

TRANSNEFT

MANAGEMENT'S DISCUSSION AND ANALYSIS
OF THE GROUP'S FINANCIAL POSITION
AND RESULTS OF ITS OPERATIONS

FOR THE YEAR ENDED 31 DECEMBER 2017





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(in millions of Russian roubles, if not stated otherwise)

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The following analysis provides an overview of the financial position of Transneft and its subsidiaries (hereinafter – the “Group”) as at 31 December 2017 and results of operations for the year ended 31 December 2017, compared to the year ended 31 December 2016, as well as, other important factors which could affect the future results of the Group. This analysis should be read in conjunction with the consolidated financial statements prepared in accordance with International financial reporting standards (hereinafter – “IFRS”) for the year ended 31 December 2017.

Key financial and operating results

| | Year ended 31 December 2017 | Year ended 31 December 2016 | Change, % |
|---|--------------------------------|--------------------------------|--------------|
| Revenue | 884,337 | 848,134 | 4.3 |
| Profit for the year | 191,805 | 232,907 | (17.6) |
| Earnings before interest, income tax, depreciation and amortisation (EBITDA*) | 408,694 | 408,780 | (0.02) |
| Oil delivered to consignees, mln tons | 477.5 | 483.4 | (1.2) |
| including: | | | |
| Russian oil refineries, mln tons | 243.7 | 245.2 | (0.6) |
| transshipment into the CPC-R system, mln tons | 0.02 | 0.39 | (94.9) |
| exports to neighboring countries, mln tons | 18.6 | 18.6 | - |
| exports to other countries, mln tons | 215.2 | 219.1 | (1.8) |
| Oil products delivered to consignees, mln tons | 33.1 | 33.1 | - |
| including: | | | |
| Russia's domestic market, mln tons | 9.6 | 9.3 | 3.2 |
| exports to the Customs Union member countries, mln tons | 0.6 | 1.3 | (53.8) |
| exports to other countries, mln tons | 22.9 | 22.6 | 1.3 |

* Less crude oil sale and purchase operations under contracts with Rosneft and China National United Oil Corporation.

The main non-operating factors which influenced the profit for the period are disclosed in the table below:

| | Year ended 31 December 2017 | Year ended 31 December 2016 | Absolute change | Change, % |
|--|--------------------------------|--------------------------------|--------------------|---------------|
| Profit for the year | 191,805 | 232,907 | (41,102) | (17.6) |
| Net gain from foreign exchange differences | (9,301) | (41,299) | 31,998 | (77.5) |
| Net interest expense | 25,267 | 35,590 | (10,323) | (29.0) |
| Net gain from operations with financial instruments | (334) | (3,956) | 3,622 | (91.6) |
| Share of profit from associates and jointly controlled entities | (15,847) | (19,519) | 3,672 | (18.8) |
| Changes in impairment provision of property, plant and equipment | 23,533 | - | 23,533 | x |
| Gain from disposal of subsidiaries | (117) | (998) | 881 | (88.3) |
| Adjusted profit for the year | 215,006 | 202,725 | 12,281 | 6.1 |



1. General information and overview of the Group's activities

Public joint stock company Transneft was incorporated in accordance the Russian Government Resolution No. 810 dated 14 August 1993, hereinafter the "Company".

According to its Charter Transneft was established for the purpose of generating profit.

The main areas of Transneft's and its subsidiaries' operations are as follows:

- providing services of transporting oil and oil products via trunk pipelines in the Russian Federation as well as outside of Russia including interstate and intergovernmental agreements;
- raising of and making investments in development of the oil trunk pipeline and oil products trunk pipeline network including production of goods, works and services for servicing trunk oil pipeline and trunk oil products pipeline system to maintain its working condition, increase efficiency and safety of its operations;
- performing of scientific, technical, production, financial and foreign economic activities including mediating activity in the territory of the Russian Federation and outside of Russia;
- carrying out works relating to use of information constituting state secrets (protection of state secrets), provision of services for keeping state secrets safe;
- operating of oil and oil products trunk pipeline transport, sale of and storage of oil and oil products;
- carrying out activities to organize departmental protection of fuel and energy complex facilities owned by the Company and (or) companies, more than 50 percent of voting shares (stakes in the authorized capital) of which are owned by the Company and (or) companies, whose decisions the Company has the ability to determine, and the products supplied under the state contract.

The Group also provides services of oil compounding, crude oil sales, connection of facilities to the trunk oil and oil products pipeline system.

Transneft is also responsible for oil transportation planning and management on foreign territory, for exercising control of oil storage at and delivery to foreign oil receipt-and-delivery facilities, and for data collection and summarizing.

The Group as at 31 December 2017 possesses an extensive network of trunk oil pipelines with a total length of approximately 51.5 thousand km and trunk oil products pipelines with a total length of some 16.9 thousand km.

During the year ended 31 December 2017 the Group transported more than 84% of oil produced in Russia and more than 26% of light oil products produced in Russia, as well as significant volume of hydrocarbons and oil products from CIS countries.

Transneft's key competitive advantages include:

- a monopoly position in the oil pipeline transport market;
- a low ratio of operating costs to total oil transportation volume compared to railway or water transport;
- average level of oil transportation tariffs, compared to those in the CIS and Europe. Information about some of them as per 100 tons-kilometers as at 31 December 2017 is presented below:
 - average tariff through oil trunk pipelines of Transneft – USD 0.88/100 tkm;
 - average tariff of AO KazTransOil (Kazakhstan) – USD 1.46/100 tkm (USD 1.75/100 tkm for export, USD 1.17/100 tkm – domestic);
 - tariff of TAL Pipeline for transportation of oil through Trieste – Ingolstadt direction (Italy, Austria, Germany) – USD 0.99/100 tkm;
 - tariff of Transpetrol (Slovakia) – USD 1.69/100 tkm;
 - tariff of MERO (Czech) – USD 2.87/100 tkm;
 - average tariff of AO Ukrtransnafta for transportation of oil in the direction of Hungary, Slovakia – USD 1.48/100 tkm;
 - average tariff Przyjaźń (Poland) – 1.05 USD/100 tkm;
 - average tariff of OAO Gomeltransneft Druzhba – USD 0.79/100 tkm;
 - average tariff of OAO Polotsktransneft Druzhba – USD 0.67/100 tkm;
 - average tariff of Transnafta (Serbia) – USD 2.68/100 tkm;
 - average tariff of JANAF (Croatia) – USD 3.53/100 tkm;
 - average tariff for transportation of oil through oil pipeline Baku-Tbilisi-Ceyhan (WTC Co consortium) – USD 1.87/100 tkm.



1.1. Key investment projects of the Group

Transneft pays considerable attention to comprehensive development of its trunk pipeline network, promotion of scientific and technical progress, and implementation of new equipment and technology. Transneft's capital investment policy is aimed at achieving system-wide targets for production base development, as well as expansion, reconstruction, and technical upgrades of pipeline transport facilities.

Fulfillment by Transneft of investment projects provides development of the system of trunk pipelines that allows to redistribute operationally export flows to both the Western and Eastern directions depending on the market situation.

The following investment projects were completed during 2017:

- Project "Yug". 1st stage. Reconstruction of trunk pipelines Tikhoretsk – Novorossiysk;
- Project "Yug". 2nd stage. Construction of oil products trunk pipeline Volgograd – Tikhoretsk;
- Construction of MNPP Volgogradskiy NPZ – GPS Tinguta;
- Reconstruction of MN Kuybishev – Tikhortsik and MN Girnovsk – Volgograd for the supplying of crude oil to Volgograd NPZ in the amount to 14.5 mln tons annually;
- Increase of carrying capacity of MN Yaroslavl – Moscow;
- Pipeline system "East Siberia – the Pacific Ocean". Section GNPS Taishet – NPS Skovorodino. Pressure alarm system of the trunk pipeline;
- Expansion of the trunk pipeline system Skovorodino – Mohe to 30 mln tons annually.

The largest investment projects for construction and expansion of pipeline systems under realization are:

- Expansion of the ESPO pipeline system in the GNPS Taishet – NPS Skovorodino section to 80 mln tons annually;
- Expansion of the ESPO pipeline system in the NPS Skovorodino – SMNP Kozmino to 50 mln tons annually;
- Oil pipeline TS ESPO – Komsomolskiy NPZ;
- Development of the trunk pipeline system for increase of deliveries of oil products to Primorsk Sea Port to 25 mln tons (Project "Sever");
- Reconstruction of the trunk pipeline system for increase of transportation volumes of oil products to the Moscow area.

1.2. Environmental policy

The Group is aware of the potential danger of its technologically challenging production activities to the environment, will develop and operate the oil and petroleum products transportation main system, carry out related activities in such a way as to not cause harm to the environment and ensure the highest level of environmental safety of its activities. The Group, being a key element of the energy industry of the Russian Federation and ensuring the final results of its activities, determines environmental protection as the highest and most constant priority, ensuring a high level of environmental safety of the Group's production facilities.

The Group's management is fully informed of the conditions of all fixed assets and the pace of their wear and tear, and uses these data to plan reconstruction or building of new facilities.

The amount of funding of the ecological safety program, building and reconstruction of environmental facilities and acquisition of environmental protection equipment enable Transneft to meet the strictest Russian and international environmental standards.

As at today all subsidiaries of Transneft have developed, introduced and certified the environmental management System. All subsidiaries of the Company have received the international certificates of conformity to the standard ISO 14001-2004.



2. Tariffs and key macroeconomic factors affecting the Group's performance

2.1. Oil and oil products transportation tariffs

Transneft provides tariff-based oil and oil products transportation services to consignors.

Tariff rates are currently calculated in accordance with the Rules of state regulation of tariffs or their maximum limits for services of natural monopolies with respect to transportation of oil and oil products via trunk pipelines, approved by a Decree of the Government of the Russian Federation of 29.12.2007 No. 980, as well as in accordance with the Regulations on setting fees for services of transportation of oil via trunk pipelines, approved by an Order of the Federal Tariff Service of Russia of 17.08.2005 No. 380-e/2, the Methodology of setting tariffs on oil products transportation via trunk pipelines of the Russian Federation approved by Federal Energy Commission of Russia of 16.10.2002 No. 70-e/5, as well as, by the Decree of the Government of the Russian Federation of 14.03.2014 No. 377-r.

During 2016 and 2017 Transneft was performing its core operations:

- a) of transporting oil, by charging fees for its services in accordance with oil transportation tariff rates approved by orders of the state regulatory body for natural monopolies – the Federal Tariff Service of Russia (FTS of Russia) and Federal Antimonopoly Service (FAS of Russia)¹:
- Order of the FTS of Russia of 22.12.2009 No. 455-t/1 Concerning the setting of fees for sea port services provided to OOO Specialized Oil Loading Sea Port Kozmino;
 - Order of the FTS of Russia of 03.12.2013 No. 225-e/6 Concerning the setting of fees for the services of OAO AK Transneft for transportation of oil via the Purpe – Samotlor trunk pipeline system rendered to OAO NK Rosneft;
 - Order of the FTS of Russia of 31.10.2014 No. 240-e/2 Concerning the setting of fee for the service of OAO AK Transneft for transportation of oil via the Ephimoffka – OOO LUKOIL-Volgogradneftepererabotka route rendered for OAO LUKOIL;
 - Order of the FAS of Russia of 07.09.2015 No. 814/15 Concerning the setting of tariff for the service of AO Transneft-Terminal for filling oil from trunk pipelines of OAO AK Transneft into railway tank cars on the territory of Grushevaya industrial site of the transshipment complex Sheskharis;
 - Order of the FAS of Russia of 15.10.2015 No. 964/15 Concerning the setting of tariff for the service of OAO AK Transneft for delivery of oil to AO NNK-Khabarovskiy NPZ;
 - Order of the FAS of Russia of 22.10.2015 No. 991/15 Concerning the setting of tariff for the service of OAO AK Transneft for delivery of oil by oil trunk pipeline system (with amendments included by the order of the FAS of Russia of 13.09.2016 No. 1289/16 Concerning the amendments to the order of the FAS of Russia of 22.10.2015 No. 991/15 Concerning the setting of tariff for the services of OAO AK Transneft for transportation of oil through trunk pipeline system);
 - Order of the FAS of Russia of 30.12.2015 No. 1359/15 Concerning the setting of tariff for the service of OAO AK Transneft for delivery of oil to OOO Il'skiy NPZ;
 - Order of the FAS of Russia of 30.12.2015 No. 1360/15 Concerning the setting of tariff for the service of OAO AK Transneft for delivery of oil through Tikhoretsk – Tuapse-2 route provided to OAO NK Rosneft;
 - Order of the FAS of Russian of 26.05.2016 No. 666/16 Concerning the setting of tariff for the services of OAO AK Transneft for delivery of oil via Uhta – Yaroslavl trunk pipeline through Uhta – OOO LUKOIL – UNP route provided to PJSC LUKOIL;
 - Order of the FAS of Russia of 26.05.2016 No. 667/16 Concerning the setting of tariff for the services of OAO AK Transneft for delivery of oil via Uhta – Yaroslavl trunk pipeline through Synya – Pechora route provided to OOO SK RUSVIETPETRO;
 - Order of the FAS of Russia of 01.07.2016 No. 876/16 Concerning the setting of tariff for the services of OAO AK Transneft for delivery of oil via Uhta – Yaroslavl trunk pipeline through Pechora – Chickshino provided to AO NNK – Pechoranefit;
 - Order of the FAS of Russia of 29.08.2016 No. 1216/16 Concerning the setting of tariff for the services of Transneft for delivery of oil via Uhta – Yaroslavl trunk pipeline through Urdoma – Privodino provided to AO NK – Neftisa;
 - Order of the FAS of Russia of 29.08.2016 No. 1217/16 Concerning the setting of tariff for the services of Transneft for delivery of oil via Uhta – Yaroslavl trunk pipeline through Uhta - Sindor provided to OOO Nizhneomrinskaya nefit;

¹ the FAS of Russia is a successor of the FTS of Russia. Decree of the President of the Russian Federation of 21.07.2015 No.373 Concerning different issues on state administration and control in antimonopoly and tariff regulation.



2.1. Oil and oil products transportation tariffs (continued)

- Order of FAS of Russia of 09.12.2016 No. 1742/16 Concerning the setting of tariff for the services of Transneft for delivery of oil via route Tchikshino - Zelenoborsk of the trunk pipeline system Usa - Ukhta, provided to OOO Zarubezhneft – oil production Kharyaga;
 - Order of FAS of Russia of 23.12.2016 No. 1825/16 Concerning the setting of tariff for the services of Transneft for delivery of oil via trunk pipeline system;
 - Order of FAS of Russia of 26.12.2016 No. 1863/16 Concerning the setting of tariff for the services of Transneft for delivery of oil through Tikhoretsk – Tuapse-2 route provided to Rosneft;
 - Order of FAS of Russia of 26.12.2016 No. 1842/16 Concerning the setting of tariff for the services of Transneft-Terminal for loading of oil into railway tank cars on the territory of Grushevaya industrial site of the transshipment complex Sheskhari from trunk pipeline system of Transneft;
 - Order of FAS of Russia of 27.03.2017 No. 392/17 Concerning the setting of tariff for the services of Transneft for transportation of oil through Sindor-Mikun route of Uhta-Yaroslavl pipeline provided to OOO TSNPSEI;
 - Order of FAS of Russia of 28.04.2017 No. 580/17 Concerning the setting of network tariff for the services of Transneft for transportation of oil via Kuyumba-Taishet trunk pipeline system and amending of the order of the FAS of Russia of 23.12.2016 No. 1825/16 Concerning the setting of tariff for the services of Transneft for delivery of oil via trunk pipeline system;
 - Order of FAS of Russia of 13.03.2017 No. 294/17 Concerning the setting of tariff for the services of Transneft for delivery of oil from trunk pipeline system to OOO Tomskneftepererabotka.
- b) of transporting oil products, by charging fees for its services in accordance with fee rates approved by Transneft in accordance with orders of the FTS of Russia, the FAS of Russia:
- Order of the FTS of Russia of 30.04.2013 No. 90-e/2 Concerning the setting of maximum tariff rates for services of OAO AK Transneft for execution of orders and scheduling deliveries of oil products which are in transit to LPDS Sokur and are further exported outside the customs territory of the Russian Federation and the states - members of the Customs Union;
 - Order of the FTS of Russia of 30.05.2014 No. 132-e/2 Concerning the setting of tariff for services rendered by OAO AK Transneft for transportation of oil products through the route “LUKOIL – Nizhegorodnefteorgsynthet” – MP “Primorsk” for OAO NK LUKOIL;
 - Order of the FTS of Russia of 07.10.2014 No.223-e/1 Concerning the setting of tariff for the services of OAO AK Transneft and its affiliated parties for transportation of oil products by trunk pipelines;
 - Order of the FTS of Russia of 24.12.2014 No.307-e/1 Concerning the setting of maximum rates of tariff for the services of OAO AK Transneft and its affiliated entities for loading of oil products from trunk pipeline system and making amendments to the Order of the FTS of Russia of 07.10.2014 No.223-e/1;
 - Order of the FTS of Russia of 10.02.2015 No.19-e/2 Concerning the setting of maximum rate of tariff for the services of OAO AK Transneft and making amendments to appendix 1 of the Order of the FTS of Russia of 07.10.2014 No.223-e/1;
 - Order of the FTS of Russia of 11.06.2015 No. 234-e/4 Concerning the setting of tariff for the services rendered by OAO AK Transneft for transportation of oil products through OOO KINEF – MP “Primorsk” route for OAO Surgutneftegaz;
 - Order of the FAS of Russia of 15.10.2015 No. 965/15 Concerning the setting limit for maximum tariff rates for the services of OAO AK Transneft for filling of oil products from trunk pipeline network;
 - Order of the FAS of Russia of 01.07.2016 No. 875/16 Concerning the setting limit for maximum tariff rates for the services of OAO AK Transneft and its affiliated parties for filling of oil products from trunk pipeline network and making amendments to the order of the FST of Russia of 07.10.2014 No. 223-e/1 Concerning the setting of tariff for the services of OAO AK Transneft and its affiliated parties for transportation of oil products by trunk pipelines;
 - Order of the FAS of Russia of 26.12.2016 No. 1843/16 Concerning the setting limit for maximum tariff rates for the services of Transneft and its affiliated parties for filling of oil products from trunk pipeline network and making amendments to the order of 07.10.2014 of the FST of Russia No. 223-e/1 Concerning the setting of tariff for the services of OAO AK Transneft and its affiliated parties for transportation of oil products by trunk pipelines;
 - Order of the FAS of Russia of 26.12.2016 No. 1844/16 Concerning the setting limit for maximum tariff rates for the services of Transneft for filling of oil products from trunk pipeline network;
 - Order of the FAS of Russia of 14.04.2017 No. 501/17 Concerning the setting of tariff for the services of Transneft for transportation of oil products through PSP Antipinskiy NPZ-DT (loading from AO Antipinskiy NPZ) – MP Primorsk;



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2.1. Oil and oil products transportation tariffs (continued)

- Order of the FAS of Russia of 01.12.2017 No. 1627/17 Concerning the setting of tariff for services of Transneft for oil products transportation services through PSP Volgograd (loading from OOO LUKOIL-VOLGOGRADNEFTEPERERABOTKA) – MP Novorossiysk (PK Sheskharis) provided to PJSC LUKOIL.

2.2. The rouble's exchange rate against foreign currencies

Services for transportation of oil through trunk oil pipelines which are located in the territory of the Russian Federation are paid for in Russian roubles.

Oil products transportation services are paid for in the following main currencies:

- in the Russian Federation - Russian roubles;
- in the Republic of Belarus - US dollars;
- in the Republic of Kazakhstan - the rouble equivalent calculated at the exchange rate of the Kazakhstan tenge established by the Bank of Russia on the payment date.

Fluctuations of US Dollar and Kazakhstan tenge do not significantly affect the Group's operating results as the portion of revenue which is paid for in US Dollars or rouble equivalent, calculated at the Kazakhstan tenge exchange rate, established by Bank of Russia at the date of payment, in the total revenue is relatively small.

| | Year ended 31 December 2017 | Year ended 31 December 2016 | Change, % |
|--|--------------------------------|--------------------------------|-----------|
| Change in the rouble's exchange rate against the US dollar for the reporting year, % | (5.04) | (16.77) | x |
| Average exchange rate for the year (roubles per US dollar) | 58.35 | 67.03 | (13.0) |
| Exchange rate at the end of the year (roubles per US dollar) | 57.60 | 60.66 | (5.0) |

2.3. Inflation rates

Russia's inflation rates as per Federal state statistics service during the period in question were as follows:

| | Year ended 31 December 2017 | Year ended 31 December 2016 | Change, pp |
|---------------------------|--------------------------------|--------------------------------|------------|
| Rouble inflation (CPI), % | 2.5 | 5.4 | (2.9) |

2.4. Taxation

Most of the Group's companies are incorporated in the Russian Federation and subject to taxation under the Tax Code of the Russian Federation.

The amount of taxes accrued by the Group (except for taxes and contributions accrued in connection with salaries) was as follows:

| | Year ended 31 December 2017 | Year ended 31 December 2016 | Change, % |
|------------------------|--------------------------------|--------------------------------|-----------|
| Current income tax | 49,363 | 55,613 | (11.2) |
| Property tax | 29,392 | 21,704 | 35.4 |
| Other taxes and levies | 1,178 | 957 | 23.1 |

Income tax

The federal income tax rate in 2017 is 3.0% (for the same period of 2016 – 2.0%), while the regional tax rates range from 12.5% to 17.0% (from 13.5% to 18% for the same period of 2016). The Group's international operations are taxable at rates established by the laws of countries where they took place.

Property tax

The amount of property tax increased by RUB 7,688 or by 35.4%. The increase was a result of putting into use of fixed assets, revaluation of property, plant and equipment at replacement cost in accounting under Russian accounting standards which was held at 31 December 2016, increase of a tax rate applied to trunk pipelines as well as constructions which are integral technological part of these pipelines. These properties are taxed at the rates set locally by regions of the Russian Federation and cannot be more than 1.3% during 2016, 1.6% during 2017.

Other taxes and levies

Other taxes and levies mainly include land tax, transport tax and other taxes and levies.



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3. Analysis of the Group's performance

The table below presents consolidated statement of profit or loss and other comprehensive income for the year ended 31 December 2017 and the relative period of preceding year.

| | Year ended 31 December 2017 | Year ended 31 December 2016 | Absolute change | Change, % |
|---|--------------------------------|--------------------------------|--------------------|---------------|
| Revenue | 884,337 | 848,134 | 36,203 | 4.3 |
| Revenue from oil transportation services | 631,459 | 614,139 | 17,320 | 2.8 |
| Revenue from oil products transportation services | 66,035 | 64,485 | 1,550 | 2.4 |
| Revenue from crude oil sales | 150,182 | 142,299 | 7,883 | 5.5 |
| Other revenue | 36,661 | 27,211 | 9,450 | 34.7 |
| Operating expenses net of amortisation and depreciation | (476,062) | (439,917) | (36,145) | 8.2 |
| Operating profit net of amortisation and depreciation | 408,275 | 408,217 | 58 | 0.01 |
| Amortisation and depreciation | (152,637) | (128,523) | (24,114) | 18.8 |
| Operating profit | 255,638 | 279,694 | (24,056) | (8.6) |
| Other expenses | (13,686) | (7,456) | (6,230) | 83.6 |
| Share of profit from associates and jointly controlled entities | 15,847 | 19,519 | (3,672) | (18.8) |
| Profit before income tax and finance income/ (costs) | 257,799 | 291,757 | (33,958) | (11.6) |
| Net finance (costs)/ income | (15,632) | 9,665 | (25,297) | x |
| Profit before income tax | 242,167 | 301,422 | (59,255) | (19.7) |
| Income tax expense | (50,362) | (68,515) | 18,153 | (26.5) |
| Profit for the reporting year | 191,805 | 232,907 | (41,102) | (17.6) |
| Other comprehensive income, net of income tax | 578 | 2,321 | (1,743) | (75.1) |
| Total comprehensive income, net of income tax | 192,383 | 235,228 | (42,845) | (18.2) |



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3.1. Revenue

| Revenue by type of operations | Year ended 31 December 2017 | Share of total revenue, % | Year ended 31 December 2016 | Share of total revenue, % | Absolute change | Change, % |
|---|-----------------------------|---------------------------|-----------------------------|---------------------------|-----------------|------------|
| Revenue from crude oil transportation services | 631,459 | 71.4 | 614,139 | 72.5 | 17,320 | 2.8 |
| exports, except the CIS | 356,371 | 40.3 | 351,834 | 41.5 | 4,537 | 1.3 |
| exports in the CIS | 17,781 | 2.0 | 16,743 | 2.0 | 1,038 | 6.2 |
| domestic sales | 257,307 | 29.1 | 245,562 | 29.0 | 11,745 | 4.8 |
| Revenue from oil products transportation services | 66,035 | 7.5 | 64,485 | 7.6 | 1,550 | 2.4 |
| Revenue from oil compounding services | 6,201 | 0.7 | 6,015 | 0.7 | 186 | 3.1 |
| Revenue from sales of crude oil in the domestic market | 9,445 | 1.1 | 15,186 | 1.8 | (5,741) | (37.8) |
| Revenue from sales of oil products | 5,108 | 0.6 | 2,851 | 0.3 | 2,257 | 79.2 |
| Other revenue | 25,352 | 2.8 | 18,345 | 2.1 | 7,007 | 38.2 |
| Total revenue (without revenue from export sales of crude oil) | 743,600 | 84.1 | 721,021 | 85.0 | 22,579 | 3.1 |
| Revenue from export sales of crude oil | 140,737 | 15.9 | 127,113 | 15.0 | 13,624 | 10.7 |
| Total revenue | 884,337 | 100.0 | 848,134 | 100.0 | 36,203 | 4.3 |

For the year ended 31 December 2017, the Group's revenue increased by RUB 36,203 or by 4.3%, attributable mainly to an increase in revenue from crude oil transportation services, increase in revenue from export sales of crude oil and other revenue. Without taking into account revenue from export sales of crude oil, revenue for the year ended 31 December 2017 increased by RUB 22,579 or 3.1% compared to the same period of the previous year and accounted for 84.1% of total revenue as for the reporting period.

3.1.1. Oil and oil products transportation services

Increase in revenue from oil transportation services amounted to RUB 17,320 or by 2.8% for the year ended 31 December 2017 comparable to the same period of 2016 and was attributable to change in tariffs, change in oil transportation turnover and turnover volumes.

Increase in revenue from oil products transportation services by RUB 1,550 or by 2.4% for the year ended 31 December 2017 compared to the same period of 2016 was driven by changes in tariffs, as well as, changes in turnover volumes and turnover.

3.1.2. Revenue from sales of crude oil and oil products

Revenue from export sales of crude oil was driven by oil sales to the People's Republic of China under a 20-year contract with China National United Oil Corporation to supply 6 mln tons of crude oil annually effective 1 January 2011. This contract was signed as collateral for a loan obtained from the China Development Bank. The respective oil volumes are being purchased from Rosneft.

Increase in revenue from export sales of crude oil by RUB 13,624 or 10.7% as for the year ended 31 December 2017 compared to the year ended 31 December 2016 was mainly a result of growth in average oil market price per barrel set in USD as well as decrease of average USD/RUB exchange rate during the reporting period as compared to the same period of the previous year which resulted in the growth of oil price per barrel set in RUB for the year ended 31 December 2017 as compared to the year ended 31 December 2016.

Decrease in revenue from domestic sales of crude oil as for the year ended 31 December 2017 by RUB 5,741 or by 37.8% compared to the relative period of the previous year was a result of decrease of sale volumes of crude oil.

Increase in revenue from sales of oil products by RUB 2,257 or 79.2% as for the year ended 31 December 2017 compared to the relative period of the previous year was a result of growth of sale volumes of oil products.



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3.1.3. Revenue from oil compounding services

Growth in revenue from oil compounding services by RUB 186 or by 3.1% as for the year ended 31 December 2017 compared to the year ended 31 December 2016 was a result of increase in oil compounding volumes by 2.5% (43,729.3 thousand tons for the year ended 31 December 2017, 42,674.9 thousand tons for the year ended 31 December 2016).

3.1.4. Other revenue

Other revenue includes revenue from technological connection of facilities to the trunk pipelines, expansion of throughput capacity of the trunk pipelines, oil and oil products storage services, communication services, diagnostic services, construction services, information services related to oil transportation, rent services, resale of goods, organisation of transporting of cargos, revenue from provision of other services.

Increase in other revenue as for the year ended 31 December 2017 compared to the relative period of the previous year by RUB 7,007 or 38.2% was mainly driven by recognition of revenue from connection of facilities to the trunk oil and oil products pipeline system and expansion of throughput capacity of the trunk oil and oil products pipelines.

3.2. Operating expenses net of depreciation and amortisation

Operating expenses net of amortisation and depreciation for the year ended 31 December 2017, and the year ended 31 December 2016, are detailed in the table below:

| Operating expense line items | Year ended 31 December 2017 | Share of total expenses, % | Year ended 31 December 2016 | Share of total expenses, % | Absolute change | Change, % |
|---|-----------------------------|----------------------------|-----------------------------|----------------------------|-----------------|------------|
| Salaries, insurance contributions and social expenses | 149,878 | 31.5 | 144,639 | 32.9 | 5,239 | 3.6 |
| Energy | 41,718 | 8.8 | 38,438 | 8.7 | 3,280 | 8.5 |
| Materials | 33,851 | 7.1 | 29,505 | 6.7 | 4,346 | 14.7 |
| Repair and maintenance of relevant technical condition of pipeline | 17,790 | 3.7 | 15,746 | 3.6 | 2,044 | 13.0 |
| Insurance expenses | 6,070 | 1.3 | 7,059 | 1.6 | (989) | (14.0) |
| Pension expense | 5,412 | 1.1 | 4,392 | 1.0 | 1,020 | 23.2 |
| Cost of crude oil sold in the domestic market | 8,497 | 1.8 | 13,497 | 3.1 | (5,000) | (37.0) |
| Cost of oil products sold | 4,639 | 1.0 | 2,956 | 0.7 | 1,683 | 56.9 |
| Cost of other goods for resale sold | 2,513 | 0.5 | 746 | 0.2 | 1,767 | 3.4 times |
| Other operating expenses | 36,044 | 7.5 | 33,901 | 7.6 | 2,143 | 6.3 |
| Operating expenses (net of export crude oil sales and taxes) | 306,412 | 64.3 | 290,879 | 66.1 | 15,533 | 5.3 |
| Cost of export crude oil sales (including export custom duties) | 141,156 | 29.7 | 127,676 | 29.0 | 13,480 | 10.6 |
| Taxes (other than income tax) | 28,494 | 6.0 | 21,362 | 4.9 | 7,132 | 33.4 |
| Operating expenses net of depreciation and amortisation | 476,062 | 100.0 | 439,917 | 100.0 | 36,145 | 8.2 |

For the year ended 31 December 2017, compared to the year ended 31 December 2016, the amount of operating expenses net of depreciation and amortisation increased by RUB 36,145 or by 8.2%.

Increase of the operating expenses net of amortisation and depreciation was driven by the following factors:

- increase in the cost of export crude oil sales (ref. to 3.2.6);
- increase of other taxes (ref. to 3.2.7);
- increase of salaries (ref. to 3.2.1);



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3.2 Operating expenses net of amortisation and depreciation (continued)

After applying inflation rates*, operating expenses net of amortisation and depreciation for the year ended 31 December 2017, and for the year ended 31 December 2016, were as follows:

| Operating expense line items | Year ended 31 December 2017 | Share of total expenses, % | Inflation rates (2017 to 2016), %* | Year ended 31 December 2016 (inflated to 2017) | Share of total expenses, % | Absolute change | Change, % |
|---|-----------------------------|----------------------------|------------------------------------|--|----------------------------|-----------------|------------|
| Salaries, insurance contributions and social expenses | 149,878 | 31.5 | 3.9 | 150,280 | 32.2 | (402) | (0.3) |
| Energy | 41,718 | 8.8 | 10.5 | 42,474 | 9.1 | (756) | (1.8) |
| Materials | 33,851 | 7.1 | 3.4 | 30,508 | 6.5 | 3,343 | 11.0 |
| Repair and maintenance of relevant technical condition of pipeline | 17,790 | 3.7 | 3.4 | 16,281 | 3.5 | 1,509 | 9.3 |
| Insurance expenses | 6,070 | 1.3 | 3.9 | 7,334 | 1.6 | (1,264) | (17.2) |
| Pension expense | 5,412 | 1.1 | 3.9 | 4,563 | 1.0 | 849 | 18.6 |
| Cost of crude oil sold in the domestic market | 8,497 | 1.8 | 9.4 | 14,766 | 3.2 | (6,269) | (42.5) |
| Cost of oil products sold | 4,639 | 1.0 | 12.9 | 3,337 | 0.7 | 1,302 | 39.0 |
| Cost of other goods for resale sold | 2,513 | 0.5 | 3.4 | 771 | 0.2 | 1,742 | 3.3 times |
| Other operating expenses | 36,044 | 7.5 | 3.4 | 35,054 | 7.4 | 990 | 2.8 |
| Operating expenses (net of export crude oil sales and taxes) | 306,412 | 64.3 | X | 305,368 | 65.4 | 1,044 | 0.3 |
| Cost of export crude oil sales (including export custom duties) | 141,156 | 29.7 | 9.4 | 139,678 | 29.9 | 1,478 | 1.1 |
| Taxes (other than income tax) | 28,494 | 6.0 | 3.4 | 22,088 | 4.7 | 6,406 | 29.0 |
| Operating expenses net of amortisation and depreciation | 476,062 | 100.0 | X | 467,134 | 100.0 | 8,928 | 1.9 |

*The inflation rates used are based on the prepared by the Ministry of Economic Development forecast of social-economic development of the Russian Federation for 2018 and forecast periods of 2019 and 2020.

Unit costs are analysed by Oil transportation and Oil products transportation activities based on indicators developed under the Russian Accounting Standards

Unit costs are calculated using operating expenses indicator based on aggregated RAS data which considers the previous year data adjusted for conditions of the reporting period. For calculation of inflated unit costs the index of inflation is used which is based on the prepared by the Ministry of Economic Development forecast of social-economic development of the Russian Federation for 2018 and forecast periods of 2019 and 2020.

Unit costs for transportation of oil as per 100 tons-kilometers as for the year ended 31 December 2017 and for the year ended 31 December 2016 were as follows:

| | Year ended 31 December 2017 | Year ended 31 December 2016 | Absolute change | Change, % |
|---|-----------------------------|-----------------------------|-----------------|-----------|
| Oil transportation services | | | | |
| Turnover, mln tons x km | 1,211,230 | 1,219,134 | (7,904) | (0.6) |
| Unit costs per 100 tons x km, RUB (2016 figures inflated to 2017) | 18.60 | 18.58 | 0.02 | 0.1 |
| Unit costs per 100 tons x km net of new facilities expenditure, RUB (2016 figures inflated to 2017) | 18.30 | 18.58 | (0.28) | (1.5) |



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3.2 Operating expenses net of amortisation and depreciation (continued)

Unit costs for oil products transportation per ton as for the year ended 31 December 2017 and as for the year ended 31 December 2016 were as follows:

| | Year ended 31 December 2017 | Year ended 31 December 2016 | Absolute change | Change, % |
|---|--------------------------------|--------------------------------|--------------------|--------------|
| Oil products transportation services | | | | |
| Volume turnover, mln of tons | 33.1 | 33.1 | - | - |
| Unit costs per ton, RUB (2016 figures inflated to 2017) | 852.27 | 756.16 | 96.11 | 12.7 |
| Unit costs per ton net of new facilities expenditure, RUB (2016 figures inflated to 2017) | 816.19 | 756.16 | 60.03 | 7.9 |

3.2.1. Salaries, insurance contributions and social expenses

Salaries comprise wages, accrual of provision for annual bonus, provision for unused vacation and other remuneration in accordance with IAS 19 Employee benefits.

The increase in salaries, insurance contributions and social expenses for the year ended 31 December 2017 compared to the year ended 31 December 2016 in the amount of RUB 5,239 or 3.6% was mainly influenced by an increase of insurance contributions made to state off-budget funds caused by increase of the limit for their accrual, indexation of wages held in 2017.

3.2.2. Pension expense

Transneft has set the protection of the life and health of its employees as well as the creation of safe working conditions for them as its highest priority. One of the key tasks of social policy is to create conditions for effective work and social protection of workers.

An important area of social protection of employees of the industry is a non-state pension system providing various options for pension plans.

Pension expenses changed under following factors which influence expenses:

- pension liabilities of JSC "NPF "Transneft" are included in the consolidated financial statements of the Group;
- recognition of obligations of the Group under defined benefit plan in accordance with IAS 19 "Employee benefits" and related expenses accrued.

| | Year ended 31 December 2017 | Year ended 31 December 2016 | Absolute change | Change, % |
|--|--------------------------------|--------------------------------|--------------------|--------------|
| Employers' contributions to JSC "NPF "Transneft" in favor of employees | 4,295 | 4,209 | 86 | 2.0 |

3.2.3. Energy

Energy expenses for the year ended 31 December 2017 increased by RUB 3,280 or 8.5% compared to the same period of the previous year. The increase of energy (power) expenses was caused by growth of weighted-average tariff for energy (power) and by growth of energy purchased because of putting into use Zapolyarie-Purpe, Kuyumba-Taishet trunk oil pipelines.

The movement of energy consumption for oil transporting and oil products transporting subsidiaries of the Group is presented in the table below:

| | Year ended 31 December 2017 | Year ended 31 December 2016 | Absolute change | Change,% |
|---------------------------------|--------------------------------|--------------------------------|--------------------|----------|
| Consumption of energy, mln kW*h | 14,259 | 14,480 | (221) | (1.5) |

3.2.4. Materials

The cost of materials for the year ended 31 December 2017 as compared to the same period of 2016, increased by RUB 4,346 or 14.7%. Increase of material expenses was mainly caused by increase of anti-turbulent additives, capital and current repairs produced by the Group itself, as well as, preparation and putting into use of new pipeline facilities.



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3.2.5. Repair and maintenance of relevant technical condition of pipeline

The amount of expense for repair and maintenance of relevant technical condition of pipeline increased as for the reporting period by RUB 2,044 or by 13.0% as compared to the relative period of the previous year because of performing planned capital repairment works.

3.2.6. Cost of crude oil and oil products sold

The cost of export crude oil sales for the year ended 31 December 2017 in the amount of RUB 141,156 includes cost of sales in the amount of RUB 110,763 of crude oil purchased from Rosneft under a contract signed in April 2009 and custom duties in the amount of RUB 30,393. This figure is a result of oil supplies to the People's Republic of China (ref. to 3.1.2.).

Decrease in cost of oil sold in the domestic market as for the year ended 31 December 2017 amounted to RUB 5,000 or 37.0% as compared to the relative period of 2016 and was caused by decrease in sale volumes of oil by the Group's subsidiaries.

Increase in cost of oil products sold in the domestic market as for the year ended 31 December 2017 by RUB 1,683 or 56.9% compared to the relative period of 2016 was caused by growth of sale volumes of oil products by the Group's subsidiaries.

3.2.7. Taxes (other than income tax)

The amount of the Group's other taxes recognised in operating expenses primarily contains property tax, tax on land and transport tax. The increase of these items by RUB 7,132 or 33.4% was mainly caused by the increase of the property tax expense (ref. to 2.4).

3.2.8. Other operating expenses

Other expenses include communication services, rent expenses, transportation services, business trip expenses, the summarised gains and losses relating to disposal of property, plant and equipment and other assets, fines and penalties received and paid, changes in provision for bad debts, as well as other income and expenses.

3.3. Share of results from associates and jointly controlled entities

The Group holds a number of financial investments in associated and jointly controlled entities reported on an equity method basis. The main activities of those entities are stevedoring operations, towing services, ship repair and the provision of additional port services, cargo handling, transport of oil products, wholesale of electric and heat power.

The decrease of the amount of profit recognised by the Group in "Share of profit from associates and jointly controlled entities" as for the year ended 31 December 2017 as compared to the relative period of 2016 amounted to RUB 3,672 or 18.8%, and was mainly caused by recognition of impairment loss of OOO NMT, as well as the results of PJSC NCSP and the closed combined mutual fund "Gazprombank-Finansoviy".

3.4. Finance income and costs

Interest income and expenses

Interest income is generated from depositing available cash in bank accounts, deposits as well as investing in fixed-income securities.

| Interest income | Year ended 31 December 2017 | Year ended 31 December 2016 | Absolute change | Change, % |
|---|--------------------------------|--------------------------------|--------------------|--------------|
| Interest income from cash and equivalents | 4,675 | 2,458 | 2,217 | 90.2 |
| Interest income from other financial assets | 14,315 | 17,701 | (3,386) | (19.1) |
| Other interest income | 11,763 | 793 | 10,970 | 14.8 times |
| Total interest receivable | 30,753 | 20,952 | 9,801 | 46.8 |
| Less interest income on the temporary investment of borrowings | (296) | (1,305) | 1,009 | (77.3) |
| Total interest income recognised in the statement of profit or loss and other comprehensive income | 30,457 | 19,647 | 10,810 | 55.0 |



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3.4. Finance income and costs (continued)

Accrued interest expenses and amounts of capitalized interest expenses for the relevant periods were as follows:

| Interest expenses | Year ended 31 December 2017 | Year ended 31 December 2016 | Absolute change | Change, % |
|--|--------------------------------|--------------------------------|--------------------|--------------|
| Interest expense on loans and borrowings | 48,712 | 46,883 | 1,829 | 3.9 |
| Distribution of investment income to pension liabilities | 6,744 | 6,747 | (3) | - |
| Other interest expenses | 4,023 | 5,044 | (1,021) | (20.2) |
| Total interest expenses | 59,479 | 58,674 | 805 | 1.4 |
| Less finance costs to be capitalised | (3,755) | (3,437) | (318) | 9.3 |
| Total interest expense recognised in the statement of profit or loss and other comprehensive income | 55,724 | 55,237 | 487 | 0.9 |

The amount of interest expenses was composed of:

- interest payable on loan obtained in 2009 from the China Development Bank Corporation with a maturity after five years from the moment of receipt;
- interest payable on non-convertible interest-bearing documentary marketable bonds for the year ended 31 December 2017 and for the relevant period of 2016;
- interest payable on the loan received in 2017 maturing in 8 years after receipt;
- interest payable on Eurobonds issued by the Group in 2008 for the year ended 31 December 2017 and for the relevant period of 2016;
- interest payable on series 01-03 of non-convertible interest-bearing documentary bonds for the year ended 31 December 2017 and for the relevant period of 2016.

The dynamics of interest expenses as for the year ended 31 December 2017 as compared to the similar period of 2016 was mainly driven by growth of share of the borrowings denominated in Russian roubles, increase of LIBOR and decline of USD/RUB average exchange rate during the year ended 31 December 2017 compared to the year ended 31 December 2016 (ref. to 2.2).

During the year ended 31 December 2017, interest in the amount of RUB 3,459 was capitalised as part of cost of assets under construction (for the year ended 31 December 2016 – RUB 2,132) including:

- interest expenses to be capitalised in the amount of RUB 3,755 (for the year ended 31 December 2016 – RUB 3,437);
- interest income to be excluded from interest expenses to be capitalised in the amount of RUB 296 (for the year ended 31 December 2016 – RUB 1,305).

Foreign currency exchange gains and losses

The amount of foreign currency exchange gains and losses for the year ended 31 December 2017 and for the year ended 31 December 2016, was a result of changes in the exchange rate of the US dollar to the Russian rouble.

Due to a remeasurement of assets and liabilities denominated in foreign currency at the end of every month, foreign currency gains and losses arise, which are presented in the consolidated financial statements on a gross basis.



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3.4. Finance income and costs (continued)

Foreign exchange differences by sources are disclosed in the table below:

| | Year ended 31 December 2017 | Year ended 31 December 2016 | Absolute change | Change, % |
|--|--------------------------------|--------------------------------|--------------------|---------------|
| Foreign exchange gains on financial assets | 17,708 | 47,805 | (30,097) | (63.0) |
| Foreign exchange gains on loans and borrowings | 52,459 | 197,775 | (145,316) | (73.5) |
| Other foreign exchange gains | 7,553 | 21,687 | (14,134) | (65.2) |
| Total foreign exchange gains recognised in the statement of profit or loss and other comprehensive income | 77,720 | 267,267 | (189,547) | (70.9) |
| Foreign exchange loss on financial assets | (30,489) | (103,982) | 73,493 | (70.7) |
| Foreign exchange loss on loans and borrowings | (30,346) | (83,648) | 53,302 | (63.7) |
| Other foreign exchange loss | (7,584) | (38,338) | 30,754 | (80.3) |
| Total foreign exchange loss recognised in the statement of profit or loss and other comprehensive income | (68,419) | (225,968) | 157,549 | (69.7) |
| Net foreign exchange gain | 9,301 | 41,299 | (31,998) | (77.5) |

Dynamics of exchange differences presented in the table was driven by lesser strengthening of RUB to USD during the year ended 31 December 2017 as compared to the strengthening of RUB to USD as for the year ended 31 December 2016 (ref. to 2.2).

3.5. Reconciliation of profit and earnings before interest, income tax, depreciation and amortisation (EBITDA)

| | Year ended 31 December 2017 | Year ended 31 December 2016 | Change, % |
|---|--------------------------------|--------------------------------|---------------|
| Profit for the year | 191,805 | 232,907 | (17.6) |
| Adjustments for: | | | |
| income tax expense | 50,362 | 68,515 | (26.5) |
| amortisation and depreciation | 152,637 | 128,523 | 18.8 |
| result of crude oil sales to China | 419 | 563 | (25.6) |
| net finance costs/ (income) | 15,632 | (9,665) | x |
| share of profit from associates and jointly controlled entities | (15,847) | (19,519) | (18.8) |
| other expenses | 13,686 | 7,456 | 83.6 |
| EBITDA* | 408,694 | 408,780 | (0.02) |

* Less crude oil sale and purchase operations under contracts with Rosneft and the China National United Oil Corporation.

EBITDA is a useful indicator for investors, as it reflects the Group's operating performance, including its ability to finance capital expenditures, company acquisitions, and other investments, as well as its ability to raise and service borrowings and loans. Some investors, analysts, and rating agencies tend to use EBITDA as a basis for estimating and projecting the efficiency and value of oil & gas companies. This indicator should not be considered separately, as an alternative to net income, operating income, or any other of Group's performance indicators reported in its consolidated financial statements.



4. Cash flow analysis

| | Year ended 31 December 2017 | Year ended 31 December 2016 | Absolute change | Change, % |
|--|--------------------------------|--------------------------------|--------------------|-----------|
| Cash flows from operating activities | 327,101 | 317,570 | 9,531 | 3.0 |
| Cash flows used for purchase of property, plant and equipment (net) | (306,199) | (319,958) | 13,759 | (4.3) |
| Free cash flow/ (outflow) | 20,902 | (2,388) | 23,290 | x |
| Cash flows from other investing activities | 32,027 | 69,250 | (37,223) | (53.8) |
| Cash flows used in financing activities | (51,183) | (72,510) | 21,327 | (29.4) |
| Net cash flow/ (outflow) | 1,746 | (5,648) | 7,394 | x |
| Change in cash and cash equivalents due to deviation of currency exchange rate | (170) | (12,479) | 12,309 | (98.6) |
| Net increase/ (decrease) in cash and cash equivalents | 1,576 | (18,127) | 19,703 | x |

Positive free cash flow for the year ended 31 December 2017 amounted to RUB 20,902 (negative free cash flow as for the year ended 31 December 2016 amounted to RUB 2,388).

4.1. Operating activities

Cash received from operating activities is the Group's main source of cash. The net cash generated from operating activities amounted to RUB 327,101 for the year ended 31 December 2017, which is RUB 9,531 or 3.0% higher than for the year ended 31 December 2016.

The main factors which influenced on increase of cash generated from operating activities for the year ended 31 December 2017 as compared to the similar period in 2016 were as follows:

- increase in cash receipts from customers by RUB 54,044;
- increase in cash paid to suppliers by RUB 23,629;
- decrease in refunds of insurance contributions, VAT and other taxes from the budget by RUB 18,023;
- increase in income tax paid amounting to RUB 3,313.

4.2. Investing activities

The primary factors resulting in an decrease in cash used in investing activities by RUB 23,464 or 9.4% as for the year ended 31 December 2017 compared to the same period of 2016 were:

- decrease in the net amount of purchase of property, plant and equipment by RUB 13,759 as compared to the relative period of the previous year;
- decrease of cash received from other investing activities amounted to RUB 37,223 because of the following operations:
 - increase in net cash inflow as for the year ended 31 December 2017 from purchase-and-sale transactions of debt securities, equity securities and allocation-closure of deposits in the amount of RUB 21,997 compared to the year ended 31 December 2016;
 - increase in consideration paid for acquisition of share of associates and jointly controlled entities by RUB 85,813 which was a result of acquisition of 57.41% share in closed combined mutual investment fund "Gazprombank – Finansoviy" for RUB 60,000, acquisition of 25% in share capitals of AO Ust-Luga Oil and Sandmark Operations Limited for RUB 38,160 as for the year ended 31 December 2017 compared to the acquisition of the 50% share in the share capital of OOO "NMT" in the amount of USD 159 mln (RUB 12,497 at the exchange rate of Bank of Russia on the date of payment) as for the year ended 31 December 2016;
 - increase in dividends received and other cash proceeds from associates and jointly controlled entities for the amount of RUB 26,454 during the year ended 31 December 2017 compared to the same period of 2016;



- decrease in net loans granted by RUB 2,308 as compared to the relative period of the previous year.

4.3. Financing activities

The main factors which influenced on cash outflow from financing activities for the year ended 31 December 2017 in the amount of RUB 51,183 as compared to cash outflow from financing activities as for the year ended 31 December 2016 in the amount of RUB 72,510 were:

- net proceeds in the amount of RUB 117,813 from issuance of non-convertible interest-bearing documentary bonds and draw of loans in the amount of RUB 197,020 as for the year ended 31 December 2017 and in the amount of RUB 79,207 as for the year ended 31 December 2016;
- increase of cash flows used for repayment of bonds, loans and borrowings as for the year ended 31 December 2017 as compared to the relative period of 2016 by RUB 60,701 which was a result of the following operations:
 - for the year ended 31 December 2017 monthly repayments and early repayments of the loan to China Development Bank in the total amount of USD 2,467 mln (RUB 144,864 at the rate of Central Bank of the Russian Federation on the dates of operations), RUB denominated bonds were repaid (repurchased) in the amount of RUB 45,195;
 - during the year ended 31 December 2016 monthly repayments of loan to China Development Bank were made in the amount of USD 1,827 mln (RUB 118,944 at the rate of Central Bank of the Russian Federation on the date of operation), RUB denominated bonds were repaid (repurchased) in the amount of RUB 10,414;
- increase in dividends paid by RUB 45,358;
- fulfillment of obligations under derivatives which was included in the amount shown in Other cash used in financing activities as for the year ended 31 December 2016.

4.4. Disclosure of cash flows from operating activities using indirect method

Cash flows received from operating activities using the indirect method are disclosed in the table below in addition to the consolidated statement of cash flows prepared using the direct method and disclosed in the consolidated financial statements prepared in accordance with IFRS for the year ended 31 December 2017.

Under the indirect method, the net cash flow from operating activities is determined by adjusting profit before tax for the effects of:

- (a) changes during the reporting period in inventories and operating receivables and payables;
- (b) non-cash items such as amortisation and depreciation, provisions, unrealized foreign currency gains and losses, interest income and expenses, share of profit from associates and jointly controlled entities;
- (c) all other items for which the cash effects are investing or financing cash flows.



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4.4. Disclosure of cash flows from operating activities using indirect method (continued)

| | Year ended 31 December 2017 | Year ended 31 December 2016 |
|---|--------------------------------|--------------------------------|
| OPERATING ACTIVITIES | | |
| Profit before income tax | 242,167 | 301,422 |
| Adjustments for: | | |
| Amortisation and depreciation | 152,637 | 128,523 |
| Loss from disposal of property, plant and equipment | 91 | 1,249 |
| Finance income | (109,177) | (290,908) |
| Finance costs | 124,809 | 281,243 |
| Gain on disposal of subsidiaries | (117) | (998) |
| Share of profit from associates and jointly controlled entities | (15,847) | (19,519) |
| Other | 14,080 | (5,611) |
| Operating profit before changes in working capital and reserves | 408,643 | 395,401 |
| Changes in operating assets and liabilities: | | |
| Changes in inventories | 1,266 | 2,939 |
| Changes in trade and other receivables relating to operating activity and VAT assets | 11,885 | (1,652) |
| Changes in trade and other payables, and accruals relating to operating activity | 3,515 | 15,609 |
| Cash flows from operating activities before payment of income tax expense and interest | 425,309 | 412,297 |
| Income tax paid | (52,391) | (49,078) |
| Income tax refund | 403 | 597 |
| Interest paid | (46,220) | (46,246) |
| Net cash flows received from operating activities | 327,101 | 317,570 |



5. Liquidity analysis

| | 31 December 2017 | 31 December 2016 | Change, % |
|-------------------------------------|------------------|------------------|-----------|
| Current assets | 457,864 | 535,607 | (14.5) |
| including: | | | |
| cash and cash equivalents | 76,162 | 74,586 | 2.1 |
| short-term bank deposits and bonds* | 265,306 | 349,529 | (24.1) |
| Current liabilities | 280,455 | 293,464 | (4.4) |
| Net working capital | 177,409 | 242,143 | (26.7) |
| Current ratio | 1.6 | 1.8 | x |
| Quick ratio** | 1.4 | 1.6 | x |
| Debt / EBITDA | 1.7 | 1.7 | x |
| Debt / Equity | 0.4 | 0.4 | x |

* The main part of short-term bank deposits and bonds consist of deposits and bonds issued by banks and other companies with credit ratings at Ba1 – Ba2 at the Moody's adjusted scale. Thus, short-term bank deposits and bonds consist of highly reliable or reliable financial instruments issued by credit organisations and companies.

** Quick ratio = (Cash and cash equivalents + Current financial assets + Short-term receivables) / Current liabilities

The following are the contractual undiscounted cash flows of financial liabilities, including estimated interest payments at the rates actual at 31 December 2017 and 31 December 2016 accordingly, with amounts denominated in foreign currency recalculated using the Central Bank of the Russian Federation exchange rates at 31 December 2017 and 31 December 2016 accordingly.

31 December 2017:

| | Carrying amount | Contractual cash flows | | | | | | |
|--------------------------|-----------------|------------------------|----------------|----------------|----------------|----------------|---------------|-------------------|
| | | Total | 2018 | 2019 | 2020 | 2021 | 2022 | More than 5 years |
| Loans and borrowings | 688,910 | 891,421 | 150,491 | 139,811 | 102,263 | 103,022 | 94,422 | 301,412 |
| Trade and other payables | 60,459 | 60,630 | 59,259 | 1,195 | 176 | - | - | - |
| | 749,369 | 952,051 | 209,750 | 141,006 | 102,439 | 103,022 | 94,422 | 301,412 |

31 December 2016:

| | Carrying amount | Contractual cash flows | | | | | | |
|--------------------------|-----------------|------------------------|----------------|----------------|----------------|---------------|---------------|-------------------|
| | | Total | 2017 | 2018 | 2019 | 2020 | 2021 | More than 5 years |
| Loans and borrowings | 701,552 | 895,916 | 155,594 | 140,634 | 143,184 | 54,811 | 68,786 | 332,907 |
| Trade and other payables | 85,823 | 85,823 | 85,720 | - | 103 | - | - | - |
| | 787,375 | 981,739 | 241,314 | 140,634 | 143,287 | 54,811 | 68,786 | 332,907 |

The debt structure as at 31 December 2017 assumes the possible redemption date for non-convertible interest-bearing documentary bonds in the amount of RUB 12,264 at the possible offer date (2018).

The debt structure as at 31 December 2016 assumes the possible redemption date for non-convertible interest-bearing documentary bonds in the amount of RUB 45,208 at the possible offer date (2017).