</b>	<b>147,873</b>	<b>53,720</b>

**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- 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 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 IFRS 9, *Financial instruments*, 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.

**27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)**

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 natural gas derivatives 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).

The amounts recognized by the Group in respect of the natural gas derivative contracts measured in accordance with IFRS 9, *Financial instruments*, are as follows:

<i>Commodity derivatives</i>	<b>At 31 December 2018</b>	<b>At 31 December 2017</b>
Within other non-current and current assets	11,710	3,822
Within other non-current and current liabilities	(10,895)	(3,982)

	<b>Year ended 31 December:</b>	
<i>Included in other operating income (loss)</i>	<b>2018</b>	<b>2017</b>
Operating income (loss) from natural gas foreign trading	(2,278)	289
Change in fair value	(450)	(9)

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:

	<b>Year ended 31 December:</b>	
<i>Effect on the fair value</i>	<b>2018</b>	<b>2017</b>
Increase by ten percent	(2,021)	(1,572)
Decrease by ten percent	2,021	1,572

**Recognition and remeasurement of the shareholders' loans to joint ventures.** Terms and conditions of certain 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.

**27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)**

The following table summarizes the movements in the carrying amounts of shareholders' loans provided to Yamal LNG and Terneftegas, which are accounted for at fair value through profit or loss:

	Year ended 31 December:	
	2018	2017
<b>At 1 January</b>	<b>207,051</b>	<b>198,454</b>
Repayment of the loans and accrued interest	(1,673)	(910)
Subsequent remeasurement at fair value recognized in profit (loss) as follows:		
– Interest income (using the effective interest rate method)	11,940	13,106
– Foreign exchange gain (loss), net	42,535	3,579
– Remaining effect from changes in fair value (attributable to free cash flows of the borrowers and interest rates)	3,492	(7,178)
<b>At 31 December</b>	<b>263,345</b>	<b>207,051</b>

Fair value measurement of shareholders' loans to joint ventures is determined using benchmark interest rates adjusted for the borrower credit risk and internal 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.

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</i>	Year ended 31 December:	
	2018	2017
Increase by one percent	(10,036)	(11,560)
Decrease by one percent	10,650	12,536

**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.



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

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**27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)***(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.

The carrying amounts of the Group's financial instruments are denominated in the following currencies:

<i>At 31 December 2018</i>	<b>Russian rouble</b>	<b>US dollar</b>	<b>Euro</b>	<b>Other</b>	<b>Total</b>
<i>Financial assets</i>					
<i>Non-current</i>					
Long-term loans receivable	6,012	107,713	118,790	-	232,515
Trade and other receivables	342	2	-	63	407
Commodity derivatives	-	-	2,397	-	2,397
Other	-	-	-	7	7
<i>Current</i>					
Trade and other receivables	21,379	13,577	18,393	1,084	54,433
Current portion of long-term loans receivable	-	20,694	19,692	-	40,386
Commodity derivatives	-	-	9,313	-	9,313
Short-term bank deposits with original maturity more than three months	-	27,788	-	-	27,788
Cash and cash equivalents	6,804	11,194	22,588	886	41,472
<i>Financial liabilities</i>					
<i>Non-current</i>					
Long-term debt	(1,007)	(161,090)	(7,946)	-	(170,043)
Long-term lease liabilities	(337)	(7,043)	(1)	(92)	(7,473)
Commodity derivatives	-	-	(2,403)	-	(2,403)
<i>Current</i>					
Short-term debt and current portion of long-term debt	-	(2,120)	-	-	(2,120)
Current portion of long-term lease liabilities	(20)	(2,222)	(2)	(81)	(2,325)
Trade and other payables	(35,341)	(4,489)	(15,709)	(243)	(55,782)
Commodity derivatives	-	-	(8,492)	-	(8,492)
<b>Net exposure</b>	<b>(2,168)</b>	<b>4,004</b>	<b>156,620</b>	<b>1,624</b>	<b>160,080</b>

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**27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)**

<i>At 31 December 2017</i>	<b>Russian rouble</b>	<b>US dollar</b>	<b>Euro</b>	<b>Other</b>	<b>Total</b>
<b>Financial assets</b>					
<i>Non-current</i>					
Long-term loans receivable	5,313	96,686	109,473	-	211,472
Trade and other receivables	425	4	-	-	429
Commodity derivatives	-	-	1,705	-	1,705
Other	-	-	-	10	10
<i>Current</i>					
Trade and other receivables	21,822	16,360	3,730	2,591	44,503
Current portion of long-term loans receivable	-	891	-	-	891
Commodity derivatives	-	-	2,117	-	2,117
Cash and cash equivalents	16,392	36,449	12,745	357	65,943
<b>Financial liabilities</b>					
<i>Non-current</i>					
Long-term debt	-	(134,561)	(6,887)	-	(141,448)
Long-term lease liabilities	(340)	(5,360)	(3)	(73)	(5,776)
Commodity derivatives	-	-	(649)	-	(649)
<i>Current</i>					
Short-term debt and current portion of long-term debt	(1,022)	(13,280)	-	-	(14,302)
Current portion of long-term lease liabilities	(116)	(1,349)	(2)	(53)	(1,520)
Trade and other payables	(25,651)	(3,563)	(3,505)	(213)	(32,932)
Dividends payable to non-controlling interest	(1,633)	-	-	-	(1,633)
Commodity derivatives	-	-	(3,333)	-	(3,333)
<b>Net exposure</b>	<b>15,190</b>	<b>(7,723)</b>	<b>115,391</b>	<b>2,619</b>	<b>125,477</b>

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 ten percent increase in exchange rates and no changes in the portfolio of instruments and other variables at 31 December 2018 and 2017, respectively:

<i>Effect on profit before income tax</i>	<b>Increase in exchange rate</b>	<b>Year ended 31 December:</b>	
		<b>2018</b>	<b>2017</b>
RUB / USD	10%	400	(772)
RUB / EUR	10%	15,662	11,539

The effect of a corresponding ten 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.

**27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)**

**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 wholesale natural gas prices on the domestic market (excluding residential customers) in the first half of 2017. From 1 July 2017, regulated wholesale natural gas prices were increased by 3.9 percent, and from 21 August 2018 by 3.4 percent.

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. The Group's natural gas purchase and sales contracts in the domestic market are not considered to meet the definition of a derivative and are not within the scope of *IFRS 9, Financial Instruments*. However, to effectively manage the margins achieved through its natural gas trading activities, management has established targets for volumes sold to wholesale traders and end-customers.

**LNG supplies on international markets.** The Group sells liquefied natural gas purchased primarily from its joint venture Yamal LNG on international markets under short- and long-term contracts at prices based on benchmark natural gas prices at the major natural gas hubs and benchmark crude oil prices. The Group's LNG purchase and sales contracts are not considered to meet the definition of a derivative and are not within the scope of *IFRS 9, Financial Instruments*.

**LNG regasification activity in Europe.** The Group purchases and sells regasified LNG in Europe primarily at prices linked to natural gas prices at major European natural gas hubs. Regasified LNG purchase and sales contracts are not considered to meet the definition of a derivative and are not within the scope of *IFRS 9, Financial Instruments*.

**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 short- and long-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 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 supplies.** 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 primarily based on benchmark 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 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 crude oil prices of Brent dated, or Dubai, plus a premium or a discount, and on a transaction-by-transaction basis or based on benchmark crude oil prices of Brent and Urals or a combination thereof 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 prices. The Group's liquid hydrocarbons purchase and sales contracts are entered to meet supply requirements to fulfil contract obligations or for own consumption and are not within the scope of *IFRS 9, Financial Instruments*.

**27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)***(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 2018		At 31 December 2017	
	RR million	Percent	RR million	Percent
At fixed rate	172,163	100%	141,448	91%
At variable rate	-	-	14,302	9%
<b>Total debt</b>	<b>172,163</b>	<b>100%</b>	<b>155,750</b>	<b>100%</b>

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:	
	2018	2017
Increase by 100 basis points	-	143

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 2018 and 2017, 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.

**27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)**

Most of the Group's international natural gas and 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.

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 &amp; Poor's</i>	<b>At 31 December 2018</b>	<b>At 31 December 2017</b>
Investment grade rating	30,285	14,676
Non-investment grade rating	2,438	12,661
No external rating	21,710	17,166
<b>Total trade and other receivables</b>	<b>54,433</b>	<b>44,503</b>

The table below highlights the Group's cash, cash equivalents and short-term bank deposits with original maturity more than three months to published credit ratings of its banks and/or their parent companies:

<i>Moody's, Fitch and/or Standard &amp; Poor's</i>	<b>At 31 December 2018</b>	<b>At 31 December 2017</b>
Investment grade rating	40,759	49,857
Non-investment grade rating	28,462	15,916
No external rating	39	170
<b>Total cash, cash equivalents and short-term bank deposits with original maturity more than three months</b>	<b>69,260</b>	<b>65,943</b>

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 2018</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>	2,416	13,786	129,124	33,831	179,157
<i>Interest</i>	8,775	8,494	13,371	5,739	36,379
Lease liabilities	2,408	2,396	6,294	-	11,098
Trade and other payables	55,782	-	-	-	55,782
<b>Total financial liabilities</b>	<b>69,381</b>	<b>24,676</b>	<b>148,789</b>	<b>39,570</b>	<b>282,416</b>
<i>At 31 December 2017</i>					
Debt at fixed rate					
<i>Principal</i>	-	8,890	107,061	32,055	148,006
<i>Interest</i>	7,272	7,272	16,655	6,163	37,362
Debt at variable rate					
<i>Principal</i>	14,314	-	-	-	14,314
<i>Interest</i>	168	-	-	-	168
Lease liabilities	1,606	1,494	4,393	937	8,430
Trade and other payables	32,932	-	-	-	32,932
Dividends payable to non-controlling interest	1,633	-	-	-	1,633
<b>Total financial liabilities</b>	<b>57,925</b>	<b>17,656</b>	<b>128,109</b>	<b>39,155</b>	<b>242,845</b>

The following table represents the maturity profile of the Group's derivative commodity contracts based on undiscounted cash flows:

<i>At 31 December 2018</i>	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	Total
Cash inflow	133,167	47,403	42,251	222,821
Cash outflow	(132,409)	(47,367)	(42,292)	(222,068)
<b>Net cash flows</b>	<b>758</b>	<b>36</b>	<b>(41)</b>	<b>753</b>
<i>At 31 December 2017</i>				
Cash inflow	45,120	29,028	54,785	128,933
Cash outflow	(46,422)	(28,182)	(54,572)	(129,176)
<b>Net cash flows</b>	<b>(1,302)</b>	<b>846</b>	<b>213</b>	<b>(243)</b>

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**27 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)**

**Reconciliation of liabilities arising from financing activities.** The movements in the Group's liabilities arising from financing activities were as follows:

	Long-term debt and interest payables	Long-term lease liabilities	Total
<b>At 1 January 2017</b>	<b>218,586</b>	<b>256</b>	<b>218,842</b>
Cash flows	(63,144)	(567)	(63,711)
<b>Non-cash movements</b>			
Non-cash additions	-	7,623	7,623
Interest accrued	10,235	119	10,354
Foreign exchange movements	(8,706)	(135)	(8,841)
<b>At 31 December 2017</b>	<b>156,971</b>	<b>7,296</b>	<b>164,267</b>
Cash flows	(22,313)	(2,192)	(24,505)
<b>Non-cash movements</b>			
Non-cash additions	249	2,480	2,729
Interest accrued	8,702	474	9,176
Foreign exchange movements	28,995	1,758	30,753
Acquisition of subsidiaries	1,010	-	1,010
Reclassification to assets held for sale (see Note 5)	-	(18)	(18)
<b>At 31 December 2018</b>	<b>173,614</b>	<b>9,798</b>	<b>183,412</b>

**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.

At the reporting date, the Group had investment grade ratings of BBB by Standard & Poor's, BBB by Fitch Ratings and Baa3 by Moody's Investors Service. Subsequent to the balance sheet date, in February 2019, the Group's credit rating was upgraded to Baa2 by Moody's Investors Service. 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's 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 and bank deposits with maturity more than three months). There were no changes to the Group's approach to capital management during 2018. At 31 December 2018 and 2017, the Group's capital totaled RR 971,157 million and RR 847,646 million, respectively.



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**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 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 60 days (prior to 28 November 2017, this restriction applied to new financing with a maturity of more 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 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.

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 2018, the Group had contractual capital expenditures commitments aggregating approximately RR 376 billion (at 31 December 2017: RR 49 billion) mainly for construction of infrastructure for future LNG projects (through 2028) and for development at the North-Russkoye (through 2021), the Salmanovskoye (Utrenneye) (through 2023), the Yarudeyskoye (through 2020), the East-Tarkosalinskoye (through 2021) and the Yurkharovskoye (through 2019) fields all in accordance with duly signed agreements. These amounts at 31 December 2018 included RR 266 billion related to the Arctic LNG 2 project, which assets were classified as held for sale (at 31 December 2017: RR 11 billion).

In September 2016, the Group and Eni S.p.A. (hereinafter referred to as the "Concessionaries") formed a joint operation with a 50 percent participation interest held by each Concessionary under 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 Group's commitments with regard to this joint operation relate to performance obligations of the Concessionaries to conduct mandatory work program exploration activities as stipulated by the Concession Contract. 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.

**28 CONTINGENCIES AND COMMITMENTS (CONTINUED)**

The Group's commitments with regard to its joint operation in Lebanon relate to performance obligations of the Right holders to conduct minimum work commitment exploration activities as stipulated by the Exploration and Production Agreements (see Note 1). The maximum amount to be paid to the Republic of Lebanon by the Group in case of non-performance during the first exploration period of up to three years ending in 2021 (may be extended for a period not exceeding one year) is EUR 13.5 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.

**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-vessels owners, LNG-terminal owners) in favor of the Group's joint venture OAO Yamal LNG and its subsidiary totaled USD 1.4 billion and EUR 7.2 billion at 31 December 2018 (at 31 December 2017: USD 3.0 billion and EUR 6.6 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 aggregated amount of non-financial guarantees issued by the Group to a Russian bank in favor of the Group's joint venture Cryogas-Vysotsk totaled EUR 232 million at 31 December 2018 (at 31 December 2017: EUR 49 million).

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.

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

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

**28 CONTINGENCIES AND COMMITMENTS (CONTINUED)**

The majority 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><b>Subsidiaries:</b></i>		
Salmanovskoye (Utrenneye)	OOO Arctic LNG 2	2120
Yurkharovskoye	OOO NOVATEK-Yurkharovneftegas	2034
Upper-Tiuteyskoye		
and West-Seyakhinskoye	OOO NOVATEK-Yurkharovneftegas	2044
West-Yurkharovskoye	OOO NOVATEK-Yurkharovneftegas	2029
East-Tarkosalinskoye	OOO NOVATEK-Tarkosaleneftgas	2043
North-Russkoye	OOO NOVATEK-Tarkosaleneftgas	2031
Kharbeyskoye	OOO NOVATEK-Tarkosaleneftgas	2036
Urengoyskoye (within the Olimpiyskiy license area)	OOO NOVATEK-Tarkosaleneftgas	2059
Khancheyevskoye	OOO NOVATEK-Tarkosaleneftgas	2044
East-Tazovskoye	OOO NOVATEK-Tarkosaleneftgas	2033
Dorogovskoye	OOO NOVATEK-Tarkosaleneftgas	2033
North-Khancheyevskoye + Khadyryakhinskoye	OOO NOVATEK-Tarkosaleneftgas	2029
Dobrovolskoye (within the Olimpiyskiy license area)	OOO NOVATEK-Tarkosaleneftgas	2059
South-Khadyryakhinskoye	OOO NOVATEK-Tarkosaleneftgas	2031
Geofizicheskoye	OOO Arctic LNG 1	2034
Gydanskoye	OOO Arctic LNG 1	2044
Yarudeyskoye	OOO Yargeo	2029
East-Urengoyskoye + North-Esetinskoye (within the West Yaro Yakhinsky license area)	OOO Severneft Urengoy	2025
Beregovoe	AO NOVATEK-Pur	2070
Urengoyskoe (within the Ust-Yamsoveyskiy license area)	OOO Urengoyskaya gasovaya kompaniya	2024
<i><b>Joint ventures:</b></i>		
South-Tambeyskoye	OOO Yamal LNG	2045
Urengoyskoye (within the Samburgskiy and Yevo-Yakhinsky license areas)		
	AO Arcticgas	2034
Yaro-Yakhinskoye	AO Arcticgas	2034
Samburgskoye	AO Arcticgas	2034
North-Chaselskoye	AO Arcticgas	Life of field
Yevo-Yakhinskoye	AO Arcticgas	2034
North-Urengoyskoye	ZAO Nortgas	2038
Termokarstovoye	ZAO Terneftgas	2097

**28 CONTINGENCIES AND COMMITMENTS (CONTINUED)**

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.

**PAO NOVATEK****Notes to 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 2018 and 2017 are set out below:

	Ownership percent at 31 December:		Country of incorporation	Principal activities
	2018	2017		
<b>Subsidiaries:</b>				
OOO NOVATEK-Yurkharovneftegas	100	100	Russia	Exploration and production
OOO NOVATEK-Tarkosaleneftegas	100	100	Russia	Exploration and production
OOO Yargeo	51	51	Russia	Exploration, development and production
AO NOVATEK-Pur (formerly AO Geotransgas)	100	-	Russia	Exploration and production
OOO Arctic LNG 1	100	100	Russia	Exploration and development
OOO Arctic LNG 2	100	100	Russia	Exploration and development, construction of LNG plant
OOO Arctic LNG 3	100	100	Russia	Exploration and development
OOO NOVATEK-NTC	100	100	Russia	Scientific and technical support of exploration and development
OOO NOVATEK-Murmansk	100	100	Russia	Construction of large-scale offshore structures
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
<b>Joint ventures:</b>				
OOO Yamal LNG	50.1	50.1	Russia	Exploration and development, production of LNG
AO Articgas (see Note 7)	50	53.3	Russia	Exploration and production
ZAO Nortgas	50	50	Russia	Exploration and production
ZAO Terneftegas	51	51	Russia	Exploration and production
OOO Cryogas-Vysotsk	51	51	Russia	Construction of medium-scale LNG plant
Rostock LNG GmbH	49	-	Germany	Construction of medium-scale LNG transshipment terminal

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

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

**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>	<b>Year ended 31 December:</b>	
	<b>2018</b>	<b>2017</b>
<b>Transactions</b>		
Other revenues	3,258	1,481
Purchases of natural gas and liquid hydrocarbons	(280,570)	(137,784)
Materials, services and other	(133)	(193)
Other operating income (loss)	119	-
Interest income on loans issued	12,511	13,640
Dividends declared	8,500	2,383
<hr/>		
<i>Related parties – joint ventures</i>	<b>At 31 December 2018</b>	<b>At 31 December 2017</b>
<b>Balances</b>		
Long-term loans receivable	232,515	211,472
Current portion of long-term loans receivable	40,386	891
Trade receivables	330	246
Trade payables and accrued liabilities	26,194	19,785

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.

In September 2018, TOTAL S.A. acquired an additional shareholding in NOVATEK increasing its' participating interest in the Company to 19.4%. From here on, the Group considers TOTAL as a shareholder of significant influence, and starting from 1 October 2018, discloses balances and operations with TOTAL and its subsidiaries as related parties transactions.

<i>Related parties – entities with significant influence and their subsidiaries</i>	<b>Year ended 31 December:</b>	
	<b>2018</b>	<b>2017</b>
<b>Transactions</b>		
Revenue from oil and gas sales	16,511	-
Other operating income (loss)	(459)	-
<hr/>		
<i>Related parties – entities with significant influence and their subsidiaries</i>	<b>At 31 December 2018</b>	<b>At 31 December 2017</b>
<b>Balances</b>		
Trade and other receivables	2,271	-
Trade payables and accrued liabilities	350	-

**PAO NOVATEK**

**Notes to the Consolidated Financial Statements**

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

**30 RELATED PARTY TRANSACTIONS (CONTINUED)**

<i>Related parties – entities under control of key management personnel</i>	<b>Year ended 31 December:</b>	
	<b>2018</b>	<b>2017</b>
<b>Transactions</b>		
Purchases of construction services (capitalized within property, plant and equipment)	(7,107)	(661)
Liquid hydrocarbons transportation by rail	(9,449)	(9,496)
Materials, services and other	(4)	(16)
<hr/>		
<i>Related parties – entities under control of key management personnel</i>	<b>At 31 December 2018</b>	<b>At 31 December 2017</b>
<b>Balances</b>		
Advances for construction	3,704	195
Prepayments and other current assets	715	565
Trade payables and accrued liabilities	2,104	504

Transactions with related parties also included loans, which were provided to one of the Group's subsidiaries by its non-controlling shareholder (see Note 14).

**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, in the following amounts:

<i>Related parties – members of the key management personnel</i>	<b>Year ended 31 December:</b>	
	<b>2018</b>	<b>2017</b>
Board of Directors	128	133
Management Committee	3,151	2,138
<b>Total compensation</b>	<b>3,279</b>	<b>2,271</b>

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.



### 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".

The Group's management reviews financial information on the results of operations of the reporting segment prepared based on IFRS. The CODM assesses reporting segment performance based on profit comprising among others revenues, depreciation, depletion and amortization, interest income and expense, income tax and other items as presented in the Group's consolidated statement of income. The CODM also reviews capital expenditures of the reporting segment for the period defined as additions to property, plant and equipment (see Note 6).

**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, other gas and gas condensate refined products, liquefied petroleum gas and crude oil;
- *Countries of Europe (primarily, the Netherlands, Belgium, Sweden, Denmark, France, Finland, the United Kingdom, Italy, Poland and Montenegro)* – sales of naphtha, stable gas condensate, gas condensate refined products, crude oil, liquefied petroleum gas and natural gas and exploration activities within joint operations;
- *Countries of the Asia-Pacific region (primarily, China, Taiwan, Republic of Korea, Japan, India and Singapore)* – sales of naphtha, stable gas condensate, natural gas and crude oil;
- *Countries of North America (primarily, the USA)* – sales of naphtha and other gas condensate refined products;
- *Countries of the Middle East (primarily, Oman, UAE and Lebanon)* – sales of naphtha and stable gas condensate and exploration activities within joint operations;
- *Countries of Latin America (primarily, Brazil)* – sales of natural gas.

Geographical information of oil and gas sales for the years ended 31 December 2018 and 2017 is as follows:

	Year ended 31 December:	
	2018	2017
Russia	406,621	351,318
Europe	278,367	152,439
Asia-Pacific region	138,992	77,204
North America	26,867	25,962
The Middle East	11,742	-
Latin America	4,786	-
Less: export duties	(41,614)	(27,104)
Total outside Russia	419,140	228,501
<b>Total oil and gas sales</b>	<b>825,761</b>	<b>579,819</b>

Revenues pertaining to geographical information are prepared based on the products geographical destination. For products transported by tankers, the geography is determined based on the location of the port of discharge/transshipment designated by the Group's customer. Substantially all of the Group's operating assets are located in the Russian Federation.

**Major customers.** For the years ended 31 December 2018 and 2017, the Group had one major customer to whom individual revenue exceeded 10 percent of total external revenues, which represented 14 percent (RR 115.4 billion) and 19 percent (RR 110.3 billion) of total external revenues, respectively. The Group's major customer resides within the Russian Federation.

**32 NEW ACCOUNTING PRONOUNCEMENTS**

The following new standards and interpretations have been issued that are mandatory for the annual periods beginning on or after 1 January 2019, and which the Group has not early adopted:

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.

Amendments to IFRS 3, Business combinations (issued in October 2018 and effective for annual periods beginning on or after 1 January 2020, early adoption is permitted). These amendments revise the definition of a business with the aim to make its application less complicated. In addition, they introduce an optional "concentration test" that, if met, eliminates the need for further assessment. Under this concentration test, where substantially all of the fair value of gross assets acquired is concentrated in a single asset (or a group of similar assets), the assets acquired would not represent a business. The Group will apply the new definition of a business in accounting for future transactions starting from 1 January 2020.

## **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, and are presented comprising amounts classified as assets held for sale and amounts allocated to fair values of the identified assets in acquisitions of subsidiaries (see Note 5). These costs do not include LNG liquefaction and transportation operations (amounts in millions of Russian roubles).

	<b>Year ended 31 December:</b>	
	<b>2018</b>	<b>2017</b>
<b>Costs incurred in exploration and development activities</b>		
Acquisition of unproved properties	66	1,040
Acquisition of proved properties	17,633	10,594
Exploration costs	12,379	7,958
Development costs	59,946	16,481
<b>Total costs incurred in exploration and development activities</b>	<b>90,024</b>	<b>36,073</b>
The Group’s share in joint ventures’ cost incurred in exploration and development activities	29,401	19,214
	<b>At 31 December 2018</b>	<b>At 31 December 2017</b>
<b>Capitalized costs relating to oil and gas producing activities</b>		
Proved and unproved properties	91,496	70,327
Wells, related equipment and facilities	279,361	265,308
Support equipment and facilities	126,970	101,861
Uncompleted wells, related equipment and facilities	78,843	27,312
<b>Total capitalized costs relating to oil and gas producing activities</b>	<b>576,670</b>	<b>464,808</b>
Less: accumulated depreciation, depletion and amortization	(193,834)	(159,677)
<b>Net capitalized costs relating to oil and gas producing activities</b>	<b>382,836</b>	<b>305,131</b>
The Group’s share in joint ventures’ capitalized costs relating to oil and gas producing activities	456,277	452,403

UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)

Results of Operations for Oil and Gas Producing Activities

Results of operations for oil and gas producing activities of the Group's subsidiaries and the Group's share in the results of operations of joint ventures are shown below (amounts in millions of Russian roubles).

	Year ended 31 December:	
	2018	2017
<i>Subsidiaries</i>		
Revenues from oil and gas sales (less transportation)	242,078	200,331
Lifting costs	(14,938)	(13,161)
Taxes other than income tax	(57,821)	(48,611)
Depreciation, depletion and amortization	(27,051)	(30,077)
Exploration expenses	(7,012)	(1,819)
Social expenses and charity <sup>(1)</sup>	(1,171)	(1,526)
Other operating expenses <sup>(2)</sup>	(388)	(488)
<b>Total operating expenses</b>	<b>(108,381)</b>	<b>(95,682)</b>
<b>Results of operations for oil and gas producing activities before income tax</b>	<b>133,697</b>	<b>104,649</b>
Less: related income tax expenses	(25,123)	(20,048)
<b>Results of operations for oil and gas producing activities of the Group's subsidiaries</b>	<b>108,574</b>	<b>84,601</b>
<i>Group's share in joint ventures</i>		
Revenues from oil and gas sales (less transportation)	193,396	98,432
Lifting costs	(5,527)	(4,570)
Taxes other than income tax	(37,306)	(34,533)
Depreciation, depletion and amortization	(19,786)	(17,512)
Exploration expenses	(332)	(261)
Social expenses and charity <sup>(1)</sup>	(106)	(791)
<b>Total operating expenses</b>	<b>(63,057)</b>	<b>(57,667)</b>
<b>Results of operations for oil and gas producing activities before income tax</b>	<b>130,339</b>	<b>40,765</b>
Less: related income tax expenses	(21,738)	(6,889)
<b>Group's share in results of operations for oil and gas producing activities of joint ventures</b>	<b>108,601</b>	<b>33,876</b>
<b>Total results of operations for oil and gas producing activities of the Group's subsidiaries and joint ventures</b>	<b>217,175</b>	<b>118,477</b>

<sup>(1)</sup> Represent social expenses and compensatory payments related mainly to continued support of charities and social programs in the regions where we perform our production and development activities.

<sup>(2)</sup> Represent mainly materials, services and other expenses, as well as administrative expenses being by nature operating expenses relating to fields in exploration and development stage.

The results of operations for hydrocarbons producing activities are presented only for volumes produced by the Group's subsidiaries and joint ventures and do not include general corporate overheads, processing costs incurred after saleable hydrocarbons are received, such as stable gas condensate processing costs and natural gas liquefaction costs. Revenues from oil and gas sales are calculated based on hydrocarbons production volumes and netback prices determined at the point of marketable products production and do not include export duties, transportation expenses to customers, storage, sales and other similar expenses.

**UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)**

Operating expenses include only the amounts directly related to the extraction of natural gas, gas condensate and crude oil, such as lifting costs (materials, services and other expenses, as well as administrative expenses being by nature operating expenses of oil and gas producing activities), taxes other than income tax, depreciation, depletion and amortization and other expenses. Income tax expense is calculated based on income tax rates applicable to each Group's subsidiary and joint venture.

**Proved Oil and Gas Reserves**

The following information presents the quantities of proved oil and gas reserves and changes thereto as at and for the years ended 31 December 2018 and 2017.

The Group estimates its oil and gas reserves in accordance with rules promulgated by the Securities and Exchange Commission (SEC) for proved 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 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.

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 2120. 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 including volumes of natural gas consumed in hydrocarbons production and development activities. Production and reserves of the South-Tambeyskoye field of Yamal LNG are reported at 60 percent including an additional 9.9 percent interest not owned by the Group, since the Group assumes certain economic and operational risks related to this interest.

**UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)**

For convenience, reserves estimates are provided both in English and Metric units.

Net proved reserves of natural gas are presented below.

	Net proved reserves		Group's share in joint ventures		Total net proved reserves	
	Billions of cubic feet	Billions of cubic meters	Billions of cubic feet	Billions of cubic meters	Billions of cubic feet	Billions of cubic meters
<b>At 31 December 2016</b>	<b>36,985</b>	<b>1,047</b>	<b>28,285</b>	<b>801</b>	<b>65,270</b>	<b>1,848</b>
Changes attributable to:						
Revisions of previous estimates	(76)	(2)	374	10	298	8
Extension and discoveries	1,485	42	1,154	33	2,639	75
Acquisitions <sup>(1)</sup>	8,117	230	-	-	8,117	230
Production	(1,523)	(43)	(716)	(20)	(2,239)	(63)
<b>At 31 December 2017</b>	<b>44,988</b>	<b>1,274</b>	<b>29,097</b>	<b>824</b>	<b>74,085</b>	<b>2,098</b>
Changes attributable to:						
Revisions of previous estimates	288	8	433	13	721	21
Extension and discoveries	483	14	1,294	36	1,777	50
Acquisitions <sup>(2)</sup>	3,426	97	-	-	3,426	97
Disposals <sup>(3)</sup>	-	-	(699)	(20)	(699)	(20)
Production	(1,478)	(42)	(951)	(27)	(2,429)	(69)
<b>At 31 December 2018</b>	<b>47,707</b>	<b>1,351</b>	<b>29,174</b>	<b>826</b>	<b>76,881</b>	<b>2,177</b>
<b>Net proved developed reserves (included above)</b>						
At 31 December 2016	14,399	407	8,487	240	22,886	647
At 31 December 2017	12,685	359	12,820	363	25,505	722
At 31 December 2018	12,187	345	14,103	399	26,290	744
<b>Net proved undeveloped reserves (included above)</b>						
At 31 December 2016	22,586	640	19,798	561	42,384	1,201
At 31 December 2017	32,303	915	16,277	461	48,580	1,376
At 31 December 2018	35,520	1,006	15,071	427	50,591	1,433

<sup>(1)</sup> In 2017, the Group acquired oil and gas exploration and production licenses for the Upper-Tiuteyskoye, the West-Seyakhinskoye and the Gydanskoye fields and 100 percent ownership interests in OOO Severneft-Urengoy (merged into OOO NOVATEK-Yurkharovneftegas in January 2019), AO Eurotek and AO South-Khadyryakhinskoye (merged into OOO NOVATEK-Tarkosaleneftgas in May 2018), which held exploration and production licenses for the West-Yaroyakhinskiy, the Syskonsyninskiy and the South-Khadyryakhinskiy license areas, respectively.

<sup>(2)</sup> In 2018, the Group acquired 100 percent ownership interests in AO Geotransgas (renamed to AO NOVATEK-Pur in November 2018) and OOO Urengoyetskaya gasovaya kompaniya (merging into OOO NOVATEK-Yurkharovneftegas in January 2019), exploration and production license holders of the the Beregovoy and the Ust-Yamsoveyskiy license areas, respectively.

<sup>(3)</sup> In the first quarter of 2018, the Group and PAO Gazprom Neft completed the final stage of the previously commenced restructuring procedures. As a result of the transaction, the Group's effective interest in AO Arcticgas decreased from 53.3 to 50 percent.

**UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)**

The net proved reserves of natural gas reported in the table above included reserves attributable to a non-controlling interest in a Group's subsidiary of 238 billion cubic feet (seven billion cubic meters) and 167 billion cubic feet (five billion cubic meters) at 31 December 2018 and 2017, respectively, and reserves attributable to an additional 9.9 percent interest in Yamal LNG not owned by the Group (see above) of 2,471 billion cubic feet (70 billion cubic meters) and 2,386 billion cubic feet (68 billion cubic meters) at 31 December 2018 and 2017, respectively.

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	
	Millions of barrels	Millions of metric tons	Millions of barrels	Millions of metric tons	Millions of barrels	Millions of metric tons
<b>At 31 December 2016</b>	<b>623</b>	<b>73</b>	<b>691</b>	<b>81</b>	<b>1,314</b>	<b>154</b>
Changes attributable to:						
Revisions of previous estimates	33	4	(12)	(2)	21	2
Extension and discoveries	61	8	62	7	123	15
Acquisitions <sup>(1)</sup>	40	5	-	-	40	5
Production	(55)	(7)	(43)	(5)	(98)	(12)
<b>At 31 December 2017</b>	<b>702</b>	<b>83</b>	<b>698</b>	<b>81</b>	<b>1,400</b>	<b>164</b>
Changes attributable to:						
Revisions of previous estimates	31	4	50	5	81	9
Extension and discoveries	35	4	88	11	123	15
Acquisitions <sup>(2)</sup>	77	9	-	-	77	9
Disposals <sup>(3)</sup>	-	-	(31)	(4)	(31)	(4)
Production	(53)	(7)	(46)	(5)	(99)	(12)
<b>At 31 December 2018</b>	<b>792</b>	<b>93</b>	<b>759</b>	<b>88</b>	<b>1,551</b>	<b>181</b>
<b>Net proved developed reserves (included above)</b>						
At 31 December 2016	275	33	326	37	601	70
At 31 December 2017	307	38	359	41	666	79
At 31 December 2018	340	42	387	44	727	86
<b>Net proved undeveloped reserves (included above)</b>						
At 31 December 2016	348	40	365	44	713	84
At 31 December 2017	395	45	339	40	734	85
At 31 December 2018	452	51	372	44	824	95

<sup>(1)</sup> In 2017, the Group acquired oil and gas exploration and production licenses for the Upper-Tiuteyskoye, the West-Seyakhinskoye and the Gydanskoye fields and 100 percent ownership interests in OOO Severneft-Urengoy (merged into OOO NOVATEK-Yurkharovneftegas in January 2019), AO Eurotek and AO South-Khadyryakhinskoye (merged into OOO NOVATEK-Tarkosaleneftgas in May 2018), which held exploration and production licenses for the West-Yaroyakhinskiy, the Syskonsyninskiy and the South-Khadyryakhinskiy license areas, respectively.

<sup>(2)</sup> In 2018, the Group acquired 100 percent ownership interests in AO Geotransgas (renamed to AO NOVATEK-Pur in November 2018) and OOO Urengoyskaya gasovaya kompaniya (merging into OOO NOVATEK-Yurkharovneftegas in January 2019), exploration and production license holders of the the Beregovoy and the Ust-Yamsoveyskiy license areas, respectively.

<sup>(3)</sup> In the first quarter of 2018, the Group and PAO Gazprom Neft completed the final stage of the previously commenced restructuring procedures. As a result of the transaction, the Group's effective interest in AO Arcticgas decreased from 53.3 to 50 percent.



**UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)**

The net proved reserves of crude oil, gas condensate and natural gas liquids reported in the table above included reserves attributable to a non-controlling interest in a Group's subsidiary of 82 million barrels (11 million metric tons) and 65 million barrels (eight million metric tons) at 31 December 2018 and 2017, respectively, and reserves attributable to an additional 9.9 percent interest in Yamal LNG not owned by the Group (see above) of 22 million barrels (two million metric tons) and 17 million barrels (two million metric tons) at 31 December 2018 and 2017, respectively.



**PAO NOVATEK**

**MANAGEMENT'S DISCUSSION AND ANALYSIS  
OF FINANCIAL CONDITION  
AND RESULTS OF OPERATIONS**

**FOR THE YEAR ENDED 31 DECEMBER 2018**

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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 2018 and for the year then ended in conjunction with our audited consolidated financial statements as of and for the year ended 31 December 2018. 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").

**OVERVIEW**

We are one of the Russia's largest natural gas producers and leaders in terms of proved natural gas reserves in the world under the Petroleum Resources Management System ("PRMS") and the Securities 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.

The natural gas assets of our subsidiaries and joint ventures include projects where we sell natural gas through the Unified Gas Supply System in the Russian domestic market and liquefied natural gas ("LNG") delivered to international markets. In the fourth quarter of 2017, our joint venture OAO Yamal LNG commenced producing LNG at the first train of its liquefaction plant, and in the third and the fourth quarters of 2018, the second and the third LNG trains were launched.

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 natural gas liquids ("NGL"). 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 (by rail and from the port of Ust-Luga on the Baltic Sea by tankers).

A significant part of our NGL produced at the Purovsky Plant is dispatched via pipeline for refining by OOO SIBUR Tobolsk at its refining facilities (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 liquefied petroleum gas ("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. NGL sold directly from the Purovsky Plant and sales of LPG received from the processing at the Tobolsk Refining Facilities are presented within LPG sales in this report.

We deliver our crude oil to both domestic and international markets.

**RECENT DEVELOPMENTS****Implementing our Yamal LNG project**

The Group, jointly with our international partners TOTAL S.A., China National Petroleum Corporation and Silk Road Fund Co. Ltd., through our joint venture OAO Yamal LNG, undertakes an integrated project on natural gas production, liquefaction and shipping. The project envisages the production of liquefied natural gas at the plant with an annual capacity of 17.4 million tons, including 5.5 million tons for each of the first three LNG trains and 0.9 million tons for the fourth LNG train, based on the feedstock resources of the South-Tambeyskoye field located in YNAO (the "Yamal LNG project"). Yamal LNG is the holder of the LNG export license and more than 95% of LNG volumes produced within the first three trains of the project have been contracted under long-term agreements for sale to international markets, mainly to the Asia-Pacific Region ("APR") and to the European market. To ensure these deliveries, long-term agreements for time chartering of LNG ice-class carriers have been signed. Ten LNG Arc7 ice-class carriers transport LNG from the project as at the date of this report.

In the fourth quarter of 2017, Yamal LNG started producing LNG at the first LNG train with an annual capacity of 5.5 million tons, and, in December 2017, commenced shipping of LNG from the port of Sabetta by Arc7 ice-class LNG tankers.

In July 2018, production of LNG at the second LNG train commenced and, in early August, Yamal LNG shipped the first LNG cargo produced from the second LNG train.

In November 2018, Yamal LNG commenced initial production of LNG at the third LNG train and, by December, the production train reached the full nameplate capacity.

The commencement of LNG production at the second and third LNG trains was performed well ahead of schedule (six months and more than a year, respectively) and on budget. Reaching the full nameplate capacity of 16.5 million tons per annum from the three LNG trains positions Yamal LNG as one of the largest suppliers of LNG to international gas importing markets.

In total, during 2018, 8.4 million tons of LNG and 717 thousand tons of stable gas condensate were shipped from the port of Sabetta. LNG was delivered under both short-term and long-term contracts. In the second half of 2018, four LNG cargoes were delivered from the port of Sabetta via the Northern Sea Route passage navigating the Eastern direction to Chinese ports by Arc7 ice-class LNG tankers, shortening the LNG voyage time by more than one third compared to delivering LNG by the traditional route via the Suez Canal and the Strait of Malacca. These shipments represented the first voyages with Russian LNG via the Northern Sea Route without escort of an icebreaker and commenced the seasonal LNG shipments eastbound via the Northern Sea Route.

The fourth LNG train at Yamal LNG is currently in the final design phase, and procurement of equipment has commenced. The fourth LNG train will be constructed based on a proprietary liquefaction technology developed by the Group's engineers and using mainly Russian-made equipment (see below).

**Implementing our Arctic LNG 2 project**

The Group through its wholly owned subsidiary OOO Arctic LNG 2 undertakes a project to construct a new LNG plant on the Gydan peninsula based on the hydrocarbon resources of the Salmanovskoye (Utrenneye) field (the "Arctic LNG 2 project").

The plant will be built on gravity-based platforms and will consist of three processing trains with an annual capacity of 6.6 million tons of LNG per year each, or an aggregate capacity of 19.8 million tons of LNG per year. The licenses for natural gas liquefaction technology were purchased from Linde AG. In the fourth quarter of 2018, the Group completed the FEED work on the LNG plant construction, signed an agreement on the design and construction of gravity-based platforms, as well as concluded several contracts on supply of equipment, including turbo machinery equipment (gas turbine compressors, gas turbine generators and other) for the three liquefaction trains of the plant. The FID decision is expected to be taken in the second half of 2019.

Gravity-based platforms and other major units for the Arctic LNG 2 plant will be produced at our own center for construction of large-scale marine facilities located in the Murmansk region, which will also be used for the Group's subsequent LNG projects. Currently, loading berths and dry docks are under construction, soil excavating works are performed, basements for the gravity-based platforms construction plant, the concrete plant and the workers' rotating village are in progress of construction. The use of gravity-based platforms technology for the plant construction, as well as localizing production (most of the equipment for the plant construction will be produced in the Russian domestic market) will contribute to lower LNG liquefaction costs compared to other LNG projects.

In 2018, we continued full-scale exploration activities at the Salmanovskoye (Utrenneye) field, conducted processing and interpretation of new and existing seismic data, and drilled several exploration wells. As a result of the works performed, two new hydrocarbon deposits were discovered at the Salmanovskoye (Utrenneye) field and commercial viability of the mid-Jurassic deposits was confirmed. The reserves of the two new deposits within the Salmanovskoye (Utrenneye) license area under the Russian reserve category C1+C2 totaled 405 bcm of natural gas and 40 million tons of gas condensate. The new deposits expand the field's reserve potential as well as open additional opportunities for implementing the Arctic LNG 2 project.

In May 2018, PAO NOVATEK and TOTAL S.A. agreed in principle on the acquisition by TOTAL of a 10% participation interest in the Arctic LNG 2 project. The transaction is expected to be closed no later than 31 March 2019.

#### **Obtaining a patent for natural gas liquefaction technology**

In March 2018, the Group obtained a patent for its proprietary natural gas liquefaction technology called "Arctic Cascade". The patented LNG technology is based on a two-stage liquefaction process ensuring high energy efficiency due to the maximum use of the colder ambient temperature in the arctic climate. Our proprietary technology intends to use mainly Russian-made equipment and achieve a decrease in the overall cost of liquefaction, as well as develop a domestic technological base for the Group's future LNG projects.

#### **Logistics improvement and transportation costs optimization**

In line with our long-term strategy to effectively manage logistics and to optimize shipping costs of our Arctic projects, in 2018, the Group established two wholly owned subsidiaries:

- In May 2018, the Group established a subsidiary OOO Maritime Arctic Transport to manage and optimize transportation costs, and to build up the unique competencies of Arctic navigation.
- In April 2018, we established a subsidiary OOO NOVATEK-Kamchatka to build an LNG transshipment terminal on the Kamchatka Peninsula with throughput of 20 million tons of LNG per annum. In September 2018, the Group signed an agreement of intent with the Ministry of the Russian Federation for the Development of the Far East and the Government of the Kamchatka Territory on supporting and providing assistance in the implementation of this project. Construction of the transshipment complex will contribute to the logistics optimization of LNG deliveries from the Arctic region to the customers in the Asian Pacific Region ("APR"), promoting the Northern Sea Route, as well as boil-off gas deliveries potential to supplement the peninsula's needs in natural gas.

In September 2018, the Group and the State Corporation Rosatom signed an agreement of intent to establish a joint venture for the purpose of jointly developing, financing and implementing a project to create an LNG-fueled icebreaker fleet to support the Group's Arctic projects in frozen water areas along the Northern Sea Route.

In October 2018, the Group and Fluxys Germany Holding GmbH arranged a joint venture, Rostock LNG GmbH, with 49% and 51% participation interests, respectively, to undertake a project to construct and operate a medium-scale LNG transshipment terminal with capacity of approximately 300 thousand tons per annum located in the port of Rostock in Germany. The terminal will receive LNG carriers with further LNG deliveries made via trucks to consumers. Additionally, the terminal will perform bunkering services and LNG transshipment onto bunkering barges. In October 2018, Rostock LNG GmbH signed a land lease agreement with the administration of the port of Rostock to construct an LNG transshipment terminal. The LNG transshipment terminal project in Germany is an important marketing channel for our LNG deliveries and will allow us to develop medium-scale LNG production, including the LNG plant in the port of Vysotsk.

**Increasing our resource base and production facilities**

In December 2018, AO Arcticgas, a joint venture of the Group and PAO Gazprom Neft, commenced commercial production of crude oil at the Yaro-Yakhinskoye field. The field's crude oil production capacity is estimated at 1.2 million tons per annum. The launch of the crude oil program at the Yaro-Yakhinskoye field will significantly contribute to the Group's liquids production growth.

In February 2018, based on the results of an auction held by AK ALROSA (PAO), the Group acquired 100% participation interests in companies Maretiom Investments Limited and Velarion Investments Limited, which owned 100% participation interests in AO Geotransgas and OOO Urengoyskaya gasovaya kompaniya, respectively, for RR 30.3 billion. Geotransgas (renamed to AO NOVATEK-Pur in December 2018) and Urengoyskaya gasovaya kompaniya (merged into OOO NOVATEK-Yurkharovneftegas in January 2019) held the licenses for exploration and production of hydrocarbons within the Beregovoy license area, which is currently producing hydrocarbons, and the Ust-Yamsoveyskiy license area, respectively. The aggregate proved, probable and possible reserves of the Beregovoye and the Urengoyskoye fields located within the Beregovoy and the Ust-Yamsoveyskiy license areas appraised under the PRMS reserve methodology as of 31 December 2018 totaled 125.2 bcm of natural gas and 11.6 million tons of liquid hydrocarbons.

During 2018, the Group also obtained rights for the usage of five more license areas located in close proximity to other Group's assets:

- In November 2018, the Group won an auction held by the Federal Agency for the Use of Natural Resources of the Russian Federation for the right for geological research works, exploration and production of hydrocarbons at the South-Leskinskiy license area. The license area is located on the Gydan peninsula in the Krasnoyarsk Region and borders with the Group's Tanamskiy license area. As of 31 December 2018, the license area's recoverable resources under the category D of the Russian reserve classification totaled 126 bcm of natural gas and approximately 16 million tons of liquid hydrocarbons. The payment for the license was set at RR 2,041 million.
- In April 2018, we obtained the right for geological research works at the Palkurtoiskiy license area. The license area is located in the YNAO and borders with other Group license areas (the North-Tanamskiy, the Nyavuyahskiy, the West-Solpatinskiy and the Centralno-Nadoyakhskiy). As of 31 December 2018, the license area's recoverable resources under the category D of the Russian reserve classification totaled 278 bcm of natural gas and approximately 49 million tons of liquid hydrocarbons.
- In April 2018, we obtained the right for geological research works at the Centralno-Nadoyakhskiy license area. The license area is located in the YNAO and borders with the Group's West-Solpatinskiy and the Tanamskiy license areas. As of 31 December 2018, the license area's recoverable resources under the category D of the Russian reserve classification totaled 258 bcm of natural gas and 144 million tons of liquid hydrocarbons.
- In March 2018, the Group won an auction held by the Federal Agency for the Use of Natural Resources of the Russian Federation for the right for geological research works, exploration and production of hydrocarbons at the Payutskiy license area. The license area is located in the Krasnoyarsk Region in close proximity to the Group's license areas on the Gydan peninsula, the West-Solpatinskiy, the North-Tanamskiy, the Nyavuyahskiy and Tanamskiy license areas. As of 31 December 2018, the license area's reserves and recoverable resources under the category C+D of the Russian reserve classification totaled 54 bcm of natural gas. The payment for the license amounted to RR 66 million.
- In January 2018, the Group acquired a 100% participation interest in OOO Chernichnoye for RR 616 million. OOO Chernichnoye is a holder of the license for geological research works, exploration and production of hydrocarbons within the Chernichniy license area located in the YNAO in close proximity to the Termokarstovoye field of our joint venture ZAO Terneftegas. As of 31 December 2018, the license area's reserves under the category B of the Russian reserve classification totaled 17.7 bcm of natural gas and 7.8 million tons of liquid hydrocarbons.



In addition, based on the results of drilling and wells testing we discovered the new Nyakhartinskoye and North-Obskoye fields:

- At the Nyakhartinskiy license area we discovered a new natural gas and gas condensate field bearing the same name. Natural gas and gas condensate reserves of the newly discovered field will be determined after completion of the well test. The materials with the reserves appraisal will be submitted to the Russian State Reserves commission for final confirmation in 2019. The discovery of the new field in close proximity to our Yurkharovskoye field will contribute to maintaining the Group's hydrocarbon production in the area of the Unified Gas Supply System projects.
- At the North-Obskiy license area we discovered a new natural gas and gas condensate field bearing the same name. The reserves of this newly discovered field under the category C1+C2 of the Russian reserve classification amounted to 322 bcm of natural gas and 16 million tons of gas condensate. The discovery of this new field is integral for another our future LNG project.

### **Medium-scale LNG plant**

In July 2017, NOVATEK acquired a 51% ownership interest in OOO Cryogas-Vysotsk, which implements a project on constructing the first train of a medium-scale LNG plant for natural gas liquefaction with annual capacity of 660 thousand tons, located at the port of Vysotsk on the Baltic Sea. LNG is expected to be sold to customers in the North West Europe, the Baltic region and the Russian domestic markets via both tankers and trucks, as well as for marine bunkering in the form of bunkering fuel.

Currently, the construction works at the first train are completed, and commissioning works are being finalized. The launch of the first LNG train is expected in the first quarter of 2019.

### **The change in the participation interest in AO Arcticgas**

In the first quarter of 2018, the Group and PAO Gazprom Neft completed the final stage of the previously commenced restructuring procedures to achieve parity shareholdings in our joint venture AO Arcticgas:

- In January 2018, Yamal Development and SeverEnergiya were merged with Arcticgas. As a result, the Group and Gazprom Neft obtained direct participation interests in Arcticgas of 53.3% and 46.7%, respectively.
- In March 2018, Gazprom Neft subscribed to an additional share emission of Arcticgas for a total cash consideration of RR 32.1 billion.

As a result of the aforementioned transactions, the Group's participation interest in Arcticgas decreased from 53.3% to 50.0%. The Group continues to recognize the entity as a joint venture and accounts for this investment under the equity method.

### **International oil and gas projects**

In January 2018, the Group, TOTAL S.A. and Eni S.p.A., through their subsidiaries NOVATEK Lebanon SAL, Total E&P Liban SAL and Eni Lebanon B.V. (hereinafter referred to as the "Right holders"), entered into Exploration and Production Agreements for Petroleum Activities with the Lebanese Republic for the exploration and production of hydrocarbons on offshore blocks 4 and 9 located in the Eastern Mediterranean (hereinafter referred to as the "Exploration and Production Agreements"). The Exploration and Production Agreements stipulate that the Right holders are committed to undertake specified joint upstream activities during the exploration phase within five years. The Group is assigned a 20% participating interest, and Total E&P Liban SAL was appointed as the operator.

**BASIS OF PRESENTATION**

Certain changes have been made to the presentation of oil and gas production costs per unit of production in this report to conform to the reporting practices of the Group's domestic and international peers in the oil and gas industry. The comparative data for 2017 have been recalculated in accordance with this approach.

Oil and gas production costs include only the amounts directly related to the extraction of natural gas, gas condensate and crude oil, such as materials, services and other expenses, administrative expenses being by nature operating expenses of oil and gas producing activities, taxes other than income tax, depreciation, depletion and amortisation. Oil and gas production costs exclude processing costs incurred after saleable hydrocarbons are received, such as stable gas condensate processing costs and natural gas liquefaction costs, as well as transportation and other marketing expenses. Previously, such processing and transportation expenses were presented within oil and gas production costs.

In addition to reporting oil and gas production costs per unit in our subsidiaries, we now also disclose oil and gas production costs per unit in our joint ventures, as well as combined weighted average oil and gas production costs per unit for the Group's subsidiaries and joint ventures.

Oil and gas production and reserves in the current report are calculated based on 100% of our subsidiaries production and reserves and our proportionate share in the production and reserves of our joint ventures including volumes of natural gas consumed in oil and gas producing and development activities. At the same time, production costs per barrel of oil equivalent are calculated based on production volumes net of the volume of consumed natural gas. Production and reserves of the South-Tambeyskoye field developed by the Group's joint venture Yamal LNG is reported at 60% including an additional 9.9% interest not owned by the Group, since the Group assumes certain economic and operational risks related to this interest.

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millions of Russian roubles except as stated	Year ended 31 December:		Change %
	2018	2017	
<b>Financial results</b>			
Total revenues <sup>(1)</sup>	831,758	583,186	42.6%
Operating expenses	(603,912)	(419,859)	43.8%
Normalized EBITDA <sup>(2),(3)</sup>	415,296	256,464	61.9%
Normalized profit attributable to shareholders of PAO NOVATEK <sup>(3)</sup>	162,097	156,387	3.7%
Normalized profit attributable to shareholders of PAO NOVATEK <sup>(3)</sup> , excluding the effect of foreign exchange gains (losses) <sup>(4)</sup>	232,930	156,166	49.2%
Normalized earnings per share <sup>(3)</sup> (in Russian roubles)	53.79	51.85	3.7%
Normalized earnings per share <sup>(3)</sup> , excluding the effect of foreign exchange gains (losses) <sup>(4)</sup> (in Russian roubles)	77.29	51.78	49.3%
Net debt <sup>(5)</sup>	102,903	89,807	14.6%
<b>Production volumes <sup>(6)</sup></b>			
Hydrocarbons production (million barrels of oil equivalent)	549.1	513.3	7.0%
Daily production (million barrels of oil equivalent per day)	1.50	1.41	7.0%
<b>Sales volumes</b>			
Natural gas sales volumes (million cubic meters)	72,134	65,004	11.0%
Crude oil sales volumes (thousand tons)	4,542	4,616	(1.6%)
Naphtha sales volumes (thousand tons)	4,185	4,102	2.0%
Liquefied petroleum gas sales volumes (thousand tons)	2,676	2,648	1.1%
Other stable gas condensate refined products (thousand tons)	2,498	2,641	(5.4%)
Stable gas condensate sales volumes (thousand tons)	1,908	1,918	(0.5%)
<b>Oil and gas SEC reserves <sup>(6)</sup></b>			
Total proved reserves (billion barrels of oil equivalent)	15.8	15.1	4.4%
Total natural gas proved reserves (trillion cubic meters)	2.18	2.10	3.8%
Total liquids proved reserves (million tons)	181	164	10.4%
<b>Cash flow results</b>			
Net cash provided by operating activities	216,349	180,399	19.9%
Cash used for capital expenditures <sup>(7)</sup>	94,038	29,871	214.8%
Free cash flow <sup>(8)</sup>	122,311	150,528	(18.7%)

<sup>(1)</sup> Net of VAT, export duties, excise and fuel taxes.

<sup>(2)</sup> 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.

<sup>(3)</sup> Excluding the effect from the disposal of interests in joint ventures.

<sup>(4)</sup> Excluding the effect of foreign exchange gains (losses) of subsidiaries and our proportionate share in foreign exchange gains (losses) of our joint ventures (see "Profit attributable to shareholders and earnings per share" below).

<sup>(5)</sup> Net Debt represents our total debt net of cash, cash equivalents and bank deposits with original maturity more than three months.

<sup>(6)</sup> Oil and gas production and reserves are calculated based on 100% of production and reserves of our subsidiaries and our proportionate share in the production and reserves of our joint ventures including fuel gas. Production and reserves of the South-Tambeyskoye field of Yamal LNG are reported at 60% (see "Basis of presentation" above).

<sup>(7)</sup> 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.

<sup>(8)</sup> Free cash flow represents the difference between Net cash provided by operating activities and Cash used for capital expenditures.

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Reconciliation of EBITDA and normalized EBITDA is as follows:

<i>millions of Russian roubles</i>	<b>Year ended 31 December:</b>		<b>Change %</b>
	<b>2018</b>	<b>2017</b>	
<b>Profit</b>	<b>182,947</b>	<b>166,470</b>	<b>9.9%</b>
Depreciation, depletion and amortization	33,094	34,523	(4.1%)
Impairment expenses (reversals), net	287	52	n/a
Loss (income) from changes in fair value of derivative financial instruments	450	9	n/a
Total finance expense (income)	(38,608)	(14,658)	163.4%
Total income tax expense	45,587	34,369	32.6%
Share of loss (profit) of joint ventures, net of income tax	37,258	(22,430)	n/a
<b>EBITDA from subsidiaries</b>	<b>261,015</b>	<b>198,335</b>	<b>31.6%</b>
<b>Share in EBITDA of joint ventures</b>	<b>155,926</b>	<b>58,129</b>	<b>168.2%</b>
<b>EBITDA</b>	<b>416,941</b>	<b>256,464</b>	<b>62.6%</b>
Net gain on disposal of interests in joint ventures	(1,645)	-	n/a
<b>Normalized EBITDA</b>	<b>415,296</b>	<b>256,464</b>	<b>61.9%</b>
<b>Normalized EBITDA from subsidiaries</b>	<b>259,370</b>	<b>198,335</b>	<b>30.8%</b>

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Exchange rate, RR for one foreign currency unit <sup>(1)</sup>	1Q		2Q		3Q		4Q		Year		Change Y-o-Y, %
	2018	2017	2018	2017	2018	2017	2018	2017	2018	2017	
<b>US dollar (USD)</b>											
Average for the period	56.88	58.84	61.80	57.15	65.53	59.02	66.48	58.41	62.71	58.35	7.5%
At the beginning of the period	57.60	60.66	57.26	56.38	62.76	59.09	65.59	58.02	57.60	60.66	(5.0%)
At the end of the period	57.26	56.38	62.76	59.09	65.59	58.02	69.47	57.60	69.47	57.60	20.6%
Depreciation (appreciation) of RR to US dollar	(0.6%)	(7.1%)	9.6%	4.8%	4.5%	(1.8%)	5.9%	(0.7%)	20.6%	(5.0%)	n/a
<b>Euro</b>											
Average for the period	69.87	62.65	73.75	62.79	76.18	69.29	75.92	68.78	73.95	65.90	12.2%
At the beginning of the period	68.87	63.81	70.56	60.60	72.99	67.50	76.23	68.45	68.87	63.81	7.9%
At the end of the period	70.56	60.60	72.99	67.50	76.23	68.45	79.46	68.87	79.46	68.87	15.4%
Depreciation (appreciation) of RR to Euro	2.5%	(5.0%)	3.4%	11.4%	4.4%	1.4%	4.2%	0.6%	15.4%	7.9%	n/a

<sup>(1)</sup> 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).

Average for the period	1Q		2Q		3Q		4Q		Year		Change Y-o-Y, %
	2018	2017	2018	2017	2018	2017	2018	2017	2018	2017	
<b>Benchmark natural gas prices <sup>(2)</sup></b>											
NBP, USD per mmbtu	8.1	6.0	7.3	4.8	8.4	5.5	8.4	6.9	8.0	5.8	37.9%
<b>Benchmark crude oil prices <sup>(3)</sup></b>											
Brent, USD per barrel	66.8	53.7	74.4	49.6	75.2	52.1	68.8	61.3	71.3	54.2	31.5%
Urals, USD per barrel	65.2	52.2	72.5	48.7	74.2	50.9	68.3	60.4	70.1	53.1	32.0%
Urals, RR per barrel	3,709	3,071	4,481	2,783	4,862	3,004	4,541	3,528	4,396	3,098	41.9%
<b>Benchmark crude oil prices excluding export duties <sup>(4)</sup></b>											
Urals, USD per barrel	49.2	40.4	56.0	37.2	55.7	40.0	48.9	47.2	52.5	41.2	27.4%
Urals, RR per barrel	2,798	2,377	3,461	2,126	3,650	2,361	3,251	2,757	3,292	2,404	36.9%
<b>Benchmark oil products <sup>(5)</sup> and liquefied petroleum gas <sup>(6)</sup> prices, USD per ton</b>											
Naphtha Japan	582	497	640	445	666	468	575	570	616	495	24.4%
Naphtha CIF NWE	574	485	636	432	652	463	552	555	604	484	24.8%
Jet fuel	647	513	709	483	710	520	684	591	688	527	30.6%
Gasoil	588	481	647	446	661	476	637	545	633	488	29.7%
Fuel oil	370	318	417	300	436	305	420	351	411	319	28.8%
Liquefied petroleum gas	422	395	456	336	541	391	453	459	470	396	18.7%
<b>Export duties, USD per ton <sup>(7)</sup></b>											
Crude oil, stable gas condensate	117.0	86.5	120.6	84.3	134.8	79.8	141.5	96.3	128.5	86.7	48.2%
Naphtha	64.3	47.6	66.2	46.3	74.1	43.8	77.8	52.9	70.6	47.7	48.0%
Jet fuel, gasoil	35.1	25.9	36.1	25.3	40.4	23.9	42.4	28.9	38.5	26.0	48.1%
Fuel oil	117.0	86.5	120.6	84.3	134.8	79.8	141.5	96.3	128.5	86.7	48.2%
Liquefied petroleum gas	0.0	0.0	0.0	0.0	8.9	0.0	36.2	0.0	11.3	0.0	n/a

<sup>(2)</sup> Based on natural gas prices at the National Balancing Point (NBP), the natural gas hub in the United Kingdom.

<sup>(3)</sup> Based on Brent (dtd) and Russian Urals CIF Rotterdam spot assessments prices.

<sup>(4)</sup> Export duties per barrel were calculated based on export duties per ton divided by the coefficient 7.3.

<sup>(5)</sup> 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.

<sup>(6)</sup> Based on spot prices for propane-butane mix at the Belarusian-Polish border (DAF, Brest).

<sup>(7)</sup> 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**

Commodity price volatility continues to exert significant influence on financial and operational 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 reporting period, the Group achieved strong operating results and remained free cash flow positive.

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 60 days (prior to 28 November 2017, the aforementioned restrictions related to new credit facilities with maturity of more 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 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 our joint investment projects on time as planned, including, but not limited to, attracting financing from domestic and non-US capital markets.

**Natural gas prices**

We sell our natural gas to customers in the Russian domestic market, mainly through trunk pipelines and regional distribution networks, and deliver LNG purchased primarily from our joint venture OAO Yamal LNG to international markets (starting from December 2017). In addition, we sell on the European market regasified liquefied natural gas arising during the transshipment of LNG (boil-off gas), as well as during the regasification of purchased LNG at our own regasification stations in Poland.

The Group's natural gas prices in Russia are strongly influenced by the prices set by the Federal Anti-Monopoly Service, 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 2017, wholesale natural gas prices for sales to all customer categories (excluding residential customers) on the domestic market remained unchanged. Effective 1 July 2017, the Regulator increased wholesale natural gas prices by 3.9%, and, from 21 August 2018 – by 3.4%.

In October 2018, the Ministry of Economic Development of the Russian Federation published the "Forecast of Socio-economic Development of the Russian Federation for the period until 2024" stating that wholesale natural gas prices for sales to all customer categories (excluding residential customers) will be increased from July 2019 by an average of 1.4% and from July 2020 to 2024 by 3.0% on an annual basis. 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 on the domestic market 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.

The Group's natural gas prices on international markets are influenced by many factors, such as the balance between supply and demand fundamentals, weather, the geography of sales, the delivery terms to name a few. The Group sells LNG on international markets under short-term and long-term contracts with prices based on the prices for natural gas at major natural gas hubs and on the benchmark crude oil prices. The Group's prices for regasified LNG sold as natural gas on the Polish market are based on the prices regulated by the Energy Regulatory Office of Poland.

The following table shows our aggregate average realized natural gas sales prices on the domestic and international markets (excluding VAT, where applicable):

	Year ended 31 December:		Change %
	2018	2017	
Average natural gas price, RR per mcm	5,201	3,810	36.5%
Average natural gas price, USD per mcm <sup>(1)</sup>	82.3	65.3	26.0%

<sup>(1)</sup> Operations initially priced in Russian roubles were translated into US dollars using the average exchange rate for the period.

In 2018, our aggregate average price for natural gas sold in the Russian Federation and on the international markets increased by 36.5% mainly due to the commencement of LNG sales to international markets from December 2017, as well as an increase in the regulated Russian domestic price effective 1 July 2017 and 21 August 2018 by 3.9% and 3.4%, respectively.

#### 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 lag 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 declining crude oil prices, the export duty rate is calculated based on higher prices compared to the actual prices, resulting 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. We export SILCO (low-sulfur “Siberian Light Crude Oil”) and ESPO (“East Siberia – Pacific Ocean”) grades of crude oil to international markets with a premium or a discount to the benchmark Brent and Dubai crude oil depending on current market situation.

The following table shows our average realized net stable gas condensate and refined products, crude oil and LPG sales prices. Average realized net prices are shown net of VAT, export and import duties, excise and fuel taxes expense, where applicable:

<i>Russian roubles or US dollars per ton <sup>(1)</sup></i>	<b>Year ended 31 December:</b>		<b>Change %</b>
	<b>2018</b>	<b>2017</b>	
<b>Stable gas condensate</b>			
Average net price, RR per ton	25,473	17,719	43.8%
Average net price, USD per ton	403	303	33.0%
<b>Naphtha</b>			
Average net price, RR per ton	35,789	27,301	31.1%
Average net price, USD per ton	572	467	22.5%
<b>Other stable gas condensate refined products</b>			
Average net price, RR per ton	35,682	25,899	37.8%
Average net price, USD per ton	570	443	28.7%
<b>Crude oil</b>			
Average net price, RR per ton	23,394	16,702	40.1%
Average net price, USD per ton	373	286	30.4%
<b>LPG</b>			
Average net price, RR per ton	21,015	15,116	39.0%
Average net price, USD per ton	335	259	29.3%

<sup>(1)</sup> Operations initially priced in Russian roubles were translated into US dollars using the average exchange rate for the period.

In 2018, our weighted-average realized net prices for our liquid hydrocarbons increased compared to 2017 due to an increase in the underlying benchmark prices for these products excluding export duties (see “Selected macro-economic data” above). Our weighted-average realized net prices in Russian roubles terms increased to a greater extent compared to US dollar prices as a result of 7.5% Russian rouble depreciation relative to the US dollar in 2018 compared to 2017.

The dynamics of our weighted-average realized net prices for each product category also reflects changes in volumes sold within periods and changes in the geography of shipments which may significantly impact our average prices in periods of high benchmark prices volatility on international markets. In addition, specifics of pricing mechanism for each particular product (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 other factors) also have an impact on the dynamics of our weighted-average realized net prices.



**Transportation tariffs***Natural gas by pipelines*

We transport our natural gas within the Russian Federation territory 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 2017 and 2018, the average tariff for natural gas transportation through the trunk pipeline did not change. 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 October 2018, the increase in tariffs for natural gas transportation through the trunk pipeline beginning in 2019 through 2024 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*

Substantially all of our stable gas condensate and LPG (excluding volumes sold ex-works from the Purovsky Plant and the Tobolsk Refining Facilities) we transport 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.

Effective January 2018, railroad freight transportation tariffs for all types of hydrocarbons were increased by 5.4% relative to the 2017 tariffs and did not change until the end of 2018. In January 2019, the Regulator increased the aforementioned tariffs by 3.56% relative to the 2018 tariffs.

In 2017 and 2018, 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 markets. In November 2018, the discount co-efficient was extended until the end of 2021. 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, refined products and liquefied natural gas by tankers*

We deliver part of our stable gas condensate and substantially all stable gas condensate refined products, as well as liquefied natural gas (excluding volumes purchased and sold to customers in the same location) to international markets by chartered tankers. In addition to time chartering expenses, we also may incur transshipment, bunkering, port charges and other expenses depending on the delivery terms, which are included in the transportation by tankers expense category. Our tanker transportation expenses are also influenced by the distance to the final port of destination, tanker availability, seasonality of deliveries and other factors.

*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.

Effective 1 January 2018, crude oil transportation tariffs through the pipeline network within the Russian Federation territory were increased by an average of 3.9% relative to the 2017 tariffs and remained unchanged until the end of 2018. Effective 1 January 2019, transportation tariffs were increased by an average of 3.87% compared to 2018 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.

Information regarding UPT, export duties and excise taxes described below is based on the Tax Code of the Russian Federation and the law "On Customs Tariff" effective as at 31 December 2018. Amendments to the taxation that became effective 1 January 2019 are described below in the section "*Completion of the tax maneuver in the oil and gas industry*".

*UPT – natural gas and gas condensate*

In 2017 and 2018, in accordance with the Tax Code of the Russian Federation, the UPT rates for natural gas and gas condensate were calculated monthly according to a formula based on which the set base UPT rate was 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 was multiplied by an adjusting coefficient (set at 6.5 in both reporting periods), and the UPT rate for natural gas also took into account a parameter characterizing natural gas transportation costs (set at zero in both reporting periods and did not affect the UPT rate).

The base UPT rate in both periods was 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 was calculated monthly primarily based 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 was 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.

Effective January 2018, in accordance with the Tax Code of the Russian Federation, the Group began to apply a tax deduction on gas condensate produced for processing into NGL. The amount of the tax deduction is calculated monthly by multiplying a coefficient of NGL recovery from gas condensate processing, the quantity of gas condensate produced and processed, and the tax deduction rate in Russian roubles per ton of NGL derived. The tax deduction rate is determined as a serial number of the respective month starting from January 2018 multiplied by RR 147 per ton, and, from January 2021, the tax deduction rate will be fixed at RR 5,280 per ton of produced NGL.

#### *UPT – crude oil*

In both reporting periods, the UPT rate for crude oil was calculated as a product of a coefficient characterizing the dynamics of world crude oil prices and the base UPT rate adjusted for parameters characterizing crude oil production peculiarities at the particular area. The result was then additionally increased by RR 306 per ton in 2017 and by RR 357 per ton in 2018 (in 2019, RR 428 per ton).

In 2017 and 2018, the base crude oil UPT rate was set at RR 919 per ton. In both reporting periods, 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, Khancheyskoye 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. Therefore, the adjusted base UPT rate for crude oil produced at these fields for the Group amounted to RR 360 per ton.

#### *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 (“monitoring period”). In both reporting periods, 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 30% of the difference between the average Urals crude oil price and USD 182.5 per ton.

The export duty rates for oil products are calculated based on the export duty rate for crude oil adjusted by a coefficient set for each category of oil products. The export duty rates for our exported stable gas condensate refined products as a percentage of the crude oil export duty rate are presented below:

	% from the crude oil export duty rate
Naphtha	55%
Jet fuel	30%
Gasoil	30%
Fuel oil	100%

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:

Average LPG price, USD per ton (P)	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	$135 + 0.7 \times (P - 740)$

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. In 2017 and 2018, the Group did not sell excisable goods of own production on the domestic market.

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 tax rate in both reporting periods amounted to 670 Polish zloty per ton, and the fuel tax rate was increased from 159.71 Polish zloty per ton in 2017 to 162.27 Polish zloty per ton in 2018).

#### *Completion of the tax maneuver in the oil and gas industry*

In August 2018, as part of the completion of the tax maneuver in the oil and gas industry, federal laws introducing changes to the Law of the Russian Federation "On Customs Tariff" and to the Tax Code of the Russian Federation were adopted. The amendments envisage a phased decrease in crude oil and stable gas condensate export duty rate from 1 January 2019 with a respective increase in UPT rates for crude oil and gas condensate, introduction of excise tax deductions for processors of raw oil, as well as other amendments to tax and customs legislation.

Starting from January 2019, the export duty rate for stable gas condensate and crude oil began to gradually decrease by 1/6<sup>th</sup> annually from 30% of crude oil price to 0% in 2024. At the same time, the UPT rate for crude oil is increasing by the same amount in Russian rouble terms. The UPT rate for gas condensate is increasing by 75% of the amount of a decrease in the export duty rate (since the share of NGL received from processing of extracted gas condensate is subject to a UPT deduction).

Where Urals crude oil price in Russian rouble terms in the current monitoring period (from the 15th calendar day in the previous month to the 14th calendar day of the current month) exceeds its average for the previous three monitoring periods by 15%, the export duty rate for stable gas condensate and crude oil may be increased by the Russian Federation government to 45% of crude oil price, and the export duty rates for oil products – to 60% of the export duty rate for crude oil. In this case, the UPT rate for crude oil will decrease by the amount of the corresponding increase in the export duty rate, and the UPT rate for gas condensate – by 75% of this amount.

The export duty rates for oil products are still based on the export duty rate for crude oil adjusted by a coefficient set for each category of oil products. Thus, in case extracted crude oil and gas condensate are further sent for processing, the amount of an increase in UPT rate for crude oil and gas condensate exceeds the amount of a decrease in export duty rates for oil products received from processing. To compensate for this difference, effective January 2019, the so called "negative excise" was introduced: organizations that process raw oil (crude oil, stable gas condensate, vacuum gasoil, tar, fuel oil) are subject to excise tax payments and simultaneously become entitled to an excise tax deduction at a double rate. Effective 1 January 2019, the Group began applying the tax deduction on excise tax for stable gas condensate sent to processing at our Ust-Luga Complex.

#### *Social contributions*

In both reporting periods, 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 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 2017, 2018 and 2019:

	2017		2018		2019	
	Base, RR thousand	Rate, %	Base, RR thousand	Rate, %	Base, RR thousand	Rate, %
Pension Fund of the Russian Federation	less 876 above 876	22.0% 10.0%	less 1,021 above 1,021	22.0% 10.0%	less 1,150 above 1,150	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 755 above 755	2.9% 0.0%	less 815 above 815	2.9% 0.0%	less 865 above 865	2.9% 0.0%

**OIL AND GAS RESERVES**

We do not file with the Securities and Exchange Commission ("SEC") nor we 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 2018 and 2017, 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 responsible for geology and geophysics, gas and liquids commercial operations, engineering and capital construction, production, and long-term financial planning, and also 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 about the Group's oil and gas production and reserves under SEC and PRMS reserve classifications is presented based on 100% of production and reserves attributable to all consolidated subsidiaries (whether or not wholly owned) and our proportionate share in the production and reserves in companies accounted for by the equity method based on our equity ownership interest, including volumes of natural gas consumed in oil and gas production and development activities (primarily, as fuel gas). Production and reserves of the South-Tambeyskoye field of Yamal LNG are reported at 60% including an additional 9.9% interest not owned by the Group, since the Group assumes certain economic and operational risks related to this interest (see "Basis of presentation" above).

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 year ended 31 December:		Change %
	2018	2017	
<b>Natural gas, billions of cubic meters</b>	<b>2,177</b>	<b>2,098</b>	<b>3.8%</b>
Subsidiaries	1,351	1,274	6.0%
Share in joint ventures	826	824	0.2%
<b>Liquids, millions of metric tons</b>	<b>181</b>	<b>164</b>	<b>10.4%</b>
Subsidiaries	93	83	12.0%
Share in joint ventures	88	81	8.6%
<b>Combined reserves, millions of boe</b>	<b>15,789</b>	<b>15,120</b>	<b>4.4%</b>
Production, millions of boe	549	513	7.0%
Acquisitions <sup>(1)</sup> , millions of boe	712	1,543	(53.9%)
Disposals <sup>(2)</sup> , millions of boe	160	-	n/a
<b>Reserves replacement ratio <sup>(3)</sup>, %</b>	<b>222%</b>	<b>435%</b>	
<b>Normalized reserves replacement ratio <sup>(3), (4)</sup>, %</b>	<b>121%</b>	<b>134%</b>	

<sup>(1)</sup> In 2018, acquisitions represent reserves attributable to the Beregovoy and the Ust-Yamsoveyskiy license areas acquired in the first quarter (see "Recent developments" above), and in 2017 – reserves obtained through participation in auctions (the Gydanskiy, the Verhnetiuteyskiy and the West-Seyakhinskiy license areas) and new assets acquisitions (the South-Khadyryakhinskiy, the Syskonsynyninskiy and the West-Yaroyakhinskiy license areas).

<sup>(2)</sup> Represent reserves attributable to the disposal of the 3.3% participation interest in Arcticgas in the first quarter of 2018.

<sup>(3)</sup> The reserves replacement ratio is calculated as the change in reserves increased for the production for the year divided by production for the year.

<sup>(4)</sup> Excluding reserves acquisitions and disposals.

Our total proved reserves under the SEC reserve classification methodology as at the end of 2018 increased by 669 million boe, or 4.4%, to 15,789 million boe, which amounted to a reserve replacement ratio of 222%.

Additions to hydrocarbons SEC proved reserves of our subsidiaries were due to successful exploration works at the Salmanovskoye (Utrenneye) and the Yarudeyskoye fields, as well as due to production drilling at our North-Russkoye field. Our share in the hydrocarbons reserves of our joint ventures increased as a result of successful exploration works at the Urengoyenskoye field (Samburgskiy license area) of Arcticgas, as well as production drilling at the South-Tambeyskoye and the Yaro-Yakhinskoye fields of Yamal LNG and Arcticgas, respectively.

Changes in our hydrocarbons reserves in 2018 were also impacted by acquisitions of new assets in the beginning of 2018 (the Beregovoy and the Ust-Yamsoveyskiy license areas), on the one hand, and the disposal of the 3.3% participation interest in Arcticgas in the first quarter of 2018, on the other hand (see "Recent developments" above). Excluding new licenses acquired and the disposal of participation interest in Arcticgas, the reserves replacement ratio amounted to 121%.

The following table provides for the Group's PRMS proved, proved and probable, and 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 2018	31 December 2017	31 December 2018	31 December 2017	31 December 2018	31 December 2017
Proved reserves (1P reserves)	2,362	2,300	210	192	17,241	16,661
Proved and probable reserves (2P reserves)	4,021	3,879	387	366	29,619	28,471
Proved, probable and possible reserves (3P reserves)	5,029	4,876	520	509	37,348	36,196

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 2018 and 2017 under both reserves reporting methodologies:

<i>Number of years</i>	SEC		PRMS	
	At 31 December: 2018	2017	At 31 December: 2018	2017
Total proved reserves to production	29	29	31	32
Total proved and probable reserves to production	-	-	54	55
Total proved, probable and possible reserves to production	-	-	68	71

## OPERATIONAL HIGHLIGHTS

### Oil and gas production costs per unit of production

Oil and gas production costs on a barrel of oil equivalent (boe) basis are calculated by dividing oil and gas production costs by the barrel of oil equivalent of hydrocarbons produced during the year.

Oil and gas production costs include only the amounts directly related to the extraction of natural gas, gas condensate and crude oil and exclude processing costs incurred after saleable hydrocarbons are received, such as stable gas condensate processing costs and natural gas liquefaction costs, as well as transportation and other marketing expenses. Oil and gas production costs comprise of lifting costs (materials, services and other expenses, as well as administrative expenses being by nature operating expenses of oil and gas producing activities), taxes other than income tax and depreciation, depletion and amortization which are disclosed in the "Unaudited Supplemental Oil and Gas Disclosures" in the consolidated financial statements.

Natural gas, gas condensate and crude oil volumes produced are converted to a barrel of oil equivalent based on the relative energy content of each fields' hydrocarbons. Natural gas production volumes used for calculation of production costs per boe differ from the volumes presented in the section "Natural gas production volumes" as the former excludes volumes of natural gas consumed in oil and gas production and development activities (see "Basis of presentation" above).



The following tables set forth information with respect to oil and gas production costs on a barrel of oil equivalent basis of our subsidiaries and joint ventures, as well as combined weighted average oil and gas production costs for the Group's subsidiaries and joint ventures for the reporting periods in Russian roubles and US dollars.

RR per boe	Year ended 31 December:		Change %
	2018	2017 <sup>(1)</sup>	
Subsidiaries			
Production costs per boe:			
Lifting costs	47.1	40.1	17.5%
Taxes other than income tax	181.7	148.0	22.8%
Total production costs before DDA per boe	228.8	188.1	21.6%
Depreciation, depletion and amortization	84.6	91.4	(7.4%)
Total production costs of subsidiaries per boe	313.4	279.5	12.1%
Joint ventures			
Production costs per boe:			
Lifting costs	26.3	26.8	(1.9%)
Taxes other than income tax	169.6	202.2	(16.1%)
Total production costs before DDA per boe	195.9	229.0	(14.5%)
Depreciation, depletion and amortization	93.3	102.7	(9.2%)
Total weighted average production costs of joint ventures per boe <sup>(2)</sup>	289.2	331.7	(12.8%)
Subsidiaries and joint ventures			
Production costs per boe:			
Lifting costs	38.5	35.6	8.1%
Taxes other than income tax	176.8	166.6	6.1%
Total production costs before DDA per boe	215.3	202.2	6.5%
Depreciation, depletion and amortization	88.2	95.2	(7.4%)
Total weighted average production costs of subsidiaries and joint ventures per boe <sup>(3)</sup>	303.5	297.4	2.1%

<sup>(1)</sup> Figures for 2017 were recalculated based on the changes made to the presentation of oil and gas production costs (see "Basis of presentation" above).

<sup>(2)</sup> Calculated based on the Group's share in the production of each joint venture.

<sup>(3)</sup> Calculated based on 100% of the Group's subsidiaries production and our share in the production of each joint venture.

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**Management's Discussion and Analysis of Financial Condition and Results of Operations  
for the year ended 31 December 2018**

USD per boe <sup>(2)</sup>	Year ended 31 December:		Change %
	2018	2017 <sup>(1)</sup>	
Subsidiaries			
Production costs per boe:			
Lifting costs	0.75	0.69	8.7%
Taxes other than income tax	2.90	2.54	14.2%
Total production costs before DDA per boe	3.65	3.23	13.0%
Depreciation, depletion and amortization	1.35	1.56	(13.5%)
Total production costs of subsidiaries per boe	5.00	4.79	4.4%
Joint ventures			
Production costs per boe:			
Lifting costs	0.42	0.46	(8.7%)
Taxes other than income tax	2.70	3.47	(22.2%)
Total production costs before DDA per boe	3.12	3.93	(20.6%)
Depreciation, depletion and amortization	1.49	1.75	(14.9%)
Total weighted average production costs of joint ventures per boe <sup>(3)</sup>	4.61	5.68	(18.8%)
Subsidiaries and joint ventures			
Production costs per boe:			
Lifting costs	0.61	0.61	0.0%
Taxes other than income tax	2.82	2.85	(1.1%)
Total production costs before DDA per boe	3.43	3.46	(0.9%)
Depreciation, depletion and amortization	1.41	1.64	(14.0%)
Total weighted average production costs of subsidiaries and joint ventures per boe <sup>(4)</sup>	4.84	5.10	(5.1%)

<sup>(1)</sup> Figures for 2017 were recalculated based on the changes made to the presentation of oil and gas production costs (see "Basis of presentation" above).

<sup>(2)</sup> Production costs in US dollars per boe were translated from Russian roubles amounts using the average exchange rate for the period (see "Selected macro-economic data" above).

<sup>(3)</sup> Calculated based on the Group's share in the production of each joint venture.

<sup>(4)</sup> Calculated based on 100% of the Group's subsidiaries production and our share in the production of each joint venture.

**Hydrocarbon production and sales volumes**

In 2018, our operational results were significantly impacted by the production launch of the first three LNG trains at Yamal LNG (see "Recent developments" above), as well as the acquisitions of new production assets at the end of 2017 and during the first quarter of 2018. As a result, our total natural gas and liquids production increased by 8.5% and by 0.2%, respectively.

In 2018, our total natural gas sales volumes increased by 7,130 mmcm, or 11.0%, primarily due to sales of LNG purchased from our joint venture Yamal LNG to international markets, as well as an increase in volumes sold in the Russian Federation.

In 2018, our liquids sales volumes changed marginally (decreased by 117 thousand tons, or 0.7%).

*Natural gas production volumes*

The following table presents natural gas production of the Group's subsidiaries by major production fields and our proportionate share in natural gas production of joint ventures by entities:

<i>millions of cubic meters if not stated otherwise</i>	<b>Year ended 31 December:</b>		<b>Change %</b>
	<b>2018</b>	<b>2017</b>	
<b>Production by subsidiaries from:</b>			
Yurkharovskoye field	27,745	30,540	(9.2%)
East-Tarkosalinskoye field	6,627	7,379	(10.2%)
Khancheyevskoye field	1,942	2,242	(13.4%)
Yarudeyskoye field	1,500	1,362	10.1%
Beregovoye field	1,204	-	n/a
East-Urengoyskoye + North-Esetinskoye field (West-Yaroyakhinskiy license area)	705	77	n/a
Other fields	2,137	1,513	41.2%
<b>Total natural gas production by subsidiaries <sup>(1)</sup></b>	<b>41,860</b>	<b>43,113</b>	<b>(2.9%)</b>
<b>Group's proportionate share in the production of joint ventures:</b>			
Arcticgas	13,698	13,964	(1.9%)
Yamal LNG <sup>(2)</sup>	8,213	776	n/a
Nortgas	3,789	4,291	(11.7%)
Terneftegas	1,246	1,255	(0.7%)
<b>Total Group's proportionate share in the natural gas production of joint ventures <sup>(1)</sup></b>	<b>26,946</b>	<b>20,286</b>	<b>32.8%</b>
<b>Total natural gas production including proportionate share in the production of joint ventures</b>	<b>68,806</b>	<b>63,399</b>	<b>8.5%</b>
<i>Average daily natural gas production including proportionate share in the production of joint ventures</i>	<i>188.5</i>	<i>173.7</i>	<i>8.5%</i>
<i>The Group's proportionate share in LNG production of joint ventures (thousands of tons) <sup>(2)</sup></i>	<i>5,152</i>	<i>162</i>	<i>n/a</i>

<sup>(1)</sup> Natural gas production includes natural gas volumes consumed in oil and gas production and development activities (primarily, as fuel gas):

in subsidiaries	1,413	1,382	2.2%
in joint ventures (Group's proportionate share)	333	307	8.5%

<sup>(2)</sup> Natural gas and LNG production at Yamal LNG are reported at 60% (see "Basis of presentation" above).

In 2018, our total natural gas production (including our proportionate share in the production of joint ventures) increased by 5,407 mmcm, or 8.5%, to 68,806 mmcm from 63,399 mmcm in 2017. The main factors positively impacting our production growth were the commencement of natural gas production at Yamal LNG resulting from the start of LNG production at the first three LNG trains of the LNG liquefaction plant, as well as the acquisition by the Group of new production assets at the end of 2017 and during the first quarter of 2018 (the Beregovoy, the West-Yaroyakhinskiy and the Syskonsyninskiy license areas). These positive factors allowed us to fully compensate for the decrease in production at mature fields of our subsidiaries (the Yurkharovskoye, the East-Tarkosalinskoye and the Khancheyevskoye fields) and at our joint venture Nortgas, which resulted mainly from natural declines in the reservoir pressure at the current gas producing horizons.

Our proportionate share in the production of Arcticgas decreased by 1.9% as a result of a decrease in the Group's effective participation interest in Arcticgas from 53.3% to 50.0% in March 2018 (see "Recent developments" above). Excluding the effect from the decrease in participation interest, our proportionate share in the production of Arcticgas would have increased by 3.1%.

#### *Natural gas sales volumes*

In 2018, our total natural gas sales volumes increased by 7,130 mmcm, or 11.0%, to 72,134 mmcm from 65,004 mmcm in 2017.

<i>millions of cubic meters</i>	Year ended 31 December:		Change %
	2018	2017	
Production by subsidiaries	41,860	43,113	(2.9%)
Purchases from the Group's joint ventures	24,892	15,297	62.7%
Other purchases	8,119	8,300	(2.2%)
<b>Total production and purchases</b>	<b>74,871</b>	<b>66,710</b>	<b>12.2%</b>
Own usage <sup>(1)</sup>	(1,561)	(1,507)	3.6%
Decrease (increase) in natural gas inventory balance	(1,176)	(199)	n/a
<b>Total natural gas sales volumes</b>	<b>72,134</b>	<b>65,004</b>	<b>11.0%</b>
<i>Sold to end-customers</i>	<i>61,901</i>	<i>61,560</i>	<i>0.6%</i>
<i>Sold ex-field</i>	<i>4,172</i>	<i>3,338</i>	<i>25.0%</i>
<b>Subtotal sold in the Russian Federation</b>	<b>66,073</b>	<b>64,898</b>	<b>1.8%</b>
<b>Sold on international markets</b>	<b>6,061</b>	<b>106</b>	<b>n/a</b>

<sup>(1)</sup> Own usage associated primarily with volumes of natural gas consumed in oil and gas producing and development activities (primarily, as fuel gas), the maintaining of refining process at the Purovsky Plant, and methanol production.

In 2018, natural gas purchases from our joint ventures increased by 9,595 mmcm, or 62.7%, to 24,892 mmcm from 15,297 mmcm in 2017 primarily due to the commencement of purchases of LNG produced by Yamal LNG for subsequent sale on international markets from December 2017, and an increase in purchases of natural gas from Arcticgas in order to fulfill our Russian domestic contractual sales obligations.

Other natural gas purchases 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. In 2018, we purchased from third parties 7,413 mmcm of natural gas on the Russian domestic market, and 706 mmcm of natural gas on international markets. In 2017, we purchased almost all natural gas volumes from third parties on the Russian domestic market.

As of 31 December 2018, our cumulative natural gas inventory balance, mainly representing our inventory balances of natural gas in the UGSF, aggregated 2,209 mmcm and increased by 1,176 mmcm during the year as compared to an increase by 199 mmcm in 2017. Natural gas inventory balances tend to fluctuate period-to-period depending on the Group's demand for natural gas withdrawal from the UGSF for the sale in the subsequent periods.

*Liquids production volumes*

The following table presents liquids production of the Group's subsidiaries by major production fields and our proportionate share in the liquids production of joint ventures by entities:

thousands of tons	Year ended 31 December:		Change %
	2018	2017	
<b>Production by subsidiaries from:</b>			
Yarudeyskoye field	3,439	3,596	(4.4%)
East-Tarkosalinskoye field	1,347	1,291	4.3%
Yurkharovskoye field	1,249	1,489	(16.1%)
Khancheyskoye field	223	274	(18.6%)
Other fields	288	109	164.2%
<b>Total liquids production by subsidiaries</b>			
	<b>6,546</b>	<b>6,759</b>	<b>(3.2%)</b>
<i>including crude oil</i>	<i>4,704</i>	<i>4,779</i>	<i>(1.6%)</i>
<i>including gas condensate</i>	<i>1,842</i>	<i>1,980</i>	<i>(7.0%)</i>
<b>Group's proportionate share in the production of joint ventures:</b>			
Arcticgas	3,999	4,190	(4.6%)
Yamal LNG <sup>(1)</sup>	542	25	n/a
Terneftegas	403	421	(4.3%)
Nortgas	310	379	(18.2%)
<b>Total Group's proportionate share in the liquids production of joint ventures</b>			
	<b>5,254</b>	<b>5,015</b>	<b>4.8%</b>
<b>Total liquids production including proportionate share in the production of joint ventures</b>			
	<b>11,800</b>	<b>11,774</b>	<b>0.2%</b>
<i>Average daily liquids production including proportionate share in the production of joint ventures</i>			
	<i>32.3</i>	<i>32.3</i>	<i>0.2%</i>

<sup>(1)</sup> Production at South-Tambeyskoye field of Yamal LNG is reported at 60% (see "Basis of presentation" above).

In 2018, our total liquids production (including our proportionate share in the production of joint ventures) increased by 26 thousand tons, or 0.2%, to 11,800 thousand tons from 11,774 thousand tons in 2017. The main factors positively impacting our production growth were the commencement of gas condensate production at Yamal LNG at the end of 2017, as well as the acquisition by the Group of new production assets. These positive factors fully compensated for the effect of a decrease in the Group's effective participation interest in Arcticgas from 53.3% to 50.0% in March 2018 (see "Recent developments" above) as well as a decrease in gas condensate production at mature fields of our subsidiaries and joint ventures mainly 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 2018, our total liquids sales volumes decreased marginally by 117 thousand tons, or 0.7%, to 15,822 thousand tons from 15,939 thousand tons in 2017.

<i>thousands of tons</i>	Year ended 31 December:		Change %
	2018	2017	
Production by subsidiaries	6,546	6,759	(3.2%)
Purchases from the Group's joint ventures	9,368	9,315	0.6%
Other purchases	226	173	30.6%
<b>Total production and purchases</b>	<b>16,140</b>	<b>16,247</b>	<b>(0.7%)</b>
Losses <sup>(1)</sup> and own usage <sup>(2)</sup>	(211)	(249)	(15.3%)
Decreases (increases) in liquids inventory balances	(107)	(59)	81.4%
<b>Total liquids sales volumes</b>	<b>15,822</b>	<b>15,939</b>	<b>(0.7%)</b>
<i>Naphtha export</i>	<i>4,185</i>	<i>4,102</i>	<i>2.0%</i>
<i>Other stable gas condensate refined products export</i> <sup>(3)</sup>	<i>2,396</i>	<i>2,524</i>	<i>(5.1%)</i>
<i>Other stable gas condensate refined products domestic</i> <sup>(3)</sup>	<i>102</i>	<i>117</i>	<i>(12.8%)</i>
<b>Subtotal stable gas condensate refined products</b>	<b>6,683</b>	<b>6,743</b>	<b>(0.9%)</b>
<i>Crude oil export</i>	<i>1,549</i>	<i>1,523</i>	<i>1.7%</i>
<i>Crude oil domestic</i>	<i>2,993</i>	<i>3,093</i>	<i>(3.2%)</i>
<b>Subtotal crude oil</b>	<b>4,542</b>	<b>4,616</b>	<b>(1.6%)</b>
<i>LPG export</i>	<i>593</i>	<i>536</i>	<i>10.6%</i>
<i>LPG domestic</i>	<i>2,083</i>	<i>2,112</i>	<i>(1.4%)</i>
<b>Subtotal LPG</b>	<b>2,676</b>	<b>2,648</b>	<b>1.1%</b>
<i>Stable gas condensate export</i>	<i>274</i>	<i>342</i>	<i>(19.9%)</i>
<i>Stable gas condensate domestic</i>	<i>1,634</i>	<i>1,576</i>	<i>3.7%</i>
<b>Subtotal stable gas condensate</b>	<b>1,908</b>	<b>1,918</b>	<b>(0.5%)</b>
<b>Other oil products</b>	<b>13</b>	<b>14</b>	<b>(7.1%)</b>

<sup>(1)</sup> 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.

<sup>(2)</sup> Own usage associated primarily with the maintaining of refining process at the Ust-Luga Complex, as well as bunkering of chartered tankers.

<sup>(3)</sup> Other stable gas condensate refined products include jet fuel, gasoil and fuel oil received from the processing of stable gas condensate at the Ust-Luga Complex.

Our sales volumes of naphtha and other stable gas condensate refined products fluctuate from period-to-period depending on changes in inventory balances, with volumes of the products received from processing at the Ust-Luga Complex staying relatively flat. Our sales volumes of stable gas condensate represent the volumes remaining after we deliver most of our stable gas condensate for further processing to our Ust-Luga Complex, as well as volumes purchased by the Group for subsequent sale on international markets, including purchases from our joint venture Yamal LNG.

In the 2018 reporting period, our liquids inventory balances increased by 107 thousand tons to 1,069 thousand tons as of 31 December 2018 as compared to an increase in inventory balances by 59 thousand tons to 962 thousand tons in 2017. Our liquids inventory balances may vary period-to-period depending on shipping schedules and final destinations (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 year ended 31 December 2018**
**RESULTS OF OPERATIONS FOR THE YEAR ENDED 31 DECEMBER 2018  
COMPARED TO THE YEAR ENDED 31 DECEMBER 2017**

The following table and discussion is a summary of our consolidated results of operations for the years ended 31 December 2018 and 2017. Each line item is also shown as a percentage of our total revenues.

<i>millions of Russian roubles</i>	Year ended 31 December:			
	2018	% of total revenues	2017	% of total revenues
<b>Total revenues <sup>(1)</sup></b>	<b>831,758</b>	<b>100.0%</b>	<b>583,186</b>	<b>100.0%</b>
<i>including:</i>				
natural gas sales	375,198	45.1%	247,663	42.5%
liquids sales	450,563	54.2%	332,156	57.0%
Operating expenses	(603,912)	(72.6%)	(419,859)	(72.0%)
Other operating income (loss)	(2,307)	(0.3%)	424	0.1%
<b>Profit from operations before disposals of interests in joint ventures</b>	<b>225,539</b>	<b>27.1%</b>	<b>163,751</b>	<b>28.1%</b>
Net gain on disposal of interests in joint ventures	1,645	0.2%	-	n/a
<b>Profit from operations</b>	<b>227,184</b>	<b>27.3%</b>	<b>163,751</b>	<b>28.1%</b>
Finance income (expense)	38,608	4.6%	14,658	2.5%
Share of profit (loss) of joint ventures, net of income tax	(37,258)	(4.4%)	22,430	3.8%
<b>Profit before income tax</b>	<b>228,534</b>	<b>27.5%</b>	<b>200,839</b>	<b>34.4%</b>
Total income tax expense	(45,587)	(5.5%)	(34,369)	(5.9%)
<b>Profit</b>	<b>182,947</b>	<b>22.0%</b>	<b>166,470</b>	<b>28.5%</b>
Less: profit (loss) attributable to non-controlling interest	(19,205)	(2.3%)	(10,083)	(1.7%)
<b>Profit attributable to shareholders of PAO NOVATEK</b>	<b>163,742</b>	<b>19.7%</b>	<b>156,387</b>	<b>26.8%</b>
<b>Normalized profit attributable to shareholders of PAO NOVATEK, excluding the effect of foreign exchange gains (losses)</b>	<b>232,930</b>	<b>28.0%</b>	<b>156,166</b>	<b>26.8%</b>

<sup>(1)</sup> 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 2018 and 2017:

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %	Change <sup>(1)</sup>		
	2018	2017		Total	Due to volume <sup>(2)</sup>	Due to price <sup>(3)</sup>
Natural gas sales	375,198	247,663	51.5%	127,535	27,164	100,371
Stable gas condensate refined products sales	238,886	180,394	32.4%	58,492	(1,460)	59,952
<i>Naphtha</i>	149,770	111,979	33.7%	37,791	2,273	35,518
<i>Other refined products</i>	89,116	68,415	30.3%	20,701	(3,732)	24,433
Crude oil sales	106,257	77,102	37.8%	29,155	(1,240)	30,395
Liquefied petroleum gas sales	56,243	40,016	40.6%	16,227	439	15,788
Stable gas condensate sales	48,607	33,993	43.0%	14,614	(180)	14,794
Other products sales	570	651	(12.4%)	(81)	n/a	n/a
<b>Total oil and gas sales</b>	<b>825,761</b>	<b>579,819</b>	<b>42.4%</b>	<b>245,942</b>	<b>n/a</b>	<b>n/a</b>
Other revenues	5,997	3,367	78.1%	2,630	n/a	n/a
<b>Total revenues</b>	<b>831,758</b>	<b>583,186</b>	<b>42.6%</b>	<b>248,572</b>	<b>n/a</b>	<b>n/a</b>

<sup>(1)</sup> The figures reflect the impact of sales volumes and average realized net prices factors on the change in total revenues from hydrocarbons sales in millions of Russian roubles for the respective periods.

<sup>(2)</sup> The amount of the change in total revenues due to sales volumes is calculated for each product category as a product of the average realized net price for the previous reporting period and the change in sales volumes.

<sup>(3)</sup> The amount of the change in total revenues due to average realized net prices is calculated for each product category as a product of the volume sold in the current reporting period and the change in average realized net prices.

*Natural gas sales*

Revenues from natural gas sales represent our revenues from natural gas sales in the Russian Federation (to end-customers and wholesale traders), revenues from LNG sales to international markets, as well as revenues from sales of regasified LNG to customers in Europe.

The commencement of sales of LNG purchased primarily from our joint venture Yamal LNG to international markets from December 2017, as well as increases in sales prices and volumes in the Russian domestic market resulted in an increase in our aggregate average price by 36.5% and sales volumes by 11.0% (see "Natural gas prices" and "Natural gas sales volumes" above). As a result, in 2018, our total revenues from natural gas sales increased by RR 127,535 million, or 51.5%, compared to 2017.

*Stable gas condensate refined products sales*

Stable 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 2018, our revenues from sales of stable gas condensate refined products increased by RR 58,492 million, or 32.4%, to RR 238,886 million from RR 180,394 million in 2017 due to an increase in average realized prices.

In 2018, our revenues from sales of naphtha increased by RR 37,791 million, or 33.7%, as compared to 2017. In the years ended 31 December 2018 and 2017, we exported 4,185 thousand and 4,102 thousand tons of naphtha, respectively, mainly to the APR, and the European and North America markets. We sold naphtha at different delivery terms: CIF, CFR, DAP, DES and FOB. Our average realized net price, excluding export duties, where applicable, increased by RR 8,488 per ton, or 31.1%, to RR 35,789 per ton from RR 27,301 per ton in 2017 (see "Stable gas condensate and refined products, liquefied petroleum gas and crude oil prices" above).



In 2018, our total revenues from sales of jet fuel, gasoil and fuel oil on the domestic and export markets increased by RR 20,701 million, or 30.3%, as compared to 2017. In the years ended 31 December 2018 and 2017, we exported in aggregate 2,396 thousand and 2,524 thousand tons of these products mainly to the European markets, or 95.9% and 95.6% of total sales volumes (on both the domestic and export markets), respectively. The export delivery terms were CIF, DAP, DES, FOB and CFR (only in 2018). Our average realized net price, excluding export duties, where applicable, increased by RR 9,783 per ton, or 37.8%, to RR 35,682 per ton from RR 25,899 per ton in 2017 (see "Stable gas condensate and refined products, liquefied petroleum gas and crude oil prices" above).

#### *Crude oil sales*

In 2018, our revenues from crude oil sales increased by RR 29,155 million, or 37.8%, compared to 2017 due to an increase in average realized prices.

In 2018, we sold 2,993 thousand tons, or 65.9% of our total crude oil sales volumes, domestically as compared to sales of 3,093 thousand tons, or 67.0%, in 2017. The remaining 1,549 thousand tons of crude oil, or 34.1% of our total crude oil sales volumes, in 2018 and 1,523 thousand tons, or 33.0%, in 2017 were sold to the European and the APR markets under FOB and FCA (only in 2017) delivery terms.

Our average realized net price, excluding export duties, where applicable, increased by RR 6,692 per ton, or 40.1%, to RR 23,394 per ton from RR 16,702 per ton in 2017 (see "Stable gas condensate and refined products, liquefied petroleum gas and crude oil prices" above).

#### *Liquefied petroleum gas sales*

In 2018, our revenues from sales of LPG increased by RR 16,227 million, or 40.6%, compared to 2017 primarily due to an increase in average realized prices.

In 2018, we sold 2,083 thousand tons of LPG, or 77.8% of our total LPG sales volumes, on the domestic market compared to sales of 2,112 thousand tons, or 79.8%, in 2017. The remaining 593 thousand tons of LPG, or 22.2% of our total LPG sales volumes, in 2018 and 536 thousand tons, or 20.2%, in 2017 were sold to the European markets (primarily to the Polish market) under free carrier FCA (at terminal points in Poland) delivery terms and also under DAP (at the border of the customer's country) delivery terms in 2017.

Our average realized LPG net price, excluding export and import duties, excise and fuel taxes expense, where applicable, in 2018 increased by RR 5,899 per ton, or 39.0%, to RR 21,015 per ton from RR 15,116 per ton in 2017 (see "Stable gas condensate and refined products, liquefied petroleum gas and crude oil prices" above).

#### *Stable gas condensate sales*

In 2018, our revenues from sales of stable gas condensate increased by RR 14,614 million, or 43.0%, compared to 2017 due to an increase in average realized prices.

In 2018, we sold 1,634 thousand tons of stable gas condensate, or 85.6% of our total stable gas condensate sales volumes, on the domestic market compared to sales of 1,576 thousand tons, or 82.2%, in 2017. The remaining 274 thousand tons of stable gas condensate, or 14.4% of our total stable gas condensate sales volumes, in 2018 were sold to the APR, the Middle East and European markets under CFR and DAF delivery terms compared to sales of 342 thousand tons, or 17.8%, in 2017 to the European markets and the APR under DAP, CIF and CFR delivery terms.

Our average realized net price, excluding export duties, where applicable, increased by RR 7,754 per ton, or 43.8%, to RR 25,473 per ton from RR 17,719 per ton in 2017 (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 2018, our revenues from other products sales decreased by RR 81 million, or 12.4%, to RR 570 million from RR 651 million in 2017.

*Other revenues*

Other revenues include revenue from transportation, geological and geophysical research services, repair and maintenance of energy equipment services, and other services. In 2018, other revenues increased by RR 2,630 million, or 78.1%, to RR 5,997 million from RR 3,367 million in 2017 primarily due to an increase in revenues from tankers transporting third party goods by RR 2,238 million.

**Operating expenses**

In 2018, our total operating expenses increased by RR 184,053 million, or 43.8%, to RR 603,912 million compared to RR 419,859 million in 2017 mainly due to an increase in purchases of natural gas and liquid hydrocarbons as a result of an increase in volumes of natural gas purchased from our joint ventures (in particular, with the commencement of LNG production at the first three LNG trains at Yamal LNG), as well as an increase in the average purchase prices for hydrocarbons (see "Purchases of natural gas and liquid hydrocarbons" below), which in turn allowed us to earn higher revenues from hydrocarbons sales.

<i>millions of Russian roubles</i>	Year ended 31 December:			
	2018	% of total revenues	2017	% of total revenues
Purchases of natural gas and liquid hydrocarbons	319,990	38.5%	161,443	27.7%
Transportation expenses	145,664	17.5%	137,192	23.5%
Taxes other than income tax	58,768	7.1%	49,494	8.5%
Depreciation, depletion and amortization	33,094	4.0%	34,523	5.9%
Materials, services and other	22,675	2.7%	20,768	3.6%
General and administrative expenses	22,282	2.7%	17,170	2.9%
Exploration expenses	7,012	0.8%	1,819	0.3%
Impairment expenses (reversals), net	287	n/a	52	n/a
Changes in natural gas, liquid hydrocarbons and work-in-progress	(5,860)	n/a	(2,602)	n/a
<b>Total operating expenses</b>	<b>603,912</b>	<b>72.6%</b>	<b>419,859</b>	<b>72.0%</b>

*Purchases of natural gas and liquid hydrocarbons*

In 2018, our purchases of natural gas and liquid hydrocarbons increased significantly by RR 158,547 million, or 98.2%, to RR 319,990 million from RR 161,443 million in 2017.

<i>millions of Russian roubles</i>	Year ended 31 December:		Change
	2018	2017	%
Unstable gas condensate	155,360	107,082	45.1%
Natural gas	150,811	51,053	195.4%
Other hydrocarbons	13,819	3,308	317.7%
<b>Total purchases of natural gas and liquid hydrocarbons</b>	<b>319,990</b>	<b>161,443</b>	<b>98.2%</b>

In 2018, our purchases of unstable gas condensate from our joint ventures increased by RR 48,278 million, or 45.1%, as compared to 2017 due to an increase in purchase prices, which are impacted by international crude oil prices excluding export duties (see "Selected macro-economic data" above).

In 2018, our purchases of natural gas increased by RR 99,758 million, or 195.4%, as compared to 2017 mainly due to the commencement of LNG purchases from Yamal LNG for subsequent sale on international markets from December 2017, as well as an increase in volumes of natural gas purchased from Arcticgas in order to fulfill our contractual sales obligations on the domestic market. In addition, our purchases of natural gas increased due to an increase in purchase prices on the domestic market that are influenced by the regulated natural gas prices (see "Natural gas prices" above).

Other hydrocarbons purchases represent our purchases of oil products, LPG, stable gas condensate and crude oil for subsequent resale depending on the demand for these types of products. In 2018, our purchases of other hydrocarbons increased by RR 10,511 million, or 317.7%, as compared to 2017 mainly due to purchases of stable gas condensate from Yamal LNG for subsequent sale on international markets, as well as an increase in prices and volumes of LPG purchases for subsequent small volume wholesale and retail sales.

*Transportation expenses*

In 2018, our total transportation expenses increased by RR 8,472 million, or 6.2%, to RR 145,664 million as compared to RR 137,192 million in 2017.

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2018	2017	
Natural gas transportation			
by trunk and low-pressure pipelines	96,146	93,686	2.6%
Stable gas condensate and			
liquefied petroleum gas transportation by rail	30,643	29,832	2.7%
Stable gas condensate and refined products,			
crude oil and liquefied natural gas transportation by tankers	10,145	5,980	69.6%
Crude oil transportation by trunk pipelines	8,557	7,622	12.3%
Other	173	72	140.3%
<b>Total transportation expenses</b>	<b>145,664</b>	<b>137,192</b>	<b>6.2%</b>

In 2018, our expenses for natural gas transportation by trunk and low-pressure pipelines increased by RR 2,460 million, or 2.6%, to RR 96,146 million from RR 93,686 million in 2017 mainly due to an increase in the proportion of sales to our end-customers located at more distant regions from our production fields in the current reporting period as compared to the previous year.

In 2018, our total expenses for stable gas condensate and LPG transportation by rail increased by RR 811 million, or 2.7%, to RR 30,643 million from RR 29,832 million in 2017. The increase was due to a 6.5% increase in weighted average transportation cost per unit mainly resulted from a 5.4% increase in the regulated railroad transportation tariffs effective January 2018 (see "Transportation tariffs" above). The impact of this factor was partially offset by a 3.6% decrease in volumes of liquids sold and transported via rail.

In 2018, our total transportation expenses for hydrocarbons delivered by tankers to international markets increased by RR 4,165 million, or 69.6%, to RR 10,145 million from RR 5,980 million in 2017 primarily due to the commencement of sales of LNG purchased mainly from Yamal LNG to international markets from December 2017, as well as a 7.5% depreciation of the average exchange rate of the Russian rouble relative to the US dollar (since all our tankers transportation expenses are US dollar denominated).

In 2018, our expenses for crude oil transportation to customers by trunk pipeline increased by RR 935 million, or 12.3%, to RR 8,557 million from RR 7,622 million in 2017. The increase was due to an increase in the proportion of crude oil sales to more distant regions from our production fields, as well as a 3.9% increase in the regulated transportation tariffs effective 1 January 2018 (see "Transportation tariffs" above).

*Taxes other than income tax*

In 2018, taxes other than income tax increased by RR 9,274 million, or 18.7%, to RR 58,768 million from RR 49,494 million in 2017 primarily due to an increase in unified natural resources production tax expense.

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2018	2017	
Unified natural resources production tax (UPT)	54,644	45,459	20.2%
Property tax	3,595	3,673	(2.1%)
Other taxes	529	362	46.1%
<b>Total taxes other than income tax</b>	<b>58,768</b>	<b>49,494</b>	<b>18.7%</b>

In 2018, our unified natural resources production tax expense increased by RR 9,185 million, or 20.2%, to RR 54,644 million from RR 45,459 million in 2017 mainly due to an increase in UPT rates for crude oil and natural gas as a result of an increase in benchmark crude oil prices, as well as due to changes in the formula for crude oil UPT rate calculation effective 1 January 2018 (see "Our tax burden and obligatory payments" above).

*Depreciation, depletion and amortization*

In 2018, our depreciation, depletion and amortization ("DDA") expense decreased by RR 1,429 million, or 4.1%, to RR 33,094 million from RR 34,523 million in 2017 primarily due to an increase in proved reserves. This effect was partially offset as a result of consolidating new production assets at the end of 2017 and in the first quarter of 2018.

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 2018, our materials, services and other expenses increased by RR 1,907 million, or 9.2%, to RR 22,675 million compared to RR 20,768 million in 2017.

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2018	2017	
Employee compensation	9,815	9,032	8.7%
Repair and maintenance	2,948	2,853	3.3%
Complex of services for preparation, transportation and processing of hydrocarbons	2,009	1,914	5.0%
Materials and supplies	1,963	1,966	(0.2%)
Electricity and fuel	1,311	1,221	7.4%
Liquefied petroleum gas volumes reservation expenses	1,155	918	25.8%
Fire safety and security expenses	976	749	30.3%
Transportation services	822	727	13.1%
Rent expenses	416	308	35.1%
Insurance expense	340	307	10.7%
Other	920	773	19.0%
<b>Total materials, services and other</b>	<b>22,675</b>	<b>20,768</b>	<b>9.2%</b>

Employee compensation relating to operating personnel increased by RR 783 million, or 8.7%, to RR 9,815 million compared to RR 9,032 million in 2017 due to the acquisition of new production assets at the end of 2017 and in the first quarter of 2018, an indexation of base salaries effective from 1 July 2018 and the related increase in social contributions for medical and social insurance and to the Pension Fund.

Repair and maintenance services expenses, electricity and fuel, fire safety and security, and transportation services expenses increased mainly due to the acquisition of new production assets at the end of 2017 and in the first quarter of 2018.

Complex of services for preparation, transportation and processing of hydrocarbons expenses mainly relate to transportation of our NGL produced at the Purovsky Plant for further processing at the Tobolsk Refining Facilities. These expenses increased by RR 95 million, or 5.0%, to RR 2,009 million compared to RR 1,914 million in 2017 primarily due to an increase in the contract rate for services at the Tobolsk Refining Facilities from the beginning of 2018.

In 2018, liquefied petroleum gas volumes reservation costs increased by RR 237 million, or 25.8%, to RR 1,155 million from RR 918 million in 2017 due to an increase in LPG volumes sold through our subsidiary in Poland and a 12.1% depreciation of the average exchange rate of the Russian rouble relative to the Polish zloty, 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.

Other items of our materials, services and other expenses changed marginally.

*General and administrative expenses*

In 2018, our general and administrative expenses increased by RR 5,112 million, or 29.8%, to RR 22,282 million compared to RR 17,170 million in 2017.

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2018	2017	
Employee compensation	15,807	11,065	42.9%
Social expenses and compensatory payments	2,484	2,735	(9.2%)
Legal, audit and consulting services	1,122	839	33.7%
Business travel expense	621	560	10.9%
Fire safety and security expenses	471	419	12.4%
Advertising expenses	465	410	13.4%
Repair and maintenance expenses	229	231	(0.9%)
Rent expense	176	90	95.6%
Other	907	821	10.5%
<b>Total general and administrative expenses</b>	<b>22,282</b>	<b>17,170</b>	<b>29.8%</b>

Employee compensation relating to administrative personnel increased by RR 4,742 million, or 42.9%, to RR 15,807 million in 2018 from RR 11,065 million in 2017 due to an increase in accrued provision for bonuses to key management, an indexation of base salaries effective from 1 July 2018 and the related increase in social contributions for medical and social insurance and to the Pension Fund, as well as the acquisition of new assets at the end of 2017 and in the first quarter of 2018.

In 2018, our social expenses and compensatory payments amounted to RR 2,484 million compared to RR 2,735 million in 2017. In 2018 and 2017, we made compensatory payments, which mainly related to the development of the Yarudeyskoye field in both reporting periods, and also the Salmanovskoye (Utrenneye) field in 2018, and amounted to RR 673 million and RR 1,466 million, respectively. We also incur social expenses, which in both periods related 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.

In 2018, legal, audit, and consulting services expenses increased by RR 283 million, or 33.7%, to RR 1,122 million compared to RR 839 million in 2017 primarily due to an increase in information services related to the expansion of the Group's activities.

Other items of our general and administrative expenses changed marginally.

*Exploration expenses*

In 2018, our exploration expenses significantly increased by RR 5,193 million, or 285.5%, to RR 7,012 million from RR 1,819 million in 2017 mainly due to an increase in exploration works performed at the Shtormovoy, the Verhnetiuteyskiy and the West-Seyakhinskiy, the Gydanskiy, the North-Obskiy, the North-Russkiy, the North-Tanamskiy and the West-Solpatinskiy license areas.

The increase in exploration works will ensure timely preparation of reserves at our promising fields for development and further progress of the Group's hydrocarbons production projects in line with our long-term strategy. 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 science and technology center associated with the exploration activities at our fields. Exploration expenses fluctuate period-to-period in accordance with the approved exploration work schedule at our production subsidiaries.

*Impairment expenses*

In 2018 and 2017, we recognized net impairment expenses of RR 287 million and RR 52 million, respectively, which in both periods related to impairments of trade accounts receivables.

*Changes in natural gas, liquid hydrocarbons and work-in-progress*

In the years ended 31 December 2018 and 2017, we recorded reversals of RR 5,860 million and RR 2,602 million, respectively, to changes in inventory expense due to increases in our natural gas and stable gas condensate refined products inventory balances, as well as an increase in the cost of hydrocarbons purchases in both reporting periods as a result of an increase in benchmark crude oil prices.

In the years ended 31 December 2018 and 2017, our cumulative natural gas inventory balance representing mainly our inventory balances of natural gas in the Underground Gas Storage Facilities ("UGSF") increased by 1,176 mmcm and 199 mmcm, respectively. Natural gas inventory balances tend to fluctuate period-to-period depending on the Group's demand for natural gas withdrawals for the sale in the subsequent periods.

In 2018, our cumulative liquid hydrocarbons inventory balances, recognized as inventory in transit or in storage, increased by 107 thousand tons mainly due to an increase in inventory balance of stable gas condensate refined products in storage at our Ust-Luga Complex. In 2017, our cumulative liquid hydrocarbons inventory balances increased by 59 thousand tons mainly due to an increase in inventory balance of naphtha in tankers in transit not realized at the reporting date. 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>	2018			2017		
	At 31 December	At 1 January	Increase / (decrease)	At 31 December	At 1 January	Increase / (decrease)
<b>Natural gas (millions of cubic meters)</b>	<b>2,209</b>	<b>1,033</b>	<b>1,176</b>	<b>1,033</b>	<b>834</b>	<b>199</b>
<i>incl. Gazprom's UGSF</i>	<i>2,106</i>	<i>870</i>	<i>1,236</i>	<i>870</i>	<i>787</i>	<i>83</i>
<b>Liquid hydrocarbons (thousand tons)</b>	<b>1,069</b>	<b>962</b>	<b>107</b>	<b>962</b>	<b>903</b>	<b>59</b>
<i>incl. stable gas condensate</i>						
<i>refined products</i>	<i>578</i>	<i>464</i>	<i>114</i>	<i>464</i>	<i>395</i>	<i>69</i>
<i>stable gas condensate</i>	<i>276</i>	<i>290</i>	<i>(14)</i>	<i>290</i>	<i>307</i>	<i>(17)</i>
<i>crude oil</i>	<i>109</i>	<i>103</i>	<i>6</i>	<i>103</i>	<i>105</i>	<i>(2)</i>

**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 2018, we recognized other operating loss of RR 2,307 million compared to other operating income of RR 424 million in 2017.

In 2018, we purchased and sold approximately 7.0 bcm of natural gas, as well as various derivative commodity instruments within our trading activities, and recognized the aggregate realized loss from trading activities of RR 2,278 million as compared to RR 289 million of income in 2017. At the same time, we recognized a non-cash loss of RR 450 million in 2018 as a result of a decrease in the fair value of the aforementioned contracts as compared to RR nine million of non-cash loss in 2017. The effect of the change in fair value of the commodity contracts fluctuate from period to period depending on the forecast prices for hydrocarbons on international markets and other macroeconomic parameters and may or may not reflect actual future cash flows from trading activities.

**Net gain on disposal of interests in joint ventures**

In the first quarter of 2018, the Group and PAO Gazprom Neft completed the final stage of the previously commenced restructuring procedures to achieve parity shareholdings in our joint venture AO Arcticgas (see "Recent developments" above). As a result, the Group's participation interest in Arcticgas decreased from 53.3% to 50.0%, and the Group recognized a gain on the disposal of the 3.3% participation interest in Arcticgas in the amount of RR 1,645 million.

**Profit from operations and EBITDA**

In 2018, our profit from operations and EBITDA including our proportionate share of joint ventures increased due to the commencement of LNG production at the first three LNG trains at Yamal LNG (see "Recent developments" above), an increase in natural gas sales volumes in the Russian domestic market, and an increase in average realized liquid hydrocarbons and natural gas prices.

Our aggregate EBITDA including our proportionate share of joint ventures, but excluding the effect from the disposal of interests in joint ventures, increased to RR 415,296 million from RR 256,464 million in 2017. Our cumulative profit from operations including our proportionate share of joint ventures, but excluding the effect from the disposal of interests in joint ventures, amounted to RR 349,750 million as compared to RR 203,605 million in 2017, including profit from operations of our subsidiaries in the amount of RR 225,539 million and RR 163,751 million, respectively.

**Finance income (expense)**

In 2018, we recorded net finance income of RR 38,608 million compared to RR 14,658 million in 2017.

<i>millions of Russian roubles</i>	<b>Year ended 31 December:</b>		<b>Change %</b>
	<b>2018</b>	<b>2017</b>	
Accrued interest expense on loans received	(8,702)	(10,235)	(15.0%)
Less: capitalized interest	5,032	3,391	48.4%
Provisions for asset retirement obligations:			
effect of the present value discount unwinding	(602)	(749)	(19.6%)
Interest expense on lease liabilities	(474)	(119)	298.3%
<b>Interest expense</b>	<b>(4,746)</b>	<b>(7,712)</b>	<b>(38.5%)</b>
Interest income	14,003	15,872	(11.8%)
Change in fair value of non-commodity financial instruments	3,492	(7,178)	n/a
Foreign exchange gain (loss), net	25,859	13,676	89.1%
<b>Total finance income (expense)</b>	<b>38,608</b>	<b>14,658</b>	<b>163.4%</b>

In 2018, our interest expense decreased by RR 2,966 million, or 38.5%, to RR 4,746 million primarily due to repayments of the Group's borrowings, as well as an increase in the amount of capitalised interest costs on borrowings as a result of the increased volume of capital expenditures and assets under construction.

Interest income decreased by RR 1,869 million, or 11.8%, to RR 14,003 million in 2018 from RR 15,872 million in 2017. In both reporting periods, interest income primarily related to loans provided to our joint ventures for the development and expansion of their activities. According to IFRS 9 "*Financial instruments*", the Group accounts for the most of these loans as at fair value through profit or loss with a portion of changes in fair value relating to interest income (calculated based on the amortised cost of the loans using the effective interest method) presented separately from other factors of changes in fair value (such as changes in interest rates and expected maturities).

In 2018, we recognized a non-cash gain of RR 3,492 million compared to a non-cash loss of RR 7,178 million in 2017 due to the remeasurement of the shareholders' loans issued by the Group to our joint ventures in accordance with IFRS 9 "*Financial instruments*". 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 2018, we recorded a net foreign exchange gain of RR 25,859 million compared to RR 13,676 million in 2017 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 2018, the Group's proportionate share of loss of joint ventures amounted to RR 37,258 million as compared to the share of profit of joint ventures in the amount of RR 22,430 million in 2017.

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2018	2017	
<b>Share in profit from operations</b>	<b>124,211</b>	<b>39,854</b>	<b>211.7%</b>
<b>Share in finance income (expense)</b>			
Share in interest income (expense), net	(35,900)	(10,805)	232.3%
Share in foreign exchange gain (loss), net	(109,663)	(12,828)	n/a
Share in change in fair value of non-commodity financial instruments	(15,273)	13,336	n/a
<b>Total share in finance income (expense)</b>	<b>(160,836)</b>	<b>(10,297)</b>	<b>n/a</b>
Share in total income tax benefit (expense)	(633)	(7,127)	(91.1%)
<b>Total share of profit (loss) of joint ventures, net of income tax</b>	<b>(37,258)</b>	<b>22,430</b>	<b>n/a</b>

Our proportionate share in the profit from operations of our joint ventures significantly increased by RR 84,357 million, or approximately three-fold, mainly due to the production launch at the first three LNG trains at Yamal LNG, as well as an increase in revenues from liquid hydrocarbons sales in our joint ventures as a result of higher average realized prices.

In 2018, our proportionate share in the finance expense of our joint ventures significantly increased by RR 150,539 million compared to 2017.

The main factor impacting the increase in our share in finance expense was the recognition of a significant non-cash foreign exchange loss in the current year (our share amounted to RR 109.7 billion compared to our share of RR 12.8 billion in the previous year) primarily related to the revaluation of foreign currency denominated loans in our joint venture Yamal LNG. We assess that the impact of foreign currency risk relating to the debt portfolio of Yamal LNG is to a large extent mitigated by the fact that all of its products are delivered to international markets and its revenues are denominated in foreign currencies.

In addition, our share in interest expense increased by RR 25.1 billion mainly due to the commencement of LNG production at Yamal LNG and ceasing capitalizing the respective interest expense.

The remaining change related to the recognition of a non-cash loss from the remeasurement of the fair value of shareholders' loans in Yamal LNG and Terneftegas (our share amounted to RR 15.3 billion) in the current year as compared to the recognition of a non-cash gain (our share amounted to RR 13.3 billion) in 2017.

**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 the joint ventures in which it holds at least a 50% interest is subject to a zero withholding tax rate according to the Russian tax legislation, and also does not result in a tax charge.

Without the effect of net profit (loss) and dividends from joint ventures, the effective income tax rate (total income tax expense calculated as a percentage of profit before income tax) in 2018 and 2017, was 17.3% and 19.3%, respectively.

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for the year ended 31 December 2018****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 7,355 million, or 4.7%, to RR 163,742 million in 2018 compared to RR 156,387 million in 2017. In 2018, the Group's profit was significantly impacted by the recognition of substantial non-cash foreign exchange effect on foreign currency denominated loans of the Group and its joint ventures (in 2017, foreign exchange effect was less significant). Excluding the effect of foreign exchange gains (losses), as well as the one-time effect from the disposal of interests in joint ventures, our profit attributable to shareholders of PAO NOVATEK increased by RR 76,764 million, or 49.2%, and amounted to RR 232,930 million in 2018 compared to RR 156,166 million in 2017 (see the table below):

<i>millions of Russian roubles</i>	<b>Year ended 31 December:</b>		<b>Change %</b>
	<b>2018</b>	<b>2017</b>	
Profit attributable to shareholders of PAO NOVATEK	163,742	156,387	4.7%
Net gain on disposal of interests in joint ventures	(1,645)	-	n/a
<b>Normalized profit attributable to shareholders of PAO NOVATEK</b>	<b>162,097</b>	<b>156,387</b>	<b>3.7%</b>
Foreign exchange (gains) losses	(25,859)	(13,676)	89.1%
Income tax expense (benefit) relating to foreign exchange (gains) losses	5,172	2,735	89.1%
Share of foreign exchange (gains) losses of joint ventures	109,663	12,828	n/a
Share of income tax expense (benefit) relating to foreign exchange (gains) losses of joint ventures	(18,143)	(2,108)	n/a
<b>Normalized profit attributable to shareholders of PAO NOVATEK, excluding the effect of foreign exchange gains (losses)</b>	<b>232,930</b>	<b>156,166</b>	<b>49.2%</b>

Our weighted average basic and diluted earnings per share, calculated from the profit attributable to shareholders of PAO NOVATEK increased by RR 2.48 per share, or 4.8%, to RR 54.33 per share in 2018 from RR 51.85 per share in 2017. Excluding the effects of foreign exchange gains (losses) and the disposal of interests in joint ventures, our weighted average basic and diluted earnings per share increased by RR 25.51, or 49.3%, to RR 77.29 per share in 2018 from RR 51.78 per share in 2017.

## 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 2018 and 2017:

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2018	2017	
Net cash provided by <b>operating</b> activities	216,349	180,399	19.9%
Net cash used for <b>investing</b> activities	(153,046)	(58,275)	162.6%
Net cash used for <b>financing</b> activities	(93,658)	(103,837)	(9.8%)

*Net cash provided by operating activities*

Our net cash provided by operating activities increased by RR 35,950 million, or 19.9%, to RR 216,349 million compared to RR 180,399 million in 2017 primarily due to an increase in profit from operations before disposals of interests in joint ventures adjusted for non-cash items, net of related income tax, as well as an increase in dividends received from our joint ventures. These effects were partially offset by changes in working capital, which vary period-to-period depending on various factors.

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2018	2017	
Profit from operations before disposals of interests in joint ventures	225,539	163,751	37.7%
Non-cash adjustments <sup>(1)</sup>	34,580	35,129	(1.6%)
Changes in working capital and long-term advances given	(6,454)	5,816	n/a
Dividends received from joint ventures	8,500	2,383	256.7%
Interest received	1,311	5,949	(78.0%)
Income taxes paid	(47,127)	(32,629)	44.4%
<b>Total net cash provided by operating activities</b>	<b>216,349</b>	<b>180,399</b>	<b>19.9%</b>

<sup>(1)</sup> Include adjustments for depreciation, depletion and amortization, net impairment expenses (reversals), change in fair value of non-commodity financial instruments and some other adjustments.

Profit from operations before disposals of interests in joint ventures adjusted for non-cash items increased due to the production launch at the first three LNG trains at Yamal LNG, an increase in natural gas sales volumes in the Russian domestic market, and an increase in average realized liquid hydrocarbons and natural gas prices (see "Profit from operations and EBITDA" above).

In 2018 and 2017, we received RR 8,500 million and RR 2,383 million of dividends, respectively, from our joint venture Nortgas.

*Net cash used for investing activities*

In 2018, our net cash used for investing activities increased by RR 94,771 million, or 162.6%, to RR 153,046 million compared to RR 58,275 million in 2017.

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2018	2017	
Cash used for capital expenditures	(94,038)	(29,871)	214.8%
Payments for acquisition of subsidiaries net of cash acquired	(30,492)	(15,706)	94.1%
Net decrease (increase) in bank deposits			
with original maturity more than three months	(26,161)	-	n/a
Payments for mineral licenses	(327)	(9,786)	(96.7%)
Loans provided to joint ventures	(3,429)	(5,211)	(34.2%)
Repayments of loans provided to joint ventures	1,573	8,246	(80.9%)
Proceeds from disposals of property, plant and equipment and materials for construction	2,133	-	n/a
Acquisition of joint ventures	(2)	(1,583)	(99.9%)
Additional capital contributions to joint ventures	-	(2,269)	n/a
Other	(2,303)	(2,095)	9.9%
<b>Net cash used for investing activities</b>	<b>(153,046)</b>	<b>(58,275)</b>	<b>162.6%</b>

Cash used for capital expenditures increased by RR 64,167 million, or three-fold, as compared to 2017 primarily due to investments in our LNG projects, the ongoing development of the North-Russkiy and the East-Tazovskiy fields, as well as exploration drilling at the North-Obskiy license area. In addition, our capital expenditures in both reporting periods related to ongoing development of crude oil deposits at the East-Tarkosalinskoye and the Yarudeyskoye fields (see "Capital expenditures" below).

In 2018, the Group acquired 100% participation interests in AO Geotransgas, OOO Urengoyetskaya gasovaya kompaniya and OOO Chernichnoye for RR 30,492 million net of cash acquired (see "Recent developments" above). In 2017, we acquired 100% participation interests in OOO Severneft-Urengoy, AO Eurotek and AO South-Khadyryakhinskoye for RR 15,706 million net of cash acquired.

The Group's cash management involves periodic cash placement on bank deposits with different maturities. Deposits are reported in "Cash and cash equivalents" if opened for three months or less, or otherwise in "Short-term bank deposits with original maturity more than three months". Transactions with bank deposits with original maturity more than three months are classified as investing activities in the Consolidated Statement of Cash Flows. In 2018, the net increase in bank deposits with original maturity more than three months amounted to approximately RR 26 billion.

In 2018, we made a one-time payment fee to expand the borders of our Salmanovskiy (Utrenniy) license area in the amount of RR 167 million and paid RR 66 million for the acquisition of a license to use the Payutskiy license area. In addition, we paid RR 35 million for participation in the auction for the right to use the South-Leskinskiy license area (according to the results of the auction, the license fee payment was set at RR 2,041 million). In 2017, we paid RR 9,727 million for the acquisition of the right to use the Gydanskoye, the Shtormovoye, the Verhnetiuteyskoye and the West-Seyakhinskoye license areas. In addition, in both periods, we paid a part of a one-time payment fee for the exploration and production license for our discovered Kharbeyskoye field in the amount of RR 59 million.

In 2018, we provided loans to our joint venture Yamal LNG in the aggregate amount of RR 3,243 million for financing the construction of the fourth LNG train. In addition, in 2018 and 2017, we provided loans to our joint venture Cryogas-Vysotsk in the amount of RR 186 million and RR 5,211 million, respectively. At the same time, in the years ended 31 December 2018 and 2017, we received RR 1,573 million and RR 8,246 million, respectively, due to partial repayments of the loans provided to Terneftegas and Yamal Development (only in 2017).

In 2018, we received RR 2,133 million from disposals of property, plant and equipment and materials for construction, which primarily related to the assignment of rights to our joint venture Yamal LNG under concluded contracts for design and equipment production for the fourth LNG train, as well as materials purchased for this purpose.

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In 2017, the Group acquired a 51% ownership interest in OOO Cryogas-Vysotsk for RR 1,583 million and made a capital contribution to it in the amount of RR 2,269 million.

*Net cash used for financing activities*

In 2018, our net cash used for financing activities decreased by RR 10,179 million, or 9.8%, to RR 93,658 million as compared to RR 103,837 million in the corresponding period in 2017.

<i>millions of Russian roubles</i>	<b>Year ended 31 December:</b>		<b>Change %</b>
	<b>2018</b>	<b>2017</b>	
Proceeds from (repayments of) long-term debt, net	(14,107)	(53,035)	(73.4%)
Proceeds from (repayments of) short-term debt, net	(150)	(192)	(21.9%)
Dividends paid to shareholders of PAO NOVATEK	(51,980)	(42,075)	23.5%
Dividends paid to non-controlling interest	(20,068)	-	n/a
Interest on debt paid	(3,024)	(6,526)	(53.7%)
Purchase of treasury shares	(2,137)	(1,442)	48.2%
Payments of lease liabilities	(2,192)	(567)	286.6%
<b>Net cash used for financing activities</b>	<b>(93,658)</b>	<b>(103,837)</b>	<b>(9.8%)</b>

In 2018, the Group fully repaid a loan obtained under our syndicated credit line facility in the amount of RR 12,966 million (USD 231 million), as well as a loan obtained by a Group subsidiary from its non-controlling shareholder. In 2017, the Group partially repaid a loan obtained under our syndicated credit line facility in the amount of RR 26,736 million (USD 462 million) according to the loan's maturity schedule, fully repaid the four-year Russian rouble denominated Eurobonds in the amount of RR 14 billion, as well as partially repaid a loan obtained by a Group subsidiary from its non-controlling shareholder.

In both periods, the total amount of short-term loans repayments substantially corresponded to the amount of proceeds and mainly related to operations with short-term loans to finance trade activities.

The remaining change related primarily to dividends paid, the repayment of interest on borrowings and loans and shares buy-back.

**Liquidity and working capital**

The following table shows the Group's liquidity and credit measures as of 31 December 2018 and 2017:

	31 December 2018	31 December 2017	Change, %
<b>Absolute amounts, RR million</b>			
Net debt <sup>(1)</sup>	102,903	89,807	14.6%
Net working capital position <sup>(2)</sup>	186,297	69,478	168.1%
<b>Liquidity and credit ratios</b>			
Current ratio <sup>(3)</sup>	2.74	1.83	49.7%
Total debt to total equity	0.19	0.20	(5.0%)
Long-term debt to long-term debt and total equity	0.16	0.15	6.7%
Net debt to total capitalization <sup>(4)</sup>	0.09	0.09	0.0%
Net debt to normalized EBITDA from subsidiaries <sup>(5)</sup>	0.40	0.45	(11.1%)
Interest coverage ratio <sup>(6)</sup>	30	19	57.9%

<sup>(1)</sup> Net debt represents total debt less cash, cash equivalents and bank deposits with original maturity more than three months.

<sup>(2)</sup> Net working capital position represents current assets less current liabilities.

<sup>(3)</sup> Current ratio is calculated as current assets divided by current liabilities.

<sup>(4)</sup> Total capitalization represents total debt, total equity and deferred income tax liability.

<sup>(5)</sup> 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.

<sup>(6)</sup> Interest coverage ratio is calculated as normalized EBITDA from subsidiaries divided by accrued interest on debt, including capitalized interest.

In each quarter of 2017 and 2018, the Group demonstrated high operating results and achieved 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 both reporting periods, 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:	
	2018	2017
Arctic LNG 2 project	22,729	8,593
North-Russkiy and East-Tazovskiy license areas	17,602	2,679
Infrastructure for future LNG projects <sup>(1)</sup>	16,421	2,641
East-Tarkosalinskoye field	6,820	4,215
Yarudeyskoye field	4,693	4,489
Yurkharovskoye field	4,215	1,800
North-Obsskiy license area	3,330	1,281
West-Yurkharovskoye field	2,961	914
Gydanskiy license area	2,303	282
Ust-Luga Complex	1,477	223
Beregovoye field	1,400	-
Geofizicheskoye field	914	256
Ust-Yamsoveyskiy license area	846	-
Dorogovskoye field	770	22
Verhnetiuteyskoye and West-Seyakhinskoye fields	662	82
Nyakhartinskiy license area	642	36
West-Yaroyakhinskiy license area	578	23
Office buildings	3,093	1,046
Other	4,280	1,837
<b>Capital expenditures</b>	<b>95,736</b>	<b>30,419</b>

<sup>(1)</sup> Includes, among others, the project for the construction of a center to build and fabricate large-scale marine facilities located in the Murmansk region.

Total capital expenditures on property, plant and equipment in 2018 significantly increased by RR 65,317 million, or 214.7%, to RR 95,736 million from RR 30,419 million. In both reporting periods, a significant part of our capital expenditures related to the development of our LNG projects: the Arctic LNG 2 project and the project for the construction of a center to build and fabricate large-scale marine facilities located in the Murmansk region. In this regard, we continued to invest in the development of the Salmanovskoye (Utrenneye) field and the development of the front-end engineering design (FEED) for the Arctic LNG 2 plant, as well as continued constructing our center in the Murmansk region (constructing buildings and facilities foundations for gravity-based platforms construction site and concrete plant, building berths and other works).

In both reporting periods, we also continued ongoing development of the Yarudeyskoye and the East-Tarkosalinskoye field's crude oil deposits. In the current reporting period, we significantly increased our capital expenditures related to the ongoing development activities at the North-Russkiy and the East-Tazovskiy fields, as well as exploration drilling at the North-Obsskiy and the Gydanskiy license areas. In addition, in 2018, we invested in the project for construction of a hydrocracker unit at our Ust-Luga Complex, which will allow us to increase the depth of processing of stable gas condensate and output of light oil products.

The "Office buildings" line in the table above represents our capital expenditures related to construction of our new office buildings in Moscow and Novy Urengoy.

The "Other" line 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 or processing facilities takes place upon the completion of the fixed assets construction stages and depends on the approved fixed assets launch schedule.

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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 expenditures:

<i>millions of Russian roubles</i>	Year ended 31 December:		Change %
	2018	2017	
<b>Total additions to property, plant and equipment per Note "Property, plant and equipment" in the Group's IFRS Consolidated Financial Statements</b>	<b>98,484</b>	<b>48,064</b>	<b>104.9%</b>
Less: acquisition of mineral licenses	(268)	(10,022)	(97.3%)
Less: right-of-use assets <sup>(1)</sup> additions	(2,480)	(7,623)	(67.5%)
<b>Capital expenditures</b>	<b>95,736</b>	<b>30,419</b>	<b>214.7%</b>
Add (less): change in accounts payable, capitalized foreign exchange losses and other non-cash adjustments	(1,698)	(548)	209.9%
<b>Cash used for capital expenditures <sup>(2)</sup></b>	<b>94,038</b>	<b>29,871</b>	<b>214.8%</b>

<sup>(1)</sup> Related mainly to long-term agreements on time chartering of marine tankers.

<sup>(2)</sup> 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 and joint ventures.

In 2018, the Group won auctions for geological research works, exploration and hydrocarbons production at the Payutskiy and the South-Leskinskiy license areas and paid in the aggregate RR 101 million. In addition, we paid a one-time fee in the amount of RR 167 million to expand the borders of the Salmanovskiy (Utrenniy) license area (see "Net cash used for investing activities" above).

In 2017, the Group won auctions for geological research works, exploration and hydrocarbons production at license areas, which include the Gydanskoye, the Shtormovoye, the Verhnetiuteyskoye and the West-Seyakhinskoye fields and paid in the aggregate RR 9,727 million. In addition, in the "acquisition of mineral licenses" line in the table above we recognized RR 295 million related to the stated one-time payment fee for the exploration and production license for our discovered Kharbeyskoye field.



**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 and the Euro. As of 31 December 2018, the total amount of our debt denominated in foreign currency was RR 171,156 million, or 99.4% of our total borrowings at that date. Changes in the value of the Russian rouble relative to foreign currencies will impact the value in Russian rouble terms of our foreign currency-denominated costs, debt, receivables at our foreign subsidiaries and loans provided to our joint ventures. We believe that the risks associated with our foreign currency exposure are partially mitigated by the fact that a portion of our total revenues, 50.7% in 2018, 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 assess that the impact of foreign currency risk relating to the debt portfolio of Yamal LNG is to a large extent mitigated by the fact that all of its products are delivered to international markets and its revenues are denominated in foreign currencies.

As of 31 December 2018, the Russian rouble depreciated by 20.6% and 15.4% against the US dollar and the Euro, respectively, compared to 31 December 2017.

**Commodity risk**

Our export prices for natural gas, stable gas condensate and refined products, LPG and crude oil are primarily linked to international natural gas, crude oil and oil products prices and/or a combination thereof. 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 stable 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.

Within our trading activities, 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 within the Russian Federation territory 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 the domestic market. 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.

**Forward-looking statements**

This report includes forward-looking statements concerning 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.

**Off balance sheet activities**

As of 31 December 2018, 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**

<b>APR</b>	Asian-Pacific Region
<b>bbl</b>	barrel
<b>bcm</b>	billion cubic meters
<b>boe</b>	barrels of oil equivalent
<b>btu</b>	British thermal unit
<b>CBR</b>	Central Bank of Russian Federation
<b>CFR</b>	"Cost and freight"
<b>CIF</b>	"Cost, insurance and freight"
<b>DAP</b>	"Delivery at point of destination"
<b>DDA</b>	depreciation, depletion and amortization
<b>DES</b>	"Delivery to the port of destination ex-ship"
<b>FCA</b>	"Free carrier"
<b>FEED</b>	Front-End Engineering Design
<b>FOB</b>	"Free on board"
<b>Forecast of the Ministry of Economic Development</b>	The document " <i>Forecast of Socio-economic Development of the Russian Federation for the period till 2024</i> " prepared by the Ministry of Economic Development of the Russian Federation or the similar document prepared for another period
<b>GTS</b>	Gas Transmission System part of the UGSS
<b>IFRS</b>	International Financial Reporting Standards
<b>List</b>	the OFAC's Sectoral Sanctions Identification List
<b>LNG</b>	liquefied natural gas
<b>LPG</b>	liquefied petroleum gas
<b>mcm</b>	thousand cubic meters
<b>MET</b>	mineral extraction tax
<b>NGL</b>	natural gas liquids
<b>OFAC</b>	Office of Foreign Assets Control
<b>PRMS</b>	Petroleum Resources Management System
<b>Purovsky Plant</b>	Purovsky Gas Condensate Plant
<b>Regulator</b>	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. Effective July 2015, Federal Anti-Monopoly Service fulfills the Regulator's role.
<b>RR</b>	Russian rouble(s)
<b>RZD</b>	OAo Russian Railways, Russia's state-owned monopoly railway operator
<b>SEC</b>	Securities and Exchange Commission
<b>Tobolsk Refining Facilities</b>	Refining facilities of OOO SIBUR Tobolsk
<b>UGSF</b>	Underground Gas Storage Facilities
<b>UGSS</b>	Unified Gas Supply System owned and operated by PAO Gazprom
<b>UPT</b>	unified natural resources production tax
<b>USD, US dollar</b>	United States Dollar
<b>Ust-Luga Complex</b>	Gas Condensate Fractionation and Transshipment Complex located at the port of Ust-Luga on the Baltic Sea
<b>VAT</b>	value added tax
<b>Yamal LNG project</b>	A large-scale project on constructing a liquefied natural gas plant with an annual capacity of 17.4 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
<b>YNAO</b>	Yamal-Nenets Autonomous Region

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## 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