Volga Gas plc

Annual Report and Accounts

for the year ended 31 December 2016

Volga Gas plc is an independent oil and gas exploration and production company focused on the Volga Region of Russia. It has 100% interests in four oil and gas exploration and production licences in the Saratov and Volgograd regions.

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Strategic Report

Overview of 2016

- Group production in 2016 increased by 99% compared to 2015
- Throughput of gas at the processing plant running at the target plateau rate of 1 million cubic metres per day during 2H 2016
- Successfully exporting 48% of condensate sales in 2016
- Ten-fold increase in EBITDA* compared to 2015 and net cash increased by US$9.0 million
- Profit before tax of US$1.9 million (2015: loss before tax of US$4.6 million)

Overview

Increased production from the VM field

- Production from the VM#3 and VM#4 wells, completed in 2015, was in line with increased expectations.
- Sufficient well capacity to sustain planned plateau of 1 million cubic metres per day of total production.

Increased throughput at the Dobrinskoye gas processing plant

- Maximum output of one million cubic metres per day achieved in 2H 2016.
- Conversion to Redox-based gas sweetening.
- Construction of LPG extraction.

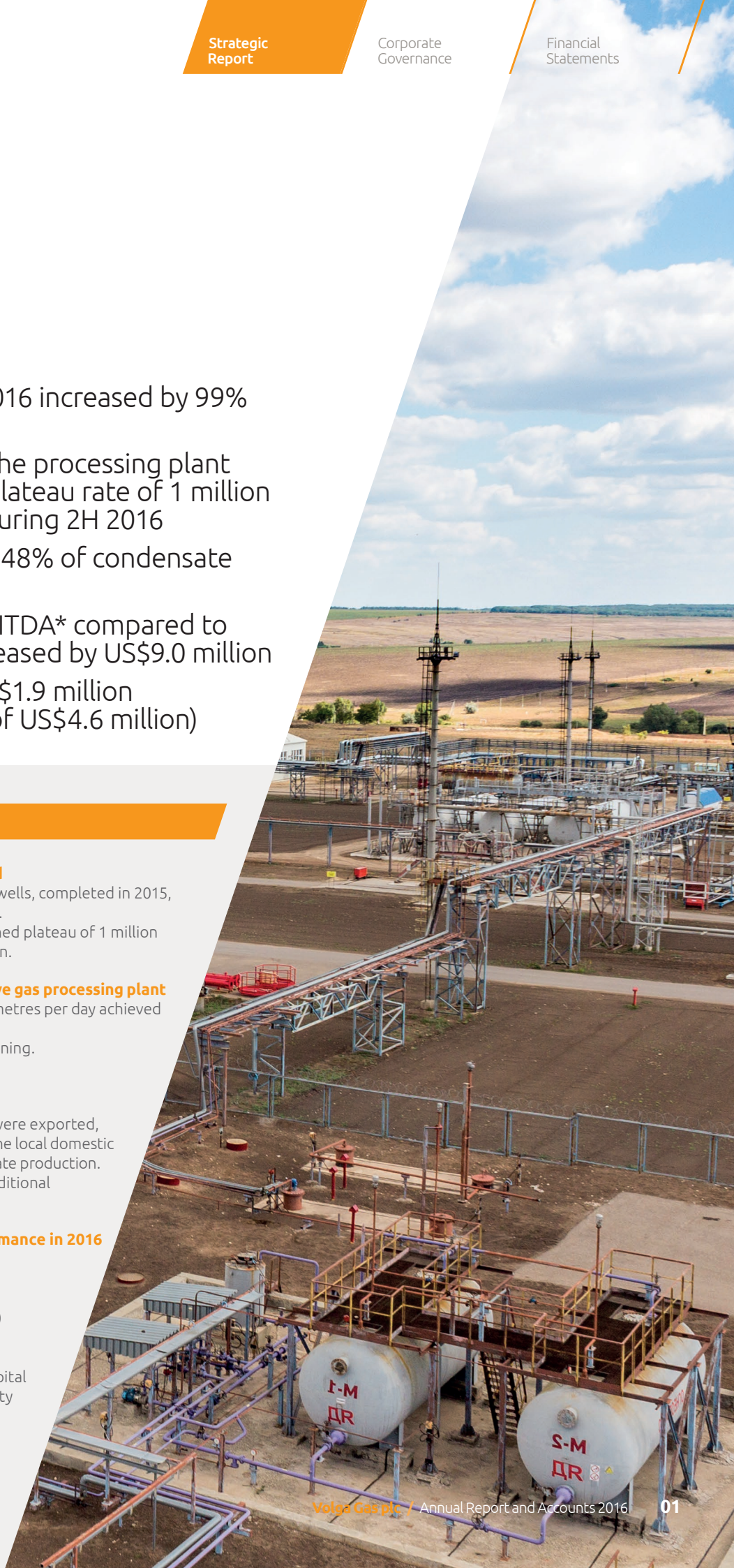
Exports of condensate and oil

- During 2016 48% of condensate sales were exported, eliminating exposure to periods when the local domestic market was unable to take our condensate production.
- Export routes developed to provide additional commercial flexibility to the business.

Significantly improved financial performance in 2016

- EBITDA* increased to US$9.6 million (2015: US$0.9 million)
- Profit before tax of US$1.9 million (2015: loss before tax of US$4.6 million)
- Driven by increased production and recovery in oil prices and the Ruble.
- Strong cash generation and modest capital expenditure requirements leave capacity for resumption of distributions to shareholders.

* reconciliation of EBITDA is disclosed in Operational and Financial Summary on page 1



Volga at a Glance

Our assets are located in an established oil and gas province. The area benefits from the existing rail, road and pipeline infrastructure and proximity to Russia's main energy markets.

Dobrinskoye gas processing plant

2016 Progress
Increased maximum throughput to one million cubic metres (35.3 million cubic feet) per day and achieved average throughput of 32.3 mmcf/d during December 2016.

2017 Objectives
Improve cost efficiency of the current plant operations.
Conversion to Redox-based gas sweetening to significantly reduce processing costs and substantially eliminate waste disposal requirements.
Construction of LPG extraction plant to increase revenues.

Vostochny Makarovskoye ("VM") gas/condensate field

2016 Progress
High levels of production achieved from the VM#3 and VM#4 wells completed during 2015.

2017 Objectives
Workover on VM#2 to enhance well productivity. Upgrade to production management systems.

Dobrinskoye gas/condensate field

2016 Progress
Managed production from the Dobrinskoye #26 well.

2017 Objectives
Continue to maintain production from the existing wells and maximise long-term extraction of gas and condensate.

Uzenskoye oil field

2016 Progress
Successful workovers and introduction of downhole pumping increased Uzenskoye production in 2016 by 69%.

2017 Objectives
Maintain production profile and seek to maximise extraction of oil from existing wells.
Horizontal well drilling into the undeveloped shallower reservoir in Uzen.

Commercial

2016 Progress
Commenced exports of condensate to broaden the commercial options of the business in light of market difficulties experienced earlier in 2015.

2017 Objectives
Seek to improve the cost-effectiveness of exports and develop further export channels.

Chairman's Statement

Mikhail Ivanov
Chairman

"A successful year for Volga Gas"

Dear Shareholder,
In spite of continuing challenging conditions experienced by the oil and gas industry worldwide, and for Russia generally, 2016 has been a successful year for Volga Gas. Production has recovered from the reverses seen in 2015 and has been at the highest rate in the Group's ten year history. Revenues have more than doubled compared to 2015 and underlying profitability has been restored. Oil prices, that started 2016 at levels not seen for over ten years have recovered substantially, doubling from the low point seen in January. The Russian Ruble has also had a similar though less marked recovery against the US Dollar.

On an operational level, the results of 2016 were better than anticipated by management. Having successfully concluded the development drilling on the Vostochny Makarovskoye ("VM") field in 2015, this field, the Group's principal producing asset, has been operating at close to the planned plateau production rate of one million cubic metres per day of gas plus associated condensate for most of the second half of 2016. This production is the core of stable production which provides the main cash-generation engine for the Group. In addition, workover activity conducted during early 2016 enabled a significant recovery in oil production from the Uzen oil field such that the production rate in 2016 was more than twice the level budgeted by management at the start of the year, even though the contribution to the Group's total output from this field is modest.

The results of 2016 have also been enhanced by some important commercial initiatives undertaken by management, notably the commencement of export sales of condensate, and more recently of some oil, to customers in the Baltic states neighbouring Russia. While the netback realisations on export sales, after taking into account export taxes and transport costs, are slightly lower than for domestic sales, exports have enabled production to be maintained during periods in which the local domestic market is less active. There have also been several cost reduction initiatives, individually not significant, but which have enabled overall production costs to be lower than budgeted.

As a result of these developments, profitability and cash generation has increased materially during 2016.

Capital expenditure in 2016 has been modest as the Board decided to restrain spending while the oil price was low, as it was at the start of the year. Such expenditure that has been undertaken was directed towards maintenance of the core assets and to projects able to provide immediate enhancements to profitability. Consequently, the net cash position has increased by US$9.0 million since the start of 2016.

The key strategic development underway is the further enhancement of the existing gas processing facilities, first to introduce a more efficient process for the sweetening of the gas and secondly to capture for sale the liquid petroleum gases ("LPG") that are currently vented and flared. The former is intended to achieve significant cost savings and enable higher production rates of over one million cubic metres per day of gas, while the latter will provide an additional and potentially highly profitable product stream. While these projects were first considered in 2015, further work undertaken in 2016 has enabled modifications to the plans which will enable the same results to be delivered at significantly lower capital expenditure than originally contemplated.

The Chief Executive's Report covers both the work undertaken during the year on this and the plans to be implemented in 2017.

While the immediate outlook is more positive than it was a year ago, the finances of the Group will continue to be conservatively managed. Capital investment will continue to be at a modest level and focused on enhancing the profits from the gas and condensate production and on developing the proved oil reserves of the Company.

The Group holds significant reserves in its three principal fields, confirmed in the recently completed independent report detailed below in the Operational Review by our Chief Executive Officer. These reserves form the basis of sustainable production with growth potential in the near term. These assets provide a platform for the Group to grow in the future, both through successful exploration and by selective, value-accretive acquisitions. The Board believes that Volga Gas has a strong asset base and the financial and operational capability to develop and extend these assets to provide long-term value growth for our shareholders. Meanwhile, in recognition of the strong financial position of the Group and the confidence in the continued and sustainable profitability, the Board has decided to resume payment of dividends to shareholders. The Board is recommending total dividends of US$0.062per ordinary share, comprising US$0.007 per ordinary share in respect of the profits generated in the year ended 31 December 2016 and a special dividend of US$0.055 per ordinary share.

Mikhail Ivanov
Chairman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Chief Executive's Report

Andrey Zozulya
Chief Executive Officer

"Strong production performance from our fields"

As the Chairman has noted, Volga Gas achieved a significant improvement in its operational and financial performance in 2016 compared to 2015 with overall production increased by 99%, revenues up by 121% in US Dollar terms and a return to profitability. Some of this was a result of the recovery in oil prices that took place steadily through the year, but much of this was as a result of the successful drilling and well workover activity that took place during 2015 and early in 2016, as well as the efficiency improvements implemented early in 2016.

The main driver of the performance was the Vostochny Makarovskoye ("VM") field on which we successfully concluded development drilling towards the end of 2015. With the necessary well capacity available through the year and having completed the required upgrades to the gas plant, we were able to produce at the full plateau rate of 1 million m3 per day (35.3 mmcf/d) of gas plus associated condensate for much of the second half of 2016 – apart from periods of planned plant maintenance and for testing of potential new gas sweetening processes, described further below.

Another important factor in the production performance of 2016 was the commencement of exports of condensate. During 2015, there were periods in which the regional domestic market was unable to take our condensate, leading to shut-ins at various periods. With the development of export channels, such market disruptions as occurred during 2016 had little or no impact on our ability to continue to sell condensate and therefore keep production going for the full year.

Another factor in the Group's overall production in 2016 was the recovery in oil production from the mature Uzenskoye field. Workovers on existing producing wells done in April and May 2016 led to a 160% increase in daily production rates from this field. Although this was still a minor part of the Group total, it made a useful contribution to the profit recovery of the Group.

In line with the Board's financial strategy at the start of 2016, committed capital investment was kept to minimum levels in 2016. Nevertheless, the technical teams continued to work on projects that are expected to have material positive impact on the short and medium-term performance of Volga Gas. These include new wells on the Uzenskoye field to develop the proved but undeveloped Albian reservoir in the field, and projects that would significantly improve the output and efficiency of the Dobrinskoye gas processing plant and with significant reductions in the required capital expenditure compared to earlier proposals.

2017 objectives and medium-term strategy

Management has three key objectives in 2017 relating to the operation of the gas processing plant:

- Introduction of a new gas sweetening process using the Redox process. It is expected that this can be achieved with only minor modifications to the existing process plant. This should lead to a significant reduction in the cost of chemicals consumed in the gas sweetening process and elimination of bulk waste which needs to be disposed of safely.
- Construction of additional modules for the capture, storage and sale of liquid petroleum gases ("LPGs") from the gas and condensate streams produced from the VM and Dobrinskoye fields. LPGs, primarily comprising propane and butane, are currently either included in the sales gas stream or flared. The LPG project will provide an additional product stream which is expected to increase total sales volumes by approximately 10% and to enhance profitability. The construction of the project is expected, subject to the necessary regulatory approvals, to commence during Q2 2017 and be completed before the end of 2017. The capital investment in the project is estimated at US$4.0 million.
- Disposal of accumulated waste chemicals resulting from the current gas sweetening process. During 2016 a pilot project for disposal by injection into a disused gas well was undertaken. Management expects to receive regulatory approval for this operation to be undertaken for the waste accumulated on-site.

The other key objective for management in 2017 is the development of the currently undeveloped crude oil reserves in the shallow Albian reservoir in the Uzen oil field. A first horizontal well is shortly to be drilled on the field. If successful, further wells may be drilled. The horizontal wells are expected to add up to 1,000 barrels per day of incremental oil production and to produce over 2 million barrels of oil over their economic lives.

Reserves update

A new independent reserve report has recently been completed. While the new reserve estimates result in a net reduction in proved reserves, there was an overall increase in proved and probable reserves. Details are contained in the Operational Review on pages 8 and 9.

Current trading and outlook

Between January and March 2017, Group production averaged 7,245 barrels of oil equivalent per day, in line with management's plan. Production in March 2017 was impacted by planned maintenance and seasonal disruptions, after averaging over 8,100 boepd in January and February 2017. The gas plant is consistently operating at planned capacity of one million m³ per day, with condensate output running at over 2,000 barrels per day, approximately half of which is being sold to export markets. International oil prices have maintained their higher levels reached in December 2016. Oil production is now a minor part of the Group's output and has suffered moderate disruption as the mild winter caused difficulties in collection of oil by our customers.

In the current environment, and at current production rates, management expects the Group's financial performance in 2017 to improve further on that of 2016. Meanwhile, new capital expenditure commitments remain within projected cash generation, permitting a resumption of a sustainable distribution policy for shareholders.

Andrey Zozulya
Chief Executive Officer

Operational Review

Operations overview

Group production in 2016, at an average daily rate of 6,507 boepd, was 99% higher than the 3,278 boepd achieved in 2015. Three were three reasons for this: higher production capacity from the VM field on which the new wells were put on production at the end of 2015, commencement of condensate exports which allowed production to remain uninterrupted during periods when the local domestic market was disrupted and, less materially but also positive, the recovery in oil production from the Uzen oil field.

Combined with a steady recovery in oil prices through the year and a rebound in the Ruble, netback revenues in US Dollar terms increased by 102% compared to 2015, taking into account the export taxes and transportation costs associated with the exports of condensate. In addition, as a result of more accurate fiscal metering introduced at the start of 2016, the formula for calculating Mineral Extraction Tax charged on gas and condensate was reduced. This, combined with various cost reduction measures, contributed to a near ten-fold increase in EBITDA, which was US$9.6 million in 2016 compared to US$0.9 million in 2015 and enabled the Group to report a profit before tax of US$1.9 million (2015: loss before tax of US$4.6 million).

In addition to managing higher levels of production, much of the operational activity in 2016 was directed towards further enhancements to the gas plant processes, sustaining higher output from the gas and condensate fields and drilling of new horizontal wells on the Uzen oil field.

Gas/condensate production

The Dobrinskoye and VM fields are managed as a single business unit. Production from the fields is processed at the gas plant located next to the Dobrinskoye field, extracting the condensate and processing the gas to pipeline standards before input into Gazprom's regional pipeline system via an inlet located at the plant. During 2015, two production wells on the VM field, VM#3 and VM#4 were drilled. VM#4 was put on production during November 2015 while the completion and first production from the VM#3 well was deferred until spring of 2016 when the gas plant upgrades enabled the higher throughput rates to utilise its full capacity.

With a total of four wells in the principal reservoir, the Evlano Livinskiy carbonate, and a further well in the secondary Bobrikovskiy sandstone reservoir, management considers the VM field to be fully developed and capable of producing at the plateau rate of 1.0 mmcm/d (35.3 mmcf/d) with associated condensate of 2,000 bpd – a total of approximately 7,800 boepd.

During January and February 2015, and again during May and June 2015, production of gas and condensate had to be temporarily suspended since it was not possible to sell the condensate produced in the local market. (Gas and condensate are produced simultaneously from the wells and once the storage capacity at the gas plant is full, it is necessary to cease production.) At the end of 2015, however, Volga Gas commenced export sales of condensate and with this channel available it was possible to continue production steadily throughout 2016 in spite of similar market disruptions being experienced.

Production during 2016 averaged 25.5 mmcf/d of gas and 1,557 bpd of condensate (2015: 12.5 mmcf/d of gas and 784 bpd condensate), an overall increase of 103% in equivalent barrels of oil terms. Nevertheless, this production rate is below the full capacity of the existing wells as the gas processing plant's operations continue to be fine-tuned. This is covered in more detail below. However, during December 2016, the output averaged 32.2 mmcf/d of gas and 1,799 bpd of condensate, a total of 7,167 boepd, more closely reflecting management's estimate of the actual capabilities of the wells.

During 2016, gas continued to be sold to Trans Nafta under contract at a fixed Ruble contract gas sales price of RUR 4,201 per mcm which has been in force since July 2015. However, as of December 2016, a proportion of the gas sales have been made directly to Gazprom which has resulted in a modest increase in the net realisations. In US Dollar terms, however, the recovery of the Ruble has led to the gas sales price rising from US$1.29/mcf in January to US$1.68/mcf in December. The average gas sales price for 2016 was US$1.51/mcf (2015: US$1.49).

Prior to late 2015 condensate was sold entirely into the local domestic market. However, with the periods of low domestic demand which impacted our business during 2015, channels for exporting condensate were developed and the first cargoes of condensate were sold to export customers in the Baltic region during November and December 2015. During 2016 approximately 48% of total sales of condensate were to export customers (2015: 2%).

During 2016 the average condensate netback price (after accounting for export taxes and transportation costs) was US$24.83 per barrel (2015: US$23.89).

Average unit production costs on the gas condensate fields increased moderately to US$5.19 per boe in 2016 (2015: US$5.06). The recovery in the Ruble, in which effectively all the costs are denominated, and higher costs associated with chemicals consumed in gas processing and higher costs of waste disposal, were partly offset by other cost savings.

Gas processing plant

During the first half of 2016, the Dobrinskoye gas processing plant was consistently operating at average rates of 750,000 m³ per day (26.5 million cubic feet per day). Since August 2016, the flow rates from the gas fields were increased to test the capability of the plant to process at the planned higher rate of one million m³/day (35.3 mmcf/d). As a result, management is confident that the gas plant is capable of sustained throughput at the rate of 35.3 mmcf/d. This was actually achieved in the month of December 2016.

While the physical process plant and pipelines were designed to operate at 1 million m³ per day, the need to dispose of bulky spent chemicals used in gas sweetening remains a constraint on the operations.

During 2016, technical studies and tests were conducted for alternative sweetening chemical processes. As a result of these tests, management has decided that a switch to Redox-based gas sweetening would be the optimal solution for the gas plant. The key advantage of this process is that the chemical used can be easily regenerated and reused resulting in significantly lower chemical costs and eliminating much of the bulk waste materials. The existing process units can be used for this with only minor modification. Full scale trials of the Redox-based sweetening process are continuing through April 2017.

As announced on 29 November 2016, the Board has given preliminary authorisation to a project based at the Group's Dobrinskoye gas processing plant for the capture, storage and sale of LPG.

Oil, gas and condensate reserves

	Oil & condensate (mmbbl)	Gas (bcf)	LPG (tonnes) (000)	Total (mmboe)
As at 31 December 2015				
Proved reserves	12.989	142.6	–	36.698
Proved plus probable reserves	14.293	153.5	–	39.879
Production: 1 January – 31 December 2016	0.828	9.3	–	2.382
Revisions to estimates:				
Proved reserves	(1.210)	(34.8)	277	(3.697)
Proved plus probable reserves	(1.312)	(12.7)	367	0.908
As at 31 December 2016				
Proved reserves	**10.951**	**98.5**	**277**	**30.619**
Proved plus probable reserves	**12.153**	**131.5**	**367**	**38.405**

Notes
1. Volga Gas (through its wholly-owned subsidiaries PGK and GNS) is the operator and has a 100% interest in four licences to explore for and produce oil, gas and condensate in the Volga region.
2. The reserve estimates as at 31 December 2016 were independently assessed by OOO Geostream Assets Management. The full reserve report is available on the Company's website: www.volgagas.com. The estimates at 31 December 2015 were based on the reserve evaluation conducted by Miller and Lents in 2012 and adjusted for subsequent production.
3. The reserve estimates were prepared in metric units: tonnes for oil, condensate and LPG and standard cubic metres for gas. The conversion ratios from tonnes to barrels applied in the table above were 7.833 barrels per tonne of oil, 8.75 barrels per tonne of condensate and 11.75 barrels per tonne of LPG. One cubic metre equates to 35.3 cubic feet and one barrel of oil equivalent is given by 6,000 standard cubic feet of gas.
4. The above reserve estimates, prepared in accordance with reserve definitions prepared by the Oil and Gas Reserves Committee of the SPE, have been reviewed and verified by Mr Andrey Zozulya, Director and Chief Executive Officer of Volga Gas plc, for the purposes of the Guidance Note for Mining, Oil and Gas companies issued by the London Stock Exchange in June 2009. Mr Zozulya holds a degree in Geophysics and Engineering from the Groznensky Oil & Gas Institute and is a member of the Society of Petroleum Engineers.

LPGs, primarily comprising propane and butane, are currently either included in the sales gas stream or flared.

The LPG project will provide an additional product stream which is expected to increase total sales volumes by approximately 10% and to enhance profitability.

The construction of the project is expected, subject to the necessary regulatory approvals, to commence during Q2 2017 and be completed before the end of 2017. The total capital investment in the project is estimated at US$5.0 million.

Oil production

The Uzen oil field has been producing oil from a cretaceous Aptian reservoir at a depth of approximately 1,000 metres since 2009. Until 2016 it produced under natural reservoir pressure drive. As the oil was produced, the oil-water contact in the reservoir rose and the wells at the edge of the field were shut in as water cut increased. Consequently, by the start of 2016, production had declined to 300 bopd from three wells. During H1 2016 workovers were conducted on the producing wells to block off water inflow into the well bores and to install electrical submersible pumps to provide artificial lift on the wells. As a result of these activities, the ongoing oil production rate increased from approximately 450 bpd to over 850 bpd and these rates were sustained through the rest of 2016.

During November and December 2016, a sidetrack from the currently non-producing Uzen #4 well was being drilled with the intention of producing oil from a potentially bypassed "attic" in the Aptian reservoir. However, during the drilling of a deviated section from the existing vertical well, the drill bit and certain directional drilling tools supplied by Schlumberger became stuck in the well, as a result of a faulty pump interrupting drilling mud circulation. Various attempts were made to release the stuck drill bit but without success. Consequently the operation was suspended. Given the attractiveness of accessing incremental reserves in a side track well, Volga Gas will recommence drilling a sidetrack having appointed a new drilling contractor.

Volga Gas has, however, incurred costs of US$1.6 million, primarily for replacement of the directional drilling tools belonging to Schlumberger.

There remain significant proved undeveloped reserves in the shallower Albian reservoir. Following a technical study carried out during 2015, management recommended a development plan for this reservoir would be to drill up to two horizontal production wells. The cost of each of these wells is currently estimated to be US$3.0 million and would expect to develop over 2 million barrels of reserves at a capital cost of $3.00 per barrel of reserves. The first horizontal well is to commence drilling as soon as Eurasia Drilling, the newly-appointed contractor, has mobilised its rig onto the prepared location.

The Group's oil production, whilst of modest scale, has been very profitable and a useful contributor to cash flow. With successful development of the Albian reserves, this would become a more important contributor to future profitability.

Exploration

During 2016, as a result of the decision to minimise expenditures, exploration activity was confined to internal technical studies.

Nevertheless, the Group has identified a number of exploration targets in the Karpenskiy Licence Area at shallow horizons of between 1,000 and 2,000 metres depth. These provide low-cost opportunities to add potentially material oil reserves. While management recognises the potential of these prospects, the immediate priority is to maximise the value and cash generation from proved resources.

The Group has fulfilled all its licence commitments on the Karpenskiy Licence Area and further drilling in the area is discretionary. Nevertheless, future development of the oil potential in the Group's licences is a key element of management's medium-term strategy.

Oil, gas and condensate reserves as of 1 January 2017

In December 2016 Volga Gas commissioned an independent evaluation of the Group's oil, gas and condensate reserves. This has resulted in an overall reduction of proved reserves of 3.7 mmboe, or 10.8%, but an overall increase of 0.9 mmboe in proved and probable ("2P") reserves, a 2.4% increase.

The principal changes to the reserve estimates arose from a downgrade in reserves from the Dobrinskoye field, accounting for a 3.5 mmboe reduction in proved reserves and of 2.7 mmboe in 2P reserves. This was offset by increases in reserves at the Uzen field by 2.3 million barrels of proved and 1.7 million barrels of 2P reserves. On the VM field, there was a reduction of 2.8 mmboe in proved reserves but a net increase of 1.7 mmboe in 2P reserves, reflecting a more conservative basis of estimation. Within the VM reserves, a proportion of gas reserves have been reclassified as LPG to reflect the fact that when LPG extraction takes place a proportion of gas currently sold down the pipeline will be converted into LPG.

The independent assessment of the reserves and net present value of future net revenue ("NPV") attributable to the Group's three principal fields, Dobrinskoye, Vostochny Makarovskoye and Uzenskoye, as at 31 December 2016, was prepared in accordance with reserve definitions set by the Oil and Gas Reserves Committee of the Society of Petroleum Engineers ("SPE").

The table above shows the proved and probable reserves as at 31 December 2016 and changes from previous estimates.

Andrey Zozulya
Chief Executive Officer

Financial Review

Vadim Son
Chief Financial Officer

"Strong cash generation and profitability"

Results for the year

In 2016, the Group generated US$39.4 million in turnover (2015: US$17.8 million) from the sale of 837,837 barrels of crude oil and condensate (2015: 438,910 barrels) and 9,210 million cubic feet of natural gas (2015: 4,545 million cubic feet).

The average price realised for liquids sold in the domestic market was the equivalent of US$30.59 per barrel (2015: US$25.16 per barrel). During 2016 approximately 48% of condensate sales were to export customers in the Baltic States (2015: 2%). Export sales incur selling expenses such as export taxes and transportation costs of US$4.1 million (2015: US$ 0.3 million) whereas for domestic sales the selling price is effectively a wellhead netback price. The average netback price for liquids sales, calculated by deducting selling expenses from revenue attributed to oil and condensate sales, in 2016 was US$25.70 (2015: US$24.43).

The gas sales price during 2016 averaged US$1.51 per thousand cubic feet (2015: US$1.49 per thousand cubic feet), the increase being entirely attributable to the movement in the Ruble/US Dollar exchange rate. The sales price of gas in Rubles was unchanged in 2016 (increased by 8.1% in July 2015), although in December 2016 the Company commenced sales directly to Gazprom which resulted in a small increase in realised price. Production activities generated a gross profit of US$13.1 million in 2016 (2015: US$2.2 million).

In 2016, the total cost of production increased to US$11.0 million (2015: US$7.4 million), with variable costs driven by higher production volumes, some Ruble inflation and the effect of the recovery in the Ruble on our predominantly Ruble-denominated costs. Unit field operating costs fell to US$3.93 per boe (2015: US$5.03 per boe), partly as a result of fixed costs shared among higher volumes and partly from cost efficiencies. Production-based taxes were US$10.3 million (2015: US$5.9 million) reflecting higher volumes and the impact of oil prices and Ruble exchange rates on Mineral Extraction Tax ("MET") rates as well as the impact of further formula changes that came into effect on 1 January 2016. More accurate metering of unstabilised condensate enabled a relative reduction of volumes taxed. MET paid in 2016 represented 29% of netback revenues (2015: 35% of revenues).

Operating and administrative expenses in 2016 were US$4.5 million (2014: US$3.4 million).

The Group experienced a ten-fold increase in EBITDA (defined in the operational and financial summary on page 11 as operating profit before non-cash charges, including exploration expense, depletion and depreciation) to US$9.6 million (2015: US$0.9 million).

Since the Group uses proved reserves as a basis of calculation of the annual depletion charge, the unit rate of Depletion, Depreciation and Amortisation ("DD&A") increased as a result of the 10.8% reduction in proved reserves. This, combined with the 99% increase in production, led to a DD&A charge in 2016 of US$5.0 million (2015: US$2.4 million).

With exploration and evaluation expenses of US$0.3 million in 2016 (2015: US$0.6 million) and a provision of US$1.8 million for the write-off of development assets, mainly arising from compensation payable in relation to the stuck hole in the Uzen#4 sidetrack (2015: US$3.0 million), the Group recorded an operating profit for 2016 of US$2.5 million (2015: operating loss of US$5.0 million).

Including net interest income of US$0.2 million (2015: US$0.1 million) and other net losses of US$0.8 million (2015: net gain of US$0.3 million), the Group recognised a profit before tax of US$1.9 million (2015: loss before tax of US$4.6 million) and reported net profit after tax of US$1.2 million (2015: net loss after tax of US$4.1 million) after a deferred tax charge of US$0.7 million (2014: deferred tax credit of US$0.6 million).

Cash flow

Group cash flow from operating activities was US$13.3 million (2015: US$1.2 million). Net working capital movements contributed cash inflow of US$2.9 million in 2016 (2015: US$0.8 million), which included movements in prepayments of US$1.9 million from export customers (2015: US$0.9 million). With lower capital expenditures in 2016, the net outflow from investing activities was US$4.6 million (2015: US$8.7 million). Net cash inflow from financing activities was US$3.6 million (2015: outflow of US$1.0 million).

Dividend

In July 2014, the Board announced the adoption of a policy to distribute approximately 50% of consolidated net profit after tax as a cash dividend. Dividends of US$0.05 per ordinary share were declared in respect of the year ended 31 December 2014. In light of the material reduction in the oil price, adverse financial conditions prevailing in Russia and the losses incurred, no dividends were paid in 2016. However, in recognition of the recovery in profitability and the financial position of the Group, the Board

considers it an appropriate time to resume distributions. Consequently the Board is recommending a dividend of US$0.007 per ordinary share in respect of 2016 and in addition a special dividend of US$0.055 per ordinary share, subject to approval at the Annual General Meeting on 19 May 2017.

Capital expenditure

During 2016 capital expenditure of US$4.2 million was incurred (2015: US$10.4 million), of which US$3.9 million was incurred on development and producing assets (2015: US$9.8 million) and US$0.3 million incurred on exploration (2015: US$0.6 million). Capital expenditure in 2016 includes final payments for drilling on the VM field, drilling and workovers on the Uzen oil field and upgrades to the gas processing plant.

Balance sheet and financing

As at 31 December 2016, the Group held cash and bank deposits of US$19.7 million (2015: US$6.8 million). All of the Group's cash balances are held in bank accounts in the UK and Russia and the majority of the Group's cash is held in US Dollars.

In December 2016, the Group drew down from a RUR 240 million (US$4.0 million) of bank facility, which is to be utilised to fund purchases of equipment for the LPG project. Total debt as at 31 December 2016 was US$4.0 million (2015: nil).

As at 31 December 2016, the Group's intangible assets increased to US$3.5 million (2015: US$2.9 million). Property, plant and equipment, increased to US$55.9 million (2015: US$48.3 million), primarily reflecting the impact of foreign exchange adjustments. The carrying values of the Group's assets relating to its main cash generating units have been subject to impairment testing. The result of the impairment tests, including sensitivity analysis around the central economic assumptions as detailed in Note 4(b) to the Accounts, showed no requirement for impairment, although as noted above there were impairments and write-offs relating to unsuccessful operations.

For the year ending 31 December 2016, the Group recorded a currency retranslation income of US$10.5 million (2015: expense of US$15.3 million) in its Other comprehensive income, relating to the movement of the Ruble against the US Dollar.

The Group's committed capital expenditures are less than expected cash flow from operations and cash-on-hand and such expenditures can be managed in light of the volatility in international oil prices and the Ruble. The Group may consider additional debt facilities to fund the longer-term development of its existing licences and operational facilities as appropriate.

The Group's financial statements are presented on a going concern basis, as outlined in note 2.1 to the Accounts.

Vadim Son
Chief Financial Officer

Five year financial and operational summary

Sales volumes	2016	2015	2014	2013	2012
Oil & condensate (barrels '000)	828	439	604	547	530
Gas (mcf)	9,320	4,545	5,671	3,128	1,193
Total (boe '000)	**2,381**	**1,196**	**1,549**	**1,069**	**728**

Operating Results (US$ 000)	2016	2015	2014	2013	2012
Oil and condensate sales	25,380	11,041	27,220	26,067	25,526
Gas sales	14,032	6,786	12,203	8,554	2,769
Revenue	**39,412**	**17,827**	**39,423**	**34,621**	**28,295**
Field operating costs	(9,367)	(6,016)	(7,805)	(5,946)	(3,776)
Production-based taxes	(10,255)	(5,877)	(8,344)	(8,095)	(8,951)
Depletion, depreciation and amortisation	(5,037)	(2,345)	(4,656)	(2,611)	(2,280)
Other production expenses	(1,601)	(1,352)	(1,709)	(1,799)	(1,562)
Cost of sales	**(26,260)**	**(15,589)**	**(22,514)**	**(18,451)**	**(16,569)**
Gross profit	**13,152**	**2,238**	**16,909**	**16,170**	**11,726**
Selling expenses	(4,052)	(319)	–	–	–
Exploration expenses	(265)	(635)	–	(2,519)	(8,475)
Write-off of development assets	(1,798)	(2,950)	–	(1,439)	(188)
Operating, administrative & other expenses	(4,526)	(3,377)	(4,157)	(4,029)	(8,969)
Operating profit/(loss)	**2,511**	**(5,043)**	**12,752**	**8,183**	**(5,906)**

Net realisation	2016	2015	2014	2013	2012
Oil & condensate (US$/barrel)	30.65	25.16	45.07	47.63	48.21
Oil & condensate netback (US$/barrel)	25.76	24.43	–	–	–
Gas (US$/mcf)	1.51	1.49	2.15	2.73	2.32

Operating data (US$/boe)	2016	2015	2014	2013	2012
Production and selling costs	3.93	5.03	5.04	5.56	5.18
Production-based taxes	4.31	4.91	5.39	7.58	12.29
Depletion, depreciation and other	2.12	1.98	3.01	2.44	3.13

EBITDA calculation (US$ 000)	2016	2015	2014	2013	2012
Operating profit/(loss)	2,511	(5,043)	12,752	8,183	(5,906)
Exploration expenses	265	635	–	2,519	8,475
DD&A and other non-cash expenses	6,857	5,319	4,656	4,050	5,413
EBITDA	**9,634**	**911**	**17,408**	**14,752**	**7,982**
EBITDA per boe	4.05	0.76	11.24	13.81	10.96

Netback realisation for oil and condensate is calculated by deducting selling expenses from oil, gas and condensate sales.

Principal Risks and Uncertainties

The Group is subject to various risks relating to political, economic, legal, social, industry, business and financial conditions. The following risk factors, which are not exhaustive, are particularly relevant to the Group's business activities:

Volatility of oil prices

The supply, demand and prices for oil are influenced by factors beyond the Group's control. These factors include global and regional demand and supply, exchange rates, interest and inflation rates and political events. A significant prolonged decline in oil and gas prices could impact the profitability of the Group's activities.

All of the Group's revenues and cash flows come from the sale of oil, gas and condensate. If sales prices should fall below and remain below the Group's cost of production for any sustained period, the Group may experience losses and may be forced to curtail or suspend some or all of the Group's production, at the time such conditions exist. In addition, the Group would also have to assess the economic impact of low oil and gas prices on its ability to recover any losses the Group may incur during that period and on the Group's ability to maintain adequate reserves.

The Group does not currently hedge its crude oil production to reduce its exposure to oil price volatility as the structure of taxes applied to oil and condensate production in Russia effectively reduce the exposure to international market prices for oil. In addition, the Ruble exchange rate has tended to move with the oil price, reducing the overall volatility of oil prices when translated into Russian Rubles.

Market risks

The Group's revenues generated from oil and condensate production have typically been from sales to local domestic customers. There have been periods when the local market has been unable to purchase condensate, causing temporary suspension of production and loss of revenues. Since November 2015, the Group has been selling up to 50% of its condensate into regional export markets to mitigate this risk. Gas sales are made, via an intermediary, into the domestic market via the Gazprom pipeline network. In December 2016, the Group commenced sales of gas directly to Gazprom. The region in which the Group operates is reliant on external gas supplies. Consequently, the risk of insufficient demand for the Group's gas is considered low. Gas sales have generally been conducted as expected, subject to occasional constraints during pipeline maintenance operations.

Oil and gas production taxes

The Group's sales generated from oil and gas production are subject to Mineral Extraction Taxes, which form a material proportion of the total costs of sales. The rates of these taxes are subject to changes by the Russian government. Changes to rates which came into effect during 2015 and in 2016 materially increased the rates on crude oil, condensate and natural gas. With oil prices at low levels and Russian government budgets under pressure, there are risks of further adverse changes to production taxes.

Exploration and reserve risks

Whilst the Group will seek to apply the latest technology to assess exploration licences, the exploration for, and development of, hydrocarbons is speculative and involves a high degree of risk. These risks include the uncertainty that the Group will discover sufficient commercially exploitable oil or gas resources in unproved areas of its licences. Unsuccessful exploration efforts may result in impairment to the balance sheet value of exploration assets.

In December 2016 the Group commissioned a reserve evaluation based on reporting standards set by the Society of Petroleum Engineers. The revisions to the Group's reserve estimates are shown in the Operational Review on pages 8 and 9. If the actual results of producing the Group's fields are significantly different to expectations, there may be changes in the future estimates of reserves. These may impact the balance sheet carrying values of the Group's property, plant and equipment.

Environmental risk

The oil and gas industry is subject to environmental hazards, such as oil spills, gas leaks, ruptures and discharges of petroleum products and hazardous substances, including waste materials generated by the sweetening process currently in use at the Dobrinskoye gas processing plant. These environmental hazards could expose the Group to material liabilities for property damages, personal injuries, or other environmental harm, including costs of investigating and remediating contaminated properties.

The Group is subject to stringent environmental laws in Russia with regard to its oil and gas operations. Failure to comply with such laws and regulations could subject the Group to material administrative, civil or criminal penalties or other liabilities. Additionally, compliance with these laws may, from time to time, result in increased costs to the Group's operations, impact production, or increase the costs of potential acquisitions.

The Group liaises closely with the Federal Service of Environmental, Technological and Nuclear Resources of the Saratov and Volgograd Oblasts on potential environmental impact of its operations and conducts environmental studies both as required by, and in addition to, its licence obligations to mitigate any specific risk. The Group's operations are regularly subject to independent environmental audit. The Group did not incur any material costs relating to the compliance with environmental laws during the period.

Risk of operating oil and gas properties

The oil and gas business involves certain operating hazards, such as well blowouts, cratering, explosions, uncontrollable flows of oil, gas or well fluids, fires, pollution and releases of toxic substances. Any of these operating hazards could cause serious injuries, fatalities, or property damage, which could expose the Group to liabilities. The settlement of these liabilities could materially impact the funds available for the exploration and development of the Group's oil and gas properties. The Group maintains insurance against many potential losses and liabilities arising from its operations in accordance with customary industry practices, but the Group's insurance coverage cannot protect it against all operational risks.

Foreign currency risk

The Group's capital expenditures and operating costs are predominantly in Russian Rubles ("RUR") while a minority of administrative expense is in US Dollars, Euros and Pounds Sterling. Revenues are predominantly received in RUR so the operating profitability is not materially exposed to moderate short-term exchange rate movements. The functional currency of the Group's operating subsidiaries is the

RUR and the Group's assets and liabilities are predominantly RUR-denominated. As the Group's presentational currency is the US Dollar, the significant devaluation of the RUR against the US Dollar negatively impacts the Group's financial statements.

Business in Russia

Amongst the risks that face the Group in conducting business and operations in Russia are:

- Economic instability, including in other countries or the global economy, that could lead to consequences such as hyperinflation, currency fluctuations and a decline in per capita income in the Russian economy.
- Governmental and political instability that could disrupt, delay or curtail economic and regulatory reform, increase centralised authority or result in nationalisations.
- Social instability from any ethnic, religious, historical or other divisions that could lead to a rise in nationalism, social and political disturbances or conflict.
- Uncertainties in the developing legal and regulatory environment, including, but not limited to, conflicting laws, decrees and regulations applicable to the oil and gas industry and foreign investment.
- Unlawful or arbitrary action against the Group and its interests by the regulatory authorities, including the suspension or revocation of their oil or gas contracts, licences or permits or preferential treatment of their competitors.
- Lack of independence and experience of the judiciary, difficulty in enforcing court or arbitration decisions and governmental discretion in enforcing claims.
- Unexpected changes to the federal and local tax systems.
- Laws restricting foreign investment in the oil and gas industry.
- The imposition of sanctions upon certain entities in Russia.

The Group's operations and financial management have not to date been impacted directly by any sanctions.

Legal systems

Russia, and other countries in which the Group may transact business in the future, have or may have legal systems that are less well developed than those in the United Kingdom. This could result in risks such as:

- Potential difficulties in obtaining effective legal redress in the court of such jurisdictions, whether in respect of a breach of contract, law or regulation, including an ownership dispute.
- A higher degree of discretion on the part of governmental authorities.
- The lack of judicial or administrative guidance on interpreting applicable rules and regulations.
- Inconsistencies or conflicts between and within various laws, regulations, decrees, orders and resolutions.
- Relative inexperience of the judiciary and courts in such matters.

In certain jurisdictions, the commitment of local business people, government officials and agencies and the judicial system to abide by legal requirements and negotiated agreements may be more uncertain, creating particular concerns with respect to licences and agreements for business. These may be susceptible to revision or cancellation and legal redress may be uncertain or delayed. There can be no assurance that joint ventures, licences, licence applications or other legal arrangements will not be adversely affected by the jurisdictions in which the Group operates.

Liquidity risk

At 31 December 2016 the Group had US$19.7 million (2015: US$6.8 million) of cash and cash equivalents of which US$16.1 million was held in bank accounts in Russia (2015: $2.0 million). A significant proportion of the cash held in Russia is expected to be placed in the UK during 2017 ahead of proposed dividend payments. As at 31 December 2016, total bank debt was US$4.0 million (2015: nil). The Group has fully drawn on the debt facilities available as at 31 December 2016. The Group intends to fund its ongoing operations and development activities from its cash resources and cash generated by its established operations. At 31 December 2016 the Group has budgeted capital expenditures US$12.3 million of which US$4.0 million is allocated to the LPG project and US$5.7 million is for the Uzen horizontal well. There were approximately US$4.9 million of accounts payable relating to capital expenditures and other expenses incurred in the year ended 31 December 2016 (2015: US$1.5 million).

The Board considers that the Group will have sufficient liquidity to meet its obligations after payment of proposed dividends of US$5.0 million. All current and planned capital expenditures are discretionary and may be deferred or cancelled in the light of the Group's cash generation and liquidity position.

Through its ordinary course activities, the Group is exposed to legal, operational and development risk that could delay growth in its cash generation from operations or may require additional capital investment that could place increased burden on the Group's available financial resources.

The Group is also exposed to fraudulent transfers of funds from its bank accounts. During the year ended 31 December 2015, the Group enhanced its protections and procedures after suffering such fraudulent transfers.

Capital risk

The Group manages capital to ensure that it is able to continue as a going concern whilst maximising the return to shareholders. The Group is not subject to any externally imposed capital requirements. The Board regularly monitors the future capital requirements of the Group, particularly in respect of its ongoing development programme. Management expects that the cash generated by the operating fields will be sufficient to sustain the Group's operations and committed capital investment for the foreseeable future and has a policy of maintaining a minimum level of liquidity to cover forward obligations. Further short-term debt facilities may be arranged to provide financial headroom for future development activities.

Vadim Son
Chief Financial Officer

The Strategic Report, which comprises pages 2 to 12, was approved by the Board on 3 April 2017 and signed on its behalf by

Caros Consulting Ltd.
Company Secretary

Board of Directors

Mikhail Ivanov Non-Executive Chairman

Mr Ivanov was Chief Executive Officer of the Company from its foundation until 5 May 2015. Mr Ivanov was also a Partner and Director of Oil and Gas Projects at Baring Vostok Capital Partners. He has a long history of involvement in the oil sector. He worked for over ten years at Schlumberger, the international oil services company, where he served as head of its Iran operations and was responsible for business development in Russia. Prior to joining Schlumberger, he founded and headed two companies that focused on oil production and service. Mr Ivanov holds an MS degree in Geophysics from Novosibirsk State University and an MBA from the Kellogg School of Management of Northwestern University. He is an elected member of the Society of Petroleum Engineers.

Appointed to the Board: 25 July 2006
Appointed as Chairman: 5 June 2015
Committee membership: n/a

Andrey Zozulya Chief Executive Officer, Executive Director

Mr Zozulya is a Russian citizen and has over 20 years' experience in the oil sector in Russia both with major oil and oil service companies, including over ten years with Schlumberger. He also has experience of operating in the Saratov region in which Volga Gas' operations are based. He has a degree in Geophysics and Engineering from the Groznensky Oil & Gas Institute and is a member of the Society of Petroleum Engineers.

Appointed to the Board: 5 May 2015
Committee membership: n/a

Michael Calvey Non-Executive Director

Mr Calvey is a Senior Partner of Baring Vostok Capital Partners and a Director of Baring Private Equity International and is on the Boards of several of Baring Vostok's portfolio companies. He began working in Moscow in 1994 as one of the members of the consulting committee of the First NIS Regional Fund. He is a member of the investment committees of three Baring Vostok funds. He is also a member of the Investment Committees of the Baring Asia and Baring India funds. Before 1994, Mr Calvey lived in London and New York, where he worked at the European Bank for Reconstruction and Development ("EBRD") and Salomon Brothers. At EBRD he was responsible for investments in the energy sector of Central and Eastern Europe. At Salomon Brothers Mr Calvey worked on mergers and acquisitions and capital market projects in the oil and gas sector. He is a member of the Boards of the Atlantic Council and the Emerging Markets Private Equity Association.

Appointed to the Board: 29 September 2006
Committee membership: Audit, Nomination

Ronald Freeman Non-Executive Director

Mr Freeman is a member of the Executive Committee of the Atlantic Council of the United States (Washington DC), and a past independent Director on the Boards of Sberbank, Severstal, and Troika Dialog. From 1973 to 1991 and from 1997 until his retirement from Citigroup as co-head of European Investment Banking in 2000, he was an investment banker specialising in financing and mergers and acquisition for companies in the oil and gas industry with Salomon Brothers, now a unit of Citigroup. From 1991 to 1997, he was head of the Banking Department of the European Bank for Reconstruction and Development (London).

Appointed to the Board: 14 March 2007
Committee membership: Audit, Nomination, Remuneration

Aleksey Kalinin Non-Executive Director

Mr Kalinin served as Chairman of the Board from 14 March 2007 until 5 June 2015, remaining as a Non-Executive Director. Mr Kalinin is a Senior Partner of Baring Vostok Capital Partners. He joined Baring Vostok in 1999 from Alfa Capital, where he served for six years as the Director of the Department for Direct Investments. Mr Kalinin represents the interests of Baring Vostok's funds on the Board of Directors of a wide range of portfolio companies. He has a doctorate from the Moscow Power Engineering Institute, where he conducted scientific research, lectured for 12 years and served as the Director of the Youth Center for Scientific and Technical Creativity.

Appointed to the Board: 29 September 2006
Committee membership: Remuneration

Vladimir Koshcheev Non-Executive Director

Mr Koshcheev currently acts as President of Joint Stock Company "NPO POG". Until 2009 he was President of Pervaya Investizionno–Stroitelnaya Company LLC, Spinaker LLC. He has been Chairman of CJSC AKSM since 2002. Mr Koshcheev was President of Privolzhskaya Neftyanaya Company LLC between 2003 and 2005 and was previously a shareholder in – and acted as President of – Vesla. Mr Koshcheev received a specialist diploma from Moscow State Technical University in 1978 and he is a member of the Russian Academy of Natural Sciences.

Appointed to the Board: 29 September 2006
Committee membership: n/a

Stephen Ogden Non-Executive Director

Mr Ogden is a Non-Executive Director of the West African shopping mall operator, Persianas. He was previously a Non-Executive Director of United Confectioneries (Russia), Heineken Russia and Metropolis Media (former Yugoslavia). Mr Ogden was Chief Financial Officer of the Bochkarev Brewery in St Petersburg from 1997 to 2002. Prior to becoming Chief Financial Officer of Bochkarev, Mr Ogden was an auditor with KPMG and PricewaterhouseCoopers, and Financial Controller of CS First Boston (Moscow). Mr Ogden has a joint honours degree in economics & politics from Durham University, England, and is a qualified British chartered accountant.

Appointed to the Board: 14 March 2007
Committee membership: Audit, Nomination, Remuneration

Corporate Governance Statement

Introduction
The Board's overriding objective is to ensure that the Group delivers long-term capital appreciation for its shareholders.

Compliance
As Volga Gas plc is quoted on the AIM market of the London Stock Exchange, it is neither required to comply with the 2014 UK Corporate Governance Code that was published by the Financial Reporting Council (the "Code") nor issue a statement of compliance with it. Nevertheless, the Board fully supports the principles set out in the Code and seeks to follow these as best practice wherever this is appropriate having regard to the size of the Company, the resources available to it and the interpretation of the Code in the Quoted Companies Alliance Corporate Governance Code for Small and Mid-sized Quoted Companies.

Details are provided below of how the Company applies the elements of the Code that are deemed appropriate.

Board of Directors
Role of the Board
The Board's role is to provide leadership to the Group within a framework of prudent and effective controls which enables risk to be assessed and managed. The Board sets the Group's strategic aims and ensures that the necessary financial and human resources are in place for the Group to meet its objectives, and reviews management's performance in meeting these objectives. The Board sets and monitors the Group's values and standards and ensures that the Group's obligations to shareholders and other stakeholders are understood and met.

The Board has a formal schedule of matters reserved for its approval, including:
- Strategic and policy considerations
- Annual budget, including capital expenditure
- Interim and final financial statements
- Dividend policy, share buy-backs or other distributions
- Management structure and appointments
- Mergers, acquisitions, disposals
- Capital raising
- Significant changes in accounting policies
- Appointment or removal of directors or the company secretary

Board composition
The Board currently comprises one executive director and six non-executive directors, of whom three are deemed to be independent and three non-independent:
- Mikhail Ivanov – Non-Executive Chairman
- Andrey Zozulya – Executive Director and CEO
- Michael Calvey – Non-Executive
- Ronald Freeman – Independent Non-Executive
- Aleksey Kalinin – Non-Executive
- Vladimir Koshcheev – Independent Non-Executive
- Stephen Ogden – Independent Non-Executive

Tony Alves served as Director, Chief Financial Officer and Company Secretary until 10 June 2016.

There is a clear division of responsibilities between the executive and non-executive directors.

Board balance and independence
The Board recognises that Messrs Kalinin and Calvey are not independent by virtue of their direct management responsibilities for the limited partnerships comprising Baring Vostok Private Equity Funds III and IV, the Company's controlling shareholder ("Controlling Shareholder"). However, in light of the value, experience and contacts which they afford to the Company at this stage of its development and by virtue of the Relationship Agreement, which, inter alia, ensures that the Controlling Shareholder does not exercise undue influence over the Company or prevent it from acting independently of the Controlling Shareholder, the Board believes that the continued presence of Messrs Kalinin and Calvey on the Board is beneficial for the Company. Mr Kalinin also serves as Chairman of the Board and was not considered to be independent on his appointment.

Notwithstanding under the provisions of the 2014 UK Corporate Governance Code as a "Smaller Company" the Company meets the requirements to have at least two independent non-executives on the Board.

All directors are permitted access to independent professional advice in the course of execution of their duties, at the Company's expense.

The Board has established the following committees:

Audit Committee
The Audit Committee was established in March 2007 and comprises three directors:
Mr Ogden – Chairman
Mr Freeman
Mr Calvey

The Audit Committee is responsible for selecting the Group's independent auditors, pre-approving all audit and non-audit related services, reviewing with management and the independent auditors the Group's financial statements, significant accounting and financial policies and practices, audit scope and adequacy of internal audit and control systems. The Audit Committee keeps the independence and objectivity of the auditor under review and a formal statement of independence is received from the external auditor each year. The Audit Committee meets at least twice each year.

Remuneration Committee
The Remuneration Committee was also established in March 2007 and comprises three directors:
Mr Freeman – Chairman
Mr Ogden
Mr Kalinin

The Remuneration Committee is responsible for reviewing the performance of the directors and for determining compensation of the Company's key employees, including the chief executive officer, chief financial officer, and other key personnel as may be determined from time to time by the Remuneration Committee. The Remuneration Committee meets at least twice each year.

The Directors' Remuneration Report is set out on pages 21 to 22.

Nomination Committee
The Nomination Committee was established in March 2007 and comprises three directors:
Mr Freeman – Chairman
Mr Ogden
Mr Calvey

The Nomination Committee is responsible for reviewing the structure, size and composition of the Board, making recommendations to the Board concerning plans for succession for both executive and non-executive directors including the Chief Executive and other senior management, preparing a description of the role and capabilities required for a particular appointment and identifying and nominating candidates to fill Board positions as and when they arise.

Board meetings

The Board met four times during the year ended 31 December 2016 (2015: four times) with the following attendance:

	2015	2016
Mikhail Ivanov	4	4
Andrey Zozulya (attended all meetings since appointment)	4	2
Tony Alves (resigned on 10 June 2016)	2	4
Michael Calvey	4	4
Ronald Freeman	4	4
Aleksey Kalinin	4	4
Vladimir Koshcheev	4	4
Stephen Ogden	4	4

Indemnification of directors

In accordance with the Company's Articles of Association and to the extent permitted by the law of England and Wales, directors are granted an indemnity from the Company in respect of liabilities incurred as a result of their office. In respect of those matters for which the directors may not be indemnified, the Company maintained a directors' and officers' liability insurance policy throughout the financial year. This policy has been renewed for the next financial year.

Re-election of directors

The Company requires that all directors stand for re-election at intervals of no more than three years. Accordingly, Messrs Calvey, Ivanov and Koshcheev will retire at the forthcoming AGM and will seek re-election by shareholders.

Internal controls

The directors acknowledge their responsibility for the system of internal controls for the Group and for reviewing its effectiveness. Any system of internal control can only provide reasonable, and not absolute, assurance that material financial irregularities will be detected or that the risk of failure to achieve business objectives is eliminated.

The Group's risk and controls framework covers all material risks and controls including those of an operational, financial, and compliance nature. Internal control procedures consist, inter alia, of formal delegations of expenditure authority by the Board to executive management, and controls relating to key stages of transactions including supplier approval, contract signature, and payment release.

In response to an unauthorised withdrawal of cash from Group bank accounts in an apparent cyberattack in 2015, management performed a remediation and improvement of internal controls around the Group's cash handling procedures and security, including IT control processes. No such incidents have re-occurred.

The directors consider that the frequency of Board meetings and level of detail presented to the Board for its consideration in relation to the operations of the Group provide an appropriate process to identify, evaluate and manage significant risks relevant to its operations on a continuous basis, and this process is considered to be in accordance with the revised guidance on internal control published in October 2005 ("Turnbull Guidance").

In addition to formal Board meetings, management prepare detailed financial and operational reports on a monthly basis which is disseminated and discussed within the Board.

Investor relations

The Company places considerable importance on communication with shareholders and engages them on a wide range of issues. The Group has an ongoing programme of dialogue and meetings between the executive directors and institutional investors, fund managers and analysts. At these meetings a wide range of relevant issues including strategy, performance, management and governance are discussed within the constraints of the information already made public.

The Company is equally interested in the views and concerns of private shareholders and to this end ensures that the executive directors represent the Company at forums where private investors are present.

Shareholders have the opportunity to meet and question the Board at the Annual General Meeting which will be held on 19 May 2017, at which the Chairman, the Chairman of the Audit Committee and all executive directors are expected to be available. The notice of the AGM is posted to all shareholders at least 21 working days before the meeting. Financial and other information is available on the Company's website (www.volgagas.com).

By order of the Board

Caros Consulting Ltd.
Company Secretary
3 April 2017

Report of the Directors

The directors present their report together with the Group's audited consolidated financial statements for the period from 1 January 2016 to 31 December 2016.

Results and dividend

The Group's results are set out on pages 24 to 29 and show net profit of US$1.2 million for the year ended 31 December 2016 (2015: net loss of US$4.1 million). The directors propose to pay a dividend in respect of the year ended 31 December 2016 of $0.007 per ordinary share in respect of the profits earned in the year ended 31 December 2016, and a special dividend of $0.055 per ordinary share. No dividends were declared in respect of the year ended 31 December 2015 although a final dividend of US$0.0125 was paid in 2015 in respect of the year ended 31 December 2014.

Principal activities, business review and future developments

Volga Gas is a public limited company registered in England and Wales with registered number 5886534, and was incorporated in the United Kingdom on 25 July 2006 and admitted to trading on the AIM market of the London Stock Exchange on 25 April 2007. Volga Gas operates primarily through subsidiary companies as set out in Note 2.2 to the accounts. The principal activity of the Group is the exploration, development and production of its gas, condensate and oil fields in the Volga Region of European Russia. During the year, the Group owned 100% interests in four licence areas in the Saratov and Volgograd regions: Karpenskiy, Vostochny-Makarovskoye, Dobrinskoye, and Urozhainoye-2.

The Group's business strategy is to maximise the economics of production from the Vostochny Makarovskoye, Dobrinskoye and Uzenskoye fields and to explore the potentially prospective structures on the Group's licence areas. The Group also evaluates acquisition opportunities as part of its overall strategy of growing value for its shareholders.

Highlights of the Group's activities for the period ended 31 December 2016 are:

- Increases in production from both the Vostochny Marakovskoye ("VM") and the Uzen fields.
- Material improvement in financial performance and financial condition of the Group.
- Establishment of export channels for condensate sales.
- Commencement of projects for further enhancements to production and cost efficiency.

The Group's activities are described in greater detail in the Chief Executive's Report on page 6 and in the Operational Review on pages 8 and 9. The principal risks associated with the Group's activities are set out in the Risks and Uncertainties section in pages 12 to 13.

Key performance indicators

Given the nature of the business and that the Group has only three operating fields, the directors are of the opinion that further analysis using KPI's is not appropriate for an understanding of the development, performance or position of our business at this time. The directors are of the opinion that the Operational Review on pages 8 and 9 provides the relevant information.

Going concern

Having made appropriate enquiries and having examined the major areas that could affect the Group's financial position, the directors are satisfied that the Group has adequate resources to continue in operation for the foreseeable future. Accordingly they consider it appropriate to adopt the going concern basis in preparing the financial statements as described in note 2.1.

Directors

The directors who served during the year were:

Aleksey Kalinin, Chairman – Non-Executive
Mikhail Ivanov, Chairman
Michael Calvey, Non-Executive
Tony Alves, Chief Financial Officer (resigned on 10 June 2016)
Ronald Freeman, Non-Executive
Vladimir Koshcheev, Non-Executive
Stephen Ogden, Non-Executive
Andrey Zozulya, Chief Executive Officer

Messrs Calvey, Ivanov and Koshcheev will retire by rotation and offer themselves for re-election in accordance with the Company's Articles of Association.

Directors' interests

The directors serving during the year had the following beneficial interests in the shares of the Company:

	Ordinary shares of 1p each	
	31 December 2016	31 December 2015
Mikhail Ivanov	1,000,000	1,000,000
Andrey Zozulya	100,000	-
Tony Alves (resigned on 10 June 2016)	25,000	25,000
Michael Calvey[1]	-	-
Ronald Freeman	55,000	55,000
Aleksey Kalinin[1]	-	-
Vladimir Koshcheev	419,210	419,210
Stephen Ogden	205,000	205,000

1 Mr Calvey and Mr Kalinin are Co-Managing Partners of Baring Vostok Capital Partners Limited, a related party to Baring Vostok Investments PCC Limited, Baring Vostok Nominees Limited and Dehus Dolmen Nominees Limited. As such Mr Calvey and Mr Kalinin have an indirect beneficial interest in the Company.

Substantial shareholders

On 31 March 2017 the following parties had notifiable interests of 3% or greater in the nominal value of the Company's issued 1p ordinary shares:

	Number of shares	Percentage
Baring Vostok Nominees Ltd[1]	39,620,000	48.90
Mr Nicholas Mathys	10,610,000	13.10
Dehus Dolmen Nominees Ltd[2]	7,906,889	9.76
Baring Vostok Investments PCC Limited[3]	4,860,460	5.93
BNP Paribas Investment Partners S.A.	3,336,860	4.12
BlackRock Investment Management (UK) Limited	3,094,791	3.82
JP Morgan Asset Management (UK) Limited	2,761,720	3.41

1 Baring Vostok Nominees Ltd is a nominee vehicle which holds the interests of the limited partnerships which comprise Baring Vostok Private Equity Fund III.
2 Dehus Dolmen Nominees Ltd is a nominee vehicle which holds the interests of the limited partnerships which comprise Baring Vostok Private Equity Fund IV.
3 Baring Vostok Investments PCC Limited is a closed-end investment company registered in Guernsey and advised by Baring Vostok Capital Partners Group Limited, which also advises the Baring Vostok Private Equity Funds.

Options granted

An Executive Share Option Plan was adopted by the Company in July 2008 following which options over a total of 1,706,196 shares were granted to Mikhail Ivanov and to Tony Alves. All outstanding options lapse by 31 May 2017. During 2016 no further options (2015: nil) were granted. The details of these option grants are disclosed in the Remuneration Report below.

Interests in contracts

There were no contracts or arrangements during the period in which a director of the Company was materially interested and which were significant in relation to the business of the Group.

Creditors payment policy and practice

The Group aims to pay all its creditors promptly. For trade creditors it is the Group's policy to:

(i) agree the terms of the payment at the start of the business with that supplier;
(ii) ensure that suppliers are aware of the terms of the payment; and
(iii) pay in accordance with contractual and other obligations

Political and charitable contributions

No political or charitable contributions were made in the year (2015: nil).

Employment policies

The Group is committed to pursuing an equal opportunities employment policy, covering recruitment and selection, training, development, appraisal and promotion. The Group recognises the diversity of its employees, its customers, and the community at large and seeks to use employees' talents to the fullest. This approach extends to the fair treatment of people with disabilities, in relation to their recruitment, training and development. Full consideration is given to staff members who become disabled during employment.

Employee communication

The Group is committed to effective communications, which it maintains through regular information releases and staff briefings. Formal communications with employees take place through these channels. With respect to the Group's operations in Russia and the recruitment of Russian employees, announcements, contracts, interviews and advertisements are conducted in the English and Russian languages, as applicable.

Health, safety and the environment

The Group's policy and practice is to comply with health, safety and environmental regulations and requirements of the countries in which it operates, to protect its employees, contractors, assets and the environment.
The Group closely monitors its environmental obligations under the terms of its licence agreements. In particular, portions of the Karpenskiy Licence Area are located in the Saratovskiy Federal Nature Reserve and Tulipannaya Steppe Natural Sanctuary, which are protected by Russian environmental law. In accordance with Russian environmental law, all economic activity within the protected area is approved by the Russian government. The Group has ensured that all its activities minimise the impact on this sensitive environment.

UK Bribery Act

The Company has adopted Anti-Corruption and Anti-Bribery Policies and a framework of adequate procedures for managing the Volga Gas Group's responsibilities in relation to the UK Bribery Act 2010.

Market Abuse Regime ("MAR")

On 1 July 2016 the MAR came into effect. The Company has updated its procedures and records in respect of insider information and dealings by persons discharging managerial responsibilities (PDMRs), or their connected persons in compliance with the new regime.

Report of the Directors continued

Share capital
The Company has authorised ordinary share capital of 330,720,100 shares of 1p each. Under a special resolution by the shareholders of the Company on 5 June 2016, the directors have authority to allot shares up to an aggregate nominal value of £1,000,000 of which £150,000 could be issued non-pre-emptively, in accordance with sections 570 and 573 of the Companies Act 2006. This authority will expire the earlier of (i) 15 months from the passing of the Resolution, or (ii) the conclusion of the Annual General Meeting of the Company to be held in 2017.

Capital risk management
The Group's objectives when managing the balance of equity and debt capital are (a) to safeguard the Group's ability to continue as a going concern, (b) provide returns for shareholders and benefits for other stakeholders and (c) to maintain an optimal capital structure to reduce the cost of capital. In order 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.
To date the Group has been funded primarily by equity capital. It is the Group's policy to fund its capital investments primarily from retained cash and cash generated from operations although modest levels of debt may continue to be utilised when the Board considers it appropriate. In December 2016, one of the Group's operating subsidiaries entered into a US$4.0 million debt facility.

Corporate Governance
The Company's statement on Corporate Governance can be found in the Corporate Governance Statement on pages 15 to 17 of these financial statements and form part of this report by reference.

Statement of disclosure of information to auditor
As at the date of this report the serving directors confirm that;
- so far as the directors are aware, there is no relevant audit information of which the Company's auditor is unaware; and
- they have taken all steps that they ought to have taken as directors in order to make themselves aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

Auditor
The Group's auditor, KPMG LLP, has indicated its willingness to continue in office and in accordance with Section 489 of the Companies Act 2006, and a resolution concerning its reappointment will be proposed at the next Annual General Meeting.

Statement of Directors' responsibilities in respect of the Annual Report, Strategic Report, Directors' Report and the Financial Statements
The directors are responsible for preparing the Annual Report, Strategic Report and the Directors' Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare Group and Parent Company financial statements for each financial year. As required by the AIM Rules for Companies of the London Stock Exchange they are required to prepare the Group financial statements in accordance with IFRSs as adopted by the EU and applicable law and have elected to prepare the Parent Company financial statements on the same basis.

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and Parent Company and of their profit or loss for that period. In preparing each of the Group and Parent Company financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and the Parent Company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Parent Company's transactions and disclose with reasonable accuracy at any time the financial position of the Parent Company and enable them to ensure that its financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.
The directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Electronic communications
The maintenance and integrity of the Volga Gas plc website (www.volgagas.com) is the responsibility of the directors; the work carried out by the auditor does not involve consideration of these matters and, accordingly, the auditor accepts no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website. The Company's website is maintained in compliance with Rule 26 of the AIM Rules for Companies. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

On behalf of the Board

Caros Consulting Ltd.
Company Secretary
3 April 2017

Directors Remuneration Report

In common with the Board's commitment to compliance with the appropriate aspects of the 2014 UK Corporate Governance Code, the Company has adopted the Principles of Good Governance relating to directors' remuneration. The Company discloses certain information relating to directors' remuneration in this report, which is not audited.

Remuneration Committee

The Company established a Remuneration Committee in April 2007, as set out in the Corporate Governance statement on page 16. The Remuneration Committee advises the Board on Group compensation policy as it relates to executive directors and other key members of management, and may obtain advice from independent remuneration consultants appointed by the Company. The Remuneration Committee comprises Ronald Freeman (Chairman), Stephen Ogden and Aleksey Kalinin, who are all non-executive directors. Executive directors may be invited to attend meetings of the Remuneration Committee but do not vote on their own remuneration or incentives. The Remuneration Committee meets as required.

Remuneration policy

The Company's policy is to maintain levels of compensation for the Group that are comparable and competitive with peer group companies, so as to attract and retain individuals of the highest calibre, by rewarding them as appropriate for their contribution to the Group's performance.

Executive directors' employment agreement and terms of appointment

The terms of each executive director's appointment are set out in their service agreements. Each executive director agreement is based on similar terms, with no fixed duration. Each service agreement sets out details of basic salary and share options as applicable.

All executive director employment agreements can be terminated either by the director concerned or by the Company on giving six months' notice during the first 24 months of service and thereafter by giving three months' notice.

The executive directors do not participate in any Group pension scheme and their remuneration is not pensionable.
The executive directors are eligible for payment of cash bonuses and participation in any share-based incentive plan the Board implements. For the year ended 31 December 2017, the Chief Executive Officer may, on meeting certain specified operational and financial objectives agreed with the Remuneration Committee, be awarded a bonus payment of up to 100% of his basic salary.

Basic salaries

The basic salary of each executive director is established by reference to their responsibilities and individual performance.

Non-executive directors' terms, conditions and fees

The non-executive directors have been engaged under the terms of their letters of appointment. These engagements are for two years and can be terminated upon one month's notice by either party. Reappointment is subject to the Company's Articles of Association which provide that one third of the directors shall be required to retire each year.

Fees

The fees paid to non-executive directors are determined by the Board and reviewed periodically to reflect current rates and practice commensurate with the size of the Company and their roles.

The remuneration of the non-executive directors is a matter for the Chairman of the Board and the Chief Executive Officer. In the event of the appointment of an independent non-executive chairman his remuneration would be a matter for the Chairman of the Remuneration Committee and the Chief Executive Officer.

Audited information – Directors' detailed emoluments

	Salary US$ 000	Bonus US$ 000	Compensation for loss of office US$ 000	Fees US$ 000	Aggregate remuneration for the year 31 December 2016 US$ 000	Aggregate remuneration for the year 31 December 2015 US$ 000
Executive directors						
M. Ivanov	–	–	–	120	**120**	235
A. Zozulya	194	65	–	–	**259**	130
A. Alves (resigned 10 June 2016)	117	–	39	10	**166**	300
Non-executive directors						
M. Calvey	–	–	–	–	**–**	–
R. Freeman	–	–	–	50	**50**	50
A. Kalinin	–	–	–	–	**–**	–
V. Koshcheev	–	–	–	–	**–**	–
S. Ogden	–	–	–	50	**50**	50

Directors Remuneration Report continued

Director's emoluments comprised salaries of US$311,000 (2015: US$595,000), bonuses US$65,000 (2015: nil), non-executive directors' fees of US$230,000 (2015: US$170,000) and compensation for loss of office to Chief Financial Officer of US$ 39,000 (2015: nil). There were no share grant expenses in 2016 (2015: nil).

During the year ended 31 December 2016, Mr Zozulya was awarded a performance related bonus of US$65,000. He elected to invest substantially all of this in the shares of the Company. Accordingly, the Company purchased 100,000 of its ordinary shares in the market and transferred these shares to Mr Zozulya. The balance of the bonus, amounting to US$2,688, is payable in cash.

Directors' interests in the share capital of the Company

The directors' interests in the share capital of the Company are disclosed in the Report of the Directors on page 18. On 13 January 2017, Baring Vostok Investment PCC Limited, a party associated with Messrs Calvey and Kalinin, purchased 4,860,460 ordinary shares of the Company. There have been no other changes in the interest of any director between 1 January 2017 and the date of this report.

Directors' share options

The Company adopted an Executive Share Option Plan ("ESOP") on 14 July 2008, which was subsequently amended on 17 December 2008. Under the terms of this Plan, up to a maximum of 2,843,661 shares (equivalent to approximately 5% of the then issued share capital) may be allocated and subject to performance criteria and vesting periods as specified by the Remuneration Committee.

During 2008, the Company granted options to acquire 1,137,464 ordinary shares to Mr Ivanov under the terms of the ESOP. The options may be exercised at a price of 405p per share and vest in equal portions on May 2010, 2011 and 2012 and will remain outstanding until 31 May 2017. On 17 December 2008, Mr Alves was granted options to acquire up to 568,732 ordinary shares in the Company at an exercise price of 100p per share, of which options vested over 195,503 shares. These options lapsed on 17 December 2016 (2015: nil). During 2016 no further options were granted (2015:nil) and none were exercised (2015: nil). There were no share grant expenses in 2016 (2015: nil).

By order of the Board

Caros Consulting Ltd.
Company Secretary
3 April 2017

Company registration number: 05886534

INDEPENDENT AUDITOR'S REPORT

TO THE MEMBERS OF VOLGA GAS PLC

We have audited the financial statements of Volga Gas plc for the year ended 31 December 2016 which comprise the Group Income Statement, the Group Statement of Comprehensive Income, the Group and Parent Company Balance Sheets, the Group and Parent Company Cash Flow Statements, the Group and Parent Company Statements of Changes in Equity and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards ("IFRSs") as adopted by the EU and, as regards the Parent Company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members, as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditor

As explained more fully in the Directors' Responsibilities Statement set out on page 20 the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate.

Opinion on financial statements

In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the Parent Company's affairs as at 31 December 2016 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with IFRSs as adopted by the EU;
- the Parent Company financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion the information given in the Strategic Report and the Directors' Report for the financial year is consistent with the financial statements.

Based solely on the work required to be undertaken in the course of the audit of the financial statements and from reading the Strategic Report and the Directors' Report:

- we have not identified material misstatements in those reports; and
- in our opinion, those reports have been prepared in accordance with the Companies Act 2006.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the Parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the Parent Company financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Adrian Wilcox (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
15 Canada Square
London
E14 5GL
3 April 2017

The accompanying notes on pages 30 to 47 are an integral part of these financial statements.

Group Income Statement

(presented in $US 000)

Year ended 31 December	Notes	2016	2015
Continuing operations			
Revenue	5	39,412	17,827
Cost of sales	6	(26,260)	(15,589)
Gross profit		**13,152**	**2,238**
Selling expenses	6(b)	(4,052)	(319)
Operating and administrative expenses	6	(4,526)	(3,377)
Exploration and evaluation expense		(265)	(635)
Write-off of development assets	6(c)	(1,798)	(2,950)
Operating profit/(loss)		**2,511**	**(5,043)**
Interest income	7	183	117
Interest expense		(3)	–
Other gains and losses – net	8	(763)	306
Profit/(loss) for the year before tax		**1,928**	**(4,620)**
Deferred income tax	9	(739)	559
Current income tax		(2)	(3)
Profit/(loss) for the year before non-controlling interests		**1,187**	**(4,064)**
Attributable to:			
The owners of the Parent Company		**1,187**	**(4,064)**
Basic profit/(loss) per share (in US Dollars)	10	0.0146	(0.050)
Diluted profit/(loss) per share (in US Dollars)	10	0.0146	(0.050)
Weighted average number of shares outstanding		*81,017,800*	*81,017,800*

The Company has elected to take the exemption under section 408 of the Companies Act 2006 to not present the Parent Company income statement. The loss for the Parent Company for the year was US$1,023,750 (2015: US$102,956,000)

Group Statement of Comprehensive Income

(presented in US$ 000)

Year ended 31 December	2016	2015
Profit/(loss) for the year attributable to equity shareholders of the Company	**1,187**	**(4,064)**
Other comprehensive income items that may be reclassified to profit and loss:		
Currency translation differences	10,495	(15,301)
Total comprehensive (expense) for the year	**11,682**	**(19,365)**
Attributable to:		
The owners of the Parent Company	**11,682**	**(19,365)**

Group Balance Sheet

(presented in US$ 000)

At 31 December	Notes	2016	2015
ASSETS			
Non-current assets			
Intangible assets	11	3,460	2,867
Property, plant and equipment	12	55,908	48,290
Other non-current assets		4	155
Deferred tax assets	9	1,536	1,098
Total non-current assets		**60,908**	**52,410**
Current assets			
Cash and cash equivalents	13	19,718	6,769
Inventories	14	981	1,067
Other receivables	15	3,007	1,449
Total current assets		**23,706**	**9,285**
Total assets		**84,614**	**61,695**
EQUITY AND LIABILITIES			
Equity			
Share capital	16	1,485	1,485
Share premium (net of issue costs)	16	–	–
Other reserves	17	(75,622)	(86,117)
Accumulated profits	18	141,224	140,037
Equity attributable to the shareholders of the Parent		**67,087**	**55,405**
Non-current liabilities			
Asset retirement obligation		175	146
Deferred tax liabilities	9	3,429	1,995
Bank loan	20	3,802	–
Total non-current liabilities		**7,406**	**2,141**
Current liabilities			
Bank loan	20	158	–
Trade and other payables	19	9,963	4,149
Total current liabilities		**10,121**	**4,149**
Total equity and liabilities		**84,614**	**61,695**

Approved by the Board of Directors on 3 April 2017 and signed on its behalf by

Andrey Zozulya
Chief Executive Officer

Group Cash Flow Statement

(presented in US$ 000)

Year ended 31 December	Notes	2016	2015
Profit/(loss) for the year before tax		**1,928**	**(4,620)**
Adjustments to profit/(loss) before tax:			
Depreciation		5,060	2,369
E & E expense		265	635
Write-off of development assets		1,749	2,950
Inventory write-off		536	–
Foreign exchange differences		892	(942)
Operating cash flow prior to working capital		**10,430**	**392**
Working capital changes			
(Increase)/decrease in trade and other receivables		(1,091)	(1,144)
Increase/(decrease) in payables		3,745	1,893
(Increase)/decrease in inventory		201	22
Cash flow from operations		**13,285**	**1,163**
Income tax paid		(2)	(3)
Net cash flow generated from operating activities		**13,283**	**1,160**
Cash flows from investing activities			
Expenditure on exploration and evaluation	11	(499)	(554)
Purchase of property, plant and equipment	12	(4,534)	(8,117)
Net cash used in investing activities		**(5,033)**	**(8,671)**
Cash flows from financing activities			
Bank loans drawn		3,947	–
Equity dividends paid		–	(1,013)
Net cash outflow from financing activities		**3,947**	**(1,013)**
Effect of exchange rate changes on cash and cash equivalents		752	(474)
Net increase/(decrease) in cash and cash equivalents		**12,949**	**(8,998)**
Cash and cash equivalents at beginning of the year	13	6,769	15,767
Cash and cash equivalents at end of the year	**13**	**19,718**	**6,769**

The accompanying notes on pages 30 to 47 are an integral part of these financial statements.

Company Balance Sheet

(presented in US$ 000)

Company registration number: 05886534

At 31 December	Notes	2016	2015
ASSETS			
Non-current assets			
Investments	21	50,475	50,475
Intercompany receivables	23	4,711	4,735
Total non-current assets		**55,186**	**55,210**
Current assets			
Cash and cash equivalents	13	3,415	4,529
Other receivables	15	11	22
Total current assets		**3,426**	**4,551**
Total assets		**58,612**	**59,761**
EQUITY AND LIABILITIES			
Equity			
Share capital	16	1,485	1,485
Share premium (net of issue costs)	16	–	–
Share grant expense reserve	17	5,233	5,233
Accumulated profit/(loss)	18	50,573	51,597
Total equity		**57,291**	**58,315**
Current liabilities			
Intercompany payables		1,321	1,357
Trade and other payables	19	–	89
Total current liabilities		**1,321**	**1,446**
Total equity and liabilities		**58,612**	**59,761**

Approved by the Board of Directors on 3 April 2017 and signed on its behalf by

Andrey Zozulya
Chief Executive Officer

Company Cash Flow Statement

(presented in US$ 000)

Year ended 31 December	Notes	2016	2015
(Loss) for the period before tax		**(1,024)**	**(102,956)**
Adjustments to loss before tax:			
Impairment expense		–	101,759
Operating cash flow prior to working capital		**(1,024)**	**(1,197)**
Working capital changes			
(Increase)/decrease in receivables		(68)	(118)
Increase/(decrease) in payables		(22)	71
Cash flow from operations		**(1,114)**	**(1,244)**
Income tax paid		–	
Net cash flow generated from operating activities		**(1,114)**	**(1,244)**
Cash flows from investing activities			
Decrease in intercompany receivables		–	–
Net cash from investing activities		**–**	**–**
Cash flows from financing activities			
Equity dividends paid		–	(1,013)
Net cash used in financing activities		**–**	**(1,013)**
Effect of exchange rate changes on cash and cash equivalents		–	–
Net (decrease)/increase in cash and cash equivalents		**(1,114)**	**(2,257)**
Cash and cash equivalents at beginning of the year	13	4,529	6,786
Cash and cash equivalents at end of the year	**13**	**3,415**	**4,529**

The accompanying notes on pages 30 to 47 are an integral part of these financial statements.

Group Statement of Changes in Shareholders' Equity

(presented in US$ 000)

	Notes	Share Capital	Share Premium	Currency Translation Reserves	Share Grant Reserve	Accumulated Profit/(Loss)	Total Equity
Opening equity at 1 January 2016		**1,485**	**–**	**(91,350)**	**5,233**	**140,037**	**55,405**
Profit for the year		–	–	–	–	1,187	1,187
Transactions with owners		–	–	–	–	–	–
Currency translation differences		–	–	10,495	–	–	10,495
Total comprehensive income		–	–	10,495	–	1,187	11,682
Closing equity at 31 December 2016		**1,485**	**–**	**(80,855)**	**5,233**	**141,224**	**67,087**
Opening equity at 1 January 2015		**1,485**	**–**	**(76,049)**	**5,233**	**145,114**	**75,783**
Loss for the year		–	–	–	–	(4,064)	(4,064)
Transactions with owners							
Equity dividends paid		–	–	–	–	(1,013)	(1,013)
Total transactions with owners		–	–	–	–	(1,013)	(1,013)
Currency translation differences		–	–	(15,301)	–	–	(15,301)
Total comprehensive income		–	–	(15,301)	–	(4,064)	(19,365)
Closing equity at 31 December 2015		**1,485**	**–**	**(91,350)**	**5,233**	**140,037**	**55,405**

Company Statement of Changes in Shareholders' Equity

(presented in US$ 000)

	Notes	Share Capital	Share Premium	Share Grant Reserve	Accumulated Profit/(loss)	Total Equity
Opening equity at 1 January 2016		**1,485**	**–**	**5,233**	**51,597**	**58,315**
Loss for the year		–	–	–	(1,024)	(1,024)
Closing equity at 31 December 2016		**1,485**	**–**	**5,233**	**50,573**	**57,291**
Opening equity at 1 January 2015		**1,485**	**–**	**5,233**	**155,566**	**162,284**
Loss for the year		–	–	–	(102,956)	(102,956)
Equity dividends paid		–	–	–	(1,013)	(1,013)
Closing equity at 31 December 2015		**1,485**	**–**	**5,233**	**51,597**	**58,315**

The accompanying notes on pages 30 to 47 are an integral part of these financial statements.

Notes to the IFRS Consolidated Financial Statements

For the year ended 31 December 2016

(presented in US$ 000)

1. General information

Volga Gas plc (the "Company" or "Volga") is a public limited company registered in England and Wales with registered number 5886534. The Company was incorporated on 25 July 2006. The principal activities of the Company and its subsidiaries (the "Group") are the acquisition, exploration and development of hydrocarbon assets and production of hydrocarbons in the Volga Region of the Russian Federation. Its registered office is 40 Dukes Place London EC3A 7NH. The Company's shares are admitted to trading on the AIM market of the London Stock Exchange.

These Group consolidated financial statements were authorised for issue by the Board of Directors on 3 April 2017.

2. Summary of significant accounting policies

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

2.1 Basis of preparation

Both the Parent Company financial statements and the Group financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRSs"), as adopted by the European Union ("EU"), International Financial Reporting Interpretations Committee ("IFRIC") interpretations, and the Companies Act 2006 applicable to companies reporting under IFRS. The consolidated financial statements have been prepared under the historical cost convention and in accordance with applicable accounting standards.

The preparation of financial statements in conformity with IFRSs requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in note 4.

No income statement is presented for Volga Gas plc as permitted by Section 408 of the Companies Act 2006.

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Strategic Report in pages 1 to 13; the financial position of the Group, its cash flows, liquidity position and borrowing facilities are described in the Financial Review on pages 10 and 11. In addition, the Group's objectives, policies and processes for measuring capital, financial risk, management objectives, details of financial instruments and exposure to credit and liquidity risks are described in note 3. Having reviewed the future cash flow forecasts of the Group, the directors have concluded that the Group will continue to have access to sufficient funds in order to meet its obligations as they fall due for at least the foreseeable future and thus continue to adopt the going concern basis of accounting in preparing the annual financial statements.

Disclosure of impact of new and future accounting standards

(a New and amended standards and interpretations:
There are no IFRSs or IFRIC interpretations that are effective for the first time for the financial year beginning on 1 January 2016 that have a material impact on the Group.

In accordance with the transitional provisions of IFRS 10, the Group reassessed the control conclusion for its investees at 1 January 2016. No modifications of previous conclusions about control regarding the Group's investees were required.

(b) Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Group.
The following Adopted IFRSs have been issued but have not been applied by the Group in these financial statements. Their adoption is not expected to have a material effect on the financial statements unless otherwise indicated:

- Amendments to IFRS 2: Classification and Measurement of Share-based Payment Transactions (effective date to be confirmed)
- Amendments to IFRS 4: Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts (effective date to be confirmed)
- IFRS 9 Financial Instruments (effective date 1 January 2018)
- IFRS 15 Revenue from Contract with Customers (effective date 1 January 2018)
- IFRS 16 Leases (effective date to be confirmed)
- Amendments to IAS 7: Disclosure Initiative (effective date 1 January 2017)
- Amendments to IAS 12: Recognition of Deferred Tax Assets for Unrealised Losses (effective date 1 January 2017)
- The Group is yet to assess the full impact of these new standards and amendments but does not expect them to have a material impact on the financial statements, with the main effect being the requirement for additional disclosures.

2.2 Consolidation

(a) Subsidiaries

The consolidated financial statements include the financial statements of the Company and its subsidiaries. Subsidiaries are entities controlled by the Group. The Group controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. In assessing control, the Group takes into consideration potential voting rights that are currently exercisable. The acquisition date is the date on which control is transferred to the acquirer. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. Losses applicable to the non-controlling interests in a subsidiary are allocated to the non-controlling interests even if doing so causes the non-controlling interests to have a deficit balance.

Investments in subsidiaries are accounted for at cost less impairment. Cost is adjusted to reflect changes in consideration arising from contingent consideration amendments. Cost also includes direct attributable costs of investment.

2. Summary of significant accounting policies continued

Intercompany transactions, balances and unrealised gains on transactions between Group companies are eliminated; unrealised losses are also eliminated unless the cost cannot be recovered.

The Company and its subsidiaries outside the Russian Federation maintain their financial statements in accordance with IFRSs as adopted by the EU. The Russian subsidiaries of the Group maintain their statutory accounting records in accordance with the Regulations on Accounting and Reporting of the Russian Federation. The consolidated financial statements are based on these statutory accounting records, appropriately adjusted and reclassified for fair presentation in accordance with International Financial Reporting Standards as adopted by the EU.

A list of the Company's subsidiaries is provided in Note 21.

2.3 Segment reporting

Segmental reporting follows the Group's internal reporting structure.

Operating segments are defined as components of the Group where separate financial information is available and reported regularly to the chief operating decision maker ("CODM"), which is determined to be the Board of Directors of the Company. The Board of Directors decides how to allocate resources and assesses operational and financial performance using the information provided.

The CODM receives monthly IFRS-based financial information for the Group and its development and production entities. There were two development and production entities during both 2015 and 2016. These entities both engage in upstream production, gathering and sale of hydrocarbons, with common operational management and control. Management has determined that the operations of these production and development entities are sufficiently homogenous (all are concerned with upstream oil and gas development and production activities) for these to be aggregated for the purpose of IFRS 8, "Operating Segments". Common economic drivers for the operations are international oil prices, export and Mineral Extraction Taxes and the costs of drilling, completing and operating wells and production facilities. The Group has other entities that engage as either head office or in a corporate capacity or as holding companies. Management has concluded that due to application of the aggregation criteria that separate financial information for segments is not required.

No geographic segmental information is presented as all of the Group's operating activities are based in the Russian Federation.

Management has determined therefore that the operations of the Group comprise one class of business, being oil and gas exploration, development and production and the Group operates in only one geographic area – the Russian Federation.

The Group's gas sales, representing a substantial proportion of revenues, are made to a single customer. Details are provided in Note 3.1 (b).

2.4 Foreign currency translation

(a) Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The consolidated financial statements are presented in US Dollars, which is the Company's functional and the Group's presentation currency.

The functional currency of the Group's subsidiaries that are incorporated in the Russian Federation is the Russian Rouble ("RUR"). It is the management's view that the RUR best reflects the financial results of its Cyprus subsidiaries because they are dependent on entities based in Russia that operate in an RUR environment in order to recover their investments. As a result, the functional currency of the subsidiaries continues to be the RUR.

(b) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

Foreign exchange gains and losses that relate to cash and cash equivalents, borrowings and other foreign exchange gains and losses are presented in the income statement within "Other gains and losses".

(c) Group companies

The results and financial position of all the Group entities (none of which has the currency of a hyper-inflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

(i) assets and liabilities for each balance sheet item presented are translated at the closing rate at the date of that balance sheet;
(ii) income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the rate on the dates of the transactions); and
(iii) all resulting exchange differences are recognised in other comprehensive income.

The major exchange rates used for the revaluation of the closing balance sheet at 31 December 2016 were:

- GBP 1.233: US$ (2015: 1.517)
- EUR 1.052: US$ (2015: 1.091)
- US$ 1:60.657: RUR (2015: 72.883)

Notes to the IFRS Consolidated Financial Statements continued

2. Summary of significant accounting policies continued

2.5 Oil and gas assets

The Company and its subsidiaries apply the successful efforts method of accounting for Exploration and Evaluation ("E&E") costs, in accordance with IFRS 6 "Exploration for and Evaluation of Mineral Resources". Costs are accumulated on a field-by-field basis.

Capital expenditure is recognised as property, plant and equipment or intangible assets in the financial statements according to the nature of the expenditure and the stage of development of the associated field, i.e. exploration, development, production.

(a) Exploration and evaluation assets

Costs directly associated with an exploration well, including certain geological and geophysical costs, and exploration and property leasehold acquisition costs, are capitalised as intangible assets until the determination of reserves is evaluated. If it is determined that a commercial discovery has not been achieved, these costs are charged to expense after the conclusion of appraisal activities. Exploration costs such as geological and geophysical that are not directly related to an exploration well are expensed as incurred.

Once commercial reserves are found, exploration and evaluation assets are tested for impairment and transferred to development assets. No depreciation or amortisation is charged during the exploration and evaluation phase.

(b) Development assets

Expenditure on the construction, installation or completion of infrastructure facilities such as platforms, pipelines and the drilling of development wells into commercially proved reserves, is capitalised within property, plant and equipment. When development is completed on a specific field, it is transferred to producing assets as part of property, plant and equipment. No depreciation or amortisation is charged during the development phase.

(c) Oil and gas production assets

Production assets are accumulated generally on a field-by-field basis and represent the cost of developing the commercial reserves discovered and bringing them into production together with E&E expenditures incurred in finding commercial reserves and transferred from the intangible E&E assets as described above.

The cost of production assets also includes the cost of acquisitions and purchases of such assets, directly attributable overheads, finance costs capitalised and the cost of recognising provisions for future restoration and decommissioning.
Where major and identifiable parts of the production assets have different useful lives, they are accounted for as separate items of property, plant and equipment. Costs of minor repairs and maintenance are expensed as incurred.

(d) Depreciation/amortisation

Oil and gas properties are depreciated or amortised using the unit-of-production method. Unit-of-production rates are based on proved reserves, which are oil, gas and other mineral reserves estimated to be recovered from existing facilities using current operating methods. Oil and gas volumes are considered produced once they have been measured through meters at custody transfer or sales transaction points at the outlet valve on the field storage tank.

(e) Impairment – exploration and evaluation assets

Exploration and evaluation assets are tested for impairment prior to reclassification to development tangible assets, or whenever facts and circumstances indicate that an impairment condition may exist. An impairment loss is recognised for the amount by which the exploration and evaluation assets' carrying amount exceeds their recoverable amount. The recoverable amount is the higher of the exploration and evaluation assets' fair value less costs to sell and their value in use. For the purposes of assessing impairment, the exploration and evaluation assets subject to testing are grouped with existing cash generating units of production fields that are located in the same geographical region.

(f) Impairment – proved oil and gas production properties

Proved oil and gas properties are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. The cash generating unit applied for impairment test purposes is generally the field, except that a number of field interests may be grouped together where the cash flows of each field are interdependent, for instance where surface infrastructure is used by one or more field in order to process production for sale.

(g) Decommissioning

Provision is made for the cost of decommissioning assets at the time when the obligation to decommission arises. Such provision represents the estimated discounted liability (the discount rate used currently being at 10% per annum) for costs which are expected to be incurred in removing production facilities and site restoration at the end of the producing life of each field. A corresponding item of property, plant and equipment is also created at an amount equal to the provision. This is subsequently depreciated as part of the capital costs of the production facilities. Any change in the present value of the estimated expenditure attributable to changes in the estimates of the cash flow or the current estimate of the discount rate used are reflected as an adjustment to the provision and the property, plant and equipment. The unwinding of the discount is recognised as a finance cost.

2.6 Other business and corporate assets

Property, plant and equipment not associated with exploration and production activities are carried at cost less accumulated depreciation. These assets are also evaluated for impairment when circumstances dictate.

2. Summary of significant accounting policies continued

Land is not depreciated. Depreciation of other assets is calculated on a straight-line basis as follows:

Machinery and equipment	6–10 years
Office equipment in excess of US$5,000	3–4 years
Vehicles and other	2–7 years

Depreciation methods, useful lives and residual values are reviewed at each balance sheet date.

2.7 Financial assets

The Group classifies its financial assets in the following categories:

(a) Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss are financial assets held for trading. This category comprises derivatives unless they are effective hedging instruments. The Group had no financial assets in this class as at 31 December 2016 or 31 December 2015.

(b) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. This category comprises trade and other receivables, term bank deposits and cash and cash equivalents in balance sheet.

2.8 Inventories

Crude oil inventories are stated at the lower of cost of production and net realisable value. Materials and supplies inventories are recorded at average cost and are carried at amounts which do not exceed the expected recoverable amount from use in the normal course of business. Cost comprises direct materials and, where applicable, direct labour plus attributable overheads based on a normal level of activity and other costs associated in bringing inventories to their present location and condition.

2.9 Trade and other receivables

Trade and other receivables are recorded initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate.

2.10 Cash and cash equivalents

Cash and cash equivalents include cash in hand, and deposits held at call with banks.

2.11 Share capital

Ordinary shares are classified as equity.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

2.12 Trade payables

Trade payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

2.13 Current and deferred income tax

The tax expense for the period comprises current and deferred tax. Tax is recognised in the income statement, except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case the tax is also recognised in other comprehensive income or directly in equity, respectively.

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the end of the reporting period in the countries where the Company's subsidiaries operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax is recognised, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the end of the reporting period and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes' assets and liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

Notes to the IFRS Consolidated Financial Statements continued

2. Summary of significant accounting policies continued

2.14 Employee benefits

(a) Share-based compensation

The fair value of the employee services received in exchange for the grant of the options is recognised as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted, excluding the impact of any non-market vesting conditions (for example, profitability and sales growth targets). Non-market vesting conditions are included in assumptions about the number of options that are expected to vest. The option plan currently in place for certain of the directors is an equity-settled share option plan.

The Company measures the equity instruments granted to employees at the fair value at grant date. The fair value of fully-vested shares is expensed immediately. The fair value of shares with vesting requirements is estimated using the Black-Scholes option pricing model. This value is recognised as an expense over the vesting period on a straight-line basis. The estimate is revised, as necessary, if subsequent information indicates that the number of equity instruments expected to vest differs from previous estimates.

(b) Social obligations

Wages, salaries, contributions to the Russian Federation state pension and social insurance funds, paid annual leave, sick leave and bonuses are accrued in the year in which the associated services are rendered by the employees of the Group.

2.15 Revenue recognition

Revenue comprises the fair value of the consideration received or receivable for the sale of oil and gas in the ordinary course of the Group's activities. Revenue is shown net of value added tax, returns, rebates and discounts and after eliminating sales within the Group. Revenue from the sale of oil or gas is recognised when the oil/gas is delivered to customers and title has transferred. In 2016 and 2015, the Group's revenue related to sales of crude oil and condensate collected directly by – or delivered to – customers and gas sales made at the entry to the gas distribution system.

2.16 Prepayments

Prepayments are carried at cost less provision for impairment. A prepayment is classified as non-current when the goods or services relating to the prepayment are expected to be obtained after one year, or when the prepayment relates to an asset which will itself be classified as non-current upon initial recognition. Prepayments to acquire assets are transferred to the carrying amount of the asset once the Group has obtained control of the asset and it is probable that future economic benefits associated with the asset will flow to the Group. Other prepayments are written-off to profit or loss when the goods or services relating to the prepayments are received. If there is an indication that the assets, goods or services relating to a prepayment will not be received, the carrying value of the prepayment is written-down accordingly and a corresponding impairment loss is recognised in profit or loss for the year.

2.17 Provisions

Provisions for environmental restoration, restructuring costs and legal claims are recognised when: the Group has a present legal or constructive obligation as a result of past events; it is probable that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Restructuring provisions comprise lease termination penalties and employee termination payments. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as interest expense.

3. Financial risk management

3.1 Financial risk factors

The Group's activities expose it to a variety of financial risks: market risk (including foreign exchange risk, price risk, and cash flow interest rate risk), credit risk, and liquidity risk. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance.

(a) Market risk

(i) Foreign exchange risk

The Group is exposed to foreign exchange risk arising from currency exposures, primarily with respect to the RUR. Foreign exchange risk arises from future commercial transactions, recognised assets and liabilities.

At 31 December 2016, if the US Dollar had weakened/strengthened by 5% against the RUR with all other variables held constant, post-tax profit for the year would have been US$476,000 (2015: US$56,000) higher/lower, mainly as a result of foreign exchange gains/losses on translation of RUR-denominated trade payables and financial assets. At 31 December 2016, if the US Dollar had weakened/strengthened by 5% against the Euro ("EUR") with all other variables held constant, post-tax profit for the year would have been US$1,000 (2015: US$1,000) higher/lower, mainly as a result of foreign exchange gains/losses on translation of EUR-denominated interest charges and financial liabilities. At 31 December 2016, if the US Dollar had weakened/strengthened by 5% against the Pound Sterling ("GBP") with all other variables held constant, post-tax profit for the year would have been US$7,000 (2015: US$3,000) higher/lower, mainly as a result of foreign exchange gains/losses on translation of GBP-denominated trade payables and financial assets.

3. Financial risk management continued

If the US Dollar had weakened/strengthened by 5% against the RUR with all other variables held constant, shareholders equity would have been US$2.9 million (2015: US$2.3 million) higher/lower, as a result of translation of RUR-denominated assets. The sensitivity of shareholders equity to changes in the exchange rates between US Dollar against GBP or EUR is immaterial.

The following table shows the currency structure of financial assets and liabilities:

At 31 December 2016	Rubles US$ 000	US Dollars US$ 000	Euros US$ 000	Sterling US$ 000	Total US$ 000
Financial assets					
Cash and cash equivalents	6,747	12,810	13	148	19,718
Total financial assets	**6,747**	**12,810**	**13**	**148**	**19,718**
Financial liabilities (before provision for UK taxes)	11,389	–	–	–	11,389

At 31 December 2015	Rubles US$ 000	US Dollars US$ 000	Euros US$ 000	Sterling US$ 000	Total US$ 000
Financial assets					
Cash and cash equivalents	1,089	5,622	14	44	6,769
Total financial assets	**1,089**	**5,622**	**14**	**44**	**6,769**
Financial liabilities (before provision for UK taxes)	3,217	–	–	–	3,217

(ii) Price risk

The Group is not exposed to price risk as it does not hold financial instruments of which the fair values or future cash flows will be affected by changes in market prices. The Group is not directly exposed to the levels of international marker prices of crude oil or oil products, although these clearly influence the prices at which it sells its oil and condensate. Mineral Extraction Taxes ("MET") are calculated by reference to Urals' oil prices and are therefore directly influenced by this. Taking into account the marginal rates of export taxes and MET, management estimates that if international oil prices had been US$5 per barrel higher or lower and all other variables been unchanged, the Group's profit before tax would have been US$2.7 million higher or lower (2015: $1.4 million).

(iii) Cash flow and fair value interest rate risk

As the Group currently has no significant interest-bearing assets and liabilities, the Group's income and operating cash flows are substantially independent of changes in market interest rates.

(b) Credit risk

The Group's maximum credit risk exposure is the fair value of each class of assets, presented in note 3.1(a)(i) of US$19,718,000 and US$6,769,000 at 31 December 2016 and 2015 respectively.

The Group's principal financial asset is cash and credit risk arises from cash and cash equivalents and deposits with banks and financial institutions. It is the Group's policy to monitor the financial standing of these assets on an ongoing basis. Bank balances are held with reputable and established financial institutions.

The Group's oil and condensate sales are normally undertaken on a prepaid basis and accordingly the Group has no trade receivables and consequently no credit risk associated with the related trade receivables. Gas sales accounting for 35.6% of Group revenues in 2016 (2015: 38.4%) were made to OOO Trans Nafta. As at 31 December 2016 there were trade receivables of US$2.0 million (31 December 2015: US$1.0 million) relating to gas sales. As at 31 December 2016 there was no provision for bad debts (2015: nil).

Rating of financial institution (Fitch)		31 December 2016 US$ 000	31 December 2015 US$ 000
Barclays Bank	A	3,627	4,794
ZAO Raiffeisenbank	BBB-	15,840	1,579
Unicreditbank	BBB-	214	202
Other		37	194
Total bank balance		**19,718**	**6,769**

Notes to the IFRS Consolidated Financial Statements continued

3. Financial risk management continued

(c) Liquidity risk

Cash flow forecasting is performed by Group finance. Group finance monitors rolling forecasts of the Group's liquidity requirements to ensure it has sufficient cash to meet operational needs. The Group believes it has sufficient liquidity headroom to fund its currently planned exploration and development activities.

The Group expects to fund its capital investments, as well as its administrative and operating expenses, through 2017 using a combination of cash generated from its oil and gas production activities, existing working capital and, when appropriate, medium-term bank borrowings. If the Group is unsuccessful in generating enough liquidity to fund its expenditures, the Group's ability to execute its long-term growth strategy could be significantly affected. The Group may need to raise additional equity or debt finance as appropriate to fund investments beyond its current commitments.

(d) Capital risk management

The Group manages capital to ensure that it is able to continue as a going concern whilst maximising the return to shareholders. The Group is not subject to any externally-imposed capital requirements. The Board regularly monitors the future capital requirements of the Group, particularly in respect of its ongoing development programme. Management expects that the cash generated by the operating fields will be sufficient to sustain the Group's operations and future capital investment for the foreseeable future. During December 2016, one of the Group's operating subsidiaries entered into a loan agreement of RUR 240 million to fund its LPG project (see note 20). This loan, which has a three-year amortising term, benefits from an interest rate subsidy provided by the regional Government. Further short-term debt facilities may be arranged to provide financial headroom for future development activities.

3.2 Fair value estimation

Effective 1 January 2009, the Group adopted the amendment to IFRS 7 for financial instruments that are measured in the balance sheet at fair value. This requires disclosure of fair value measurements by Level of the following fair value measurement hierarchy:

- Quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1).
- Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) (Level 2).
- Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) (Level 3).

The Group has no financial assets and liabilities that are required to be measured at fair value.

4. Critical accounting estimates and judgements

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

a) Carrying value of fixed assets, intangible assets and impairment

Fixed assets and intangible assets are assessed for impairment when events and circumstances indicate that an impairment condition may exist. The carrying value of fixed assets and intangible assets are evaluated by reference to their value in use and primarily looks to the present value of management's best estimate of the cash flows expected to be generated from the asset. In identifying cash flows management firstly determine the cash generating unit or group of assets that give rise to the cash flows.

The cash generating unit ("CGU") is the lowest level of asset at which independent cash flows can be generated. For this purpose the directors consider the Group to have two CGUs: the VM and Dobrinskoye fields and the Dobrinskoye gas processing plant are treated as a single CGU, and the Uzen oil field is a separate CGU.

The estimation of forecast cash flows involves the application of a number of significant judgements and estimates to a number of variables including production volumes, commodity prices, operating costs, capital investment, hydrocarbon reserves estimates and discount rates. Key assumptions and estimates in the impairment models relate to:

- International oil prices: flat real prices reflecting the actual levels pertaining in the period between 31 December 2016 and 1 March 2017 – Urals oil price of US$53 per barrel. No forward price escalation is assumed.
- Selling prices for oil, condensate and LPG that reflect international oil prices, less export taxes at the current applicable official rates and a price differential of $5 per barrel to reflect transportation costs.
- Gas sales price of RUR 3,898 per mcm excluding VAT.
- Production profiles based on remaining reserves in the Proved category and approved field development plans. In the Group's base case, however, LPG revenues are not assumed although, as indicated below, the capital expenditures for this project are included.
- Capital expenditures required to deliver the above production profiles and to maintain the production assets throughout the field life. Total development capital expenditure assumed is US$18 million with future maintenance capital expenditure of up to US$1 million per annum. This includes US$5 million for the LPG extraction project.
- Cost assumptions are based on current experience and expectations and are broadly in line with unit costs experienced in the year ended 31 December 2016. The projections assume that the current gas sweetening process is maintained. If Redox-based sweetening is successfully implemented, however, the Group expects to realise significant cost savings.
- Export and mineral extraction taxes reflect rates set by current legislation.
- The model reflects real terms cash flows with no inflationary escalation of revenues or costs.
- A real discount rate of 12% per annum is utilised in the models.
- An exchange rate of RUR60 to US$1.00 is assumed.

4. Critical accounting estimates and judgements continued

In addition to the base case a number of sensitivity cases have been carried out: varying oil and gas prices by 10%, varying operating expenditure by 10%, varying capital expenditure by 20% and using a 15% real discount rate.

As at 31 December 2016, the Group's impairment testing of the property, plant and equipment related to each CGU indicated that no impairment was required. In addition, the sensitivities described above yielded net present values in excess of carrying value for each CGU. Furthermore, two initiatives planned by the Group in 2017: a switch to Redox-based gas sweetening and construction of an LPG extraction module, are each expected to result in material increases in the value in use of the relevant CGU.

(b) Estimation of oil and gas reserves

Estimates of oil and gas reserves are inherently subjective and subject to periodic revision. In addition, the results of drilling and other exploration or development activity will often provide additional information regarding the Group's reserve base that may result in increases or decreases to reserve volumes. Such revisions to reserves can be significant and are not predictable with any degree of certainty. Management considers the estimation of reserves to represent a significant judgement in the context of the financial statements as reserve volumes are used as the basis for assessing the useful life of oil and gas assets, applying depreciation to oil and gas assets and in assessing the carrying value of oil and gas assets. Decreases in reserve estimates can lead to significant impairment of oil and gas assets where revisions (positive or negative) can have a significant effect on depreciation rates from period to period. Management have considered the sensitivity of this key assumption and in order for an impairment issue to present itself to the Group, reserve estimates would need to reduce by more than 12% below the level of recently revised proved reserves as at 31 December 2016. Decrease of proved reserves by 10% would result in 10% increase of depreciation & amortisation.

An independent assessment of the reserves and net present value of future net revenues ("NPV") attributable to the Group's fields, Dobrinskoye, Vostochny Makarovskoye, Sobolevskoye and Uzenskoye, as at 31 December 2016, was prepared in accordance with reserve definitions set by the Oil and Gas Reserves Committee of the Society of Petroleum Engineers ("SPE"). The latest assessment resulted in revisions that increased the level of proved and probable reserves as at 31 December 2016 by 2.4% and decreased the level of proved reserves by 10.8%.

5. Revenue

Year ended 31 December	2016 US$ 000	2015 US$ 000
Oil	7,523	4,081
Condensate	17,857	6,875
Gas	14,032	6,871
Total revenues	**39,412**	**17,827**

All revenue is generated from the sale of oil and gas in the ordinary course of the Group's activities.

6. Cost of sales and administrative expenses – Group

Cost of sales and administrative expenses are as follows:

Year ended 31 December	2016 US$ 000	2015 US$ 000
Production expenses	10,968	7,367
Mineral extraction taxes	10,255	5,877
Depletion, depreciation and amortisation	5,037	2,345
Cost of sales	**26,260**	**15,589**

Notes to the IFRS Consolidated Financial Statements continued

6. Cost of sales and administrative expenses – Group continued

Total expenses are analysed as follows:

Year ended 31 December		2016 US$ 000	2015 US$ 000
Export sales-related expenses	(b)	4,052	319
Field operating expenses		9,367	6,016
Mineral extraction tax		10,255	5,876
Depreciation & amortisation	(a)	5,059	2,369
Exploration & evaluation		265	635
Write-off of development assets	(c)	1,798	2,950
Inventory write-off	(d)	529	–
Salaries & staff benefits	(e)	3,177	2,471
Directors' emoluments and other benefits	(f)	645	765
Audit fees	(g)	314	203
Taxes other than payroll and mineral extraction		38	44
Legal & consulting		291	480
Other		1,110	742
Total		**36,900**	**22,870**

(a) Depreciation: substantially, all depreciation relates to oil and gas assets and is included within cost of sales.
(b) Selling expense: comprise export taxes and costs associated with delivering gas condensate sales to export customers.
(c) Write-off of development assets: in the year ended 31 December 2016, the principal source of the write-off of development assets was the US$1.650 million compensation payable to Schlumberger for logging tools stuck in the Uzen #4 well sidetrack. The write-off incurred in the year ended 31 December 2015 was related mainly to the Sobolevskoye field.
(d) Inventory write-off: in the year ended 31 December 2016, certain obsolete and unused items of production equipment were transferred from producing assets to inventory and then written-off (2015: nil).
(e) Staff and salaries: the average monthly number of employees (including executive directors) employed by the Group was:

Year ended 31 December	2016	2015
Exploration and production	163	149
Administration and support	42	42
Total	**205**	**191**

Their aggregate remuneration (excluding executive directors) comprised:

Year ended 31 December	2016 US$ 000	2015 US$ 000
Wages and salaries	2,476	1,859
Payroll taxes & social contribution	656	577
Staff benefits	45	35
Total	**3,177**	**2,471**

The average monthly number of employees employed by the Company was:

Year ended 31 December	2016	2015
Chief Executive and Chief Financial Officers	1.4	2
Non-Executive Directors	5	5
	6.4	6.4

Only directors are employed by the Company.

6. Cost of sales and administrative expenses – Group continued

(f) Directors' emoluments and other benefits:

	Salary US$ 000	Bonus US$ 000	Compensation for loss of office US$ 000	Fees US$ 000	Aggregate remuneration for the year 31 December 2016 US$ 000	Aggregate remuneration for the year 31 December 2015 US$ 000
Executive directors						
M. Ivanov	–	–	–	120	**120**	235
A. Zozulya	194	65	–	–	**259**	130
A. Alves (resigned 10 June 2016)	117	–	39	10	**166**	300
Non-executive directors						
M. Calvey	–	–	–	–	**–**	–
R. Freeman	–	–	–	50	**50**	50
A. Kalinin	–	–	–	–	**–**	–
V. Koshcheev	–	–	–	–	**–**	–
S. Ogden	–	–	–	50	**50**	50

Director's emoluments comprised salaries of US$311,000 (2015: US$595,000), bonuses US$65,000 (2015: nil), non-executive directors' fees of US$230,000 (2015: US$170,000) and compensation for loss of office to Chief Financial Officer of US$ 39,000 (2015: nil).

There were no share grant expenses in 2016 (2015: nil).

(g) Audit Fees – Group and Company: Disclosure of the fees paid to the Company's auditor and its associates is given in Note 22.

7. Finance income – Group

Finance income comprises interest earned during the period on cash balances with different banks (note 13).

8. Other gains and losses – Group

Year ended 31 December	2016 US$ 000	2015 US$ 000
Foreign exchange (loss)/gain	(892)	942
Recovery of/(loss from) unauthorised bank transfers	37	(727)
Other gains	92	91
Total other (losses)/gains	**(763)**	**306**

9. Current and deferred income tax – Group

Year ended 31 December	2016 US$ 000	2015 US$ 000
Current tax:		
Current income tax	(2)	(3)
Adjustments to tax charge in respect of prior periods	–	–
Total current tax	**(2)**	**(3)**
Deferred tax:		
Adjustments to tax charge in respect of prior periods		–
Origination and reversal of timing differences	(739)	559
Total deferred tax	**(739)**	**559**
Total tax (charge)/credit	**(741)**	**556**

Notes to the IFRS Consolidated Financial Statements continued

9. Current and deferred income tax – Group continued

The tax charge in the Group income statement differs from the theoretical amount that would arise using the weighted average tax rate applicable to profits of the consolidated entities as follows:

Year ended 31 December	2016 US$ 000	2015 US$ 000
Profit/(loss) before income tax	1,928	(4,620)
Tax calculated at domestic tax rates applicable to (profits)/losses in the respective countries	(386)	1,038
Tax effect of items which are not deductible or assessable for taxation purposes:		
Non-deductible expenses	(132)	(122)
Tax losses for which no deferred tax asset was recognised	(223)	(328)
Other tax adjustments	–	(32)
Income tax (charge)/credit	**(741)**	**556**

The weighted average applicable tax rate was 20.0% (2015: 22.5%).

Deferred taxation is attributable to the temporary differences that exist between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes. The tax effects of temporary differences that give rise to deferred taxation are presented below:

	31 December 2016	Differences recognition and reversal	31 December 2015	Differences recognition and reversal	31 December 2014
Tax effects of taxable temporary differences:					
Property, plant & equipment	(4,228)	(465)	(3,763)	1,620	(5,383)
Total	**(4,228)**	**(465)**	**(3,763)**	**1,620**	**(5,383)**
Tax effect of deductible temporary differences:					300
Tax losses carry forward	1,713	(1,153)	2,866	(745)	3,611
Trade and other payables	623	623	–	–	–
Total	**2,336**	**(530)**	**2,866**	**(745)**	**3,611**
Net tax effect of temporary differences	**(1,892)**	**(995)**	**(897)**	**875**	**(1,772)**

Deferred income tax assets are recognised for tax loss carry forwards to the extent that the realisation of the related tax benefit through the future taxable profits is probable. As at 31 December 2016, deferred income tax assets of US$1,536,000 (2015: US$1,098,000) and deferred tax liabilities of US$3,429,000 (2015: US$1,995,000) have been recognised. Tax losses in respect of Cyprus and the UK do not expire. The Group has not recognised a deferred tax asset of US$1,210,070 in respect of tax losses and other short-term timing differences in the UK and Cyprus (2015: US$ 1,175,592).

10. Basic and diluted profit per share – Group

Profit per share is calculated by dividing the profit attributable to equity holders of the Company by the weighted average number of ordinary and diluted shares in issue during the year.

Year ended 31 December	2016	2015
Net profit/(loss) attributable to equity shareholders (US$ per share)	0.0146	(0.050)
Diluted net profit attributable to equity shareholders	0.0146	(0.050)
Net profit/(loss) attributable to equity shareholders (US$ 000)	1,187	(4,064)
Basic weighted number of shares	81,017,800	81,017,800
Dilutive share options outstanding	–	–
Diluted number of shares	81,017,800	81,017,800

As at 31 December 2016 all outstanding options in amount of 1,137,464 shares (2015: 1,332,967) were excluded from the weighted average diluted number of shares calculation because their effect would have been anti-dilutive. The average market value of the Company's shares for the purpose of calculating the dilutive effect of share options was based on quoted market prices for the year during which the options were outstanding.

11. Intangible assets – Group

Intangible assets represent exploration and evaluation assets such as licences, studies and exploratory drilling, which are stated at historical cost, less any impairment charges or write-offs.

	Work in progress: exploration and evaluation	Exploration and evaluation	Total
At 1 January 2016	117	2,750	2,867
Additions	–	254	254
Write-offs and impairments	–	(240)	(240)
Transfers	–	–	–
At 31 December 2016	**117**	**2,764**	**2,881**
Exchange adjustments	23	556	579
At 31 December 2016	**140**	**3,320**	**3,460**

	Work in progress: exploration and evaluation	Exploration and evaluation	Total
At 1 January 2015	151	3,595	3,746
Additions	–	606	606
Write-offs and impairments	–	(635)	(635)
Transfers	–	–	–
At 31 December 2015	**151**	**3,566**	**3,717**
Exchange adjustments	(34)	(816)	(850)
At 31 December 2015	**117**	**2,750**	**2,867**

12. Property, plant and equipment – Group

Movements in property, plant and equipment, for the year ended 31 December 2016 are as follows:

	Development assets US$ 000	Land & buildings US$ 000	Producing assets US$ 000	Other US$ 000	Total US$ 000
At 1 January 2016	1,137	650	55,879	498	58,164
Additions	2,341	–	1,564	–	3,905
Write-offs and impairments	(57)	–	(917)	–	(974)
Transfers	(294)	–	294	–	–
Exchange adjustments	432	130	11,359	100	12,021
At 31 December 2016	**3,559**	**780**	**68,179**	**598**	**73,116**
Accumulated depreciation					
At 1 January 2016	–	–	(9,399)	(475)	(9,874)
Adjustment for assets written-off	–	–	195	15	210
Depreciation	–	–	(5,028)	(32)	(5,060)
Exchange adjustments	–	–	(2,387)	(97)	(2,484)
At 31 December 2016	–	–	(16,619)	(589)	(17,208)
Net book value at 31 December 2016	**3,559**	**780**	**51,560**	**9**	**55,908**

Notes to the IFRS Consolidated Financial Statements continued

12. Property, plant and equipment – Group continued

Movements in property, plant and equipment, for the year ended 31 December 2015 are as follows:

	Development assets US$ 000	Land & buildings US$ 000	Producing assets US$ 000	Other US$ 000	Total US$ 000
At 1 January 2015	8,523	842	57,944	701	68,010
Additions	378	–	9,422	–	9,800
Write-offs and impairments	(673)	–	(2,338)	(51)	(3,062)
Transfers	(6,181)	–	6,181	–	–
Exchange adjustments	(910)	(192)	(15,330)	(152)	(16,584)
At 31 December 2015	**1,137**	**650**	**55,879**	**498**	**58,164**
Accumulated depreciation					
At 1 January 2015	–	–	(9,589)	(599)	(10,188)
Adjustment for assets written-off	–	–	10	51	61
Depreciation	–	–	(2,384)	(66)	(2,450)
Exchange adjustments	–	–	2,564	139	2,703
At 31 December 2015	–	–	(9,399)	(475)	(9,874)
Net book value at 31 December 2015	**1,137**	**650**	**46,480**	**23**	**48,290**

13. Cash and cash equivalents – Group and Company

	Group		Company	
	2016 US$ 000	2015 US$ 000	2016 US$ 000	2015 US$ 000
Cash at bank and on hand	19,718	6,769	3,415	4,529
Total cash and cash equivalents	**19,718**	**6,769**	**3,415**	**4,529**

An analysis of Group cash and cash equivalents by bank and currency is presented in the table below:

		Group		Company	
At 31 December Bank	Currency	2016 US$ 000	2015 US$ 000	2016 US$ 000	2015 US$ 000
United Kingdom					
Barclays Bank PLC	USD	3,479	4,750	3,267	4,485
Barclays Bank PLC	GBP	148	44	148	44
Russian Federation					
Unicreditbank	RUR	82	70	–	–
Unicreditbank	USD	131	195	–	–
ZAO Raiffeisenbank	RUR	6,628	825	–	–
ZAO Raiffeisenbank	USD	9,200	740	–	–
ZAO Raiffeisenbank	EUR	13	132	–	–
Other banks and cash on hand	RUR	37	13	–	–
Total cash and cash equivalents		**19,718**	**6,769**	**3,415**	**4,529**

14. Inventories – Group

At 31 December	2016 US$ 000	2015 US$ 000
Production consumables and spare parts	796	704
Crude oil inventory	185	363
Total inventories	**981**	**1,067**

15. Other receivables – Group

At 31 December	Group 2016 US$ 000	Group 2015 US$ 000	Company 2016 US$ 000	Company 2015 US$ 000
VAT receivable	154	80	11	22
Prepayments	725	298	–	–
Trade receivables	2,067	987	–	–
Other accounts receivable	61	84	–	–
Total other receivables	**3,007**	**1,449**	**11**	**22**

Prepayments are to contractors and relate to initial advances made in respect of drilling, construction and other projects. Trade receivables relate to sales of gas and condensate. The receivables were settled on schedule subsequent to the balance sheet date.

16. Share capital and share premium – Group

The following summarises the movement in the share capital and share premium of the Company for the years ended 2014 and 2015.

	Number of shares	Share capital US$ 000	Share premium US$ 000
At 1 January 2015	81,017,800	1,485	–
Issues of shares	–	–	–
At 31 December 2015	**81,017,800**	**1,485**	**–**
At 1 January 2016	81,017,800	1,485	–
Issues of shares	–	–	–
At 31 December 2016	**81,017,800**	**1,485**	**–**

The total number of authorised ordinary shares is 330,720,100 (2015: 330,720,100) with a par value of £ 0.01 per share (2015: £ 0.01 per share).

Share-based compensation

Share options and other share-based awards have been granted to certain directors.
On 15 July 2008 the Group announced a new Executive Share Option Plan ("ESOP"). During 2008, the Company granted options to acquire 1,137,464 ordinary shares to Mikhail Ivanov. The options may be exercised at a price of 405p per share, vested in equal portions on May 2010, 2011 and 2012 and will remain outstanding until May 2017. In January 2009, the Company granted share options to Tony Alves under the ESOP, of which 195,503 share options were vested, had an exercise price of £1.00 and lapsed on 17 December 2016. As at 31 December 2016 the total number of options outstanding were 1,137,464 (2015: 1,332,967) with a weighted average exercise price of 405p per share (2015: 360.2p per share). During this two-year period there were no options forfeited, exercised or granted.

There were no share grant expenses in 2016 (2015: nil).

17. Other reserves – Group

At 31 December	2016 US$ 000	2015 US$ 000
Currency translation reserves	(80,855)	(91,350)
Share grant reserve	5,233	5,233
Total other reserves	**(75,622)**	**(86,117)**

Currency translation reserve

The currency translation reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign operations.

Notes to the IFRS Consolidated Financial Statements continued

18. Accumulated profit/(loss) – Group and Company

At 31 December	Group 2016 US$ 000	Group 2015 US$ 000	Company 2016 US$ 000	Company 2015 US$ 000
Retained profits	140,037	145,114	51,597	155,566
Profit/(loss) for the year	1,187	(4,064)	(1,024)	(102,956)
Equity dividends paid	–	(1,013)	–	(1,013)
Accumulated profit/(loss)	**141,224**	**140,037**	**50,573**	**51,597**

Dividends
After the balance sheet date dividends of US$0.062 per ordinary share were proposed by the Board of Directors (2015: nil). The dividends are not recognised as liabilities and there are no tax consequences.

19. Trade and other payables

At 31 December	Group 2016 US$ 000	Group 2015 US$ 000	Company 2016 US$ 000	Company 2015 US$ 000
Trade payables	4,861	2,467	–	89
Taxes other than profit tax	2,266	750	–	–
Customer advances	2,836	932	–	–
Total	**9,963**	**4,149**	**–**	**89**

The maturity of the Group's and the Company's financial liabilities are all between zero to three months. Customer advances are prepayments for oil and condensate sales, normally one month in advance of delivery.

20. Bank loan

At 31 December	2016 US$ 000	2015 US$ 000
Non-current liabilities		
Secured bank loan	3,802	–
Current liabilities		
Current portion of secured bank loan	158	–
Total bank loan	**3,960**	**–**

In December 2016, the Group received a bank loan of total amount of RUR 240 million (US$3.96 million), which will be utilised to fund purchases of equipment for the LPG project and should be fully repaid by 2019 (repayments in 2017: US$0.16 million; 2018: US$1.9 million; 2019: US$1.9 million). Interest is charged at a fixed rate of 11.45% per annum. The bank loan as at 31 December 2016 has been secured by charges over the shares of the Group's Russian operating subsidiaries as detailed in Note 21 below.

21. Investments – Company

Investments in subsidiaries, comprising ordinary share capital, are accounted for at cost. The Company's subsidiaries are as follows:

Name	Jurisdiction	Nature of operations	% Owned	From
Woodhurst Holdings Ltd	Cyprus	Intermediate holding company	100%	October 2005
Pre-Caspian Gas Company	Russia	Oil & gas exploration and production	100%	May 2006
Gazneftеservice	Russia	Oil & gas exploration and production	100%	September 2006
Shropak Investments Ltd	Cyprus	Dormant	100%	June 2007
Volga Gas (Cyprus) Ltd	Cyprus	Intermediate holding company	100%	August 2007
Geopotential	Russia	Special purpose entity	100%	October 2008
Volga Gas Finance Ltd	UK	Intermediate holding company	100%	March 2010

To avoid certain legal restrictions on land ownership, in October 2008 Pre-Caspian Gas Company acquired a 99% shareholding in ZAO Gazservice. Subsequently, Pre-Caspian Gas Company sold an unimproved plot of land to ZAO Gazservice at cost basis. During the year ended 31 December 2016, Gazservice was merged into Geopotential.

The registered office addresses of the subsidiaries are as follows:

Name	Registered office address
Woodhurst Holdings Ltd Shropak Investments Ltd Volga Gas (Cyprus) Ltd	All at: Archbishop Makarios Avenue, Capital Centre, 9th Floor, 1505 Nicosia, Cyprus
Pre-Caspian Gas Company Geopotential	both at: 65, Ulitsa Kiseleva, Saratov, 410012, Russia
Gazneftеservice	24. Ulista Pushkina, Zhirnovsk, Volgagrad Region, 403790, Russia
Volga Gas Finance Ltd	40 Dukes Place, London EC3A 7NH, UK

	31 December 2015 US$ 000	Additions US$ 000	Impairment US$ 000	31 December 2016 US$ 000
Investments in Woodhurst Holdings	48,924	–		48,924
Investments in Volga Gas (Cyprus)	1,551	–	–	1,551
Total investments	**50,475**	**–**		**50,475**

The Company funds its activities in the Russian Federation via Woodhurst Holdings ("Woodhurst"), the Company's Cyprus-registered subsidiary. As at 31 December 2016 no impairment was considered necessary.

22. Audit fees – Group and Company

During the year the Group (including its overseas subsidiaries) obtained the following services from the Company's auditor and associates:

Year ended 31 December	2016 US$ 000	2015 US$ 000
Fees payable to Company's auditor for the audit of Parent Company and consolidated financial statements	292	183
Audit of the Company's subsidiaries pursuant to legislation	22	52
Other services pursuant to legislation	3	3
Total	**317**	**238**

Notes to the IFRS Consolidated Financial Statements continued

23. Related Party Transactions – Group and Company

The Group is controlled by Baring Vostok Private Equity Funds III and IV (registered office address for both companies: 1 Royal Plaza, Royal Avenue, St Peter Port, Guernsey, GY1 2HL), which respectively own 48.9% and 9.76% (in aggregate 58.66%) of the Company's shares. The Baring Vostok Private Equity Funds exercise their control through a number of nominee holding companies. The remaining 41.34% of the shares are widely held.

The following transactions concerning purchases of goods and services were carried out by the Group with related parties:

			Year ended 31 December	
Related party	Relationship	Nature of transactions	2016 US$ 000	2015 US$ 000
Baring Vostok Cyprus Limited	Affiliated with controlling shareholder	Rent, services	–	–

Year-end balances arising from transactions with related parties:

Due to related parties	31 December 2016 US$ 000	31 December 2015 US$ 000
Baring Vostok (Cyprus) Limited	12	12

All transactions with related parties were made on a commercial basis.

The following transactions were carried out between the Company and its wholly-owned subsidiaries:

			Year ended 31 December
Related party	Relationship	Nature of transactions	2015
Woodhurst Holdings Limited	100% directly-owned subsidiary	Reduction of receivables due	–

Year-end balances arising from transactions with subsidiaries

	31 December 2016 US$ 000	31 December 2015 US$ 000
Accounts receivable from subsidiaries		
Woodhurst Holdings Limited	4,735	4,735
Accounts payable to subsidiaries		
Woodhurst Holdings Limited	1,357	1,357

Key management

Key management of the Company is considered to comprise the directors and the Chief Financial Officer, who is not a director. Details of key management compensation are summarised below.

Year ended 31 December	2016 US$ 000	2015 US$ 000
Salaries and short-term benefits	444	595
Compensation for loss of office	39	–
Fees	230	170
Total key management compensation	**713**	**765**

24. Contingencies and commitments

24.1 Capital commitments

As of the balance sheet date all material licence work obligations have been met and all of the Group's capital expenditures and work programmes are discretionary. As of the balance sheet date, the Board had approved a work programme for 2017 with a total capital expenditure budget of US$12.3 million of which US$1.4 million had been contracted. The remainder is expected to be incurred but had not been committed to or contracted as at the balance sheet date.

24.2 Taxation

Russian tax, currency and customs legislation is subject to varying interpretations and changes which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant regional and federal authorities. Recent events within the Russian Federation suggest that the tax authorities may be taking a more assertive position in their interpretation of the legislation and assessments, and it is possible that transactions and activities that have not been challenged in the past may be challenged. As a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review, but under certain circumstances, reviews may cover longer periods.

At 31 December 2016, management believes that its interpretation of the relevant legislation is appropriate and the Group's tax, currency and customs positions will be sustained.

24.3 Restoration, rehabilitation, and environmental costs

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

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

24.4 Oilfield licences

The Group is subject to periodic reviews of its activities by governmental authorities with respect to the requirements of its oilfield licences. Management of the Group correspond with governmental authorities to agree on remedial actions, if necessary, to resolve any findings resulting from these reviews. Failure to comply with the terms of a licence could result in fines, penalties, licence limitation, suspension or revocation. The Group's management believes any issues of non-compliance would be resolved through negotiations or corrective actions without any materially adverse effect on the financial position or the operating results of the Group.

The principal licences of the Group and their expiry dates are:

Field	Licence holder	Licence expiry date
Karpenskiy	OOO Pre-Caspian Gas Company	2031
Urozhainoye-2	OOO Pre-Caspian Gas Company	2032
Vostochny-Makarovskoye	OOO Gaznefteservice	2026
Dobrinskoye	OOO Gaznefteservice	2026

Glossary of Technical Terms

2-D seismic	geophysical data that depicts the subsurface strata in two dimensions.
3-D seismic	geophysical data that depicts the subsurface strata in three dimensions. 3-D seismic typically provides a more detailed and accurate interpretation of the subsurface strata than 2-D seismic.
Abandonment	application of a cement plug to close a well and welding of a steel plate to the top of the well.
Bbl	the standard barrel of crude oil or other petroleum product (42 US gallons (approximately 159 litres).
bcf	billion cubic feet.
bcm	billion cubic metres.
best estimate	the term "best estimate" is used here as a generic expression for the estimate considered to be the closest to the quantity that will actually be recovered from the accumulation between the date of the estimate and the time of abandonment.
boe	barrels of oil equivalent, being for natural gas the energy equivalent of one barrel of oil. The usual ratio is to equate 6,000 cubic feet to one barrel of oil equivalent.
condensate	liquid hydrocarbons associated with the production from a primarily natural gas reservoir.
field	means an area consisting of either a single reservoir or multiple reservoirs, all grouped on or related to the same individual geological structural feature and/or stratigraphic condition.
gas	natural gas.
gas processing facilities	together with the laboratory, gathering pipelines and storage facilities (if any), a plant comprising one or more units such that after conditioning the gas will be of pipeline quality as, specified by Gazprom, such units may include dehydration, sweetening and separation of natural gas liquids.
gas-water contact	bounding surface in a reservoir above which predominantly gas occurs and below which predominantly water occurs.
hydrocarbons	compounds formed from the elements hydrogen (H) and carbon (C) and existing in solid, liquid or gaseous forms.
Kungurian salt	a layer of salt laid down during the lower Permian age which occurs in the Northern Caspian Petroleum Province.
licence area	the particular subsoil plot specified in the subsoil licence issued by the applicable Russian federal authority, which the licence holder has the right to use for the purpose and on the terms specified in the subsoil licence. A licence area may contain one or more fields or may encompass only a portion of a field.
mcm	thousand cubic metres.
mmbbls	million barrels.
mmBOE	million barrels of oil equivalent.
natural gas	hydrocarbons that are gaseous at one atmosphere of pressure at 20°C. It can be divided into lean gas, primarily methane but often containing some ethane and smaller quantities of heavier hydrocarbons (also called sales gas) and wet gas, which is primarily ethane, propane and butane as well as smaller amounts of heavier hydrocarbons; partially liquid under atmospheric pressure.
petroleum	naturally occurring liquids and gases which are predominantly comprised of hydrocarbon compounds.
possible reserves	are those unproved reserves that, on the available evidence and taking into account technical and economic factors, have a 10% chance of being produced.
probable reserves	are those reserves in which hydrocarbons have been located within the geological structure with a lesser degree of certainty because fewer wells have been drilled and/or certain operational tests have not been conducted. Probable reserves are those reserves that, on the available evidence and taking into account technical and economic factors, have a better than 50% chance of being produced.
prospective resources	are those quantities of hydrocarbons which are estimated, on a given date, to be potentially recoverable from undiscovered accumulations.
proved plus probable reserves	sum of the proved reserves and the probable reserves calculated in accordance with SPE standards.
proved reserves	include reserves that are confirmed with a high degree of certainty through an analysis of development history and/or volume method analysis of the relevant geological and engineering data. Proved reserves are those that, based on the available evidence and taking into account technical and economic factors, have a better than 90% chance of being produced.
reserves	quantities of petroleum which are anticipated to be commercially recoverable from known accumulations from a given date forward.
reservoir	a porous and permeable underground formation containing a natural accumulation of producible natural gas and/or oil that is confined by impermeable rock or water barriers and is separate from other reservoirs.
risk factor	for contingent resources means the estimated chance, or probability, that the volumes will be commercially extracted; for prospective resources means the chance or probability of discovering hydrocarbons in sufficient quantity for them to be tested to the surface; this, then, is the chance or probability of the prospective resource maturing into a contingent resource.
SPE standards	reserves definitions consistent with those approved in 2007 by the Society of Petroleum Engineers and the World Petroleum Congresses.
sub-salt	below the Kungurian salt layer.
supra-salt	above the Kungurian salt layer.

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