PAO NOVATEK

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

FOR THE YEARS ENDED
31 DECEMBER 2016 AND 2015

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GENERAL PROVISIONS

You should read the following discussion and analysis of our financial condition and results of operations as of 31 December 2016 and for the year then ended in conjunction with our audited consolidated financial statements as of and for the years ended 31 December 2016 and 2015. The consolidated financial statements and the related notes thereto have been prepared in accordance with International Financial Reporting Standards (IFRS).

The financial and operating information contained in this "Management's Discussion and Analysis of Financial Condition and Results of Operations" comprises information of PAO NOVATEK, its consolidated subsidiaries and joint ventures (hereinafter jointly referred to as "we" or the "Group").

This report includes forward-looking statements concerned future possible events that can impact operational and financial results of the Group. Forward-looking statements can be identified by words such as "believes", "anticipates", "expects", "estimates", "intends", "plans" and similar expressions. Forward-looking statements are made based on the current situation with definite and indefinite risks and uncertainties. Actual future results could differ materially from those discussed in the forward-looking statements as they are dependent on various factors beyond and under the control of management.

OVERVIEW

We are one of the Russia's largest natural gas producers and leaders in terms of proved natural gas reserves in the Russian Federation under the Petroleum Resources Management System ("PRMS") and the Security and Exchange Commission ("SEC") reserve reporting methodologies.

Our exploration and development, production and processing of natural gas, gas condensate and crude oil are conducted mainly within the Russian Federation.

In accordance with Russian law, we currently sell all of our produced natural gas volumes exclusively in the Russian domestic market.

Several wholly owned subsidiaries of the Group (OOO Arctic LNG 1, OOO Arctic LNG 2, and OOO Arctic LNG 3) and the Group's joint venture OAO Yamal LNG are the holders of liquefied natural gas ("LNG") export licenses. The aforementioned subsidiaries hold licenses for exploration and production on the Salmanovskoye (Utrenneye) and Geofizicheskoye fields, and the North-Obskiy and Trekhbugorniy license areas located on the Gydan peninsula and the Gulf of Ob. Yamal LNG holds the exploration and production license for the South-Tambeyskoye field located in the north-eastern part of the Yamal peninsula in the Yamal-Nenets Autonomous Region ("YNAO").

We deliver our extracted unstable gas condensate through our own pipelines to our Purovsky Gas Condensate Plant (the "Purovsky Plant") for processing into stable gas condensate and liquefied petroleum gas ("LPG"). The Purovsky Plant allows us to process more than 12 million tons of unstable gas condensate per annum.

Most of our stable gas condensate is sent for further processing to our Gas Condensate Fractionation and Transshipment Complex located at the port of Ust-Luga on the Baltic Sea (the "Ust-Luga Complex"). The Ust-Luga Complex processes our stable gas condensate into light and heavy naphtha, jet fuel, gasoil and fuel oil, nearly all of which we sell to the international markets allowing us to increase the added value of our liquid hydrocarbons sales. The Ust-Luga Complex allows us to process about seven million tons of stable gas condensate annually.

The excess volumes of stable gas condensate received from the processing at the Purovsky Plant over volumes sent for further processing to the Ust-Luga Complex are sold on both the domestic and international markets (from the port of Ust-Luga on the Baltic Sea by tankers and to European markets by rail).

A significant part of our LPG produced at the Purovsky Plant is dispatched via pipeline for refining by OOO SIBUR Tobolsk at its refining facility (the "Tobolsk Refining Facilities"). The remaining volumes are sold directly from the Purovsky Plant without incurring additional transportation expenses. After processing at the Tobolsk Refining Facilities we receive LPG with higher added value, the majority of which are transported by rail to our end-customers in the domestic and international markets with the remaining portion sold directly from the Tobolsk Refining Facilities without incurring additional transportation expenses.

We deliver our crude oil to both domestic and international markets.

The Group, jointly with our international partners TOTAL S.A., China National Petroleum Corporation and China's Silk Road Fund Co. Ltd., through our joint venture OAO Yamal LNG, undertakes a large-scale project on constructing a liquefied natural gas plant with an annual capacity of 16.5 million tons based on the feedstock resources of the South-Tambeyskoye field (the "Yamal LNG project"). The Yamal LNG project also requires the construction of transportation infrastructure, including the seaport and the international airport. The launch of the first train of the LNG plant and start of liquefied natural gas shipments is planned in 2017. It is expected that the produced LNG will be sold mainly to the Asian-Pacific Region ("APR") and to the European market. The Yamal LNG project has now concluded the sale of more than 95% of LNG volumes produced under long-term contractual agreements.

RECENT DEVELOPMENTS

Increasing our production and utilization of refining capacity

At the end of 2014 and in the first half of 2015, OOO SeverEnergia, the Group's joint venture with PAO Gazprom Neft, and ZAO Terneftegas, the Group's joint venture with TOTAL S.A., launched additional production facilities. As a result, the Group's gas condensate production has increased significantly enabling us to fill the capacity of processing facilities of our Ust-Luga Complex (effective January 2015) and our Purovsky Plant (effective May 2015).

In December 2015, we commenced commercial production at the Yarudeyskoye oil field and at the end of the month we reached the nameplate production capacity of approximately 3.5 million tons of crude oil per annum. The successful launch and production ramp-up of the Yarudeyskoye field allowed us to significantly increase our production of crude oil and represented the majority of liquids production growth in 2016.

Implementing our Yamal LNG project

Currently, the Yamal LNG project is in the final stage of preparation for the launch of the first train of the LNG plant and the start of liquefied natural gas shipments planned in 2017. Most of the infrastructure required for the launch is now completed, including the sea port and the international airport, production wells drilled, and all of the modules for the first LNG train have been delivered and installed. More than 95% of LNG volumes produced within the project have been contracted under long-term agreements and we have signed long-term agreements for time chartering of LNG ice class carriers to ensure future LNG deliveries.

In 2015, the Ministry of Finance subscribed for and purchased two tranches of Yamal LNG's bonds in the aggregate amount of RR 150 billion (nominal amount of USD 2.36 billion) allocated from the National Wealth Fund. The bonds will be repaid in equal installments from 2022 to 2030 in Russian roubles at the US dollar exchange rate at the date of payment. Interest is paid semi-annually starting from September 2015.

In 2016, Yamal LNG also signed credit line facility agreements to raise project financing for the total amount of approximately EUR 13.9 billion and CNY 7.6 billion, with the repayment period commencing from December 2019 through June 2031:

- in April 2016 – with PAO Sberbank and AO Gazprombank (with insurance coverage by the Russian Agency for Export Credit and Investment Insurance), the Export-Import Bank of China, and the China Development Bank;

- in December 2016 – with the Italian bank Intesa Sanpaolo (with insurance coverage by the Italian export-credit agency SACE and the French export-credit agency COFACE), and the Japan Bank for International Cooperation.

Signing of these credit agreements and the bonds placement completely cover the project's external finance needs and contribute to its further successful realization.

In December 2015, NOVATEK and China's Silk Road Fund Co. Ltd. signed an agreement on the acquisition of a 9.9% equity stake in Yamal LNG by the fund. In March 2016, the transaction was closed upon the completion of the conditions precedent. As a result of this transaction, the Group's interest in Yamal LNG was reduced from 60% to 50.1%. The Group continues to exercise joint control over Yamal LNG and, accordingly, recognizes the project as a joint venture. The entrance of Silk Road Fund Co. Ltd. to the Yamal LNG project is an important step in the execution of our long-term development strategy for this project.

Development of our operations at Gydan peninsula and the Gulf of Ob

The Group's wholly owned subsidiaries OOO Arctic LNG 1, OOO Arctic LNG 2, and OOO Arctic LNG 3 have significant hydrocarbon resources on the Gydan peninsula and the Gulf of Ob and are the holders of the liquefied natural gas export licenses. The aforementioned subsidiaries hold exploration and production licenses for the Salmanovskoye (Utrenneye) and Geofizicheskoye fields as well as the North-Obskiy and Trekhbugorniy license areas.

In 2016, we continued full-scale exploration activities in this region, conducted processing and interpretation of new and existing seismic data, drilled several exploration wells for the purpose of delineating the resource base and defining a plan to develop these fields.

The estimated aggregate proved, probable and possible reserves of the Salmanovskoye (Utrenneye) and Geofizicheskoye fields appraised under the PRMS reserve methodology as of 31 December 2016 totaled 1.24 trillion cubic meters of natural gas and 53.7 million tons of liquid hydrocarbons. The resources of the North-Obskiy license area according to the Russian reserve classification C3+D1L as of 31 December 2016 totaled 1.1 trillion cubic meters of natural gas and 71 million tons of liquid hydrocarbons. The resources of the Trekhbugorniy license area according to the Russian reserve classification C3+D as of 31 December 2016 amounted to approximately 1.0 trillion of cubic meters of natural gas and 92 million tons of liquid hydrocarbons.

In addition, we significantly expanded our resource base on the Gydan peninsula in 2016 and obtained the rights for the usage of five new license areas.

- In October 2016, based on results of auction held by the Federal Agency for the Use of Natural Resources of the Russian Federation, the Group won the right for geological research works, exploration and production of hydrocarbons at the Tanamskiy license area. The license area is located on the Gydan peninsula in the Krasnoyarsk region in close proximity to other license areas of the Group on the peninsula. As of 31 December 2016, the field's recoverable hydrocarbon resources according to the Russian reserve classification C3+D totaled approximately 1.2 billion barrels of oil equivalent. The payment for the license amounted to RR 467 million.

- In June 2016, the Group obtained mineral licenses for exploration works at the West-Solpatinskiy and Nyavuyahskiy license areas adjacent to the Ladertoyskiy license area, and the North-Tanamskiy license area located in the YNAO. As of 31 December 2016, the aggregate recoverable resources of these three new license areas according to the Russian reserve classification C3+D totaled approximately 560 billion cubic meters ("bcm") of natural gas and approximately 57 million tons of liquid hydrocarbons.

- In April 2016, the Group acquired a 100% equity stake in OOO Evrotek-Yuh for RR six million. Evrotek-Yuh is a holder of the license for geological research works, exploration and production of hydrocarbons within Ladertoyskiy license area located in the YNAO. As of 31 December 2016, the license area's reserves and recoverable resources according to the Russian reserve classification ABC1+C2+C3 totaled approximately 39 bcm of natural gas and approximately six million tons of liquid hydrocarbons.

The Group considers the Gydan peninsula and the Gulf of Ob as one of the most important regions for implementing our future strategic projects. We are studying different alternatives for developing and monetizing our hydrocarbon resources in this region and are presently conducting feasibility studies for a new LNG plant construction based on the resources of the Salmanovskoye (Utrenneye) field. It is contemplated to build the plant on gravity-based platforms which will be constructed, jointly with other major units for the plant, at our own center for construction of large-scale offshore structures located in Murmansk region. In the end of 2016, we acquired several properties for the construction of the project infrastructure, including a berth with an access road, and currently we are preparing project documentation for the plant and infrastructure construction.

Increasing our resource base in YNAO

In addition to obtaining the aforementioned five new license areas on the Gydan peninsula in 2016, the Group, based on auction results held by the Federal Agency for the Use of Natural Resources of the Russian Federation, won the right for the usage of two additional license areas in YNAO.

- In September 2016, the Group obtained the right for geological research works, exploration and production of hydrocarbons at the Syadorskiy license area. The acquisition of the new license area located in the northern part of the Yamal peninsula in YNAO expands the Group's resource base for implementing our future projects in this region. As of 31 December 2016, the field's natural gas reserves according to the Russian reserve classification C1 amounted to approximately 25 bcm, and recoverable resources according to the Russian reserve classification C3+D totaled approximately 63 bcm of natural gas and approximately 19 million tons of liquid hydrocarbons. The payment for the license amounted to RR 404 million.

- In April 2016, the Group obtained the right for geological research works, exploration and production of hydrocarbons at the Nyakhartinskiy license area. The license area is located in the YNAO in close proximity to our Yurkharovskoye field, which will allow us to develop the new area using the existing well-developed infrastructure of one of our core production assets. As of 31 December 2016, the field's recoverable resources according to the Russian reserve classification C3+D totaled 215 bcm of natural gas and more than 70 million tons of liquid hydrocarbons. The payment for the license amounted to RR 1,057 million.

International oil and gas projects

In September 2016, the Group and the Italian energy company Eni (the "Concessionaries") through their wholly owned subsidiaries entered into a concession contract with the State of Montenegro for the exploration and production of hydrocarbons on four offshore blocks located in the Adriatic Sea (the "Concession Contract"). The participation interest of each Concessioner is 50%, and Eni was appointed as the operator.

According to the Concession Contract, the Concessionaries are committed to perform 3D-seismic exploratory works and to drill several exploration wells during the exploration phase of up to seven years. The Concessionaries are currently preparing for performing exploration works that are planned to commence in early 2017.

The participation in the Concession Contract contributes to the Group's ability to realize future international joint projects, as well as enables the Group to gain experience working in offshore projects.

LNG market development

In July 2016, NOVATEK through its wholly owned subsidiary Novatek Gas and Power GmbH performed its first trading operation for the purchase and sale of liquefied natural gas on the spot market. The first LNG cargo was purchased in Trinidad and Tobago and supplied to Chile. This operation allowed the Group to gain experience in LNG trading and will contribute to our successful entry to the global LNG market. The financial result from the LNG trading activity was recorded in "Other operating income (loss)".

In December 2016, we acquired a 100% participation interest in a company Blue Gaz Sp. z o.o. for total cash consideration of RR 26 million (PLN two million) to expand the Groups' activities in Poland. The company purchases liquefied natural gas in Poland, regasifies it at its own regasification station and sells natural gas to customers in Poland.

Change in the participation interest in SeverEnergia

In August 2015, as part of the next stage of restructuring procedures, NOVATEK contributed a 6.4% ownership interest in Artic Russia B.V. to the capital of Yamal Development. Simultaneously, the Group and Gazprom Neft made contributions to the capital of Yamal Development by converting loans (including accrued interest) in the amount of RR 2.5 billion and RR 14.9 billion, respectively. As a result of these transactions the Group's effective participation interest in SeverEnergia decreased from 54.9% to 53.3%. It is expected that further procedures towards achieving parity shareholdings in SeverEnergia will be completed in the foreseeable future.

Extension and conclusion of new natural gas supply contracts

In 2015 and 2016, we continued forming and optimizing our natural gas supply agreements portfolio. The Group concluded and extended a number of large natural gas supply contracts:

- concluded a contract with PAO Enel Russia for the supply of approximately 2.0 bcm of natural gas per annum starting from January 2016 until the end of 2018;

- concluded a number of contracts with the companies of the Novolipetsk Steel Group for the supply of 2.8 bcm of natural gas per annum starting from January 2016 until 2020 which were subsequently extended to 2025; and

- extended the natural gas supply contract with PAO Mosenergo for an additional four years until the end of 2019, with annual supply volumes of approximately 9.1 bcm.

Contract extensions and concluding new major agreements are important steps for maintaining and increasing our client base.

SELECTED DATA

millions of Russian roubles except as stated	Year ended 31 December: 2016	2015	Change %
Financial results			
Total revenues [(1)]	537,472	475,325	13.1%
Operating expenses	(385,499)	(335,042)	15.1%
Normalized EBITDA [(2),(3)]	242,407	214,189	13.2%
Normalized profit attributable to shareholders of PAO NOVATEK [(3)]	200,118	73,407	172.6%
Normalized profit attributable to shareholders of PAO NOVATEK [(3)], excluding the effect of foreign exchange gains (losses)	133,759	132,509	0.9%
Normalized earnings per share [(3)] (in Russian roubles)	66.30	24.30	172.8%
Normalized earnings per share [(3)], excluding the effect of foreign exchange gains (losses) (in Russian roubles)	44.31	43.87	1.0%
Net debt [(4)]	168,464	329,518	(48.9%)
Production volumes [(5)]			
Hydrocarbons production (million barrels of oil equivalent)	537.0	521.6	3.0%
Daily production (million barrels of oil equivalent per day)	1.47	1.43	3.0%
Sales volumes			
Natural gas sales volumes (million cubic meters)	64,709	62,465	3.6%
Crude oil sales volumes (thousand tons)	4,650	1,090	326.6%
Naphtha sales volumes (thousand tons)	4,113	4,120	(0.2%)
Stable gas condensate sales volumes (thousand tons)	2,812	2,786	0.9%
Liquefied petroleum gas sales volumes (thousand tons)	2,713	2,306	17.6%
Other gas condensate refined products (thousand tons) [(6)]	2,549	2,573	(0.9%)
Oil and gas SEC reserves [(7)]			
Total proved reserves (billion barrels of oil equivalent)	12.8	12.8	(0.3%)
Total natural gas proved reserves (trillion cubic meters)	1.75	1.77	(1.1%)
Total liquids proved reserves (million tons)	152	143	6.3%
Cash flow results			
Net cash provided by operating activities	173,791	132,864	30.8%
Cash used for capital expenditures [(8)]	34,413	50,584	(32.0%)
Free cash flow [(9)]	139,378	82,280	69.4%

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

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

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

(4) Net Debt represents our total debt net of cash and cash equivalents.

(5) Hydrocarbons production and daily production are calculated based on 100% of net production of our subsidiaries and our proportionate share in the production of our joint ventures.

(6) Other gas condensate refined products include jet fuel, gasoil and fuel oil.

(7) Oil and gas reserves are presented under SEC reserve classification and include 100% of reserves attributable to all consolidated subsidiaries and our proportionate share in the reserves of our joint ventures.

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

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

Our financial results fluctuate period-on-period due to the recognition of non-cash foreign exchange gains (losses) resulting from the Russian rouble appreciation/depreciation relative to the foreign currencies.

In 2016, the Russian rouble appreciated relative to the US dollar and Euro by 17% and 20%, respectively, whereas in 2015, the Russian rouble depreciated relative to the US dollar and Euro by 30% and 17%, respectively. As a result, we recognized significant non-cash foreign exchange gains in 2016 compared to significant non-cash foreign exchange losses in 2015. These foreign exchange gains (losses) primarily related to the US dollar- and Euro-denominated borrowings of Yamal LNG, our joint venture. We believe that the risk of currency movements arising in relation to the debt portfolio of Yamal LNG will be fully mitigated due to its revenues denominated in foreign currency as all liquefied natural gas volumes will be delivered to and sold in international markets once commercial production commences.

Excluding the one-off effect from the disposal of interests in joint ventures and the effect of foreign exchange gains and losses, the Group's profit attributable to shareholders of PAO NOVATEK was relatively flat and amounted to RR 133,759 million compared to 132,509 million in 2015.

Reconciliation of EBITDA and normalized EBITDA is as follows:

millions of Russian roubles	**Year ended 31 December: 2016**	**2015**	**Change %**
Profit	**265,073**	**74,119**	**257.6%**
Depreciation, depletion and amortization	34,631	19,980	73.3%
Impairment expenses (reversals), net	178	(204)	n/a
Loss (income) from changes in fair value of derivative financial instruments	1,778	1,006	76.7%
Total finance expense (income)	7,941	16,182	(50.9%)
Total income tax expense	43,091	18,822	128.9%
Share of loss (profit) of joint ventures, net of income tax	(90,839)	31,607	n/a
EBITDA from subsidiaries	**261,853**	**161,512**	**62.1%**
Share in EBITDA of joint ventures	53,626	53,666	(0.1%)
EBITDA	**315,479**	**215,178**	**46.6%**
Net gain on disposal of interests in joint ventures	(73,072)	(989)	n/a
Normalized EBITDA	**242,407**	**214,189**	**13.2%**
Normalized EBITDA from subsidiaries	**188,781**	**160,523**	**17.6%**

SELECTED MACRO-ECONOMIC DATA

Exchange rate, RR for one foreign currency unit [(1)]	1Q		2Q		3Q		4Q		Year		Change
	2016	**2015**	**2016**	**2015**	**2016**	**2015**	**2016**	**2015**	**2016**	**2015**	**Y-o-Y, %**
US dollar (USD)											
Average for the period	74.63	62.19	65.89	52.65	64.62	62.98	63.07	65.94	67.03	60.96	10.0%
At the beginning of the period	72.88	56.26	67.61	58.46	64.26	55.52	63.16	66.24	72.88	56.26	29.5%
At the end of the period	67.61	58.46	64.26	55.52	63.16	66.24	60.66	72.88	60.66	72.88	(16.8%)
Depreciation (appreciation) of RR to US dollar	(7.2%)	3.9%	(5.0%)	(5.0%)	(1.7%)	19.3%	(4.0%)	10.0%	(16.8%)	29.5%	n/a
Euro											
Average for the period	82.34	70.43	74.40	58.24	72.15	70.11	68.13	72.27	74.23	67.78	9.5%
At the beginning of the period	79.70	68.34	76.54	63.37	71.21	61.52	70.88	74.58	79.70	68.34	16.6%
At the end of the period	76.54	63.37	71.21	61.52	70.88	74.58	63.81	79.70	63.81	79.70	(19.9%)
Depreciation (appreciation) of RR to euro	(4.0%)	(7.3%)	(7.0%)	(2.9%)	(0.5%)	21.2%	(10.0%)	6.9%	(19.9%)	16.6%	n/a

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

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Average for the period	1Q		2Q		3Q		4Q		Year		Change
	2016	**2015**	**2016**	**2015**	**2016**	**2015**	**2016**	**2015**	**2016**	**2015**	**Y-o-Y, %**
Benchmark crude oil prices [(2)]											
Brent, USD per barrel	33.9	53.9	45.6	61.9	45.9	50.5	49.3	43.8	43.7	52.4	(16.6%)
Urals, USD per barrel	32.2	52.9	43.8	61.7	44.0	49.6	48.1	42.0	42.1	51.4	(18.1%)
Urals, RR per barrel	2,403	3,290	2,886	3,249	2,843	3,124	3,034	2,769	2,822	3,133	(9.9%)
Benchmark crude oil prices excluding export duties [(3)]											
Urals, USD per barrel	24.7	35.1	34.6	43.8	31.8	32.0	35.5	29.4	31.7	34.9	(9.2%)
Urals, RR per barrel	1,843	2,183	2,280	2,306	2,055	2,015	2,239	1,939	2,125	2,128	(0.1%)
World market prices for oil products [(4)] **and liquefied petroleum gas** [(5)]**, USD per ton**											
Naphtha Japan	345	493	411	563	389	462	450	444	399	490	(18.6%)
Naphtha CIF NWE	320	468	400	538	382	431	440	413	386	461	(16.3%)
Jet fuel	342	565	437	603	437	503	484	439	425	526	(19.2%)
Gasoil	310	519	410	574	409	480	453	405	396	493	(19.7%)
Fuel oil	147	292	215	338	249	253	288	202	225	270	(16.7%)
Liquefied petroleum gas	232	316	225	364	326	352	403	367	299	350	(14.6%)
Export duties, USD per ton [(6)]											
Crude oil, stable gas condensate	54.9	129.6	67.2	130.6	88.7	128.5	91.7	92.3	75.6	120.3	(37.2%)
Liquefied petroleum gas	0.0	16.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	4.0	n/a
Naphtha	39.0	110.1	47.6	110.9	62.9	109.2	65.0	78.4	53.6	102.2	(47.6%)
Jet fuel	22.0	62.1	26.8	62.6	35.4	61.6	36.6	44.3	30.2	57.7	(47.7%)
Gasoil	22.0	62.1	26.8	62.6	35.4	61.6	36.6	44.3	30.2	57.7	(47.7%)
Fuel oil	45.0	98.5	55.0	99.2	72.7	97.6	75.1	70.1	62.0	91.3	(32.1%)

(2) Based on Brent (dtd) and Russian Urals CIF Rotterdam spot assessments prices as provided by Platts.

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

(4) Based on Naphtha C+F (cost plus freight) Japan, Naphtha CIF NWE, Jet CIF NWE, Gasoil 0.1% CIF NWE, Fuel Oil 1.0% CIF NWE prices provided by Platts.

(5) Based on spot prices for propane-butane mix at the Belarusian-Polish border (DAF, Brest) as provided by Argus.

(6) Export duties are determined by the Russian Federation government in US dollars and are paid in Russian roubles (see "Our tax burden and obligatory payments" below).

CERTAIN FACTORS AFFECTING OUR RESULTS OF OPERATIONS

Current economic conditions

Since 2014, the Russian economy has experienced weakening macro-economic conditions which became especially apparent during the fourth quarter of 2014 with the severe devaluation of the Russian rouble, the contraction of the Country's gross domestic product, a significant increase in the Central Bank's lending rates, increased inflation and other factors. The domestic economic situation was further exasperated by the rapid commodity price decline in global oil markets. As a result, in January and February 2015, both Standard & Poor's (S&P) and Moody's downgraded the Russian sovereign rating to below investment rating status as well as made the corresponding downward adjustments to Russian issuers, including NOVATEK. We strongly disagree with such assessment of our credit rating because our operating results and cash flow generating capabilities to support our liquidity position remain strong.

In 2015 and 2016, the Central Bank's lending rates gradually decreased, whereas the Russian rouble exchange rates relative to world currencies and benchmark commodity prices in international markets remained volatile. Commodity price volatility continues to exert significant influence on financial and operations results in the global oil and gas industry. Our financial results are obviously impacted by these global developments as our export sales are linked to the specific underlying benchmark commodity prices but we believe our business model, representing one of the lowest cost producers in the world, insulates us from severe financial and operational stress. In each quarter of 2015 and 2016, the Group achieved strong operating results and remained free cash flow positive. In November 2016, S&P restored our credit rating to investment grade after the downgrade in January 2015.

Management continues to closely monitor the economic and political environment in Russia and abroad, including the domestic and international capital markets, to determine if any further corrective and/or preventive measures are required to sustain and grow our business. We also closely monitor the present commodity price environment and its impact on our business operations. We do not expect any asset impairments or write-offs resulting from a lower commodity price environment.

We conduct regular reviews of our capital expenditure program and existing debt obligations. In our opinion, the Group's financial position is stable and expected operating cash flows are sufficient to service and repay our debt, as well as to execute our planned capital expenditure programs.

Political events in Ukraine in the beginning of 2014 have prompted a negative reaction by the world community, including economic sanctions levied by the United States of America, Canada and the European Union against certain Russian individuals and legal entities. In July 2014, NOVATEK was included on the OFAC's Sectoral Sanctions Identification List (the "List"), which imposed sanctions that prohibit individuals or legal entities registered or working on the territory of the United States from providing new credit facilities to the Group for longer than 90 days. Despite the inclusion on the List, the Group may conduct any other activities, including financial transactions, with U.S. investors and partners. NOVATEK was included on the List even though the Group does not conduct any business activities in Ukraine, nor does it have any impact on the political and economic processes taking place in this country. Management has assessed the impact of the sanctions described above on the Group's activities taking into consideration the current state of the world economy, the condition of domestic and international capital markets, the Group's business, and long-term projects with foreign partners. We have concluded that the inclusion on the List does not significantly impede the Group's operations and business activities in any jurisdiction, nor does it affect the Group's assets and exchange listed shares and debt, and does not have a material effect on the Group's financial position.

We together with our international partners are undertaking all necessary actions to implement the joint investment projects on time as planned, including, but not limited to, attracting financing from domestic and non-US capital markets.

Natural gas prices

The Group's natural gas prices on the domestic market are strongly influenced by the prices set by a federal executive agency of the Russian Federation that carries out governmental regulation of prices and tariffs for products and services of natural monopolies in energy, utilities and transportation (the "Regulator"), as well as present market conditions. During the first half of 2015, the Federal Tariffs Service ("FTS") fulfilled the Regulator's role. In July 2015, a Decree of the President of the Russian Federation became effective abolishing the FTS and transferring its functions to the Federal Anti-Monopoly Service.

In 2015, wholesale natural gas prices for sales to all customer categories (excluding residential customers) on the domestic market were increased by the Regulator effective 1 July by 7.5% and remained unchanged through the end of 2016.

In November 2016, the Ministry of Economic Development of the Russian Federation published the "Forecast of Socio-economic Development of the Russian Federation for 2017 and planned period 2018 and 2019" stating that wholesale natural gas prices for sales to all customer categories (excluding residential customers) will be increased from 1 July 2017, 2018 and 2019 by an average of 3.9%, 3.4% and 3.1%, respectively. The Russian Federation government continues to discuss various concepts relating to the natural gas industry development, including natural gas prices and transportation tariffs growth rates on the domestic market.

The specific terms for delivery of natural gas affect our average realized prices. The majority of our natural gas volumes are sold directly to end-customers in the regions of natural gas consumption, so transportation tariff to the end customer's location is included in the contract sales price. The remaining volumes of natural gas are sold "ex-field" to wholesale gas traders, in which case the buyer is responsible for the payment of further gas transportation tariff. Sales to wholesale gas traders allow us to diversify our natural gas sales without incurring additional commercial expenses.

We deliver natural gas to residential customers in the Chelyabinsk and Kostroma regions of the Russian Federation at regulated prices through our subsidiaries OOO NOVATEK-Chelyabinsk and OOO NOVATEK-Kostroma, respectively. We disclose such residential sales within our end-customers category.

In addition, we periodically sell natural gas at the Saint-Petersburg International Mercantile Exchange based on market conditions. We disclose such sales within our sales to end-customers category.

In 2016, our average natural gas price on end-customers sales was relatively flat due to an increase in the proportion of sales to our end-customers located closer to our production fields in 2016 as compared to 2015, on one hand, and an increase in wholesale natural gas prices by 7.5% effective 1 July 2015, on the other hand. The change in the sales geography also reduced our average transportation expense per mcm by 4.0%, despite an average 2.0% increase in the natural gas regulated transportation tariff effective 1 July 2015 (see "Transportation tariffs" below). As a result, the average natural gas price on end-customers sales excluding transportation expenses increased by 2.7%.

The following table shows our average realized natural gas sales prices (excluding VAT):

	Year ended 31 December:		**Change**
Russian roubles per mcm	**2016**	**2015**	**%**
Average natural gas price to end-customers [1]	3,677	3,678	(0.0%)
Average natural gas transportation expense for sales to end-customers	(1,423)	(1,483)	(4.0%)
Average natural gas price on end-customer sales excluding transportation expense	2,255	2,196	2.7%
Average natural gas price ex-field (wholesale traders)	2,051	1,965	4.4%
Total average natural gas price excluding transportation expense	**2,239**	**2,180**	**2.7%**

[1] Includes cost of transportation.

Stable gas condensate and refined products, crude oil and liquefied petroleum gas prices

Crude oil, stable gas condensate, LPG and oil products prices on international markets have historically been volatile depending on, among other things, the balance between supply and demand fundamentals, the ability and willingness of oil producing countries to sustain or change production levels to meet changes in global demand and potential disruptions in global crude oil supplies due to war, geopolitical developments, terrorist activities or natural disasters.

The actual prices we receive for our liquid hydrocarbons on both the domestic and international markets are dependent on many external factors beyond the control of management. Among many other factors volatile movements in benchmark crude oil and oil products prices can have a positive and/or negative impact on the contract prices we receive for our liquids sales volumes.

In addition, our actual realized net export prices for crude oil, stable gas condensate and its refined products are affected by the so-called "export duty lag effect". This effect is due to the differences between actual crude oil prices for a certain period and crude oil prices based on which export duty rate is calculated for the same period (see "Our tax burden and obligatory payments" below). In periods when crude oil prices are rising, the duty lag effect normally has a positive impact on the Group's financial results, as the export duty rates are set on the basis of lower crude oil prices compared to the actual prices. Conversely, in periods of crude oil prices decline, the export duty rate is calculated based on higher prices compared to the actual prices, which results in a negative financial impact.

Most of our liquid hydrocarbons sales prices on both the international and domestic markets include transportation expenses in accordance with the specific terms of delivery. The remaining portion of our liquids volumes is sold without additional transportation expenses (ex-works sales of liquefied petroleum gas from the Purovsky Plant and the Tobolsk Refining Facilities, as well as certain other types of sales).

We commonly sell our stable gas condensate and refined products, as well as liquefied petroleum gas to the international markets with a premium to the respective international benchmark reference products prices. Our crude oil sold to the international markets is commonly traded with a discount to the benchmark Brent crude oil in case of SILCO grade sales (low-sulfur "Siberian Light Crude Oil") and with a premium to the benchmark Dubai crude oil in case of ESPO grade sales (crude oil delivered by the pipeline "East Siberia – Pacific ocean").

The following table shows our average realized stable gas condensate and refined products, crude oil and LPG sales prices. Average realized net prices are shown net of VAT, export duties, excise and fuel taxes expense, where applicable:

Russian roubles or US dollars per ton	Year ended 31 December: 2016	2015	Change %
Stable gas condensate			
Export contract price, USD per ton	358	394	(9.1%)
Net export price, USD per ton	286	282	1.4%
Net export price, RR per ton	19,430	16,842	15.4%
Domestic price, RR per ton	14,550	14,601	(0.3%)
Naphtha			
Export contract price, USD per ton	424	494	(14.2%)
Net export price, USD per ton	373	390	(4.4%)
Net export price, RR per ton	25,067	23,203	8.0%
Other gas condensate refined products			
Export contract price, USD per ton	377	473	(20.3%)
Net export price, USD per ton	335	401	(16.5%)
Net export price, RR per ton	22,432	24,064	(6.8%)
Domestic price, RR per ton	18,328	19,320	(5.1%)
Crude oil			
Export contract price, USD per ton	303	371	(18.3%)
Net export price, USD per ton	229	250	(8.4%)
Net export price, RR per ton	15,084	14,922	1.1%
Domestic price, RR per ton	13,451	12,967	3.7%
LPG			
Export contract price, USD per ton (1)	488	506	(3.6%)
Net export price, USD per ton (1)	349	385	(9.4%)
Net export price, RR per ton	23,407	23,457	(0.2%)
Domestic price, RR per ton	8,693	11,707	(25.7%)

(1) For operations in Polish zloty price in US dollars was translated from Russian roubles using the average exchange rate for the period.

Crude oil, stable gas condensate and gas condensate refined products

In 2016, our average realized export contract prices for stable gas condensate, gas condensate refined products and crude oil decreased compared to 2015 primarily due to decreases in the underlying respective product prices on the international markets (see "Selected macro-economic data" above). Our weighted-average stable gas condensate export contract price decreased to a lesser extent as a result of uneven distribution of sales volumes within periods, changes in the geography of shipments and significant volatility of benchmark crude oil prices on international markets.

A significant decrease in average export duties for liquid hydrocarbons sales (see "Selected macro-economic data" above), as well as an average 10.0% appreciation of the US dollar relative to the Russian rouble in 2016 compared to 2015 had a positive impact on our average realized net export prices. As a result, our average realized net export prices in Russian roubles terms increased for stable gas condensate, naphtha and crude oil. Our average realized net export prices for other gas condensate refined products in Russian rouble terms decreased but were also in line with the benchmark crude oil prices movements for these products net of the respective export duties.

In 2016, our average realized domestic prices for crude oil, stable gas condensate and its refined products changed marginally compared to 2015 as a result of the respective changes in benchmark crude oil prices excluding export duties in Russian roubles terms, and specifics of pricing mechanism for each particular product on the domestic market (such as time lag of international benchmark crude oil prices and export duty rates used in price calculation, price setting on an individual transaction basis for some deliveries and others).

Liquefied petroleum gas

In 2016, our average realized LPG export contract price decreased compared to 2015 due to a decrease in the underlying benchmark prices for LPG on international markets used in price calculation (see "Selected macro-economic data" above), which was partially offset by changes in sales geography (increase in the share of sales to Poland where the contract price is higher than prices for sales to other countries according to the delivery terms). Our average realized LPG net export price in Russian roubles terms stayed relatively flat as a result of a 10.0% appreciation of the average exchange rate of the US dollar relative to the Russian rouble in 2016 compared to 2015.

In 2016, our average realized LPG domestic price decreased compared to 2015 mainly due to a decrease in the underlying benchmark prices for LPG on international markets and increased transportation tariffs as these figures form the basis for the price setting of some LPG deliveries.

Transportation tariffs

Natural gas

We transport our natural gas through our own pipelines into the Unified Gas Supply System ("UGSS"), which is owned and operated by PAO Gazprom, a Russian Federation government controlled monopoly. Transportation tariffs charged to independent producers for the use of the Gas Transmission System ("GTS"), as part of the UGSS, are set by the Regulator (see "Terms and abbreviations" below).

In accordance with the existing methodology of calculating transportation tariffs for natural gas produced in the Russian Federation for shipments to consumers located within the customs territory of the Russian Federation and the member states of the Customs Union Agreement (Belarus, Kazakhstan, Kyrgyzstan and Tajikistan), the transportation tariff consists of two parts: a rate for the utilization of the trunk pipeline and a transportation rate per mcm per 100 kilometers (km). The rate for utilization of the trunk pipeline is based on an "input/output" function, which is determined by where natural gas enters and exits the trunk pipeline and includes a constant rate for end-customers using Gazprom's gas distribution systems. The constant rate is deducted from the utilization rate for end-customers using non-Gazprom gas distribution systems.

In the first half of 2015, the transportation rate was set at RR 12.79 per mcm per 100 km (excluding VAT), and the rate for utilization of the trunk pipeline was set in the range from RR 57.18 to RR 2,048.11 per mcm (excluding VAT).

Effective 1 July 2015, the average tariff for natural gas transportation through the trunk pipeline was increased by 2.0% and remained unchanged through the end of 2016. The transportation rate amounted to RR 13.04 per mcm per 100 km (excluding VAT), and the rate for utilization of the trunk pipeline was set in the range from RR 62.57 to RR 2,014.16 per mcm (excluding VAT).

According to the Forecast of the Ministry of Economic Development of the Russian Federation published in November 2016, the increase in tariffs for natural gas transportation through the trunk pipeline in 2017 to 2019 will not exceed the growth rate for wholesale natural gas prices (see "Natural gas prices" above). The Russian Federation government continues to discuss various concepts relating to the natural gas industry development, including natural gas prices and transportation tariffs growth on the domestic market.

Stable gas condensate and LPG by rail

We transport stable gas condensate and LPG (excluding volumes sold ex-works from the Purovsky Plant and the Tobolsk Refining Facilities) by rail owned by Russia's state-owned monopoly railway operator – OAO Russian Railways ("RZD").

The railroad transportation tariffs are set by the Regulator and vary depending on the type of a product, direction and the length of the transport route. In addition, the Regulator sets the range of railroad tariffs as a percentage of the regulated tariff within which RZD may vary railroad transportation tariffs within the Russian Federation territory based on the type of product, direction and length of the transportation route taking into account current railroad transportation and market conditions.

During 2015, railroad freight transportation tariffs for all types of hydrocarbons did not change. Effective 3 January 2016, railroad freight transportation tariffs for all types of hydrocarbons were increased by 9% relative to the 2015 tariffs and did not change until the end of 2016. In January 2017, the Regulator increased the aforementioned tariffs by 6.1% relative to the 2016 tariffs.

In 2015 and 2016, we applied the discount coefficient of 0.94 to the existing railroad transportation tariffs for stable gas condensate deliveries from the Limbey rail station to the port of Ust-Luga and to end-customers on the domestic and export (only in 2016) markets. In December 2016, the discount co-efficient was extended until the end of 2017. The discount coefficient is set by the decision of the Management Board of RZD as part of the Strategic Partnership Agreement between the Group and RZD.

Stable gas condensate and refined products by tankers

We deliver part of our stable gas condensate and substantially all stable gas condensate refined products to international markets by chartered tankers via the port of Ust-Luga on the Baltic Sea. The tanker transportation cost is determined by standard shipping terms, the distance to the final port of destination, tanker availability and seasonality of deliveries.

Crude oil

We transport nearly all of our crude oil through the pipeline network owned by PAO Transneft, Russia's state-owned monopoly crude oil pipeline operator. The Regulator sets tariffs for transportation of crude oil through Transneft's pipeline network, which includes transport, dispatch, pumping, loading, charge-discharge, transshipment and other related services. The Regulator sets tariffs for each separate route of the pipeline network, so the overall expense for the transport of crude oil depends on the length of the transport route from the producing fields to the ultimate destination, transportation direction and other factors.

During 2015, crude oil transportation tariffs within the Russian Federation territory through the pipeline network did not change. Effective 1 January 2016, crude oil transportation tariffs were increased by an average of 5.76% relative to the 2015 tariffs and remained unchanged until the end of 2016. Effective 1 January 2017, crude oil transportation tariffs were increased by an average of 3.6% compared to 2016 tariffs.

Our tax burden and obligatory payments

We are subject to a wide range of taxes imposed at the federal, regional, and local levels, many of which are based on revenue or volumetric measures. In addition to income tax, significant taxes and obligatory payments to which we are subject include VAT, unified natural resources production tax ("UPT", commonly referred as "MET" – mineral extraction tax), export duties, property tax and social contributions to non-budget funds.

In practice, Russian tax authorities often have their own interpretation of tax laws that rarely favors taxpayers, who have to resort to court proceedings to defend their position against the tax authorities. Differing interpretations of tax regulations exist both among and within government ministries and organizations at the federal, regional and local levels, creating uncertainties and inconsistent enforcement. Tax declarations, together with related documentation such as customs declarations, are subject to review and investigation by a number of authorities, each of which may impose fines, penalties and interest charges. Generally, taxpayers are subject to an inspection of their activities for a period of three calendar years immediately preceding the year in which the audit is conducted. Previous audits do not completely exclude subsequent claims relating to the audited period. In addition, in some instances, new tax regulations may have a retroactive effect.

We have not employed any tax minimization schemes using offshore or domestic tax zones in the Russian Federation.

The tax maneuver in the oil and gas industry

In November 2014, as part of the tax maneuver in the oil and gas industry, a federal law №366-FZ "Concerning introducing changes to the second part of the Tax Code of the Russian Federation and certain legislative acts of the Russian Federation" was adopted which envisages the increase in national budgetary income as a result of the phased (during three years) increases in UPT rates with a simultaneous decrease in excise taxes and export duties (see below).

UPT – natural gas and gas condensate

In accordance with the Tax Code of the Russian Federation, the UPT rates for natural gas and gas condensate are calculated monthly according to a formula based on which the set base UPT rate is multiplied by the base value of a standard fuel equivalent and a coefficient characterizing the difficulty of extracting natural gas and gas condensate from each particular field. In addition, the formula for gas condensate UPT rate is multiplied by an adjusting coefficient, and the UPT rate for natural gas also takes into account a parameter characterizing natural gas transportation costs (the latter was set at zero for 2015 and 2016 and did not affect the UPT rate).

The base UPT rate is set at RR 35 per one thousand cubic meters of extracted natural gas and at RR 42 per one ton of extracted gas condensate. The base value of a standard fuel equivalent is calculated monthly and depends primarily on natural gas prices, Urals crude oil prices and crude oil export duty rate.

A coefficient characterizing the difficulty of extracting natural gas and gas condensate is defined as a minimum value from the coefficients characterizing either the reserves' depletion, the field's geographical location, the deposit's (or reservoir's) depth, assignment of the field to the regional gas supply chain or particular features of certain field deposits development.

In 2015, the adjusting coefficient for gas condensate UPT rate calculation was set at 4.4 and was increased to 5.5, or 25.0%, from 1 January 2016. Effective 1 January 2017, the adjusting coefficient for the Group was set at 6.5 (increased by 18.2% in relation to 2016).

UPT – crude oil

In both reporting periods, the UPT rate for crude oil was calculated as the base UPT rate multiplied by a coefficient characterizing the dynamics of world crude oil prices, and the resulting product was further decreased by a parameter characterizing crude oil production peculiarities. The base crude oil UPT rate in 2015 was set at RR 766 per ton and was increased to RR 857 per ton effective 1 January 2016. Effective 1 January 2017, the base UPT rate was set at RR 919 per ton.

In 2015 and 2016, in accordance with the Tax Code of the Russian Federation, we applied a reduced UPT rate for crude oil produced at our Yurkharovskoye, East-Tarkosalinskoye, 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. In 2016, the UPT rate for crude oil produced at the aforementioned fields was calculated using an effective rate of RR 298 per ton (increased by 26.3% compared to 2015) multiplied by a coefficient characterizing the dynamics of world crude oil prices. From 1 January 2017, the effective rate was set at RR 360 per ton. In November 2016, amendments were made to the Tax Code of the Russian Federation that envisage additional increase in the overall crude oil UPT rates calculated using a formula described above in 2017 to 2019 by RR 306, RR 357 and RR 428 per ton, respectively.

Export duties and excise taxes

According to the Law of the Russian Federation "On Customs Tariff" we are subject to export duties on our exports of liquid hydrocarbons (stable gas condensate and refined products, LPG and crude oil). Formulas for export duty rates calculation are set by the Russian Federation government. Based on the set formulas the Ministry of Economic Development calculates and publishes export duty rates on a monthly basis (see "Selected macro-economic data" above).

The export duty rate for stable gas condensate and crude oil for the next calendar month is calculated based on the average Urals crude oil price for the period from the 15th calendar day in the previous month to the 14th calendar day of the current month. In 2015, the calculation of the export duty rate in US dollars per ton when the average Urals crude oil price is more than USD 182.5 per ton (or USD 25 per barrel) was set as follows: USD 29.2 plus 42% of the difference between the average Urals crude oil price and USD 182.5 per ton. As part of the tax maneuver in the oil and gas industry (see above), effective 1 January 2016, the set percentage should have been decreased to 36%. However, in order to increase state budget income in 2016 in the anticipation of a lower crude oil price environment, in November 2015, the Russian Federation government made a decision not to adjust the formula for crude oil export duty rate calculation in 2016 and to keep a set percentage at the 2015 level of 42%. Effective 1 January 2017, the set percentage was reduced to 30%.

The export duty rates for oil products is calculated based on the export duty rate for crude oil which is adjusted by a coefficient set for each category of oil products. The export duty rates for our exported gas condensate refined products as a percentage of the crude oil export duty rate are presented below:

% from the crude oil export duty rate	**2015**	**2016**	**2017 and further**
Naphtha	85%	71%	55%
Jet fuel	48%	40%	30%
Gasoil	48%	40%	30%
Fuel oil	76%	82%	100%

The phased decrease in export duty rates for oil products (except fuel oil) is also implemented as part of the tax maneuver in the oil industry with a simultaneous increase in the UPT rates for gas condensate and crude oil (see above).

The export duty rate for LPG for the next calendar month is calculated based on the average LPG price at the Polish border (DAF, Brest) for the period from the 15th calendar day in the previous month to the 14th calendar day of the current month. The formula for LPG export duty rate calculation is presented in the table below:

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)

As the average LPG price for the export duty rate calculation was below USD 490 per ton, in 2015 and 2016 (except for January 2015), we applied a zero export duty rate in respect of our LPG export sales.

In accordance with the Tax Code of the Russian Federation, producers of excisable goods (petrol, diesel fuel, medium distillates and others) that sell those goods on the domestic market are subject to excise tax payments. The Group does not sell excisable goods of own production on the domestic market and, therefore, does not pay excise taxes in Russia.

Most of our LPG sales in Poland are subject to excise and fuel taxes in accordance with the local legislation. The amount of excise and fuel tax payments depends on the volume of excisable goods sold and the respective tax rates (the excise and fuel tax rates in 2015 and 2016 did not change and amounted to 670 and 159.71 Polish zloty per ton, respectively).

Social contributions

In 2015 and 2016, the rates for social contributions to the Pension Fund of the Russian Federation, the Federal Compulsory Medical Insurance Fund and the Social Insurance Fund of the Russian Federation paid by the employer on behalf of employees did not change and were set at 22.0%, 5.1% and 2.9%, respectively (cumulatively 30.0%).

The employer applies the aforementioned rates for social contributions to the Pension Fund of the Russian Federation and the Social Insurance Fund of the Russian Federation until the annual income of an employee exceeds the maximum taxable base set by the Russian Federation government. For the portion of the annual income exceeding the maximum base the reduced rates are applied: 10.0% for the Pension Fund of the Russian Federation and nil for the Social Insurance Fund of the Russian Federation.

The rate for social contributions to the Federal Compulsory Medical Insurance Fund does not vary with the employee's annual income.

The table below provides for the rates and maximum taxable bases set by the Russian Federation government for social contributions in 2015, 2016 and 2017:

	2015		**2016**		**2017**	
	Base, RR thousand	**Rate, %**	**Base, RR thousand**	**Rate, %**	**Base, RR thousand**	**Rate, %**
Pension Fund of the Russian Federation	less 711	22.0%	less 796	22.0%	less 876	22.0%
	above 711	10.0%	above 796	10.0%	above 876	10.0%
Federal Compulsory Medical Insurance Fund	No limit	5.1%	No limit	5.1%	No limit	5.1%
Social Insurance Fund of the Russian Federation	less 670	2.9%	less 718	2.9%	less 755	2.9%
	above 670	0.0%	above 718	0.0%	above 755	0.0%

OIL AND GAS RESERVES

We do not file with the Securities and Exchange Commission ("SEC") nor are obliged to report our reserves in compliance with these standards. However, we have consistently disclosed proved oil and gas reserves as unaudited supplemental information in the Group's IFRS audited consolidated financial statements. The Group's total proved reserves, comprised of proved developed and proved undeveloped reserves, as of 31 December 2016 and 2015, are provided using the SEC reserves reporting classification. We also provide additional information about our hydrocarbon reserves based on the widely-industry accepted PRMS reserves reporting classification, which in addition to total proved reserves discloses information on our probable and possible reserves.

The Group's reserves are located in the Russian Federation, primarily in the Yamal-Nenets Autonomous Region (Western Siberia), thereby representing one geographical area.

The Group's oil and gas estimation and reporting process involves an annual independent external appraisal, as well as internal technical appraisals of reserves. The internal technical appraisals of reserves are performed by the Group's qualified technical staff working directly with the oil and gas reserves and are periodically updated during the year based on evaluations of new wells, performance reviews, new technical information and other studies.

The annual independent external appraisal of our reserves is performed by independent petroleum engineers, DeGolyer and MacNaughton ("D&M"). The Group provides D&M annually with engineering, geological and geophysical data, actual production histories and other information necessary for reserves appraisal. The method or combination of methods used in the analysis of each reservoir is tempered by experience with similar reservoirs, stages of development, quality and completeness of basic data, and production history. Our reserves estimates were prepared using standard geological and engineering methods generally accepted in the oil and gas industry. The Group and D&M's technical staffs meet to review and discuss the information provided, and upon completion of the process, senior management reviews and approves the final reserves estimates issued by D&M.

The Reserves Management and Assessment Group ("RMAG") is comprised of qualified technical staff from various departments – geological and geophysical, gas and liquids commercial operations, engineering and capital construction, production, long-term financing planning and includes representatives from the Group's subsidiaries, which are the principal holders of the mineral licenses for geological research works, exploration and production of hydrocarbons. The person responsible for overseeing the work of the RMAG is a member of the Management Board.

The approval of the final reserve estimates is the sole responsibility of the Group's senior management.

The information below provides for our oil and gas reserves under SEC and PRMS reserve classifications including 100% of reserves attributable to all consolidated subsidiaries (whether or not wholly owned), as well as our proportionate share of reserves in companies accounted for by the equity method based on our equity ownership interest.

The table below provides proved oil and gas reserves under SEC reserve classification in Metric units and on a total barrel of oil equivalent basis:

	As of and for the years ended 31 December:		Change
	2016	2015	%
Natural gas, billions of cubic meters	**1,755**	**1,775**	**(1.1%)**
Subsidiaries	1,029	1,034	(0.5%)
Share in joint ventures	726	741	(2.0%)
Liquids, millions of metric tons	**152**	**143**	**6.3%**
Subsidiaries	73	68	7.4%
Share in joint ventures	79	75	5.3%
Combined reserves, millions of boe	**12,775**	**12,817**	**(0.3%)**
Production, millions of boe	537	522	3.0%
Disposals (1), millions of boe	351	74	n/a
Reserves replacement ratio (2), %	**92%**	**133%**	
Normalized reserves replacement ratio (3), %	**168%**	**148%**	

(1) Represent reserves attributable to the disposal of a 9.9% participation interest in Yamal LNG in March 2016 and to the disposal of a 1.6% effective ownership interest in SeverEnergia in August 2015.

(2) The reserves replacement ratio is calculated as the difference between the reserves at the end of the year and the reserves at the beginning of the year plus production for the year and dividing the sum by production for the year.

(3) Excluding the effect of the disposal of a 9.9% participation interest in Yamal LNG in March 2016 and the disposal of a 1.6% effective ownership interest in SeverEnergia in August 2015.

Excluding the effect from the disposal of a 9.9% participation interest in Yamal LNG, our total proved reserves under SEC reserve classification increased by 2.8% and we effectively replaced 168% of our production as calculated under the normalized reserves replacement ratio. Additions to our natural gas proved reserves were primarily due to revisions of previous estimates at our Salmanovskoye (Utrenneye) field and at the South-Tambeyskoye field of our joint venture Yamal LNG, as well as reserves added due to successful exploration works at our Kharbeyskoye and Dorogovskoye fields discovered in June 2013 and August 2014, respectively. Additions to our liquid hydrocarbons proved reserves mainly related to revisions of previous estimates and extensions of the reserves at our Yarudeyskoye and Salmanovskoye (Utrenneye) fields. The launch of additional production facilities at our subsidiaries and joint ventures during 2015 allowed us to increase overall production of natural gas and liquid hydrocarbons in 2016 by 15 million boe, or 3.0% (see "Recent developments" above).

The following table provides for the Group's PRMS proved, probable and possible reserves in Metric units and on a total barrel of oil equivalent basis:

	Natural gas, billions of cubic meters		Liquid hydrocarbons, millions of metric tons		Combined reserves, millions of boe	
	31 December 2016	31 December 2015 (1)	31 December 2016	31 December 2015(1)	31 December 2016	31 December 2015(1)
Proved reserves	1,987	2,118	181	177	14,530	15,344
Probable reserves	1,080	1,034	138	121	8,226	7,773
Proved and probable	**3,067**	**3,152**	**319**	**298**	**22,756**	**23,117**
Possible reserves	594	662	122	110	4,874	5,230
Proved, probable and possible	**3,661**	**3,814**	**441**	**408**	**27,630**	**28,347**

(1) At 31 December 2015, the Group's share in reserves of joint ventures included reserves attributable to the 9.9% interest in Yamal LNG classified as held for sale (the transaction was completed in March 2016).

As we continue to invest capital into the development of our fields, we anticipate that we will increase our resource base as well as migrate reserves among the reserve categories.

The below table contains information about reserve to production ratios as of 31 December 2016 and 2015 under both reserves reporting methodologies:

	SEC		**PRMS**	
	At 31 December:		**At 31 December:**	
Number of years	**2016**	**2015**	**2016**	**2015**
Total proved reserves to production	24	25	27	29
Total proved and probable reserves to production	-	-	42	44
Total proved, probable and possible reserves to production	-	-	51	54

OPERATIONAL HIGHLIGHTS

Oil and Gas Production Costs

Oil and gas production costs are derived from our results of operations for oil and gas producing activities as reported in the "Unaudited Supplemental Oil and Gas Disclosures" in our consolidated financial statements and relate to the fields of our consolidated subsidiaries. Oil and gas production costs do not include general corporate overheads or their associated tax effects. The following tables set forth certain operating information with respect to our oil and gas production costs during the years presented in millions of Russian roubles and on a barrel of oil equivalent (boe) basis in Russian roubles and US dollars:

	Year ended 31 December:		Change
millions of Russian roubles	2016	2015	%
Production costs:			
Lifting costs	13,865	10,705	29.5%
Taxes other than income tax	43,844	36,296	20.8%
Transportation expenses	76,356	83,574	(8.6%)
Total production costs before DDA	**134,065**	**130,575**	**2.7%**
Depreciation, depletion and amortization ("DDA")	32,049	17,522	82.9%
Total production costs	**166,114**	**148,097**	**12.2%**

	Year ended 31 December:		Change
RR per boe	2016	2015	%
Production costs:			
Lifting costs	38.4	30.1	27.6%
Taxes other than income tax	121.4	102.1	18.9%
Transportation expenses	211.3	235.1	(10.1%)
Total production costs before DDA	**371.1**	**367.3**	**1.0%**
Depreciation, depletion and amortization	88.7	49.3	79.9%
Total production costs	**459.8**	**416.6**	**10.4%**

	Year ended 31 December:		Change
USD per boe (1)	2016	2015	%
Production costs:			
Lifting costs	0.57	0.49	16.3%
Taxes other than income tax	1.81	1.67	8.4%
Transportation expenses	3.16	3.87	(18.3%)
Total production costs before DDA	**5.54**	**6.03**	**(8.1%)**
Depreciation, depletion and amortization	1.32	0.80	65.0%
Total production costs	**6.86**	**6.83**	**0.4%**

(1) Production costs in US dollars per boe were translated from Russian roubles per boe using the average exchange rate for the period (see "Selected macro-economic data" above).

Oil and gas production costs represent the amounts directly related to the extraction of natural gas, gas condensate and crude oil from the reservoir and other related costs; including lifting costs, taxes other than income tax (unified natural resources production tax, property tax and other taxes), insurance expenses and shipping, transportation and handling costs to end-customers. The average production cost on a barrel of oil equivalent basis is calculated by dividing the applicable costs by the respective barrel of oil equivalent of our hydrocarbons produced during the year. Natural gas, gas condensate and crude oil volumes produced at our fields are converted to a barrel of oil equivalent based on the relative energy content of each fields' hydrocarbons.

Our lifting costs, as presented in the tables above, differ from lifting costs as reflected in the "Unaudited Supplemental Oil and Gas Disclosures", in that the lifting costs as presented in the Group's IFRS consolidated financial statements include changes in balances of natural gas and liquid hydrocarbons to more appropriately match costs incurred to revenues under the IFRS matching principles. A reconciliation of lifting costs as reflected in the "Unaudited Supplemental Oil and Gas Disclosures" is set forth below:

millions of Russian roubles	**Year ended 31 December: 2016**	**2015**	**Change %**
Lifting costs presented in "Oil and Gas Production Costs" above	13,865	10,705	29.5%
Change in balances of natural gas and hydrocarbon liquids stated at cost in the Group's Consolidated Statement of Financial Position	368	(603)	n/a
Lifting costs per "Unaudited Supplemental Oil and Gas Disclosures"	**14,233**	**10,102**	**40.9%**

Hydrocarbon production and sales volumes

In 2016, our total natural gas sales volumes increased by 2,244 mmcm, or 3.6%, as a result of sales of additional natural gas volumes to our end-customers and wholesale traders, as well as restoring sales to one of our major customers who did not take full contracted volumes in 2015 due to technical reasons. Natural gas volumes produced at mature fields of our subsidiaries decreased, but were offset to a significant extent by an increase in the production of our joint ventures.

In 2016, our liquids sales volumes increased significantly by 3,962 thousand tons, or 30.7%, primarily due to the commencement of crude oil commercial production at the Yarudeyskoye field in December 2015.

Natural gas production volumes

In 2016, our total natural gas production (including our proportionate share in the production of joint ventures) decreased by 1,802 mmcm, or 2.7%, to 66,103 mmcm from 67,905 mmcm in 2015.

millions of cubic meters	**Year ended 31 December:** **2016**	**2015**	**Change %**
Production by subsidiaries from:			
Yurkharovskoye field	33,766	35,979	(6.2%)
East-Tarkosalinskoye field	8,015	9,075	(11.7%)
Khancheyskoye field	2,473	2,510	(1.5%)
Other fields	1,981	1,608	23.2%
Total natural gas production by subsidiaries	**46,235**	**49,172**	**(6.0%)**
Group's proportionate share in the production of joint ventures:			
SeverEnergia (Arcticgas)	13,682	12,624	8.4%
Nortgas	5,023	5,395	(6.9%)
Terneftegas	1,163	714	62.9%
Total Group's proportionate share in the natural gas production of joint ventures	**19,868**	**18,733**	**6.1%**
Total natural gas production including proportionate share in the production of joint ventures	**66,103**	**67,905**	**(2.7%)**

In 2016, total natural gas volumes produced by our subsidiaries decreased by 2,937 mmcm, or 6.0%, to 46,235 mmcm from 49,172 mmcm in 2015 due to natural declines in the reservoir pressure at the current gas producing horizons at our mature fields (Yurkharovskoye, East-Tarkosalinskoye and Khancheyskoye). The decrease was partially offset by the launch of the Yarudeyskoye field in December 2015.

In 2016, our proportionate share in the production of our joint ventures increased by 1,135 mmcm, or 6.1%, to 19,868 mmcm from 18,733 mmcm in 2015 primarily as a result of the production growth in SeverEnergia. The production of SeverEnergia increased due to reaching the nameplate production capacity of the second phase of the Urengoyskoye field in February 2015, as well as the launch of the Yaro-Yakhinskoye field in April 2015, the nameplate production capacity of which was reached in June 2015. In addition, effective May 2015, our joint venture Terneftegas commenced production at the Termokarstovoye field and reached the nameplate production capacity in June 2015. The production at the mature field of Nortgas decreased due to natural declines in the reservoir pressure at the current gas producing horizons.

Natural gas sales volumes

In 2016, our total natural gas sales volumes increased by 2,244 mmcm, or 3.6%, to 64,709 mmcm from 62,465 mmcm in 2015.

millions of cubic meters	**Year ended 31 December: 2016**	**2015**	**Change %**
Production by subsidiaries	46,235	49,172	(6.0%)
Purchases from the Group's joint ventures	10,058	7,152	40.6%
Other purchases	8,108	6,626	22.4%
Total production and purchases	**64,401**	**62,950**	**2.3%**
Own usage [(1)]	(185)	(207)	(10.6%)
Decrease (increase) in GTS, UGSF and own pipeline infrastructure	493	(278)	n/a
Total natural gas sales volumes	**64,709**	**62,465**	**3.6%**
Sold to end-customers	*59,646*	*58,054*	*2.7%*
Sold ex-field	*5,063*	*4,411*	*14.8%*

[(1)] Own usage associated primarily with the maintaining of refining process at the Purovsky Plant, as well as heat and electric energy generation in some of our subsidiaries.

In 2016, natural gas purchases from our joint ventures increased by 2,906 mmcm, or 40.6%, to 10,058 mmcm from 7,152 mmcm in 2015 primarily due to an increase in purchases from SeverEnergia (through its wholly owned subsidiary, OAO Arcticgas) and the commencement of purchases from Terneftegas as a result of the launch of the Termokarstovoye field in May 2015, the nameplate production capacity of which was reached in June 2015.

Other natural gas purchases increased by 1,482 mmcm, or 22.4%, to 8,108 mmcm from 6,626 mmcm in 2015, and are included in our natural gas volumes for sale, which allows us to coordinate sales across geographic regions as well as to optimize end-customers portfolios.

As of 31 December 2016, our natural gas inventory balance in the GTS, the UGSF and our own pipeline infrastructure aggregated 834 mmcm and decreased by 493 mmcm during the year as compared to an increase by 278 mmcm in 2015.

Liquids production volumes

In 2016, our total liquids production (including our proportionate share in the production of joint ventures) increased by 3,347 thousand tons, or 36.8%, to 12,441 thousand tons from 9,094 thousand tons in 2015.

thousands of tons	**Year ended 31 December: 2016**	**2015**	**Change %**
Production by subsidiaries from:			
Yarudeyskoye field	3,556	184	n/a
Yurkharovskoye field	1,813	2,126	(14.7%)
East-Tarkosalinskoye field	1,354	1,365	(0.8%)
Khancheyskoye field	353	392	(9.9%)
Other fields	118	131	(9.9%)
Total liquids production by subsidiaries	**7,194**	**4,198**	**71.4%**
including crude oil	*4,784*	*1,434*	*233.6%*
including gas condensate	*2,410*	*2,764*	*(12.8%)*
Group's proportionate share in the production of joint ventures:			
SeverEnergia (Arcticgas)	4,300	4,016	7.1%
Nortgas	519	622	(16.6%)
Terneftegas	428	258	65.9%
Total Group's proportionate share in the liquids production of joint ventures	**5,247**	**4,896**	**7.2%**
Total liquids production including proportionate share in the production of joint ventures	**12,441**	**9,094**	**36.8%**

In 2016, the volumes of liquids produced by our subsidiaries significantly increased by 2,996 thousand tons, or 71.4%, primarily due to the commencement of crude oil commercial production at the Yarudeyskoye field in December 2015 and reaching the nameplate production capacity by the end of the month (see "Recent developments" above). At the same time gas condensate production decreased due to the natural declines in the concentration of gas condensate at our mature fields (Yurkharovskoye, East-Tarkosalinskoye and Khancheyskoye) as a result of decreasing reservoir pressure at the current gas condensate producing horizons.

In 2016, our proportionate share in liquids production of joint ventures increased by 351 thousand tons, or 7.2%, to 5,247 thousand tons from 4,896 thousand tons in 2015 mainly as a result of production growth at SeverEnergia. The production of SeverEnergia increased due to reaching the nameplate production capacity of the second phases of the Urengoyskoye field in February 2015, as well as the launch of the Yaro-Yakhinskoye field in April 2015, the nameplate production capacity of which was reached in June 2015. In addition, our joint venture Terneftegas commenced production at the Termokarstovoye field in May 2015 and reached the nameplate production capacity in June 2015. The production at the mature field of Nortgas decreased due to natural declines in the concentration of gas condensate as a result of decreasing reservoir pressure at the current gas condensate producing horizons.

Liquids sales volumes

In 2016, our total liquids sales volumes increased by 3,962 thousand tons, or 30.7%, to 16,850 thousand tons from 12,888 thousand tons in 2015 mainly due to an increase in the production of crude oil in our subsidiaries, as well as an increase in gas condensate production of our joint ventures.

thousands of tons	Year ended 31 December: 2016	2015	Change %
Production by subsidiaries	7,194	4,198	71.4%
Purchases from the Group's joint ventures	9,809	9,045	8.4%
Other purchases	124	94	31.9%
Total production and purchases	**17,127**	**13,337**	**28.4%**
Losses [1] and own usage [2]	(284)	(278)	2.2%
Filling the system of processing facilities and pipelines at the Yarudeyskoye field	-	(36)	n/a
Decreases (increases) in liquids inventory balances	7	(135)	n/a
Total liquids sales volumes	**16,850**	**12,888**	**30.7%**
Naphtha export	*4,113*	*4,120*	*(0.2%)*
Other gas condensate refined products export	*2,430*	*2,479*	*(2.0%)*
Other gas condensate refined products domestic	*119*	*94*	*26.6%*
Subtotal gas condensate refined products	***6,662***	***6,693***	***(0.5%)***
Crude oil export	*1,472*	*377*	*290.5%*
Crude oil domestic	*3,178*	*713*	*345.7%*
Subtotal crude oil	***4,650***	***1,090***	***326.6%***
Stable gas condensate export	*1,305*	*1,477*	*(11.6%)*
Stable gas condensate domestic	*1,507*	*1,309*	*15.1%*
Subtotal stable gas condensate	***2,812***	***2,786***	***0.9%***
LPG export	*549*	*551*	*(0.4%)*
LPG domestic	*2,164*	*1,755*	*23.3%*
Subtotal LPG	***2,713***	***2,306***	***17.6%***
Other oil products domestic	*13*	*13*	*0.0%*
Subtotal other oil products	***13***	***13***	***0.0%***

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

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

In 2016, our purchases of liquid hydrocarbons from joint ventures increased by 764 thousand tons, or 8.4%, due to an increase in purchases of gas condensate from SeverEnergia and Terneftegas resulting from the launch of production facilities (see "Liquids production volumes" above).

Sales volumes of jet fuel, gasoil and fuel oil received from the processing of stable gas condensate are disclosed in lines "Other gas condensate refined products export" and "Other gas condensate refined products domestic".

In 2016, our liquids inventory balances slightly decreased by seven thousand tons to 903 thousand tons as of 31 December 2016 as compared to an increase in inventory balances by 171 thousand tons to 910 thousand tons in 2015. Our liquids inventory balances may vary period-to-period depending on shipping schedules and final destinations of stable gas condensate and its refined products shipments (see "Changes in natural gas, liquid hydrocarbons and work-in-progress" below).

RESULTS OF OPERATIONS FOR THE YEAR ENDED 31 DECEMBER 2016 COMPARED TO THE YEAR ENDED 31 DECEMBER 2015

The following table and discussion is a summary of our consolidated results of operations for the years ended 31 December 2016 and 2015. Each line item is also shown as a percentage of our total revenues.

	Year ended 31 December:			
millions of Russian roubles	**2016**	**% of total revenues**	**2015**	**% of total revenues**
Total revenues [1]	**537,472**	***100.0%***	**475,325**	***100.0%***
including:				
natural gas sales	229,716	*42.7%*	222,180	*46.7%*
liquids' sales	304,141	*56.6%*	249,827	*52.6%*
Operating expenses	(385,499)	*(71.7%)*	(335,042)	*(70.5%)*
Other operating income (loss)	221	*0.0%*	(542)	*(0.1%)*
Profit from operations before disposals of interests in joint ventures	**152,194**	***28.3%***	**139,741**	***29.4%***
Net gain on disposal of interests in joint ventures	73,072	*13.6%*	989	*0.2%*
Profit from operations	**225,266**	***41.9%***	**140,730**	***29.6%***
Finance income (expense)	(7,941)	*(1.5%)*	(16,182)	*(3.4%)*
Share of profit (loss) of joint ventures, net of income tax	90,839	*16.9%*	(31,607)	*(6.6%)*
Profit before income tax	**308,164**	***57.3%***	**92,941**	***19.6%***
Total income tax expense	(43,091)	*(8.0%)*	(18,822)	*(4.0%)*
Profit	**265,073**	***49.3%***	**74,119**	***15.6%***
Less: profit (loss) attributable to non-controlling interest	(7,278)	*(1.3%)*	277	*0.1%*
Profit attributable to shareholders of PAO NOVATEK	**257,795**	***48.0%***	**74,396**	***15.7%***
Normalized profit attributable to shareholders of PAO NOVATEK, excluding the effect of foreign exchange gains (losses)	**133,759**	***24.9%***	**132,509**	***27.9%***

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

Total revenues

The following table sets forth our sales (excluding VAT, export duties, excise and fuel taxes expense, where applicable) for the years ended 31 December 2016 and 2015:

	Year ended 31 December:		Change	Change [1]		
millions of Russian roubles	2016	2015	%	Total	Due to volume [2]	Due to price [3]
Natural gas sales	**229,716**	**222,180**	**3.4%**	**7,536**	**7,137**	**399**
End-customers	*219,333*	*213,513*	*2.7%*	*5,820*	*5,857*	*(37)*
Ex-field sales	*10,383*	*8,667*	*19.8%*	*1,716*	*1,280*	*436*
Gas condensate refined products sales	**159,799**	**157,066**	**1.7%**	**2,733**	**(154)**	**2,887**
Export – naphtha	*103,103*	*95,588*	*7.9%*	*7,515*	*(150)*	*7,665*
Export – other refined products	*54,508*	*59,667*	*(8.6%)*	*(5,159)*	*(499)*	*(4,660)*
Domestic – other refined products	*2,188*	*1,811*	*20.8%*	*377*	*495*	*(118)*
Crude oil sales	**64,952**	**14,873**	**336.7%**	**50,079**	**48,303**	**1,776**
Export	*22,198*	*5,629*	*294.4%*	*16,569*	*16,332*	*237*
Domestic	*42,754*	*9,244*	*n/a*	*33,510*	*31,971*	*1,539*
Stable gas condensate sales	**47,271**	**43,997**	**7.4%**	**3,274**	**(22)**	**3,296**
Export	*25,351*	*24,887*	*1.9%*	*464*	*(2,911)*	*3,375*
Domestic	*21,920*	*19,110*	*14.7%*	*2,810*	*2,889*	*(79)*
Liquefied petroleum gas sales	**31,652**	**33,467**	**(5.4%)**	**(1,815)**	**4,735**	**(6,550)**
Export	*12,841*	*12,924*	*(0.6%)*	*(83)*	*(55)*	*(28)*
Domestic	*18,811*	*20,543*	*(8.4%)*	*(1,732)*	*4,790*	*(6,522)*
Other products sales	**467**	**424**	**10.1%**	**43**	**n/a**	**n/a**
Domestic	*467*	*424*	*10.1%*	*43*	*n/a*	*n/a*
Total oil and gas sales	**533,857**	**472,007**	**13.1%**	**61,850**	**n/a**	**n/a**
Other revenues	3,615	3,318	9.0%	297	n/a	n/a
Total revenues	**537,472**	**475,325**	**13.1%**	**62,147**	**n/a**	**n/a**

(1) The figures reflect the impact of sales volumes and average realized prices factors on the change in total revenues from hydrocarbons sales in millions of Russian roubles for the respective periods.

(2) The amount of the change in total revenues due to sales volumes is calculated for each product and selling destination as a product of the average realized price for the previous reporting period and the change in sales volumes.

(3) The amount of the change in total revenues due to average realized prices is calculated for each product and selling destination as a product of the volume sold in the current reporting period and the change in average realized prices.

Natural gas sales

Our revenues from natural gas sales increased by RR 7,536 million, or 3.4%, compared to 2015 due to an increase in volumes sold by 3.6%, while our average sales prices stayed flat. The increase in our total sales volumes was due to sales of additional natural gas volumes to our end-customers and wholesale traders, as well as restoring sales to one of our major customers who did not take full contracted volumes in 2015 due to technical reasons. Our average sales prices changed insignificantly (decreased by 0.2%) due to an increase in the proportion of sales to our end-customers located closer to our production fields in 2016 compared to 2015, as well as an increase from 7.1% to 7.8% in the proportion of natural gas sold to wholesale traders with lower average sales prices compared to end-customer sales, on one hand, and an increase in wholesale natural gas prices by 7.5% effective 1 July 2015, on the other hand (see "Natural gas prices" above).

Gas condensate refined products sales

Gas condensate refined products sales represent revenues from sales of naphtha, jet fuel, gasoil and fuel oil produced from our stable gas condensate at the Ust-Luga Complex.

In 2016, our revenues from sales of gas condensate refined products increased by RR 2,733 million, or 1.7%, as compared to 2015 primarily due to an increase in average realized net export prices for naphtha in Russian roubles terms which was partially offset by a decrease in average realized net export prices for jet fuel, gasoil and fuel oil.

In 2016, our revenues from sales of naphtha increased by RR 7,515 million, or 7.9%, as compared to 2015 due to an increase in average realized net export prices in Russian roubles terms while sales volumes changed insignificantly. In the years ended 31 December 2016 and 2015, we exported 4,113 thousand and 4,120 thousand tons of naphtha, respectively. Nearly all our naphtha volumes were sold to the APR, and the European and North America markets. Our average realized net export price, excluding export duties, increased by RR 1,864 per ton, or 8.0%, to RR 25,067 per ton (CFR, CIF, DES and FOB) from RR 23,203 per ton (CIF, CFR, DES, DAP and FOB) in 2015 (see "Stable gas condensate and refined products, liquefied petroleum gas and crude oil prices" above).

In 2016, our revenues from sales of jet fuel, gasoil and fuel oil on the domestic and export markets decreased by RR 4,782 million, or 7.8%, as compared to 2015 primarily due to a decrease in average realized net export prices in Russian roubles terms. In the years ended 31 December 2016 and 2015, we exported in aggregate 2,430 thousand and 2,479 thousand tons of these products to the European markets, or 95.3% and 96.3% of total sales volumes (on the domestic and export markets), respectively. Our average realized net export price, excluding export duties, decreased by RR 1,632 per ton, or 6.8%, to RR 22,432 per ton (CIF, DES, FOB and DAP) from RR 24,064 per ton (CIF, DES, FOB and DAP) in 2015 (see "Stable gas condensate and refined products, liquefied petroleum gas and crude oil prices" above).

Crude oil sales

In 2016, revenues from crude oil sales increased significantly by RR 50,079 million, or 4.4 times, compared to 2015 due to a significant increase in sales volumes. Our crude oil sales volumes increased by 3,560 thousand tons, or 4.4 times, to 4,650 thousand tons from 1,090 thousand tons in 2015 mainly due to the commencement of crude oil commercial production at the Yarudeyskoye field in December 2015 and reaching the nameplate production capacity by the end of the month.

In 2016, we sold 3,178 thousand tons, or 68.3% of our total crude oil sales volumes, domestically at an average price of RR 13,451 per ton (excluding VAT), representing an increase of RR 484 per ton, or 3.7%, as compared to 2015.

The remaining 1,472 thousand tons, or 31.7% of our total sales volumes, were sold primarily to the APR, and the European and the North America markets at an average net export price of RR 15,084 per ton (FOB, excluding export duties) representing an increase of RR 162 per ton, or 1.1%, as compared to 2015 (see "Stable gas condensate and refined products, liquefied petroleum gas and crude oil prices" above).

Stable gas condensate sales

In 2016, our revenues from sales of stable gas condensate increased by RR 3,274 million, or 7.4%, compared to 2015 primarily due to an increase in average realized net export prices.

In 2016, we sold 1,305 thousand tons of stable gas condensate, or 46.4% of our total sales volumes, compared to 1,477 thousand tons, or 53.0%, in 2015 to the APR and the European markets. Our average realized stable gas condensate net export price, excluding export duties, increased by RR 2,588 per ton, or 15.4%, to RR 19,430 per ton from RR 16,842 per ton (CFR, DAP, CIF and DES in both reporting periods) (see "Stable gas condensate and refined products, liquefied petroleum gas and crude oil prices" above).

In 2016, we sold 1,507 thousand tons of stable gas condensate, or 53.6% of our total sales volumes, on the domestic market compared to 1,309 thousand tons, or 47.0%, in 2015. Our average realized price remained relatively flat compared to 2015 (see "Stable gas condensate and refined products, liquefied petroleum gas and crude oil prices" above).

Liquefied petroleum gas sales

In 2016, our revenues from sales of LPG decreased by RR 1,815 million, or 5.4%, compared to 2015 due to a decrease in average realized domestic prices (see "Stable gas condensate and refined products, liquefied petroleum gas and crude oil prices" above) which was largely offset by an increase in total sales volumes.

In 2016, we sold 549 thousand tons of LPG, or 20.2% of our total LPG sales volumes, to export markets as compared to sales of 551 thousand tons, or 23.9%, in 2015. Our average realized LPG net export price, excluding export duties, excise and fuel taxes expense, changed insignificantly (decreased by RR 50 per ton, or 0.2%).

In 2015 and 2016, our LPG export delivery terms were DAP at the border of the customer's country or free carrier (FCA) at terminal points in Poland. In 2015, we also sold our LPG under carriage paid to (CPT) the Port of Temryuk (southern Russia) delivery terms. We sold most of our LPG export sales volumes to Poland in both reporting periods.

In 2016, we sold 2,164 thousand tons of LPG, or 79.8% of our total LPG sales volumes, on the domestic market compared to sales of 1,755 thousand tons, or 76.1%, in 2015. Our average realized LPG domestic price in 2016, was RR 8,693 per ton representing a decrease of RR 3,014 per ton, or 25.7%, compared to 2015 (see "Stable gas condensate and refined products, liquefied petroleum gas and crude oil prices" above).

Other products sales

Other products sales represent our revenues from the domestic sales of purchased oil products (diesel fuel and petrol) through our retail stations, sales of other purchased liquid hydrocarbons, and sales of our produced methanol. In 2016, our revenues from other products sales increased by RR 43 million, or 10.1%, to RR 467 million from RR 424 million in 2015.

Other revenues

Other revenues include revenue from transportation, geological and geophysical research services, repair and maintenance of energy equipment services, and other services. In 2016, other revenues increased by RR 297 million, or 9.0%, to RR 3,615 million from RR 3,318 million in 2015 primarily due to a RR 297 million increase in revenues from repair and maintenance of energy equipment services provided by our subsidiary NOVATEK-Energo by RR 297 million. At the same time, other revenues increased by RR 170 million in 2016 due to an increase in revenues from services for preparation of third party hydrocarbons for transportation and decreased by RR 188 million due to a decrease in revenues from tankers transporting third party goods.

Operating expenses

In 2016, our total operating expenses increased by RR 50,457 million, or 15.1%, to RR 385,499 million compared to RR 335,042 million in 2015 mainly due to the launch of the Yarudeyskoye field in December 2015 and the respective increase of certain items in transportation, taxes other than income tax expenses, depreciation, depletion and amortization, and materials, services and other expenses. Our total operating expenses as a percentage of total revenues changed insignificantly (increased to 71.7% from 70.5%).

	Year ended 31 December:			
millions of Russian roubles	**2016**	**% of total revenues**	**2015 (1)**	**% of total revenues**
Purchases of natural gas and liquid hydrocarbons	134,268	*25.0%*	120,504	*25.4%*
Transportation expenses	133,462	*24.8%*	130,229	*27.4%*
Taxes other than income tax	44,053	*8.2%*	36,630	*7.7%*
Depreciation, depletion and amortization	34,631	*6.4%*	19,980	*4.2%*
Materials, services and other	19,133	*3.6%*	14,551	*3.1%*
General and administrative expenses	18,126	*3.4%*	14,356	*3.0%*
Exploration expenses	2,087	*0.4%*	1,109	*0.2%*
Impairment expenses (reversals), net	178	*n/a*	(204)	*n/a*
Changes in natural gas, liquid hydrocarbons and work-in-progress	(439)	*n/a*	(2,113)	*n/a*
Total operating expenses	**385,499**	***71.7%***	**335,042**	***70.5%***

(1) Certain reclassifications have been made to the 2015 figures to conform to the current reporting period presentation with no effect on profit for the period or shareholder's equity. Insurance expenses relating to production assets and major part of expenses of the Group's research and development center are presented in this report within Materials, services and other expenses and Exploration expenses depending on their function, which were previously disclosed within General and administrative expenses. Accordingly, expenses in the amount of RR 807 million were reclassified from General and administrative expenses to "Materials, services and other expenses and Exploration expenses in the amount of RR 465 million and RR 342 million, respectively, for the year ended 31 December 2015.

Purchases of natural gas and liquid hydrocarbons

In 2016, our purchases of natural gas and liquid hydrocarbons increased by RR 13,764 million, or 11.4%, to RR 134,268 million from RR 120,504 million in 2015.

millions of Russian roubles	**Year ended 31 December: 2016**	**2015**	**Change %**
Unstable gas condensate	93,854	91,078	3.0%
Natural gas	38,119	27,715	37.5%
Other liquid hydrocarbons	2,295	1,711	34.1%
Total purchases of natural gas and liquid hydrocarbons	**134,268**	**120,504**	**11.4%**

In 2016, our purchases of unstable gas condensate from our joint ventures increased by RR 2,776 million, or 3.0%, as compared to 2015, due to an increase in purchases from SeverEnergia (through its wholly owned subsidiary, OAO Arcticgas) as a result of the launch of additional production capacities in the first half of 2015 (see "Liquids production volumes" above), as well as the commencement of purchases from Terneftegas effective May 2015.

In 2016, our purchases of natural gas increased by RR 10,404 million, or 37.5%, as compared to 2015 as a result of an increase in purchases from SeverEnergia and third parties, as well as the commencement of purchases from Terneftegas since May 2015 (see "Natural gas production volumes" above). In addition, purchase prices increased due to an increase in the average regulated price by 7.5% effective 1 July 2015.

Other liquid hydrocarbons purchases represent our purchases of oil products and LPG for subsequent resale depending on the demand for these types of products. In 2016, our purchases of other liquid hydrocarbons increased by RR 584 million, or 34.1%, as compared to 2015.

Transportation expenses

In 2016, our total transportation expenses increased by RR 3,233 million, or 2.5%, to RR 133,462 million as compared to RR 130,229 million in 2015.

millions of Russian roubles	**Year ended 31 December: 2016**	**2015**	**Change %**
Natural gas transportation by trunk and low-pressure pipelines	84,808	86,025	(1.4%)
Stable gas condensate and liquefied petroleum gas transportation by rail	31,838	29,273	8.8%
Gas condensate refined products, stable gas condensate and crude oil transportation by tankers	9,997	13,378	(25.3%)
Crude oil transportation by trunk pipelines	6,654	1,476	350.8%
Other	165	77	114.3%
Total transportation expenses	**133,462**	**130,229**	**2.5%**

In 2016, despite an average 2.0% increase in the natural gas regulated transportation tariff effective 1 July 2015 (see "Transportation tariffs" above), our expenses for natural gas transportation decreased by RR 1,217 million, or 1.4%, to RR 84,808 million from RR 86,025 million in 2015, due to an increase in the proportion of sales to our end-customers located closer to our production fields in the current year as compared to the previous year.

In 2016, our total expenses for stable gas condensate and LPG transportation by rail increased by RR 2,565 million, or 8.8%, to RR 31,838 million from RR 29,273 million in 2015. The increase was due to a 9.0% increase in our weighted average transportation cost per unit mainly resulted from an increase in the regulated railroad transportation tariffs effective January 2016 (see "Transportation tariffs" above). Volumes of liquids sold and transported via rail remained relatively flat between reporting periods (decreased by 0.3%).

In 2016, our total transportation expenses for liquids delivered by tankers to international markets decreased by RR 3,381 million, or 25.3%, to RR 9,997 million from RR 13,378 million in 2015 as a result of a decrease in average freight rates which fluctuate period-on-period depending on worldwide demand for tankers transportation, as well as a decrease in volumes of liquids sold and transported via tankers by 6.7%.

In 2016, our expenses for crude oil transportation to customers by trunk pipeline significantly increased by RR 5,178 million, or 4.5 times, to RR 6,654 million from RR 1,476 million in 2015, due to a significant 4.3 times increase in volumes transported as a result of the commencement of crude oil commercial production at the Yarudeyskoye field in December 2015.

Taxes other than income tax

In 2016, taxes other than income tax increased by RR 7,423 million, or 20.3%, to RR 44,053 million from RR 36,630 million in 2015 primarily due to an increase in the unified natural resources production tax expense.

millions of Russian roubles	**Year ended 31 December: 2016**	**2015**	**Change %**
Unified natural resources production tax (UPT)	40,997	33,656	21.8%
Property tax	2,793	2,603	7.3%
Other taxes	263	371	(29.1%)
Total taxes other than income tax	**44,053**	**36,630**	**20.3%**

In 2016, our unified natural resources production tax expense increased by RR 7,341 million, or 21.8%, to RR 40,997 million from RR 33,656 million in 2015 primarily due to a significant increase in crude oil production as a result of the commercial production commencement at the Yarudeyskoye field in December 2015. In addition, as a part of the tax maneuver in the oil and gas industry (see "Our tax burden and obligatory payments" above), the adjusting coefficient that is applied in the calculation of the UPT rate for gas condensate was increased by 25.0% from 1 January 2016 in relation to 2015, thus also leading to an increase in our UPT expense.

In 2016, our property tax expense increased by RR 190 million, or 7.3%, to RR 2,793 million from RR 2,603 million in 2015 mainly due to the launch of the Yarudeyskoye field in December 2015, as well as additions to property, plant and equipment at our other production subsidiaries.

Depreciation, depletion and amortization

In 2016, our depreciation, depletion and amortization ("DDA") expense increased by RR 14,651 million, or 73.3%, to RR 34,631 million from RR 19,980 million in 2015 mainly due to the launch of the Yarudeyskoye field in December 2015, as well as additions of property, plant and equipment at our production subsidiaries.

We accrue depreciation and depletion on oil and gas assets using the "units-of-production" method and straight-line method for other facilities. Our reserve base is only appraised on an annual basis as of 31 December and does not fluctuate during the year until the subsequent appraisal, whereas our depletable cost base does change each quarter due to the ongoing capitalization of our costs throughout the year.

Materials, services and other

In 2016, our materials, services and other expenses increased by RR 4,582 million, or 31.5%, to RR 19,133 million compared to RR 14,551 million in 2015 primarily due to the launch of the Yarudeyskoye field in December 2015.

	Year ended 31 December:		**Change**
millions of Russian roubles	**2016**	**2015**	**%**
Employee compensation	7,558	6,004	25.9%
Repair and maintenance	3,026	1,959	54.5%
Complex of services for preparation, transportation and processing of hydrocarbons	2,062	1,756	17.4%
Materials and supplies	1,838	1,305	40.8%
Electricity and fuel	1,101	938	17.4%
Liquefied petroleum gas volumes reservation expenses	1,017	768	32.4%
Security services	660	470	40.4%
Transportation services	641	452	41.8%
Insurance expense	372	267	39.3%
Rent expenses	257	59	n/a
Other	601	573	4.9%
Total materials, services and other	**19,133**	**14,551**	**31.5%**

Operating employee compensation increased by RR 1,554 million, or 25.9%, to RR 7,558 million compared to RR 6,004 million in 2015. The increase was due to an increase in the average number of employees as a result of the launch of the Yarudeyskoye field in December 2015, an indexation of base salaries effective from 1 July 2016 and the related increase in social contributions for medical and social insurance and to the Pension Fund.

Repair and maintenance services expenses, materials and supplies, electricity and fuel, security services and transportation increased mainly due to the launch of the Yarudeyskoye field in December 2015.

Complex of services for preparation, transportation and processing of hydrocarbons expenses mainly relate to transportation of our LPG produced at the Purovsky Plant for further processing at the Tobolsk Refining Facilities. These expenses increased by RR 306 million, or 17.4%, to RR 2,062 million in 2016 compared to RR 1,756 million in 2015 primarily due to an increase in the contract rate for services at the Tobolsk Refining Facilities at the end of 2015, as well as additional expenses for preparation of crude oil for transportation by trunk pipeline resulted from the commencement of crude oil commercial production at the Yarudeyskoye field in December 2015.

In 2016, liquefied petroleum gas volumes reservation costs increased by RR 249 million, or 32.4%, to RR 1,017 million from RR 768 million in 2015 primarily due to an increase in LPG volumes sold through our subsidiary in Poland, as well as an increase in the average exchange rate of the Polish zloty to the Russian rouble, since this expense is denominated in Polish zloty. The reservation of LPG is required in order to maintain the necessary strategic reserve in Poland in accordance with local regulation.

Insurance expense increased by RR 105 million, or 39.3%, to RR 372 million in 2016 from RR 267 million in 2015 due to an increase in insurable property valuation and the number of items of insured property, plant and equipment in our major subsidiaries.

Rent expenses increased by RR 198 million, or 4.4 times, to RR 257 million from RR 59 million in 2015 primarily due to rent of additional equipment used for stimulation of hydrocarbons production at some our fields.

General and administrative expenses

In 2016, our general and administrative expenses increased by RR 3,770 million, or 26.3%, to RR 18,126 million compared to RR 14,356 million in 2015. The main components of these expenses were employee compensation, social expenses and compensatory payments, as well as legal, audit and consulting services, which, on aggregate, comprised 85.7% and 81.8% of total general and administrative expenses in the years ended 31 December 2016 and 2015, respectively.

millions of Russian roubles	**Year ended 31 December: 2016**	**2015**	**Change %**
Employee compensation	12,327	9,364	31.6%
Social expenses and compensatory payments	2,184	1,347	62.1%
Legal, audit and consulting services	1,019	1,036	(1.6%)
Business travel expense	624	634	(1.6%)
Fire safety and security expenses	387	313	23.6%
Advertising expenses	370	253	46.2%
Rent expense	214	196	9.2%
Repair and maintenance expenses	200	458	(56.3%)
Other	801	755	6.1%
Total general and administrative expenses	**18,126**	**14,356**	**26.3%**

Employee compensation relating to administrative personnel increased by RR 2,963 million, or 31.6%, to RR 12,327 million in 2016 from RR 9,364 million in 2015. The increase was due to an increase in the average number of employees, an indexation of base personnel salaries effective 1 July 2016, as well as an increase in bonuses accrued to key management and the related increase in social contributions for medical and social insurance and to the Pension Fund.

In 2016, our social expenses and compensatory payments increased by RR 837 million, or 62.1%, to RR 2,184 million compared to RR 1,347 million in 2015 mainly due to increase in compensatory payments. These payments mainly related to the development of Yarudeyskoye, Salmanovskoye and Geofizicheskoye fields and were RR 1,029 million in 2016 compared to RR 362 million in 2015. In addition, social expenses increased due to continued support of charities and social programs in the regions where we operate. Social expenses and compensatory payments fluctuate period-on-period depending on the implementation schedules of specific programs we support.

Fire safety and security expenses increased by RR 74 million, or 23.6%, to RR 387 million in 2016 from RR 313 million in 2015 primarily due to an increase in rates charged for security services starting from January 2016.

Advertising expenses increased by RR 117 million, or 46.2%, to RR 370 million in 2016 from RR 253 million in 2015 mainly due to the conclusion of a corporate sponsorship contract for the Group's advertising during sporting events at the end of 2015.

Repair and maintenance expenses decreased by RR 258 million, or 56.3%, to RR 200 million in 2016 from RR 458 million 2015 mainly due to repair works performed at the Group's Moscow head office building in 2015 (absent in 2016).

Other items of our general and administrative expenses changed marginally.

Exploration expenses

In 2016, our exploration expenses increased by RR 978 million, or 88.2%, to RR 2,087 million from RR 1,109 million in 2015 and related in both reporting periods to exploration works performed at North-Obskiy license area, and in 2016 also to exploration works performed at the Nyakhartinskiy and Trekhbugorniy license areas. Exploration expenses include geological and geophysical research services expenditures, expenditures associated with the maintenance of license areas with non-proven reserves and other expenditures relating to exploration activity, as well as expenses of our research and development center associated with the exploration activities at our fields. The exploration expenses fluctuate period-to-period in accordance with the approved working schedule of exploration works at our production subsidiaries.

Impairment expenses (reversals)

In 2016, we recognized a net impairment expense of RR 178 million related primarily to trade accounts receivable. In 2015, we reversed a portion of previously accrued provisions in the total amount of RR 204 million as a result of revising management's estimates on the probability of recovering trade accounts receivable.

Changes in natural gas, liquid hydrocarbons and work-in-progress

In 2016, we recorded a reversal of RR 439 million to changes in inventory expense due to an increase in our gas condensate refined products inventory balances as of 31 December compared to 1 January, as well as an increase in the cost of inventories. In 2015, an increase in our natural gas and most of liquid hydrocarbons inventory balances as of 31 December compared to 1 January resulted in a reversal of RR 2,113 million to changes in inventory expense.

In 2016, our cumulative natural gas inventory balance in the Underground Gas Storage Facilities ("UGSF"), the GTS and own pipeline infrastructure decreased by 493 mmcm as compared to an increase of 278 mmcm in 2015. In 2016, we withdrew considerably more volumes of natural gas from inventory with relatively flat volumes injected into the UGSF due to higher demand for natural gas from end-customers (our total natural gas sales volumes increased by 3.6% (see "Natural gas sales volumes" above)).

In 2016, our cumulative liquid hydrocarbons inventory balances, recognized as inventory in transit or in storage, changed marginally (decreased by seven thousand tons), whereas in 2015, our cumulative inventory balances increased by 171 thousand tons. The increase in inventory balances in 2015 was mainly due to an increase in inventory balance of stable gas condensate in rail cars and tankers in transit and not realized at the reporting date, as well as an increase in inventory balance of crude oil due to the launch of the Yarudeyskoye field in December 2015. Inventory balances of stable gas condensate and refined products tend to fluctuate period-to-period depending on shipment schedules and final destination of our shipments.

The following table highlights movements in our hydrocarbons inventory balances:

	2016			**2015**		
Inventory balances in transit or in storage	**At 31 December**	**At 1 January**	**Increase / (decrease)**	**At 31 December**	**At 1 January**	**Increase / (decrease)**
Natural gas (millions of cubic meters)	**834**	**1,327**	**(493)**	**1,327**	**1,049**	**278**
including Gazprom's UGSF	*787*	*1,245*	*(458)*	*1,245*	*1,016*	*229*
Liquid hydrocarbons (thousand tons)	**903**	**910**	**(7)**	**910**	**739**	**171**
including naphtha	*267*	*184*	*83*	*184*	*305*	*(121)*
stable gas condensate	*307*	*369*	*(62)*	*369*	*219*	*150*
crude oil	*105*	*157*	*(52)*	*157*	*29*	*128*

Other operating income (loss)

Other operating income (loss) includes realized income (loss) from hydrocarbons trading on the international markets, income (loss) from the change in the fair value of the aforementioned contracts, as well as other income (loss) relating to penalty charges, disposal of materials, fixed assets and other transactions. In 2016, we recognized other operating income of RR 221 million compared to other operating loss of RR 542 million in 2015.

In 2016, within our trading activities we purchased and sold approximately 3.4 bcm of natural gas, as well as various derivative commodity instruments, and recognized the aggregate realized income from trading activities of RR 1,970 million as compared to RR 206 million of income in 2015. At the same time, we recognized a non-cash loss of RR 1,778 million in 2016 as a result of a decrease in the fair value of aforementioned contracts as compared to RR 1,006 million non-cash loss in 2015.

In addition, we recorded other operating income of RR 29 million and RR 258 million in 2016 and 2015, respectively, which in both periods primarily related to the penalties charges received from our suppliers due to non-compliance of their contractual obligations, profit (loss) on disposal of materials and fixed assets, as well as other similar transactions.

Net gain on disposal of interests in joint ventures

In December 2015, the Group and China's Silk Road Fund Co. Ltd. signed an agreement on the acquisition of a 9.9% equity stake in Yamal LNG by the fund. In March 2016, the transaction was closed upon the completion of the conditions precedent and we recognized a gain on the disposal in the amount of RR 73,072 million.

In August 2015, as part of the restructuring procedures intended to achieve parity shareholdings in SeverEnergia, we contributed a 6.4% ownership interest in joint venture Artic Russia B.V. to the capital of Yamal Development. As a result, taking into account the 50% participation interest of NOVATEK in joint venture Yamal Development, in the three months ended 30 September 2015, we recognized a gain on the disposal in the amount of RR 989 million.

Profit from operations and EBITDA

Our profit from operations significantly increased by RR 84,536 million, or 60.1%, to RR 225,266 million in 2016, as compared to RR 140,730 million in 2015. Our profit from operations before disposals of interests in joint ventures increased by RR 12,453 million, or 8.9%, to RR 152,194 million in 2016, as compared to RR 139,741 million in 2015 mainly due to a significant increase in crude oil sales volumes resulted from the commencement of commercial production at the Yarudeyskoye field in December 2015 and reaching the nameplate production capacity by the end of the month. At the same time our share in the profit from operations of our joint ventures increased by RR 1,603 million, or 5.0%, to RR 33,655 million compared to RR 32,052 million in 2015 (see "Share of profit (loss) of joint ventures, net of income tax" below).

Our EBITDA, normalized for the effect of the disposal of interests in joint ventures, increased by RR 28,218 million, or 13.2%, to RR 242,407 million in 2016 from RR 214,189 million in 2015 also mainly due to a significant increase in crude oil sales volumes.

Finance income (expense)

In 2016, we recorded a net finance expense of RR 7,941 million compared to a net finance expense of RR 16,182 million in 2015 due to the recognition of a non-cash foreign exchange loss in both reporting periods, as well as due to the recognition in 2015 of a non-cash loss from the remeasurement of the shareholders' loans issued to our joint ventures.

millions of Russian roubles	**Year ended 31 December: 2016**	**2015**	**Change %**
Accrued interest expense on loans received	(16,297)	(14,549)	12.0%
Less: capitalized interest	5,314	6,047	(12.1%)
Provisions for asset retirement obligations: effect of the present value discount unwinding	(587)	(290)	102.4%
Interest expense	**(11,570)**	**(8,792)**	**31.6%**
Interest income	18,732	12,622	48.4%
Change in fair value of non-commodity financial instruments	10,387	(10,505)	n/a
Foreign exchange gain (loss), net	(25,490)	(9,507)	168.1%
Total finance income (expense)	**(7,941)**	**(16,182)**	**(50.9%)**

In 2016, our interest expense increased by RR 2,778 million, or 31.6%, to RR 11,570 million primarily due to depreciation of the Russian rouble relative to the US dollar and Euro (most of our long-term borrowings are denominated in foreign currencies), as well as a decrease in the base used for interest capitalization as a result of additions to property, plant and equipment at Yarudeyskoye field after its launch in December 2015. The impact of these factors was reduced by repayments of a part of the Group's borrowings.

Interest income increased by RR 6,110 million, or 48.4%, to RR 18,732 million in 2016 from RR 12,622 million in 2015 due to an increase in loans provided to our joint ventures for the development and expansion of their activities, as well as a result of the average Russian rouble depreciation relative to the US dollar and Euro in 2016 compared to the average exchange rate in 2015.

In 2016, we recognized a non-cash gain of RR 10,387 million compared to a non-cash loss of RR 10,505 million in 2015 due to the remeasurement of the shareholders' loans issued by the Group to our joint ventures in accordance with IAS 39 *"Financial instruments: recognition and measurement"*. The effect of the fair value remeasurement of shareholders' loans may change period-to-period due to the change in market interest rates and other macroeconomic parameters and does not affect real future cash flows of loans repayments.

The Group continues to record non-cash foreign exchange gains and losses each reporting period due to movements between currency exchange rates. In 2016, we recorded a net foreign exchange loss of RR 25,490 million compared to a net loss of RR 9,507 million in 2015 primarily due to the revaluation of our foreign currency denominated borrowings and loans provided, as well as cash balances in foreign currency.

Share of profit (loss) of joint ventures, net of income tax

In 2016, the Group's proportionate share of profit of joint ventures amounted to RR 90,839 million as compared to the share of loss of joint ventures in the amount of RR 31,607 million in 2015.

millions of Russian roubles	Year ended 31 December: 2016	2015	Change %
Share in profit from operations	**33,655**	**32,052**	**5.0%**
Share in finance income (expense)			
Share in interest income (expense), net	(15,250)	(17,160)	(11.1%)
Share in foreign exchange gain (loss), net	102,922	(61,200)	n/a
Share in change in fair value of non-commodity financial instruments	(13,436)	9,539	n/a
Total share in finance income (expense)	**74,236**	**(68,821)**	**n/a**
Share in total income tax benefit (expense)	(17,052)	5,162	n/a
Total share of profit (loss) of joint ventures, net of income tax	**90,839**	**(31,607)**	**n/a**

Our proportionate share in the profit from operations of our joint ventures increased by RR 1,603 million, or 5.0%, primarily due to higher operating results of SeverEnergia (as a result of the launch of additional production capacities in the first half of 2015) and Terneftegas (as a result of the launch of the Termokarstovoye field in May 2015 and reaching the nameplate production capacity in June 2015). The impact of these factors was partially offset by lower operating results of Nortgas (due to natural decline in gas and gas condensate production), as well as an increase in the unified natural resources production tax expense (see "Our tax burden and obligatory payments" above).

In 2016, our proportionate share in the finance income of our joint ventures amounted to RR 74,236 million compared to the share in the finance expense of RR 68,821 million in 2015. The change in our share in finance income (expense) was primarily due to a recognition in 2016 of a significant non-cash foreign exchange gain on foreign currency denominated loans at our joint ventures Yamal LNG and Terneftegas (our share amounted to RR 102.9 billion) as compared to a significant non-cash loss (our share amounted to RR 61.2 billion) in 2015. The impact of foreign exchange gain (loss) effect was partially offset by a recognition of a non-cash loss from the remeasurement of the fair value of shareholders' loans in Yamal LNG and Terneftegas in 2016 (our share amounted to RR 13.4 billion) compared to a recognition of a non-cash gain (our share amounted to RR 9.5 billion) in 2015. The remaining changes in both reporting periods primarily related to our share in interest expense of our joint ventures.

Income tax expense

The Russian statutory income tax rate for both reporting periods was 20%.

The Group recognizes in profit before income tax its share of net profit (loss) from joint ventures, which influences the consolidated profit of the Group but does not result in additional income tax expense (benefit) at the Group's level. Net profit (loss) of joint ventures was recorded in their financial statements on an after-tax basis. The Group's dividend income from its joint ventures is subject to a zero withholding tax rate according to the Russian tax legislation as the Group holds at least a 50% interest in each of its joint ventures, and also does not result in a tax charge. In addition, during the year ended 31 December 2015, the Group recognized a deferred tax asset of RR 4,316 million related to expected disposal of 9.9% participation interest in Yamal LNG.

Without the effect of net profit (loss) and dividends from joint ventures, and the deferred tax asset relating to the 9.9% interest in Yamal LNG classified as held for sale, the effective income tax rate (total income tax expense calculated as a percentage of profit before income tax) in 2016 and 2015, was 19.8% and 18.7%, respectively.

Profit attributable to shareholders and earnings per share

As a result of the factors discussed in the respective sections above, profit attributable to shareholders of PAO NOVATEK increased by RR 183,399 million, or 246.5%, to RR 257,795 million in 2016 compared to RR 74,396 million in 2015.

The major factors that had an effect on the Group's financial result were the recognition of significant non-cash foreign exchange gains (losses) on foreign currency denominated loans of the Group and its joint ventures in both reporting periods, as well as the recognition of a gain on the disposal of interests in joint ventures in 2016. Excluding the one-time effect from the disposal of interests in joint ventures and the effect of foreign exchange gains and losses, our profit attributable to shareholders of PAO NOVATEK changed insignificantly and amounted to RR 133,759 million in 2016 compared to RR 132,509 million in 2015 (see the table below):

	Year ended 31 December:		**Change**
millions of Russian roubles	**2016**	**2015**	**%**
Profit attributable to shareholders of PAO NOVATEK	257,795	74,396	246.5%
Net gain on disposal of interests in joint ventures	(73,072)	(989)	n/a
Income tax expense relating to the disposal of interests in joint ventures	15,395	-	n/a
Normalized profit attributable to shareholders of PAO NOVATEK	**200,118**	**73,407**	**172.6%**
Foreign exchange (gains) losses	25,490	9,507	168.1%
Income tax expense (benefit) relating to foreign exchange (gains) losses	(5,098)	(1,901)	168.2%
Share of foreign exchange (gains) losses of joint ventures	(102,922)	61,200	n/a
Share of income tax expense (benefit) relating to foreign exchange (gains) losses of joint ventures	16,171	(9,704)	n/a
Normalized profit attributable to shareholders of PAO NOVATEK, excluding the effect of foreign exchange gains (losses)	**133,759**	**132,509**	**0.9%**

Our weighted average basic and diluted earnings per share, calculated from the profit attributable to shareholders of PAO NOVATEK increased by RR 60.78 per share, or 246.7%, to RR 85.41 per share in 2016 from RR 24.63 per share in 2015. Excluding the effects of the disposals of interests in joint ventures and foreign exchange gains and losses, our weighted average basic and diluted earnings per share changed insignificantly and amounted to RR 44.31 per share in 2016 compared to RR 43.87 per share in 2015.

LIQUIDITY AND CAPITAL RESOURCES

Cash flows

The following table shows our net cash flows from operating, investing and financing activities for the years ended 31 December 2016 and 2015:

	Year ended 31 December:		Change
millions of Russian roubles	**2016**	**2015**	**%**
Net cash provided by **operating** activities	173,791	132,864	30.8%
Net cash provided by (used for) **investing** activities	11,877	(159,074)	n/a
Net cash provided by (used for) **financing** activities	(156,712)	12,714	n/a

Net cash provided by operating activities

Our net cash provided by operating activities increased by RR 40,927 million, or 30.8%, to RR 173,791 million compared to RR 132,864 million in 2015. The increase was due to higher profit from operations adjusted for non-cash items, as well as changes in working capital and long-term advances given, that was partially offset by an increase in income tax payments.

	Year ended 31 December:		Change
millions of Russian roubles	**2016**	**2015**	**%**
Profit from operations before disposals of interests in joint ventures	152,194	139,741	8.9%
Non-cash adjustments (1)	36,739	20,820	76.5%
Changes in working capital and long-term advances given	11,189	(14,470)	n/a
Interest received	1,983	1,454	36.4%
Dividends received from joint ventures	-	1,850	n/a
Income taxes paid	(28,314)	(16,531)	71.3%
Total net cash provided by operating activities	**173,791**	**132,864**	**30.8%**

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

The profit from operations adjusted for non-cash items increased mainly due to a significant increase in crude oil sales volumes as a result of the commencement of commercial production at the Yarudeyskoye field in December 2015 (see "Profit from operations and EBITDA" above).

Working capital balances fluctuate from period-on-period depending on various factors. The changes in long-term advances given were mainly due to a decrease in long-term advances payments to RZD in 2016 compared to 2015, which were provided in accordance with the Strategic Partnership Agreement's installment schedule (see "Transportation tariffs" above).

The increase in income tax payments in 2016 was mainly due to an increase in the taxable profit resulted from the Group's higher operating results, as well as income tax prepayments at the beginning of 2015.

The remaining cash proceeds in both reporting periods related to interest received, as well as RR 1,850 million of dividends received from our joint venture Nortgas in 2015.

Net cash provided by (used for) investing activities

In 2016, our net cash provided by investing activities amounted to RR 11,877 million compared to RR 159,074 million used for investing activities in 2015.

millions of Russian roubles	Year ended 31 December: 2016	2015	Change %
Cash used for capital expenditures	(34,413)	(50,584)	(32.0%)
Payments for mineral licenses	(1,928)	-	n/a
Proceeds from disposal of stakes in joint ventures net of costs to sell and income tax paid, net	72,412	-	n/a
Additional capital contributions to joint ventures	(19,565)	-	n/a
Loans provided to joint ventures	(6,645)	(108,570)	(93.9%)
Repayments of loans provided to joint ventures	6,038	3,710	62.7%
Payments for acquisition of subsidiaries net of cash acquired	(2,961)	(3,630)	(18.4%)
Other	(1,061)	-	n/a
Net cash provided by (used for) investing activities	**11,877**	**(159,074)**	**n/a**

Cash used for capital expenditures decreased by RR 16,171 million, or 32.0%, as compared to 2015. In 2016, cash was mainly used for the development of the Yarudeyskoye and East-Tarkosalinskoye field's crude oil deposits, maintenance of production at our Yurkharovskoye field and the development of the Salmanovskoye (Utrenneye) field. In addition, we purchased a land plot in the northern part of the Ust-Luga port, bordering with the territory of our Ust-Luga Complex, for implementing Group's future projects.

In 2016, we made a payment in the amount of RR 1,928 million for the acquisition of exploration and production licenses for the Nyakhartinskiy, Syadorskiy and Tanamskiy license areas (see "Recent developments" above).

In 2016, we received RR 72,412 million (net of costs to sell and income tax paid) for the sale of the 9.9% equity stake in Yamal LNG in March 2016.

In September 2016, we made capital contributions to Yamal LNG in the amount of RR 19,565 million as part of the financing commitment by the Group as a result of the disposal of the 9.9% equity stake in Yamal LNG to China's Silk Road Fund Co. Ltd. on the same terms that were previously applied upon the entrance of TOTAL S.A. and China National Petroleum Corporation into the Yamal LNG project.

In 2016, we provided loans to our joint venture Yamal LNG in the amount of RR 6,645 million as compared to RR 108,570 million provided to Yamal LNG and Yamal Development in 2015. At the same time, in 2016 and 2015, we received RR 6,038 million and RR 3,710 million, respectively, due to a partial repayment of the loans provided to Terneftegas and Yamal Development.

In 2016 and 2015, we paid RR 2,929 million (USD 39 million) and RR 3,630 million (USD 62 million), respectively, for 100% equity stake in AO Office acquired in August 2014. In addition, in April and December 2016, the Group acquired companies OOO Evrotek-Yuh and Blue Gaz Sp. z o.o. for RR six million and RR 26 million, respectively (see "Recent developments" above).

Net cash provided by (used for) financing activities

In 2016, our net cash used for financing activities amounted to RR 156,712 million as compared to RR 12,714 million provided by financing activities in 2015.

millions of Russian roubles	**Year ended 31 December:** 2016	2015	**Change** %
Proceeds from (repayments of) long-term debt, net	(76,380)	29,105	n/a
Proceeds from (repayments of) short-term debt, net	(26,340)	27,180	n/a
Dividends paid	(41,653)	(35,640)	16.9%
Interest paid	(11,423)	(7,149)	59.8%
Purchase of treasury shares	(916)	(782)	17.1%
Net cash provided by (used for) financing activities	**(156,712)**	**12,714**	**n/a**

In 2016, we obtained a long-term loan from a Russian subsidiary of a foreign bank in the amount of RR 6,373 million (EUR 100 million). At the same time, the Group fully repaid five-year US dollar denominated Eurobonds in the amount of RR 46,756 million (USD 600 million) and partially repaid a loan obtained under our syndicated credit line facility in the amount of RR 30,265 million (USD 462 million) according to the loan's maturity schedule, as well as partially repaid a loan obtained by a Group subsidiary from its non-controlling shareholder.

In 2015, we received funds under the loan agreement with China's Silk Road Fund in the amount of RR 55,215 million (EUR 0.73 billion) for financing of the Yamal LNG project as part of the transaction for the sale of the Group's 9.9% equity stake in Yamal LNG, and also one of the Group's subsidiaries obtained long-term loans from its non-controlling shareholder in the amount of RR 16,130 million. At the same time, the Group fully repaid three-year tenor non-convertible Russian rouble denominated exchange-traded bonds in the amount of RR 20 billion, as well as partially repaid a loan obtained under our syndicated credit line facility in the amount of RR 22,240 million (USD 346 million) according to the loan's maturity schedule.

During 2016, we repaid short-term loans from a Russian bank in the amount of RR 20,000 million and from the non-controlling shareholder of our subsidiary in the amount of RR 1,300 million obtained in 2015. In addition, in both reporting periods, we obtained short-term loans to finance trade activities. In the current reporting period net repayments from these loans amounted to RR 5,040 million, while in 2015 net proceeds amounted to RR 5,880 million.

The remaining change primarily related to an increase in dividends paid and interest paid on borrowings and loans.

Liquidity and working capital

The following table shows our liquidity and credit measures as of 31 December 2016 and 2015:

	31 December 2016	31 December 2015	Change, %
Absolute amounts, RR million			
Net debt (1)	168,464	329,518	(48.9%)
Net working capital position (2)	23,969	(41,203)	n/a
Liquidity and credit ratios			
Current ratio (3)	1.22	0.76	60.5%
Total debt to total equity	0.33	0.84	(60.7%)
Long-term debt to long-term debt and total equity	0.20	0.37	(45.9%)
Net debt to total capitalization (4)	0.19	0.41	(53.7%)
Net debt to normalized EBITDA from subsidiaries (5)	0.89	2.05	(56.6%)
Interest coverage ratio (6)	12	11	9.1%

(1) Net debt represents total debt less cash and cash equivalents.

(2) Net working capital position represents current assets plus assets held for sale less current liabilities.

(3) Current ratio is calculated as current assets plus assets held for sale divided by current liabilities.

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

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

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

In 2016, we repaid short- and long-term debt in the aggregate amount of approximately RR 142 billion. As a result, the Group's net debt decreased significantly by 48.9% and net working capital position amounted to RR 24.0 billion as of 31 December 2016.

In each quarter of 2015 and 2016, the Group achieved strong operating results and retained positive free cash flow. The Group's management believes that it presently has and will continue to have the ability to generate sufficient cash flows (from operating and financing activities) to repay all its current liabilities as they become due and to finance the Group's capital construction programs.

Capital expenditures

In 2015 and 2016, our capital expenditures represent our investments primarily relating to developing our oil and gas properties. The following table shows capital expenditures at our main fields, processing facilities and other assets:

	Year ended 31 December:	
millions of Russian roubles	2016	2015
Yarudeyskoye field	8,677	25,826
East-Tarkosalinskoye field	4,393	8,745
Yurkharovskoye field	3,480	7,562
Salmanovskoye (Utrennee) field	2,682	6,165
Khancheyskoye field	1,845	1,480
Infrastructure for future LNG projects	1,342	409
North-Russkoye field	1,131	1,124
North-Khancheyskoye + Khadyryakhinskoye field	74	1,422
Other	6,764	4,826
Capital expenditures	**30,388**	**57,559**

Total capital expenditures on property, plant and equipment in 2016 decreased by RR 27,171 million, or 47.2%, to RR 30,388 million from RR 57,559 million in 2015. In both reporting periods, our main capital expenditures related to the development of the Yarudeyskoye and East-Tarkosalinskoye field's crude oil deposits, Yurkharovskoye field's production maintenance, as well as the development of the Salmanovskoye (Utrenneye) field. In addition, the Group is performing feasibility studies for our future LNG projects and invested in the development of a project for construction of our own center in Murmansk region which will build large-scale offshore structures (see "Recent Developments" above).

The "Other" line in the table above represents our capital expenditures related to other fields and processing facilities of the Group, as well as unallocated capital expenditures as of the reporting date. The allocation of capital expenditures by fields takes place upon the completion of the fixed assets construction stages and depends on the approved fixed assets launch schedule. At the end of 2016, we purchased for RR 3,990 million a land plot with other immovable items in the northern part of the Ust-Luga port, adjacent to the territory of our Ust-Luga Complex, for implementing Group's future projects (expenditures are included in the line "Other" in the table above).

The following table presents the reconciliation of our capital expenditures and additions to property, plant and equipment per Note "Property, plant and equipment" in the Group's IFRS Consolidated Financial Statements, and cash used for capital investments:

millions of Russian roubles	**Year ended 31 December: 2016**	**2015**	**Change %**
Total additions to property, plant and equipment per Note "Property, plant and equipment" in the Group's IFRS Consolidated Financial Statements	**32,316**	**57,559**	**(43.9%)**
Less: acquisition of mineral licenses	(1,928)	-	n/a
Capital expenditures	**30,388**	**57,559**	**(47.2%)**
Add (less): capitalized foreign exchange differences, change in accounts payable and other non-cash adjustments	4,025	(6,975)	n/a
Cash used for capital expenditures [1]	**34,413**	**50,584**	**(32.0%)**

[1] Represents purchases of property, plant and equipment, materials for construction and capitalized interest paid per Consolidated Statement of Cash Flows net of payments for mineral licenses and acquisition of subsidiaries.

QUALITATIVE AND QUANTITATIVE DISCLOSURES AND MARKET RISKS

We are exposed to market risk from changes in commodity prices, foreign currency exchange rates and interest rates. We are exposed to commodity price risk as our prices for crude oil, stable gas condensate and refined products destined for export sales are linked to international crude oil prices and other benchmark price references. We are exposed to foreign exchange risk to the extent that a portion of our sales, costs, receivables, loans and debt are denominated in currencies other than Russian roubles. We are subject to market risk from changes in interest rates that may affect the cost of our financing. From time to time we may use derivative instruments, such as commodity forward contracts, commodity price swaps, commodity options, foreign exchange forward contracts, foreign currency options, interest rate swaps and forward rate agreements, to manage these market risks, and we may hold or issue derivative or other financial instruments for trading purposes.

Foreign currency risk

Our principal exchange rate risk involves changes in the value of the Russian rouble relative to the US dollar. As of 31 December 2016, the total amount of our long-term debt denominated in US dollars was RR 154,915 million, or 71.5% of our total borrowings at that date. Changes in the value of the Russian rouble relative to foreign currencies will impact our foreign currency-denominated costs and expenses, our debt service obligations for foreign currency-denominated borrowings, as well as receivables at our foreign subsidiaries in Russian rouble terms. We believe that the risks associated with our foreign currency exposure are partially mitigated by the fact that a portion of our total revenues, 40.9% in 2016, was denominated in foreign currencies.

In addition, our share of profit (loss) of joint ventures is also exposed to foreign currency exchange rate movements due to the significant amount of foreign currency-denominated borrowings in our joint ventures, mostly in Yamal LNG. We expect that once commercial production commences, foreign currency risk relating to the debt portfolio of Yamal LNG will be mitigated by the fact that all of its products will be delivered to international markets and its revenues will be denominated in foreign currencies.

As of 31 December 2016, the Russian rouble appreciated by 16.8% and 19.9% against the US dollar and the Euro, respectively, compared to 31 December 2015 (see "Selected macro-economic data" above).

Commodity risk

Substantially all of our stable gas condensate and refined products, LPG and crude oil export sales are sold under spot market contracts. Our export prices are primarily linked to international crude oil and oil products prices. External factors such as geopolitical developments, natural disasters and the actions of the Organization of Petroleum Exporting Countries affect crude oil prices and thus our export prices.

The weather is another factor affecting demand for natural gas. Changes in weather conditions from year to year can influence demand for natural gas and to some extent gas condensate and refined products.

From time to time we may employ derivative instruments to mitigate the price risk of our sales activities. In our consolidated financial statements all derivative instruments are recognized at their fair values. Unrealized gains or losses on derivative instruments are recognized within other operating income (loss), unless the underlying arrangement qualifies as a hedge.

The Group purchases and sells natural gas on the European market under long-term contracts based on formulas with reference to benchmark natural gas prices quoted for the North-Western European natural gas hubs, crude oil and oil products prices and/or a combination thereof. Therefore, the Group's financial results from natural gas foreign trading activities are subject to commodity price volatility based on fluctuations or changes in the respective benchmark reference prices.

Pipeline access

We transport substantially all of our natural gas through the Gas Transmission System ("GTS") owned and operated by PAO Gazprom, which is responsible for gathering, transporting, dispatching and delivering substantially all natural gas supplies in Russia. Under existing legislation, Gazprom must provide access to the GTS to all independent suppliers on a non-discriminatory basis provided there is capacity available that is not being used by Gazprom. In practice, Gazprom exercises considerable discretion over access to the GTS because it is the sole owner of information relating to capacity. There can be no assurance that Gazprom will continue to provide us with access to the GTS; however, we have not been denied access in prior periods.

Ability to reinvest

Our business requires significant ongoing capital expenditures in order to grow our production and meet our strategic plans. An extended period of reduced demand for our hydrocarbons available for sale and the corresponding revenues generated from these sales would limit our ability to maintain an adequate level of capital expenditures, which in turn could limit our ability to increase or maintain current levels of production and deliveries of natural gas, gas condensate, crude oil and other associated products; thereby, adversely affecting our financial and operating results.

Off balance sheet activities

As of 31 December 2016, we did not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which are typically established for the purpose of facilitating off-balance sheet arrangements.

TERMS AND ABBREVIATIONS

APR	Asian-Pacific Region
bbl	barrel
bcm	billion cubic meters
boe	barrels of oil equivalent
CBR	Central Bank of Russian Federation
CFR	"Cost and freight"
CIF	"Cost, insurance and freight"
CNY	Chinese Yuan
DAP	"Delivery at point of destination"
DDA	depreciation, depletion and amortization
DES	"Delivery to the port of destination ex-ship"
FCA	"Free carrier"
FOB	"Free on board"
Forecast of the Ministry of Economic Development	The document *"Forecast of Socio-economic Development of the Russian Federation for 2015 and planned period 2016 and 2017"* prepared by the Ministry of Economic Development of the Russian Federation or the similar document prepared for another period
FTS	Federal Tariffs Service
GTS	Gas Transmission System part of the UGSS
IFRS	International Financial Reporting Standards
List	the OFAC's Sectoral Sanctions Identification List
LNG	liquefied natural gas
LPG	liquefied petroleum gas
mcm	thousand cubic meters
MET	mineral extraction tax
OFAC	Office of Foreign Assets Control
PRMS	Petroleum Resources Management System
Purovsky Plant	Purovsky Gas Condensate Plant
Regulator	A federal executive agency of the Russian Federation that carries out governmental regulation of prices and tariffs for products and services of natural monopolies in energy, utilities and transportation. During the first half of 2015, the Federal Tariffs Service fulfilled the Regulator's role. In July 2015, a Decree of the President of the Russian Federation became effective abolishing the FTS and transferring its functions to the Federal Anti-Monopoly Service
RR	Russian rouble(s)
RZD	OAO Russian Railways, Russia's state-owned monopoly railway operator
S&P	Standard & Poor's
SEC	Securities and Exchange Commission
Tobolsk Refining Facilities	Refining facilities of OOO SIBUR Tobolsk
UGSF	Underground Gas Storage Facilities
UGSS	Unified Gas Supply System owned and operated by PAO Gazprom
UPT	unified natural resources production tax
USD, US dollar	United States Dollar
Ust-Luga Complex	Gas Condensate Fractionation and Transshipment Complex located at the port of Ust-Luga on the Baltic Sea
VAT	value added tax
Yamal LNG project	A large-scale project on constructing a liquefied natural gas plant with an annual capacity of 16.5 million tons based on the feedstock resources of the South-Tambeyskoye field located at the northeast of the Yamal Peninsula that Group undertakes jointly with TOTAL S.A., China National Petroleum Corporation and China's Silk Road Fund Co. Ltd., through its joint venture OAO Yamal LNG
YNAO	Yamal-Nenets Autonomous Region