

## Financial Results

### Kubanenergo PJSC Accounting (Financial) Statements



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"Kubanenergo PJSC Accounting (Financial) Statements for 2016 was prepared in accordance with the applicable laws of the Russian Federation. Unqualified audit reports on fairness of both accounting statements made in accordance with the Russian Accounting Standards and consolidated statements made in accordance with the International Financial Reporting Standards were received."

The accounting statement of Kubanenergo PJSC for 2016 is prepared based on the applicable standards and provisions of the Russian Federation regulating accounting and reporting (the "RAS"):

- Federal Law "On Accounting" No. 402-FZ of 12/6/2011;
- Order of the Ministry of Finance of the Russian Federation "On Forms of Accounting Statements of Organizations" No. 66n of 7/2/2010;
- Order of the Ministry of Finance of the Russian Federation "On Amendments to Forms of Accounting Statements of Organizations Approved by Order of the Ministry of Finance of the Russian Federation No. 66n of 7/2/2010" No. 124n of 10/5/2011;
- Order of the Ministry of Finance of the Russian Federation "On Approval of Regulations on Accounting and Reporting in Russian Federation" No. 34n of 7/29/1998;
- Chart of accounts of financial and economic activities of organizations approved by Order of the Ministry of Finance of the Russian Federation No. 94n of 10/31/2000;
- Accounting Regulations "Company's Accounting Policy", PBU 1/2008 approved by Order of the Ministry of Finance of the Russian Federation No. 106n of 10/6/2008.

*The annual financial statements of Kubanenergo PJSC for 2016 prepared in accordance with the Russian Accounting Standards (RAS) include:*

1. Balance sheet;
2. Statement of Financial Results;
3. Statement of Changes in Equity;
4. Cash Flow Statement;
5. Notes;
6. Audit Report.

*Basic Provisions of Kubanenergo PJSC Accounting Policy:*

Accounting of the Company's fixed assets is performed in accordance with the Accounting Regulation "Accounting of Fixed Assets" (PBU 6/01) approved by Order of the Ministry of Finance of the Russian Federation No. 26n of 3/30/2001. Depreciation of fixed assets is accrued

linearly based on their useful life. Depreciation is not accrued on fully depreciated items of fixed assets.

Work in progress is assessed at its actual cost of production.

Recognition of expenses as deferred expenses and equating them to assets with posting them in accounts and statements are in accordance with the principal approach approved by the Company. This approach is based on understanding of the time fact of probability of obtaining economic benefits from the asset by the Company in the future and sufficiently reliable evaluation of its value.

Advances relating to the acquisition of a non-current asset in the future as well as raw materials and supplies intended to the creation of fixed assets are stated in Fixed Assets (line 1150).

Actually commissioned real estate facilities with capital investments completed in full and primary documents duly executed are entered into accounts as fixed assets in a separate sub-account of Real Estate Facilities without Registration of Title. Depreciation of these facilities is accrued pursuant to the standard procedure on the first day of the month following the month of commissioning.

Accounting of the Company's revenues and other income is performed in accordance with the Accounting Regulations "Company Income" (PBU 9/99) approved by Order of the Ministry of Finance of the Russian Federation No. 32n of 5/6/1999.

The Company established the estimated liabilities resulting from the possible payment of compensation for unused vacations, outstanding claims of power suppliers to compensate for losses and electric power transmission services, provisions for litigations and other employee benefits, in accordance with PBU 8/2010 on "Provisions, Contingent Liabilities and Contingent Assets", approved by Order of the Ministry of Finance of the Russian Federation No. 167n of 12/13/2010.

The Company has a provision for doubtful accounts receivable which have not been repaid or with a high degree of probability will not be paid in due time stipulated by the agreement and are not secured by warrants. The provision is corrected on a quarterly basis.

The Company establishes a provision for devaluation of financial investments in case of a constant significant reduction of their cost.

*Corrections relating to previous periods.*

Due to the change of administrative expenses accounting procedure in the Accounting Policy for 2016, the corrections are introduced to Administrative Expenses (line 2220) and to Cost of Sales Figures (line 2120) of the Statement of Financial Results amounting to 76,485 RUB thou over the corresponding period of 2015.

*The Company prepared the consolidated financial statements in accordance with the requirements of Federal Law "On Consolidated Financial Statements" No. 208-FZ of 7/27/2010.*

## Results of Financial and Economic Activities of the Company



**Olga Vyacheslavovna Ocheredko**  
Deputy Director General  
for Economy and Finance

"As of the end of the financial year, the Company's net profit amounted to RUB 2,141 mln, which is RUB 688 mln more than in 2015. As of the end of 2016, Debt/EBITDA ratio amounted to 2.11.

In 2016, the Company developed and implemented the Program of Operating Efficiency Improvement and Expenses Reduction of Kubanenergo for 2016–2020, aimed at the optimization of expenses, reduction of specific costs of power-generating equipment operation, reduction of power losses in the grids, and energy efficiency improvement. The Program efficiency criteria take into account the target values specified by the Development Strategy of the Electric Grid Complex of the Russian Federation (approved by Decree of the Government of the Russian Federation No. 511-r of 4/3/2013) as well as by Directive of the Government of the Russian Federation No. 4750p-P13 of 7/4/2016. As of the end of the reporting period, the target values for operating expenses reduction against the 2015 level were achieved."

### Analysis of the Results of the Company's Financial and Economic Activities

As of the end of 2016, the revenue from sales of goods (services) amounted to RUB 41,726.2 mln, which is RUB 6,022.0 mln (16.9%) more than in 2015, including the revenue from electric power transmission RUB 39,262.4 mln (RUB 4,859.3 mln more than in 2015). This growth results from the increase by 601.9 mln kWh of scope of services performed and from the growth of straight-line rate for the "other" consumer group transmission services approved by REC-PTD KT in the 2 half of the year 2016 compared to the 1 half of the year 2016.

The net cost including the administrative costs amounted to RUB 35,927.8 mln, which is RUB 2,778.5 mln (8.4%) more than in 2015. This growth is caused by the increase of the electricity purchases to compensate for losses, the costs of services of distribution grid companies, the depreciation of fixed and intangible assets and other expenses.

Profit before tax amounted to RUB 3,506.2 mln, which is RUB 1,290.5 mln (58.2%) more than in 2015.

As of the end of 2016, the net profit of the Company amounted to RUB 2,140.5 mln (RUB 688.0 mln (47.4%) more than in 2015). This increase is caused by the growth of revenue from the electricity transmission as a result of net electricity supply and transmission tariff growth.

*Main financial and economic indicators, RUB mln*

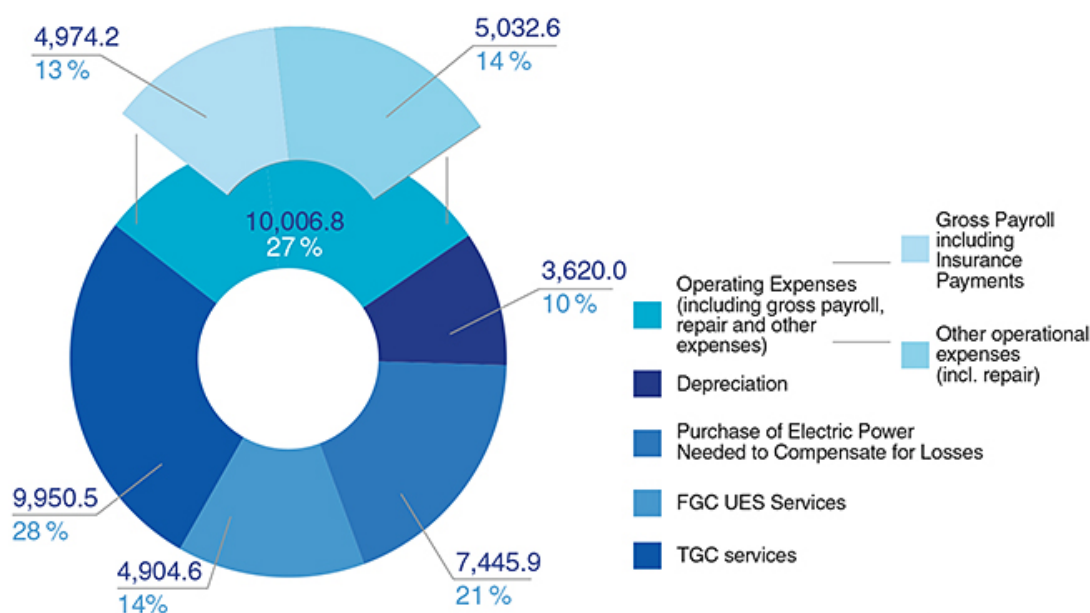
Item No.	Indicator	2016	2015	2014
1	<b>Revenue from products (services) sales, including:</b>	41,726	35,704	29,393
1.1	<i>from power transmission</i>	39,262	34,403	28,464
1.2	<i>from technological connection</i>	2,381	1,213	848
1.3	<i>from sales of electric power</i>	0	0	0
1.4	<i>from other activities</i>	83	88	81
2	<b>Net costs of products (services)</b>	-35,830	-33,149	-29,919
3	Gross profit	5,896	2,555	-525

4	Administrative expenses	-98	0	0
5	Selling expenses	0	0	0
6	Profit (loss) from sales	5,798	2,555	-525
7	Interest receivable	90	479	634
8	Interest payable	-1,889	-2,261	-1,801
9	Affiliation income	0	0.06	0
10	Other income, total	2,616	6,851	3,039
11	Other costs, total	-3,109	-5,407	-5,084
12	<b>Income (loss) before tax</b>	<b>3,506</b>	<b>2,216</b>	<b>-3,736</b>
13	Income tax and other payments	-1,366	-763	104
14	<b>Net profit</b>	<b>2,141</b>	<b>1,452</b>	<b>-3,632</b>
15	<b>EBITDA<sup>13*</sup></b>	<b>9,015</b>	<b>7,670</b>	<b>540</b>

### Structure of Expenses

As of the end of 2016, net costs (including administrative expenses) amounted to RUB 35,927.8 mln, which is RUB 2,778.5 mln more than in 2015. This growth is caused by the increase of the electricity purchases to compensate for losses, the costs of services of distribution grid companies, the depreciation of fixed and intangible assets and other expenses.

*Net Costs Structure (including administrative and business expenses in 2016, RUB mln and %:*



As of the end of 2016, the electricity purchased to compensate for losses amounted to RUB 7,445.9 mln (21% of total expenses). In absolute terms, when compared to 2015, the increase amounted to RUB 963.1 mln, resulting from the growth of the average cost of the electricity purchased to compensate for losses.

The cost of PJSC FGC UES services amounted to RUB 4,904.6 mln (14% of total expenses). The absolute growth against 2015 amounted to RUB 103.3 mln, and is caused by the growth of actual net power flow when compared to the same period of the previous year as well

<sup>13</sup> EBITDA was calculated in accordance with the following procedure:  
EBITDA = Profit Before Tax (PBT) + Interests Payable + Depreciation.

as by the growth of tariff rates for the loss compensation in UNEG networks and for the electric grid maintenance.

As of the end of 2016, the cost of the distribution grid companies services amounted to RUB 9,950.5 mln (28% of total expenses). When compared to the previous year, the cost growth amounted to RUB 1,146.7 mln due to increase of the amount of the electric power transmitted through the grids of related grid companies and of their number.

As of the end of 2016, depreciation of fixed and intangible assets amounted to RUB 3,620.0 mln which is RUB 427.4 more than in 2015 due to commissioning of fixed assets under the approved investment program of the Company.

In 2016, the personnel costs, including the insurance payments, amounted to RUB 4,974.2 mln (13.0% of total expenses), which is RUB 652.1 mln (15.0%) more than at the year end 2015. The increase of costs under this item was caused by:

- the growth of tariff sums due to the tariff rates adjustment (position salary) through increase of an employee tariff multiplier within the remuneration level pursuant to the “Regulation on Personnel Competency Evaluation” (Attachment 2 to the “Regulation on Personnel Compensation and Benefits of Kubanenergo PJSC”);
- the growth of sums paid as the compensation for termination of employment contract upon mutual agreement by the parties;
- the increase of special bonus payments to the personnel for identification of unaccounted electric power consumption under the reports on unaccounted and non-contractual electric power consumption, for commissioning of capital facilities and technical re-equipment.

Other expenses in 2016 amounted to RUB 5,032.6 mln (14% of total expenses), which is RUB 514.1 mln less than at the year end 2015. The main reason for the costs reduction is the decrease of costs for the technological connection to the grids of other companies amounting to RUB 1,217.1 mln due to the recognition of the costs for the technological connection of 220 kV Buzhora SS to the PJSC FGC UES grids in December 2015.

*The Program of Operating Efficiency Improvement and Expenses Reduction*  
The Program of Operating Efficiency Improvement and Expenses Reduction of Kubanenergo PJSC for 2016–2020 was approved by the Company’s Board of Directors on 4/22/2016 (Minutes No. 235/2016 of 4/25/2016). Implementation of measures under the Program is covered by the Business Plan, Investment Program, Energy Conservation and Energy Efficiency Improvement Program, Innovative Development Program and other dedicated programs developed by the Company.

The Program efficiency criteria take into account the target values specified by the Development Strategy of the Electric Grid Complex of the Russian Federation (approved by Decree of the Government of the Russian Federation No. 511-r of 4/3/2013) as well as by Directive of the Government of the Russian Federation No. 4750p-P13 of 7/4/2016.

The reduction of controllable operating costs in 2016 against 2012 for implementation of the Development Strategy of the Electric Grid Complex of the Russian Federation approved by Executive Order of the Government of the Russian Federation No. 511-p of 4/3/2013 amounted to RUB 623 mln or 15%, with the target value of 15%.

The reduction of operating costs in accordance with Directive of the Government of the Russian Federation No. 4750p-P13 of 7/4/2016 in 2016 against 2015 amounted to 38%, which conforms with the target value (10%).

As part of the operating efficiency improvement program, the Company implemented the following key measures:

1. Improvement of equipment, buildings, structures maintenance and overhaul control efficiency:

- re-breakdown of work techniques by process areas: 35–220 kV OHL, 35–110 kV SS; 0.4–10 kV distribution grids (OHL, TSS). Reduction of contractor resources and increase of the Company’s own resources in the amount of RUB 0.9 mln;



2. Improvement of the working capital management efficiency:
  - optimization of accounts receivable in the amount of RUB 1,679.5 mln;
  - optimization of current liabilities in the amount of RUB 89.7 mln;
3. Improvement of the fixed assets management efficiency:
  - reduction of costs for the non-core assets maintenance and management, including their disposal effects in the amount of RUB 0.7 mln;
  - consolidation of electric grid facilities in the amount of RUB 349 mln.
4. Improvement of energy efficiency:
  - measures, aimed at reduction of electric power losses in accordance with the Dedicated Power Losses Reduction Program of Kubanenergo PJSC for 2016 till 2020, and the Energy Conservation and Energy Efficiency Improvement Program of Kubanenergo PJSC for 2016–2020 in the amount of RUB 256.9 thou;
  - measures aimed at efficient use of fuel and energy resources in the amount of RUB 1.3 mln;
5. Other measures:
  - measures aimed at reduction of non-contractual electric power consumption in the amount of RUB 69.1 mln.

*Analysis of the Company's financial status and operations results*

Indicator/Year	As of 12/31/2014	As of 12/31/2015	As of 12/31/2016
<b>Liquidity Ratio and Current Paying Capacity</b>			
Absolute liquidity ratio	0.44	0.12	0.11
Quick assets ratio	0.72	0.38	0.79
Current liquidity ratio	0.81	0.45	0.92
Working Capital to Current Assets Ratio	-0.24	-1.26	-0.10
<b>Turnover and Efficiency Ratio</b>			
Accounts payable turnover ratio	2.50	2.77	3.26
Growth rates correlation of accounts receivable and accounts payable	0.79	1.21	1.84
Correlation of total accounts receivable and accounts payable	0.33	0.40	0.73
Share of accounts receivable in revenue	0.11	0.12	0.14
<b>Financial Stability Indicators</b>			
Equity Ratio	0.48	0.50	0.53
Total debt/EBITDA ratio	32.27	2.23	2.11
EBITDA/ %	0.30	3.50	4.76

As of the end of 2016, the absolute liquidity ratio reduced when compared to 2015 due to the reduction of finance. However, the Quick and Current Ratios, as well as the Working Capital to Current Assets Ratio showed upward trend when compared to the previous year due to the growth of accounts receivable and reduction of short-term loan funds, resulting from substitution of short-term loans with long-term ones, as well as from the reduction of accounts payables.

The Turnover and Efficiency Ratio growth in 2016 results from the increase of accounts receivables and decrease of accounts payables of the Company.

As of 12/31/2016, the Equity Ratio was 0.53, which is 0.03 higher than in 2015. The Ratio increased due to the Company equity capital growth through receiving of profit at the year end 2016 in the amount of RUB 2,140.5 mln, as well as due to the issue of additional Company's shares. The growth of EBITDA and interests paid ratio, as well as the reduction of total debt and EBITDA ratio are attributed to the growth of EBITDA and the reduction of interests paid by the Company in the reporting period.

## Accounts Receivable

### *Analysis of Changes in Accounts Receivable, RUB mln*

	As of 12/31/2016	As of 12/31/2015	As of 12/31/2014
<b>Accounts Receivable, including:</b>	<b>7,119.42</b>	<b>4,900.77</b>	<b>3,830.30</b>
Payments whereon are expected later than in 12 months after the reporting date	12.61	12.43	14.98
– purchasers and customers	-	-	-
– bills receivable	-	-	-
– advances paid	-	-	-
– other accounts receivable	12.61	12.43	14.98
Payments whereon are expected within 12 months after the reporting date	7,106.81	4,888.35	3,815.32
– purchasers and customers	6,410.58	4,601.99	3,267.64
<i>for power transmission</i>	6,381.93	4,591.30	3,223.64
– bills receivable	-	-	-
– subsidiaries' and affiliates' dividends in arrears	-	-	-
– participants' (founders') authorized capital payments in arrears	-	-	-
– advances paid	13.37	25.24	18.25
– other accounts receivable	682.86	261.12	529.42

The total accounts receivable of Kubanenergo PJSC as of 12/31/2016, net of the doubtful debts provision, amounted to RUB 7,119.42 mln.

As of 12/31/2016, the provision for doubtful debts amounted to RUB 2,447.22 mln, including the doubtful receivables in the amount of RUB 2,339.92 mln (reflected in the balance sheet as a reduction of accounts receivable) and the provision for advances paid for the acquisition of fixed assets in the amount of RUB 107.30 mln (reflected in the balance sheet under non-current assets, as a reduction of arrear in advances).

To reduce the accounts receivable, the Company performs claims work, including the pre-court and court dispute settlement procedures. In the reporting period, unrecoverable receivables in the amount of RUB 0.94 mln were written off.

Receivables for rendered services related to transmission of electric power to contractors of Kubanenergo PJSC as of 12/31/2016 (excluding the reserve for doubtful debts) amounted to RUB 6,381.93 mln. Disputable receivables amount to RUB 1,022.467 mln.

Growth of receivables for rendered services related to transmission of electric power (taking into account debts before deduction of the reserve for doubtful debts) amount to RUB 1,662.82 mln (27.06%) as compared to the amount of receivables in 2015 is caused by non-payments of Kubanenergobyt OJSC affiliated with the TNS Energo Group of Companies the debt of which totaled to RUB 4,507.61 mln as of 12/31/2016, including the doubtful debt in the amount of RUB 671.49 mln, that makes 2.5 settling periods with the average monthly accrual of RUB 1,810.22 mln.

#### *Receivables management:*

Following the Company claims work for legal collection of receivables for the power transmission services performed in 2016, favorable judicial decisions were received in 18 legal

cases totaling to RUB 466 mln. Claims for the recovery of RUB 29 mln were dismissed. The share of claims satisfied in the Company's favor was 94%.

In 2015, the claims for the amount of RUB 98 mln were satisfied in the Company's favor (6 legal cases).

Following the results of judicial decisions, enforcement orders for the amount of RUB 304 mln were received in 2016, of which RUB 266 mln or 88% were satisfied. During the previous year, enforcement orders for the amount of RUB 455 mln were received, of which RUB 4 mln or 1% were satisfied.

## Accounts Payable

### *Analysis of Changes in Short-Term Accounts Payable, RUB mln*

	As of 12/31/2016	As of 12/31/2015	As of 12/31/2014
<b>Short-term accounts payable, including</b>	<b>8,280.20</b>	<b>11,799.75</b>	<b>10,619.88</b>
– suppliers and contractors	4,837.35	4,343.66	7,795.37
– bills payable			
– salary payable to personnel	212.34	181.16	122.58
– payables to state extra-budgetary funds	93.94	86.76	66.36
– taxes and duties payable	654.43	1,502.99	183.79
– advances received	1,922.41	3,860.09	2,187.28
– profit payable to stockholders (founders)	0.04		
– other accounts payable	559.70	1,825.09	264.50

In 2016, the short-term payables decreased by RUB 3,519.55 mln when compared to 2015 and amounted to RUB 8,280.20 mln as of 12/31/2016.

The following changes were observed:

- debts to suppliers and contractors increased by RUB 493.70 mln due to the growth of arrears in payments for the electricity transit services by RUB 387.84 mln;
- arrears in advances received decreased by RUB 1,937.68 mln, the bulk of the arrear includes advances for technical integration in the amount of RUB 1,909.49 mln.
- salary payable to personnel increased by RUB 31.17 mln, this liability is included into current liabilities;
- taxes and duties payable decreased by RUB 848.56 mln;
- other accounts payable decreased by RUB 1,265.39 mln.

As of the end of 2016, the overdue accounts payable of Kubanenergo PJSC amounted to RUB 2,073.36 mln.

In 2016, long-term accounts payable amounted to RUB 1,429.37 mln.

## Loans and Credits

In 2016, Kubanenergo PJSC raised loans amounting to RUB 13,220 mln, including:

- long-term loans in the amount of RUB 10,771 mln;
- short-term loans in the amount of RUB 2,449 mln.

The raised long-term loans are used for financing investment activities, payment of dividends, as well as for repayment of loans with higher interest rates, to reduce the interest expenses of the Company. Due to refinancing, the share of long-term borrowings in the debt portfolio of the Company was increased and the average cost of Kubanenergo PJSC loan funds was reduced.

In 2016, the short-term loans were raised as part of overdraft loans and were paid off in full as of 12/31/2016.



During 2016, the Company paid off:

- short-term loans in the amount of RUB 9,978 mln;
- long-term loans in the amount of RUB 1,330 mln.

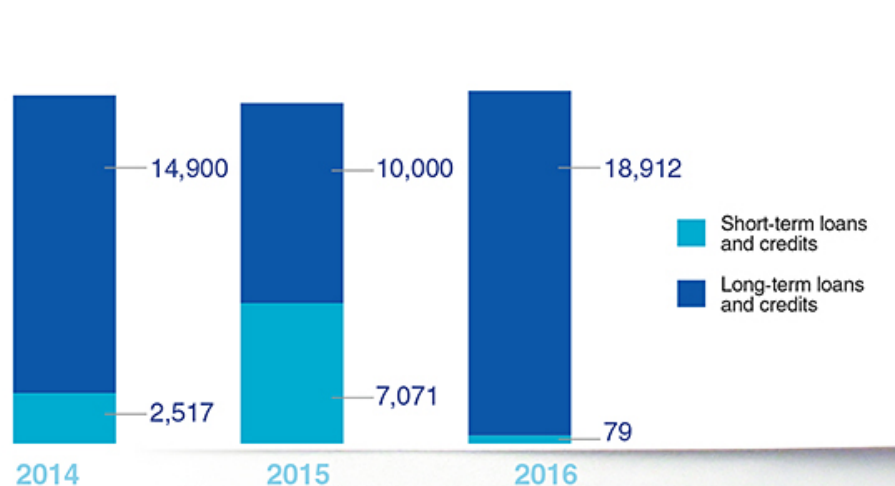
The actual amount of outstanding short-term loans and credits of Kubanenergo PJSC amounted to RUB 79 mln as of 12/31/2016, and included interests on bonds and on the loan granted by PJSC Sberbank, due to the timing difference between the accrual and payment under the loan contract terms.

The total short-term loan interests qualified as Company's expenses in 2016 amounted to RUB 540 mln.

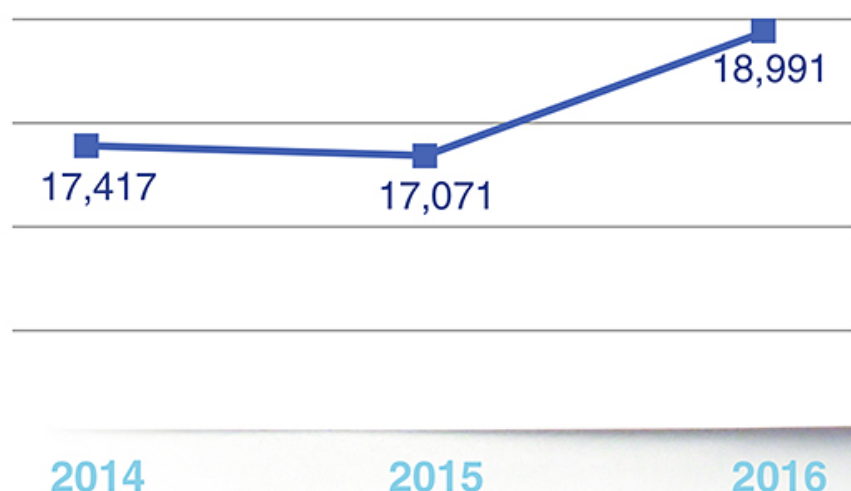
As of 12/31/2016, the total outstanding long-term loans and credits amounted to RUB 18,912 mln. The total long-term loan interests qualified as Company's expenses in 2016 amounted to RUB 1,349 mln.

Kubanenergo PJSC has no debts under loans and credits. The total outstanding interest for 2016 amounted to RUB 1,889 mln.

*The structure of the Company's debt portfolio for 2014–2016, RUB mln:*



*Dynamics of the Company's debt portfolio for 2014–2016, RUB mln:*



Kubanenergo PJSC did not cooperate with rating agencies. The Company has not been credit rated since 2009.

#### Company's Bond Issues

As of 12/31/2016, Kubanenergo PJSC placed two issues of exchange bonds under the Exchange Bonds Program (identification number 4-00063-A-001R-02E of 8/26/2015) approved on 7/29/2015 by the Board of Directors (Minutes No. 217/2015 of 7/31/2015):

- Issue of series 001R-02 bonds in the amount of RUB 3,400 mln under the following terms and conditions:

- ✓ maturity: ten (10) years;
- ✓ bonds acquisition offer under the agreement with bond holders not later than after 4 years;
- ✓ coupon rate set when placing bonds: from the 1<sup>st</sup> to the 14<sup>th</sup> coupon – 12.63% per annum;

- Issue of series 001R-01 bonds in the amount of RUB 3,600 mln under the following terms and conditions:

- ✓ maturity: ten (10) years, without offer;
- ✓ coupon rate: 10.44% per annum;

The bonds were placed in 2015. The borrowed funds are used to repay the loans with higher interest rates in order to reduce interest expenses of the Company. Kubanenergo PJSC has no arrears on bond issues.

On 9/20/2016, Kubanenergo PJSC Board of Directors approved Kubanenergo PJSC 002R series Exchange Bonds Program (Minutes No. 251/2016). On 10/24/2016, the Exchange Bonds Program was assigned identification number 4-00063-A-002R-02E. The Program allows for the placement of certified interest-bearing inconvertible bearer exchange bonds subject to mandatory deposit with the total nominal price of all exchange bonds issues, placed under the 002R series Exchange Bonds Program, of RUB 25 bln, inclusive, maturing on the day no later than within 10,920 days after the day of placement of the exchange bonds issue under the Exchange Bonds Program placed by public offering. In 2016, these bonds were not placed.