9. CONSOLIDATED FINANCIAL STATEMENTS

CONTENT

OAO TMK

Consolidated Statement of Cash Flows

for the year ended December 31, 2014

(All amounts in thousands of US dollars)

	NOTES	2014	2013
Operating activities			
Profit/(loss) before tax		(201,373)	312,383
Adjustments to reconcile profit/(loss) before tax to operating cash flows:			
Depreciation of property, plant and equipment		266,574	276,787
Amortisation of intangible assets	17	37,081	49,102
Loss on disposal of property, plant and equipment	7	4,395	5,861
Impairment of goodwill	17	151,369	1,080
Impairment of property, plant and equipment	16	1,135	4,243
Foreign exchange loss, net		301,246	49,189
Finance costs		232,685	252,247
Finance income		(6,641)	(7,164)
Gain on disposal of subsidiary	10	–	(1,862)
Gain on changes in fair value of derivative financial instruments		(2,080)	(8,377)
Share of profit of associates	11	(273)	(176)
Allowance for net realisable value of inventory		8,782	1,246
Allowance for doubtful debts		7,943	15,628
Movement in provisions		6,550	(5,989)
Operating cash flows before working capital changes		**807,393**	**944,198**
Working capital changes:			
Increase in inventories		(129,879)	(65,273)
Increase in trade and other receivables		(75,990)	(158,946)
(Increase)/decrease in prepayments		(20,801)	22,900
Increase in trade and other payables		41,362	162,818
Increase/(decrease) in advances from customers		25,981	(120,060)
Cash generated from operations		**648,066**	**785,637**
Income taxes paid		(53,316)	(82,204)
Net cash flows from operating activities		**594,750**	**703,433**
Investing activities			
Purchase of property, plant and equipment and intangible assets		(293,061)	(396,794)
Proceeds from sale of property, plant and equipment		5,623	6,451
Acquisition of subsidiaries		(59,750)	(38,300)
Disposal of subsidiary		–	(1,906)
Issuance of loans		(557)	(580)
Proceeds from repayment of loans issued		1,765	1,610
Interest received		3,196	3,456
Dividends received		80	2,674
Net cash flows used in investing activities		**(342,704)**	**(423,389)**
Financing activities			
Proceeds from share capital increase	29 (i)	101,536	–
Proceeds from borrowings		1,576,886	1,562,500
Repayment of borrowings		(1,422,984)	(1,655,971)
Interest paid		(250,654)	(253,616)
Payment of finance lease liabilities		(7,117)	(5,337)
Acquisition of non-controlling interests	29 (vi)	(193)	–
Contributions from non-controlling interest owners	27	1,013	2,525
Dividends paid to equity holders of the parent		(46,950)	(52,727)
Dividends paid to non-controlling interest shareholders		(4,083)	(4,185)
Net cash flows used in financing activities		**(52,546)**	**(406,811)**
Net increase/(decrease) in cash and cash equivalents		**199,500**	**(126,767)**
Net foreign exchange difference		(39,900)	(4,996)
Cash and cash equivalents at January 1		93,298	225,061
Cash and cash equivalents at December 31		**252,898**	**93,298**

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

OAO TMK

Notes to the Consolidated Financial Statements for the year ended December 31, 2014

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

Corporate Information

These consolidated financial statements of OAO TMK and its subsidiaries (the "Group") for the year ended December 31, 2014 were authorised for issue in accordance with a resolution of the General Director on March 4, 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 December 31, 2014, 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 of the Financial Statements

Basis of Preparation

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

The consolidated financial statements have been prepared on an accrual basis and under the historical cost convention, except as disclosed in the accounting policies below.

All Group's subsidiaries and associates have a December 31 accounting year-end.

Functional and Presentation Currency

The presentation currency for the purpose of these consolidated financial statements of the Group is the US dollar because the presentation in US dollars is convenient for the major current and potential users of the Group's financial statements.

The functional currency of the Group's entities is the currency of their primary economic environment. The functional currencies of the Group's entities are the Russian rouble, US dollar, Euro, Romanian lei and Canadian dollar.

9. CONSOLIDATED FINANCIAL STATEMENTS

CONTENT

Basis of Preparation of the Financial Statements (continued)

Functional and Presentation Currency (continued)

On consolidation, assets and liabilities of Group companies reported in their functional currencies are translated into US dollars, the Group's presentation currency, at year-end exchange rates. Income and expense items are translated into US dollars at the weighted average rates of exchange or at the rate on the date of the transaction for significant items.

Transactions in foreign currencies are initially recorded in the functional currency at the rate ruling at the date of transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency spot rate of exchange ruling at the end of reporting period. All resulting differences are taken to the income statement with the exception of differences on foreign currency borrowings accounted for as hedges of net investment in foreign operations. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as 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 was determined.

Significant Estimates and Assumptions

The preparation of the consolidated financial statements requires management to exercise judgement and to make estimates and assumptions that affect the reported amounts of assets and liabilities as well as disclosures. These estimates and judgements are based on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results may differ from such estimates, and estimates can be revised in the future, either negatively or positively, depending upon the outcome or changes in expectations based on the facts surrounding each estimate.

The estimates and assumptions which can cause a significant adjustment to the carrying amount of assets and liabilities within the next financial year are discussed below:

Impairment of Property, Plant and Equipment

The Group assesses at each reporting date whether there is any indication that an asset may be impaired. If any such indication exists, the Group estimates the asset's recoverable amount. This requires an estimation of the value in use of the cash-generating unit to which the item is allocated.

The value in use calculation is based on discounted cash flow-based (DCF) methods, which require the Group to make estimates of the expected future cash flows and to choose the suitable discount rate. These estimates may have a material impact on the recoverable value and the amount of the property, plant and equipment impairment.

Assets that suffered an impairment loss are tested for possible reversal of the impairment at each reporting date if indications exist that impairment losses recognised in prior periods no longer exist or have decreased.

Significant Estimates and Assumptions (continued)

Useful Lives of Items of Property, Plant and Equipment

The Group assesses the remaining useful lives of items of property, plant and equipment at least at each financial year-end. If expectations differ from previous estimates, the changes accounted for as changes in accounting estimates in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

Fair Value of Assets and Liabilities Acquired in Business Combinations

The Group is required to recognise separately, at the acquisition date, the identifiable assets, liabilities and contingent liabilities acquired or assumed in the business combination at their fair values, which involves estimates. Such estimates are based on valuation techniques, which require considerable judgment in forecasting future cash flows and developing other assumptions.

Impairment of Goodwill and Intangible Assets with Indefinite Useful Lives

The group tests at least annually whether goodwill and intangible assets with indefinite useful lives have suffered any impairment. The recoverable amount of cash-generating unit to which goodwill and intangible assets with indefinite useful lives allocated is determined based on value in use calculations. These calculations require the use of estimates. Revisions to the estimates may significantly affect the recoverable amount of the cash-generating unit.

Employee Benefits Liability

The Group companies provide a number of post-employment and other long-term benefits to their employees (pensions, lump-sum post-employment payments, jubilee payments, etc.). Such benefits are recognised as defined benefit obligations. The Group uses the actuarial valuation method for measurement of the present value of defined benefit obligations and related current service cost. An actuarial valuation involves making various assumptions that may differ from actual developments in the future. These include the determination of the discount rate, future salary increases, mortality rates, rates of employee turnover and others. In the event that further changes in the key assumptions are required, the future amounts of the employment benefit costs may be affected materially.

Allowance for Doubtful Debts

Allowances for doubtful debts represent the Group's estimates of losses that could arise from the failure and inability of customers to make payments when due. These estimates are based on the ageing of customers' balances, specific credit circumstances and the Group's historical doubtful debts experience. Changes in the economy, industry or specific customer conditions may require adjustments to the allowance for doubtful accounts recorded in the consolidated financial statements.