

PJSC "FARMAK"

Consolidated Financial Statements
for the Year Ended 31 December 2016

PJSC "FARMAK"

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PJSC "FARMAK"

STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

Management is responsible for the preparation of the consolidated financial statements that present fairly the consolidated financial position of Public Joint Stock Company ("PJSC") "Farmak" (hereinafter, the "Company") and its subsidiaries (hereinafter jointly, the "Group") as of 31 December 2016 and the consolidated results of its operations, cash flows, and changes in equity for the year then ended, in compliance with International Financial Reporting Standards ("IFRS").

In preparing the consolidated financial statements, management is responsible for:

- Properly selecting and applying accounting policies;
- Presenting information, including accounting policies, in a manner that provides relevant, reliable, comparable, and understandable information;
- Providing additional disclosures when compliance with the specific requirements in IFRS are insufficient to enable users to understand the impact of particular transactions, other events, and conditions on the Group's consolidated financial position and financial performance; and
- Making an assessment of the Group's ability to continue as a going concern.


Management is also responsible for:

- Designing, implementing, and maintaining an effective and sound system of internal controls, throughout the Group;
- Maintaining adequate accounting records that are sufficient to show and explain the Group's transactions and disclose with reasonable accuracy at any time the consolidated financial position of the Group, and which enable them to ensure that the consolidated financial statements of the Group comply with IFRS;
- Maintaining statutory accounting records in compliance with the legislation of Ukraine;
- Taking such steps as are reasonably available to them to safeguard the assets of the Group; and
- Preventing and detecting fraud and other irregularities.

The consolidated financial statements of the Group for the year ended 31 December 2016 were approved by management on 20 April 2017.

On behalf of management of PJSC "Farmak":



F. I. Zhebrovska
General Director

V. G. Smarodina,
Chief Financial Officer

INDEPENDENT AUDITOR'S REPORT

To the Shareholders of PJSC "Farmak":

Opinion

We have audited the consolidated financial statements of PJSC "Farmak" (hereinafter, the "Company") and its subsidiaries (hereinafter jointly, the "Group"), which comprise the consolidated statement of financial position as of 31 December 2016, and the consolidated statement of profit or loss and other comprehensive income, the consolidated statement of changes in equity, and the consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as of 31 December 2016, and its consolidated financial performance and consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRSs").

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing ("ISAs"). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Consolidated Financial Statements section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (the "IESBA Code") together with the ethical requirements that are relevant to our audit of the consolidated financial statements in Ukraine, and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Why the matter was determined to be a key audit matter? How the matter was addressed in the audit?

Accounting for acquisition of business

Refer to Note 8 "*Acquisition of Subsidiaries*", Note 9 "*Goodwill*" and Note 18 "*Liabilities in a Business Combination*"

Accounting for Nord Farm Group acquisition as well as the impairment analysis of goodwill acquired and remeasurement of fair value of contingent consideration as of the year end was considered a key audit matter due to the following:

- The Group is required to make a number of judgments for identification of intangible assets acquired and fair value of acquired assets and liabilities;
- The value of contingent consideration is determined by a number of significant unobservable inputs and using management's judgment and estimates, including forecasted future sales of Nord Farm, the overall market size for new Farmak products to be launched in this market, and the potential impact of competitors' products expected to be launched in the future;
- Judgment involved in impairment analysis of goodwill as of the reporting date included assumptions of future profitability, revenue growth, margins, and forecasted cash flows, and the selection of an appropriate discount rate.

Our procedures included the following:

- Inspecting the terms of the Sale-Purchase Agreement to determine whether the accounting treatment of contingent consideration arrangements is appropriate based on the criteria of IFRS;
- Using our internal valuation specialists to assist us in:
 - Auditing purchase price allocation, including identification of separately identifiable intangible assets in accordance with IFRS as of the acquisition date;
 - Considering appropriateness of the discount rate used for the purposes of goodwill impairment analysis as of 31 December 2016;
 - Assessing key cash flow assumptions for the purposes of impairment analysis of goodwill and valuation of contingent consideration as of 31 December 2016;
- Comparing forecasted future cash flows, including assumptions relating to revenue growth rates and operating margins against historical trends to assess reliability of management's forecasts, in addition to comparing forecast assumptions to external market analysis for the purposes of goodwill impairment analysis and valuation of contingent consideration as of the acquisition date and 31 December 2016;
- Performing sensitivity analysis in respect of future sales forecasts of Nord Farm Group and weighted probabilities assigned to the calculation of contingent consideration;
- Reviewing respective disclosures made in the consolidated financial statements.

Our procedures concluded that the key judgments used by management and the resulting valuation conclusions were appropriate.

Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements

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

In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure, and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the consolidated financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the audit of the Group. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are, therefore, the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.



20 April 2017

PJSC "FARMAK"

**CONSOLIDATED STATEMENT OF FINANCIAL POSITION
AS OF 31 DECEMBER 2016
In Ukrainian Hryvnias and in thousands**

| | Notes | 2016 | 2015 |
|--|-------|------------------|------------------|
| Assets | | | |
| <i>Non-current assets</i> | | | |
| Property, plant and equipment | 6 | 1,908,820 | 1,700,094 |
| Prepayments for property, plant and equipment | 6 | 59,266 | 55,192 |
| Intangible assets | 7 | 72,278 | 36,556 |
| Goodwill | 9 | 255,905 | - |
| Investments in associate | | 2,304 | 3,195 |
| Deferred tax assets | 20 | 30,165 | 36,252 |
| Other non-current assets | | 1,127 | 3,015 |
| Total non-current assets | | 2,329,865 | 1,834,304 |
| <i>Current assets</i> | | | |
| Inventories | 10 | 879,547 | 715,024 |
| Trade and other accounts receivable | 11 | 1,040,252 | 591,638 |
| Prepayments made | 12 | 41,459 | 30,949 |
| Taxes recoverable and prepaid, other than income tax | 13 | 42,711 | 69,702 |
| Current income tax prepaid | | 1,508 | 20,175 |
| Cash and cash equivalents | 14 | 44,020 | 182,549 |
| Total current assets | | 2,049,497 | 1,610,037 |
| Total assets | | 4,379,362 | 3,444,341 |
| Equity and liabilities | | | |
| <i>Equity</i> | | | |
| Share capital | 15 | 54,479 | 57,650 |
| Foreign currency translation reserve | | 7,346 | 2,683 |
| Retained earnings | | 2,521,487 | 2,070,560 |
| Total equity attributable to equity holders of the Company | | 2,583,312 | 2,130,893 |
| Non-controlling interests | | (181) | (358) |
| Total equity | | 2,583,131 | 2,130,535 |
| <i>Non-current liabilities</i> | | | |
| Loans and borrowings | 16 | 248,270 | 261,278 |
| Finance lease obligations | | 10,786 | - |
| Retirement and other employee benefit obligations | 17 | 28,566 | 20,331 |
| Liabilities in a business combination | 18 | 85,287 | - |
| Other non-current liabilities | | - | 1,085 |
| Total non-current liabilities | | 372,909 | 282,694 |
| <i>Current liabilities</i> | | | |
| Loans and borrowings | 16 | 642,520 | 592,506 |
| Trade and other accounts payable | 19 | 723,330 | 425,979 |
| Finance lease obligations | | 7,331 | 6,215 |
| Income tax payable | | 34,195 | - |
| Taxes payable, other than income tax | | 15,946 | 6,412 |
| Total current liabilities | | 1,423,322 | 1,031,112 |
| Total liabilities | | 1,796,231 | 1,313,806 |
| Total equity and liabilities | | 4,379,362 | 3,444,341 |

On behalf of management of PJSC "Farmak":

F. I. Zhebrovska,
General Director

V. G. Smarodina
Chief Financial Officer

PJSC "FARMAK"

**CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2016**

In Ukrainian Hryvnias and in thousands

| | Notes | 2016 | 2015 |
|---|-------|------------------|------------------|
| Revenue | 21 | 5,112,352 | 3,578,033 |
| Cost of sales | 22 | (2,398,495) | (1,467,686) |
| Gross profit | | 2,713,857 | 2,110,347 |
| Selling and distribution expenses | 23 | (1,094,302) | (832,050) |
| General and administrative expenses | 24 | (467,233) | (316,668) |
| Research and development costs | 25 | (158,974) | (158,824) |
| Other operating income | | 7,431 | 40,204 |
| Other operating expense | 26 | (40,811) | (34,037) |
| Operating profit | | 959,968 | 808,972 |
| Finance income | | 3,032 | 1,696 |
| Finance costs | 27 | (50,480) | (29,048) |
| Net foreign exchange loss | | (83,848) | (287,884) |
| Share in profit of associate | | 1,350 | 1,543 |
| Profit before income tax | | 830,022 | 495,279 |
| Income tax expense | 20 | (152,821) | (89,864) |
| Profit for the year | | 677,201 | 405,415 |
| Other comprehensive income/(loss) | | | |
| <i>Items that will not be reclassified subsequently to profit or loss</i> | | | |
| Revaluation of defined benefit obligations | 17 | (1,517) | (5,184) |
| <i>Items that may be reclassified subsequently to profit or loss</i> | | | |
| Exchange differences on translating foreign operations | | 4,663 | 1,099 |
| Total comprehensive income for the year | | 680,347 | 401,330 |
| Profit for the year attributable to: | | | |
| Equity holders of the Company | | 677,024 | 405,385 |
| Non-controlling interests | | 177 | 30 |
| | | 677,201 | 405,415 |
| Total comprehensive income for the year attributable to: | | | |
| Equity holders of the Company | | 680,170 | 401,300 |
| Non-controlling interests | | 177 | 30 |
| | | 680,347 | 401,330 |

On behalf of management of PJSC "Farmak":

F. I. Zhebrovska,
General Director

V. G. Smarodina,
Chief Financial Officer

PJSC "FARMAK"

**CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2016
In Ukrainian Hryvnias and in thousands**

| | Notes | 2016 | 2015 |
|---|--------|----------------|----------------|
| Operating activities | | | |
| Profit before income tax | | 830,022 | 495,279 |
| Adjustments for: | | | |
| Depreciation and amortization | | 198,482 | 160,065 |
| Net loss on disposal of property, plant and equipment and intangible assets | 26 | (973) | 2,194 |
| Share in profit of associate | | (1,350) | (1,543) |
| Loss on write down of raw materials and finished goods | 26 | 16,007 | 11,680 |
| Changes in provision for impairment and write off of accounts receivable | 23, 26 | 824 | 5,238 |
| Changes in fair value of contingent consideration | 31 | 7,523 | - |
| Finance costs | | 50,480 | 29,048 |
| Finance income | | (3,032) | (1,696) |
| Net foreign exchange loss | | 93,513 | 266,584 |
| Operating profit before changes in working capital | | 1,191,496 | 966,849 |
| Changes in working capital: | | | |
| Increase in inventories | | (111,310) | (265,329) |
| Increase in trade and other accounts receivable | | (358,080) | (107,018) |
| Increase in prepayments made | | (7,308) | (6,926) |
| Decrease in taxes recoverable and prepaid, other than income tax | | 31,649 | 6,200 |
| Increase in trade and other accounts payable and other liabilities | | 103,911 | 44,150 |
| Increase in liabilities in a business combination | | 76,430 | - |
| Increase/(decrease) in taxes payable, other than income tax | | 5,169 | (1,760) |
| Cash generated from operating activities | | 931,957 | 636,166 |
| Interest paid | | (60,451) | (51,215) |
| Income tax paid | | (91,923) | (81,153) |
| Net cash generated from operating activities | | 779,583 | 503,798 |
| Investing activities | | | |
| Acquisition of property, plant and equipment and intangible assets | | (430,622) | (397,284) |
| Proceeds on disposal of property, plant and equipment | | 3,353 | 1,718 |
| Net cash outflow due to acquisition of subsidiaries | 8 | (183,372) | - |
| Dividends received from associate | | 2,262 | 2,722 |
| Interest received | | 1,701 | 1,067 |
| Net cash used in investing activities | | (606,678) | (391,777) |
| Financing activities | | | |
| Proceeds from loans and borrowings | | 218,419 | 93,684 |
| Repayment of loans and borrowings | | (285,208) | (105,283) |
| Repayment of finance lease obligations | | (13,792) | (13,159) |
| Repurchase of treasury shares | | (198,058) | - |
| Dividends paid | | (32,962) | (2,340) |
| Net cash used in financing activities | | (311,601) | (27,098) |


PJSC "FARMAK"

**CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2016 (CONTINUED)**
In Ukrainian Hryvnias and in thousands

| | Notes | 2016 | 2015 |
|---|-------|---------------|----------------|
| Net (decrease)/increase in cash and cash equivalents | | (138,696) | 84,923 |
| Cash and cash equivalents, as of 1 January | 14 | 182,549 | 96,835 |
| Effect of exchange rate changes on balances of cash and cash equivalents held in foreign currencies | | 167 | 791 |
| Cash and cash equivalents, as of 31 December | 14 | <u>44,020</u> | <u>182,549</u> |

Non-cash transactions for the year ended 31 December 2016 were represented by property, plant and equipment received under finance lease obligations in the amount of UAH 18,936 thousand (2015: nil).

On behalf of management of PJSC "Farmak":



F. I. Zhebrovska,
General Director



V. G. Smaragina,
Chief Financial Officer

PJSC "FARMAK"

**CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2016
In Ukrainian Hryvnias and in thousands**

| | Share capital | Foreign currency translation reserve | Retained earnings | Total equity attributable to equity holders of the Company | Non- controlling interests | Total equity |
|---|---------------|---|----------------------|--|----------------------------------|------------------|
| As of 1 January 2015 | 57,650 | 1,584 | 1,684,033 | 1,743,267 | (388) | 1,742,879 |
| Profit for the year | - | - | 405,385 | 405,385 | 30 | 405,415 |
| Other comprehensive income/(loss) for the year | - | 1,099 | (5,184) | (4,085) | - | (4,085) |
| Total comprehensive income for the year | - | 1,099 | 400,201 | 401,300 | 30 | 401,330 |
| Dividends declared (Note 15) | - | - | (13,674) | (13,674) | - | (13,674) |
| As of 31 December 2015 | 57,650 | 2,683 | 2,070,560 | 2,130,893 | (358) | 2,130,535 |
| Profit for the year | - | - | 677,024 | 677,024 | 177 | 677,201 |
| Other comprehensive income/(loss) for the year | - | 4,663 | (1,517) | 3,146 | - | 3,146 |
| Total comprehensive income for the year | - | 4,663 | 675,507 | 680,170 | 177 | 680,347 |
| Repurchase of treasury shares (Note 15) | (3,171) | - | (194,887) | (198,058) | - | (198,058) |
| Effect on initial recognition of receivables from the Group's shareholder at fair value | - | - | (7,655) | (7,655) | - | (7,655) |
| Dividends declared (Note 15) | - | - | (22,038) | (22,038) | - | (22,038) |
| As of 31 December 2016 | 54,479 | 7,346 | 2,521,487 | 2,583,312 | (181) | 2,583,131 |

On behalf of management of PJSC "Farmak":

F. I. Zhebrovska,
General Director

V. G. Smarodina,
Chief Financial Officer

PJSC "FARMAK"

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

In Ukrainian Hryvnias and in thousands

1. GENERAL INFORMATION

PJSC "Farmak" (the "Company") is a public joint stock company incorporated in Ukraine. The principal operating office of the Company is located at: 63 Frunze Str., Kyiv, 04080, Ukraine. The principal activities of the Company and its subsidiaries (jointly, the "Group") are production and distribution of generic pharmaceutical drugs. The products manufactured by the Company are sold mainly in Ukraine and exported to more than 20 countries, mostly to the CIS (Commonwealth of Independent States) countries.

Subsidiaries, consolidated structured entity, and associate of the Company at the end of the respective reporting periods were as follows:

| Entity's name | Principal activity | Place of the entity's incorporation and operation | The Company's effective ownership interest as of 31 December | |
|---|---|---|--|------|
| | | | 2016 | 2015 |
| Subsidiaries: | | | | |
| SE "Baza Vidpochynku "Smuhlianka" | Recreation center | Ukraine, Odesa | 100% | 100% |
| LLC "Farmakhim" | Property leasehold and operations with securities | Ukraine, Kharkiv | 100% | 100% |
| LLC "Berenika" | Production and sale of drugs | Ukraine, Zhytomyr | 100% | 100% |
| Farmak Invest Limited | Investments | Cyprus, Nicosia | 100% | 100% |
| KWW Kotkowski Wierzbicki Wegrzyn Sp. z o.o. | Investments | Poland, Warsaw | 100% | - |
| NORD FARM Sp. z o.o. | Distribution of drugs | Poland, Warsaw | 100% | - |
| ARENAPHARMA Sp. z o.o. | Production and sale of drugs | Poland, Warsaw | 100% | - |
| Consolidated structured entity*: | | | | |
| LLC "Simpozium" | Business travel, conference services | Ukraine, Kyiv | - | - |
| Associate: | | | | |
| LLC "Farmak SP" | Distribution of drugs | Poland, Warsaw | 26% | 26% |

* As described in Note 5, management concluded that the Company had a practical ability to direct the relevant activities of the structured entity unilaterally and, hence, the Company had control over the entity. As such, the entity was consolidated in these consolidated financial statements.

The Group's ultimate controlling party is Ms. Filia Ivanivna Zhebrovska.

2. OPERATING ENVIRONMENT

In the recent years, Ukraine has been in a political and economic turmoil. Crimea, an autonomous republic of Ukraine, was effectively annexed by the Russian Federation. In 2016, an armed conflict with separatists continued in certain parts of Luhanska and Donetska regions. These events resulted in higher inflation, devaluation of the national currency against major foreign currencies, decrease of GDP, illiquidity and volatility of financial markets. In January 2016, the agreement on the free trade area between Ukraine and the EU came into force. As a result, the Russian Federation implemented a trade embargo or import duties on key Ukrainian export products. In response, Ukraine implemented similar measures against Russian products.

In 2016, average inflation amounted to 13.9% comparing to 48.7% in 2015. Despite the fact that the cumulative inflation in Ukraine for the three latest years slightly exceeded 100%, management believes that the Ukrainian economy is not hyperinflationary due to slowing down of inflation during 2016 and lack of qualitative characteristics of the hyperinflationary economic environment.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2016
In Ukrainian Hryvnias and in thousands**

The economic situation began to stabilize in 2016, which resulted in GDP growth around 1% and stabilization of Ukrainian Hryvnia. This allowed the National Bank of Ukraine to ease some foreign exchange restrictions imposed during 2014-2015, including decrease of the required share of foreign currency proceeds sale to 65% and permission of dividends remittance. However, certain other restrictions were prolonged. Significant external financing is required to support the economy. During 2015 and 2016, Ukraine received the first tranches of extended fund facilities (EFF) agreed with the IMF. Further stabilization of the economic and political situation depends, to a large extent, upon success of the Ukrainian government's efforts, yet further economic and political developments are currently difficult to predict.

3. APPLICATION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS ("IFRS")

Adoption of new and revised International Financial Reporting Standards

In the current year, the Group has adopted the following Standards and Interpretations for the first time:

- Amendments to IFRS 10 *Consolidated Financial Statements*, IFRS 12 *Disclosure of Interests in Other Entities*, and IAS 28 *Investments in Associates and Joint Ventures* (2011) – Investment Entities: Applying the Consolidation Exception;
- Amendments to IFRS 11 *Joint Arrangements* – Accounting for Acquisition of Interests in Joint Operations;
- Amendments to IAS 1 *Presentation of Financial Statements* – Disclosure Initiative;
- Amendments to IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets* – Clarification of Acceptable Methods of Depreciation and Amortization;
- Amendments to IAS 16 *Property, Plant and Equipment* and IAS 41 *Agriculture* – Agriculture: Bearer Plants;
- IFRS 14 *Regulatory Deferral Accounts*;
- Amendments to IAS 27 *Consolidated and Separate Financial Statements* – Equity Method in Separate Financial Statements;
- Annual Improvements to IFRSs 2012-2014 Cycle.

The adoption of these new and revised Standards and Interpretations has not resulted in any significant changes to the amounts reported in the consolidated financial statements.

New and revised IFRSs in issue but not yet effective

At the date of authorization of these consolidated financial statements, the following Standards and Interpretations, as well as amendments to the Standards were in issue but not yet effective:

| Standards/Interpretations | Effective for annual accounting periods beginning on or after: |
|---|---|
| IFRS 9 <i>Financial Instruments</i> | 1 January 2018 |
| IFRS 15 <i>Revenue from Contracts with Customers</i> (and the related Clarifications) | 1 January 2018 |
| IFRS 16 <i>Leases</i> | 1 January 2019 |
| Amendments to IFRS 2 <i>Share-based Payment</i> – Classification and Measurement of Share-based Payment Transactions | 1 January 2018 |
| Amendments to IFRS 10 <i>Consolidated Financial Statements</i> and IAS 28 <i>Investments in Associates and Joint Ventures</i> – Sale or Contribution of Assets between an Investor and its Associate or Joint Venture | The effective date is not determined |
| Amendments to IAS 12 <i>Income Taxes</i> – Recognition of Deferred Tax Assets for Unrealized Losses | 1 January 2017 |
| Amendments to IAS 7 <i>Statement of Cash Flows</i> – Disclosure Initiative | 1 January 2017 |
| Amendments to IFRS 4 <i>Insurance Contracts</i> – Applying IFRS 9 <i>Financial Instruments</i> with IFRS 4 <i>Insurance Contracts</i> | 1 January 2018 |
| IFRIC 22 <i>Foreign Currency Transactions and Advance Consideration</i> | 1 January 2018 |
| Amendments to IAS 40 <i>Investment Property</i> – Transfers of Investment Property | 1 January 2018 |
| Annual Improvements to IFRSs 2014-2016 Cycle | 1 January 2018 |

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2016
In Ukrainian Hryvnias and in thousands**

Management is currently evaluating the impact of the adoption of these Amendments and Standards on future consolidated financial statements of the Group.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Statement of compliance

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards.

Basis of preparation

The consolidated financial statements have been prepared on the assumption that the Group is a going concern and will continue in operation for the foreseeable future.

These consolidated financial statements have been prepared on the historical cost basis. Historical cost is generally based on the fair value of the consideration given in exchange for goods and services.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique. In estimating the fair value of an asset or a liability, the Group takes into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date.

Fair value for measurement and/or disclosure purposes in these consolidated financial statements is determined on such a basis, except for share-based payment transactions that are within the scope of IFRS 2 *Share-based Payment*, leasing transactions that are within the scope of IAS 17 *Leases*, and measurements that have some similarities to fair value but are not fair value, such as net realizable value in IAS 2 *Inventories* or value in use in IAS 36 *Impairment of Assets*.

In addition, for financial reporting purposes, fair value measurements are categorized into Levels 1, 2, or 3 based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value measurement in its entirety, which are described as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date;
- Level 2 inputs are inputs (other than quoted prices included within Level 1) that are observable for the asset or liability, either directly or indirectly; and
- Level 3 inputs are unobservable inputs for the asset or liability.

Functional and presentation currency

Items included in the consolidated financial statements of each of the Group's entities are measured using the currency of the primary of the economic environment in which the entity operates ("the functional currency"). The functional currency of the entities registered in Ukraine and Cyprus is Ukrainian Hryvnia ("UAH"), and the entities registered in Poland – Polish Zloty ("PLN"). These consolidated financial statements are presented in Ukrainian Hryvnias, and all amounts are rounded to the nearest thousand, unless otherwise indicated.

Basis of consolidation

These consolidated financial statements incorporate the financial statements of the Company and entities (including the structured entity) controlled by the Company and its subsidiaries. Control is achieved when the Company:

- Has power over the investee;
- Is exposed, or has rights, to variable returns from its involvement with the investee; and
- Has the ability to use its power over investee to affect its returns.

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The Company reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control listed above.

When the Company has less than a majority of the voting rights of an investee, it has power over the investee when the voting rights are sufficient to give it the practical ability to direct the relevant activities of the investee unilaterally. The Company considers all relevant facts and circumstances in assessing whether or not the Company's voting rights in an investee are sufficient to give it power, including:

- The size of the Company's holding of voting rights relative to the size and dispersion of holdings of the other vote holders;
- Potential voting rights held by the Company, other vote holders or other parties;
- Rights arising from other contractual arrangements; and
- Any additional facts and circumstances that indicate that the Company has, or does not have, the current ability to direct the relevant activities at the time that decisions need to be made, including voting patterns at previous shareholders' meetings.

Consolidation of an investee begins when the Company obtains control over the investee and ceases when the Company loses control over the investee. Specifically, income and expenses of an investee acquired or disposed of during the year are included in the consolidated statement of profit or loss and other comprehensive income from the date the Company gains control until the date when the Company ceases to control the investee.

Profit or loss and each component of other comprehensive income are attributed to equity holders of the Company and to non-controlling interests. Total comprehensive income of subsidiaries is attributed to equity holders of the Company and to non-controlling interests even if this results in the non-controlling interests having a deficit balance.

When necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with the Group's accounting policies.

All intragroup assets and liabilities, equity, income, expenses and cash flows relating to transactions between entities of the Group are eliminated in full on consolidation.

Non-controlling interests

Non-controlling interests represent the equity in a subsidiary not attributable, directly or indirectly, to the Company's equity holders.

Non-controlling interests are presented separately in the consolidated statement of profit or loss and other comprehensive income within equity in the consolidated statement of financial position, separately from the Company's shareholders' equity.

Changes in the Group's ownership interests in investees

Changes in the Group's ownership interests in investees that do not result in the Group losing control over the investees are accounted for as equity transactions. The carrying amounts of the Group's interests and the non-controlling interests are adjusted to reflect the changes in their relative interests in the investees. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received is recognized directly in equity and attributed to equity holders of the Company.

When the Group loses control over an investee, a gain or loss is recognized in profit or loss and is calculated as the difference between (i) the aggregate of the fair value of the consideration received and the fair value of any retained interest and (ii) the previous carrying amount of the assets and liabilities of the investee and any non-controlling interests. All amounts previously recognized in other comprehensive income in relation to that investee are accounted for as if the Group had directly disposed of the related assets or liabilities of the investee (i.e. reclassified to profit or loss or transferred directly to retained earnings).

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Business combinations

Acquisitions of businesses are accounted for using the acquisition method. The consideration transferred in a business combination is measured at fair value, which is calculated as the sum of the acquisition-date fair values of the assets transferred by the Group, liabilities incurred by the Group to the former owners of the acquire, and the equity interests issued by the Group in exchange for control of the acquire. Acquisition-related costs are generally recognized in profit or loss as incurred.

At the acquisition date, the identifiable assets acquired and the liabilities assumed are recognized at their fair value.

Goodwill is measured as the excess of the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree, and the fair value of the acquirer's previously held equity interest in the acquiree (if any) over the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed. If, after reassessment, the net of the acquisition-date amounts of the identifiable assets acquired and liabilities assumed exceeds the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree and the fair value of the acquirer's previously held interest in the acquiree (if any), the excess is recognized immediately in profit or loss as a bargain purchase gain.

Non-controlling interests that are present ownership interests and entitle their holders to a proportionate share of the entity's net assets in the event of liquidation may be initially measured either at fair value or at the non-controlling interests' proportionate share of the recognized amounts of the acquiree's identifiable net assets. The choice of measurement basis is made on a transaction-by-transaction basis. Other types of non-controlling interests are measured at fair value or, when applicable, on the basis specified in another IFRS.

When the consideration transferred by the Group in a business combination includes assets or liabilities resulting from a contingent consideration arrangement, the contingent consideration is measured at its acquisition-date fair value and included as part of the consideration transferred in a business combination. Changes in the fair value of the contingent consideration that qualify as measurement period adjustments are adjusted retrospectively, with corresponding adjustments against goodwill. Measurement period adjustments are adjustments that arise from additional information obtained during the 'measurement period' (which cannot exceed one year from the acquisition date) about facts and circumstances that existed at the acquisition date.

The subsequent accounting for changes in the fair value of the contingent consideration that do not qualify as measurement period adjustments depends on how the contingent consideration is classified. Contingent consideration that is classified as equity is not re-measured at subsequent reporting dates and its subsequent settlement is accounted for within equity. Contingent consideration that is classified as an asset or a liability is re-measured at subsequent reporting dates in accordance with IAS 39 *Financial Instruments: Recognition and Measurement*, or IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, as appropriate, with the corresponding gain or loss being recognized in profit or loss.

If the initial accounting for a business combination is incomplete by the end of the reporting period in which the combination occurs, the Group reports provisional amounts for the items for which the accounting is incomplete. Those provisional amounts are adjusted during the measurement period, or additional assets or liabilities are recognized, to reflect new information obtained about facts and circumstances that existed at the acquisition date that, if known, would have affected the amounts recognized at that date.

Goodwill

Goodwill arising on an acquisition of a business is carried at cost as established at the date of acquisition of the business less accumulated impairment losses, if any.

For the purposes of impairment testing, goodwill is allocated to each of the Group's cash-generating units (or groups of cash-generating units) that is expected to benefit from the synergies of the combination.

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A cash-generating unit to which goodwill has been allocated is tested for impairment annually, or more frequently when there is indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than its carrying amount, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro rata based on the carrying amount of each asset in the unit. Any impairment loss for goodwill is recognized directly in profit or loss in the consolidated statement of profit or loss and other comprehensive income. An impairment loss recognized for goodwill is not reversed in subsequent periods.

On disposal of the relevant cash-generating unit, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

Investment in associate

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

The results and assets and liabilities of associate are incorporated in these consolidated financial statements using the equity method of accounting. Under the equity method, an investment in an associate is initially recognized in the consolidated statement of financial position at cost and adjusted thereafter to recognize the Group's share in profit or loss and other comprehensive income of the associate.

When an entity of the Group transacts with an associate of the Group, profits and losses resulting from the transactions with the associate are recognized in the Group's consolidated financial statements only to the extent of interests in the associate that are not related to the Group.

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable in normal course of business. Revenue is reduced by estimated customer returns, discounts, rebates, value added tax and other sale taxes and duties.

Revenue from the sale of goods is recognized when the goods are delivered and titles have been transferred, at which time all the following conditions are satisfied:

- The Group has transferred to the buyer the significant risks and rewards of ownership of the goods;
- The Group retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;
- The amount of revenue can be measured reliably;
- It is probable that the economic benefits associated with the transaction will flow to the Group; and
- The costs incurred or to be incurred in respect of the transaction can be measured reliably.

Value added tax

Revenue, expenses, and assets are recognized net of the amount of value added tax ("VAT"), except:

- Where VAT incurred on a purchase of assets or services is not recoverable from the taxation authority, in which case VAT is recognized as a part of the cost of acquisition of the asset or as a part of the expense item, as applicable; and
- When accounts receivable and accounts payable are stated with reference to the amount of VAT.

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Leases

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

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Group as lessee

Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalized at the commencement of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are recognized immediately in profit or loss.

Capitalized leased assets are depreciated over the shorter of the estimated useful life of the asset and the lease term, if there is no reasonable certainty that the Group will obtain ownership by the end of the lease term.

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

Group as lessor

Rental income from operating leases is recognized on a straight-line basis over the term of the relevant lease. Initial direct costs incurred in negotiating an operating lease are added to the carrying amount of the leased asset and recognized over the lease term on the same basis as rental income. Rental income is recognized as other operating income in the period in which it is earned.

Foreign currencies

Transactions in currencies other than the respective functional currency are treated as transactions in foreign currencies. Transactions in foreign currencies are initially recognized at the rates of exchange ruling at the dates of the transactions. At the end of each reporting period, monetary items denominated in foreign currencies are retranslated at the rates prevailing at that date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing at the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences on monetary items are recognized in profit or loss in the period in which they arise.

For the purposes of presenting these consolidated financial statements, the assets and liabilities of the Group's foreign operations are translated into UAH using exchange rates prevailing at the end of each reporting period. Income and expense items are translated at the average exchange rates for the period, unless exchange rates fluctuate significantly during that period, in which case the exchange rates at the dates of the transactions are used. Exchange differences arising, if any (foreign currency translation reserve), are recognized in other comprehensive income and accumulated in equity (and attributed to non-controlling interests as appropriate).

On the disposal of a foreign operation (i.e. a disposal of the Group's entire interest in a foreign operation), all of the exchange differences accumulated in equity in respect of that operation attributable to the equity holders of the Company are reclassified to profit or loss.

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Goodwill and fair value adjustments to identifiable assets acquired and liabilities assumed through acquisition of a foreign operation are treated as assets and liabilities of the foreign operation and translated at the rate of exchange prevailing at the end of each reporting period. Exchange differences arising are recognized in other comprehensive income.

Relevant exchange rates used for preparing these consolidated financial statements were as follows:

| Currency | As of 31 December 2016 | Average exchange rate for 2016 | As of 31 December 2015 | Average exchange rate for 2015 |
|-----------------|---------------------------------------|---|---------------------------------------|---|
| UAH/USD | 27.1909 | 25.5513 | 24.0007 | 21.8290 |
| UAH/EUR | 28.4226 | 28.2919 | 26.2231 | 24.2054 |
| UAH/RUB | 0.4511 | 0.3831 | 0.3293 | 0.3617 |
| UAH/PLN | 6.4390 | 6.4903 | - | - |

Loan and borrowing costs

Loan and borrowing costs comprise interest expense, finance lease costs, other non-current interest-bearing payables, and debt service costs.

Loan and borrowing costs directly attributable to the acquisition, construction, or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the loan and borrowing costs eligible for capitalization.

All other loan and borrowing costs are recognized in profit or loss in the period in which they are incurred.

Research and development costs

Research and development costs include expenditures related to research and development of generic drugs and predominantly relate to preclinical and clinical trials, staff costs, cost of raw materials and supplies relating to development of such generic drugs, and registration of new drugs. Expenditure on research activities is recognized as an expense in the reporting period in which it is incurred. Expenditure on the research and development of an individual generic drug is recognized as an intangible asset if, and only if, all of the following have been demonstrated:

- The technical feasibility to complete the intangible asset so that it will be available for use or sale;
- The intention to complete the intangible asset and use or sell it;
- The ability to use or sell the intangible assets;
- The ability of the intangible asset to generate probable future economic benefits;
- The availability of adequate technical, financial and other resources to complete the development and use or sale of the intangible asset; and
- The ability to measure reliably the expenditure attributable to the intangible asset during its development.

Post-employment and other non-current benefit obligations

Defined benefit pension obligations

The Company is obliged to compensate the State Pension Fund of Ukraine for pensions that are paid by the state to employees of the Company who worked in hazardous environment and, therefore, are eligible for early retirement and pensions until the normal retirement age as defined by the statutory regulations and pays the defined benefits to certain employees upon their retirement. Amount of such payments depends upon employee's service period. These obligations represent non-current benefits to employees and are not funded.

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These defined benefit plans (the "Plans") are not funded and have no respective Plan assets.

The Company's net obligation in respect of these Plans is calculated separately for each Plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods. The benefit is then discounted to determine the present value of the obligation, which is recorded in the consolidated statement of financial position. A discount rate is estimated using the effective yield of high-class corporate or government securities with the same maturity as the respective retirement obligation and traded in the world stock markets and is adjusted on average expected inflation rate.

Defined benefit costs are categorized as follows:

- Service cost (including current service cost, past service cost, as well as gains and losses on curtailments and settlements);
- Net interest income/(expense); and
- Remeasurement.

The Company presents the first two components of defined benefit costs in profit or loss in the line item "Staff Costs". Curtailment gains and losses are accounted for as past service costs.

State defined contribution pension plan

The employees of the Company receive pension benefits from the government in accordance with the laws and regulations of Ukraine. The Company pays to the State Pension Fund of Ukraine an amount based on each employee's wages. The Company's costs for these contributions are included in the line item "Staff Costs". These amounts are expensed when incurred.

Taxation

Income tax expense represents the sum of the current tax and deferred tax.

Current tax

The tax currently payable is based on taxable profit for the year. Taxable profit differs from 'profit before tax' as reported in the consolidated statement of profit or loss and other comprehensive income because of items of income or expense that are taxable or deductible in other years and items that are never taxable or deductible. The Group's current tax is calculated using tax rates that have been enacted by the end of the reporting period.

Deferred tax

Deferred tax is recognized on temporary differences between the carrying amounts of assets and liabilities in the consolidated financial statements and the corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are generally recognized for all taxable temporary differences. Deferred tax assets are generally recognized for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilized. Such deferred tax assets and liabilities are not recognized if the temporary difference arises from the initial recognition of assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit. In addition, deferred tax liabilities are not recognized if the temporary difference arises from the initial recognition of goodwill.

Deferred tax liabilities are recognized for taxable temporary differences associated with investments in subsidiaries and associate, except where the Group is able to control the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognized to the extent that it is probable that temporary difference are expected to reverse in the foreseeable future and there will be sufficient taxable profits against which to utilize the benefits of the temporary differences.

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The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax liabilities and assets are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realized, based on tax rates and tax laws that have been enacted or substantively enacted by the end of the reporting period.

The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

Current and deferred tax for the year

Current and deferred tax are recognized in consolidated statement of profit or loss and other comprehensive income, except when they relate to items that are recognized in other comprehensive income or directly in equity, in which case the current and deferred tax are also recognized in other comprehensive income or directly in equity respectively.

Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities, and the deferred tax assets and deferred tax liabilities relate to income taxes levied by the same taxation authority on the same taxable entity.

Property, plant and equipment

Property, plant and equipment are carried at historical cost, less any accumulated depreciation and accumulated impairment losses. The historical cost of a property, plant and equipment item comprises:

- Its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates;
- Any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management of the Group.

The cost of self-constructed assets includes the cost of materials, staff costs, and an appropriate portion of production overheads.

Capitalized costs include major expenditures for improvements and replacements that extend the useful lives of the assets or increase their revenue generating capacity. Repairs and maintenance expenditures that do not meet the foregoing criteria for capitalization are charged to profit or loss as incurred.

Depreciable amount is the cost of the item of property, plant and equipment, less its residual value. The residual value is the estimated amount that an entity would currently obtain from disposal of the item of property, plant and equipment, after deducting the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life.

Depreciation of property, plant and equipment is designed to write off the depreciable amount over the useful life of the asset and is calculated using a straight line method. Land is not depreciated. Useful lives of the groups of property, plant and equipment are as follows:

| | |
|-----------------------------|-------------|
| Buildings and constructions | 10-80 years |
| Machinery and equipment | 4-30 years |
| Vehicles | 4-10 years |
| Office equipment | 2-8 years |
| Other depreciable assets | 3-8 years |

The residual value, the useful life, and depreciation methods are reviewed at each financial year-end. The effect of any changes from previous estimates is accounted for as a change in an accounting estimate on a prospective basis.

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An item of property, plant and equipment is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset or disposal. Any gain or loss arising on disposal or retirement of the property, plant and equipment item (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is recognized in profit or loss.

Construction in progress comprises costs directly related to construction of property, plant and equipment. Construction in progress is not depreciated until the assets are available for use, i.e. when they are in the location and condition necessary for them to be capable of operating in the manner intended by management.

Intangible assets

Intangible assets with finite useful lives are carried at cost, less accumulated amortization and accumulated impairment losses. Amortization of intangible assets is recognized on a straight-line basis over their estimated useful lives. The estimated useful life and amortization method are reviewed at the end of each reporting period, with the effect of any changes in estimate being accounted for on a prospective basis.

Useful lives of the groups of intangible assets are as follows:

| | |
|-------------------------|------------|
| Software and licenses | 2-10 years |
| Other intangible assets | 2-10 years |

An intangible asset is derecognized on disposal or when no future economic benefits are expected from use or disposal. Gains or losses arising from derecognition of an intangible asset, measured as the difference between the net disposal proceeds and the carrying amount of the asset, are recognized in profit or loss when the asset is derecognized.

Intangible assets acquired in a business combination

Intangible assets acquired in a business combination and recognized separately from goodwill are initially recognized at their fair value at the acquisition date (which is regarded as their cost).

Subsequent to initial recognition, intangible assets acquired in a business combination are reported at cost less accumulated amortization and accumulated impairment losses, on the same basis as intangible assets that are acquired separately.

Impairment of property, plant and equipment and intangible assets other than goodwill

At the end of each reporting period, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). When it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Recoverable amount is the higher of fair value of the asset or cash-generating unit less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognized immediately in profit or loss.

When an impairment loss subsequently reverses, the carrying amount of the asset (or cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset (or cash-generating unit) in prior years.

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Inventories

Inventories of the Group comprise raw materials, finished goods, packaging materials, work in progress, merchandise for resale, and other inventories.

Cost of inventories include purchase costs (less any indirect taxes) and, where applicable, those costs that have been incurred in bringing the inventories to their present location and condition. When inventories are released to production, sale or otherwise disposed, cost of inventories is determined using weighted average method.

Inventories are valued at the lower of cost and net realizable value. Net realizable value represents the estimated selling price in the ordinary course of business less estimated costs of completion and costs necessary to make a sale.

Contingent liabilities acquired in a business combination

Contingent liabilities acquired in a business combination are initially measured at fair value at the acquisition date. At the end of subsequent reporting periods, such contingent liabilities are measured at the higher of: a) the amount that would be recognized in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* and b) the amount initially recognized less cumulative amortization recognized in accordance with IAS 18 *Revenue*.

Contingent assets and liabilities

Contingent assets are not recognized in the consolidated financial statements but disclosed when an inflow of economic benefits is probable.

Contingent liabilities are not recognized in the consolidated financial statements unless it is probable that an outflow of economic resources will be required to settle the obligation, and it can be reasonably estimated. They are disclosed in the consolidated financial statements unless the possibility of an outflow of resources embodying economic benefits is remote.

Financial instruments

Financial assets and financial liabilities are recognized in the Group's consolidated financial statements when the Group becomes a party to the contractual provisions of the instrument.

Financial assets and financial liabilities are initially recognized at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognized immediately in profit or loss. The accounting policies for subsequent remeasurement of these items are disclosed in the respective accounting policies set out below.

The effect of initial recognition of financial assets and liabilities obtained/incurred at terms different from market is recognized net of tax effect as income or expense, except for financial assets and liabilities with shareholders' or entities under common control, whereby the effect is recognized through equity.

Financial assets and financial liabilities are offset and the net amounts are reported in the consolidated statement of financial position only when the Group has a legally enforceable right to set-off the recognized amounts and intends to either settle on a net basis, or to realize the asset and settle the liability simultaneously.

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Effective interest rate method

The effective interest rate method is a method of calculating the amortized cost of a financial asset (liability) and of allocating interest income (expense) over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (payments) including all fees and points paid or received that form an integral part of the effective interest rate, transaction costs, and other premiums or discounts through the expected life of the financial asset (liability), or, where appropriate, a shorter period, to the net carrying amount on initial recognition.

Financial assets

Financial assets are classified into the following specified categories: financial assets 'at fair value through profit or loss', 'held-to-maturity' investments, 'available-for-sale' financial assets and 'loans and receivables'. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition. Financial assets of the Group include mainly cash and cash equivalents and trade and other accounts receivable.

Cash and cash equivalents

Cash and cash equivalents comprise cash on hand and with banks and short-term bank deposits with an original maturity within three months.

For the purpose of the consolidated statement of cash flows, cash and cash equivalents consist of cash and short-term bank deposits as defined above.

Trade and other accounts receivable

Trade and other accounts receivable with fixed or determinable payments that are not quoted in an active market are classified as receivables. Trade and other accounts receivable are measured at amortized cost using the effective interest rate method, less any impairment. Interest income is recognized by applying the effective interest rate, except for short-term receivables when the effect of discounting is immaterial.

Impairment of financial assets

Financial assets are assessed for indicators of impairment at the end of each reporting period. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been negatively affected.

The objective evidence of impairment could include:

- Significant financial difficulty of the issuer or counterparty; or
- Breach of contract, such as default or delinquency in interest or principal payments; or
- It is becoming probable that the borrower will enter bankruptcy or financial re-organization; or
- The disappearance of an active market for that financial asset because of financial difficulties.

For certain categories of financial assets, such as trade accounts receivable, assets are assessed for impairment on a collective basis even if they were assessed not to be impaired individually. Objective evidence of impairment for a portfolio of accounts receivable could include the Group's past experience of collecting payments, as well as observable changes in national or local economic conditions that correlate with default on accounts receivable.

For financial assets carried at amortized cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate.

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The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of accounts receivable, where the carrying amount is reduced through the use of an allowance account. When a trade receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognized in profit or loss.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through profit or loss to the extent that the carrying amount of the financial asset at the date the impairment is reversed does not exceed what the amortized cost would have been had the impairment not been recognized.

Derecognition of financial assets

The Group derecognizes a financial asset only when the contractual rights to the cash flows from the asset expire; or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity.

If the Group neither transfer nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group recognizes its retained interest in the asset and an associated liability for amounts it may have to pay. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognize the financial asset and also recognizes a collateralized borrowing for the proceeds received.

Financial liabilities and equity instruments

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangements and the definitions of a financial liability and an equity instrument.

Share capital

The Company's share capital is recognized at the value of consideration received by the Company. All subsequent capital increases are recognized at the fair value of the consideration received.

Own equity instruments repurchased by the Company are deducted from equity. No gain or loss is recognized in the consolidated statement of profit or loss and other comprehensive income on the purchase, sale, issue or cancellation of the Group's own equity instruments.

Financial liabilities

Financial liabilities are classified as either financial liabilities 'at fair value through profit or loss' or 'other financial liabilities'.

Other financial liabilities

Other financial liabilities of the Group include loans and borrowings, finance lease obligations, and trade and other accounts payable that are classified as 'other financial liabilities'. Other financial liabilities are initially measured at fair value less transaction costs, and subsequently are measured at amortized cost using the effective interest rate method.

Derecognition of financial liabilities

The Group derecognizes financial liabilities when, and only when, the Group's obligations are discharged, cancelled or they expire. Upon full derecognition of a financial liability, the difference between the carrying amount of the financial liability derecognized and the consideration paid and payable is recognized in profit or loss.

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Reclassification of the comparative financial information presented

Certain reclassifications were made by the Group to bring the information presented in the consolidated financial statements for the year ended 31 December 2015 in conformity with the way of presentation of the consolidated financial statements for the year ended 31 December 2016. Such reclassifications had no significant effect on these consolidated financial statements.

5. CRITICAL ACCOUNTING JUDGMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

In the application of the Group's accounting policies, which are described in Note 4, management of the Group is required to make judgments, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered by the management to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects current or future periods.

Critical judgments in applying accounting policies

The following are the critical judgments, apart from those involving estimations, that management has made in the process of applying the Group's accounting policies and that have the most significant effect on the amounts recognized in the consolidated financial statements.

Control over LLC "Simpozium"

Note 1 describes that LLC "Simpozium" is a consolidated structured entity of the Group even though the Group has no ownership or voting rights in it. Management of the Group has concluded that the Group has control over this company due to the fact that the Group: (1) receives substantially all of the returns related to its operations and net assets (the entity performs its relevant activities exclusively for the Group); (2) has the current ability to direct the entity's activities that most significantly affects these returns. As of 31 December 2016 and 2015, 100% of net assets of the entity are presented as non-controlling interest in the consolidated statement of financial position.

Recognition of research and development costs

Costs incurred on research and development projects are recognized as intangible assets only when they meet the recognition criteria described in the Group's accounting policies. As of today, no research and development costs have met those recognition criteria. Accordingly, all of the Group's research and development costs to date have been expensed when incurred (Note 25).

Segment information

Management considers that the Group is operating as a single operating business segment. In making this judgment, management has analyzed definition of operating segment under IFRS 8 and concluded that there are no business activities within the Group whose operating results are reviewed and analyzed separately.

Determination of production facilities in Shostka city as a cash-generating unit

Management has concluded that, for the purposes of analyzing the impairment of property, plant and equipment, the production facilities used for manufacturing active pharmaceutical ingredients in Shostka city, Ukraine, should not be treated as a separate cash-generating unit due to the absence of a complete production cycle and active market for the products manufactured in those premises, as well as due to the interrelation of cash flows between the production facilities in Shostka city and Kyiv.

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Key sources of estimation uncertainty

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

Allowance for impairment of accounts receivable

The allowance for impairment of accounts receivable is based on the Group's assessment of the collectability of outstanding amounts. The determination of such estimates requires significant judgment, and takes into consideration the history of losses, the age of the receivable, customer specific facts and circumstances, experience of collecting payments, as well as observable changes in national or local economic conditions that correlate with default on accounts receivable. Such estimates are regularly revised by the Group and, if required, respectively adjusted in the consolidated statement of profit or loss and other comprehensive income in the period when they become known.

Impairment of goodwill

Determining whether goodwill is impaired requires an estimation of the value in use of the cash-generating units to which goodwill has been allocated. The value in use calculation requires that management estimates the future cash flows expected to arise from the cash-generating unit and a suitable discount rate in order to calculate its present value.

As discussed in Note 9, no impairment of goodwill was identified as of 31 December 2016.

Impairment of property, plant and equipment

IFRS require that an entity assess at the end of each reporting period whether there is any indication that assets may be impaired. If any such indication exists, the Company shall estimate the recoverable amount of the asset in order to determine amount of impairment loss (if impairment took place). Evaluation of whether the indications of impairment are present as of the reporting date, including analysis of both internal and external factors, requires that management apply estimates. No impairment has been recognized by the Group in relation to property, plant and equipment, in any of the reporting periods included in consolidated financial statements.

Useful lives of property, plant and equipment

The estimation of the useful life of an item of property, plant and equipment is a matter of management's judgment based upon experience with similar assets. In determining the useful life of an asset, management considers the expected usage, estimated obsolescence, physical deterioration and tear, and the physical environment in which the asset is operated. Changes in any of these conditions or estimates may result in adjustments for future depreciation rates which are accounted for prospectively.

Net realizable value of inventories

In accordance with IAS 2 *Inventories*, inventories are carried at the lower of cost and net realizable value. In assessing net realizable value of inventories, the Group applies different professional judgments in the determination of:

- Estimated selling prices of inventories in the normal course of business, less estimated costs of sales completion; and
- Degree of the subsequent use of inventories.

At each reporting date, the Group assesses the inventories' carrying amounts and, if required, writes down the cost of inventories to their net realizable value (Note 10).

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Measurement of the fair value of contingent consideration

The contingent consideration transferred by the Group within the framework of a business combination is classified as financial liability (Note 18).

In the course of measuring the fair value of the contingent consideration, the Group uses different professional judgments:

- Estimated future revenue of Nord Farm Group;
- Estimated cash flows and achieving the margin of earnings before interest, taxes, depreciation, and amortization (EBITDA) by Nord Farm Group;
- Weighted average probability by all possible performance;
- A discount rate to reflect the time value of money.

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6. PROPERTY, PLANT AND EQUIPMENT

As of 31 December 2016 and 2015, movements in property, plant and equipment were as follows:

| Cost | Land | Buildings and constructions | Machinery and equipment | Vehicles | Office equipment | Other depreciable assets | Capital construction in progress and uninstalled equipment | Total |
|---|--------------|--|--|-----------------|-----------------------------|---|---|------------------|
| As of 31 December 2014 | 962 | 534,987 | 965,399 | 99,741 | 35,180 | 2,834 | 352,288 | 1,991,391 |
| Additions | 3,623 | 26,188 | 85,274 | 23,336 | 8,852 | 779 | 316,098 | 464,150 |
| Reclassifications | - | - | (19,762) | - | 19,762 | - | - | - |
| Internal transfers | - | 11,666 | 89,120 | 1,606 | 1,497 | - | (103,889) | - |
| Disposals | (72) | (3,512) | (3,549) | (1,715) | (1,241) | - | (36) | (10,125) |
| As of 31 December 2015 | 4,513 | 569,329 | 1,116,482 | 122,968 | 64,050 | 3,613 | 564,461 | 2,445,416 |
| Additions | 376 | 25,974 | 160,873 | 56,491 | 22,155 | 2,545 | 115,639 | 384,053 |
| Acquisitions through business combination | - | 1,826 | - | 6,580 | 40 | - | 777 | 9,223 |
| Reclassifications | - | - | (1,056) | - | 1,056 | - | - | - |
| Transfers to investment property | - | - | (682) | - | (39) | - | - | (721) |
| Internal transfers | 572 | 166,723 | 219,573 | 1,669 | 4,492 | 770 | (393,799) | - |
| Effect of foreign currency exchange differences | - | (4) | (4) | 33 | - | - | 15 | 40 |
| Disposals | - | (494) | (1,199) | (5,452) | (1,687) | (48) | (226) | (9,106) |
| As of 31 December 2016 | 5,461 | 763,354 | 1,493,987 | 182,289 | 90,067 | 6,880 | 286,867 | 2,828,905 |

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| | Land | Buildings and constructions | Machinery and equipment | Vehicles | Office equipment | Other depreciable assets | Capital construction in progress and uninstalled equipment | Total |
|--|--------------|-----------------------------------|-------------------------------|-----------------|---------------------|--------------------------------|---|------------------|
| Accumulated depreciation | | | | | | | | |
| As of 31 December 2014 | - | (98,283) | (444,557) | (38,098) | (18,388) | (1,317) | - | (600,643) |
| Depreciation charges | - | (17,747) | (107,678) | (14,608) | (10,845) | (748) | - | (151,626) |
| Reclassifications | - | - | 9,133 | - | (9,133) | - | - | - |
| Disposals | - | 683 | 3,440 | 1,676 | 1,148 | - | - | 6,947 |
| As of 31 December 2015 | - | (115,347) | (539,662) | (51,030) | (37,218) | (2,065) | - | (745,322) |
| Depreciation charges | - | (22,532) | (110,011) | (30,907) | (17,844) | (893) | - | (182,187) |
| Transfers to investment property | - | - | 648 | - | 25 | - | - | 673 |
| Reclassifications | - | - | 398 | - | (398) | - | - | - |
| Effect of foreign currency exchange differences | - | - | - | (19) | - | - | - | (19) |
| Disposals | - | 97 | 1,096 | 3,907 | 1,624 | 46 | - | 6,770 |
| As of 31 December 2016 | - | (137,782) | (647,531) | (78,049) | (53,811) | (2,912) | - | (920,085) |
| Net book value | | | | | | | | |
| As of 31 December 2015 | 4,513 | 453,982 | 576,820 | 71,938 | 26,832 | 1,548 | 564,461 | 1,700,094 |
| As of 31 December 2016 | 5,461 | 625,572 | 846,456 | 104,240 | 36,256 | 3,968 | 286,867 | 1,908,820 |

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As of 31 December 2016, included in capital construction in progress and uninstalled equipment were mainly equipment and construction works in respect of the new plant for production of active pharmaceutical ingredients in Shostka city, Ukraine and construction works and equipment for modernization of current productions in Kyiv. In 2016, the Group put into operation the main part of the new plant in Shostka city and launched the commercial production of active pharmaceutical ingredients in certain areas of the plant.

Pledged assets

As of 31 December 2016 and 2015, the carrying amounts of the Group's property, plant and equipment used as a collateral for loans and borrowings (Note 16) were as follows:

| | 2016 | 2015 |
|-----------------------------|----------------|----------------|
| Buildings and constructions | 312,378 | 312,157 |
| Machinery and equipment | 286,423 | 291,052 |
| Vehicles | 30 | 57 |
| Total | 598,831 | 603,266 |

Fully depreciated assets

Items of machinery and equipment and other fixed assets included in property, plant and equipment of the Group and recorded as of 31 December 2016 at cost in the amount of UAH 163,012 thousand (2015: UAH 143,648 thousand) were fully depreciated but remained in use.

Finance leases

The carrying amounts of vehicles held under finance leases as of 31 December 2016 amounted to UAH 13,192 thousand (2015: UAH 9,714 thousand).

Prepayments for property, plant and equipment

As of 31 December 2016 and 2015, prepayments for property, plant and equipment were represented by prepayments for construction works and equipment for the workshop for production of substances in Shostka city, construction works for reconstruction of workshop #3, and modernization of equipment of main production plants.

7. INTANGIBLE ASSETS

As of 31 December 2016 and 2015, movements in intangible assets were as follows:

| | Software and licenses | Other intangible assets | Intangible assets in progress | Total |
|-------------------------------|-----------------------|-------------------------|-------------------------------|----------------|
| Cost | | | | |
| As of 31 December 2014 | 37,338 | 22,051 | 4,577 | 63,966 |
| Additions | 5,979 | 7,876 | 3,852 | 17,707 |
| Internal transfers | | 252 | (252) | - |
| Disposals | (5,838) | (3) | - | (5,841) |
| As of 31 December 2015 | 37,479 | 30,176 | 8,177 | 75,832 |
| Additions | 14,983 | 5,729 | 31,197 | 51,909 |
| Internal transfers | 1,665 | 7,494 | (9,159) | - |
| Disposals | (700) | (9,312) | - | (10,012) |
| As of 31 December 2016 | 53,427 | 34,087 | 30,215 | 117,729 |

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| | Software and licenses | Other intangible assets | Intangible assets in progress | Total |
|---------------------------------|----------------------------------|--|--|-----------------|
| Accumulated amortization | | | | |
| As of 31 December 2014 | (18,584) | (11,793) | - | (30,377) |
| Amortization charges | (6,132) | (8,600) | - | (14,732) |
| Disposals | 5,833 | - | - | 5,833 |
| As of 31 December 2015 | (18,883) | (20,393) | - | (39,276) |
| Amortization charges | (7,263) | (8,905) | - | (16,168) |
| Disposals | 700 | 9,293 | - | 9,993 |
| As of 31 December 2016 | (25,446) | (20,005) | - | (45,451) |
| Net book value | | | | |
| As of 31 December 2015 | 18,596 | 9,783 | 8,177 | 36,556 |
| As of 31 December 2016 | 27,981 | 14,082 | 30,215 | 72,278 |

Intangible assets in progress comprise costs directly related to acquisition and development of items of intangible assets, including software development in the amount of UAH 16,577 thousand and purchase of drugs dossiers which are in the process of registration in the amount of UAH 13,638 thousand. Intangible assets in progress are neither amortized nor transferred to software and licenses or other intangible assets until they are ready for intended use.

Fully amortized assets

Items of intangible assets recorded as of 31 December 2016 at cost in the amount of UAH 16,762 thousand (2015: UAH 16,835 thousand) were fully amortized but remained in use.

8. ACQUISITION OF SUBSIDIARIES

On 3 February 2016, the Group acquired 100% of shares in KWW Kotkowski Wierzbicki Wegrzyn Sp. z o.o. which, in turn, owned 100% of shares in the companies NORD FARM Sp. z o.o. and ARENAPHARMA Sp. z o.o. (jointly, "Nord Farm Group").

Nord Farm Group is specializing in marketing and sales of pharmaceuticals, biologically active additives and medications in the market of Poland. For the purpose of acquisition a specific entity, Farmak Invest Limited, was established under the laws of Cyprus.

Nord Farm Group was acquired within the framework of further extension of the Group's activities in the area of pharmaceutical distribution.

Consideration transferred

| | Nord Farm Group |
|--|----------------------------|
| Cash | 183,628 |
| Deferred liabilities | 6,901 |
| Contingent consideration arrangement (Note 18) | 69,529 |
| Total | 260,058 |

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Acquired assets and recognized liabilities at the acquisition date

| | Nord Farm Group |
|--|----------------------------|
| Non-current assets | |
| Property, plant and equipment | 9,223 |
| Deferred tax assets | 2,171 |
| Current assets | |
| Inventories | 69,101 |
| Trade and other accounts receivable | 98,669 |
| Prepayments made | 488 |
| Taxes recoverable and prepaid, other than income tax | 4,727 |
| Cash and cash equivalents | 256 |
| Other current assets | 421 |
| Non-current liabilities | |
| Finance lease obligations | (1,433) |
| Deferred tax liabilities | (147) |
| Current liabilities | |
| Loans and borrowings | (15,016) |
| Trade and other accounts payable | (154,732) |
| Income tax payable | (483) |
| Finance lease obligations | (3,703) |
| Taxes payable, other than income tax | (4,336) |
| Total cost of net assets | 5,206 |

Goodwill arising on acquisition

| | Nord Farm Group |
|--|----------------------------|
| Consideration transferred | 260,058 |
| Less: Fair value of identifiable net assets acquired | (5,206) |
| Goodwill arising on acquisition | 254,852 |

Goodwill arose in the acquisition of Nord Farm Group because cost of business combination included a control premium. In addition, the amount paid for business combination effectively included the amounts in relation to the benefit of expected synergies, revenue growth, future market development and the assembled workforce of Nord Farm Group and the Group. These benefits are not recognized separately from goodwill, since they do not meet the recognition criteria for identifiable intangible assets.

No goodwill position arising from these acquisitions is expected to be included in deductible expenses for taxation purposes.

Net cash outflow on acquisition of subsidiaries

| | 2016 |
|---|----------------|
| Consideration paid in cash | 183,628 |
| Less: cash and cash equivalents balances acquired | (256) |
| Total | 183,372 |

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As of 31 December 2016, the initial accounting for business combination has only been provisionally estimated in respect of fair values of assets, liabilities, contingent consideration arrangement, and goodwill.

Impact of acquisitions on the results of the Group

Included in the Group's profit for 2016 was the amount of UAH 554 thousand attributable to the additional business generated by Nord Farm Group. Revenue for the year includes UAH 501,357 thousand in respect of Nord Farm Group.

Had this business combination been effected at 1 January 2016, the Group's revenue would have amounted to UAH 5,156,071 thousand, and profit would have amounted to UAH 677,527 thousand. The management considers these 'pro-forma' numbers to represent an approximate measure of the performance of the combined group on an annualised basis and to provide a reference point for comparison in future periods.

9. GOODWILL

As of 31 December 2016, goodwill was as follows:

| | 2016 |
|---|----------------|
| Cost | 255,905 |
| Accumulated impairment losses | - |
| Cost | 2016 |
| As of 1 January | - |
| Amounts recognized from business combination (Note 8) | 254,852 |
| Effect of foreign exchange differences | 1,053 |
| As of 31 December | 255,905 |

Goodwill has been allocated for impairment testing purposes fully to Nord Farm Group as a separate cash-generating unit.

The recoverable amount of Nord Farm Group is determined based on cash flows projections based on the five-year plan approved by management and the discount rate of 13.31% per annum. Cash flows beyond that five-year period have been extrapolated using a steady 2.50% per annum growth rate. This growth rate does not exceed the long-term average estimated growth rate for the pharmaceutical market in Poland. The management believes that any reasonably possible further change in key assumptions on which recoverable amount is based would not cause the carrying value of the cash-generating unit to exceed its recoverable amount.

The key assumptions used in calculation of the recoverable amount of Nord Farm are as follows:

| | |
|--|---|
| Budgeted revenue | Average revenue for the period immediately before the budget period is increased with reference to estimated further growth at the cost of launch and extension of new product sales. The management expects that the planned average annual revenue growth rate of 8% per year is reasonably achievable. |
| Budgeted gross profit | Average gross profit for the period immediately before the budget period is increased for expected efficiency improvements. The management expects efficiency improvements of 6% per year to be reasonably achievable. |
| Change in procurement prices and inflation rates | Forecasted consumer price indices in Poland and Ukraine during the budget period. Index figures are estimated by management based on the actual data for the period immediately before the budget period and forecasts obtained from external sources for the relevant period. |

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10. INVENTORIES

As of 31 December 2016 and 2015, inventories were as follows:

| | 2016 | 2015 |
|------------------------|----------------|----------------|
| Raw materials | 293,615 | 232,802 |
| Finished goods | 278,450 | 323,114 |
| Packaging materials | 133,049 | 100,860 |
| Merchandise for resale | 82,847 | 1,413 |
| Work in progress | 78,849 | 41,694 |
| Other inventories | 12,737 | 15,141 |
| Total | 879,547 | 715,024 |

Cost of inventories recognized as expense and included in cost of sales (Note 22) for the year ended 31 December 2016 amounted to UAH 1,384,462 thousand (2015: UAH 952,731 thousand).

The amount of inventory write-downs recognized in other operating expense (Note 26) for the year ended 31 December 2016 was UAH 16,007 thousand (2015: UAH 11,680 thousand). Such write-downs relate to raw materials and finished goods and are recognized based on results of stock counts and quality inspections performed by the Group.

In addition, as of 31 December 2016, inventories were used as a collateral to secure for loan agreements for the total amount of UAH 150,833 thousand (Note 16).

11. TRADE AND OTHER ACCOUNTS RECEIVABLE

As of 31 December 2016 and 2015, trade and other accounts receivable were as follows:

| | 2016 | 2015 |
|--|------------------|----------------|
| Trade accounts receivable | 979,590 | 609,045 |
| Other accounts receivable | 94,814 | 11,659 |
| | 1,074,404 | 620,704 |
| Allowance for impairment of accounts receivable | (34,152) | (29,066) |
| Total current trade and other accounts receivable | 1,040,252 | 591,638 |

As of 31 December 2016, trade and other accounts receivable included balances with related parties in the amount of UAH 95,215 thousand (2015: UAH 22,105 thousand) (Note 28).

As of 31 December 2016, other accounts receivable included receivables from the Company's equity holder in the amount of UAH 82,505 thousand.

No interest is charged on trade accounts receivable. The credit period on sales of goods was generally 30-120 days in 2016 (2015: 30-90 days).

As of 31 December 2016 and 2015, the aging analysis of past due but not impaired accounts receivable was as follows:

| | Total | Impaired accounts receivable | Neither past due nor impaired | Past due but not impaired | | | |
|------|------------------|---|--|----------------------------------|-----------------------|------------------------|---------------------------|
| | | | | Up to 3 months | 3-6 months | 6-12 months | Over 12 months |
| 2016 | 1,074,404 | 34,152 | 860,920 | 145,191 | 15,004 | 9,624 | 9,513 |
| 2015 | 620,704 | 29,066 | 564,684 | 17,066 | 9,422 | 401 | 65 |

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Accounts receivable which are past due but not impaired represent the amounts at the end of the reporting period for which the Group has not recognized an allowance for impairment because there has not been a significant change in credit quality, and the amounts are still considered recoverable.

As of 31 December 2016 and 2015, the aging analysis of impaired accounts receivable was as follows:

| | 2016 | 2015 |
|----------------|---------------|---------------|
| 6-12 months | - | 2,350 |
| Over 12 months | 34,152 | 26,716 |
| Total | 34,152 | 29,066 |

Movements in the allowance for impairment of accounts receivable for the years ended 31 December 2016 and 2015 were as follows:

| | 2016 | 2015 |
|--|---------------|---------------|
| As of 1 January | 29,066 | 21,022 |
| Impairment losses recognized in respect of accounts receivable | 4,031 | 5,026 |
| Write-offs of irrecoverable amounts during the year | - | (16) |
| Losses on translation differences | 1,553 | 3,189 |
| Accounts receivable reimbursed | (498) | (155) |
| As of 31 December | 34,152 | 29,066 |

12. PREPAYMENTS MADE

As of 31 December 2016 and 2015, prepayments made were as follows:

| | 2016 | 2015 |
|--|---------------|---------------|
| Prepayments to suppliers for raw materials | 25,266 | 14,442 |
| Prepayments to suppliers for services | 13,664 | 16,804 |
| Deferred expense | 2,779 | - |
| | 41,709 | 31,246 |
| Allowance for impairment of prepayments made | (250) | (297) |
| Total | 41,459 | 30,949 |

As of 31 December 2016, included in prepayments made were balances with related parties in the amount of UAH 6,970 thousand (2015: UAH 6,266 thousand) (Note 28).

13. TAXES RECOVERABLE AND PREPAID, OTHER THAN INCOME TAX

As of 31 December 2016 and 2015, taxes recoverable and prepaid, other than income tax were as follows:

| | 2016 | 2015 |
|-----------------|---------------|---------------|
| VAT recoverable | 42,309 | 69,623 |
| Other taxes | 402 | 79 |
| Total | 42,711 | 69,702 |

Subsequent to the reporting date, the Group received VAT recoverable in the amount of UAH 32,235 thousand.

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14. CASH AND CASH EQUIVALENTS

For the purpose of the consolidated statement of cash flows, cash and cash equivalents consist of cash and short-term bank deposits with the original maturity of up to three months.

As of 31 December 2016 and 2015, cash and cash equivalents were as follows:

| | <u>2016</u> | <u>2015</u> |
|-----------------------------|----------------------|-----------------------|
| Cash on hand and with banks | 36,844 | 107,024 |
| Short-term bank deposits | <u>7,176</u> | <u>75,525</u> |
| Total | <u>44,020</u> | <u>182,549</u> |

Balances of cash with banks earned interest income at floating rates based on daily bank deposit rates. As of 31 December 2016 and 2015, short-term bank deposits were represented by deposits on demand and overnight.

15. SHARE CAPITAL

As of 31 December 2016 and 2015, authorized, registered and fully paid share capital comprised 7,273,200 ordinary shares at a par value of UAH 5 per share. All shares have equal voting rights. The holders of ordinary shares are entitled to receive dividends as declared and to one vote per share at Annual General Shareholders' Meetings.

As of 31 December 2016 and 2015, the carrying amount of the Group's share capital amounted to UAH 57,650 thousand, being the original share capital amount adjusted for the effect of historical hyperinflation under IAS 29 in the amount of UAH 21,284 thousand.

As of 31 December 2016 and 2015, the ownership structure of the Group's share capital was as follows:

| | <u>2016</u> | | <u>2015</u> | |
|--------------------------------------|-----------------------------|----------------------------------|-----------------------------|----------------------------------|
| | <u>Number of shares</u> | <u>Ownership interest, %</u> | <u>Number of shares</u> | <u>Ownership interest, %</u> |
| <i>Immediate shareholders:</i> | | | | |
| FARMAK GROUP N.V. | 4,945,090 | 67.99% | 4,910,153 | 67.51% |
| Individuals (< 2% individually) | 839,078 | 11.54% | 884,673 | 12.16% |
| Foyil Capital Limited | 508,552 | 6.99% | 508,552 | 6.99% |
| Farmak International Holding GmbH | 420,364 | 5.78% | 820,390 | 11.28% |
| LLC "Farmakhim" | 400,026 | 5.50% | - | - |
| Legal entities (< 2% individually) | 135,749 | 1.87% | 114,495 | 1.58% |
| F.I. & P. Holdings Limited | <u>24,341</u> | <u>0.33%</u> | <u>34,937</u> | <u>0.48%</u> |
| Total | <u>7,273,200</u> | <u>100.00%</u> | <u>7,273,200</u> | <u>100.00%</u> |

Dividends

In April 2016, the General Shareholders' Meeting approved distribution of dividends for the year ended 31 December 2015 of UAH 3.03 per share for the total amount of UAH 22,038 thousand. In March 2015, the General Shareholders' Meeting approved distribution of dividends for the year ended 31 December 2014 of UAH 1.88 per share for the total amount of UAH 13,674 thousand.

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Treasury shares repurchased

In November 2016, the Group's subsidiary, LLC "Farmakhim", repurchased shares of PJSC "Farmak" from one of the equity holders of PJSC "Farmak", Farmak International Holding GmbH, in the number of 400,026 shares, which constitutes 5.5% of the Group's share capital. The fair value of treasury shares amounted to UAH 198,058 thousand, and the excess of fair value of treasury shares over their nominal value was recognized directly in equity in the consolidated statement of changes in equity in the amount of UAH 194,887 thousand.

16. LOANS AND BORROWINGS

As of 31 December 2016 and 2015, outstanding loans and borrowings were as follows:

| Secured loans and borrowings: | Currency | Weighted average interest rate | 2016 | Weighted average interest rate | 2015 |
|---|----------|--------------------------------|----------------|--------------------------------|----------------|
| Borrowings from EBRD ¹⁾ | EUR | 5.29% | 398,923 | 4.87% | 412,542 |
| Credit line facilities from Ukrainian banks | USD | 6.43% | 479,909 | 7.39% | 441,242 |
| Loan from a foreign bank | PLN | 3.16% | 9,947 | - | - |
| Borrowing from a related party | EUR | 6.50% | 2,011 | - | - |
| Total loans and borrowings | | | 890,790 | | 853,784 |
| Less: Short-term loans and borrowings and current portion of long-term loans and borrowings | | | (642,520) | | (592,506) |
| Long-term loans and borrowings | | | 248,270 | | 261,278 |

¹⁾ During the year ended 31 December 2016, the Group received a tranche under the loan agreement with the European Bank for Reconstruction and Development ("EBRD") in the amount of EUR 5,000 thousand and made a scheduled repayment of a part of the borrowing in the amount of EUR 6,714 thousand, as a result of which total amounts outstanding under the loan agreement with EBRD as of 31 December 2016 amounted to EUR 14,000 thousand.

Loan agreements with EBRD have established limitations on disposal of assets and distribution of dividends, and other restrictions on the Group's activities. In addition, certain financial covenants are stipulated for under the terms and conditions of those loan agreements. For the years ended 31 December 2016 and 2015, the Group was in compliance with those covenants.

The table below summarizes the Group's loans and borrowings attracted at fixed and floating interest rates as of 31 December 2016 and 2015:

| | 2016 | 2015 |
|-------------------------|----------------|----------------|
| Floating interest rates | 820,802 | 853,784 |
| Fixed interest rates | 69,988 | - |
| Total | 890,790 | 853,784 |

As of 31 December 2016 and 2015, the loans and borrowings were secured by the following types of assets pledged:

| | 2016 | 2015 |
|--|----------------|----------------|
| Property, plant and equipment (Note 6) | 598,831 | 603,266 |
| Finished goods (Note 10) | 150,833 | - |
| Investment property | 30 | 57 |
| Total | 749,694 | 603,323 |

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In addition, as of 31 December 2016, future cash proceeds on sales were used as a collateral under loan agreements for the total amount of UAH 35,000 thousand (2015: UAH 35,000 thousand).

Credit line agreements entered into with domestic banks also establish requirements to certain financial ratios and contain the condition of cross default, when a failure to comply with one debt obligation is treated as default in respect of the other. For the years ended 31 December 2016 and 2015, the Group was in compliance with those covenants and did not breach the condition of cross default.

Undrawn credit line facilities available to the Group as well as contractual maturity profile of the Group's borrowings are disclosed in Note 30.

17. RETIREMENT EMPLOYEE BENEFIT OBLIGATIONS

Reconciliation of present value of retirement and other non-current employee benefit obligations for the years ended 31 December 2016 and 2015 was as follows:

| | 2016 | 2015 |
|---|---------------|---------------|
| Balance at the beginning of the year | 22,502 | 17,409 |
| Including: | | |
| Non-current obligations | 20,331 | 15,890 |
| Current obligations | 2,171 | 1,519 |
| Current service cost | 930 | 863 |
| Interest expense | 4,051 | 2,611 |
| Past service cost | 5,051 | (1,515) |
| Actuarial losses recognized in other comprehensive income | 1,517 | 5,184 |
| Benefits paid during the year | (2,205) | (2,050) |
| Balance at the end of the year | 31,846 | 22,502 |
| Including: | | |
| Non-current obligations | 28,566 | 20,331 |
| Current obligations | 3,280 | 2,171 |

Amounts recognized in profit or loss in respect of defined benefit obligations were as follows:

| | 2016 | 2015 |
|----------------------|---------------|--------------|
| Interest expense | 4,051 | 2,611 |
| Current service cost | 930 | 863 |
| Past service cost | 5,051 | (1,515) |
| Total | 10,032 | 1,959 |

During the year ended 31 December 2016, the Group included in other comprehensive income actuarial losses in the amount of UAH 1,517 thousand (2015: UAH 5,184 thousand).

Key assumptions used for actuarial valuation as of 31 December 2016 and 2015 were as follows:

| | 31 December 2016 | 31 December 2015 |
|-------------------------------|-----------------------------|-----------------------------|
| Discount rate | 18% | 18% |
| Estimated payroll growth rate | 10% | 10% |

To determine a discount rate, management uses market yields on highly liquid corporate bonds adjusted for the estimated effect of differences by maturities. Payroll growth rates are based on management's expectations regarding growth of payroll in the future.

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18. LIABILITIES IN A BUSINESS COMBINATION

As of 31 December 2016, liabilities in a business combination were as follows:

| | 2016 |
|---|---------------|
| Contingent consideration arrangement (Note 8) | 77,587 |
| Deferred liabilities (Note 8) | 7,700 |
| Total | 85,287 |

Under the contingent consideration arrangement within the framework of Nord Farm Group acquisition, the Group is required to pay the sellers an additional amount that will depend on the net sales value of Nord Farm Group for the period from 2016 to 2018 and EBITDA margin for 2018. The amount of this additional payment may be from nil to EUR 5.7 million. Management believes it is highly probable that this payment will be required to be made in 2019. Management recognized the cost of contingent consideration on acquisition in the amount of UAH 69,529 thousand (Note 8) and reassessed the estimated fair value of the liability in the amount of UAH 77,587 thousand as of 31 December 2016 at the discount rate of 10.7%. Other key assumptions regarding future cash flows used by management for the purpose of assessing the contingent consideration are disclosed in Note 31.

Based on purchase agreement of Nord Farm Group, the Group is required to pay the sellers the additional compensation of EUR 300 thousand in 2018, which is non-refundable and not contingent on performance results as described above.

19. TRADE AND OTHER ACCOUNTS PAYABLE

As of 31 December 2016 and 2015, trade and other accounts payable were as follows:

| | 2016 | 2015 |
|--|----------------|----------------|
| Trade accounts payable for: | | |
| Raw materials | 383,244 | 213,053 |
| Services | 119,904 | 44,424 |
| Property, plant and equipment and intangible assets | 15,389 | 39,589 |
| | 518,537 | 297,066 |
| Other accounts payable: | | |
| Payables to employees | 157,884 | 80,428 |
| Accrued liabilities | 34,551 | 29,746 |
| Current portion of retirement and other non-current employee benefit obligations | 3,280 | 2,171 |
| Prepayments received | 1,824 | 136 |
| Dividends payable | 518 | 11,442 |
| Other accounts payable | 6,736 | 4,990 |
| | 204,793 | 128,913 |
| Total | 723,330 | 425,979 |

Trade accounts payable are non-interest bearing and are normally settled within a 30-day period.

As of 31 December 2016, included in trade accounts payable of the Group for raw materials and services were balances with related parties in the amount of UAH 63,054 thousand (2015: UAH 104,146 thousand) (Note 28).

As of 31 December 2016, included in the Group's payables to employees were balances with the Group's key management personnel in the amount of UAH 22,960 thousand (2015: UAH 1,387 thousand) (Note 28).

As of 31 December 2016, included in accrued liabilities were royalties payable to related parties (key management personnel) in the amount of UAH 5,138 thousand (2015: UAH 3,836 thousand) (Note 28).

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20. INCOME TAX EXPENSE

Components of income tax expense for the reporting years ended 31 December 2016 and 2015 comprised the following:

| | 2016 | 2015 |
|---------------------------------|----------------|---------------|
| Current income tax | | |
| Current income tax expense | 144,710 | 71,817 |
| Deferred income tax | | |
| Deferred income tax expense | 8,111 | 18,047 |
| Total income tax expense | 152,821 | 89,864 |

The Group's profit was subject to taxation in Ukraine and Poland. During the year ended 31 December 2016, the Group was subject to corporate income tax at the rate of 18% in Ukraine and 19% in Poland (2015: 18% in Ukraine).

Profit before income tax multiplied by the statutory tax rate and actual income tax expense for the years ended 31 December can be reconciled as follows:

| | 2016 | 2015 |
|--|----------------|----------------|
| Profit before income tax | 830,022 | 495,279 |
| Income tax expense at the statutory tax rates of 18% | 149,404 | 89,150 |
| Effect of non-deductible expenses, net | 3,417 | 714 |
| Total income tax expense | 152,821 | 89,864 |

As of 31 December 2016 and 2015, deferred tax assets and liabilities related to the following:

| | At the end of the year | Reported in consolidated profit or loss | Acquired in a business combination | At the beginning of the year |
|---|-----------------------------------|--|---|---|
| 31 December 2016 | | | | |
| Trade and other accounts receivable | 6,482 | (1,045) | 1,215 | 6,312 |
| Trade and other accounts payable, other non-current liabilities | 5,013 | (341) | 809 | 4,545 |
| Inventories | 1,616 | 832 | - | 784 |
| Property, plant and equipment | 17,196 | (7,557) | - | 24,753 |
| Prepayments made | (142) | - | - | (142) |
| Deferred income tax expense | | (8,111) | | |
| Net deferred tax assets | 30,165 | | 2,024 | 36,252 |
| 31 December 2015 | | | | |
| Trade and other accounts receivable | 6,312 | 3,426 | - | 2,886 |
| Trade and other accounts payable, other non-current liabilities | 4,545 | (10,759) | - | 15,304 |
| Inventories | 784 | (1,495) | - | 2,279 |
| Property, plant and equipment | 24,753 | (9,790) | - | 34,543 |
| Prepayments made | (142) | 571 | - | (713) |
| Deferred income tax expense | | (18,047) | | |
| Net deferred tax assets | 36,252 | | - | 54,299 |

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21. REVENUE

Revenue for the years ended 31 December 2016 and 2015 was as follows:

| | 2016 | 2015 |
|--|------------------|------------------|
| Revenue from sales of finished goods | 4,583,154 | 3,552,022 |
| Revenue from sales of merchandise for resale | 514,824 | 18,767 |
| Other revenue | 14,374 | 7,244 |
| Total | 5,112,352 | 3,578,033 |

For the year ended 31 December 2016, included in revenue from sales of finished goods were sales to related parties in the amount of UAH 26,355 thousand (2015: UAH 15,038 thousand) (Note 28).

22. COST OF SALES

Cost of sales for the years ended 31 December 2016 and 2015 was as follows:

| | 2016 | 2015 |
|--|------------------|------------------|
| Raw materials and supplies | 1,384,462 | 952,731 |
| Cost of merchandise for resale | 335,410 | 11,722 |
| Staff costs | 275,911 | 183,480 |
| Royalties | 114,879 | 87,443 |
| Depreciation and amortization | 110,148 | 99,085 |
| Repairs and maintenance of property, plant and equipment | 81,402 | 58,088 |
| Energy, water and other utilities | 79,571 | 62,647 |
| Other expense | 16,712 | 12,490 |
| Total | 2,398,495 | 1,467,686 |

Royalties

There are two types of royalties accrued by the Group: amounts relating to trademarks and items of intellectual property transferred to the Group by individuals. In the latter instance, such individuals include both current and former employees of the Company as well as third parties. Monthly and quarterly royalty expenses represent a contractually agreed percentage of a corresponding product turnover.

For the year ended 31 December 2016, royalties to the Group's key management personnel amounted to UAH 37,711 thousand (2015: UAH 29,161 thousand) (Note 28).

23. SELLING AND DISTRIBUTION EXPENSES

Selling and distribution expenses for the years ended 31 December 2016 and 2015 were as follows:

| | 2016 | 2015 |
|---|------------------|----------------|
| Marketing and advertising expenses | 466,727 | 345,234 |
| Staff costs | 277,873 | 166,220 |
| Representative office costs | 164,799 | 173,585 |
| Transportation costs | 102,611 | 71,999 |
| Registration fees | 33,071 | 43,769 |
| Depreciation and amortization | 26,651 | 20,688 |
| Maintenance of property, plant and equipment | 10,923 | 5,208 |
| Changes in allowance for impairment and write-offs of accounts receivable | 1,100 | (30) |
| Other expense | 10,547 | 5,377 |
| Total | 1,094,302 | 832,050 |

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Representative office costs for the year ended 31 December 2016 included staff costs related to employees of such representative offices in the amount of UAH 112,097 thousand (2015: UAH 136,092 thousand).

Marketing and advertising expenses for the year ended 31 December 2016 included income tax of non-residents providing advertising services in the amount of UAH 11,136 thousand (2015: UAH 18,214 thousand).

24. GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses for the years ended 31 December 2016 and 2015 were as follows:

| | 2016 | 2015 |
|--|----------------|----------------|
| Staff costs | 296,252 | 207,658 |
| Maintenance of property, plant and equipment | 43,350 | 31,503 |
| Depreciation and amortization | 33,264 | 26,117 |
| Consulting and other professional services | 32,511 | 12,775 |
| Taxes, other than income tax | 21,730 | 10,196 |
| Communication services | 8,637 | 7,310 |
| Bank charges | 7,933 | 7,533 |
| Transportation costs | 4,044 | 1,860 |
| Other expense | 19,512 | 11,716 |
| Total | 467,233 | 316,668 |

Staff costs for the year ended 31 December 2016 included remuneration to the Group's key management personnel in the amount of UAH 78,037 thousand (2015: UAH 43,100 thousand) (Note 28).

25. RESEARCH AND DEVELOPMENT COSTS

Research and development costs of the Group for the years ended 31 December 2016 and 2015 were represented by: preclinical and clinical trials related to generic drugs; and preclinical and clinical trials in respect of a self-developed drugs.

26. OTHER OPERATING EXPENSE

Other operating expense for the years ended 31 December 2016 and 2015 was as follows:

| | 2016 | 2015 |
|---|---------------|---------------|
| Charity and donations | 16,993 | 14,171 |
| Loss on write down of raw materials and finished goods (Note 10) | 16,007 | 11,680 |
| Change in fair value of contingent consideration | 7,523 | - |
| Fines and penalties | 1,297 | 637 |
| Net (profit)/loss on disposal of property, plant and equipment and intangible assets, net | (973) | 2,194 |
| Change in allowance for impairment and write-offs of accounts receivable | (276) | 5,268 |
| Other expense | 240 | 87 |
| Total | 40,811 | 34,037 |

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27. FINANCE COSTS

Finance costs for the years ended 31 December 2016 and 2015 were as follows:

| | 2016 | 2015 |
|---|---------------|---------------|
| Interest expense on loans and borrowings | 58,578 | 48,395 |
| Finance lease costs | 2,009 | 3,462 |
| Other expense | 5,567 | 3,787 |
| Less: Amounts included in initial cost of qualifying assets | (15,674) | (26,596) |
| Total | 50,480 | 29,048 |

For qualifying assets, the weighted average capitalization rate of the funds borrowed during the year ended 31 December 2016 amounted to 7.27% (2015: 7.24%).

28. RELATED PARTY DISCLOSURES

The Group's transactions with its related parties for the years ended 31 December 2016 and 2015 were as follows:

| | Revenue from sales of finished goods | Rental income | Purchase of raw materials and supplies | Purchase of services |
|--|---|----------------------|---|---------------------------------|
| 2016 | | | | |
| Entities under common control | - | 792 | (469,161) | (66,533) |
| Associate | 14,216 | - | - | (275) |
| Other related parties (family members of ultimate controlling party) | 12,139 | 512 | (13,794) | (11,084) |
| Total | 26,355 | 1,304 | (482,955) | (77,892) |
| 2015 | | | | |
| Entities under common control | - | 1,038 | (325,060) | (49,479) |
| Associate | 12,255 | - | - | - |
| Other related parties (family members of ultimate controlling party) | 2,783 | 633 | (14,333) | (16,789) |
| Total | 15,038 | 1,671 | (339,393) | (66,268) |

Revenue from sales of finished goods to entities under common control and associate comprised revenue from sales of pharmaceuticals produced by the Group. Sales to related parties were performed on market terms.

Purchases of raw materials and supplies from entities under common control mainly comprised purchases of raw and packaging materials. Purchases of services from entities under common control comprised mainly royalties, purchases of repair and construction services.

Charities to other related parties for the year ended 31 December 2016 amounted to UAH 11,349 thousand (2015: UAH 10,970 thousand).

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As of 31 December 2016 and 2015, the Group's outstanding balances with its related parties were as follows:

| | Trade and other accounts receivable | Prepayments made | Trade and other accounts payable |
|---|--|-----------------------------|---|
| 2016 | | | |
| Entities under common control | 83,050 | - | 60,862 |
| Associate | 3,505 | - | - |
| Other related parties (family members of ultimate controlling party) | 8,660 | 6,970 | 2,192 |
| Total | 95,215 | 6,970 | 63,054 |
| 2015 | | | |
| Entities under common control | 651 | - | 101,300 |
| Associate | 9,513 | - | - |
| Other related parties (family members of ultimate controlling party) | 11,941 | 6,266 | 2,846 |
| Total | 22,105 | 6,266 | 104,146 |

As of 31 December 2016, trade and other accounts receivable from entities under common control included the amount of UAH 82,505 thousand due from the Company's equity holder, Farmak International Holding GmbH.

Treasury shares repurchased

During the year ended 31 December 2016, the Group repurchased 5.5% of own shareholder's capital from one of the Company's equity holders (Note 15).

Transactions and balances with the Group's key management personnel

Key management personnel of the Group consists of the Company's General Director and members of the Board of Directors. Key management personnel totaled to 11 persons as of 31 December 2016 and 2015.

The Group's transactions with its key management personnel for the years ended 31 December 2016 and 2015 were as follows:

| | 2016 | 2015 |
|--|----------------|---------------|
| Short-term benefits, including: | | |
| Remuneration and related taxes | 78,037 | 43,100 |
| Royalties | 37,711 | 29,161 |
| Total | 115,748 | 72,261 |

As of 31 December 2016 and 2015, the Group's outstanding balances with its key management personnel were as follows:

| | 2016 | 2015 |
|---|---------------|--------------|
| Royalties accrued | 5,138 | 3,836 |
| Payables for remuneration and related taxes | 22,960 | 1,387 |
| Loans granted | (47) | (61) |
| Total | 28,051 | 5,162 |

As of 31 December 2016, some members of key management personnel were entitled to post-employment defined benefit plans according to their employment contracts. The amounts of such benefits as of 31 December 2016 in the amount of UAH 25,647 thousand were included in retirement and other employee benefit obligations (2015: UAH 16,683 thousand).

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29. CONTINGENCIES AND CONTRACTUAL COMMITMENTS

Taxation

Ukraine's tax environment is characterized by complexity in tax administering, arbitrary interpretation by tax authorities of tax laws and regulations that, inter alia, can increase fiscal pressure on tax payers. Inconsistent application, interpretation, and enforcement of tax laws can lead to litigation which, as a consequence, may result in the imposition of additional taxes, penalties, and interest, and these amounts could be material. Facing current economic and political issues, the Government has implemented certain reforms in the tax system of Ukraine by adopting the Law of Ukraine "On Amending the Tax Code of Ukraine and Certain Laws of Ukraine" which is effective from 1 January 2015, except for certain provisions which take effect at a later date.

Most significant changes to the Tax Code concern a revision of rules governing the payment of Value Added Tax ("VAT"), a revision of rules on computation of corporate income tax, and introduction of real estate (property) tax, in the following way:

- According to the Law, the output VAT to be paid to tax authorities is based on the supply of goods or services, net of input VAT if this VAT is determined to have been paid to tax authorities by the Company's suppliers. Also, the minimal tax base for VAT input on goods and services purchased was introduced and special VAT accounts for every taxpayer to be opened at the State Treasury of Ukraine for the VAT purposes. The purpose of these special VAT accounts is to guarantee fulfilment of VAT liabilities by the taxpayers.
- It has significantly changed general rules for assessment of an item of taxation, as well as terms and procedures for submission of tax returns. In accordance with the Tax Code requirements, the item of taxation shall be determined based on the profit before income tax (upon certain adjustments) as defined in the taxpayer's financial statements submitted to the tax authorities together with the tax returns. However, the Tax Code has not regulated a rather broad range of transactions arising from the need to reflect in tax reports intermediary balances accounted for in the Group's consolidated financial statements as of 31 December 2014. Such an uncertainty may refer to estimation and reflection of accruals, collaterals, and allowances for impairment losses, which, in turn, may result in assessment of additional tax liabilities, fines, and penalties, if tax authorities challenge certain interpretations based on the Group's management's estimates. The Group's management believes it has accrued all effective taxes based on its interpretation of the tax legislation.
- A new real estate (property) tax was introduced which is to be levied based on the floor area of the Group's buildings (subject to certain reliefs).

Management believes that the Group has been in compliance with all requirements of the effective tax legislation and currently is assessing the possible impact of the introduced amendments.

According to the Group's management, future tax examinations could raise issues or assessments, which are contrary to the Group's tax filings and could lead to additional taxes, fines and penalties. Management of the Group believes that its interpretation of the relevant legislation is appropriate and that the Group has complied with all regulations and accrued or paid all taxes and withholdings that are applicable. At the same time, in the event of the contrary treatment of such transactions by tax authorities, the Group's management assessed the amount of potential contingent tax liabilities in respect of tax accounting of deductible expenses as of 31 December 2016 and 2015 to be immaterial for the purposes of these consolidated financial statements. Most tax returns of the Group for the period ended 31 December 2009 were examined by tax authorities without significant disagreements or imposition of additional tax liabilities.

In accordance with the effective legislation, tax returns are subject to examination within three years after their submission. The risk of additional tax assessments as a result of recurring tax audits significantly decreases with the passage of time.

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Transfer pricing

The Group imports goods and purchases services which may potentially be in the scope of the new Ukrainian transfer pricing ("TP") regulations. The Group submitted the controlled transaction report for the year ended 31 December 2015 within the required deadline. Management believes that the Group prepared all necessary documentation on controlled transactions for the year ended 31 December 2015 as required by the legislation and continues preparing them for the year ended 31 December 2016. The report on controlled transactions for the year ended 31 December 2016 shall be prepared by the Company by 1 October 2017.

Management believes that the Group is in compliance with TP requirements. As the practice of implementation of the new transfer pricing rules has not yet developed and wording of some clauses of the rules may be subject to various interpretations, the impact of challenge of the Group's transfer pricing positions by the tax authorities cannot be reliably estimated.

Legal issues

In the ordinary course of business, the Group is subject to legal actions and complaints. Management of the Group believes that the ultimate liability, if any, arising from such legal actions or complaints, will not have a material effect on the consolidated financial position or results of future operations of the Group.

Capital expenditure commitments

As of 31 December 2016, the Group had outstanding commitments in respect of purchases of property, plant and equipment for the total amount of UAH 116,882 thousand (2015: UAH 122,854 thousand).

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's financial instruments comprise cash and cash equivalents, trade and other accounts receivable, investments in associate, loans and borrowings, finance lease obligations, trade and other accounts payable.

The Group did not enter into any derivative transactions. The Group's overall risk management program focuses on the unpredictability and inefficiency of the Ukrainian financial markets and seeks to minimize potential adverse effects on the consolidated financial position of the Group.

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

Market risk

The Group's activities primarily expose to the financial risks of changes in foreign currency exchange rates and interest rates. Market risk exposures are measured using sensitivity analysis which evaluates the impact of a reasonably possible change in interest or foreign currency rates during a year.

Foreign currency risk

Foreign currency risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign currency exchange rates.

The Group's exposure to foreign currency risk is mainly attributed to the exchange rate fluctuations of UAH against USD, EUR and RUB experienced by Ukraine-based entities of the Group.

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The official exchange rates of UAH against the above mentioned currencies, as established by the National Bank of Ukraine as of the respective dates, were as follows:

| | EUR | USD | RUB |
|------------------------|---------|---------|--------|
| As of 31 December 2016 | 28.4226 | 27.1909 | 0.4511 |
| As of 31 December 2015 | 26.2231 | 24.0007 | 0.3293 |

As of the reporting dates, the carrying amounts of the foreign currency denominated monetary assets and liabilities of Ukraine-based entities of the Group were as follows:

| | USD | | RUB | | EUR | |
|---------------------------------------|------------------|------------------|---------------|---------------|------------------|------------------|
| | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 |
| Financial assets | | | | | | |
| Cash and cash equivalents | 11,824 | 82,310 | - | 95 | 2,324 | 2,176 |
| Trade and other accounts receivable | 245,597 | 105,268 | 61,843 | 28,777 | 13,377 | 20,426 |
| Total financial assets | 257,421 | 187,578 | 61,843 | 28,872 | 15,701 | 22,602 |
| Financial liabilities | | | | | | |
| Loans and borrowings | 479,909 | 441,242 | - | - | 400,827 | 412,542 |
| Finance lease obligations | 13,056 | 6,215 | - | - | - | - |
| Trade and other accounts payable | 73,778 | 92,999 | 3,894 | 6,205 | 137,818 | 82,501 |
| Liabilities in a business combination | - | - | - | - | 85,287 | - |
| Total financial liabilities | 566,743 | 540,456 | 3,894 | 6,205 | 623,932 | 495,043 |
| Total net position | (309,322) | (352,878) | 57,949 | 22,667 | (608,231) | (472,441) |

Short-term and long-term loans and borrowings, cash and cash equivalents, trade and other accounts receivable and payable, and finance lease obligations denominated in foreign currency give rise to the Group's foreign exchange exposures. The Group has not entered into transactions designed to hedge these foreign currency risk exposures.

The following table details the Group's sensitivity to a 25% increase in UAH exchange rate against relevant foreign currencies, with all other variables remaining unchanged. 25% is the sensitivity rate used when reporting foreign currency risk internally to key management personnel and represents management's assessment of the reasonably possible change in foreign exchange rates. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the period end for a 25% change in foreign currency exchange rates. A positive value below indicates an increase in profit before income tax where UAH devaluates by 25% against the relevant currency. A negative value below indicates a decrease in profit before income tax where UAH devaluates by 25% against the relevant currency. For a 25% appreciation of UAH against the relevant currency, there would be an equal and opposite impact on profit before income tax as the amounts noted per the devaluation.

| 2016 | Devaluation of UAH | Effect on profit before income tax |
|---------|--------------------|------------------------------------|
| UAH/EUR | 25.00% | (152,058) |
| UAH/USD | 25.00% | (77,331) |
| UAH/RUB | 25.00% | 14,487 |

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| 2015 | Devaluation of UAH | Effect on profit before income tax |
|-------------|-------------------------------|---|
| UAH/EUR | 50.00% | (236,221) |
| UAH/USD | 50.00% | (176,439) |
| UAH/RUB | 50.00% | 11,334 |

Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Group's exposure to market risk for changes in interest rates relates primarily to the Group's borrowings with floating interest rates. Management monitors the market interest rates with sufficient regularity to minimize the Group's exposure to interest rate risk.

The sensitivity analysis below have been determined based on the exposure to interest rates at the end of the reporting period. For floating rate liabilities, the analysis is prepared assuming the amount of the liability outstanding at the end of the reporting period was outstanding for the whole year. A 100 basis points increase or 25 basis points decrease is used when reporting interest rate risk internally to key management personnel and represents management's assessment of the reasonably possible change in interest rates.

The following table details impact on profit before income tax if interest rates change and all other variables remain constant.

| 2016 | Increase/ (decrease) in basis points | Effect on profit before income tax |
|---------------------------------|---|---|
| Change in interest rate EURIBOR | 100 | (3,989) |
| Change in interest rate EURIBOR | (25) | 997 |
| Change in interest rate LIBOR | 100 | (4,119) |
| Change in interest rate LIBOR | (25) | 1,030 |
| 2015 | Increase/ (decrease) in basis points | Effect on profit before income tax |
| Change in interest rate EURIBOR | 100 | (4,125) |
| Change in interest rate EURIBOR | (25) | 1,031 |
| Change in interest rate LIBOR | 100 | (4,412) |
| Change in interest rate LIBOR | (25) | 1,103 |

Liquidity risk

Liquidity risk is the risk that the Group will not be able to settle all liabilities as they are due. The Group's objective is to maintain balance between continuity and flexibility of funding through the use of credit terms provided by suppliers and banks.

The Group analyzes the aging of its assets and the maturity of its liabilities and plans its liquidity depending on the expected repayment terms of the respective financial instruments. In instances of insufficient or excessive liquidity in individual entities, the Group relocates resources and funds among the Group entities to achieve optimal financing of the business needs of each entity.

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The table below summarizes the original contractual maturity profile of the Group's financial liabilities as of 31 December 2016 and 2015 based on undiscounted payments:

| 2016 | Weighted average effective interest rate | On demand | Up to 3 months | From 3 to 6 months | From 6 to 12 months | From 1 to 5 years | Total |
|---|---|----------------------|---------------------------|-------------------------------|--------------------------------|------------------------------|------------------|
| Loans and borrowings | 6.18% | - | 484,951 | 59,353 | 116,543 | 258,138 | 918,985 |
| Finance lease obligations | 24.64% | - | 2,563 | 2,257 | 4,273 | 13,328 | 22,421 |
| Trade and other accounts payable | n/a | 171,420 | 532,984 | 849 | 16,253 | - | 721,506 |
| Retirement and other employee benefit obligations | n/a | - | - | - | - | 28,566 | 28,566 |
| Liabilities in a business combination | n/a | - | - | - | - | 85,287 | 85,287 |
| Guarantees issued | n/a | - | 52 | 52 | 104 | 2,237 | 2,445 |
| Total | | 171,420 | 1,020,550 | 62,511 | 137,173 | 387,556 | 1,779,210 |
| 2015 | Weighted average effective interest rate | On demand | Up to 3 months | From 3 to 6 months | From 6 to 12 months | From 1 to 5 years | Total |
| Loans and borrowings | 7.21% | - | 486,278 | 42,022 | 82,675 | 274,999 | 885,974 |
| Finance lease obligations | 24.25% | - | 4,489 | 2,876 | - | - | 7,365 |
| Trade and other accounts payable | n/a | 136,412 | 270,789 | 6,456 | 12,186 | - | 425,843 |
| Retirement and other employee benefit obligations | n/a | - | - | - | - | 20,331 | 20,331 |
| Liabilities in a business combination | n/a | - | - | - | - | 1,085 | 1,085 |
| Guarantees issued | n/a | - | 48 | 8,214 | 97 | 2,305 | 10,664 |
| Total | | 136,412 | 761,604 | 59,568 | 94,958 | 298,720 | 1,351,262 |

The amounts included above for guarantees issued are the maximum amounts the Group could be forced to repay under the arrangement for the full guaranteed amount if that amount is claimed by the counterparty under the guarantee agreement.

The Group has access to credit line facilities, of which UAH 268,918 thousand were undrawn as of 31 December 2016 (2015: UAH 380,341 thousand).

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Credit risk

Credit risk is the risk that counterparty will not meet its obligations under a financial instrument or customer contract leading to a financial loss to the Group. Financial instruments which potentially subject the Group to significant concentrations of credit risk consist principally of cash and cash equivalents and trade accounts receivable. The Group's maximum exposure to credit risk as of 31 December 2016 amounted to UAH 994,458 thousand (2015: UAH 767,928 thousand).

The Group's cash and cash equivalents are primarily held with major reputable banks located in Ukraine. Management carries out continuous monitoring of the financial position in respect of the financial institutions where the Group's cash and cash equivalents are placed. The credit risk for the Group relates to the default of banks on their obligations and is limited to the balance of cash and cash equivalents placed with banks.

The Group mainly trades with reputable and credit-worthy customers both in the domestic and export markets. It is the Group's policy that all customers who wish to trade on credit terms are subject to credit verification procedures. Furthermore, in 2012, the Group implemented additional procedure for monitoring of customers' financial information on a quarterly basis. Other exposures are monitored and analyzed on a case-by-case basis and the Group's management believes that credit risk is appropriately reflected in impairment allowances recognized against assets.

Revenue after deduction of discounts and rebates from the Group's top six customers in 2016 amounted to UAH 2,736,772 thousand (2015: UAH 2,185,507 thousand), with the balances on settlements with those customers as of 31 December 2016 amounting to UAH 400,692 thousand (2015: UAH 354,677 thousand).

The Group has no significant credit risk exposure to any of its counterparties. Concentration of credit risk in respect of any counterparty did not exceed 14% of the total amount of monetary assets during the year.

In addition, the Group is exposed to credit risk in relation to financial guarantees provided by the Group. The Group's maximum exposure in this respect is the maximum amount the Group could have to pay if the guarantee is called on.

Capital management

The Group considers debt and shareholders' equity as primary sources of funding. The Group's objectives, when managing capital, are to ensure the Group's ability to provide returns to the shareholders and benefits to other stakeholders as well as to provide for financing of the Group operations. The Group's capital management policies aim to ensure and maintain an optimal capital structure to reduce the overall costs of capital raising and flexibility relating to the Group's access to capital markets.

| | 2016 | 2015 |
|-------------------------------------|------------------|------------------|
| Loans and borrowings (Note 16) | 890,790 | 853,784 |
| Finance lease obligations | 18,117 | 6,215 |
| Cash and cash equivalents (Note 14) | (44,020) | (182,549) |
| Net debt | 864,887 | 677,450 |
| Total equity | 2,583,131 | 2,130,535 |
| Equity and net debt | 3,448,018 | 2,807,985 |
| Gearing ratio | 25.1% | 24.1% |

Management monitors the Group's capital structure on a regular basis and may adjust its capital management policies and objectives following changes in the operating environment, market trends or its development strategy.

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31. FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value represents the amount at which the instrument could be exchanged between knowledgeable willing participants in an arm's length transaction, other than in a forced or liquidation sale.

Except as detailed in the following table, management of the Group considers that the carrying amounts of financial assets and liabilities recognized in the consolidated financial statements approximate their fair values:

| | Carrying amounts | | Fair value | |
|--|------------------|---------|------------|---------|
| | 2016 | 2015 | 2016 | 2015 |
| Financial liabilities (current and non-current) | | | | |
| Loans and borrowings | 890,790 | 853,784 | 892,369 | 857,085 |
| Finance lease obligations | 18,117 | 6,215 | 15,034 | 6,577 |

Fair values of the financial instruments presented above correspond to Level 2 of fair value hierarchy and have been determined by discounting future contractual cash flows at the year-end market interest rates available to the Group for similar financial instruments. Future cash flows are measured, directly or indirectly, on the basis of observable inputs. The measurements use one or more observable quoted prices in the markets considered to be active.

Contingent consideration

The fair value of contingent consideration has been determined using average weighted probabilities for all possible performance outcomes. To reflect the time value of money, the liability has been discounted using the discount rate of 10.7%. Changes in the fair value that occurred due to changes in estimated net sales value and EBITDA margin are included in other operating expense in the consolidated statement of profit or loss and other comprehensive income.

Change in fair value

| | Contingent consideration |
|--|-------------------------------------|
| 31 December 2016 | |
| Opening balance | - |
| Acquisition | 69,529 |
| Change in fair value | 7,523 |
| Effect of foreign exchange differences | 535 |
| At the end of the year | 77,587 |

32. SUBSEQUENT EVENTS

Before these consolidated financial statements were authorized for issue, the Group had no subsequent events that would require disclosures.

33. APPROVAL OF THE CONSOLIDATED FINANCIAL STATEMENTS

These consolidated financial statements were approved by management and authorized for issue on 20 April 2017.