

## CEO STATEMENT

*Dear Stakeholders and Partners of HMS Group,*

### Summary of 2013

Business development in 2013 lagged behind expectations. HMS Group experienced several challenges arising from both external and internal factors. The most influential external factor was the slowdown of the Russian economy which resulted in delays in large tenders targeted by HMS. Consequently, the market provided no material growth opportunities. The deterioration in the construction market for oil and gas fields also had a negative effect on our performance. The key internal challenges included our withdrawal from the active M&A strategy that had previously supported the Group's growth and working capital restraints. Despite these setbacks, we were able to demonstrate a generally strong performance in 2013.



Artem Molchanov,  
Chief Executive Officer

HMS Group reported a backlog of Rub 22.3 billion. As a result of a couple of material projects and a constant flow of small- and medium-sized orders from our customers, we managed to attain an order intake worth Rub 34.8 billion.

The Group's revenue was Rub 32.4 billion in 2013. The largest share of our revenue (Rub 17.6 billion) was generated by our oldest and largest industrial pumps division, which demonstrated a traditionally strong performance. The oil and gas division experienced an anticipated decrease in revenue following the completion of the high-margin Vankor project and contributed Rub 7.7 billion to the Group's revenue. The new compressors segment achieved impressive results with Rub 4.2 billion in revenue. In the EPC segment, revenue decreased to Rub 2.8 billion due to the poor results of the construction sub-segment.

The weaker margins had a negative impact on profitability in 2013. The Group's EBITDA was Rub 5.2 billion, 14% lower than last year. Net income increased by 50% to Rub 1.2 billion. In order to provide returns to our shareholders we made a decision to pay dividends of Rub 400 million. The level of dividends as a proportion of net profit (from continuing operations) is consistent with the previous practice.

### 2013 achievements and challenges

Although it was a challenging year, we achieved sound results in our key business segments. We continued our successful cooperation with one of our key strategic partners — Transneft. In July, we signed a Rub 1.5 billion contract for the production and delivery of 8 pump units for the Zapolarye — Purpe oil pipeline. HMS was awarded this material contract thanks to our strong record of performance in the East Siberia — Pacific Ocean (ESPO) and ESPO-2 projects.

Our compressor business has been developing in line with the Group's strategy aimed at boosting its growth through participating in large, high-margin projects and enhancing our competencies in this area. In 2013, we managed to successfully deliver complex compressor equipment as a part of a series of contracts signed in 2012, valued at more than Rub 2.5 billion. In addition, in August, HMS signed a single Rub 1 billion contract for the manufacturing and delivery of a booster compressor station with a gas-turbine engine to be installed at a petrochemical complex in the South of Russia. Furthermore, HMS bought NIITurbocompressor (NIITK), the leading Russian project and design institute, focused on compressor technology, to strengthen our position in the compressor market. We are satisfied with the results achieved so far and see attractive opportunities for our compressor business going forward.

In 2013, three new large-scale projects were brought on stream. The largest of them is a milestone project

to supply an integrated solution for a major Siberian gas field. During the next 2 years, HMS Group will design, manufacture, deliver and install a complex technology facility, including compressors, pumps, tanks, vessels, filters, coolers and other components for a total of Rub 5.7 billion.

Our target markets are not just limited to the oil and gas sector. In 2013, we continued to execute our key project in the water utility sector comprising the delivery of three customized water pump stations to Turkmenistan. We completed the design stage and delivered most of the contracted equipment. In the power generation sector, we made good progress in the delivery of equipment for Leningradskaya NPP and Novovoronezhskaya NPP.

2013 year was also memorable for our development of an innovative device for real-time measurement of oil and associated gas flows without a traditional separator. The product is a result of close cooperation between HMS engineers and experts from the international company, Invensys Operations Management. The new product has already successfully passed tests at some oil fields and received positive feedback from a number of leading oil companies, which indicates the prospect of solid demand for this product.

We are also very pleased with the results of German pumps manufacturer, Apollo Goessnitz, our first international acquisition. This business has noticeably strengthened the Group's position in the pumps market. In 2013, Apollo produced different types of pumps for a number of international projects: vertical high-pressure pumps for one of the world's largest oil and gas platforms, Troll A, in the North Sea; processing pumps to pump ammonium nitrate for a plant in Egypt; and a bespoke pump to transfer wax bearing products for a petrochemical plant in the Samara region.

HMS Group constantly pays attention to upgrading its equipment and technology. In 2013, as part of the Group's modernisation programme, we put into operation a new casting shop at Nasosenergomash and a new complex for tank and vessels production at Sibneftemash.

2013 brought new challenges that we are continuing to address. The deterioration in payment terms that HMS has been facing since the beginning of last year led to a growth in working capital needs. Although we managed to respond to working capital restraints by the end of the year and decrease working capital to 19% of revenue, we cannot exclude its growth going forward due to uncertainties in relation to prepayments under large contracts. Due to its increase in working capital, the Group's total debt reached Rub 12.4 billion, while net debt to EBITDA ratio was 2.0x, within its internal limit of 2.5x.

## Strategy evolution

Navigating through challenging markets, we chose to concentrate our efforts on programmes designed to promote our operational excellence.

In 2013, HMS Group started to introduce optimisation measures at its previously acquired companies targeting the further development of its core business segments — industrial pumps, compressors, oil and gas equipment and EPC. We suspended the Group's "growth through acquisitions" strategy and shifted to organic development. Our updated strategy focuses on the optimisation of our asset portfolio, the reduction of operating losses and the improvement of the Group's financial performance.

Following careful consideration, we made a decision to divest our underperforming non-core construction business. In line with this decision, we disposed of one of our construction subsidiaries, SKMN, and intend either to sell or close-down the second one.

## Outlook 2014

Despite the mixed business climate and uncertainties relating to tenders, we believe that HMS will continue to benefit in the long term. We consider that the compressor market offers a lot of potential and we expect that the disposal of our loss-making construction business will lead to an increase in the Group's overall profitability. We believe in the Group's strong fundamentals as well as attractive industry opportunities, which should assist us in achieving better performance in future periods.

Yours faithfully,

Artem Molchanov

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