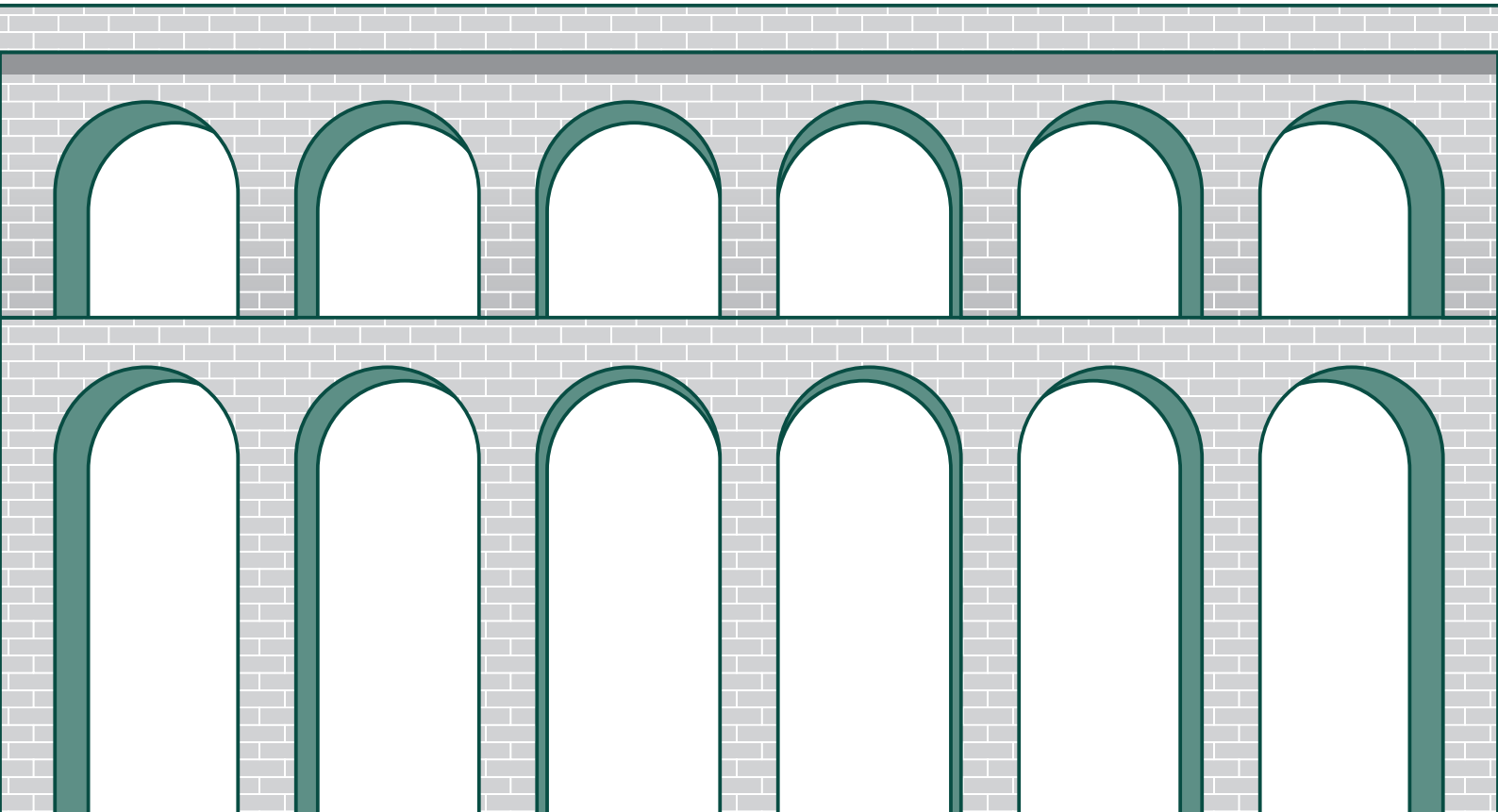
Annual report 2016

Pharmstandard

Bridging interests

Соединяя интересы



Annual report 2016

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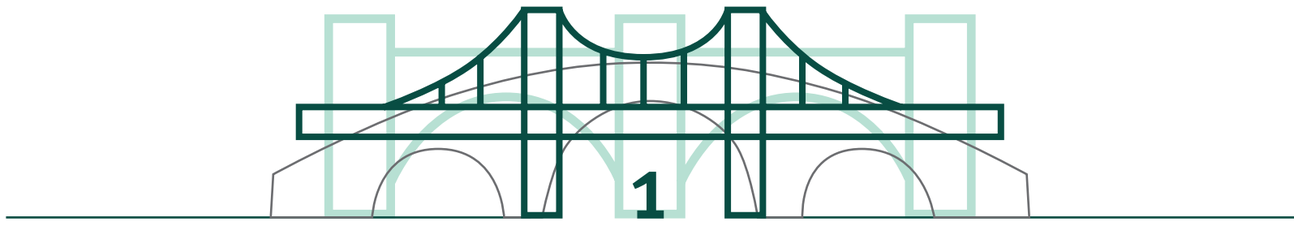


Pharmstandard today

The principal activities of Pharmstandard JSC (Pharmstandard PJSC[1] until 22 May 2017); (hereinafter also JSC "Pharmstandard", Pharmstandard or the Company) and its subsidiaries (hereinafter also Pharmstandard Group or the Group) are production, marketing, promotion and distribution of pharmaceutical products, substances and medical equipment.

1 The name Pharmstandard PJSC will be used in relation to 2016 and earlier period

1.1

CEO statement

Dear colleagues and partners,

Our principal achievement in 2016 is a 30%[2] increase in revenues to RR 62 billion amid rather conservative growth in the wider market (up 8% in monetary terms), which confirms our leadership in the industry.

The strong revenue performance was driven, among other factors, by the import substitution strategy that we have continued to follow by localizing the production of pharmaceuticals in partnership with other companies. While the cost to produce these pharmaceuticals is about twice as high as own brands, we have managed to maintain the group-wide gross margin at the level of 2015 owing to the optimized use of human capital and better capacity utilization. For example, labor productivity per employee has grown more than 30% and has reached RR 9 million and 88 thousand packs, while capacity utilization across the Group has improved by 5% on average[3].

Over the past five years, we have launched the domestic production of 90,pharmaceuticals, including 52 foreign pharmaceuticals. These domestic pharmaceuticals also include VEDs and biological drugs requiring a complex production process. Our strategy has a strong localization focus: unlike two years ago when localization efforts were focused mostly on secondary packaging, we have now established the full-cycle of production[4] of nearly half of the localized pharmaceuticals. The development of partnership with global market leaders also includes distribution of their products in the commercial segment, supplying to regional and Federal state programs on providing the population with medicines, as well as transportation. In 2016, Pharmstandard was finally formed as a company, bridging the interests of various groups, including pharmaceuticals developers, manufacturers, doctors, regulators, patients and customers, as well as offering a comprehensive solution in the pharmaceutical market of Russia: localization of production, procurement of raw materials, quality control, supply, distribution, market access.

However a ramp-up in production cannot be achieved without investment. In 2016 we channeled over RR 2,9 billion in production upgrades and in new equipment and facilities, including the construction of a tablet and lyophilisate production line in Ufa, the development of small-batch manufacturing in Kursk, and the installation of systems and equipment required to conform with GMP standards. We have implemented a GMP-compliant quality management system, which we maintain and constantly improve across all our production entities.

2 Hereinafter the total of absolute and relative terms (if applicable) may differ from 100% due to rounding

3 Excluding recently added production capacity

4 Hereinafter, the full cycle of production refers to the production of finished pharmaceutical product (FPP) without the production of substances.

Pharmstandard became a private company in 2016. In June, Pharmstandard's shareholders received an offer from Augment Investments Limited to acquire their shares. As a result, after purchasing 4,538,675 shares Augment Investments Limited increased its shareholding to 98.12% by 14 September 2016 while three months later it became the holder of 100% in Pharmstandard upon completion of mandatory purchase.

While becoming a private company, we have continued to improve our corporate governance and compliance controls in line with corporate ethics principles. In particular, in 2016 we have improved compliance systems across all entities of Pharmstandard Group and included an anti-corruption clause in all our contracts. We have also revised and approved the new edition of Marketing practice code. We continue preparing the IFRS consolidated financial statements, annual reports and other corporate documents that help our partners gain deeper insight into the Company and better understand our business.

In conclusion, I would like to thank our entire team for their hard work and enthusiasm, as our achievements would not have been possible without our people. At Pharmstandard, we make significant efforts to source and recruit the best talent and form the corporate culture that will help employees to maximize their output and fully realize their potential.

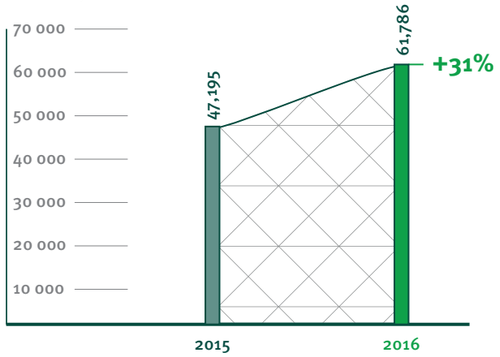
Chief Executive Officer

Pharmstandard JSC

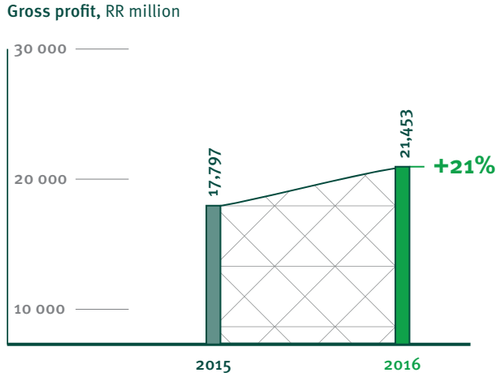
Grigory A. Potapov

1.2 Performance highlights

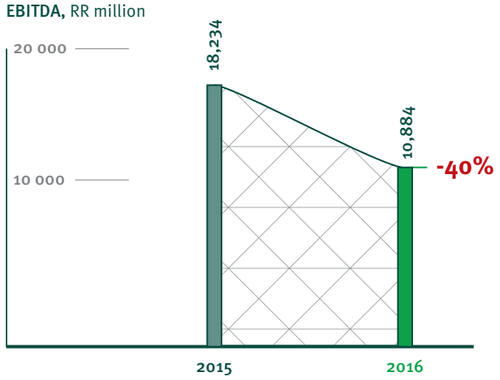
Revenues, RR million



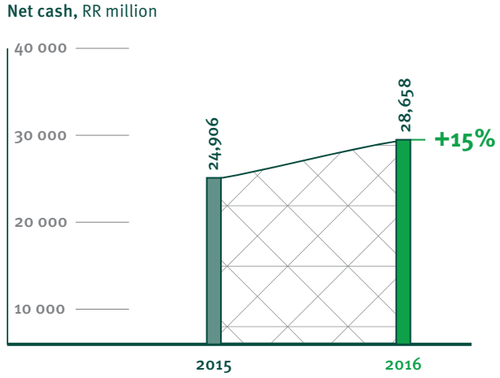
Gross profit, RR million



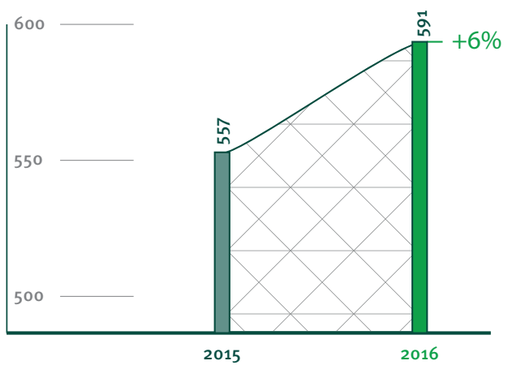
EBITDA, RR million



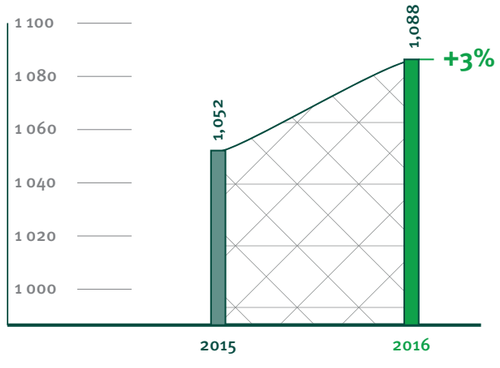
Net cash, RR million



Production, million packs



FPP capacity, million packs



1.3 Milestone events in 2016

January 2016 The Company commenced production of metered-dose aerosols at Pharmstandard-Leksredstva's new production line in Kursk. The production line's output in 2016 included Beklometazone-aeronative, Ipratepol-aeronative, Ipratropium-aeronative, Fenoterol-aeronative and Salbutamol-Pharmstandard.

29 March 2016 Pharmstandard and Japanese pharmaceutical R&D company Eisai signed a cooperation agreement relating to the localization of production of Eisai products at Pharmstandard's facilities in Russia. The agreement relates to Eisai's oncology therapies, Halaven® (eribulin) and Lenvima® (lenvatinib), as well as the its global epilepsy therapy, Fycompa® (perampanel). Under the agreement, important stages in the manufacturing process for both eribulin and lenvatinib will be completed in Ufa, while for perampanel these will be performed in Kursk.

26 May 2016 Pharmstandard International, a wholly-owned subsidiary of Pharmstandard PJSC, acquired a 2.3% interest in Transmedics, the company that develops a portable ex-vivo organ perfusion system for transplantation.

22 June 2016 The Company received a mandatory offer from Augment Investments Limited to acquire 5,250,186 ordinary shares of the Company from other shareholders (as of the offer date, Augment Investments Limited and the Company's affiliate Pharmstandard-Leksredstva jointly owned 86,11% of the Company's ordinary shares).

17 August 2016 Pharmstandard International, a wholly-owned subsidiary of Pharmstandard PJSC, acquired a 9.6% interest in Avelas Biosciences, a developer of diagnostic products for detecting cancer-positive margins. The consideration was paid in two tranches, in August 2016 and March 2017.

16 August 2016 Pharmstandard and Ferring Pharmaceuticals announced the beginning of a strategic partnership to establish fully integrated production of Traktocile (atosiban) and Pabal (carbetocin), the drugs used for the treatment of early labor and prevention of postpartum hemorrhage. High-tech aseptic full-cycle production of injectable medicines will be set up in Ufa at Pharmstandard-UfaVITA's plant in 2016-2018. With the annual output of around 40,000 packs of Traktocile and 15,000 packs of Pabal, the plant is expected to fully satisfy the demand in Russia and the Eurasian Economic Union. The production will be carried out in accordance with national and European requirements of Good Manufacturing Practice (GMP).

14 September 2016 The Company received a notice concerning the results of the mandatory offer from Augment Investments Limited. As a result of the mandatory offer, Augment Investments Limited became the holder of 98.12% in the Company, having acquired 4,538,675 ordinary shares. Following that, Augment Investments Limited announced the Mandatory squeeze-out of the remaining shares.

24 November 2016 Pharmstandard and GE Healthcare announced the beginning of localization of production of contrast medicines at Pharmstandard-UfaVITA's production facilities. The contrast medicines Visipaque® (Iodixanol), Omnipaque® (Iohexol) and Omniscan® (Gadodiamide) are used for the diagnostics of non-infectious pathologies. The localization will be conducted in two stages: packaging and release quality control, followed by the launch of the production of finished pharmaceutical products.

29 November 2016 Pharmstandard PJSC's global depositary receipts were delisted and officially removed from trading.

12 December 2016 The Company announced the completion of the procedure of mandatory squeeze-out, whereby Augment Investments Limited became holder of 100% in the Pharmstandard PJSC (directly and indirectly).

24 March 2017 Shares of Pharmstandard PJSC were removed from the list of securities admitted to trading on Moscow Stock Exchange MICEX-RTS PJSC.

22 May 2017 The new edition of Company's Charter was registered and its name was changed from Pharmstandard PJSC to Pharmstandard JSC.

1.4 Management responsibility statement

Directors are responsible for preparing this Annual Report of Pharmstandard JSC, including consolidated financial statements in accordance with applicable laws and regulations. Each of the Directors indicated in the Section 4 Corporate Governance of this Annual Report 2016 confirms that, to the best of his or her knowledge:

- the Company's IFRS consolidated financial statements give true and fair view of its assets, liabilities, financial position and results;
- the Business Report section of the Annual Report includes a fair review of the Company's business development and performance, its industry position, as well as a description of key risks and uncertainties affecting the Company's business

Chief Executive Officer

Pharmstandard JSC

Grigory A. Potapov

1.5 Company's mission

Development and manufacturing of advanced pharmaceutical products, which meet the healthcare requirements and patients' expectations.

1.6 Company's strategy

The Company's strategy is based on five major principles of development. The Company takes consistent and continuous steps in line with these principles.

PRINCIPLE	STRATEGY PROGRESS IN 2016
Increase share of high-margin drugs and medical equipment in the Company's product portfolio	The share of revenues from high-margin drugs in the Company's pharmaceutical portfolio increased in 2016, driven largely by Combilipen and Phosphogliv, which contributed 35% to the total revenue increase. The growth leader among third-party products was Revlimid, which was also the top selling drug in this segment.
Increase local content in projects delivered jointly with the world's leading pharmaceutical companies	In 2016, over 47% of partners' products were manufactured locally on a fully integrated basis, compared to around 37% a year ago. Over 60% of localized pharmaceuticals produced at Pharmstandard's facilities in 2016 were foreign.
Expand involvement in the national import substitution program	In 2016, the number of foreign partners' pharmaceuticals produced at Pharmstandard's facilities more than doubled from the 2015 level, from 46 to 97.
Develop and introduce new drugs, expand the product range and dosage forms to fully meet the market demand and consumer expectations	In 2016, Pharmstandard companies obtained authorization to produce six own pharmaceuticals. Pharmstandard-Medtechnika expanded its portfolio with a new range of equipment that has no counterparts in the domestic market and may serve as a quality substitute for modern equipment manufactured abroad. The range of the company's import-substitution products has now been fully formed.
Automate production planning to improve process management and cost control	In 2014, the Company launched a business project to implement an automated manufacturing control system based on SAP ERP. Implementation of the integrated management information system based on SAP will enable the Company to perform all operations, providing life-cycle products, as well as the accounting for such transactions into a single information environment that will enhance the handling of all processes, and most importantly - the quality of the products.

2

Russia’s pharmaceutical market review

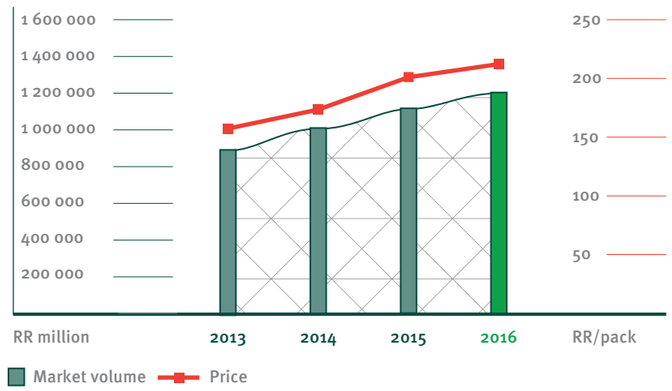
2.1 General information on Russia’s pharmaceutical market[5]

Market review 2016

In 2016, the Russian market of pharmaceuticals and food supplements was worth RR 1,210 billion[6] with a total of 5.7 billion packages produced, up 8% and 2%, respectively, from the previous year.

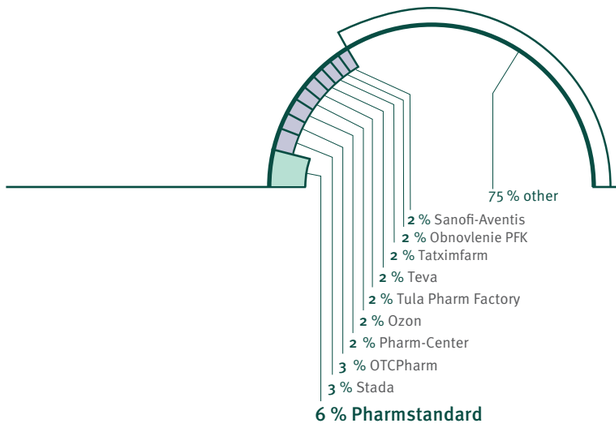
Average price per package soared by 6% YoY to RR 213. Prices of vital and essential drugs (VED) under government price controls rose by 4%, while other drugs increased by 7% in price.

Russian pharmaceutical market dynamics

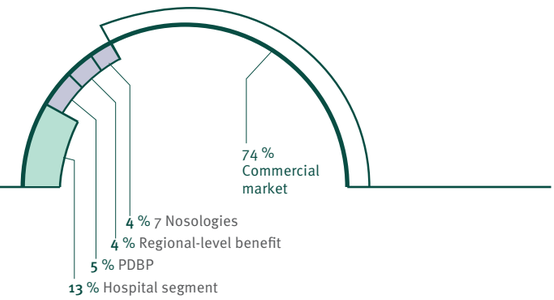


With the market share of 5.9% in 2016, Pharmstandard retained its top position among drug and food supplement manufacturers (in volume terms).

Russian pharmaceutical market structure by company
(in volume terms)



Market structure in 2016,(in value terms)



5 Hereinafter market performance and compare results of JSC “Pharmstandard” market indicators are presented according to IMS Health as of Feb.2017.

6 In consumer prices

Russian pharmaceutical market structure

Russia's pharmaceutical market comprises a commercial market and a government procurement market, covering the following:

- / Hospital segment
- / 7 High-Cost Nosologies Federal Program (7 Nosologies)
- / Public Drug Benefit Program (PDBP)
- / Regional-level drug benefit channel

Commercial market

The commercial market is the dominant segment, comprising 74% of the pharmaceutical market in value terms and 87% in volume terms.

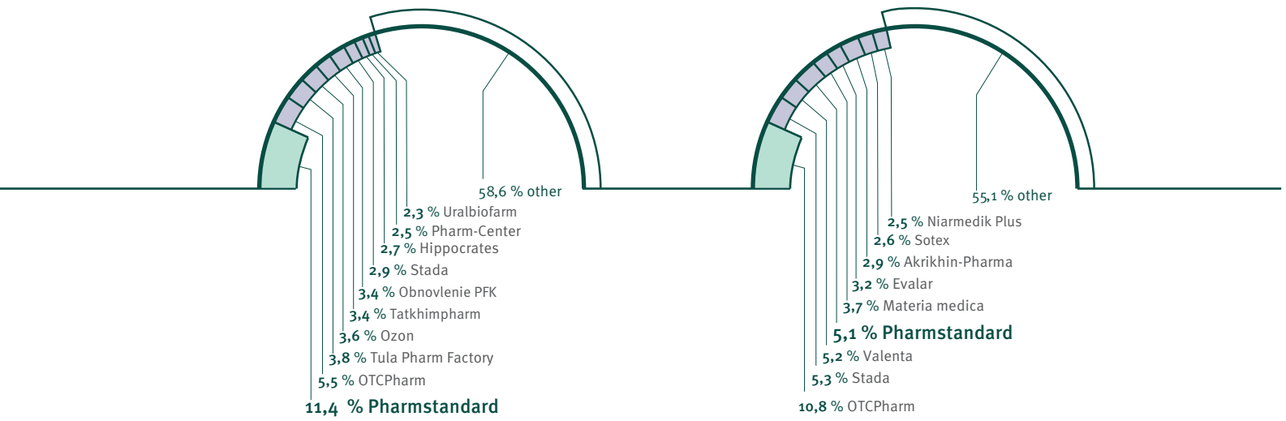
Consumption in the commercial segment increased by 4% (in volume terms), mostly due to increased consumption of prescription products (up 6% from a year ago).

In value terms, the commercial segment grew by 9.7% YoY.

Domestic products contribute 30%, or around RR 268 billion to the value of the commercial segment.

Pharmstandard holds the top place among domestic producers in volume terms (11.4%) and the fourth place in value terms (5.1%).

Commercial market structure by domestic manufacturer
(in volume terms)



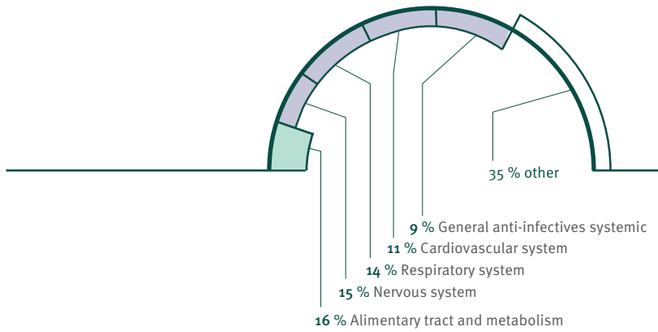
Commercial market structure by domestic manufacturer
(in value terms)

For details on the government procurement market, see Section 3.5 Government Procurement

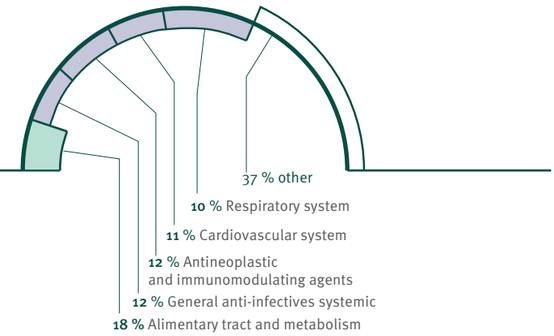
Russian pharmaceutical market structure by ATC classification category

Pharmstandard medicines are present in 14 of 15 ATC categories.

Russian pharmaceutical market structure by ATC classification category category
(in volume terms)



Russian pharmaceutical market structure by ATC classification category
(in value terms)



Russian pharmaceutical market structure and dynamics
(in value terms, RR million)

	2015		2016		
SEGMENT	**RR**	**SHARE**	**RR**	**SHARE**	**16/15**
Commercial market	814,410	72.6%	893,390	73.8%	9.7%
Hospital segment	159,740	14.2%	153,824	12.7%	(3.7%)
PDBP	52,018	4.6%	57,406	4.7%	10.4%
Regional-level benefit	49,291	4.4%	55,439	4.6%	12.5%
7 Nosologies	46,758	4.2%	50,081	4.1%	7.1%
TOTAL	**1,122,217**	**100%**	**1,210,140**	**100%**	**7.8%**

Russian pharmaceutical market structure and dynamics
(in volume terms, million packs)

	2015		2016		
SEGMENT	**PACKS**	**SHARE**	**PACKS**	**SHARE**	**16/15**
Commercial market	4,742	85.2%	4,920	86.8%	3.7%
Hospital segment	696	12.5%	618	10.9%	(11.2%)
PDBP	79	1.4%	76	1.3%	(3.3%)
Regional-level benefit	42	0.8%	49	0.9%	15.2%
7 Nosologies	3	0.1%	3	0.1%	0.4%
TOTAL	**5,563**	**100%**	**5,667**	**100%**	**1.9%**

Average manufacturer's price dynamics in the Russian pharmaceutical market by segment (RR/pack)

SEGMENT	**2015**	**2016**	**16/15**
7 Nosologies	13,487	14,387	6.7%
Regional-level benefit	1,155	1,128	(2.3%)
PDBP	659	752	14.1%
Hospital segment	229	249	8.5%
Commercial market	172	182	5.7%
TOTAL AVERAGE	**202**	**213**	**5.9%**

Russian pharmaceutical market structure and dynamics by manufacturer origin
(in value terms, RR million)

	2015		2016		
IMPORT/LOCAL	**RR**	**SHARE**	**RR**	**SHARE**	**16/15**
Import	809,656	72.1%	848,568	70.1%	4.8%
Local	312,561	27.9%	361,573	29.9%	15.7%
TOTAL	**1,122,217**	**100%**	**1,210,140**	**100%**	**7.8%**

Russian pharmaceutical market structure and dynamics by manufacturer origin
(in volume terms, million packs)

	2015		2016		
IMPORT/LOCAL	**PACKS**	**SHARE**	**PACKS**	**SHARE**	**16/15**
Import	3,242	58.3%	3,308	58.4%	2.0%
Local	2,321	41.7%	2,359	41.6%	1.6%
TOTAL	**5,563**	**100%**	**5,667**	**100%**	**1.9%**

Russian pharmaceutical market structure and dynamics by drug status
(in value terms, RR million)

	2015		2016		
RX/OTC	**RR**	**SHARE**	**RR**	**SHARE**	**16/15**
RX	666,704	59.4%	709,254	58.6%	6.4%
OTC	403,255	35.9%	448,671	37.1%	11.3%
Food supplements	52,258	4.7%	52,216	4.3%	(0.1%)
TOTAL	**1,122,217**	**100%**	**1,210,140**	**100%**	**7.8%**

Russian pharmaceutical market structure and dynamics by drug status
(in volume terms, million packs)

	2015		2016		
RX/OTC	**PACKS**	**SHARE**	**PACKS**	**SHARE**	**16/15**
RX	3,102	55.8%	3,198	56.4%	3.1%
OTC	2,087	37.5%	2,099	37.0%	0.6%
Food supplements	374	6.7%	370	6.5%	(1.1%)
TOTAL	**5,563**	**100%**	**5,667**	**100%**	**1.9%**

Russian pharmaceutical market structure and dynamics by product inclusion on the VED list
(in value terms, RR million)

	2015		2016		
VED/NON-VED	**RR**	**SHARE**	**RR**	**SHARE**	**16/15**
VED listed	532,769	47.5%	571,188	47.2%	7.2%
Non-VED listed	589,448	52.5%	638,953	52.8%	8.4%
TOTAL	**1,122,217**	**100%**	**1,210,140**	**100%**	**7.8%**

Russian pharmaceutical market structure and dynamics by product inclusion on the VED list
(in volume terms, million packs)

	2015		2016		
VED/NON-VED	**PACKS**	**SHARE**	**PACKS**	**SHARE**	**16/15**
VED listed	2,573	46.2%	2,640	46.6%	2.6%
Non-VED listed	2,990	53.8%	3,026	53.4%	1.2%
TOTAL	**5,563**	**100%**	**5,667**	**100%**	**1.9%**

Russian pharmaceutical market structure and dynamics by product inclusion on the VED list
(in volume terms, million packs)

VED/NON-VED	**2015**	**2016**	**16/15**
VED listed	207,03	216,27	4.5%
Non-VED listed	197,05	211,06	7.1%
TOTAL	**201,66**	**213,49**	**5.9%**

2.2 Key regulatory changes in the Russian Federation in 2016

General information on the Russian pharmaceutical legislation

The major legal act for the pharmaceutical industry is Federal Law No. 61-FZ “On Circulation of Medicines” dated 12 April 2010, which regulates the circulation of medicines (development, testing and trials, state registration, manufacture, transportation, import/export, advertising, dispensation, etc).

Furthermore, the legislation on circulation of medicines comprises other federal laws such as:

- Federal Law No. 323-FZ “On Fundamentals of Health Protection in the Russian Federation” dated 21 November 2011, which regulates relations arising in the sphere of health protection of citizens in the Russian Federation and determines legal, organizational and economic basis of health protection of citizens; health protection rights and obligations of citizens and specific population groups, and the warranty of these rights; powers and responsibilities of Russian government bodies of all levels in the sphere of health protection; rights and obligations of medical and other organizations involved in health protection activities; rights and obligations of medical professionals and pharmaceutical personnel;
- Federal Law No. 3-FZ “On Narcotic Drugs and Psychotropic Substances” dated 8,January 1998, which establishes the legal framework for the government control over the turnover of narcotic drugs, psychotropic substances and their precursors, and for the countering of illicit trafficking;
- Federal Law No. 38-FZ “On Advertising” dated 13 March 2006, which was adopted with a view to developing the markets of goods, work and services on the basis of fair competition, ensuring the unity of economic space, and securing consumer rights to fair and reliable advertising;
- Federal Law No. 135-FZ “On Protection of Competition” dated 26 July 2006, which establishes the organizational and legal basis for the protection of competition.

The next level of legal acts constituting the legislation on circulation of medicines is represented by other statutory legal acts of the Russian Federation. This category includes decrees of the President of the Russian Federation, regulations and orders of the Government of the Russian Federation, and statutory legal acts of the federal executive authorities, for example:

- Decree No. 598 of the President of the Russian Federation dated 7 May 2012,“On Improvement of State Policy in the Sphere of Health Care,” which introduces activities to be implemented by the Government of the Russian Federation in the sphere of health care, including the introduction of the strategy of pharmaceutical support for the population of the Russian Federation until 2025;

- Resolution No. 865 of the Government of the Russian Federation dated 29 October 2010,"On State Regulation of Prices for Medicines Included in the List of Vital and Essential Drugs," which establishes the rules for the circulation of medicines included in the list of vital and essential drugs;
- Order No. 428n of the Ministry of Health of Russia dated 22 October 2012,"On Approval of the Administrative Procedure of the Russian Federation Ministry of Health for the State Service of Registering Pharmaceuticals for Medical Use," which regulates the procedure of the registration of medicines for further circulation in the territory of the Russian Federation;
- Order No. 1222n of the Ministry of Health and Social Development of the Russian Federation dated 28 December 2010, which approves the rules for the wholesale trade of medicines for medical use;
- Order No. 756n of the Ministry of Health and Social Development of the Russian Federation dated 26 August 2010, which endorses the procedure for working out the general pharmacopoeia entries, pharmacopoeia entries and their inclusion in the state pharmacopoeia and placing the information on the state pharmacopoeia on the official website;
- Resolution No. 91 of the Government of the Russian Federation dated 17 February 2011,"On the Federal Target Program "Development of the Pharmaceutical and Medical Industry of the Russian Federation for the Period up to 2020 and beyond";
- Order No. 965 of the Ministry of Industry and Trade of the Russian Federation dated 23 October 2009 "On the Approval of the Strategy of Pharmaceutical Industry Development up to 2020";
- Order No. 66 of the Ministry of Health of Russia dated 13 February 2013 "On the Approval of the Strategy of Pharmaceutical Support for the Russian Population until 2025 and its Implementation Plan."

General information on changes to laws and other legal acts of the Russian Federation regulating the pharmaceutical market

In 2016, no major amendments were made to Federal Law No. 61-FZ "On Circulation of Medicines" dated 12 April 2010.

The adoption of Federal Law No. 350-FZ "On Amendments to Article 61 of the Federal Law 'On Circulation of Medicines' and Article 3 of the Federal Law 'On Amendments to the Federal Law 'On Circulation of Medicines" dated 3 July 2017 has changed the regulatory framework governing the application of prices for medicines included in the list of vital and essential drugs.

The interchangeability of Russian-registered drugs designated for medical use shall be established through comparison against the reference drug in accordance with the procedure adopted by the Government of the Russian Federation, as well as by reference to the parameters indicated in Part 1 Article 27.1 of Federal Law No. 61"On Circulation of Medicines" dated 12 April 2010.

Federal Law No. 261-FZ "On Amendments to the Federal Law "On the State Regulation of the Production and Distribution of Ethanol and Alcoholic and Alcohol-Containing Products and on the Restricted Consumption (Drinking) of Alcoholic Products" and Certain Legislative Acts of the Russian Federation" was adopted on 3 July 2016 in order to clarify the regulatory framework governing restrictions on the production and distribution of ethanol and alcoholic and alcohol-containing products, including alcohol-containing medicines. The Law introduces the definitions of "alcohol-containing medicines" and "alcohol-containing medical goods." Organizations engaged in the production of ethanol for the purpose of producing alcohol-containing medicines and alcohol-containing medical goods are now required to record and declare the amount of ethanol produced, supplied and/or consumed for own needs, as prescribed by the Government of the Russian Federation. The Law imposes a ban on any retail sales of ethanol.

In addition, administrative liability has been imposed on the production and distribution (excluding retail sale) of alcoholic beverages in consumer plastic containers.

New requirements pertaining to patient information leaflets for medicines which were filed for registration on 21 October 2016 have been approved by Order No. 724n of the Ministry of Health of Russia dated 21 September 2016. Pursuant to the Order, a patient information leaflet should be concise and clear (with no repetitions in the same section), should not allow varying interpretations, and should provide sufficient and understandable information to ensure correct self-administration of a given medicine, whether prescribed or over-the-counter.

Federal Law No. 180-FZ "On Biomedical Cell Products" dated 23 June 2016,became effective on 1,January 2017. The Law regulates the circulation of biomedical cell products designed for preventive care, diagnosis and treatment of diseases or conditions, pregnancy maintenance and medical rehabilitation. The definitions of "biomedical cell product," "cell line," "cell differentiation," "donor of biological material," "safety of a biomedical cell product," "effectiveness of a biomedical cell product" and other concepts which are critical to the circulation of biomedical cell products were for the first time enshrined in the legislation.

Key changes to public procurement legislation in 2016

Significant amendments to Federal Law No. 44-FZ became effective from 1 September 2016.

With these amendments, goods produced under an investment contract may now be purchased from a single supplier. A procuring entity is allowed to purchase these goods without a competitive bidding process, if the supplier is listed in the register of single suppliers.

A special investment contract is a contract whereby one party (the investor) undertakes to establish industrial production in Russia, while the other party (the Russian Federation or its constituent entity) pledges to provide investor incentives envisaged by law.

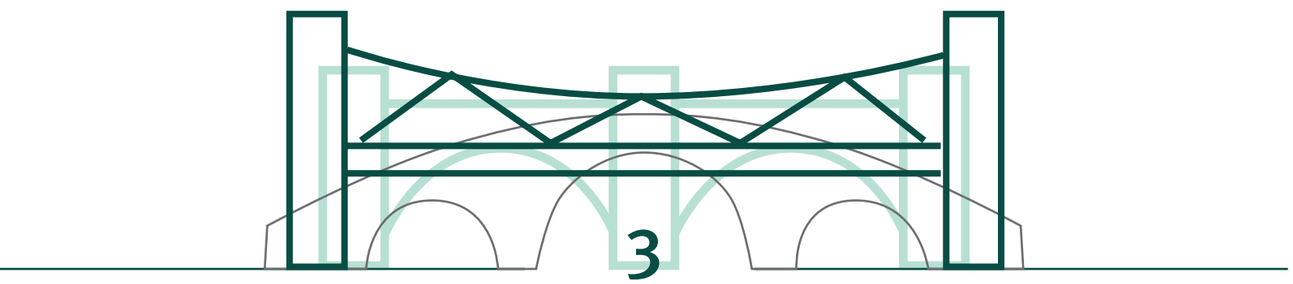
The lawmaker also noted that the procuring entity must terminate the contract if supplied products do not meet the requirements set forth in the procurement notice (documentation) or if the supplier has provided inaccurate information about compliance with the above requirements.

Order No. 795 issued by the Russian Ministry for Economic Development on 30,October 2015approved the procedure for Public Hearings that must be held if the initial (maximum) price of a contract entered into with a single supplier exceeds RR 1 billion. The procedure was revised in 2016. Under the revised procedure, should the procuring entity violate the deadline for posting its response to comments or proposals on the official website of the unified information system for public procurement, the violation shall be automatically recorded in the system.

The unified information system for public procurement, launched on www.zakupki.gov.ru, was introduced on 1 January 2016 by orders Nos. 354 and 355 of the Treasury of Russia dated 22 December 2015.

Resolution No. 1132 of the Government of the Russian Federation dated 31 October 2014 and Order No. 173n of the Russian Finance Ministry dated 29 December 2014 have introduced a requirement that a register of contracts entered into by a procuring entity under Federal Law No. 223-FZ "On Procurement of Goods, Work and Services by Certain Types of Legal Entities" dated 18 July 2011 should contain information and documents relating to the revision, performance or termination of such contracts, and the provision of copies of signed contracts.

Resolution No. 1217 of the Government of the Russian Federation dated 11 November 2015 and Letter No. 34016-EE/D28iof the Russian Ministry for Economic Development have expanded the list of goods, work and services procured by certain types of legal entities under an electronic procurement procedure, as prescribed by Federal Law No. 223-FZdated 18 July 2011.



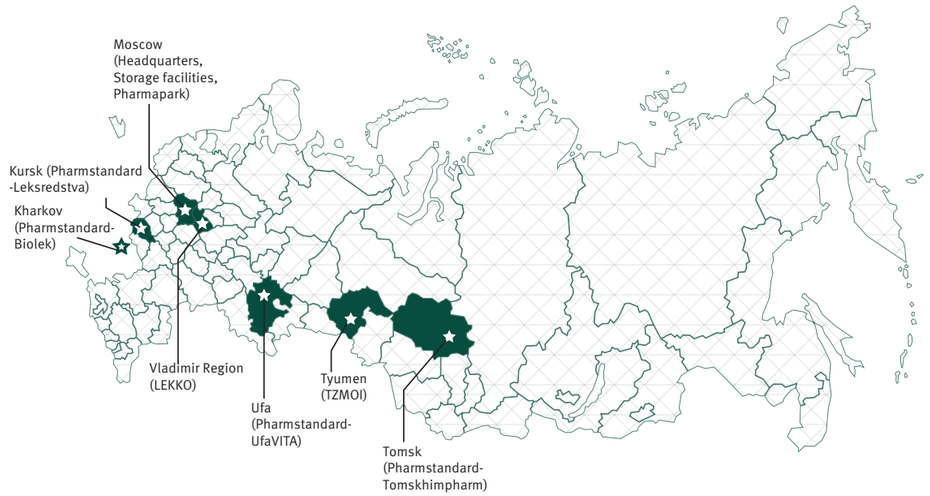
3

Company's business overview

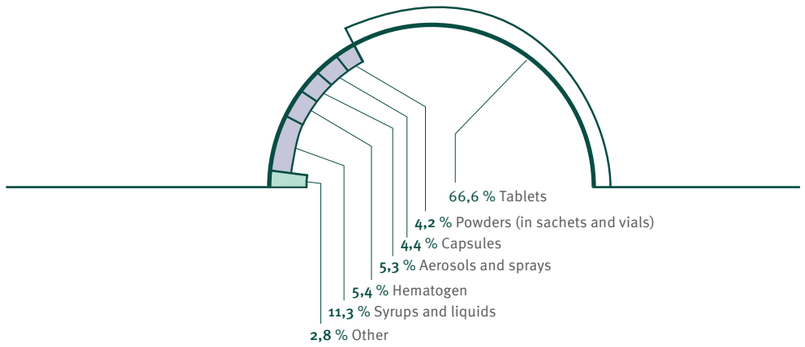
3.1 Manufacturing facilities

In 2016, the Group had seven manufacturing facilities, which can be broadly divided into three main production categories: pharmaceutical products, medical equipment and substances.

Pharmstandard Group's production geography



All manufacturing facilities can cumulatively produce 1.1 million packs of pharmaceutical products, 636,000 liters of substances[7] and 2,710 units of medical equipment. Pharmaceutical plants manufacture finished products in the following dosage forms:



Hematogen production soared over 26% in 2016 and was classified as a separate category (for reasons, see Section 3.3 Pharmaceutical portfolio).

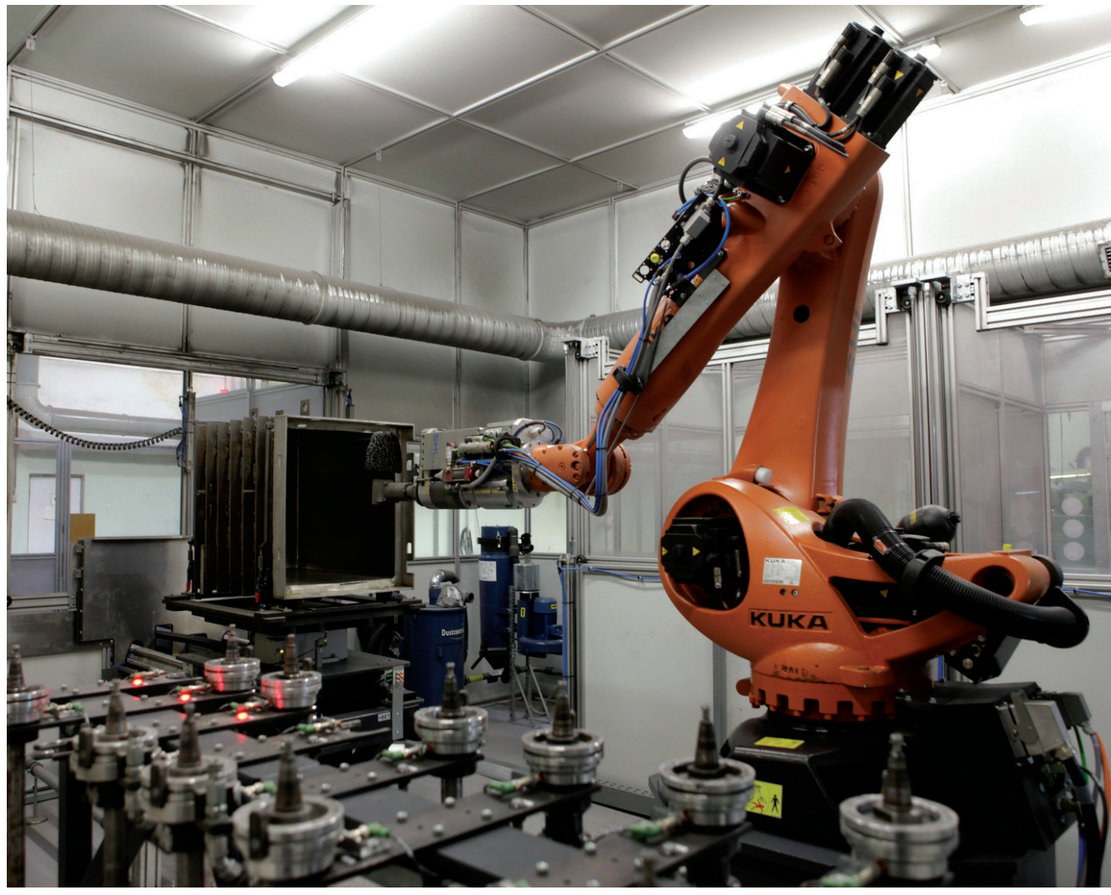
7 Excluding substances produced by Pharmstandard-Leksredstva

Company	Finished dosage form	Number of shifts	Manufacturing capacity in 2015, ooo packs	Utilization rate 2015, (%)	Manufacturing capacity in 2016, ooo packs	Utilization rate 2016, (%)
Pharmstandard-Leksredstva OJSC	Syrups and liquids	3	67,586	65%	66,655	80%
	Tablets	3	394,723	65%	420,353	68%
	Aerosols and sprays	3	27,265	65%	39,850	74%
	Powders	3	5,486	33%	5,476	63%
	Capsules	3	51,600	50%	39,947	58%
	Hematogen	3	60,000	40%	58,666	62%
	Test strips	3	-	-	11,130	8%
TOTAL			606,660		642,076	
Pharmstandard-UfaVITA OJSC	Solutions for injection (ampules)	3	22,650	54%	25,524	51%
	Lyophilic colloids	3	395	96%	1,552	21%
	Tablets	3	97,200	64%	126,550	46%
	Vitamins (ferrohematogen)	3	17,136	26%	-	-
	Pre-filled syringes	3	-	-	1,299	73%
	Biosulin (vials and cartridges)	3	3,500	30%	3,640	13%
TOTAL			140,881		158,565	
Pharmstandard-Tomskhimpharm OJSC	Syrups and liquids	3	5,400	2%	5,400	0%
	Tablets	3	187,935	30%	173,865	19%
	Aerosols and sprays	3	9,600	13%	8,165	17%
	Ointments and creams	3	2,271	29%	2,218	76%
TOTAL			205,206		189,648	
LEKKO CJSC	Tablets	3	4,730	27%	3,802	23%
	Capsules	3	9,180	52%	8,218	66%
	Syrups and liquids	3	52,680	63%	50,762	66%
	Powders	3	21,475	45%	24,735	22%
	Aerosols and sprays	3	9,920	5%	9,920	7%
TOTAL			97,985		97,438	
Pharmstandard-Biolek PJSC	Syrups and liquids	3	257	42%	-	-
	Solutions for injection (ampules)	3	631	8%	328,3	24%
	Lyophilisate	3	-		3,88	27%
	Powders	3	113	30%	-	-
TOTAL			1,001		332	
Total finished pharmaceutical products			**1,051,734**		**1,088,059**	
TZMOI JSC	Steam sterilizers (under 100L)	3	2500	31%	2500	6%
	Steam sterilizers (100L+)	3	110	47%	110	85%
	Washing units	3	100	39%	100	85%
TOTAL			2,710		2,710	

In addition, the capacity of Pharmapark for manufacturing of substances has reached 636 liters in 2016.

OUTPUT IN 2016

In 2016, Group companies produced a total of 591 million packs of pharmaceuticals, 135 liters of substances for sale[8] and 317 units of medical equipment. Pharmstandard is Russia's largest producer and the only private pharmaceutical company featured in the national list of systemically important companies[9].

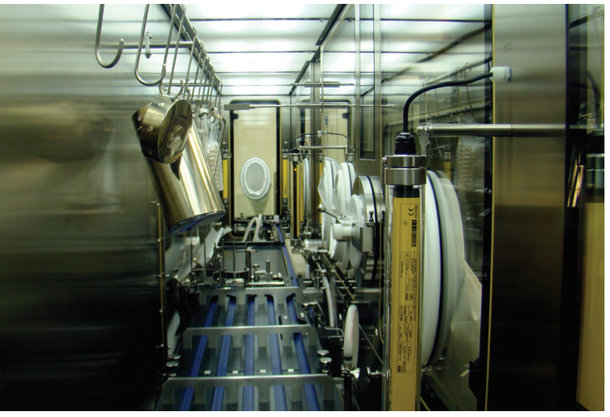


8 Excluding substances produced for internal consumption

9 The list comprises major Russia-based companies which have a significant impact on GDP, employment and social stability

Table. Output of Pharmstandard Group companies by dosage form

Name	Number of SKUs	Output by dosage form (million packs)						
		Syrups and liquids	Tablets	Aero-sols and sprays	Cap-sules	Powders and sachets	Other	Total
Pharmstandard-Leksredstva	265	52.2	279.4	30.0	20.9	5.0	37.2	424.7
Pharmstandard-UfaVITA	151	15.3	53.3		0.03		14.4	83.0
Pharmstandard-Tomskhimpharm	70		33.4	1.4			1.7	36.5
LEKKO	25	33.8	0.9	0.7	0.5	5.4	4.9	46.2
Pharmstandard-Biolek	30	0.1					0.1	0.2
PHARMAPARK[10]	12	0.4						0.4
TOTAL	553	102	367	32	21	10	58	591



Pharmstandard-Leksredstva

Pharmstandard-Leksredstva produced a total of 425 million packs in 2016, up 14% from 372 million in the previous year.

The stronger performance was driven by the following factors:

- / Higher sales across most product categories
- / Portfolio diversification (production under own brands and third-party brands)
- / Launch of new products under contract manufacturing agreements (Mycoderil, Codelac Neo, and Codelac Broncho)

Pharmstandard-UfaVITA

Pharmstandard-UfaVITA produced a total of 83 million packs in 2016, up 3.5% from 81 million a year earlier.

The growth was propelled by the launch of drugs produced under own brands and the production of new drugs transferred from other domestic and foreign manufacturers.

10 Excluding substances

Pharmstandard-Tomskhimpharm

Pharmstandard-Tomskhimpharm produced a total of 36 million packs in 2016, down 34% from a year earlier. The decline was largely due to ongoing upgrades on existing facilities aimed at optimizing production processes and increasing profit margins.

Sub-optimal production was transferred to Pharmstandard-Leksredstva where there is substantial manufacturing capacity to improve profitability, leaving Pharmstandard-Tomskhimpharm to focus on small-batch production of high-margin drugs.

LEKKO

LEKKO's output in 2016 was 46.2 million packs, virtually the same as in 2015.

Pharmstandard-Biolek

In 2016, Pharmstandard-Biolek was focused on the production of free and encapsulated drugs (liposomes), as well as on immunobiological and diagnostic products.

The company's total output in 2016 was 1,593,100 packs, up 1.9% from a year earlier. The growth was due to an increase in orders and sales in Ukraine and the launch of new brands (Cytochrome C, Encadum, Ectericide, etc.).

Pharmapark

Pharmapark's output in 2016,consisted of finished pharmaceutical products (355 000 packs) and substances for sale (135,liters). Finished pharmaceutical products are manufactured at Pharmstandard-UfaVITA's facilities on a contract basis, with release quality control performed by Pharmstandard-UfaVITA (two product items) and Pharmapark (one product item).

The output decreased from the previous year amid falling demand for certain drugs, primarily Altevir®. At the same time, pre-filled syringes were gradually replaced with cheaper ampules as a dosage form for Interferon Alpha-2b and Epoetin Beta.

TZMOI (Tyumen Plant of Medical Equipment and Tools)

In 2016, TZMOI produced 138 and 94 steam sterilizers with a capacity under 100L and 100L+, respectively, and 85 washing and disinfection units.

LAUNCH OF NEW CAPACITIES AND MODERNIZATION IN 2016

Pharmstandard follows its development strategy by building new plants and acquiring process equipment and laboratory tools to manufacture new products and control quality.

The following initiatives were completed in 2016 to expand existing capacity and product range:

Pharmstandard-Leksredstva

The plant's central laboratory building has been renovated, with a small-series section added; the construction of a packaging warehouse has been completed; workshop No. 3 is currently under renovation to expand area No. 6 (equipment purchase is underway); section No. 2 of workshop No. 6 has been put into operation, with a packaging line for blood-glucose test strips installed; a storage area for endocrine active substances has been created; new equipment has been acquired to replace old equipment and upgrade existing production facilities.

Pharmstandard-UfaVITA

The construction stage of a 10 500 sq. m 6-storey building has been completed (the building will host production of GMP-compliant finished pharmaceuticals that include tablets and lyophilisates); the construction of a new boiler house to improve hot water and utility steam supply is nearing completion (the facility was put into test operation in February 2017); an Insulin production section in workshop No. 4 has been renovated in preparation for the launch of the Gazyva® production, with qualification and validation activities currently underway; renovation continued on workshop No. 4 to create a new small-series section for drugs produced by aseptic processing (liquids and lyophilisates in vials and liquids in syringes).

Pharmstandard-Tomskhimpharm

Construction and mounting work has been completed and equipment worth RR 52 million has been purchased (most of the equipment will be used for new production, which is scheduled to start in 2017); warehousing facilities have been upgraded to comply with GMP requirements, additional equipment has been installed in a tablet production workshop and validation and quality control departments.

LEKKO

Capital construction work covering workshop No. 2 (installation of a BWT water treatment, distribution and storage system), building No. 8 (preparation for the launch of soft pharmaceuticals production in workshop No. 7), and workshop No. 3 (development of a freeze-drying process); equipment purchases for other workshops.

Pharmstandard-Biolek

Renovation of an energy supply system (a major capital construction project in 2016), a biological control laboratory, utility networks, premises for growth media production and a warehouse for printed materials; equipment purchases for the Validation Department and a RIG production area.

Pharmapark

As part of the current EU GMP compliance program, the company opened microbiological, pharmaceutical and biological control laboratories and put into operation a centralized water-for-injection (WFI) plant; a section for chemical synthesis and purification of a highly productive erythropoietin producer has been put into operation to increase eukaryotic production.

INVESTMENT PLANS FOR 2017

Pharmstandard-Leksredstva

Capital construction plans include the following:

- Organize production of pulmonary powders in building No. 17
- Renovate and replace equipment in section No. 2 of workshop No. 3 to expand manufacturing capacity
- Renovate section No. 2 of workshop No. 2
- Renovate and air-condition the first and second floors of the central warehouse
- Build a covered storage area for pallets and vials

Pharmstandard-UfaVITA

Acting on its plan for a phased GMP implementation, the company will perform the following construction and renovation activities:

- Continue preparation activities in the new building that will host production of finished pharmaceuticals, and establish two laboratories, one focused on production process improvements and advanced quality control methods, and the other (under the QC Department) on phased-control activities
- Open a small-series production area, purchase equipment and organize the manufacturing of injection-molded products
- Build a new gas-fueled boiler house to increase hot water and utility steam supply

Commissioning is scheduled for Q1 2017

LEKKO

The company will acquire production and laboratory equipment, and conduct renovation work on building No. 2

Pharmstandard-Biolek

The work will be focused on renovating existing premises and upgrading the biological control laboratory and the vivarium.

Pharmapark

The company plans to upgrade the mammalian eukaryotic cell cultivation area, so that up to three chemically-synthesized producers can be obtained at the same time.

3.2

Quality management

Pharmstandard Group has implemented and continuously improves a quality management system across all its manufacturing entities.

The system has been developed and implemented in compliance with the following standards and regulations:

- / European Commission Directive 2003/94/EC
- / Rules of Good Manufacturing Practice, approved by Order No. 916 of the Ministry of Industry and Trade of the Russian Federation dated 14 June 2013
- / Rules of Good Distribution Practice of the Eurasian Economic Union (EEU), approved by Resolution No. 80 of the EEU Council dated 3 November 2016
- / Russian National Standard GOST ISO 9001-2015,"Quality Management Systems. Requirements"

The quality management system at Tyumen Plant of Medical Equipment and Tools JSC is compliant with the following standards:

- / EN ISO 13485 (EN ISO 13485:2012 + AC:2012,– ISO 13485:2003 + Cor. 1:2009) "Medical Devices — Quality Management Systems — Regulatory Requirements"
- / EN ISO 9001 (ISO 9001:2008) "Quality Management Systems — Requirements"

All manufacturing entities are regularly inspected by the following Russian authorities:

- / Ministry of Industry and Trade of the Russian Federation ("Minpromtorg")
- / Federal Service for Supervision in the Area of Health Care of the Russian Federation ("Roszdravnadzor")

Audits are also performed by the following Russian and foreign partners:

№	COMPANY	AUDITOR
1	Pharmstandard-Leksredstva OJSC	Johnson & Johnson Celgene Nativa Alvogen OTCPharm
2	Pharmstandard-UfaVITA OJSC	Merck GE HealthCare Johnson & Johnson Ferring Biogen Biocad Celgene Takeda Amgen Nanolek Pfizer Novartis AbbVie OTCPharm Sanofi
3	Pharmstandard-Tomskhimpharm OJSC	OTCPharm

In 2016, Pharmstandard started cooperation with F.Hoffmann-La Roche Ltd, Astra Zeneka, Baxalta, BioIntegrator, Bristol Myers Squibb, Chemical Diversity Research Institute (IIHRI), MosTek LLC, Novartis, PARAMED LLC, Takeda, Scientific Research Institute of Epidemiology and Microbiology of Russia's Ministry of Health under the name of N.F. Gamaleya, taking a consistent approach to quality management under cooperation agreements with the new partners. Responsibilities for managing the quality of pharmaceutical products across the entire value chain are clearly set in relevant QMAs.

With the ratification of the Agreement on Unified Principles and Rules for the Circulation of Pharmaceuticals in the Eurasian Economic Union dated 23 December 2014 and the adoption of a legal framework for pharmaceutical regulation in the EEU, Pharmstandard Group's distribution and manufacturing entities continue to enhance the existing quality management systems in line with EEU's Good Distribution Practice (GDP). Further improvements to quality management systems have been scheduled for 2017.

In 2016, the Group started the second phase of a project to implement a SAP-based system for business process management and performance assessment:

1) Business requirements aimed at maintaining and improving the quality of Pharmstandard's products were developed, with the following actions taken to guarantee product quality:
   - / Inspection of incoming raw materials and checking the quality of raw materials used in production
   - / In-process inspections and outgoing quality control
   - / Product stability assessment
   - / Deviation management
   - / Vendor and supplier product monitoring
   - / Change management
   - / Information support for validation and metrology processes
   - / Quality assurance and quality control of stored raw materials and finished products
   - / Management and information support of claim handling process

2) Design concepts were developed to integrate the implemented SAP solutions into Pharmstabndard's IT infrastructure.

3) Software solutions to support the new business requirements are being implemented.

4) The Group has made significant progress in ensuring that documentation for each product series is automatically generated and downloaded from SAP.

In 2016, the Group developed and tested the Claim module based on the PharmSED2 program, which is designed to register all customer complaints received from various sources and ensure they are addressed in a timely manner. Work is nearing completion to connect a 24/7 call center to the Claim module in order to reduce response times to critical customer complaints.

Validation and qualification

An important part of the validation and qualification process is an annual Validation Master Plan that is designed to ensure that the required level of quality is maintained throughout the entire supply chain, from manufacturing to storage, distribution and delivery of all products, including temperature-sensitive drugs.

In line with the Validation Master Plan, the Company performed qualification tests on warehousing facilities, computer systems and equipment used in a cold chain.

The structure of the documentation used by the Validation Department was revised.

The Validation Policy was updated to reflect new approaches.

To ensure that the right quality of dispatched products is maintained, the Group introduced a unified process to fill insulated containers and optimized its storage processes at the same time.

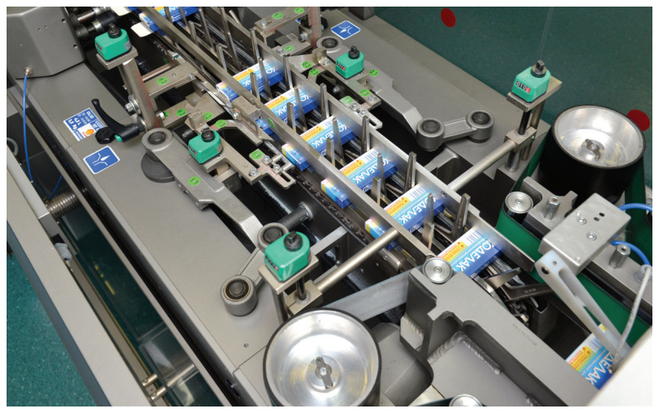
The Group's plants also completed their 2016 validation activities as planned.

Quality management at Group companies

Pursuant to Order No. 916 of the Ministry of Industry and Trade of the Russian Federation dated 14 June 2013,"On Approval of Rules of Good Manufacturing Practice", authorized persons of all Group companies have passed state certification.

Group companies hold the following documents confirming the validity of their quality management system:

№	COMPANY	DOCUMENT NAME AND NUMBER	ISSUING AUTHORITY	EXPIRY DATE
1	Pharmstandard-Leksredstva OJSC	EU GMP "Good Manufacturing Practice (EU GMP)" compliance certificate based on Directive 2003/94/EC, No. ZVA/LV/2015/002H dated 19 February 2015	State Agency of Medicines of the Republic of Latvia	12 December 2017
		GOST R ISO 9001-2015 (ISO 9001:2015) "Quality Management System as Applied to the Development and Manufacture of Pharmaceuticals" compliance certificate No. ROSS RU.IMo0.Io037 dated 25 May 2016	VNIIS-CERT quality management certification agency, VNIIS OJSC, Moscow	25 May 2019
		Statement on compliance of the manufacturer (foreign manufacturer) of controlled drugs with the Rules of Good Manufacturing Practice, No. GMP-0003-000100/16 dated 12 June 2016	Minpromtorg	12 July 2019
		GOST ISO 13485-2011 (ISO 13485:2003) "Quality Management System as Applied to the Manufacturing (Secondary Packaging) and Quality Control of Sealed Tubes with Glucose Test Strips", No. OSM RU.03-S2b-221 dated 29 November 2016	VNIIS-CERT quality management certification agency, VNIIS OJSC, Moscow	29 November 2019



№	COMPANY	DOCUMENT NAME AND NUMBER	ISSUING AUTHORITY	EXPIRY DATE
2	Pharmstandard-UfaVITA OJSC	EU GMP "Good Manufacturing Practice (EU GMP)" compliance certificate based on Directive 2003/94/EC, No. ZVA/LV/2015/004H dated 30 April 2015	State Agency of Medicines of the Republic of Latvia	20 February 2018
		GOST R ISO 9001-2015 (ISO 9001:2015) "Quality Management System as Applied to the Development and Manufacture of Pharmaceuticals" compliance certificate No. ROSS RU.IMo0.Io035 dated 22 May 2016	VNIIS-CERT quality management certification agency, VNIIS OJSC, Moscow	22 May 2019
		Statement on compliance of the manufacturer of controlled drugs with the Rules of Good Manufacturing Practice, No. GMP-0002-000125/16 dated 10 October 2016	Minpromtorg	7 June 2019
3	Pharmstandard-Tomskhimpharm OJSC	GOST R ISO 9001-2015,"Quality Management System as Applied to the Development and Manufacture of Pharmaceuticals" compliance certificate No. ROSS RU.IMo0.Io0366 dated 18 May 2016	VNIIS-CERT quality management certification agency, VNIIS OJSC, Moscow	18 May 2019
		Statements on compliance of the manufacturer of controlled drugs with the Rules of Good Manufacturing Practice are to be obtained from Minpromtorg for manufacturing sites based at the following locations: - 32 Proletarskaya st., Tomsk; - 89 Rosa Luxembourg st., Tomsk; Inspection is scheduled for 14-15 December 2016	-	-
4	Pharmstandard-Biolek PJSC	Permits to work with Risk Group 3 and Risk Group 4,pathogens issued for the following areas: - antitoxin production area of the vaccine and serum section (permit No. 65-15 dated 16 April 2015); - rabies virus antigen production area (permit No. 66-15 dated 16 April 2015); - virology laboratory of the QC Department (permit No. 81-15 of 20 May 2015); - biological control laboratory of the QC Department (permit No. 64-15 of 16 April 2015);	State Sanitary and Epidemiological Service of Ukraine for the Kharkiv region	16 April 2020 16 April 2020 16 May 2017 16 April 2020
5	LEKKO CJSC	GOST R ISO 9001-2015 (ISO 9001:2015) "Quality Management System as Applied to the Development, Manufacture, Storage and Sale of Pharmaceuticals" compliance certificate No. ROSS RU.IS11.K01127 dated 11 March 2016	VNIIS-CERT quality management certification agency, VNIIS OJSC, Moscow	11 March 2019
		Statement on compliance of the manufacturer (foreign manufacturer) of controlled drugs with the Rules of Good Manufacturing Practice, No. GMP-0013-000111/16 dated 20 July 2016	Minpromtorg	20 July 2019

№	COMPANY	DOCUMENT NAME AND NUMBER	ISSUING AUTHORITY	EXPIRY DATE
6	Pharmapark LLC	GOST R ISO 9001-2015 (ISO 9001:2015) “Quality Management System as Applied to the Development, Manufacture, Storage and Sale of Pharmaceuticals (Biological Medicines) and Pharmaceutical Substances, Including Substances Produced by Aseptic Processing” compliance certificate No. ROSS RU.IS11. K01145 dated 20 June 2016	VNIIS-CERT quality management certification agency, VNIIS OJSC, Moscow	23 December 2018
		Statements on compliance of the manufacturer of controlled drugs with the Drug Manufacturing and Quality Control Rules: - No. GMP-0010-000011/15 dated 13 February 2015 (the manufacturing site located at 8 Nauchny proezd, Bldg. 1 Moscow) - No. GMP-0010-000012/15 dated 13 February 2015 (the manufacturing site located at Petrovo-Dalneye settlement, Krasnogorsk district, Moscow region)	Minpromtorg	8 July 2017
7	Tyumen Plant of Medical Equipment and Tools JSC	EN ISO 13485 “Medical Devices. Quality Management Systems. Requirements for Regulatory Purposes” compliance certificate No. D1236900009 dated 28 November 2016	mdc medical device certification GmbH	27 November 2019
		EN ISO 9001 (ISO 9001:2008) “Quality Management Systems. Requirements” compliance certificate No. D1236900010 dated 28 November 2016	mdc medical device certification GmbH	15 September 2018
		DSTU ISO 10012:2005 (ISO 10012:2003) “Measurement Management Systems. Requirements for Measurement Processes and Measuring Equipment” compliance certificate No. 01-008/2016 dated 18 August 2016	Kharkov Regional Scientific and Production Center of Standardization, Metrology and Certification	18 August 2019
		ISO 13485:2005 (ISO 13485:2008) “Medical Devices. Quality Management Systems. Requirements for Regulatory Purposes” compliance certificate No. UA 2.003.8408-14 dated 9 April 2014		8 April 2019
		ISO 9001:2008,“Manufacture of In-Vitro Diagnostic Medical Devices” compliance certificate No. UA 2.003.08400-14 dated 3 April 2014	Kharkov Regional Scientific and Production Center of Standardization, Metrology and Certification	2 April 2019
		GOST ISO 9001-2011 (ISO 9001:2008) “Quality Management System as Applied to the Development, Manufacture, Storage and Sale of Pharmaceuticals” compliance certificate No. ROSS RU.UA.11. K01019 dated 4 June 2014	National Accreditation Agency of Ukraine	4 June 2017

Pharmacy depots of Pharmstandard JSC and Pharmstandard LLC

Based on the results of the pharmacy depots re-certification audits in 2016, the certification authorities confirmed the validity of the existing certificates of compliance with GOST ISO 9001-2011,“Quality Management System. Requirements”.

1. Pharmstandard JSC
Certificate No. ROSS RU.IS11.K01090 dated 18 September 2015
valid until 18 September 2018

2. Pharmstandard LLC
Certificate No. ROSS RU.IS11.K01092 dated 29 September 2015
valid until 18 September 2018

A total of seven external audits were conducted on Pharmstandard JSC’s pharmacy depot by Johnson & Johnson LLC, Celgene International, Sanofi Russia JSC, Bristol-Myers Squibb, Takeda Pharmaceuticals LLC, Baxter CJSC and Roche CJSC.

There was one external audit on Pharmastard LLC’s pharmacy depot conducted by PIQ-PHARMA LEK LLC.

3.3 Pharmaceutical portfolio

The Company’s pharmaceutical portfolio is traditionally divided into several groups: over-the-counter (OTC), prescription (RX) and third-party products (TPP). Prescription and OTC drugs are further divided into branded and unbranded. Branded drugs have a registered trademark, while non-branded drugs don’t have a unique brand. Revenues from these groups are presented in the table below.

RR million	2015	2016	16/15
Own products	**11,660**	**13,147**	13%
Over-the-counter drugs (OTC)	**5,094**	**5,829**	14%
Branded	1,615	1,956	21%
Non-branded	3,479	3,873	11%
Prescription drugs (RX)	**6,566**	**7,318**	11%
Branded	5,254	5,927	13%
Non-branded	1,311	1,391	6%
TPP	**26,408**	**36,222**	37%
SUBSTANCES	**2,005**	**3,325**	15%
PHARMACEUTICAL PORTFOLIO, TOTAL	**40,073**	**52,694**	29%

In 2016 the Group’s pharmaceutical portfolio included 240 brands (553 SKUs):

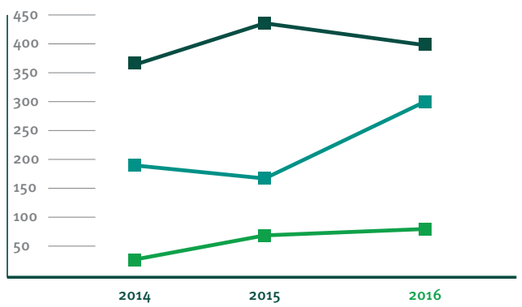
Finished pharmaceutical products (FPP) were the largest group in the range followed by food supplements and substances.

3.3.A Portfolio of own products

The Group's portfolio of own products includes such well-known names as Phosphogliv, Combilipen, Octolipen, Biosulin and Tuberculin. Sales of own products totaled RR 13.1 billion.

Phosphogliv is the sales leader among own products and among promoted products and is one of the top three products on the market used to treat liver ailments. In 2016 Phosphogliv grew by 17% in terms of sales revenue (to RR 1.9 billion) and 12% in terms of units sold (to 3.9 million). Phosphogliv's share[11] of a contracting hepatoprotector market rose 1.3% to 10.6% in terms of units sold. In money terms, Phosphogliv was among the top five hepatoprotectors (fourth place), capturing 8.3% market share. Phosphogliv was the top seller in terms of units sold in the noncommercial segment of the hepatoprotector market. It has led this segment for four years running, gaining market share at a rate of 1.8% annually and reaching 30.1%. Phosphogliv also leads the noncommercial segment in money terms, with a market share of 25.9% and sales of RR 706 million. In April 2016, according to PrIndex,[12] Phosphogliv was the top pharmaceutical (33% market share) used by gastroenterologists and general practitioners to treat liver ailments.

Combilipen prescriptions, thousand per year



Combilipen is second in terms of sales among both own products and among promoted products and leads the category of B-complex injection vitamins (B1, B6, B12) in terms of units sold. Combilipen has been the sales leader and a growth driver in this category for three years. Combilipen's sales volume in 2016 was RR 1.2 billion (over 8,million units). According to IMS Health data, commercial sales account for 95.5% of the market of B-complex injection vitamins. Combilipen is second in terms of revenue, with a 42% market share growing at a rate of 5%, although the category as a whole is exhibiting a downward trend (-4%) in sales. According to the market research company Ipsos Comcon, Combilipen's commercial use by neurologists remains at a high level, and its use by general practitioners and surgeons is showing strong growth.

Corvalol is the third best seller in the portfolio of own products. Sales in 2016 were RR 798 million, or 39 million units.

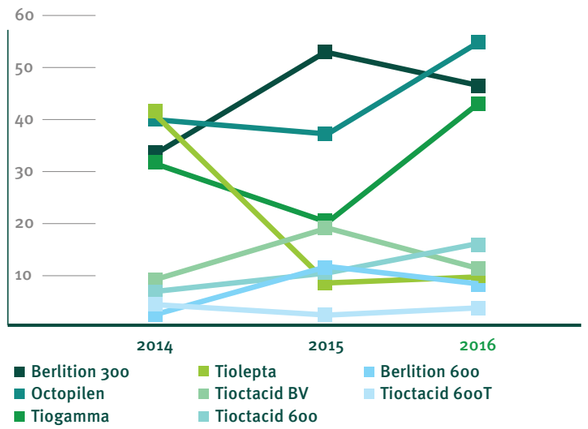
11 Hereinafter, IMS Health data is used to characterize the competitive environment (sales as compared with those of competitors, market share, etc.)

12 Hereinafter, PrIndex "Monitoring of Pharmaceutical Use".

Biosulin is the fourth best seller in the portfolio of own products. Sales in 2016 were RR 602 million, or 0.9 million units. Thanks to this brand, Pharmstandard is fourth-largest by revenue among all insulin manufacturers on the market and leads the market among domestic companies. Biosulin is the eighth best-selling brand, showing 25% growth in sales compared to 2015. It should be noted that the insulin market as a whole is currently seeing a shift from foreign to Russian manufacturers.

Octolipen is number five in the portfolio of own products and third among promoted products. In 2016 sales were over RR 600 million (1.9 million units) demonstrating 23% growth in money terms and 8% growth in terms of units sold. Octolipen leads the lipoic acid commercial market in terms of units sold, with a 41% market share, and is growing in absolute terms and increasing its market share. Octolipen is second in terms of sales revenue, with a 24% market share in its category, but is growing strongly in absolute terms and increasing its market share. In the category of lipoic acid for oral use, the 600-mg segment is the largest in money terms. Octolipen leads the segment in terms of units sold, with almost a 50% market share (according to IMS Health data). According to Ipsos Comcon, Octolipen is the lipoic acid most frequently prescribed by endocrinologists.

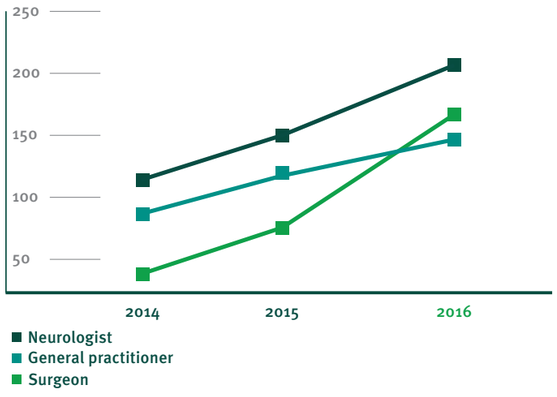
Octopilen prescriptions by endocrinologists, thousand per year



Inhalyptum is the sixth best seller in the portfolio of own products, with sales revenue of RR 552 million in 2016 (19% growth) and over 11 million units sold (34% growth).

Artrozan is among the top five promoted products in terms of sales revenue in 2016: RR 462 million (53% growth), more than 2 million of units sold (33% growth). Artrozan is also one of the top five drugs in the Meloxicam category (in terms of both revenue and units sold) and has shown growth in sales for three years running. This category is characterized by a high rate of growth in terms of units sold and a low rate of growth in revenue (10% and 4%, respectively), which means a decreasing average retail price. Artrozan's 23% growth in revenue is far ahead of the category as a whole, and its market share has increased from 6.8% in 2013 to 12.1% in 2016. This has to do with the fact that the Company was able to raise the retail price, while staying in the low price range characteristic of Artrozan. According to Ipsos Comcon, doctors in all areas of specialization (neurologists, surgeons, general practitioners) are putting Artrozan to an increasing number of uses.

Artrosan prescriptions, thousand per year

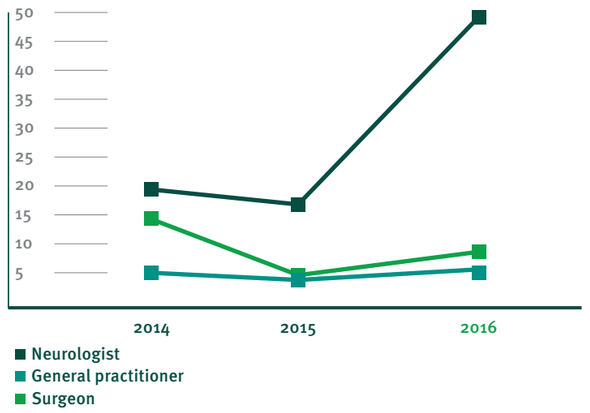


In 2015,we began producing Tuberculin at our plant in Ufa and also at LEKKO. Whereas Pharmstandard's sales of Tuberculin in 2014 totaled RR 405 million, all of it manufactured by Pharmstandard-Biolek PJSC, sales in 2016 came to RR 451 million with only 30% produced by Pharmstandard-Biolek PJSC.

Sales of Ferrohematogen grew 40% in 2016 to RR 363 million (31.7 million units). This increase has to do with the market release of the new Ferrohematogen bars for children, which are being actively promoted by pharmacy chains and via Internet advertising campaign. This new product accounted for 20% of the brand's sales in 2016. In 2016, according to IMS Health data, the Ferrohematogen brand led its category in terms of revenue, capturing a 35.3% market share. Its share in terms of units sold was 26% (+5%). In 2016,the Hematogen category as a whole saw a 5% drop in terms of units sold and a negligible decline in revenue. The Ferrohematogen brand, however, demonstrated strong growth for the third year in a row.

In 2016, according to IMS Health, the Gabapentinoid category fell 63% in volume terms and 69% in value terms due to the sharp decline in the Pregabalin group (-79% in volume and -77% in value terms). At the same time, our own Convalis (INN Gabapentin) showed over 200% growth in sales in terms of both revenue (+226% from RR 39 million to RR 127 million) and units sold (+206%). Thanks to the growth in sales of Convalis, the Gabapentin group in general showed 105% growth in terms of units sold and 77% in terms of revenue. Convalis is first in the Gabapentin group in terms of units sold (37% market share) and second in terms of sales revenue (29% market share). According to Ipsos Comcon , Convalis is the most prescribed by doctors (neurologists, surgeons, general practitioners) in Gabapentin group.

Convalis prescriptions, thousand per year



New own products launched in 2016

In 2016,Pharmstandard's plants set up production of their own products and third party products under the contract manufacturing. For more details on the contract manufacturing, see Section 3.3.B Business partners and contract manufacturing.

In 2016,Pharmstandard companies received registration certificates for production of six own products:

№	Product	Plant
1	Exfotanz film-coated tablets, 160 mg + 10 mg; 160 mg + 5 mg; 80 mg + 5 mg	Pharmstandard-Tomskhimpharm OJSC
2	Gliclazide modified-release tablets, 30 mg, 60 mg	Pharmstandard-Tomskhimpharm OJSC
3	Corvalol Phyto tablets (without phenobarbital)	Pharmstandard-Leksredstva OJSC
4	Gendevit food supplement - Pharmstandard dragee	Pharmstandard-UfaVITA OJSC
5	Undevit food supplement - Pharmstandard dragee	Pharmstandard-UfaVITA OJSC
6	Clarithromycin film-coated sustained-release tablets, 500 mg	Pharmstandard-Tomskhimpharm OJSC

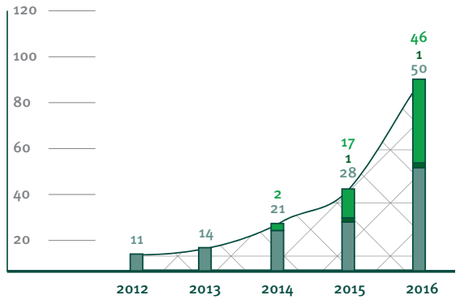
3.3.B Business partners and contract manufacturing

Pharmstandard produces, promotes and sells pharmaceuticals in cooperation with many top international and local manufacturers, such as Abbott, AbbVie, Celgene, CHIESI, GE HealthCare, Genzyme, Johnson & Johnson, Kemwell Biopharma, MARVEL BIOSCIENCE, Merck, Novartis, Roche, Servier, Generium, Biocad, Nativa and Sanofi-Aventis, maximally localizing their products in order to make them more affordable for customers in Russia.

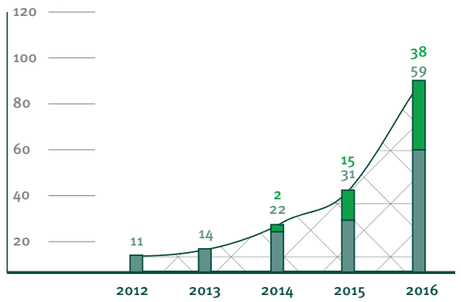
In 2016 Pharmstandard completed localization of new products, including new product forms, of the following companies: Johnson & Johnson, Servier, Merck, Celgene, Novartis, Roche and GE Healthcare.

In only the last five years, at its plants Pharmstandard have localized production of 90 third-party companies. In accordance with the strategy of import substitution, the depth of localization is being increased: while only secondary packaging was done in 2013, in 2016 saw full-finish production of 46 of 97 localized products and one product of primary and secondary packaging. Meanwhile, we are developing relations with both foreign and domestic partners.

Depth of localization at Pharmstandard companies in 2010-2016 (number of products)*



Localization at Pharmstandard facilities in 2012-2016, by foreign and domestic manufacturers (number of products)*



* Including OTCPharm pharmaceutical products localized in 2015. Pharmaceuticals transferred to OTCPharm were regarded as own products in 2014.

In 2016, our plants manufactured 9 of the top 15 TPPs promoted and sold by the Group. There are plans to localize another two of these pharmaceuticals.

In the future, the Company plans to continue expanding the range and depth of localization of foreign partners' pharmaceuticals. The assortment of pharmaceutical products will be substantially expanded in such areas as endocrinology, oncology, oncohematology, pulmonology, hepatitis, multiple sclerosis and rheumatology. The Company plans to pursue projects involving the development of new molecules in cooperation with foreign partners.

3.3.C Vital and essential drugs in 2016-2017

The regulation of prices for pharmaceuticals in the list of vital and essential drugs (hereinafter, "VED") is based on principles and methods legislated in 2015:

- Federal Law No. 61-FZ "On Circulation of Medicines" dated 12 April 2010;
- The Methodology for calculating maximum sale prices set by pharmaceutical manufacturers for medicines on the VED list (hereinafter, the "Methodology") (approved by Decree No. 979 of the Russian Government dated 15 September 2015);
- The Rules for the state registration and reregistration of maximum sale prices set by pharmaceutical manufacturers for medicines on the VED list (hereinafter, the "Rules") (approved by Resolution No. 865 of the Russian Government dated 29 October 2010,as amended by the Resolution No. 979 of the Russian Government dated 15 September 2015).

Regulation No. 2724-r of the Russian Government dated 26 December 2015,made changes in the VED list for 2016, effective 1 March 2016. Before 1 March 2016, the VED list approved by Regulation No. 2782-r of the Russian Government of 30 December 2014 applied.

Key aspects of the state regulation of VED pricing and circulation in 2016:

In 2016 the Federal Antimonopoly Service carried out the first stage of an international comparative study of prices for expensive pharmaceuticals. Based on its findings, the Service appealed to manufacturers to voluntarily reduce the registered maximum sale prices of drugs included in the "7 Nosologies" program to the minimum level in other countries. All companies that received the appeal lowered their maximum sale prices to the minimum level.

Registration/re-registration of maximum sale prices for VED in 2016

Re-registration of maximum sale prices in 2016,was conducted with due regard to the anticipated inflation rate (6.4%) established by Federal Law No. 359-FZ "On the Federal Budget for 2016 and the Planning Period of 2017,and 2018" dated 14,December 2015. In accordance with the law, Pharmstandard companies re-registered 39 maximum sale prices for VED (excerpts were obtained from the reregistration order) for 24 international non-proprietary names (INN) / 26 trade names.

Of these 39 reregistered VED prices, 35 were for own products and 4,for TPPs (Atimos and MabThera).

Four maximum sale prices for TPPs in the VED list were reduced (2 INNs/2 trade names).

Regulation No. 2724-r of the Russian Government dated 26 December 2015 made changes in the VED list for 2016, effective 1 March 2016. Before 1 March 2016, the VED list approved by Regulation No. 2782-r of the Russian Government of 30 December 2014 applied.

Some changes in the VED list effective 1,March 2016,relate to pharmaceuticals produced by Pharmstandard Group:

1) Pharmaceuticals with INN Telaprevir (trade name: Incivo, made by Pharmstandard-UfaVITA) were excluded;

2) Two new INNs were added: Bacteria Allergen (trade name: BIOLEK Tuberculin PPD-L, made by Pharmstandard-UfaVITA, LEKKO), Beclomethasone + Formoterol (trade name: Foster, made by Pharmstandard-Leksredstva).

3) A new pharmaceutical form was added - "solution for subcutaneous injection" (INN Rituximab, trade name: MabThera).

In 2016, steps were undertaken to register 38 maximum sale prices (with update of the State Register) for pharmaceuticals manufactured or owned by companies of Pharmstandard Group (12,INNs/12,trade names).

INN	Brand name	Number of product forms affected by registration in 2016:		
		maximum sale prices registered	maximum sale prices re-registered	maximum sale prices reduced
Bacteria Allergens	BIOLEK Tuberculin PPD-L	7		
Aminophylline	Euphylline		1	
Ascorbic acid	Ascorbic acid		1	
Acetylsalicylic acid	Acetylsalicylic acid		1	
Bedaquiline	Sirturo	1		
Beclomethasone + Formoterol	Foster	1		
Gadodiamide	Omniscan	3		
Desmopressin	Minirin	2		
Digoxin	Digoxin	1		
Dornaze alpha	Pulmozyme			1
Soluble Insulin [human gene engineered]	Biosulin R		1	
Insulin isophane (human gene engineered)	Biosulin N		1	
Interferon alpha-2b	Altevir		3	
Human leukocyte Interferon	Human leukocyte Interferon		1	
Iohexol	Omnipaque	10		
Calcium and magnesium asparaginate	Asparcam		1	
Calcium gluconate	Calcium gluconate		1	
Clarithromycin	Clarithromycin	4		
Co-Trimoxazole	Co-Trimoxazole		1	
Co-Trimoxazole [Sulfamethoxazole + Trimethoprim]	Co-Trimoxazole		1	
Lenalidomid	Revlimid			4
Lidocaine	Lidocaine		1	
Losartan	Bloctran		3	
Metronidazole	Metronidazole		2	
Nitroglycerin	Nitroglycerin		1	
	Nitrospray		1	
Pancreatin	Pancreatin		1	
Paracetamol	Paracetamol		2	
	Paracetamol for children		2	
Rituximab	MabThera	2	3	
Lipoic acid	Octolipen	3	2	
Topiramate	Toreal	2		
Trihexyphenidyl	Cyclodol		1	
Filgrastim	Neupomax	2	2	
Formoterol	Atimos		1	
Phospholipids + glycyrrhizic acid	Phosphogliv		1	
	Phosphogliv forte		1	
Enalapril	Renipril		2	
TOTAL:		**38**	**39**	**5**

VED in Pharmstandard Group's sales structure

As of 1 March 2017, Pharmstandard Group has 534 SKUs (both own products and TPPs) for 142 INNs (for the entire range of product forms and dosages) with registered VED maximum sale prices.

Revenues from sales of VEDs account for 72% (RR 35,307 million) of revenues on the Russian domestic market.

Own VED sales in 2016 reached RR 5,870 million or 44% of total sales of Pharmstandard Group's own products. As compared with 2015, own VED sales increased by 24% (RR 1,146 million).

The sales of the third-party VED in 2016 amounted to RR 29,437 million, or 83% of TPP sales.

As compared with 2015, third-party VED sales rose 26% (RR 6,001 million).

The number of VED names (including all pharmaceutical forms and dosages) sold by Pharmstandard in 2016 increased by 25% to 213 items in 2016, as compared with 171 in 2015.

Among all Pharmstandard VEDs the largest share is with prescription drugs: 92% of sales revenues in 2016.

Type of product	OTC/ RX	2015		2016		16/15	
		Number of products	% of total	Number of products	% of total	Number of products	%
All (own + TPP)	OTC	14	8%	16	8%	2	14%
	RX	157	92%	197	92%	40	25%
TOTAL:		**171**	**100%**	**213**	**100%**	**42**	25%
Own products	OTC	14	15%	14	18%	0	0%
	RX	78	85%	64	82%	-14	(18%)
TOTAL:		**92**	**100%**	**78**	**100%**	**-14**	(15%)
TPP	OTC	0	0%	2	1%	2	0%
	RX	79	100%	133	99%	54	68%
TOTAL:		**79**	**100%**	**135**	**100%**	**56**	71%

Price changes in 2017

As of the date of the Annual report, the regulatory framework for the registration/re-registration of maximum sale prices for VEDs was based on principles/methods legislated in 2012 and amended in 2015.

Under Government Regulation No. 2885-r of 28 December 2016, the VED List for 2017 remains unchanged.

The Federal Antimonopoly Service recommended manufacturers to reduce voluntary the registered maximum sale prices of drugs included in the Seven Nosologies program, to the minimum price level in other countries. As a result of this maximum sale prices were reduced not only for reference VEDs, but for substitutes as well.

Re-registration of maximum sale prices for VEDs in 2017

In compliance with the law, Pharmstandard Group companies have submitted or plan to submit documents to the Ministry of Health for the re-registration of 31,prices (for products manufactured or owned by Pharmstandard companies) within the anticipated inflation rate (21 INNs/24 trade names). The anticipated inflation rate established by the Federal Law No. 415-FZ "On the Federal Budget for 2017,and the Planning Period of 2018 and 2019" dated 19 December 2016 is 4.0%.

INN	Brand name	Number of product forms affected by registration in 2017
Alvelon-MF	Alvelon-MF	1
Aminophylline	Euphylline	1
Ascorbic acid	Ascorbic acid	1
Acetylsalicylic acid	Acetylsalicylic acid	1
Digoxin	Digoxin	2
Soluble Insulin [human gene engineered]	Biosulin R	1
Insulin isophane (human gene engineered)	Biosulin N	1
Human leukocyte Interferon	Human leukocyte Interferon	1
Calcium and magnesium asparaginate	Asparcam	1
Calcium gluconate	Calcium gluconate	1
Clarithromycin	Clarithromycin	1
Co-Trimoxazole	Co-Trimoxazole	1
Levofloxacin	Levofloxacin	3
Lidocaine	Lidocaine	1
Losartan	Bloctran	2
Metronidazole	Metronidazole	1
Nitroglycerin	Nitroglycerin	1
	Nitrospray	1
Pancreatin	Pancreatin	1
Paracetamol	Paracetamol	2
	Paracetamol for children	1
Lipoic acid	Octolipen	2
Phospholipids + glycyrrhizic acid	Phosphogliv	1
	Phosphogliv forte	1
Enalapril	Renipril	2
TOTAL:		**32**

3.4 Marketing and promotion

During the first six months of 2016, Pharmstandard's marketing and promotion activities were conducted by the following three specialized business units:

- Marketing and Promotion of Hepatic Drugs in Russia
- Marketing and Promotion of Cardiac Drugs in Russia
- Marketing and Promotion of Neurology Drugs in Russia

This approach, while providing a high level of expertise within each specialized group, was suboptimal, as it did not allow Pharmstandard to unlock the existing potential and reach out to a wider target audience without tapping additional resources. Thus, in July 2016,marketing and promotion business units were restructured.

Currently, there are two separate departments — one dealing with the marketing function, and the other with the promotion function.

The Marketing Department comprises two groups, which are responsible for managing the Company's original and generic brands, and for handling projects conducted in partnership with other companies.

The Promotion Department is split into three groups, each with a dedicated focus on a specific target audience. The new approach has helped to widen the reach to unique specialists within each target audience (especially when communicating with therapists and pharmacies), optimize the portfolio of promoted products across each line, and attract new target audiences.

After the restructuring, the headcount of both departments has not changed markedly, with more than 320,people employed as of 31 December 2016.

Marketing and promotion functions remain focused on promoting both original drugs and branded generics among medical professionals, pharmaceutical personnel and end consumers.

The 2016 list of promoted drugs included 12 brands and over 20 dosage forms.

Unique brands
Akorta
Artrozan
Bloctran GT
Bloctran
Combilipen
Combilipen tabs
Convalis
Nitrospray
Octolipen
Phosphogliv capsules
Phosphogliv lyophilisate
Phosphogliv forte

Revenues from promoted drugs (excluding third-party drugs) were RR 4.6 billion, or 8.6% of total revenue from pharmaceutical sales in 2016.

The strategic development of marketing and promotion functions in 2016,was based on the following principles:

- Maintaining a close focus on the current needs of healthcare practitioners with a view to expanding specialized product portfolios in the long term

/ Achieving improved performance of promotion teams by harnessing advanced analytics and standardized algorithms in such areas as customer monitoring, daily and monthly activity planning, following up on marketing investments, and customer sales planning with follow-up activities
/ Providing employees with continuous multi-level training to promote deep subject-matter expertise and essential business skills required to achieve business objectives (with distance learning remaining an important training method in 2016, the Company was in a position to offer effective and regular training while optimizing operating costs).

These principles enable Pharmstandard to produce robust long-term plans for driving sales and profit margins of its promoted products.

The Company's promotion strategy in 2016 focused on the following own brands: Phosphogliv, Combilipen, Octolipen, Artrozan and Convalis.

Phosphogliv and Combilipen were among 100,top-selling domestic brands and topped the sales chart of the Company's own products in 2016. Convalis was the fastest growing own brand in terms of revenue, up 226% from the previous year.

For details about own brands, see Section 3.3 A Portfolio of own products.

3.5 Government procurement

The Company's key business priorities include building strong partnerships with global market leaders to supply their products to Russia under national and regional drug procurement programs.

According to IMS Health, Russia's government procurement market expanded by 3% to reach RR 317 billion in 2016. The growth was largely driven by contracts under regional procurement programs (+12%) and the PDBP (+10%). More funding was also made available under the Seven High-cost Nosologies Federal Program (7% up). The hospital segment shrank by 3%.

Sales structure and dynamics in the government procurement market in value terms, RR billion including VAT

SEGMENT	2015	2016	2016 SHARE	16/15
Hospital segment	160	154	49%	(3%)
PDBP	52	57	18%	10%
7 Nosologies	47	50	16%	7%
Regional-level benefit	49	55	17%	12%
TOTAL	**308**	**317**	**100%**	3%

If measured in volume terms, the government procurement market shrank by 6% in 2016, mainly due to lower sales in the hospital segment.

Sales structure and dynamics in the government procurement market in volume terms, million packs

SEGMENT	2015	2016	2016 SHARE	16/15
Hospital segment	672	617	83%	(8%)
PDBP	79	76	10%	(3%)
7 Nosologies	3	3	0%	0%
Regional-level benefit	43	49	7%	16%
TOTAL	**797**	**746**	**100%**	(6%)

Key players

The top five players in Russia's government procurement market, RR billion:

COMPANY	2015	2016	2016 SHARE	16/15	2015 PLACE	2016 PLACE
SANOFI-AVENTIS	16.0	15.3	4.8%	(5%)	2	1
BIOCAD	8.2	13.8	4.3%	+68%	9	2
ROCHE	19.0	13.2	4.1%	(31%)	1	3
ABBVIE	9.0	11.7	3.7%	+29%	7	4
NOVARTIS	9.9	10.6	3.3%	+6%	4	5
TOTAL:	**62.1**	**64.5**	**20.3%**	+4%		
OTHER PLAYERS	**245.6**	**252.6**	**79.7%**	+3%		

Under the partnership agreements with the above companies, Pharmstandard Group is involved in manufacturing (Mabthera, Actemra, Tasigna, Pulmozyme and Cerezyme) and distribution of a significant volume of their pharmaceutical products.

According to IMS Health, Pharmstandard's share in the sales of top 50,medical products in 2016 totaled 31%, or RR 35.9 billion. In 2016 Pharmstandard recorded a 24% increase in its sales, which was far above the growth rates of the entire market and the top 50 segment in particular, standing at 3% and 10%, respectively.

№	TRADE NAME	CORPORATION	2015	2016	2016 SHARE	16/15
1	Revlimid (lenalidomide)	CELGENE	4.8	8.8	2.8%	86%
2	Soliris (eculizumab)	ALEXION PHARMA SW	4.6	5.8	1.8%	26%
3	Lantus solostar (insulin glargine)	SANOFI-AVENTIS	5.1	5.7	1.8%	11%
4	Kaletra (lopinavir*ritonavir)	ABBVIE	5.0	5.4	1.7%	7%
5	Acellbia (rituximab)	BIOCAD	5.4	5.4	1.7%	0%
6	Natrium chloratum (sodium)	-	5.1	4.6	1.5%	(9%)
7	Prevenar 13 (vaccine, pneumococcal)	PFIZER	4,4	4.4	1.4%	(1%)
8	Herceptin (trastuzumab)	ROCHE	6.0	3.7	1.2%	(39%)
9	Boramilan fs (bortezomib)	F-SYNTEZ	5.4	3.6	1.1%	(34%)
10	Remicade (infliximab)	MERCK	3.3	3.3	1.0%	0%
11	Aksoglatiran fs (glatiramer acetate)	F-SYNTEZ		2.8	0.9%	
12	Humira (adalimumab)	ABBVIE	1.9	2.6	0.8%	36%
13	Symbicort turbuhal (budesonide*formoterol)	ASTRAZENECA	2.6	2.4	0.8%	(5%)
14	Coagil-vii (eptacog alfa (activated))	GENERIUM	2.7	2.4	0.7%	(13%)
15	Levemir flexpen (insulin detemir)	NOVO NORDISK	1.7	2.2	0.7%	30%
16	Herticad (trastuzumab)	BIOCAD		2.2	0.7%	
17	Nplate (romiplostim)	AMGEN	2.2	2.2	0.6%	2%
18	Mabthera (rituximab)	ROCHE	3.5	2.0	0.6%	(42%)
19	Reyataz (atazanavir)	BRISTOL MYERS SQUIBB	2.0	2.0	0.6%	1%
20	Elaprase (idursulfase)	SHIRE	2.0	2.0	0.6%	0%
21	Isentress (raltegravir)	MERCK SHARP DOHME	1.7	2.0	0.6%	14%

Production at Pharmstandard facilities
Distribution by Pharmstandard

№	TRADE NAME	CORPORATION	2015	2016	2016 SHARE	16/15
22	Genfaxon (interferon beta-1a)	LABORATORIO TUTEUR	2.4	1.9	0.6%	(21%)
23	Rebif 44 (interferon beta-1a)	SERONO	0.9	1.7	0.5%	90%
24	Viekira pak (dasabuvir* ombitasvir* paritaprevir* ritonavir)	ABBVIE	0.3	1.7	0.5%	569%
25	Avastin (bevacizumab)	ROCHE	3.1	1.6	0.5%	(47%)
26	Velcade (bortezomib)	JOHNSON & JOHNSON	2.4	1.6	0.5%	(33%)
27	Advate (octocog alfa)	BAXTER INT	0.3	1.6	0.5%	500%
28	Nexavar (sorafenib)	BAYER HEALTHCARE	1.5	1.6	0.5%	6%
29	Zoladex (goserelin)	ASTRAZENECA	1.5	1.5	0.5%	0%
30	Octanate (factor viii)	OCTAPHARMA	1.6	1.5	0.5%	(6%)
31	Sovigripp (vaccine, influenza)	MICROGEN	1.1	1.5	0.5%	37%
32	Kemeruvir (darunavir)	PHARMASYNTEZ	0.8	1.5	0.5%	84%
33	Tasigna (nilotinib)	NOVARTIS	1.3	1.4	0.5%	10%
34	Pulmozyme (dornase alfa)	ROCHE	1.3	1.4	0.5%	8%
35	Sutent (sunitinib)	PFIZER	1.2	1.4	0.4%	24%
36	Imbruvica (ibrutinib)	JOHNSON & JOHNSON	0.2	1.4	0.4%	675%
37	Intelence (etravirine)	JOHNSON & JOHNSON	1.2	1.4	0.4%	15%
38	Copaxone teva (glatiramer acetate)	TEVA	5.1	1.4	0.4%	(73%)
39	Grippol plus (azoximer*vaccine, influenza)	PETROVAX	0.2	1.4	0.4%	498%
40	Tracleer (bosentan)	ACTELION PHARMAC.	1.4	1.3	0.4%	(1%)
41	Infibeta (interferon beta-1b)	GENERIUM	1.1	1.3	0.4%	25%
42	Curosurf (poractant alfa)	CHIESI PHARM	1.4	1.3	0.4%	(9%)
43	Afinitor (everolimus)	NOVARTIS	1.3	1.3	0.4%	3%
44	Eralfon (epoetin alfa)	SOTEX	1.2	1.3	0.4%	7%
45	Octofactor (moroctocog alfa)	GENERIUM	0.0	1.3	0.4%	4,131%
46	Erbitux (cetuximab)	SERONO	0.9	1.2	0.4%	32%
47	Enbrel (etanercept)	PFIZER	1.0	1.2	0.4%	28%
48	Novorapid flexpen (insulin aspart)	NOVO NORDISK	0.9	1.2	0.4%	33%
49	Taxacard (paclitaxel)	BIOCAD	0.5	1.2	0.4%	152%
50	Clexan (enoxaparin sodium)	SANOFI-AVENTIS	1.3	1.2	0.4%	(9%)
	TOTAL:		**106.4**	**116.8**	**36.8%**	10%
	Other		201.4	200.3	63.2%	(1%)

Production at Pharmstandard facilities
Distribution by Pharmstandard

In 2016, 12 out of the top 15 third-party products (TPP) were sold by Pharmstandard Group in the government procurement market. Revenue from TPP sales reached RR 36.2 billion, or 59% of the total consolidated revenue of the Group.

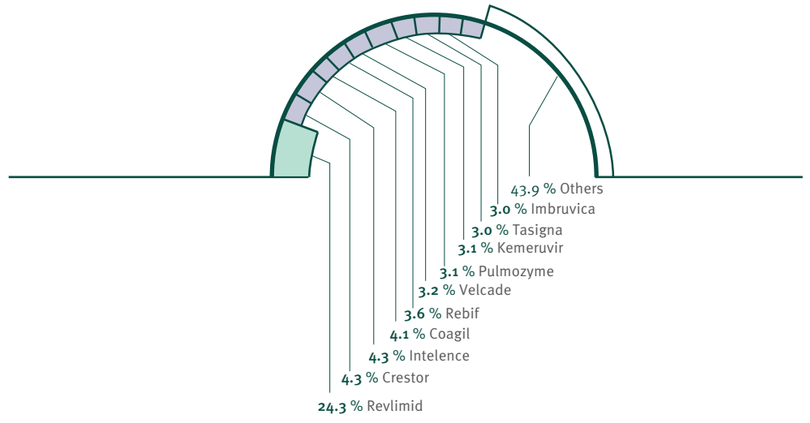
Sales of top 15,TPP in 2015-2016

		2015		2016		16/15	
№	BRAND	MILLION PACKS	RR MILLION	MILLION PACKS	RR MILLION	PACKS	RR
1	Revlimid	0.019	8,135.0	0.023	8,817.2	23.4%	8.4%
2	Crestor			0.533	1,552.3		
3	Intelence	0.051	849.6	0.092	1,546.9	81.5%	82.1%
4	Coagil	0.006	267.0	0.033	1,495.8	456.8%	460.2%
5	Rebif	0.211	1,749.1	0.149	1,304.4	(29.3%)	(25.4%)
6	Velcade	0.019	707.3	0.041	1,157.3	121.2%	63.6%
7	Pulmozyme	0.149	1,081.7	0.158	1,139.0	5.5%	5.3%
8	Kemeruvir	0.049	863.6	0.071	1,118.3	45.2%	29.5%
9	Tasigna	0.008	1,050.6	0.008	1,096.5	0.1%	4.4%
10	Imbruvica	0.000	58.6	0.002	1,094.1	2,152.9%	1,767.4%
11	Erbitux	0.009	149.1	0.061	959.1	546.4%	543.1%
12	Imudon	3.171	893.2	3.209	905.7	1.2%	1.4%
13	Genferon	0.000	-	3.065	842.5		
14	Diaskintest	0.468	586.2	0.677	835.7	44.6%	42.6%
15	Actemra	0.043	642.6	0.046	738.0	5.9%	14.8%
	Top 15,TPP	4.203	17,033.7	8.168	24,602.7	94.3%	44.4%
	Other TPP	27.074	9,374.4	25.045	11,619.1	(7.5%)	23.9%
	Total TPP	31.278	26,408.1	33.213	36,221.8	6.2%	37.2%

Top 10 TPP accounted for 56% of the Group's total TPP sales. All of them, except Crestor, were traded in the government procurement market.

In 2016, Pharmstandard signed a series of agreements with leading pharmaceutical companies to distribute new medical products in Russia. The most meaningful medical products added to the Company's portfolio in 2016 were Tyverb and Votrient (Novartis), Yervoy (Bristol-Myers Squibb) and Adcetris (Takeda).

Product share in the total TPP sales



3.6

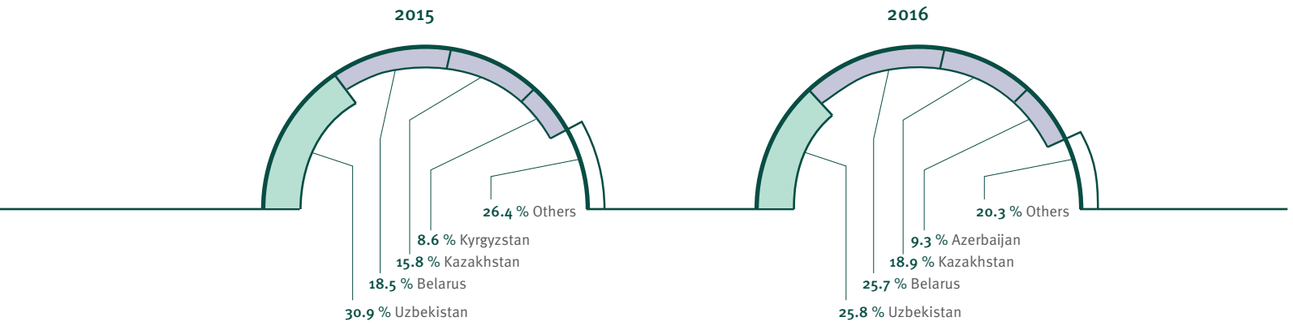
Exports

Pharmstandard Group is focused on increasing and diversifying its exports. Currently, it exports to 16,markets, mainly CIS countries and neighboring FSU countries.

Top export markets for the Group in 2016,included Uzbekistan, which accounted for 25.8% of its total exports, followed by Belarus with 25.7%, Kazakhstan with 18.9% and Azerbaijan with 9.3%.

Pharmstandard's revenue from exports rose 27.8% to RR 488.2 million in 2016,compared with 2015.

Exports by country



Key trends in CIS markets

Republic of Uzbekistan:

- / Uzbekistan's pharmaceutical market totaled USD 1.38 billion in 2016;
- / Annual growth rate for the market has averaged 15%-20%, except for 2015;
- / Antimicrobial (AM) drugs have the largest market share;
- / 170,local producers of drugs and medical products, with this market showing growth;
- / Registered drugs: 1,865 (CIS), 4,494 (non-CIS) and 2,322 (Uzbekistan); registered medical products and equipment: 957.

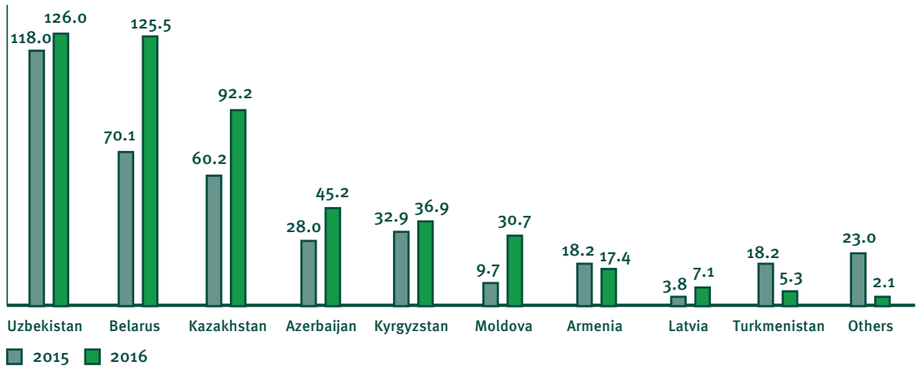
Republic of Belarus:

- / Belarus' pharmaceutical market totaled USD 830.8 million, down 4% from the 2015 level;
- / The market shrank in value terms amid a 2% decrease in imports caused by their replacement with domestically manufactured products and control over domestic drug prices that remained unchanged despite fluctuations in the Belarusian Ruble to US dollar rate;
- / However, Pharmstandard's exports to Belarus increased by 79%, driven by TV advertising, quarterly promotional events and the successful performance of the promotion team;
- / According to the Belarusian Ministry of Health, domestically made medicines accounted for 51.9% of the country's market in value terms in 2016. According to the National Statistics Committee (Belstat), the output of the Belarusian pharmaceutical industry totaled RR 892 million, with state-run companies accounting for 70% of it;
- / Registered drugs as of 1 March 2017: 4,500 including 1,600 produced domestically.

Republic of Kazakhstan:

- / Kazakhstan's pharmaceutical market totaled USD 1.27 billion in 2016;
- / Pharmstandard's exports to Kazakhstan increased by 53% on the back of successful promotion efforts;
- / Kazakhstan has one of the largest hospital segments among CIS countries, which makes up 45%-50% of the entire domestic pharmaceutical market;
- / Kazakhstan adheres to GMP and places a strong focus on the development of the domestic pharmaceutical industry.

Total sales by country in 2015-2016, RR million



COUNTRY	2015, RR MILLION	% OF TOTAL SALES	2016, RR MILLION	% OF TOTAL SALES	16/15, (RR MILLION)	16/15
Uzbekistan	118.0	30.9%	126.0	25.8%	8.0	6.8%
Belarus	70.1	18.3%	125.5	25.7%	55.4	79.0%
Kazakhstan	60.2	15.8%	92.2	18.9%	32.0	53.2%
Azerbaijan	28.0	7.3%	45.2	9.3%	17.2	61.3%
Kyrgyzstan	32.9	8.6%	36.9	7.5%	3.9	11.9%
Moldova	9.7	2.5%	30.7	6.3%	20.9	214.8%
Armenia	18.2	4.8%	17.4	3.6%	-0.8	(4.6%)
Latvia	3.8	1.0%	7.1	1.5%	3.3	86.4%
Turkmenistan	18.2	4.8%	5.3	1.1%	-12.9	(71.1%)
Other	23.0	6.0%	2.1	0.4%	-20.9	(91.0%)
TOTAL EXPORTS	**382.2**	**100.0%**	**488.2**	**100.0%**	**106.1**	27.8%

3.7 Medical equipment

In 2016, revenue from sales of medical equipment amounted to RR 1,806 million, up 15% from the previous year.

Growth in volume terms by equipment category was as follows:

MEDICAL EQUIPMENT SALES (UNITS)	2015	2016	16/15
Steam sterilizers (100L or more)	716	585	(18.3%)
Steam sterilizers (under 100L)	760	314	(58.7%)
Plasma sterilizers	20	18	(10.0%)
Equipment for recycling and disinfection	117	225	92.3%
Water distillers and water collectors	3,850	4,278	11.1%
Washing and disinfection units	102	178	74.5%
Endoscope washing and disinfection devices	16	17	6.3%
Consumables	38,691,931	77,528,455	100.4%
Other	47,327	133,419	181.9%

The growth of sales was driven by a number of factors, with the key factor being the consistent efforts under the Company's development strategy to form a comprehensive product portfolio in order to ensure an ample supply of domestic equipment that would fully satisfy the infection control needs of healthcare providers. Another major driver was continued optimization, both internally and externally, that resulted in significant efficiency gains.

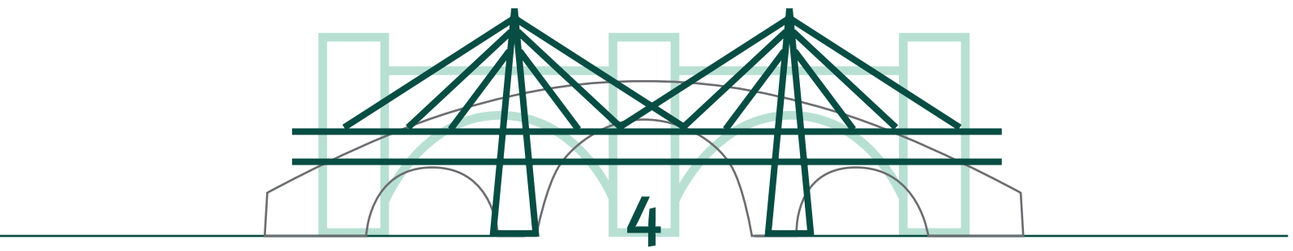
The total market growth in value terms was 27% in 2016. Pharmstandard-Medtechnika LLC, whose market share is calculated as the ratio of wins to the total number of tenders in the infection control equipment segment, has kept its market share at 34%, close to the 2015 level, confirming its position as the largest supplier.

Pharmstandard-Medtechnika LLC has increasing its market share for several years in a row, with the most notable achievements in 2016 being the following:

- / Expansion of the product portfolio with a new range of equipment that has no counterparts in the domestic market and may serve as a quality substitute for modern equipment manufactured abroad (the range of the company's import-substitution products has now been fully formed)
- / Continued development of expertise in complex integrated equipment projects, with a number of major projects to prepare and equip centralized sterilization units for various healthcare institutions, including perinatal centers throughout Russia, successfully completed
- / Strengthening of the sales team and relations with partners and dealers in order to support the launch of new products
- / Active engagement in medical waste disposal programs and maintaining the market share in this segment, with comprehensive solutions to support integrated on-site decontamination added to the existing service offering
- / Continued efforts toward increasing customer satisfaction and loyalty through improved service quality

Pharmstandard-Medtechnika LLC intends to further develop its business and expand presence in the relevant market segment. Activities planned for 2017 include the following:

- / Proactively pursue new products that have no counterparts in the domestic market, including endoscope processing and storage systems.
- / Promote an integrated infection control solution for healthcare providers leveraging fully on cutting-edge domestic technologies and equipment, and establish national reference centers to define a common protocol.
- / Further optimize the sales and service functions as part of ongoing efforts to improve customer satisfaction through strengthening ties with authorized service centers, automating business processes and enhancing quality control.



Corporate governance

Corporate governance

The Company's corporate policy is based on a principle of respect for the rights and legitimate interests of its shareholders, enables the Company to deliver strong performance translated into greater business value, new jobs and the Company's financial stability and profitability.

Principles of trust between all people involved in corporate relationships drive to the Company's successful business performance. The principles of the Company's corporate policies are designed to foster trust in relations at the governance level.

Shareholding structure

SHAREHOLDING STRUCTURE AS OF 31 DECEMBER 2016:	
Augment Investments Limited	36,355,683 shares (96.2%)
Pharmstandard – Leksredstva OJSC	1,436,920 shares (3.8%)
TOTAL NUMBER OF ORDINARY SHARES ISSUED BY THE COMPANY	**37,792,603 SHARES (100%)**

On 22 June 2016, the Company received a mandatory offer from Augment Investments Limited, registered at Demokritiu, 15 Panaretos Eliana Complex 104, P.O. Box 4041, Potamos Germasogias, Limassol, Cyprus, to purchase the issuer's securities.

The sender of the mandatory offer and its affiliates held the following stake in the issuer: 86.11%, of which 82.31% was held by Augment Investments Limited and 3.80% by Pharmstandard – Leksredstva OJSC, its affiliate.

On 14 October 2016, the Company received notification about Mandatory squeeze-out from Augment Investments Limited for the purchase of rest of the shares. Augment Investments Limited became entitled to send the Mandatory squeeze-out after the Company's shareholders had accepted the mandatory offer from Augment Investments Limited to purchase the Company's shares whereby Augment Investments Limited purchased 12.01% of the Company's ordinary registered shares to hold a total of 37,081,092 ordinary registered shares, including the shares acquired by Augment Investments Limited and its affiliates previously, making up 98.12% of the Company's ordinary registered shares.

On 29 November 2016, GDRs for the Company's ordinary shares (four GDRs representing one share) were delisted from the Official List of the UK Financial Conduct Authority and the admission of the GDRs to trading on the London Stock Exchange's main market was canceled.

On 8 December 2016, the Company's securities were transferred from the second to third level of securities admitted to trading on Moscow Stock Exchange MICEX-RTS PJSC.

On 12 December 2016, the Company announced the completion of the procedure of mandatory squeeze-out whereby Augment Investments Limited became the holder of 100% in the Company, including:

1) 96.2% (36,355,683 shares) held directly; and

2) 3.8% (1,436,920 shares) held indirectly, through Pharmstandard – Leksredstva OJSC, an entity under the control of Augment Investments Limited.

General Shareholders' Meeting

The General Shareholders' Meeting is the Company's highest governing body. The date and location of the General Meeting is determined by decision of the Board of Directors and is announced in a press release. The Annual General Shareholders' Meeting is held no earlier than two months and no later than six months after the end of the financial year. Shareholders (a shareholder) that own(s) a combined total of least 2% of the Company's voting shares may propose items for the inclusion in the agenda of the Annual General Shareholders' Meeting and nominate candidates for the Board of Directors and Audit Commission of the Company.

Extraordinary General Shareholders' Meetings are held by decision of the Board of Directors at its own initiative or pursuant to a request by the Audit Commission, the Company's auditor or shareholders (a shareholder) that own(s) at least 10% of the Company's voting shares on the date of the request.

A General Shareholders' Meeting must be announced no later than thirty days before its scheduled date. In cases stipulated by law, a General Shareholders' Meeting must be announced no later than seventy days before its scheduled date. The competence of the General Shareholders' Meeting and the decision-making procedure are established by law and the Company's Charter.

Meetings held in 2016

The Company's Annual General Shareholders' Meeting to discuss 2015,results was held on 20 May 2016 in the city of Dolgoprudny, Moscow Region (Minutes No. 26 of 20 May 2016). Shareholders owning 67.2108,% of the Company's outstanding voting shares participated. The Annual General Shareholders' Meeting approved the Company's annual report, annual financial statements, profit and loss accounts and the distribution of profit and loss for the 2015,financial year. It elected members of the Board of Directors and the Audit Commission, and approved auditors for 2016 Russian and international audits. It also approved amendments to the Company's Charter, and to the General Shareholders' Meeting Preparation and Conduct Regulation and the Board of Director Regulation.

There were no extraordinary General Shareholders' Meetings in 2016.

Board of Directors

The Company's Board of Directors is responsible for overall management of Pharmstandard's business. The Board of Directors determines priority business areas for the Company and approves business plans and feasibility reports for the Company's investment projects.

The Directors undergo annual appraisal for their competence, experience, performance and alignment with the Company's strategic objectives. The Directors bring economic, financial and business administration expertise and have unique experience in business management in the Russian pharmaceutical industry, financial strategy planning and implementation, and economic system management.

The Board of Directors consists of 11 Directors, and 2 of them are independent directors.

The members of the Board of Directors in 2016-2017:

1. **Aleksandr Archakov** - Independent Director of Pharmstandard JSC since 2015. Mr. Archakov graduated from the 2nd Moscow State Medical University named after N.I. Pirogov (currently known as Russian National Research Medical University). He was Vice President of the Russian Academy of Medical Sciences from 2011 to 2014 and has been serving as academic advisor at Federal State Scientific Institution "Research Institute of Biomedical Chemistry named after V.N. Orekhovich" since 2015.

2. **Vladimir Chupikov** - a graduate of Novosibirsk State University, Mr. Chupikov was General Director of Pharmstandard LLC from 2007 to 2014. Since 2015, he has been Operations Director of the Company and a member of the Management Board.

3. **Sergei Dushelikhinsky** - Commercial Director of the Company since 2006 and a member of the Board of Directors since June 2008. Mr. Dushelikhinsky graduated from Moscow Technical University. He has over 13 years of experience in sales of pharmaceuticals.

4. **Viktor Fedlyuk** - Deputy General Director for Legal Affairs of the Company since 2006 and a member of the Board of Directors since June 2008. Mr. Fedlyuk graduated from the Ukrainian National Academy of Law and has over 18 years of experience in legal practice. From 1996 to 2003, Mr. Fedlyuk worked for Sibneft OJSC.

5. **Georgy Golukhov** - graduated from the 2nd Moscow State Medical University named after N.I. Pirogov (currently known as Russian National Research Medical University). In 2012-2014, Mr. Golukhov served as Minister of the Moscow Government, heading the Moscow Health Department. Since 2014, he has been President of State Healthcare Institution "City Clinical Hospital # 31 of the Moscow Health Department."

6. **Viktor Kharitonin** - Chairman of the Board of Directors since May 2006 and Executive Director of the Company. He also holds director's position on the Boards of directors of OTCPharm PJSC and Tyumen Plant of Medical Equipment and Tools JSC. Mr. Kharitonin graduated from Novosibirsk State University.

7. **Marina Markova** - Deputy General Director for Finance and Economics of Pharmstandard JSC since 2014. Ms. Markova graduated from Moscow Aviation Institute.

8. **Yury Ponomarev** - Independent Director of the Company has been serving as General Director of YuAERO LLC since 2012.

9. **Grigory Potapov** - Chairman of the Management Board and General Director of Pharmstandard JSC since 2015. He graduated from Moscow State University named after M.V. Lomonosov. Mr. Potapov was First Deputy General Director for Economics and Investment of Federal State Unitary Enterprise "Microgen Scientific and Production Association" in 2013-2014.

10. **Andrei Reus** held the position of General Director of Oboronprom United Industrial Corporation OJSC and General Director of Management Company United Engine Corporation OJSC OJSC from 2008 to 2012. In 2012-2013 he held the position of General Director of Constanta Group LLC. Since 2013, Mr. Reus has been General Director of Nonprofit Partnership Eurasian Center for Integrative Studies and Communications.

11. **Ivan Tyryshkin** - graduated from the Russian Academy of Economics. In 2008-2015, he was President of Rusgrain Holding Company OJSC and concurrently served as General Director of Faberge LLC. Currently, Mr. Tyryshkin is Development Director of SKRIN JSC and holds position on the boards in the following companies: Russian self-regulatory organization National Association of Securities Market Participants (NAUFOR), RTS Nonprofit Partnership for the Development of Financial Market, RTS-Tender LLC and Independent Registrar Company JSC.

Meetings held in 2016

The Board of Directors held 74 meetings in 2016, which mainly focused on related party translations. Another focus were decisions regarding the management of the Company's rights arising out of its participation in other entities (through the holding of participatory interests, shares and units), including voting on items on the agenda of these entities' highest management bodies and the approval of internal documents.

Management Board

The Management Board is the Company's collective executive body that acts in the interests of its shareholders in compliance with decisions of the General Shareholders' Meeting and the Board of Directors. The Management Board is responsible for implementing the Company's objectives, growth strategy and policies and managing the Company's day-to-day operations within the competence specified by the Company's Charter.

The key role and responsibilities of the Management Board are:

- / protecting the rights and lawful interests of the shareholders
- / developing proposals for the Company's growth strategy
- / implementing the Company's financial and economic policies, developing solutions for key business operation issues and coordinating the Company's business units
- / improving internal controls and risk monitoring
- / increasing returns from the Company's assets and maximizing the Company's profits

The Management Board is headed by the General Director.

The members of the Management Board:

1. Dmitry Zaitsev, Deputy General Director for Intellectual Property of Pharmstandard JSC since 2007. Mr. Zaitsev graduated from Moscow State University of Railway Engineering and Moscow State Law Academy.
2. Grigory Potapov, General Director and Chairman of the Management Board of the Company. See the curriculum vitae in the Board of Directors section.
1. Vladimir Chupikov, Operating Director of the Company. See the curriculum vitae in the Board of Directors section.

Audit Committee

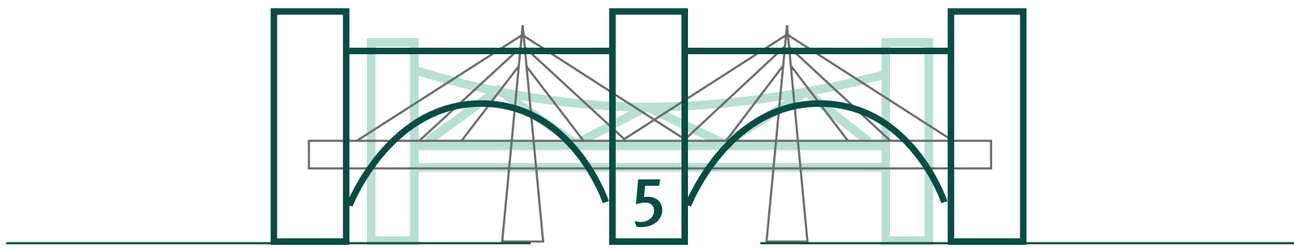
The Audit Committee elected in 2016 includes the following persons:

1. Aleksandr Archakov, Chairman
2. Yury Ponomarev, Member
3. Andrey Reus, Member

The Audit Committee's main purpose is to develop and make recommendations to the Company's Board of Directors on matters concerning:

- / the evaluation of candidates for engagement as the Company's auditor
- / the evaluation of reports issued by the Company's auditor
- / the evaluation of the Company's internal control procedures and the preparation of proposals for improving them

Activities within the competence of the Audit Committee include oversight of the performance of the external auditor and the Company's financial reporting process to develop relevant recommendations to the Board of Directors. When performing its functions, the Audit Committee cooperates with the Company's Auditor, its Audit Commission and, where necessary, business units.



Human capital and corporate and social responsibility

5.1

Human capital

Commitment, dedication and loyalty of our people are crucial for achieving Pharmstandard's ambitious goals.

Recognizing unique contribution our people make to our business, our leaders place a strong focus on human resource management to ensure the efficient use, optimal structure and high motivation of our workforce. Our employees value the stability of their job and expect to be provided with requisite opportunities for professional development, training and career growth. Our continuous business growth in defiance of market volatility enables us to make long-term investments in human capital to create a strong team of professionals and drive our sustainable development.

The Group's headcount rose from 6,450 in 2015 to 6,966 in 2016, largely due to staff expansion in Kursk (Pharmstandard-Leksredstva) and Ufa (Pharmstandard-UfaVITA) as a result of increased specialization and technology accumulation at major production facilities with a view to achieving improved performance, better use of equipment and establishing dedicated competence centers. A growing number of localization projects that we handle jointly with foreign partners further sparked the need for production capacity expansion. Also, the adjustment of information on the headcount of LLC "Pharmstandard" reflected the growth (included in "Other").

COMPANY	HEADCOUNT AS OF 31 DECEMBER 2016
Pharmstandard JSC	1,068
Pharmstandard- Leksredstva OJSC	1,883
Pharmstandard-UfaVITA OJSC	1,939
Pharmstandard-Tomskhimpharm OJSC	505
LEKKO CJSC	272
Pharmstandard-Biolek PJSC	426
Pharmapark LLC	224
TZMOI JSC	101
Biomed JSC	143
Pharmstandard-Medtekhnika LLC	128
Others	277
TOTAL	**6,966**

Most of our workforce is therefore comprised of production staff (c. 5,000), followed by field promotion staff (over 370), while corporate office personnel (650) account for a modest 10% of total headcount, which makes a good balance between management and operations functions.

Pharmstandard Group has a stable workforce at all levels, from junior staff to top managers, with employee turnover in 2016 less than 10%. Only 25% of all employees leaving during the year were made redundant, while the remaining separations were due to personal circumstances (change of residence, pursuit of new career opportunities, etc.)

With almost 80% of our production staff and 50% of administrative staff staying in their jobs for at least three years, we are in the position to guarantee high standards of manufacturing practices and build a robust talent pool of key executive personnel required to preserve our market leadership.

We are keen on retaining our human capital and the competencies that our employee acquire while working with us. As a rapidly growing business, whenever structural changes occur we make every effort to ensure maximum group-wide mobility and give preference to internal candidates over outside applicants. These are the principles our management followed when embarking on a restructuring initiative that affected our marketing and promotion teams, most of whom have managed to fit into the new structure.

At the same time, we maintain a close focus on our people agenda to avoid stagnation, diversify our staff and augment our expertise with new talent coming from other companies.

Management is confident that an appropriate age and gender balance provides the Group with a competitive advantage and allows it to maintain leadership on the domestic market.

Due to the nature of the pharmaceutical industry, most of the Group's employees are women (over 60% of total headcount in 2016). Management's approach to compensation and career development is to provide all employees with equal opportunities regardless of gender. Thanks to this approach, around a third (30%) of senior managers and women' share among middle-level managers increased from 57% in 2014 to 61% in 2016.

We build an environment that values diversity, providing candidates from other countries with equal job opportunities. We have employees from Latvia, Ukraine and a number of CIS countries such as Belarus, Kazakhstan, Armenia, Tajikistan and Uzbekistan.

Our workforce features an even distribution among all age groups, with the average age of 37,years. Management holds great respect for employees approaching the retirement age and provides opportunities for retirees to continue their employment after retirement.

Knowledge and competence play a key role in our industry, and we are proud that over 80% of staff in our head office (Pharmstandard JSC) have higher education, of which more than 45% in medicine or pharmacy, and 20,employees are PhDs.

TThe Company invests heavily in human capital, with professional development being a key area of its investment agenda (over RR 22 million spent in 2016). A strong focus is placed on training across all aspects of GMP compliance.

For the training of our specialists we employ both internal resources as well as third parties (where it is necessary to increase competence or to implement best market practices).

In 2016, more than 100,employees passed training in external organizations and more than 400,people took part in corporate training programs. In addition, the Company introduces online learning programme in a form of standalone courses or webinars. More than 1050 of the Group's staff took part in a remote corporate learning over the last year.

Pharmstandard offers compensation and rewards that attract, retain and motivate employees. Management makes sure that the level of pay is not only linked to the performance of the entire organization, but also takes into account employee's individual contribution and is competitive against other local employers.

Compensation consists mostly of a fixed component that includes base salary and allowances (statutory and performance-related). A variable component includes quarterly and other bonuses, plus an annual bonus payable to senior management. All components of the pay system are designed to motivate and reward excellent performance.

Total compensation is reviewed annually by management to ensure it reflects changes in market conditions and individual performance. The pay level in 2016 increased by 7% on average, which is in line with market indicators.

Apart from remuneration there are other benefits, such as voluntary health insurance, life insurance, partly paid vouchers to children's summer camps. Our costs on social purposes equaled RR 114 mln in 2016.

In the nearest future, we intend to further develop existing incentives, rewards and benefits to create a more flexible system that takes into account the level of responsibility, professional expertise and competence, as well as individual and team performance and employees' personal contribution. This will allow us to better meet the expectations of our employees and become a more attractive employer.

5.2 Corporate social responsibility

For a number of years, the Group's corporate social responsibility activities have been centered on the following three areas:

- / Maintaining employer's responsibility towards employees
- / Maintaining producer's responsibility towards consumers
- / Maintaining a reputation as a responsible business and contributing to civil society and local communities

Pharmstandard Group has a well-deserved reputation as a responsible employer

In doing business, we are focused on compliance with laws and regulations and our internal corporate procedures. This approach is fully applicable to our HR team as it bases its relations with employees on strict adherence to Russian labor laws and respect for human rights, such as the right to information and personal data privacy.

The Group's entities strictly comply with internal procedures for personal data processing, as prescribed by Federal Law No. 152-FZ of 27 July 2006,"On Personal Data" and the Council of Europe's Convention for the Protection of Individuals (ETS No. 108). Prior to signing an employment contract, employees are provided full access to applicable internal rules and regulations; they may also seek expert advice regarding any such rules and regulations at any time during their employment.

Our extensive connections with Western companies operating in Russia make us part of the community governed by internationally recognized core social standards in the area of employment which are enshrined in International Labor Organization's conventions (no child labor, no forced labor and no discrimination at work, freedom of association, right to collective bargaining, occupational health and safety, etc.).

Given the dominance of production and operations staff in the Group's workforce, management is committed to creating a safe working environment in order to protect health and safety of employees. Alongside initiatives aimed at improving the working environment, the Group's entities conduct regular assessments of working conditions and workstations by reference to hazard groups and classes.

Improvements made in 2016 resulted in better working conditions for 748 employees, including 595 women. These activities included improvements in lighting, ventilation, amenities, automation of manual tasks, etc.

There are fixed-site medical stations across the Group's production facilities, with appropriate first-aid kits available in all areas, including office premises. Employees engaged in heavy work or working in harmful conditions undergo mandatory preliminary health checks and periodic medical examinations.

Those employees who do not have inpatient medical cover are provided with a comprehensive VHI package.

All remote workers whose job involves itinerant work also hold life insurance policies that include personal accident and critical illness cover.

In addition to the compensation package, the Company offers significant social benefits, such as meal allowances, lump-sum medical treatment allowances to employees and their family members, financial assistance to retired employees, labor and war veterans, jubilee payments, as well as social support under family and children's programs.

At major production entities in Kursk (Pharmstandard-Leksredstva), Ufa (Pharmstandard-UfaVITA) and Tomsk (Pharmstandard-Tomskhimpharm) management engages actively with trade unions to ensure compliance with collective bargaining agreements covering over 60% of production staff.

The Group's total social spending in 2016 exceeded RR 62 million, with over RR 55 million spent by production entities.

Consumer safety and health are a top priority for our business

At Pharmstandard, we are committed to responsible business practices, as we fully understand our role as one of Russia's major producers of pharmaceuticals and a key contributor to the government program of substituting expensive imported drugs with local medicines.

We are focused on making high-quality products that are designed to effectively address people's health needs and improve the quality of their life. With that in mind, we constantly strive to enhance our production technologies and quality assurance procedures. Over the past two years, we completed the restructuring of our quality assurance function to improve controls across the entire value chain, from ingredient suppliers to end consumers.

Integrity, reliability, and consumer health and safety are especially important in our business, and we actively embrace them in our day-to-day practices. We contribute to the development of Russia's economy by establishing fair, long-lasting and mutually beneficial relationships with our suppliers and customers.

Support for socially significant initiatives

Throughout its corporate history, Pharmstandard has widely supported various socially significant programs and charitable initiatives. Over the past year, we continued cooperation with a number of local charities.

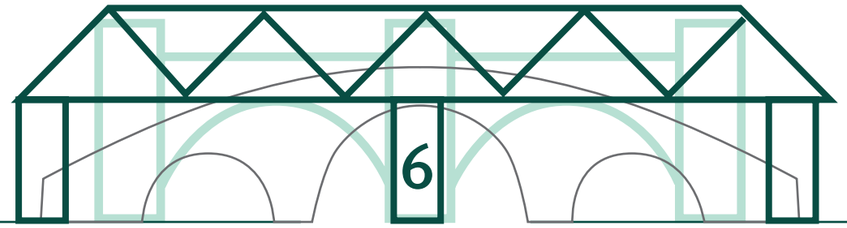
We have provided financial support for Talent and Success, a charitable organization that sees its goal as identifying, developing and supporting children with outstanding academic potential at an early age, helping them to receive education in the natural sciences, music and arts, develop sports skills, and focus on selected subjects.

We have also helped the Gift of Life, a charity founded by actresses Dina Korzun and Chulpan Khamatova to raise money for treating and rehabilitating children with cancer and blood disorders.

Another charity that we have supported is Absolute–Help. The charity runs various social adaptation projects for orphans and graduates of special schools.

Our production entities actively engage with local communities in various charitable initiatives at municipal and regional levels, such as the World of Childhood marathon, target programs for restoring historical sites and monuments, sponsoring socially and economically significant municipal events, etc.

In 2016,the Group granted over RR 157 million on charity.



Management's review and assessment of financial position and performance

6.1 Management's review and assessment of financial position and performance

The following discussion of the financial position and performance should be considered in combination with the consolidated financial statements, notes thereon and other information disclosed in this annual report.

The Company's performance

The Group's revenue structure in 2016,by source in percentage of total revenue (percentages may not add up to 100% due to rounding) was as follows:

- Sales of pharmaceutical products – 85.3%
- Income from contract manufacturing – 7.5%
- Agency fees – 4.2%
- Sales of medical equipment – 2.9%

Pharmaceutical products and medical equipment are primarily sold under direct contracts with wholesale distributors and/or healthcare institutions and public procurement contracts awarded through open auctions.

The table below summarizes and compares the Group's financial performance in 2015-2016 absolute terms (in RR million) and as a percentage of sales.

	PHARMSTANDARD'S CONSOLIDATED RESULTS					
	2016	% OF SALES	2015	% OF SALES	16/15, RR MILLION	16/15
REVENUE	**61,786**	**100.0%**	**47,195**	**100.0%**	**14,591**	**30.9%**
Pharmaceutical products	**52,694**	**85.3%**	**40,951**	**86.8%**	**11,743**	**28.7%**
Prescription drugs (Rx)	7,318	11.8%	6,566	13.9%	752	11.5%
Branded	5,927	9.6%	5,255	11.1%	672	12.8%
Non-branded	1,391	2.3%	1,311	2.8%	80	6.1%
Over-the-counter drugs (OTC)	5,829	9.4%	5,094	10.8%	735	14.4%
Branded	1,956	3.2%	1,615	3.4%	341	21.1%
Non-branded	3,873	6.3%	3,479	7.4%	394	11.3%
Third-party products (TPPs)	36,222	58.6%	26,408	56.0%	9,814	37.2%
Sales of other products and substances	3,325	5.4%	2,883	6.1%	442	15.3%
Contract manufacturing	4,661	7.5%	2,690	5.7%	1,971	73.3%
Agency fees	2,625	4.2%	1,979	4.2%	646	32.6%
Medical equipment	1,806	2.9%	1,575	3.3%	231	14.7%
COST OF SALES	**(40,333)**	**(65.3%)**	**(29,398)**	**(62.3%)**	**(10,935)**	**37.2%**
GROSS PROFIT	**21,453**	**34.7%**	**17,797**	**37.7%**	**3,656**	**20.5%**
Selling and distribution costs	(2,694)	(4.4%)	(2,534)	(5.4%)	(160)	6.3%
General and administrative expenses	(3,244)	(5.2%)	(2,687)	(5.7%)	(557)	20.7%
Net other income and expenses[13]	(5,861)	(9.5%)	4,623	9.8%	(10,484)	(226.8%)

	PHARMSTANDARD'S CONSOLIDATED RESULTS					
	2016	% OF SALES	2015	% OF SALES	16/15, RR MILLION	16/15
Finance income and expenses	1,098	1.8%	479	1.0%	619	129.3%
EBITDA[14]	**10,884**	**17.6%**	**18,234**	**38.6%**	**(7,350)**	**(40.3%)**
PROFIT BEFORE INCOME TAX	**10,753**	**17.4%**	**17,678**	**37.5%**	**(6,925)**	**(39.2%)**
Income tax	(2,750)	(4.5%)	(3,747)	(7.9%)	996	(26.6%)
NET PROFIT	**8,002**	**13.0%**	**13,931**	**29.5%**	**(5,929)**	**(42.6%)**

For the purpose of the comparative analysis and the comparability of 2015 and 2015 data, the Group's 2015 financial performance indicators were adjusted, with the respective changes in the Group's portfolio structure having no impact on the financial performance indicators of the Company. Further analysis was performed taking account of the above adjustments to the 2015 financial statements.

The table above has a separate line for the share of TPP sales in total revenue in 2015 and 2016 to provide a more detailed overview of this business segment. Please note that this approach to portfolio structuring does not affect results for pharmaceutical sales.

Consolidated revenue

The Group's consolidated revenue amounted to RR 61,786 million in 2016 versus RR 47,195 million in 2015. The year-on-year growth of 30.9%, or RR 14,591 million, in 2016 was driven by higher sales of TPPs and higher revenue from contract manufacturing, including under contracts with OTCPharm.

Pharmaceutical products

Sales in this category include fill-finish pharmaceutical products manufactured by the Group's plants and third-party products purchased for resale.

Pharmaceutical sales increased by 28.7% to RR 52,694 million in 2016 from RR 40,951 million in 2015. The shares of own pharmaceutical products, TPPs and substances in the Group's total pharmaceutical sales were 25%, 69% and 6%, respectively, in 2016.

Sales of own pharmaceutical products amounted to RR 16,472 million in 2016, 13% up on the 2015 level. OTC and Rx drugs accounted for 44% and 56% of sales of own pharmaceutical products, respectively.

Sales of Rx drugs in the Group's portfolio increased by RR 752,million, or 11%, to RR 7,318 million. The increase was primarily driven by sales of Combilipen, Artrozan and Biosulin which grew by 24%, 53% and 28% respectively.

Sales of Pharmstandard OTC drugs rose by 14% to RR 5,829 million in 2016. Drugs seeing the largest sale growth were Corvalol (+86%), Phosphogliv (+21%) and Inhalyptum (+36%).

The Group's revenue from the TPP segment rose by RR 9,814 million, or 37%, to RR 36,222 million in 2016 from RR 26,408 million a year earlier. The sales were primarily led by Coagil, Imbruvica and Erbitux. TPPs were the main growth driver of pharmaceutical sales supported by the expansion of the product line and higher sales under public procurement contracts.

Sales of other products and substances increased by RR 442 million, or 15%, from RR 2,883 million in 2015 to RR 3,325 million in 2016.

13 Net other income and expenses comprise other income and expense, including gains and losses from investments in associates.

14 EBITDA is Earnings before Interest, Taxes, Depreciation and Amortization.

Contract manufacturing

Revenue from contract manufacturing went up by RR 1,971 million to RR 4,662 million in 2016. The revenue growth in contact manufacturing is attributable to toll manufacturing, including for OTCPharm PJSC.

Agency fees

Agency fee income totaled RR 2,625 million in 2016, which was 33% up on the 2015 level. The increase in agency fee income can largely be attributed to agency agreements concluded with OTCPharm PJSC for the distribution of its products.

Medical equipment

Sales of medical equipment increased by RR 231 million, or 15%, to RR 1,806 million in 2016,compared with RR 1,575 million the previous year.

Third-party products

For the purposes of greater visibility, sales of TPPs, which are made under federal programs, are treated as a separate business segment.

Top selling TPPs

The top drivers of TPP sales in 2016 were Crestor, absent from the TPP portfolio in 2015, as well as Coagil and Imbruvica whose sales soared by more than 100% in 2016. The growth in Coagil sales was largely due to higher demand under the 7 Nosologies program. Overall, TPP sales rose by RR 9,814 million, or 37.2%, to RR 36,222 million in 2016 against RR 26,408 million in 2015.

7 Nosologies program

The 7 Nosologies program is designed as a government mechanism for providing access to high-cost medicines for patients with rare diseases. Medicines are procured with public funds under a centralized procedure. Apart from Coagil, which was a top selling drug among TPPs in 2016, Revlimid also performed well in the market, with its sales growing by 8%.

	2016		2015		16/15		
PRODUCT	**SALES, RR MILLION**	**% OF TPP SALES**	**SALES, RR MILLION**	**% OF TPP SALES**	**RR MILLION**	**%**	**% OF TOTAL GROWTH**
Coagil	1,496	4.1%	267	1.0%	1,229	460.2%	12.5%
Revlimid	8,817	24.3%	8,135	30.8%	682	8.4%	7.0%
Tysabri	600	1.7%	46	0.2%	554	1,205.8%	5.6%
Velcade	1,157	3.2%	707	2.7%	450	63.6%	4.6%
Pulmozyme	1,139	3.1%	1,082	4.1%	57	5.3%	0.6%
Infibeta	1	0.0%	4	0.0%	(3)	(79.6%)	0.0%
Octofactor	529	1.5%	702	2.7%	(173)	(24.7%)	(1.8%)
Cerezyme	506	1.4%	750	2.8%	(244)	(32.5%)	(2.5%)
Rebif	1,304	3.6%	1,749	6.6%	(445)	(25.4%)	(4.5%)
TOTAL SALES UNDER THE FEDERAL PROGRAM	**15,550**	**42.9%**	**13,442**	**50.9%**	**2,108**	**15.7%**	**21.5%**

Total sales under the 7,Nosologies program increased by RR 2,108 million, or 21.5%, from RR 13,442 million in 2015 to RR 15,550 million in 2016.

Cost of sales

Cost of sales include costs of materials and components, costs involved in purchasing goods from third-party producers, production overheads, direct labor costs, trademark amortization and depreciation of fixed assets, as well as toll manufacturing services.

(RR MILLION)	2016	% OF SALES	2015	% OF SALES	16/15 (RR MILLION)	16/15 (%)
REVENUE	**61,786**	**100.0%**	**47,195**	**100.0%**	**14,591**	30.9%
COST OF SALES	**40,333**	**65.3%**	**29,398**	**62.3%**	**10,935**	37.2%
Materials and components	8,913	14.4%	7,333	15.5%	1,580	21.6%
TPPs	27,139	43.9%	18,257	38.7%	8,882	48.7%
Overheads	2,587	4.2%	2,422	5.1%	165	6.8%
Depreciation and amortization	1,039	1.7%	869	1.8%	170	19.5%
Direct labor costs	655	1.1%	517	1.1%	138	26.6%
GROSS PROFIT	**21,453**	**34.7%**	**17,797**	**37.7%**	**3,656**	20.5%

Cost of sales increased by RR 10,935 million, or 37.2%, from RR 29,398 million in 2015 to RR 40,333 million in 2016. The increase in cost of sales in absolute terms was due to growth in sales.

The combined share of costs of materials and components and costs of TPPs rose insignificantly, by 2%, year-on-year to 89% of total cost of sales in 2016.

The following factors were behind the increase in total cost of sales in 2016:

1) Costs of materials and components grew by 21.6% from RR 7,333 million in 2015 to RR 8,913 million in 2016.

2) Costs of TPPs increased by RR 8,882 million from RR 18,257 million in 2015 to RR 27,139 million in 2016, primarily driven by the expansion of the product line.

3) Overheads increased from RR 2,422 million in 2015 to RR 2,587 million in 2016, driven by the higher utilization of production capacity, including under contract manufacturing agreements.

4) Amortization and depreciation charges grew from RR 869 million in 2015 to RR 1,039 million in 2016.

5) Direct labor costs increased by 26.6% from RR 517 million in 2015 to RR 655 million in 2016, with higher production and employees' salary review being the contributing factors.

The table below shows movements in revenue and cost of sales for the following segments: own pharmaceutical products, TPPs, medical equipment, contract manufacturing and agency fees.

SEGMENT	2016			2015		
	REVENUE	COST OF SALES	GROSS PROFIT	REVENUE	COST OF SALES	GROSS PROFIT
Pharmaceutical products	16,472	8,229	8,243	14,543	7,701	6,842
TPP	36,222	27,139	9,083	26,408	18,257	8,151
Medical equipment	1,806	1,422	384	1,575	1,177	398
Contract manufacturing and agency fees	7,286	3,543	3,743	4,669	2,263	2,406
TOTAL	**61,786**	**40,333**	**21,453**	**47,195**	**29,398**	**17,797**

SEGMENT	16/15 (RR MILLION)			16/15 (%)		
	REVENUE	COST OF SALES	GROSS PROFIT	REVENUE	COST OF SALES	GROSS PROFIT
Pharmaceutical products	1,929	528	1,401	13%	7%	20%
TPP	9,814	8,882	932	37%	49%	11%
Medical equipment	231	245	(14)	15%	21%	(3%)
Contract manufacturing and agency fees	2,617	1,280	1,337	56%	57%	56%
TOTAL	**14,591**	**10,935**	**3,656**	31%	37%	21%

Own pharmaceutical products

The cost of sales for pharmaceutical products increased by RR 528 million, or 7%, to RR 8,229 million in 2016 compared with 2015, driven by a 13% growth in their sales.

TPPs

The cost of sales for TPPs increased by RR 8,882 million, or 49%, from RR 18,257 million in 2015 to RR 27,139 million in 2016, driven by a 37% growth in their sales which were led by Coagil and Imbruvica.

Contract manufacturing and agency fees

The cost of sales for contract manufacturing rose by RR 1,280 million to RR 3,543 million in 2016,compared with 2015, driven by new contracts with third parties and OTCPharm PJSC.

Medical equipment

The cost of sales for medical equipment increased by 21% to RR 1,422 million compared with 2015 as their sales rose by 15%. The year-on-year increase in their cost of sales in 2016 was due to changes in the structure of sales and higher prices of materials.

Gross profit

Gross profit is calculated as sales revenue less cost of sales.

(RR MILLION)	2016	% OF SALES	2015	% OF SALES	16/15,RR MILLION	16/15
Revenue	61,786	100.0%	47,195	100,0%	14,591	30.9%
Cost of sales	40,333	65.3%	29,398	62,3%	10,935	37.2%
Gross profit	21,453	34.7%	17,797	37,7%	3,656	20.5%

The Group's gross profit increased by 20.5% from RR 17,797 million in 2015 to RR 21,453 million in 2016,

with its gross margin ratio dropping from 37.7% in 2015 to 34.7% in 2016. The margins were brought down by higher supplier prices amid macroeconomic volatility and changes in the structure of sales caused by an increase in the share of TPPs whose margins have traditionally been lower. The margin ratio of TPPs dropped from 31% in 2015 to 25% in 2016,due to the increased share of low-margin products in the TPP portfolio resulting in changes in the structure of sales.

Selling and distribution costs

Selling and distribution (S&D) costs mainly comprise advertising and marketing costs.

S&D costs grew by RR 160 million, or 6.3%, from RR 2,534 million in 2015 to RR 2,694 million in 2016. The year-on-year growth can largely be attributed to higher personnel costs, which increased by RR 95 million, or 7,1%, after employees' salary review, and higher advertising and marketing costs, which went up by RR 26 million, or 11.3%, due to heavier advertising to drive sales.

Other S&D costs such as freight transport and insurance, communications, business travel and rent combined increased by RR 39 million, or 4.1%, from RR 968 million in 2015 to RR 1,008 million in 2016.

General and administrative expenses

General and administrative (G&A) expenses comprise administrative staff payroll costs, information and consulting services and other expenses.

The Group's total G&A expenses increased by RR 55 million, or 20.7%, from RR 2,687 million in 2015 to RR 3,244 million in 2016. The share of G&A expenses in total sales remained almost unchanged, at 5.2% in 2016 versus 5.7% in 2015.

The increase in G&A expenses in absolute terms was primarily driven by the following factors:

1) Increase in labor costs by 15.0% from RR 1,696 million in 2015 to RR 1,950 million in 2016,after the review of administrative staff salaries
2) Increase in expenses for information and advisory services by 67% from RR 296 million in 2015 to RR 495 million in 2016

Net other income and expenses[15]

Net other expenses amounted to RR 5,861 million in 2016 versus net other income in the amount of RR 4,623 million in 2015.

The year-on-year movement in this item line in 2016,can largely be attributed to the following factors:

1) Recognition of foreign exchange loss in the amount of RR 4,676 million in 2016,versus the recognition of foreign exchange gain in the amount of RR 4,323 million in 2015,(- RR 8,999 million)
2) Income recognized in 2015 from the transfer of rights to Pentalgin® to OTCPharm PJSC for a consideration of RR 380 million
3) Increase in written-down R&D expenses to RR 924 million in 2016 from RR 163 million in 2015 due to the suspension of some non-performing projects
4) Income generated from suppliers' discounts in 2015 which were not offered in 2016

Finance income and expenses

Financial income primarily includes interest income on short-term financial instruments, cash deposits with banks and loans issued.

Financial income rose by RR 619 million, or 40%, from RR 946 million in 2015 to RR 1,565 million in 2016.

Financial expenses can largely be attributed to interest on loans issued by external parties. Financial expenses remained unchanged, at RR 476 million, in 2016,compared with the previous year.

EBITDA

EBITDA[16],dropped by 40% from RR 18,234 million in 2015,to RR 10,884 million in 2016. The EBITDA margin amounted to 17.6% in 2016 versus 38.6% in 2015. It was brought down by an increase in the share of low-margin TPPs in revenue, foreign exchange losses and losses from participation in other companies.

Income tax expense

Income tax expense amounted to RR 2,750 million in 2016,versus RR 3,747 million in 2015. The effective tax rate was 25.6% in 2016 versus 21.2% in 2015.

Net profit

The Group's net profit decreased by 42.6% from RR 13,931 million in 2015 to RR 8,002 million in 2016. Its net profit margin dropped from 29.5% in 2015,to 13.0% in 2016.

Capital management

The Company's main objectives in managing capital are to enable the Company to continue as a going concern, thus ensuring returns for shareholders, and to maintain an optimal capital structure for purposes of reducing the cost of capital. The Company manages and adjusts its capital structure in line with changes in economic conditions. To maintain or adjust the capital structure, the Company may adjust the amount of dividends or investments in favor of retained earnings, return capital to shareholders, issue new shares or dispose of assets to reduce debt.

Pharmstandard monitors capital using a gearing ratio, which is a ratio of net debt to total capital plus net debt. The Company's policy is to keep this ratio at no more than 60%. Pharmstandard's net debt includes loans and borrowings, trade and other payables, less cash and cash equivalents. Capital includes equity attributable to the shareholders of the parent. The gearing ratio has been declining every year.

Liquidity management is primarily driven by the need to increase the working capital of the Group, finance capital expenditures, reconstruct manufacturing facilities, implement GMPs, expand the product range and increase the profit margins of the product portfolio through the targeted acquisitions of subsidiaries and intangible assets.

In 2015-16, the Company financed its operating and investing activities with available cash and short-term loans. In the future, the Company also plans to finance its acquisitions and joint projects with other pharmaceutical companies using available cash and, where necessary, external debt.

The following table summarizes the Group's cash flows in 2015-2016:

CASH FLOWS	YEAR ENDED 31,DECEMBER 2016, RR MILLION	YEAR ENDED 31,DECEMBER 2015, RR MILLION
Net cash from operating activities	12,249	15,625
Net cash used in investing activities	(9,170)	(9,896)
Net cash from / (used in) financing activities	(86)	35
Cash and cash equivalents at the end of the year	17,387	14,397

Net cash from operating activities

15, Net other income and expenses comprise other income and expense, including gains and losses from investments in associates.
16, EBITDA is Earnings before Interest, Taxes, Depreciation and Amortization.

All cash flows from operating activities in the periods covered by the Group's consolidated financial statements largely came from sales of pharmaceutical products and medical equipment, agency fees for the distribution of counterparties' products and charges for contract manufacturing services.

The Group offers its distributors a payment delay of 90,to 120,days from the date of dispatch under standard commercial contracts and tied credit on individual terms. Under public procurement contracts, payment delays may not exceed 90,days from the date the Group complied with its obligations under the contract. Under joint commercial projects involving third-party producers, payment delays vary from contract to contract, being within a range of 6 to 150 days from the date of dispatch.

In 2016, net cash from operating activities amounted to RR 12,249 million.

In 2016, the Group recorded **growth in revenue** in the following segments:

1) OTC drugs:

Revenue from the OTC segment increased by RR 735 million. The largest growth in sales was posted by the following drugs :

- Corvalol (RR 368 million)
- Phosphogliv (RR 203 million)
- Inhalyptum (RR 139 million)

2) Rx drugs:

Revenue from this segment grew by RR 752 million, largely driven by higher sales of the following drugs:

- Combilipen (RR 237 million)
- Artrozan (RR 160 million)
- Biosulin (RR 130 million)

3) TPPs

Revenue from this segment grew by RR 9,814 million, driven by the launch of new products and higher sales of existing products:

- Crestor (RR 1,552 million) (New product)
- Coagil (RR 1,228 million)
- Imbruvica (RR 1,035 million)
- Genferon (RR 842 million) (New product)
- Erbitux (RR 810 million)
- Intelence (RR 697 million)
- Revlimid (RR 682 million)
- Betaloc (RR 625 million) (New product)
- Tysabri (RR 554 million)
- Velcade (RR 450 million)

4) Medical equipment

Revenue from this segment grew by RR 231 million. The growth was primarily driven by consistent efforts made under the Company's development strategy to upgrade and enhance its product portfolio by launching the domestic production of new types of equipment in accordance with national import substitution policies, as well as to improve internal and external processes.

5) Agency fees and contract manufacturing for OTCPharm PJSC and other counterparties grew by RR 2,617 million.

Cash outflow from an increase in receivables amounted to RR 1,141 million in 2016. These receivables are expected to be collected in the first half of 2017.

Cash inflow from an increase in the Group's payables amounted to RR 5,489 million due to an increase in payables to a related party of OTCPharm PJSC under an agency agreement. These payables are expected to be settled in Q2,2017.

Cash outflow from inventory amounted to RR 3,018 million in 2016. The movements in the Group's inventory were primarily caused by increased sales of TPPs.

Income tax paid by the Group in 2016,amounted to RR 2,785 million in 2016,compared with RR 4,881 million in 2015. The decrease was largely due to an increase in foreign exchange losses.

Net cash used in investing activities

In 2016 and 2015, net cash used in investing activities amounted to RR 9,170 million and RR 9,896 million, respectively.

The most significant investing activities in these periods included:

(i) Purchase of shares for investment and transactions involving the issuance of debt, including to related parties

(Ii) Purchase of property, construction and upgrade of manufacturing facilities, purchase of GMP-compliant and other equipment, with these investing activities amounting to RR 2,867 million in 2016 and RR 2,312 million in 2015.

The above investments were primarily aimed at developing the Group's manufacturing and logistics facilities and equipping its plants to comply with GMPs (for details, see Section 3.1 Manufacturing facilities).

Investments in R&D activities amounted to RR 492million in 2016; a number of non-performing projects for a total value of RR 924 million were suspended.

In 2016, the Company invested a total of RR 3,980 million (USD 61 million) (2015: RR 678 million (USD 11 million)) in innovative companies in the US and Canada. In addition, it purchased 17.75% of shares of OTCPharm PJSC for a consideration of RR 4,763 million.

In 2016, the Group issued RR 839,million (2015: RR 4,675 million) in loans to related parties and RR 2,358 million (2015: RR 1,850 million) in loans to third parties. For details, see Notes 15 and 16 to the consolidated financial statements. In 2016, the Group also collected RR 2,377 million (2015: RR 1,298 million) in loans from third parties and RR 971,million (2015: RR 72 million) in loans from related parties.

Net cash inflow from the repayment of promissory notes amounted to RR 2,565 million (2015: net cash outflow for the purchase of promissory notes in the amount of RR 1,090 million).

Net cash outflow for short-term deposits amounted to RR 84 million in 2016 (2015: net cash outflow in the amount of RR 99 million).

Net cash used in financing activities

Net cash outflow for financing activities amounted to RR 86 million in 2016 (2015: net cash inflow from financing activities in the amount of RR 35 million).

In 2016, the Group repaid short-term loans in the amount of RR 4,018 million and raised short-term debt in the amount of RR 4,000 million.

6.2

Risk management

In the ordinary course of business, the Group is exposed to various risks that may have a significant impact on its operating and financial performance, reputation and share price. To mitigate and eliminate these risks, the Group's management takes a comprehensive approach that focuses on risk monitoring, establishing dedicated policies to deal with external parties, and negotiating contracts aimed at protecting the Group's interests. The responsibility for the risk management policy is shared by the Audit Committee of the Board of Directors, Audit Commission, Controlling and Auditing Office, and Internal Audit and Control Department to the extent of authority of each of the listed bodies.

Qualitative and quantitative review of market risks

COUNTRY RISK	
Description Russia continues economic reforms and the development of its legal, tax and regulatory frameworks as required by a market economy. The future stability of the Russian economy is largely dependent upon these reforms and developments and the effectiveness of economic, financial and monetary measures undertaken by the government. The Russian economy is exposed to the impact of external market factors, especially the cost of energy supplies and declining growth rates of the global economy. A new risk emerged in 2014, triggered by negative political developments in Ukraine that were followed by economic sanctions against Russia and downgrades of its sovereign credit ratings. Despite positive trends in the Russian economy in 2016, driven primarily by growing oil prices (from 1st January 2016,to the 31st December 2016, Brent rose from USD 37.60 to USD 56.14 per barrel) and the resulting revision of the country's credit rating by major rating agencies from "negative" to "stable", Russia has been unable to break free from the negative effects of the higher cost of capital and uncertainty about future economic growth. The sanctions imposed on Russia by a number of countries remain in place and, according to the Central Bank of Russia, will constitute a major impediment to the country's economic growth over the next two years. The Group has operations in Ukraine. From 1,January 2014 to the date of Pharmstandard's 2016 financial statements, the Ukrainian hryvna (UAH) lost around 299% against major foreign currencies based on the National Bank of Ukraine UAH exchange rate to the US dollar and euro.	Impact Pharmstandard's principle activities are concentrated in Russia, which is home to six of the Group's seven production sites (one site is located in Ukraine). Russia is also the Group's major sales market. The current crisis in Russia and Ukraine may adversely affect the Group's financial position, operating performance and business prospects. Solution Management monitors the situation closely and takes necessary steps to minimize any adverse effects to the extent possible. Further negative developments in political, macroeconomic and/or foreign-trade conditions may have an impact on the Group's financial position and operating performance, and the extent of such impact cannot be determined at the moment. Nevertheless, management believes it is taking all appropriate measures to support the sustainability of the Group's business in the current circumstances.
CREDIT RISK	
Description In accordance with Pharmstandard's general business principles, almost all of our commercial sales are made on credit. Credit conditions depend on credit and marketing policies with respect to a given customer.	Impact Credit risk for the Group mainly arises when distributors refuse to fulfill their payment obligations under sale and purchase agreements. Solution We address credit risks, based on a policy that products can only be sold to customers with an appropriate credit history. We also perform daily monitoring of sales and receivables using effective internal control procedures and take appropriate measures based on our findings. Our credit committee, including the CEO, Deputy CEO for Finance and relevant directors, determines the Credit Policy, which is revised from time to time depending on the circumstances. Under the Credit Policy, customers are divided into two categories: (i) those served on prepayment basis, and (ii) those served on deferred payment basis within the credit limit approved for each specific customer. For certain customers credit limits are set provided that their payment obligations have been secured by a bank guarantee (in the amount of the credit limit), surety, a letter of credit or another similar instrument. The Company strives to diversify the Group's commercial and credit risks. For example, in 2016 about 32% of the Group's sales were made through five major distributors, same as a year ago. The carrying value of receivables, less allowances, is the maximum credit risk exposure at the end of each quarter. We believe that we do not have other significant credit risk exposure, except that to five or six customers. Allowance for doubtful accounts receivable grew moderately in 2016, compared with the 2015 level. Although the ability to collect receivables may be affected by a variety of economic factors, the Group's management believes that there is no significant risk of losses under relevant contracts. The Company formed the allowance for doubtful accounts receivable, exercising due care and skepticism and taking into account the current economic situation both in Russia and globally. We do not see any significant credit risks during the sale of products under government contracts. Given the sufficient and stable government funding of the healthcare sector in Russia, the Group does not experience any difficulties in settlements with procuring entities, with the turnover of accounts receivable ranging from 45,to 50,days on average.
CURRENCY RISK	

Description A part of our payables, cash and receivables, as well as some of our investments may be nominated in currencies other than the Russian ruble, which is the functional currency of all Russian companies and the reporting currency of the Group.	Impact We are exposed to currency risk in transactions denominated in a currency other than our functional currency. Such transactions usually include certain purchases of main raw materials for Pharmstandard, acquisitions of intangible assets and non-controlling interests, investments in associates, and certain long-term and short-term investments made in 2014-2016 that are denominated in USD or EUR. Exchange rate fluctuations may thus affect our cost of goods sold, operating expenses and costs reported in our consolidated financial statements as well as financial investments and accounts payable recorded in Pharmstandard's balance sheet. Solution Pharmstandard mitigates its currency risk by monitoring exchange rates applicable to its cash, payables, loans and borrowings. In particular, this risk is mitigated through the use of new forecasting methods and control over each individual foreign currency transaction. Our effective budgeting system helps management to make timely decisions on all companies of the Group.
LIQUIDITY RISK	
Description A liquidity shortage may render the Group temporarily unable to fulfill its obligations to suppliers or creditors.	Impact Management believes that Pharmstandard currently has sufficient amount of cash, including freely available cash reserves and cash deposits, to maintain a relevant liquidity level. Solution Our policy for minimizing liquidity risk is to maintain sufficient cash and cash equivalents or to ensure available funding in the form of external credit sufficient to meet our operating and financial commitments. We perform ongoing monitoring to identify any cash shortages and to make sure we meet the repayment deadlines. We also plan and control our daily cash flows.
INTEREST RATE RISK	
Description Interest rates on commercial loans in 2016 were mostly range-bound at 12-13% p.a., depending on the borrower's financial stability and contract terms.	Impact We do not believe that Pharmstandard is currently exposed to a serious risk of changes in interest rates, as all of the Group's financial instruments were short-term at 31 December 2016. Solution Currently, we believe there is no indication that the existing interest rates on deposits and borrowings may change markedly in the short term. However, given a significant amount of internal funds, management may decide to finance current operations and investing activities with own cash or equity in order to minimize interest rate risk. Note also that the Group's credit policy is aimed at attracting borrowings at fixed rates.

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Independent auditor’s report and Consolidated financial statements for the year ended 31 December 2016

Independent auditor's report

To the Shareholders and Management of
PJSC "Pharmstandard"

We have audited the accompanying consolidated financial statements of PJSC "Pharmstandard", which comprise the consolidated statement of financial position as at 31 December 2016, and the consolidated statement of comprehensive income, consolidated cash flow statement and consolidated statement of changes in equity for the year then ended, and a summary of significant accounting policies and other explanatory information.

Audited entity's responsibility for the consolidated financial statements

Management of PJSC "Pharmstandard" is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on the fairness of these consolidated financial statements based on our audit.

We conducted our audit in accordance with the federal standards on auditing effective in the Russian Federation. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing audit procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The audit procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of PJSC "Pharmstandard" and its subsidiaries as at 31 December 2016, and their financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards

A.B. Khorovitch
Partner
Ernst & Young LLC

25 April 2017

Details of the audited entity

Name: PJSC "Pharmstandard"

Record made in the State Register of Legal Entities on 5 May 2006, State Registration Number 02№005162109.

Address: Russia 141701, Moscow region, Dolgoprudny, Likhachevsky drive, 5 "b".

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.

Consolidated statement of financial position as at 31 December 2016

(in thousands of Russian rubles)

	Notes	2016	2015
ASSETS			
NON-CURRENT ASSETS			
Property, plant and equipment	10	12,258,096	10,818,849
Intangible assets	11	2,874,966	3,554,506
Long-term financial assets	2, 16	8,608,184	4,824,042
Investments in associates and joint venture	6, 7	6,170,395	6,230,297
Deferred tax asset	28	600,905	721,657
		30,512,546	**26,149,351**
CURRENT ASSETS			
Inventories	12	12,881,951	10,200,182
Trade and other receivables	2, 13	17,279,573	16,346,568
VAT recoverable		217,762	143,515
Prepayments		571,938	618,548
Short-term financial assets	2, 15	15,342,354	14,598,049
Income tax prepayments		316,868	168,163
Cash and short term deposits	2, 14	17,386,578	14,397,241
		63,997,024	**56,472,266**
TOTAL ASSETS		**94,509,570**	**82,621,617**
EQUITY AND LIABILITIES			
EQUITY ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT			
Share capital	21	37,793	37,793
Treasury shares		(1,437)	(1,437)
Foreign currency translation reserve		721,573	954,051
Revaluation reserve for investments available for sale		167,462	515,608
Retained earnings		60,398,262	52,157,943
		61,323,653	**53,663,958**
NON-CONTROLLING INTERESTS		**1,471,969**	**1,764,555**
TOTAL EQUITY		**62,795,622**	**55,428,513**

	Notes	2016	2015
NON-CURRENT LIABILITIES			
Deferred tax liability	28	342,142	315,268
Other non-current liabilities	20	101,775	84,813
		443,917	**400,081**
CURRENT LIABILITIES			
Trade and other payables	2, 19	26,270,389	20,970,110
Short-term borrowings and loans	2, 17	4,070,794	4,089,436
Income tax payable		341,283	375,169
Taxes payable other than income tax	18	587,565	1,358,308
		31,270,031	**26,793,023**
TOTAL LIABILITIES		**31,713,948**	**27,193,104**
TOTAL EQUITY AND LIABILITIES		**94,509,570**	**82,621,617**

Signed and authorized for release on behalf of the Board of Directors of PJSC “Pharmstandard”

Chief Executive Officer G.A. Potapov

Chief Financial Officer M.A. Markova

22 April 2017

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Consolidated statement of comprehensive income for the year ended 31 December 2016

(in thousands of Russian rubles)

	Notes	2016	2015
Revenue	22	61,786,424	47,194,938
Cost of sales	23	(40,332,965)	(29,397,598)
GROSS PROFIT		**21,453,459**	**17,797,340**
Selling and distribution costs	24	(2,694,180)	(2,534,272)
General and administrative expenses	25	(3,243,775)	(2,687,072)
Operating profit		15,515,504	12,575,996
Other income	26	1,836,451	7,185,802
Other expenses	27	(6,488,169)	(2,191,341)
Interest income		1,565,452	945,840
Interest expense		(467,173)	(466,942)
Share in loss of a joint venture and associates, net	6, 7	(1,209,306)	(371,479)
PROFIT BEFORE INCOME TAX		**10,752,759**	**17,677,876**
Income tax expense	28	(2,750,482)	(3,746,776)
PROFIT FOR THE YEAR		**8,002,277**	**13,931,100**
OTHER COMPREHENSIVE INCOME			
To be reclassified to profit or loss in subsequent periods			
Exchange differences on translation of foreign operations		(219,301)	208,136
Revaluation of investments available for sale		(371,375)	515,608
Income tax effect		23,229	–
Total other comprehensive (loss)/ income		(567,447)	723,744
TOTAL COMPREHENSIVE INCOME FOR THE YEAR, NET OF TAX		**7,434,830**	**14,654,844**
PROFIT FOR THE YEAR			
Attributable to:			
Equity holders of the parent		8,234,961	13,749,466
Non-controlling interests		(232,684)	181,634
		8,002,277	**13,931,100**

	Notes	2016	2015
TOTAL COMPREHENSIVE INCOME FOR THE YEAR, NET OF TAX			
Attributable to:			
Equity holders of the parent		7,654,337	14,489,565
Non-controlling interests		(219,507)	165,279
		7,434,830	**14,654,844**
EARNINGS PER SHARE (IN RUSSIAN RUBLES)			
basic and diluted, based on profit for the year attributable to equity holders of the parent	21	226,51	378,20

Signed and authorized for release on behalf of the Board of Directors of PJSC “Pharmstandard”

Chief Executive Officer G.A. Potapov

Chief Financial Officer M.A. Markova

22 April 2017

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Consolidated cash flow statement for the year ended 31 December 2016

(in thousands of Russian rubles)

	Notes	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES			
Profit before income tax		10,752,759	17,677,876
Adjustments for:			
Depreciation and amortization	23, 24, 25, 27	1,295,469	1,098,966
Charge of impairment – accounts receivable, net	13	161,438	761,963
Write-down of inventories to net realizable value, net	12	273,602	138,382
(Reversal)/charge of impairment – property, plant and equipment	10, 26, 27	(55,233)	120,327
Impairment of intangible assets and write-off of unsuccessful R&D projects	27	939,387	–
(Reversal)/charge of impairment – loans issued, net	26, 27	(1,013,039)	1,067,538
Loss on write-off of inventories		62,281	82,095
Gain on disposal of property, plant and equipment	10, 26	(22,212)	(64,967)
Share in loss of a joint venture and associates		1,209,306	371,479
Unrealized foreign exchange differences		2,041,870	(3,396,960)
Gain from transactions with promissory notes	26	(20,329)	(10,639)
Income from restructuring of accounts payable	26	–	(1,712,681)
Interest income		(1,565,452)	(945,840)
Interest expense		467,173	466,942
OPERATING CASH FLOWS BEFORE WORKING CAPITAL CHANGES		**14,527,020**	**15,654,481**
(Increase)/decrease in trade and other receivables	13	(1,140,535)	997,366
Increase in inventories	12	(3,017,652)	(3,358,793)
Increase in VAT recoverable		(74,247)	(27,211)
Decrease/(increase) in prepayments		46,610	(299,261)
Increase in trade and other payables	19	5,488,828	6,881,580
(Decrease)/increase in taxes payable other than income tax	18	(770,743)	702,683
CASH GENERATED FROM OPERATIONS		**15,059,281**	**20,550,845**
Income tax paid	28	(2,785,446)	(4,880,527)
Interest paid		(475,740)	(464,707)
Interest received		451,115	419,577
NET CASH FROM OPERATING ACTIVITIES		**12,249,209**	**15,625,188**

	Notes	2016	2015
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of property, plant and equipment	10	(2,866,599)	(2,312,247)
Payments related to R&D projects	11	(491,970)	(603,260)
Cash paid for acquisition of share in associates	6, 7	(2,604,292)	(112,926)
Cash received from sale of property, plant and equipment		299,312	153,820
Cash received from return of deposits		386,936	1,053,656
Cash paid for investments available for sale		(6,138,428)	(678,017)
Cash received from return of short-term loans issued to third parties		2,377,277	1,297,669
Short-term bank deposits placed		(471,411)	(200,000)
Short-term bank deposits placed with the related bank		–	(952,198)
Loans issued to third parties		(2,358,399)	(1,849,980)
Loans issued to related parties		(838,818)	(4,674,782)
Loans repaid by related parties		971,063	72,000
Cash paid for purchase of promissory notes from related bank		–	(2,489,169)
Cash received from transactions with promissory notes		2,565,221	1,399,416
NET CASH USED IN INVESTING ACTIVITIES		**(9,170,108)**	**(9,896,018)**
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from borrowings and loans	17	4,000,001	4,083,151
Repayment of borrowings and loans	17	(4,018,262)	(4,001,300)
Dividends paid by a subsidiary to non-controlling shareholders	31	(67,721)	(46,719)
NET CASH (USED IN)/FROM FINANCING ACTIVITIES		**(85,982)**	**35,132**
NET INCREASE IN CASH AND CASH EQUIVALENTS		**2,993,119**	**5,764,302**
Net foreign exchange differences		(3,782)	91,391
Cash and cash equivalents at the beginning of the year	14	14,397,241	8,541,548
CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR	**2, 14**	**17,386,578**	**14,397,241**

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Consolidated statement of changes in equity for the year ended 31 December 2016

(in thousands of Russian rubles)

EQUITY ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT									
	Share capital	Treasury shares	Foreign currency translation reserve		Revaluation reserve for investments available for sale	Retained earnings	Total	Non-controlling interests	Total equity
BALANCE AT 1 JANUARY 2015	**37,793**	**(1,437)**	**729,560**		**–**	**38,408,477**	**39,174,393**	**1,645,947**	**40,820,340**
Profit for the year	–	–	–		–	13,749,466	13,749,466	181,634	13,931,100
Other comprehensive income for the year	–	–	224,491		515,608	–	740,099	(16,355)	723,744
TOTAL COMPREHENSIVE INCOME FOR THE YEAR	**–**	**–**	**224,491**		**515,608**	**13,749,466**	**14,489,565**	**165,279**	**14,654,844**
Establishment of a subsidiary (Note 1)	–	–	–		–	–	–	48	48
Dividends paid by a subsidiary (Note 31)	–	–	–		–	–	–	(46,719)	(46,719)
BALANCE AT 31 DECEMBER 2015	**37,793**	**(1,437)**	**954,051**		**515,608**	**52,157,943**	**53,663,958**	**1,764,555**	**55,428,513**
Profit for the year	–	–	–		–	8,234,961	8,234,961	(232,684)	8,002,277
Other comprehensive loss for the year	–	–	(232,478)		(348,146)	–	(580,624)	13,177	(567,447)
TOTAL COMPREHENSIVE INCOME FOR THE YEAR	**–**	**–**	**(232,478)**		**(348,146)**	**8,234,961**	**7,654,337**	**(219,507)**	**7,434,830**
Change in ownership structure within the Group (Note 1)	–	–	–		–	5,358	5,358	(5,358)	–
Dividends paid by a subsidiary (Note 31)	–	–	–		–	–	–	(67,721)	(67,721)
BALANCE AT 31 DECEMBER 2016	**37,793**	**(1,437)**	**721,573**		**167,462**	**60,398,262**	**61,323,653**	**1,471,969**	**62,795,622**

7.1 Corporate information

The principal activities of PJSC “Pharmstandard” (“the Company”) and its subsidiaries (“the Group”) are production and wholesale distribution of pharmaceutical products and medical equipment. The Company was incorporated in the Russian Federation. Since May 2007, the Company’s shares were publicly traded. In 2016, Augment Investments Limited acquired 100% of the Company’s shares, and subsequently on 29 November 2016 the global depositary receipts of PJSC “Pharmstandard” were excluded the from the quotation list of the London Stock Exchange and trading in shares on the Moscow Stock Exchange was suspended. On 30 January 2017, the Company’s shareholders decided to delist shares and terminate the public status of PJSC “Pharmstandard”. In accordance with this decision the shares of PJSC “Pharmstandard” were excluded from the list of securities admitted to organized trading on the Moscow Stock Exchange starting 24 March 2017 (Note 32). The Group’s head office is registered at Likhachevsky proezd, 5B, Dolgoprudny, Moscow region, Russian Federation, and its manufacturing facilities are based in Moscow region, Vladimir region, Kursk, Tomsk, Ufa, Tyumen (all in Russian Federation) and Kharkov (Ukraine). The Company holds interest in the following subsidiaries, associates and joint ventures as at 31 December 2016 and 2015:

Entity	Country of incorporation	Activity	2016 effective share, %	2015 effective share, %
SUBSIDIARIES				
1. Pharmstandard LLC	Russian Federation	Central procurement	100	100
2. Pharmstandard-Leksredstva OJSC	Russian Federation	Manufacturing of pharmaceutical products	100	100
3. Pharmstandard-Tomskhimpharm OJSC	Russian Federation	Manufacturing of pharmaceutical products	90,78	90,78
4. Pharmstandard-UfaVITA OJSC	Russian Federation	Manufacturing of pharmaceutical products	100	100
5. Pharmstandard-Biolek PJSC	Ukraine	Manufacturing of pharmaceutical products	96,93	96,93
6. TZMOI OJSC	Russian Federation	Manufacturing of medical equipment	100	100
7. MDR Pharmaceuticals	Cyprus	Finance and holding company	50,05	50,05
8. Bigpearl Trading Limited (c)	Cyprus	Intermediary holding company	50,005	50,005
9. Pharmapark LLC (c)	Russian Federation	Manufacturing of pharmaceutical products	50,005	50,005
10. Biomed named after I.I. Mechnikov JSC (c)	Russian Federation	Manufacturing of pharmaceutical products	49,845	49,845
11. Pharmatsevticheskiye innovatsii OJSC (c)	Russian Federation	Asset holder	50,005	50,005
12. EKK OJSC (c)	Russian Federation	Sundry activity	35,29	35,29
13. LEKKO CJSC	Russian Federation	Manufacturing of pharmaceutical products	100	100
14. Moldildo Trading Limited	Cyprus	Intermediate holding company	75	75
15. Pharmstandard-Medtechnika LLC	Russian Federation	Sales of medical equipment	75	75
16. Pharmstandard International S.A.	Luxembourg	Venture investments	100	100
17. Sellthera Pharm LLC	Russian Federation	Development and manufacturing company	75	75
18.Pharmstandard-Plazma LLC (b)	Russian Federation	Manufacturing of pharmaceutical products	52	100
19. MasterPlazma LLC	Russian Federation	Manufacturing of pharmaceutical products	52	52
JOINT VENTURES AND ASSOCIATES				
20. NauchTechStroy Plus LLC (NTS+)	Russian Federation	Research and development company	37,5	37,5
21. Argos Therapeutics Inc. (a)	USA	Research and development company	32,10	27,65
22. Biocad Holdings Limited	Cyprus	Research, development and manufacturing of pharmaceutical products	20	20
23. Barskiy Lug LLC (d)	Russian federation	letting of business premises	49	–

(a) The Group’s share increased due to purchase of additional emission of shares (Note 7.1).

(b) In 2016 the share changed due to changes in group structure. In 2017, the Group decided to merge Pharmstandard – Plasma LLC with MasterPlasma LLC.

(c) These subsidiaries comprised “Bioprocess” group of companies acquired by the Company in July 2012. The Group exercises control over these entities through its controlling interest in Bigpearl Trading Limited.

(d) On 5 February 2016, the Group purchased share in Barskiy Lug LLC. Assets, liabilities and activities of this company are insignificant for the Group.

These consolidated financial statements were authorized for issue by the Board of Directors of PJSC “Pharmstandard” on 22 April 2017.

7.2 Basis of preparation of the financial statements

To ensure consistency with the presentation of data in the consolidated statement of financial position for the year ended 31 December 2016, comparative information for the year ended 31 December 2015 was appropriately reclassified.

Adjustments are detailed below:

	Before adjustments	Adjustments	After adjustments
ASSETS			
NON-CURRENT ASSETS			
Long-term financial assets	4,686,936	137,106	4,824,042
CURRENT ASSETS			
Trade and other receivables	17,187,541	(840,973)	16,346,568
Short-term financial assets	13,902,848	695,201	14,598,049
Cash and short term deposits	14,388,575	8,666	14,397,241
LIABILITIES			
CURRENT LIABILITIES			
Trade and other payables	20,975,024	(4,914)	20,970,110
Short-term borrowings and loans	4,084,522	4,914	4,089,436

Statement of compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB").

Basis of accounting

The Group's Russian entities maintain their accounting records in Russian rubles ("RR") and prepare their statutory financial statements in accordance with the Regulations on Accounting and Reporting of the Russian Federation. The Group's Ukrainian subsidiary maintains its accounting records in Ukrainian hryvnia ("UAH") and prepares its statutory financial statements in accordance with IFRS. The other Group's foreign entities located in the USA, Cyprus and Luxembourg primarily maintain their accounting records in US dollars and prepare their statutory accounting records in accordance with US GAAP, IFRS and the local regulations respectively. When necessary the local statutory financial statements have been adjusted to present these consolidated financial statements in accordance with IFRS. These adjustments principally relate to valuation and depreciation of property, plant and equipment, valuation and amortization of intangible assets, certain valuation allowances, using fair values for certain assets, acquisition accounting for business combinations and the resulting income tax effects, and also to consolidation of subsidiaries and equity accounting of associates and joint ventures.

The consolidated financial statements have been prepared under the historical cost convention except as disclosed in the summary of significant accounting policies below. For example, certain short-term assets are recorded at fair value and non-current assets classified as held for sale are recorded at the lower of carrying amount and fair value less costs to sell.

7.3 Changes in accounting policies

The accounting policies adopted are consistent with those of the previous financial period except that the Group has adopted the following new and amended IFRS and IFRIC interpretations as at 1 January 2016. They did not have a significant impact on the Group's annual consolidated financial statements:

- Amendments to IFRS 11 Joint Arrangements: Accounting for Acquisitions of Interests - amendments to IFRS 11 require that a joint operator should account for the acquisition of an interest in a joint operation that constitutes a business in accordance with the principles of IFRS 3 Business Combinations. The amendments also clarify that a previously held interest in a joint operation is not remeasured on the acquisition of an additional interest in the same joint operation if joint control is retained. In addition, a scope exclusion has been added to IFRS 11 to specify that the amendments do not apply when the parties sharing joint control, including the reporting entity, are under common control of the same ultimate controlling party.
- Amendments to IAS 16 and IAS 38: Clarification of Acceptable Methods of Depreciation and Amortisation - the amendments clarify the revenue-based depreciation method cannot be used to depreciate property, plant and equipment and may only be used in very limited circumstances to amortise intangible assets.
- The amendments to IAS 1 Presentation of Financial Statements – the amendments clarify, rather than significantly change, the existing IAS 1 requirements.
- Amendments to IFRS 14 Regulatory Deferral Accounts.
- Amendments to IAS 27: Equity Method in Separate Financial Statements
- Amendments to IFRS 10, IFRS 12 and IAS 28 Investment Entities: Applying the Consolidation Exception.
- Amendments to IAS 16 and IAS 41 Agriculture: Bearer Plants.
- Annual Improvements 2012-2014 Cycle.

The Group did not early apply the standards, clarifications or amendments issued but not yet effective.

IFRSs and Interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC) but are not yet effective

The standards and interpretations that are issued, but not yet effective, up to the date of issuance of the Group's financial statements are disclosed below. The Group intends to adopt these standards, if applicable, when they become effective. The Group is currently evaluating the impact of following standards and amendments on the consolidated financial statements.

Amendments effective for annual periods beginning on or after 1 January 2017 with early application permitted:

- Amendments to IAS 7 Disclosure Initiative
  The amendments require entities to provide disclosures about changes in their liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes.
- Amendments to IAS 12 Recognition of Deferred Tax Assets for Unrealised Losses
  The amendments clarify that unrealised losses on debt instruments measured at fair value in the financial statements but at cost for tax purposes can give rise to deductible temporary differences.
- Annual Improvements 2014-2016 Cycle
  - Improvement of IFRS 12.

Amendments effective for annual periods beginning on or after 1 January 2018 with early application permitted:

- IFRS 9 Financial Instruments
  The standard will replace IAS 39 Financial Instruments: Recognition and Measurement and all previous versions of IFRS 9. IFRS 9 brings together all three aspects of the accounting for financial instruments project: classification and measurement, impairment and hedge accounting. Except for hedge accounting, retrospective application is required but providing comparative information is not compulsory.

/ IFRS 15 Revenue from Contracts with Customers
The new revenue standard will supersede all current revenue recognition requirements under IFRS. Either a full retrospective application or a modified retrospective application is required. IFRS 15 establishes a five-step model to account for revenue arising from contracts with customers. The Group plans to adopt the new standard on the required effective date using the full retrospective method. The Group analyses existing contracts under new requirements and evaluates the impact of the new standard of the consolidated financial statements.
/ IFRIC Interpretation 22 Foreign Currency Transactions and Advance Consideration
The interpretation clarifies that in determining the spot exchange rate to use on initial recognition of the asset or liability related to advance consideration in foreign currency, the date of the transaction is the date on which an entity initially recognises the non-monetary asset or non-monetary liability arising from the advance consideration.
/ Amendments to IFRS 2 Classification and Measurement of Share-based Payment Transactions
Amendments address three main areas: the effects of vesting conditions on the measurement of a cash-settled share-based payment transaction; the classification of a share-based payment transaction with net settlement features for withholding tax obligations; and accounting where a modification to the terms and conditions of a share-based payment transaction changes its classification from cash settled to equity settled.
/ Amendments to IFRS 4 Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts
The amendments address concerns arising from implementing the new financial instruments Standard, IFRS 9, before implementing the new insurance contracts standard that the Board is developing to replace IFRS 4. The amendments introduce two options for entities issuing insurance contracts: a temporary exemption from applying IFRS 9 and an overlay approach. The temporary exemption is first applied for reporting periods beginning on or after 1 January 2018.
/ Amendments to IAS 40 Transfers of Investment Property
The amendments clarify when an entity should transfer property, including property under construction or development into or out of investment property.
/ Annual Improvements 2014-2016 Cycle
  / Improvement of IFRS 1;
  / Improvement of IAS 28.

Amendments effective for annual periods beginning on or after 1 January 2019 with early application permitted:

/ IFRS 16 Lease
IFRS 16 will supersede all current lease recognition requirements under IFRS and 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. New standard substantially differs from the existing IFRS requirements.
/ Amendments to IFRS 10 and IAS 28: Sale or Contribution of Assets between an Investor and its Associate or Joint Venture – the effective date has been deferred indefinitely.

7.4.1 Basis of consolidation

Subsidiaries

Subsidiaries are fully consolidated at the date of acquisition, being the date on which the Group obtains control over a subsidiary, and continue to be consolidated until the date when such control ceases. All intercompany transactions, balances and unrealized gains on transactions between Group companies are eliminated in full; unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Where necessary, accounting policies for subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

Non-controlling interest is the equity in a subsidiary not attributable, directly or indirectly, to the Group. The interests of non-controlling shareholders are initially measured at the non-controlling interests' proportionate share of the fair value of the acquiree's identifiable net assets.

Subsequent to acquisition, the carrying amount of non-controlling interests is the amount of those interests at initial recognition adjusted for the non-controlling interests' share of subsequent changes in equity. Total comprehensive income within a subsidiary is attributed to the non-controlling interest even if that results in a deficit balance.

Non-controlling interest is presented as an equity item, separately from the equity of the owners of the parent.

Business combinations

The acquisition method of accounting is used to account for business combinations by the Group. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any non-controlling interest. For each business combination, the Group measures the non-controlling interest in the acquired subsidiary at the proportionate share of the acquiree's identifiable net assets. Acquisition costs incurred are expensed and included in administrative expenses.

The excess of purchase consideration over the Group's share of the fair value of identifiable net assets is recorded as goodwill (Note 4.6). If the cost of the acquisition is less than the Group's share of the fair value of identifiable net assets of the subsidiary acquired the difference is recognized directly in profit or loss.

Investments in associates and joint ventures

An associate is an entity over which the Group has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but is not control or joint control over those policies.

A joint venture is a type of joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the joint venture. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require unanimous consent of the parties sharing control.

The results and liabilities of associates and joint ventures are included in these consolidated financial statements from the date on which the investee becomes an associate or a joint venture, using the equity method of accounting. The Group discontinues the use of the equity method from the date when the investment ceases to be an associate or a joint venture. Investments in associates and joint ventures are carried in the consolidated statement of financial position at cost and adjusted for by post-acquisition changes in the Group's share of net assets of the associate or joint venture, less any impairment in the value of individual investments resulting from revaluation. Losses of an associate or joint venture in excess of the Group's interest in that associate or joint venture (which includes any long-term interests, that in substance form part of the Group's net investment in the associate or joint venture) are recognized only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the associate or joint venture.

Any excess of the cost of acquisition over the Group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities of the associate recognized at the date of acquisition is recognized as goodwill. The goodwill is included within the carrying amount of the investment and is assessed for impairment as part of that investment. Any excess of the Group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities over the cost of acquisition is recognized immediately in profit or loss in the period in which the investment is acquired.

7.4.2 Cash and short-term deposits

Cash and short-term deposits in the consolidated statement of financial position comprise cash at banks and on hand, short-term deposits with an original maturity of three months or less and cash deposits placed to secure participation in the open public tenders with an original maturity of three months or less.

7.4.3 Value added tax

The Russian and Ukrainian tax legislation permits settlement of value added tax ("VAT") on a net basis within one legal entity.

VAT is payable upon invoicing and delivery of goods, performing work or rendering services, as well as upon collection of prepayments from customers. VAT on purchases, even if they have not been settled at the reporting date, is deducted from the amount of VAT payable.

Where allowance has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT.

7.4.4 Inventories

Inventories are recorded at the lower of cost and net realizable value. The cost of inventories is determined on a first in, first out basis. The cost of finished goods and work in progress comprises raw material, direct labor, other direct costs and related production overheads (based on normal operating capacity) but excludes borrowing costs. The cost of third parties' products comprises expenditures directly attributable to purchase of these products Net realizable value is the estimated selling price set in the ordinary course of business, less estimated costs necessary to manufacture finished goods and sell them.

7.4.5 Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and impairment losses. Depreciation is calculated on a straight-line basis. The depreciation periods, which represent the estimated useful economic lives of the respective assets, are as follows:

	NUMBER OF YEARS
Buildings	10 to 50
Plant and machinery	5 to 30
Equipment, motor vehicles and other	2 to 7

The asset's residual values, useful lives and depreciation methods are reviewed and adjusted as appropriate, at each financial year-end. Land is not depreciated.

Repair and maintenance expenditure is expensed as incurred. Major renewals and improvements are capitalized, and replaced assets are derecognized. Gains and losses arising from the retirement of property, plant and equipment are included in profit or loss as incurred.

7.4.6 Goodwill

Goodwill on an acquisition of a subsidiary is included in intangible assets. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses.

Goodwill is reviewed for impairment annually or more frequently if any events or changes in circumstances indicate that the carrying amount may be impaired. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units or groups of units. Each unit or group of units to which the goodwill is allocated represents the lowest level within the Group at which the goodwill is monitored for internal management purposes.

Impairment is determined by assessing the recoverable amount of the cash-generating unit (group of cash-generating units) to which the goodwill relates. Where the recoverable amount of the cash-generating unit (group of cash-generating units) is less than the carrying amount, an impairment loss is recognized. Where goodwill forms part of a cash-generating unit (group of cash-generating units) and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

7.4.7 Intangible assets other than goodwill

Intangible assets acquired separately from business combinations are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is their fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses.

Intangible assets with a finite life are amortized on a straight-line basis over the useful economic lives (for trademarks useful economic life is estimated between 15 and 20 years; for patents useful economic life is estimated accordingly to period which is reflected in patent, but not more than 20 years) and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Amortization periods and methods for intangible assets are reviewed at least at each financial year-end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortization period or method, as appropriate, and treated as changes in accounting estimates. The amortization expense on intangible assets with finite lives is recognized in profit or loss in the expense category consistent with the function of the intangible asset.

Development is the application of research findings or other knowledge to a plan or design for the production of a new product before commercial production or use of the product has begun. Development costs are all directly attributable costs necessary to create, produce and prepare the asset to be capable of operating in the manner intended by management. Development costs are capitalized as an intangible asset if all of the following criteria are met:

a) The technical feasibility of completing the asset so that it will be available for use or sale;
b) The intention to complete the asset and use or sell it;
c) The ability to use or sell the asset;
d) The asset will generate probable future economic benefits and demonstrate the existence of a market or the usefulness of the asset if it is to be used internally;
e) The availability of adequate technical, financial and other resources to complete the development and to use or sell it; and
f) The ability to measure reliably the expenditure attributable to the intangible asset.

Amortization of development costs starts upon receipt of regulatory approval when the asset becomes available for use and is transferred to the designated category of intangible assets other than goodwill.

Expenditure on an intangible item that was initially recognized as an expense shall not be recognized as part of the cost of an intangible asset at a later date.

7.4.8 Investments and other financial assets

Financial assets within the scope of IAS 39 are classified as either financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, or available-for-sale investments, as appropriate. The Group does not have held-to-maturity investments or financial assets at fair value through profit or loss.

When financial assets are recognized initially, they are measured at fair value, plus, in the case of financial assets not at fair value through profit or loss, directly attributable transaction costs. The Group determines the classification of its financial assets on initial recognition and, where allowed and appropriate, re-evaluates this designation at each financial year end. All regular way purchases and sales of financial assets are recognized on the trade date, which is the date that the Group commits to purchase the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the market place.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement loans and receivables are carried at amortized cost using the effective interest method less any allowance for impairment. Gains and losses are recognized in profit or loss when the loans and receivables are derecognized or impaired, as well as through the amortization process. Interest receivable on deposits is classified as other receivables.

Available-for-sale financial investments

Available-for-sale ("AFS") financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified in any other categories. After initial measurement, available-for-sale investments are measured at fair value with changes in fair value recognized in other comprehensive income. If an available-for-sale asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortization) and its current fair value, less any impairment loss previously recognized in the profit or loss, is transferred from other comprehensive income to profit or loss. Reversals in respect of equity instruments classified as available-for-sale are not recognized in profit or loss. Impairment losses on debt instruments are reversed through profit or loss, if the increase in fair value of the instrument can be objectively related to an event, occurring after the impairment loss was recognized.

Fair value

The fair value of investments that are actively traded in organized financial markets is determined by reference to quoted market bid prices at the close of business on the reporting date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions; reference to the current market value of another instrument, which is substantially the same; discounted cash flow analysis or other valuation models.

Amortized cost

Loans and receivables are measured at amortized cost. This is computed using the effective interest method less any allowance for impairment. The calculation takes into account any premium or discount on acquisition and includes transaction costs and fees that are an integral part of the effective interest rate.

Impairment of financial assets

The Group assesses, at each reporting date, whether there is objective evidence that a financial asset or a group of financial assets is impaired.

Assets carried at amortized cost

If there is objective evidence that an impairment loss on assets carried at amortized cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not been incurred) discounted at the financial asset's effective interest rate (i.e. the effective interest rate computed at initial recognition). The carrying amount of the asset is reduced through use of an allowance account. The amount of the loss shall be recognized in profit or loss. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed, to the extent that the carrying amount of the asset does not exceed its amortized cost at the reversal date. Any subsequent reversal of an impairment loss is recognized in profit or loss.

Available-for-sale financial investments

For AFS financial investments, the Group assesses at each reporting date whether there is objective evidence that an investment or a group of investments is impaired. In the case of equity investments classified as AFS, objective evidence would include a significant or prolonged decline in the fair value of the investment below its cost. 'Significant' is evaluated against the original cost of the investment and 'prolonged' against the period in which the fair value has been below its original cost. When there is evidence of impairment, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognized in profit or loss – is reclassified from OCI to the statement of profit or loss. Impairment losses on equity investments are not reversed through profit or loss; increases in their fair value after impairment are recognized in OCI.

The determination of what is 'significant' or 'prolonged' requires judgment. In making this judgment, the Group evaluates, among other factors, the duration or extent to which the fair value of an investment is less than its cost.

7.4.9 Borrowings

Borrowings are initially recognized at the fair value of the consideration received less directly attributable transaction costs. After initial recognition, borrowings are subsequently measured at amortized cost using the effective interest method.

Borrowing costs directly attributable to the acquisition, construction or production of an asset that necessarily takes a substantial period of time to get ready for its intended use or sale are capitalized as part of the cost of the asset. All other borrowing costs are expensed.

7.4.10 Income taxes

Income tax expense comprises current and deferred tax. Current tax is calculated based on the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, including any adjustment to income tax payable for previous years.

Deferred income taxes are provided for all temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes, except where the deferred income taxes arise from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither accounting nor taxable profit or loss.

A deferred tax asset is recorded only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilized. Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realized or the liability is settled, based on tax rates that have been enacted or substantively enacted at the reporting date.

Deferred tax assets and deferred tax liabilities can be offset only if: (a) a Group entity has a legally enforceable right to set off current tax assets against current tax liabilities; and (b) the deferred tax assets and the deferred tax liabilities relate to income taxes levied by the same taxation authority (c) on either: (i) the same taxable entity; or (ii) different taxable entities which intend either to settle current tax liabilities and assets on a net basis, or to realize the assets and settle the liabilities simultaneously, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered.

Deferred income tax liabilities are provided on temporary differences arising on investments in subsidiaries, associates and joint ventures, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

In respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are recognized only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilized.

The effect from a change in tax rates is recognized in profit or loss except to the extent that it relates to items previously charged to other comprehensive income.

7.4.11 Leases

Operating lease payments are recognized as an expense in profit or loss on a straight-line basis over the lease term.

7.4.12 Derecognition of financial assets and liabilities

Financial assets

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognized when the rights to receive cash flows from the asset have expired.

Financial liabilities

A financial liability is derecognized when the obligation under the liability is discharged or cancelled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognized in profit or loss.

7.4.13 Provisions

Provisions are recognized when the Group has a legal or constructive obligation as a result of past events, and it is probable that an outflow of resources will be required to settle the obligation and a reliable estimate of the amount can be made.

Expense relating to any provision is presented in profit or loss. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as a finance cost.

7.4.14 Equity

Share capital

Ordinary shares are classified as equity.

Dividends

Dividends declared by the Group are recognized as a liability and deducted from equity at the reporting date only if they are declared before or on the reporting date. Such dividends are disclosed when

they are proposed before the reporting date or proposed or declared after the reporting date but before the consolidated financial statements are authorized for issue.

Treasury shares

Own equity instruments that are reacquired are recognized at cost and deducted from equity. No gain or loss is recognized in the consolidated statement of comprehensive income on the purchase, sale, issue or cancellation of the Group's own equity instruments. Any difference between the face value of shares and the consideration paid for treasury shares is recognized in retained earnings.

7.4.15 Revenue

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured, regardless of when the payment is being made. Revenue is measured at the fair value of the consideration received or receivable, excluding discounts and rebates, taking into account contractually defined terms of payment and excluding taxes or duties.

7.4.16 Employee benefits

In 2016, under provision of the Russian legislation, the Group paid social contributions ("SC") to state non-budgetary funds as follows:

- Contributions to the Pension Fund to form the retirement pension at the rate of 22%; the regressive rate of 10% was applied to payments for the insured persons, which are over RR 796 calculated as a cumulative total from the beginning of the year;
- Contributions for compulsory medical insurance were calculated at the rate of 5.1%;
- Social insurance contributions (for temporary disability) were calculated at the rate of 2.9%, there were no social insurance contributions from payments for insured persons over RR 718 calculated as a cumulative total from the beginning of the year;
- Social insurance contributions (for industrial accidents) were paid depending on the professional risk class at the Group's entity and ranged from 0.2%-0.7%.

The Group's SC are expensed in the year to which they relate.

SC accrued during the year ended 31 December 2016 amounted to RR 958,094 (2015: RR 857,129) and was classified as labor costs in these consolidated financial statements.

7.4.17 Foreign currency transactions

The consolidated financial statements are presented in Russian rubles, which is the functional currency of the Company and its Russian subsidiaries. Transactions in foreign currencies are initially recorded in the functional currency at the exchange rate ruling at the date of transaction. Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency rate of exchange ruling at the reporting date. All resulting differences are taken to profit or loss. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions.

At 31 December 2016, the exchange rates used for the translation of foreign currency balances were 1 United States dollar = 60.66 rubles; 1 euro = 63.81 rubles; 1 Ukrainian hryvnia = 2.24 rubles (2015: 1 United States dollar = 72.88 rubles; 1 euro = 79.70 rubles; 1 Ukrainian hryvnia = 3.05 rubles).

The functional currency of the Ukrainian subsidiary is the Ukrainian hryvnia. The functional currencies of the other foreign operations is the United States dollar (US$). As at the reporting date, the assets and liabilities of those subsidiaries having functional currency different from the Russian ruble are translated into the presentation currency of the Group (the Russian ruble) at the rate of exchange ruling at the reporting date and its statement of comprehensive income and cash flow statement are translated at the exchange rate prevailing at the date of transaction. The exchange differences arising on the translation are taken to a separate component of equity through other comprehensive income.

7.4.18 Impairment of non-financial assets

The Group assesses, at each reporting date, whether there is any indication that an asset or a cash-generating unit (CGU) may be impaired. The assets or CGUs subject to such assessment are primarily property, plant and equipment and trade marks. If any such indication exists, the Group makes an estimate of the asset's or CGU's recoverable amount. An asset's or CGU's recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use. The recoverable amount is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets. Where the carrying amount of an asset or CGU exceeds its recoverable amount, the asset or CGU is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessment of the time value of money and the risks specific to the assets or CGUs.

7.4.19 Government grants

Government grants are recognized where there is reasonable assurance that the grant will be received and all the attached conditions will be complied with. When the grant relates to an expense item, it is recognized as income on a systematic basis over the periods that the costs, which it is intended to compensate, are expensed. When the grant relates to an asset, it is recognized as income in accordance with amortization of the related asset.

7.4.20 Share-based payments

For equity-settled share-based payment transactions, the Group measures the goods or services received, and the corresponding increase in equity, directly, at the fair value of the goods or services received, unless that fair value cannot be estimated reliably. If the Group cannot estimate reliably the fair value of the goods or services received, the Group measures their value, and the corresponding increase in equity, indirectly, by reference to the fair value of the equity instruments granted.

7.5 Significant accounting judgments and estimates

The key assumptions concerning the future events and other sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next reporting year, are described below.

Impairment of non-financial assets other than goodwill

The determination of any impairment involves the use of estimates that include, but are not limited to, the cause, timing and amount of a cash flow. The determination of the recoverable amount of an asset or a cash-generating unit involves the use of estimates by management. Methods used to determine the value in use include discounted cash flow-based methods, which require the Group to make an estimate of the expected future cash flows from the asset or cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. These estimates, including the methodologies used, may have a material impact on the fair value and, ultimately, the amount of any asset impairment.

The following factors are considered in assessing impairment of major specific assets of the Group:

- Property, plant and equipment: changes in current competitive conditions, expectations of growth in the industry, increased cost of capital, changes in the future availability of financing, technological obsolescence, discontinuance of service, current replacement costs and other changes in circumstances that indicate impairment exists.
- Trademarks, patents, licenses and development costs: changes in current competitive conditions, changes in the regulations, expectations of growth in the industry, increased cost of capital, changes in the future availability of financing, introduction of alternative products on the market and other changes in circumstances indicating that impairment exists.

Impairment of goodwill

The Group determines whether goodwill is impaired at least on an annual basis. This requires an estimation of the value in use of the cash-generating units to which the goodwill is allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. The carrying amount of goodwill at 31 December 2016 is RR 1,604,692 (2015: RR 1,681,531). More details are provided in Note 11.

Allowance for doubtful accounts receivable

The Group maintains an allowance for doubtful accounts receivable to account for estimated losses resulting from the inability of customers to make required payments. When evaluating the adequacy of an allowance for doubtful accounts receivable, management bases its estimates on the aging of accounts receivable balances and historical write-off experience, customer credit worthiness and changes in customer payment terms. If the financial conditions of customers were to deteriorate, actual write-offs might be higher than expected. As at 31 December 2016, allowances for doubtful accounts receivable amounted to RR 1,134,349 (2015: RR 985,450). More details are provided in Note 13.

Write-down of inventories to net realizable value

The Group determines the adjustments for write-down of inventories to net realizable value based on their expected future value in use and realizable value. The net realizable value is the estimated selling price in the ordinary course of business less estimated costs of sale or distribution. Selling prices and costs of sale are subject to change as new information becomes available. Revisions to the estimates may significantly affect future operating results.

Current tax liabilities

Russian and Ukrainian tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Further, the interpretation of tax legislation by tax authorities as applied to the transactions and activity of the Group's entities may not coincide with that of management. As a result tax authorities may challenge transactions and the Group's entities may be assessed additional taxes penalties and interest, which can be significant.

In Russia and Ukraine the periods remain open to review by the tax and customs authorities with respect to tax liabilities for three calendar years preceding the year of review. Under certain circumstances, reviews may cover longer periods. As at 31 December 2016, management believes that its interpretation of the relevant legislation is appropriate and that the Group's tax, currency and customs positions will be sustained. More details are provided in Note 29.

Leases

The determination of whether an arrangement is, or contains a lease is based on the substance of the arrangement at the inception date of the lease, i.e. whether the fulfillment of the arrangement is dependent on the use of a specific asset or assets, or the arrangement conveys a right to use the asset.

7.6 Investments in joint venture NTS+

Main purpose of NTS+ is to participate in building of a research and development center in the Vladimir Region of the Russian Federation specialized in bioengineering of pharmaceutical products and universal diagnostic researches.

Movements in the carrying amount of investments were as follows:

	2016	2015
AT 1 JANUARY	**436,638**	**349,452**
Contribution to the share capital (without change in share)	–	112,926
Group's share of loss for the year	(64,148)	(25,740)
AT 31 DECEMBER	**372,490**	**436,638**

Summarized financial information of this joint venture and reconciliation with the carrying amount of the investment in consolidated financial statements are set out below:

	2016	2015
Current assets including cash and cash equivalents of RR 22,941 (2015: RR 37,413)	1,059,213	222,189
Property, plant and equipment, and other non-current assets	2,253,008	2,089,307
Current liabilities	(2,303,205)	(1,147,128)
Long-term loans and other non-current liabilities	(15,709)	–
EQUITY	**993,307**	**1,164,368**
Group's share as of 31 December	37,5%	37,5%
CARRYING AMOUNT OF THE INVESTMENT	**372,490**	**436,638**

Summarized statement of profit or loss of NTS+ is detailed below:

	2016	2015
General and administrative expenses	(160,293)	(147,885)
Financial expenses, net	(136,907)	(81,832)
Other income, including income from non-core operations and rent of RR 138,979 (2015: RR 130,960)	142,605	193,341
Other expenses	(17,112)	(7,840)
LOSS BEFORE INCOME TAX	**(171,707)**	**(44,216)**
Income tax benefit/(expense)	645	(24,424)
LOSS AND TOTAL COMPREHENSIVE LOSS FOR THE YEAR	**(171,062)**	**(68,640)**
GROUP'S SHARE OF LOSS AND TOTAL COMPREHENSIVE LOSS FOR THE YEAR	**(64,148)**	**(25,740)**

The Group has no any commitments in respect of the joint venture's operations.

7.7 Investments in associates

7.7.1 Investments in Argos Therapeutics, Inc

Argos Therapeutics, Inc. ("Argos") is a biopharmaceutical company registered in Delaware, USA, focused on the development and commercialization of fully personalized immunotherapy for the treatment of cancer and infectious diseases based on its Arcelis™ technology platform. In accordance with the share purchase agreement, the Company received the right to appoint two members to the Board of Directors. Therefore, the Company received a significant influence over Argos and recognized it as an associate, applying the equity method for its accounting.

In April and December 2015, Argos issued additional ordinary shares. As a result of these transactions the Group's interest in Argos was diluted to 27.65%. Dilution was accounted for as deemed disposal which resulted in a gain of RR 184,194 including accumulated foreign exchange gains of RR 3,276 reclassified to profit for the year.

In 2016, the Group purchased 7,258,730 shares from additional issue of Argos shares for cash consideration in the amount of US$ 38,881 thousand (RR 2,588,184). As a result of purchase of shares the Group's interest in Argos increased and resulting loss amounted to RR 283,263, including RR 20,276 accumulated foreign exchange loss reclassified to profit for the year.

Together with the shares of the additional issue, Argos distributed warrants providing the shareholder's with the right to purchase additional shares at a fixed price, as well as the possibility of cash settlement on a net basis. The effect of recognizing the obligation for warrants on the book value of the investment was RR 407,449 loss.

As of 31 December 2016, the Group's share was 32.10% (2015: 27.65%).

Movements in the carrying amount of investments were as follows:

	2016	2015
AT 1 JANUARY	**724,762**	**1,629,895**
Acquisition of shares	2,588,184	–
Group's share of loss for the year	(1,085,986)	(1,332,834)
(Loss)/gain from changes in the Group's share	(283,263)	184,194
Loss on recognition of warrants in Argos's financial statements	(407,449)	–
Foreign exchange differences in other comprehensive income	(167,102)	243,509
AT 31 DECEMBER	**1,369,146**	**724,764**

Summarized financial information about assets and liabilities of this associate is set out below:

	2016	2015
Cash and cash equivalents	3,213,201	449,187
Other current assets	153,366	193,186
Property, plant and equipment, and other non-current assets	2,529,550	1,626,553
Current liabilities	(1,856,698)	(594,928)
Non-current liabilities	(3,665,185)	(3,729,395)
EQUITY/(EQUITY DEFICIT)	**374,234**	**(2,055,397)**
Share of the Group's ownership as at 31 December	32,10%	27,65%
CARRYING NET ASSETS/(DEFICIT)	**120,129**	**(568,284)**
Goodwill arising from acquisition of shares of the associate	1,249,017	1,293,048
CARRYING AMOUNT OF INVESTMENTS	**1,369,146**	**724,764**

Summarized statement of comprehensive income of Argos is detailed below:

	2016	2015
Revenue	63,379	31,596
Research and development expenses	(2,567,922)	(3,782,732)
General and administrative expenses	(952,117)	(671,208)
Other expenses	(98,075)	(136,607)
LOSS AND TOTAL COMPREHENSIVE LOSS FOR THE YEAR	**(3,554,735)**	**(4,558,951)**
The Group's share of loss for the year	(1,085,986)	(1,332,834)
(Loss)/gain from changes in the Group's share	(283,263)	184,194
Loss on recognition of warrants in Argos's financial statements	(407,449)	–
TOTAL RECOGNIZED IN LOSS FOR THE YEAR	**(1,776,698)**	**(1,148,640)**

7.7.2 Investments in Biocad Holding Limited

Biocad Holding Limited ("Biocad") is a company registered under the law of Cyprus. It is the controlling shareholder in several companies involved in the research and development, production and distributing of various pharmaceutical and biopharmaceutical products, primarily in the Russian Federation. These major subsidiaries are Russian legal entities: Biocad CJSC, Biocad Pharm LLC, I-Mab LLC. Biocad has also several insignificant subsidiaries registered in other jurisdictions.

In accordance with the shareholder's agreement, the Group obtained significant influence over strategic and operating policies of the Biocad, so it is recognized as associate applying the equity method of accounting.

As of 31 December 2016, the Group's share in Biocad was 20% (2015: 20%).

Movements in the carrying amount of investments were as follows:

	2016	2015
AT 1 JANUARY	**5,068,895**	**4,339,963**
Group's share of profit for the year	631,540	802,901
Effect of the pre-acquisition profit distribution (a)	–	(73,969)
Dividends	(1,190,681)	–
Forex in other comprehensive income	(80,995)	–
AT 31 DECEMBER	**4,428,759**	**5,068,895**

(a) According to agreement the Company was not entitled to receive dividends from the pre-acquisition profit.

Summarized financial information of assets and liabilities of Biocad is set out below:

	2016	2015
Cash and cash equivalents	1,804,167	3,903,375
Other current assets	5,748,497	6,967,355
Property, plant and equipment	2,869,038	1,560,173
Intangible assets	3,362,360	4,042,122
Trade and other payables	(1,323,921)	(825,416)
Other current liabilities	(307,149)	(206,947)
Non-current liabilities	(1,531,077)	(1,618,069)
EQUITY	**10,621,915**	**13,822,593**
Share of the Group's ownership	20%	20%
CARRYING VALUE OF NET ASSETS	**2,124,383**	**2,764,519**
Goodwill arising from acquisition of the associate	2,304,376	2,304,376
CARRYING AMOUNT OF INVESTMENTS	**4,428,759**	**5,068,895**

Summarized consolidated statement of profit or loss of Biocad is detailed below:

	2016	2015
Revenue	11,724,199	9,048,736
Cost of sales	(2,103,260)	(1,096,119)
Research and development expenses	(2,302,948)	(1,081,565)
General and administrative expenses	(2,960,659)	(2,431,745)
Other expenses, net	(479,802)	171,755
Income tax expense	(719,830)	(596,557)
PROFIT FOR THE PERIOD	**3,157,700**	**4,014,505**
GROUP'S SHARE OF PROFIT FOR THE PERIOD	**631,540**	**802,901**

7.8 Segment information

For the management purposes, the Group is divided into two reportable operating segments: (1) production and wholesale of pharmaceutical products and (2) production and wholesale of medical equipment.

No operating segments have been aggregated to form the above reportable operating segments.

Management monitors the segments' assets, liabilities, sales, gross profit, segments' results and budgets of these business segments separately for the purpose of making decisions about resource allocation and performance assessment. For the management purposes, budgets of income and expense are planned and analyzed for each of operating segments separately.

Segment result is segment revenue less segment expenses. Segment expenses consist of cost of sales, selling and distribution costs, general and administrative expenses and other income and expenses that can be directly attributed to the segment on a reasonable basis.

Segment assets consist primarily of property, plant and equipment, intangible assets including goodwill allocated to specified segment, inventories, financial assets, receivables and operating cash. Segment liabilities comprise operating liabilities and exclude items such as taxation and certain corporate liabilities. Capital expenditures comprise additions to property, plant and equipment.

There were no significant intercompany transactions between these operating segments.

The following tables present revenue and profit information regarding the Group's operating segments:

Year ended 31 December 2016	**Production and wholesale of pharmaceutical products (Pharmaceutical products)**	**Production and wholesale of medical equipment**	**Group**
Sales to external customers	59,980,202	1,806,222	61,786,424
TOTAL REVENUE	**59,980,202**	**1,806,222**	**61,786,424**
Gross profit	21,068,473	384,986	21,453,459
SEGMENT RESULT	**10,799,663**	**64,123**	**10,863,786**
Interest income, net			1,098,279
Share in loss of a joint venture and associates, net			(1,209,306)
PROFIT BEFORE INCOME TAX			**10,752,759**
Income tax expense			(2,750,482)
PROFIT FOR THE YEAR			**8,002,277**
Segment assets	92,069,387	1,522,410	93,591,797
Unallocated assets			917,773
TOTAL ASSETS			**94,509,570**
Segment liabilities	26,826,016	199,738	27,025,754
Unallocated liabilities			4,688,194
TOTAL LIABILITIES			**31,713,948**

Year ended 31 December 2016	Production and wholesale of pharmaceutical products (Pharmaceutical products)	Production and wholesale of medical equipment	Group
Acquisition of property, plant and equipment (Note 10)	2,911,854	25,068	2,936,922
Depreciation and amortization (Notes 10 and 11)	1,331,466	18,537	1,350,003
Reversal of impairment loss on property, plant and equipment (Note 10)	1,860	53,373	55,233
Loss from impairment of intangible assets (Note 11)	14,895	–	14,895

As at 31 December 2016, unallocated liabilities of RR 4,688,194 include loans and borrowings of RR 4,004,769, income tax payable of RR 341,283 and deferred tax liability of RR 342,142.

Year ended 31 December 2015	Production and wholesale of pharmaceutical products (Pharmaceutical products)	Production and wholesale of medical equipment	Group
Sales to external customers	45,619,799	1,575,139	47,194,938
TOTAL REVENUE	**45,619,799**	**1,575,139**	**47,194,938**
Gross profit	17,398,803	398,537	17,797,340
SEGMENT RESULT	**17,666,051**	**(95,594)**	**17,570,457**
Interest income, net			478,898
Share in loss of a joint venture and associates, net			(371,479)
PROFIT BEFORE INCOME TAX			**17,677,876**
Income tax expense			(3,746,776)
PROFIT FOR THE YEAR			**13,931,100**
Segment assets	79,908,489	1,823,308	81,731,797
Unallocated assets			889,820
TOTAL ASSETS			**82,621,617**
Segment liabilities	21,920,571	575,268	22,495,839
Unallocated liabilities			4,697,265
TOTAL LIABILITIES			**27,193,104**
Acquisition of property, plant and equipment (Note 10)	2,232,838	17,960	2,250,798
Depreciation and amortization (Notes 10 and 11)	1,114,500	28,999	1,143,499
Loss from impairment of property, plant and equipment (Note 10)	27,850	92,477	120,327

As at 31 December 2015, unallocated liabilities of RR 4,697,265 include loans and borrowings of RR 4,006,828, income tax payable of RR 375,169 and deferred tax liability of RR 315,268.

The main assets of the Group are located in the Russian Federation, and revenue is mainly generated from transactions in the Russian Federation.

Revenue from sales to one customer in the Pharmaceutical products segment individually amounted to more than 10% of the Group's total revenue in this segment:

CUSTOMER	2016	2015
Ministry of Health of the Russian Federation and its regional branches (only open public tenders)	19,037,815	13,615,890
Sales share	31%	29%

7.9 Balances and transactions with related parties

2016	Short-term financial assets – (a), Note 15	Cash and short-term deposits placed with the related bank – Note 14	Trade and other receivables and prepayments – (c) Note 13	Trade and other payables – (d) Note 19
Parent	10,263,282	–	–	–
Other related parties	54,516	–	911,701	7,326,962
Joint venture	2,000,677	–	140,110	6,585
TOTAL	**12,318,475**	**–**	**1,051,811**	7,333,547

2015	Short-term financial assets – (a), Note 15	Cash and short-term deposits placed with the related bank – Note 14	Trade and other receivables and prepayments – (c) Note 13	Trade and other payables – (d) Note 19
Parent	10,904,479	–	–	–
Other related parties1	1,323,961	12,346,788	2,836,072	3,167,863
Joint venture	816,995	–	116,500	704
TOTAL	**13,045,435**	**12,346,788**	**2,952,572**	3,168,567

(a) This item is detailed in sub-sections "Loans provided to parent", "Loans provided to Joint venture and other related parties" and "Promissory notes of related parties" below.

(b) This item is primarily comprised of receivables from PJSC "OTCPharm" (OTCPharm) for sale of raw materials, finished products and contract manufacturing services, agency fee receivables from sale of certain related party products and prepayments for rent and other services.

(c) This item primarily comprised payables to OTCPharm for sales of branded OTC medicines in accordance with the agency agreement in the amount of RR 6,233,263 as of 31 December 2016 (2015: RR 2,380,642).

Significant transactions with related parties

STATEMENT OF COMPREHENSIVE INCOME ITEM	RELATIONSHIP	2016	2015
Agency fee income (included in revenue) (A)	Other related parties	1,736,084	1,177,419
Contract manufacturing revenue from OTCpharm and Biocad (included in revenue) (B)	Other related parties	3,439,780	2,437,685
Revenue from sale of active pharmaceutical ingredients to OTCPharm (included in revenue) (C)	Other related parties	1,792,149	877,481
Revenue from sale of finished products to OTCPharm (included in revenue) (C)	Other related parties	407,514	56,131
Revenue from sale of third-parties products (included in revenue)	Associate and other related parties	4,438	34,401
Revenue from sale of third-parties products to OTCPharm (included in revenue) (C)	Other related parties	-	183,023
Interest income from deposits placed with the related bank	Other related parties	-	10,604
Interest income from loans provided to the parent and other related parties	Parent and other related parties	776,063	603,372
License fees (included in selling and distribution cost)	Other related parties	(34)	(1,429)
Warehouse rental expenses (included in selling and distribution cost)	Other related parties	(5,584)	(65,992)
Office rental expenses (included in general and administrative expenses)	Other related parties	(27,475)	(140,455)
Cost of sales (D)	Other related parties	(2,245,347)	(213,112)
Consulting on venture investments (included in general and administrative expenses) (E)	Other related parties	(90,515)	(97,908)
Other income (F)	Other related parties	180,525	658,280
Other expenses	Other related parties	(10,285)	(11,246)
Advertising	Other related parties	-	(8,157)
Research and development expenditures	Other related parties	(35,864)	(4,708)
Purchase of promissory notes from the related bank (H)	Other related parties	-	5,063,068
Sale of promissory notes to the related bank (H)	Other related parties	-	786,698
Purchase of land, buildings and other property, plant and equipment	Other related parties	104,745	39,962
Income from sale of R&D	Other related parties	36,835	-
Purchase of R&D	Other related parties	(13,129)	(14,222)

(A) Agency fee income

The Company entered into agency contracts with related parties for distribution and sales of certain medicines owned by those related parties.

(B) Contract manufacturing revenue

The Group entered into a number of contract manufacturing agreements with OTCPharm for production of over-the-counter medicines and also with Biocad for production of Rx medicines (Note 22).

(C) Revenue from sales to OTCPharm

The Group supplies certain APIs and finished products to OTCPharm in accordance with the standard distribution agreements (Note 22).

(D) Cost of sales

The Group entered into purchase agreements for supply of third-party products (mainly Koagil VII and Diaskintest) manufactured by a related party. Total cost of sales in the amount of RR 2,245,347 (2015: RR 213,112) comprises the cost of the above medicines of RR 1,365,340 (2015: RR 195,862), which the Group mainly sold at open public tenders. The remaining amount included in cost of sales primarily represents cost of raw materials and third-party products purchased from other related parties.

As at 31 December 2016, outstanding inventories of these products amounted to RR 146,424 (31 December 2015: RR 62,278).

(E) Consulting on venture investments

This item primarily comprises expenses on venture investments consulting incurred by a related party in the course of search, analysis and monitoring of operations of R&D startups, which may be potential investment targets of Pharmstandard International S.A.

(F) Other income

Other income primarily includes income from operating lease of cars and warehouses to OTCPharm, income from royalty, utilities, sale of materials and other income from transactions with other related parties.

(G) Purchase of promissory notes

Beginning 1 January 2016, related bank stopped being related to the Group. So the Group accounts for sales and payments of promissory notes held as of 31 December 2015 as transactions with third parties.

In 2015, the Group purchased short-term promissory notes from the related bank for RR 2,479,668. The par value of the promissory notes is RR 2,500,000. As at 31 December 2015, the Group recognized the promissory notes as cash and short-term deposits. Further, the Group sold them in January 2016 and recognized income from sale in the amount of RR 20,329.

In 2015, the Company purchased ordinary promissory notes of the related bank, which were recognized as short-term financial assets of RR 1,173,411 as at 31 December 2015 (refer to Promissory notes of related parties section below).

In 2015, the Group purchased promissory notes of the third parties for cash consideration of RR 780,817 from the related bank and then sold them back to the related bank for cash consideration in the amount RR 786,698. Income from this transaction was recognized in the amount of RR 5,881 (Note 26).

In 2015, the Group purchased promissory notes of RR 629,172 from the related bank. Further the Group sold those promissory notes to a third party for cash consideration of RR 633,930 and recognized income from this transaction in the amount of RR 4,758 (Note 26).

Loans issued to the parent

In 2015 and 2016, the Company's parent, Augment Investments Limited ("Augment") registered under the laws of Cyprus, asked the Company to issue short-term interest-bearing loans for financing Augment's current business operations not related to the activities of the Group.

As at 31 December 2016, the outstanding amount of unsecured short-term loans issued to Augment amounted to US$ 169,202 thousand (RR 10,263,282) including interest payable in amount US$ 14,482 thousand (RR 878,447) and bearing interest of 5% to 6.19% p.a. (LIBOR + 4.5%) (2015: US$ 151,224 thousand (RR 10,904,479) including interest payable US$ 9,624 thousand (RR 584,289); interest rate of 4% to 5.25% p.a.). Loans are unsecured.

In 2016, the Company's parent has repaid part of loans in total amount of US$ 10,000 thousand (RR 733,596). All other loans' maturity dates were extended until 2017.

In 2016 the Group has issued new loans in total amount of US$ 23,120 thousand (RR 1,736,199). The maturity date is 2017.

Loans issued to associate and other related parties

In 2015 and 2016, the Company issued to a joint venture several unsecured short-term loans in Rubles bearing interest of 12% to 15% p.a. In 2016, joint venture has repaid part of the loan in the amount of RR 75,000. The remaining loans were extended until 2017.

In 2016, the Company issued loans of RR 1,070,300 bearing an interest of 12% to 15% p.a. The maturity date is in 2017.

As of 31 December 2016 outstanding amount of unsecured short-term loans to joint venture was RR 2,000,677, including interest in amount RR 246,527.

As of 31 December 2016 outstanding amount of unsecured short-term loans to other related party was RR 111,972, including interest in amount RR 11,972, and interest rate was 10% p.a. In 2016, the other related party ceased to meet the criteria of affiliation with the Group.

In 2016, the Company issued loans to other related party in the amount of RR 109,015, including interest accrued RR 11,515, with an interest rate of 13% p.a. In 2016 an impairment allowance was accrued for one of the loans in the total amount of RR 54,499 due to the poor financial position of the borrower. As of December 31, 2016, the outstanding amount of an unsecured short-term loan, net of a provision, was RR 54,516, including interest payable RR 5,766.

Promissory notes of related parties

In 2015, the Company purchased ordinary promissory notes of the related bank with par value of US$ 10,500 thousand and US$ 5,600 thousand, bearing an interest rate of 4% p.a. The promissory notes are payable on demand, but not earlier that 7 August 2017 and not later than 9 August 2017. The acquisition price amounted to 100% of the par value of the promissory notes. The promissory notes were pledged to the related bank as collateral for a third party's bank guarantee. In December 2015, the collateral agreements were early terminated. These promissory notes were early repaid on 19 January 2016.

As at 31 December 2015, the promissory notes in the amount of RR 1,211,989 were recorded as short-term financial assets.

Compensation to key management personnel

For the year ended 31 December 2016, total compensation to key management personnel amounted to RR 112,729 (2015: RR 71,551). Such compensation represents payroll and bonuses included in general and administrative expenses.

7.10 Property, plant and equipment

Property, plant and equipment consist of the following:

Balance at 31 December 2016	Land	Buildings	Plant and machinery	Equipment, motor vehicles and other	Assets under construction	Total
COST						
BALANCE AT 1 JANUARY 2016	**451,720**	**5,475,863**	**7,170,967**	**1,082,146**	**2,072,289**	**16,252,985**
Additions	8,152	100,115	106,117	193,364	2,529,174	2,936,922
Transfers	–	488,628	835,987	55,951	(1,380,566)	–
Disposals	(14)	(5,046)	(147,103)	(78,510)	(191,954)	(422,627)
Foreign exchange differences	–	(41,336)	(57,748)	(4,869)	(28,208)	(132,161)
BALANCE AT 31 DECEMBER 2016	**459,858**	**6,018,224**	**7,908,220**	**1,248,082**	**3,000,735**	**18,635,119**
ACCUMULATED DEPRECIATION AND IMPAIRMENT						
BALANCE AT 1 JANUARY 2016	**–**	**1,042,603**	**3,793,440**	**471,753**	**126,340**	**5,434,136**
Depreciation charge	–	172,991	818,047	203,683	–	1,194,721
Disposals	–	(1,255)	(89,159)	(55,113)	–	(145,527)
Impairment charge, net (Notes 26, 27)	–	30,155	(52,703)	(40)	(32,645)	(55,233)
Foreign exchange differences	–	(10,253)	(26,169)	(2,863)	(11,789)	(51,074)
BALANCE AT 31 DECEMBER 2016	**–**	**1,234,241**	**4,443,456**	**617,420**	**81,906**	**6,377,023**
NET BOOK VALUE						
BALANCE AT 1 JANUARY 2016	**451,720**	**4,433,260**	**3,377,527**	**610,393**	**1,945,949**	**10,818,849**
BALANCE AT 31 DECEMBER 2016	**459,858**	**4,783,983**	**3,464,764**	**630,662**	**2,918,829**	**12,258,096**

Balance at 31 December 2015	Land	Buildings	Plant and machinery	Equipment, motor vehicles and other	Assets under construction	Total
COST						
BALANCE AT 1 JANUARY 2015	**442,564**	**5,025,080**	**5,939,127**	**920,834**	**2,012,973**	**14,340,578**
Additions	9,156	35,974	155,585	284,256	1,765,827	2,250,798
Transfers	–	436,637	1,231,139	4,437	(1,672,213)	–
Disposals	–	(1,657)	(130,631)	(125,746)	(13,516)	(271,550)
Foreign exchange differences	–	(20,171)	(24,253)	(1,635)	(20,782)	(66,841)
BALANCE AT 31 DECEMBER 2015	**451,720**	**5,475,863**	**7,170,967**	**1,082,146**	**2,072,289**	**16,252,985**

Balance at 31 December 2015	Land	Buildings	Plant and machinery	Equipment, motor vehicles and other	Assets under construction	Total
ACCUMULATED DEPRECIATION AND IMPAIRMENT						
BALANCE AT 1 JANUARY 2015	**–**	**807,136**	**3,199,550**	**417,051**	**99,510**	**4,523,247**
Depreciation charge	–	162,486	654,988	170,743	–	988,217
Disposals	–	(1,025)	(66,499)	(115,173)	–	(182,697)
Impairment charge, net (Notes 26, 27)	–	77,540	15,222	226	27,339	120,327
Foreign exchange differences	–	(3,534)	(9,821)	(1,094)	(509)	(14,958)
BALANCE AT 31 DECEMBER 2015	**–**	**1,042,603**	**3,793,440**	**471,753**	**126,340**	**5,434,136**
NET BOOK VALUE						
BALANCE AT 1 JANUARY 2015	**442,564**	**4,217,944**	**2,739,577**	**503,783**	**1,913,463**	**9,817,331**
BALANCE AT 31 DECEMBER 2015	**451,720**	**4,433,260**	**3,377,527**	**610,393**	**1,945,949**	**10,818,849**

In 2016, the Group accrued an allowance for impairment of property, plant and equipment due to their conservation and uncertain plans for the further use, and also reversed allowance accrued in prior periods for objects being in use in 2016.

In 2016 and 2015, the Group did not receive any loans for capital construction and had no new qualifying assets, therefore no borrowing costs were capitalized.

The Group assets include only a minor portion of land on which the Group's factories and buildings, comprising the Group's principal manufacturing facilities, are located, whilst the major portion of the land is held under operating lease agreements with the state municipal bodies. The lease agreements specify lease terms between 1 and 20 years. Long-term agreements have an option to extend the lease term for another 10 years and include a land purchase option after termination of the lease. Purchase price will be determined based on fair value of the land as determined by the municipal authorities. The total amount of rental payments for the use of the land during 2016 was RR 35,521 (2015: RR 32,182). Such payments are reassessed by the state authorities on an annual basis. No such reassessment has been completed for 2017 and beyond as at the date of approval of these consolidated financial statements for issue.

In 2014, the Group entered into a number of operating lease agreements with OTCPharm, a related party. In accordance with agreements the Group leased out to OTCPharm cars and warehouses with net book value of RR 159,336 as at 31 December 2016 (2015: RR 194,766). Income from operating lease in the amount of RR 139,947 is recognized as other income (2015: RR 128,261) (Notes 9 and 26).

7.11 Intangible assets

31 December 2016	Goodwill	Trademarks, patents and licenses	Development costs	Total
COST				
BALANCE AT 1 JANUARY 2016	**1,681,531**	**1,478,483**	**816,582**	**3,976,596**
Additions	–	–	491,968	491,968
Disposals (Note 27)	–	–	(924,492)	(924,492)
Foreign exchange differences	(76,839)	–	–	(76,839)
BALANCE AT 31 DECEMBER 2016	**1,604,692**	**1,478,483**	**384,058**	**3,467,233**
ACCUMULATED AMORTIZATION AND IMPAIRMENT				
BALANCE AT 1 JANUARY 2016	**–**	**422,090**	**–**	**422,090**
Amortization	–	155,282	–	155,282
Impairment (Note 27)	–	14,895	–	14,895
BALANCE AT 31 DECEMBER 2016	**–**	**592,267**	**–**	**592,267**
NET BOOK VALUE				
BALANCE AT 1 JANUARY 2016	**1,681,531**	**1,056,393**	**816,582**	**3,554,506**
BALANCE AT 31 DECEMBER 2016	**1,604,692**	**886,216**	**384,058**	**2,874,966**

31 December 2015	Goodwill	Trademarks, patents and licenses	Development costs	Total
COST				
BALANCE AT 1 JANUARY 2015	**1,730,040**	**1,478,483**	**180,882**	**3,389,405**
Additions	–	–	635,700	635,700
Foreign exchange differences	(48,509)	–	–	(48,509)
BALANCE AT 31 DECEMBER 2015	**1,681,531**	**1,478,483**	**816,582**	**3,976,596**
ACCUMULATED AMORTIZATION AND IMPAIRMENT				
BALANCE AT 1 JANUARY 2015	**–**	**266,808**	**–**	**266,808**
Amortization	–	155,282	–	155,282
BALANCE AT 31 DECEMBER 2015	**–**	**422,090**	**–**	**422,090**
NET BOOK VALUE				
BALANCE AT 1 JANUARY 2015	**1,730,040**	**1,211,675**	**180,882**	**3,122,597**
BALANCE AT 31 DECEMBER 2015	**1,681,531**	**1,056,393**	**816,582**	**3,554,506**

Carrying amount and remaining amortization period of major trademarks and patents as at 31 December are as follows:

Name	Carrying amount		Remaining amortization period (years)	
	2016	2015	2016	2015
SIRTURO®	614,210	690,987	7	8
EPOSTIM®	105,247	124,383	6	7
PEGALTEVIR®	61,823	105,487	3	4

Impairment testing of goodwill

Goodwill acquired through business combinations has been allocated for impairment testing purposes to the following groups of cash-generating units, which are also reportable segments of the Group:

/ Production and wholesale of pharmaceutical products unit (Pharmaceutical products); and
/ Production and wholesale of medical equipment unit (Medical equipment).

Carrying amount of goodwill allocated to each cash generating unit:

	Pharmaceutical products		Equipment		Total	
	2016	2015	2016	2015	2016	2015
CARRYING AMOUNT OF GOODWILL	1,385,838	1,462,677	218,854	218,854	1,604,692	1,681,531

Decrease of carrying amount of goodwill in the Pharmaceutical products segment resulted from foreign exchange differences arising from translation of the subsidiaries' results into the Russian rubles.

The recoverable amount of the cash-generating units was based on a value-in-use calculation using actual cash flow projections obtained from the five-year financial budgets approved by management (average growth rate of 1.4%); the cash flow projections beyond the five-year period were conservative. They were calculated using the extrapolation method and did not account for the potential market growth. The discount rate applied to cash flow projections is 12.78% (2015: 9.19%).

Key assumptions used in value-in-use calculations

The calculation of value-in-use for both Pharmaceutical products and Equipment cash-generating units is most sensitive to the following assumptions:

/ Discount rates;
/ Raw materials price inflation;
/ Currency rates changes;
/ Growth rates used to extrapolate cash flows beyond the budget period.

Discount rates – discount rates reflect management's estimate of the risks specific to each unit. This is the benchmark used by management to assess operating performance and to evaluate future investment proposals. In determining appropriate discount rates for each unit, regard has been given to the Capital Assets Pricing Model calculation at the reporting date.

Raw material price inflation – past actual raw materials price movements, including the effect of the devaluation of the Russian ruble for US dollar denominated raw materials, have been used as an indicator of future price movements.

Currency exchange rates changes – estimated values based on current values on the foreign exchange market.

Growth rate estimates – rates are based on published industry research.

Sensitivity to changes in assumptions

Management believes that no reasonably possible change in any of the above key assumptions would cause the carrying value of the each cash-generating unit to materially exceed its recoverable amount.

7.12 Inventories

Inventories consist of the following:

	2016	2015
Raw materials – at cost	3,155,998	3,187,204
Work in progress – at cost	1,824,281	936,366
Finished products – at net realizable value	7,901,672	6,076,612
	12,881,951	**10,200,182**

The write-downs of inventories to net realizable value and reversal of write-downs were as follows:

	2016	2015
BALANCE AT 1 JANUARY	175,489	136,209
Additional write-downs	303,961	154,699
Unused amounts reversed	(30,359)	(16,317)
Utilized during the year	(47,015)	(100,843)
Foreign exchange differences	(2,650)	1,741
BALANCE AT 31 DECEMBER	399,426	175,489

7.13 Trade and other receivables

	2016	2015
Trade receivables (net of allowance for impairment of RR 1,134,349 (2015: RR 985,450))	16,242,844	13,468,997
Trade receivables – related parties (Note 9)	913,832	2,516,872
Other receivables – related parties (Note 9) (a)	122,897	360,699
	17,279,573	**16,346,568**

(a) Major part of other receivables comprises the royalties payable.

As at 31 December 2016, RR 838,287 of trade and other receivables were denominated in currencies other than Russian ruble (primarily in US dollars) (2015: RR 2,682,171).

Movements in the allowance for impairment of trade receivables were as follows:

	2016	2015
BALANCE AT 1 JANUARY	985,450	225,186
Additional allowance	687,803	890,950
Unused amounts reversed	(526,365)	(128,987)
Utilized during the year	(6,472)	(1,146)
Foreign exchange differences	(6,067)	(553)
BALANCE AT 31 DECEMBER	1,134,349	985,450

7.14 Cash and short term deposits

Cash and short-term deposits consist of the following:

	2016	2015
Cash in bank – Russian rubles	9,902,149	2,052,124
Cash in bank – US dollars and euro	6,705,949	2,953,997
Cash at bank – Ukrainian hryvnia	5,338	1,285
Short-term trade promissory notes with the maturity of less than 90 days (Note 9)	–	2,479,668
Short-term bank deposits – Russian rubles (a)	418,162	553,808
Short-term bank deposits – US dollars and euro (a)	121,544	1,039,615
Short-term bank deposits placed with the related bank, provided as collateral – euro (c) (Note 9)	–	996,226
Short-term bank deposits – Ukrainian hryvnia	84,373	72,624
Short-term bank deposits placed with the related bank – Russian ruble (a) (Note 9)	–	2,604,700
Short-term bank deposits placed with the related bank – US dollars (a) (Note 9)	–	1,513,741
Short-term deposits to secure participation in open public tenders – Russian rubles (b)	149,063	129,453
	17,386,578	**14,397,241**

(a) Deposits denominated in Russian rubles bear interest rates of 7.62% to 8.47% p.a. (2015: 6.5% to 10.65% p.a.). Deposits denominated in US dollars and euro bear interest rates of 0.79% p.a. (2015: 0.2% to 1.17% p.a.)

(b) These cash deposits are restricted for use and are placed to secure the Group's participation in open public tenders.

(c) As at the reporting date, these deposits denominated in euro were provided as collateral to the related bank. The interest rate was 0.6%. In February 2016, the deposits were released from pledge; the deposits were early terminated.

In 2015 substantially all cash and short-term deposits of the Group were placed in the related bank (Note 9). Cash balances with the related bank carry no interest. Since 1 January 2016, this bank has ceased to be related.

7.15 Short-term financial assets

	2016	2015
SHORT-TERM LOANS AND DEPOSITS		
Short-term loan issued to the parent – US dollars (Note 9)	10,263,282	10,904,479
Short-term loans issued to third parties – Russian rubles (a)	253,376	–
Short-term loans issued to third parties – US dollars (b)	2,463,058	1,067,538
Promissory notes – Russian rubles	–	1,337,136
Promissory notes in the related bank – US dollars(Note 9)	–	1,211,989
Short-term loans issued to related parties – Russian rubles (Note 9)	2,109,692	928,967
Short-term bank deposits – US dollars	286,692	–
Short-term bank deposits – Russian rubles	–	202,217
Allowance for impairment of loans issued to third parties (b)	–	(1,067,538)
Allowance for impairment of loans issued to related parties (Note 9)	(54,499)	–
INVESTMENTS AVAILABLE FOR SALE		
Securities and other	20,753	13,261
	15,342,354	**14,598,049**

(a) In 2016, the Company provided unsecured short-term loans to third parties with maturity in 2017 and fixed interest rate of 10.00% to 13.00% p.a (2015: 6.5% to 18% p.a).

(b) In 2015, the Company provided secured loan bearing fixed interest rate of 9% p.a. to a third-party to finance certain projects that were of potential interest to the Group in the future. In 2015, due to a violation of the loan repayment schedule, the Group accrued bad debt allowance in the amount of RR 1,067,538 for the loan and interest receivable. In April 2016, this loan was restructured and partially reclassified to long-term financial assets in the amount of RR 664,125 according to a new debt repayment schedule. Bad debt allowance was released because the borrower complied with the payment schedule (Note 26).
In addition, in 2014-2015 the Company provided to another third-party unsecured long-term loans maturing on 31 December 2017 and bearing fixed interest rate of 9% p.a. to finance certain investment project of potential interest to the Group in the future, and loan repayment is secured with the future economic benefits from this project, estimated by the management of the Group on the basis of relevant long-term business plans. In 2016, this loan was reclassified to short-term financial assets in the amount of RR 2,180,654 in accordance with its maturity.

7.16 Long-term financial assets

	2016	2015
LONG-TERM LOANS AND DEPOSITS		
Long-term loans issued to third party – Russian rubles (a)	–	38,100
Long-term loan issued to third party – US dollars (Note 15b)	664,125	2,180,654
Other long-term assets	10,816	8,076
INVESTMENTS AVAILABLE FOR SALE		
Quoted equity shares	6,096,337	1,317,317
Unquoted equity shares	1,836,906	1,279,895
	8,608,184	**4,824,042**

(a) On 9 June 2014 the Company issued unsecured long-term loan to third party with fixed interest rate of 15% p.a. The loan was closed before maturity as of 31 December 2016.

As at 31 December 2016, financial investments available for sale include the following quoted equity shares:

(i) RR 1,315,202 (2015: RR 343,291) investments in preferred (further converted into ordinary) and ordinary shares of Protagonist Therapeutics, Inc. ("Protagonist") registered in the USA, Delaware. Protagonist is developing orally stable peptides and peptidomimetics for treatment of methabolic and inflammatory bowel diseases. Since 2016, Protagonist shares have been listed on NASDAQ, the fair value of investments in Protagonist is determined on the basis of published quotations of prices in the active market. The increase in the cost of investments for the 12 months of 2016 is reflected in the revaluation reserve for available-for-sale instruments and is reflected in other comprehensive income in the amount of RR 793,300 (net of disposal of the reserve for revaluation of investments in connection with the sale of a portion of shares reflected in other comprehensive income in the amount of RR 89,360)

(ii) RR 1,134,304 (2015: RR 1,317,317) investments in preferred (further converted into ordinary) and ordinary shares of Proteon Therapeutics, Inc. ("Proteon") registered in the USA, Delaware. Proteon is a biopharmaceutical company developing novel, first-in-class pharmaceuticals to improve the patency and functional lifetime of arteriovenous fistula for patients with renal and vascular diseases; Proteon is listed on NASDAQ, fair value of investment in Proteon is determined by reference to published price quotations on active market. The decrease in the cost of investments for the 12 months of 2016 is reflected in other comprehensive income in the amount of RR 1,048,530.

(iii) RR 4,646,831 investments in ordinary shares of related party PJSC OTCPharm located in Moscow, Russian Federation. OTCPharm is the largest company in the Russian pharmaceutical market of OTC products. The main activity of OTCPharm and its subsidiaries is the production, marketing and promotion, distribution of pharmaceutical products. Shares of OTCPharm are listed on the Moscow Stock Exchange, the fair value of investments in OTCPharm is determined based on published quotes in the active market. The decrease in the cost of investments for the 12 months of 2016 is reflected in the revaluation reserve for available-for-sale instruments in the amount of RR 116,145 (effect of income tax amounted RR 23,229.)

As at 31 December 2016, financial investments available for sale include following unquoted equity shares:

(i) RR 429,488 (2015: RR 516,054) investments in preferred shares of Allena Pharmaceuticals ("Allena") registered in the USA, Delaware. Allena is a company developing and commercializing non-systemic protein therapeutics to treat metabolic and orphan diseases, including hyperoxaluria and kidney stones.

(ii) RR 46,719 (2015: RR 56,136) investments in preferred shares of Engene Inc. ("Engene"), located in Canada, Montreal. Engene works with a highly flexible nucleotide delivery technology targeting mucosal tissues to treat numerous prevalent and chronic diseases via the induction or suppression of protein expression levels.

(iii) RR 303,284 (2015: RR 364,414) investments in preferred (further converted into ordinary) and ordinary shares of Jounce Therapeutics Inc ("Jounce"), registered in the USA, Delaware. Jounce is working on creation of cancer treatment mechanisms that ensure an optimal involvement of the immune system.

(iv) RR 395,133 investments in preferred shares of TransMedics, Inc. ("TransMedics"), registered in the state of Delaware, USA. TransMedics specializes in the development of portable medical devices, the Organ Care System (OCS LUNG, OCS HEART, OCS LIVER) for improved quality, viability and utilization of organs intended for transplantation.

(v) RR 151,642 investments in preferred shares of Avelas Biosciences, Inc. ("Avelas"), registered in the state of Delaware, USA. Avelas develops peptide products cleaved by matrix metalloproteinases to form cell-penetrating peptides conjugated with fluorophore for intraoperative fluorescence diagnostics of the positive surgical edge of the tumor, as well as regional lymph nodes.

(vi) RR 60,658 investments in privileged shares of Cleome Holdings Limited, registered in the Republic of Cyprus, owning a group of companies that provide services in the field of personal and medical genetics (providing customers with access to genetic information, full genome sequencing services).

(vii) RR 424,598 investments in preferred shares of Neon Therapeutics, Inc. (hereinafter referred to as Neon), registered in the state of Delaware, USA. Neon is developing personalized neoepitope vaccines for the treatment of oncological diseases, based on tumor sequencing data and proprietary bioinformatics algorythm.

(viii) Warrants in the amount of RR 25,384, giving the right to purchase ordinary shares of Argos Theraputics. Inc.

The Group has no control or significant influence over these entities.

7.17 Short-term borrowings and loans

	2016	2015
Short-term loan – Russian rubles (a)	4,069,261	4,087,522
Other loans	1,533	1,914
	4,070,794	**4,089,436**

(a) As at 31 December 2016, this item included RR 4,003,653 unsecured loan issued by Sberbank, with an interest rate of 9.87% p.a., and RR 65,608 unsecured loan with an interest rate of 7.5% p.a. (2015: RR 4,004,914, issued by Sberbank, with an interest rate of 11.85% p.a. and RR 82,608 unsecured loan with an interest rate of 7.5% p.a.).

7.18 Taxes payable other than income tax

Taxes payable, other than income tax, consist of the following:

	2016	2015
Value-added tax	422,550	1,213,297
Social taxes	98,889	87,356
Property tax	18,753	19,965
Other taxes	47,373	37,690
	587,565	**1,358,308**

7.19 Trade and other payables

	2016	2015
Trade payables	3,966,208	6,826,871
Payables for products procurement – third parties (a)	13,279,185	9,402,620
Payables for products procurement, raw materials and other payables – related parties (Note 9)	1,100,284	787,925
Issued promissory notes – US dollars and euro (b)	445,356	542,454
Payables to employees	658,342	590,034
Payables to OTCPharm (on the agency contract) – related party (Note 9)	6,233,263	2,380,642
Other payables (c)	587,751	439,564
	26,270,389	**20,970,110**

(a) These balances represent payables for products of third parties manufactured by other pharmaceutical companies.

(b) This balance primarily represents interest free promissory notes issued by the Company's Ukrainian subsidiary Pharmstandard-Biolek before the date of acquisition. The promissory notes are payable to the companies affiliated with the former shareholders of Pharmstandard-Biolek. These promissory notes are payable on demand.

(c) These balances primarily represent payables to third parties for services and equipment.

As at 31 December 2016, RR 1,278,455 (2015: RR 2,519,263) of trade payables were denominated in currencies other than Russian ruble, primarily in US dollars and euro.

7.20 Other non-current liabilities

	2016	2015
Deferred income	91,000	69,000
Other	10,775	15,813
	101,775	**84,813**

The subsidiary of the Group (Pharmapark LLC) received government grants to finance certain development costs. This amount represents cash proceeds from government grants and it will be credited to profit or loss over useful life of the intangible asset recognized upon completion of the development stage.

7.21 Share capital

In accordance with its charter documents the share capital of the Company is RR 37,793. The authorized number of ordinary shares is 37,792,603 with par value of 1 (one) Russian ruble. All authorized shares have been issued and fully paid. As of 31 December 2016 and 31 December 2015, the Group's subsidiaries own 3.8% of the Company's shares, the value of these shares is presented within equity in the line treasury shares.

As at 31 December 2016 and 31 December 2015, Victor Kharitonin, a Russian citizen, was the ultimate controlling shareholder of the Group.

Earnings per share are calculated by dividing the net income attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the period. The Company has no dilutive potential ordinary shares; therefore, the diluted earnings per share equal basic earnings per share.

Earnings per share

Earnings per share are as follows:

	2016	2015
Weighted average number of ordinary shares outstanding	36,355,683	36,355,683
Profit for the year attributable to the ordinary shareholders	8,234,961	13,749,466
Basic and diluted earnings per share, Russian rubles	226,51,	378,2

7.22 Revenue

Revenue breakdown by product groups comprised the following:

	2016	2015
PHARMACEUTICAL PRODUCTS		
OVER THE COUNTER ("OTC")	**5,829,140**	**5,093,937**
PRESCRIPTION		
Branded	5,926,536	5,254,168
Non-branded	1,391,009	1,311,484
	7,317,545	**6,565,652**
Third parties products (a)	36,221,808	26,408,120
Other – substances and APIs	3,325,074	2,882,904
TOTAL PHARMACEUTICAL PRODUCTS	**52,693,567**	**40,950,613**
Contractual manufacturing (Note 9) – (b)	4,661,569	2,690,107
Agency fee income (Note 9) – (c)	2,625,066	1,979,079
Medical equipment	1,806,222	1,575,139
	61,786,424	**47,194,938**

(a) Third parties products sales include sales of branded pharmaceutical products such as Velcade®, Mabtera®, Koagil VII, Mildronate®, IRS® 19®, Imudon®, Prezista®, Revlimid®, Cerezim®, Pulmozim® and other manufactured by other pharmaceutical companies.

(b) Since 2014, the Group provides contract manufacturing services primarily to OTCPharm and Biocad (Note 9).

(c) The Company holds agency contracts for distribution and sale of certain products owned by related and third parties.

7.23 Cost of sales

The components of cost of sales were as follows:

	2016	2015
Materials, components and other	8,913,289	7,332,715
Third parties products	27,139,167	18,256,953
Production overheads	2,586,827	2,421,604
Depreciation and amortization	1,038,981	869,272
Direct labor costs	654,701	517,054
	40,332,965	**29,397,598**

7.24 Commercial costs

Selling and distribution costs were as follows:

	2016	2015
Labor costs	1,434,092	1,339,123
Advertising	252,208	226,671
Freight, communication and insurance of goods in transit	222,444	217,450
Rent	154,338	159,205
Materials, maintenance and utilities	138,126	130,139
Trainings and other services	124,928	96,111
Certification expenses	102,211	118,611
Travel and entertainment expenses	93,712	101,136
Commission and license fees	66,287	41,174
Depreciation	50,044	56,099
Other expenses	55,790	48,553
	2,694,180	2,534,272

7.25 General and administrative expenses

General and administrative expenses were as follows:

	2016	2015
Labor costs	1,950,278	1,695,642
Legal, audit and advisory services	494,892	295,997
Rent	259,916	223,741
Materials, maintenance and utilities	196,613	172,503
Depreciation	140,417	109,553
Taxes other than income tax	33,746	30,972
Communication expenses	30,703	27,350
Travel and entertainment expenses	29,692	29,034
Property and other insurance	29,520	23,999
Other	77,998	78,281
	3,243,775	**2,687,072**

7.26 Other income

Other income comprised the following:

	2016	2015
Reversal of impairment – financial assets (Note 15)	1,067,538	–
Income from non-core operations (a)	196,015	234,621
Reversal of impairment – property, plant and equipment (Note 10)	86,430	29,386
Income received as penalties	35,257	12,336
Foreign exchange gain	34,022	4,630,371
Gain on disposal of property, plant and equipment	22,212	64,967
Gain from transactions with promissory notes (Note 9)	20,329	10,639
Gain from restructuring of accounts payable	–	1,380,151
Gain from write-off of accounts payable	–	332,530
Other income	374,648	490,801
	1,836,451	**7,185,802**

(a) Income from non-core operations comprises of operational lease, income from sale of materials and other assets not included in other categories. In 2016 depreciation of leased-out assets was RR 66,027 (2015: RR 64,042).

7.27 Other expenses

Other expenses comprised the following:

	2016	2015
Foreign exchange loss	4,710,046	307,740
Research expenses (b)	924,492	163,379
Charity	176,162	24,803
Other taxes and penalties (a)	163,593	281,958
Allowance for impairment of loans issued (Note 15)	54,499	1,067,538
Delisting expenses	41,585	–
Bank charges	41,419	42,010
Impairment of property, plant and equipment (Note 10)	31,197	149,713
Biolek expenses resulting from suspension of production	29,602	19,507
Impairment of intangible assets (Note 11)	14,895	–
Other	300,679	134,693
	6,488,169	2,191,341

(a) Other taxes and penalties primarily include property tax expenses and penalties accrual as a result of tax audit.

(b) These expenses represent certain non-recurring research projects. In addition, in 2016, the Group decided to terminate several R&D projects (development stage), with no positive result.

7.28 Income tax

	2016	2015
Income tax expense – current	2,579,627	4,279,608
Deferred tax expense/(benefit) – origination and reversal of temporary differences	170,855	(532,832)
INCOME TAX EXPENSE	**2,750,482**	**3,746,776**

Profit before tax for the purposes of the consolidated financial statements is reconciled to tax expense as follows:

	2016	2015
PROFIT BEFORE INCOME TAX	**10,752,759**	**17,677,876**
THEORETICAL TAX CHARGE AT RUSSIAN STATUTORY RATE OF 20%	**2,150,552**	**3,535,575**
Effect of the difference in tax rates in countries other than Russia	(2,072)	(364)
Tax effect from the increase in additional paid-in capital of the joint venture	–	22,585
Effect from intra-group dividends eliminated in consolidation	22,802	19,729
(taxed at rate of 13-15%)	159,419	–
Effect from dividends received from associate	33,551	47,053
Adjustments in respect of income tax of previous years	241,861	74,296
Share of results of associates and joint venture	54,632	–
Deferred tax from retained earnings of associated company	89,737	47,902
INCOME TAX EXPENSE	**2,750,482**	**3,746,776**

Movements in deferred tax balances were as follows:

	1 January 2015	Temporary differences recognition and reversal in profit and loss	31 December 2015	Temporary differences recognition and reversal in profit and loss	Temporary differences recognition and reversal in OCI	31 December 2016
TAX EFFECTS OF TAXABLE AND DEDUCTIBLE TEMPORARY DIFFERENCES – (LIABILITY)/ASSET						
Property, plant and equipment	(561,863)	30,910	(530,953)	(33,914)	–	(564,867)
Intangible assets	26,653	12,956	39,609	173,808	–	213,417
Financial assets	–	157,470	157,470	(232,178)	23,229,	(51,479)
Inventories	437,003	135,596	572,599	(41,947)	–	530,652
Trade and other receivables	(84,960)	190,887	105,927	75,674	–	181,601
Trade and other payables	16,090	(9,730)	6,360	(94,533)	–	(88,173)
Other	40,634	14,743	55,377	(17,765)	–	37,612
TOTAL NET DEFERRED TAX (LIABILITY)/ ASSET	**(126,443)**	**532,832**	**406,389**	**(170,855)**	**23,229,**	**258,763**

Deferred tax is presented in the statement of financial position as follows:

	2016	2015
Deferred tax asset	600,905	721,657
Deferred tax liability	(342,142)	(315,268)
TOTAL NET DEFERRED TAX ASSET	**258,763**	**406,389**

The recognition and reversals of temporary differences primarily relates to the following:

- / depreciation of property, plant and equipment in excess of the depreciation for tax purposes;
- / write down of inventory to net realizable value, unrealized profit due to intragroup purchases of materials, discounts recognized in taxation as other income;
- / fair value adjustments on acquisition;
- / fair value of financial instruments in excess of the cost of these instruments for tax purpose;
- / impairment of trade receivables;
- / amortization of trade marks in excess of the amortization for tax purposes; and
- / deemed cost adjustments upon conversion to IFRS.

The aggregate amount of temporary differences associated with investments in subsidiaries for which deferred tax liabilities have not been recognized was approximately RR 42,780,449 as at 31 December 2016 (2015: RR 39,706,832).

7.29 Contingencies, commitments and operating risks

Operating environment of the Group

Russia, where majority of the Group's operations are located, continues economic reforms and development of its legal, tax and regulatory frameworks as required by a market economy. The future stability of the Russian economy is largely dependent upon these reforms and developments and the effectiveness of economic, financial and monetary measures undertaken by the government.

The Russian economy was negatively impacted by a significant drop in crude oil prices and sanctions imposed on Russia by several countries. Interest rates in rubles remain high. The combination of these factors has led to a reduction in the availability of capital, and an increase in its value, as well as an increase in uncertainty about further economic growth, which could adversely affect the Group's financial position, results of operations and economic prospects. Management of the Group believes that it is taking appropriate measures to maintain the Group's economic stability in the current environment.

The Group also operates in Ukraine. Since 2014, the economic and political situation in Ukraine has deteriorated significantly. As a result, Ukraine has experienced a fall in gross domestic product, a significant negative balance of payments and a sharp reduction in foreign currency reserves. Furthermore, in 2015 – 2016 the Ukrainian hryvnia significantly devalued to major foreign currencies and the National Bank of Ukraine imposed certain restrictions on foreign currency operations. Restrictions have also been introduced for certain cross-border settlements, including payments of dividends. International rating agencies have downgraded sovereign debt ratings for Ukraine. Currently, a loan program extension, which may necessitate certain austerity measures, is being negotiated by Ukraine with the International Monetary Fund. The combination of the above events has resulted in a deterioration of liquidity and much tighter credit conditions where credit is available.

Management believes it is taking appropriate measures to support the sustainability of the Group's business in the current circumstances.

Taxation

Russian tax, currency and customs legislation can be interpreted in different ways and is susceptible to frequent changes. The interpretation made by the Group's management of the legislation in question as applied to the operations and activities of the Group's enterprises may be challenged by the relevant regional or federal authorities.

Certain amendments to legislation were passed in 2015, which are aimed at combating tax evasion through the use of low-tax jurisdictions and aggressive tax planning structures. In particular, those amendments include definitions of the concepts of beneficial ownership and tax residence of legal entities at their actual place of business, and an approach to the taxation of controlled foreign companies.

These changes, as well as recent trends in the application and interpretation of certain provisions of Russian tax legislation, indicate that the tax authorities may take a tougher line in interpreting the law and checking tax returns. As a result, tax authorities may raise questions about transactions and accounting methods which they did not question before. This may result in significant amounts of additional tax charges, penalties and fines being imposed. It is not possible to determine claim amounts for suits which may be but have not actually been filed, or to assess the likelihood of an adverse outcome. Tax audits may cover the three calendar years immediately preceding the year in which the audit occurs. In certain circumstances an audit can also cover earlier periods.

The management is of the opinion that, as at 31 December 2016, it has correctly interpreted the relevant provisions of law, and it is highly likely that the Group's position in regard to tax, currency and customs legislation will remain unchanged.

Because of the uncertainties associated with the Russian tax and legal systems, the ultimate amount of taxes, penalties and interest assessed, if any, may be in excess of the amount expensed to date and accrued as at 31 December 2016. Should the tax authorities decide to issue a claim and prove successful in the court, they would be entitled to recover the amount claimed, together with fines (in Russia amounting to 20% of such amount and interest at the rate of 1/300 of the Central Bank of the Russian Federation rate for each day of delay for late payment of such amount). Management believes that it is not probable that the ultimate outcome of such matters would result in a liability. Therefore, no provision for these contingencies was recorded in these consolidated financial statements.

Russian transfer pricing legislation

The new Russian transfer pricing legislation allows the Russian tax authority to apply transfer pricing adjustments and impose additional profits tax liabilities in respect of all "controlled" transactions if the transaction price differs from the market level of prices. A list of "controlled" transactions includes transactions performed with related parties based on domestic and cross-border agreements and certain types of cross-border transactions with independent parties. The transfer pricing rules for domestic transactions apply only if the amount of all transactions with related party exceeds RR 1 billion (apart from some exceptions provided by the Tax Code); all cross-border transactions with related parties are controlled without application of any financial thresholds. In cases where the domestic transaction resulted in an accrual of additional tax liabilities for one party, another party could apply the symmetrical adjustment to its profit tax liabilities according a special notification issued by the authorized body in due course.

Special transfer pricing rules apply to transactions with securities and derivatives.

In 2012-2016, the Group determined its tax liabilities arising from "controlled" transactions using actual transaction prices.

Due to the uncertainty and absence of current practice of application of the current Russian transfer pricing legislation, the Russian tax authorities may challenge the level of prices applied by the Group under the "controlled" transactions and assess additional tax liabilities unless the Group is able to demonstrate the use of market prices with respect to the "controlled" transactions, and that there has been proper reporting to the Russian tax authorities, supported by appropriate available transfer pricing documentation.

Insurance policies

The Group holds insurance policies in relation to its property, plant and equipment, which cover majority of property, plant and equipment items. The Group holds no insurance policies in relation to its operations, or in respect of public liability.

Operating lease agreements

The Group entered into a number of operating lease agreements for warehouses. Rental agreements are revised on an annual basis.

Commitment liabilities and guarantees

In June and September 2016, the Group provided an unsecured guarantees in the amount of RR 5,397 million and RR 1,750 million respectively to a third party to secure obligations of the parent company within the process of the Company's shares buyback. These guaranties become effective since September 2016 and until April and September 2020 respectively. The management believes that the financial risk associated with these guarantees is remote.

7.30 Financial instruments and financial risk management objectives and policies

Fair values

Management believes that fair value of cash and cash equivalents, short-term and long-term financial assets, trade and other receivables and payables, and borrowings and loans approximate their carrying amounts due to their short maturity.

Fair value hierarchy

The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

- Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;
- Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly;
- Level 3: techniques based on the inputs with significant effect on the recorded fair value which are not based on observable market data.

31 December 2016				
	Total	**Level 1**	**Level 2**	**Level 3**
ASSETS MEASURED AT FAIR VALUE				
Unquoted equity shares (Note 16)	**1,836,906**	–	–	1,836,906
Quoted equity shares (Note 16)	**6,096,337**	6,096,337	–	–
ASSETS FOR WHICH FAIR VALUES ARE DISCLOSED				
Short-term loans issued (Note 15)	**15,034,909**	–	–	15,034,909
Long-term loans issued (Note 16)	**664,125**	–	–	664,125
Securities (Note 15)	**20,753**	18,216	–	2,537

31 December 2015				
	Total	**Level 1**	**Level 2**	**Level 3**
ASSETS MEASURED AT FAIR VALUE				
INVESTMENTS AVAILABLE FOR SALE				
Unquoted equity shares (Note 16)	**1,279,895**	–	–	1,279,895
Quoted equity shares (Note 16)	**1,317,317**	1,317,317	–	–
ASSETS FOR WHICH FAIR VALUES ARE DISCLOSED				
Short-term loans issued (Note 15)	**11,833,446**	–	–	11,833,446
Long-term loans issued (Note 16)	**2,218,754**	–	–	2,218,754
Securities (Note 15)	**2,562,386**	10,725	–	2,551,661

In 2016 and 2015, there were no transfers between levels of the fair value hierarchy either.

Financial risk management objectives and policies

The Group's principal financial instruments comprise bank loans, short-term and long-term bank deposits, and cash and cash equivalents. The main purpose of these financial instruments is to raise finance for the Group's operations and investment activities. The Group has various other financial assets and liabilities such as promissory notes, trade receivables, trade and other payables, which relate directly to its operations. During the year, the Group did not undertake active trading in financial instruments.

The main risks arising from the Group's financial instruments are interest rate risk, liquidity risk, foreign currency risk and credit risk. Management reviews and agrees policies for managing each of these risks which are summarized below.

Interest rate risk

Management believes that the Group does not have significant interest rate risk as at 31 December 2016 and 31 December 2015. The most of the Groups' short-term financial investments (loans and bank deposits, see Notes 14, 15 and 16) are issued at fixed interest rates based on current market rates at the date of initial recognition and short-term borrowings and loans (Note 17) are received at fixed interest rates based on current market rates at the date of initial recognition.

Foreign exchange risk

The Group has certain US dollar and euro-denominated cash and short-term deposits (Note 14), short-term and long-term financial assets (Note 15 and 16), trade and other payables (Note 19), and trade and other receivables (Note 13). Therefore, the Group is exposed to foreign exchange risk.

The Group monitors the foreign exchange risk by analyzing changes in exchange rates in the currencies in which its cash, financial assets and payables are denominated. However, the Group does not have formal arrangements to mitigate this foreign exchange risk.

The tables below shows the sensitivity to a reasonably possible change in the US dollar and euro exchange rates, with all other variables held constant, of the Group's profit before tax:

	Increase/ decrease in US$ rate	**Effect on profit before tax**
AS AT 31 DECEMBER 2016		
US dollar/ruble exchange rate	+20,00%	3,468,433
US dollar/ruble exchange rate	-20,00%	(3,468,433)

	Increase/ decrease in US$ rate	**Effect on profit before tax**
AS AT 31 DECEMBER 2015		
US dollar/ruble exchange rate	+40,00%	7,607,250
US dollar/ruble exchange rate	-13,00%	(2,472,356)

	Increase/ decrease in euro rate	**Effect on profit before tax**
AS AT 31 DECEMBER 2016		
Euro/ruble exchange rate	+20,00%	617,962
Euro/ruble exchange rate	-20,00%	(617,962)

	Increase/ decrease in euro rate	**Effect on profit before tax**
AS AT 31 DECEMBER 2015		
Euro/ruble exchange rate	+43,00%	1,511,501
Euro/ruble exchange rate	-15,00%	(527,268)

	Increase/ decrease in US$ rate	**Effect on profit before tax**
AS AT 31 DECEMBER 2016		
US dollar/Ukrainian hryvnia exchange rate	+53,00%	(243,583)
US dollar /Ukrainian hryvnia exchange rate	-13,00%	59,747

	Increase/ decrease in US$ rate	**Effect on profit before tax**
AS AT 31 DECEMBER 2015		
US dollar/Ukrainian hryvnia exchange rate	+67,00%	(668,512)
US dollar/Ukrainian hryvnia exchange rate	-18,00%	179,600

	Increase/ decrease in euro rate	**Effect on profit before tax**
AS AT 31 DECEMBER 2016		
Euro/Ukrainian hryvnia exchange rate	+53,00%	(162,257)
Euro/Ukrainian hryvnia exchange rate	-15,00%	45,922

	Increase/ decrease in euro rate	**Effect on profit before tax**
AS AT 31 DECEMBER 2015		
Euro/Ukrainian hryvnia exchange rate	+67,00%	(355,990)
Euro/Ukrainian hryvnia exchange rate	-18,00%	95,639

Liquidity risk

The Group's policy is to maintain sufficient cash and cash equivalents or have available funding through an adequate amount of committed credit facilities to meet its operating and financial commitments. The Group performs continuous monitoring of cash deficit risks and continuous monitoring of repayment of its financial liabilities on time. The Group performs daily cash flow planning and control procedures.

The table below summarizes the maturity profile of the Group's non-derivative financial liabilities based on contractual undiscounted payments, including interest.

As at 31 December 2014	Total	Less than 4 months	4 to 6 months	6 to 12 months	More than 12 months
Borrowings and loans (Note 17)	**4,321,156**	121,743	119,402	4,080,011	–
Trade and other payables (Note 19)	**25,825,032**	25,825,032	–	–	–
Other non-current liabilities (Note 20)	**10,775**	–	–	–	10,775
TOTAL	**30,156,963**	**25,946,775**	**119,402**	**4,080,011**	**10,775**

As at 31 December 2015	Total	Less than 4 months	4 to 6 months	6 to 12 months	More than 12 months
Borrowings and loans (Note 17)	**4,446,600**	124,307	119,393	4,202,900	–
Trade and other payables (Note 19)	**20,422,742**	20,422,742	–	–	–
Other non-current liabilities (Note 20)	**15,813**	–	–	–	15,813
TOTAL	**24,885,155**	**20,547,049**	**119,393**	**4,202,900**	**15,813**

Credit risk

Financial assets, which potentially are subject to credit risk, consist principally of trade receivables. The Group has policies in place to ensure that sales of products and services are made to customers with an appropriate credit history. Sales to customers are made in accordance with annually approved Marketing and Credit policy. The Group daily monitors sales and receivables conditions using appropriate internal control procedures.

The carrying amount of accounts receivable, net of allowance for impairment, represents the maximum amount exposed to credit risk. Although collection of receivables could be affected by economic factors, management believes that there is no significant risk of loss to the Group beyond the allowance already recorded.

Cash and deposits are placed in the bank that was treated as a related bank in prior periods. Although the bank ceased to be affiliated with the Group, the Group continues to use it for most its payments and settlements due to the long history of cooperation. At that, the management analyses the bank's financial position and assets' structure and quality on a regular basis in order to minimize the credit risk.

The table below summarizes the maturity profile of the Group's trade and other receivables:

	Total	Neither impaired nor past due	Not impaired but past due				
			Less 1 month	1-2 months	2-3 months	3-6 months	More than 6 months
31 DECEMBER 2016	**17,279,573**	13,928,374	2,535,700	150,990	59,628	257,746	347,135
31 DECEMBER 2015	**16,346,568**	12,125,733	2,242,195	269,450	182,784	620,688	905,718

Sales concentration to a small group of customers

The Group works with five distributors that together represent about 32% of the Group's revenue for 2016, excluding sales to the Ministry of Health of the Russian Federation and its departments under open public tenders. It is common practice of the Russian pharmaceutical market to work with the limited number of large distributors.

Capital management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and to maintain an optimal capital structure to reduce the cost of capital. The Group manages its capital structure and makes adjustments to it, in light of changes in economic conditions. To maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt.

The Group monitors capital using a gearing ratio, which is net debt divided by total capital plus net debt. The Group's policy is to keep the gearing ratio not more than 60%. The Group's net debt includes borrowings and loans, trade and other payables, less cash and cash equivalents. Capital includes equity attributable to the equity holders of the parent.

	2016	2015
Borrowings and loans	4,070,794	4,089,436
Trade and other payables	26,270,389	20,970,110
Less: cash and short-term deposits	(17,386,578)	(14,397,241)
NET DEBT	**12,954,605**	**10,662,305**
Equity attributable to the equity holders of the parent	61,323,653	53,663,958
CAPITAL AND NET DEBT	**74,278,258**	**64,326,263**
Gearing ratio	17%	17%

7.31 Material partly-owned subsidiaries

Proportion of equity interest held by non-controlling interests is summarized below:

Name	Country of incorporation and operation	2016 % share	2015 % share
Pharmstandard-Tomskhimpharm OJSC	Russian Federation	9,22	9,22
OTHER			
Pharmstandard-Biolek PJSC	Ukraine	3,07	3,07
MDR Pharmaceuticals	Cyprus	49,95	49,95
Bigpearl Trading Limited	Cyprus	49,995	49,995
Pharmapark LLC	Russian Federation	49,995	49,995
Biomed named after I. I.Mechnikov JSC	Russian Federation	50,155	50,155
Pharmatsevticheskiye Innovatsii LLC	Russian Federation	49,995	49,995
EKK JSC	Russian Federation	64,71	64,71
Moldildo Trading Limited	Cyprus	25	25
Pharmstandard-Medtechnika LLC	Russian Federation	25	25
Cellthera Pharm LLC	Russian Federation	25	25
MasterPlazma LLC	Russian Federation	48	48
Pharmstandard-Plazma LLC	Russian Federation	48	–

The summarized financial information of these subsidiaries is provided below. This information is based on amounts before inter-company eliminations:

Summarized statement of profit or loss for 2016	Pharmstandard-Tomskhimpharm OJSC	Other
Revenue	2,327,884	3,731,966
Cost of sales	(1,755,931)	(2,046,384)
Selling and distribution costs	(409,124)	(558,110)
Administrative expenses	(127,401)	(505,286)
Other income (expense), net	(8,384)	(1,028,692)
Financial income (expense), net	10,680	(212,921)
PROFIT/(LOSS) BEFORE INCOME TAX	**37,724**	**(619,427)**
Income tax	(9,350)	41,459
PROFIT/(LOSS) FOR THE YEAR	**28,374**	**(577,968)**
Attributable to non-controlling interests	2,616	(235,300)

Summarized statement of profit or loss for 2015	Pharmstandard-Tomskhimpharm OJSC	Other
Revenue	2,422,508	3,530,696
Cost of sales	(1,742,814)	(2,101,134)
Selling and distribution costs	(485,892)	(475,419)
Administrative expenses	(135,331)	(460,536)
Other income (expense), net	416,350	(6,135)
Financial income (expense), net	3,388	53,968
PROFIT/(LOSS) BEFORE INCOME TAX	**478,209**	**541,440**
Income tax	(96,862)	(99,826)
PROFIT/(LOSS) FOR THE YEAR	**381,347**	**441,614**
Attributable to non-controlling interests	34,321	147,313

Summarized statement of financial position as at 31 December 2016	Pharmstandard-Tomskhimpharm OJSC	Other
Inventories, receivables, cash and short-term deposits and other current assets	3,749,554	3,812,579
Property, plant and equipment, intangible assets and other non-current financial assets	417,443	2,933,165
Trade, other payables and other current liabilities	(227,539)	(4,588,385)
Deferred tax liabilities and other non-current liabilities	(25,091)	(131,981)
TOTAL EQUITY	**3,914,367**	**2,025,378**
Attributable to:		
Non-controlling interests	360,905	1,111,064

Summarized statement of financial position as at 31 December 2015	Pharmstandard-Tomskhimpharm OJSC	Other
Inventories, receivables, cash and short-term deposits and other current assets	3,710,925	3,373,824
Property, plant and equipment, intangible assets and other non-current financial assets	479,590	2,450,300
Trade, other payables and other current liabilities	(277,348)	(2,747,249)
Deferred tax liabilities and other non-current liabilities	(27,173)	(282,168)
TOTAL EQUITY	**3,885,994**	**2,794,707**
Attributable to:		
Non-controlling interests	349,739	1,414,816

Dividends paid by a subsidiary

In 2016, Bigpearl Trading Limited (Cyprus), a Company's subsidiary, paid non-controlling shareholders dividends of RR 67,721 (2015: RR 46,719).

7.32 Events after the reporting period

On 27 January 2017, Jounce Therapeutics Inc. carried out the initial placement of its 6,365,000 ordinary shares on NASDAQ. On 31 January 2017, Pharmstandard International S.A. purchased ordinary shares of Jones Therapeutics Inc. for a cash consideration of US$ 1,000 thousand (RR 60,161). Thus, the Group increased its share in the company's capital from 2.04% to 2.06%. Jounce Therapeutics Inc. is registered in the United States and specializes in the development of antibodies against targets of immunosuppressive control for oncological indications.

On 30 January 2017 Pharmstandard International S.A. acquired ordinary shares of EnGene Inc. for a cash consideration of EUR 13 thousand (RR 848) and further on 1 March 2017 acquired preferred shares of EnGene Inc. for a cash consideration of US$ 839 thousand (RR 48,646). Thus, the Group increased its share in the company's capital from 4.18% to 6%. EnGene Inc. is registered in Canada and is developing the delivery of nucleotides (DNA and RNAi) to mucosal tissues for the treatment of chronic diseases through suppression or induction of protein synthesis.

In 2017 the independent monitoring committee (IDMC) recommended the Group's associate Argos Pharmaceuticals to discontinue Phase 3 clinical trials of the lead product candidate AGS-003 due to its potential futility. Consequently, Argos Pharmaceuticals market quotes at NASDAQ fell from US$ 4.9 on 31 December 2016 to US$ 0.5 on the date of these consolidated financial statements. Argos intends to conduct the detailed analysis of the results and discuss with FDA the possibility to continue the trial to assess the drug's longer-term benefits.

On 24 March 2017, shares of PJSC "Pharmstandard" were excluded from the list of securities admitted to organized trading on the Moscow Stock Exchange in accordance with the decision taken on 30 January 2017 at the extraordinary general meeting of shareholders of PJSC "Pharmstandard".

On 27 March 2017, the Group entered in a newly created joint venture JSC "KirovPlasma". The authorized capital of the company will be 80 million rubles. The company will develop and establish production of drugs from human blood plasma at the plant in Kirov. The Group's share in the authorized capital of the enterprise is 37.5%.

On 30 March 2017 Pharmstandard International S.A. acquired preferred shares of Avelas Biosciences for a cash consideration of US$ 2,500 thousand (RR 142,560). Thus, taking into account the dilution, the Company's share is 9.46%. Avelas Biosciences is registered in the US and develops peptide products cleaved by matrix metalloproteinases to form cell-penetrating peptides conjugated with fluorophore for intraoperative fluorescence diagnostics of the positive surgical edge of the tumor, as well as regional lymph nodes.

On 21 April 2017, the Company sold 50% shares in the capital of its subsidiary, PJSC "Pharmstandard-Biolek", to a third party a for a total consideration of US$ 1.8 million. After this transaction, the ownership interest equaled to 46.93%. The Company lost control over the company PJSC "Pharmstandard-Biolek".

8

Glossary

List of main acronyms and abbreviations:

API – Active Pharmaceutical Ingredient
EBITDA – earnings before interest, taxes, depreciation and amortization
GDP – good distribution practice
GMP – good manufacturing practice
SKU – stock keeping unit
VED – vital and essential drug
INN - international nonproprietary name
YoY – year over year
ATC group - Anatomical Therapeutic Chemical group
TPP – third-party product
FPP – finished pharmaceutical product
OTC - over-the-counter drugs
Rx - Prescription drugs

Measurement units:

RR – Russian ruble
USD – United States dollar