

## OPERATING PERFORMANCE

### Financial summary

*(Figures in brackets are for the twelve months ended December 31, 2012)*

- Backlog increased by 18% year-on-year to Rub 22.3 billion (Rub 19.0 billion) and order intake was up 5% year-on-year to Rub 34.8 billion (Rub 33.1 billion) driven by a steady demand for pumps, compressors and oil & gas equipment
- Revenue increased by 3% year-on-year to Rub 32.4 billion (Rub 31.5 billion)
- EBITDA<sup>1</sup> totaled Rub 5.2 billion, down 14% year-on-year (Rub 6.1 billion); EBITDA margin was 16.2% compared to 19.4% in the previous year
- Operating profit was Rub 4.2 billion, almost flat year-on-year; operating margin stood at 13%
- Profit for the period from continuing operations reached Rub 2.1 billion, down 12% year-on-year; earnings per share (EPS) were Rub 16.79 (Rub 17.99)
- Profit for the period including the results of discontinued operations decreased from Rub 2.3 billion to Rub 1.15 billion; earnings per share (EPS) were Rub 8.99 (Rub 17.91)
- Total debt contracted by 5% year-on-year to Rub 12.7 billion (Rub 13.4 billion)
- Net debt decreased by 8% year-on-year to Rub 11.1 billion (Rub 12.1 billion), resulting in Net debt-to-EBITDA ratio at 2.1x (2.0x)
- Return on capital employed  
ROCE<sup>2</sup> was 13.9% versus 18.7% in the previous year

### Group performance

The Group's backlog as of December 31, 2013 amounted to Rub 22.3 billion, up 18% year-on-year, caused mainly by the growth in the oil & gas equipment.

The backlog of orders in all business segments, excluding industrial pumps, demonstrated positive dynamics in the reporting period. In the oil & gas equipment business segment, HMS Group more than doubled its backlog, successfully replacing the Vankor contract with a new promising Rub 5.7 billion contract, and the segment's backlog achieved Rub 8 billion as of 31 December 2013.

In the compressors business segment, the backlog grew by 17% to Rub 2.3 billion supported by a stable inflow of orders for compressors. Meanwhile, the core industrial pumps business segment showed negative dynamics in 2013: its backlog decreased by a quarter to Rub 8.8 billion as a result of delay in launch of new large projects by Russian oil and gas majors due to uncertainties in the economy. In the EPC business segment, HMS Group built up a solid Rub 3.3 billion backlog in the reporting period, up 72% year-on-year. Both sub-segments of the division — project and design (EP) and construction (C) — grew by 77% and 65% year-on-year respectively.

The order intake<sup>3</sup> in 2013 increased by 5% year-on-year to Rub 34.8 billion. The decrease in orders for industrial pumps was more than compensated by the growth of orders in all other business segments.

Stable performance of industrial pumps and compressors business segments was the main

driver behind the Group's performance in 2013. The Group's revenue grew by 3% year-on-year to Rub 32,358 million. EBITDA declined 14% year-on-year to Rub 5,238 million, reflecting the lack of high-margin projects and poor performance of construction sub-segment. As a result, EBITDA margin for 12 months 2013 stood at 16.2%.

<i>Rub million</i>	<b>2013</b>	<b>2012</b>	<b>Change y-o-y</b>
Revenue from continuing operations	32,358	31,460	3%
EBITDA	5,238	6,101	(14)%
EBITDA margin	16.2%	19.4%	(320) bps

The Group's cost of sales, which traditionally accounts for about 70% of total revenue, grew by 7% year-on-year from Rub 21,627 million to Rub 23,238 million driven by a full year consolidation of KKM and Apollo in 2013 compared to their partial consolidation in 2012.

<i>Rub million</i>	<b>2013</b>	<b>% of revenue</b>	<b>2012</b>	<b>% of revenue</b>	<b>Change y-o-y</b>
<b>Total cost of sales</b>	<b>23,238</b>	<b>72%</b>	<b>21,627</b>	<b>69%</b>	<b>7%</b>
Supplies and raw materials	10,567	33%	10,935	35%	(3)%
Labour costs	5,374	17%	5,100	16%	5%
Cost of goods sold	2,799	9%	2,222	7%	26%
Other expenses	4,498	14%	3,370	11%	33%

The key components of cost of sales — supplies and raw materials combined with cost of goods sold — accounted for 41% in 2013, almost the same share as in 2012.

Labour costs grew 5% year-on-year of Rub 5,374 million, or 17% of revenue.

Distribution and transportation expenses in absolute terms were up 11% year-on-year, and achieved Rub 1,377 million in 2013. As a percentage of revenue, they comprised 4% in both periods.

General and administrative expenses totaled to Rub 3,970 million for 2013, up 5% year-on-year, but remained flat year-on-year at 12% as a percentage of revenue.

The Group's operating profit was almost flat year-on-year and totaled Rub 4,179 million in 2013. Operating margin stood at 13% in the reporting period. In 2013, the Group posted Rub 439 million impairment of the construction business and Rub 955 million extra gain from the bargain M&A, which contributed Rub 516 million to HMS' operating profit.

Interest expenses increased by 25% to Rub 1,522 million compared to Rub 1,220 million in 2012 and comprised 4.7% of revenue versus 3.9% in the previous year.

In 2013, the Group accrued an income tax expense of Rub 524 million. Effective tax rate decreased from 25% to 20% in 2013 due to non-taxable effects of the impairment of the construction business and the gain from the bargain M&A deals.

The Group's profit for the period including the results of discontinued operations decreased twofold to Rub 1,156 million mainly because of HMS' lower operating profit, higher finance costs and the loss from SKMN.

## Segment performance

### Industrial pumps business segment

*The industrial pumps business segment designs, engineers, manufactures and supplies a diverse range of pumps and pump-based integrated solutions to customers in the oil*

and gas, power generation and water utilities sectors in Russia, the CIS and internationally. The business segment's principal products include customized pumps and integrated solution as well as pumps manufactured to standard specifications. It also provides aftermarket maintenance and repair services and other support for its products.

<i>Rub million</i>	<b>2013</b>	<b>2012</b>	<b>Change y-o-y</b>
Revenue	17,595	17,066	3%
EBITDA	3,816	4,279	(11)%
EBITDA margin	21.7%	25.1%	(338) bps

The industrial pumps business segment's revenue increased by 3% year-on-year to Rub 17,595 million from Rub 17,066 million in 2012, while EBITDA decreased by 11% year-on-year to Rub 3,816 million. EBITDA margin stood at healthy 21.7%.

The segment's results in the reporting period were supported by the ESPO (+ Rub 1,204 million), Zapolyarye-Purpe (+ Rub 501 million) and Turkmenia (+ Rub 2,303 million) projects. Excluding these projects, industrial pumps demonstrated a 12% growth both in revenue and EBITDA year-on-year backed on a stable inflow of orders for standard and customized pumps.

#### **Oil & gas equipment business segment**

The oil & gas equipment business segment manufactures and installs modular pumping stations, automated metering equipment, oil, gas and water processing and preparation units and other equipment and systems for use primarily in oil extraction and transportation. The segment's core products are equipment packages and systems installed inside a self-contained, free-standing structure, which can be transported on trailers and delivered to and installed on the customer's site as a modular but fully integrated part of the customer's technological process.

<i>Rub million</i>	<b>2013</b>	<b>2012</b>	<b>Change y-o-y</b>
Revenue	7,743	7,828	(1)%
EBITDA	883	1,397	(37)%
EBITDA margin	11.4%	17.8%	(644) bps

Revenue in the oil & gas equipment business segment demonstrated a minor decrease by 1% year-on-year in 2013 to Rub 7,743 million, compared to Rub 7,828 million in 2012. The segment's EBITDA dropped by 37% year-on-year to Rub 883 million in the reporting period versus Rub 1,397 million in 2012. Last year, the segment implemented a lucrative Vankor project, which contributed Rub 2,709 million to its revenue. Excluding Vankor, the segment's revenue grew by 51% year-on-year. In 2013, the oil & gas equipment business segment served exclusively small and medium-sized orders for standard tanks and vessels and measuring equipment. Achieved EBITDA margin at 11.4% in 2013 is an average margin for that type of business activity.

#### **Compressors business segment**

The compressors business segment designs, manufactures and supplies a diverse range of compressors and compressor-based solutions, including compressor units and compressor stations, to customers in the oil and gas, petrochemical, metals and mining and other basic industries in Russia. The business segment's principal products include customized compressors, series-produced compressors built to standard specifications, and compressor-based integrated solutions.

<i>Rub million</i>	<b>2013</b>	<b>2012*</b>	<b>Change y-o-y</b>
Revenue	4,207	3,066	37%

EBITDA	572	266	115%
EBITDA margin	13.6%	8.7%	490 bps

*\*including the results of KKM for the full 2012 year*

KKM was the key contributor to the segment's results as an impact of project and design center NIITK, bought in 2Q 2013, was immaterial. The contracts, signed by KKM since its joining HMS Group, boosted the compressors segment's revenue and EBITDA, which grew by 37% and 115% year-on-year respectively. In 2013, EBITDA margin achieved 13.6%.

Integration of KKM is far from completion. According to the integration plan, a number of issues are to be addressed to reach sustainability and further growth of the segment.

#### Engineering, procurement and construction (EPC) business segment

*The engineering, procurement and construction (EPC) business segment provides design and engineering services, project management and construction works for projects for customers in the oil and gas upstream and midstream and water utilities sectors.*

<i>Rub million</i>	<b>2013</b>	<b>2012</b>	<b>Change y-o-y</b>
Revenue EPC	2,808	5,140	(45)%
Project and Design	2,209	2,204	0%
Construction	599	2,936	(80)%
EBITDA EPC	(204)	341	(160)%
Project and Design	267	125	114%
Construction	(472)	216	(318)%
EBITDA margin EPC	(7.3)%	6.6%	(1,392) bps
Project and Design	12.1%	5.7%	644 bps
Construction	(78.8)%	7.4%	(8,621) bps

#### Discontinued operations (results of SKMN)

<i>Rub million</i>	<b>2013</b>	<b>2012</b>	<b>Change y-o-y</b>
Revenue	2,647	2,545	(45)%
EBITDA	(43)	112	(132)%
EBITDA margin	(2.6)%	4.4%	(659) bps

The EPC business segment delivered weak results in 2013 with revenue declining almost twofold to Rub 2,808 million and EBITDA turning negative to Rub –204 million.

The segment's poor performance was attributable to the construction sub-segment, which generated negative Rub –472 million EBITDA in the reporting period. Revenue in the construction sub-segment declined from Rub 2,936 to Rub 599 million. Project and design sub-segment's profitability growth was not able to offset the weak performance of the construction business in 2013. And as a result, the EPC segment's EBITDA margin turned at negative 7.3%.

<sup>1</sup>**EBITDA** - is defined as operating profit/loss adjusted for other income/expenses, depreciation and amortization, impairment of assets, provision for obsolete inventory,

provision for impairment of accounts receivable, unused vacation allowance, defined benefits scheme expenses, warranty provisions, provision for legal claims, provision for VAT and other taxes receivable, other provisions, excess of fair value of net assets acquired over the cost of acquisition. This measurement basis excludes the effects of non-recurring income and expenses on the results of the operating segments.

<sup>2</sup>**ROCE** - is calculated as EBIT divided by average total debt plus average equity

<sup>3</sup>**intake** - Under management accounts