

Lenta Limited and subsidiaries

Consolidated financial statements

For the year ended 31 December 2016

Lenta Limited and subsidiaries

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Lenta Limited and subsidiaries

Statement of management's responsibilities for the preparation and approval of the consolidated financial statements for the year ended 31 December 2016

The following statement is made with a view to the respective responsibilities of management in relation to the consolidated financial statements of Lenta Limited and its subsidiaries ("the Group").

Management is responsible for the preparation of these consolidated financial statements that present fairly the financial position of Lenta Limited and its subsidiaries ("the Group") as at 31 December 2016 and the results of its operations, cash flows and changes in shareholders' equity for the year then ended, in compliance with International Financial Reporting Standards ("IFRS").

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

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

Management is also responsible for:

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

The consolidated financial statements of the Group for the year ended 31 December 2016 were approved by management on 15 February 2017.

On behalf of the Management as authorised by the Board of Directors.



Jan Dunning
(CEO of Lenta Ltd)



Jago Lemmens
(CFO of Lenta Ltd)

Independent auditor's report

To the Shareholders and Board of Directors of Lenta Limited

Opinion

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

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

Basis for opinion

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

Key audit matters

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

We have fulfilled the responsibilities described in the Auditor's responsibilities for the audit of the consolidated financial statements section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying consolidated financial statements.

Capitalisation of construction costs

The Group incurs significant expenditures related to the construction of new retail stores, a part of which was capitalised under IAS 16 *Property, Plant and Equipment*. Capitalisation of construction costs was a matter of most significance in our audit because the balance of property, plant and equipment as of 31 December 2016 is significant to the consolidated financial statements. Information in respect of the balance of property, plant and equipment as of 31 December 2016 and additions for the year then ended is disclosed in Note 9 to the consolidated financial statements.

We obtained understanding of the Group's capitalisation policy and tested controls over authorisation, timeliness and accuracy of recording of property, plant and equipment additions. We compared the Group's investment budget with actual capital expenditures. On a sample basis we tested capital expenditures to supporting documents. We analysed aging of assets under construction.

Recognition of suppliers' allowances

The Group receives various types of allowances from suppliers in connection with the purchase of goods for resale in the form of volume discounts and other payments. The recognition of allowances was a matter of most significance in our audit because of its material impact on trade and other receivables, cost of goods sold and inventories. In addition, management exercises judgement in determining the period over which these allowances should be recognised considering the nature and the level of fulfilment of the Group's obligations and estimates of purchase volumes. Information about suppliers' rebates receivable and accounts receivable on suppliers' advertising as of 31 December 2016 is disclosed in Note 14 to the consolidated financial statements.

We understood and tested the design and operating effectiveness of internal controls over the recognition of allowances from suppliers. We agreed performance obligations to supporting documents approved by individual suppliers. We analysed the assumptions underlying management estimates of amounts receivable. On a sample basis we received direct confirmations of outstanding balances from suppliers. We agreed the balances of suppliers' allowances receivables to the post year-end cash settlements.

Other information included in the Group's 2016 annual report

Other information consists of the information included in the Annual report, other than the consolidated financial statements and our auditor's report thereon. Management is responsible for the other information. The Group's 2016 Annual report is expected to be made available to us after the date of this auditor's report.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

Responsibilities of management and Board of Directors for the financial statements

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

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

Board of Directors is responsible for overseeing the Group's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

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

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

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

- ▶ Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- ▶ Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

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

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

The partner in charge of the audit resulting in this independent auditor's report is Ilya Ananyev.



Ilya Ananyev
Partner
Ernst & Young LLC

15 February 2017

Details of the audited entity

Name: Lenta Ltd
Registered 16 July 2003.
Address: Road Town, Tortola, BVI.

Details of the auditor

Name: Ernst & Young LLC
Record made in the State Register of Legal Entities on 5 December 2002, State Registration Number 1027739707203.
Address: Russia 115035, Moscow, Sadovnicheskaya naberezhnaya, 77, building 1.
Ernst & Young LLC is a member of Self-regulated organization of auditors "Russian Union of auditors" (Association) ("SRO RUA"). Ernst & Young LLC is included in the control copy of the register of auditors and audit organizations, main registration number 11603050648.

Lenta Limited and subsidiaries

Consolidated statement of financial position as at 31 December 2016 (in thousands of Russian roubles)

	Note	31 December 2016	31 December 2015
Assets			
Non-current assets			
Property, plant and equipment	9	147,812,289	104,016,458
Prepayments for construction	10	7,741,743	6,528,355
Leasehold rights	11	3,744,009	3,047,168
Intangible assets other than leasehold rights	12	1,890,176	1,092,329
Long-term portion of cash flow hedging instruments	31	62,618	355,414
Deferred tax asset	22	123,508	–
Other non-current assets		199,131	–
Total non-current assets		161,573,474	115,039,724
Current assets			
Inventories	13	27,490,941	22,781,732
Trade and other receivable	14	17,035,789	13,646,894
Advances paid	15	2,669,761	2,264,911
Taxes recoverable	16	3,920,940	1,257,764
Advance payments for income tax		–	288,119
Prepaid expenses		131,932	217,711
Short-term portion of cash flow hedging instruments	31	309,592	439,050
Cash and cash equivalents	17	13,037,767	22,455,945
Total current assets		64,596,722	63,352,126
Total assets		226,170,196	178,391,850
Equity and liabilities			
Equity			
Share capital	18, 20	284	284
Additional paid-in capital	18	26,216,147	26,216,147
Share options	28	668,200	338,016
Hedging reserve	18	431,570	724,642
Retained earnings		31,052,910	19,850,882
Total equity		58,369,111	47,129,971
Liabilities			
Non-current liabilities			
Long-term borrowings	21	66,955,931	65,149,097
Deferred tax liabilities	22	7,359,998	5,229,804
Long-term portion of cash flow hedging instruments	31	2,137	24,564
Total non-current liabilities		74,318,066	70,403,465
Current liabilities			
Trade and other payables	23	56,171,598	48,820,207
Advances received		340,062	219,705
Other taxes payable	24	1,111,306	927,084
Current income tax payable		568,345	–
Short-term portion of cash flow hedging instruments	31	46,588	99,564
Short-term borrowings and short-term portion of long-term borrowings	21	35,245,120	10,773,277
Short-term obligations under finance leases		–	18,577
Total current liabilities		93,483,019	60,858,414
Total liabilities		167,801,085	131,261,879
Total equity and liabilities		226,170,196	178,391,850

The accompanying notes on pages 12-68 are an integral part of these financial statements.

Lenta Limited and subsidiaries

Consolidated statement of profit or loss and other comprehensive income for the year ended 31 December 2016 (in thousands of Russian roubles)

	Note	Year ended 31 December 2016	Year ended 31 December 2015
Sales		306,352,092	252,763,075
Cost of sales	25	(238,584,029)	(196,457,910)
Gross profit		67,768,063	56,305,165
Selling, general and administrative expenses	26	(46,442,510)	(36,044,771)
Other operating income	27	3,086,079	2,584,310
Other operating expense	27	(716,375)	(512,533)
Operating profit		23,695,257	22,332,171
Interest expense		(10,084,573)	(10,044,858)
Interest income		851,813	767,905
Ineffective portion of change in fair value of cash flow hedging instruments	31	—	6,308
Foreign exchange gains/(losses)		90,751	(189,423)
Profit before income tax		14,553,248	12,872,103
Income tax expense	22	(3,351,220)	(2,584,010)
Profit for the year		11,202,028	10,288,093
Other comprehensive income			
<i>Other comprehensive income to be reclassified to profit or loss in subsequent periods</i>			
Net loss from cash flow hedges	19	(366,340)	(2,326,519)
Income tax relating to the components of OCI	22	73,268	465,304
Other comprehensive loss for the year, net of tax		(293,072)	(1,861,215)
Total comprehensive income for the year, net of tax		10,908,956	8,426,878
Earnings per share (in thousands of Russian roubles per share) (Note 20)			
- basic and diluted, for profit for the year attributable to equity holders of the parent		0.115	0.112

The accompanying notes on pages 12-68 are an integral part of these financial statements.

Lenta Limited and subsidiaries

Consolidated statement of cash flows for the year ended 31 December 2016 (in thousands of Russian roubles)

	Note	Year ended 31 December 2016	Year ended 31 December 2015
Cash flows from operating activities			
Profit before income tax		14,553,248	12,872,103
<i>Adjustments for:</i>			
Net loss on disposal of property, plant and equipment		262,048	53,596
Net loss on disposal of intangible assets		–	6,486
Net loss on disposal of leasehold rights		1,279	59,235
Interest expense		10,084,573	10,044,858
Interest income		(851,813)	(767,905)
Inventory write-down / (reversal of write-down) to NRV	13	325,443	(38,710)
Change in bad debt allowance and impairment of advances and prepayments for construction	10, 14, 27	178,504	194,665
Depreciation and amortisation	9, 26	7,694,569	5,686,264
Share options expense	28	330,184	184,124
Ineffective portion of change in fair value of cash flow hedging instruments	31	–	(6,308)
		32,578,035	28,288,408
<i>Movements in working capital</i>			
Increase in trade and other receivables		(3,399,994)	(2,120,455)
(Increase)/decrease in advances paid	15	(406,727)	486,213
Increase in prepaid expenses		(33,427)	(52,232)
Increase in inventories	13	(4,821,288)	(3,113,641)
Increase in trade and other payables	23	5,159,820	1,228,784
Increase in advances received		115,017	5,754
(Decrease)/increase in net other taxes payable	16, 24	(1,281,209)	1,187,747
Cash from operating activities		27,910,227	25,910,578
Income taxes paid		(289,411)	(896,352)
Interest received		942,997	656,052
Interest paid		(8,845,027)	(9,745,887)
Net cash generated from operating activities		19,718,786	15,924,391
Cash flows from investing activities			
Purchases of property, plant and equipment		(41,688,957)	(30,434,839)
Acquisition of subsidiaries, net of cash acquired		(11,100,481)	–
Purchases of intangible assets other than leasehold rights		(1,088,745)	(486,224)
Purchases of leasehold rights		(630,989)	(557,827)
Proceeds from sale of property, plant and equipment		251,937	109,264
Net cash used in investing activities		(54,257,235)	(31,369,626)
Cash flows from financing activities			
Proceeds from borrowings		65,422,079	89,717,940
Repayments of borrowings		(40,283,231)	(85,565,000)
Repayments of obligations under financial lease		(18,577)	(16,888)
Proceeds from issue of new shares	18	–	21,788,593
Payment of loan commission		–	(59,250)
Net cash generated from financing activities		25,120,271	25,865,395
Net (decrease)/increase in cash and cash equivalents		(9,418,178)	10,420,160
Cash and cash equivalents at the beginning of the period	17	22,455,945	12,035,785
Cash and cash equivalents at the end of the period	17	13,037,767	22,455,945

The accompanying notes on pages 12-68 are an integral part of these financial statements.

Lenta Limited and subsidiaries

Consolidated statement of changes in equity for the year ended 31 December 2016 (in thousands of Russian roubles)

	Share capital	Additional paid-in capital	Hedging reserve	Share options reserve	Retained earnings	Total equity
Balance at 1 January 2016	284	26,216,147	724,642	338,016	19,850,882	47,129,971
Profit for the period	–	–	–	–	11,202,028	11,202,028
Other comprehensive income/(loss)	–	–	(293,072)	–	–	(293,072)
Total comprehensive income/(loss)	–	–	(293,072)	–	11,202,028	10,908,956
Share-based payments (Note 28)	–	–	–	330,184	–	330,184
Balance at 31 December 2016	284	26,216,147	431,570	668,200	31,052,910	58,369,111

	Share capital	Additional paid-in capital	Hedging reserve	Share options reserve	Retained earnings	Total equity
Balance at 1 January 2015	284	4,427,554	2,585,857	153,892	9,562,789	16,730,376
Profit for the period	–	–	–	–	10,288,093	10,288,093
Other comprehensive income/(loss)	–	–	(1,861,215)	–	–	(1,861,215)
Total comprehensive income/(loss)	–	–	(1,861,215)	–	10,288,093	8,426,878
Share-based payments (Note 28)	–	–	–	184,124	–	184,124
Issue of shares (Note 18, 28)	–	21,788,593	–	–	–	21,788,593
Balance at 31 December 2015	284	26,216,147	724,642	338,016	19,850,882	47,129,971

Notes

Additional paid-in capital: Additional paid-in capital is the difference between the fair value of consideration received and nominal value of the issued shares.

The accompanying notes on pages 12-68 are an integral part of these financial statements.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

1. The Lenta Group and its operations

The Lenta Group (the “Group”) comprises Lenta Limited (“the Company”) and its subsidiaries. The Group’s principal business activity is the development and operation of hypermarket and supermarket stores in Russia.

The Company was incorporated as a company limited by shares under the laws of the British Virgin Islands (BVI) on 16 July 2003. The Company’s registered address is at Road Town, Tortola, BVI. The registered office of the Group’s main operating entity, Lenta LLC, is located at 112, Savushkina Street, 197374, Saint-Petersburg, Russia.

Starting from March 2014 the Company’s shares were listed on the London Stock Exchange and Moscow Exchange in the form of Global Depositary Receipts (GDR). In 2015 two more public offerings took place at the London Stock Exchange and Moscow Exchange in the form of GDRs.

At 31 December 2015 and 2016 the Group has one main operational fully owned subsidiary, Lenta LLC, a legal entity registered under the laws of the Russian Federation. The principal activity of Lenta LLC is retail trade. Other subsidiaries including newly acquired (see Note 7) are property or investment holding companies by its nature.

2. Basis of preparation and significant accounting policies

Statement of compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (IASB).

2.1 Basis of preparation

The consolidated financial statements have been prepared on a historical cost basis, except for as described in accounting policies below. The consolidated financial statements are presented in Russian roubles and all values are rounded to the nearest thousand (RUB 000), except when otherwise indicated.

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the periods presented unless otherwise stated.

Management has considered the Group’s cash flow forecasts for the period ending 31 March 2018, which take into account the current and expected economic situation in Russia, the Group’s financial position, available borrowing facilities, and loan covenant compliance, planned store opening program and the anticipated cash flows and related expenditures from retail stores.

Accordingly, management is satisfied that it is appropriate to adopt the going concern basis of accounting in preparing the consolidated financial information for these consolidated financial statements.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

2. Basis of preparation and significant accounting policies (continued)

2.1 Basis of preparation (continued)

At 31 December 2016, the Group had net current liabilities of RUB 28,886,297 thousand (net current assets at 31 December 2015: 2,493,712 thousand).

Unused credit facilities available as of 31 December 2016 were RUB 44,150,000 thousand. Management believes that operating cash flows and available borrowing capacity will provide it adequate resources to fund its liabilities for the next year.

2.2 Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and other entities controlled by the Company (its subsidiaries) as at 31 December 2016. Control is achieved when the Group 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. Specifically, the Group controls an investee if and only if the Group has:

- ▶ Power over the investee (i.e. existing rights that give it the current ability to direct the relevant activities of the investee);
- ▶ Exposure, or rights, to variable returns from its involvement with the investee; and
- ▶ The ability to use its power over the investee to affect its returns.

Generally, there is a presumption that a majority of voting rights result in control. To support this presumption and when the Group has less than a majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

- ▶ The contractual arrangement with the other vote holders of the investee;
- ▶ Rights arising from other contractual arrangements;
- ▶ The Group's voting rights and potential voting rights.

The Group re-assesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control. Consolidation of a subsidiary begins when the Group obtains control over the subsidiary and ceases when the Group loses control of the subsidiary. Assets, liabilities, income and expenses of a subsidiary acquired or disposed of during the year are included in the statement of comprehensive income from the date the Group gains control until the date the Group ceases to control the subsidiary.

Profit or loss and each component of other comprehensive income (OCI) are attributed to the equity holders of the parent of the Group and to the non-controlling interests, even if this results in the non-controlling interests having a deficit balance. When necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with the Group's accounting policies. All intra-group assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the Group are eliminated in full on consolidation.

A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction. If the Group loses control over a subsidiary, it derecognises the related assets (including goodwill), liabilities, non-controlling interest and other components of equity while any resultant gain or loss is recognised in profit or loss. Any investment retained is recognised at fair value.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

2. Basis of preparation and significant accounting policies (continued)

2.2 Basis of consolidation (continued)

Subsidiaries are those companies (including special purpose entities) in which the Group, directly or indirectly, has an interest of more than one half of the voting rights or otherwise has power to govern the financial and operating policies so as to obtain economic benefits and which are neither associates nor joint ventures. The existence and effect of potential voting rights that are presently exercisable or presently convertible are considered when assessing whether the Group controls another entity. Subsidiaries are consolidated from the date on which control is transferred to the Group (acquisition date) and are de-consolidated from the date that control ceases.

2.3 Summary of significant accounting policies

Business combinations and goodwill

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the aggregate of the consideration transferred measured at acquisition date fair value and the amount of any non-controlling interest in the acquiree. For each business combination, the Group elects whether to measure the non-controlling interest in the acquiree at fair value or at the proportionate share of the acquiree's identifiable net assets. Acquisition-related costs are expensed as incurred and included in administrative expenses.

When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

If the business combination is achieved in stages, the previously held equity interest is remeasured at its acquisition date fair value and any resulting gain or loss is recognised in profit or loss.

Any contingent consideration to be transferred by the acquirer will be recognised at fair value at the acquisition date. Subsequently contingent consideration classified as an asset or liability is measured at fair value with changes in fair value recognised either in profit or loss. Contingent consideration that is classified as equity is not remeasured and subsequent settlement is accounted for within equity.

Goodwill is initially measured at cost, being the excess of the aggregate of the consideration transferred and the amount recognised for non-controlling interest over the net identifiable assets acquired and liabilities assumed.

If the fair value of the net assets acquired is in excess of the aggregate consideration transferred, the gain is recognised in profit or loss.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

2. Basis of preparation and significant accounting policies (continued)

2.3 Summary of significant accounting policies (continued)

Where goodwill has been allocated to a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the disposed operation is included in the carrying amount of the operation when determining the gain or loss from disposal. Goodwill disposed in these circumstances is measured based on the relative values of the disposed operation and the portion of the cash-generating unit retained.

Current versus non-current classification

The Group presents assets and liabilities in statement of financial position based on current/non-current classification. An asset is current when it is:

- ▶ Expected to be realised or intended to sold or consumed in normal operating cycle;
- ▶ Held primarily for the purpose of trading;
- ▶ Expected to be realised within twelve months after the reporting period; or
- ▶ Cash or cash equivalent unless restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period.

All other assets are classified as non-current. A liability is current when:

- ▶ It is expected to be settled in normal operating cycle;
- ▶ It is held primarily for the purpose of trading;
- ▶ It is due to be settled within twelve months after the reporting period; or
- ▶ There is no unconditional right to defer the settlement of the liability for at least twelve months after the reporting period.

The Group classifies all other liabilities as non-current.

Deferred tax assets and liabilities are classified as non-current assets and liabilities.

Fair value measurement

The Group measures financial instruments, such as, derivatives at fair value at each balance sheet date. Also, fair values of financial instruments measured at amortised cost are disclosed in Note 30.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- ▶ In the principal market for the asset or liability; or
- ▶ In the absence of a principal market, in the most advantageous market for the asset or liability.

The principal or the most advantageous market must be accessible to by the Group.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

2. Basis of preparation and significant accounting policies (continued)

2.3 Summary of significant accounting policies (continued)

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- ▶ Level 1 – quoted (unadjusted) market prices in active markets for identical assets or liabilities.
- ▶ Level 2 – valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable.
- ▶ Level 3 – valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Group determines whether transfers have occurred between Levels in the hierarchy by re-assessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

For the purpose of fair value disclosures, the Group has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy as explained above.

Functional and presentation currency

The presentation and functional currency of all Group entities is the Russian rouble ("RUB"), the national currency of the Russian Federation, the primary economic environment in which operating entities function.

Transactions in foreign currencies are initially recorded by the Group's entities at the functional currency spot rates at the date the transaction first qualifies for recognition.

Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency spot rates of exchange at the reporting date. Differences arising on settlement or translation of monetary items are recognised in profit or loss.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

2. Basis of preparation and significant accounting policies (continued)

2.3 Summary of significant accounting policies (continued)

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value is determined. The gain or loss arising on translation of non-monetary items measured at fair value is treated in line with the recognition of gain or loss from change in fair value of the item.

Property, plant and equipment

Property, plant and equipment are initially recorded at purchase or construction cost. Cost of replacing major parts or components of property, plant and equipment items is capitalised and the replaced part is retired. All other repair and maintenance costs are expensed as incurred.

Property, plant and equipment are stated at cost, net of accumulated depreciation and accumulated impairment losses, if any.

Gains and losses on disposals determined by comparing net proceeds with the respective carrying amount are recognised in profit or loss.

Construction in progress comprises costs directly related to the construction of property, plant and equipment including an appropriate allocation of directly attributable variable overheads that are incurred in construction. Depreciation of an asset begins when it is available for use, i.e. when it is in the location and condition necessary for it to be capable of operating in the manner intended by management. Construction in progress is reviewed regularly to determine whether its carrying value is recoverable and whether appropriate impairment loss has been recognised.

Properties in the course of construction for production, rental or administrative purposes, or for purposes not yet determined, are carried at cost, less any recognised impairment loss. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

Depreciation

Depreciation of property, plant and equipment is calculated using the straight-line method to write off their cost to their residual values over their estimated useful lives:

	Useful lives in years
Buildings	30
Land improvements	30
Machinery and equipment	5 to 15
Other	3 to 5

Leasehold rights

Leasehold rights acquired as part of hypermarket development projects are separately reported at cost less accumulated amortisation and accumulated impairment losses. These leasehold rights are amortised to profit or loss over the term of the lease, which is 49 years. If the Group further purchases the land plot previously leased, the carrying amount of the related leasehold right as of the date of purchase transaction is reclassified to the cost of land plot purchased.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

2. Basis of preparation and significant accounting policies (continued)

2.3 Summary of significant accounting policies (continued)

Finance leases

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

Assets held under finance leases are recognised as assets at their fair value at the inception of the lease or, if lower, at the present value of the minimum lease payments. The corresponding liability to the lessor is included in the statement of financial position as a finance lease obligation.

Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly to the profit and loss, unless they are directly attributable to qualifying assets, in which case they are capitalised in accordance with the Group's general policy on borrowing costs.

Operating lease payments are recognised as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

Intangible assets

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is their fair value at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and accumulated impairment losses.

Internally generated intangible assets, excluding capitalised development costs, are not capitalised and expenditure is reflected in profit and loss in the period in which the expenditure is incurred.

The useful lives of intangible assets are assessed as either finite or indefinite.

Intangible assets with finite lives are amortised over the useful economic life (which is from 3 to 7 years) using a straight-line method to write off their cost to their residual values and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at the end of each reporting period. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are considered to modify the amortisation period or method, as appropriate, and are treated as changes in accounting estimates. The amortisation expense on intangible assets with finite lives is recognised in the statement of profit or loss and other comprehensive income as the expense category that is consistent with the function of the intangible assets or included into the carrying amount of an asset as appropriate.

Intangible assets with indefinite useful lives are not amortised, but are tested for impairment annually, either individually or at the cash-generating unit level. The assessment of indefinite life is reviewed annually to determine whether the indefinite life continues to be supportable. If not, the change in useful life from indefinite to finite is made on a prospective basis.

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the profit or loss when the asset is derecognised.

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

2. Basis of preparation and significant accounting policies (continued)

2.3 Summary of significant accounting policies (continued)

Impairment of non-financial assets

At each reporting date, the Group reviews the carrying amounts of its non-financial assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). 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. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating unit, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

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

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

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

Income taxes

Income taxes have been provided for in the consolidated financial statements in accordance with management's interpretation of the relevant legislation enacted or substantively enacted as at the reporting date. The income tax charge comprises current tax and deferred tax and is recognised in the consolidated statement of profit or loss and other comprehensive income unless it relates to transactions that are recognised, in the same or a different period, directly in equity. In the case of a business combination, the tax effect is taken into account in calculating goodwill or determining the excess of the acquirer's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities over cost of consideration paid.

Current tax is the amount expected to be paid to or recovered from the taxation authorities in respect of taxable profits or losses for the current and prior periods. Deferred income tax is recorded using the balance sheet liability method for tax loss carry-forwards and temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred tax balances are measured at tax rates enacted or substantively enacted at the reporting date, which are expected to apply to the period when the temporary differences will reverse or the tax loss carry-forwards will be utilised. Deferred tax assets and liabilities are netted only within the individual companies of the Group. Deferred tax assets for deductible temporary differences and tax loss carry-forwards are recorded only to the extent that it is probable that future taxable profit will be available against which the deductions can be utilised.

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

2. Basis of preparation and significant accounting policies (continued)

2.3 Summary of significant accounting policies (continued)

Deferred tax liabilities are recognised for all taxable temporary differences, except:

- ▶ When the deferred tax liability arises from the initial recognition of goodwill or an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.
- ▶ In respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, when the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognised for all deductible temporary differences, the carry-forward of unused tax credits and any unused tax losses to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry-forward of unused tax credits and unused tax losses can be utilised, except:

- ▶ When the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.
- ▶ In respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are recognised only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each reporting date 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.

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 reporting date, 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.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost of inventory is determined on the weighted average basis. Net realisable value is the estimated selling price in the ordinary course of business, less the cost of completion and selling expenses. Cost comprises the direct cost of goods, transportation and handling costs. Cost of sales comprises only cost of inventories sold through retail stores and inventory write-downs made during the period.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

2. Basis of preparation and significant accounting policies (continued)

2.3 Summary of significant accounting policies (continued)

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets are capitalised as part of the cost of that asset, other borrowing costs are recognised in profit or loss in the period in which they are incurred. A qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale. For the purposes of borrowing costs recognition, a substantial period of time is considered to be a period of twelve months or more.

To the extent that the Group borrows funds generally and uses them for the purpose of obtaining a qualifying asset, the Group determines the amount of borrowing costs eligible for capitalisation by applying a capitalisation rate to the expenditures on that asset. The capitalisation rate is the weighted average of the borrowing costs applicable to the borrowings of the Group that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining a qualifying asset.

Revenue recognition

The sole source of revenue is retail sales. Revenue from the sale of goods is recognised at the point of sale.

The Group generates and recognises sales to retail customers in its stores at the point of sale. Retail sales are in cash and through bank cards. Revenues are measured at the fair value of the consideration received or receivable, recognised net of value added tax and are reduced for estimated customer returns. Historical information in relation to the timing and frequency of customer returns is used to estimate and provide for such returns at the time of sale.

Income generated from rental of spaces for small trading outlets within the Group's stores is recognised in the end of each month on a straight-line basis over the period of the lease, in accordance with the terms of the relevant lease agreements.

Interest income is recognised on a time-proportion basis using the effective interest rate method. Interest income is included into the Interest income line in the statement of comprehensive income.

Suppliers' allowances

The Group receives various types of allowances from vendors in the form of volume discounts and other forms of payments that effectively reduce the cost of goods purchased from the vendor. These allowances received from suppliers are recorded as a reduction in the price paid for the products and reduce cost of goods sold in the period the products are sold. Where a rebate agreement with a supplier covers more than one year, the rebates are recognised in the period in which they are earned.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

2. Basis of preparation and significant accounting policies (continued)

2.3 Summary of significant accounting policies (continued)

Employee benefits

The Group is subject to mandatory contributions to the Russian Federation defined contribution state pension benefit fund. Wages, salaries, contributions to the state pension and social insurance funds, paid annual leave and sick leave, bonuses, and non-monetary benefits are accrued in the year in which the associated services are rendered by the employees of the Group.

Share-based payments

Certain employees (including senior executives) of the Group receive remuneration in the form of share-based payments, whereby employees render services as consideration for equity instruments (equity-settled transactions).

The cost of equity-settled transactions is determined by the fair value at the date when the grant is made using an appropriate valuation model.

That cost is recognised, together with a corresponding increase in share options reserve in equity, over the period in which the performance and/or service conditions are fulfilled in employee benefits expense (Note 28). The cumulative expense recognised for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Group's best estimate of the number of equity instruments that will ultimately vest. The statement of profit or loss expense or credit for a period represents the movement in cumulative expense recognised as at the beginning and end of that period and is recognised in employee benefits expense (Note 28).

No expense is recognised for awards that do not ultimately vest, except for equity-settled transactions for which vesting is conditional upon a market or non-vesting condition. These are treated as vested irrespective of whether or not the market or non-vesting condition is satisfied, provided that all other performance and/or service conditions are satisfied.

When the terms of an equity-settled award are modified, the minimum expense recognised is the expense had the terms had not been modified, if the original terms of the award are met. An additional expense is recognised for any modification that increases the total fair value of the share-based payment transaction, or is otherwise beneficial to the employee as measured at the date of modification.

Pre-opening costs

Operating expenses incurred during the process of opening of new stores were recorded in the Group's consolidated statement of profit or loss and other comprehensive income. These expenses do not meet capitalisation criteria under IAS 16 *Property, Plant and Equipment* and include rent, utilities and other operating expenses.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

2. Basis of preparation and significant accounting policies (continued)

2.3 Summary of significant accounting policies (continued)

Segment reporting

The Group's business operations are located in the Russian Federation and relate primarily to retail sales of consumer goods. Although the Group operates through different stores and in various regions within the Russian Federation, the Group's chief operating decision maker reviews the Group's operations and allocates resources on an individual store-by-store basis. The Group has assessed the economic characteristics of the individual stores and determined that the stores have similar margins, similar products, similar types of customers and similar methods of distributing such products. Therefore, the Group considers that it only has one reportable segment under IFRS 8. Segment performance is evaluated based on a measure of revenue and earnings before interest, tax, depreciation and amortisation (EBITDA). EBITDA is non-IFRS measure. Other information is measured in a manner consistent with that in the consolidated financial statements.

Seasonality

The Group's business operations are stable during the year with limited seasonal impact, except for a significant increase of business activities in December.

Financial assets

General description

Financial assets are classified into the following specified categories: at fair value through profit or loss ("FVTPL"); held-to-maturity investments, "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.

All financial assets are recognised initially at fair value plus, in the case of financial assets not at fair value through profit or loss, directly attributable transaction costs.

Loans and receivables

Trade receivables, loans, and other receivables that have fixed or determinable payments that are not quoted in an active market are classified as loans and receivables. Loans and receivables are measured at amortised cost using the effective interest rate method.

Cash and cash equivalents

Cash and short-term deposits in the statement of financial position comprise cash at banks and on hand and short-term deposits with a maturity of three months or less.

Impairment of financial assets

Financial assets are assessed for indicators of impairment at each reporting date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the financial asset have been impacted. For financial assets carried at amortised cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate.

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

2. Basis of preparation and significant accounting policies (continued)

2.3 Summary of significant accounting policies (continued)

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 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 profit or loss.

With the exception of AFS equity instruments, 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 profit or loss 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

A financial asset is derecognised when:

- ▶ The rights to receive cash flows from the asset have expired;
- ▶ The Group has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a “pass-through” arrangement; and either (a) the Group has transferred substantially all the risks and rewards of the asset, or (b) the Group has neither transferred nor retained substantially all the risks and rewards of the asset but has transferred control of the asset.

When the Group has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, and has neither transferred nor retained substantially all of the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group’s continuing involvement in the asset.

In that case, the Group also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Group has retained.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Financial liabilities and equity instruments issued by the Group

Treasury shares

Own equity instruments that are reacquired (treasury shares) are recognised at cost and deducted from equity. No gain or loss is recognised in the statement of profit or loss and other comprehensive income on the purchase, sale, issue or cancellation of the Group’s own equity instruments. Any difference between the carrying amount and the consideration, if reissued, is recognised in additional paid-in capital. Voting rights related to treasury shares are nullified for the Group and no dividends are allocated to them. Share options exercised during the reporting period are satisfied with treasury shares.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

2. Basis of preparation and significant accounting policies (continued)

2.3 Summary of significant accounting policies (continued)

Share capital

Ordinary shares are classified as equity. Transaction costs of a share issue are shown within equity as a deduction from the equity.

Additional paid-in capital

Additional paid-in capital represents the difference between the fair value of consideration received and the nominal value of the issued shares.

Earnings per share

Basic earnings per share amounts are calculated by dividing the net profit for the year attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the year.

Diluted earnings per share amounts are calculated by dividing the net profit attributable to ordinary equity holders of the parent (after adjusting for interest on the convertible preference shares) by the weighted average number of ordinary shares outstanding during the year plus the weighted average number of ordinary shares that would be issued on conversion of all the dilutive potential ordinary shares into ordinary shares.

Classification as debt or equity

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement. An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments are recorded at the proceeds received, net of transaction costs.

Financial liabilities

Financial liabilities of the Group, including borrowings and trade and other payables, are initially recognised at fair value, net of transaction costs, and 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.

Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount is reported in the consolidated statement of financial position if there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, to realise the assets and settle the liabilities simultaneously.

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

2. Basis of preparation and significant accounting policies (continued)

2.3 Summary of significant accounting policies (continued)

Derivative financial instruments and hedge accounting

Initial recognition and subsequent measurement

The Group uses derivative financial instruments, such as interest rate swaps and caps, to hedge its interest rate risks. Such derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently re-measured at fair value. Derivatives are carried as financial assets when the fair value is positive and as financial liabilities when the fair value is negative.

Any gains or losses arising from changes in the fair value of derivatives are taken directly to profit or loss, except for the effective portion of cash flow hedges, which is recognised in OCI and later reclassified to profit or loss when the hedge item affects profit or loss.

At the inception of a hedge relationship, the Group formally designates and documents the hedge relationship to which the Group wishes to apply hedge accounting and the risk management objective and strategy for undertaking the hedge. The documentation includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the entity will assess the effectiveness of changes in the hedging instrument's fair value in offsetting the exposure to changes in the hedged item's fair value or cash flows attributable to the hedged risk. Such hedges are expected to be highly effective in achieving offsetting changes in fair value or cash flows and are assessed on an ongoing basis to determine that they actually have been highly effective throughout the financial reporting periods for which they were designated.

Swaps and caps used by the Group that meet the strict criteria for hedge accounting are accounted for as cash flow hedges. The effective portion of the gain or loss from the hedging instrument is recognised in other comprehensive income in the cash flow hedge reserve, while any ineffective portion is recognised immediately in profit or loss as other operating expenses.

Designation of a hedge relationship takes effect prospectively from the date all of the criteria are met. In particular, hedge accounting can be applied only from the date all of the necessary documentation is completed. Therefore, hedge relationships cannot be designated retrospectively.

Amounts recognised as OCI are transferred to profit or loss when the hedged transaction affects profit or loss, such as when the hedged financial income or financial expense is recognised or when a forecast sale occurs.

When the hedged item is the cost of a non-financial asset or non-financial liability, the amounts recognised as OCI are transferred to the initial carrying amount of the non-financial asset or liability.

If the hedging instrument expires or is sold, terminated or exercised without replacement or rollover (as part of the hedging strategy), or if its designation as a hedge is revoked, or when the hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss previously recognised in OCI remains separately in equity until the forecast transaction occurs or the foreign currency firm commitment is met.

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

2. Basis of preparation and significant accounting policies (continued)

2.3 Summary of significant accounting policies (continued)

Current versus non-current classification

Derivative instruments are classified as current or non-current or separated into current and non-current portions based on an assessment of the facts and circumstances (i.e., the underlying contracted cash flows):

- ▶ When the Group expects to hold a derivative as an economic hedge for a period beyond 12 months after the reporting date, the derivative is classified as non-current (or separated into current and non-current portions) consistent with the classification of the underlying item.

3. Significant accounting judgments, estimates and assumptions

In the application of the Group's accounting policies, which are described in Note 2 above, management is required to make judgments, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

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

Judgments that have the most significant effect on the amounts recognised in these consolidated financial statements and estimates that can cause a significant adjustment to the carrying amount of assets and liabilities within the next financial year include:

Judgments

Operating lease commitments – Group as lessor

The Group has entered into premises leases. The Group has determined, based on an evaluation of the terms and conditions of the arrangements, such as the lease term not constituting a substantial portion of the economic life of the commercial property, that it retains all the significant risks and rewards of ownership of these properties and accounts for the contracts as operating leases.

Assets versus business acquisition

From time to time in the normal course of business the Group acquires the companies that are a party to a lease contract, own the land plot or store in which the Group is interested. If at the date of acquisition by the Group, the company does not constitute an integrated set of activities and assets that 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 investor, the Group treats such acquisitions as a purchase of assets (a leasehold right, land plot or store) in the consolidated financial statements. The exercise of judgment determines whether a particular transaction is treated as a business combination or as a purchase of assets.

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

3. Significant accounting judgments, estimates and assumptions (continued)

Estimates and assumptions

The key assumptions concerning the future and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are described below. The Group based its assumptions and estimates on parameters available when the consolidated financial statements were prepared. Existing circumstances and assumptions about future developments, however, may change due to market changes or circumstances arising beyond the control of the Group. Such changes are reflected in the assumptions when they occur.

Leases renewal assumption

It is presumed that the initial land leases contracted for short terms will be renewed for 49 years at completion of construction of department stores. Thus, any long-term prepayments at the inception of the leases are presumed to have a 49-year useful life. Should the Group fail to renew the land lease contracts for a 49-year period, leasehold rights would have to be written off at the end of the initial lease term.

Inventory valuation

Management reviews the inventory balances to determine if inventories can be sold at amounts greater than or equal to their carrying amounts plus costs to sell. This review also includes the identification of slow moving inventories, which are written down based on inventories ageing and write down rates. The write down rates are determined by management following the experience of sales of such items.

Tax legislation

Russian tax, currency and customs legislation is subject to frequent changes and varying interpretations. Management's interpretation of such legislation in applying it to business transactions of the Group may be challenged by the relevant regional and federal authorities enabled by law to impose fines and penalties. Recent events in the Russian Federation suggest that the tax authorities are taking a more assertive position in their interpretation of the legislation and assessments and as a result, it is possible that the transactions that have not been challenged in the past may be challenged. Fiscal periods remain open to review by the tax authorities in respect of taxes for the three calendar years preceding the year of tax review. Under certain circumstances reviews may cover longer periods. While the Group believes it has provided adequately for all tax liabilities based on its understanding of the tax legislation, the above facts may create additional financial risks for the Group.

Fair value measurement of financial instruments

When the fair value of financial assets and financial liabilities recorded in the statement of financial position cannot be derived from active markets, their fair value is determined using valuation techniques including the discounted cash flow model. The inputs to these models are taken from observable markets where possible, but where this is not feasible, a degree of judgment is required in establishing fair values. The judgments include considerations of inputs such as liquidity risk, credit risk and volatility. Changes in assumptions about these factors could affect the reported fair value of financial instruments. See Note 30 for further discussion.

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

3. Significant accounting judgments, estimates and assumptions (continued)

Estimates and assumptions (continued)

Impairment of non-financial assets

The Group reviews the carrying amounts of its assets to determine whether there is any indication that those assets are impaired. Impairment exists when the carrying value of an asset or cash generating unit exceeds its recoverable amount, which is the higher of its fair value less costs to sell and its value in use.

The fair value less costs to sell calculation is based on available data from binding sales transactions, conducted at arm's length, for similar assets or observable market prices less incremental costs for disposing of the asset.

Due to their subjective nature, these estimates will likely differ from future actual results of operations and cash flows, and it is possible that these differences could be material.

The value in use calculation is based on a discounted cash flow model. In determining the value in use calculation, future cash flows are estimated from each store based on cash flows projection utilising the latest budget information available. The discounted cash flow model requires numerous estimates and assumptions regarding the future rates of market growth, market demand for the products and the future profitability of products.

Share-based payments

The Group measures the cost of equity-settled transactions by reference to the fair value of the equity instruments at the date at which they are granted. Estimating fair value for share-based payment transactions requires determination of the most appropriate valuation model, which is dependent on the terms and conditions of the grant. This estimate also requires determination of the most appropriate inputs to the valuation model including the expected life of the share option, volatility and dividend yield and making assumptions about them. The assumptions and models used for estimating fair value for share-based payment transactions are disclosed in Note 28.

4. Adoption of new or revised standards and interpretations

The accounting policies adopted in the preparation of the consolidated financial statements are consistent with those followed in the preparation of the Group's annual consolidated financial statements for the year ended 31 December 2015, except for the adoption of new or revised standards and interpretations effective as of 1 January 2016.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

4. Adoption of new or revised standards and interpretations (continued)

The nature and the impact of each new standard and amendment are described below:

IFRS 14 Regulatory Deferral Accounts

IFRS 14 is an optional standard that allows an entity, whose activities are subject to rate-regulation, to continue applying most of its existing accounting policies for regulatory deferral account balances upon its first-time adoption of IFRS. Entities that adopt IFRS 14 must present the regulatory deferral accounts as separate line items on the statement of financial position and present movements in these account balances as separate line items in the statement of profit or loss and OCI. The standard requires disclosure of the nature of, and risks associated with, the entity's rate-regulation and the effects of that rate-regulation on its financial statements.

Since the Group is an existing IFRS preparer and is not involved in any rate-regulated activities, this standard does not apply.

Amendments to IFRS 11 Joint Arrangements: Accounting for Acquisitions of Interests

The amendments to IFRS 11 require that a joint operator accounting for the acquisition of an interest in a joint operation, in which the activity of the joint operation constitutes a business, must apply the relevant IFRS 3 *Business Combinations* principles for business combination accounting. The amendments also clarify that a previously held interest in a joint operation is not remeasured on the acquisition of an additional interest in the same joint operation if joint control is retained. In addition, a scope exclusion has been added to IFRS 11 to specify that the amendments do not apply when the parties sharing joint control, including the reporting entity, are under common control of the same ultimate controlling party. The amendments apply to both the acquisition of the initial interest in a joint operation and the acquisition of any additional interests in the same joint operation and are applied prospectively. These amendments do not have any impact on the Group as there has been no interest acquired in a joint operation during the period.

Amendments to IAS 16 and IAS 38: Clarification of Acceptable Methods of Depreciation and Amortisation

The amendments clarify the principle in IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets* that revenue reflects a pattern of economic benefits that are generated from operating a business (of which the asset is a part) rather than the economic benefits that are consumed through use of the asset. As a result, a revenue-based method cannot be used to depreciate property, plant and equipment and may only be used in very limited circumstances to amortise intangible assets. The amendments are applied prospectively and do not have any impact on the Group, given that it has not used a revenue-based method to depreciate its non-current assets.

Amendments to IAS 16 and IAS 41 Agriculture: Bearer Plants

The amendments change the accounting requirements for biological assets that meet the definition of bearer plants. Under the amendments, biological assets that meet the definition of bearer plants will no longer be within the scope of IAS 41 *Agriculture*. Instead, IAS 16 will apply. After initial recognition, bearer plants will be measured under IAS 16 at accumulated cost (before maturity) and using either the cost model or revaluation model (after maturity). The amendments also require that produce that grows on bearer plants will remain in the scope of IAS 41 measured at fair value less costs to sell. For government grants related to bearer plants, IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* will apply. The amendments are applied retrospectively and do not have any impact on the Group as it does not have any bearer plants.

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

4. Adoption of new or revised standards and interpretations (continued)

Amendments to IAS 27: Equity Method in Separate Financial Statements

The amendments allow entities to use the equity method to account for investments in subsidiaries, joint ventures and associates in their separate financial statements. Entities already applying IFRS and electing to change to the equity method in their separate financial statements have to apply that change retrospectively.

These amendments do not have any impact on the Group's consolidated financial statements.

Annual improvements 2012-2014 cycle

These improvements include:

IFRS 5 Non-current Assets Held for Sale and Discontinued Operations

Assets (or disposal groups) are generally disposed of either through sale or distribution to the owners. The amendment clarifies that changing from one of these disposal methods to the other would not be considered a new plan of disposal, rather it is a continuation of the original plan. There is, therefore, no interruption of the application of the requirements in IFRS 5. This amendment is applied prospectively.

IFRS 7 Financial Instruments: Disclosures

(i) Servicing contracts

The amendment clarifies that a servicing contract that includes a fee can constitute continuing involvement in a financial asset. An entity must assess the nature of the fee and the arrangement against the guidance for continuing involvement in IFRS 7 in order to assess whether the disclosures are required. The assessment of which servicing contracts constitute continuing involvement must be made retrospectively. However, the required disclosures need not be provided for any period beginning before the annual period in which the entity first applies the amendments.

(ii) Applicability of the amendments to IFRS 7 to condensed interim financial statements

The amendment clarifies that the offsetting disclosure requirements do not apply to condensed interim financial statements, unless such disclosures provide a significant update to the information reported in the most recent annual report. This amendment is applied retrospectively.

IAS 19 Employee Benefits

The amendment clarifies that market depth of high quality corporate bonds is assessed based on the currency in which the obligation is denominated, rather than the country where the obligation is located. When there is no deep market for high quality corporate bonds in that currency, government bond rates must be used. This amendment is applied prospectively.

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

4. Adoption of new or revised standards and interpretations (continued)

Annual improvements 2012-2014 cycle (continued)

IAS 34 Interim Financial Reporting

The amendment clarifies that the required interim disclosures must either be in the interim financial statements or incorporated by cross-reference between the interim financial statements and wherever they are included within the interim financial report (e.g., in the management commentary or risk report). The other information within the interim financial report must be available to users on the same terms as the interim financial statements and at the same time. This amendment is applied retrospectively.

These amendments do not have any impact on the Group.

Amendments to IAS 1 Disclosure Initiative

The amendments to IAS 1 clarify, rather than significantly change, existing IAS 1 requirements. The amendments clarify:

- ▶ The materiality requirements in IAS 1;
- ▶ That specific line items in the statement(s) of profit or loss and OCI and the statement of financial position may be disaggregated;
- ▶ That entities have flexibility as to the order in which they present the notes to financial statements;
- ▶ That the share of OCI of associates and joint ventures accounted for using the equity method must be presented in aggregate as a single line item, and classified between those items that will or will not be subsequently reclassified to profit or loss.

Furthermore, the amendments clarify the requirements that apply when additional subtotals are presented in the statement of financial position and the statement(s) of profit or loss and OCI. These amendments do not have any impact on the Group.

Amendments to IFRS 10, IFRS 12 and IAS 28 Investment Entities: Applying the Consolidation Exception

The amendments address issues that have arisen in applying the investment entities exception under IFRS 10 *Consolidated Financial Statements*. The amendments to IFRS 10 clarify that the exemption from presenting consolidated financial statements applies to a parent entity that is a subsidiary of an investment entity, when the investment entity measures all of its subsidiaries at fair value. Furthermore, the amendments to IFRS 10 clarify that only a subsidiary of an investment entity that is not an investment entity itself and that provides support services to the investment entity is consolidated. All other subsidiaries of an investment entity are measured at fair value. The amendments to IAS 28 *Investments in Associates and Joint Ventures* allow the investor, when applying the equity method, to retain the fair value measurement applied by the investment entity associate or joint venture to its interests in subsidiaries.

These amendments are applied retrospectively and do not have any impact on the Group as the Group does not apply the consolidation exception.

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

5. Standards issued but not yet effective

The standards and interpretations that are issued, but not yet effective, up to the date of issuance of the Group's financial statements are disclosed below. The Group intends to adopt these standards, if applicable, when they become effective.

IFRS 9 Financial Instruments

In July 2014, the IASB issued the final version of IFRS 9 *Financial Instruments* that replaces IAS 39 *Financial Instruments: Recognition and Measurement* and all previous versions of IFRS 9. IFRS 9 brings together all three aspects of the accounting for the financial instruments project: classification and measurement; impairment; and hedge accounting. IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early application permitted. Except for hedge accounting, retrospective application is required, but providing comparative information is not compulsory. For hedge accounting, the requirements are generally applied prospectively, with some limited exceptions.

The Group plans to adopt the new standard on the required effective date. During 2016, the Group has performed a high-level impact assessment of all three aspects of IFRS 9. This preliminary assessment is based on currently available information and may be subject to changes arising from further detailed analyses or additional reasonable and supportable information being made available to the Group in the future. The Group does not expect a significant impact on its balance sheet or equity on applying the classification and measurement requirements of IFRS 9.

IFRS 9 requires the Group to record expected credit losses on all of its debt securities, loans and trade receivables, either on a 12-month or lifetime basis. The Group will need to perform a more detailed analysis which considers all reasonable and supportable information, including forward-looking elements to determine the extent of the impact.

The Group believes that all existing hedge relationships that are currently designated in effective hedging relationships will still qualify for hedge accounting under IFRS 9. As IFRS 9 does not change the general principles of how an entity accounts for effective hedges, the Group does not expect a significant impact as a result of applying IFRS 9.

IFRS 15 Revenue from Contracts with Customers

IFRS 15 was issued in May 2014 and establishes a new five-step model that will apply to revenue arising from contracts with customers. Under IFRS 15 revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer.

The new revenue standard will supersede all current revenue recognition requirements under IFRS. Either a full retrospective application or a modified retrospective application is required for annual periods beginning on or after 1 January 2018. Early adoption is permitted. The Group is currently assessing the impact of IFRS 15 and plans to adopt the new standard on the required effective date.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

5. Standards issued but not yet effective (continued)

Amendments to IFRS 10 and IAS 28: Sale or Contribution of Assets between an Investor and its Associate or Joint Venture

The amendments address the conflict between IFRS 10 and IAS 28 in dealing with the loss of control of a subsidiary that is sold or contributed to an associate or joint venture. The amendments clarify that the gain or loss resulting from the sale or contribution of assets that constitute a business, as defined in IFRS 3, between an investor and its associate or joint venture, is recognised in full. Any gain or loss resulting from the sale or contribution of assets that do not constitute a business, however, is recognised only to the extent of unrelated investors' interests in the associate or joint venture. The IASB has deferred the effective date of these amendments indefinitely, but an entity that early adopts the amendments must apply them prospectively. The Group will apply these amendments when they become effective.

IAS 7 Disclosure Initiative – Amendments to IAS 7

The amendments to IAS 7 *Statement of Cash Flows* are part of the IASB's *Disclosure Initiative* and require an entity to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes. On initial application of the amendment, entities are not required to provide comparative information for preceding periods. These amendments are effective for annual periods beginning on or after 1 January 2017, with early application permitted. Application of the amendments will result in additional disclosures provided by the Group.

IAS 12 Recognition of Deferred Tax Assets for Unrealised Losses – Amendments to IAS 12

The amendments clarify that an entity needs to consider whether tax law restricts the sources of taxable profits against which it may make deductions on the reversal of that deductible temporary difference. Furthermore, the amendments provide guidance on how an entity should determine future taxable profits and explain the circumstances in which taxable profit may include the recovery of some assets for more than their carrying amount. Entities are required to apply the amendments retrospectively. However, on initial application of the amendments, the change in the opening equity of the earliest comparative period may be recognised in the opening retained earnings (or in another component of equity, as appropriate), without allocating the change between opening retained earnings and other components of equity. Entities applying this relief must disclose that fact. These amendments are effective for annual periods beginning on or after 1 January 2017 with early application permitted. If an entity applies the amendments for an earlier period, it must disclose that fact. These amendments are not expected to have any impact on the Group.

IFRS 2 Classification and Measurement of Share-based Payment Transactions – Amendments to IFRS 2

The IASB issued amendments to IFRS 2 *Share-based Payment* that address three main areas: the effects of vesting conditions on the measurement of a cash-settled share-based payment transaction; the classification of a share-based payment transaction with net settlement features for withholding tax obligations; and accounting where a modification to the terms and conditions of a share-based payment transaction changes its classification from cash settled to equity settled.

On adoption, entities are required to apply the amendments without restating prior periods, but retrospective application is permitted if elected for all three amendments and other criteria are met. The amendments are effective for annual periods beginning on or after 1 January 2018, with early application permitted. The Group is assessing the potential effect of the amendments on its consolidated financial statements.

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

5. Standards issued but not yet effective (continued)

IFRS 16 Leases

IFRS 16 was issued in January 2016 and it replaces IAS 17 *Leases*, IFRIC 4 *Determining whether an Arrangement Contains a Lease*, SIC-15 *Operating Leases-Incentives* and SIC-27 *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to account for all leases under a single on-balance sheet model similar to the accounting for finance leases under IAS 17. The standard includes two recognition exemptions for lessees – leases of 'low-value' assets (e.g., personal computers) and short-term leases (i.e., leases with a lease term of 12 months or less). At the commencement date of a lease, a lessee will recognise a liability to make lease payments (i.e., the lease liability) and an asset representing the right to use the underlying asset during the lease term (i.e., the right-of-use asset). Lessees will be required to separately recognise the interest expense on the lease liability and the depreciation expense on the right-of-use asset. Lessees will be also required to remeasure the lease liability upon the occurrence of certain events (e.g., a change in the lease term, a change in future lease payments resulting from a change in an index or rate used to determine those payments). The lessee will generally recognise the amount of the remeasurement of the lease liability as an adjustment to the right-of-use asset. Lessor accounting under IFRS 16 is substantially unchanged from today's accounting under IAS 17. Lessors will continue to classify all leases using the same classification principle as in IAS 17 and distinguish between two types of leases: operating and finance leases.

IFRS 16 also requires lessees and lessors to make more extensive disclosures than under IAS 17.

IFRS 16 is effective for annual periods beginning on or after 1 January 2019. Early application is permitted, but not before an entity applies IFRS 15. A lessee can choose to apply the standard using either a full retrospective or a modified retrospective approach. The standard's transition provisions permit certain reliefs.

The Group is assessing the potential effect of the amendments on its consolidated financial statements.

IFRS 1 First-time Adoption of International Financial Reporting Standards – Amendments to IFRS 1

The amendment repeals short-term exemptions for first-time adopters. The amendment is effective from 1 January 2018. These amendments are not expected to have any impact on the Group.

IAS 28 Investments in Associates and Joint Ventures – Amendments to IAS 28

The amendments clarifies that an entity that is a venture capital organisation, or other qualifying entity, may elect, at initial recognition on an investment-by-investment basis, to measure its investments in associates and joint ventures at fair value through profit or loss. If an entity that is not itself an investment entity has an interest in an associate or joint venture that is an investment entity, the entity may, when applying the equity method, elect to retain the fair value measurement applied by that investment entity associate or joint venture to the investment entity associate's or joint venture's interests in subsidiaries. This election is made separately for each investment entity associate or joint venture, at the later of the date on which (a) the investment entity associate or joint venture is initially recognised; (b) the associate or joint venture becomes an investment entity; and (c) the investment entity associate or joint venture first becomes a parent. The amendments should be applied retrospectively and are effective from 1 January 2018, with earlier application permitted. If an entity applies those amendments for an earlier period, it must disclose that fact. These amendments are not expected to have any impact on the Group.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

5. Standards issued but not yet effective (continued)

IFRS 12 Disclosure of Interests in Other Entities – Amendments to IFRS 12

The amendments clarify that the disclosure requirements in IFRS 12, other than those in paragraphs B10-B16, apply to an entity's interest in a subsidiary, a joint venture or an associate (or a portion of its interest in a joint venture or an associate) that is classified (or included in a disposal group that is classified) as held for sale. The amendments are effective from 1 January 2017 and must be applied retrospectively. These amendments are not expected to have any impact on the Group.

IFRIC Interpretation 22 Foreign Currency Transactions and Advance Consideration

The interpretation clarifies that in determining the spot exchange rate to use on initial recognition of the related asset, expense or income (or part of it) on the derecognition of a non-monetary asset or non-monetary liability relating to advance consideration, the date of the transaction is the date on which an entity initially recognises the nonmonetary asset or non-monetary liability arising from the advance consideration. If there are multiple payments or receipts in advance, then the entity must determine a date of the transactions for each payment or receipt of advance consideration.

Entities may apply the amendments on a fully retrospective basis. Alternatively, an entity may apply the interpretation prospectively to all assets, expenses and income in its scope that are initially recognised on or after: (i) the beginning of the reporting period in which the entity first applies the interpretation or (ii) the beginning of a prior reporting period presented as comparative information in the financial statements of the reporting period in which the entity first applies the interpretation. Early application of interpretation is permitted and must be disclosed. First-time adopters of IFRS are also permitted to apply the interpretation prospectively to all assets, expenses and income initially recognised on or after the date of transition to IFRS.

The amendments are intended to eliminate diversity in practice, when recognising the related asset, expense or income (or part of it) on the derecognition of a nonmonetary asset or non-monetary liability relating to advance consideration received or paid in foreign currency.

The amendments are effective for annual periods beginning on or after 1 January 2018.

These amendments are not expected to have any impact on the Group.

IAS 40 Investment property – Amendments to IAS 40

The amendments clarify when an entity should transfer property, including property under construction or development into, or out of investment property. The amendments state that a change in use occurs when the property meets, or ceases to meet, the definition of investment property and there is evidence of the change in use. A mere change in management's intentions for the use of a property does not provide evidence of a change in use.

Entities should apply the amendments prospectively to changes in use that occur on or after the beginning of the annual reporting period in which the entity first applies the amendments. An entity should reassess the classification of property held at that date and, if applicable, reclassify property to reflect the conditions that exist at that date. Retrospective application in accordance with IAS 8 is only permitted if that is possible without the use of hindsight. Early application of the amendments is permitted and must be disclosed. The amendments will eliminate diversity in practice. The amendments are effective for annual periods beginning on or after 1 January 2018.

These amendments are not expected to have any impact on the Group.

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

5. Standards issued but not yet effective (continued)

Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts – Amendments to IFRS 4

The amendments address concerns arising from implementing the new financial instruments Standard, IFRS 9, before implementing the new insurance contracts standard that the Board is developing to replace IFRS 4. The amendments introduce two options for entities issuing insurance contracts: a temporary exemption from applying IFRS 9 and an overlay approach.

These amendments are not expected to have any impact on the Group.

Temporary exemption from IFRS 9

The optional temporary exemption from IFRS 9 is available to entities whose activities are predominantly connected with insurance. The temporary exemption permits such entities to continue to apply IAS 39 *Financial Instruments: Recognition and Measurement* while they defer the application of IFRS 9 until 1 January 2021 at the latest. Predominance must be initially assessed at the annual reporting date that immediately precedes 1 April 2016 and before IFRS 9 is implemented. Also the evaluation of predominance can only be reassessed in rare cases. Entities applying the temporary exemption will be required to make additional disclosures.

The overlay approach

The overlay approach is an option for entities that adopt IFRS 9 and issue insurance contracts, to adjust profit or loss for eligible financial assets; effectively resulting in IAS 39 accounting for those designated financial assets. The adjustment eliminates accounting volatility that may arise from applying IFRS 9 without the new insurance contracts standard. Under this approach, an entity is permitted to reclassify amounts between profit or loss and other comprehensive income (OCI) for designated financial assets. An entity must present a separate line item for the amount of the overlay adjustment in profit or loss, as well as a separate line item for the corresponding adjustment in OCI.

The temporary exemption is first applied for reporting periods beginning on or after 1 January 2018. An entity may elect the overlay approach when it first applies IFRS 9 and apply that approach retrospectively to financial assets designated on transition to IFRS 9. The entity restates comparative information reflecting the overlay approach if, and only if, the entity restates comparative information when applying IFRS 9.

The overlay approach requires an entity to remove from profit or loss additional volatility that may arise if IFRS 9 is applied with IFRS 4. When applying the temporary exemption, entities must still provide extensive disclosure that require the application of some aspects of IFRS 9.

The amendments are effective for annual periods beginning on or after 1 January 2018

These amendments are not expected to have any impact on the Group.

6. Operating segments

The Group's principal business activity is the development and operation of food retail stores located in Russia. Risks and returns are affected primarily by economic development in Russia and by the development of Russian food retail industry.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

6. Operating segments (continued)

The Group has no significant assets outside the Russian Federation (excluding investments in its foreign wholly owned intermediate holding subsidiary Zoronvo Holdings Limited, which is eliminated on consolidation). Due to the similar economic characteristics of food retail stores, the Group's management has aggregated its operating segments represented by stores into one reportable operating segment. Within the segment all business components are similar in respect of:

- ▶ The products;
- ▶ The customers;
- ▶ Centralised Group structure (commercial, operational, logistic, finance, HR and IT functions are centralised).

The Group's operations are regularly reviewed by the chief operating decision maker, represented by the CEO, to analyse performance and allocate resources within the Group. The CEO assesses the performance of operating segments based on the dynamics of revenue and earnings before interest, tax, depreciation, amortisation (EBITDA).

The accounting policies used for the operating segment are the same as accounting policies applied for the consolidated financial statements.

The segment information for the year ended 31 December 2016 and 2015 is as follows:

	Year ended 31 December 2016	Year ended 31 December 2015
Sales	306,352,092	252,763,075
EBITDA	31,389,826	28,018,435

Reconciliation of EBITDA to IFRS profit for the year is as follows:

	Year ended 31 December 2016	Year ended 31 December 2015
EBITDA	31,389,826	28,018,435
Interest expense	(10,084,573)	(10,044,858)
Interest income	851,813	767,905
Income tax expense (see Note 22)	(3,351,220)	(2,584,010)
Depreciation/amortisation (see Note 9, 11, 12, 26)	(7,694,569)	(5,686,264)
Ineffective portion of the change in fair value of cash flow hedging instruments (see Note 31)	–	6,308
Foreign exchange gain/(loss)	90,751	(189,423)
Profit for the year	11,202,028	10,288,093

7. Acquisition of subsidiaries

On 30 November 2016 the Group purchased the Kesko food retail business in Russia ("KFR"), operating under the K-Ruoka brand. The Group became the owner of 100% participatory interests in six KFR companies registered in Russia and dealing in food and non-food retail business through a chain of 11 hypermarkets. As a result, cost of acquisition of all of the participatory interests in six KFR companies for the Group amounted to RUB 11,296,152, including cash consideration paid of RUB 11,414,113, less adjustment for working capital of RUB 117,961 at acquisition date.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

7. Acquisition of subsidiaries (continued)

The financial position and results of operations of KFR were included in the Group's consolidated financial statements beginning from 30 November 2016. As of the date of issuance of these consolidated financial statements, the Group and Kesko Food Russia Holding Oy (the seller) have not finalised the working capital adjustment of the acquired entities and the Group has not completed its purchase price allocation in accordance with IFRS 3 *Business Combinations*. Accordingly, the acquisition of KFR has been accounted for based on provisional values.

The Group assigned provisional values to net assets acquired based on estimates of an independent appraiser. The Group will finalise the purchase price allocation within 12 months from the acquisition date.

Provisional fair values of the identifiable assets and liabilities of KFR at the date of acquisition were:

	Provisional values at the acquisition date
Property, plant and equipment (Note 9)	9,992,668
Prepayments for construction	10,590
Leasehold rights (Note 11)	751,919
Deferred tax asset (Note 22)	208,137
Inventories	213,364
Trade and other receivable	123,296
Advances paid	47,398
VAT and other taxes recoverable	312,766
Cash and cash equivalents	313,632
Deferred tax liability (Note 22)	(74,296)
Trade and other payables	(589,532)
Advances received	(5,340)
Current income tax payable	(8,450)
Fair value of the identifiable net assets	11,296,152
Total acquisition cost	11,296,152

The fair value of the trade and other receivables amounts to RUB 123,296. The gross amount of trade receivables is RUB 126,096, of which RUB 2,800 have been impaired. It is expected that the rest contractual amounts can be collected.

During the year ended 31 December 2016 cash flow of acquisition was as follows:

	Cash flow of acquisition
Cash paid	11,414,113
Less cash acquired with subsidiaries	(313,632)
Net cash flow on acquisition	11,100,481

From the date of acquisition the contribution to revenue and profit before tax of KFR was RUB 1,053,797 and RUB 19,252 respectively. It is not practicable to determine contribution to revenue and profit before tax of KFR if it had been acquired at the beginning of the year ended 31 December 2016 due to different management and operational styles of acquired business and the Group.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

8. Balances and transactions with related parties

The transactions with related parties are made on terms equivalent to those that prevail in arm's length transactions.

The consolidated financial statements include the following balances with related parties:

Entities with significant influence over the Group:

	31 December 2016	31 December 2015
EBRD		
Long-term loans payable	–	4,520,527
Accrued liabilities	75	6,559
Interest accrued	–	1,691
TPG Capital		
Accrued liabilities	3,260	13,848

The following transactions were carried out with related parties:

Entities with significant influence over the Group:

	Year ended 31 December 2016	Year ended 31 December 2015
EBRD		
Repayments of borrowings	(4,554,240)	–
Interest expense	340,077	833,200
Directors fee	–	25,483
Business trip expenses	155	323
Consulting services	75	–
TPG Capital		
Directors fee	28,784	23,642
Business trip expenses	1,214	19,919
Consulting services	–	2,807

Remuneration to the members of the Board of Directors and key management personnel is as follows:

	Year ended 31 December 2016	Year ended 31 December 2015
Short-term benefits	666,246	682,421
Long-term benefits (share-based payments, Note 28)	280,693	158,645
Total remuneration	946,939	841,066

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

9. Property, plant and equipment

	Land	Land improve- ments	Buildings	Machinery and equipment	Assets under construction	Total
Cost						
Balance at 1 January 2016	12,582,774	7,116,578	71,205,405	29,434,011	3,564,759	123,903,527
Additions	19,046	–	–	66	41,041,432	41,060,544
Transfers from construction in progress	3,397,951	2,642,680	23,360,680	11,769,060	(41,170,371)	–
Transfers from leasehold rights	618,314	–	–	–	–	618,314
Acquisition of subsidiaries (Note 7)	1,253,373	309,987	6,089,079	2,323,192	17,037	9,992,668
Disposals	(857)	(5,420)	(163,705)	(565,266)	(164,791)	(900,039)
Balance at 31 December 2016	17,870,601	10,063,825	100,491,459	42,961,063	3,288,066	174,675,014
Accumulated depreciation and impairment						
Balance at 1 January 2016	–	1,041,933	8,647,931	10,197,205	–	19,887,069
Charge for the year	–	258,724	2,702,141	4,376,332	–	7,337,197
Disposals	–	(529)	(24,140)	(336,872)	–	(361,541)
Balance at 31 December 2016	–	1,300,128	11,325,932	14,236,665	–	26,862,725
Net book value						
Balance at 1 January 2016	12,582,774	6,074,645	62,557,474	19,236,806	3,564,759	104,016,458
Balance at 31 December 2016	17,870,601	8,763,697	89,165,527	28,724,398	3,288,066	147,812,289
	Land	Land improve- ments	Buildings	Machinery and equipment	Assets under construction	Total
Cost						
Balance at 1 January 2015	9,971,338	5,488,814	54,610,275	21,331,730	4,542,748	95,944,905
Additions	–	–	87,269	611	27,642,190	27,730,070
Transfers from construction in progress	2,035,686	1,650,598	16,510,017	8,370,416	(28,566,717)	–
Transfers from leasehold rights	655,359	–	–	–	–	655,359
Disposals	(79,609)	(22,834)	(2,156)	(268,746)	(53,462)	(426,807)
Balance at 31 December 2015	12,582,774	7,116,578	71,205,405	29,434,011	3,564,759	123,903,527
Accumulated depreciation and impairment						
Balance at 1 January 2015	–	848,274	6,621,417	7,257,007	–	14,726,698
Charge for the year	–	193,659	2,028,335	3,138,721	–	5,360,715
Disposals	–	–	(1,821)	(198,523)	–	(200,344)
Balance at 31 December 2015	–	1,041,933	8,647,931	10,197,205	–	19,887,069
Net book value						
Balance at 1 January 2015	9,971,338	4,640,540	47,988,858	14,074,723	4,542,748	81,218,207
Balance at 31 December 2015	12,582,774	6,074,645	62,557,474	19,236,806	3,564,759	104,016,458

During the year ended 31 December 2016 and the year ended 31 December 2015 the Group is not involved in acquisition of any assets that would satisfy the definition of qualifying assets for the purposes of borrowing costs capitalisation. Thus, no borrowings costs were capitalised during those periods.

Land and buildings with a carrying amount of RUB 3,956,848 thousand were pledged under secured loan agreement with EBRD as at 31 December 2015. All pledged assets were released upon termination of the loan agreement with EBRD on 30 June 2016 (see Note 21).

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

9. Property, plant and equipment (continued)

No property, plant and equipment is held by the Group under finance leases at 31 December 2016.

At 31 December 2015 the carrying amount of property, plant and equipment held under finance leases is RUB 37,532 thousand.

Depreciation and amortisation expense

The amount of depreciation charged during the year ended 31 December 2016 and year ended 31 December 2015 is presented within depreciation and amortisation in the Group's consolidated statement of profit or loss and other comprehensive income and statement of cash flows as follows:

	Year ended 31 December 2016	Year ended 31 December 2015
Depreciation of property, plant and equipment (Note 9)	7,337,197	5,360,715
Amortisation of intangible assets (Note 12)	290,898	257,940
Leasehold rights amortisation (Note 11)	66,474	67,609
Total depreciation and amortisation	7,694,569	5,686,264

See Note 29 for capital commitments.

10. Prepayments for construction

Prepayments for construction are represented by advances given to the constructors for the building of the stores and to suppliers.

Prepayments are regularly monitored on the subject of impairment. An impairment analysis is performed at each reporting date on an individual basis for counterparties. A provision for impairment is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of prepayments. As at 31 December 2016 the Group impaired RUB 378,672 of prepayments (31 December 2015: RUB 235,995).

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

11. Leasehold rights

Leasehold rights as at 31 December 2016 consist of the following:

	<u>Leasehold rights</u>
Cost	
At 1 January 2016	3,255,655
Additions	630,989
Acquisition of subsidiaries (Note 7)	751,919
Disposals	(1,279)
Transfer to PPE	(657,637)
At 31 December 2016	3,979,647
Accumulated amortisation	
At 1 January 2016	208,487
Charge for the year	66,474
Transfer to PPE	(39,323)
At 31 December 2016	235,638
Net book value	
At 1 January 2016	3,047,168
At 31 December 2016	3,744,009

Leasehold rights as at 31 December 2015 consisted of the following:

	<u>Leasehold rights</u>
Cost	
At 1 January 2015	3,486,162
Additions	557,827
Disposals	(63,559)
Transfer to PPE	(724,775)
At 31 December 2015	3,255,655
Accumulated amortisation	
At 1 January 2015	214,618
Charge for the year	67,609
Disposals	(4,324)
Transfer to PPE	(69,416)
At 31 December 2015	208,487
Net book value	
At 1 January 2015	3,271,544
At 31 December 2015	3,047,168

Amortisation expense is included in selling, general and administrative expenses (Note 26).

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

12. Intangible assets other than leasehold rights

Intangible assets other than leasehold rights as at 31 December 2016 consist of the following:

	<u>Software</u>	<u>Trade marks</u>	<u>Total</u>
Cost			
At 1 January 2016	2,078,687	549	2,079,236
Additions	1,088,745	–	1,088,745
At 31 December 2016	3,167,432	549	3,167,981
Accumulated amortisation			
At 1 January 2016	986,358	549	986,907
Amortisation for the period	290,898	–	290,898
At 31 December 2016	1,277,256	549	1,277,805
Net book value			
At 1 January 2016	1,092,329	–	1,092,329
At 31 December 2016	1,890,176	–	1,890,176

Intangible assets other than leasehold rights as at 31 December 2015 consisted of the following:

	<u>Software</u>	<u>Trade marks</u>	<u>Total</u>
Cost			
At 1 January 2015	1,603,385	549	1,603,934
Additions	486,224	–	486,224
Disposals	(10,922)	–	(10,922)
At 31 December 2015	2,078,687	549	2,079,236
Accumulated amortisation			
At 1 January 2015	732,870	533	733,403
Amortisation for the period	257,924	16	257,940
Disposals	(4,436)	–	(4,436)
At 31 December 2015	986,358	549	986,907
Net book value			
At 1 January 2015	870,515	16	870,531
At 31 December 2015	1,092,329	–	1,092,329

Amortisation expense is included in selling, general and administrative expenses (Note 26).

13. Inventories

	<u>31 December 2016</u>	<u>31 December 2015</u>
Goods for resale (at lower of cost and net realisable value)	26,191,962	21,809,738
Raw materials	1,298,979	971,994
Total inventories	27,490,941	22,781,732

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

13. Inventories (continued)

Raw materials are represented by inventories used in own production process in butchery, bakery and culinary.

	31 December 2016	31 December 2015
Goods for resale (at cost)	27,437,087	22,729,419
Write down to net realisable value	(1,245,125)	(919,681)
Goods for resale (at lower of cost and net realisable value)	26,191,962	21,809,738

During the reporting period the Group wrote down inventories to their net realisable value, which resulted in recognition of expenses within cost of sales in the consolidated statement of profit or loss and other comprehensive income for the year ended 31 December 2016 in the amount of RUB 325,443 thousand (compared to RUB 38,710 thousand of expense reversal recognised in the year ended 31 December 2015).

14. Trade and other receivables

	31 December 2016	31 December 2015
Accounts receivable on rental and other services and on suppliers' advertising	12,892,578	9,727,574
Suppliers' rebates receivable	3,858,738	3,643,232
Other receivables	352,258	307,105
Bad debt allowance	(67,785)	(31,017)
Total trade and other receivables	17,035,789	13,646,894

Receivables are due normally within 25 days according to the terms of standard contracts. Outstanding receivables are regularly monitored. An impairment analysis is performed at each reporting date on an individual basis for counterparties. A provision for impairment of receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. Usually for receivables over 365 days the allowance for doubtful debts is 100%, unless there are strong indications from the nature of the agreement underlying the debt that no allowance is needed as the long term of the receivable is in line with the agreement. Allowances for doubtful debts are recognised against receivables of under 365 days based on estimated irrecoverable amounts determined by reference to past default experience of each particular counterparty and an analysis of the counterparty's current financial position.

Amounts receivable from suppliers and accounts receivable on rental and other services disclosed above include amounts (see below for ageing analysis) that are past due at the end of the reporting period for which the Group has not recognised an allowance for doubtful debts because there has not been a significant change in credit quality and the amounts are still considered recoverable. The Group does not hold any collateral or other credit enhancements over these balances.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

14. Trade and other receivables (continued)

Ageing of trade and other receivables that are past due but not impaired as at 31 December 2016:

	<u>0-60 days overdue</u>	<u>60-120 days overdue</u>	<u>120-365 days overdue</u>	<u>Neither past due nor impaired</u>	<u>Total</u>
Suppliers' volume rebates receivable	322,208	5,613	22,260	3,486,694	3,836,775
Accounts receivable on rental and other services	758,337	53,411	60,141	11,975,546	12,847,435
Other receivables	64,594	9,814	20,689	256,482	351,579
Total	<u>1,145,139</u>	<u>68,838</u>	<u>103,090</u>	<u>15,718,722</u>	<u>17,035,789</u>

Ageing of trade and other receivables that were past due but not impaired as at 31 December 2015:

	<u>0-60 days overdue</u>	<u>60-120 days overdue</u>	<u>120-365 days overdue</u>	<u>Neither past due nor impaired</u>	<u>Total</u>
Suppliers' volume rebates receivable	87,469	8,326	30,827	3,513,960	3,640,582
Accounts receivable on rental and other services	1,206,134	45,621	43,801	8,406,211	9,701,767
Other receivables	80,450	4,157	1,376	218,562	304,545
Total	<u>1,374,053</u>	<u>58,104</u>	<u>76,004</u>	<u>12,138,733</u>	<u>13,646,894</u>

15. Advances paid

	<u>31 December 2016</u>	<u>31 December 2015</u>
Advances to suppliers of goods	1,162,541	788,124
Advances for services	1,109,412	1,066,570
Guarantee payments under lease contracts	397,808	410,217
Total advances paid	<u>2,669,761</u>	<u>2,264,911</u>

16. Taxes recoverable

Taxes recoverable as at 31 December 2016 are represented by a VAT recoverable of RUB 3,920,940 thousand (31 December 2015: RUB 1,257,764 thousand).

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

17. Cash and cash equivalents

	31 December 2016	31 December 2015
Rouble short-term deposits	5,669,714	16,612,228
Rouble denominated cash in transit	5,272,838	2,258,241
Rouble denominated cash on hand and balances with banks	2,062,814	3,556,009
Foreign currency denominated cash on hand and balances with banks	32,401	29,467
Total cash and cash equivalents	13,037,767	22,455,945

Cash in transit represents cash receipts made during the last day of the reporting period (29-31 December), which were sent to banks but not deposited into the respective bank accounts until the next reporting period.

Significant rouble denominated cash in transit result from the business seasonality, indicating higher levels of retail sales in holiday periods such as the New Year's Eve as well as the closing day in relation to the official banking days in Russia. If the closing day is on non-banking days, the amount of cash in transit increases.

Short-term deposits are made for varying periods of between one day and three months, depending on the immediate cash requirements of the Group, and earn interest at the respective short-term deposit rates.

18. Issued capital and reserves

Issued capital

As at 31 December 2016 the Company's share capital is comprised of 97,318,746 authorised and issued ordinary shares (as at 31 December 2015: 97,318,746) with equal voting rights. The shares have no par value.

All outstanding ordinary shares are entitled to an equal share in any dividend declared by the Company. According to the BVI Business Companies Act No. 16 of 2004, no dividends can be declared and paid unless the Board of Directors determines that immediately after the payment of the dividend the Group will be able to satisfy its liabilities as they become due in the ordinary course of its business and the realisable value of the assets of the Group will not be less than the sum of its total liabilities, other than deferred taxes, as shown in the books of account, and its capital. In accordance with Russian legislation, Lenta LLC, the Company's primary operating subsidiary registered under the laws of the Russian Federation, may distribute profits as dividends or transfer them to reserves (fund accounts) limited to the retained earnings recorded in its financial statements prepared in accordance with Russian Accounting Rules. No dividends to holders of ordinary shares are declared for the year ended 31 December 2016 and for the year ended 31 December 2015.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

18. Issued capital and reserves (continued)

Issued capital (continued)

The movements in the number of shares for the year ended 31 December 2016 and for the year ended 31 December 2015 are as follows.

	31 December 2016 No.	31 December 2015 No.
Authorised share capital (ordinary shares with no par value)	unlimited	unlimited
Issued and fully paid (no par value)	97,318,746	97,318,746
	31 December 2016 No.	31 December 2015 No.
Balance of shares outstanding at beginning of financial year	97,318,746	86,053,394
Additional issue of shares	–	11,265,352
Balance of shares outstanding at the end of financial year	97,318,746	97,318,746

In year 2015 11,265,352 ordinary shares were issued by the Group for a cash consideration of RUB 21,788,593 thousand net of directly attributable issuance costs. The whole amount of the consideration received was recorded as increase in additional paid-in capital, as the shares have no par value.

Share options reserve

The share options reserve is used to recognise the value of equity-settled share-based payments provided to employees, including key management personnel, as part of their remuneration. Refer to Note 28 for further details of these plans.

Hedging reserve

The hedging reserve is used to recognise the effective portion of the gain or loss from the hedging instrument and later reclassified to profit or loss when the hedge item affects profit or loss.

19. Components of other comprehensive income (OCI)

	Year ended 31 December 2016	Year ended 31 December 2015
Cash flow hedges		
Reclassification during the year to profit or loss	(410,581)	(1,800,556)
Related tax effect	82,116	360,111
Gain/(loss) arising during the year	44,241	(525,963)
Related tax effect	(8,848)	105,193
Net loss during the year	(293,072)	(1,861,215)

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

20. Earnings per share

	Year ended 31 December 2016	Year ended 31 December 2015
Earnings per share (in thousands of Russian roubles per share)		
- basic and diluted, for profit for the period attributable to equity holders of the parent	0.115	0.112

The calculation of basic earnings per share for reporting periods is based on the profit attributable to shareholders (for the year ended 31 December 2016: RUB 11,202,028 thousand, for the year ended 31 December 2015: RUB 10,288,093 thousand) and a weighted average number of ordinary shares outstanding during the respective periods, calculated as shown below.

	Year ended 31 December 2016	Year ended 31 December 2015
Number of issued shares at the beginning of period	97,318,746	86,053,394
Number of shares issued in October 2015	–	4,225,352
Number of shares issued in March 2015	–	7,040,000
Number of shares at the end of reporting period	97,318,746	97,318,746
Weighted average number of shares	97,318,746	92,252,707

The Group has issued share-based payments' (Note 28) instruments that could potentially dilute basic earnings per share in the future. These instruments have no material effect on dilution of earnings per share for the periods presented.

21. Borrowings

Short-term borrowings:

	Currency	31 December 2016	31 December 2015
Fixed rate bonds (liability for interests)	RUB	713,803	760,097
Fixed rate long-term bank loans (liability for interests)	RUB	32,612	30,138
Floating rate long-term bank loans (liability for interests)	RUB	803,918	14,575
Floating rate short-term bank loans (liability for interests)	RUB	3,266	–
Fixed rate short-term bank loans (liability for interests)	RUB	82,853	–
Short-term portion of floating rate long-term bank loans	RUB	3,270,650	–
Short-term portion of fixed rate long-term bank loans	RUB	11,400,000	–
Fixed rate short-term bank loans	RUB	18,938,018	–
Fixed rate bonds	RUB	–	9,968,467
Total short-term borrowings and short-term portion of long-term borrowings		35,245,120	10,773,277

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

21. Borrowings (continued)

Long-term borrowings:

	<u>Currency</u>	<u>31 December 2016</u>	<u>31 December 2015</u>
Fixed rate bonds	RUB	16,958,600	9,973,156
Fixed rate long-term bank loans	RUB	16,931,549	9,951,940
Floating rate long-term bank loans	RUB	33,065,782	45,224,001
Total long-term borrowings		66,955,931	65,149,097

The Groups' borrowings as at 31 December 2016 and 31 December 2015 are denominated in Russian roubles.

On 27 January 2016 the Group received RUB 7,000,000 thousand under non-revolving credit line agreement with PJSC Rosbank with maturity period of 3 years. The loan bears financial covenants.

On 18 February 2016 coupons 7-11 on 03 series bonds issued in March 2013 were reset at 11.75% per annum, put option right on early redemption after 2.5 years (August 2018).

On 3 March 2016 the Group executed an offer of 03 series bonds with total nominal value of RUB 586,583 thousand, and completed book building for the offering on the same day at price amounting to 100.75% of nominal value.

On 24 February 2016 coupons 7-11 on 01 series bonds issued in March 2013 were reset at 11.75% per annum, put option right on early redemption after 2.5 years (September 2018).

On 10 March 2016 right on early redemption of 01 series bonds was not exercised by the holders.

On 24 February 2016 coupons 7-12 on 02 series bonds issued in March 2013 were reset at 11% per annum, put option right on early redemption after 3 years (March 2019). On 10 March 2016 the Group executed an offer of 02 series bonds with total nominal value of RUB 2,999,979 thousand.

The funds raised from the issue of the bonds are used on business expansion.

On 9 June 2016 the Group signed revolving credit line of RUB 5,000,000 thousand with PJSC Bank Saint-Petersburg.

On 21 June 2016 revolving credit line of RUB 5,000,000 thousand was agreed with JSC Rosselkhozbank. The credit line has financial covenants.

On 30 June 2016 termination of loan agreement with EBRD was signed upon the prepayment of the entire outstanding principal amount of RUB 4,554,240 thousand.

On 03 November 2016 the Group received RUB 10,000,000 thousand under non-revolving credit line agreement with PJSC Sberbank. The loan bears financial covenants.

On 9 November 2016 the Group signed revolving credit line of RUB 3,000,000 thousand with PJSC Rosbank. The credit line bears financial covenants. At the reporting date the Group draw down RUB 1,000,000 thousand.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

21. Borrowings (continued)

On 18 November 2016 the Group signed revolving credit line of RUB 15,000,000 thousand with PJSC Sberbank. At the reporting date the Group draws down RUB 6,400,000 thousand. The loan bears a financial covenant.

On 15 December 2016 the Group signed 5 year loan agreement of RUB 8,500,000 thousand with JSC UniCredit Bank. The loan bears financial covenants.

On 22 December 2016 the Group signed 4 year non-revolving credit line of RUB 4,000,000 thousand with JSC Raiffeisenbank. The loan bears financial covenants.

During the year ended 31 December 2016 the Group received RUB 28,600,000 thousand under credit agreements concluded before 1 January 2016 and repaid RUB 29,775,669 thousand.

As at 31 December 2016 the Group had RUB 44,150,000 thousand of unused credit facilities (as at 31 December 2015: RUB 45,300,000 thousand).

As at 31 December 2016 the Group is in compliance with all financial covenants of loan agreements.

22. Income taxes

The Group's income tax expense for the year ended 31 December 2016 and 31 December 2015 is as follows:

	Year ended 31 December 2016	Year ended 31 December 2015
Current tax expense	1,137,425	632,900
Deferred tax expense	2,213,795	1,944,919
Adjustments in respect of current income tax of previous year	–	6,191
Income tax expense recognised in profit for the year	3,351,220	2,584,010
	Year ended 31 December 2016	Year ended 31 December 2015
Tax effect related to effective portion of change in the fair value of cash flow hedging instruments	(73,268)	(465,304)
Income tax (benefit)/expense recognised in OCI	(73,268)	(465,304)
	Year ended 31 December 2016	Year ended 31 December 2015
Profit before tax	14,553,248	12,872,103
Theoretical tax charge at 20%	(2,910,649)	(2,574,421)
Difference in tax rates for foreign companies and specific tax regime in Russia	(101,269)	157,125
Add tax effect of non-deductible expenses	(339,302)	(160,523)
- share option expenses	(66,037)	(36,825)
- others	(273,265)	(123,698)
Adjustments in respect of current income tax of previous years	–	(6,191)
Income tax expense	3,351,220	2,584,010

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

22. Income taxes (continued)

Differences between IFRS and Russian statutory tax regulations give rise to temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and their tax bases. The tax effect of the movements in these temporary differences, recorded at the rate of 20% is detailed below.

	1 January 2016	Differences in recognition and reversals recognised in profit or loss	Differences in recognition and reversals recognised in other comprehen- sive income	Deferred tax on acquisition of subsidiaries (Note 7)	31 December 2016
Tax effect of (taxable)/ deductible temporary differences					
Property, plant and equipment	–	(68,668)	–	199,467	130,799
Consulting and other accruals	–	(8,529)	–	8,529	–
Other	–	(7,432)	–	141	(7,291)
Total deferred assets	–	(84,629)	–	208,137	123,508

	1 January 2016	Differences in recognition and reversals recognised in profit or loss	Differences in recognition and reversals recognised in other comprehen- sive income	Deferred tax on acquisition of subsidiaries (Note 7)	31 December 2016
Tax effect of (taxable)/ deductible temporary differences					
Property, plant and equipment	(5,116,612)	(2,360,501)	–	(142,047)	(7,619,160)
Leasehold rights	(428,445)	(2,382)	–	–	(430,827)
Unused vacation and employee bonuses accrual	257,209	4,462	–	–	261,671
Suppliers' bonuses	(70,733)	69,859	–	–	(874)
Borrowings	(194,331)	65,058	–	–	(129,273)
Intangible assets other than leasehold rights	(20,769)	(3,307)	–	–	(24,076)
Inventory	415,175	96,393	–	58,712	570,280
Bad debt allowance	48,059	30,029	–	1,861	79,949
Finance leasing	3,418	(3,418)	–	–	–
Consulting and other accruals	65,920	48,061	–	7,558	121,539
Customs duty payable	37,618	(37,618)	–	–	–
Cash flow hedging instruments	(227,606)	(3,898)	73,268	–	(158,236)
Other	1,293	(31,904)	–	(380)	(30,991)
Total deferred tax liabilities	(5,229,804)	(2,129,166)	73,268	(74,296)	(7,359,998)

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

21. Income taxes (continued)

	1 January 2015	Differences in recognition and reversals recognised in profit or loss	Differences in recognition and reversals recognised in other comprehen- sive income	31 December 2015
Tax effect of (taxable)/deductible temporary differences				
Property, plant and equipment	(3,241,091)	(1,875,521)	–	(5,116,612)
Leasehold rights	(450,356)	21,911	–	(428,445)
Unused vacation and employee bonuses accrual	144,820	112,389	–	257,209
Suppliers' bonuses	(157,358)	86,625	–	(70,733)
Borrowings	(79,040)	(115,291)	–	(194,331)
Intangible assets other than leasehold rights	(17,386)	(3,383)	–	(20,769)
Inventory	586,189	(171,014)	–	415,175
Bad debt allowance	13,236	34,823	–	48,059
Finance leasing	6,947	(3,529)	–	3,418
Consulting and other accruals	46,769	19,151	–	65,920
Customs duty payable	30,677	6,941	–	37,618
Cash flow hedging instruments	(634,903)	(58,007)	465,304	(227,606)
Other	1,307	(14)	–	1,293
Total deferred tax (liabilities)/assets	(3,750,189)	(1,944,919)	465,304	(5,229,804)

The temporary taxable differences associates with undistributed earnings of subsidiaries amount to RUB 59,399,304 thousand and RUB 54,229,761 thousand as of 31 December 2016 and 2015, respectively. A deferred tax liability on these temporary differences was not recognised, because management believed that it was in a position to control the timing of reversal of such differences and has no intention to reverse them in the foreseeable future.

23. Trade and other payables

	31 December 2016	31 December 2015
Trade payables	46,612,578	42,002,004
Accrued liabilities and other creditors	4,437,082	3,586,669
Payables for purchases of property, plant and equipment	5,121,938	3,231,534
Total trade and other payables	56,171,598	48,820,207

The trade and other payables are denominated in:

	31 December 2016	31 December 2015
Russian roubles	55,569,398	48,601,870
USD	418,393	122,582
EUR	165,950	94,991
GBP	17,857	764
Total trade and other payables	56,171,598	48,820,207

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

24. Other taxes payable

	31 December 2016	31 December 2015
Social taxes	559,625	490,231
Property tax	381,379	270,774
Personal income tax	157,637	134,089
Other taxes	12,665	31,990
Total other taxes payable	1,111,306	927,084

25. Cost of sales

Cost of sales for the years ended 31 December 2016 and 31 December 2015 consists of the following:

	Year ended 31 December 2016	Year ended 31 December 2015
Cost of goods sold	204,373,681	167,408,885
Cost of own production	24,810,938	21,710,294
Supply chain cost	3,795,679	3,185,448
Losses due to inventory shortages and write down to net realisable value	5,603,731	4,153,283
Total cost of sales	238,584,029	196,457,910

Cost of goods sold is reduced by rebates and promotional bonuses received from suppliers.

The cost of own production consists of the following:

	Year ended 31 December 2016	Year ended 31 December 2015
Raw materials	20,497,106	17,925,511
Labour costs	3,492,856	2,947,684
Utilities	700,859	752,180
Repairs and maintenance	120,117	84,919
Total cost of own production	24,810,938	21,710,294

Cost of sales for the year ended 31 December 2016 includes employee benefits expense of RUB 3,492,856 thousand (year ended 31 December 2015: RUB 4,092,406 thousand) of which contributions to state pension fund are comprised of RUB 499,517 thousand (year ended 31 December 2015: RUB 609,388 thousand).

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

26. Selling, general and administrative expenses

	Year ended 31 December 2016	Year ended 31 December 2015
Employee benefits	17,522,506	14,558,823
Depreciation and amortisation (Note 9, 11, 12)	7,694,569	5,671,219
Advertising	3,324,415	2,313,536
Premises lease	3,167,843	2,349,035
Utilities and communal payments	2,959,131	1,964,640
Professional fees	2,615,199	1,822,108
Cleaning	1,789,987	1,432,304
Repairs and maintenance	1,636,793	1,264,894
Security services	1,300,135	973,180
Taxes other than income tax	1,263,223	1,096,846
Land and equipment lease	267,793	323,045
Pre-opening costs	743,348	640,596
Other	2,157,568	1,634,545
Total selling, general and administrative expenses	46,442,510	36,044,771

Employee benefits for the year ended 31 December 2016 include contributions to state pension fund of RUB 2,234,917 thousand (year ended 31 December 2015: RUB 1,844,088 thousand).

Pre-opening costs for the year ended 31 December 2016 include employee benefits of RUB 414,530 thousand (year ended 31 December 2015: RUB 360,904 thousand) of which contributions to state pension fund are comprised RUB 46,496 thousand (year ended 31 December 2015: RUB 39,742 thousand).

Professional fees for the year ended 31 December 2016 include fees billed by Ernst & Young LLC: for the audit of the consolidated financial statements in the amount of RUB 25,186 thousand (for the year ended 31 December 2015: RUB 29,565 thousand) and for consulting and other non-audit services in the amount of RUB 20,725 thousand (for the year ended 31 December 2015: RUB 5,699 thousand).

27. Other operating income and expenses

Other operating income is comprised of the following:

	Year ended 31 December 2016	Year ended 31 December 2015
Rental income	973,959	752,755
Penalties due by suppliers	788,786	904,528
Sale of secondary materials	497,245	295,743
Advertising income	488,599	422,002
Amounts received from lawsuit settlement	188,089	–
Gain on property, plant and equipment disposal	17,165	62,250
Other	132,236	147,032
Total other operating income	3,086,079	2,584,310

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

27. Other operating income and expenses (continued)

Other operating expenses are comprises of the following:

	Year ended 31 December 2016	Year ended 31 December 2015
Loss from fixed assets and leasehold rights disposal	280,492	181,567
Change in bad debt allowance and impairment of advances and prepayments for construction (Note 10, 14)	178,504	194,665
Amounts paid in settlement of lawsuit	125,870	–
Penalties for breach of a contracts with suppliers	61,653	1,311
Penalties from government authorities	18,185	65,351
Other	51,671	69,639
Total other operating expenses	716,375	512,533

28. Share-based payments

Long-term incentive plan

During the year 2014 the Group approved a long-term incentive plan (LTIP) to certain members of management, according to which the Company granted award shares in 2014, 2015 and 2016 along with the communication of the terms of award to participants.

The monetary amount of the award to be granted to the participants of the plan was calculated based on the annual base salary on the grant date, target award interest, business results co-efficient and individual performance rating co-efficient.

Under terms of Tranche 2014 the shares are to be released in phases:

- ▶ 1st 25% on the first anniversary of the award (1 April 2015);
- ▶ 2nd 25% on the second anniversary of the award (1 April 2016);
- ▶ 50% on the third anniversary of the award (1 April 2017), provided that employment conditions are met.

With respect to the first phase no shares were issued in April 2015 and April 2016, the Group plans to release shares till the end of 2017.

The vesting date of 100% of Tranche 2015 is 1 April 2018. The vesting dates of awards granted during 2016 year are 31 December 2018 and 1 April 2019.

The fair value of the award shares was estimated based on the GDR price on Moscow Exchange on the award grant date.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

28. Share-based payments (continued)

Long-term incentive plan (continued)

Total expense recognised for the services received from the employees covered by long-term incentive plan for the year ended 31 December 2016 and the year ended 31 December 2015 is shown in the following table:

	Year ended 31 December 2016	Year ended 31 December 2015
Expense arising from the equity-settled long-term incentive plan payments	139,355	28,925

Share value appreciation rights

During the 2013 the Group granted share value appreciation rights (SVARs) to certain members of top management as part of management long-term incentive plan. Each SVAR entitles the holder to a quantity of ordinary shares in Lenta Ltd based on an increase in the share price over a predetermined exercise price subject to meeting the performance conditions.

Movements during the year

The following table illustrates the number and weighted average exercise prices (WAEP) of, and movements in, SVARs:

	2016 Number	2016 WAEP	2015 Number	2015 WAEP
Outstanding at 1 January	594,211	RUB 1,516	594,211	USD 49.84
Granted during the year	42,000	RUB 2,214	–	–
Forfeited during the year	–	–	–	–
Exercised during the year	–	–	–	–
Expired during the year	–	–	–	–
Outstanding at 31 December	636,211	RUB 1,562	594,211	RUB 1,516
Exercisable at 31 December	–	–	–	–

In March 2015 modifications to the SVARs were agreed including deferral of exercise date of SVARs that are to be vested in April 2015 by one year.

On 17 July 2015 the Remuneration Committee of Lenta Ltd agreed on certain changes in the management long-term incentive plan, which is based on share value appreciation rights. Whereas the plan has been set up using financial parameters denominated in USD, all financial parameters are now changed into Russian roubles using the exchange rate on the date of the grant (1 April 2013). As a result, the exercise price for the remaining outstanding options will be changed from USD 49.84 to RUB 1,516 per share. The vesting schedule has been revised and fixed, as a result of which the remaining 80% of the initial grant will now vest in 2 stages: 30% on 1 April 2017 and the remaining 50% on 1 April 2018.

During the year ended 31 December 2016 additional tranche of share value appreciation rights (SVARs) was granted to certain members of top management as part of management long-term incentive plan.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

28. Share-based payments (continued)

Movements during the year (continued)

The weighted average remaining contractual life for the SVARs outstanding as at 31 December 2016 was 1.76 years (31 December 2015: 2.3 years).

The weighted average exercise price for options outstanding as at 31 December 2016 is RUB 1,562 thousand (31 December 2015: RUB 1,516 thousand).

The weighted average fair value of options outstanding as at 31 December 2016 is RUB 0.89 thousand (year ended 31 December 2015: RUB 0.86 thousand).

The expense recognized for the services received from the employees covered by SVARs plan during the year is shown in the following table:

	Year ended 31 December 2016	Year ended 31 December 2015
Expense arising from the equity-settled SVARs transaction	190,828	155,199

The fair value of the management SVARs is estimated at the grant date using the Black Scholes option pricing model, taking into account the terms and conditions upon which the SVARs were granted.

29. Commitments

Capital expenditure commitments

At 31 December 2016 the Group has contractual capital expenditure commitments in respect of property, plant and equipment and intangible assets totalling RUB 21,055,701 thousand net of VAT (31 December 2015: RUB 19,370,442 thousand net of VAT).

Operating lease commitments

Where the Group is the lessee, the future minimum lease payments under non-cancellable operating leases are as follows:

	31 December 2016	31 December 2015
Not later than 1 year	4,353,739	3,786,074
Later than 1 year and not later than 5 years	17,616,198	14,664,366
Later than 5 years	32,311,175	33,247,702
Total operating lease commitments	54,281,112	51,698,142

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

30. Financial instruments

Categories of financial instruments

	<u>31 December 2016</u>	<u>31 December 2015</u>
Financial assets		
Cash	13,037,767	22,455,945
Trade and other receivables	17,035,789	13,646,894
Cash flow hedging instruments	372,210	794,464
Financial liabilities		
Cash flow hedging instruments	48,725	124,128
At amortised cost		
Floating rate long-term borrowings	33,869,700	45,238,576
Fixed rate long-term borrowings and bonds	34,636,564	20,395,179
Fixed rate short-term borrowings	30,420,871	10,288,619
Floating rate short-term borrowings	3,273,916	–
Trade and other payables	56,171,598	47,058,158
Obligations under finance leases	–	18,577
Total financial liabilities at amortised cost	<u><u>158,372,649</u></u>	<u><u>122,999,109</u></u>

Fair values

The following table provides the fair value measurement hierarchy of the Group's financial assets and liabilities. Quantitative disclosures of fair value measurement hierarchy for financial assets and financial liabilities as at 31 December 2016:

	<u>31 December 2016</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Financial assets measured at fair value				
Cash flow hedging instruments	372,210	–	372,210	–
Financial liabilities measured at fair value				
Cash flow hedging instruments	48,725	–	48,725	–
Financial liabilities for which fair values are disclosed				
Fixed rate bonds	18,260,825	18,260,825	–	–
Floating rate borrowings	37,143,616	–	37,143,616	–
Fixed rate borrowings	47,002,207	–	47,002,207	–

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

30. Financial instruments (continued)

Fair values (continued)

	<u>31 December 2015</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Financial assets measured at fair value				
Cash flow hedging instruments	794,464	–	794,464	–
Financial liabilities measured at fair value				
Cash flow hedging instruments	124,128	–	124,128	–
Financial liabilities for which fair values are disclosed				
Fixed rate bonds	20,632,997	20,632,997	–	–
Floating rate borrowings	45,238,576	–	45,238,576	–
Fixed rate borrowings	9,479,907	–	9,479,907	–
Obligations under finance leases	18,577	–	18,577	–

During the year ending 31 December 2016 and 31 December 2015, there are no transfers between Level 1, Level 2 and Level 3 of fair value measurements.

Set out below, is a comparison by class of the carrying amounts and fair value of the Group's financial instruments, other than those with carrying amounts are reasonable approximations of fair values:

	<u>31 December 2016</u>		<u>31 December 2015</u>	
	<u>Carrying amount</u>	<u>Fair value</u>	<u>Carrying amount</u>	<u>Fair value</u>
Financial assets				
Cash flow hedging instruments	372,210	372,210	794,464	794,464
Financial liabilities				
Interest-bearing loans and borrowings				
Obligations under finance leases	–	–	18,577	18,577
Floating rate borrowings	37,143,616	37,143,616	45,238,576	45,238,576
Fixed rate borrowings and bonds	65,057,435	65,263,032	30,683,798	30,112,904
Derivative liabilities				
Cash flow hedging instruments	48,725	48,725	124,128	124,128
Total financial liabilities	<u>102,249,776</u>	<u>102,455,373</u>	<u>76,065,079</u>	<u>75,494,185</u>

The management assessed that the carrying amounts of cash and short-term deposits, trade receivables, trade payables and other current liabilities approximate their fair values largely due to the short-term maturities of these instruments.

The fair value of the financial assets and liabilities is included at the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

30. Financial instruments (continued)

Fair values (continued)

The following methods and assumptions are used to estimate the fair values:

- ▶ Fair values of the Group's interest-bearing borrowings and loans are determined by using DCF method using discount rate that reflects the issuer's borrowing rate as at the end of the reporting period. The own non-performance risk as at 31 December 2016 and 31 December 2015 is assessed to be insignificant.
- ▶ The fair value of bonds is based on the price quotations at the reporting date at Moscow exchange where transactions with bonds take place with sufficient frequency and volume.
- ▶ The Group enters into derivative financial instruments with financial institution with investment grade credit ratings. Derivatives valued using valuation techniques with market observable inputs are interest rate swaps and caps. The most frequently applied valuation techniques include swap models, using present value calculations, and option pricing model for caps. The models incorporate various inputs including the credit quality of counterparties and interest rate curves. As at 31 December 2016 and 31 December 2015, the marked-to-market value of derivative positions is net of a credit valuation adjustment attributable to derivative counterparty default risk. The changes in counterparty credit risk had no material effect on the hedge effectiveness assessment for derivatives designated in hedge relationships and other financial instruments recognised at fair value.

31. Hedge and hedging instruments

The Group entered into interest rate swaps and caps provided by VTB Bank PJSC to mitigate the risk of a rising MosPrime interest rate. Caps provide security for 4 quarters during the full periods of the agreement, so the termination date would be the earlier of the expiry date or the fourth settlement date for the floating amounts paid by VTB Bank PJSC to the Group.

As at period end the Group had the following interest rate financial instruments:

Type of instrument	Notional amount 2016	Notional amount 2015	Fixed interest rate	Fixed commission	Effective date	Expiry date
Interest rate swap	12,500,000	12,500,000	7.64%	n/a	31 March 2015	12 April 2018
Interest rate swap	900,000	900,000	7.54%	n/a	31 December 2013	12 November 2018
Interest rate swap	–	1,000,000	15.35%	n/a	31 December 2014	31 December 2016
Interest rate cap	10,000,000	10,000,000	12.00%	0.54%	31 December 2014	12 April 2018
Interest rate cap	900,000	900,000	12.00%	0.45%	31 December 2013	12 November 2018

Derivative financial instruments are classified in the statement of financial position as follows:

	31 December 2016	31 December 2015
Non-current asset	62,618	355,414
Current assets	309,592	439,050
Non-current liability	(2,137)	(24,564)
Current liability	(46,588)	(99,564)
Net derivative asset	323,485	670,336

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

31. Hedge and hedging instruments (continued)

The Group performs fair value assessment of the fair values of swaps and caps at the reporting date:

	31 December 2016	31 December 2015
Swaps	372,210	755,481
Caps	(48,725)	(85,145)
Net derivative asset	323,485	670,336

Starting 1 July 2013 the Group applied cash flow hedge accounting of swaps and caps that meet prescribed criteria, including preparation of all necessary documentation. Hedge accounting was applied prospectively from designation.

Retrospective and prospective effectiveness of cash flow hedges (swaps and caps) was measured by the Group using the "dollar offset" method. The effective portion of the gain on or loss from the hedging instrument was recognised in other comprehensive income in hedging reserve.

The effect from changes in fair value of financial instruments is recognised as follows:

	Year ended 31 December 2016	Year ended 31 December 2015
Profit or loss		
Ineffective portion of the change in the fair value of cash flow hedging instruments	–	6,308
Reclassification from hedge reserve into interest expense	410,581	1,800,556
	410,581	1,806,864
Other comprehensive income		
Effective portion of the change in the fair value of cash flow hedging instruments	44,241	(525,963)
Reclassification from hedge reserve into interest expense	(410,581)	(1,800,556)
	(366,340)	(2,326,519)

32. Financial risk management

The Group's principal financial liabilities, other than derivatives, comprise of loans and borrowings, trade and other payables. The main purpose of these financial liabilities is to finance the Group's operations and to provide guarantees to support its operations. The Group's principal financial assets include loans, trade and other receivables, and cash and short-term deposits that derive directly from its operations. The Group also enters into derivative transactions.

The Group is exposed to market risk, credit risk and liquidity risk. The Group's senior management oversees the management of these risks. The Group's financial risk activities are governed by appropriate policies and procedures and financial risks are identified, measured and managed in accordance with the Group's policies and risk objectives. All derivative activities for risk management purposes are carried out by specialists that have the appropriate skills, experience and supervision. It is the Group's policy that no trading in derivatives for speculative purposes may be undertaken.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

32. Financial risk management (continued)

The Board of Directors reviews and agrees policies for managing each of these risks, which are summarised below.

Market risk

Market risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises the following types of risk: interest rate risk, currency risk, and other price risk, such as equity price risk. Financial instruments affected by market risk include loans and borrowings, cash equivalents and derivative financial instruments.

Foreign currency risk

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

During the year ended 31 December 2016 and year ended 31 December 2015, the Group does not attract any amounts of foreign currency denominated borrowings, and as a consequence is not materially exposed to foreign currency risk. The only balances that are exposed to foreign currency risk are accounts payables to several foreign suppliers.

At 31 December 2016 and at 31 December 2015 there are no significant amounts in foreign currencies.

Whenever possible, the Group tries to mitigate the exposure to foreign currency risk by matching the statement of financial position, and revenue and expense items in the relevant currency.

Foreign currency sensitivity

The following table demonstrates the sensitivity to a reasonably possible change in the US dollar exchange rate, with all other variables held constant.

	<u>Change in USD rate</u>	<u>Effect on profit before tax</u>
Year ended 2016	20.00%	(83,682)
	-20.00%	83,682
Year ended 2015	40.00%	(49,033)
	-13.00%	15,936

The following table demonstrates the sensitivity to a reasonably possible change in the EUR exchange rate, with all other variables held constant.

	<u>Change in EUR rate</u>	<u>Effect on profit before tax</u>
Year ended 2016	20.00%	(33,195)
	-20.00%	33,195
Year ended 2015	43.00%	(40,846)
	-15.00%	14,249

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

32. Financial risk management (continued)

Foreign currency sensitivity (continued)

Foreign currency exchange rate reasonable possible change range was prepared for the purpose of market risk disclosures in accordance with IFRS 7 and is derived from statistical data, in particular time series analysis.

Interest rate risk

Interest rate risk is the risk that the fair value of future cash flows of the financial instrument will fluctuate because of changes in market interest rates.

The Group's exposure to the risk of changes in market interest rates relates primarily to the Group's long-term debt obligations with floating interest rates. As at 31 December 2016 these obligations are represented with long-term borrowing (Note 21), which bears interest of MosPrime 1-3m plus margin. In order to hedge the risk of rising MosPrime interest rate, the Group entered into interest rate swaps and caps (Note 31).

Interest rate sensitivity

The following tables demonstrate the sensitivity to a reasonably possible change in MosPrime rates, on that portion of loans and borrowings affected, after the impact of hedge accounting. With all other variables held constant, the Group's profit before tax and OCI are affected through the impact on floating rate borrowings, as follows:

	Profit or loss		OCI	
	200 bp increase	400 bp decrease	200 bp increase	400 bp decrease
2016				
Variable rate instruments	(775,287)	1,550,574	–	–
Interest rate swaps and caps	337,619	(576,600)	313,312	(647,145)
Cash flow sensitivity (net)	(437,668)	973,974	313,312	(647,145)
	Profit or loss		OCI	
	600 bp increase	500 bp decrease	600 bp increase	500 bp decrease
2015				
Variable rate instruments	(2,647,200)	2,647,200	–	–
Interest rate swaps and caps	1,519,500	(855,009)	1,761,327	(1,358,130)
Cash flow sensitivity (net)	(1,127,700)	1,792,191	1,761,327	(1,358,130)

The range of reasonable possible changes in MosPrime rate was prepared for the purpose of market risk disclosures in accordance with IFRS 7 and is based on risk metrics that are derived from statistical data, in particular time series analysis.

The Group is exposed to cash flow interest rate risk as it borrows funds at floating interest rates. During the year ended 31 December 2016 all of the Group's borrowings are denominated in Russian roubles. The Group evaluates its interest rate exposure and hedging activities on a regular basis and acts accordingly in order to align with the defined risk limits set by the executive board. To ensure optimal hedging strategies various scenarios are simulated taking into consideration refinancing, renewal of existing positions, alternative financing and financial hedging instruments.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

32. Financial risk management (continued)

Interest rate sensitivity (continued)

The Group manages its cash flow interest rate risk by the use of floating to fixed interest rate swaps and caps. Such financial instruments have the economic benefit of converting borrowings issued at variable rates to fixed interest rates. The Group's hedging instruments as at the reporting date are detailed in Note 30 of these financial statements. The sensitivity analyses below have been determined based on the net exposure of interest bearing borrowings. The net exposure of the Group to interest rate fluctuations as at 31 December 2016 is as follows:

	31 December 2016
Total floating rate borrowings (gross of direct issue costs)	36,928,571
Less notional amount of interest rate financial instruments (Note 32)	<u>(24,300,000)</u>
Net exposure to interest rate fluctuations	<u>12,628,571</u>
% of floating rate borrowings exposed to interest rate fluctuations	34%

Credit risk

Credit risk is the risk that counterparty may default or not meet its obligations to the Group on a timely basis, leading to financial loss to the Group. Financial assets, which are potentially subject to credit risk, consist principally of cash in bank accounts and cash in transit, loans and receivables.

In determining the recoverability of receivables the Group performs a risk analysis considering the credit quality of the counterparty, the ageing of the outstanding amount and any past default experience.

Trade receivables

The Group has no significant concentrations of credit risk. Concentration of credit risk with respect to receivables is limited due to the Company's customer and vendor base being large and unrelated. Credit is only extended to counterparties subject to strict approval procedures. The Group trades only with recognised, creditworthy third parties who are registered in the Russian Federation. It is the Group's policy that all customers who are granted credit terms have a history of purchases from the Group. The Group also requires these customers to provide certain documents such as incorporation documents and financial statements. In addition, receivable balances are monitored on an ongoing basis with the result that the Group's exposure to bad debts is not significant. Sales to retail customers are made in cash, debit cards or via major credit cards.

Cash and cash equivalents

Credit risk from investing activities is managed by the Group's treasury department in accordance with the Group's policy. Investments of surplus funds are made only with approved counterparties. Cash is placed in financial institutions, which are considered at time of deposit to have minimal risk of default.

The maximum exposure to credit risk at the reporting date of trade receivables is the carrying value as presented in the statement of financial position. The maximum exposure to credit risk at the reporting date of cash and cash equivalents is RUB 12,853,791 thousand (31 December 2015: RUB 22,317,167 thousand).

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

32. Financial risk management (continued)

Liquidity risk

The Group monitors its risk to a shortage of funds using a recurring liquidity planning tool. This tool considers the maturity of its financial assets and liabilities and projected cash flows from operations. The Group objective is to maintain a continuity of funding and flexibility through the use of bank overdrafts and bank loans. Each year the Group analyses its funding needs and anticipated cash flows, so that it can determine its funding needs.

The table below summarises the maturity profile of the Group's financial liabilities at 31 December 2016, 31 December 2015 bases on contractual undiscounted cash flows of the financial liabilities based on the earliest date on which the Group is required to pay. The table includes both interest and principal cash flows. When the amount payable is not fixed for the entire term of the instrument, such as variable rate interest payments, the amount disclosed in the table is determined by reference to the conditions (e.g. MosPrime index) existing at the reporting date:

31 December 2016

	Less than 12 months	1-5 years	Over 5 years	Total
Borrowings	43,797,302	68,974,211	14,415,411	127,186,924
Trade and other payables	56,171,598	–	–	56,171,598
Amounts payable under swaps and caps	58,106	16,238	–	74,344
Total	100,027,006	68,990,449	14,415,411	183,432,866

31 December 2015

	Less than 12 months	1-5 years	Over 5 years	Total
Borrowings	19,945,156	72,189,546	15,328,782	107,463,484
Trade and other payables	47,058,158	–	–	47,058,158
Amounts payable under swaps and caps	100,216	74,344	–	174,560
Finance leasing	19,850	–	–	19,850
Total	67,123,380	72,263,890	15,328,782	154,716,052

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 reviews its capital needs periodically to determine actions to balance its overall capital structure through shareholders' capital contributions or new share issues, return of capital to shareholders as well as the issue of new debt or the redemption of existing debt. The Group is guided in its decisions by an established financing policy, which stipulates leverage ratios, interest coverage, covenants compliance, appropriateness of balance between long-term and short-term debt, requirements to diversification of funding sources. Dividends are to be declared based on the capital requirements of the business and with reference to continuing compliance with the financial policy.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

32. Financial risk management (continued)

Capital management (continued)

The capital structure of the Group consists of debt, which includes the borrowings disclosed in Note 21, obligations under finance leases less cash and cash equivalents and equity attributable to equity holders of the parent, comprising issued capital, reserves and retained earnings as disclosed in Note 18.

Net debt of the Group is comprises of the following:

	31 December 2016	31 December 2015
Borrowings	102,201,051	75,922,374
Obligations under finance leases	–	18,577
Cash and cash equivalents (Note 17)	(13,037,767)	(22,455,945)
Net debt	89,163,284	53,485,006

Net debt is a non-IFRS indicator and, therefore, its calculation may differ between companies, however it is one of the key indicators that are commonly used by investors and other users of financial statements in order to evaluate financial condition of the Group.

33. Contingencies

Operating environment of the Group

The Group sells products that are sensitive to changes in general economic conditions that impact consumer spending. Future economic conditions and other factors, including sanctions imposed, consumer confidence, employment levels, interest rates, consumer debt levels and availability of consumer credit could reduce consumer spending or change consumer purchasing habits. A general slowdown in the Russian economy or in the global economy, or an uncertain economic outlook, could adversely affect consumer spending habits and the Group's operating results.

Russia continues economic reforms and development of its legal, tax and regulatory frameworks as required by a market economy. The future stability of the Russian economy is largely dependent upon these reforms and developments and the effectiveness of economic, financial and monetary measures undertaken by the government.

The Russian economy has been negatively impacted by a decline in oil prices and sanctions imposed on Russia by a number of countries. The rouble interest rates remained high. The combination of the above resulted in reduced access to capital, a higher cost of capital and uncertainty regarding economic growth, which could negatively affect the Group's future financial position, results of operations and business prospects. Management believes it is taking appropriate measures to support the sustainability of the Group's business in the current circumstances.

Lenta Limited and subsidiaries

Notes to the consolidated financial statements for the year ended 31 December 2016 (in thousands of Russian roubles)

33. Contingencies (continued)

Legal contingencies

Group companies are involved in a number of lawsuits and disputes that arise in the normal course of business. Management assesses the maximum exposure relating to such lawsuits and disputes to be RUB 511,656 thousand as at 31 December 2016 (31 December 2015: RUB 6,449 thousand). Management believes there is no exceptional event or litigation likely to affect materially the business, financial performance, net assets or financial position of the Group, which have not been disclosed in these consolidated financial statements.

Russian Federation tax and regulatory environment

The government of the Russian Federation continues to reform the business and commercial infrastructure in its transition to a market economy. As a result the laws and regulations affecting businesses continue to change rapidly. These changes are characterised by poor drafting, different interpretations and arbitrary application by the authorities. In particular taxes are subject to review and investigation by a number of authorities who are enabled by law to impose fines and penalties. While the Group believes it has provided adequately for all tax liabilities based on its understanding of the tax legislation, the above facts may create tax risks for the Group. Management also assesses the maximum exposure from possible tax risks to be RUB 288,582 thousand (31 December 2015: RUB 126,793 thousand). No tax provisions are recorded as at 31 December 2016 and 31 December 2015. Management continues to monitor closely any developments related to these risks and regularly reassesses the risk and related liabilities, provisions and disclosures.

Land leases

Certain lease agreements for land plots containing a short lease term expired prior to the date of these financial statements. The Group initiated the process of renewal of the lease agreements for 49 years and believes that the risks relating to the operations of the respective stores are insignificant. No provisions in this respect are accrued as at 31 December 2016 and 31 December 2015.

Environmental matters

The enforcement of environmental regulation in the Russian Federation is evolving and the enforcement posture of government authorities is continually being reconsidered. The Group periodically evaluates its obligations under environmental regulations. As obligations are determined, they are recognised immediately. Potential liabilities, which might arise as a result of changes in existing regulations, civil litigation or legislation, cannot be estimated but could be material. In the current enforcement climate under existing legislation, management believes that there are no significant liabilities for environmental damage.

34. Events occurring after the reporting period

There were no significant events after the reporting date other than disclosed elsewhere in the consolidated financial statements.