OAO TMK

Unaudited Interim Condensed Consolidated Financial Statements

Three-month period ended March 31, 2015

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Three-month period ended March 31, 2015

Contents

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улучшаем мир

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Report on review of interim condensed consolidated financial statements

To the Shareholders and Board of Directors OAO TMK

Introduction

We have reviewed the accompanying interim consolidated statement of financial position of OAO TMK and its subsidiaries ("Group") as of March 31, 2015 and the related interim consolidated statements of income, comprehensive income, changes in equity and cash flows for the three-month period then ended and condensed explanatory notes. Management is responsible for the preparation and presentation of these interim condensed consolidated financial statements in accordance with IAS 34, *Interim Financial Reporting* ("IAS 34"). Our responsibility is to express a conclusion on these interim condensed consolidated financial statements based on our review.

Scope of review

We conducted our review in accordance with International Standard on Review Engagements 2410, *Review of Interim Financial Information Performed by the Independent Auditor of the Entity*. A review of interim financial statements consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying interim condensed consolidated financial statements are not prepared, in all material respects, in accordance with IAS 34.

Ernst & Young LLC

May 21, 2015

Moscow, Russia

OAO TMK

Unaudited Interim Consolidated Income Statement

Three-month period ended March 31, 2015

(All amounts in thousands of US dollars, unless specified otherwise)

	NOTES	Three-month period ended March 31, 2015	Three-month period ended March 31, 2014
Revenue	1	1,134,055	1,466,083
Sales of goods		*1,115,711*	*1,442,348*
Rendering of services		*18,344*	*23,735*
Cost of sales	2	(881,781)	(1,184,756)
Gross profit		**252,274**	**281,327**
Selling and distribution expenses	3	(67,758)	(89,951)
Advertising and promotion expenses		(1,786)	(4,451)
General and administrative expenses	4	(53,066)	(76,722)
Research and development expenses	5	(4,052)	(3,757)
Other operating income	6	1,345	2,606
Other operating expenses	6	(4,947)	(7,387)
Foreign exchange loss, net		(23,604)	(62,854)
Finance costs		(66,449)	(55,334)
Finance income		3,856	884
Gain on changes in fair value of derivative financial instruments		–	1,640
Share of profit/(loss) of associates	9	34	(227)
Profit/(loss) before tax		**35,847**	**(14,226)**
Income tax expense	7	(6,072)	(1,494)
Profit/(loss) for the period		**29,775**	**(15,720)**
Attributable to:			
Equity holders of the parent entity		30,104	(15,643)
Non-controlling interests		(329)	(77)
		29,775	**(15,720)**
Earnings/(loss) per share attributable to the equity holders of the parent entity, basic and diluted (in US dollars)		**0.03**	**(0.02)**

The accompanying notes are an integral part of these unaudited interim condensed consolidated financial statements.

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Unaudited Interim Consolidated Statement of Comprehensive Income

Three-month period ended March 31, 2015

(All amounts in thousands of US dollars)

	NOTES	Three-month period ended March 31, 2015	2014
Profit/(loss) for the period		**29,775**	**(15,720)**
Items that may be reclassified subsequently to profit or loss:			
Exchange differences on translation to presentation currency[a]		(34,692)	(60,275)
Foreign currency loss on hedged net investment in foreign operations[b]	20 (ii)	(34,787)	(92,856)
Income tax[b]	20 (ii)	6,957	18,571
		(27,830)	**(74,285)**
Movement on cash flow hedges[a]	20 (iii)	(342)	427
Income tax[a]	20 (iii)	71	(101)
		(271)	**326**
Other comprehensive loss for the period, net of tax		**(62,793)**	**(134,234)**
Total comprehensive loss for the period, net of tax		**(33,018)**	**(149,954)**
Attributable to:			
Equity holders of the parent entity		(30,513)	(144,195)
Non-controlling interests		(2,505)	(5,759)
		(33,018)	**(149,954)**

(a) Other comprehensive loss for the period, net of income tax, was attributable to equity holders of the parent entity and to non-controlling interests as presented in the table below:

	Three-month period ended March 31, 2015	2014
Exchange differences on translation to presentation currency attributable to:		
Equity holders of the parent entity	(32,516)	(54,593)
Non-controlling interests	(2,176)	(5,682)
	(34,692)	**(60,275)**
Movement on cash flow hedges attributable to:		
Equity holders of the parent entity	(271)	326
	(271)	**326**

(b) The amount of foreign currency loss on hedged net investment in foreign operations, net of income tax, was attributable to equity holders of the parent entity.

The accompanying notes are an integral part of these unaudited interim condensed consolidated financial statements.

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Unaudited Interim Consolidated Statement of Financial Position

At March 31, 2015

(All amounts in thousands of US dollars)

	NOTES	March 31, 2015		December 31, 2014	
ASSETS					
Current assets					
Cash and cash equivalents	10	87,033		252,898	
Trade and other receivables		773,156		728,340	
Inventories	11	1,007,152		1,046,907	
Prepayments and input VAT		90,152		105,143	
Prepaid income taxes		13,166		7,939	
Other financial assets		167	**1,970,826**	596	**2,141,823**
Non-current assets					
Investments in associates	9	1,236		1,247	
Property, plant and equipment	12	2,513,028		2,610,170	
Goodwill	13	432,113		403,861	
Intangible assets	13	310,713		273,242	
Deferred tax asset		155,750		144,843	
Other non-current assets		23,447	**3,436,287**	74,202	**3,507,565**
TOTAL ASSETS			**5,407,113**		**5,649,388**
LIABILITIES AND EQUITY					
Current liabilities					
Trade and other payables	14	723,605		722,696	
Advances from customers		35,714		63,162	
Accounts payable to related parties	18	433		43,484	
Provisions and accruals	15	24,048		41,397	
Interest-bearing loans and borrowings	16	478,190		758,805	
Finance lease liability		5,256		5,545	
Dividends payable		138		1,889	
Income tax payable		8,130	**1,275,514**	6,483	**1,643,461**
Non-current liabilities					
Interest-bearing loans and borrowings	16	2,558,471		2,410,900	
Finance lease liability		45,125		47,641	
Deferred tax liability		211,969		205,667	
Provisions and accruals	15	27,413		22,916	
Employee benefits liability		20,549		21,044	
Other liabilities		28,980	**2,892,507**	26,899	**2,735,067**
Total liabilities			**4,168,021**		**4,378,528**
Equity	20				
Parent shareholders' equity					
Issued capital		336,448		336,448	
Treasury shares		(319,149)		(319,149)	
Additional paid-in capital		485,993		485,756	
Reserve capital		16,390		16,390	
Retained earnings		1,525,569		1,495,465	
Foreign currency translation reserve		(880,600)		(820,254)	
Other reserves		9,697	1,174,348	9,968	1,204,624
Non-controlling interests			64,744		66,236
Total equity			**1,239,092**		**1,270,860**
TOTAL LIABILITIES AND EQUITY			**5,407,113**		**5,649,388**

The accompanying notes are an integral part of these unaudited interim condensed consolidated financial statements.

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Unaudited Interim Consolidated Statement of Changes in Equity

Three-month period ended March 31, 2015

(All amounts in thousands of US dollars)

	Attributable to equity holders of the parent									
	Issued capital	**Treasury shares**	**Additional paid-in capital**	**Reserve capital**	**Retained earnings**	**Foreign currency translation reserve**	**Other reserves**	**Total**	**Non-controlling interests**	**TOTAL**
At January 1, 2015	**336,448**	**(319,149)**	**485,756**	**16,390**	**1,495,465**	**(820,254)**	**9,968**	**1,204,624**	**66,236**	**1,270,860**
Profit/(loss) for the period	–	–	–	–	30,104	–	–	**30,104**	(329)	**29,775**
Other comprehensive loss for the period, net of tax	–	–	–	–	–	(60,346)	(271)	**(60,617)**	(2,176)	**(62,793)**
Total comprehensive income/(loss) for the period, net of tax	**–**	**–**	**–**	**–**	**30,104**	**(60,346)**	**(271)**	**(30,513)**	**(2,505)**	**(33,018)**
Contributions from non-controlling interest owners (Note 18)	–	–	–	–	–	–	–	**–**	1,250	**1,250**
Recognition of the change in non-controlling interests in the subsidiary as an equity transaction (Note 20 iv)	–	–	237	–	–	–	–	**237**	(237)	**–**
At March 31, 2015	**336,448**	**(319,149)**	**485,993**	**16,390**	**1,525,569**	**(880,600)**	**9,697**	**1,174,348**	**64,744**	**1,239,092**

The accompanying notes are an integral part of these unaudited interim condensed consolidated financial statements.

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Unaudited Interim Consolidated Statement of Changes in Equity

Three-month period ended March 31, 2015 (continued)

(All amounts in thousands of US dollars)

	Attributable to equity holders of the parent									
	Issued capital	**Treasury shares**	**Additional paid-in capital**	**Reserve capital**	**Retained earnings**	**Foreign currency translation reserve**	**Other reserves**	**Total**	**Non-controlling interests**	**TOTAL**
At January 1, 2014	**326,417**	**(319,149)**	**391,192**	**16,390**	**1,737,098**	**(120,467)**	**2,311**	**2,033,792**	**95,827**	**2,129,619**
Loss for the period	–	–	–	–	(15,643)	–	–	**(15,643)**	(77)	**(15,720)**
Other comprehensive income/(loss) for the period, net of tax	–	–	–	–	–	(128,878)	326	**(128,552)**	(5,682)	**(134,234)**
Total comprehensive income/(loss) for the period, net of tax	**–**	**–**	**–**	**–**	**(15,643)**	**(128,878)**	**326**	**(144,195)**	**(5,759)**	**(149,954)**
Recognition of the change in non-controlling interests in the subsidiary as an equity transaction	–	–	–	–	(483)	–	–	**(483)**	483	**–**
At March 31, 2014	**326,417**	**(319,149)**	**391,192**	**16,390**	**1,720,972**	**(249,345)**	**2,637**	**1,889,114**	**90,551**	**1,979,665**

The accompanying notes are an integral part of these unaudited interim condensed consolidated financial statements.

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Unaudited Interim Consolidated Cash Flow Statement

Three-month period ended March 31, 2015

(All amounts in thousands of US dollars)

	NOTES	Three-month period ended March 31, 2015	2014
Operating activities			
Profit/(loss) before tax		35,847	(14,226)
Adjustments to reconcile profit/(loss) before tax to operating cash flows:			
Depreciation of property, plant and equipment		50,196	64,447
Amortisation of intangible assets	13	8,198	9,348
(Gain)/loss on disposal of property, plant and equipment	6	557	(122)
Foreign exchange loss, net		23,604	62,854
Finance costs		66,449	55,334
Finance income		(3,856)	(884)
Gain on changes in fair value of derivative financial instruments		–	(1,640)
Share of (profit)/loss of associates	9	(34)	227
Allowance for net realisable value of inventory		(107)	1,825
Allowance for doubtful debts		826	(501)
Movement in provisions		(13,083)	(9,535)
Operating cash flows before working capital changes		**168,597**	**167,127**
Working capital changes:			
(Increase)/decrease in inventories		5,956	(21,588)
(Increase)/decrease in trade and other receivables		(6,349)	27,268
Decrease in prepayments		11,979	6,015
Decrease in trade and other payables		(46,262)	(27,642)
Decrease in advances from customers		(23,856)	(14,408)
Cash generated from operations		**110,065**	**136,772**
Income taxes paid		(14,358)	(5,645)
Net cash flows from operating activities		**95,707**	**131,127**
Investing activities			
Purchase of property, plant and equipment and intangible assets		(38,887)	(67,885)
Proceeds from sale of property, plant and equipment		270	1,833
Acquisition of subsidiaries, net of cash acquired	8	670	–
Issuance of loans		(40)	(18)
Proceeds from repayment of loans issued		300	599
Interest received		1,880	639
Net cash flows used in investing activities		**(35,807)**	**(64,832)**
Financing activities			
Proceeds from borrowings		290,505	470,868
Repayment of borrowings		(427,199)	(479,032)
Interest paid		(67,501)	(61,527)
Payment of finance lease liabilities		(1,728)	(1,569)
Contributions from non-controlling interest owners	18	1,250	–
Dividends paid to equity holders of the parent		(5,576)	(24,661)
Net cash flows used in financing activities		**(210,249)**	**(95,921)**
Net decrease in cash and cash equivalents		**(150,349)**	**(29,626)**
Net foreign exchange difference		(15,516)	4,282
Cash and cash equivalents at January 1		252,898	93,298
Cash and cash equivalents at March 31		**87,033**	**67,954**

The accompanying notes are an integral part of these unaudited interim condensed consolidated financial statements.

Corporate Information

These interim condensed consolidated financial statements of OAO TMK and its subsidiaries (the "Group") for the three-month period ended March 31, 2015 were authorised for issue in accordance with a resolution of the General Director on May 21, 2015.

OAO TMK (the "Company"), the parent company of the Group, is an open joint stock company ("OAO"). Both registered and principal office of the Company is 40/2a Pokrovka Street, Moscow, the Russian Federation.

As at March 31, 2015, the Company's controlling shareholder was TMK Steel Limited. TMK Steel Limited is ultimately controlled by D.A. Pumpyanskiy.

The Group is one of the world's leading producers of steel pipes for the oil and gas industry, a global company with extensive network of production facilities, sales companies and representative offices.

The principal activities of the Group are the production and distribution of seamless and welded pipes, including pipes with the entire range of premium connections backed by extensive technical support. Research centres established in Russia and in the United States are involved in new product design and development, experimental and validation testing and advanced metallurgical research.

Basis of Preparation

Basis of Preparation

These interim condensed consolidated financial statements have been prepared in accordance with International Accounting Standard ("IAS") 34 *Interim Financial Reporting*. Accordingly, these interim condensed consolidated financial statements do not include all the information and disclosures required in the annual financial statements and should be read in conjunction with the Group's annual consolidated financial statements for the year ended December 31, 2014. Operating results for the three-month period ended March 31, 2015 are not necessarily indicative of the results that may be expected for the year ending December 31, 2015.

Changes in Accounting Policies

In the preparation of these interim condensed consolidated financial statements, the Group followed the same accounting policies and methods of computation as compared with those applied in the annual consolidated financial statements for the year ended December 31, 2014.

The nature and the impact of the adoption of new and revised standards, which became effective on January 1, 2015, on the Group's accounting policy is described below.

Basis of Preparation (continued)

Changes in Accounting Policies (continued)

IAS 19 Employee Benefits (amendments) – Defined Benefit Plans: Employee Contributions

This amendment clarifies the requirements that relate to how contributions from employees or third parties that are linked to service should be attributed to periods of service. The adoption of these amendments did not have any impact on the financial position or performance of the Group.

Improvements to IFRSs 2010-2012 cycle, 2011-2013 cycle

In December 2013, the IASB issued "Annual Improvements to IFRSs". The documents set out amendments to International Financial Reporting Standards primarily with a view of removing inconsistencies and clarifying wording. Amendments are generally intended to clarify requirements rather than result in substantive changes to current practice. The adoption of these improvements did not have any impact on the financial position or performance of the Group.

The Group has not early adopted any other standard, interpretation or amendment that has been issued but is not yet effective.

Index to the Notes

(All amounts are in thousands of US dollars, unless specified otherwise)

1) Segment Information

Operating segments reflect the Group's management structure and the way financial information is regularly reviewed. For management purposes, the Group is organised into business divisions based on geographical location, and has three reportable segments:

- Russia segment represents the results of operations and financial position of plants located in Russian Federation and the Sultanate of Oman, a finishing facility in Kazakhstan, Oilfield service companies and traders located in Russia, Kazakhstan, the United Arab Emirates and Switzerland;
- Americas segment represents the results of operations and financial position of plants and traders located in the United States of America and Canada;
- Europe segment represents the results of operations and financial position of plants located in Romania and traders located in Italy and Germany.

Management monitors the operating results of operating segments separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance is evaluated based on Adjusted EBITDA. Adjusted EBITDA is determined as profit/(loss) for the period excluding finance costs and finance income, income tax (benefit)/expense, depreciation and amortisation, foreign exchange (gain)/loss, impairment/(reversal of impairment) of non-current assets, movements in allowances and provisions (except for provisions for bonuses), (gain)/loss on disposal of property, plant and equipment, (gain)/loss on changes in fair value of financial instruments, share of (profit)/loss of associates and other non-cash items. Group financing (including finance costs and finance income) is managed on a group basis and is not allocated to operating segments.

The following tables present revenue and profit information regarding the Group's reportable segments:

Three-month period ended March 31, 2015	**Russia**	**Americas**	**Europe**	**TOTAL**
Revenue	748,178	327,173	58,704	**1,134,055**
Cost of sales	(553,074)	(286,342)	(42,365)	**(881,781)**
GROSS PROFIT	**195,104**	**40,831**	**16,339**	**252,274**
Selling, general and administrative expenses	(84,232)	(34,042)	(8,388)	**(126,662)**
Other operating expenses, net	(3,273)	(299)	(30)	**(3,602)**
OPERATING PROFIT	**107,599**	**6,490**	**7,921**	**122,010**
ADD BACK:				
Depreciation and amortisation	34,885	20,156	3,353	**58,394**
(Gain)/loss on disposal of property, plant and equipment	265	327	(35)	**557**
Allowance for net realisable value of inventory	(1,188)	1,060	21	**(107)**
Allowance for doubtful debts	90	234	502	**826**
Movement in other provisions	3,649	(257)	(255)	**3,137**
	37,701	**21,520**	**3,586**	**62,807**
ADJUSTED EBITDA	**145,300**	**28,010**	**11,507**	**184,817**

(All amounts are in thousands of US dollars, unless specified otherwise)

1) Segment Information (continued)

Three-month period ended March 31, 2015	**Russia**	**Americas**	**Europe**	**TOTAL**
RECONCILIATION TO PROFIT BEFORE TAX:				
Adjusted EBITDA	**145,300**	**28,010**	**11,507**	**184,817**
Reversal of adjustments from operating profit to EBITDA	(37,701)	(21,520)	(3,586)	**(62,807)**
OPERATING PROFIT	**107,599**	**6,490**	**7,921**	**122,010**
Foreign exchange gain/(loss), net	(23,435)	(1,673)	1,504	**(23,604)**
OPERATING PROFIT AFTER FOREIGN EXCHANGE GAIN/(LOSS)	**84,164**	**4,817**	**9,425**	**98,406**
Finance costs				**(66,449)**
Finance income				**3,856**
Share of profit of associates				**34**
PROFIT BEFORE TAX				**35,847**

Three-month period ended March 31, 2014	**Russia**	**Americas**	**Europe**	**TOTAL**
Revenue	981,128	418,035	66,920	**1,466,083**
Cost of sales	(756,958)	(374,203)	(53,595)	**(1,184,756)**
GROSS PROFIT	**224,170**	**43,832**	**13,325**	**281,327**
Selling, general and administrative expenses	(127,538)	(37,654)	(9,689)	**(174,881)**
Other operating income/(expenses), net	(3,756)	(1,027)	2	**(4,781)**
OPERATING PROFIT	**92,876**	**5,151**	**3,638**	**101,665**
ADD BACK:				
Depreciation and amortisation	51,825	18,724	3,246	**73,795**
Gain/ (loss) on disposal of property, plant and equipment	(744)	731	(109)	**(122)**
Allowance for net realisable value of inventory	2,046	127	(348)	**1,825**
Allowance for doubtful debts	(658)	20	137	**(501)**
Movement in other provisions	7,420	(469)	798	**7,749**
	59,889	**19,133**	**3,724**	**82,746**
ADJUSTED EBITDA	**152,765**	**24,284**	**7,362**	**184,411**

Three-month period ended March 31, 2014	**Russia**	**Americas**	**Europe**	**TOTAL**
RECONCILIATION TO LOSS BEFORE TAX:				
Adjusted EBITDA	**152,765**	**24,284**	**7,362**	**184,411**
Reversal of adjustments from operating profit to EBITDA	(59,889)	(19,133)	(3,724)	**(82,746)**
OPERATING PROFIT	**92,876**	**5,151**	**3,638**	**101,665**
Foreign exchange loss, net	(62,097)	(467)	(290)	**(62,854)**
OPERATING PROFIT AFTER FOREIGN EXCHANGE LOSS	**30,779**	**4,684**	**3,348**	**38,811**
Finance costs				**(55,334)**
Finance income				**884**
Gain on changes in fair value of derivative financial instruments				**1,640**
Share of loss of associates				**(227)**
LOSS BEFORE TAX				**(14,226)**

(All amounts are in thousands of US dollars, unless specified otherwise)

1) Segment Information (continued)

The following table presents additional information of the Group's reportable segments:

Segment assets	Russia	Americas	Europe	TOTAL
At March 31, 2015	3,458,851	1,594,024	354,238	**5,407,113**
At December 31, 2014	3,541,125	1,698,579	409,684	**5,649,388**

The following table presents the revenues from external customers for each group of products and services:

Sales to external customers	Seamless pipes	Welded pipes	Other operations	TOTAL
Three-month period ended March 31, 2015	697,239	384,340	52,476	**1,134,055**
Three-month period ended March 31, 2014	977,338	424,244	64,501	**1,466,083**

2) Cost of Sales

Cost of sales was as follows:

	Three-month period ended March 31,	
	2015	**2014**
Raw materials and consumables	552,742	751,997
Staff costs including social security	130,004	184,434
Energy and utilities	71,586	113,225
Depreciation and amortisation	48,452	64,686
Contracted manufacture	23,385	36,370
Repairs and maintenance	21,156	29,738
Freight	16,281	21,143
Taxes	7,722	10,624
Professional fees and services	6,870	9,471
Rent	3,865	3,552
Travel	558	757
Insurance	111	197
Communications	110	197
Other	1,168	1,394
Total production cost	**884,010**	**1,227,785**
Change in own finished goods and work in progress	(5,538)	(50,584)
Cost of sales of externally purchased goods	3,448	4,292
Obsolete stock, write-offs	(139)	3,263
Cost of sales	**881,781**	**1,184,756**

(All amounts are in thousands of US dollars, unless specified otherwise)

3) Selling and Distribution Expenses

Selling and distribution expenses were as follows:

	Three-month period ended March 31,	
	2015	**2014**
Freight	34,636	49,411
Staff costs including social security	11,801	16,947
Depreciation and amortisation	6,959	8,816
Professional fees and services	6,043	5,764
Consumables	4,094	5,153
Bad debt expense	1,379	(490)
Rent	1,211	1,665
Travel	514	984
Utilities and maintenance	469	774
Communications	224	309
Insurance	220	285
Other	208	333
	67,758	**89,951**

4) General and Administrative Expenses

General and administrative expenses were as follows:

	Three-month period ended March 31,	
	2015	**2014**
Staff costs including social security	32,938	46,400
Professional fees and services	7,615	11,195
Depreciation and amortisation	2,208	3,192
Utilities and maintenance	2,102	3,482
Insurance	1,775	1,919
Communications	1,636	1,887
Travel	936	1,739
Rent	917	1,203
Taxes	907	974
Transportation	879	1,559
Consumables	620	873
Other	533	2,299
	53,066	**76,722**

5) Research and Development Expenses

Research and development expenses were as follows:

	Three-month period ended March 31,	
	2015	**2014**
Staff costs including social security	1,639	1,806
Depreciation and amortisation	1,098	1,043
Professional fees and services	816	368
Consumables	197	140
Travel	116	234
Utilities and maintenance	60	92
Other	126	74
	4,052	**3,757**

(All amounts are in thousands of US dollars, unless specified otherwise)

6) Other Operating Income and Expenses

Other operating income was as follows:

	Three-month period ended March 31,	
	2015	2014
Gain from penalties and fines	572	1,683
Gain on disposal of property, plant and equipment	–	122
Other	773	801
	1,345	**2,606**

Other operating expenses were as follows:

	Three-month period ended March 31,	
	2015	2014
Social and social infrastructure maintenance expenses	2,044	3,335
Penalties, fines and claims	1,307	1,488
Loss on disposal of property, plant and equipment	557	–
Sponsorship and charitable donations	539	2,123
Other	500	441
	4,947	**7,387**

7) Income Tax

Income tax expense was as follows:

	Three-month period ended March 31,	
	2015	2014
Current income tax expense	12,498	3,971
Adjustments in respect of income tax of previous periods	16	364
Deferred tax benefit related to origination and reversal of temporary differences	(6,442)	(2,841)
Total income tax expense	**6,072**	**1,494**

8) Acquisition of Subsidiaries

Acquisition of Metal Scrap Companies

On February 9, 2015, the Group acquired from entity under common control 100% interest in OOO ChermetService-Snabzhenie (and its subsidiaries) specialising on scrap supply to steel plants, which includes collection, processing, distribution of ferrous scrap and comprehensive procurement services. ChermetService-Snabzhenie is one of the leaders in the Russian steel scrap market. The acquisition will allow the Group to establish a complete scrap supply cycle at its facilities, which will guarantee the Group’s feedstock security.

(All amounts are in thousands of US dollars, unless specified otherwise)

8) Acquisition of Subsidiaries (continued)

Acquisition of Metal Scrap Companies (continued)

The fair values of assets acquired, liabilities assumed and purchase consideration were preliminary determined as follows at the acquisition date:

	February 9, 2015
Cash	2,233
Trade and other receivables (including receivables from the Group in the amount of 27,068)	44,643
Inventories	2,470
Prepayments and input VAT	2,194
Property, plant and equipment	10,963
Intangible assets	36,421
Deferred tax assets	231
Other non-current assets	3,408
Total assets	**102,563**
Trade and other payables	(32,264)
Interest-bearing loans and borrowings	(45,885)
Deferred tax liability	(8,022)
Total liabilities	**(86,171)**
Total identifiable net assets	**16,392**
Goodwill	**24,928**
Purchase consideration	**41,320**

Since the valuation of the assets and liabilities of ChermetService-Snabzhenie is still in process, the values were determined provisionally. Goodwill arising on the acquisition of ChermetService-Snabzhenie related to the expected synergy from integration of the acquired subsidiaries into the Group.

In October-November 2014, the Group paid 2,729 million Russian roubles for the acquisition of these metal scrap companies. As at December 31, 2014, the prepaid amount was included in other non-current assets.

Acquisition of Well Completions Business in Canada

In February 2015, the Group acquired well completions business located in Canada for 8,315, including contingent consideration in the amount of 2,011. The acquisition will allow the Group to enter the well completions market and to enlarge the range of products and services offered to its clients. The fair value of the net identifiable assets of the acquiree as at the date of acquisition was provisionally determined in the amount of 6,117. The excess in the amount of 2,198 of the purchase consideration over the fair value of net assets was recognised as goodwill. The Group paid 1,563 of purchase consideration for the acquisition of the business.

(All amounts are in thousands of US dollars, unless specified otherwise)

9) Investments in Associates

The movement in investments in associates was as follows in the three-month period ended March 31, 2015:

	March 31, 2015
Balance at January 1	1,247
Share of profit of associates	34
Currency translation adjustment	(45)
Balance at March 31	**1,236**

10) Cash and Cash Equivalents

Cash and cash equivalents were denominated in the following currencies:

	March 31, 2015	December 31, 2014
Russian rouble	40,513	163,557
US dollar	40,121	84,214
Euro	5,171	3,335
Romanian lei	357	1,043
Other currencies	871	749
	87,033	**252,898**

The above cash and cash equivalents consisted primarily of cash at banks. As at March 31, 2015, the restricted cash amounted to 10,229 (December 31, 2014: 1,139).

11) Inventories

Inventories consisted of the following:

	March 31, 2015	December 31, 2014
Finished goods and work in process	610,379	617,354
Raw materials and supplies	419,105	452,782
Gross inventories	**1,029,484**	**1,070,136**
Allowance for net realisable value of inventory	(22,332)	(23,229)
Net inventories	**1,007,152**	**1,046,907**

(All amounts are in thousands of US dollars, unless specified otherwise)

12) Property, Plant and Equipment

Movement in property, plant and equipment in the three-month period ended March 31, 2015 was as follows:

	Land and buildings	Machinery and equipment	Transport and motor vehicles	Furniture and fixtures	Leasehold improve-ments	Construction in progress	TOTAL
COST							
Balance at January 1, 2015	1,023,064	2,509,724	56,435	56,511	28,813	194,343	**3,868,890**
Additions	–	–	–	–	–	33,779	**33,779**
Assets put into operation	3,482	33,123	307	977	531	(38,420)	**–**
Disposals	(283)	(6,103)	(336)	(258)	–	(222)	**(7,202)**
Increase due to acquisition of subsidiaries	4,994	2,382	14	4,011	8	–	**11,409**
Currency translation adjustments	(37,467)	(81,682)	1,499	(5,482)	(225)	(6,743)	**(130,100)**
BALANCE AT MARCH 31, 2015	**993,790**	**2,457,444**	**57,919**	**55,759**	**29,127**	**182,737**	**3,776,776**
ACCUMULATED DEPRECIATION AND IMPAIRMENT							
Balance at January 1, 2015	(214,935)	(973,538)	(25,238)	(38,232)	(6,777)	–	**(1,258,720)**
Depreciation charge	(6,933)	(41,006)	(1,091)	(1,654)	(349)	–	**(51,033)**
Disposals	68	5,804	317	235	–	–	**6,424**
Currency translation adjustments	7,803	29,358	1,353	1,058	9	–	**39,581**
BALANCE AT MARCH 31, 2015	**(213,997)**	**(979,382)**	**(24,659)**	**(38,593)**	**(7,117)**	**–**	**(1,263,748)**
NET BOOK VALUE AT MARCH 31, 2015	**779,793**	**1,478,062**	**33,260**	**17,166**	**22,010**	**182,737**	**2,513,028**
NET BOOK VALUE AT JANUARY 1, 2015	**808,129**	**1,536,186**	**31,197**	**18,279**	**22,036**	**194,343**	**2,610,170**

Capitalised Borrowing Costs

The amount of borrowing costs capitalised during the three-month period ended March 31, 2015 was 498. The capitalisation rate was 11.69%.

(All amounts are in thousands of US dollars, unless specified otherwise)

13) Goodwill and Other Intangible Assets

Movement in intangible assets in the three-month period ended March 31, 2015 was as follows:

	Patents and trademarks	Goodwill	Software	Customer and supplier relationships	Proprietary technology	Other	TOTAL
COST							
Balance at January 1, 2015	211,591	564,793	12,833	472,300	14,100	5,663	**1,281,280**
Additions	103	–	9	–	–	665	**777**
Disposals	–	–	–	–	–	(82)	**(82)**
Increase due to acquisition of subsidiaries	–	27,126	–	37,745	2,646	44	**67,561**
Currency translation adjustments	(50)	729	(506)	4,802	–	(259)	**4,716**
BALANCE AT MARCH 31, 2015	**211,644**	**592,648**	**12,336**	**514,847**	**16,746**	**6,031**	**1,354,252**
ACCUMULATED AMORTISATION AND IMPAIRMENT							
Balance at January 1, 2015	(368)	(160,932)	(12,477)	(416,117)	(11,548)	(2,735)	**(604,177)**
Amortisation charge	(28)	–	(20)	(6,700)	(441)	(1,009)	**(8,198)**
Disposals	–	–	–	–	–	3	**3**
Currency translation adjustments	17	397	489	–	–	43	**946**
BALANCE AT MARCH 31, 2015	**(379)**	**(160,535)**	**(12,008)**	**(422,817)**	**(11,989)**	**(3,698)**	**(611,426)**
NET BOOK VALUE AT MARCH 31, 2015	**211,265**	**432,113**	**328**	**92,030**	**4,757**	**2,333**	**742,826**
NET BOOK VALUE AT JANUARY 1, 2015	**211,223**	**403,861**	**356**	**56,183**	**2,552**	**2,928**	**677,103**

The carrying amounts of goodwill and intangible assets with indefinite useful lives were allocated among cash generating units as follows:

	March 31, 2015		December 31, 2014	
	Goodwill	Intangible assets with indefinite useful lives	Goodwill	Intangible assets with indefinite useful lives
American division	322,572	208,700	322,572	208,700
Middle East division	36,241	–	36,241	–
Oilfield subdivision	16,497	–	17,143	–
European division	5,180	–	5,805	–
Other cash-generating units	51,623	1,606	22,100	1,606
	432,113	**210,306**	**403,861**	**210,306**

The Group determines whether goodwill and intangible assets with indefinite useful lives are impaired on an annual basis and when circumstances indicate that the carrying value may be impaired. At March 31, 2015, there were indicators of impairment of certain cash generating units, therefore, the Group performed impairment tests in respect of these units. As a result of the tests, the Group determined that the carrying values of these cash-generating units do not exceed their recoverable amounts. Consequently, no impairment losses were recognised in the three-month period ended March 31, 2015. Should the Group performance and market conditions deviate (other than temporary) from management plans assumed in the impairment estimates, the carrying values of certain cash-generating units may become higher than their recoverable amounts. For details on sensitivity of the assumptions used in the impairment tests refer to the annual financial statements.

(All amounts are in thousands of US dollars, unless specified otherwise)

14) Trade and Other Payables

Trade and other payables consisted of the following:

	March 31, 2015	December 31, 2014
Trade payables	561,022	530,501
Accounts payable for property, plant and equipment	35,997	52,429
Liabilities for VAT	29,959	39,523
Payroll liabilities	21,572	21,095
Liabilities for property tax	12,333	12,980
Accrued and withheld taxes on payroll	13,201	11,361
Sales rebate payable	5,837	9,440
Liabilities under put options of non-controlling interest shareholders in subsidiaries	6,651	6,639
Notes issued to third parties	1,095	3,133
Liabilities for other taxes	984	1,309
Other payables	34,954	34,286
	723,605	**722,696**

15) Provisions and Accruals

Provisions and accruals consisted of the following:

	March 31, 2015	December 31, 2014
Current		
Provision for bonuses	5,712	17,190
Accrual for long-service bonuses	3,697	9,396
Accrual for unused annual leaves, current portion	4,429	3,060
Current portion of employee benefits liability	2,253	2,366
Environmental provision, current portion	1,325	1,351
Other provisions	6,632	8,034
	24,048	**41,397**
Non-current		
Accrual for unused annual leaves	16,960	14,062
Environmental provision	4,075	4,133
Provision for bonuses	455	770
Other provisions	5,923	3,951
	27,413	**22,916**

(All amounts are in thousands of US dollars, unless specified otherwise)

16) Interest-Bearing Loans and Borrowings

Interest-bearing loans and borrowings consisted of the following:

	March 31, 2015	December 31, 2014
Current		
Bank loans	330,337	265,439
Interest payable	29,214	30,841
Current portion of non-current borrowings	118,932	152,135
Current portion of bearer coupon debt securities	–	311,000
Unamortised debt issue costs	(293)	(610)
Total short-term loans and borrowings	**478,190**	**758,805**
Non-current		
Bank loans	1,684,876	1,571,236
Bearer coupon debt securities	1,000,000	1,311,000
Unamortised debt issue costs	(7,473)	(8,201)
Less: current portion of non-current borrowings	(118,932)	(152,135)
Less: current portion of bearer coupon debt securities	–	(311,000)
Total long-term loans and borrowings	**2,558,471**	**2,410,900**

The Group's borrowings were denominated in the following currencies:

	Interest rates	March 31, 2015	Interest rates	December 31, 2014
Russian rouble	Fixed 7.99%-18.5%	974,668	Fixed 7.99%-13%	958,177
US dollar			Fixed 5.25%	313,262
	Fixed 6.75%	513,788	Fixed 6.75%	505,235
	Fixed 7.75%	504,984	Fixed 7.75%	514,521
	Fixed 4.99%-10.8%	555,904	Fixed 4.99%-5.8%	406,272
	Variable: Libor (1m) + 2.25%-2.75% Libor (3m) + 2.75%-4.5%	412,858	Variable: Libor (1m) + 2.25%-2.75% Libor (3m) + 2.75%-4.5%	386,679
Euro			Fixed 5.19%	11,540
	Variable: Euribor (1m) + 1.15%-3.75% Euribor (3m) + 1.7%-3% Euribor (6m) + 1.25%	74,459	Variable: Euribor (1m) + 1.15%-3.5% Euribor (3m) + 1.7%-3%	74,019
		3,036,661		**3,169,705**

Unutilised Borrowing Facilities

As at March 31, 2015, the Group had unutilised borrowing facilities in the amount of 655,507 (December 31, 2014: 879,656).

Convertible Bonds

In February 2015, the Group redeemed its 5.25% convertible bonds due 2015 convertible into Global Depositary Receipts each representing four ordinary shares of OAO TMK. To redeem the bonds the Group used cash generated from operating and financing activities.

(All amounts are in thousands of US dollars, unless specified otherwise)

17) Fair Value of Financial Instruments

Fair Value of Financial Instruments Carried at Fair Value

The Group's derivative financial instruments carried at fair value comprised of interest rate swaps. Their use was governed by the policies consistent with the overall risk management strategy of the Group. The derivatives were designated as hedging instruments in cash flow hedges. As at March 31, 2015, the balance of interest rate swaps was 2,204 (December 31, 2014: 2,076). The derivatives were measured by the Group using valuation techniques based on observable market data (Level 2 fair value measurement hierarchy). The valuation techniques incorporated various inputs including the credit quality of counterparties and interest rate curves.

Fair Value of Financial Instruments not Carried at Fair Value

For financial assets and financial liabilities that are liquid or having a short-term maturity (cash and cash equivalents, short-term accounts receivable, short-term loans) the carrying amounts approximate to their fair values.

The following table shows financial instruments which carrying values differ from fair values:

	March 31, 2015		December 31, 2014	
	Par value	**Fair value**	**Par value**	**Fair value**
Financial liabilities				
Fixed rate long-term bank loans	1,224,008	1,152,903	1,161,283	1,089,008
Variable rate long-term bank loans	397,598	389,477	408,379	405,099
5.25 per cent convertible bonds	–	–	311,000	289,043
6.75 per cent loan participation notes due 2020	500,000	391,230	500,000	291,665
7.75 per cent loan participation notes due 2018	500,000	444,500	500,000	320,000

For quoted debt instruments (bonds and loan participation notes) the fair values were determined based on quoted market prices. The fair values of unquoted debt instruments were estimated by discounting future cash flows using rates currently available for debt on similar terms, credit risk and remaining maturities.

18) Related Parties Disclosures

Compensation to Key Management Personnel of the Group

Key management personnel comprise members of the Board of Directors, the Management Board and certain executives of the Group.

The compensation to key management personnel included:

- Wages, salaries, social security contributions and other short-term benefits in the amount of 3,788 (three-month period ended March 31, 2014: 4,438).
- Provision for performance bonuses in the amount of 835 (three-month period ended March 31, 2014: 1,356).

(All amounts are in thousands of US dollars, unless specified otherwise)

18) Related Parties Disclosures (continued)

Compensation to Key Management Personnel of the Group (continued)

The amounts disclosed above were recognised as general and administrative expenses in the income statement for the three-month periods ended March 31, 2015 and 2014.

The balance of loans issued to key management personnel amounted to 380 as at March 31, 2015 (December 31, 2014: 517).

Transactions with the Parent of the Company

In December 2014, the Group approved interim dividends in respect of six months 2014, from which 266,796 thousand Russian roubles (4,896 at the exchange rate at the date of approval) related to the parent of the Company. In the three-month period ended March 31, 2015, interim dividends were fully paid.

In February 2015, the Group increased share capital of the subsidiary Completions Development S.a r.l. The share capital increase was partially financed by the parent of the Company, an owner of non-controlling interest in Completions Development S.a r.l. Contribution received from the parent of the Company amounted to 1,250.

Transactions with Entities under Common Control with the Company

The following table provides balances with entities under common control with the Company:

	March 31, 2015	December 31, 2014
Trade and other receivables	23,687	4,731
Cash and cash equivalents	14,436	80,550
Prepayments	23	10
Prepayment for acquisition of subsidiary (Note 8)	–	48,506
Advances received	(2,509)	(2,825)
Other accounts payable	(433)	(480)
Accounts payable for raw materials	–	(38,262)

The following table provides the summary of transactions with entities under common control with the Company:

	Three-month period ended March 31,	
	2015	2014
Purchases of raw materials	26,700	122,751
Purchase of property, plant and equipment	–	3,850
Purchases of other goods and services	1,053	1,653
Sales revenue	1,599	2,281
Finance income	1,432	16

19) Contingencies and Commitments

Operating Environment of the Group

Significant part of the Group's principal assets is located in the Russian Federation and USA, therefore its significant operating risks are related to the activities of the Group in these countries.

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.

In 2014, the Russian economy was negatively impacted by a significant drop in crude oil prices and a significant devaluation of the Russian Rouble, as well as sanctions imposed on Russia by several countries. The combination of the above resulted in reduced access to capital, a higher cost of capital, increased inflation and uncertainty regarding economic growth. These trends continued to a certain extent in the beginning of 2015, which could negatively affect the Group's future financial position, results of operations and business prospects.

Although the US economy is growing, the drop in oil prices may result in the decline in oil exploration, drilling and production activities. As a result, the demand for the oil pipes in the US market may decrease accordingly. Significant decline in demand could have a negative impact on 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.

Taxation

Tax, currency and customs legislation is subject to varying interpretations and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant regional and federal authorities. Management believes that it has paid or accrued all taxes that are applicable. Where uncertainty exists, the Group has accrued tax liabilities based on management's best estimate of the probable outflow of resources embodying economic benefits, which will be required to settle these liabilities.

Up to the date of authorisation of these consolidated financial statements for issuance, the court proceedings and pre-trial disputes had not been finalised for the claims in the amount of 150,239 thousand Russian roubles (2,570 at the exchange rate as at March 31, 2015). Management believes that the Group's position is justified and it is not probable that the ultimate outcome of these matters will result in material losses for the Group. Consequently, the amounts of the claims being contested by the Group were not accrued in the consolidated financial statements for the three-month period ended March 31, 2015.

(All amounts are in thousands of US dollars, unless specified otherwise)

19) Contingencies and Commitments (continued)

Contractual Commitments

The Group had contractual commitments for the acquisition of property, plant and equipment from third parties in the amounts of 120,566 and 135,904 as at March 31, 2015 and December 31, 2014, respectively (contractual commitments were expressed net of VAT). As at March 31, 2015, the Group had advances of 10,051 with respect to commitments for the acquisition of property, plant and equipment (December 31, 2014: 15,627). These advances were included in other non-current assets.

Under contractual commitments disclosed above, the Group opened unsecured letters of credit in the amount of 31,079 (December 31, 2014: 22,500).

Insurance Policies

The Group maintains insurance against losses that may arise in case of property damage, accidents, transportation of goods. The Group also maintains corporate product liability and directors and officers liability insurance policies. Nevertheless, any recoveries under maintained insurance coverage that may be obtained in the future may not offset the lost revenues or increased costs resulting from a disruption of operations.

Legal Claims

During the period, the Group was involved in a number of court proceedings (both as a plaintiff and a defendant) arising in the ordinary course of business. Management believes there are no current legal proceedings or other claims outstanding, which could have a material effect on the results of operations or financial position of the Group.

Guarantees of Debts of Others

The Group guaranteed debts of others outstanding at March 31, 2015 in the amount of 252 (December 31, 2014: 494).

20) Equity

i) Share Capital

	March 31, 2015	**December 31, 2014**
Number of shares		
Authorised		
Ordinary shares of 10 Russian roubles each	991,907,260	991,907,260
Issued and fully paid		
Ordinary shares of 10 Russian roubles each	991,907,260	991,907,260

(All amounts are in thousands of US dollars, unless specified otherwise)

20) Equity (continued)

ii) Hedges of Net Investment in Foreign Operations

As at March 31, 2015, a proportion of the Group's US dollar-denominated borrowings in the amount of 1,197,710 (December 31, 2014: 1,197,710) was designated as hedges of net investment in the Group's foreign subsidiaries.

The effectiveness of the hedging relationship was tested using the dollar offset method by comparing the cumulative gains or losses due to changes in US dollar / Russian rouble spot rates on the hedging instrument and on the hedged item. In the three-month period ended March 31, 2015, the effective portion of net losses from spot rate changes in the amount of 2,163,496 thousand Russian roubles (34,787 at historical exchange rates), net of income tax of 432,699 thousand Russian roubles (6,957 at historical exchange rates), was recognised in other comprehensive loss.

iii) Movement on Cash Flow Hedges

The Group hedges its exposure to variability in cash flows attributable to interest rate risk using interest rate swaps.

The details of movement on cash flow hedges during the three-month period ended March 31, 2015 are presented in the following table:

	Interest rate swap contracts
Loss arising during the period	(739)
Recognition of realised results in the income statement	397
Movement on cash flow hedges	**(342)**
Income tax	71
Movement on cash flow hedges, net of tax	**(271)**

iv) Recognition of the Change in Non-controlling Interests in the Subsidiary as an Equity Transaction

In the three-month period ended March 31, 2015, the non-controlling interest's share of profit in OOO TMK-INOX amounted to 237. This amount was charged to additional paid-in capital.