

INDEPENDENT AUDITOR’S REPORT TO THE MEMBERS OF POLYMETAL INTERNATIONAL PLC

OPINION ON FINANCIAL STATEMENTS OF POLYMETAL INTERNATIONAL PLC

In our opinion:



- the financial statements give a true and fair view of the state of the Group’s affairs as at 31st December 2016 and of its profit for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union; and
- have been properly prepared in accordance with the Companies (Jersey) Law, 1991.

The financial statements that we have audited comprise:

- the Consolidated Income Statement;
- the Consolidated Statement of Comprehensive Income;
- the Consolidated Balance Sheet;
- the Consolidated Statement of Cash Flows;
- the Consolidated Statement of Changes in Equity;
- the Significant accounting policies; and
- the related Notes 1 to 34.

The financial reporting framework that has been applied in their preparation is applicable law and IFRSs as adopted by the European Union.

SUMMARY OF OUR AUDIT APPROACH





Key risks	<div>The key risks that we identified in the current year were:<ul style="list-style-type: none">Recoverability of operating and development assets and goodwillRecoverability of exploration and evaluation assetsValuation and existence of metal inventoriesAccounting for and valuation of acquisitionsWithin this report, any new risks are identified with  and any risks which are the same as the prior year identified with .</div>
Materiality	The materiality that we used in the current year was US\$21 million, which was determined on the basis of 4% of Profit before tax, adjusted for net foreign exchange gains and losses.
Scoping	Our audit scope focused primarily on nine key reportable segments (Voro, Okhotsk, Dukat, Omolon, Varvara, Amursk/Albazino, Mayskoye, Kyzyl and Armenia) and the corporate entities such that 100% of revenue (2015: 100%) and 97% of total assets (2015: 97%) were subject to a full scope audit, which is consistent with last year’s approach.
Significant changes in our approach	The Group completed two acquisitions in the year (Kapan and Komar) and the accounting for these involves management judgement and has been included as a new key risk in the current year.

GOING CONCERN AND THE DIRECTORS’ ASSESSMENT OF THE PRINCIPAL RISKS THAT WOULD THREATEN THE SOLVENCY OR LIQUIDITY OF THE GROUP.

<div>We have reviewed the directors’ statement regarding the appropriateness of the going concern basis of accounting contained within Note 1 to the financial statements and the directors’ statement on the longer-term viability of the Group, contained within the Directors’ report on page 100.</div> <div>We are required to state whether we have anything material to add or draw attention to in relation to:<ul style="list-style-type: none">the Directors’ confirmation on page 100 that they have carried out a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity;the disclosures on pages 66-69 that describe those risks and explain how they are being managed or mitigated;the Directors’ statement in Note 1 to the financial statements about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them and their identification of any material uncertainties to the Group ability to continue to do so over a period of at least twelve months from the date of approval of the financial statements; andthe Directors’ explanation on page 100 as to how they have assessed the prospects of the Group, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.</div>	<div>We confirm that we have nothing material to add or draw attention to in respect of these matters.</div> <div>We agree with the Directors’ adoption of the going concern basis of accounting and we did not identify any such material uncertainties. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the Company’s ability to continue as a going concern.</div>
<div>Independence We are required to comply with the Financial Reporting Council’s Ethical Standards for Auditors and confirm that we are independent of the Company and we have fulfilled our other ethical responsibilities in accordance with those standards.</div>	We confirm that we are independent of the Group and we have fulfilled our other ethical responsibilities in accordance with those standards. We also confirm we have not provided any of the prohibited non-audit services referred to in those standards.

OUR ASSESSMENT OF RISKS OF MATERIAL MISSTATEMENT

The assessed risks of material misstatement described below are those that had the greatest effect on our audit strategy, the allocation of resources in the audit and directing the efforts of the engagement team.

Recoverability of operating and development assets and goodwill (Notes 18 and 19 and Page 80 of the Audit and Risk Committee Report) 	
<div>Risk description </div>	<div>As a consequence of continued volatility in gold and silver prices, foreign exchange rates and the political and economic uncertainties in Russia, the assessment of recoverability of the operating and development assets (carried at US\$1,625 million) and goodwill (carried at US\$17 million) remains a key judgment.</div> <div>Management has assessed whether any indicators of impairment, or impairment reversal, existed at its nine cash generating units (‘CGUs’) (as set out in Note 5) and development projects. Where goodwill is allocated to that CGU (at Dukat and Mayskoye), management performed formal impairment testing as at 31 December 2016 to assess whether the recoverable amount of the CGU exceeds its net book value.</div>
<div>How the scope of our audit responded to the risk </div>	<div>We challenged management’s assessments as to whether indicators of impairment (or impairment reversal) exist for the Group’s CGUs and development projects through critical assessment of developments in the wider economic environment and the performance of each of the CGUs in the year and through meetings with local and Group operational management.</div> <div>Where such indicators were identified, and for the CGUs with goodwill allocated to them, we obtained the valuation models used to determine the recoverable amount of those CGUs. We challenged the assumptions underpinning the models, including the discount rate used, the expected commodity prices, capital and operating expenditure forecasts, production profiles and foreign exchange rates. This was achieved by comparison to third party documentation, the review of reserves and resources reports, consultation with Deloitte specialists (to assess critically the discount rate applied), discussions with operational management and sensitivity analyses. We assessed whether assumptions had been determined and applied consistently across the Group.</div> <div>We assessed management’s ability to forecast accurately by comparing their 2016 forecasts to 2016 actual financial results.</div>
<div>Key observations </div>	No impairments or impairment reversals were identified in the current year.

INDEPENDENT AUDITOR’S REPORT TO THE MEMBERS OF POLYMETAL INTERNATIONAL PLC CONTINUED

Recoverability of exploration and evaluation assets	
(Notes 3 and 18 and Page 80 of the Audit and Risk Committee Report)	
<div>Risk description</div> <div></div>	<div>At 31 December 2016, the Group held US\$140 million in respect of exploration and evaluation (E&E assets). Recoverability is dependent on the expected future success of exploration activities. E&E expenditure is capitalised once it has been determined that the mineral property can be developed economically. The evaluation of each asset’s future prospects requires significant judgement.</div>
<div>How the scope of our audit responded to the risk</div> <div></div>	<div>We reviewed and challenged management’s assumptions used in assessing the recoverability of the Group’s exploration and evaluation assets. We assessed the recoverability of assets by meeting with operational management to discuss material E&E assets, reviewing drilling and other testing results in the year and confirming future development plans. We reviewed licence conditions to ensure there were no breaches of key terms. We reviewed Board-approved budgets for 2017 to check that specific exploration project spend was committed and we performed detailed testing to assess the validity of costs capitalised in the year.</div>
<div>Key observations</div> <div></div>	<div>No additional impairments of E&E assets were identified from the work performed.</div>
Valuation and Existence metal inventories	
(Note 21 and Page 80 of the Audit and Risk Committee Report)	
<div>Risk description</div> <div></div>	<div>At 31 December 2016 the Group held US\$395 million in respect of metal inventories on the Balance Sheet. Management’s determination of the contained metal levels in ore stockpiles and work in progress involves the use of sampling techniques and related valuation models. The assessment of the recoverability of metal inventories requires judgement both in the calculation of expected costs to process and refine ore stock piles to produce concentrate or doré for sale, and in estimating future prices to be realised on sale.</div>
<div>How the scope of our audit responded to the risk</div> <div></div>	<div>We tested the existence of metal inventories through attending inventory counts performed by management’s experts and assessing the controls surrounding measuring the net realisable value of the inventory at a sample of operating locations and performing roll forward testing from the count dates through to year end by testing management’s metal inventory models. We assessed management’s experts’ methodology, expertise and objectivity. We tested the recoverability of metal inventories through the recalculation of projected net realisable values based on expected commodity prices (which were consistent with prices used in the Group’s property, plant and equipment and goodwill impairment calculations) and costs to complete. We also performed substantive analytical procedures on management’s inventory costing calculations. We tested inventories for obsolescence by reviewing management’s strategic mine plans and assessing whether there is appropriate provisioning in place, in particular where stockpiles are no longer expected to be used.</div>
<div>Key observations</div> <div></div>	<div>No additional write-downs of metal inventories were identified from the work performed.</div>
Accounting for and valuation of acquisitions	
(Note 4 and Page 80 of the Audit and Risk Committee Report)	
<div>Risk description</div> <div></div>	<div>The appropriate accounting treatment of acquisitions which have completed during 2016 (Kapan in Armenia for US\$38 million and Komar in Kazakhstan for US\$120 million) is a key judgement, specifically in respect of determining whether each of the acquisitions is a business combination or an asset acquisition, and estimating the fair value of the contingent consideration. The key judgements and inputs to determination of the fair value of the deferred contingent consideration include expected commodity prices, production profiles and the discount rates applied.</div>
<div>How the scope of our audit responded to the risk</div> <div></div>	<div>We challenged management’s assessment of whether the acquisitions meet the definition of a business under IFRS 3 Business combinations. We challenged management’s key assumptions underpinning the contingent consideration liability models through critical assessment of key inputs within the model. On Komar, we involved our internal valuation specialists to test the output of the Monte-Carlo model used.</div>
<div>Key observations</div> <div></div>	<div>We are satisfied that both acquisitions had been accounted for appropriately. We found that the assumptions used by management in the valuation of the deferred contingent consideration were reasonable.</div>

These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

OUR APPLICATION OF MATERIALITY

We define materiality as the magnitude of misstatement in the financial statements that makes it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced. We use materiality both in planning the scope of our audit work and in evaluating the results of our work.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

Materiality	US\$21 million (2015: US\$16 million).
Basis for determining materiality	4% (2014: 4%) of Profit before tax, adjusted for net foreign exchange gains and losses.
Rationale for the benchmark applied	Pre-tax profit is adjusted to exclude net foreign exchange gain and losses recognised which would, if included, significantly distort materiality year on year. In our professional judgement, we believe that the use of an adjusted profit measure is appropriate as the amounts which have been excluded from the Group’s profit before tax which would otherwise distort the level of materiality determined and are not reflective of the Group’s trading activity.

We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of US\$420,000 (2015: US\$320,000), as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the Audit Committee on disclosure matters that we identified when assessing the overall presentation of the financial statements.

AN OVERVIEW OF THE SCOPE OF OUR AUDIT

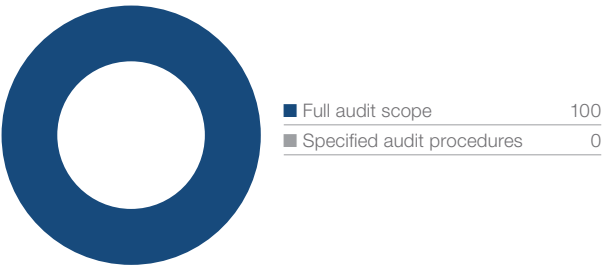
Our Group audit was scoped by obtaining an understanding of the Group and its environment, including Group-wide controls and assessing the risks of material misstatement across the Group. Our audit scope focused primarily on nine key reportable segments (Voro, Okhotsk, Dukat, Omolon, Varvara, Amursk/Albazino, Mayskoye, Kyzyl and Armenia) and the corporate entities such that 100% of revenue (2015: 100%) and 97% of total assets (2015: 97%) were subject to a full scope audit, which is consistent with last year’s approach.

At the parent entity level we also tested the consolidation process and carried out analytical procedures to confirm our conclusion that there were no significant risks of material misstatement in the aggregated financial information of the remaining components not subject to audit.

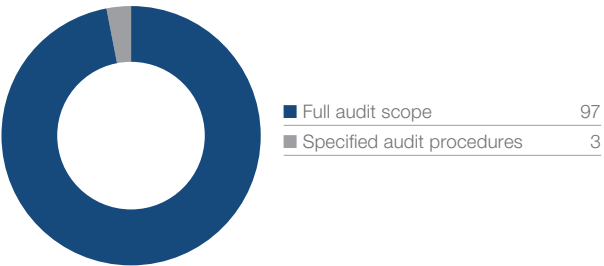
The group audit team was involved in the work of the component auditors at all stages of the audit process. The signing partner and senior members of the Group engagement team visited the head office in St. Petersburg on multiple occasions in the year and continued to follow a programme of regular planned visits to the Group’s other business units. The Group audit team directed and reviewed in detail the work performed on significant risks by the component auditors.

Our audit work was executed at levels of materiality applicable to each individual component, which were between US\$10.5 million and US\$18.9 million (2015: US\$8.0 million and US\$10.4 million).

GROUP REVENUE (%)



TOTAL ASSETS (%)



INDEPENDENT AUDITOR’S REPORT TO THE MEMBERS OF POLYMETAL INTERNATIONAL PLC CONTINUED

MATTERS ON WHICH WE ARE REQUIRED TO REPORT BY EXCEPTION

Adequacy of explanations received and accounting records	
<p>Under the Companies (Jersey) Law, 1991 we are required to report to you if, in our opinion:</p> <ul style="list-style-type: none">• we have not received all the information and explanations we require for our audit; or• proper accounting records have not been kept by the parent Company, or proper returns adequate for our audit have not been received from branches not visited by us; or• the financial statements are not in agreement with the accounting records and returns.	<p>We have nothing to report in respect of these matters.</p>
Corporate Governance Statement	
<p>Under the Listing Rules we are also required to review part of the Corporate Governance Statement relating to the Company's compliance with certain provisions of the UK Corporate Governance Code.</p>	<p>We have nothing to report arising from our review.</p>
Our duty to read other information in the Annual Report	
<p>Under International Standards on Auditing (UK and Ireland), we are required to report to you if in our opinion information in the Annual Report is:</p> <ul style="list-style-type: none">• materially inconsistent with the information in the audited financial statements; or• apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Group acquired in the course of performing our audit; or• otherwise misleading. <p>In particular, we are required to consider whether we have identified any inconsistencies between our knowledge acquired during the audit and the directors' statement that they consider the Annual Report is fair, balanced and understandable and whether the Annual Report appropriately discloses those matters that we communicated to the Audit and Risk Committee which we consider should have been disclosed.</p>	<p>We confirm that we have not identified any such inconsistencies or misleading statements.</p>

OTHER MATTER

In our opinion, the part of the Directors’ Remuneration Report to be audited has been properly prepared in accordance with the provisions of the UK Companies Act 2006 as if that Act had applied to the Company.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITOR

As explained more fully in the Directors’ Responsibilities Statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). We also comply with International Standard on Quality Control 1 (UK and Ireland). Our audit methodology and tools aim to ensure that our quality control procedures are effective, understood and applied. Our quality controls and systems include our dedicated professional standards review team and independent partner reviews.

This report is made solely to the Company’s members, as a body, in accordance with Article 113A of the Companies (Jersey) Law, 1991. Our audit work has been undertaken so that we might state to the Company’s members those matters we are required to state to them in an auditor’s report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company’s members as a body, for our audit work, for this report, or for the opinions we have formed.

SCOPE OF THE AUDIT OF THE FINANCIAL STATEMENTS

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group’s circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.



James Leigh
FCA (Senior statutory auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Recognised Auditor
London, UK

14 March 2017

CONSOLIDATED INCOME STATEMENT

	Notes	Year ended	
		31 December 2016 US\$m	31 December 2015 US\$m
Revenue	6	1,583	1,441
Cost of sales	7	(846)	(779)
Gross profit		737	662
General, administrative and selling expenses	11	(120)	(127)
Other operating expenses	12	(36)	(51)
Share of loss of associates and joint ventures	20	–	(4)
Operating profit		581	480
Gain on disposal of subsidiary	4	–	1
Net foreign exchange gains/(losses)		65	(133)
Change in fair value of contingent consideration liability	28	(22)	4
Finance income		3	5
Finance costs	15	(63)	(81)
Profit before income tax		564	276
Income tax expense	16	(169)	(55)
Profit for the financial year		395	221
Profit for the year attributable to:			
Equity shareholders of the Parent		395	221
		395	221

		Year ended	
		31 December 2016 US\$	31 December 2015 US\$
Profit per share			
Basic	30	0.93	0.52
Diluted	30	0.93	0.52

	Year ended			
	31 December 2016 cents per share	31 December 2015 cents per share	31 December 2016 US\$m	31 December 2015 US\$m
Final dividend proposed in relation to the year (Note 17)	18	13	77	56
Interim dividend (Note 17)	9	8	38	34
Special dividend (Note 17)	15	30	64	127
			179	217

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Year ended	
	31 December 2016 US\$m	31 December 2015 US\$m
Profit for the financial year	395	221
<i>Items that may be reclassified subsequently to profit or loss</i>		
Exchange differences on translating foreign operations	280	(582)
Currency exchange differences on intercompany loans forming part of net investment in foreign operations, net of income tax	(56)	(58)
Total comprehensive income/(loss) for the financial year	619	(419)
	Year ended	
	31 December 2016 US\$m	31 December 2015 US\$m
Total comprehensive income/(loss) for the financial year attributable to:		
Equity Shareholders of the Parent	619	(419)
	619	(419)

CONSOLIDATED BALANCE SHEET

		31 December 2016 US\$m	31 December 2015 US\$m
	Notes		
Assets			
Property, plant and equipment	18	1,805	1,360
Goodwill	19	17	14
Investments in associates and joint ventures	20	25	2
Non-current loans and receivables		10	13
Deferred tax asset	16	38	57
Non-current inventories	21	113	99
Total non-current assets		2,008	1,545
Current inventories	21	493	353
Current VAT receivable		61	60
Trade and other receivables	22	70	39
Prepayments to suppliers		31	25
Income tax prepaid		18	8
Cash and cash equivalents	23	48	52
Total current assets		721	537
Total assets		2,729	2,082
Liabilities and shareholders' equity			
Accounts payable and accrued liabilities	26	(133)	(77)
Current borrowings	24	(98)	(287)
Income tax payable		(8)	(22)
Other taxes payable		(34)	(32)
Current portion of contingent consideration liability	28	(14)	(2)
Total current liabilities		(287)	(420)
Non-current borrowings	24	(1,280)	(1,063)
Contingent consideration liability	28	(62)	(24)
Deferred tax liability	16	(78)	(50)
Environmental obligations	25	(37)	(33)
Other non-current liabilities		(4)	(5)
Total non-current liabilities		(1,461)	(1,175)
Total liabilities		(1,748)	(1,595)
NET ASSETS		981	487
Stated capital account	30	2,010	1,969
Share-based compensation reserve	31	12	6
Translation reserve		(1,241)	(1,465)
Retained earnings/(accumulated loss)		200	(23)
Total equity		981	487

Notes on pages 114 to 157 form part of these financial statements. These financial statements are approved and authorised for issue by the Board of Directors on 14 March 2017 and signed on its behalf by:



Vitaly Nesis
Group Chief Executive



Bobby Godsell
Chairman of the Board of Directors

CONSOLIDATED STATEMENT OF CASH FLOWS

	Notes	Year ended	
		31 December 2016 US\$m	31 December 2015 US\$m
Net cash generated by operating activities	33	530	491
Cash flows from investing activities			
Purchases of property, plant and equipment	18	(271)	(205)
Net cash outflow on business combinations	4	(107)	–
Acquisition of JV	20	(21)	(7)
Kyzyl put option exercise	4	–	(68)
Loans advanced, net		(2)	(22)
Other investing activities		–	2
Net cash used in investing activities		(401)	(300)
Cash flows from financing activities			
Borrowings obtained	24	1,436	723
Repayments of borrowings	24	(1,410)	(696)
Dividends paid	17	(158)	(300)
Contingent consideration payment	28	(2)	(1)
Net cash used in by financing activities		(134)	(274)
Net decrease in cash and cash equivalents		(5)	(83)
Cash and cash equivalents at the beginning of the financial year	23	52	157
Effect of foreign exchange rate changes on cash and cash equivalents		1	(22)
Cash and cash equivalents at the end of the financial year	23	48	52

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Notes	Number of Polymetal International shares outstanding	Stated capital account	Share-based compensation reserve	Translation reserve	Share purchase obligation	Retained earnings	Total equity
Balance at 1 January 2015		420,819,943	1,939	2	(825)	(219)	(29)	868
Profit for the financial year		–	–	–	–	–	221	221
Other comprehensive income, net of income tax		–	–	–	(640)	–	–	(640)
Share based compensation	31	–	–	4	–	–	–	4
Shares allotted to employees	31	36,089	–	–	–	–	–	–
Issue of shares to acquire non-controlling interest	30	1,746,692	13	–	–	–	(13)	–
Issue of shares in exchange for asset acquisitions	4	1,618,154	13	–	–	–	–	13
Issue of shares to acquire share in joint venture	4	429,260	4	–	–	–	–	4
Share purchase obligation exercise	4	–	–	–	–	219	14	233
Dividends	17	–	–	–	–	–	(216)	(216)
Balance at 31 December 2015		424,650,138	1,969	6	(1,465)	–	(23)	487
Profit for the financial year		–	–	–	–	–	395	395
Other comprehensive income, net of income tax		–	–	–	224	–	–	224
Share based compensation	31	–	–	7	–	–	–	7
Shares allotted to employees	31	110,850	1	(1)	–	–	–	–
Issue of shares to acquire non-controlling interest	30	898,875	14	–	–	–	(14)	–
Issue of shares in exchange for asset acquisitions	4	1,120,690	11	–	–	–	–	11
Issue of shares for business acquisition	4	1,481,785	15	–	–	–	–	15
Dividends	17	–	–	–	–	–	(158)	(158)
Balance at 31 December 2016		428,262,338	2,010	12	(1,241)	–	200	981

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. GENERAL

CORPORATE INFORMATION

Polymetal Group (the Group) is a leading gold and silver mining group, operating in Russia, Kazakhstan and Armenia.

Polymetal International plc (the Company) is the ultimate parent entity of Polymetal Group. The Company was incorporated in 2010 as a public limited company under Companies (Jersey) Law 1991 and has its place of business in Cyprus. Its shares are traded on the London and Moscow stock exchanges.

SIGNIFICANT SUBSIDIARIES

As at 31 December 2016 the Company held the following significant mining and production subsidiaries:

Name of subsidiary	Deposits	Country of incorporation	Effective interest held, %	
			31 December 2016	31 December 2015
JSC Gold of Northern Urals	Voro	Russia	100	100
LLC Okhotskaya Mining and Exploration Company	Avlayakan	Russia	100	100
Svetloye LLC	Svetloye	Russia	100	100
JSC Magadan Silver	Dukat	Russia	100	100
	Lunnoye			
	Arylakh			
	Goltsovoye			
Mayskoye Gold Mining Company LLC	Mayskoye	Russia	100	100
Omolon Gold Mining Company LLC	Birkachan	Russia	100	100
	Tsokol			
	Dalneye			
	Oroch			
	Sopka Kvartsevaya			
	Olcha			
Albazino Resources Ltd	Albazino	Russia	100	100
Amur Hydrometallurgical Plant LLC	N/A	Russia	100	100
JSC Varvarinskoye	Varvara	Kazakhstan	100	100
Bakyrchik Mining Venture LLP	Bakyrchik	Kazakhstan	100	100
JSC Inter Gold Capital	Bolshevik	Kazakhstan	100	100
JSC Komarovskoye Mining Company	Komar	Kazakhstan	100	–
Kapan MPC CJSC	Kapan	Armenia	100	–

GOING CONCERN

In assessing its going concern status, the Group has taken account of its financial position, anticipated future trading performance, its borrowings and other available credit facilities, and its forecast compliance with covenants on those borrowings and its capital expenditure commitments and plans. As at 31 December 2016, the Group held US\$48 million of cash and had net debt of US\$1,330 million. It has undrawn facilities of US\$998 million, of which US\$873 million are considered committed.

The Board is satisfied that the Group's forecasts and projections, having taken account of reasonably possible changes in trading performance, show that the Group has adequate resources to continue in operational existence for at least the next 12 months from the date of this report without material uncertainty and that it is appropriate to adopt the going concern basis in preparing the consolidated financial statements for the year ended 31 December 2016.

While assessing the Group's longer-term viability, the Board confirms that taking into account the Group's current position and based upon the robust assessment of the principal risks facing the Group and stress-testing based assessment of Group's prospects, the Board has a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period to 31 December 2019. Please refer to Longer-term viability statement on page 100 of this Annual Report.

BASIS OF PRESENTATION

The Group's annual consolidated financial statements for the year ended 31 December 2016 are prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union. The financial statements have been prepared on the historical cost basis, except for certain financial instruments which are measured at fair value as of end of the reporting period and share-based payments which are recognised at fair value as of measurement date.

The following accounting policies have been applied in preparing the consolidated financial statements for the year ended 31 December 2016.

AMENDED ACCOUNTING STANDARDS ADOPTED BY THE ENTITY

The following new accounting pronouncements which became effective in the current reporting period:

Amendments to IFRS 11 *Accounting for Acquisitions of Interest in Joint Operations*. The amendments to IFRS 11 provide guidance on how to account for the acquisition of an interest in a joint operation in which the activities constitute a business as defined in IFRS 3 *Business Combination* and state that the relevant principles on accounting for business combinations in IFRS 3 and other standards should be applied. The same requirements should be applied to the formation of a joint operation if and only if an existing business is contributed to the joint operation by one of the parties that participate in the joint venture. A joint operator is also required to disclose the relevant information required by IFRS 3 and other standards for business combinations. Entities should apply the amendments prospectively to acquisitions of interest in joint operations occurring from the beginning of annual periods beginning on or after 1 January 2016. The Group has determined that amendments to IFRS 11 do not impact its consolidated financial statements as it does not have any arrangements considered joint operations.

Amendments to IAS 1 *Presentation of Financial Statements*: Disclosure. Initiative provides guidance on the use of judgement in presenting financial statement information, including: the application of materiality; order of notes; use of subtotals; accounting policy referencing and disaggregation of financial and non-financial information. Amendments are effective for annual periods beginning on or after 1 January 2016. The Group has determined that amendments to IAS 1 do not impact its consolidated financial statements.

NEW ACCOUNTING STANDARDS ISSUED BUT NOT YET EFFECTIVE

IFRS 15 *Revenue from Contracts with Customers*. In May 2014, the IASB issued IFRS 15 Revenue from Contracts with Customers ('IFRS 15'), which covers principles that an entity shall apply to report information to users of financial statements about the nature, amount, timing, and uncertainty of revenue and cash flows arising from a contract with a customer. Application of the standard is mandatory for annual reporting periods beginning on or after January 1, 2018, with earlier application permitted. The Group is in the process of determining the impact of IFRS 15 on its consolidated financial statements with the primary focus being understanding those sales contracts where the timing and amount of revenue recognised could differ under IFRS 15, which may occur for example if contracts with customers incorporate performance obligations not currently recognised separately, or where such contracts incorporate variable consideration. As the Group's revenue is predominantly derived from arrangements in which the transfer of risks and rewards coincides with the fulfilment of performance obligations, the timing and amount of revenue recognised is unlikely to be materially affected for the majority of sales.

IFRS 9 *Financial instruments*. In July 2014, the IASB issued the final version of IFRS 9 'Financial Instruments' ('IFRS 9'). This standard is effective for annual periods beginning on or after January 1, 2018, and permits early adoption. IFRS 9 provides a revised model for recognition, measurement and impairment of financial instruments. IFRS 9 also includes a substantially reformed approach to hedge accounting. The Group is in the process of determining the impact of IFRS 9 on its consolidated financial statements and does not expect it to have a material impact on its consolidated financial statements.

IFRS 16 *Leases*. This standard is effective for annual periods beginning on or after January 1, 2019, and permits early adoption. IFRS 16 replaces the following standards and interpretations: IAS 17 *Leases* and IFRIC 4 *Determining whether an Arrangement contains a Lease*. The new standard provides a single lessee accounting model for the recognition, measurement, presentation and disclosure of leases. IFRS 16 applies to all leases including subleases and requires lessees to recognise assets and liabilities for all leases, unless the lease term is 12 months or less, or the underlying asset has a low value. Lessors continue to classify leases as operating or finance. The Group is in the process of determining the impact of IFRS 16 on its consolidated financial statements and does not expect it to have a material impact on its consolidated financial statements.

Amendments to IFRS 10 *Consolidated Financial Statements* and IAS 28 *Joint Ventures*: Sale or Contribution of Assets between an Investor and its Associate or Joint Venture remove an inconsistency between the two standards on the accounting treatment for gains and losses arising on the sale or contribution of assets by an investor to its associate or joint venture. Following the amendment, such gains and losses may only be recognised to the extent of the unrelated investor's interest, except where the transaction involves assets that constitute a business. The Group does not expect it to have a material impact on its consolidated financial statements.

Amendments to IFRS 2 *Share based payment: Classification and Measurement of Share-Based Payment transactions*. On 20 June 2016, the International Accounting Standards Board (IASB) published final amendments to IFRS 2 that clarify the classification and measurement of share-based payment transactions. IASB has now added guidance on accounting for cash-settled share-based payment transactions that include a performance condition, classification of share-based payment transactions with net settlement features and accounting for modifications of share-based payment transactions from cash-settled to equity-settled. Amendments are effective for annual periods beginning on or after 1 January 2018. The Group is in the process of determining the impact of amendments to IFRS 2 on its consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

CONTINUED

2. SIGNIFICANT ACCOUNTING POLICIES

BASIS OF CONSOLIDATION

SUBSIDIARIES

The consolidated financial statements of the Group include the financial statements of the Company and its subsidiaries, from the date that control effectively commenced until the date that control effectively ceased. Control is achieved where the Company is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee.

Income and expenses of subsidiaries acquired or disposed of during the period are included in the consolidated income statement from the effective date of acquisition and up to the effective date of disposal, as appropriate.

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

All intra-group balances, transactions and any unrealised profits or losses arising from intra-group transactions are eliminated on consolidation.

Changes to the Group's ownership interests that do not result in a loss of control over the subsidiaries are accounted for as equity transactions. The carrying amount of the Group's interests and non-controlling interests are adjusted to reflect the change in their relative interests in the subsidiaries. Any difference between the amount by which the non-controlling interest is adjusted and the fair value of the consideration paid or received is recognised directly in equity and attributed to the owners of the Company.

When the Group loses control of a subsidiary, the profit or loss on the disposal is calculated as the difference between 1) the aggregated fair value of the consideration received and the fair value of any retained interest and 2) the previous carrying amount of the assets (including goodwill), and liabilities of the subsidiary and non-controlling interests.

BUSINESS COMBINATIONS

IFRS 3 *Business Combinations* applies to a transaction or other event that meets the definition of a business combination. When acquiring new entities or assets, the Group applies judgement to assess whether the assets acquired and liabilities assumed constitute an integrated set of activities, whether the integrated set is capable of being conducted and managed as a business by a market participant, and thus whether the transaction constitutes a business combination, using the guidance provided in the standard. Acquisitions of businesses are accounted for using the acquisition method. The consideration for each acquisition is measured at the aggregate of the fair values (at the date of exchange) of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree. Acquisition-related costs are recognised in the consolidated income statement as incurred. Transaction costs incurred in connection with the business combination are expensed. Provisional fair values are finalised within 12 months of the acquisition date.

Where applicable, the consideration for the acquisition may include an asset or liability resulting from a contingent consideration arrangement. Contingent consideration is measured at its acquisition-date fair value and included as part of the consideration transferred in a business combination. Subsequent changes in such fair values are adjusted against the cost of acquisition retrospectively with the corresponding adjustment against goodwill where they qualify as measurement period adjustments. Measurement period adjustments are adjustments that arise from additional information obtained during the measurement period about facts and circumstances that existed at the acquisition date. The measurement period may not exceed one year from the effective date of the acquisition. The subsequent accounting for contingent consideration that does not qualify for as a measurement period adjustment is based on how the contingent consideration is classified. Contingent consideration that is classified as equity is not subsequently remeasured. Contingent consideration that is classified as an asset or liability is remeasured at subsequent reporting dates in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* or IAS 39 *Financial Instruments Recognition and Measurement* with the corresponding amount being recognised in profit or loss.

The identifiable assets acquired and the liabilities assumed are recognised at their fair value at the acquisition date, except that:

- deferred tax assets or liabilities and liabilities or assets related to employee benefit arrangements are recognised and measured in accordance with IAS 12 *Income Taxes* and IAS 19 *Employee Benefits*, respectively;
- liabilities or equity instruments related to share-based payment arrangements of the acquiree or share-based payment arrangements of the Group entered into to replace share-based payment arrangements of the acquiree are measured in accordance with IFRS 2 *Share-based Payment* at the acquisition date; and
- assets (or disposal groups) that are classified as held for sale in accordance with IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* are measured in accordance with that Standard.

Where a business combination is achieved in stages, the Group's previously held interests in the acquired entity are remeasured to fair value at the acquisition date (i.e. the date the Group attains control) and the resulting gain or loss, if any, is recognised in the consolidated income statement. Amounts arising from interests in the acquiree prior to the acquisition date that have previously been recognised in equity are reclassified to profit or loss, where such treatment would be appropriate if that interest was disposed of.

GOODWILL AND GOODWILL IMPAIRMENT

Goodwill arising in a business combination is recognised as an asset at the date that control is acquired (the acquisition date). 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 the Group's interest in the fair value of the acquiree's identifiable net assets 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 equity interest in the acquiree (if any), the excess is recognised immediately in the consolidated income statement as a bargain purchase gain.

Goodwill is not amortised but is reviewed for impairment at least annually. For the purpose of impairment testing, goodwill is allocated to each of the Group's cash-generating units expected to benefit from the synergies of the combination. Cash-generating units to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an 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 on the basis of the carrying amount of each asset in the unit. An impairment loss recognised for goodwill is not reversed in a subsequent period.

On disposal of a subsidiary, the attributable goodwill is included in the determination of the profit or loss on disposal.

ACQUISITION OF MINING LICENCES

The acquisition of mining licences is often effected through a non-operating corporate entity. As these entities do not represent a business, it is considered that the transactions do not meet the definition of a business combination and, accordingly, the transaction is accounted for as the acquisition of an asset. The net assets acquired are accounted for at cost. Where asset acquisition is achieved in stages net assets acquired are accounted for sum of cost of the original interest acquired and the cost of additional interest acquired.

INVESTMENTS IN ASSOCIATES AND JOINT VENTURES

An associate is an entity over which the Group has significant influence and that is neither a subsidiary nor an interest in a joint arrangement. Significant influence constitutes the power to participate in the financial and operating policy decisions of the investee but does not extend to a control or joint control over the enactment of those policies. The results and assets and liabilities of associates are incorporated in the consolidated financial statements using the equity method of accounting.

A joint arrangement is defined as an arrangement of which two or more parties have joint control. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require unanimous consent of the parties sharing control.

A joint operation is a joint arrangement in which the parties that share joint control have rights to the assets, and obligations for the liabilities, relating to the arrangement. This includes situations where the parties benefit from the joint activity through a share of the output, rather than by receiving a share of the results of trading. In relation to its interest in a joint operation, the Group recognises: its share of assets and liabilities; revenue from the sale of its share of the output and its share of any revenue generated from the sale of the output by the joint operation; and its share of expenses.

A joint venture is a joint arrangement in which the parties that share joint control have rights to the net assets of the arrangement and is accounted for using the equity accounting method.

When entering in a new joint arrangement, the Group applies judgement to assess whether the parties that have joint control over the arrangement have rights to the assets, and obligations for the liabilities, relating to the arrangement (joint operation) or rights to the net assets of the arrangement (joint venture), using the guidance provided in the standard. When a joint arrangement has been structured through a separate vehicle, consideration has been given to the legal form of the separate vehicle, the terms of the contractual arrangement and, when relevant, other facts and circumstances.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
CONTINUED

2. SIGNIFICANT ACCOUNTING POLICIES CONTINUED

EQUITY METHOD OF ACCOUNTING

Under the equity method, an investment in an associate or a joint venture is initially recognised in the consolidated balance sheet at cost and adjusted thereafter to recognise the Group's share of the profit or loss and other comprehensive income of the investee.

Any excess of the cost of acquisition over the Group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities of an investee at the date of acquisition is recognised as goodwill, which is included within the carrying amount of the investment.

The requirements of IAS 39 are applied to determine whether it is necessary to recognise any impairment loss with respect to the Group's investments. Where an indicator of impairment exists or the carrying value of the asset contains goodwill with an indefinite useful life, the entire carrying amount of the investment (including goodwill) is tested for impairment in accordance with IAS 36 Impairment of Assets (IAS 36) as a single cash generating unit through the comparison of its recoverable amount (the higher of value in use and fair value less costs to sell) with its carrying amount.

When a Group entity transacts with its investees, profits and losses resulting from the transactions with the investee are recognised in the Group's consolidated financial statements only to the extent of interests in the associate or the joint venture that are not related to the Group.

FUNCTIONAL AND PRESENTATION CURRENCY

The functional currency for each entity in the Group is determined as the currency of the primary economic environment in which it operates. For all Russian entities the functional currency is the Russian Rouble (RUB). The functional currency of the Group's entities located and operating in Kazakhstan (JSC Varvarinskoye, Bakyrchik Mining Venture LLP, JSC Inter Gold Capital, JSC Komarovskoye Mining Company) is the Kazakh Tenge (KZT). The functional currency of the Group's entity located and operating in Armenia (Kapan MPC CJSC) is the Armenian Dram (AMD). The functional currency of the parent company Polymetal International plc and its intermediate holding companies is U.S. Dollar.

The Group has chosen to present its consolidated financial statements in U.S. Dollars (US\$), as management believes it is a more convenient presentation currency for international users of the consolidated financial statements of the Group as it is a common presentation currency in the mining industry. The translation of the financial statements of the Group entities from their functional currencies to the presentation currency is performed as follows:

- all assets and liabilities are translated at closing exchange rates at each reporting period end date;
- all income and expenses are translated at the average exchange rates for the periods presented, except for significant transactions that are translated at rates on the date of such transactions;
- resulting exchange differences are recognised in other comprehensive income and presented as movements relating to the effect of translation to the Group's presentation currency within the Translation reserve in equity; and
- in the consolidated statement of cash flows, cash balances at the beginning and end of each reporting period presented are translated using exchange rates prevalent at those respective dates. All cash flows in the period are translated at the average exchange rates for the periods presented, except for significant transactions that are translated at rates on the date of transaction.

On the disposal of a foreign operation (i.e. a disposal of the Group's entire interest in a foreign operation, or a disposal involving loss of control over a subsidiary that includes a foreign operation, a disposal involving loss of joint control over a jointly controlled entity that includes a foreign operation, or a disposal involving loss of significant influence over an associate that includes a foreign operation), all of the exchange differences accumulated in equity in respect of that operation attributable to the owners of the Company are reclassified to profit or loss.

In the case of a partial disposal that does not result in the Group losing control over a subsidiary that includes a foreign operation, the proportionate share of accumulated exchange differences are re-attributed to non-controlling interests and are not recognised in the consolidated income statement. For all other partial disposals (i.e. reductions in the Group's ownership interest in associates or jointly controlled entities that do not result in the Group losing significant influence or joint control), the proportionate share of the accumulated exchange differences is reclassified to the consolidated income statement.

Goodwill and fair value adjustments on identifiable assets and liabilities acquired arising on the 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 recognised in equity.

Exchange rates used in the preparation of the consolidated financial statements were as follows:

	Russian Rouble/U.S. Dollar	Kazakh Tenge/U.S. Dollar	Armenian Dram/U.S. Dollar
31 December 2015			
Year end	72.9	339	484
Average for:			
January	61.9	184	475
February	64.7	185	478
March	60.3	185	478
April	52.9	186	474
May	50.6	186	480
June	54.5	186	475
July	57.1	187	477
August	65.2	207	480
September	66.8	258	481
October	63.1	275	473
November	65.0	303	480
December	69.7	323	483
31 December 2016			
Year end	60.7	333	484
Average for:			
January	76.3	362	486
February	77.2	359	494
March	70.5	345	487
April	66.7	337	481
May	65.7	333	478
June	65.3	337	478
July	64.3	341	477
August	64.9	344	475
September	64.6	339	474
October	62.7	332	475
November	64.4	339	478
December	62.2	334	483

The Russian Rouble, Kazakh Tenge and Armenian Dram are not freely convertible currencies outside the Russian Federation, Kazakhstan and Armenia, accordingly, any translation of Russian Rouble, Kazakh Tenge and Armenian Dram denominated assets and liabilities into U.S. Dollar for the purpose of the presentation of consolidated financial statements does not imply that the Group could or will in the future realise or settle in U.S. Dollars the translated values of these assets and liabilities.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
CONTINUED

2. SIGNIFICANT ACCOUNTING POLICIES CONTINUED

FOREIGN CURRENCY TRANSACTIONS

Transactions in currencies other than an entity's functional currencies (foreign currencies) are recorded at the exchange rates prevailing on the dates of the transactions. All monetary assets and liabilities denominated in foreign currencies are translated at the exchange rates prevailing at the reporting date. Non-monetary items carried at historical cost are translated at the exchange rate prevailing on the date of transaction. Non-monetary items carried at fair value are translated at the exchange rate prevailing on the date on which the most recent fair value was determined. Exchange differences arising from changes in exchange rates are recognised in the consolidated income statement. Exchange differences generated by monetary items that forms part of the intragroup net investment in the foreign operation are recognised in the consolidated financial statements within foreign currency translation reserve.

PROPERTY, PLANT AND EQUIPMENT

MINING ASSETS

Mining assets include the cost of acquiring and developing mining assets and mineral rights. Mining assets are depreciated to their residual values using the unit-of-production method based on proven and probable ore reserves according to the JORC Code, which is the basis on which the Group's mine plans are prepared. Changes in proven and probable reserves are dealt with prospectively. Depreciation is charged on new mining ventures from the date that the mining asset is capable of commercial production (Note 5). In respect of those mining assets whose useful lives are expected to be less than the life of the mine, depreciation over the period of the asset's useful life is applied.

Mineral rights for the assets under development are included within Exploration and development. When a production phase is started, mineral rights are transferred into Mining assets and are depreciated as described below.

CAPITAL CONSTRUCTION-IN-PROGRESS

Capital construction-in-progress assets are measured at cost less any recognised impairment. Depreciation commences when the assets are ready for their intended use.

EXPLORATION AND DEVELOPMENT ASSETS

Mineral exploration and evaluation costs, including geophysical, topographical, geological and similar types of costs, are capitalised into exploration assets if management concludes that future economic benefits are likely to be realised based on current internal assessment of exploration results and identified mineral resources.

Exploration and evaluation expenditures are transferred to development assets when commercially-viable reserves are identified, so that the entity first establishes proved and probable reserves in accordance with JORC Code and respective mining plan and model are prepared and approved. At the time of reclassification exploration and evaluation assets are assessed for impairment based on the economic models prepared.

The costs to remove any overburden and other waste materials to initially expose the ore body, referred to as stripping costs, are capitalised as a part of mining assets when these costs are incurred.

NON-MINING ASSETS

Non-mining assets are depreciated to their residual values on a straight-line basis over their estimated useful lives. When parts of an item of property, plant and equipment are considered to have different useful lives, they are accounted for and depreciated separately. Depreciation methods, residual values and estimated useful lives are reviewed at least annually.

Estimated useful lives are as set out below:

- Machinery and equipment 5-20 years
- Transportation and other assets 3-10 years

Assets held under finance leases are depreciated over the shorter of the lease term and the estimated useful lives of the assets.

Gains or losses on disposal of property, plant and equipment are determined by comparing the proceeds from disposal with the asset's carrying amount at the date. The gain or loss arising is recognised in the consolidated income statement.

STRIPPING COSTS

During the production phase of a mine when the benefit from the stripping activity is the improved access to a component of the ore body in future periods, the stripping costs in excess of the average ore to waste ratio for the life of mine of that component are recognised as a non-current asset. After initial recognition, the stripping activity asset is depreciated on a systematic basis (unit-of-production method) over the expected useful life of the identified component of the ore body made accessible as a result of the stripping activity.

ESTIMATED ORE RESERVES

Estimated proven and probable ore reserves reflect the economically recoverable quantities which can be legally recovered in the future from known mineral deposits. The Group's reserves are estimated in accordance with JORC Code.

LEASES

OPERATING LEASES

Operating lease payments are recognised as an expense on a straight-line basis over the lease term. Contingent rentals arising under operating leases are recognised as an expense in the period in which they are incurred.

IMPAIRMENT OF PROPERTY, PLANT AND EQUIPMENT

An impairment review of property, plant and equipment is carried out when there is an indication that those assets have suffered an impairment loss. If any such indication exists, the carrying amount of the asset is compared to the estimated recoverable amount of the asset in order to determine the extent of the impairment loss (if any). Where 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 less costs to sell and value in use. The carrying amounts of all the cash-generating units are assessed against their recoverable amounts determined based on a fair value less costs to sell calculation. Fair value is based on the application of the Discounted Cash Flow Method (DCF) using post-tax cash flows. The DCF method is attributable to the development of proved and probable reserves and certain resources where a relevant resource-to-reserve conversion ratio can be reasonably applied.

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 recognised as an expense immediately in the consolidated income statement.

Where 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 only to the extent that the increased carrying amount does not exceed the original carrying amount that would have been determined had no impairment loss been recognised in prior periods. Impairment loss may be subsequently reversed if there has been a significant change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised.

A reversal of an impairment loss is recognised in the consolidated income statement immediately.

INVENTORIES

METAL INVENTORIES

Inventories including refined metals, metals in concentrate and in process, doré and ore stockpiles are stated at the lower of production cost or net realisable value. Production cost is determined as the sum of the applicable expenditures incurred directly or indirectly in bringing inventories to their existing condition and location. Work in-process, metal concentrate, and doré and refined metal are valued at the average total production costs at each asset's relevant stage of production (i.e. the costs are allocated proportionally to unified metal where unified metal is calculated based on prevailing market metal prices). Ore stockpiles are valued at the average cost of mining that ore. Where ore stockpiles and work in-process are not expected to be processed within 12 months, those inventories are classified as non-current.

Net realisable value represents the estimated selling price for that product based on forward metal prices for inventories which are expected to be realised within 12 months, and the flat long-term metal prices non-current inventories, less estimated costs to complete production and selling costs.

CONSUMABLES AND SPARE PARTS

Consumables and spare parts are stated at the lower of cost or net realisable value. Cost is determined on the weighted average moving cost. The portion of consumables and spare parts not reasonably expected to be used within one year is classified as a long-term asset in the Group's consolidated balance sheet. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

FINANCIAL INSTRUMENTS

Financial assets and financial liabilities are recognised when a Group entity becomes a party to the contractual provisions of the instrument.

Financial assets and financial liabilities are initially measured 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 recognised immediately in the consolidated income statement.

FINANCIAL INSTRUMENTS DESIGNATED AS FAIR VALUE THROUGH PROFIT AND LOSS (FVTPL)

- A financial instrument other than a financial instrument held for trading may be designated as at FVTPL upon initial recognition if:
 - such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
 - the financial instrument forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Group's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
 - it forms part of a contract containing one or more embedded derivatives, and IAS 39 Financial Instruments: Recognition and Measurement permits the entire combined contract (asset or liability) to be designated as at FVTPL.

Financial instruments at FVTPL are stated at fair value, with any gains or losses arising on remeasurement recognised in profit or loss. Fair value is determined in the manner described in Note 28.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

CONTINUED

2. SIGNIFICANT ACCOUNTING POLICIES CONTINUED

EFFECTIVE INTEREST RATE METHOD

The effective interest rate method is a method of calculating the amortised cost of a financial instrument and of allocating interest income or expense over the relevant period. The effective interest rate is the rate that discounts estimated future cash receipts or 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 instrument, or, where appropriate, a shorter period, to the net carrying amount on initial recognition.

FINANCIAL ASSETS

Non-derivative financial assets are classified into the following specified categories: FVTPL, available for sale (AFS) 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. No financial instruments have been classified as available for sale and FVTPL.

LOANS AND RECEIVABLES

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans and receivables are measured at amortised cost using the effective interest rate method, less any impairment. Interest income is determined by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

IMPAIRMENT OF FINANCIAL ASSETS

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at the end of each reporting period. Financial assets are considered to be impaired when 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 affected. For equity investments classified as AFS, a significant or prolonged decline in the fair value of the security below its cost is considered to be objective evidence of impairment.

For all other financial assets objective evidence of impairment could include:

- significant financial difficulty of the issuer or counterparty; or
- breach of contract, such as a default or delinquency in interest or principal payments; or
- it becoming probable that the borrower will enter bankruptcy or financial re-organisation; or
- the disappearance of an active market for that financial asset because of financial difficulties.

For financial assets carried at amortised cost, the amount of the impairment loss recognised 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.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables, 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 recognised in the consolidated income statement.

For financial assets measured at amortised cost, 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 recognised, the previously recognised impairment loss is reversed through the consolidated income statement to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

DERECOGNITION OF FINANCIAL ASSETS

The Group derecognises 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 transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group recognises 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 recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

FINANCIAL LIABILITIES

OTHER FINANCIAL LIABILITIES

Other financial liabilities (including borrowings) are subsequently measured at amortised cost using the effective interest rate method.

DERECOGNITION OF FINANCIAL LIABILITIES

The Group derecognises financial liabilities when, and only when, the Group's obligations are discharged, cancelled or they expire. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in the consolidated income statement.

EMBEDDED DERIVATIVES

Derivatives embedded in non-derivative host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contracts and the hybrid contracts are not measured at FVTPL. Further details of derivative financial instruments are disclosed in Note 28.

BORROWING COSTS

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 borrowing costs eligible for capitalisation.

All other borrowing costs are recognised in the consolidated income statement in the period in which they are incurred.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents comprise cash balances, cash deposits and highly liquid investments with original maturities of three months or fewer, which are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value.

PROVISIONS

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that the Group will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the reporting date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

ENVIRONMENTAL OBLIGATIONS

An obligation to incur environmental restoration, rehabilitation and decommissioning costs arises when disturbance is caused by the development or ongoing production of mining assets. Such costs arising from the decommissioning of plant and other site preparation work, discounted to their net present value using a risk-free rate applicable to the future cash flows, are provided for and capitalised at the start of each project, as soon as the obligation to incur such costs arises. These costs are recognised in the consolidated income statement over the life of the operation, through the depreciation of the asset in the cost of sales line and the unwinding of the discount on the provision in the finance costs line. Costs for restoration of subsequent site damage which is created on an ongoing basis during production are provided for at their net present values and recognised in the consolidated income statement as extraction progresses.

Changes in the measurement of a liability relating to the decommissioning of plant or other site preparation work (that result from changes in the estimated timing or amount of the cash flow or a change in the discount rate), are added to or deducted from the cost of the related asset in the current period. If a decrease in the liability exceeds the carrying amount of the asset, the excess is recognised immediately in the consolidated income statement.

The provision for closure cost obligations is remeasured at the end of each reporting period for changes in estimates and circumstances. Changes in estimates and circumstances include changes in legal or regulatory requirements, increased obligations arising from additional mining and exploration activities, changes to cost estimates and changes to the risk free interest rate.

EMPLOYEE BENEFIT OBLIGATIONS

Remuneration paid to employees in respect of services rendered during a reporting period is recognised as an expense in that reporting period. The Group pays mandatory contributions to the state social funds, including the Pension Fund of the Russian Federation and Kazakhstan, which are expensed as incurred.

TAXATION

Income tax expense represents the sum of the tax currently payable and deferred tax. Income taxes are computed in accordance with the laws of countries where the Group operates.

CURRENT TAX

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

CONTINUED

2. SIGNIFICANT ACCOUNTING POLICIES CONTINUED

DEFERRED TAX

Deferred tax is recognised 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 recognised for all taxable temporary differences. Deferred tax assets are generally recognised 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 utilised. Such deferred tax assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences associated with investments in subsidiaries and associates, and interests in joint ventures, except where the Group is able to control 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 recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

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 assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realised, 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.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

Current and deferred tax is recognised in the consolidated income statement, except when they relate to items that are recognised in the consolidated statement of comprehensive income or directly in equity, in which case, the current and deferred tax is also recognised in consolidated statement of comprehensive income or directly in equity respectively. Where current tax or deferred tax arises from the initial accounting for a business combination, the tax effect is included in the accounting for the business combination.

UNCERTAIN TAX POSITIONS

Provision for uncertain tax positions is recognised within current tax when management determines that it is probable that a payment will be made to the tax authority. For such tax positions the amount of the probable ultimate settlement with the related tax authority is recorded. When the uncertain tax position gives rise to a contingent tax liability for which no provision is recognised, the Group discloses tax-related contingent liabilities and contingent assets in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.

REVENUE RECOGNITION

Revenue is derived principally from the sale of gold and silver bullions and copper, gold and silver concentrate and is measured at the fair value of consideration received or receivable, after deducting discounts.

Revenue from the sale of gold and silver bullion and sale of copper, gold and silver concentrate is recognised when the risks and rewards of ownership are transferred to the buyer, the Group retains neither a continuing degree of involvement nor control over the goods sold, the amount of revenue can be measured reliably, and it is probable that the economic benefits associated with the transaction will flow to the Group. Revenue from the sale of gold and silver bullion represents the invoiced value of metal shipped to the buyer, net of value added tax (VAT).

SALE OF GOLD AND SILVER BULLION

The Group processes doré produced in the Russian Federation (at Dukat, Okhotsk operations, Voro, Omolon, and Amursk/Albazino) into London Good Delivery Bars prior to sale. This final stage of processing is carried out on a toll-treatment basis at four state-owned refineries. The Group sells gold and silver bullion to banks through long-term agreements. The sales price, as determined in the agreement, may be variable based upon the London Bullion Market Association (LBMA) spot or fixed price, however the Group does not enter into fixed price contracts. For domestic sales, title passes from the Group to the purchaser at the refinery gate with revenue recognised at that point. For export sales, once the gold and/or silver bars have been approved for export by Russian customs, they are then transported to the vault of the purchaser, which is typically located in London. Title passes and revenue is recognised at the point when the gold and/or silver bars are received by the purchaser.

SALES OF COPPER, ZINC, GOLD AND SILVER CONCENTRATE

The Group sells copper, zinc, gold and silver concentrate under pricing arrangements where final prices are determined by quoted market prices in a period subsequent to the date of sale. Concentrate sales are initially recorded based on forward prices for the expected date of final settlement. Revenue is recorded at the time of shipment, which is also when risks and rewards pass to the buyer. Revenue is calculated based on the copper, gold and silver content in the concentrate and using the forward London Bullion Market Association (LBMA) or London Metal Exchange (LME) price to the estimated final pricing date, adjusted for the specific terms of the relevant agreement. Until final settlement occurs, adjustments to revenue are made to take into account the changes in metal quantities upon receipt of new information and assay. Revenue is presented net of refining and treatment charges which are subtracted in calculating the amount to be invoiced.

The Group's sales of copper, zinc, gold and silver concentrate are based on a provisional price and as such, contain an embedded derivative that is required to be separated from the host contract for accounting purposes. The host contract is the receivable from the sale of the concentrate at the forward exchange price at the time of sale. The embedded derivative, which does not qualify for hedge accounting, is measured at FVTPL with changes in its fair value recognised within revenue in the consolidated income statement for each period prior to the final settlement.

SHARE-BASED COMPENSATION

The Group applies IFRS 2 *Share-based Payments* to account for share-based compensation. IFRS 2 requires companies to recognise compensation costs for share-based payments to employees based on the grant-date fair value of the award.

The fair value of the awards granted under Performance Share Plan (as defined in the Remuneration report) is estimated using a Monte-Carlo model valuation (see Note 31).

Awards which are granted under Deferred Share Awards plan and are released over a period of three years, are measured at share price at a grant date and are prorated across periods to the different vest dates (see Note 31).

The fair value of the awards granted is recognised as a general, administrative and selling expense over the vesting period with a corresponding increase in the share-based compensation reserve. Upon the exercise of the awards the amounts recognised within the share-based compensation reserve are transferred to stated capital account.

EARNINGS PER SHARE

Earnings per share calculations are based on the weighted average number of common shares outstanding during the period. Diluted earnings per share are calculated using the treasury stock method, whereby the proceeds from the potential exercise of dilutive stock options with exercise prices that are below the average market price of the underlying shares are assumed to be used in purchasing the Company's common shares at their average market price for the period.

3. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

In the course of preparing financial statements, management necessarily makes judgements and estimates that can have a significant impact on the financial statements. The determination of estimates requires judgements which are based on historical experience, current and expected economic conditions, and all other available information. The most significant areas requiring the use of management judgements and estimates relate to:

- Accounting for acquisitions;
- Impairment of operating and development assets;
- Recoverability of exploration and evaluation assets;
- Taxation;
- Assessment of fair value;
- Ore reserves; and
- Valuation of stockpiles and work in-process.

CRITICAL ACCOUNTING JUDGEMENTS ACCOUNTING FOR ACQUISITIONS

To determine the appropriate accounting approach to be followed for an acquisition transaction, the Group applies judgement to assess whether the acquisition is of a business, and therefore within scope of IFRS 3 Business Combinations, or is of a group of assets that do not constitute a business and is therefore outside scope of IFRS 3. In making this determination, management evaluates the inputs, processes and outputs of the asset or entity acquired. Judgement is used to determine whether an integrated set of activities and assets is capable of being conducted and managed for the purpose of providing a return in the form of dividends, lower costs or other economic benefits directly to investors or other owners, members or participants. Major acquisitions in the year included Kapan and Komar (Note 4). They have been assessed as business combinations under IFRS 3 and have thus been accounted for at their fair values.

Under IFRS 11 *Joint Arrangements*, joint arrangements are classified as joint operations or joint ventures based on the rights and obligations of the parties to the joint arrangements (Note 2). When entering in a new joint arrangement, the Group applies judgement to assess whether the parties that have joint control over the arrangement have rights to the assets, and obligations for the liabilities, relating to the arrangement (joint operation) or rights to the net assets of the arrangement (joint venture), using the guidance provided in the standard. When a joint arrangement has been structured through a separate vehicle, consideration is given to the legal form of the separate vehicle, the terms of the contractual arrangement and, when relevant, other facts and circumstances. In 2015 Polymetal entered into a joint arrangement with OJSC Polyus Gold in advancing the development of the Nezhda gold deposit in Yakutia, Russia (Note 20). The arrangement was structured through a separate vehicle with each party entitled to its share of the net assets and thus was accounted for as a joint venture.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

CONTINUED

3. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY CONTINUED

IMPAIRMENT OF OPERATING AND DEVELOPMENT ASSETS

Mining operations require significant technical and financial resources to operate and as such their value may be sensitive to a range of characteristics unique to each asset. Key sources of estimation uncertainty can include ore reserve estimates and cash flow projections, both of which are discussed separately below under 'Assessment of fair value'.

Entities are required to conduct impairment tests where there is an indication of impairment of an asset or a 'cash-generating unit', where an asset does not generate cash inflows that are largely independent of those from other assets. For goodwill, an annual impairment test is required.

Operating and economic assumptions, which could affect the valuation of assets using discounted cash flows, are updated regularly as part of the Group's planning and forecasting processes. Judgement is required to determine whether any economic or operating assumptions represent significant changes in the service potential of an asset or CGU. Discounted cash flow models are prepared on the basis of such assumptions to determine whether there are any indicators of impairment or impairment reversal.

In addition, indicators for impairment reversal must be assessed for assets (other than goodwill) previously impaired. Any change to operational plans or assumptions, economic parameters, or the passage of time, could result in an impairment reversal, or further impairment, if an indicator is identified.

In making the assessment for impairment, assets that do not generate independent cash inflows are allocated to an appropriate cash-generating unit. Management necessarily applies its judgement in allocating assets that do not generate independent cash inflows to appropriate cash-generating units, and also in estimating the timing and value of underlying cash flows within the value-in-use calculation. Subsequent changes to the cash-generating unit allocation or to the timing of cash flows could impact the carrying value of the respective assets. Refer to Note 19 for further information.

RECOVERABILITY OF EXPLORATION AND EVALUATION ASSETS

Exploration and evaluation assets include mineral rights and exploration and evaluation costs, including geophysical, topographical, geological and similar types of costs.

Exploration and evaluation costs are capitalised if management concludes that future economic benefits are likely to be realised and determines that economically viable extraction operation can be established as a result of exploration activities and internal assessment of mineral resources.

A high degree of confidence that the Group will determine the sufficient probability of future benefits viable requires a significant degree of judgment and assessment of all relevant factors such as the nature and objective of the project; the project's current stage and the extent of exploration and evaluation that has been performed; project timeline; current estimates of the project's net present value, including sensitivity analyses for the key assumptions; and the main risks of the project.

KEY SOURCES OF ESTIMATION UNCERTAINTY

ASSESSMENT OF FAIR VALUE

The assessment of fair value is subjective as it is based on the use of different valuation assumptions. Polymetal principally use the assessment of fair value in accounting for cash flow projections for impairment testing, financial instruments and in accounting for net assets acquired and liabilities assumed in business combinations.

CASH FLOW PROJECTIONS FOR IMPAIRMENT TESTING

Expected future cash flows used in discounted cash flow models are inherently uncertain and could materially change over time. They are significantly affected by a number of factors including ore reserves, together with economic factors such as commodity prices, exchange rates, discount rates and estimates of production costs and future capital expenditure.

- Ore reserves – Recoverable reserves and resources are based on the proven and probable reserves and resources in existence. Reserves and resources are incorporated in projected cash flows, based on ore reserve statements and exploration and evaluation work undertaken by appropriately qualified persons.
- Commodity prices – Commodity prices are based on latest internal forecasts, benchmarked against external sources of information. Polymetal currently use a flat real long-term gold and silver price of US\$1,200 per ounce (2015: US\$1,100) and US\$16 per ounce (2015: US\$14), respectively.
- Foreign exchange rates – Foreign exchange rates are based on latest internal forecasts, benchmarked with external sources of information for relevant countries of operation. Management have analysed RUB/US\$ rate movements for the year ended 31 December 2016. RUB/\$US exchange rate is estimated at 60 RUB/\$US (2015: RUB/\$US 72).
- Discount rates – The Group used a post-tax real discount rate of 9.0% (2015: 9.0%). Cash flow projections used in fair value less costs of disposal impairment models are discounted based on this rate. Specific risks, such as asset and country risks, may result in adjustments to the rate.
- Operating costs, capital expenditure and other operating factors – Cost assumptions incorporate management experience and expectations, as well as the nature and location of the operation and the risks associated there with. Underlying input cost assumptions are consistent with related output price assumptions. Other operating factors, such as the timelines of granting licences and permits are based on management's best estimate of the outcome of uncertain future events at the balance sheet date.

NET ASSETS ACQUIRED AND LIABILITIES ASSUMED IN BUSINESS COMBINATIONS

In accordance with the Group's policy, the Group allocates the cost of the acquired entity to the assets acquired and liabilities assumed based on their fair values as estimated on the date of acquisition. Any difference between the cost of the acquired entity and the fair value of the assets acquired and liabilities assumed is recorded as goodwill. The Group exercises significant judgement in the process of identifying tangible and intangible assets and liabilities, valuing these assets and liabilities, and estimating their remaining useful lives. The valuation of these assets and liabilities is based on assumptions and criteria that, in some cases, include management's estimates of discounted future cash flows.

If actual results are not consistent with estimates and assumptions considered, the Group may have to adjust its estimates of the fair values of assets and liabilities recognised and the goodwill balance during the measurement period. Such a re-measurement could have an impact on the amounts reported in the consolidated income statement in current and future periods.

The Group's acquisitions classified as business combinations are disclosed in Note 4.

ORE RESERVES

An ore reserve estimate is an estimate of the amount of product that can be economically and legally extracted from the Group's properties. Ore reserve estimates are used by the Group in the calculation of: depletion of mining assets using the units-of-production method; impairment charges and in forecasting the timing of the payment of decommissioning and land restoration costs. Also, for the purpose of impairment review and the assessment of the timing of the payment of decommissioning and land restoration costs, management may take into account mineral resources in addition to ore reserves where there is a high degree of confidence that such resources will be extracted.

In order to calculate ore reserves, estimates and assumptions are required about geological, technical and economic factors, including quantities, grades, production techniques, recovery rates, production costs, transport costs, commodity demand, commodity prices, discount rates and exchange rates. Estimating the quantity and/or grade of ore reserves requires the size, shape and depth of ore bodies to be determined by analysing geological data such as the logging and assaying of drill samples. This process may require complex and difficult geological judgements and calculations to interpret the data.

Ore reserve estimates may change from period to period as additional geological data becomes available during the course of operations or if there are changes in any of the aforementioned assumptions. Such changes in estimated reserves may affect the Group's financial results and financial position in a number of ways, including the following:

- asset carrying values due to changes in estimated future cash flows;
- depletion charged in the consolidated income statement where such charges are determined by using the units-of-production method;
- provisions for decommissioning and land restoration costs where changes in estimated reserves affect expectations about the timing of the payment of such costs;
- carrying value of deferred tax assets and liabilities where changes in estimated reserves affect the carrying value of the relevant assets and liabilities; and
- contingent consideration liabilities where these are determined by the future production levels.

TAXATION

The Group is subject to income tax and mining taxes in the Russian Federation, Kazakhstan and Armenia. There is a level of judgement required in determining the tax due when dealing with different domestic tax legislations. Where, based on management judgement, there is a probable liability for additional tax, a provision is recorded. During the year ended 31 December 2016 Polymetal identified a total exposure of approximately US\$13 million in respect of contingent liabilities for income and mining taxes (Note 27). Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and mining tax provisions in the period in which such determination is made.

Deferred tax assets are reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised (Note 16). There is an application of judgement in assessing the amount, timing and probability of future taxable profits and repatriation of retained earnings. These factors affect the determination of the appropriate rates of tax to apply and the recoverability of deferred tax assets. These judgements are influenced, inter alia, by factors such as estimates of future production, commodity lines, operating costs, future capital expenditure and dividend policies. If actual results differ from these estimates or if these estimates must be adjusted in future periods, the financial position, results of operations and cash flows may be negatively affected.

VALUATION OF STOCKPILES AND WORK IN-PROCESS

In determining mine operating costs recognised in the consolidated income statement, the Group's management uses survey and assay techniques to estimate quantities of ore stacked on leach pads and in process and the recoverable gold and silver in this material to determine the average costs of finished goods sold during the period.

The assessment of the recoverability of metal inventories requires judgement both in terms of calculating expected costs to process and refine ore stock piles to produce concentrate or doré for sale, and in terms of estimating future prices to be realised on sale (Note 21). Changes in these estimates can result in a change in mine operating costs of future periods and carrying amounts of inventories.

The key assumptions used in determining the net realisable value of inventories at 31 December 2016 are consistent with those used for goodwill impairment testing.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
CONTINUED

4. ACQUISITIONS AND DISPOSALS

(A) YEAR ENDED 31 DECEMBER 2016

KAPAN

In March 2016 Polymetal entered into binding agreements with Dundee Precious Metals Inc (Dundee). for the acquisition of CJSC Dundee Precious Metals Kapan ('DPMK'), the holding company for the Kapan Gold Mine ('Kapan') in the Republic of Armenia.

The asset comprises a fully mechanised underground mine with a current capacity of approximately 400 ktpa, a conventional 750 ktpa flotation concentrator and various infrastructure facilities. The mine produces gold, copper, silver and zinc concentrates sold to international markets.

On 28 April 2016 the Group acquired 100 per cent of the shares of DPMK.

Kapan meets the definition of a business pursuant to IFRS 3 and thus it was accounted for at fair value using the acquisition method.

CONSIDERATION TRANSFERRED

The total consideration for the shares at completion comprised US\$38 million consisting of US\$14 million payable in cash (including post-closing working capital adjustment amounting to US\$5 million) and US\$15 million paid through the issue of 1,481,785 new ordinary shares of the Company. In addition, Dundee will receive a 2% NSR (Net Smelter Return) royalty on the future production from the Kapan Gold Mine capped at US\$25 million.

The fair value of the 1,481,785 ordinary shares issued as part of the consideration paid for Kapan was determined based on spot price as of acquisition date, being US\$10.28, and amounts to US\$15 million.

The net smelter return royalty described above meets the definition of contingent consideration. The fair value of the contingent consideration was determined based on the life-of-mine model of the Kapan mine by discounting projected cash flows to the acquisition date. The following metal price assumptions, consistent with the assumptions adopted for the long-term planning at the time of acquisition, were used for the fair value calculation: Au – US\$1,250/oz, Ag – US\$17/oz, Cu – US\$4,500/tonne, Zinc – US\$1,800/tonne, real post-tax discount rate of 9.04%. At the acquisition date, the estimated fair value of the contingent consideration amounted to US\$9 million. As of 31 December 2016 contingent consideration approximates to US\$9 million (Note 28).

ASSETS ACQUIRED AND LIABILITIES RECOGNISED AT THE DATE OF ACQUISITION

As of date of finalisation of the interim consolidated financial statements for the period ended 30 June 2016 the fair value of the assets acquired and liabilities recognised at the date of acquisition was provisionally accounted for, as well as the amount of the post-closing working capital adjustment. A post-closing working capital adjustment of US\$5 million is outstanding as of 31 December 2016 and is included in account payable.

The amounts recognised in respect of the identifiable assets acquired and liabilities assumed and its reconciliation to the provisionally accounting are set out in the table below:

	Provisional accounting US\$m	Fair value adjustments US\$m	Final accounting US\$m
Assets acquired and liabilities recognised at the date of acquisition			
Cash and cash equivalents	1	–	1
Mineral rights	17	(17)	–
Property, plant and equipment	4	17	21
Inventories	11	5	16
Account receivable	12	–	12
Accounts payable and accrued liabilities	(8)	–	(8)
Taxes payable	(12)	–	(12)
Environmental obligations	(1)	–	(1)
Deferred taxes	9	–	9
Net assets acquired	33	5	38
Consideration transferred			
Cash	9	5	14
Fair value of shares issued	15	–	15
Contingent consideration	9	–	9
Total consideration	33	5	38
Net cash out flow on acquisition	8	–	8
Cash consideration payable as of 31 December 2016	–	–	5

No significant financial assets were acquired in business combination. The fair value of the accounts receivable approximates to its carrying value.

IMPACT OF THE ACQUISITION ON THE RESULT OF THE GROUP

Kapan contributed US\$2 million to the Group's profit for the period between the date of acquisition and the reporting date. Revenue for the period amounts to US\$29 million.

If the Kapan acquisition had been completed on the first day of the financial year, the revenue of the Group would have been US\$1,588 million, and the profit for the period would have been US\$391 million.

KOMAR

On 4 April 2016 Polymetal entered into a binding agreement with Kazzinc LTD, a subsidiary of Glencore International plc, for the acquisition of Orion Minerals LLP, the holding company for the Komarovskoye Gold Deposit (Komar) in the Republic of Kazakhstan.

The asset comprises an active open pit mine and a 500 Ktpa heap leach facility with grid power available on site. Polymetal aims to mine, deliver by rail and process at Varvara up to 1 Mtpa of ore with potential to increase Varvara's annual production by approximately 70 Koz at lower cash costs.

The acquisition of Komar was completed on 1 August 2016, following receipt of all required regulatory approvals.

Management considers that the control over Komar was obtained on the date of the deal completion. Komar meets the definition of a business pursuant to IFRS 3 thus it was accounted for at fair value using the acquisition method.

The total consideration for Komar is US\$100 million payable in cash. In addition, a deferred consideration contingent upon future production levels and gold price performance, will be paid to Kazzinc LTD. The royalty is calculated on a quarterly basis, based on contained gold in ore mined per relevant quarter and is payable at gold prices above US\$1,250 per ounce. The royalty is capped at a total consideration of US\$80 million.

CONSIDERATION TRANSFERRED

Deferred consideration described above meets definition of the contingent consideration. The fair value of the contingent consideration was determined based on the life-of-mine model of the Komar mine and calculated using Monte-Carlo modelling. Projected cash flows were discounted to the acquisition date at a discount rate of 9.04%. Gold price volatility was assessed at 18.08%, average gold price for one quarter to the valuation date was 1,291 US\$/ounce. As at acquisition date the estimated contingent consideration amounts to US\$20 million. As of 31 December 2016 contingent consideration approximates to US\$18 million (Note 28).

ASSETS ACQUIRED AND LIABILITIES RECOGNISED AT THE DATE OF ACQUISITION

At the date of finalisation of these consolidated financial statements, the calculation of environmental obligations and the calculation of deferred taxes had not been finalised and they have therefore only been provisionally determined based on the directors' best estimate.

The management believes that this business acquisition does not give rise to goodwill and excess of consideration over identifiable net asset assets of the acquiree should be fully attributed the mineral rights. The amount recognised in respect of the identifiable assets acquired and liabilities assumed are set out in the table below:

	US\$m
Assets acquired and liabilities recognised at the date of acquisition	
Cash and cash equivalents	1
Property, plant & equipment	140
Inventories	7
Accounts receivable	1
Accounts payable and accrued liabilities	(2)
Environmental obligations	(1)
Deferred income taxes	(25)
Other liabilities	(1)
Net assets acquired	120
Consideration transferred	
Cash	100
Contingent consideration	20
Total consideration	120
Net cash out flow on acquisition	99

No significant financial assets were acquired in business combination.

IMPACT OF THE ACQUISITION ON THE RESULT OF GROUP

No significant acquisition-related costs were incurred.

Komar contributed US\$1 million to the Group's profit for the period between the date of acquisition and the balance sheet date. Revenue for the period amounts to US\$1 million, which excludes revenue from ore sales to JSC Varvariskoye amounting to US\$10 million since the acquisition date and US\$17 million for the year ended 31 December 2016.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
CONTINUED

4. ACQUISITIONS AND DISPOSALS CONTINUED

If Komar acquisition had been completed on the first day of the financial year, the revenue of the Group would have been US\$1,583 million, and the profit for the period would have been US\$395 million.

SAUM MINING COMPANY LLC

On 2 December 2016 Polymetal International plc acquired an 80% stake in Saum Mining Company LLC, a licence holder for the Saum polymetallic deposit ('Saum'). Polymetal has issued 1,120,690 new Company shares, representing 0.26% of Polymetal's total increased share capital in connection with the acquisition of an 80% stake in Saum from an unrelated party. The total transaction value is approximately US\$10.7 million.

The Saum licence covers an area of 34.2 km² in Russia's Sverdlovsk region in the Ural Mountains and is located and approximately 240 km from Polymetal's Voro processing plant. Polymetal plans to prepare an Ore Reserves estimate in Q4 2017. Further drilling is planned on the property in 2017 and 2018.

Saum does not meet the definition of a business pursuant to IFRS 3, as it represents acquisition of mining license through a non-operating corporate entity, and thus it is accounted for as an acquisition of a group of assets. The Group purchased mineral rights of US\$10 million and other current assets of US\$1 million.

(B) YEAR ENDED 31 DECEMBER 2015
BUSINESS COMBINATIONS AND ASSET ACQUISITIONS
KYZYL PURCHASE PRICE ALLOCATION

On 4 September 2014 the Group acquired 100 per cent of the share capital of Altynalmas Gold Ltd (AAG), the holding company for the Kyzyl gold project in Kazakhstan.

The adjusted fair values of the identifiable assets and liabilities of Kyzyl as at the date of acquisition are presented in the following table:

Table with 4 columns: Assets acquired and liabilities recognised at the date of acquisition, Provisional amount previously reported US\$m, Adjustments US\$m, Adjusted amounts US\$m. Rows include Cash and cash equivalents, Mineral rights, Property, plant and equipment, Other assets, Environmental obligations, Contingent liabilities, Deferred tax liability, Other liabilities, and Net assets acquired.

SETTLEMENT OF THE KYZYL PUT OPTION

In accordance with Kyzyl acquisition terms, the Seller (Sumeru Gold B.V.) was entitled to a put option giving it a right to require Polymetal to acquire or procure acquirers for the consideration shares, described below, by notice to Polymetal during the one month period immediately following the first anniversary of completion at a price per consideration share equal to US\$9.57027. On completion Polymetal recognised the repurchase obligation at the net present value of maximum repayment of US\$300 million, which approximated to US\$273 million, with a corresponding decrease in equity. At the same time the Group recognised the seller put option fair value in amount of US\$55 million within consideration transferred with corresponding increase in equity.

The put option had an exercise period from 4 September to 4 October 2015.

In September 2015 the Group agreed to the following settlement mechanism for the put option:

- Polymetal settled the full contractual put option liability to the Seller and delivered a cash payment in the amount of US\$300 million;
- Simultaneously, Polymetal transferred the right to receive consideration shares to Otkritie Investments Cyprus Limited in exchange for a cash consideration of US\$232 million. The cash consideration payable by Otkritie to Polymetal represented the average closing price of the Polymetal shares for the agreed quotation period being one month ended five business days before the date of signing the assignment agreement, which was US\$7.41 per share, multiplied by the number of Consideration Shares.

As a result the net amount of US\$68 million was paid by Polymetal and the consideration shares remained in issue. On the put option being exercised, both the liability of US\$300 million and the corresponding balance in equity of US\$219 million were derecognised. After the cash payment has been taken into account, the balancing figure of US\$14 million was recognised within retained earnings.

PRIMORSKOYE

In July 2015 Polymetal purchased a 100% interest in Primorskoye LLC, the company holding the licence for the Primorskoye silver-gold property located in the Magadan region of Russia from Decamor Investments Limited. The consideration for the acquisition comprised the initial consideration of US\$4 million payable by issuing 533,301 new Polymetal International plc shares and the deferred conditional cash

consideration payable in February 2017. The deferred consideration will be determined as the higher of US\$13,333 per tonne of contained silver equivalent (translating into US\$0.415 per silver equivalent ounce) based on the audited reserves estimate of the deposit, and US\$8 million.

Primorskoye did not meet the definition of a business pursuant to IFRS 3, as it represents acquisition of mining license though a non-operating corporate entity, and thus it was accounted for as an acquisition of a group of assets. The Group purchased mineral rights of US\$11 million.

LV GOLD MINING

In April 2015 the Group purchased a 25% stake in CJSC LV Gold Mining, the company owning the Lichkvaz exploration licence in Armenia (including related shareholder loans). The consideration comprised 429,260 shares equal to US\$4 million. Polymetal has also entered into an 'earn-in' agreement for financing of exploration, technical research and a JORC feasibility study in exchange for a right to increase its share in the project up to 50% after the completion of these tasks. The arrangements constituted a joint venture and the investment was accounted for using the equity method at cost of US\$4 million as of 30 June 2015.

On 11 November 2015, Polymetal signed an agreement to purchase the remaining 75% of LV Gold mining shares. The purchase price comprised 1,047,756 Polymetal International plc shares and a deferred consideration in an amount equal to 2% of value of precious metals in the ore extracted from the Lichkvaz deposit in the future during the life of mine. Under the contract the seller has also assigned to Polymetal an intercompany loan receivable of US\$0.3 million in exchange for additional 37,097 Polymetal International plc shares. Total consideration payable in shares was valued at US\$9 million and the contingent consideration was valued at US\$5 million.

LV Gold Mining did not meet the definition of a business pursuant to IFRS 3, as it represents acquisition of mining license though a non-operating corporate entity, thus it was accounted for as an acquisition of a group of assets. The acquisition was achieved in stages and accounted for at cost which was the total of the cost of the original 25% interest and of the additional 75% interest. The Group purchased mineral rights of US\$20 million.

DISPOSAL OF SUBSIDIARY
KHAKANDJINSKOYE LLC

On 26 October 2015 the Group sold its subsidiary Khakandjinskoye LLC, which held the Khakanja licence, for the cash consideration of US\$0.5 million to an unrelated party. Total net assets disposed of amounted to US\$(0.7) million, resulting in a gain on disposal of subsidiary amounting to US\$1.2 million.

5. SEGMENT INFORMATION

The Group has nine reportable segments:

- Voro (CJSC Gold of Northern Urals);
- Okhotsk operations (LLC Okhotskaya Mining and Exploration Company; Svetloye LLC);
- Dukat (JSC Magadan Silver)
- Omolon (Omolon Gold Mining Company LLC);
- Varvara (JSC Varvarinskoye; JSC Komarovskoye Mining Company);
- Amursk/Albazino (Albazino Resources Ltd, Amur Hydrometallurgical Plant LLC);
- Mayskoye (Mayskoye Gold Mining Company LLC);
- Kyzyl (Bakyrchik Mining Venture LLP, Inter Gold Capital LLP); and
- Armenia ('Kapan MPC' CJSC, 'LV Gold Mining' CJSC).

Reportable segments are determined based on the Group's internal management reports and are separated based on the Group's geographical structure. Minor companies and activities (management, exploration, purchasing and other companies) which do not meet the reportable segment criteria are disclosed within corporate and other segment. Each segment is engaged in gold, silver or copper mining and related activities, including exploration, extraction, processing and reclamation. The Group's segments are based in the Russian Federation, Kazakhstan and Armenia.

The measure which management and the Chief Operating Decision Maker (the CODM) use to evaluate the performance of the Group is segment Adjusted EBITDA, which is defined as profit for the period adjusted for depreciation and amortisation, write-downs and reversals of inventory to net realisable value, share-based compensation expenses, rehabilitation expenses, bad debt allowance, gains or losses arising on acquisition or disposal of subsidiaries, foreign exchange gains or losses, changes in the fair value of contingent consideration, finance income, finance costs, income tax expenses and other tax exposure accrued within other operating expenses. The accounting policies of the reportable segments are consistent with those of the Group's accounting policies under IFRS.

Revenue shown as corporate and other comprises, principally, intersegment revenue relating to the supply of inventories, spare parts and fixed assets, and rendering management services to the Group's production entities. Intersegment revenue is recognised based on costs incurred plus a fixed margin basis. External revenue shown within corporate and other represents revenue from services provided to third parties by the Group's non-mining subsidiaries.

Business segment current assets and liabilities, other than current inventory, are not reviewed by the CODM and therefore are not disclosed in these consolidated financial statements. The segment adjusted EBITDA reconciles to the profit before income tax as shown on the next page.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
CONTINUED

5. SEGMENT INFORMATION CONTINUED

The segment adjusted EBITDA reconciles to the profit before income tax as follows:

	Voro	Okhotsk	Dukat	Omolon	Varvara	Amursk/ Albazino	Armenia	Mayskoye	Kyzyl	Total reportable segments	Corporate and other	Intersegment operations and balances	Total
Period ended 31 December 2016 (US\$m)													
Revenue from external customers	157	179	497	207	101	294	29	119	–	1,583	–	–	1,583
Intersegment revenue	–	–	–	–	–	6	–	–	–	6	196	(202)	–
Cost of sales, excluding depreciation, depletion and write-down of inventories to net realisable value	36	82	188	78	61	121	19	96	–	681	134	(149)	666
Cost of sales	47	98	224	112	72	160	23	125	–	861	134	(149)	846
Write-down of metal inventories to net realisable value	–	(5)	1	(14)	–	–	–	(3)	–	(21)	–	–	(21)
Depreciation included in cost of sales	(11)	(10)	(37)	(20)	(11)	(37)	(4)	(22)	–	(152)	–	–	(152)
Write-down of non-metal inventories to net realisable value	–	(1)	–	1	–	(2)	–	(4)	–	(6)	–	–	(6)
Rehabilitation expenses	–	–	–	(1)	–	–	–	–	–	(1)	–	–	(1)
General, administrative and selling expenses, excluding depreciation, amortisation and share based compensation	4	7	10	7	4	7	3	6	5	53	69	(12)	110
General, administrative and selling expenses	10	13	16	13	5	14	3	12	6	92	79	(51)	120
Intercompany management services	(6)	(5)	(6)	(6)	(1)	(7)	–	(6)	–	(37)	(2)	39	–
Depreciation included in SGA	–	(1)	–	–	–	–	–	–	(1)	(2)	(1)	–	(3)
Share based compensation	–	–	–	–	–	–	–	–	–	–	(7)	–	(7)
Other operating expenses excluding additional tax charges	4	1	16	6	–	5	1	4	3	40	10	(2)	48
Other operating expenses	5	1	2	6	–	5	3	3	3	28	10	(2)	36
Bad debt allowance	–	–	–	–	–	–	–	–	–	–	–	–	–
Additional mining taxes and VAT exposures, penalties and accrued interest	(1)	–	14	–	–	–	(2)	1	–	12	–	–	12
Share of income of associates and joint ventures	–	–	–	–	–	–	–	–	–	–	–	–	–
Adjusted EBITDA	113	89	283	116	36	167	6	13	(8)	815	(17)	(39)	759
Depreciation expense	11	11	37	20	11	37	4	22	1	154	1	–	155
Rehabilitation expenses	–	–	–	1	–	–	–	–	–	1	–	–	1
Write-down of non-metal inventories to net realisable value	–	1	–	(1)	–	2	–	4	–	6	–	–	6
Write-down of metal inventories to net realisable value	–	5	(1)	14	–	–	–	3	–	21	–	–	21
Share-based compensation	–	–	–	–	–	–	–	–	–	–	7	–	7
Bad debt allowance	–	–	–	–	–	–	–	–	–	–	–	–	–
Additional mining taxes and VAT exposures, penalties and accrued interest	1	–	(14)	–	–	–	2	(1)	–	(12)	–	–	(12)
Operating profit/(loss)	101	72	261	82	25	128	–	(15)	(9)	645	(25)	(39)	581
Net foreign exchange gains													65
Change in fair value of contingent consideration liability													(22)
Finance income													3
Finance costs													(63)
Profit before tax													564
Income tax expense													(169)
Profit for the financial period													395
Current metal inventories	38	43	52	49	43	62	6	29	–	322	–	(7)	315
Current non-metal inventories	5	32	28	30	13	18	7	28	3	164	23	(9)	178
Non-current segment assets:													
Property, plant and equipment, net	49	96	182	92	217	281	50	162	556	1,685	144	(24)	1,805
Goodwill	–	–	5	–	–	–	–	12	–	17	–	–	17
Non-current inventories	2	7	8	78	4	6	1	8	–	114	–	(1)	113
Investments in associates and joint ventures	–	–	–	–	–	–	–	–	–	–	25	–	25
Total segment assets	94	178	275	249	277	367	64	239	559	2,302	192	(41)	2,453
Additions to non-current assets:													
Property, plant and equipment	7	32	33	23	16	41	13	22	92	279	9	–	288
Acquisitions	–	–	–	–	140	–	21	–	–	161	10	–	171

	Voro	Okhotsk	Dukat	Omolon	Varvara	Amursk/ Albazino	Mayskoye	Kyzyl	Total reportable segments	Corporate and other	Intersegment operations and balances	Total
For the year ended 31 December 2015 (US\$m)												
Revenue from external customers	163	129	441	224	96	255	133	–	1,441	–	–	1,441
Intersegment revenue	1	–	–	1	–	9	–	–	11	212	(223)	–
Cost of sales, excluding depreciation, depletion and write-down of inventories to net realisable value	43	59	184	101	64	97	88	–	636	158	(182)	612
Cost of sales	54	70	222	135	86	128	108	–	803	158	(182)	779
Write-down of metal inventories to net realisable value	–	1	–	(6)	(8)	–	–	–	(13)	–	–	(13)
Depreciation included in cost of sales	(12)	(11)	(38)	(24)	(14)	(31)	(21)	–	(151)	–	–	(151)
Write-down of non-metal inventories to net realisable value	–	(1)	(1)	(4)	–	–	1	–	(5)	–	–	(5)
Rehabilitation expenses	1	–	1	–	–	–	–	–	2	–	–	2
General, administrative and selling expenses, excluding depreciation, amortization and share based compensation	5	20	8	7	5	7	7	7	66	64	(12)	118
General, administrative and selling expenses	11	26	15	12	6	12	11	8	101	71	(45)	127
Intercompany management services	(6)	(4)	(6)	(5)	(1)	(5)	(4)	–	(31)	(2)	33	–
Depreciation included in SGA	–	(2)	(1)	–	–	–	–	(1)	(4)	(1)	–	(5)
Share based compensation	–	–	–	–	–	–	–	–	–	(4)	–	(4)
Other operating expenses excluding additional tax charges	1	2	9	5	2	8	4	7	38	(6)	16	48
Other operating expenses	2	2	4	10	2	8	5	7	40	(5)	16	51
Bad debt allowance	(1)	–	–	(5)	–	–	–	–	(6)	(1)	–	(7)
Additional mining taxes and VAT exposures, penalties and accrued interest	–	–	5	–	–	–	(1)	–	4	–	–	4
Share of income of associates and joint ventures	–	–	–	–	–	–	–	–	–	(4)	–	(4)
Adjusted EBITDA	115	48	240	112	25	152	34	(14)	712	(8)	(45)	659
Depreciation expense	12	13	39	24	14	31	21	1	155	1	–	156
Rehabilitation expenses	(1)	–	(1)	–	–	–	–	–	(2)	–	–	(2)
Write-down of non-metal inventories to net realisable value	–	1	1	4	–	–	(1)	–	5	–	–	5
Write-down of metal inventories to net realisable value	–	(1)	–	6	8	–	–	–	13	–	–	13
Share-based compensation	–	–	–	–	–	–	–	–	–	4	–	4
Bad debt allowance	1	–	–	5	–	–	–	–	6	1	–	7
Additional mining taxes and VAT exposures, penalties and accrued interest	–	–	(5)	–	–	–	1	–	(4)	–	–	(4)
Operating profit / (loss)	103	35	206	73	3	121	13	(15)	539	(14)	(45)	480
Net foreign exchange losses												(133)
Gain on disposal of subsidiary												1
Change in fair value of contingent consideration liability												4
Finance income												5
Finance costs												(81)
Profit before tax												276
Income tax expense												(55)
Profit for the financial period												221
Current metal inventories	28	31	50	28	21	38	28	–	224	–	(2)	222
Current non-metal inventories	4	25	20	24	10	13	26	1	123	15	(7)	131
Non-current segment assets:												
Property, plant and equipment, net	46	61	169	70	68	241	136	460	1,251	127	(18)	1,360
Goodwill	–	–	4	–	–	–	10	–	14	–	–	14
Non-current inventories	1	13	6	64	4	6	7	–	101	–	(2)	99
Investments in associates and joint ventures	–	–	–	–	–	–	–	–	–	2	–	2
Total segment assets	79	130	249	186	103	298	207	461	1,713	144	(29)	1,828
Additions to non-current assets:												
Property, plant and equipment	7	36	33	28	20	38	21	32	215	10	–	225
Acquisition of group of assets	–	–	11	–	–	–	–	–	11	20	–	31

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

6. REVENUE

Revenue analysed by geographical regions of customers is presented below:

	Year ended	
	31 December 2016 US\$m	31 December 2015 US\$m
Sales within the Russian Federation	899	1,052
Sales to Kazakhstan	295	217
Sales to Europe	205	33
Sales to East Asia	184	139
Total	1,583	1,441

Included in revenues for the year ended 31 December 2016 are revenues which arose from sales to three of the Group's largest customers amounting to US\$416 million, US\$281 million and US\$206 million, respectively (2015: US\$501 million, US\$185 million and US\$162 million, respectively). Presented below is an analysis of revenue from gold, silver, zinc and copper sales:

	Year ended 31 December 2016				Year ended 31 December 2015			
	Thousand ounces/ tonnes (unaudited) shipped	Thousand ounces/ tonnes (unaudited) payable	Average price (U.S. Dollar per troy ounce/ tonne payable) (unaudited)	US\$m	Thousand ounces/ tonnes (unaudited) shipped	Thousand ounces/ tonnes (unaudited) payable	Average price (U.S. Dollar per troy ounce/ tonne payable) (unaudited)	US\$m
Gold (thousand ounces)	882	880	1,216	1,070	875	864	1,127	974
Silver (thousand ounces)	31,099	30,666	16.30	500	31,494	31,190	14.75	460
Copper (tonnes)	1,689	1,634	4,896	8	1,578	1,488	4,704	7
Zinc (tonnes)	3,246	2,800	1,786	5	–	–	–	–
Total				1,583				1,441

7. COST OF SALES

	Year ended	
	31 December 2016 US\$m	31 December 2015 US\$m
Cash operating costs		
On-mine costs (Note 8)	320	267
Smelting costs (Note 9)	259	261
Purchase of ore and semi-finished goods from third parties	27	5
Purchase of ore from related parties (Note 32)	11	–
Mining tax	82	97
Total cash operating costs	699	630
Depreciation and depletion of operating assets (Note 10)	162	154
Rehabilitation expenses (Note 25)	1	(2)
Total costs of production	862	782
Increase in metal inventories	(51)	(27)
Write-down of metal inventories to net realisable value (Note 21)	21	13
Write-down of non-metal inventories to net realisable value (Note 21)	6	5
Idle capacities and abnormal production costs	8	6
Total	846	779

Mining tax includes royalties payable in Russian Federation, Kazakhstan and Armenia. Mining tax in Russian Federation and Kazakhstan is calculated based on the value of the precious metals extracted in the period. This value is usually determined based on the realised selling price of precious metals or, in case if there were no sales during the period, cost of production of metals extracted (Russian Federation) or the average market price (Kazakhstan) during the period. Royalty payable in Armenia is calculated as a percentage of actual sales during the reporting period.

Mining tax in respect of the metal inventories produced or sold during the year is recognised within cost of sales, while the additional mining tax accruals in respect of various disputes with tax authorities are recognised within other expenses (see Note 12).

Idle capacities and abnormal production costs were expensed as incurred and relate to Mayskoye where the processing plant was stopped from November 2015 to February 2016 while underground mining was ramping up due to the redevelopment of underground workings using a new mining method and idle capacities when processing plants are stopped for general maintenance.

8. ON-MINE COSTS

	Year ended	
	31 December 2016 US\$m	31 December 2015 US\$m
Services	139	120
Labour	97	78
Consumables and spare parts	79	67
Other expenses	5	2
Total (Note 7)	320	267

9. SMELTING COSTS

	Year ended	
	31 December 2016 US\$m	31 December 2015 US\$m
Consumables and spare parts	114	115
Services	93	94
Labour	50	50
Other expenses	2	2
Total (Note 7)	259	261

10. DEPLETION AND DEPRECIATION OF OPERATING ASSETS

	Year ended	
	31 December 2016 US\$m	31 December 2015 US\$m
On-Mine	117	104
Smelting	45	50
Total (Note 7)	162	154

Depreciation of operating assets excludes depreciation relating to non-operating assets (included in general, administrative and selling expenses) and depreciation related to assets employed in development projects where the charge is capitalised. Depreciation expense, which is excluded from the Group's calculation of Adjusted EBITDA (see Note 5), also excludes amounts absorbed into unsold metal inventory balances.

11. GENERAL, ADMINISTRATIVE AND SELLING EXPENSES

	Year ended	
	31 December 2016 US\$m	31 December 2015 US\$m
Labour	87	88
Services	10	14
Share based compensation	7	4
Depreciation	3	5
Other	13	16
Total	120	127

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

CONTINUED

12. OTHER OPERATING EXPENSES, NET

	Year ended	
	31 December 2016 US\$m	31 December 2015 US\$m
Provision for investment in Special Economic Zone	14	–
Taxes, other than income tax	11	12
Exploration expenses	10	24
Social payments	10	8
Reversal of additional mining taxes, VAT, penalties and accrued interest	(12)	(4)
Bad debt allowance	–	7
Housing and communal services	4	4
Loss on disposal of property, plant and equipment	1	1
Change in estimate of environmental obligations (Note 25)	(5)	(4)
Other expenses	3	3
Total	36	51

From 1 January 2016 Omolon Gold Mining Company LLC and JSC Magadan Silver are entitled to the decreased statutory Income tax rate of 18% for the operations held in the Special Economic zone of the Russian Far East, as well as decreased mining tax rate (paying 60% of standard mining tax rates). In return for obtaining this tax relief the members of the regional free economic zone are obliged to invest 50% of their tax savings each year to the Special economic zone Development Programme, amounting to US\$14 million in the reporting year.

Mining taxes, VAT, penalties and accrued interest have been accrued in respect of various disputes with the Russian and Armenian tax authorities. During the year ended 31 December 2016 following the favourable court decisions the Group has recognised the reversal of the previously recognised and paid additional mining tax charge at Magadan Silver amounting to US\$14 million.

During the year ended 31 December 2015 the Group partially released several mining tax provisions at Magadan Silver following the completion of the tax audits.

Total provision for tax exposures, penalties and accrued interest as of 31 December 2016 is US\$14 million (2015: US\$3.5 million), which includes US\$11 million of mining tax exposures (including interest and penalties), which were identified and recognised at Kapan mine purchase price allocation (Note 4). As of 31 December total provision at Kapan amounts to US\$13 million, which includes US\$2 million of interest and penalties accrued from acquisition to the reporting date.

Exploration expenses include write downs of US\$1 million (2015: US\$8 million) recognised within Exploration and Development assets (Note 18). Operating cash flow spent on exploration activities amounts to US\$11 million (2015: US\$13 million).

13. EMPLOYEE COSTS

	Year ended	
	31 December 2016 US\$m	31 December 2015 US\$m
Wages and salaries	215	199
Social security costs	51	49
Share based compensation	7	4
Total payroll costs	273	252
Reconciliation:		
Less: employee costs capitalised	(26)	(25)
Less: employee costs absorbed into unsold metal inventory balances	(5)	(4)
Employee costs included in operating costs	242	223

The weighted average number of employees during the year ended 31 December 2016 and year ended 31 December 2015 was:

	Year ended	
	31 December 2016 Number	31 December 2015 Number
Dukat	1,910	1,856
Amursk/Albazino	1,356	1,286
Okhotsk operations	1,263	1,140
Varvara	1,111	789
Mayskoye	895	828
Voro	878	924
Armenia	770	–
Omolon	759	752
Kyzyl	406	414
Corporate and other	1,465	1,303
Total	10,813	9,292

Compensation of key management personnel is disclosed within Note 32.

14. AUDITOR'S REMUNERATION

	Year ended	
	31 December 2016 US\$m	31 December 2015 US\$m
Fees payable to the auditor and their associates for the audit of the Company's Annual Report		
United Kingdom	0.30	0.31
Overseas	0.75	0.68
Total audit fees	1.05	0.99
Audit-related assurance services – half year review	0.39	0.40
Total audit and half-year review fees	1.44	1.39
Other services	0.03	0.03
Total non-audit fees	0.03	0.03
Total fees	1.47	1.42

15. FINANCE COSTS

	Year ended	
	31 December 2016 US\$m	31 December 2015 US\$m
Interest expense on borrowings	59	52
Unwinding discount on repurchase obligation (Note 4)	–	24
Unwinding of discount on environmental obligations (Note 25)	4	5
Total	63	81

Interest expense on borrowings excludes borrowing costs capitalised in the cost of qualifying assets of US\$5 million and US\$4 million during the years ended 31 December 2016 and 2015, respectively. These amounts were calculated based on the Group's general borrowing pool and by applying an effective interest rate of 4.33% and 4.06%, respectively, to cumulative expenditure on such assets.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
CONTINUED

16. INCOME TAX

The amount of income tax expense for the years ended 31 December 2016 and 31 December 2015 recognised in profit and loss is as follows:

Table with 3 columns: Description, 31 December 2016 US\$m, 31 December 2015 US\$m. Rows include Current income taxes, Deferred taxes, and Total.

A reconciliation between the reported amounts of income tax expense attributable to income before income tax is as follows:

Table with 3 columns: Description, 31 December 2016 US\$m, 31 December 2015 US\$m. Rows include Profit before income tax, Statutory income tax expense, Effect of dissolution of subsidiary, Non-deductible interest expense, Current year losses not recognised, Effect of Special Economic Zone, Effect of different tax rates, Non-taxable net foreign exchange gains, Other non-taxable income, and Total income tax expense.

The actual tax expense differs from the amount which would have been determined by applying the statutory rate of 20% for the Russian Federation, Kazakhstan and Armenia to profit before income tax as a result of the application of relevant jurisdictional tax regulations, which disallow certain deductions which are included in the determination of accounting profit.

As from 1 January 2016 Omolon Gold Mining Company LLC and JSC Magadan Silver are entitled to the decreased statutory income tax rate of 18% for the operations held in the Special Economic zone of the Russian Far East (Note 12), the rate of 18% was used in calculation of income tax provision and deferred tax positions for those entities.

For several entities, the tax calculation is prepared in local currencies that differ from the functional currency of the entity. In the year ended 31 December 2015 this resulted in exchange gains and losses excluded from tax computations in the local currency that gave rise to significant permanent differences.

In the normal course of business, the Group is subject to examination by tax authorities throughout the Russian Federation and Kazakhstan. Of the large operating companies of the Group, the tax authorities have audited LLC Okhotskaya Mining and Exploration Company CJSC up to 2014, Omolon Gold Mining Company LLC up to 2013, CJSC Gold of Northern Urals and CJSC Magadan Silver up to 2012, Mayskoye Gold Mining Company LLC up to 2010, and JSC Varvarinskoye for the period up to 2010.

TAX EXPOSURES RECOGNISED IN INCOME TAX

During the year ended 31 December 2016 and the year ended 31 December 2015 no individual significant exposures were identified as probable and provided for. Management has identified a total exposure (covering taxes and related interest and penalties) of approximately US\$4 million in respect of uncertain tax positions (31 December 2015: US\$16 million) which relate to income tax.

INCOME TAX AMOUNTS INCLUDED IN OTHER COMPREHENSIVE INCOME

An analysis of tax by individual item presented in the Consolidated statement of comprehensive income is presented below:

Table with 3 columns: Description, 31 December 2016 US\$m, 31 December 2015 US\$m. Rows include Net foreign exchange losses on net investment in foreign operation, Current tax (benefit)/expense, Deferred tax (benefit), and Total income tax recognised in other comprehensive income.

Current and deferred tax assets recognised within other comprehensive income relates to the tax losses originated by foreign currency exchange losses, allowable for tax purposes and generated by monetary items that forms part of the intragroup net investment in the foreign operation.

DEFERRED TAXATION

Deferred taxation is attributable to the temporary differences that exist between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes.

The following are the major deferred tax liabilities and assets recognised by the Group and movements thereon during the reporting period.

Table with 10 columns: Description, Environmental obligation US\$m, Inventories US\$m, Property, plant, and equipment and other non-current assets US\$m, Trade and other payables US\$m, Tax losses US\$m, Long-term loans and payables US\$m, Intercompany loans US\$m, Other US\$m, Total US\$m. Rows include At 1 January 2015, Charge to income statement, Recognised in other comprehensive income, Exchange differences, At 31 December 2015, Charge to income statement, Acquisition (Note 4), Recognised in other comprehensive income, Exchange differences, and At 31 December 2016.

Deferred tax assets and liabilities are offset where the Group has a legally enforceable right to do so. The following analysis shows deferred tax balances presented for financial reporting purposes:

Table with 3 columns: Description, 31 December 2016 US\$m, 31 December 2015 US\$m. Rows include Deferred tax liabilities, Deferred tax assets, and Total.

Tax losses carried forward represent amounts available for offset against future taxable income generated by ZK Mayskoye LLC, JSC Varvarinskoye, Bakyrchik Mining Venture LLP and CJSC Kapan MPC during the period up to 2026. Each legal entity within the Group represents a separate tax-paying component for income tax purposes.

The Group believes that recoverability of the recognised deferred tax asset (DTA) of US\$105 million at 31 December 2016 is more likely than not based upon expectations of future taxable income in the Russian Federation and Kazakhstan and available tax planning strategies.

Losses incurred in certain taxable entities in recent years have created a history of losses as of 31 December 2016. The Group has concluded that there is sufficient evidence to overcome the recent history of losses based on forecasts of sufficient taxable income in the carry-forward period.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

CONTINUED

16. INCOME TAX CONTINUED

The Group's estimate of future taxable income is based on established proven and probable reserves which can be economically developed. The related detailed mine plans and forecasts provide sufficient supporting evidence that the Group will generate taxable earnings to be able to fully realise its net DTA even under various stressed scenarios. The amount of the DTA considered realisable, however, could be reduced in the near term if estimates of future taxable income during the carryforward period are reduced due to delays in production start dates, decreases in ore reserve estimates, increases in environmental obligations, or reductions in precious metal prices.

Effective from 1 January 2017 there are changes introduced to the Russian Federation tax law regarding loss carryforwards. Loss carryforwards will be limited to 50% of taxable profit in tax years 2017 through 2020. From 2021 the limitation will expire and it will be possible to fully utilise loss carryforwards against the corporate tax base in a given year. In addition to the above, the current 10-year carryforward period for losses will be eliminated, meaning that losses incurred from 2007 can be carried forward for an indefinite period until fully utilised.

The Group's tax losses carried forward are allocated to the future periods as follows:

	31 December 2016 US\$m	31 December 2015 US\$m
Year ended 31 December 2016	–	3
31 December 2017	–	4
31 December 2018	–	11
31 December 2019	10	18
31 December 2020	9	17
31 December 2021	16	24
31 December 2022	20	37
31 December 2023	18	64
31 December 2024	73	97
31 December 2025	361	373
31 December 2026	18	–
Total loss carried forward for tax purposes	525	648

No deferred tax asset has been recognised in respect of remaining US\$96 million (2015: US\$54 million) as it is not considered probable that there will be future taxable profits against which the losses can be utilised. Increase in 2016 is related to the Svetloye tax losses, accumulated by 1 January 2016, were the entity has received tax relief as Regional Investment Project and is entitled to the statutory income tax rate of 0% up to 2021, thus will not be able to utilise accumulated losses. Included in unrecognised tax losses are losses of US\$30 million that mainly expires in 2025. Other losses may be carried forward indefinitely in accordance with enacted changes to Russian Federation legislation described above.

The deferred tax liabilities for taxes that would be payable on the unremitted earnings of certain of the Group subsidiaries have not been recognised as the Group has determined that the undistributed profit of its subsidiaries will not be distributed in the foreseeable future. The temporary differences associated with investments in subsidiaries, for which deferred tax liabilities have not been recognised, amount to US\$2,147 million (2015: US\$1,318 million).

17. DIVIDENDS

Dividends recognised during the years ended 31 December 2016 and 31 December 2015 are detailed in the below:

	Dividends				
	Cents per share	US\$m	Approved and deducted from the equity in	Proposed in relation to the year	Paid in
Special dividend 2014	20	84	December 2014	2014	January 2015
Final dividend 2014	13	55	May 2015	2014	May 2015
Interim dividend 2015	8	34	September 2015	2015	September 2015
Special dividend 2015	30	127	December 2015	2015	December 2015
Final dividend 2015	13	56	May 2016	2015	May 2016
Interim dividend 2016	9	38	September 2016	2016	September 2016
Special dividend 2016	15	64	December 2016	2016	December 2016
Final dividend 2016	18	77	N/A	2016	N/A
Total dividends for the year ended 31 December 2015			216	217	300
Total dividends for the year ended 31 December 2016			158	179	158

18. PROPERTY, PLANT AND EQUIPMENT

	Development assets US\$m	Exploration assets US\$m	Mining assets US\$m	Non-mining assets US\$m	Capital construction in-progress US\$m	Total US\$m
Cost						
Balance at 1 January 2015	902	117	1,564	58	79	2,720
Additions	41	11	76	5	92	225
Transfers	(58)	–	101	(3)	(40)	–
Change in decommissioning liabilities	–	–	4	–	–	4
Acquisition of group of assets (Note 4)	–	30	–	1	–	31
Disposals and write-offs incl. fully depleted mines	(2)	(6)	(160)	(2)	(1)	(171)
Translation to presentation currency	(365)	(54)	(411)	(15)	(26)	(871)
Balance at 31 December 2015	518	98	1,174	44	104	1,938
Additions	39	26	143	7	73	288
Transfers	(28)	–	73	(2)	(43)	–
Change in decommissioning liabilities	–	–	(3)	–	–	(3)
Acquisitions (Note 4)	–	10	152	9	–	171
Disposals and write-offs incl. fully depleted mines	–	(1)	(23)	(2)	(1)	(27)
Translation to presentation currency	35	7	234	9	17	302
Balance at 31 December 2016	564	140	1,750	65	150	2,669
Accumulated depreciation, amortisation and impairment						
Balance at 1 January 2015	–	–	(735)	(20)	–	(755)
Charge for the period	–	–	(173)	(4)	–	(177)
Disposals and write-offs	–	–	153	1	–	154
Transfers	–	–	(1)	1	–	–
Translation to presentation currency	–	–	196	4	–	200
Balance at 31 December 2015	–	–	(560)	(18)	–	(578)
Charge for the period	–	–	(182)	(5)	–	(187)
Disposals and write-offs incl fully depleted mines	–	–	18	1	–	19
Translation to presentation currency	–	–	(115)	(3)	–	(118)
Balance at 31 December 2016	–	–	(839)	(25)	–	(864)
Net book value						
1 January 2015	902	117	829	38	79	1,965
31 December 2015	518	98	614	26	104	1,360
31 December 2016	564	140	911	40	150	1,805

Mining assets, exploration and development assets at 31 December 2016 included mineral rights with net book value which amounted to US\$756 million (31 December 2015: US\$582 million) and capitalised stripping costs with net book value of US\$32 million (31 December 2015: US\$33 million). Mineral rights of the Group comprise assets acquired upon acquisition of subsidiaries and asset acquisitions.

No property, plant and equipment was pledged as collateral at 31 December 2016 or at 31 December 2015.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
CONTINUED

19. GOODWILL

Table with 3 columns: Description, 31 December 2016 US\$m, 31 December 2015 US\$m. Rows include Cost and Accumulated impairment losses, At 1 January, Translation effect, and At 31 December.

Goodwill has been allocated for impairment testing purposes to the following cash-generating units:

Table with 3 columns: Description, 31 December 2016 US\$m, 31 December 2015 US\$m. Rows include Mayskoye, Dukat, and Total.

The carrying amount of goodwill is reviewed annually to determine whether it is in excess of its recoverable amount. The recoverable amount of the cash-generating unit is determined based on a fair value less costs to sell calculation.

The DCF method used is based on proved and probable reserves and uses the following key assumptions:

- production volumes;
- commodity prices;
- proved and probable reserves;
- production costs;
- Rouble exchange rates; and
- discount rates.

Recoverable reserves and resources are based on the proven and probable reserves and resources in existence at the end of the year. Estimated production volumes are based on detailed life of mine plans and take into account development plans for the mines approved by management as part of the long-term planning process.

The key assumptions used as at 31 December 2016 by the Group were as follows:

COMMODITY PRICES

Commodity prices are based on latest internal forecasts, benchmarked against external sources of information. In the impairment tests performed, the flat real long-term gold and silver of US\$1,200 per ounce (2015: US\$1,100), US\$16 per ounce (2015: US\$14), respectively.

DISCOUNT RATE

The Group used a post-tax real discount rate of 9.0% (2015: 9.0%).

PRODUCTION COSTS

Production costs are based on management’s best estimates over the life of the mine, and reflect past experience.

ROUBLE EXCHANGE RATES

Management have analysed RUB/US\$ rate movements for the year ended 31 December 2016. For the purposes of the impairment test, RUB/\$US exchange rate is estimated at 60 RUB/\$US (2015: RUB/\$US 72).

SENSITIVITY ANALYSIS

For Dukat and Mayskoye management has performed an analysis as to whether a reasonably possible adverse change to any of the key assumptions would lead to impairment.

The following scenarios were considered as reasonably possible and were used for this sensitivity analysis:

- 10% simultaneous decrease in gold and silver prices over the life of mine;
- 10% decrease in Rouble exchange rates;
- 10% increase in operating expenses over the life of mine; and
- 0.5% increase in the discount rate applied.

Each of the sensitivities above has been determined by assuming that the relevant key assumption moves in isolation, and without regard to potential mine plan changes and other management decisions which would be taken to respond to adverse changes in existing management projections. An adverse change in a key assumption described above would not cause the aggregate carrying amount to exceed the aggregate recoverable amount of the cash-generating units, except for Mayskoye CGU, where a 10% decrease in gold and silver prices or a 10% strengthening of Rouble against US Dollar would cause the carrying amount to exceed the recoverable amount by US\$36 million and US\$20 million, respectively.

20. INVESTMENTS IN ASSOCIATES AND JOINT VENTURES

Table with 5 columns: Description, 31 December 2016 Voting power %, 31 December 2016 Carrying value US\$m, 31 December 2015 Voting power %, 31 December 2015 Carrying value US\$m. Rows include Nezhda, GRK Amilkan, Aktogai Mys LLC, Proeks LLC, and Total.

JSC SOUTH-VERKHoyANSK MINING COMPANY

In December 2015 Polymetal International plc entered into a joint arrangement with OJSC Polyus Gold, under which Polymetal will participate in advancing the development of the Nezhdaninskoye gold deposit (Nezhda) in Yakutia, Russia. The arrangement allows Polymetal to acquire up to 50% in the joint venture entity holding 100% of JSC South-Verkhoyansk Mining Company (‘SVMC’) through an earn-in mechanism. SVMC, which was a 100% subsidiary of Polyus Gold as of 31 December 2015, holds the mining and exploration license for the Nezhda as well as certain infrastructure adjacent to the deposit.

On 19 January 2016 Polymetal obtained a 15.3% interest in the joint venture entity holding 100% of the Company for the total cash consideration of US\$18 million.

In November 2016 Polymetal increased its share in JSC South-Verkhoyansk Mining Company to 17.66% for cash consideration of US\$3 million.

The arrangement is structured through a separate vehicle and constitutes a joint venture under IFRS 11 Joint arrangements and the investment is accounted for using the equity method.

As of 31 December 2016 the entity did not hold any significant cash balances and did not record any significant amounts of revenue, depreciation and amortisation, interest income and expenses, income tax.

GRK AMIKAN

GRK Amikan is a production company which holds 100% interest in Veduga gold deposit in the Krasnoyarsk region of the Russian Federation. During the year ended 31 December 2016 the Group has purchased ore from GRK Amikan for the total amount of US\$11 million (2015: nil) (Note 32) and eliminated unrealised profit on inventories not yet processed against its share of net profit in GRK Amikan.

AKTOGAI MYS LLC

In June 2015 the Group signed an agreement to purchase 25% stake in the Aktogai Mys LLC, company owning the Dolinnoye exploration licence in Kazakhstan (including related shareholder loans). Polymetal has also entered into an ‘earn-in’ agreement for financing of exploration and technical research and may increase its share in the project up to 50% after the completion of these tasks. The arrangements constitute a joint venture and the investment is accounted for using the equity method.

The Group’s share of losses of Aktogai Mys LLC exceeded its interest in the joint venture due to foreign currency exchange losses recognised by Aktogai Mys LLC, therefore the carrying amount of the investment was written down to nil. Total accumulated unrecognised Group’s share of loss as of 31 December 2016 is nil (2015: US\$1 million).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

CONTINUED

20. INVESTMENTS IN ASSOCIATES AND JOINT VENTURES CONTINUED

PROEKS LLC

In November 2015 the Group acquired 24.9% share in a diamond exploration project located in North-West of Russian Federation for the cash consideration of US\$2 million. The Group determined that it has significant influence in the entity and the investment is accounted for using the equity method.

GRK Amikan, Aktogai Mys LLC and Proeks LLC do not represent equity method investments that are individually material.

The following table summarises the aggregate financial position and the Group's share of net profit/(losses) of the investments:

	Nezhda	Non-significant investments	Total	Total
	31 December 2016 US\$m	31 December 2016 US\$m	31 December 2016 US\$m	31 December 2015 US\$m
Non-current assets	48	51	99	54
Current assets	9	50	59	18
Non-current liabilities	(7)	(80)	(87)	(79)
Current liabilities	(1)	(8)	(9)	(3)
Equity	(49)	(13)	(62)	10
Revenue	–	41	41	17
Net income/(loss)	(2)	12	10	(24)
Group's share in investment net income/(loss)less prior year unrecognised losses	–	2	2	(8)
Share of profit recognised for the year less inventories unrealised profit eliminations	–	–	–	(4)
Unrecognised share of losses for the year	–	–	–	(4)

21. INVENTORIES

	31 December 2016 US\$m	31 December 2015 US\$m
Inventories expected to be recovered after twelve months		
Consumables and spare parts	33	26
Ore stock piles	80	69
Work in-process	–	4
Total non-current inventories	113	99
Inventories expected to be recovered in the next twelve months		
Ore stock piles	157	97
Copper, gold and silver concentrate	95	74
Work in-process	42	30
Metal for refinery	6	14
Refined metals	3	–
Doré	12	7
Total metal inventories	315	222
Consumables and spare parts	178	131
Total	493	353

WRITE-DOWNS OF METAL INVENTORIES TO NET REALISABLE VALUE

The Group recognised the following (write-downs)/reversals to net realisable value of its metal inventories:

	Year ended 31 December 2016				Year ended 31 December 2015
	Okhotsk operations US\$m	Dukat US\$m	Omolon US\$m	Mayskoye US\$m	Total operating segments US\$m
Ore stock piles	(5)	1	(9)	(1)	(14)
Ore in heap leach piles	–	–	(5)	–	(5)
Copper, gold and silver concentrate	–	–	–	(2)	(2)
Total	(5)	1	(14)	(3)	(21)

The key assumptions used as at 31 December 2016 in determining net realisable value of inventories (including the commodity price assumptions for long-term stockpiles) were consistent with those used in the goodwill impairment review (Note 19). For short-term metal inventories applicable forward prices as of 31 December 2016 were used.

During the year ended 31 December 2016 the Group provided for obsolete consumables and spare parts inventory in the amount of US\$6 million (year ended 31 December 2015: write-down of US\$5 million).

The amount of inventories held at net realisable value at 31 December 2016 is US\$45 million (31 December 2015: US\$26 million).

22. TRADE AND OTHER RECEIVABLES

	31 December 2016 US\$m	31 December 2015 US\$m
Receivables from provisional copper, gold and silver concentrate sales	35	12
Other trade receivables	3	–
Non-trade receivables	22	15
Short-term loans provided to related parties	7	–
Short-term loans provided to third parties	6	15
Total trade and other receivables	73	42
Less: Allowance for doubtful debts	(3)	(3)
Total	70	39

The average credit period on sales of copper, gold and silver concentrate at 31 December 2016 was 20 days (2015: 21 days). No interest is charged on trade receivables. The Group's allowance for doubtful debt relates to its non-trade receivables. There are no trade receivables either past due or impaired as at 31 December 2016 (31 December 2015: US\$ nil).

23. CASH AND CASH EQUIVALENTS

	31 December 2016 US\$m	31 December 2015 US\$m
Bank deposits – U.S. dollar	31	21
Current bank accounts – RUB	8	3
– foreign currencies	9	28
Total	48	52

Bank deposits as at 31 December 2016 bear an interest rate of 0.3%-6% per annum for US Dollar denominated deposits and 16% for KZT deposits (2015: 0.3%-5.56% per annum for US Dollar deposits) with an average maturity at inception of 15 days (2015: 23 days) with US\$14 million being demand deposits.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

CONTINUED

24. BORROWINGS

Borrowings at amortised cost:

Actual interest rate at 31 December				31 December 2016			31 December 2015		
Type of rate	2016	2015		Current US\$m	Non-current US\$m	Total US\$m	Current US\$m	Non-current US\$m	Total
Secured loans from third parties									
<i>U.S. Dollar denominated</i>	floating	3.85%	4.00%	98	638	736	263	584	847
<i>U.S. Dollar denominated</i>	fixed	4.10%	NA	–	61	61	–	–	–
Total				98	699	797	263	584	847
Unsecured Loans from third parties									
<i>U.S. Dollar denominated</i>	floating	3.96%	3.34%	–	500	500	24	406	430
<i>U.S. Dollar denominated</i>	fixed	7.50%	7.50%	–	78	78	–	73	73
<i>EUR denominated</i>	fixed	2.85%	NA	–	3	3	–	–	–
Total				–	581	581	24	479	503
				98	1,280	1,378	287	1,063	1,350

BANK LOANS

The Group has a number of borrowing arrangements with various lenders. These borrowings consist of unsecured and secured loans and credit facilities denominated in U.S. Dollars. Where security is provided it is in form of a pledge of revenue from certain sales agreements.

Movements in borrowings for the year ended 31 December 2016 are reconciled as follows:

1 January 2016 US\$m	Borrowings obtained US\$m	Repayments of borrowings US\$m	Net foreign exchange losses US\$m	Translation to presentation currency US\$m	Arrangement fee amortisation US\$m	31 December 2016 US\$m
1,350	1,436	(1,410)	108	(108)	2	1,378

At 31 December 2016, the Group had undrawn borrowing facilities of US\$998 million (31 December 2015: US\$1,196 million). The Group complied with its debt covenants throughout 2016 and 2015.

The table below summarises maturities of borrowings:

	31 December 2016 US\$m	31 December 2015 US\$m
Year ended, 31 December 2016	–	287
31 December 2017	98	157
31 December 2018	632	669
31 December 2019	538	221
31 December 2020	110	16
Total	1,378	1,350

25. ENVIRONMENTAL OBLIGATIONS

Environmental obligations include decommissioning and land restoration costs and are recognised on the basis of existing project business plans as follows:

	31 December 2016 US\$m	31 December 2015 US\$m
Opening balance	33	46
Changes in estimates for the year:		
Change in estimate of environmental obligations	(5)	(4)
Decommissioning liabilities recognised as increase in PPE	(3)	4
Rehabilitation liabilities	1	(2)
Effect of unwinding of discount	4	5
Acquired in business combinations	2	–
Amounts paid in the year	–	(1)
Disposal of subsidiary (Note 4)	–	(1)
Translation effect	5	(14)
Closing balance	37	33

The principal assumptions are related to Russian Rouble, Kazakh Tenge and Armenian Dram projected cash flows. The assumptions used for the estimation of environmental obligations were as follows:

	2016	2015
Discount rates	7.1%-14.67%	7.1%-12.5%
Inflation rates	(0.45%)-8.5%	4.0%-8.7%
Expected mine closure dates	1-34 years	1-26 years

The Group does not hold any assets that are legally restricted for purposes of settling environmental obligations.

26. TRADE PAYABLES AND ACCRUED LIABILITIES

	31 December 2016 US\$m	31 December 2015 US\$m
Trade payables	51	37
Accrued liabilities	36	26
Labour liabilities	12	8
Provision for investment in Special Economic Zone (Note 12)	14	–
Consideration payable to Dundee (Note 4)	5	–
Account payable to related parties	4	–
Advances received	3	2
Other payables	8	4
Total	133	77

In 2016, the average credit period for payables was 31 Days (2015: 29 days). There was no interest charged on the outstanding payables balance during the credit period. The Group has financial risk management policies in place, which include budgeting and analysis of cash flows and payment schedules to ensure that all amounts payable are settled within the credit period.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
CONTINUED

27. COMMITMENTS AND CONTINGENCIES

COMMITMENTS

CAPITAL COMMITMENTS

The Group’s budgeted capital expenditure commitments as at 31 December 2016 amounted to US\$64 million (2015: US\$18 million).

During the year ended 31 December 2016 the Group signed a memorandum with East-Kazakhstan Oblast Administration (local Kazakhstan government), where the Group (namely its subsidiaries Bakyrchik Mining Venture LLP and Inter Gold Capital LLP) agrees to participate in financing of certain social and infrastructure development project of the region. During the year ended 31 December 2016 the Group paid US\$2 million under this programme and total social expenses commitment at 31 December 2016 amounts to US\$31 million, allocated to the future periods as follows:

Table with 2 columns: Commitment period, 31 December 2016 US\$m. Rows: Within one year (2), From one to five years (20), Thereafter (9), Total (31).

FORWARD SALE COMMITMENTS

The Group has certain physical gold and silver forward sale commitments which are priced at the prevailing market price, calculated with reference to the LBMA or LME gold price, which are accounted for as executed as the Group expects to and has historically physically delivered into these contracts.

OPERATING LEASES: GROUP AS A LESSEE

During the year ended 31 December 2016 the Group recognised US\$5 million as operating lease expenses (2015: US\$6 million).

The land in the Russian Federation and Kazakhstan on which the Group’s production facilities are located is owned by the state. The Group leases this land through operating lease agreements, which expire in various years through to 2058.

Future minimum lease payments due under non-cancellable operating lease agreements at the end of the period were as follows:

Table with 3 columns: 31 December 2016 US\$m, 31 December 2015 US\$m. Rows: Due within one year (2, 1), From one to five years (3, 2), Thereafter (2, 1), Total (7, 4).

CONTINGENCIES

OPERATING ENVIRONMENT

Emerging markets such as Russia and Kazakhstan are subject to different risks than more developed markets, including economic, political and social, and legal and legislative risks. Laws and regulations affecting businesses in Russia continue to change rapidly, tax and regulatory frameworks are subject to varying interpretations. The future economic direction of Russia and Kazakhstan is heavily influenced by the fiscal and monetary policies adopted by the government, together with developments in the legal, regulatory, and political environment.

Because Russia and Kazakhstan produce and export large volumes of oil and gas, their economies are particularly sensitive to the price of oil and gas on the global market. During 2014-2015 and then in the first quarter of 2016, the oil price decreased significantly, which led to substantial decrease of the Russian Ruble exchange rate. On 20 August 2015, the Government and the National Bank of Kazakhstan announced a transition to a new monetary policy based on free floating Tenge exchange rate, and cancelled the currency corridor. In 2015 and in the first quarter of 2016 Tenge depreciated significantly against major foreign currencies.

Starting from 2014, sanctions have been imposed in several packages by the U.S. and the E.U. on certain Russian officials, businessmen and companies.

In the first quarter of 2015 two international credit agencies downgraded Russia’s long-term foreign currency sovereign rating to the speculative level with the negative outlook.

The above mentioned events have led to reduced access of the Russian businesses to international capital markets, increased inflation, economic recession and other negative economic consequences. The impact of these economic developments on future operations and financial position of the Group has not been material.

TAXATION

Russian tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management’s interpretation of such legislation as applied to the transaction and activity of the companies of the Group may be challenged by the relevant regional and federal authorities and as a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

During 2016 and 2015 the Group has been involved in a number of litigations in Russia, Kazakhstan and Armenia. Management has identified a total exposure (covering taxes and related interest and penalties) of US\$13 million in respect of contingent liabilities (2015: US\$46 million), including US\$4 million related to income tax (2015: US\$16 million).

28. FAIR VALUE ACCOUNTING

The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable as follows:

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly or indirectly; and
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

At 31 December 2016 and 31 December 2015, the Group held the following financial instruments:

Table with 5 columns: Instrument, 31 December 2016 US\$m (Level 1, Level 2, Level 3, Total). Rows: Receivables from provisional copper, gold and silver concentrate sales (35), Contingent consideration liability ((76)), Total (41).

Table with 5 columns: Instrument, 31 December 2015 US\$m (Level 1, Level 2, Level 3, Total). Rows: Receivables from provisional copper, gold and silver concentrate sales (12), Contingent consideration liability ((26)), Total (14).

During the reporting periods, there were no transfers between Level 1 and Level 2.

The carrying values of cash and cash equivalents, trade and other receivables, trade and other payables and short-term debt recorded at amortised cost approximate to their fair values because of the short maturities of these instruments. The estimated fair value of the Group’s debt, calculated using the market interest rate available to the Group as at 31 December 2016, is US\$1,269 million, and the carrying value as at 31 December 2016 is US\$1,378 million (see Note 24). Carrying values of the other long-term loans provided to related parties as at 31 December 2016 and 31 December 2015 approximated to their fair values.

RECEIVABLES FROM PROVISIONAL COPPER, GOLD AND SILVER CONCENTRATE SALES

The fair value of receivables arising from copper, gold and silver concentrate sales contracts that contain provisional pricing mechanisms is determined using the appropriate quoted forward price from the exchange that is the principal active market for the particular metal. As such, these receivables are classified within Level 2 of the fair value hierarchy.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
CONTINUED

28. FAIR VALUE ACCOUNTING

CONTINGENT CONSIDERATION LIABILITIES

The table below sets forth a summary of changes in the fair value of the Group's Level 3 financial liabilities for the year ended 31 December 2016:

	31 December 2016							31 December 2015
	Omolon US\$m	Kyzyl US\$m	Primorskoye US\$m	Lichkvaz US\$m	Kapan US\$m	Komar US\$m	Total US\$m	US\$m
Opening balance	13	–	7	6	–	–	26	19
Additions (Note 4)	–	–	–	–	9	20	29	12
Change in fair value, included in profit or loss	4	19	–	1	–	(2)	22	(4)
Unwind of discount	–	–	1	–	–	–	1	–
Settlement	(2)	–	–	–	–	–	(2)	(1)
Total contingent consideration	15	19	8	7	9	18	76	26
Less current portion of contingent consideration liability	(5)	–	(8)	–	(1)	–	(14)	(2)
	10	19	–	7	8	18	62	24

In 2008, the Group recorded a contingent consideration liability related to the acquisition of 98.1% of the shares in JSC Omolon Gold Mining Company (Omolon). The fair value of the contingent consideration liability was determined using a valuation model which simulates expected production of gold and silver at the Kubaka mine and future gold and silver prices to estimate future revenues of Omolon. This liability is revalued at each reporting date based on 2% of the life-of-mine revenues with the resulting gain or loss recognised in the consolidated income statement. The liability recognised as at 31 December 2016 was US\$15 million, including current portion of US\$5 million.

During the year ended 31 December 2014 the Group completed the acquisition of Altynalmas Gold Ltd, the holding company for the Kyzyl gold project in Kazakhstan. The fair value of the related contingent consideration liability was estimated using the Monte-Carlo model. The liability was revalued at the 31 December 2016 using the same method with updated inputs as of reporting date and amounts to US\$19 million (2015: nil), having increased due to lower volatility assumption input.

During the year ended 31 December 2015 the Group the recorded a contingent consideration liability related to the acquisition of 100% interest in Primorskoye (Note 4). Deferred conditional cash consideration, which will be determined as the highest of US\$13,333 per tonne of contained silver equivalent (translating into US\$0.415 per silver equivalent ounce) based on the audited reserves estimate of the deposit, and US\$8 million, was revalued at 31 December 2016 at US\$8 million.

In March 2017 it was agreed to determine Primorskoye deferred consideration based on the mineral resource estimate and, therefore, as of 1 March 2017 the deferred consideration equals to US\$9.7 million, which is US\$13,333 per tonne of contained silver equivalent in Measured and Indicated Mineral Resources (or US\$0.415 per silver equivalent ounce). In accordance with the updated agreement, the deferred consideration will be payable by 815,348 newly issued Polymetal International shares.

During the year ended 31 December 2015 the Group completed the acquisition of LV Gold Mining (Lichkvaz), the company owning the Lichkvaz exploration licence in Armenia (Note 4). The fair value of the related contingent consideration liability is calculated using a valuation model which simulates expected production of metals and future gold, silver and copper prices to estimate future value of the metals in the actually extracted ore. The liability recognised at 31 December 2016 was US\$7 million.

During the year ended 31 December 2016 the Group completed the acquisition of DPMK, the company owning the Kapan mine and processing plant in Armenia (Note 4). The seller is entitled to receive a 2% NSR (Net Smelter Return) royalty on future production from the Kapan Gold Mine capped at US\$25 million. At the 31 December 2016, the fair value of the contingent consideration was estimated at US\$8 million, including current portion of US\$1 million.

On 1 August 2016 the Group completed the acquisition of Orion Minerals LLP, the holding company for the Komarovskoye Gold Deposit (Komar) in the Republic of Kazakhstan (Note 4). The seller is entitled to the contingent consideration that was determined based on the LOM model of the Komar mine and calculated using Monte-Carlo modelling. At the 31 December 2016, the fair value of the contingent consideration was estimated at US\$18 million.

Assumptions used in the valuation of the Omolon, Kapan and Lichkvaz are consistent with those used in goodwill impairment test (Note 19), such as long-term metal prices and discount rates. Estimated production volumes are based on life of mine plans and are approved by management as part of the long-term planning process.

Monte-Carlo modelling for Kyzyl and Komar contingent consideration liabilities was performed with following inputs:

- Gold price volatility: 16.23%-18.23%
- Share price volatility: 41.9%
- Constant correlation between gold and share price: 90%
- Dividend yield: 2%.

The Directors consider that a reasonably possible change in a valuation assumption would not have a material impact on the financial statements for contingent considerations payable.

COMMODITY FORWARD CONTRACTS

The Group enters into forward contracts for the physical delivery of metals which will be priced according to the prevailing London Bullion Market Association or London Metal Exchange index. The Group's policy is not to enter into fixed priced contracts. The forward sales contracts qualify for the normal purchase/sales or 'own use' exemption for accounting purposes and are outside the scope of IAS 39 *Financial Instruments: Recognition and Measurement*.

29. RISK MANAGEMENT ACTIVITIES

CAPITAL MANAGEMENT

The Group manages its capital to ensure that entities in the Group will be able to continue as a going concern while maximising the return to stakeholders through the optimisation of the debt and equity balance. The Group's overall strategy is to provide value to stakeholders by maintaining an optimal short-term amd long-term capital structure, reducing cost of capital, and to safeguard the ability to support the operating requirements on an ongoing basis, continuing the exploration and development activities.

The capital structure of the Group consists of net debt (borrowings as detailed in Note 24 offset by cash and bank balances as detailed in Note 23 and equity of the Group comprising the Stated Capital account, reserves and retained earnings as detailed in Note 30.

The Group's committed borrowings are subject to certain financial covenants. Compliance with covenants is reviewed on a semi-annual basis and the Group's Board is satisfied with forecast compliance with covenants on those borrowings.

The Group's Board reviews the capital structure of the Group on a semi-annual basis. As part of this review, the Board considers the cost of capital and the risks associated with each class of capital.

MAJOR CATEGORIES OF FINANCIAL INSTRUMENTS

The Group's principal financial liabilities comprise borrowings, derivatives, trade and other payables. The Group has various financial assets such as accounts receivable, loans advanced and cash and cash equivalents.

	31 December 2016 US\$m	31 December 2015 US\$m
Financial assets		
<i>Financial assets at FVTPL</i>		
Receivables from provisional copper, gold and silver concentrate sales	35	12
<i>Loans and receivables, including cash and cash equivalents</i>		
Cash and cash equivalents	48	52
Trade, non-trade and other receivables	35	27
Non-current loans and receivables	10	13
Total financial assets	128	104
Financial liabilities		
<i>Financial liabilities at FVTPL</i>		
Contingent consideration liability	76	26
<i>Financial liabilities at amortised cost</i>		
Borrowings	1,378	1,350
Trade and other payables	82	41
Total financial liabilities	1,536	1,417

Trade and other payables exclude employee benefits and social security.

The main risks arising from the Group's financial instruments are foreign currency and commodity price risk, interest rate, credit and liquidity risks.

At the end of the reporting period, there are no significant concentrations of credit risk for receivables designated at FVTPL. The carrying amount reflected above represents the Group's maximum exposure to credit risk for such receivables.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
CONTINUED

29. RISK MANAGEMENT ACTIVITIES CONTINUED

DERIVATIVE FINANCIAL INSTRUMENTS

Presented below is a summary of the Group’s derivative contracts recorded on the consolidated balance sheet at fair value.

Table with 4 columns: Consolidated balance sheet location, 31 December 2016 US\$m, 31 December 2015 US\$m. Row: Receivable from provisional copper, gold and silver concentrate sales, Accounts receivable, 35, 12.

Table with 4 columns: Location of gain (loss) recorded in profit or loss, 31 December 2016 US\$m, 31 December 2015 US\$m. Row: Receivable from provisional copper, gold and silver concentrate sales, Revenue, (7), (6).

FOREIGN CURRENCY AND COMMODITY PRICE RISK

In the normal course of business the Group enters into transactions for the sale of its commodities, denominated in U.S. Dollars. In addition, the Group has assets and liabilities in a number of different currencies (primarily Russian Rouble and Kazakh Tenge). As a result, the Group is subject to transaction and translation exposure from fluctuations in foreign currency exchange rates.

The Group does not currently use derivative instruments to hedge its exposure to foreign currency risk.

The carrying amounts of monetary assets and liabilities denominated in foreign currencies other than functional currencies of the individual Group entities at 31 December 2016 and 31 December 2015 were as follows:

Table with 5 columns: Assets (31 December 2016 US\$m, 31 December 2015 US\$m), Liabilities (31 December 2016 US\$m, 31 December 2015 US\$m). Rows: U.S. Dollar, Euro, GBP, Total.

U.S. Dollar denominated assets and liabilities disclosed above exclude balances outstanding held in Polymetal International plc and its intermediate holding companies, where functional currency is United States Dollar (US\$) as described in Note 2.

Currency risk is monitored on a monthly basis by performing a sensitivity analysis of foreign currency positions in order to verify that potential losses are at an acceptable level.

The table below details the Group’s sensitivity to changes in exchange rates by 10% which is the sensitivity rate used by the Group for internal analysis. The analysis was applied to monetary items denominated in respective currencies at the reporting dates.

Table with 3 columns: 31 December 2016 US\$m, 31 December 2015 US\$m. Rows: Profit or loss (RUB to U.S. Dollar), Profit or loss (KZT to U.S. Dollar).

PROVISIONALLY PRICED SALES

Under a long-established practice prevalent in the industry, copper, gold and silver concentrate sales are provisionally priced at the time of shipment. The provisional prices are finalised in a contractually specified future period (generally one to three months) primarily based on quoted LBMA or LME prices. Sales subject to final pricing are generally settled in a subsequent month. The forward price is a major determinant of recorded revenue.

INTEREST RATE RISK

The Group is exposed to interest rate risk because entities in the Group borrow funds at both fixed and floating interest rates. The risk is managed by the Group by maintaining an appropriate mix between fixed and floating rate borrowings. The Group does not currently hedge its exposure to interest rate risk.

The Group’s exposure to interest rates on financial assets and financial liabilities are detailed in the liquidity risk section of this note.

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 period. A 100 basis point increase or 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.

If interest rates had been 100 basis points higher/lower and all other variables were held constant, the Group’s profit for the year ended 31 December 2016 would have decreased/increased by US\$13 million (2015: US\$11 million). This is mainly attributable to the Group’s exposure to interest rates on its variable rate borrowings.

The Group’s sensitivity to interest rates has increased during the current period mainly due to the increase in variable rate debt instruments.

CREDIT RISK

Credit risk is the risk that a customer may default or not meet its obligations to the Group on a timely basis, leading to financial losses to the Group. The Group’s financial instruments that are potentially exposed to concentration of credit risk consist primarily of cash and cash equivalents and loans and receivables.

Accounts receivable are regularly monitored and assessed and where necessary an adequate level of provision is maintained. Trade accounts receivable at 31 December 2016 and 31 December 2015 are represented by provisional copper, gold and silver concentrate sales transactions. A significant portion of the Group’s trade accounts receivable is due from reputable export trading companies. With regard to other loans and receivables the procedures of accepting a new customer include checks by a security department and responsible on-site management for business reputation, licences and certification, creditworthiness and liquidity. Generally, the Group does not require any collateral to be pledged in connection with its investments in the above financial instruments. Credit limits for the Group as a whole are not set up.

The credit risk on liquid funds is limited because the counterparties are banks with high credit-ratings assigned by international credit-rating agencies. The major financial assets at the balance sheet date other than trade accounts receivable presented in Note 23 are cash and cash equivalents at 31 December 2016 of US\$48 million (2015: US\$52 million).

LIQUIDITY RISK

Liquidity risk is the risk that the Group will not be able to settle its liabilities as they fall due.

The Group’s liquidity position is carefully monitored and managed. The Group manages liquidity risk by maintaining detailed budgeting, cash forecasting processes and matching the maturity profiles of financial assets and liabilities to help ensure that it has adequate cash available to meet its payment obligations.

The following tables detail the Group’s remaining contractual maturity for its financial liabilities with agreed repayment periods. The tables have been drawn up based on the undiscounted cash flows of financial liabilities based on the earliest date on which the Group can be required to pay. The tables include both interest and principal cash flows. To the extent that interest flows are floating rate, the undiscounted amount is derived from interest rate curves at the end of the reporting period. The contractual maturity is based on the earliest date on which the Group may be required to pay.

Presented below is the maturity profile of the Group’s financial liabilities as at 31 December 2016:

Table with 7 columns: Less than 3 months, 3-12 months, 1-5 years, More than 5 years, 31 December 2016 US\$m, 31 December 2015 US\$m. Rows: Borrowings, Accounts payable and accrued expenses, Contingent consideration (Note 28), Total.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
CONTINUED

30. STATED CAPITAL ACCOUNT AND RETAINED EARNINGS

As at 31 December 2016, the Company's issued share capital consisted of 428,262,338 ordinary shares (2015: 424,650,138 ordinary shares) of no par value, each carrying one vote. The Company does not hold any shares in treasury (2015: none). The ordinary shares reflect 100% of the total issued share capital of the Company.

The movements in the Stated Capital account in the year were as follows:

	Stated capital account, no. of shares	Stated capital account, US\$m
Balance at 1 January 2015	420,819,943	1,939
Issue of shares to acquire non-controlling interest in Tarutin	1,746,692	13
Issue of shares in accordance with Deferred Share Awards plan (Note 31)	36,089	–
Issue of shares for LV Gold Mining CJSC (Note 4)	1,514,113	13
Issue of shares for Primorskoye (Note 4)	533,301	4
Balance at 31 December 2015	424,650,138	1,969
Issue of shares in accordance with Deferred Share Awards plan	110,850	1
Issue of shares for Kapan (Note 4)	1,481,785	15
Issue of shares to acquire an additional 25% interest in Tarutin	898,875	14
Issue of shares for Saum Mining Company LLC (Note 4)	1,120,690	11
Balance at 31 December 2016	428,262,338	2,010

On 18 August 2016, the Group increased its interest in LLC Vostochny Basis (holder of the licence for the Tarutinskoye copper deposit (Tarutin) from 50% to 75%. The Group has purchased an additional 25% from the unrelated party for a consideration of US\$14 million, payable through 898,875 newly issued Polymetal International plc shares. The Group has previously determined that LLC Vostochny Basis meets the definition of a subsidiary and it was consolidated from the date of the 25% share acquisition. The increase in interest in Tarutin was recognised as an acquisition of the non-controlling interest and recognised within equity. As of 31 December 2016 and during the year ended 31 December 2016 Tarutin does not give rise to a significant non-controlling interest to be presented within equity, income statement and statement of comprehensive income.

Reserves available for distribution to shareholders are based on the available cash in the Company under Jersey law. As Russian, Kazakh and Armenian legislation identifies the basis of distribution of the dividends as accumulated profit, the ability to distribute cash up to the Company from the Russian, Kazakh and Armenian operating companies will be based on the statutory historical information of each stand-alone entity. Statutory financial statements in the Russian Federation are prepared in accordance with Russian accounting standards which differs from IFRS, while Kazakhstan and Armenia have adopted IFRS from 1 January 2006 and 1 January 2011, respectively. However, current legislation and other statutory regulations dealing with distribution rights are open to legal interpretation; consequently, actual distributable reserves may differ from the amount of accumulated profit in accordance with statutory financial statements.

WEIGHTED AVERAGE NUMBER OF SHARES: DILUTED EARNINGS PER SHARE

Both basic and diluted earnings per share were calculated by dividing profit for the year attributable to equity holders of the parent by the weighted average number of outstanding common shares before/after dilution respectively. The calculation of the weighted average number of outstanding common shares after dilution is as follows:

	Year ended	
	31 December 2016	31 December 2015
Weighted average number of outstanding common shares	426,135,182	422,958,680
Dilutive effect of share appreciation plan	259,452	290,522
Weighted average number of outstanding common shares after dilution	426,394,634	423,249,202

There were no adjustments required to earnings for the purposes of calculating the diluted earnings per share in the current interim period (year ended 31 December 2015: nil).

At 31 December 2016 and 31 December 2015 the outstanding LTIP awards issued under 2014, 2015 and 2016 tranches represent anti-dilutive potential ordinary shares with respect to earnings per share from continuing operations as these are out the money as of reporting date.

The awards issued under management bonus deferral award plan are dilutive as of 31 December 2016 and 31 December 2015 being contingently issued shares and are included in the calculation of diluted EPS based on the weighted average number of shares that would be issuable if the end of the reporting period were the end of the contingency period.

31. SHARE-BASED PAYMENTS

For the year ended 31 December 2016, share-based compensation in the amount of US\$7 million including US\$1 million of management bonus deferral award (2015: US\$3 million and US\$1 million, respectively) was recognised in general, administrative and selling expenses in the consolidated income statement (Note 11).

As at 31 December 2016 the Group has three portions amounting to US\$3, US\$6, US\$7 million of unrecognised share-based compensation expense related to non-vested equity-settled stock appreciated rights with expected amortisation period of 1.2, 2.2 and 3.2 years, respectively.

As at 31 December 2015 the Group has two portions amounting to US\$4 and US\$6 million of unrecognised share-based compensation expense related to non-vested equity-settled stock appreciated rights with expected amortisation period of 2.2 and 3.2 years, respectively.

During the year ended 31 December 2015 36,089 shares under management bonus plan deferral award were released and issued in accordance with the plan.

No further disclosures are provided on a grounds of materiality.

32. RELATED PARTIES

Related parties are considered to include shareholders, affiliates, associates, joint ventures and entities under common ownership and control with the Group and members of key management personnel.

As of 31 December 2016 outstanding balances owed to or from related parties composed of long-term loans provided to equity method investments of US\$1 million (2015: US\$6 million) and short-term loans of US\$7 million and interest receivable in respect of these loans of US\$1 million (2015: US\$1 million).

During the year ended the Group has purchased ore from its associate GRK Amikan (Note 20) for the total amount of US\$11 million (2015: nil) and accounts payable amounting US\$4 million are outstanding as of 31 December 2016 (2015: nil).

No significant transactions with related parties took place during the year ended 31 December 2015.

Carrying values of other long-term loans provided to related parties as at 31 December 2016 and 31 December 2015 approximate their fair values.

The amounts outstanding at the balance sheet dates are unsecured and expected to be settled in cash. No expense has been recognised in the reporting period for bad or doubtful debts in respect of the amounts owed by related parties.

The remuneration of directors and other members of key management personnel during the periods was as follows:

	Year ended	
	31 December 2016 US\$m	31 December 2015 US\$m
Share-based payments	2	1
Short-term benefits of board members	2	2
Short-term employee benefits	1	2

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

CONTINUED

33. NOTES TO THE CONSOLIDATED STATEMENT OF CASH FLOWS

	Notes	Year ended	
		31 December 2016 US\$m	31 December 2015 US\$m
Profit before tax		564	276
Adjustments for:			
Depreciation and depletion, recognised in income statement		155	156
Additional mining taxes, penalties and accrued interest	12	(12)	(4)
Provision for investment in Special Economic Zone	12	14	–
Write-down of exploration assets and construction in progress	18	2	9
Write-down non-metal inventory to net realisable value	21	6	5
Write-down of metal inventory to net realisable value	21	21	13
Change in estimate of environmental obligations		(5)	(4)
Share-based compensation	11, 31	7	4
Finance costs	15	63	81
Finance income		(3)	(5)
Loss on disposal and write-down of assets	12	1	1
Change in contingent consideration liability	28	22	(4)
Change in allowance for doubtful debts	12	–	7
Rehabilitation expenses		1	(2)
Loss from equity method investments	20	–	4
Foreign exchange loss		(65)	133
Gain on disposal of subsidiary		–	(1)
Other non-cash expenses		1	5
Movements in working capital			
Increase in inventories before impairment		(50)	(26)
Decrease /(Increase) in VAT receivable		14	(23)
(Increase)/Decrease in trade and other receivables		(4)	19
Decrease/(Increase in prepayments) to suppliers		2	(13)
Increase in trade and other payables		17	22
(Increase)/Decrease in other taxes payable		(6)	7
Cash generated from operations		745	660
Interest paid		(61)	(52)
Interest received		1	3
Income tax paid		(155)	(120)
Net cash generated by operating activities		530	491

Non-cash transactions during the year ended 31 December 2016 represent the issuance of shares amounting to US\$40 million in respect of the business combinations, the acquisition of assets and acquisition of non-controlling interest (2015: the issuance of shares amounting to US \$17 million in respect of the acquisition of stake in joint venture and the acquisition of assets).

Cash flows related to exploration and development amounted to US\$56 million for the year ended 31 December 2016 (2015: US\$41 million). During the year ended 31 December 2016 capital expenditure, related to new projects, amounts to US\$121 million (2015: US\$66 million).

34. SUBSEQUENT EVENTS

In January 2017 the Group has increased its interest in LLC Vostochny Basis (holder of the licence for the Tarutinskoye copper deposit (Tarutin) from 75% to 100%. The Group purchased the additional 25% from an unrelated party for a consideration of US\$10 million, payable through the issue of 893,575 new Polymetal International plc shares. The Group has previously determined that LLC Vostochny Basis meets the definition of a subsidiary and consolidated Vostochny Basis LLC as of the reporting date. Increase in ownership in Tarutin will be recognised as an acquisition of non-controlling interest and recognised within equity. A reserve estimate for the deposit is expected in Q3 2017, with mining planned to commence in 2018 with the goal to deliver and process up to 300 Kt of ore at Varvara in order to produce 4-5 Kt of copper per annum in 2018-2020.

In January 2017 the Group has entered into an agreement with Polar Silver Resources Ltd, under which Polymetal will participate in the development of the Prognoz silver deposit in Yakutia, Russia ('Prognoz'). The arrangement will allow Polymetal to acquire up to 50% indirect interest in Prognoz. Under the agreement, Polymetal will acquire a 5% indirect interest in Prognoz for US\$3 million in cash through the purchase of 10% of Polar's share capital. Polar currently indirectly holds a 50% interest in Prognoz, with the remaining 50% owned by a group of private investors. Polymetal will have an obligation to undertake 25 km of diamond drilling, and complete a technical study resulting in an externally audited JORC-compliant reserves estimate for the property before 31 March 2019. Total capital expenditures required to perform the drilling and complete the technical study are expected at US\$10 million per annum during FY 2017-2019.

In March 2017 the deferred consideration for the acquisition of the Primorskoye property was finalised. Under the deal terms, the deferred consideration is based on the reserve estimate and paid in cash. However, the parties agreed for the deferred consideration to be based on the mineral resource estimate and paid in Polymetal International shares. Therefore, the deferred consideration is equal to US\$9.7 million, which is US\$13,333 per tonne of contained silver equivalent in Measured and Indicated Mineral Resources (or US\$0.415 per silver equivalent ounce). The deferred consideration is payable by 815,348 newly issued Company shares representing 0.19% of Polymetal's total increased share capital.