

**Explanatory Note to  
Item 2 of the Agenda of  
the Annual General  
Meeting of Shareholders  
of PJSC ALROSA**

The accounting records of PJSC ALROSA (hereinafter, the Company) are maintained according to the Federal Law On Accounting and the associated Accounting Regulations adopted by the decrees of the Ministry of Finance of Russia, and by the Company's Accounting Policy.

Comprehensive integrated SAP ERP-based system is used for online accounting, record of availability and movement of all assets and liabilities, recognition of commercial operations of branches, representative offices and divisions of the Company in the accounts and generating accounting (financial) statements of the Company.

The auditor's report signed by the auditors of AO PricewaterhouseCoopers Audit on February 10, 2017, based on the results of the audit of the Company's financial status, confirms that the Company's accounting statements fairly, in all material respects, reflect the Company's financial condition as of December 31, 2016, its financial performance and cash flow for 2016 according to the Russian Accounting Standards.

**The analysis of forms of the Company's accounting (financial) statements for 2016**

**ANALYSIS OF THE BALANCE SHEET**

As of December 12, 2016, the balance sheet currency totals RUB 683,397 million and increased by RUB 84,790 million (by 14.2%) as compared to the previous year.

The balance sheet **Assets**: non-current assets increased by RUB 53,517 million to RUB 535,407 million, current assets increased by RUB 31,273 million to RUB 147,989 million.

Main changes in the assets are as follows:

- ✓ property, plant and equipment and interest-bearing investments – decrease by RUB 7,045 million (by 3%) to RUB 253,105 million, including:

commissioning of new facilities – increase of value by RUB 42,214 million, disposal of property, plant and equipment – decrease by RUB 34,380 million (RUB 16,626 million and RUB 17,754, respectively),

decrease in value of incomplete construction by RUB 14,867 million to RUB 34,452 million, commissioning of facilities of completed construction – by RUB 42,204 million.

- ✓ inventory stock – increase by RUB 10,485 million (by 18%), out of which the increase of rough diamonds, polished diamonds, diamond grinding powder stock remainder – by RUB 3,371 million, and decrease in volume terms (carats) – by 839 thousand carats (by 6.7%).
- ✓ accounts receivable – decrease by RUB 9,155 million (by 30%), including due to tax overpayment for 2015 – by RUB 4,859 million, the overdue debt in total debt amounted to RUB 727 million (3.5%).
- ✓ finance investments – increase by RUB 76,688 million (by 35%), out of which the adjustment up to the market value of shares listed on the market – RUB 57,742 million, amount of investments in the authorized capitals of subsidiaries – RUB 9,019 million.
- ✓ cash – increase by RUB 10,153 million (by 64.8%), including increase by RUB 12,844 million in deposit accounts, with a decrease of cash balance on the foreign currency accounts – RUB 3,005 million.

The balance sheet **Liabilities**:

The Company's *liabilities* decreased by RUB 48,678 million (by 16.6%) to RUB 244,409 million, including:

- ✓ Borrowings decreased by RUB 79,860 million to RUB 143,249 million.

The main reasons: loan repayment – USD 720 million (RUB 48,475 million) (the balance of unliquidated liabilities as of December 31, 2016, amounted to USD 2,320 million), positive exchange difference (RUB 35,659 million) occurred during revaluation of liabilities in foreign currency,

- ✓ Deferred tax liabilities increased by RUB 10,485 million to RUB 51,295 million.

The Company's **equity** grew by RUB 133,467 million (by 43.7%) to RUB 438,988 million, including:

- ✓ Undistributed profit increased by RUB 138,284 million for the following reasons:

net profit for 2016	+ RUB 148,657 million
payments made according to the resolution of the General Meeting of Shareholders of June 30, 2016	RUB (15,442) million
previously declared and unclaimed dividends restored	+ RUB 12 million
increase in the value of retired property, plant and equipment is transferred from the capital surplus and change in the accounting method	+ RUB 5,057 million

The **main source** of the Company's fixed assets in 2016 is equity, absolute value of which (net assets) has increased since the beginning of the year by RUB 133,461 million (by 43.7%) to RUB 438,988 million.

### ANALYSIS OF PROFIT AND LOSS STATEMENT

**Proceeds** from sale of products, works, services for 2016 increased, as compared to 2015, by RUB 64,290 million (by 34.7%) and amounted to RUB 249,566 million. Main increase in the amount of RUB 63,705 million (by 40%) is associated with sale of main products: natural rough diamonds, polished diamonds and diamond grinding powders. Proceeds from sale of main products amounted to RUB 223,543 million, share in total sales – 90%.

Export – 78% of the total proceeds.

The **cost** of sold products, works, services, commercial and administrative expenses, as compared to 2015, increased by RUB 15,264 million (by 15.2%) and amounted to RUB 115,918 million.

**Other income and expenses** for 2016 – profit (RUB 52,104 million), increment in profit, as compared to 2015, amounted to RUB 110,656 million (in 2015 loss was RUB 58,552 million).

The main performance drivers of the positive result:

- ✓ Adjustment of the Company's finance investments up to the market value: increase in the value of PJSC ALROSA-Nyurba shares in 2016 – RUB 57,742 million (in 2015 – RUB 9,239 million);

- ✓ Positive exchange difference – RUB 23,221 million (in 2015 – negative exchange difference in the amount of RUB 52,238 million).

**The Company's net profit for 2016 increased by RUB 127,545 million (6 times higher) to RUB 148,657 million.**

#### **ANALYSIS OF STATEMENT ON CHANGE IN EQUITY**

The Company's equity for 2016 increased by RUB 133,467 million to RUB 438,988 million.

The **reserve fund** is RUB 737 million (0.2% of the total equity) and is generated from net profit according to the Charter and is intended for covering losses, redemption of bonds and repurchase of shares of the Company where no other funds are available, and may not be utilized for any other purpose.

The Company's **authorized capital** is formed according to the Charter and amounted to RUB 3,682 million (0.8% of the total amount of equity).

The Company's authorized capital is divided into 7,364,965,630 ordinary registered shares with par value of 50 kopecks.

The authorized capital is fully paid-up, in 2016 the Company did not announce any additional issue of shares, placement of bonds or any other issue of securities.

The Company's **capital surplus** – RUB 111,695 million (25.4 of the total amount of equity).

Decrease in the amount of the revaluation of non-current assets by RUB 4,816 million occurred due to transfer of appraisal (markdown) on retired plant and equipment from the capital surplus to retained profit.

The capital surplus (without revaluation) is RUB 50,041 million and consists mainly of share premium from additional issue of the Company's shares in 2008.

**Undistributed profit** – RUB 322,874 million (73.5% of the total equity). The undistributed profit for 2016 is RUB 148,657 million.

## **ANALYSIS OF STATEMENT OF CASH FLOW**

### **Cash flow from operating activities in 2016:**

Cash received – RUB 254,099 million, including RUB 246,426 million from sale of products, goods, works, services;

Cash paid – RUB 157,187 million, including RUB 44,818 million – payment to suppliers (contractors) for materials, works, services, RUB 35,116 million – employee compensation, RUB 24,235 million – tax payment, RUB 11,482 million – customs duties payment.

### **Cash flow from investing activities in 2016:**

Cash received – RUB 103,970 million, including RUB 68,667 million – return of funds from deposits, RUB 11,845 million – repayment of loans granted, sale of debt securities, RUB 22,267 million – dividend, interest under debt financial investments and interest participation in other companies.

Cash paid – RUB 125,476 million, including RUB 23,262 million – acquisition, creation, modernization, reconstruction and preparation for use of non-current assets, RUB 101,257 million – acquisition of debt securities, providing loans to others (including placement of short-term deposits in the amount of RUB 99,492 million).

### **Cash flow from financial activities in 2016:**

Cash received – loans in the amount of RUB 4,006 million.

Cash paid – RUB 63,856 million including payment of dividends and other profit distribution to shareholders – RUB 15,381 million, due to repayment of loans – RUB 48,475 million.

**Result of cash flow for the reporting period – RUB 15,555 million.**

The balance of cash and cash equivalent as of the beginning and the end of the reporting period – RUB 15,669 million and RUB 25,822 million, respectively.

**Free cash flow** as the result of cash flow from operating activities less payments for acquisition, creation, modernization, reconstruction and preparation for use of non-current assets in 2016 is RUB 73,649 million.

#### **ACCURAL AND PAYMENT OF TAX, DUTIES, CHARGES AND DIVIDENDS**

In 2016, the amount of assessed and paid taxes, duties, charges (hereinafter, taxes) and insurance premium is RUB 64,573 million, paid – RUB 54,445 million.

As compared to 2015, the amount of taxes and insurance premium increased by RUB 14,881 million (by 37.6%), out of which the increased income tax – RUB 16,794 (million), increase of insurance premium – by RUB 901 million.

Paid in 2016:

- ✓ The state budget of the Republic of Sakha (Yakutia) received RUB 33,562 million, that is RUB 8,389 million more than in 2015.
- ✓ The federal budget received RUB 3,945 million, including VAT – RUB 813 million, for 2015 was paid from the federal budget – RUB 570 million and reimbursed VAT – RUB 1,183 million.
- ✓ Non-budget funds, local and other budgets received RUB 16,938 million, that is RUB 1,932 million higher compared to the previous year.

The breakdown of taxes, duties and charges paid in 2016:

Name	2016		2015		Increase/decrease compared to 2015	
	RUB mln	%	RUB mln	%	RUB mln	%
Mineral extraction tax (rough diamonds)	12,038	22.1	17,485	44.2	-5,447	-22.1
Profit tax	22,077	40.6	5,283	13.4	16,794	27.2
Property tax	3,320	6.1	2,809	7.1	511	-1.0

Personal income tax	5,239	9.6	4,963	12.5	276	-2.9
Insurance premium	10,321	19.0	9,420	23.8	901	-4.9
VAT	813	1.5	-1,183	-3.0	1,996	4.5
Other taxes, charges	637	1.2	787	2.0	-150	-0.8
<b>Total:</b>	<b>54,445</b>	<b>100.0</b>	<b>39,564</b>	<b>100.0</b>	<b>14,881</b>	<b>0.0</b>

Payment of dividends according to the decision adopted by the General Meeting of Shareholders:

Name of a budget	2016 (based on results of 2015)		2015 (based on results of 2014)		Increase in 2016 comparing to 2015	
	RUB mln	%	RUB mln	%	RUB mln	%
Russian Federation represented by the Federal Agency for State Property Management	5,084	33.0	4,756	43.9	328	-10.9
Ministry of Property And Land Relations of the Republic of Sakha (Yakutia)	3,848	25.0	2,707	25.0	1,141	0.0
Administrations of the municipalities of the Republic of Sakha (Yakutia)	1,231	8.0	866	8.0	365	0.0
Others	5,230	34.0	2,497	23.1	2,733	10.9
<b>Total:</b>	<b>15,393</b>	<b>100</b>	<b>10,826</b>	<b>100.0</b>	<b>4,567</b>	<b>0.0</b>
<i>per 1 share</i>	<i>2.09</i>		<i>1.47</i>		<i>0.62</i>	