Zoltav Resources Inc.

Half year 2018 report and unaudited interim condensed consolidated financial statements

for the six months ended 30 June 2018

Zoltav Resources Inc.

Corporate information

Board of Directors
Lea Verny – Independent Non-executive Chairman
Alexander Gorodetsky − Independent Non-executive Director
Andrey Immel − Non-executive Director

Audit Committee

Lea Verny (Chairman) and Andrey Immel

Remuneration and Nomination Committee

Alexander Gorodetsky (Chairman) and Lea Verny

Corporate Administrator

CO Services Cayman Limited
P.O. Box 10008, Willow House, Cricket Square,
Grand Cayman KY1-1001, Cayman Islands

Registered Office

PO Box 10008, Willow House, Cricket Square,
Grand Cayman KY1-1001, Cayman Islands

Bankers

Barclays Private Clients International Limited
39-41 Broad Street, St Helier, Jersey, JE4 8PU,
Channel Islands

Deutsche Bank International Limited
St Paul's Gate, New Street, St Helier,
Jersey, JE4 8ZB, Channel Islands

Nominated Adviser

SP Angel Corporate Finance LLP
Prince Frederick House, 35-39, Maddox Street,
London, W1S 2PP, United Kingdom

Solicitors

Berwin Leighton Paisner
Adelaide House, London Bridge, London,
EC4R 9HA, United Kingdom

Joint Brokers

SP Angel Corporate Finance LLP
Prince Frederick House, 35-39, Maddox Street,
London, W1S 2PP, United Kingdom

Panmure Gordon (UK) Limited
1 New Change, London, EC4M 9AF,
United Kingdom

Independent Auditor

Ernst & Young LLC

Sadovnicheskaya nab., 77, bld. 1, Moscow,
115035, Russia

Registrar

Computershare Investor Services (Cayman) Limited
R&H Trust Co. Ltd, Windward 1, Regatta
Office Park, West Bay Road, Grand Cayman KY1-1103, Cayman Islands

Zoltav Resources Inc.

Chairman's statement

I am pleased to report that Zoltav delivered a 4% increase in net profit for the first half of 2018 to RUB 72 million (H1 2017: RUB 69 million). This performance was achieved as a result of our team's dedication to operational efficiency and in spite of the anticipated decline in production revenues from the Permian fields in West Bortovoy.

Whilst gas production declined by 18%, and oil and condensate production declined by 12%, this was offset by higher commodity prices, resulting in revenues decreasing by 10% in the period to RUB 831 million (H1 2017: RUB 924 million). Operational efficiencies enabled the Company to restrict the negative impact on EBITDA to just 2% at RUB 411 million (H1 2017: RUB 420 million).

The Company anticipated the decline in production since the drilling programme in the Permian fields on West Bortovoy was suspended in 2017 pending the interpretation of 3D seismic data. However, gas production in H1 2018 declined at a slower rate than predicted, primarily because Zhdanovskoye Well 8, which was anticipated to be shut down over the summer due to water intrusion, remains in production.

A new geotechnical team, led by former Bashneft and TNK-BP technical executive Yuri Krasnevsky, was appointed in May 2018 and was fully staffed and operational in June 2018. Their mandate is three-fold: to execute an exploration programme targeting the deeper structures in West Bortovoy; to enhance output from existing and new well stock producing from the shallower Permian structures; and, in the longer term, to devise a strategy to commercialise East Bortovoy. We are delighted as we believe we have been able to attract one of the best geotechnical teams in the country to the project.

The geotechnical team has undertaken a technical review of the 3D seismic acquisition programme which began in 2017 and has concluded that the 341 sq km of data acquired to date over the North Mokrous area of the Mokrousovskoye block in West Bortovoy will be sufficient to allow for the positioning of an exploration well targeting a prospective field in the Middle Devonian horizon at approximately 4,200-4,500 m true vertical depth (TVD). The Company will therefore not be required to commit further capital to the seismic acquisition programme prior to the drilling of an exploration well. While the timing of the exploration well remains on schedule to be drilled towards the end of Q1 2019, as a result of the technical review, the final interpretation of the seismic data is now expected to be completed in mid-Q1 2019.

Following the re-interpretation of existing seismic data over the Permian fields in West Bortovoy, the new geotechnical team is focused on delivering a low-risk strategy to reduce the production decline from these fields and, ultimately, to bring production back up to the Western Gas Plant's capacity. The review of operations that follows summarises the work programmes which are designed to achieve these objectives.

I would like to commend the team in Saratov for their continued commitment to operational excellence, which included a record maintenance shutdown of the Western Gas Plant of just 48 hours.

We look forward to sharing over the coming months insights from the seismic interpretation programme as we prepare for a busy work programme in 2019.

Lea Verny
Non-executive Chairman
25 September 2018

Production

Production from Zoltav's Western Gas Plant at Bortovoy averaged 6,151 boepd (829 toepd) during H1 2018, an 18% decline when compared to 7,480 boepd (1,021 toepd) in H1 2017.

Average daily production during H1 2018 was 34.9 mmcf/d (0.99 mmcm/d) of gas and 335 bbls/d (43 T/d) of oil and condensate (H1 2017: 42.6 mmcf (1.2 mmcm/d) of gas and 380 bbls/d (48 T/d) of oil and condensate).

Overall in H1 2018, the Company produced[1]

- Natural gas: 6,317 mmcf (179 mmcm) (H1 2017: 7,711 mmcf (218 mmcm))

- Oil and condensate: 66,558 bbls (7,715 t) (H1 2017: 68,713 bbls (8,753 t))

The current well stock producing from the Permian fields consists of eleven gas wells and two oil wells working via artificial lift. The well stock is in natural production decline. Following the re-interpretation of existing seismic data, the new geotechnical team is focused on delivering a low-risk strategy to reduce the production decline from these fields and, in due course, to bring the Western Gas Plant back up to capacity. The geotechnical team is also carrying out hydrodynamic studies, including flow testing, on seven wells in order to be able to make more precise production forecasts and plan well stimulations.

Development

Bortovoy

The near-term work programme includes carrying out well stimulations on ten wells by the end of the year with the objective of generating an additional 6 mmcf/d (170 mcm/d) of gas. The Company has installed a new well-head compressor on the Karpenskoye field facility in order to help achieve greater pressure equilibrium and therefore to optimise gas production rates. The compressor is currently going through the startup and commissioning phase. The Company expects to begin to see the benefits from this near-term work programme before the end of this year.

In the medium-term, the work programme envisages drilling sidetracks on existing wells (two gas wells on the Zhdanovskoye field and one oil well on the Karpenskoye field); and connecting three Soviet wells (one re-entry and two sidetracks) to the Western Gas Plant via a new pipeline. If successful, the medium-term objective is to return the Western Gas Plant to full capacity.

Long-term plans are focused on proving and commercialising the potential of the deeper Devonian structures on West Bortovoy and the development of East Bortovoy.

Each programme comprises projects which are subject to the decision of the investment committee which takes into account a range of factors including but not limited to estimated production profiles, CAPEX evaluations and risk assessments. At present, three wells are approved for workover.

Koltogor

The Koltogor Licences in the Khantiy Mansisk Autonomous Okrug, Western Siberia are not currently a focus of investment. The Company continues to monitor the activities of the Bazhen Technology Centre, launched by Gazprom Neft in 2017, which is focusing on the development of independent skills and technologies for the cost-effective development of hydrocarbons in the Bazhenov formation.

[1]Net production is the volume actually sold to customers. It comprises all extracted hydrocarbons, less own consumption and losses. The Company uses net production volumes throughout the half-year 2018 report instead of previously used total extracted volumes.

Group Reserves under PRMS as per latest report of DeGolyer and MacNaughton (May 2014):

		Proved	Probable	Proved and probable	Possible
Bortovoy Licence					
Gas	bcf	352.9	396.8	749.7	640.0
Oil & liquids	mmbbls	2.0	1.8	3.8	2.4
Gas, oil and liquids	mmboe	62.0	69.2	131.2	111.2
Koltogor Licences					
Gas	bcf	0.5	23.5	24.0	55.7
Oil	mmbbls	1.6	73.5	75.1	174.0
Total	mmboe	1.7	77.5	79.2	183.5
Total					
Gas	bcf	353.4	420.3	773.7	695.7
Oil & liquids	mmbbls	3.6	75.3	78.9	176.4
Gas, oil and liquids	mmboe	63.7	146.7	210.4	294.7

The Company is planning a re-evaluation of reserves under PRMS following completion of the exploration programme currently ongoing on the Bortovoy Licence.

Note on conversion rates

Tonnes of crude oil produced are translated into barrels using conversion rates reflecting oil density from each of the fields. Crude oil and liquid hydrocarbons expressed in barrels are translated from tonnes using a conversion rate of 7.85 barrels per tonne. Translations of cubic feet to cubic metres are made at the rate of 35.3 cubic feet per cubic metre. Translations of barrels of crude oil and liquid hydrocarbons into barrels of oil equivalent (“boe”) are made at the rate of 1 barrel per boe and of cubic feet into boe at the rate of 290 cubic feet per boe.

Financial review

The effect of recurring optimisation initiatives and new cost-cutting initiatives enabled Zoltav to generate RUB 72 million of net profit in the first half of 2018. EBITDA slightly decreased by 2% to RUB 411 million, but net cash from operations increased by 2% to RUB 377 million.

Revenue
The Group's revenues in H1 2018 decreased by 10% to RUB 831 million, compared to RUB 924 million in H1 2017.

Approximately 80% of revenue was derived from gas sold to Mezhregiongaz, a Gazprom subsidiary, at the transfer point on entry to the Central Asia – Centre gas pipeline system. The gas prices are fixed in a contract with Mezhregiongaz and are subject to indexation. The Russian Government approved a 3.4% gas price increase from 21 August 2018 and accordingly the Company signed an addendum to its contract with Mezhregiongaz.

The remaining revenue was from oil and condensate sold directly at the Western Gas Plant through a tender process to a small number of different buyers. Favourable market prices during 2018 and a diversified portfolio of buyers positively impacted average oil and condensate prices which were RUB 2,624/bbl (RUB 20,600/t) in H1 2018 compared to RUB 2,000/bbl (RUB 15,800/t) in H1 2017.

Cost of sales and G&A costs
The Group's operational and G&A costs decreased by 18% to RUB 88 million (H1 2017: RUB 108 million), mostly driven by maintenance optimisation and chemicals usage efficiency (mostly methanol).

Total cost of sales was RUB 547 million (H1 2017: RUB 585 million). This comprised RUB 179 million of mineral extraction tax (H1 2017: RUB 192 million), RUB 220 million of depreciation and depletion of assets (H1 2017: RUB 218 million) and RUB 148 million of other cost of sales (H1 2017: RUB 175 million).

Other expenses, mainly comprising offshore expenses, decreased by 78% to RUB 7 million (H1 2017: RUB 33 million).

Operating profit
Zoltav achieved an operating profit for H1 2018 of RUB 191 million, compared to RUB 202 million in H1 2017.

Finance costs of RUB 93 million (H1 2017: RUB 117 million) are mainly represented by interest on the remaining RUB 1,410 million Sberbank facility.

Profit before tax
Zoltav generated RUB 101 million of profit before tax, compared to RUB 99 million in H1 2017.

Taxation
Production based tax for the period was RUB 179 million (H1 2017: RUB 192 million) which is recognised in the cost of sales. The MET tax formula is based on multi-component gas composition, average gas prices and reservoir complexity and maturity. The effective MET rate applicable for the period slightly increased due to gas price growth to RUB 27/mcf or RUB 949/mcm (H1 2017: RUB 24/mcf or RUB 838/mcm).

The income tax charge for the year was RUB 29.4 million (H1 2017: RUB 30.0 million).

Net profit
The net profit recorded was RUB 72 million compared to RUB 69 million in H1 2017 due to the positive impact of operating efficiencies.

Cash
Net cash generated from operating activities was RUB 377 million (H1 2017: RUB 370 million).

Financial review

The operating subsidiary, Diall Alliance, successfully serviced its credit facility with PJSC Sberbank and repaid a further RUB 150 million of the principal amount (RUB 1,560 million at 31 December 2017) according to its schedule. The Company remains in line with the covenants of its credit facility agreement, is benefitting from lower interest rates and is actively negotiating refinance terms.

Total cash at the end of the period was RUB 315 million.

Kirill Suetov
Chief Financial Officer
25 September 2018

Lea Verny – Independent Non-executive Chairman, Senior Independent Director

Lea Verny was appointed as a non-executive director in December 2016. She has significant and high level corporate finance experience, with particular expertise in Russia. Since 2008, Lea Verny has acted as an independent financial adviser on cross-border transactions. Prior to becoming an independent consultant, Lea Verny served as a private banker with Banque Pictet, Switzerland, where she was responsible for developing the bank's activities in Russia, following a career of more than a decade with HSBC. From 2001 to 2007, Lea Verny was Head of Investment Banking for HSBC Bank plc in Moscow, during which time she advised on structured transactions for large Russian and CIS corporations including Lukoil, Rostelekom, Eastern Oil Company and Rosbank. Between 1997 and 2001, Ms Verny was a representative of HSBC Investment Bank plc in Russia, where she was responsible for establishing the bank's presence in the country and developing opportunities specifically within the oil and gas sector. Lea Verny holds a Bachelor's degree in Statistics and International Relations from the Hebrew University in Jerusalem as well as an MBA from INSEAD in France.

Alexander Gorodetsky – Independent Non-executive Director

Alexander Gorodetsky was appointed as a non-executive director in September 2015. He is currently the general partner of Strategy Capital Advisor Limited, a private equity fund established in 2009 with a mandate to invest in projects, including within the oil and gas sector, across the former Soviet Union. Prior to Strategy Capital Advisor Limited, Alexander Gorodetsky was first deputy to the chairman of East One Group, an international investment advisory group providing strategic and investment management services. During his time at East One Group, he assisted in the strategic development of over 25 portfolio companies including GEO ALLIANCE Group, one of the leading independent oil and gas exploration and production groups in Ukraine. From 2000-2006, Alexander Gorodetsky was president/business unit leader for TNK-BP Ukraine. He contributed significantly to the increased brand awareness of TNK-BP in the Ukrainian market, where it is among the leading oil and gas companies. He began his career in 1995 within Alfa-Eco, a leading gas and oil trading business in Russia.

Andrey Immel − Non-executive Director

Andrey Immel was appointed as a non-executive director in September 2015. He is an experienced Russian corporate lawyer. He has, since 2012, been the head of the legal department of Moscow-based Contact-Service LLC, a real estate company, where his responsibilities include corporate governance and the provision of legal support for transactions. From 2008-2012, Andrey Immel worked for Himuglemet, a manufacturer of conveyer band and other components for coal mines, both as legal counsel and as a corporate and tax lawyer. His responsibilities included legal due diligence and support for corporate transactions.

Statement of directors' responsibilities

The Directors confirm that, to the best of their knowledge, these condensed consolidated interim financial statements have been prepared in accordance with IAS 34 as adopted by the European Union, and that the interim management report includes a fair review of the information required by the Disclosure and Transparency rules 4.2.7R and 4.2.8R, namely:

- an indication of important events that have occurred in the first six months and their impact on the condensed consolidated financial statements, and description of the principal risks and uncertainties for the remaining six months of the financial year; and
- material related party transactions in the first six months and any material changes in related party transactions described in the Last Annual report.

A list of Directors is maintained on the Zoltav Resources Inc. website: www.zoltav.com.

For and on behalf of the Board:

Lea Verny
Non-executive Chairman
25 September 2018

Report on review of interim financial information

To the Shareholders and Board of Directors of
Zoltav Resources Inc.

Introduction

We have reviewed the accompanying interim condensed consolidated financial statements of Zoltav Resources Inc. and its subsidiaries, which comprise the interim condensed consolidated statement of financial position as at 30 June 2018, interim condensed consolidated statement of comprehensive income, interim condensed consolidated statement of changes in equity and interim condensed consolidated statement of cash flows for the six-month period then ended, and notes to the interim consolidated financial statements, including a summary of significant accounting policies (interim financial information). Management of Zoltav Resources Inc. is responsible for the preparation and presentation of this interim financial information in accordance with IAS 34, *Interim Financial Reporting*. Our responsibility is to express a conclusion on this interim financial information based on our review.

Scope of review

We conducted our review in accordance with International Standard on Review Engagements 2410, *Review of Interim Financial Information Performed by the Independent Auditor of the Entity*. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying interim financial information is not prepared, in all material respects, in accordance with IAS 34, *Interim Financial Reporting*.

T.L. Okolotina
Partner
Ernst & Young LLC
25 September 2018

Details of the entity
Name: Zoltav Resources Inc.
Record made in the Registar of Companies, Cayman Islands on 18 November 2003, Registration Number 130605.
Address: PO Box 10008, Willow House, Cricket Square, Grand Cayman KY1-1001, Cayman Islands.

Details of the auditor
Name: Ernst & Young LLC
Record made in the State Register of Legal Entities on 5 December 2002, State Registration Number 1027739707203.
Address: Russia 115035, Moscow, Sadovnicheskaya naberezhnaya, 77, building 1.
Ernst & Young LLC is a member of Self-regulated organization of auditors “Russian Union of auditors” (Association) (“SRO RUA”). Ernst & Young LLC is included in the control copy of the register of auditors and audit organizations, main registration number 11603050648.

Interim condensed consolidated statement of comprehensive income

for the six months ended 30 June 2018

(in '000s of Russian rubles, unless otherwise stated)

	Note	Six months ended 30 June 2018 (unaudited)	Six months ended 30 June 2017 (unaudited)
Revenue	**3**	**830,574**	**924,450**
Cost of sales			
Mineral extraction tax		(178,998)	(192,212)
Depreciation and depletion		(219,739)	(217,809)
Other cost of sales		(148,019)	(175,412)
Total cost of sales		**(546,756)**	**(585,433)**
Gross profit		**283,818**	**339,017**
Operating, administrative and selling expenses		(88,236)	(108,094)
Other income		2,774	4,000
Other expenses		(7,346)	(33,010)
Operating profit		**191,010**	**201,913**
Impairment of exploration and evaluation assets		(6,482)	–
Finance income		9,303	13,674
Finance costs		(92,740)	(116,549)
Profit before tax		**101,091**	**99,038**
Income tax expense	4	(29,483)	(30,043)
Profit for the period attributable to owners of the parent being total comprehensive income		**71,608**	**68,995**

		RUB	**RUB**
Earnings per share attributable to owners of the parent			
Basic	**8**	0.50	0.49
Diluted	**8**	0.50	0.48

Kirill Suetov
Chief Financial Officer
25 September 2018

The accompanying notes on pages 14-30 are an integral part of these interim condensed consolidated financial statements.

Zoltav Resources Inc.

Interim condensed consolidated statement of financial position

as at 30 June 2018

(in '000s of Russian rubles, unless otherwise stated)

	Note	As at 30 June 2018 (unaudited)	As at 31 December 2017
Assets			
Non-current assets			
Exploration and evaluation assets	**5**	3,409,682	3,259,353
Property, plant and equipment	**6**	3,827,147	4,007,302
Total non-current assets		**7,236,829**	**7,266,655**
Current assets			
Inventories		30,794	20,877
Trade and other receivables		131,601	152,574
Other current non-financial assets		13,919	11,400
Cash and cash equivalents	**12.3**	314,502	286,754
Total current assets		**490,816**	**471,605**
Total assets		**7,727,645**	**7,738,260**
Equity and liabilities			
Share capital	**7**	970,218	970,218
Share premium		5,498,009	5,498,009
Other reserves		1,343,566	1,366,172
Accumulated losses		(2,468,774)	(2,562,988)
Total equity		**5,343,019**	**5,271,411**
Non-current liabilities			
Borrowings	**10**	972,835	1,253,014
Provisions	**11**	397,124	386,152
Other payables		65,350	62,771
Deferred tax liabilities		300,312	270,836
Total non-current liabilities		**1,735,621**	**1,972,773**
Current liabilities			
Borrowings	**10**	439,127	309,172
Finance lease liability		806	1,666
Other taxes payable		112,384	89,381
Trade and other payables		96,688	93,857
Total current liabilities		**649,005**	**494,076**
Total liabilities		**2,384,626**	**2,466,849**
Total equity and liabilities		**7,727,645**	**7,738,260**

The accompanying notes on pages 14-30 are an integral part of these interim condensed consolidated financial statements.

Zoltav Resources Inc.

Interim condensed consolidated statement of cash flows

for the six months ended 30 June 2018

(in '000s of Russian rubles, unless otherwise stated)

	Note	Six months ended 30 June 2018 (unaudited)	Six months ended 30 June 2017 (unaudited)
Cash flows from operating activities			
Profit before tax		**101,091**	**99,038**
Adjustments for:			
Depreciation and depletion	**6**	222,593	218,620
Impairment of exploration and evaluation assets	**5**	6,482	–
Finance costs		92,740	116,549
Finance income		(9,303)	(13,674)
Loss on disposal of property, plant and equipment, net of income from sale of property, plant and equipment		237	19,202
Expected credit loss		4,721	–
Change in the estimates of decommissioning and environmental restoration provision		(1,931)	445
Other income and expenses		(1,236)	3,306
Operating cash inflows before working capital changes		**415,394**	**443,486**
(Increase)/decrease in inventories		(9,040)	7,619
Change in trade and other receivables and other current non-financial assets		14,052	16,771
Decrease in trade and other payables		359	(17,614)
Increase in other taxes payables		23,003	3,574
Net cash from operating activities before tax and interests paid		**443,768**	**453,836**
Interest received		8,984	14,254
Interest paid	**10**	(75,408)	(98,442)
Income tax paid		(7)	(46)
Net cash flows from operating activities		**377,337**	**369,602**
Cash flows from investing activities			
Proceeds from sale of property, plant and equipment		2,257	5,830
Capital expenditure on exploration and evaluation activities		(144,265)	(8,317)
Purchase of property, plant and equipment		(57,855)	(163,700)
Net cash used in investing activities		**(199,863)**	**(166,187)**
Cash flows from financing activities			
Repayment of obligations under finance leases		(173)	–
Repayment of borrowings	**10**	(150,000)	(150,000)
Net cash used in financing activities		**(150,173)**	**(150,000)**
Net change in cash and cash equivalents		**27,301**	**53,415**
Net foreign exchange difference		447	99
Cash and cash equivalents at the beginning of the period		286,754	294,254
Cash and cash equivalents at the end of the period		**314,502**	**347,768**

The accompanying notes on pages 14-30 are an integral part of these interim condensed consolidated financial statements.

Interim condensed consolidated statement of changes in equity

for the six months ended 30 June 2018

(in '000s of Russian rubles, unless otherwise stated)

		Attributable to owners of the Parent					
	Note	**Share capital**	**Share premium**	**Capital reserve**	**Employee share-based compen-sation reserve**	**Accumulated losses**	**Total equity**
At 1 January 2017		**970,218**	**5,498,009**	**1,343,566**	**85,775**	**(1,356,179)**	**6,541,389**
Profit for the period		–	–	–	–	68,995	68,995
Total comprehensive income		**–**	**–**	**–**	**–**	**68,995**	**68,995**
At 30 June 2017 (unaudited)		**970,218**	**5,498,009**	**1,343,566**	**85,775**	**(1,287,184)**	**6,610,384**
At 1 January 2018		**970,218**	**5,498,009**	**1,343,566**	**22,606**	**(2,562,988)**	**5,271,411**
Employee share-based compensation	9	–	–	–	(22,606)	22,606	**–**
Transactions with owners		**–**	**–**	**–**	**(22,606)**	**22,606**	**–**
Profit for the period		–	–	–	–	71,608	71,608
Total comprehensive income		**–**	**–**	**–**	**–**	**71,608**	**71,608**
At 30 June 2018 (unaudited)		**970,218**	**5,498,009**	**1,343,566**	**–**	**(2,468,774)**	**5,343,019**

(in '000s of Russian rubles, unless otherwise stated)

1. Background

1.1 The Company and its operations

Zoltav Group (the Group) comprises Zoltav Resources Inc. (the Company), together with its subsidiaries:

Name	**Place of incorporation**	**Function**	**Share of the Group in a subsidiary as of 30 June 2018 and 31 December 2017**
CenGeo Holdings Limited (hereinafter "CenGeo Holdings")	Cyprus	Holding company	100%
CJSC SibGeCo (hereinafter "SibGeCo")	Russia	Operating company	100%
Royal Atlantic Energy (Cyprus) Limited (hereinafter "Royal")	Cyprus	Holding company	100%
Diall Alliance LLC (hereinafter "Diall")	Russia	Operating company	100%
Zoltav Resource LLC	Russia	Management company	100%

The Company was incorporated in the Cayman Islands on 18 November 2003. The principal activities of the Company and its subsidiaries is the acquisition, exploration, development and production of hydrocarbons in the Russian Federation. The Company's shares are listed on the Alternative Investment Market of the London Stock Exchange.

1.2 Russian business environment

The Group's operations are primarily located in the Russian Federation.

The Russian Federation displays certain characteristics of an emerging market. Its economy is particularly sensitive to oil and gas prices. The legal, tax and regulatory frameworks continue to develop and are subject to frequent changes and varying interpretations. The economy is negatively impacted by oil price fluctuations, ongoing political tension in the region and international sanctions against certain Russian companies and individuals. The financial markets continue to be volatile.

The combination of the above resulted in reduced access to capital, a higher cost of capital and uncertainty regarding economic growth, which could negatively affect the Group's future financial position, results of operations and business prospects. Management believes it is taking appropriate measures to support the sustainability of the Group's business in the current circumstances.

2. Significant accounting policies

2.1 Basis of preparation

These interim condensed consolidated financial statements have been prepared in accordance with International Accounting Standard ("IAS") 34 "Interim Financial Reporting", as adopted by the European Union. Accordingly, these interim condensed consolidated financial statements do not include all the information and disclosures required for a complete set of financial statements, and should be read in conjunction with the Group's annual consolidated financial statements for the year ended 31 December 2017, which were prepared in accordance with International Financial Reporting Standards, as adopted by the European Union.

Operating results for the six-month period ended 30 June 2018 are not necessarily indicative of the results that may be expected for the year ending 31 December 2018.

(in ‘000s of Russian rubles, unless otherwise stated)

2.2 Going concern

The consolidated financial statements have been prepared on a going concern basis as the Directors have concluded that the Group will continue to have access to sufficient funds in order to meet its obligations as they fall due for at least the foreseeable future as explained further in the Directors Report. The Group’s current liabilities exceed current assets by 158,189 as at 30 June 2018. For mitigation factors, please, see Note 12.1.

2.3 Disclosure of impact of new and future accounting standards

a) Adoption of new and amended standards

In the preparation of these consolidated financial statements, the Group followed the same accounting policies and methods of computation as compared with those applied previously, except for the adoption of new standards and interpretations and revision of the existing standards as of 1 January 2018. The Group has not early adopted any other standard, interpretation or amendment that has been issued but is not yet effective.

New/revised standards and Interpretations adopted as of 1 January 2018	**Effective for annual periods beginning on or after**
Amendments to IAS 40 – *Transfers of Investment Property*	1 January 2018
Amendments to IFRS 4 – Applying IFRS 9 *Financial Instruments* with IFRS 4 *Insurance Contracts*	1 January 2018
Annual improvements to IFRSs 2014-2016 cycle	1 January 2018
IFRS 9 *Financial Instruments*	1 January 2018
IFRS 15 *Revenue from Contracts with Customers*	1 January 2018
Clarification to IFRS 15 *Revenue from Contracts with Customers*	1 January 2018
IFRIC 22 *Foreign Currency Transactions and Advance Consideration*	1 January 2018
Amendments to IFRS 2 – *Classification and Measurement of Share-based Payment Transactions*	1 January 2018

IFRS 9 Financial Instruments: Classification and Measurement

a) Classification

Loans as well as trade receivables are held to collect contractual cash flows and are expected to give rise to cash flows representing solely payments of principal and interest. The Group analysed the contractual cash flow characteristics of those instruments and concluded that they meet the criteria for amortised cost measurement under IFRS 9. Therefore, reclassification for these instruments is not required.

b) Impairment

IFRS 9 requires the Group to now use an expected credit loss model for its trade receivables measured at amortised cost and cash in banks, either on a 12-month or lifetime basis. The Group expects to apply the simplified approach and record lifetime expected losses on all trade receivables measured at amortised cost. Given the short-term nature of these assets, these changes had no significant impact.

IFRS 15 Revenue from Contracts with Customers

(in '000s of Russian rubles, unless otherwise stated)

IFRS 15 was issued in May 2014 and establishes a new five-step model that will apply to revenue arising from contracts with customers. Under IFRS 15 revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer.

The principles in IFRS 15 provide a more structured approach to measuring and recognising revenue. The new revenue standard is applicable to all entities and will supersede all current revenue recognition requirements under IFRS. Either a full or modified retrospective application is required for annual periods beginning on or after 1 January 2018 with early adoption permitted. Given the basic terms of revenue contracts, reliable customers and absence of significant finance component in sales, the Group assessed that the impact of IFRS 15 was not significant.

Other new standards and amendments applied for the first time in 2018 did not have a significant impact on the consolidated financial statements of the Group.

b) New accounting pronouncements

A number of new and amended standards were not effective as of 30 June 2018 and have not been applied in these consolidated financial statements.

Standards issued but not yet effective in the European Union	**Effective for annual periods beginning on or after**
IFRS 16 *Leases*	1 January 2019
Amendments to IFRS 9: *Prepayment Features with Negative Compensation*	1 January 2019
Annual improvements to IFRSs 2015-2017 cycle	1 January 2019*
IFRS 17 *Insurance Contracts*	1 January 2021*
IFRIC 23 *Uncertainty over Income Tax Treatments*	1 January 2019*
Amendments to IAS 28: *Long-term Interests in Associates and Joint Ventures*	1 January 2019*
Amendments to IAS 19: *Plan Amendment, Curtailment or Settlement*	1 January 2019*
Amendments to References to the Conceptual Framework in IFRS Standards	1 January 2020*

* Subject to EU endorsement.

IFRS 16 Leases

IFRS 16 was issued in January 2016 and it replaces IAS 17 *Leases*, IFRIC 4 *Determining whether an Arrangement contains a Lease*, SIC-15 *Operating Leases – Incentives* and SIC-27 *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to account for all leases under a single on-balance sheet model similar to the accounting for finance leases under IAS 17.

IFRS 16 is effective for annual periods beginning on or after 1 January 2019. Early application is permitted, but not before an entity applies IFRS 15. A lessee can choose to apply the standard using either a full retrospective or a modified retrospective approach. The standard's transition provisions permit certain reliefs.

In 2018, the Group will continue to assess the potential effect of IFRS 16 on its financial statements.

From application of the other standards issued but not yet effective the Group expects no effect on its consolidated financial statements.

2.4 Segment reporting

The management of the Company analyses the segment information based on IFRS numbers. As of 30 June 2018 the Company has one segment – revenue from gas and oil products sales - which generates all of its revenues. The segment has all of its assets located in the Russian Federation. Management has therefore determined that the operations of the Group comprise one operating segment and the Group operates in only one geographic area – the Russian Federation. Segment financial indicators are considered based on EBITDA and net profit results. During the first six months of 2018 the Company generated 80.4% of its revenue from Gazprom Mezhregiongaz Saratov LLC (2017: 85.4%).

2.5 Foreign currency translation

a) Functional and presentation currency

The functional currency of the Group entities is the Russian ruble ("RUB"), the currency of the primary economic environment in which the Group operates.

The presentation currency is RUB, which the Board considers more representative for users of these consolidated financial statements to better assess the performance of the Group.

b) Transactions and balances

Transactions in foreign currencies are initially recorded by the Group's entities at their respective functional currency spot rates at the date the transaction first qualifies for recognition.

Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency spot rates of exchange at the reporting date.

Differences arising on the settlement or translation of monetary items are recognised in profit or loss.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions.

(in '000s of Russian rubles, unless otherwise stated)

2. Significant accounting policies (continued)

c) Group companies

Loans between Group entities and related foreign exchange gains or losses are eliminated upon consolidation.

Any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities on the acquisition are treated as assets and liabilities of foreign operation and translated at the spot rate of exchange at the reporting date.

The period-end exchange rates and the average exchange rates for the respective reporting periods are indicated below.

	30 June 2018	31 December 2017
RUB/USD as at reporting date	62.7565	57.6002
	2018	**2017**
RUB/USD average for the six months ended 30 June	59.3536	57.9862

2.6 Assets and liabilities not measured at fair value but for which fair value is disclosed

Fair values analysed by level in the fair value hierarchy of assets and liabilities of the Group not measured at fair value are as follows:

	30 June 2018		31 December 2017	
	Fair value (unaudited)	Carrying value (unaudited)	Fair value	Carrying value
Financial assets				
Trade and other receivables	131,601	131,601	152,574	152,574
Total assets	**131,601**	**131,601**	**152,574**	**152,574**
Financial liabilities				
Borrowings	1,444,252	1,411,962	1,614,108	1,562,186
Trade and other payables	96,688	96,688	93,857	93,857
Obligation under finance leasing	806	806	1,666	1,666
Other non-current payables	65,455	65,350	63,328	62,771
Total liabilities	**1,607,201**	**1,574,806**	**1,772,959**	**1,720,480**

The fair value of borrowings and other non-current payables is based on cash flows discounted using a market rate of 8.62% (2016: 9.34%). The fair values of borrowings and other non-current payables are within level 2 of the fair value hierarchy. The fair value of trade and other receivables is within level 3 hierarchy.

3. Revenue

(in '000s of Russian rubles, unless otherwise stated)

The Group's operations comprise one class of business being oil and gas exploration, development and production and all revenues are from one geographic region, the Saratov Region in the Russian Federation. Companies incorporated outside of Russia provide support to the operations in Russia. The Group has concluded that revenue should be recognised at the point in time when control of the asset is transferred to the customer.

Revenue is primarily from the sale of three products:

	Six months ended 30 June	
	2018 (unaudited)	**2017 (unaudited)**
Gas sales	667,498	784,255
Oil sales	85,184	66,275
Condensate sales	73,695	72,116
Sulphur sales	4,197	1,804
Total sales	**830,574**	**924,450**

All gas sales are made to one customer, Gazprom Mezhregiongaz Saratov LLC, under a long-term contract effective until 31 December 2020 with terms reviewed annually. Condensate and oil are sold to local buyers. The sales of all products are denominated in RUB.

4. Income Tax

The Group calculates the period income tax expense using the tax rate that would be applicable to the expected total annual earnings. The major components of income tax expense in the interim condensed consolidated statement of comprehensive income are:

	Six months ended 30 June	
	2018 (unaudited)	**2017 (unaudited)**
Deferred tax expense	29,476	29,997
Current tax expense	7	46
Total	**29,483**	**30,043**

Origination and reversal of temporary differences in the period mainly relates to the property, plant and equipment, exploration and evaluation assets and provisions.

Reconciliation between expected and actual taxation charge is provided below.

	Six months ended 30 June	
	2018 (unaudited)	**2017 (unaudited)**
Profit before income tax	**101,091**	**99,038**
Theoretical tax charge at applicable income tax rate of 20%	**(20,218)**	**(19,808)**
Effect of different foreign tax rates	(2,511)	(4,545)
Effect of unrecognised tax loss	(3,695)	(4,584)
Tax effect of expenses not deductible for tax purposes	(3,059)	(1,106)

(in '000s of Russian rubles, unless otherwise stated)

Total income tax expense	**(29,483)**	**(30,043)**

The Group's income was subject to tax at the following tax rates:

	Six months ended 30 June 2018	**Six months ended 30 June 2017**
The Russian Federation	20.0%	20.0%
The Republic of Cyprus	12.5%	12.5%
Cayman Islands	0%	0%

The Group is subject to Cayman income tax, otherwise the majority of the Group's operations are located in the Russian Federation. Thus 20% tax rate is used for theoretical tax charge calculations. The effective tax rate changed due to a decrease of expenses of Zoltav Resources Inc., which are subject to 0% tax rate.

(in '000s of Russian rubles, unless otherwise stated)

5. Exploration and evaluation assets

	Sub-soil licences	Exploration and evaluation works capitalised, including seismic works	Total
Balance at 1 January 2017	**2,188,024**	**2,600,290**	**4,788,314**
Additions	7,298	85,085	**92,383**
Transfer to property, plant and equipment	–	–	**–**
Change in the estimates of decommissioning provision	–	1,785	**1,785**
Balance at 30 June 2017 (unaudited)	**2,195,322**	**2,687,160**	**4,882,482**
Balance at 1 January 2018	**1,037,728**	**2,221,625**	**3,259,353**
Additions	7,484	150,743	**158,227**
Transfer from property, plant and equipment	–	–	**–**
Change in the estimates of decommissioning provision	–	(1,416)	**(1,416)**
Impairment	(7,593)	1,111	**(6,482)**
Balance at 30 June 2018 (unaudited)	**1,037,619**	**2,372,063**	**3,409,682**

The additions during the first six months of 2018 and the first six months of 2017 are mostly represented by seismic works on the Mokrousovskoye block.

In management's opinion, as at 30 June 2018 there were no non-compliance issues in respect of the licences that would have an adverse effect on the financial position or the operating results of the Group.

Impairment

In 2017 the Group revised its investment strategy with a primary focus on exploration and further development of the deeper Devonian structures on the Bortovoy Licence. As a result, the forecasted amount of investment in the development of the Koltogor Licences cannot be confirmed. Accordingly, the probability of the development of the Koltogor Licences becomes uncertain. The Group recognised an impairment loss of the total book value of exploration and evaluation assets of the Koltogor Licences as of 31 December 2017. As of 30 June 2018 no changes in the Group's plans regarding the Bortovoy Licence occurred. Additions made in 2018 related to the Koltogor Licences (licence payments) were impaired.

(in '000s of Russian rubles, unless otherwise stated)

6. Property, plant and equipment

	Oil and gas assets	Motor vehicles	Other equipment and furniture	Construction work in progress	Total
Cost at 1 January 2017	**4,825,462**	**17,245**	**7,955**	**249,924**	**5,100,586**
Additions	9,162	3,742	82	112,677	**125,663**
Reclassification	260,404	-	-	(260,404)	**-**
Transfer from exploration and evaluation assets	-	-	-	-	**-**
Transfer to inventory	(947)	-	-	(2,591)	**(3,538)**
Change in the estimates of decommissioning provision	2,261	-	-	15	**2,276**
Disposals	(27,963)	(6,616)	-	(6,034)	**(40,613)**
Cost at 30 June 2017 (unaudited)	**5,068,379**	**14,371**	**8,037**	**93,587**	**5,184,374**
Cost at 1 January 2018	**5,202,044**	**18,075**	**7,963**	**68,582**	**5,296,664**
Additions	5,972	773	1,240	47,294	**55,279**
Reclassification	25,893	-	-	(25,893)	**-**
Transfer from exploration and evaluation assets	-	-	-	-	**-**
Transfer to current assets	-	-	-	(7,572)	**(7,572)**
Change in the estimates of decommissioning provision	(2,775)	-	-	-	**(2,775)**
Disposals	(4,941)	(3,301)	-	(22)	**(8,264)**
Cost at 30 June 2018 (unaudited)	**5,226,193**	**15,547**	**9,203**	**82,389**	**5,333,332**
Accumulated depreciation and impairment					
Balance at 1 January 2017	**(868,540)**	**(16,116)**	**(4,676)**	**-**	**(889,332)**
Depreciation and depletion	(215,534)	(2,809)	(277)	-	(218,620)
Disposals	9,878	5,703	-	-	15,581
Balance at 30 June 2017 (unaudited)	**(1,074,196)**	**(13,222)**	**(4,953)**	**-**	**(1,092,371)**
Balance at 1 January 2018	**(1,268,777)**	**(15,488)**	**(5,097)**	**-**	**(1,289,362)**
Depreciation and depletion	(221,066)	(1,307)	(220)	-	(222,593)
Disposals	2,469	3,301	-	-	5,770
Balance at 30 June 2018 (unaudited)	**(1,487,374)**	**(13,494)**	**(5,317)**	**-**	**(1,506,185)**
Net book value at 1 January 2017	**3,956,922**	**1,129**	**3,279**	**249,924**	**4,211,254**
Net book value at 30 June 2017 (unaudited)	**3,994,183**	**1,149**	**3,084**	**93,587**	**4,092,003**
Net book value at 1 January 2018	**3,933,267**	**2,587**	**2,866**	**68,582**	**4,007,302**
Net book value at 30 June 2018 (unaudited)	**3,738,819**	**2,053**	**3,886**	**82,389**	**3,827,147**

7. Share capital

At 30 June 2018, 31 December 2017	**Number of ordinary shares**	**Nominal value, USD'000**	**Nominal value, RUB'000**
Authorised (par value of USD 0.20 each)	250,000,000	50,000	1,708,672
Issued and fully paid (par value of USD 0.20 each)	141,955,386	28,391	970,218

(in '000s of Russian rubles, unless otherwise stated)

8. Earnings per share

Basic earnings per share is calculated by dividing the profit attributable to owners of the Company by the weighted average number of ordinary shares in issue during the year.

Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. The Company has share options and warrants as dilutive potential ordinary shares.

	Six months ended 30 June	
	2018 (unaudited)	**2017 (unaudited)**
Profit attributable to owners of the Company − Basic and diluted	71,608	68,995
	Number of shares	**Number of shares**
Weighted average number of shares for calculating basic earnings per share	141,955,386	141,955,386
Effect of dilutive potential ordinary shares − share options	12,375	1,952,500
Weighted average number of shares for calculating diluted earnings per share	141,967,761	143,907,886
	RUB (unaudited)	**RUB (unaudited)**
Basic earnings per share	0.50	0.49
Diluted earnings per share	0.50	0.48

9. Share-based payments

At 30 June 2018, the Company had no outstanding share options (31 December 2017: 202,500), as initial share options amounting to 22,606 expired on 11 January 2018.

Options which are lapsed or cancelled prior to their exercise date are deleted from the register of outstanding options.

10. Borrowings

	2018	**2017**
Non-revolving credit facility − current liability, as at 1 January	**1,562,186**	**1,859,949**
Including current liability	309,172	311,160
Interest accrued	75,184	99,244
Interest paid	(75,408)	(98,442)
Repayment	(150,000)	(150,000)
Non-revolving credit facility, as at 30 June (unaudited)	**1,411,962**	**1,710,751**
Including current liability	439,127	309,774

(in '000s of Russian rubles, unless otherwise stated)

10. Borrowings (continued)

In 2014, the Group entered into a non-revolving credit facility agreement with Sberbank of Russia OJSC with a maximum facility amount of 2,400,000. The contractual currency is RUB. The facility was drawn down in full in 2014. The maturity date is 30 April 2021, being the 7-year anniversary of the facility entered into. The Group is obliged to repay the principal amount of the loan in 24 tranches commencing on 11 May 2015 and on a quarterly basis from then on with a final repayment tranche payable on the maturity date. The interest rate is fixed and contracted as 10.98% per annum. In October 2017 the Group concluded an additional agreement, where the interest rate was resettled as 10.73% per annum. In February 2018 the Group concluded an additional agreement, where the interest rate was resettled as 9.71% per annum. Sberbank may unilaterally amend the interest rate in the event of increases in the refinancing rate of the Central Bank of Russia. The Group paid an upfront commission on the facility of 1% of the facility amount (24,000) and there is a drawdown charge of 0.25% per year on the balance of the facility not drawn by the Group within the established timeframe. The Group has the option to prepay the loan in whole or in part at any time, subject to the payment of a fee. The Group provided certain warranties and representations to Sberbank in the agreement. The agreement contains certain loan covenants and events of default which are customary for a facility of this type. The Group was in compliance with all covenants as of 30 June 2018 and 31 December 2017. The loan is secured by the Group, such security being granted pursuant to various pledge and mortgage deeds entered into by the Group on or about the date of the Sberbank Facility. The carrying value of property, plant and equipment pledged as of 30 June 2018 amounted to 2,673,497 (31 December 2017: 2,775,473).

The outstanding principal amount of the facility as of 30 June 2018 was 1,410,000 (31 December 2017: 1,560,000). The credit facility debt is measured at amortised cost, using the effective interest method.

Additionally the Group entered into a 100,000 revolving loan facility on 13 December 2017. The interest is 10.5% for disbursed amounts and 0.5% for the remaining part of the limit. The maturity date is 12 December 2018. There were no drawings during the six months ended 30 June 2018.

11. Decommissioning and environmental restoration provision

The decommissioning and environmental restoration provision represents the net present value of the estimated future obligations for abandonment and site restoration costs which are expected to be incurred at the end of the production lives of the gas and oil fields which is estimated to be within 20 years.

	2018	**2017**
Provision as at 1 January	**386,152**	**359,153**
Additions	2,538	-
Unwinding of discount	14,556	14,927
Change in estimate of decommissioning and environmental restoration provision	(6,122)	4,506
Provision as at 30 June (unaudited)	**397,124**	**378,586**

This provision has been created based on the Group's internal estimates. Assumptions based on the current economic environment have been made which the directors believe are a reasonable basis upon which to estimate the future liability. These estimates are reviewed regularly to take into account any material changes to the assumptions. However, actual decommissioning costs will ultimately depend upon future market prices for the necessary dismantlement works required, which will reflect market conditions at the relevant time. Furthermore, the timing is likely to depend on when the fields cease to produce at economically viable rates. This in turn will depend upon future oil prices and future operating costs, which are inherently uncertain.

The provision reflects two liabilities: one is to dismantle the property, plant and equipment assets and the other is to restore the environment. The decommissioning part of the provision is reversed when an oil well is abandoned and corresponding capitalised costs are expensed. The environmental part of the provision is reversed when the expenses on restoration are actually incurred.

The provision is reversed when the corresponding capitalised costs directly attributable to an exploration and evaluation asset are expensed as it is determined that a commercial discovery has not been achieved and the restoration of the corresponding environment has been completed.

The Group reviews the application of inflation rates used for the provision estimation each half-year end. The inflation rate used in the estimation of the provision as of 30 June 2018 was 4% in 2018, decreasing to 3.64% in 2036 (as of 31 December 2017: 3.77% in 2017, decreasing to 3.64% in 2036). The discount rates used to determine the decommissioning and environmental restoration provision are based on Russian government bond rates. As of 30 June 2018 discount rate varies from 7.74% to 7.79% (as of 31 December 2017: from 7.62% to 7.79%) depending on expected period of abandonment and site restoration for each gas and oil fields.

12. Financial instruments and financial risk management

The Group has exposure to the following risks from its use of financial instruments:

- Liquidity risk;
- Market risk;
- Credit risk.

This note presents information about the Group’s exposure to each of the above risks, the Group’s objectives, policies and processes for measuring and managing risk, and the Group’s management of capital. Further quantitative disclosures are included throughout this consolidated financial statements.

The Group’s risk management policies deal with identifying and analysing the risks faced by the Group, setting appropriate risk limits and controls, and monitoring risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group’s activities. The Group, through its internal policies, aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

12.1 Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group monitors the risk of cash shortfalls by means of current liquidity planning. The Group’s approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group’s reputation. This approach is used to analyse payment dates associated with financial assets, and also to forecast cash flows from operating activities. The contractual maturities of financial liabilities are presented including estimated interest payments.

(in '000s of Russian rubles, unless otherwise stated)

The Group's current liabilities exceed current assets by 158,189 as at 30 June 2018. The Group plans to cover liquidity gap by cash inflows from operating activity in 2018. For additional liquidity risk mitigation as of 30 June 2018 the Group has unused borrowing facility in the amount of 100,000.With all the above the Group management considers the liquidity risk as low.

The table below summarises the maturity profile of the Group's financial liabilities based on contractual undiscounted payments:

	Contractual amount	**Less than 1 year**	**1-3 years**	**Over 3 years**
Financial liabilities as at 30 June 2018 (unaudited)				
Borrowings	1,619,638	552,952	1,066,686	–
Trade and other payables	178,377	96,688	81,689	–
Obligations under finance lease	806	806	–	–
Total	**1,798,821**	**650,446**	**1,148,375**	–

	Contractual amount	**Less than 1 year**	**1-3 years**	**Over 3 years**
Financial liabilities as at 31 December 2017				
Borrowings	1,871,795	452,638	1,282,464	136,693
Trade and other payables	175,546	93,857	–	81,689
Obligations under finance lease	1,666	1,666	–	–
Total	**2,049,007**	**548,161**	**1,282,464**	**218,382**

12. Financial risk management (continued)

12.2 Market risk

Market risk includes interest risk and foreign currency exchange rate risk.

a) Interest risk

The Group has exposure to interest risk since the Group’s subsidiary, Diall Alliance LLC, entered into a non-revolving credit facility agreement with Sberbank and, according to the terms of the agreement, Sberbank may unilaterally amend the interest rate in the event of increases in refinancing rates of the Central Bank of Russia. While Sberbank actually decreased the interest rate to 9.71% from 10.73% on 16 February 2018.

b) Foreign currency exchange rate risk

The Group does not have any significant exposure to foreign currency risk, as no significant sales, purchases or borrowings are denominated in a currency other than the functional currency.

The Group’s operations are carried in the Russian Federation, where all of its revenue, costs and financing from both Sberbank and intra-group lending are denominated in RUB. As a result there is no exposure at the operating subsidiary level to foreign currency exchange risk movements.

12.3 Credit risk

Credit risk arises principally from the Group’s financial investments, trade and other receivables and cash and cash equivalents. It is the risk that the value of the Group’s investments will not be recovered and the risk that the counterparty fails to discharge its obligation in respect of the Group’s trade and other receivables and cash balances. The maximum exposure to credit risk equals the carrying value of these items in the financial statements.

The Group is largely dependent on one customer (Gazprom Mezhregiongaz Saratov LLC) for a significant portion of revenues. Gazprom Mezhregiongaz Saratov LLC accounted for 80.4% and 84.8%, of the Group’s total revenue during the first six months of 2018 and 2017, respectively. The loss or the insolvency of this customer for any reason, or reduced sales of the Group’s principal product, could significantly reduce the Group’s ongoing revenue and/or profitability, and could materially and adversely affect the Group’s financial condition. The credit rating assigned to Gazprom by Standard & Poor’s is BBB-. To manage credit risk and exposure to the loss of the key customer, the Group has entered into a long-term contract with Gazprom Mezhregiongaz Saratov LLC, effective through 31 December 2020. As for the smaller customers, the Group imposes minimum credit standards that the customers must meet before and during the sales transaction process.

Credit risk related to cash and cash equivalents is reduced by placing funds with banks with acceptable credit ratings.

(in ‘000s of Russian rubles, unless otherwise stated)

To limit exposure to credit risk on cash and cash equivalents management’s policy is to hold cash and cash equivalents in reputable financial institutions. During the first six months of 2018 cash was held mainly with Sberbank and Bank Rossiysky Capital.

To limit exposure to credit risk on cash and cash equivalents management’s policy is to hold cash and cash equivalents in reputable financial institutions.

	30 June 2018 (unaudited)	**31 December 2017**
ruBBB-, Expert RA	216,000	115,000
Ba2.ru, Moody’s	89,595	163,328
Ba1.ru, Moody’s	168	-
Ba3.ru, Moody’s	-	105
Other	8,739	8,321
Total cash and cash equivalents	**314,502**	**286,754**

12.4 Capital management

The Group considers its capital and reserves attributable to equity shareholders to be the Group’s capital. In managing its capital, the Group’s primary long-term objective is to provide a return for its equity shareholders through capital growth. Going forward, the Group may seek additional investment funds and also maintain a gearing ratio that balances risks and returns at an acceptable level, while maintaining a sufficient funding base to enable the Group to meet its working capital needs. Details of the Group’s capital are disclosed in the interim statement of changes in equity.

There have been no significant changes to management’s objectives, policies or processes in the period, nor has there been any change in what the Group considers to be capital.

The Group companies are in compliance with externally imposed capital requirements as of 30 June 2018 and 31 December 2017.

13. Commitments and contingencies

13.1 Capital commitments

Capital expenditure contracted for at the end of the reporting period but not yet incurred at 30 June 2018 was 48,420, net of VAT (31 December 2017: 483,042, net of VAT).

13.2 Insurance

The insurance industry in the Russian Federation is in a developing state and many forms of insurance protection common in other parts of the world are not generally available. The Group’s insurance currently includes cover for damage to or loss of assets, third-party liability coverage (including employer’s liability insurance), in each case subject to excesses, exclusions and limitations. However, there can be no assurance that such insurance will be adequate to cover losses or exposure to liability, or that the Group will continue to be able to obtain insurance to cover such risks. Until the Group obtains adequate insurance coverage there is a risk that the loss or destruction of certain assets could have a material adverse effect on the Group's operations and financial position.

13. Commitments and contingencies (continued)

13.3 Litigation

The Group has been involved in a number of court proceedings (both as a plaintiff and as a defendant) arising in the normal course of business. In the opinion of management there are no current legal proceedings or other claims outstanding which could have a material adverse effect on the results of operations, financial position or cash flows of the Group and which have not been accrued or disclosed in these financial statements.

No provision for litigations was accrued as at 31 December 2017 or 30 June 2018.

13.4 Taxation contingencies

Russian tax, currency and customs law allows for various interpretations and is subject to frequent changes. Management's interpretation of legislation as applied to the Company's transactions and activities may be challenged by regional or federal authorities.

The Group operates in a number of foreign jurisdictions besides Russian Federation. The Group includes companies established outside the Russian Federation that are subject to taxation at rates and in accordance with the laws of jurisdictions in which the companies of the Group are recognised as tax residents. Tax liabilities of foreign companies of the Group are determined on the basis that foreign companies of the Group are not tax residents of the Russian Federation, nor do they have a permanent representative office in the Russian Federation and are therefore not subject to income tax under Russian law, except for income tax deductions at the source.

In 2018, there was further implementation of mechanisms aimed at avoiding tax evasion using low-tax jurisdictions and aggressive tax planning structures. In particular, these changes included the definition of the concept of beneficial ownership, the tax residence of legal entities at the place of actual activities, as well as the approach to taxation of controlled foreign companies in the Russian Federation.

In addition, the concept of tax benefits for all taxes levied on the territory of the Russian Federation was legislatively established, with a focus on the presence of a business objective in the conduct of business operations, as well as confirmation of the fulfilment of obligations under the agreements concluded by the parties to the contract, or by the person to whom these obligations were transferred under a contract or law. This adjustment significantly changes the concept of recognising the fact that taxpayers receive unreasonable tax benefits, which will have a significant impact on the prevailing judicial practice. At the same time, the practical mechanism for applying this rule has not yet been fully resolved, and judicial practice on the changes introduced is not formed.

These changes and recent trends in applying and interpreting certain provisions of Russian tax law indicate that the tax authorities may take a tougher stance in interpreting legislation and reviewing tax returns. The tax authorities may thus challenge transactions and accounting methods that they have never challenged before. As a result, significant taxes, penalties and fines may be accrued. It is not possible to determine the amounts of constructive claims or evaluate the probability of a negative outcome. Tax audits may cover a period of three calendar years immediately preceding the audited year. Under certain circumstances, the tax authorities may review earlier tax periods.

These circumstances may create tax risks in the Russian Federation that are substantially more significant than in other countries. Management believes that it has provided adequately for tax liabilities based on its interpretations of applicable Russian tax legislation, official pronouncements and court decisions. However, the interpretations of the relevant authorities could differ and the impact on these consolidated financial statements if the authorities were successful in enforcing their interpretations could be significant.

13.5 Environmental matters

The Group's operations are in the upstream oil and gas industry in the Russian Federation and its activities may have an impact on the environment. The enforcement of environmental regulations in the Russian Federation is evolving and the enforcement stance of government authorities is continually being reconsidered. The Group periodically evaluates its obligations related thereto. The outcome of environmental liabilities under proposed or future legislation, or as a result of stricter interpretation and enforcement of existing legislation, cannot reasonably be estimated at present, but could be material.

Under the current levels of enforcement of existing legislation, management believes there are no significant liabilities in addition to amounts already accrued as a part of the decommissioning provision and which would have a material adverse effect on the financial position or results of the Group.

14. Related party transactions

During the period there were no operations with related parties, except for key management remunerations.

The remuneration of key management comprised of salary and bonuses in the amount 4,207 (first six months of 2017: 13,585).

15. Events after the reporting date

There were no events after the reporting date that require disclosures in the Group's interim condensed consolidated financial statements.