PAO NOVATEK

MANAGEMENT’S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION
AND RESULTS OF OPERATIONS

FOR THE YEAR ENDED 31 DECEMBER 2018

CONTENTS **Page**

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 jointtly 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 companiya, respectively, for RR 30.3 billion. Geotransgas (renamed to AO NOVATEK-Pur in December 2018) and Urengoyskaya gasovaya companiya (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 SeverEnergia 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.

SELECTED DATA

millions of Russian roubles except as stated	Year ended 31 December: 2018	2017	Change %
Financial results			
Total revenues [(1)]	831,758	583,186	42.6%
Operating expenses	(603,912)	(419,859)	43.8%
Normalized EBITDA [(2),(3)]	415,296	256,464	61.9%
Normalized profit attributable to shareholders of PAO NOVATEK [(3)]	162,097	156,387	3.7%
Normalized profit attributable to shareholders of PAO NOVATEK [(3)], excluding the effect of foreign exchange gains (losses) [(4)]	232,930	156,166	49.2%
Normalized earnings per share [(3)] (in Russian roubles)	53.79	51.85	3.7%
Normalized earnings per share [(3)], excluding the effect of foreign exchange gains (losses) [(4)] (in Russian roubles)	77.29	51.78	49.3%
Net debt [(5)]	102,903	89,807	14.6%
Production volumes [(6)]			
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%
Sales volumes			
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%)
Oil and gas SEC reserves [(6)]			
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%
Cash flow results			
Net cash provided by operating activities	216,349	180,399	19.9%
Cash used for capital expenditures [(7)]	94,038	29,871	214.8%
Free cash flow [(8)]	122,311	150,528	(18.7%)

(1) Net of VAT, export duties, excise and fuel taxes.

(2) EBITDA represents profit (loss) adjusted for the add-back of depreciation, depletion and amortization, net impairment expenses (reversals), finance income (expense), income tax expense, as well as income (loss) from changes in fair value of derivative financial instruments. EBITDA includes EBITDA from subsidiaries and our proportionate share in the EBITDA of our joint ventures.

(3) Excluding the effect from the disposal of interests in joint ventures.

(4) 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).

(5) Net Debt represents our total debt net of cash, cash equivalents and bank deposits with original maturity more than three months.

(6) 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).

(7) 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.

(8) Free cash flow represents the difference between Net cash provided by operating activities and Cash used for capital expenditures.

Reconciliation of EBITDA and normalized EBITDA is as follows:

millions of Russian roubles	**Year ended 31 December: 2018**	**2017**	**Change %**
Profit	**182,947**	**166,470**	**9.9%**
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
EBITDA from subsidiaries	**261,015**	**198,335**	**31.6%**
Share in EBITDA of joint ventures	**155,926**	**58,129**	**168.2%**
EBITDA	**416,941**	**256,464**	**62.6%**
Net gain on disposal of interests in joint ventures	(1,645)	-	n/a
Normalized EBITDA	**415,296**	**256,464**	**61.9%**
Normalized EBITDA from subsidiaries	**259,370**	**198,335**	**30.8%**

SELECTED MACRO-ECONOMIC DATA

Exchange rate, RR for one foreign currency unit [(1)]	1Q		2Q		3Q		4Q		Year		Change
	2018	**2017**	**2018**	**2017**	**2018**	**2017**	**2018**	**2017**	**2018**	**2017**	**Y-o-Y, %**
US dollar (USD)											
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
Euro											
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

(1) Based on the data from the Central Bank of Russian Federation (CBR). The average rates for the period are calculated as the average of the daily exchange rates on each business day (rate is announced by the CBR) and on each non-business day (rate is equal to the exchange rate on the previous business day).

● ● ●

Average for the period	1Q		2Q		3Q		4Q		Year		Change
	2018	**2017**	**2018**	**2017**	**2018**	**2017**	**2018**	**2017**	**2018**	**2017**	**Y-o-Y, %**
Benchmark natural gas prices [(2)]											
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%
Benchmark crude oil prices [(3)]											
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%
Benchmark crude oil prices excluding export duties [(4)]											
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%
Benchmark oil products [(5)] **and liquefied petroleum gas** [(6)] **prices, USD per ton**											
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%
Export duties, USD per ton [(7)]											
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

(2) Based on natural gas prices at the National Balancing Point (NBP), the natural gas hub in the United Kingdom.

(3) Based on Brent (dtd) and Russian Urals CIF Rotterdam spot assessments prices.

(4) Export duties per barrel were calculated based on export duties per ton divided by the coefficient 7.3.

(5) 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.

(6) Based on spot prices for propane-butane mix at the Belarusian-Polish border (DAF, Brest).

(7) 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 (1)	82.3	65.3	26.0%

(1) 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:

	Year ended 31 December:		**Change**
Russian roubles or US dollars per ton [(1)]	**2018**	**2017**	**%**
Stable gas condensate			
Average net price, RR per ton	25,473	17,719	43.8%
Average net price, USD per ton	403	303	33.0%
Naphtha			
Average net price, RR per ton	35,789	27,301	31.1%
Average net price, USD per ton	572	467	22.5%
Other stable gas condensate refined products			
Average net price, RR per ton	35,682	25,899	37.8%
Average net price, USD per ton	570	443	28.7%
Crude oil			
Average net price, RR per ton	23,394	16,702	40.1%
Average net price, USD per ton	373	286	30.4%
LPG			
Average net price, RR per ton	21,015	15,116	39.0%
Average net price, USD per ton	335	259	29.3%

[(1)] 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 × (P – 490)
between 640 and 740 (inclusive)	75 + 0.6 × (P – 640)
above 740	135 + 0.7 × (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 1/6th 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	22.0%	less 1,021	22.0%	less 1,150	22.0%
	above 876	10.0%	above 1,021	10.0%	above 1,150	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	2.9%	less 815	2.9%	less 865	2.9%
	above 755	0.0%	above 815	0.0%	above 865	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**	**%**
Natural gas, billions of cubic meters	**2,177**	**2,098**	**3.8%**
Subsidiaries	1,351	1,274	6.0%
Share in joint ventures	826	824	0.2%
Liquids, millions of metric tons	**181**	**164**	**10.4%**
Subsidiaries	93	83	12.0%
Share in joint ventures	88	81	8.6%
Combined reserves, millions of boe	**15,789**	**15,120**	**4.4%**
Production, millions of boe	549	513	7.0%
Acquisitions (1), millions of boe	712	1,543	(53.9%)
Disposals (2), millions of boe	160	-	n/a
Reserves replacement ratio (3), %	**222%**	**435%**	
Normalized reserves replacement ratio (3), (4), %	**121%**	**134%**	

(1) 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 Syskonsynyinskiy and the West-Yaroyakhinskiy license areas).

(2) Represent reserves attributable to the disposal of the 3.3% participation interest in Arcticgas in the first quarter of 2018.

(3) The reserves replacement ratio is calculated as the change in reserves increased for the production for the year divided by production for the year.

(4) 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 Urengoyskoye 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:

	SEC		PRMS	
	At 31 December:		At 31 December:	
Number of years	2018	2017	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: 2018	2017 [(1)]	Change %
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 [(2)]	**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 [(3)]	**303.5**	**297.4**	**2.1%**

(1) Figures for 2017 were recalculated based on the changes made to the presentation of oil and gas production costs (see "Basis of presentation" above).

(2) Calculated based on the Group's share in the production of each joint venture.

(3) Calculated based on 100% of the Group's subsidiaries production and our share in the production of each joint venture.

USD per boe [2]	Year ended 31 December: 2018	2017 [1]	Change %
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 [3]	**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 [4]	**4.84**	**5.10**	**(5.1%)**

(1) Figures for 2017 were recalculated based on the changes made to the presentation of oil and gas production costs (see "Basis of presentation" above).

(2) 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).

(3) Calculated based on the Group's share in the production of each joint venture.

(4) 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:

millions of cubic meters if not stated otherwise	**Year ended 31 December: 2018**	**2017**	**Change %**
Production by subsidiaries from:			
Yurkharovskoye field	27,745	30,540	(9.2%)
East-Tarkosalinskoye field	6,627	7,379	(10.2%)
Khancheyskoye 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%
Total natural gas production by subsidiaries (1)	**41,860**	**43,113**	**(2.9%)**
Group's proportionate share in the production of joint ventures:			
Arcticgas	13,698	13,964	(1.9%)
Yamal LNG (2)	8,213	776	n/a
Nortgas	3,789	4,291	(11.7%)
Terneftegas	1,246	1,255	(0.7%)
Total Group's proportionate share in the natural gas production of joint ventures (1)	**26,946**	**20,286**	**32.8%**
Total natural gas production including proportionate share in the production of joint ventures	**68,806**	**63,399**	**8.5%**
Average daily natural gas production including proportionate share in the production of joint ventures	*188.5*	*173.7*	*8.5%*
The Group's proportionate share in LNG production of joint ventures (thousands of tons) (2)	*5,152*	*162*	*n/a*

(1) 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%

(2) 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 Khancheyskoye 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.

	Year ended 31 December:		**Change**
millions of cubic meters	**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%)
Total production and purchases	**74,871**	**66,710**	**12.2%**
Own usage [(1)]	(1,561)	(1,507)	3.6%
Decrease (increase) in natural gas inventory balance	(1,176)	(199)	n/a
Total natural gas sales volumes	**72,134**	**65,004**	**11.0%**
Sold to end-customers	*61,901*	*61,560*	*0.6%*
Sold ex-field	*4,172*	*3,338*	*25.0%*
Subtotal sold in the Russian Federation	***66,073***	***64,898***	***1.8%***
Sold on international markets	***6,061***	***106***	***n/a***

(1) 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:

	Year ended 31 December:		Change
thousands of tons	**2018**	**2017**	**%**
Production by subsidiaries from:			
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%
Total liquids production by subsidiaries	**6,546**	**6,759**	**(3.2%)**
including crude oil	*4,704*	*4,779*	*(1.6%)*
including gas condensate	*1,842*	*1,980*	*(7.0%)*
Group's proportionate share in the production of joint ventures:			
Arcticgas	3,999	4,190	(4.6%)
Yamal LNG [(1)]	542	25	n/a
Terneftegas	403	421	(4.3%)
Nortgas	310	379	(18.2%)
Total Group's proportionate share in the liquids production of joint ventures	**5,254**	**5,015**	**4.8%**
Total liquids production including proportionate share in the production of joint ventures	**11,800**	**11,774**	**0.2%**
Average daily liquids production including proportionate share in the production of joint ventures	*32.3*	*32.3*	*0.2%*

(1) 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.

thousands of tons	Year ended 31 December: 2018	2017	Change %
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%
Total production and purchases	**16,140**	**16,247**	**(0.7%)**
Losses (1) and own usage (2)	(211)	(249)	(15.3%)
Decreases (increases) in liquids inventory balances	(107)	(59)	81.4%
Total liquids sales volumes	**15,822**	**15,939**	**(0.7%)**
Naphtha export	*4,185*	*4,102*	*2.0%*
Other stable gas condensate refined products export (3)	*2,396*	*2,524*	*(5.1%)*
Other stable gas condensate refined products domestic (3)	*102*	*117*	*(12.8%)*
Subtotal stable gas condensate refined products	***6,683***	***6,743***	***(0.9%)***
Crude oil export	*1,549*	*1,523*	*1.7%*
Crude oil domestic	*2,993*	*3,093*	*(3.2%)*
Subtotal crude oil	***4,542***	***4,616***	***(1.6%)***
LPG export	*593*	*536*	*10.6%*
LPG domestic	*2,083*	*2,112*	*(1.4%)*
Subtotal LPG	***2,676***	***2,648***	***1.1%***
Stable gas condensate export	*274*	*342*	*(19.9%)*
Stable gas condensate domestic	*1,634*	*1,576*	*3.7%*
Subtotal stable gas condensate	***1,908***	***1,918***	***(0.5%)***
Other oil products	***13***	***14***	***(7.1%)***

(1) Losses associated with processing at the Purovsky Plant, the Ust-Luga Complex and the Tobolsk Refining Facilities, as well as during railroad, trunk pipeline and tanker transportation.

(2) Own usage associated primarily with the maintaining of refining process at the Ust-Luga Complex, as well as bunkering of chartered tankers.

(3) 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).

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.

	Year ended 31 December:			
millions of Russian roubles	**2018**	**% of total revenues**	**2017**	**% of total revenues**
Total revenues [1]	**831,758**	***100.0%***	**583,186**	***100.0%***
including:				
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%*
Profit from operations before disposals of interests in joint ventures	**225,539**	***27.1%***	**163,751**	***28.1%***
Net gain on disposal of interests in joint ventures	1,645	*0.2%*	-	*n/a*
Profit from operations	**227,184**	***27.3%***	**163,751**	***28.1%***
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%*
Profit before income tax	**228,534**	***27.5%***	**200,839**	***34.4%***
Total income tax expense	(45,587)	*(5.5%)*	(34,369)	*(5.9%)*
Profit	**182,947**	***22.0%***	**166,470**	***28.5%***
Less: profit (loss) attributable to non-controlling interest	(19,205)	*(2.3%)*	(10,083)	*(1.7%)*
Profit attributable to shareholders of PAO NOVATEK	**163,742**	***19.7%***	**156,387**	***26.8%***
Normalized profit attributable to shareholders of PAO NOVATEK, excluding the effect of foreign exchange gains (losses)	**232,930**	***28.0%***	**156,166**	***26.8%***

[1] Net of VAT, export and import duties, excise and fuel taxes expense, where applicable.

Total revenues

The following table sets forth our sales (excluding VAT, export duties, excise and fuel taxes expense, where applicable) for the years ended 31 December 2018 and 2017:

millions of Russian roubles	Year ended 31 December: 2018	2017	Change %	Change [(1)] Total	Due to volume [(2)]	Due to price [(3)]
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
Naphtha	*149,770*	*111,979*	*33.7%*	*37,791*	*2,273*	*35,518*
Other refined products	*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
Total oil and gas sales	**825,761**	**579,819**	**42.4%**	**245,942**	**n/a**	**n/a**
Other revenues	5,997	3,367	78.1%	2,630	n/a	n/a
Total revenues	**831,758**	**583,186**	**42.6%**	**248,572**	**n/a**	**n/a**

(1) 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.

(2) 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.

(3) 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.

	Year ended 31 December:			
millions of Russian roubles	**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*
Total operating expenses	**603,912**	***72.6%***	**419,859**	***72.0%***

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.

	Year ended 31 December:		**Change**
millions of Russian roubles	**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%
Total purchases of natural gas and liquid hydrocarbons	**319,990**	**161,443**	**98.2%**

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.

millions of Russian roubles	Year ended 31 December: 2018	2017	Change %
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%
Total transportation expenses	**145,664**	**137,192**	**6.2%**

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.

millions of Russian roubles	Year ended 31 December: 2018	2017	Change %
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%
Total taxes other than income tax	**58,768**	**49,494**	**18.7%**

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.

millions of Russian roubles	**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%
Total materials, services and other	**22,675**	**20,768**	**9.2%**

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.

millions of Russian roubles	**Year ended 31 December:** **2018**	**2017**	**Change %**
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%
Total general and administrative expenses	**22,282**	**17,170**	**29.8%**

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:

Inventory balances in transit or in storage	**2018** At 31 December	**2018** At 1 January	**2018** Increase / (decrease)	**2017** At 31 December	**2017** At 1 January	**2017** Increase / (decrease)
Natural gas (millions of cubic meters)	**2,209**	**1,033**	**1,176**	**1,033**	**834**	**199**
incl. Gazprom's UGSF	*2,106*	*870*	*1,236*	*870*	*787*	*83*
Liquid hydrocarbons (thousand tons)	**1,069**	**962**	**107**	**962**	**903**	**59**
incl. stable gas condensate						
refined products	*578*	*464*	*114*	*464*	*395*	*69*
stable gas condensate	*276*	*290*	*(14)*	*290*	*307*	*(17)*
crude oil	*109*	*103*	*6*	*103*	*105*	*(2)*

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.

	Year ended 31 December:		Change
millions of Russian roubles	**2018**	**2017**	**%**
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%
Interest expense	**(4,746)**	**(7,712)**	**(38.5%)**
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%
Total finance income (expense)	**38,608**	**14,658**	**163.4%**

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.

millions of Russian roubles	Year ended 31 December: 2018	2017	Change %
Share in profit from operations	**124,211**	**39,854**	**211.7%**
Share in finance income (expense)			
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
Total share in finance income (expense)	**(160,836)**	**(10,297)**	**n/a**
Share in total income tax benefit (expense)	(633)	(7,127)	(91.1%)
Total share of profit (loss) of joint ventures, net of income tax	**(37,258)**	**22,430**	**n/a**

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.

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):

millions of Russian roubles	**Year ended 31 December: 2018**	**2017**	**Change %**
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
Normalized profit attributable to shareholders of PAO NOVATEK	**162,097**	**156,387**	**3.7%**
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
Normalized profit attributable to shareholders of PAO NOVATEK, excluding the effect of foreign exchange gains (losses)	**232,930**	**156,166**	**49.2%**

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:

millions of Russian roubles	Year ended 31 December: 2018	2017	Change %
Net cash provided by **operating** activities	216,349	180,399	19.9%
Net cash used for **investing** activities	(153,046)	(58,275)	162.6%
Net cash used for **financing** 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.

millions of Russian roubles	Year ended 31 December: 2018	2017	Change %
Profit from operations before disposals of interests in joint ventures	225,539	163,751	37.7%
Non-cash adjustments [(1)]	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%
Total net cash provided by operating activities	**216,349**	**180,399**	**19.9%**

[(1)] Include adjustments for depreciation, depletion and amortization, net impairment expenses (reversals), change in fair value of non-commodity financial instruments and some other adjustments.

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.

millions of Russian roubles	Year ended 31 December: 2018	2017	Change %
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%
Net cash used for investing activities	**(153,046)**	**(58,275)**	**162.6%**

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 Urengoyskaya gasovaya companiya 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.

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.

millions of Russian roubles	**Year ended 31 December:**		**Change**
	2018	**2017**	**%**
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%
Net cash used for financing activities	**(93,658)**	**(103,837)**	**(9.8%)**

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, %
Absolute amounts, RR million			
Net debt (1)	102,903	89,807	14.6%
Net working capital position (2)	186,297	69,478	168.1%
Liquidity and credit ratios			
Current ratio (3)	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 (4)	0.09	0.09	0.0%
Net debt to normalized EBITDA from subsidiaries (5)	0.40	0.45	(11.1%)
Interest coverage ratio (6)	30	19	57.9%

(1) Net debt represents total debt less cash, cash equivalents and bank deposits with original maturity more than three months.

(2) Net working capital position represents current assets less current liabilities.

(3) Current ratio is calculated as current assets divided by current liabilities.

(4) Total capitalization represents total debt, total equity and deferred income tax liability.

(5) Net debt to normalized EBITDA from subsidiaries ratio is calculated as Net debt divided by EBITDA from subsidiaries excluding the effect from the disposal of interests in joint ventures for the last twelve months.

(6) Interest coverage ratio is calculated as normalized EBITDA from subsidiaries divided by accrued interest on debt, including capitalized interest.

In 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:

	Year ended 31 December:	
millions of Russian roubles	**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 [(1)]	16,421	2,641
East-Tarkosalinskoye field	6,820	4,215
Yarudeyskoye field	4,693	4,489
Yurkharovskoye field	4,215	1,800
North-Obskiy 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
Capital expenditures	**95,736**	**30,419**

[(1)] 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-Obskiy 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.

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:

millions of Russian roubles	Year ended 31 December: 2018	2017	Change %
Total additions to property, plant and equipment per Note "Property, plant and equipment" in the Group's IFRS Consolidated Financial Statements	**98,484**	**48,064**	**104.9%**
Less: acquisition of mineral licenses	(268)	(10,022)	(97.3%)
Less: right-of-use assets [1] additions	(2,480)	(7,623)	(67.5%)
Capital expenditures	**95,736**	**30,419**	**214.7%**
Add (less): change in accounts payable, capitalized foreign exchange losses and other non-cash adjustments	(1,698)	(548)	209.9%
Cash used for capital expenditures [2]	**94,038**	**29,871**	**214.8%**

(1) Related mainly to long-term agreements on time chartering of marine tankers.

(2) 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

APR	Asian-Pacific Region
bbl	barrel
bcm	billion cubic meters
boe	barrels of oil equivalent
btu	British thermal unit
CBR	Central Bank of Russian Federation
CFR	"Cost and freight"
CIF	"Cost, insurance and freight"
DAP	"Delivery at point of destination"
DDA	depreciation, depletion and amortization
DES	"Delivery to the port of destination ex-ship"
FCA	"Free carrier"
FEED	Front-End Engineering Design
FOB	"Free on board"
Forecast of the Ministry of Economic Development	The document *"Forecast of Socio-economic Development of the Russian Federation for the period till 2024"* prepared by the Ministry of Economic Development of the Russian Federation or the similar document prepared for another period
GTS	Gas Transmission System part of the UGSS
IFRS	International Financial Reporting Standards
List	the OFAC's Sectoral Sanctions Identification List
LNG	liquefied natural gas
LPG	liquefied petroleum gas
mcm	thousand cubic meters
MET	mineral extraction tax
NGL	natural gas liquids
OFAC	Office of Foreign Assets Control
PRMS	Petroleum Resources Management System
Purovsky Plant	Purovsky Gas Condensate Plant
Regulator	A federal executive agency of the Russian Federation that carries out governmental regulation of prices and tariffs for products and services of natural monopolies in energy, utilities and transportation. Effective July 2015, Federal Anti-Monopoly Service fulfills the Regulator's role.
RR	Russian rouble(s)
RZD	OAO Russian Railways, Russia's state-owned monopoly railway operator
SEC	Securities and Exchange Commission
Tobolsk Refining Facilities	Refining facilities of OOO SIBUR Tobolsk
UGSF	Underground Gas Storage Facilities
UGSS	Unified Gas Supply System owned and operated by PAO Gazprom
UPT	unified natural resources production tax
USD, US dollar	United States Dollar
Ust-Luga Complex	Gas Condensate Fractionation and Transshipment Complex located at the port of Ust-Luga on the Baltic Sea
VAT	value added tax
Yamal LNG project	A large-scale project on constructing a liquefied natural gas plant with an annual capacity of 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
YNAO	Yamal-Nenets Autonomous Region