# Annual Report 2017

# Contents

# FIVE YEAR SUMMARY OF FINANCIAL HIGHLIGHTS AND RATIOS

## Consolidated statement of comprehensive income for the year ended 31 December

| EUR thousands | **2017** | **2016** | **2015** | **2014** | **2013** |
|---|---|---|---|---|---|
| Revenue | 140,411 | 146,758 | 191,447 | 288,725 | 340,973 |
| Cost of sales | (116,988) | (125,592) | (163,793) | (233,837) | (268,810) |
| Change in fair value of biological assets | 269 | (52) | 105 | 1,405 | 1,305 |
| **Gross profit** | 23,692 | 21,114 | 27,759 | 56,293 | 73,468 |
| Operating income (expense), net | (23,104) | (26,609) | (54,638) | (56,950) | (54,276) |
| **Operating profit** | 588 | (5,495) | (26,879) | (657) | 19,192 |
| Net finance expense and other non-operating income (expense) | (7,830) | (31,229) | (46,195) | (73,991) | (5,472) |
| Profit (loss) before tax | (7,242) | (36,724) | (73,074) | (74,648) | 13,720 |
| Income tax (expense) benefit | (104) | (2,182) | (222) | 2,233 | (2,060) |
| **Net profit (loss)** | (7,346) | (38,906) | (73,296) | (72,415) | 11,660 |
| Other comprehensive income (loss) | 13,354 | 9,879 | 14,643 | (6,241) | (11,005) |
| **Total comprehensive income** | 6,008 | (29,027) | (58,653) | (78,656) | 655 |
| **Net profit (loss) attributable to equity holders of the parent company** | (7,672) | (38,804) | (72,807) | (71,835) | 10,835 |
| Weighted average common shares outstanding, thousand | 31,250 | 31,250 | 31,250 | 31,250 | 31,250 |
| **Earnings per share, basic and diluted (EUR cents)** | (25) | (124) | (233) | (229.87) | 34.67 |

## Consolidated balance sheet as at 31 December

| EUR thousands | 2017 | 2016 | 2015 | 2014 | 2013 |
|---|---|---|---|---|---|
| Cash and cash equivalents | 1,416 | 1,044 | 907 | 10,431 | 13,056 |
| Trade and other receivables | 19,406 | 20,042 | 19,506 | 50,615 | 62,088 |
| Inventories | 8,713 | 12,878 | 12,193 | 17,779 | 29,763 |
| Other current assets | 7,279 | 8,269 | 7,985 | 12,809 | 24,338 |
| ***Total current assets*** | 36,814 | 42,233 | 40,591 | 91,634 | 129,245 |
| PPE | 99,679 | 98,763 | 117,787 | 135,401 | 187,974 |
| Investment property | 16,732 | 19,971 | 20,065 | - | - |
| Deferred income tax assets | 2,472 | 2,223 | 3,159 | 6,366 | 8,405 |
| Other non-current assets | 4,717 | 5,266 | 4,948 | 6,450 | 10,863 |
| ***Total non-current assets*** | 123,601 | 126,223 | 145,959 | 148,217 | 207,242 |
| **Total assets** | 160,415 | 168,456 | 186,550 | 239,851 | 336,487 |
| Trade and other payables | 40,778 | 43,054 | 24,659 | 22,535 | 26,948 |
| Short-term loans and borrowings | 75,800 | 87,293 | 103,410 | 96,389 | 79,284 |
| Other current liabilities | 6,281 | 4,201 | 2,469 | 2,447 | 2,510 |
| ***Total current liabilities*** | 122,859 | 134,548 | 130,538 | 121,371 | 108,742 |
| Long-terms loans and borrowings | 10,756 | 14,993 | 4,061 | 5,531 | 24,475 |
| Deferred income tax liability | 13,760 | 11,771 | 14,706 | 18,005 | 27,177 |
| Other non-current liabilities | 118 | 230 | 1,304 | 351 | 657 |
| ***Total non-current liabilities*** | 24,634 | 26,994 | 20,071 | 23,887 | 52,309 |
| **Total liabilities** | 147,493 | 161,542 | 150,609 | 145,258 | 161,051 |
| Share capital | 3,125 | 3,125 | 3,125 | 3,125 | 3,125 |
| Revaluation and other reserves | 90,048 | 83,598 | 79,902 | 71,344 | 79,162 |
| Retained earnings | (81,481) | (80,918) | (48,377) | 17,676 | 88,050 |
| ***Total equity attributable to equity holders of the parent company*** | 11,692 | 5,805 | 34,650 | 92,145 | 170,337 |
| Non-controlling interests | 1,230 | 1,109 | 1,291 | 2,448 | 5,099 |
| **Total equity** | 12,922 | 6,914 | 35,941 | 94,593 | 175,436 |
| **Total liabilities and equity** | 160,415 | 168,456 | 186,550 | 239,851 | 336,487 |

## Key data, ratios and multiples of the Group as at and for the year ended 31 December

| EUR thousands | 2017 | 2016 | 2015 | 2014 | 2013 |
|---|---|---|---|---|---|
| EBITDA | 10,279 | 5,443 | 9,852 | 17,106 | 33,437 |
| Net Debt | 85,140 | 101,242 | 106,564 | 91,489 | 90,703 |
| EBITDA Margin,% | 7.3% | 4% | 5% | 6% | 10% |
| Net Profit Margin,% | (5.2%) | (27%) | (38%) | (25%) | 3% |
| ROE | (62.8%) | (670.22%) | (211.53%) | (78.59%) | 6.85% |
| ROA | (20.0%) | (92%) | (181%) | (79%) | 9% |
| Market Capitalization | 11,538 | 14,184 | 10,780 | 10,851 | 94,190 |
| Enterprise Value (EV) | 97,149 | 116,535 | 118,635 | 104,788 | 189,992 |
| EV / EBITDA | 9.45 | 21.41 | 12.04 | 6.13 | 5.68 |
| EV / SALES | 0.69 | 0.79 | 0.62 | 0.36 | 0.56 |
| Net Debt / Equity | 6.59 | 14.64 | 2.96 | 0.97 | 0.52 |
| Net Debt / EBITDA | 8.28 | 18.60 | 10.82 | 5.35 | 2.71 |
| Net Debt / Sales | 0.61 | 0.69 | 0.56 | 0.32 | 0.27 |
| Total Debt Ratio | 0.92 | 0.96 | 0.81 | 0.61 | 0.48 |
| Debt / Equity | 11.41 | 23.36 | 4.19 | 1.54 | 0.92 |
| Current Ratio | 0.30 | 0.31 | 0.31 | 0.75 | 1.19 |
| Quick Ratio | 0.23 | 0.22 | 0.22 | 0.61 | 0.91 |
| P/E | (1.41) | (0.28) | (0.15) | (0.15) | 8.69 |
| EPS, EUR cents | (24.55) | (124.17) | (232.98) | (229.87) | 34.67 |

### Formulae for calculation of financial indicators

| | |
|---|---|
| EBITDA | Operating profit (loss) + depreciation and amortization, net of the effects of non-recurring expenditure from the operating segments such as restructuring costs, legal expenses, non-current assets impairments and other income and expenses resulted from an isolated, non-recurring events |
| NET DEBT | Short-term finance debt + long-term finance debt, net of cash and cash equivalents |
| EBITDA MARGIN, % | EBITDA/ Revenues |
| NET PROFIT MARGIN % | Net profit / Revenues |
| RETURN ON EQUITY (%) | Net Profit / Shareholders equity |
| RETURN ON ASSETS (%) | Net Profit / Total assets |
| MARKET CAPITALIZATION | Number of shares at end of financial period multiplied by closing price on last trading day of the financial period |
| ENTERPRISE VALUE (EV) | Market capitalization + net debt + minority interests |
| TOTAL DEBT RATIO | (Total current liabilities + total non-current liabilities) / Total assets |
| CURRENT RATIO | Total current assets / Total current liabilities |
| QUICK RATIO | (Total current assets - inventories) / Total current liabilities |
| P/E | Closing price on last trading day of financial year / Earnings per share |
| EPS | Net profit attributable to equity holders of the parent company / Average number of shares during the financial period |

# CEO AND CHAIRMAN'S STATEMENT

Dear Consumers, Shareholders, Partners,

After 2017, we are now more confident to state that Milkiland is successfully withstanding challenges put to its business back in 2014, when Ukraine-Russia conflict instantly put to nil our dairy exports to Russia. We suddenly lost more than 40% of sales, and even more in EBITDA. Additionally, we could not compensate this damage from our Polish plant, since Polish exporters were also banned by Russia. However, our businesses in three countries have found their ways to respond to crisis. We are opening new markets; we are back to introducing new products; we are connecting back our business disconnected by political misfortunes.

Despite of lots of difficult tasks ahead of Milkiland, we believe our company is set back to growth. Our markets started to turn their heads up, and we found new attractive destinations to develop. In revenue, we had some minor correction compared to 2016, but its quality improved; our EBITDA was better than in two previous years. We did significant steps to stabilize Milkiland financially, having achieved restructuring agreements with several creditors. Our debt during 2017 reduced in EUR by 16%; this, combined with increased EBITDA, substantially improved our debt servicing ability. All above should clear the way to final settlement of all outstanding financial claims of our creditors.

Our Russian business is currently the biggest operations of the company, holding over 60% in consolidated revenues in 2017. Russian policy of imports restrictions in some ways turned beneficial to local food producers, providing opportunities to capture market share and enhance the bottom-line. In addition to traditionally strong fresh dairy business of Ostankino, we continue to build up our cheese production in Russia, in order to get back to our Russian customers with famous hard cheese of Milkiland. Profitability of our Russian segment significantly improved, the team is in place, and we believe this part of our company is on good track to recovery.

Ukrainian business was the most heavily hit by political turmoil, since most of its revenues and profits came from exports to Russia. We had to do a lot of cost cutting and operational turnaround. Our management is working hard to find new angles to our cheese and dry milk operations in Ukraine, exploring new geographies. In 2017 we started supplies to several new markets, including Israel, China, Denmark, and the Netherlands. We are positive that ongoing Free Trade agreements process will open new opportunities for Milkiland-Ukraine, providing easier access to European markets. It is our aim to develop Ukrainian business as our exports champion, given low cost base and our sophisticated production facilities in Ukraine.

Our agricultural division also posted positive result in 2017, supported with higher yields and better EBITDA margin. Our milk farms in 2017 supplied about 11% of total milk intake in Ukraine, and our strategic goal to have 20-25% of own milk remains intact.

In Poland, our Ostrowia plant is plotting its way to earn its share in highly competitive European market. Put in operations in 2014, Ostrowia is still facing challenges of scarce milk supply and underdeveloped sales channels. In 2017, Ostrowia's relied mainly on its dry milk products, such as WPC and permeat, and, in financial terms, essentially replicated the result of the previous year. Our key goal towards Polish business is to fully restore its branded goods sales, in order to balance the volatility of commodity prices.

We believe that our team deserved a lot for its efforts in 2017, and this is evidenced by much better financial performance of Milkiland. In ongoing year, we will focus on profitability and sustainability of our Company, aiming to settle all financial issues and thus enable our further business development. Our people are well motivated to perform, our assets are in good shape, and our business partners are with us.

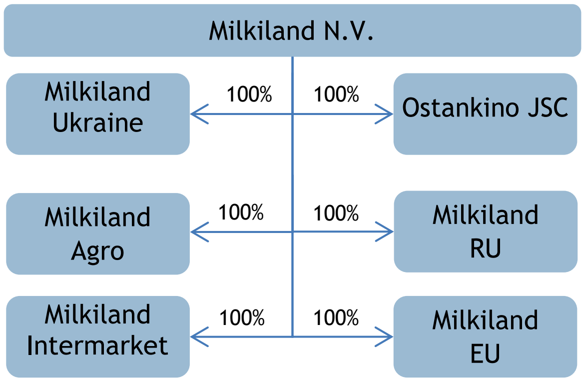
**Oleg Rozhko,**
**Chairman of the Board**

**Anatoliy Yurkevych,**
**Chief Executive Officer**

# REPORT OF THE BOARD OF DIRECTORS ON OPERATIONS FOR THE YEAR 2017

## The Group Overview

Milkiland (the Company or the Group) is an international, diversified dairy producer with core operations in Ukraine, Russia and Poland. The Group's holding company Milkiland N.V. is incorporated in the Netherlands, while commercial activities are conducted through its subsidiaries in respective geographies. The Group's aggregated structure chart is presented below.




The Group's business in Ukraine includes dairy business (Milkiland Ukraine controlling 10 dairy plants) and milk farming (Milkiland Agro), also the Company controls extensive milk collection system throughout the country. Milkiland Ukraine collects and processes about one third of the Group's milk, and produces a wide range of products that it sells both locally and overseas. Milkiland Agro is a farming subsidiary of Milkiland N.V. operating 2,625 cattle livestock, including c.1,660 milking cows. The total land area cultivated by Milkiland Agro is about 12,000 hectares.

The Group's Russian business consists of Ostankino Dairy (Ostankino) and Milkiland RU. Ostankino is the Moscow-based producer of whole milk products ranking No. 3 in the local Moscow market, the largest regional CIS dairy market. Milkiland RU is responsible for distribution of the Group's cheese products in Russia, and development of Milkiland's production base in this country.

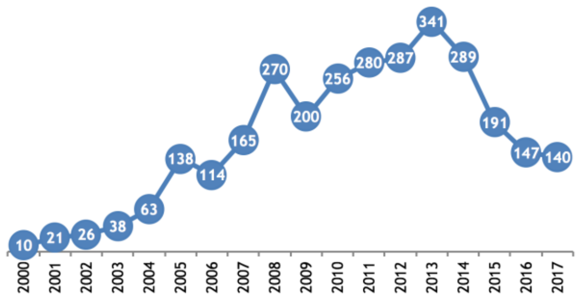
In 2012, the Group launched its EU business, having acquired Polish-based cheese plant Mazowiecka Spółdzielnia Mleczarska Ostrowia. Ostrowia is a modern cheese plant capable to produce a wide range of dairy products such as hard cheese (up to 15,000 tons p.a.), curd, processed cheese, yoghurts and variety of dry milk products.

The Group's Milkiland Intermarket was established in 2012 for the purpose of marketing the Group's products globally. Intermarket's product line mainly consists of dry milk products, butter, and hard cheese.

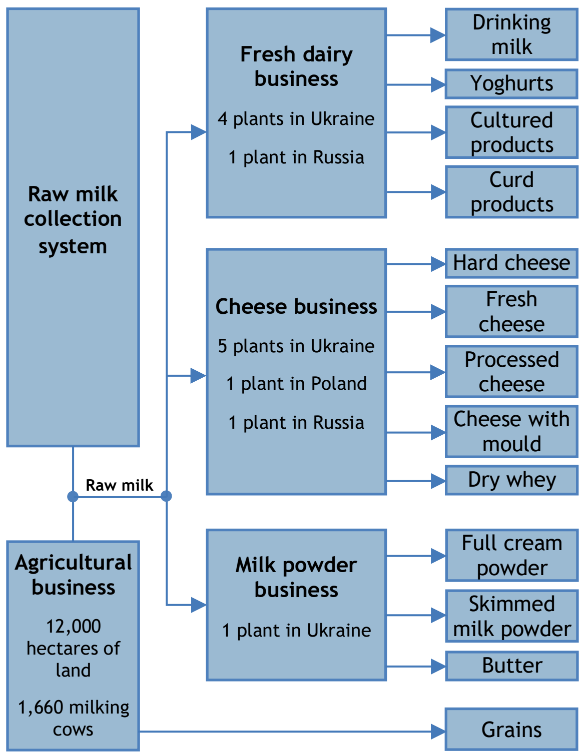
The Group's total annual milk processing capacity exceeds 1.3 million tons; product line consists of whole milk products, various types of cheese, butter, and dry milk products.

In 2017, Milkiland's consolidated revenues were EUR 140 million, representing c. 4% slide compared to 2016, as the result of the Company's focus at margin contributing products.

**Annual revenue, EUR million**




Milkiland develops as universal milk processor with production assets diversified across its local markets, and with a significant level of vertical integration, to enable reliable access to raw milk - one of the core restraints for dairy producers in Ukraine. Such model makes possible to offer a wide range of quality products to the Group's customers, while controlling costs and sustaining margins. Milkiland's business model is outlined in the diagram below:



Milkiland's milk procurement comprises its own dairy farming business (Milkiland Agro) and extensive raw milk collection system from third party farms and individual farmers. In order to secure larger volumes of in-house milk, in 2012 the Group commenced construction of the modern 6,800 stalls dairy farm. The first section of new dairy farm was put in operation. As of end-2017, the number of milking cows operated by Milkiland Agro totaled to c. 1,660. The per cow milk yield in 2017 improved by c. 16% on y-o-y basis. Milkiland Agro provided for c. 12% of the Group's total milk intake in Ukraine.

In order to secure milk supply from third parties, especially small farms and individual farmers, Milkiland established long-term partnership with nation-wiilk cooperative Moloko-Kraina that has grown to provide c. 36% of the Group's raw milk intake in Ukraine in 2017.

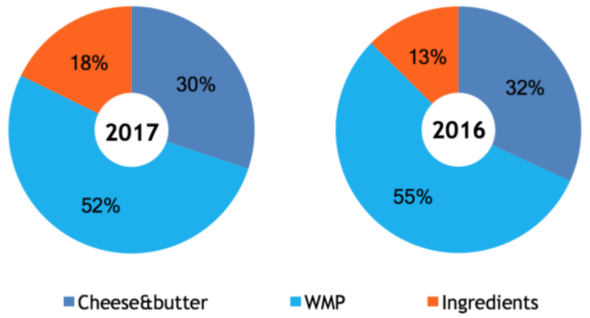
Raw milk collected by the Group is delivered to three core production streams: fresh dairy, cheese, and milk powders. This allows to deliver higher flexibility and better profitability of the business, as Milkiland can quickly switch between product lines.

Whole milk dairy and cheese are Milkiland's core product segments providing together c.82% of the Group's revenues in 2017.

Whole milk dairy business includes Moscow-based Ostankino and 4 dairy plants in Ukraine, producing a wide range of fresh dairy such as drinking milk, kefir, yoghurts, sour cream, ryazhenka, tvorog etc. Milkiland's fresh dairy is sold nation-wide in Ukraine and mainly focused on Moscow city and Central regions of Russia.

The Group's cheese business is comprised of five production units in Ukraine and Polish-based Ostrowia cheese plant. Also, Milkiland controls a cheese plant Rylsk Syrodel in Russia (Kursk region). Milkiland is one of the leading CIS players in this segment offering a wide variety of cheeses such as hard, fresh, curd and processed cheese. The Group is successful in introducing high value added specialty products such as cheese with white and blue mould, being one of the few local players in this attractive segment. The Group sells its cheese primarily in Ukraine, Russia and Kazakhstan, being one of the major CIS players in this segment.

**Revenue breakdown by product in 2017-2016**




Milkiland's milk powder business has one of the largest and most efficient drying facilities in Ukraine, operating mainly in high season, when raw milk is produced in large quantities. Milk powder and butter are sold both locally and abroad to more than 30 countries worldwide. Starting from 2012, Milkiland reinforced its positions in this segment by acquiring of Ostrowia plant, which is equipped with state-of-the-art facilities for production of high value added dry milk products (WPC-80 and permeate).

Sales of milk powder products are mostly done on B2B basis, with large international traders and food-processing companies being the Group's major customers. B2B sales comprised around 18% in the total revenue in 2017.

All Milkiland's brands are targeting a wide audience of families that are keen of healthy diet and natural dairy products. Most of the Group's products are medium priced and widely affordable.

The Company's key brands are: Dobryana, Ostankinskoye, 36 kopeyek and Ostrowia.

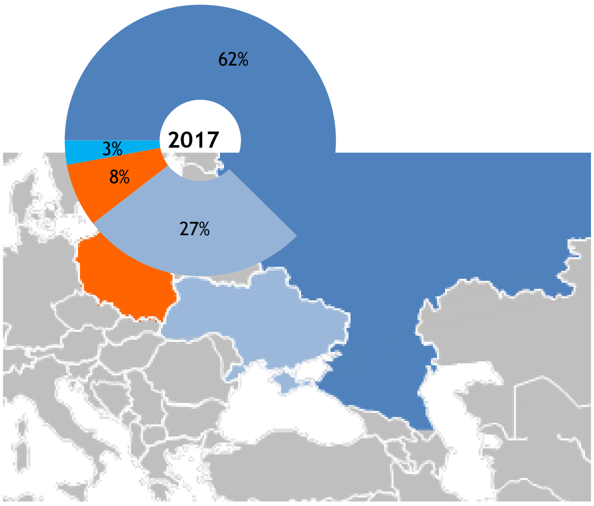
Dobryana is positioned as the Group's international brand actively deployed in Russian, Ukrainian and other CIS markets, as well as in Poland. Dobryana is also the largest selling brand of the Group.

Ostankinskoye is a traditional "medium +" brand for whole milk products produced by Ostankino Dairy, well known by Moscow consumers. The another Group's trademark in Russia is 36 kopeyek, "medium -" brand.

Under Ostrowia brand, the Group markets products locally in Poland.

In 2017, all key brands of the Group were expanded with new products, e.g. the Group entered the vast kosher products market and butter market in EU.

**Revenue breakdown by geography in 2017**




In terms of geographical revenue breakdown, Russia is the largest market for Milkiland contributing about 62% to the Group's total consolidated revenue in 2017. In Russia, the Group is active in whole milk products and hard cheese.

Sales in Ukraine account for about 27% of the Group's revenue and include all range of dairy products. Poland secured 8% of the Group's total revenue in 2017, while other countries account for 3%.

The geographical breakdown somewhat shifted in 2017 from Ukraine and Russia to other markets in response to the Group's strategy to develop sales on its key operational markets and find new export markets. For more information, refer to *Key Products, Production and Sales* section.

## Key Products, Production and Sales

Global milk supplies grew, butterfat prices went sky high and skim milk powder prices remained depressed. This is in short what the global dairy sector experienced in 2017.

Relatively strong global demand for dairy products appears to have contributed to the rise of prices in 2017, especially for products with high milk-fat content. Consumer perceptions of butterfat have changed in recent years as several studies have indicated possible lower risks of consuming butterfat and detrimental effects of alternative trans fats. In 2017, global dairy prices have diverged - butter and cheese prices posted gains while prices for whole milk powder (WMP) and skimmed milk powder (SMP) dropped by 12% and 28% y-o-y, respectively.

The stellar performer was butter with prices climbing by 40% y-o-y to peak at $6,275 per ton FOB Oceania in September 2017. In the European Union, this rise was more spectacular with values peaking at $8,140 per ton amid reports of shortages in countries such as France. The strength in global demand for milk fat has resulted in a global surplus of skim solids. At the end of 2017, the European Union held 0.4 million tons of skim milk powder in public storage from its intervention program. Most of the stocks were more than a year old. In 2017, EU shipments of SMP are estimated to have grown by nearly one third. In 2018, EU exports are forecasted to expand by another 3%.

For 2018, the global dairy price outlook points to a continued sharp correction in butter prices although strong consumer demand should keep prices from dropping far below $4,000 per ton. Cheese and WMP will likely decline moderately while SMP prices will continue to struggle at prices below $2,000 per ton due to ample exportable supplies in the European Union and the United States.

Several factors, including the drought in New Zealand, could well affect global dairy prices in 2018. Also, the fact that intervention stores were opened in Europe since March 1, 2018, with the European Commission carrying 376,000 tons of skim milk powder. Another one factor is the risk of a US exit from NAFTA after 5 rounds of 'modernizing' the agreement has failed to advance amendments to the existing agreement. Two more rounds are scheduled for 2018. Change of Chinese regulations towards tightening environmental protection regulations, with local government zones prohibiting animal farming in certain regions, is an additional factor of the influence. Furthermore, tensions in the Middle East have escalated, although this didn't lead to discernible impacts on the dairy market yet.

According to the USDA estimations, world milk production during 2017 expanded by 1.4% y-o-y; a sharp correction from the 0.2% growth registered in 2016. Further strong production growth around 1.8% is expected for 2018, with the US and EU being the largest contributors to that growth.

Since structural changes in Russian economy began in the 1990's, the dairy sector has struggled for decades with insufficient financing for modernization and replacement of local dual purpose (milk and beef) cattle with highly productive dairy breeds. Russian milk farms depended on state subsidies rather than consumer demand and did not generate profits for decades. Thus, Russia's milk production sector remains far less modernized and consolidated compared to pork, poultry, sugar, and grains. The key weakness of Russia's milk production sector is its inefficiency, but the high cost of capital has long constrained development; over time these factors resulted in high milk production costs in Russia compared to the countries that export processed dairy to Russia. As a result, the markets for raw milk and processed dairy products remain strongly dependent on the price of imports. The share of imported processed dairy from Belarus and other non-restricted suppliers remains high because the total capacity of all Russia's milk farms remains below the country's demand.

For the first time in at least a decade in Russia, milk production was more profitable than poultry or grain production in 2017. Global high prices for milkfat made milk and dairy produced in Russia price competitive to imports. Milk remains dependent on imports so further growth of industrial milk production is possible and could come at the expense of imports. However, world market experts anticipate some decline of world butter prices in 2018, which would affect forecasts. Per cow yields at commercial farms continues growing. The share of industrially processed milk is increasing at the expense of shrinking on farm consumption of fluid milk. The top 50 biggest farms, which currently account for 4.8% of total milk production in Russia, will continue to grow and increase their share in the market. Leading commercial farms benefit from replacing the local dual-purpose breeds with highly productive modern dairy cattle. However, the existing national regulation system of breeding operations is structurally inherited from the soviet times, and constrains the development of the industry.

The milking herd in Russia is forecasted to decrease 2.8% y-o-y to 6.8 million head in 2018 due to low investment in cattle in the past two years, down from 7.0 million head reported in

2017. Russia's milk production totalled 30.6 million tons in 2017, up 0.3% y-o-y. Milk production in 2018 is forecasted at almost the same level, only 0.2% less than in 2017, declining less than cow herd thanks to large farms improve per cow yields. Commercial dairies are expected to increase milk production in 2018, while backyard farms continue to decrease the output. Backyards have been reducing productivity by 2.5-3% each year over the last decade; however, the total raw milk supply in Russia has stabilized at the level of 30.5-30.6 million tons due to improvements in per cow yields by commercial farms. Cows in backyard farms average annual 3.5 tons yield compared to the average yield in the commercial sector of annual 5.7 tons per cow in 2017 (up 5.2% y-o-y). Private household still contribute large share in total raw milk supply in Russia, a 44% of total in 2017.

Wholesale prices for raw milk in RUB in 2017 were on average 14% higher y-o-y. If calculated in US dollars, the prices were 35% percent higher, due to rouble appreciation. High world prices on milkfat were the main reason for growth of commodity prices on raw milk in Russia.

Higher dairy prices may ease the impact of uncertain state support. The major concern of milk producers in Russia is the uncertainty with the traditional "per one liter" subsidies in the budget for 2018. "Subsidies for increase of dairy cattle productivity" remained the only dairy sector specific program in 2017, and replaced the "subsidies per one kg of milk sold for processing". The federal government allocated 7,964 million Russian rubles (c. EUR 120.8 million) specifically for dairy sector under this program in 2017. The amended program continued to subsidize each kg of milk sold for processing in 2017, but the rules for the farms to qualify for the subsidies have been changed.

On the trade barriers on Russian dairy market, on June 30, 2017, President Putin signed decree No. 293 extending Russia's ban on the import of agricultural products (including milk and dairy) from the countries that applied economic sanctions against Russia. The market remains favorable for domestic dairy processors as the counter-sanctions trade restrictions on significant western exporters have been extended until December 31, 2018.

In Ukraine, fluid milk production decreased in 2017 and is expected to remain on a slight downward trend in 2018. Ukraine lost a significant cheese export market in Russia in 2014 and since than the domestic market was unable to absorb additional quantities of cheese or alternative dairy products. In 2016-17, Ukrainian consumers were unable to sustain existing dairy product consumption levels due to the on-going economic and political crisis.

2017 milk output in Ukraine reached 10.3 million tons, down 0.5% y-o-y due to decreased demand from the processors in 2014-16. Milk production responds to market signals with significant lag. Availability of new export markets for Ukrainian butter and dry milk products in 2017 positively impacted the milk production in the country and could be a factor of its further growth in the current year.

Ukraine's milking cows headcount declined by 3.2% to 2.1 million heads in 2017, while average yields improved by 6.4% y-o-y to 5.6 tons annual thus supporting only slight overall raw milk production decline. The favorable world dairy market prices observed in 2017 partially alleviated the production decline, inspiring some investments into industrial milk production. Households also slowed down their animal number contraction. However, the combined impact of these investments is not sufficient to reverse the overall production decline. Over 65% of raw milk is produced in households and this situation is unlikely to change significantly unless changes in government support of the industry. Simultaneously, Ukrainian processors are increasing the share of industrially processed milk. In 2017, it reached 60% of total fluid milk purchases, in comparison to 52% in 2014.

In 2018, Ukraine's government plans to allocate UAH 4 billion (c. EUR 133 million) in state budget for dairy industry support, including new dairy farms construction through credit refund and construction costs compensation; a 1,500 Hryvnia per cow annual support for existing farms; 50% value refund for the cattle purchase; 20% value refund for the newly purchased agricultural equipment. In 2017, state budget support for dairy totaled UAH 170 million (EUR 5.66 million).

In 2017, the exchange rate in Ukraine lost its dominating influence on milk and dairy product production and trade. The industry is slowly recovering from the vast currency devaluation of 2014-16. The exchange rate remained almost stable throughout 2017. Producers benefit from reduced uncertainty over exchange rates, currency regulations, finance availability (including foreign investments), domestic prices, and stable demand, as well as uninterrupted imports of inputs. Simultaneously, Ukrainian producers lost their competitive advantage in the form of shrinking costs that are fixed in local currency.

Ukrainian milk producers and processors concentrated on the domestic market and actively searched for new foreign markets for their value-added dairy products in 2017. The country was able to respond to high world market dairy prices by slightly increased processing activity and re-direction of selected dairy products from the domestic market to foreign markets. The industry was slow to react to price fluctuations due to the significant momentum associated with current animal productivity levels and inability to increase milk production rapidly. However, high world market butter prices inspired exporters which pushed Ukraine into the top 15 butter exporters.

Ukraine's increased state support of the industry in 2018 should positively affect raw milk production if actively utilized. However, lack of investments due to still vulnerable macroeconomic environment may constrain production growth.

According to USDA, raw milk production in Ukraine is expected to decrease further 0.5% y-o-y in 2018 to 10.25 million tons. Ukraine will continue to export dried milk products and butter to utilize excess milk supply. Industry's efficiency will be improving due to increased investments in industrial milk production.

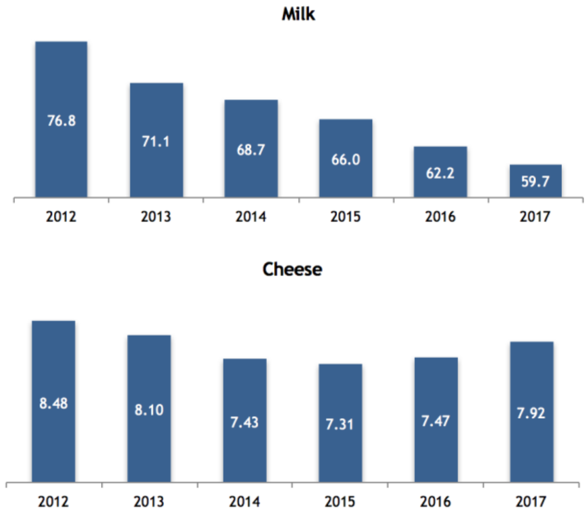
Milkiland defines its home market as former Soviet Union region, namely Russia and Ukraine. This is one of the largest food markets globally, ranking No.5 after China, EU, USA, and India, and a very dynamic one with strong growth fundamentals. Starting from 2013, upon launching of Ostrowia operations, the Group is also active in the Polish and EU market.

While per capita consumption of dairy products in Russia and Ukraine is significantly lower than in the developed EU countries, there are a lot of opportunities for using local competence to develop in these countries.

From the macroeconomic perspective, 2017 became a period of further macroeconomic stabilisation started in 2016. In particular, real GDP of Ukraine in 2017 grew by 2.5% y-o-y on the back of stronger performance of agri-sector and restoration of global prices for steel, while Russian GDP grew by 1.5% on y-o-y basis fuelled by growing adding value in the processing sectors of the economy. The inflation rate in Ukraine and Russia in 2017 stood at 13.7% and historically low 2.5%, respectively in comparison with 12.4% and 7.3% in 2016, respectively. The real income of the Ukrainian population was almost flat (0.2% of growth y-o-y), Russians even faced a decline of this rate by 1.7% in comparison with 2016, thus triggering the further stagnation of the consumer markets of these countries.

In Russia, the Dairy market is dominated by two categories, Cheese and Milk, which constitute over 60% of the Russian market by value. The third-largest product category, Yoghurt, accounts for another 20% of the market. After Russian authorities introduced a ban on dairy imports from the EU and Ukraine in mid-2014, per capita consumption of dairy products shrunk considerably limited by the supply and continued decline throughout 2015. In 2016-17, Russian consumer diets changed towards cheaper dairy products, causing per capita consumption of dairy products to increase notwithstanding lower disposable incomes.

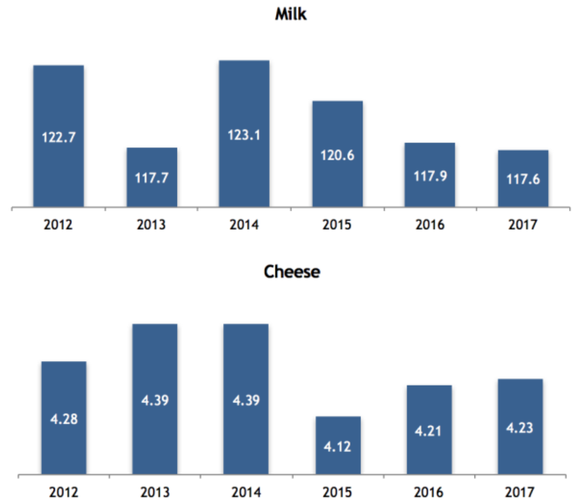
**Per capita consumption of dairy in Russia, kg**




*Source: http://www.clal.it*

In Ukraine, drinking milk represents about half of the total dairy products consumption. Only about 40% of total raw milk produced went into processing in 2017 (flat y-o-y). Cheese and butter represent another 28% of the total dairy consumption. In 2017, following a considerable drop in the consumer purchasing power, consumers continued switch to cheaper locally produced varieties, while the general dairy consumption remained stable in Ukraine.

**Per capita consumption of dairy in Ukraine, kg**




*Source: http://www.clal.it*

Milkiland is active in all main segments of the dairy market. Contrary to many players focusing on a certain market segment, the Group welcomes diversification, as additional flexibility across the product lines helps to manage prices fluctuation, both in raw materials and end products.

The Group allocates its product portfolio into three main groups based mainly on consumer base, marketing and logistics:

- Whole milk product group (white palette) includes all types of packaged fresh dairy with relatively short shelf life;
- Cheese and butter group (yellow palette) are in general longer shelf life consumer products that could be sold in package, or repackaged in retail outlets, or by weight;
- Ingredients are mainly B2B dairy products sold in bulk such as skimmed milk powder, full cream powder, dry whey, permeate, etc. Also, this segment included agricultural products of Milkiland's farms sold to third parties.

Milkiland's core strategic product groups for markets of its presence are whole milk products and cheese, where the Group sees the most significant growth potential. Milkiland considers butter and dry milk products as the basement for its export operations, including the admission to new export markets.

## Whole Milk Products Segment

Whole milk is the largest and the most diverse dairy segment in the CIS region. It includes a variety of products such as drinking milk and highly popular cultured products (sour cream, kefir, ryazhenka etc.), and also curd based snacks (tvorog, curd desserts etc.). Yoghurts are a relatively new product to the market, but their consumption has been developing.

From the market perspective, 2017 was a challenging year for the Ukrainian whole milk producers. Declining consumer purchasing power and a conflict in the Eastern Ukraine, as well as annexation of Crimea in spring 2014 led to a continuous reduction in demand for dairy products throughout 2015-17. Industry statistics showed that Ukrainian market for drinking milk solely showed an increase of 2% y-o-y to 0.95 million tons in 2017. Production of tvorog and other curd desserts totalled 67,000 tons, down c.4% y-o-y, while yoghurt, sour cream and other whole milk products (kefir, ryazhenka etc.) volumes shrank almost 3% y-o-y to 406,000 tons in 2017.

On the supply side, raw milk prices grew by c. 36% y-o-y in Hryvnia terms as a response to higher input prices correlated with international soft commodities markets caused by the Ukrainian Hryvnia devaluation. The unusually high demand for raw milk in autumn 2016 and further high demand on international butter market favouring Ukrainian export of this product caused Ukraine's price for raw milk purchased by industrial processors skyrocket throughout 2017 and average 7,500 UAH per ton of milk net of VAT for the year.

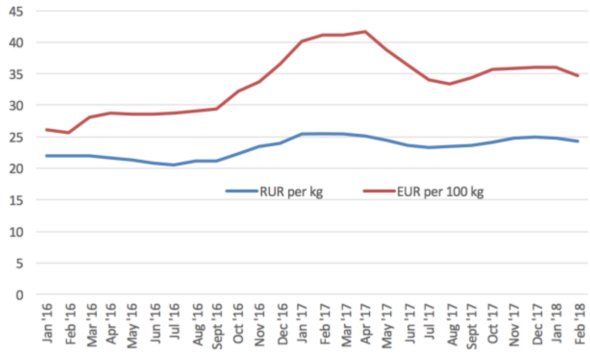
In Russia, restrictions introduced by Russian authorities on food products imported from a number of countries, including the EU and Ukraine, contributed to higher demand for locally produced food products. Nevertheless, the decline in disposable income caused consumer demand for all dairy products to decrease in Russia in 2017.

For the first time in the last five years the production of whole milk products (WMP) in Russia in 2017 declined c.1.0% y-o-y to about 11.8 million tons. In particular, drinking milk and tvorog output both fell by 1.5% y-o-y and other whole milk products, such as sour cream, yoghurt etc. fell by 1.0%. At the same time, the freed supply of raw milk on the market were processed into piling up dairy stocks in butter, cheese and skimmed milk powder, that could be stored longer than WMP with a short shelf life of maximum two weeks.

Even with trade barriers imposed against imported dairy, in 2017 Russia remained the importer of whole milk products. In raw milk equivalent the country imported about 13% of overall dairy products. Belarus delivered 90% of overall whole milk products import to Russia in 2017 while overall country's whole milk products import continued declining (-5% y-o-y) in 2017.

On the supply side, prices for raw milk in Russia grew on average by over 12% y-o-y in Rouble terms to 24,520 RUB per ton net of VAT in 2017. Thanks to Russian Rouble appreciation against Euro in 2017, the country's raw milk price grew 26% y-o-y in Euro terms to 373.5 Euro per ton in 2017.

**Russia's commodity prices for raw milk in 2016-18, net of VAT**




Source: Rosstat, CLAL

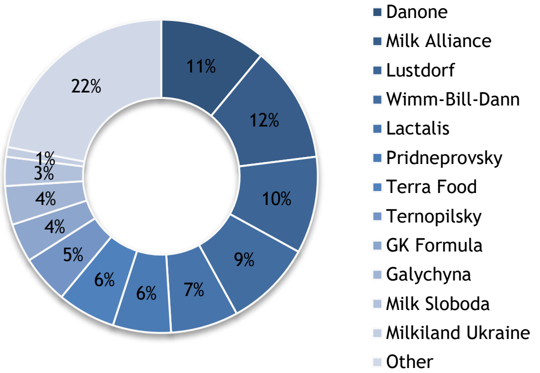
Russian embargo also created additional pressure on the local EU market where the raw milk price dropped since late 2014, as additional volumes of milk became available for processing. However, strict subsidizing and production volume controls in EU-countries finally resulted in industry restructuring and turned raw milk price trend into positive territory in 2016-17. In Poland, the average effective raw milk price grew 25% on average in 2017 and continued increasing 9% in first quarter 2018.

The Group's total 2017 whole-milk products volume sales decreased by 26% on the back of decline of those products sales in Ukraine and Russia, also due to reorientation to high value-added products production and sales.

The Group's subsidiaries in Russia benefitted from import substitution, retained its strong market share in the WMP segment. Ostankino accounted for over 3% of WMP segment sales and proved its TOP-8 player position in this segment of Russian dairy market with the solid presence in national retail chains. Ostankino Dairy is also No.3 player in Moscow city market, the largest regional market consuming over 1.5 million tons of fresh dairy annually.

In Ukraine, the Group retained its positions of a TOP-14 player in the segment with the market share of c.1% (down 0.9pp y-o-y) in 2017.

**Ukraine's whole milk products market by company in 2017, volume terms, %**

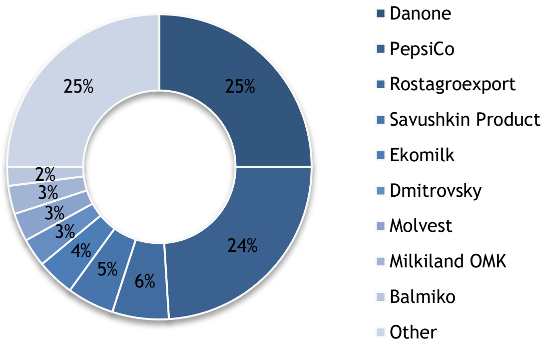



Because of a decline of the Group's output in the segment but still higher y-o-y average prices, the Group's total revenues in the fresh dairy segment declined by c. 10% and amounted to EUR 73.2 million in 2017. The segment's EBITDA skyrocketed 227% y-o-y to EUR 5.4 million mainly thanks to improved segment EBITDA on the Group's Ostankino subsidiary in Russia. The segment's 2017 EBITDA margin increased by 5.4 pp y-o-y to 7.4%.

The share of fresh dairy in the Group's 2017 consolidated revenues stood at 52%, 4 pp. less than in 2016.

Whole milk dairy segment remains Milkiland's strong strategic priority, as the Group sees high growth potential here.

**Russia's whole milk products market by company in 2017, value terms, %**




Milkiland's management believes, that the continuation of the economic growth in the key markets of Ukraine and Russia expected in 2018, will lead to growing demand for WMP products.

Also, according to the Company's estimations, c.40% of fresh dairy consumption in its core markets still falls to home-made products. Such informal consumption will diminish in favour of industrially processed dairy, thus being significant additional growth driver for the Group's business.

The Group believes that it has good assets in right places both in Russia and Ukraine to capitalize on these trends. Ostankino is uniquely located to serve Moscow population with fresh short shelf life dairy. Milkiland's Ukrainian whole milk plants are also favourably positioned nearby large cities such as Kyiv, Kharkiv, Sumy, Lviv, Dnepr and Kryvyi Rig.

## Cheese and Butter Segment

Cheese is the second-largest dairy market in the CIS after whole milk products.

In Russia, the food embargo hit the supply of cheese harder than any other dairy category. Disrupted supplies of cheese from the EU resulted in a spike in cheese prices and empty shelves in September-October of 2014. The Russian industry has gained sufficient capacity to fill the shelves in the economy product category after three years of counter-sanctions trade restrictions. Local products started replacing Belarusian imports; however, Russian products in the premium group still can't compete with quality European-made cheese. Consumer purchasing power is anticipated to recover in the current year, thus the demand for quality cheese will encourage imports in 2018.

Current trends, such as growing supply of raw milk for processing from commercial dairies, and forecasted increase of cheese consumption, are shaping a favourable outlook for cheese in 2018. Both trends encourage increase of cheese production, as additional raw milk will be available for cheese.

Some of produced cheese volumes were not absorbed by the market and formed quite large ending stocks, which stood at 64,000 tons (excluding "tvorog"), as of end-2017, the 86% above the 5-year average. These stocks will be consumed in the current year on the back of growing consumption of cheese in Russia.

In 2017, cheese market in Russia continued to be constrained by supply, as trade restrictions imposed by government on the EU and Ukrainian producers cut imports, while local cheese production however was reviving. As a result, the total Russian cheese consumption increased by c. 6% y-o-y to approximately 1.14 million tons (*source: FAS-USDA estimations*) and is expected to increase further by 0.9% y-o-y, to 1.15 million tons in 2018 despite expected price growth on dairy products in Russia.

Cheese production increased 7% y-o-y to 925,000 tons in 2017 as a result of processing the spare raw milk volumes in the market freed from lower demand for whole milk products.

Russian government authorities forecast 935,000 tons of cheese and curd production in 2018, 1% growth from the revised production estimate of 2017 on the back of reviving consumer demand.

Multiple trends from the current market will likely remain in 2018, including weak consumer demand for premium high-margin cheese and strong competition from non-banned exporters in the market. Additionally, higher prices on quality raw milk suitable for cheese production are expected to constrain the growth of cheese sector. Stable supplies of recognizable cheese and tvorog brands from reputable producers and further expansion of private labels will contribute to the anticipated growth of cheese consumption in Russia in 2018.

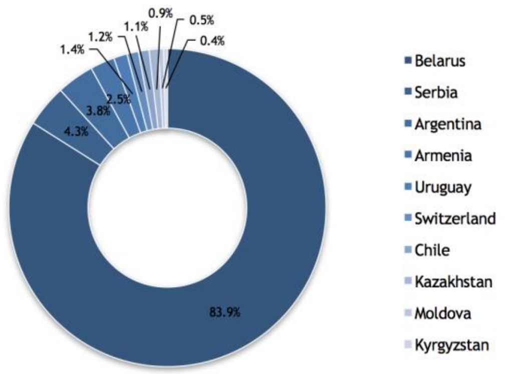
Further growth may be seen after significant recovery of the purchasing power of households, when the consumer interest shifts back to the premium and middle product categories. The macroeconomic forecasts available to date anticipate further GDP recovery by 1.8% y-o-y in 2018 (compared to 1.7% growth seen in 2017), likely followed by growth in disposable income in Russia, so the market will remain balanced with cheese supplies comparable to 2017 when large cheese stocks were formed.

As Rosstat reported in September 2017, average producer prices for hard cheese increased 8% from RUB 376,348 per ton in January 2017 to RUB 408,272 per ton in September 2017; meanwhile butter prices declined 2% during the same period. Prices on 'tvorog', which was a dairy product of choice for Russian consumers during the crisis, were on average two times less than prices for other cheeses in 2017, also increased c.8% y-o-y during nine months of 2017. The cheese market is balancing near its saturation, and manufacturers are switching their focus to quality of their products and efficiency of operations to maintain sales.

Despite stabilization of cheese supplies in the medium and economy market segments in Russia, there is no adequate replacement of premium imported cheeses. Local producers were not able to fill in the segment of premium cheeses, and consumers continue to prefer the less expensive grocery items within product groups. As a result, the middle price range varieties of cheese remain the bestselling hard and semi-hard cheeses and are increasing their share in the market. "Rossiysky" is the most popular variety of cheese, with over 60% share of total consumption.

Imports of cheese to Russia covered primarily by Belarus (84% of total) remained flat y-o-y in 2017 at 223,000 tons and accounted for c. 20% of total consumption. All the key cheese exporters, who could influence the Russian cheese market, remain excluded from competition until the end of 2018 due to the extended counter-sanctions ban. Assuming the current restrictions remain unchanged, Belarus cheese exporters will remain the major supplier and will likely maintain the volume of cheese and curd shipments to Russia.

**Import of cheese to Russia by top-10 exporters in 2017, volume terms**



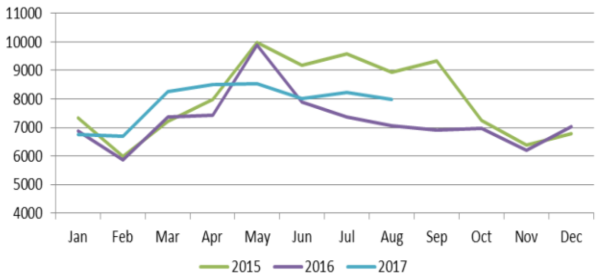

Source: Rosstat, CLAL

Once very attractive for Ukrainian processors due to availability of the Russian market, the hard cheese market is now hardly one third of what it used to be in Ukraine. Producers concentrated on the domestic market and few remaining traditional markets. Being relatively high value added products, domestic cheese consumption suffered from the economic crisis of 2013-16. However, domestic consumers changed their diets towards cheaper locally produced cheeses (e.g. cheese-like products and processed cheese) resulting in overall cheese production and consumption volume growth over 2017. Meanwhile, Ukrainian processors diverted excess milk supplies to butter and non-fat dried product to benefit from the high world market price situation.

In Ukraine, per capita cheese consumption recovered in 2017 (+0.5% y-o-y, to 4.23 kg). According to State Statistics Service of Ukraine, the total domestic production of hard and processed cheese in total increased by c.6% y-o-y to 120,000 tons in 2017 while production of traditionally popular tvorog (soft cheese) declined by almost 4% y-o-y to 67,200 tons in 2017.

Facing a shrinking supply of raw fluid milk, Ukrainian processors make their production decisions based on profitability of dairy products. Hard cheese was not a winner in 2017. The Russian market closure limited sales to export markets. Economic and political crisis pushed demand to the lower market segment with even slimmer margins. Slow economic recovery of 2016-17 did not help cheese producers as many middle-class consumers turned towards cheaper dairy products including cheese-like products. As a result of the prolonged crisis, production of hard cheese further declined.

**Ukraine's hard cheese monthly output in 2015-August 17, tons**

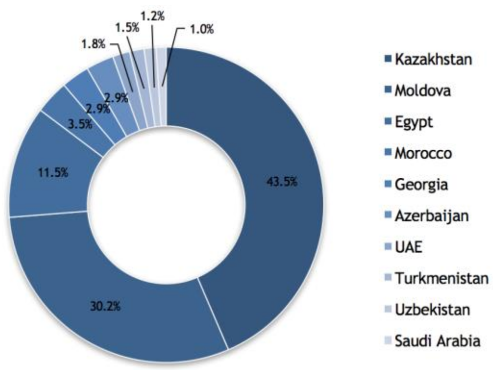



Source: State Statistics Service of Ukraine

The Russian cheese market closure in 2014 had significant impact on Ukrainian dairy market and export of dairy. Ukrainian milk producers continued to decrease cattle headcount, but despite the contraction, raw milk excess supplies remained in place in 2014-17. This additional milk was redirected to production of butter and dried milk for export markets. Ukrainian processors intensified their search for new markets demanding higher quality and cheaper milk from domestic producers.

Exports of cheese from Ukraine totaled only c. 9,100 tons in 2017, up 12% y-o-y on favorable contracts with Kazakhstan, Egypt, Morocco and Georgia. Ukraine's exports of cheese to UAE, Turkmenistan and Uzbekistan also increased over 50% y-o-y in 2017 in volume terms. Export of cheese from Ukraine accounted for 7.6% of total output in 2017 (up 0.4pp y-o-y). Ukrainian exports now go into two groups of countries: EU and Former Soviet Union countries that import predominately butter, cheese and whole dairy products, and Asian and African importers of Ukrainian dried milk.

**Export of cheese from Ukraine by top-10 importers in 2017, volume terms**

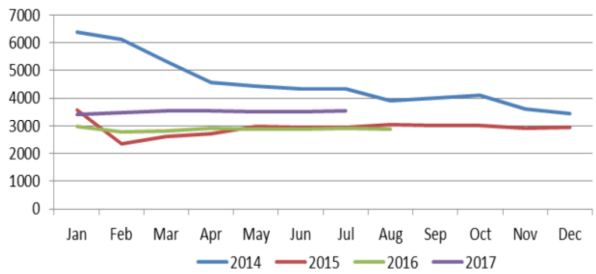



Source: State Statistics Service of Ukraine, CLAL

Imports of hard cheese from Poland for the middle-income market segment, and Germany, Netherlands and Italy for upper income consumers increased significantly by 41% y-o-y to total 10,000 tons in 2017. In 2017, Poland remained the major exporter with almost 50% market share as the hard cheese market started to recover. Import accounted for 8.3% of total cheese consumption in Ukraine in 2017.

Despite weak domestic demand, cheese manufacturers in Ukraine had to compete for more expensive raw milk with the rest of the processing industry. The higher prices did not facilitate the sector's much needed domestic consumption increase. The average cheese price in Ukraine boosted 22% y-o-y in Hryvnia terms in 2017 and increased slightly less in dollar terms due to continued depreciation of hryvnia over the year.

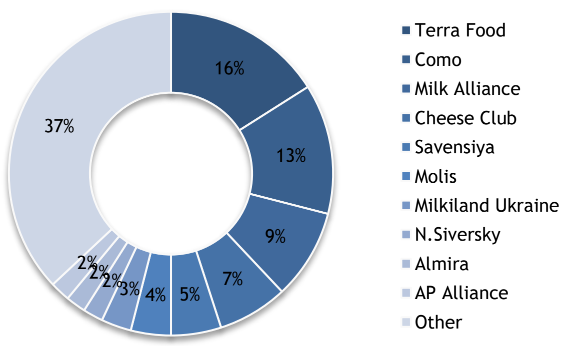
**Ukraine's hard cheese wholesale price in 2014-17, $/ton net of VAT**




Source: State Statistics Service of Ukraine

In 2017, the Group experienced an overall drop in the cheese sales in volume terms by c. 27% on y-o-y basis that was triggered by the decline in cheese sales both in Russia and Ukraine. In order partly to offset this decline, the Group concentrated on finding new markets for cheese exports. As the result, the Group's export subsidiary Milkiland Intermarket managed to increase the volume of cheese sales by 44% on y-o-y basis to c. 5.5 thousand tons. The Group remained the Top-10 cheese producer in Ukraine and in Top-15 cheese producer in Russia in 2017.

**Ukraine's cheese market by company in 2017, volume terms, %**




In butter market, Russia increased its output by 6.5% y-o-y to 262,000 tons in 2017 but anticipates a minor decline (-0.8% y-o-y) in production in 2018 to 260,000 tons. Russia currently produces approximately 72% of the milkfat it consumes, and world prices for milkfat continue influencing the market despite the trade restrictions. Producer margins in Russia strongly depend on the prices of imports: expensive imports push the wholesale butter prices up, and consequently, producer's margins increase. Good margins encouraged producers to increase output in 2017, but now butter supply has grown to a level that the current market is struggling to absorb. The market was favorable for butter producers since the last quarter of 2016 throughout 2017, when prices for milk fat, and therefore the margins from butter sales, increased after a spike in world prices. Butter stocks were 23,000 tons as of end-2017, a record high at 21% more than the 5-year average. High stocks will press on the market and constrain production growth in 2018.

Average producer prices for butter in Russia grew far above the inflation level or above 5% y-o-y, during the three quarters of 2017, but declined m-o-m in September 2017. A decline in the price of butter in the end of the "high milk season" is unusual for Russia, and indicated that the market was saturated. The average producer price was 310,271 rouble per ton in September 2017, which was down 2% from the beginning of the year.

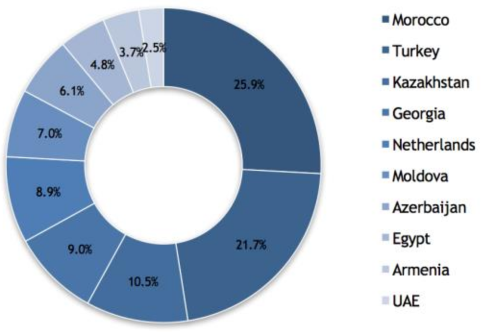
Due to the current import ban of dairy products from a number of Western suppliers and some effective control over illegal imports from FSU countries, Russia's imports of butter was estimated at 99,000 tons (-7% y-o-y). Belarus accounted for 71% of total butter import to Russia.

Russian government authorities forecast butter consumption recovery to the pre-2015 crisis level of 377,000 tons in 2018, following the 4.4% increase in consumption in 2017. After two years of volatile prices and inconsistent supply of butter, increased domestic production contribute to the recovery of butter consumption in the country.

In Ukraine, butter was one of the most traded products in 2017 due to unusually high export prices. Some processors diverted their raw milk supplies to butter, away from cheese and other products. However, production increase was not significant due to short fluid milk supplies. Increased exports increased the domestic price for butter. Due to high domestic market prices (+28% y-o-y in Hryvnia terms on average in 2017), some Ukrainian consumers were unable to afford butter and switched to margarine and vegetable oils. As such, exports were fueled by both production increase and domestic consumption decrease (-7.5% y-o-y in 2017). New exports put Ukraine in the top 15 world butter exporters.

Ukraine's exports of butter reached 30,000 tons in 2017, skyrocketing 150% over the year.

**Export of butter from Ukraine by top-10 importers in 2017, volume terms**




Source: State Statistics Service of Ukraine, CLAL

Ukraine's domestic butter output increased by 6.2% y-o-y in 2017, to 108,000 tons on the back of increased international demand.

In 2017, Milkiland's cheese & butter segment revenues declined by 10% y-o-y to EUR 42.2 million mainly depressed by national currency devaluation in Ukraine. The segment's EBITDA was practically flat on y-o-y basis and stood at c. EUR 3.8 million. EBITDA margin improved from 8.1% in 2016 to 8.9% in 2017 due to bigger contribution of more profitable Russian market and increased butter exports.

Cheese & butter segment accounted for 30% of the Group's overall 2017 revenues, down 2pp y-o-y. The Group's export subsidiary Milkiland Intermarket boosted 2017 butter exports by more than two times on y-o-y basis in volume terms and more than quadrupled in value terms thanks to favourable international market demand.

The Group's management will continue putting their efforts on the improving profitability of the cheese&butter segment by focusing on local markets and gaining a market share on the profitable Russian market. In Ukraine Milkiland offers higher value-added mould and ripe cheese to substitute the imported expensive cheese, which became less affordable for the Ukrainian consumers after the sharp devaluation.

Polish Ostrowia will focus on the development of the distribution network in the local Polish market until the Russian market is closed for the EU producers and also searching for new export opportunities in EU market.

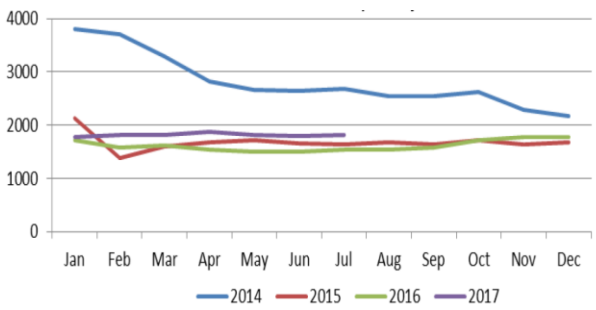
## Ingredients Segment

The Group's strategy of diversification and close integration with raw milk suppliers presumes presence in other dairy categories, such as dry milk products. This category includes skimmed milk powder (SMP), whole milk powder (WMP) and other B2B products made from whey (WPC-80 and permeate). Milkiland's sales in these categories may vary significantly from year to year, depending on global commodity prices for dry milk products. Usually, Milkiland uses high season of raw milk surplus to dry milk in order to sell it throughout the year.

Production of skimmed milk powder is closely tied to butter production. Increased demand for butter resulted in a SMP production increase. SMP remains to be one of the major exportable commodities with multiple diversified markets in Asia and Africa where Ukrainian SMP price is the major competitive advantage and maintains production levels.

The SMP export price reported in Ukraine increased in 2017 y-o-y, but the margin is much smaller compared to that of butter. The domestic market for SMP in Ukraine reflected the world market situation where significant SMP quantities in stocks depressed prices. Ukrainian processors have little ability to store SMP and the Ukrainian government does not regulate the dairy market with SMP procurement programs. All Ukrainian products are likely to be exported or consumed domestically the same year they are produced.

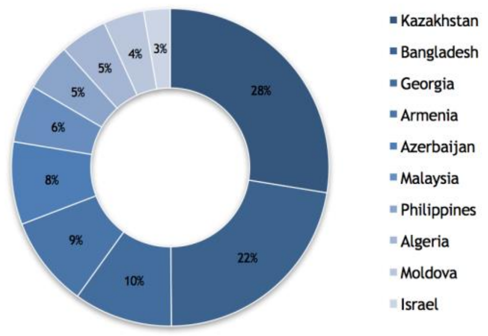
**Ukraine's dried milk wholesale price in 2014-17, $/ton net of VAT**




Source: State Statistics Service of Ukraine

In 2017, Ukraine's export of SMP reached 29,000 tons (down c.15% y-o-y) while exports of WMP almost doubled compared to 2016 and totalled 3,900 tons for the year. Ukraine's overall SMP output reached 52,000 tons in 2017 (-3.7% y-o-y). Kazakhstan, Bangladesh and Georgia accounted for 60% of Ukrainian SMP export volumes in 2017, with Kazakhstan being the largest importer with 28% share in total. Israel, Algeria and Armenia absorbed almost 63% of Ukraine's total WMP export volume in 2017, with Israel import of WMP from Ukraine leapt by almost 4 times y-o-y.

**Export of SMP from Ukraine by top-10 importers in 2017, volume terms**




Source: State Statistics Service of Ukraine, CLAL

In Russia, without state support in 2017, local producers of milk powders had no incentives to increase output because prices for milk powders were growing slower than producers' expenses. Thus, Russia remained the net importer of SMP and WMP. To reduce the dependence of the Russian dry milk market from imports, local producers invested to production increase in 2017.

According to Rosstat, 2017 production of milk powders increased: WMP by 45% y-o-y to 61,000 tons and SMP by 14% y-o-y to 72,000 tons. The export of both commodities remained at minor level.

Russia's 2017 SMP imports totaled 123,000 tons, down 9.6% y-o-y while WMP imports reached 49,000 tons (flat y-o-y) over the year.

The global downturn in dairy markets resulted in a margin squeeze for many international producers. Although, the devaluation of the national currency generally increased the profitability of export sales for Ukraine, continuous stagnation of prices for international dry milk products for two years in a row depressed rapid export growth of such from Ukraine in 2016-17 showing weak signs of recovery in 2017 in line with global SMP price rise.

In 2017, the Group's subsidiaries, Milkiland Ukraine and Milkiland Intermarket increased SMP sales by more than 40%.

As the result, Milkiland's revenues in Ingredients segment boosted by 35% on y-o-y basis and amounted to EUR 24.9 million. Segments EBITDA stood at EUR 1.08 million, representing 4.3% EBITDA margin (up 4.6% y-o-y and -1.2pp y-o-y, respectively).

## Financial Performance and Financial Position

The Table below provides selected financial data as of and for the twelve months ended 31 December 2017 and 2016 in thousand Euro.

**Selected financial data**

| | 2017 | 2016 |
|---|---|---|
| I. Revenues | 140,411 | 146,758 |
| II. Operating profit | 588 | (5,495) |
| III. Profit before tax | (7,242) | (36,724) |
| IV. Net profit | (7,346) | (38,906) |
| | | |
| V. Cash flows provided by operating activities | 10,996 | 9,540 |
| VI. Cash flows used in investing activities | (2,811) | (2,315) |
| VII. Cash flows provided by financing activities | (7,924) | (7,102) |
| VIII. Total net cash flow | 261 | 123 |
| | | |
| IX. Total assets | 160,415 | 168,456 |
| X. Current liabilities | 122,859 | 134,548 |
| XI. Non-current liabilities | 24,634 | 26,994 |
| XII. Share capital | 3,125 | 3,125 |
| XIII. Total equity | 12,922 | 6,914 |
| | | |
| XIV. Weighted average number of shares | 31,250 | 31,250 |
| XV. Profit (loss) per ordinary share, EUR cents | (24.55) | (124.17) |

## Income Statement

**Summary statement of comprehensive income, '000 EUR**

| | 2017 | 2016 |
|---|---|---|
| Revenue | 140,411 | 146,758 |
| Change in fair value of biological assets | 269 | (52) |
| Cost of sales | (116,988) | (125,592) |
| **Gross profit** | 23,692 | 21,114 |
| Operating income (expense), net | (23,104) | (26,609) |
| **Operating profit** | 588 | (5,495) |
| Net finance expense and other non-operating income/(expense) | (7,830) | (31,229) |
| Profit/(loss) before tax | (7,242) | (36,724) |
| Income tax (expense)/benefit | (104) | (2,182) |
| **Net profit/(loss)** | **(7,346)** | **(38,906)** |
| Other comprehensive income/(loss) | 13,354 | 9,879 |
| **Total comprehensive income** | **6,008** | **(29,027)** |
| **Net profit/(loss) attributable to equity holders of the parent company** | **(7,672)** | **(38,804)** |
| Weighted average number of shares (in millions), as of December 31 | 31,250 | 31,250 |
| **Earnings per share, basic and diluted (EUR cents)** | **(24.55)** | **(124.17)** |

***Revenue***

The challenges triggered by still stagnated consumer demand in the Group's key operational markets, as well as the Company's efforts aimed at reshuffling its product portfolio towards high value generated products, put pressure on the Group's revenues in 2017. As the result, the Group's revenues declined by c. 4% to c. EUR 140 million.

The Group focused on development of sales on key operational markets, as well as effectively reacted to favourable international markets for butter and skimmed milk powder, in particular by increasing exports of those dairy products. Thus, the share of Ingredients segment which includes sales of skimmed milk powder grew 5pp y-o-y to 18% of total Milkiland's revenues in 2017.

The table below sets forth an overview of the revenue generated by the Group in 2016 and 2017 by product segments.

**Breakdown of the Group's consolidated revenue by product in 2017-2016**

| | 2017 | | 2016 | | 2017 vs. 2016 | |
|---|---|---|---|---|---|---|
| | Revenue ('000 EUR) | Share in total (%) | Revenue ('000 EUR) | Share in total (%) | '000 EUR | % |
| Cheese & butter | 42,247 | 30% | 46,660 | 32% | (4,413) | -9% |
| Whole milk products | 73,248 | 52% | 81,567 | 56% | (8,319) | -10% |
| Ingredients and other | 24,916 | 18% | 18,531 | 13% | 6,385 | 34% |
| **Total** | **140,411** | 100% | **146,758** | 100% | **(6,347)** | -4% |

Sales of cheese and butter decreased by 9% y-o-y to EUR 42.2 million, due to the decline in cheese volume sales in key operational markets.

After the import ban for Ukrainian and the EU dairy products implemented by Russian authorities the Group continued facing the restricted access to Russian market for export of its Ukrainian and Polish facilities. This led to reorientation of the cheese sales to local markets, as well as at some extent to other export markets, but with lower margins. In 2017, Milkiland RU, Russian subsidiary of the Group, continued its efforts aimed at further localization of the production and sales of cheese under Milkiland's brands. However, still stagnating local consumer demand both in Ukraine and Russia led to contraction of cheese volume sales and revenues in both countries.

For more information on cheese and butter production and sales, refer section *Key Products, Production and Sales*.

Sales of whole milk products declined 10% y-o-y to EUR 73.2 million on a back of lower volume sales in Ukraine and Russia, local currency devaluation in Ukraine and lower y-o-y consumer demand in Russia. These sales represented 52% of the total consolidated revenue in 2017 vs. approx. 42% in 2012.

Ostankino, the Group's main subsidiary in Russia, experienced decline in revenues in whole milk products segment due to slow recovery of Russian dairy consumption that could not be sufficiently compensated by appreciated local currency against euro (15% y-o-y in EUR terms). This facility holds the position of main revenue contributor of the Group in 2017, delivering about 50% of sales in value terms. The Group's subsidiaries in Ukraine jointly showed the best profitability result among others with 2017 EBITDA margin of 8.8% (+1.4pp y-o-y).

For more information on whole milk production and sales, refer section *Key Products, Production and Sales*.

Sales in the Ingredients segment boosted 34% to EUR 24.9 million thanks to strong demand on the international markets for butter and supportive for SMP. Global prices for these products, in particular, dry milk powder and skimmed milk powder, grew 2-3% y-o-y on average throughout 2017 while butter price skyrocketed 65% y-o-y on average in euro terms, as well as selling volumes increase (+4% y-o-y) also contributed into segment's overall revenue growth.

For more information on Ingredients production and sales, refer section *Key Products, Production and Sales*.

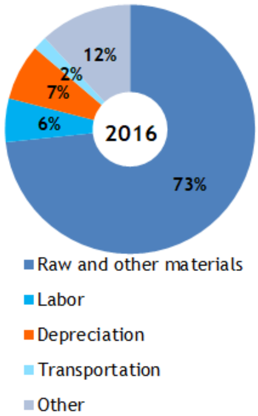
***Cost of sales***

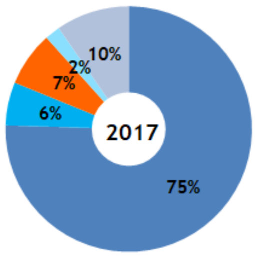
The Group's consolidated cost of sales decreased 7% to EUR 116.9 million; the main driver was 4%-deflated raw materials costs (from EUR 92.1 million to EUR 88.3 million), mainly due to decreased dairy output and milk processing volumes (-16% y-o-y).

While farm-gate raw milk prices in both Russia and Ukraine grew by 14% and 36% in local currency terms respectively, resulted in a c.20% y-o-y increase in euro terms in the average effective price for raw milk for the Group. For more information on milk markets, refer section *Key Products, Production and Sales*.

In 2017, Milkiland continued its downward integration aimed to secure raw milk supplies in Ukraine, including supporting milk cooperatives and developing in-house milk production. The Group continued cooperation with National Milk Cooperative Moloko-Kraina (a nation-wide cooperative that united a number of smaller cooperatives). In-house farming facilities focused on better per cow yields to cut the costs.

**The Group's cost of sales structure in 2016-2017**




In 2017, labour costs dropped by 6% to EUR 6.7 million due to change in local currencies exchange rate to euro, as well as cost cutting at production subsidiaries affected by the cheese exports ban. Social insurance contributions decreased accordingly (-8% y-o-y). Transportation costs were up 4% y-o-y due to increased fuel costs.

**Breakdown of the Group's cost of sales in 2017-2016, '000 EUR**

| | 2017 | | 2016 | |
|---|---|---|---|---|
| | Amount ('000 EUR) | Share in consolidated revenue, % | Amount ('000 EUR) | Share in consolidated revenue, % |
| Raw and other materials | 88,307 | 58.4% | 92,107 | 62.8% |
| Wages and salaries | 6,668 | 4.7% | 7,101 | 4.8% |
| Depreciation | 8,404 | 5.9% | 9,138 | 6.2% |
| Transportation costs | 2,359 | 1.7% | 2,263 | 1.5% |
| Gas | 3,005 | 2.1% | 3,088 | 2.1% |
| Other | 8,245 | 10.4% | 11,895 | 8.1% |
| **Total** | 116,988 | 83.2% | 125,592 | 85.6% |

***Gross profit***

As a result of decreasing top line and even bigger decrease in the costs of sales, Milkiland's gross profit increased by 12% y-o-y to EUR 23.7 million implying the rise of gross profit margin also to 16.9% in 2016 compared to 14.4% in 2016.

***Selling and distribution expense***

The Group's selling and distribution expenses decreased by c. 12% from EUR 13.1 million in 2016 to EUR 11.6 million in 2017 and represented 8.2% in the consolidated revenue in 2017 vs. 8.9% in 2016. Transportation expenses decreased slower than other selling and distribution expenses (-8% y-o-y) due to a rise in fuel prices denominated in the operating currencies. At the same time, labour-intensive costs grew by about 5% y-o-y implying the Group implemented longer awaited slight wages increase. Security and other services declined significantly (-26% y-o-y), as well as marketing and advertising expenses (-94% y-o-y), providing for postponed investment in sales volume growth for the future.

***Administrative expense***

The Group's administrative expenses decreased 6% y-o-y from EUR 13.0 million in 2016 to EUR 12.2 million in 2017, representing 8.7% in the consolidated revenue in 2017 vs. 8.9% in 2016. An 8% increase in labour costs is mainly associated with the operational currencies movements. Social insurance contributions increased by 51% y-o-y alike the wages and salaries trend. All the other costs in administrative expenses, such as representative charges, environmental charges, consulting fees etc. declined significantly over 2017, implying for the Group's costs optimization.

**Other expenses, net**

In 2017, the Group received EUR 0.7 million other operating income compared to EUR 0.5 million other expenses in 2016. Other operating income growth of 54% y-o-y and rental income of EUR o.6 million were the main contributors to the Group's receiving other operating income, net.

**Operating profit and EBITDA**

Optimization in operating costs and higher gross profit resulted in the Group's operating income of EUR 0.6 million and in an 89% boost in the consolidated EBITDA to EUR 10.3 million. EBITDA margin increased from 3.7% to 7.3% in 2017.

***Finance expense***

In 2017, financial expense related to bank borrowings declined 71% as a result of a slight decrease in debt volume (-15% y-o-y), as well as restructuring in loan portfolio and discounting of loans. The devaluation of Ukrainian Hryvnia and appreciation of Russian rouble against euro and US dollar resulted in a non-cash foreign exchange income of EUR 0.7 million in 2017, compared to loss of EUR 22.2 million in 2016.

***Profit before tax and Profit for the year***

As a result of still insufficient operating income to cover financial expenses, the Group recognized a loss before tax of EUR 7.2 million (compared to loss of EUR 36.7 million in 2016). Net loss for 2017 accounted for EUR 7.3 million vs negative result of EUR 38.9 million in 2016.

## Financial Position

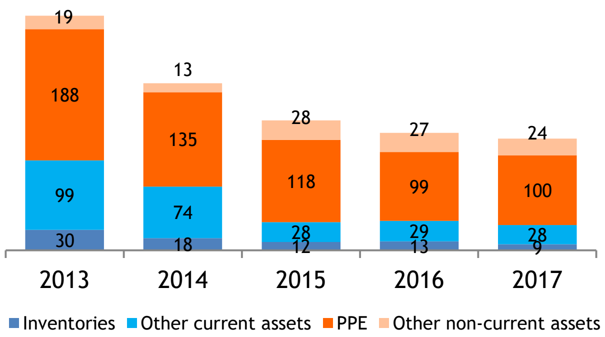
**Summary balance sheet as at December 31, ‘000 EUR**

| | 2017 | 2016 |
|---|---|---|
| Cash and cash equivalents | 1,416 | 1,044 |
| Trade and other receivables | 19,406 | 20,042 |
| Inventories | 8,713 | 12,878 |
| Current biological assets | 1,302 | 1,096 |
| Current income tax assets | 783 | 434 |
| Other taxes receivable | 5,194 | 6,739 |
| ***Total current assets*** | ***36,814*** | ***42,233*** |
| Goodwill | 1,474 | 1,558 |
| PPE | 99,679 | 98,763 |
| Investment property | 16,732 | 19,971 |
| Non-current biological assets | 1,251 | 1,383 |
| Other intangible assets | 1,993 | 2,325 |
| Deferred income tax assets | 2,472 | 2,223 |
| ***Total non-current assets*** | ***123,601*** | ***126,223*** |
| **Total assets** | **160,415** | **168,456** |
| Trade and other payables | 40,778 | 43,054 |
| Current income tax liabilities | 807 | 71 |
| Other taxes payable | 5,474 | 4,130 |
| Short-term loans and borrowings | 75,800 | 87,293 |
| ***Total current liabilities*** | ***122,859*** | ***134,548*** |
| Long-term loans and borrowings | 10,756 | 14,993 |
| Deferred income tax liability | 13,760 | 11,771 |
| Other non-current liabilities | 118 | 230 |
| ***Total non-current liabilities*** | ***24,634*** | ***26,994*** |
| **Total liabilities** | **147,493** | **161,542** |
| Share capital | 3,125 | 3,125 |
| Share premium | 48,687 | 48,687 |
| Revaluation reserve | 79,403 | 69,208 |
| Currency translation reserve | (38,042) | (34,297) |
| Retained earnings | (81,481) | (80,918) |
| ***Total equity attributable to equity holders of the parent company*** | ***11,692*** | ***5,805*** |
| Non-controlling interests | 1,230 | 1,109 |
| **Total equity** | **12,922** | **6,914** |
| **Total liabilities and equity** | **160,415** | **168,456** |

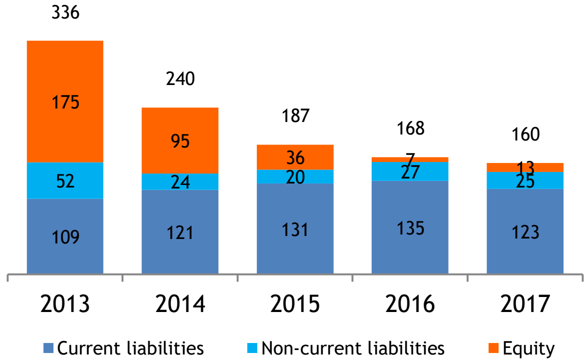
**Capital structure and solvency analysis information**

| | 2017 | 2016 |
|---|---|---|
| Total debt ratio | 0.92 | 0.96 |
| Debt to equity ratio | 11.41 | 23.36 |
| Net debt/EBITDA | 8.28 | 18.60 |
| Net debt/sales | 0.61 | 0.69 |

**Assets structure in 2013-2017, EUR million**




**Equity and liabilities of the Group in 2013-2017, EUR million**




***Assets***

The Group's total assets decreased by 10% from EUR 168.5 million as of December 31, 2016, to EUR 160.4 million as of December 31, 2017.

During 2017 cash and cash equivalents increased from EUR 1.0 million to EUR 1.4 million (+36% y-o-y).

The Group's euro-denominated inventories declined as of end-2017 to EUR 8.7 million (-32% y-o-y). Accounts receivable decreased by 28%, to EUR 9.7 million, over the year. Total trade accounts receivable decreased by 4% to EUR 19.4 million due to increase in other receivables and prepaid interest.

Other taxes receivable comprise mainly export VAT receivable from the Ukrainian government. In 2017, VAT receivable decreased by 22% y-o-y. Although the Group's export sales increased over the year, VAT recoverable payments were partially paid with the rest postponed for 2018.

Non-current assets decreased by 2% to EUR 123.6 million. A natural decline due to the devaluation of Ukrainian Hryvnia was offset by appreciation of Russian rouble and one-off add-on from revaluation of assets of the Group in Ukraine, including investment property, of EUR 17.6 million in 2017.

Current assets represented 23% of the total assets, non-current assets, 77% (75% as on December 31, 2016).

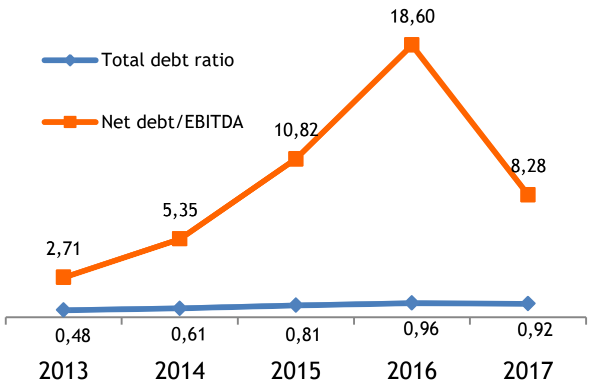
***Liabilities and equity***

The Group's total liabilities decreased by 9% y-o-y, from EUR 161.5 million to EUR 147.5 million as of December 31, 2017. Current liabilities fell 9% to EUR 122.9 million, while non-current liabilities also decreased by 9% to EUR 24.6 million. Such changes in liabilities breakdown were mainly due to repayment of debt (EUR 10.2 million) and foreign exchange gain due to operational currency movement in Ukraine and Russia against euro.

Net debt of the Group stood at EUR 85.1 million as of December 31, 2017. Total Debt Ratio constituted 0.92 vs. 0.96 in 2016. Net Debt/EBITDA ratio decreased from 18.60 to 8.28 thanks to decreased indebtedness and higher euro-denominated EBITDA.

For more information on loans and borrowings contracted by the Group, refer *to the Consolidated Financial Statements* and section *Material Factors and Events*.

**Debt ratios of the Group in 2013-2017**



Currency translation reserve increased over the reported year (EUR -38.7 million on December 31, 2017 vs. EUR -34.3 a year before).

However, the EUR 2.0 million income in retained earnings and an 18% y-o-y increase in revaluation reserve contributed to almost doubling total equity of the Group. This increase in retained earnings is mainly associated with the Group's foreign exchange income due to operational currencies appreciation.

Current liabilities represented 77% of the total equity and liabilities, non-current liabilities 15%, and equity 7% as of December 31, 2017 (80%, 16%, and 3% respectively in 2016).

Decrease in the Group's current assets and increase in short-term loans and borrowings due to reclassification of some debt liabilities of the Group, including the Loan Facility to the Syndicate of banks (for more information please refer *Material Factors and Events),* led to negative Working capital of EUR 86.1 million. At the same time, the Group's cash ratio remained stable at 0.01 in 2017.

The Group's current and quick ratios remained stable, at 0.3 and 0.2 respectively in 2017.

Over 2017 the Group's average operating cycle had changed through increase in average payment period from 98 to 131 days in 2017.

**Balance sheet items and liquidity analysis**

| **Ratios** | **Definitions** | **2017** | **2016** |
|---|---|---|---|
| Production and inventory cycle, days | Average inventory to sales revenue times number of days in the period | 28 | 31 |
| Average collection period, days | Average trade receivable to sales revenue times number of days in the period | 51 | 49 |
| Average payment period, days | Average trade payables to cost of sales times number of days in the period | 131 | 98 |
| Average operating cycle (cash conversion period), days | Total of average production and inventory cycle and average collection period less average payment period | (51) | (18) |
| Working capital, '000 EUR | Current assets less current liabilities | (86,045) | (92,315) |
| Current ratio | Current assets to current liabilities | 0.30 | 0.31 |
| Quick ratio | Current assets less inventories to current liabilities | 0.23 | 0.22 |
| Cash ratio | Cash and cash equivalents to current liabilities | 0.01 | 0.01 |
| ROE, % | | (63%) | (670%) |
| ROA, % | | (20%) | (92%) |

**Summary cash flow statement**

| | 2017 | 2016 |
|---|---|---|
| ***Cash flow from operating activities:*** | | |
| Operating cash flows before working capital changes | 10,168 | 4,938 |
| Changes in assets and liabilities, net | 2,766 | 10,625 |
| Cash provided by (used in) operations: | (1,938) | (6,023) |
| **Net cash from operating activity** | **10,996** | **9,540** |
| | | |
| ***Investing activities:*** | | |
| Proceeds from sale of property, plant and equipment | - | 131 |
| Acquisition of property, plant and equipment | (2,811) | (1,653) |
| Acquisition of subsidiaries, net of cash acquired | | (793) |
| Increase of other non-current assets | - | - |
| **Net cash from investment activity** | **(2,811)** | **(2,315)** |
| | | |
| ***Financing activities:*** | | |
| Acquisition of non-controlling interest | - | - |
| Commission paid | - | (23) |
| Dividends paid | - | - |
| Proceeds from borrowings | 2,298 | 19,495 |
| Repayment of borrowings | (10,222) | (26,574) |
| **Net cash from financial activity** | **(7,924)** | **(7,102)** |
| | | |
| **Net increase in cash** | **261** | **123** |
| Effect of exchange rate changes on cash and cash equivalents | 111 | 14 |
| Cash at beginning of the period | 1,044 | 907 |
| **Cash at the end of the period** | 1,416 | 1,044 |

Net cash at the end of the period increased by 36% to EUR 1.4 million thanks to a positive cash flow from the operating activities. Milkiland relies on cash provided by operating activities as a primary source of liquidity in addition to banking credit financing.

## Key Investments in 2017 and Sources of their Financing

In 2017, the Group's key investments were addressed mainly to maintenance of all its assets in Ukraine, Russia and Poland.

The following table represents the Group's key investments in 2013 through 2017 by type.

**Key investments in 2013 through 2017, thousands of Euros**

| | 2017 | 2016 | 2015 | 2014 | 2013 |
|---|---|---|---|---|---|
| Property, plant and equipment | 2,811 | 1,653 | 3,261 | 6,275 | 20,918 |
| Acquisition of associates and subsidiaries | - | 793 | -10 | - | 488 |
| Proceeds from sale of property, plant and equipment | - | -131 | - | - | - |
| **Total investments** | **2,811** | **2,315** | **3,251** | **6,275** | **21,406** |

Last year's investments were financed mainly from operational cash flows. For more details on the Company's financial arrangements in 2017, refer to section *Material Factors and Events*.

## Investment Plans for 2018 and Sources of their Financing

The Group's investment budget for 2018 will be limited to the maintenance costs and chosen investments to the new products introduction in the key markets of the Group. The general investment budget amount will comprise up to c. EUR 2 million.

For more information, refer to section *Fulfilment of Strategy in 2017 and Outlook for 2018.*

In 2018, the Group intends to finance its investment program mainly from its operational cash flows.

## Shareholder Structure

As of December 31, 2017, the following shareholders provided information concerning direct or indirect (through subsidiaries) ownership of at least 5% of the total votes at the General Shareholders Meeting of Milkiland N.V.

As of December 31, 2017, Milkiland N.V. does not possess any information regarding changes in the presented Shareholder Structure.

**Shareholder structure of Milkiland N.V. as of December 31, 2017**

| Shareholder | Number of shares | Percentage of owned share capital | Number of votes at the General Meeting | Percentage of votes at the General Meeting |
|---|---|---|---|---|
| 1, Inc. Cooperatief U.A. | 22,973,588 | 73.52% | 22,973,588 | 73.52% |
| R-Assets Cooperatief U.A. | 1,562,800 | 5.00% | 1,562,800 | 5.00% |
| Aviva Otwarty Fundusz Emerytalny | 2,000,000 | 6.40% | 2,000,000 | 6.40% |
| Other shareholders | 4,712,500 | 15.08% | 4,712,500 | 15.08% |
| **TOTAL** | **31,250,000** | **100.00%** | **31,250,000** | **100.00%** |

## Share Price Performance

In 2017, Milkiland share price was volatile due to a general cautious sentiment of investors about Ukraine due to macroeconomic instability and non-resolved military conflict in the East of the country. Still having significant part of its assets in Ukraine, the Group was subject of the general scepticism to the perspective of the investments to Ukrainian assets. At the same time, on a company-related risks level, long-lasting negotiations with the Syndicate of the Group's major creditors were a major reason of pressure on Milkiland N.V. quotations in 2017.

By the year-end, Milkiland was trading with EV/EBITDA'17 of 9.5

**Share price performance of Milkiland N.V., 2017**


*Source: WSE, Bloomberg*

**Milkiland N.V. significant stock quotation data, 2017-2016**

| | 2017 | 2016 |
|---|---|---|
| Opening price (PLN) | 2.01 | 1.38 |
| Highest trading price (PLN) | 2.84 | 2.64 |
| Lowest trading price (PLN) | 1.41 | 1.06 |
| Closing price (PLN) | 1.54 | 2.00 |
| Closing price (EUR) | 0.37 | 0.45 |
| Stock performance (absolute) | (23.38%) | 44.93% |
| Stock performance (relative to WIG) | 39.06% | 26.46% |
| Common shares outstanding (million) | 31.25 | 31.25 |
| EPS (EUR cents) | (22,25) | (127,49) |
| Price / earnings (P/E) as of December 31 | (1.7) | (0.4) |
| Market capitalization as of 31 December (PLN million) | 48.1 | 62.5 |
| Market capitalization as of 31 December (EUR million) | 11.5 | 14.2 |
| Net debt (EUR million) | 85.1 | 101.2 |
| EV (EUR million) as of December 31 | 97.1 | 115.6 |
| EV / EBITDA as of December 31 | 9.5 | 21.2 |
| Free float (PLN million) | 10.3 | 13.4 |
| Free float (EUR million) | 2.5 | 3.0 |
| Average daily turnover (PLN thousand) | 58.6 | 74.7 |
| Average daily turnover (EUR thousand) | 14.0 | 17.2 |

*Source: Bloomberg, management estimates*

## Management and Personnel

**Composition of the Company's Board**
As of December 31, 2017, the composition of the Board of Directors of Milkiland N.V. was as follows:

- Oleg Rozhko, (Non-Executive Director, Chairman of the Board of Directors);
- Anatoliy Yurkevych (Executive Director, Chief Executive Officer);
- Olga Yurkevich (Executive Director, Chief Operation Officer);
- Vyacheslav Rekov (Non-Executive director, member of the Audit Committee);
- Willem S. van Walt Meijer (Non-Executive director, Chairman of the Audit Committee);
- George C. Logusch (Non-Executive director);
- Pavlo Sheremeta (Non-Executive director).

For information on the Company's remuneration policy and remuneration of the members of the Board of Directors, refer to *Corporate Governance Report, section Remuneration Report*.

**Other information**
Except for Mr. Anatoliy Yurkevych and Mrs. Olga Yurkevich, who indirectly together hold 73.5% of the Company's shares, and Mr. Vyacheslav Rekov, who indirectly holds 5.0% of the Company's shares, neither member of the Company's board of Directors nor any Key Executive holds any shares or stock options over such shares in the Company.

During the last financial year, there were no agreements concluded between the Company and its management personnel, which provide for compensation in case of their resignation or being removed from their position without a good reason, or being removed as a result of the Company being merged with the another company.

**Personnel**
As of December 31, 2017, Milkiland employed 3,447 people. Out of them, 73 specialists were employed by LLC "Milkiland N.V.", the managing company of the Group, located in Kyiv, Ukraine. Another 57 persons worked for the head office of Ukrainian subsidiary of the Group - LLC "Milkiland-Ukraine".

As Milkiland's production activities are arranged through production subsidiaries (cheese and whole milk products plants), the majority of the Company's personnel is based in Ukrainian regional production units (2,147 people, including 360 employees in LLC "Milkiland Agro" and its subsidiaries).

Milkiland EU Sp. z o. o., the head company of the Polish Group in Warsaw employed 2 specialists, UA Trade Sp. z o. o., the Polish trading company of the Group, employed 9 specialists. While the Polish production facility, Ostrowia Sp. z o. o. cheese production plant had 119 employees.

The Group's Russian head-company LLC "Milkiland RU" and Moscow-based production unit JSC "Ostankino Dairy" employed 24 and 734 people, respectively. Other Russian subsidiaries had 265 employees in total.

The key companies within the Group, first of all, the managing company LLC "Milkiland N.V." and its subsidiaries such as JSC "Ostankino Dairy", LLC "Milkiland RU", and Milkiland EU Sp. z o. o., have their own HR departments and are responsible for hiring and dismissing their personnel. Candidates for top-managerial and other key positions for all companies of the Group are being selected by the HR Department of LLC "Milkiland N.V." only.

Candidates' selection is conducted through the formal procedure ensuring sufficient level of required skills and compliance to the Group's corporate culture.

Staff structure comprises about 4.7% of top managers, 10.1% other managerial stuff, and about 20.7% is service staff. The remaining 64.4% is mainly a work force.

Milkiland provides equal employment and personnel development opportunities to professionals in Ukraine, Russia and Poland regardless of their gender, religion, nationality or political preferences.

**Training and Professional Development**
The Group strongly believes that high level of competency of its employees is a key factor of efficiency and market success. In 2017, the internal and external training programs were developed for the key jobs. 1,791 employees or almost one quarter of the Group's employees were trained. Production and technical employees were trained under staff development programs focusing on production safety and quality management, including HACCP-oriented programs at JSC "Ostankino Dairy", EU quality and safety requirements at LLC "Milkiland-Ukraine". All new employees have completed skill development on-boarding programs.

## Corporate Social Responsibility

The Company recognizes that Corporate Social Responsibility is an integral part of its business practice, culture and strategy. The Company is therefore committed to running its business to ethical, legal and professional standards.

We respect human rights as an absolute and universal standard. Furthermore, the Company refrains from discrimination on any basis.

The Group, being one of the leading dairy producers, measures success not only in terms of financial criteria but also in building customer safety and satisfaction, employees' engagement, maintaining strong governance practices and supporting the communities we serve.

The Group is not only focused on environmental issues by implementing state-of-the-art technologies and making the chain and the production process more sustainable, but also undertakes a responsibility to support the local communities where the Group operates by developing social infrastructure and investing in creation other social values.

In 2017, Milkiland continued supporting of local communities in areas where production assets are located. Primarily, this is day-to-day aid such as repairs of schools and kindergartens buildings, procurement of goods and services for these social establishments, purchasing of the gifts for children, charity payments to local NGO's, support of local sports events and local community celebrations.

Milkiland's Ukrainian subsidiaries also provided social assistance to support those employees, who were drafted to the Ukrainian Army and their families.

Corporate Social Responsibility goals and values of the Group are reflected in the corporate documents such as 'Milkiland N.V. Code of Conduct', 'Milkiland N.V. Diversity Policy', 'Best Practice for GWP Listed Companies 2016', which are published at the Company's web-site: http://www.milkiland.nl/en/investors/general_information/corporate_documents/

# Material Factors and Events

## Material factors and events during the reporting period

### *Financing arrangements*

*Restructuring of the Loan Facility by a Syndicate of international Banks*

On September 24, 2014, Milkiland published an official statement that it failed to fulfil some conditions of the Loan Facility Agreement with the syndicate of international banks, namely UniCredit Bank Austria AG and ZAO Raiffeisenbank ("the Syndicate") dated 16 December 2011, and started negotiations to sign a Loan Restructuring Agreement with the banks representing the Syndicate.

On 6 January 2017, Milkiland published an official statement that JSC "Ostankino Dairy" and Milkiland N.V. received the Demand Notice under the Deed of Guarantee made between JSC "Ostankino Dairy" as a Guarantor, and Raiffeisen Bank International AG, as an Agent of the financial parties dated 14 August 2012, in relation to the Loan Facility Agreement between Milkiland N.V. and the Syndicate dated 16 December 2011.

Further in 2017, the Group was continuing the negotiations with the Syndicate, in particular, in March 2017 Milkiland contracted Alvarez&Marsal for joint preparation of the updated Independent Business Review and Options Paper for further negotiations aimed at the Loan restructuring or refinancing by the third parties.

The respective findings were presented to the Syndicate by Alvarez&Marsal in September 2017.

The Group is continuing the negotiations with the Syndicate with the involvement of Alvarez&Marsal and expecting to finish them by finding a mutually accepted way of settlement of this indebtedness in the foreseeable future.

The total sum of the Group's indebtedness to the Syndicate, as of 31 December 2017, stood at EUR 48.85 million, full sum is overdue.

*Filing the bankruptcy petition against JSC "Ostankino Dairy" by PJSC Bank "Vozrogdenie"*

On 19 April 2017, Milkiland published an official statement that the Company and JSC "Ostankino Dairy" ("Ostankino") received the information that Public JSC Bank "Vozrogdenie" ("the Creditor") filed the bankruptcy petition against Ostankino to Arbitrage Court of the City of Moscow dated 28 March 2017.

This petition claiming the introduction of surveillance procedure and the regime of temporary administration of Ostankino according to the Russian legislation, due to inability of Ostankino to repay the indebtedness to the Creditor in the total amount of RUB 309.2 million (EUR 5.13 million).

Based at the above mentioned petition, Arbitrage Court of the City of Moscow initiated the legal case on bankruptcy of Ostankino and on the hearings of this case on April 26, 2017 declared JSC "Ostankino Dairy" bankrupt, introduced the bankruptcy proceedings and appointed the bankruptcy administrator.

In order to assure a continuity of operations of Ostankino, the business of the company was reorganized. The service of the contracts with its suppliers and clients was transferred to a newly incorporated 100% subsidiary of Milkiland Group, LLC "Ostankino Dairy".

Milkiland's management believes that the settlement of the bankruptcy case of Ostankino will take a significant amount of time, including to resolve the legal claims and disputes between the creditors, and actively seeking the mutually acceptable way of such a resolution.

*Signing of the loan restructuring agreement with PJSC "OTP Bank"*

On 15 August 2017, Milkiland published an official statement with the information that the amendment agreement to Loan facility agreement between PJSC "OTP Bank" and the Group's subsidiary, PE CF "Prometey" ("the Borrower"), on restructuring of the loan in the total amount of USD 3.85 million (EUR 3.26 million), was signed on 20 July 2017.

According to the Amendment agreement, the repayment term was extended by 7 years until 30 June 2024, lowered interest rate was applied to the Borrower's indebtedness.

*Signing of the debt restructuring agreement with Pekao Bank S.A.*

On 18 August 2017, Milkiland published an official statement with the information that the Amendment agreement to Revolving Credit Facility agreement and Overdraft Credit Facility agreement between Pekao Bank S.A. ("the Bank"), from one side, and Ostrowia sp. z.o.o. ("the Borrower"), Milkiland EU and UA Trade, all together are the Group's Polish subsidiaries, and the Company, on another side, on restructuring of the indebtedness in the total amount of PLN 7.6 million (EUR 1.8 million), was signed on 31 July 2017.

The Parties agreed that the final repayment of the indebtedness shall be made on 30 June 2018.

In order to secure the repayment of the principal sum of the indebtedness, the monthly repayment schedule was applied. The Borrower also took the obligation to sell the non-core assets in the sum of not less than PLN 0.509 million (EUR 0.12 million) until 28 February 2018 and allocate the obtained proceedings for the repayment to Pekao Bank S.A.

The Parties also agreed to postpone the payment of the interest due and penalty interest accrued to the overdue debt liabilities in the total amount at PLN 0.601 million (EUR 0.143 million) until 30 June 2018.

During of the term of the Amendment agreement, the Bank took the obligation to refrain from debt enforcement of the real property consisting of the production plant of the Borrower.

The Borrower was obliged to submit to the Bank the new debt repayment proposal by 15 April 2018.

*Signing of the loan restructuring agreement with PJSC "Fist Ukrainian International Bank"*

On 26 October 2017, Milkiland published an official statement with the information that the Amendment agreement to Loan facility agreement between PJSC "First Ukrainian International Bank" and the Group's subsidiary LLC "Milkiland Ukraine" (hereinafter "the Borrower"), on restructuring of the loan in the total amount of UAH 301.7 million (EUR 9.7 million), was signed on 29 September 2017.

According to the Amendment agreement, new repayment schedule to the Borrower's indebtedness was applied. It envisages the repayment of c. 10% of the total sum of the debt by monthly instalments in the period of September 2017 - August 2018, while the remainder of the indebtedness, including outstanding interest payments were due on the date of signing of the Amendment agreement, will be delayed for repayment until 3 September 2018. The lower interest rate remained applied to the Borrower's indebtedness.

By signing of the above mentioned restructuring agreements, Milkiland managed to settle the issue of debt servicing in the Ukrainian and Polish segments of the Group's business.

*Changes in the Board of Directors*

On 15 January 2017, Milkiland published an official statement that Milkiland N.V. received the notification of the termination of appointment of Mr. Vitaliy Strukov, as the Non-executive director of the Board of Directors of Milkiland N.V. since 10 January 2017 due to Mr. Strukov's involvement in new project (outside the dairy industry).

On 7 July 2017, Milkiland published an official statement with the information on appointment of Mr. Pavlo Sheremeta as Non-executive director of the Board of Directors of Milkiland N.V., as of the date of the General Meeting, for one year period ending at the close of the annual general meeting of shareholders of Milkiland N.V. to be held in 2018.

*Postponement of the publication of the Annual Report of Milkiland Group for 2016*

On 24 April 2017, Milkiland published an official statement on getting the information from the Company's auditors, namely BDO Audit and Assurance B. V., regarding the additional time required for issuance of an independent auditors report on the consolidated financial statements of Milkiland Group as at 31 December 2016, to be included into the Annual Report of Milkiland Group for 2016.

The reason for this was the necessity of the additional assessment by the auditors of initiated legal case on bankruptcy of JSC "Ostankino Dairy" and on-going restructuring of the Russian segment of the Group's business.

Due to the aforementioned, the publication of the Annual Report of Milkiland Group for 2016 was postponed until 31 May 2017.

After that, on 19 May 2017, Milkiland received the independent auditor's report on the audit of the consolidated financial statements of Milkiland Group for 2016 from BDO Audit and Assurance B. V.

Based on that, the publication of the Annual Report of Milkiland Group for 2016 was shifted to the early date of 19 May 2017 unlike to the previously announced 31 May 2017.

*Appointment of Accon AVM as an independent auditor of Milkiland N.V. and signing the Engagement letter with this firm*

On 8 December 2017, Milkiland published an official statement on the appointment of Accon AVM Controlepraktijk B.V. (hereinafter "Accon AVM") as the external, independent auditor of Milkiland for the financial year ended 31 December 2017 according to the article 2:393 of the Dutch Civil Code, the article 17 of Regulation (EU) No 537/2014 of the European Parliament and of the Council of 16 April 2014 on specific requirements regarding statutory audit of public-interest entities and repealing Commission

Decision 2005/909/EC, the Resolution of the Board of Directors of Milkiland N.V. dated November 10, 2017.

Accon AVM is a Dutch legal entity with its registered office at: OUDE BOSSCHEWEG 5, 5301, La Zaltbommel, the Netherlands, which is entitled to provide services, as an independent auditor under the requirements of Dutch legislation, including Dutch Civil Code and Dutch Corporate Governance Code.

**Material factors and events after the reporting date**

Material factors and events after the reporting date were not identified by Milkiland's management.

## Going Concern Assumptions

The closure of the traditional Russian export market for the Group's Ukrainian and Polish subsidiaries, deep devaluation of Russian Rouble and Ukrainian hryvnya, decline of the demand for dairy in Russia and Ukraine made an adverse effect at the Group's financial position and performance in 2014-2015.

The macroeconomic stabilization of 2016 and the return of the economies of Ukraine and Russia to growth in 2017 provides to Milkiland an opportunity to capitalize on growing customers confidence and, in the nearest years, restoration of the demand for quality dairy in these key markets for the Group's business. But the timing and the dynamics of this process in not currently determinable. Due to this, adverse effect of still limited customer demand, as well as remained macroeconomic imbalances, for example, expected further devaluation of UAH, may adversely affect the Group's operations and financial performance.

As at 31 December 2017 the Group was in breach of certain financial covenants under a few bank loans mostly due to devaluation of the local currency (Please refer to Note 16, Note 31). This situation started in 2014 and is still applicable. Based on the negotiations with the main lenders about loans restructuring, the management believes that the banks will not demand accelerated repayment of the loans because of breaches of covenants in 2017.

In the course of 2017, Arbitrage Court of the City of Moscow declared the JSC "Ostankino Dairy" bankrupt based at the claim of one of its Creditors, Bank "Vozrozhdenie" (for more information please refer *Material Factors and Events).* This event caused a possible material threat to the going concern ability of Milkiland and its operations in the Russian market and Moscow region. The ability of the company to continue its operations there is dependent on coming negotiations during the bankruptcy procedures and finding of the mutually acceptable solution of the settlement of the indebtedness to Ostankino's Creditors. Please refer to Note 35 for more information on this issue.

The Group is dependent on its ability to settle the indebtedness to the Creditors in a mutually acceptable manner without entering to the enforcement and early repayment procedures.

## Fulfilment of Strategy in 2017 and Outlook for 2018

***Strategic priorities***

Milkiland's strategic goal is to become an international diversified dairy Group with clear market leadership in cheese and strong position in whole milk products segment in CIS, balanced presence in EU dairy market and ability to capitalize at global international trade of dairy products. To achieve this goal, Milkiland business has been growing both organically and through selective acquisitions, tapping the existed consolidation potential, especially in the cheese market in CIS.

Milkiland distinguishes itself as "supplier of choice" for consumers in its core markets (Russia, Ukraine and Poland) offering a full range of everyday dairy products at the highest value for money. The Group aims to achieve and maintain this by controlling the whole supply chain — from farm to supermarket's shelves, thus ensuring high quality and affordable price.

Milkiland's primary focus is fresh dairy and cheese, the largest and fast growing dairy segments of CIS dairy market. The Group believes that it knows how to create products appealing to its consumers with their healthy, genuine qualities and superior taste.

The Group is actively promoting its international and local brands, including Dobryana for CIS market, Ostankinskaya and 36 Kopeyek for Russian market, as well as Ostrowia brand, a traditional trademark well-known for Polish customers.

***Return to a positive track of the business in 2017***

In 2015-2016 Milkiland's business performance and financials were severely supressed by the combination of geo-political risks, including the continuing tension between Russia and Ukraine, negative macroeconomic performance, as well as bad shape of consumer markets in these countries.

The macroeconomic situation started to improve in 2016, then in the last year positive trends of macroeconomic stabilization in Russia and Ukraine, the core markets of the Group, became more evident.

In particular, in 2017 real GDP of Russia and Ukraine grew by 1.5% and 2.0% on y-o-y basis, respectively. Russia posted the lowest historical CPI stood at 2.5%, but Ukraine still pencilled a double-digit inflation of 13.7%. The devaluation pressure on Ukrainian hryvnia eased, while in 2017 it devalued against EUR by 6.3% only, contrary to double-digit devaluation in the previous years. At the same time, Russian rouble on the back of strengthened oil prices even revalued against EUR by c. 12.6% on average in comparison with 2016.

These positive trends, however, had some effect on restoration of the consumer demand in Ukraine, where the household consumption in 2017 grew by 7.8% on y-o-y basis, but limited influence on the situation in Russian market, where the real disposal income of population in the last year even declined by 1.7% in comparison with 2016.

At the same time, devaluation of Ukrainian hryvnya against USD and EUR in 2015-2017 provided some additional competiveness for Ukrainian export, including of such a dairy export goods, like dry milk products and butter.

Thus, in 2017 Milkiland continued its policy aimed at the growing local competence in the markets of its operations in Russia, Ukraine and Poland, as well as on participation in international trade of dairy goods through its Milkiland Intermarket subsidiary.

The cornerstone of this policy was the intention to increase the margins of the Group's business in order to restore the profitability of the business and value creation for the Group's shareholders.

***Strategy fulfilment in 2017***

Last year, Milkiland penciled a minor decline on a top-line level of the business, when the Group's revenue decreased by c. 4% to c. EUR 140 million in comparison with the year 2016.

At the same time, the efforts of the Group aimed at the production and selling of high value-added products in the markets of its operations together with the opening and development of new export markets for selling of Milkiland's products, led to almost doubling of the Group's EBITDA, which grew to c. EUR 10.3 million on y-o-y basis. Based on that, the Group's net loss significantly contracted from c. EUR 39 million in 2016 to c. EUR 6.9 million in 2017.

One of the achievements of the last year was further stabilization of the debt position of Milkiland. By signing the long-term restructuring agreements with several banks-creditors of the Group, Milkiland managed to settle the debt servicing situation in the Ukrainian and Polish segments of its business. As the results of these efforts, the Groups total debt portfolio decreased from c. EUR 102 million as of 31 December 2016 to EUR 85 million as of 31

December 2017, while Debt/EBITDA ratio corrected from 18.6 to 8.3.

In 2017, Milkiland RU, Russian subsidiary of the Group, continued its efforts aimed at further localization of the production and sales of chees under Milkiland's brands in Russia. This resulted c.8% growth of company's EBITDA, while the company's revenue remained practically flat on y-o-y basis.

Moscow-based Ostankino Dairy, the main subsidiary of the Group in Russia, penciled c. 8.5% decline in the top-line in comparison with 2016. At the same time, concentration of sales of the high-value added products under its own brands, growth of the profitability of sales in the key accounts channel, led to leap of the company's EBITDA by 5 times to c. EUR 5.3 million in comparison with 2016. One of the additional reasons for this dynamic was the low base effect, connected with the relatively low profitability of Ostankino's operations in 2016 provoked by the lack of working capital due to demands of some of the company's creditors.

In 2017 Milkiland also successfully implemented the reorganization of Ostankino's dairy business in order to continue the operations under the bankruptcy procedure initiated by one of the company's creditors, Bank Vozrozhdenie (*for additional information please refer Material Factors and Events Section)*.

In Ukraine, the Group focused its efforts on preserving its market positions in cheese segment of dairy market, as well as on development of its sales in key-accounts channel. As the result, the Group preserved its share of 3% in the above mentioned segment (flat on y-o-y basis, Top-10 player) and improved its presence on a shelfs of the leading Ukrainian retail chains. This led to c. 4% increase of the company's EBITDA to c. EUR 2.7 million, while the revenue remained flat on y-o-y basis.

Milkiland EU, the Polish subsidiary of the Group managed to generate a positive EBITDA in H1 2017 on the back of favorable global prices for its key products, WPC-80 and permeate, but then generated a negative EBITDA in Q3-Q4 2017 due to the reversed pricing trends. As the result of this volatility, the company posted minor, but negative EBITDA in 2017, almost the same as in 2016.

In 2016 Milkiland continued its vertical integration efforts by supporting of in-house milk production by Milkiland-Agro subsidiary. In particular, the company concentrated on the optimization of milking cows' headcount and improving of milk yields. As an outcome, the raw milk yield per milking cow head in 2017 increased by c. 16% to c. 6.4 tons on y-o-y basis. Positive market situation also triggered the increase of the EBITDA of Milkiland-Agro to c. EUR 1.4 million or by 7.7% in comparison with 2016.

In the last year the Group continued a policy aimed at searching of a new markets and geographical diversification of sales. In line with this policy, Milkiland Intermarket entered to the new promising export market of Israel by selling to this country the Group's made butter and dry milk products, which passed Kosher treatment. Capitalizing at the situation with some deficit of butter in the global market in the 9 months of 2017, the company managed to enter to EU dairy market, by selling of this product to Denmark and Netherlands. Milkiland Intermarket also continued the development of the distribution network for the Group's dry milk products in China. In order to expand its product matrix, the company introduced new export goods of economy segment, cheese-like products. The Group successfully sold these products in CIS and EU markets, in particular, to Belarus, Kazakhstan and Uzbekistan, as well as to Lithuania.

***Strategic outlook for 2018***

Despite some positive steps to better results and margins, in 2017 the Group did not achieve a task of restauration of profitability of its business.

The current year is expected to be crucial for reaching a break-even point for generation of the new value of the business. The Group's management is going to achieve this by continuing a policy aimed at strengthening of the market positions of Milkiland in the countries of its operations, as well as on searching for new, and advancing at the existed export markets.

Milkiland's Russian division aims its efforts on streamlining of products portfolio in order to increase the share of high value-added healthy modern dairy, as well as on growing local cheese production.

The goals of the Ukrainian division are of two major types, as follows: to strengthen the positions in the local dairy market, especially in cheese segment and several niche segments, including lactose-free dairy, special types of cheese and to build a sustainable export-oriented model of its business. Forecasted further soft devaluation of the Ukrainian Hryvnia in 2018-2019 remains the supporting factor for reaching of the export goals.

Milkiland EU in 2017 is concentrating at the development of local distribution network in Poland for locally produced cheese, including in order to compensate the volatility of the global prices for its key dry milk products. The traditional task of the searching for the new export markets for latter remains relevant in

2018. Also, the company in 2018 started a production of some new products to satisfy the preferences of the customers in the export markets.

The Group’s investment budget for 2018 will be limited on the maintenance level and some expenses on introduction to the local markets of its operations the high value-added products. The amount of the respective investments will stand on the level of c. EUR 2 million.

## Material Risk Factors and Threats to the Group

A number of risks could materially affect the Group's business, financial condition and results of operations.

Described below are the risks and uncertainties that, we believe, are material, but these risks and uncertainties may not be the only ones faced by the Group.

***Business and industry risks***

*Exports to Russia*

Russian market was the important market for the Group's cheese export from Ukraine to Russia. Every year it significantly contributed to the positive financial results of the Group in general.

Nevertheless, since 2014 Russian market is not available for Ukrainian dairy export. In April 2014, the Russian Federal Service on Customers' Rights Protection and Human Well-Being Surveillance imposed restrictions on export of dairy products produced by largest Ukrainian dairy producers, including Milkiland's Okhtyrka, because of perceived violations of Russian technical requirements. In July 2014, Russia banned all dairy and milk-containing imports from Ukraine.

In August 2014, Russian government introduced an embargo on food products imported from the countries supporting sanctions over Russian Federation on annexation of Crimea and support for insurgents in the Eastern Ukraine. The list included, inter alia, the EU countries, the USA, Canada, Australia and others.

Starting from January 1, 2016, Russia put a ban on exports of some agricultural and food products from Ukraine (including dairy products). In June 2017 Russia extended the duration of the ban till the end of 2018. There are high chances that existing embargo will be extended again for 2019.

The Group does not expect that Russia will lift existing trade barriers for Ukrainian dairy exports or allows selected producers, such as the Group or its subsidiaries, to resume deliveries in the following year. The existing ban on dairy exports from Ukraine significantly affected the Group's financial results in the past years and continues to be among the factors that influence the Group's business, financial condition and results of operations.

*Input cost increase*

The Group's business is subject to price fluctuations and shortages, which sometimes are beyond its control. This factor was present in Group's operations through 2017. In particular, the Group faced the increased prices for raw milk in Ukraine and Russia by 36% and 14% in local currency terms respectively.

Although historically the Group has been able to pass on increases in raw material prices to its consumers, there is no assurance that it will be able to do so in future as this will depend to a large extent on market conditions. Even if the Group is able to pass these costs on to consumers, an increase in selling prices could be implemented with time lag and also may inhibit consumer appetite for Group's products.

For these reasons, significant increase in price of raw materials could materially adversely affect the Group's business.

*Raw milk deficit*

Raw milk is a key input in the Group's production process and ensuring a sufficient supply of raw milk is crucial for the Group's business.

The production of raw milk in Ukraine and Russia is stagnating over last years and is subject to seasonal fluctuations, with a surplus typically being produced in spring and summer while there is a reduction in supply during the winter months.

In 2017 the milk production in Ukraine has decreased for 0.5% comparing with 2016. In 2018 the milk production in Ukraine is projected to decrease from 1% to 3% based on the data of State Statistic Service in Ukraine and FAO.

In 2017 in Russia the total milk production increased for 0.3% accordingly to RosStat. Nevertheless, for 2018 in Russia is expected the general decrease of the milk shipment for industrial processing up to 0.2% based on expected decline of milking cow herd and improving milking yield expectations.

In the following years the Group could face difficulties in sourcing supplies of raw milk on commercially acceptable terms.

Also the Group may face additional difficulties in sourcing a sufficient amount of high-quality raw milk from suppliers in Ukraine for export of dairy products with specific certification (e.g, Kosher) and other high-quality parameters.

*Exports VAT refunds*

Although not specific to the agricultural industry, the Group benefits from VAT refunds in connection with its exports sales. Because exports sales are generally taxed at the rate of 0%, the Group's input VAT is subject to reimbursement by the government.

In the past due to a high budget deficit in Ukraine, many taxpayers entitled to VAT refund did not receive such refund on a timely basis.

On January 25, 2017, the Ukrainian government adopted a new procedure on VAT refund aimed to ensure transparency and fair VAT reimbursement.

Although the Group until now managed to collect VAT receivables on exports in Ukraine in sufficient amounts, there is no guarantee that it will be able successfully receive such refunds in the future. This possibility may adversely affect its results and operations.

*Contamination of the Group's products*

As a producer of food products, the Group's business is subject to certain risks related to the actual or alleged contamination or deterioration of its ingredients or its principal products, or of similar products sold by other producers.

Such risk is a general risk for food producers. The Group takes all necessary steps to ensure the high-quality products, including implementation of the quality management systems like ISO 9001:2000, HACCP, sanitation compliance for production facilities, and exclude contamination or deterioration possibilities.

Any such actual or alleged contamination or deterioration could adversely impact the Group's reputation, sales and profitability.

*Competitive pressure*

Failure by the Group to anticipate, identify or react to changes in consumer tastes or in competitors' activities could result in reduced demand for the Group's products, which in turn could result in the Group not being able to maintain its market shares or to recover development, production and marketing costs.

Since January 1, 2016, the EU and Ukraine have provisionally applied their Deep and Comprehensive Free Trade Agreement (DCFTA). The competition on the EU and Ukrainian dairy markets is also affected by the new rules established by the DCFTA.

The DCFTA requires Ukrainian dairy producers to phase out within 7 years, the production and sales of dairy products under names that are protected in the EU as Geographic Indications. The Group historically used some of such names for own products. In order to meet the DCFTA requirements and stay competitive the Group is planning and implementing changes to Group's operations, marketing and rebranding strategies.

*Antimonopoly proceedings*

As the Group is one of the leading milk processors in Ukraine with strong positions nationwide and specifically in the regions of its operations, it could be subject of legal proceedings, including those under competition legislation, which could have an adverse effect on the Group's future business.

***Country risks***

*Economic considerations*

The global financial crisis, as well as recent political changes in Ukraine, have led to significant decrease in economies of Milkiland's home markets. The negative trends in Russian and Ukrainian economy may continue if local governments are not able to overcome crisis consequences, or if global slowdown resumes. In this case, Milkiland's business might be negatively affected.

*Exchange and interest rate risk*

Fluctuations of exchange rates of local currencies used by the Group on key markets in Russia (RUB), Ukraine (UAH), and Kazakhstan (KZT) may have an adverse effect on the financial results of the Group.

In particular, this factor is important on Ukrainian and Russian markets. Despite the recent stabilization of these currencies exchange rates, comparing to previous years, there is a possibility of further fluctuations and devaluation if the negative trends in the respective countries' economies will resume.

*Risks of legislation and judicial system*

The Russian Federation and Ukraine are still developing a modern legal framework required for proper functioning of a market economy. The significant amount of legislation still is a heritage of a Soviet period.

The often legislation changes and the rapid evolution of the respective legal systems result in ambiguities, inconsistencies and anomalies in their application. In addition, legislation in

Russia and Ukraine sometimes leaves substantial gaps in the regulatory infrastructure.

All of these factors, together with lack of transparency, make judicial decisions in the Russian Federation and Ukraine difficult to predict and makes effective redress uncertain. Additionally, court claims are often used to further political aims. The Group may be subject to these claims and may not be able to receive a fair hearing.

Additionally, court judgments are not always enforced properly or followed by law enforcement agencies. All of these weaknesses could affect the Group's ability to enforce its rights or to defend itself against claims by others, which could have a material adverse effect on the Group's business.

*Bankruptcy of Ostankino Dairy in Russia*

On March 28, 2017, the JSC Bank "Vozrozhdenie" has filed a bankruptcy petition against JSC "Ostankino Dairy", one of the key Group's subsidiaries on the Russian market, to Arbitrage Court of the City of Moscow due to the inability of JSC "Ostankino Dairy" to repay in time the indebtedness to the Creditor in the total amount of RUB 309.2 million (EUR 5.13 million).

On April 26, 2017, the court has appointed an independent arbitration administrator to manage JSC "Ostankino Dairy" during the bankruptcy proceeding.

In order to ensure a continuity of operations of Ostankino, a new company LLC "Ostankino Dairy", a 100% subsidiary of Milkiland Group, was incorporated to serve contracts with the Group's suppliers and clients in Russia.

The outcome of the bankruptcy proceeding is not foreseen yet and the case hearing may take years.

This bankruptcy proceeding could have a material adverse effect on the Group's reputation and business in general, if the Group won't be able to ensure a continuity of operations of Ostankino, and to preserve its market share on the Russian market.

*Political and governmental considerations*

The Group performs its activities in Ukraine in the environment of political and economic crisis that has aggravated since November 2013.

The assets of the Group in Ukraine are mainly located in Central, West and North-East of the country and not in the current tumultuous East of Ukraine.

However, as a possible consequence of the current crisis, the economic and financial situation in Ukraine could further deteriorate, which, inter alia, could lead to a significant devaluation of Ukrainian and Russian currencies, declining demand for FMCG goods at one of the Group's core markets, difficulties with performing foreign trade operations.

# CORPORATE GOVERNANCE REPORT

## Introduction

Milkiland N.V. (the "Company"), having its registered office in the Netherlands and which shares are admitted to trading on a regulated market, is subject to the principles and best practice provisions of the amended Dutch Corporate Governance Code (the "Code") effective as of 1 January 2017.
It can be found at:
www.commissiecorporategovernance.nl

Moreover, since Company's shares are listed on the Warsaw Stock Exchange, the Company is subject to the principles of Corporate Governance as stated in the Code of Best Practice for WSE Listed Companies in 2016 (the "WSE Code") which can be found at https://www.gpw.pl/best-practice

The Code contains principles and best practice provisions that regulate relations between the management board, the supervisory board and the general meeting of shareholders. The Company should state in its annual report how it applies the principles and best practice provisions of the Code for the first time in their annual report for the financial year 2017 and should, where applicable, explicitly explain why and to what extent a provision deviates from the principles stated in the Code.

The Company's application of the Code is described in the Report on compliance by Milkiland N.V. with the revised Dutch Corporate Governance Code of 2016 as approved on 27 August 2017 by the Board of Directors, which can be found at:
http://www.milkiland.nl/en/investors/general_information/corporate_documents/
This is to be read in conjunction with this section and is deemed to be incorporated into this section.

The Code provides that a company will be deemed compliant with the Code if it has implemented its provisions no later than 31 December 2017.

The Code provides that if a company's general meeting of shareholders explicitly approves the corporate governance structure and policy and endorses the explanation for any deviation from the best practice provisions, such company will be deemed to have complied with the Code.

## Main points of corporate governance structure

The Company is a public company with limited liability (*naamloze vennootschap*) incorporated under Dutch law, having its registered office at De Cuserstraat 93, 1081CN Amsterdam, the Netherlands. The Company has the following subsidiaries:

- Milkiland EU Sp. z o.o. (Poland) with 1 Polish subsidiary;
- LLC Milkiland-Ukraine (Ukraine) with its 19 subsidiaries in Ukraine and 3 in Panama, 1 in Marshall Islands, 1 in Scotland, 1 in Poland;
- Milkiland N.V. LLC (Ukraine);
- JSC "Ostankino Dairy" (Russian Federation),
- Milkiland RU LLC with its 3 subsidiaries in Russian Federation;
- MLK Finance Limited (Cyprus);
- Milkiland Intermarket (CY) LTD (Cyprus), with its subsidiaries – 1 in Ukraine and 1 in Kazakhstan;
- Moloko-Kraina LLC (Ukraine);
- Milkiland Agro LLC (Ukraine) with its 7 subsidiaries in Ukraine.

## Board of Directors

The Company has a one-tier corporate governance structure managed by the Board of Directors. The Board of Directors is responsible for the management of the Company, its overall results, as well as its mission, vision and strategy. The Board of Directors consists of seven directors: two Executive Directors and five Non-Executive Directors. The majority of the Board of Directors is made up of non-executive directors. All non-executive directors have provided statements of independence.

The Board of Directors charges the Executive Director(s) with the operational management of the Company, the preparation of the decision-making process of the Board of Directors and the implementation of the relevant decisions. The Executive Director(s) determine the division of duties between them. A division of tasks between the Directors may be determined by the Board of Directors. Such division shall require the approval of the General Meeting of Shareholders pursuant to article 13.4 of the Articles of Association. The Non-Executive Director(s) are charged with the supervision of duties by the Executive Directors and of the general affairs and policy of the Company.

***Board of Directors - Composition and division of duties***

During the year 2017, the composition of the Board of Directors was as follows:

Mr. Anatoliy Yurkevych: Executive Director, appointed as of August 28, 2007 and reappointed as of June 19, 2015, for another four year period; Chief Executive Officer, responsible for running the Company, implementation of strategic goals and achievement of planned financial results, age: 49, gender: male, nationality: Ukraine;

Mrs. Olga Yurkevich: Executive Director, appointed as of August 28, 2007 and reappointed as of June 19, 2015, for another four year period; Chief Production Officer, responsible for supply of raw materials, production and quality assurance, age: 71, gender: female, nationality: Kazakhstan;

Mr. Vyacheslav Rekov: Non-Executive Director, appointed as of August 28, 2007 and reappointed as of June 30, 2017 for another one year period; responsible for strategic acquisitions and integration of new businesses; maintaining communication with investors, Member of the Audit Committee, age: 43, gender: male, nationality: Ukraine;

Mr. Willem Scato van Walt Meijer: Non-Executive Director, appointed as of December 6, 2010 and reappointed as of June 30, 2017, for another one year period; Head of the Audit Committee, responsible for supervising the Board's activities in respect to provision of financial information, internal controls, relations with external auditors, age: 59, gender: male, nationality: the Netherlands;

Mr. Oleg Rozhko: Non-Executive Director, Chairman of the Board of Directors, appointed as of June 22, 2012 and reappointed as of June 30, 2017, for another one year period; responsible for coordination of the Board and ensuring that proper corporate governance is in place, age: 40, gender: male, nationality: Ukraine;

Mr. George Christopher Logusch: Non-Executive Director, appointed as of June 21, 2013 and reappointed as of June 30, 2017, for another one year period; responsible for assisting in the Company’s strategy development, risk assessment control and review of management performance, age: 73, gender: male, nationality: the United States of America, and

Mr. Pavlo Sheremeta: Non-Executive Director, appointed as of June 30, 2017, for one year period; Member of the Audit Committee, responsible for improvement of businesses processes in human resources, talent acquisition, and personnel education, ensures business strategy development, age: 46, gender: male, nationality: Ukraine.

On 30 June 2017 the Company adopted and published current division of duties and responsibilities for the Company’s Directors which can be found at the Company's website: http://www.milkiland.nl/en/investors/general_information/corporate_documents/

***Board of Directors - Terms of Reference***

The Terms of Reference of the Board of Directors, which provide for certain duties, composition, procedures and decision-making of the Board of Directors, were adopted on 28 August 2017 in accordance with article 13.4 of the Company's Articles of Association and the best practice provisions under chapter 2 of the Code. The Terms of Reference of the Board of the Company are applied and interpreted with reference to the Code and can be viewed on the Company's website: http://www.milkiland.nl/en/investors/general_information/corporate_documents/

The Chairman of the Board of Directors determines the agenda, presides over meetings of the Board of Directors and is responsible for the proper functioning of the Board of Directors. The Chairman of the Board of Directors shall always be a Non-Executive Director and is appointed by the General Meeting of Shareholders. All members of the Board of Directors have access to the advice and services of the corporate secretary, who is charged with ensuring that the Board of Directors' procedures are followed and that the Board of Directors acts in accordance with its statutory obligations under the Articles of Association. The corporate secretary is appointed by the Board of Directors for each meeting of the Board of Directors.

***Board of Directors - Issue of shares and acquisition of own shares***

According to the Articles of Association (Art. 5) the Board of Directors has the authority to propose to the General Meeting of Shareholders to issue shares. Such a proposal shall contain the price and the further terms and conditions of the issue. The General Meeting of Shareholders may resolve to designate the Board of Directors, for a fixed period not exceeding five years, as the body authorized to issue shares.

Also, the Board of Directors may be granted, by the General Meeting of Shareholders, the right to resolve upon the exclusion or limitation of pre-emptive rights.

Article 6 of the Articles of Association stipulates that the Company shall have the right to acquire fully paid-up shares in its own share capital against payment of a consideration, provided:

a. the shareholders' equity minus the acquisition price is not less than the sum of the paid and called-up part of the share capital and the reserves which must be maintained by law or under the Articles of Association;

b. the aggregate par value of the shares in its share capital to be acquired and of those already held by the Company and its subsidiaries and of those for which the Company and its subsidiaries hold a right of pledge, does not exceed half of the issued share capital; and

c. the General Meeting of Shareholders has authorized the acquisition. The authorization by the General Meeting of Shareholders will be valid for at most eighteen months and shall stipulate the number of shares that may be acquired, how they may be acquired and the upper and lower limit of the acquisition price.

For the purpose of subparagraph a. above, the determining factor shall be the amount of the shareholders' equity stated in the last adopted balance sheet minus the acquisition price.

The General Meeting of Shareholders of 2017 gave the authorization to the Board of Directors to issue, acquire own shares and to exclude or limit the pre-emptive rights.

***Board of Directors - Representation***
Executive Board Member(s) have the authority to represent the Company, including the authority to represent the Company acting individually. The Company may grant special and general powers of attorney to persons regardless of whether or not they are employed by the Company authorizing them to represent the Company and bind it vis-à-vis third parties.

***Board of Directors - Conflict of interest***
In the event that the Company has a conflict of interest with a Director, in the sense that the Director in private enters into an agreement with, or is party to a legal proceeding between him and the Company, the Company shall be represented by one of other Executive Directors. If there are no such other Directors, the Company shall be represented by two Non-Executive Directors acting individually. If there are no such Non-Executive Directors, the General Meeting of Shareholders shall appoint a person to that effect. Such person may be the Director in relation to whom the conflict of interest exists. In all other cases of a conflict of interest between the Company and a Director, the Company can also be represented by that Director. The General Meeting of Shareholders shall at all times be authorized to appoint one or more other persons to that effect.

Transactions with members of the Board of Directors in which they have significant conflicts of interest will be disclosed in the Annual Report if any.

***Board of Directors - Appointment, suspension, dismissal and profile***

Members of the Board of Directors may be appointed for a maximum period of four years. Starting on the day of the General Meeting of Shareholders at which they are appointed and ending on the day of the annual General Meeting of Shareholders that is held in the fourth year of their appointment. Members of the Board of Directors may immediately be reappointed. Members of the Board of Directors can be suspended or dismissed by the General Meeting of Shareholders. If the General Meeting of Shareholders has suspended a Director, the General Meeting of Shareholders shall within three months of the date on which the suspension has taken effect, resolve either to dismiss such Director, or to terminate or continue the suspension, failing which the suspension shall lapse. A resolution to continue the suspension may be adopted only once and in such event the suspension may be continued for a maximum period of three months commencing on the day the General Meeting of Shareholders has adopted the resolution to continue the suspension. If within the period of continued suspension the General Meeting of Shareholders has not resolved either to dismiss the Director concerned or to terminate the suspension, the suspension shall lapse.

The Company has a profile of its Directors, which indicates the size and composition of the Board of Directors, the activities and expertise and background of the Directors. The profile of the Board of Directors can be viewed on the Company's website: http://www.milkiland.nl/en/company/sovet_direktorov/

***Board of Directors - Committees***
The Board of Directors has an audit committee (the "Audit Committee"). The Board of Directors may establish any other committee as the Board of Directors shall decide. According to best practice provision 2.3.2 of chapter 2 of the Code, only Non-Executive Directors can take place in the Audit Committee, a remuneration committee and a selection and appointment committee.

The Audit Committee is responsible for annually reviewing and reassessing the adequacy of the rules governing the committee as established by the Board of Directors. The Audit Committee will be charged with advising on, and monitoring the activities of the Board of Directors, with respect to inter alia, the integrity of the Company's financial statements, the Company's financing and finance related strategies and tax planning. The members of the Audit Committee of the Company are Mr. Willem Scato van Walt Meijer (the Chairman), Mr. Vyacheslav Rekov and Mr. Pavlo Sheremeta. The Terms of Reference of the Audit Committee can be viewed on the

Company's website:
http://www.milkiland.nl/en/investors/general_information/corporate_documents/

***Board of Directors - Evaluation***
In 2018 the Company plans to develop and adopt the evaluation policy of the Board of Directors, based on which the activity and contribution of all Executive Directors and Non-Executive Directors will be evaluated. Mentioned evaluation policy will be published at the Company's website.

***Board of Directors - Miscellaneous***
None of the Executive Directors holds more than two supervisory board memberships of listed companies or is a chairman of such supervisory board other than a group company. The total number of the Company's shares held by members of the Board of Directors is 24,536,088, amounting to approximately 78.52% of the issued and paid up share capital of the Company. The shareholding of the Directors has been notified with the AFM (*Stichting Autoriteit Financiële Markten*) in the Netherlands.

With respect to acquiring ownership interest of securities and transactions in securities by the Directors, the Company follows the Company's Board Securities Rules.

With respect to acquiring shares in the Company's capital by the Directors as well as other people that are involved with the Company, the Company follows the provisions of the EU Market Abuse Directive and the Company's Insider Trading Rules that reflect the provisions of this Directive.

The Company's Board Securities Rules and Insider Trading Rules can be viewed on the Company's website:
http://www.milkiland.nl/en/investors/general_information/corporate_documents/

## Shareholders and shares

The Company's authorized capital amounts to five million Euros (EUR 5,000,000.00). The issued share capital of the Company amounts to EUR 3,125,000.00, which is divided into 31,250,000 shares with a nominal value of ten eurocent (EUR 0.10) each, all of the same class and kind. There are no shares issued with special rights or privileges attached to them. There are no restrictions imposed by the Company on the transfer of shares or certificates.

There have been no conflict of interest situations between the Company and its shareholders.

***Shares and General Meeting of Shareholders***
At least once a year, a General Meeting of Shareholders is held. General Meetings of Shareholders are convened by the Board of Directors.

In 2017, the one General Meetings of Shareholders was held. The principal decisions taken by the General Meeting of Shareholders are:

- adoption of the annual accounts for the financial year 2016, discharge of the members of the Board of Directors for their tasks during the financial year 2016;
- appointment of the external auditor as referred to in section 2:393 of the Dutch Civil Code for the financial year 2017;
- the authorization of the Board of Directors for a period of 18 months following June 30, 2017 to:
  - i) repurchase shares for a price not higher than 10% of the opening price of the Company's shares quoted on the Warsaw Stock Exchange on the day of acquisition;
  - ii) resolve to issue and/or to grant rights to subscribe for shares, which authorization is limited to 10% of the issued share capital of the Company, to be increased with an additional 10% in respect of mergers and acquisitions;
  - iii) restrict or exclude pre-emptive rights in respect of such issue of shares and/or rights to subscribe for such shares;
- reappointment of Mr. Oleg Rozhko, Mr. Willem Scato van Walt Meijer, Mr. Vyacheslav Rekov, Mr. George Christopher Logusch as a Non-Executive Directors of the Board of Directors;
- appointment of Mr. Pavlo Sheremeta to the position of a Non-Executive Director;
- approval of the division of duties and responsibilities among members of the Board of Directors.

Notices of a General Meeting of Shareholders are posted on the Company's website and are made in accordance with the relevant provisions of applicable laws and regulations. The notice convening a General Meeting of Shareholders shall be published no later than the 42nd day prior to the day of the meeting. The agenda and the explanatory notes thereto shall also be published on the Company's website at the same time. The agenda for the Annual General Meeting of Shareholders shall contain, inter alia, the adoption of the annual report, the reservation and dividend policy, a proposal to declare dividends, the proposal to grant discharge to the members of the Board of Directors from liability and, insofar applicable, the appointment of an external auditor. Shareholders, insofar entitled to make such request according to the law, can request the Board of Directors in writing to include subjects to the agenda at least 60 days before the date on which the General Meeting of Shareholders is convened.

In accordance with Dutch law, the record date for the exercise of the voting rights and the rights relating to General Meetings of Shareholders shall be the 28th day before the date of the relevant General Meeting of Shareholders. And holders of shares as per the record date will be entitled to vote, irrespective of any transfer of such shares between the record date and the date of the General Meeting of Shareholders.

At General Meetings of Shareholders, each ordinary share entitles the holder thereof to cast one vote.

The General Meeting of Shareholders is entitled to resolve to grant approval to decisions of the Board of Directors regarding the identity or the character of the Company, including major acquisitions and divestments.

***Bilateral contacts with shareholders***

To comply with the best practice provision 4.2.2 of the Code the Company developed a Policy on bilateral contacts with shareholders of Milkiland N.V. approved by the Board of Directors on 28 August 2017 that can be found on the Company's website: http://www.milkiland.nl/en/investors/general_information/corporate_documents/?PAGEN_2=1

## Internal risk management and control systems

The Board of Directors is responsible for the system of internal risk management and controls of the Company and for reviewing its operational effectiveness.

On 28 August 2017 the Board of Directors adopted the Whistleblower rules of the Company aimed to regulate the internal procedure of reporting about the irregularities of a general, operational and financial nature within Milkiland N.V. and its group companies and/or to report alleged irregularities that relate to the performance of the members of the management of the Company.
The Rules has published at its corporate website: http://www.milkiland.nl/en/investors/general_information/corporate_documents/

The internal risk management and control systems are designed to identify significant risks and to assist the Board of Directors and the Company in managing the risks that could prevent the Company from achieving its objectives.

The Board of Directors is responsible for establishing and maintaining adequate internal risk management and control systems. Such systems are designed to manage rather than eliminate the risk of failure to achieve important business objectives, and can only provide reasonable and not absolute assurance against material misstatements of loss.

## Internal audit department

In deviation from principle 1.3 of the Code the Company will not appoint a senior internal auditor because the internal audit is performed by the internal audit department under the supervision of the Audit Committee.
In the financial year 2017, the internal audit function of the Company was performed by the internal audit department and partially by licensed independent external auditors under the supervision of the Audit Committee.
In order to provide effective internal control of the financial statements preparation the internal audit department has developed and implemented a two-level system of internal control.

The first level of control (technical) foresees the checks of the prepared financial statement using mathematical formulas which allow revealing mismatches and discrepancies in the values. This level of control is provided by the chiefs of the internal audit unit. In more complicated cases the licensed independent external auditor is to be invited.

The second level of control is provided by the financial department at the level of Chief Financial Officer of Milkiland N.V. LLC (Ukraine) who performs a thorough check and afterwards presents the financial statement to the Board of Directors.

The Company recognizes the importance of internal audit and envisages improving its existing audit function. The main responsibilities of the head of internal audit involve the implementation of the internal control environment, global risk assessment and management and the realization of regular internal audit functions.

## Diversity policy

On November 10, 2016 the Board of Directors has approved the Company's Diversity Policy as recommended by provisions I.Z.1.15 of the WSE Code and provision 2.1.5 of the Code. The Diversity Policy is published at the Company website at:

http://www.milkiland.nl/en/investors/general_information/corporate_documents/
The diversity policy of the Company is a part of a long-term vision which can ensure realization of the Company's business strategy and achievement of business priorities. Diversity principles are incorporated into all aspects of human resource management in the Company, such as workforce planning, recruitment and selection, performance management, learning and development, leadership development etc.
The Company values and respects people with diverse backgrounds and perspectives.
The Company's diversity policy for employees includes several aspects:

- Equal employment opportunity - the Company encourages a gender-balanced employment of professionals with different backgrounds, a merit-based promotion, and culture that does not tolerate discrimination or harassment during the employment;
- Workplace safety - the Company provides a healthy and safe workplace with a positive working atmosphere for all employees; the Company are adapting the workplace for its employees with disabilities and all other employees to accommodate their special needs, and to make their workplace more safe and comfortable;
- Respect and inclusion - the Company ensures the understanding and fulfillment of the diversity policy by all the employees and works on improved relationships, understanding and teamwork between employees, based on mutual respect of individual diversity;
- Diversity support – the Company promotes equal pay and gender diversity within the Company and provides employment opportunities for people with disabilities.

The Company constantly improves and supports its internal and external diversity initiatives. The WSE Code and the Code recommends that the composition of management bodies of the Company shall be diverse in terms of gender, age, education, professional experience. In the Company the management and supervisory duties are performed by the Board of Directors, which in 2017 consisted of six men and one woman, of diverse age, nationality and professional background. The Company understands and supports this recommendation and considers involving more women in the Board of Directors.

## Compliance with the WSE Code and the Code

On October 13, 2015 Supervisory Board of WSE approved Best Practice for GPW Listed Companies 2016 (WSE Code), effective as from January 01, 2016. The Company incorporated in the Netherlands is subject to the provisions and principles of the Code. However, since its shares listed on WSE, the Company is subject to the principles of corporate governance set out in the WSE Code. On May 13, 2016 the Company has published its Report on compliance with WSE Code on its corporate website at:
http://www.milkiland.nl/en/investors/general_information/corporate_documents/

Since the WSE Code rules are similar to the rules provided under the Code, the Company complies with a majority of the principles and best practice provisions of the Code as well.

It is noted that the one-tier board structure of the Company deviates from the recommendations of WSE Code, which prescribes the existence and functioning of two separate governing bodies. However the Company's one-tier board structure corresponds to the recommendation of the Code and best suits to the Company's management goals.

The Company explains why it does not comply with the following recommendations of the WSE Code and the Code:

- Company pursues sponsorship and charity activities, but does not have an established policy in this respect. As a result annual reports do not publish information about a relevant policy as recommended by provision I.R.2 of the WSE Code.

The Company published the selected financial data for the last 5 years on the website in addition to the periodic financial reports to comply with provision I.Z.1.8 of the WSE Code.

On 30 June 2017 the Company published current division of duties and responsibilities for the Company's Directors on the website to comply with provisions I.Z.1.3, II.Z.1 of the WSE Code.

On 19 May 2017 the Company published on its corporate website the information about an absence of a specific internal audit rule as recommended by provision I.Z.1.11 of the WSE Code. The Company stated that it follows applicable Dutch laws regarding the audit company's rotation and the Company believes that the continuity of the external auditor limited by the applicable laws would be more beneficial for the shareholders and the Company. More information is published in the Company's Report on compliance with WSE Code and on its corporate website.

The Company explains why the following best practice provisions of the Code are not applied:

Principle 3.3 of the Code provides that the General Meeting of Shareholders shall determine the remuneration of the supervisory board members and that the remuneration of a supervisory board member is not dependent on the results of the company. In 2017 year the Remuneration Policy foresaw the Company's entitlement to grant an annual bonus to the Chairman of the Board of Directors. However, in 2018 year at the Annual General Meeting of shareholders the new Remuneration Policy will be adopted with no bonuses provided to any of the members of the Board of Directors, as well as to the Chairman of the Board of Directors.

In deviation from provision 2.3.2 and chapter 3 of the Code, the Company has not established a remuneration committee nor a selection and appointment committee. The remuneration of members of the Board of Directors of the Company is defined by shareholders on Annual General Meetings each year. The Board of Directors will conduct the relevant duties that are charged upon this committee on the basis of the Code.

Principles 2.2.1 of the Code provides that a management board member is appointed for a maximum period of four years, a member may be reappointed again for a term of not more than four years at a time. The Company does not comply with this best practice provision of the Code due to its Executive Directors Mr. Anatoliy Yurkevych and Mrs. Olga Yurkevich have been acting as an Executive Directors of the Company since 2007 year. Below the Company explains the reason for such reappointment.

Principle 2.2.2 of the Code provides that a supervisory board member is appointed for a maximum period of four years and may be reappointed one another four-year period. The supervisory board members may subsequently be reappointed again for a period of two years, which appointment may be extended by at most two years. The Company does not comply with this best practice provision of the Code due to Mr. Vyacheslav Rekov and Mr. Willem Scato van Walt Meijer have been acting as the Company's Non-Executive Directors since 2007 and 2010 years respectively. Below the Company explains the reason for such reappointment.

The Company believes that, in deviation from the provisions 2.2.1 and 2.2.2 of the Code, reappointment of the abovementioned members of the Board of Directors has a positive impact to the Company's business activity and that these members act in the best Company's interests. The Directors has a wide experience and a deep understanding of the Company's business processes and made a substantial contribution to the Company's development.

The Company's application of the Code is described in the Report on compliance by Milkiland N.V. with the revised Dutch Corporate Governance Code of 2016 as approved on 27 August 2017 by the Board of Directors, which can be found at:
http://www.milkiland.nl/en/investors/general_information/corporate_documents/
In 2018 the Company plans to publish the report on compliance with the revised Code in the 2017 financial year.

## Report of Non-Executive Directors

In 2017, Mr. Vitaliy Strukov resigned from the position of a Non-Executive Director. On the Annual General Meeting of Shareholders held in 2017 Mr. Pavlo Sheremeta was appointed as a new member of the Board of Directors as a Non-Executive Director. Mr. Vyacheslav Rekov, Mr. Willem Scato van Walt Meijer, Mr. Oleg Rozhko, and Mr. George Christopher Logusch proceeded to perform their duties as Non-Executive Directors of the Company. The profile of Non-Executive Directors of the Company is published at the Company's website.

The Non-Executive Directors are charged with supervising, monitoring and advising the Executive Directors with respect to all responsibilities of the Board of Directors. The statements of fulfillment of the independence criteria were provided by all Non-Executive Directors: Mr. Willem Scato van Walt Meijer, Mr. George Christopher Logusch, Mr. Oleg Rozhko, Mr. Vyacheslav Rekov, and Mr. Pavlo Sheremeta.

The Non-Executive Directors drew up the retirement schedule with the information regarding the total years of appointment and information on next reappointment of the members of the Board of Directors which is published at the Company's website.

In carrying out their tasks, all of the above mentioned Non-Executive Directors gave their advice and expertise for the best Company practice. Mr. Oleg Rozhko is the Chairman of the Board of Directors, Mr. Willem Scato van Walt Meijer is the Chairman of the Audit Committee and Mr. Vyacheslav Rekov and Mr. Pavlo Sheremeta are members of the Audit Committee. The Audit Committee met 10 (ten) times during the 2017 financial year. The duties of the Audit Committee were duly performed. The Audit Committee provided their Audit Committee Opinion which is a part of the Report.

Throughout the 2017 the Non-Executive Directors worked on creation and implementation the long term-value creation strategy and, as a part of this, had an active dialogue with the Executive Directors. As a result a new Code of Conduct of Milkiland N.V. was adopted by the resolution of the Board of Directors on 28 August 2017, which can be found at the Company's website: http://www.milkiland.nl/en/investors/general_information/corporate_documents/
The Non-Executive Directors monitor the execution of the Company's long-term value strategy and values by means of regular discussion and assessment of the development of the Company's strategy and values implementation and risks associated with them. There were no irregularities in the 2017 financial year that required interventions by the Non-Executive Directors.

## Remuneration policy and remuneration report

The objective of the Group's remuneration policy is to provide a compensation program allowing for the attraction, retention and motivation of members of the Board of Directors who have chartered traits, skills and background to successfully lead and manage the Company. The remuneration policy focuses on long-term value creation for the Company and its subsidiaries and takes into account the internal pay ratios within the Company.

The Remuneration Policy of the Company is adopted on 17 June 2011 and published on the Company's website: http://www.milkiland.nl/en/investors/general_information/corporate_documents/?PAGEN_2=1
The new Remuneration Policy of the Company is suggested by the Board of Directors on 23 February 2018 and will be approved on the Annual General Meeting of Shareholders. The new Remuneration Policy is based on best principles of the Code.

The remuneration of members of the Board of Directors is defined by shareholders on Annual General Meetings each year pursuant to proposals of the Board of Directors. The remuneration of the Board of Directors is not dependent on the results of the Company.

Individual-specific responsibilities are taken into consideration in respect of the determination and differentiation of the remuneration of the members of the Board of Directors.

The Group's policy towards the members of the Board of Directors and Key Executives, as well as employment contracts of the members of the Board of Directors and Key Executives do not provide for any benefits in the case of dismissal or termination of such person's service, employment contract or other similar agreement. The members of the Board of Directors and Key Executives are not granted any pensions, retirement or similar benefits.

Directors' remuneration stands for directors' fees, salaries of Executive Directors, bonuses and other incentive payments. The Company's remuneration policy in 2017 did not provide any reimbursement of Directors expenses.

Information about the remunerations accrued to the Company's Directors in 2017 for rendered services is presented in the table below.

| Name | Position in 2017 | Appointed | Gross Remuneration (EUR) | Period of accrual | Expenses reimbursement (EUR) | Total (EUR) |
|---|---|---|---|---|---|---|
| Oleg Rozhko | Chairman of the Board of Director | 22.06.2012 | 30,000 | from 01.01.2017 to 31.12.2017 | 0 | 30,000 |
| Olga Yurkevich | Executive Director, Chief Production Officer | 28.08.2007 | 25,000 | from 01.01.2017 to 31.12.2017 | 0 | 25,000 |
| Anatoliy Yurkevych | Executive Director, CEO | 28.08.2007 | 5,000 | from 01.01.2017 to 31.12.2017 | 0 | 5,000 |
| Vyacheslav Rekov | Non-executive Director, Member of Audit Committee | 28.08.2007 | 30,000 | from 01.01.2017 to 31.12.2017 | 0 | 30,000 |
| Willem Scato van Walt Meijer | Non-executive Director, Head of Audit Committee | 06.12.2010 | 50,000 | from 01.01.2017 to 31.12.2017 | 7,516 | 50,000 |
| George Christopher Logusch | Non-Executive Director | 21.06.2013 | 0 | from 01.01.2017 to 31.12.2017 | 0 | 0 |
| Pavlo Sheremeta | Non-Executive Director, Member of Audit Committee | 30.06.2017 | 25,000 | from 30.06.2017 to 31.12.2017 | 0 | 25,000 |

# REPRESENTATIONS OF THE BOARD OF DIRECTORS

## Representation of the Board of Directors on the Compliance of Annual Financial Statements

The Board of Directors hereby represents, to the best of its knowledge, that the statutory financial statements of the Company and its consolidated subsidiaries for the year ended 31 December 2017 are prepared in accordance with the applicable accounting standards and that they give a true and fair view of the assets, liabilities, financial position and the result of the Company and its consolidated subsidiaries, and that the report of the Board of Directors for the year ended December 31, 2017 gives a true and fair view of the position of the Company and its consolidated subsidiaries as at December 31, 2017 and of the development and the performance of the Company and its consolidated subsidiaries during the year ended December 31, 2017, including a description of the key risks that the Company is confronted with.

## Representation of the Board of Directors on Appointment of an Entity Qualified to Audit Annual Financial Statements

The Board of Directors hereby represents that Accon AVM, which performed the audit of the statutory financial statements of the Company for the year ended December 31, 2017, has been appointed in accordance with the applicable laws and that this entity and the accountants performing the audit met the conditions necessary to issue an impartial and independent report on the audit in accordance with the applicable provisions of law.

## Representation of the Board of Directors Relating to the System of Internal Control

In line with best practice provision 1.4.2 and provision 1.4.3 of the Code and bearing in mind the recommendations of the Code, the Company issues a declaration about the effectiveness of the system of internal control of the processes on which the financial reporting is based.

In 2017, the Board of Directors assessed the effectiveness of the system of internal controls for financial reporting. During the investigation on which this assessment was based, no shortcomings were identified that might possibly have a material impact on the financial reporting. On the basis of the results of the above assessment and the risk analysis that was carried out at the Company within the framework of governance and compliance, the Board is of the opinion, after consulting with the Audit Committee, that the system of internal controls provides a reasonable degree of certainty that the financial reporting contains no inaccuracies of material importance. There is an inherent limitation in that systems of internal control cannot provide an absolute degree (though they can provide a reasonable degree) of certainty in regards to the prevention of material inaccuracies in the financial reporting and the prevention of losses and fraud.

In our view the system of internal controls, focused on the financial reporting, functioned effectively over the past year. There are no indications that the system of internal controls will not function effectively in 2018.

## Representation of the Board of Directors on the long-term value creation and realisation

The Board of Directors is guided in its duties by the interests of the Company and its subsidiaries and focuses on the long-term value creation strategy, taking into careful consideration the relevant interests of its shareholders. The contributions made to the long-term value creation realization in the financial year 2017 are as follows:

- adoption of a new Code of Conduct of Milkiland N.V. on 28 August 2017, where the long-term value creation strategy is formulated, which can be found on the Company's website: http://www.milkiland.nl/en/investors/general_information/corporate_documents/
- making decision in line with the Company's long-term value creation strategy.

In 2018 the Board of Directors will continue developing and implementing the long-term value creation strategy as recommended by the best practice provisions of the Code

**Board of Directors of Milkiland N.V.**

**Amsterdam, 27 April 2018**

| | | |
|---|---|---|
| **A. Yurkevych** | **O. Yurkevich** | **O. Rozhko** |
| **V. Rekov** | **W.S. van Walt Meijer** | **G.C. Logusch** |
| **P. Sheremeta** | | |

# CONSOLIDATED FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2017

**MILKILAND N.V.**
**Consolidated statement of financial position**
(All amounts in euro thousands unless otherwise stated)

| | Notes | 31 December 2017 | 31 December 2016 |
|---|---|---|---|
| **ASSETS** | | | |
| **Current assets** | | | |
| Cash and cash equivalents | 6 | 1,416 | 1,044 |
| Trade and other receivables | 7 | 19,406 | 20,042 |
| Inventories | 8 | 8,713 | 12,878 |
| Current biological assets | 13 | 1,302 | 1,096 |
| Current income tax assets | | 783 | 434 |
| Other taxes receivable | 9 | 5,194 | 6,739 |
| | | **36,814** | **42,233** |
| **Non-current assets** | | | |
| Goodwill | 10 | 1,474 | 1,558 |
| Property, plant and equipment | 11 | 99,679 | 98,763 |
| Investment property | 12 | 16,732 | 19,971 |
| Non-current biological assets | 13 | 1,251 | 1,383 |
| Other intangible assets | 11 | 1,993 | 2,325 |
| Deferred income tax assets | 29 | 2,472 | 2,223 |
| | | **123,601** | **126,223** |
| **TOTAL ASSETS** | | **160,415** | **168,456** |
| **LIABILITIES AND EQUITY** | | | |
| **Current liabilities** | | | |
| Trade and other payables | 14 | 40,778 | 43,054 |
| Current income tax liabilities | | 807 | 71 |
| Other taxes payable | 15 | 5,474 | 4,130 |
| Short-term loans and borrowings | 16 | 75,800 | 87,293 |
| | | **122,859** | **134,548** |
| **Non-current liabilities** | | | |
| Loans and borrowings | 16 | 10,756 | 14,993 |
| Deferred income tax liabilities | 29 | 13,760 | 11,771 |
| Other non-current liabilities | | 118 | 230 |
| | | **24,634** | **26,994** |
| **Total liabilities** | | **147,493** | **161,542** |
| **Equity attributable to owners of the Company** | | | |
| Share capital | 17 | 3,125 | 3,125 |
| Share premium | | 48,687 | 48,687 |
| Revaluation reserve | 18 | 79,403 | 69,208 |
| Currency translation reserve | 19 | (38,042) | (34,297) |
| Retained earnings | | (81,481) | (80,918) |
| | | **11,692** | **5,805** |
| **Non-controlling interests** | | **1,230** | **1,109** |
| **Total equity** | | **12,922** | **6,914** |
| **TOTAL LIABILITIES AND EQUITY** | | **160,415** | **168,456** |

(All amounts in euro thousands unless otherwise stated)

| | Notes | 2017 | 2016 |
|---|---|---|---|
| Revenue | 21 | 140,411 | 146,758 |
| Cost of sales | 23 | (116,719) | (125,644) |
| **Gross profit** | | **23,692** | **21 114** |
| Selling and distribution expenses | 24 | (11,572) | (13,079) |
| Administrative expenses | 25 | (12,204) | (12,995) |
| Other income/(expenses), net | 26 | 672 | (535) |
| **Operating profit** | | **588** | **(5,495)** |
| Finance income | 27 | 1,130 | 18 |
| Finance expenses | 28 | (8,960) | (31,242) |
| Foreign exchange gain/(loss), net | | - | (5) |
| **Loss before income tax** | | **(7,242)** | **(36,724)** |
| Income tax expense | 29 | (104) | (2,182) |
| **Net loss for the year** | | **(7,346)** | **(38,906)** |
| **Other comprehensive income/(loss)** | | | |
| ***Items that will not be reclassified to profit or loss*** | | | |
| Gains on revaluation of properties | | 20,860 | (8,044) |
| Tax effect on revaluation of properties | | (3,555) | 1,826 |
| | | **17,305** | (6,218) |
| ***Items that may be subsequently reclassified to profit or loss*** | | | |
| Exchange differences on translating to presentation currency | | (3,951) | 16,097 |
| **Total other comprehensive income/(loss)** | | **13,354** | **9,879** |
| **Total comprehensive income/(loss)** | | **6,008** | **(29,027)** |
| **Loss attributable to:** | | | |
| Owners of the Company | | (7,672) | (38,804) |
| Non-controlling interests | | 326 | (102) |
| | | **(7,346)** | **(38,906)** |
| **Total comprehensive loss attributable to:** | | | |
| Owners of the Company | | 5,887 | (28,845) |
| Non-controlling interests | | 121 | (182) |
| | | **6,008** | **(29,027)** |
| **Earnings per share, EUR** | 33 | **(0.25)** | **(1.24)** |

(All amounts in euro thousands unless otherwise stated)

| | Notes | 2017 | 2016 |
|---|---|---|---|
| **Cash flows from operating activities:** | | | |
| **Loss before income tax** | | **(7,242)** | **(36,725)** |
| *Adjustments for:* | | | |
| Depreciation and amortization | 11 | 10,361 | 10,279 |
| (Gain)/loss from disposal and write off of inventories | 26 | 175 | 818 |
| Change in provision and write off of trade and other accounts receivable | 26 | 87 | 27 |
| Change in provision and write off of unrealized VAT | 26 | 131 | 500 |
| (Gain)/loss from disposal of non-current assets | 26 | (1,800) | 5 |
| (Gain)/loss on revaluation of property, plant and equipment | 26 | 1,130 | 502 |
| Change in fair value of biological assets | 0 | (269) | 52 |
| Operational foreign exchange results, net | 26 | (233) | (1,554) |
| Finance income | 27 | (1,130) | (18) |
| Finance expenses | 28 | 8,960 | 31,242 |
| Write off of accounts payable | 26 | (2) | (190) |
| **Operating cash flow before movements in working capital** | | **10,168** | **4,938** |
| Increase in trade and other accounts receivable | | (461) | 3,744 |
| Decrease/(increase) in inventories | | 2,464 | (1,197) |
| (Increase)/decrease in biological assets | | (172) | 775 |
| (Decrease)/increase in trade and other payables | | (1,266) | 7,015 |
| Decrease/(increase) in other taxes receivable | | 20 | (1,724) |
| Increase/(decrease) in other taxes payable | | 2,181 | 2,012 |
| **Net cash provided by operations** | | **12,934** | **15,563** |
| Income taxes paid | | (449) | (711) |
| Interest received | | 32 | 1 |
| Interest paid | | (1,521) | (5,313) |
| **Net cash provided by operating activities** | | **10,996** | **9,540** |
| **Cash flows from investing activities:** | | | |
| Acquisition of property, plant and equipment | | (2,811) | (1,653) |
| Proceeds from sale of property, plant and equipment | | - | 131 |
| Acquisition of subsidiaries, net of cash acquired | | - | (793) |
| **Net cash used in investing activities** | | **(2,811)** | **(2,315)** |
| **Cash flows from financing activities:** | | | |
| Proceeds from borrowings | | 2,298 | 19,495 |
| Repayment of borrowings | | (10,222) | (26,574) |
| Dividends paid | 20 | - | - |
| Commissions paid | | - | (23) |
| **Net cash provided by/(used in) financing activities** | | **(7,924)** | **(7,102)** |
| **Net decrease in cash and equivalents** | | **261** | **123** |
| **Cash and equivalents, beginning of year** | 6 | **1,044** | **907** |
| Effect of foreign exchange rates on cash and cash equivalents | | 111 | 14 |
| **Cash and equivalents, end of year** | 6 | **1,416** | **1,044** |

**MILKILAND N.V.**
**Consolidated statement of changes in equity**
(All amounts in euro thousands unless otherwise stated)

| | | Attributable to equity holders of the company | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Notes | Share capital | Share premium | Foreign currency translation reserve | Revaluation reserve | Retained earnings | Total stockholders' equity | Non-controlling interests | Total equity |
| **Balance at 1 January 2017** | | **3,125** | **48,687** | **(34,297)** | **69,208** | **(80,918)** | **5,805** | **1,109** | **6,914** |
| Profit/(loss) for the year | | - | - | - | - | (7,672) | **(7,672)** | 326 | **(7,346)** |
| Revaluation of PPE | | - | - | - | 17,305 | - | **17,305** | - | **17,305** |
| Other comprehensive gain/(loss), net of tax effect | | - | - | (3,745) | (1) | - | **(3,746)** | (205) | **(3,951)** |
| **Total comprehensive income for the year** | | **-** | **-** | **(3,745)** | **17,304** | **(7,672)** | **5,887** | **121** | **6,008** |
| Realized revaluation reserve, net of income tax | 18 | - | - | - | (7,109) | 7,109 | **-** | - | **-** |
| **Balance at 31 December 2017** | | **3,125** | **48,687** | **(38,042)** | **79,403** | **(81,481)** | **11,692** | **1,230** | **12,922** |
| | | | | | | | | | |
| **Balance at 1 January 2016** | | **3,125** | **48,687** | **(48,651)** | **79,866** | **(48,377)** | **34,650** | **1,291** | **35,941** |
| Profit/(loss) for the year | | - | - | - | - | (38,804) | **(38,804)** | (102) | **(38,906)** |
| Revaluation of PPE | | - | - | - | (6,220) | - | **(6,220)** | - | **(6,220)** |
| Other comprehensive gain/(loss), net of tax effect | | - | - | 14,354 | 1,825 | - | **16,179** | (80) | **16,099** |
| **Total comprehensive income for the year** | | **-** | **-** | **14,354** | **(4,395)** | **(38,804)** | **(28,845)** | **(182)** | **(29,027)** |
| Realized revaluation reserve, net of income tax | 18 | - | - | - | (6,263) | 6,263 | **-** | - | **-** |
| **Balance at 31 December 2016** | | **3,125** | **48,687** | **(34,297)** | **69,208** | **(80,918)** | **5,805** | **1,109** | **6,914** |

## Notes to the consolidated financial statements

### 1 The Group and its operations

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as endorsed by the European Union for the year ended 31 December 2017 for Milkiland N.V. (the “Company”) and its subsidiaries (together referred to as “the Group” or “Milkiland”).

The financial statements were approved by the Board of Directors of the Company on 27 April 2018 and are subject to adoption by the shareholders during the General Shareholders Meeting.

The Company was incorporated on 13 July 2007 under Dutch law as a private limited liability company (B.V.). On May 23, 2009 the Company was converted into a public limited liability company (N.V.). The address of its registered office is Amsterdamse Bos, Cuserstraat 93, 1081 CN Amsterdam, the Netherlands and the principal place of business is 9, Boryspilska Str., 02090, Kyiv, Ukraine.

As at 31 December 2017 the Company is controlled by 1, Inc. Cooperatief (holding 73.52% of shares). The Company is ultimately controlled by Anatoliy Yurkevych and Olga Yurkevich. Commencing from 6 December 2010, the Company became listed on the Warsaw Stock Exchange having placed 20% of newly issued and 2.4% of existing shares to investors.

The Company mainly acts as a holding company and exercises control over the operations of its subsidiaries.

Milkiland is a diversified dairy processing Group, producing and distributing dairy products in EU and CIS, with the key markets in Russia, Ukraine and Poland. The production facilities of the Group are located in these 3 countries and are able to process up to 1,330 thousand tons of milk per year. The plants purchase milk from local farmers and produce different kind of dairy products, including, cheese, butter, whole-milk products, as well as dry milk products.

As at 31 December 2017, the Group employed 3,447 people (2016: 4,460 people).

For the period from 1 January 2017 to 31 December 2017 the Company had the following direct and indirect subsidiaries:

| Name | Country of incorporation | Principal activity | Effective share of ownership 31 December 2017 | 31 December 2016 |
|---|---|---|---|---|
| MLK Finance Limited | Cyprus | Trade | 100.0% | 100.0% |
| Milkiland Intermarket (CY) LTD | Cyprus | Trade | 100.0% | 100.0% |
| LLC Milkiland-Kazakhstan | Kazakhstan | Trade | 100.0% | 100.0% |
| Milkiland EU sp. z.o.o. | Poland | Managing/Trade | 100.0% | 100.0% |
| Ostrowia sp. z.o.o | Poland | Production entity | 100.0% | 100.0% |
| UA TRADE Sp. z o.o. | Poland | Trade | 100.0% | 100.0% |
| JSC Ostankino Dairy | Russia | Production entity | 100.0% | 100.0% |
| LLC Ostankino Dairy | Russia | Production entity | 100.0% | - |
| LLC Milkiland RU | Russia | Managing/Trade | 100.0% | 100.0% |
| LLC Moloko-Kursk | Russia | Production entity | 100.0% | 100.0% |
| LLC Novomoskovsk Dairy Combine | Russia | Production entity | 100.0% | 100.0% |
| DE Aromat | Ukraine | Production entity | 100.0% | 100.0% |
| PE Prometey | Ukraine | Production entity | 100.0% | 100.0% |
| PE Ros | Ukraine | Production entity | 100.0% | 100.0% |
| LLC Malka-trans | Ukraine | Production entity | 100.0% | 100.0% |
| LLC Mirgorodsky Cheese Plant | Ukraine | Production entity | 100.0% | 100.0% |
| LLC Kyiv Milk Plant #1 | Ukraine | Trade | 100.0% | 100.0% |
| JSC Chernigiv Milk Plant | Ukraine | Production entity | 76.0% | 76.0% |
| PrJSC Gorodnia Milk Plant | Ukraine | Production entity | 95.2% | 95.2% |
| LLC Agrosvit | Ukraine | Agricultural | 100.0% | 100.0% |
| DE Milkiland Ukraine | Ukraine | Managing company | - | 100.0% |
| LLC Milkiland Ukraine | Ukraine | Managing company | 100.0% | 100.0% |
| DE Borznyanskiy Milk Plant | Ukraine | Production entity | 100.0% | 100.0% |
| LLC Moloko-Kraina | Ukraine | Production | 100.0% | 100.0% |
| LLC Torgovyi dim Milkiland | Ukraine | Trade | 100.0% | 100.0% |
| LLC Ukrainian Milk House | Ukraine | Trade | 100.0% | 100.0% |
| LLC Milkiland Intermarket | Ukraine | Trade | 100.0% | 100.0% |
| LLC Milkiland N.V | Ukraine | Managing company | 100.0% | 100.0% |
| PrJSC Transportnyk | Ukraine | Service provider | 70.3% | 70.3% |
| LLC Milkiland Agro | Ukraine | Agricultural | 100.0% | 100.0% |
| PJSC Iskra | Ukraine | Agricultural | - | 70.8% |
| LLC Iskra-Sloboda | Ukraine | Agricultural | - | 100.0% |
| DE Agrolight | Ukraine | Production entity | 100.0% | 100.0% |
| DE Krasnosilsky Milk | Ukraine | Agricultural | 100.0% | 100.0% |
| LLC Bahmachregionpostach | Ukraine | Grain elevator | 100.0% | 100.0% |
| ALLC Nadiya | Ukraine | Agricultural | 100.0% | 100.0% |
| LLC Uspih-Mena-Plus | Ukraine | Agricultural | 100.0% | 100.0% |
| LLC Agro-Mena | Ukraine | Agricultural | 100.0% | 100.0% |
| LLC Lendinvest 3000 | Ukraine | Investment assets | 100.0% | 100.0% |
| LLC Agrolendinvest | Ukraine | Investment assets | 100.0% | 100.0% |
| LLC Phobostrade | Ukraine | Investment assets | 100.0% | 100.0% |
| LLC Kilchensky Berig | Ukraine | Investment assets | 100.0% | 100.0% |
| PrJSC Iskra Plus | Ukraine | Agricultural | 98.1% | - |
| LLC Kholod Property | Ukraine | Production entity | 100.0% | - |
| LLC Syrnyy Mayster | Ukraine | Production entity | 100.0% | - |
| Milkiland Corporation | Panama | Trade | 100.0% | 100.0% |
| Newholm Systems S.A. | Panama | Trade | 100.0% | 100.0% |
| Agrointer Corporation | Panama | Trade | 100.0% | 100.0% |
| LLC Cross Value | Marshall Isl. | Trade | 100.0% | 100.0% |
| Dominic Supreme LP | Scotland | Trade | 100.0% | - |

During the year ended 31 December 2017, the Group finalized registration of new subsidiaries PrJSC Iskra Plus, LLC Kholod Property, LLC Syrnyy Mayster in Ukraine, LLC Ostankino Dairy in Russia and Dominic Supreme LP in Scotland.

During the year ended 31 December 2017 PJSC Iskra, LLC Iskra-Sloboda and DE Milkiland Ukraine were sold to third parties.

LLC Molochni vyroby was renamed to LLC Milkiland Ukraine.

***Going concern assumptions.***
The Group conducts significant part of its operations in Russia and Ukraine. On the back of the conflict between these two countries, which, *inter alia,* led to the closure of traditional Russian markets for Ukrainian dairy, as well as the implementation of the sanctions against Russia by US, EU and several other countries, macroeconomic situation in both countries in 2014-2015 deteriorated significantly. In particular, in 2014-2015 Ukraine faced a full scale economic crisis with the GDP drop, declining international trade and deep devaluation of the national currency. At the same time, Russian economy came to stagnation. The real income of the population in Russia and Ukraine deteriorated, which triggered the contraction of the consumption of the FMCG goods, including dairy.

The closure of the traditional Russian export market for the Group's Ukrainian and Polish subsidiaries, deep devaluation of Russian Rouble and Ukrainian hryvnya, decline of the demand for dairy in Russia and Ukraine made an adverse effect at the Group's financial position and performance in 2014-2015.

The macroeconomic stabilization of 2016 and the return of the economies of Ukraine and Russia to growth in 2017 (for additional details please refer *CEO and Chairman's Statement)* provides to Milkiland an opportunity to capitalize on growing customers confidence and, in the nearest years, restoration of the demand for quality dairy in these key markets for the Group's business. But the timing and the dynamics of this process in not currently determinable. Due to this, adverse effect of still limited customer demand, as well as remained macroeconomic imbalances, for example, expected further devaluation of UAH, may adversely affect the Group's operations and financial performance.

As at 31 December 2017 the Group was in breach of certain financial covenants under a few bank loans mostly due to devaluation of the local currency (Please refer to Note 16, Note 31). This situation started in 2014 and is still applicable. Non-compliance with covenants gives banks a formal right to demand early repayment of loans. The management notified all banks about expected prospective non-compliances. Based on the negotiations with the main lenders about loans restructuring, the management believes that the banks will not demand accelerated repayment of the loans because of breaches of covenants in 2017.

In the course of 2017, Arbitrage Court of the City of Moscow declared the JSC "Ostankino Dairy" bankrupt based at the claim of one of its Creditors, Bank "Vozrozhdenie" (for more information please refer *Material Factors and Events).* This event caused a possible material threat to the going concern ability of Milkiland and its operations in the Russian market and Moscow region. The ability of the company to continue its operations there is dependent on coming negotiations during the bankruptcy procedures and finding of the mutually acceptable solution of the settlement of the indebtedness to Ostankino's Creditors. Discontinuation of the Russian activities could impose a negative effect on the Going Concern ability of the Group. Please refer to note 35 for more information on this issue.

The above could materially affect the ability of Milkiland to continue as a going concern. The Group is dependent on its ability to settle the indebtedness to the Creditors in a mutually acceptable manner without entering to the enforcement and early repayment procedures.

## 2 Summary of significant accounting policies

***Basis of presentation.*** These consolidated financial statements of the Group have been prepared in accordance with the requirements of International Financial Reporting Standards (further - IFRS) as endorsed by the European Union and also comply with the financial reporting requirements included in Part 9 of Book 2 of the Dutch Civil Code.

These consolidated financial statements of the Group have been prepared using the historical cost convention, as modified by the revaluation of property, plant and equipment, and certain financial instruments measured in accordance with the requirements of IAS 39 *Financial instruments: recognition and measurement.*

***New and revised Standards and Interpretations to be applied by the Company***

On the whole, the accounting policies adopted are consistent with those of the previous financial year. Certain new IFRSs and Interpretations became effective from 1 January 2017. Listed below are those new or amended standards or interpretations which could be relevant to the Company:

Amendments to IAS 7 Disclosure Initiative, IAS 12 Recognition of Deferred Tax Assets for Unrealised Losses and Disclosure of Interests in Other Entities The amendments 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.

IAS 12 Recognition of Deferred Tax Assets for Unrealised Losses

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 recognized in opening retained earnings (or in another component of equity, as appropriate), without allocating the change between opening retained earnings and other components of equity.

IFRS 12 *Disclosure of Interests in Other Entities.*

Amendments have been made to clarify the scope of IFRS 12 in respect of interests in entities within the scope of IFRS 5 Non-current Assets Held for Sale and Discontinued Operations. Specifically it clarifies that entities are not exempt from all of the disclosure requirements in IFRS 12 when entities have been classified as held for sale or as discontinued operations.

The standard as amended therefore makes it clear that it is only the disclosure requirements set out in paragraphs B10 – 16 that do not need to be provided for entities within the scope of IFRS 5.

Adoption of these improvements did not have any impact on the Company's financial statements.

***IFRS and IFRIC interpretations not yet effective***

The Company has not applied the following IFRSs and Interpretations to IFRS and IAS that have been issued but are not yet effective:

IFRS 9 *Financial Instruments.* In July 2014, the IASB issued the final version of IFRS 9 which reflects all phases of the financial instruments project and replaces IAS 39 *Financial Instruments: Recognition and Measurement* and all previous versions of IFRS 9. The standard introduces new requirements for 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. Retrospective application is required, but comparative information is not compulsory. As the main financial assets used by the Company are limited to trade and other receivables, the adoption of IFRS 9 will not have a significant effect on the classification, valuation and measurement of the Company's financial assets. The company does not use hedging or derivatives accounting of which could be impacted by the new standard. The adoption of IFRS 9 will have no impact on the classification and measurement of the Company's financial liabilities.

IFRS 15 *Revenue from Contracts with Customers*. IFRS 15 establishes a new five-step model that will apply to revenue arising from contracts with customers. Under IFRS 15 revenue is recognized 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 principles in IFRS 15 provide a more structured approach to measuring and recognizing revenue.

This standard introduces a 5-step approach to revenue recognition and measurement:

Step 1: Identify the contract with a customer;
Step 2: Identify the performance obligations in the contract;
Step 3: Determine the transaction price;
Step 4: Allocate the transaction price to performance obligations in the contract; and
Step 5: Recognise revenue when (or as) the entity satisfies a performance obligation.

Company mainly recognizes the revenue at the point of time, when it transfers control over the products or services to a clients. Given the fact, that crucial part of the trading of the Company is made through sales of finished goods without any compound performance obligations, warranty period or any other services for its products, franchise, licenses, bundled offers etc., - the Company does not anticipate significant changes in the Financial Statement, as the result of the new standard implementation, except of non-significant changes, including in accounting of wholesalers loyalty programs (retro-bonuses). These bonuses dropped significantly due to the changes of legislation in the countries of the Group's operations.

The presentation and disclosure requirements of IFRS 15 are more detailed than under current IFRS, so the Group expects that the notes to the financial statements will be expended.

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.

The management of the company expects the amount of payments under leasing contracts at the level of about EUR 560 thousands at the year ended 31 December 2018.

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.

Please refer to the note 16 for detailed information regarding to the leasing agreements of the Company.

*IFRS 17 Insurance Contracts*. IAFR 17 is the new financial reporting standard for insurance contracts that addresses the recognition and measurement, presentation and disclosure of information. IFRS 17 will replace IFRS 4 Insurance Contracts, which was issued in 2005. IFRS 17 applies to all types of insurance contracts (life insurance and insurance other than life insurance, direct insurance and reinsurance), regardless of the type of an entity that issues them, as well as certain guarantees and financial instruments with discretionary participation conditions. There are several exceptions from the scope of application.

IFRS 17 becomes effective for reporting periods beginning on or after 1 January 2021, and comparative information is required. Earlier application is permitted provided that the entity also applies IFRS 9 and IAS 15 on or before the date of the first application of IAS 17. This standard is not applicable to the Company.

Amendments to IFRS 2 *Share-based Payment: Classification and Measurement of Share-based Payment Transactions.*

Amendments to IFRS 2 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. These amendments will not have any impact on the Company's financial statements.

Amendments to IFRS 4 *Insurance Contracts-Application of IFRS 9 Financial Instruments together with IFRS Insurance Contracts.*

These amendments eliminate the problems arising from the application of the new standard relating to financial instruments, IFRS 9, before the introduction of IAS 17 *Insurance Contracts*, which supersedes IFRS 4. The amendments provide for two options for entities issuing insurance contracts: temporary exemption from IFRS 9 and the overlay approach.

Amendments are effective for annual periods beginning on or after 1 January 2018. The amendments will have no impact on the Company's financial statements.

*Amendments to IFRS 10 Consolidated Financial Statements and IAS 28 Investments in Associates and Joint Ventures - 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 10, between an investor and its associate or joint venture, is recognized in full. Any gain or loss resulting from the sale or contribution of assets that do not constitute a business, however is recognized only to the extent of unrelated investors' interest 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.

Amendments to IAS 40 *Investment property*. The IASB has amended IAS 40 on transfers of property assets to, or from, investment property. A transfer is made when and only when there is an actual change in use – i.e. an asset meets or ceases to meet the definition of investment property and there is evidence of the change in use. A change in management intention alone does not support a transfer. The revised examples of evidence of a change in use included in the amended version of IAS 40 are not exhaustive – i.e. other forms of evidence may support a transfer.

Amendments are effective for annual periods beginning on or after 1 January 2018. Early application is permitted. The amendments will have no impact on the Company's financial statements.

IFRIC 22 Foreign *Currency Transactions and Advance Consideration.*

IFRIC 22 addresses how to determine the date of transaction for the purpose of determining the spot exchange rate used to translate foreign currency transactions on initial recognition in circumstances when an entity pays or receives some or all of the foreign currency consideration in advance of the recognition of the related asset, expense or income.

The interpretation states that the date of the transaction, for the purpose of determining the spot exchange rate used to translate the related asset, expense or income (or part thereof) on initial recognition, is the earlier of:

(a) The date of initial recognition of the non-monetary prepayment asset or the non-monetary income liability; and

(b) The date that the asset, expense or income (or part thereof) is recognised in the financial statements.

The amendment becomes effective for annual periods beginning on or after 1 January 2018. Early application is permitted. The amendments will have no impact on the Company's financial statements.

IFRIC 23 *Uncertainty over Income Tax Treatments.*

Whenever requirements of tax legislation are unclear in relation to a particular operation or to specific circumstances, the main criterion is whether the probability is high that the tax authority will agree with the tax claims interpretation chosen by an entity.

If the answer is positive, the entity shall reflect the same amount in the financial statements and consider the need to disclose the existence of uncertainty. If the answer is negative, the amount reported in the financial statements will differ from the amount in the tax return, because it is estimated taking into account the existing uncertainty.

To reflect this uncertainty, one of the following two estimation methods is used, depending on which one will allow to a high accuracy to predict the outcome of the uncertainty:

- the most likely amount, or

- the expected value.

The Interpretation also requires that judgments and estimates that have been formed by the entity were reviewed in the event of a change in facts and circumstances - for example, due to a tax audit or actions taken by the tax authorities, subsequent changes to the tax rules, or after the expiration of the period during which the tax authority has the right to verify the correctness of the tax calculation.

The interpretation is applied to annual periods beginning on or after 1 January 2019, early application is permitted. Currently the Company is assessing the impact of IFRIC 23 application on the financial statements.

There are no other IFRSs or IFRIC interpretations that are not yet effective that would be expected to have a material impact on the Group.

***Consolidated financial statements***. Subsidiaries are all entities (including structured entities) over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are deconsolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries. The cost of an acquisition is measured at the fair value of the assets given up, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured at their fair values at the acquisition date, irrespective of the extent of any non-controlling interest. The excess of the cost of acquisition over the fair value of the net assets of the acquired company at each exchange transaction represents goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized directly in the statement of comprehensive income.

All intergroup transactions, balances and unrealized gains on transactions between Group companies are eliminated; unrealized losses are also eliminated unless the cost cannot be recovered. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies of the Group.
Non-controlling interest is that part of the net results and of the net assets of a subsidiary, including the fair value adjustments, which is attributable to interests which are not owned, directly or indirectly, by the Group. Non-controlling interest forms a separate component of the Group’s equity.

***Segment reporting***. Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the Board of Directors that makes strategic decisions.

***Government grants***. Government grants received on capital expenditure are included in other non-current liabilities and amortized during the useful life of the asset purchased. Grants for revenue expenditure are netted against the cost incurred by the Group. Where retention of a government grant is dependent on the Group satisfying certain criteria, it is initially recognized as deferred income. When the criteria for retention have been satisfied, the deferred income balance is released to the consolidated statement of comprehensive income or amortized during the useful life of the asset purchased.

***Property, plant and equipment.*** Property, plant and equipment is stated at fair value in accordance with IAS 16 and IFRS 13. Fair value is determined by external appraisers who use either the market or cost approach for determining fair value.
Valuation of property and equipment is performed frequently enough to ensure that the fair value of a revalued asset does not differ materially from its carrying amount. Fair value is based on the valuations by external independent appraisal agencies.

Depreciation is charged to the consolidated statement of comprehensive income on a straight line basis to allocate costs of individual assets to their residual value over their estimated useful lives of the assets:

| | Useful life, years |
|---|---|
| Buildings, constructions | 20-50 |
| Plant and equipment | 5-30 |
| Other | 1-15 |

Construction in progress represents the cost of property, plant and equipment, including advances to suppliers, which has not yet been completed. No depreciation is charged on such assets until they are available for use.

Any revaluation surplus is credited to the asset revaluation reserve included in the net assets attributable to participants in the consolidated statement of financial position, except to the extent that it reverses a revaluation decrease of the same asset previously recognized in profit or loss, in which case it is recognized in profit or loss. A revaluation discount is recognized in profit or loss, except that a discount directly compensates a previous surplus of the carrying amount of these assets during a previous period and refers to the revaluation reserve.

An annual transfer from the asset revaluation reserve to retained earnings is made for the difference between the depreciation based on the revaluation carrying amount of the asset and depreciation based on the asset original cost. Additionally, accumulated depreciation as at the revaluation date is eliminated with immediate decrease of the gross carrying amount of the asset and the net amount is restated to the revalued amount of the asset. Upon disposal, any revaluation reserve relating to the particular asset being sold is transferred to retained earnings.

When each major inspection is performed, its cost is recognized in the carrying amount of the plant and equipment as replacement if the recognition criteria are satisfied.

An item of property and equipment is derecognized upon disposal or when no future economic benefits are expected from its use. Any gain or loss arising on retirement of the asset (calculated as the difference between the net disposals proceeds and the carrying amount of the asset) is included in the statement of comprehensive income in the year the asset is derecognized.

The asset's residual values, useful lives and methods of depreciation are reviewed, and adjusted if appropriate, at each financial year end.

***Intangible assets***. Intangible assets acquired separately are measured on initial recognition at an original cost. The original cost of intangible assets acquired in a business combination is their fair value as at the date of acquisition. Following the initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses. Internally generated intangible assets, excluding capitalized development costs, are not capitalized and expenditure is reflected in the statement of comprehensive income in the reporting year in which the expenditure is incurred.

The useful lives of intangible assets are assessed to be definite.

Intangible assets with definite lives are amortized over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and the amortization method for an intangible asset with a definite useful life are reviewed at least at each reporting year-end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortization period or method, as appropriate, and treated as changes in accounting estimates. The amortization expense on intangible assets with definite lives is recognized in the statement of comprehensive income in the expense category consistent with the function of the intangible asset.

Software is amortized under the straight-line method over its useful life comprising 2-4 years.
Trade Marks of purchased subsidiaries are amortized under the straight-line method over its useful life comprising 10 years.
Land lease rights of purchased subsidiaries are amortized under the straight-line method over its useful life comprising 5-7 years.
***Investment property.*** Investment property is stated at fair value in accordance with IAS 40 and IFRS 13. Fair value is determined by external appraisers who use multiple valuation techniques: cost approach and income approach for determining fair value.
Valuation of investment property is performed frequently enough to ensure that the fair value of a revalued asset does not differ materially from its carrying amount. Fair value is based on valuations by external independent appraisal agencies.

***Goodwill.*** Goodwill represents the excess of the cost of an acquisition over the fair value of the acquirer's share of the net identifiable assets, liabilities and contingent liabilities of the acquired subsidiary at the date of exchange. Goodwill on acquisitions of subsidiaries is included in Intangible assets in the statement of financial position. Goodwill is carried at cost less accumulated impairment losses, if any.

Goodwill is allocated to cash generating units for the purposes of impairment testing. The allocation is made to those cash generating units or groups of cash generating units that are expected to benefit from the business to which the goodwill arose.

***Impairment of non-financial assets.*** The Group assesses at each reporting date whether there is an indication that an asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the Group makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. 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. Impairment losses of continuing operations are recognized in the Statement of comprehensive income in those expense categories consistent with the function of the impaired asset.

An assessment is made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognized impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. If that is the case the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior years. Such reversal is recognized in profit or loss. After such a reversal the depreciation charge is adjusted in future periods to amortize the asset's revised carrying amount, less any residual value, on regular basis over its remaining useful life.

***Biological assets.*** The Group classifies livestock (primarily cattle) and unharvested crops as biological assets. Biological assets are carried at their fair value less estimated costs to sell, except when the fair value cannot be measured reliably. If fair value cannot be measured reliably, biological assets are carried at cost less accumulated depreciation and accumulated impairment losses. Costs to sell are the incremental costs directly attributable to the disposal of an asset, excluding finance costs and income taxes.

Management's estimation of the useful lives of livestock amounts to 8 years.

Gain (loss) from changes in fair value of biological assets included in the consolidated statement of comprehensive income represents the net difference between the excess of the fair value less estimated costs to sell of biological assets over their total cost at the end of reporting period, and the corresponding amount at the beginning of the reporting period.

***Agricultural produce.*** The Group classifies harvested crops as agricultural produce. After harvesting, agricultural produce is treated as inventories.

***Inventories.*** Inventories are valued at the lower of cost and realizable value.

Inventory is accounted for at FIFO method.

Cost includes acquisition costs and the costs related to inventories delivery to their location and bringing to the working condition.

Cost of the inventories manufactured and production in progress includes the cost of raw materials, direct labor input and other direct expenses, as well as appropriate overheads (as calculated in conditions of ordinary use of production capacities). Net realizable value is the estimated selling price less all estimated production costs and the estimated business and distribution costs.

***Financial instruments.*** Financial instruments reported in the Group's statement of financial position include financial investments, loans provided, trade and other receivables, cash and cash equivalents, loans received, trade and other accounts payable. Financial instruments initially are stated at fair value plus transaction costs, except financial instruments at fair value through profit and loss. Financial instruments are stated in the statement of financial position at the moment of bargain in respect of an appropriate financial instrument. Valuation order of financial instrument will be considered below.

Financial instrument or some part of a financial instrument is written off in the financial statements when the Group loses its rights or repays liabilities related to this financial instrument. When financial asset is written off, the difference between received and accrued compensation and carrying amount is recognized in the statement of comprehensive income. When a financial liability is written off, the difference between paid or accrued compensation and a current carrying amount is recognized in the statement of comprehensive income.

***Recognition of financial instruments.*** The Group recognizes financial assets and liabilities in its consolidated statement of financial position when, and only when, it becomes a party to the contractual provisions of the instrument. Financial assets and liabilities are recognized using trade date accounting.

Financial assets and liabilities are offset and the net amount is reported in the consolidated statement of financial position when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

In compliance with IAS 39 financial assets are divided into 4 categories as follows:

- financial assets at fair value through profit and loss;
- loans and accounts receivable;
- investments held to maturity;
- financial assets available for sale.

When a financial asset or financial liability is recognized initially, it is measured at its fair value plus, in the case of a financial asset or financial liability not at fair value through profit and loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset. When the Group becomes a contractual party, it determines embedded derivatives in the contract, if any. Embedded derivatives are separated from the host contract that is not assessed at fair value through profit or loss in case the economic character and risks of embedded derivatives materially differ from similar quotients of the host contract.

The Group determines the classification of its financial assets after initial recognition and, where allowed or appropriate, revaluates this designation at each financial year-end.

All acquisition or sale transactions related to financial assets on `standard terms` are recognized at the transaction date, i.e. at the date when the Group undertakes an obligation to acquire an asset. Acquisition or sale transactions on `standard terms` mean acquisition or sale of financial assets that requires to supply an asset within the term determined by legislation or rules accepted in a certain market.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in the active market. Such assets are reflected at amortized cost using the effective interest method after their initial evaluation. Amortized cost is calculated taking into account all discounts or bonuses that arose at acquisition and includes commissions being an integral part of the efficient interest rate as well as transaction costs. Gains and expenses are recognized in the statement of comprehensive income when assets are derecognized or impaired, as well as through the amortization process.
After initial recognition, extended loans are measured at fair value of the funds granted that is determined using the effective market rate for such instruments, if they materially differ from the interest rate on such loan granted. In future loans are measured at amortized cost using the effective interest rate method. Difference between the fair value of the funds granted and loan reimbursement amount is reported as interest receivable during the whole period of the loan. Amortized cost is calculated taking into account all transaction expenses and discounts or bonuses that arose at repayment.

Loans that mature more than 12 months after the consolidated statement of financial position date are included into non-current assets.

Cash and cash equivalents comprise cash balances and call deposits with original maturities of three months or less. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purpose of the consolidated statement of cash flows.

Investments held-to-maturity

If the Group has the positive intent and ability to hold debt securities to maturity, then such financial assets are classified as held-to-maturity. Held-to-maturity financial assets are recognized initially at fair value plus any directly attributable transactions costs. Subsequent to initial recognition held-to-maturity financial assets are measured at amortized cost using the effective interest method, less any impairment losses. Any sale or reclassification of a more than insignificant amount of held-to-maturity investments not close to their maturity would result in the reclassification of all held-to-maturity investments as available-for-sale, and prevent the Group from classifying investment securities as held-to-maturity for the current and the following two financial years.

Fair value

The Group disclose the classification of financial assets and financial liabilities measured at fair value using a fair value hierarchy that reflects the significance of the inputs used in making the fair value measurement. The fair value hierarchy has the following levels:

- quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1);
- inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices) (Level 2); and

- inputs for the asset or liability that are not based on observable market data (unobservable inputs) (Level 3).

The level in the fair value hierarchy within which the financial asset or financial liability is categorized is determined on the basis of the lowest level input that is significant to the fair value measurement. Financial assets and financial liabilities are classified in their entirety into only one of the three levels.

The estimated fair value of financial instruments and liabilities is determined by reference to market information using appropriate methods of evaluation. However, a qualified opinion would be necessary to interpret marketing information for the purpose of fair value estimation. Correspondingly, at evaluation it is not necessary to indicate the estimated realization amount. Using different marketing assumptions and/or valuation techniques might affect the fair value significantly.

The estimated fair value of financial assets and financial liabilities is determined using the discounted cash flows model and other appropriate valuation methods at the year-end; it does not indicate the fair value of such instruments at the reporting date of these consolidated financial statements. Such estimations do not report any bonds or discounts that might result from the proposal to sell simultaneously the whole package of certain financial instruments of the Group. The fair value estimation is based on assumptions as to future cash flows, current economic situation, risks inherent to various financial instruments and other factors.

The fair value estimation is based on existing financial instruments without any attempts to determine the cost of an expected futures transaction and the cost of assets and liabilities not considered to be financial instruments. Besides, tax ramification (branching) related to realization of non-realized profit and loss might impact the fair value estimation and therefore was not accounted for in these consolidated financial statements.

Financial assets and financial liabilities of the Group include cash and cash equivalents, receivables and payables, other liabilities and loans. Accounting policy as to their recognition and evaluation are presented in the relevant sections of these notes.
During the reporting period the Group did not use any financial derivatives, interest swaps or forward contracts to reduce currency or interest risks.

Fair value of biological assets

Due to the absence of an active market as defined by International Accounting Standard IAS 41 Agriculture, the fair value of biological assets is estimated by present valuing the net cash flows expected to be generated from the assets discounted at a current market-determined pre-tax rate.

Fair value of agricultural produce

Management estimates the fair value of agricultural produce not sold at the end of reporting period by reference to quoted prices in an active market, as required by International Accounting Standard IAS 41. In addition, costs to sell at the point of harvest are estimated and deducted from the fair value. The fair valueless costs to sell becomes the carrying value of inventories at the date of harvesting.

Non-derivative financial liabilities

At initial recognition financial liabilities can be attributed to those estimated at fair value through profit and loss, if the following criteria are met: (i) attributing to this category excludes or materially reduces inconsistence in accounting methods that might otherwise arise at liability assessment or recognition of profit or loss related to such liability; (ii) liabilities comprise a part of financial liability group that is being managed and results of which are assessed at fair value in compliance with risks management policy; (iii) financial liability includes an embedded derivative that should be reported separately in the consolidated financial statements.

As at 31 December 2017 the Group had no financial liabilities that could be attributed to those estimated at fair value through profit and loss. Trade payables and other short-term monetary liabilities, which are initially recognized at fair value, subsequently carried at amortized cost using the effective interest method. Interest bearing liabilities are subsequently measured at amortized cost using the effective interest rate method, which ensures that any interest expense over the period to repayment is at a constant rate on the balance of the liability carried in the consolidated statement of financial position.

Interest expense in this context includes initial transaction costs and discount payable on redemption, as well as any interest or coupon payable while the liability is outstanding.

**Impairment of Financial Assets**

The Group assesses at each reporting date whether there is any objective evidence that a financial asset or a group of financial assets is impaired.

Assets reported at amortized cost

If there is objective evidence that an impairment loss has been incurred in loans and accounts receivable that are reported at amortized cost, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred) discounted at initial effective interest rate for such financial asset (i.e. at the effective interest rate calculated at initial recognition). The carrying amount of the asset is reduced directly or using the reserve. The loss amount is recognized in the statement of comprehensive income.

The Group first assesses individually whether objective evidence of impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exist for an individually assessed financial asset, whether significant or not, it includes the asset into a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognized are not included in a collective assessment of impairment.

If, in a subsequent year, the amount of the estimated impairment loss decreases because of an event occurring after the impairment was recognized, the previously recognized impairment loss is recovered. Any subsequent loss recovery is recognized in the statement of comprehensive income in the amount that the carrying amount of an asset should not exceed its amortized cost at the recovery date.

Provision for impairment loss is created in receivables in case there is objective evidence (e.g. a possibility of the debtor's insolvency or other financial difficulties) that the Group might not gain all amounts due to the delivery terms. Carrying amount of receivables is than reduced through the allowance account. Impaired debts are derecognized as soon as they are considered to be bad.

Financial investments available for sale

Impairment losses on available for sale investments are recognized by transferring the cumulative loss that has been recognized in other comprehensive income, and presented in the fair value reserve in equity, to profit or loss. The cumulative loss that is removed from other comprehensive income and recognized in profit or loss is the difference between the acquisition cost, net of any principal repayment and amortization, and the current fair value, less any impairment loss previously recognized in profit or loss. Changes in impairment provisions attributable to time value are reflected as a component of interest income.

***Interest-bearing loans and borrowings.*** All loans and borrowings are initially recognized at the fair value of the cash amount received less loan related costs.

After initial recognition, interest-bearing loans and borrowings are subsequently measured at an amortized cost using the effective interest rate method. Gains and losses are recognized in net profit or loss when liabilities retired, as well as through the amortization process.

***Trade and other payables.*** Trade and other payables are recognized and initially measured under the policy for financial instruments mentioned above. Subsequently, instruments with a fixed maturity are re-measured at amortized cost using the effective interest rate method. Amortized cost is calculated by taking into account any transaction costs and any discount or premium on settlement. Financial liabilities which do not have a fixed maturity are subsequently carried at fair value.

***Leases.*** The Group leases certain property, plant and equipment. Leases of property, plant, and equipment where the Group has substantially all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalized at the lease's commencement at the lower of the fair value of the leased property and the present value of the minimum lease payments.

Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance balance outstanding. The corresponding rental obligations, net of finance charges, are included in other long-term payables. The interest element of the finance cost is charged to the statement of comprehensive income over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The property, plant and equipment acquired under finance leases are depreciated over the useful life of the asset.

***Contingencies.*** Contingent liabilities are not recognized in the consolidated financial statements unless it is probable that an outflow of economic resources will be required to settle the obligation and it can be reasonably estimated. They are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote.

***Provisions.*** Provisions are recognized when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the Group expects some or all provisions to be reimbursed, for example under an insurance contract, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the statement of comprehensive income net of any reimbursement. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as finance costs.

***Employee Benefits.*** Wages, salaries, contributions to the state pension and social insurance funds, paid annual and sick leave, bonuses and non-monetary benefits are accrued in the period when the associated services are rendered by the employees of the Company.

***Revenue and expense recognition.*** Revenue is recognized when the title of the product passes to the customer and it is probable that the economic benefits associated with the transaction will flow to the Group and the amount of the revenue can be measured reliably.
The cost of products sold is recognized at the same time as the corresponding revenue.

Revenue from services rendering under the operating lease is stated in the reporting period when such services were rendered after completion certain transaction estimated on the basis of factual rendered services proportionally to a full scope of services that are to be rendered.

Expenses are accounted for when incurred and reported in the statement of comprehensive income in the period to which they relate.

***Income taxes***

<u>Current tax</u>

Current tax assets and liabilities for the current and prior years are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the reporting date.

<u>Deferred tax</u>

Deferred income tax is provided using the consolidated statement of financial position liability method on temporary differences at the reporting date- between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

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

Where the deferred income tax liability arises from the initial recognition of goodwill or 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; and

- In respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, where the timing of the reversal of the temporary differences can be controlled by the parent company and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognized for all deductible temporary differences, carry-forward of unused tax credits and 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 utilized except for:

- where the deferred income 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; and
- in respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred income tax assets are recognized 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 utilized.

The carrying amount of deferred income tax assets is reviewed at each consolidated statement of financial position date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax assets to be utilized. Unrecognized deferred income tax assets are reassessed at each consolidated statement of financial position date and recognized to the extent that it has become probable that future taxable profit will allow the deferred income tax asset to be realized.
Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realized or the liability is settled, based on tax rates and tax laws that have been enacted or (substantively enacted) at the consolidated statement of financial position date. Income tax relating to items recognized directly in net assets attributable to participants is recognized in the net assets attributable to participants and not in the statement of comprehensive income. Deferred income tax assets and deferred income tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current tax liabilities and they relate to income taxes imposed by the same taxation authority on the same entity.

***Loans provided.*** Loans provided are accounted for at an amortized cost using the effective interest rate method.

***Trade and other accounts receivable.*** Trade and other receivables are stated at an amortised cost using the effective interest rate method. Provisions in respect to non-recoverable amounts estimated as difference between carrying amount of assets and current value of future cash flows discounted using the effective interest rate calculated at initial recognition, are stated in the statement of comprehensive income, if any impairment evidences of assets are available.

***Cash and cash equivalents.*** Cash and cash equivalents include cash in banks and cash desks, bank deposits and short term investments with maturity up to three months that can be easily converted to respective cash funds and have insignificant risk of their cost change.

***Foreign currency***

Functional and presentation currency
Items included in these financial statements of each of the Group's entities are measured in the currency that applies to the primary economic environment in which the entities operate (the functional currency). The consolidated figures are presented in euros (EUR), the Group's reporting currency. The group has decided to use euro as the presentation currency because of the listing at the Warsaw Stock Exchange.

Foreign currency transactions
Foreign currency transactions are translated into the functional currency of Group's entities using the exchange rates prevailing at the dates of the transactions or valuation where items are re-measured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at the statement of financial position date exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the statement of comprehensive income. Foreign exchange gains and losses that relate to borrowings are presented in the statement of comprehensive income within "finance income" or "finance expenses" on net basis. All other foreign exchange gains and losses are presented in the statement of comprehensive income within "Other income/(expenses), net".

Non-monetary assets and liabilities carried at historical cost are retranslated at the rates prevailing at the dates of the transactions. Non-monetary assets and liabilities carried at fair value are retranslated at the rates prevailing at the date when the fair values were determined. Foreign currency differences arising on retranslation are recognized in the statement of comprehensive income, except for differences arising on the retranslation of property revaluation under IAS 16 which are recognized in other comprehensive income.

Foreign operations
The financial statements of subsidiaries and associates are prepared in their functional currencies, which are determined based on the primary economic environment in which they operate.
Upon consolidation, the assets and liabilities of foreign operations are translated to euro at exchange rates at the statement of financial position date. The income and expenses of foreign operations are translated to euro at average exchange rate (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions).

Foreign currency differences are recognized in other comprehensive income and are presented within equity in the translation reserve. When a foreign operation is disposed of, in part or in full, the relevant amount in the translation reserve is transferred to the statement of comprehensive income.
The EUR exchange rates used in the preparation of these consolidated financial statements are as follows:

| | USD | UAH | RUB | PLN |
|---|---|---|---|---|
| Average for year ended 31 December 2017 | 1.1297 | 30.0330 | 65.9014 | 4.2576 |
| As at 31 December 2017 | 1.1993 | 33.6610 | 68.8668 | 4.1709 |
| Average for year ended 31 December 2016 | 1.1067 | 28.2704 | 74.2310 | 4.3625 |
| As at 31 December 2016 | 1.0541 | 28.6619 | 63.8111 | 4.4240 |

***Value added tax (VAT).*** VAT during sale should be paid to the tax authorities as payments from customers are received. VAT paid during acquisition of goods and services is to be deducted to VAT received during sale, when payment is made for purchased goods and services. Tax authorities allow offsetting VAT. VAT in respect of acquisitions and sales, when settlement is completed at the statement of financial position date (deferred VAT) is stated in the statement of financial position by separate amounts as current assets or liabilities. If the provision was formed to doubtful receivables, this provision is reported in full scope including VAT. Deferred liability on VAT is still being recognized in the financial accounting until receivables are repaid or written off in order provided by the Ukrainian financial accounting rules. Refer to the note 9 for the disclosure of VAT receivable.

***Dividend distribution.*** Dividend distribution to the Company's shareholders is recognized as a liability in the Group's financial statements in the period in which the dividends are approved by the company's shareholders on general meeting. Amount of the Group's retained earnings that under the current legislation can be transferred to allocation between shareholders, is calculated on the basis of respective financial statements of separate entities of the Group prepared under NAS. These amounts might differ significantly from those calculated under IFRS.

## 3 Significant accounting estimates and judgments

The preparation of the financial statements requires the management to make various estimations and assumptions that affect reporting values of the assets and liabilities as well as disclosure of information on contingent assets and liabilities at the statement of financial position date. Actual results might

differ from the current estimations. The estimations are periodically reviewed. Should adjustments be needed they are reported in the financial results of the period when they became aware.
Below are the main assumptions as to future events and other sources of uncertainties of estimates at the reporting dates that are of a great risk of the necessity to make significant adjustments to the carrying amount of assets and liabilities during the next reporting year:

***Impairment of property, plant and equipment.*** Detection of impairment indications of property, plant and equipment provides for use of estimates that include, in particular, reasons, terms and amounts of the impairment. Impairment is based upon the analysis of many factors, such as: changes in current competitive conditions, expectations of an industry recovery, capital appreciation, changes in possibilities of future financing attraction, technological obsolescence, servicing suspension, current replacement cost and other changes in circumstances that indicate the impairment.

Management's estimates are required in order to determine the compensation amount for a cash generating unit. The value in use estimation includes methods based on the estimation of expected future discounted cash flows. This requires the Group to evaluate these cash flows for cash generating units and choose a grounded discount rate to calculate a present value of cash flows.

The estimations including the applied methodology may have significant effect on the fair value and impairment amount of property, plant and equipment. Additional information is disclosed in notes 10 and 11.

***Biological assets.*** Due to the absence of an active market, the fair value of biological assets is estimated by present valuing the net cash flows, estimated future cash flows are based on management's best estimates using a discount rate representing a market rate at the reporting date for an instrument with similar terms and conditions. Where pricing models are used, inputs are based on market related measures at the statement of financial position date. Additional information is disclosed in note 13.

***Provision for doubtful accounts receivable.*** Provision for doubtful debts is charged based on factual data about accounts receivable payment and the solvency analysis of the most significant debtors. In case of worsening the clients' financial position, a factual losses volume may exceed an estimated one. Additional information is disclosed in note 7.

***Legal actions.*** The Group's management applies significant judgments during the estimation and recognition of provisions and risks of contingent liabilities associated with existing legal actions and other unsettled claims that should be settled by way of negotiations, mediation, arbitration or state interference as well as other contingent liabilities. The management's judgment is essential during the possibility of a claim settling as regards the Group or material obligations and during the determination of a possible amount of final settlement. Due to the uncertainty inherent to the estimation process, actual expenses may differ from the initial estimation of provision. These previous estimations may vary as new information becomes available, mainly, from the Group's specialists, if any, or from outside consultants, such as actuaries or lawyers. A review of these estimations may have a substantial impact on future operating results. Additional information is disclosed in note 30.

## 4 Segment information

The management has determined the operating segments based on reports reviewed by the Board of Directors that are used to make strategic decisions.

The Board considers the business from both a geographic and product perspective. Geographically, management considers the performance of business in Ukraine, Russia, Poland and Netherlands. The Netherlands segment does not meet the quantitative threshold required by IFRS 8 and is not reported.

Ukraine, Russian and Poland segments are further segregated in the following main reportable segments:

- *Cheese&butter.* This segment is involved in production and distribution of cheese and butter. This segment generated 30% (2016: 32%) of the Group's revenue;

- *Whole-milk*. This segment is involved in production and distribution of whole-milk products. This segment generated 52% (2016: 56%) of Group's revenue;
- *Ingredients* include production and distribution of dry milk, agricultural products, and other products, which - although contributing a relatively small amount of revenue to the Group, are monitored by the Board of Directors as well.

The Board of Directors assesses the performance of the operating segments based on a measure of EBITDA. This measurement basis excludes the effects of non-recurring expenditure from the operating segments such as restructuring costs, legal expenses, non-current assets impairments and other income and expenses resulted from an isolated, non-recurring event.

As information on segment assets and liabilities are not reported to the Board of Directors, this is not disclosed in these financial statements.

Inter-segment sales are priced along the same lines as sales to external customers, with an appropriate discount being applied to encourage use of group resources at a rate acceptable to local tax authorities. This policy was applied consistently throughout the current and prior period.

The segment information by country for the year ended 31 December is as follows:

| | 2017 | | | | 2016 | | | |
|---|---|---|---|---|---|---|---|---|
| | Russia | Ukraine | Poland | Total | Russia | Ukraine | Poland | Total |
| Total segment revenue | 87,637 | 41,178 | 11,696 | 140,511 | 94,395 | 41,236 | 12,015 | **147,646** |
| Inter-segment revenue | - | - | (100) | (100) | - | - | (888) | **(888)** |
| Revenue from external customers | 87,637 | 41,178 | 11,596 | 140,411 | 94,395 | 41,236 | 11,127 | **146,758** |
| **EBITDA** | **6,717** | **3,708** | **(54)** | **10,371** | **3,439** | **3,059** | **(39)** | **6,459** |
| EBITDA margin | 8% | 9% | 0% | 7% | 4% | 7% | 0% | **4%** |
| Depreciation and amortization | 3,505 | 5,101 | 1,755 | 10,361 | 3,193 | 5,255 | 1,831 | **10,279** |

Inter-segment revenue is related to inter-group sales of dairy goods, mainly cheese, produced in Ukraine to be sold in the Russian market to third party customers.

The segment information by product for the year ended 31 December is as follows:

| | 2017 | | | | 2016 | | | |
|---|---|---|---|---|---|---|---|---|
| | Cheese & butter | Whole-milk products | Ingredients | Total | Cheese & butter | Whole-milk products | Ingredients | Total |
| **Total segment revenue** | 42,246 | 73,248 | 25,017 | 140,511 | **47,082** | **81,567** | **18,997** | **147,646** |
| **Inter-segment revenue** | - | - | (100) | (100) | **(422)** | **-** | **(466)** | **(888)** |
| **Revenue from external customers** | 42,246 | 73,248 | 24,917 | 140,411 | **46,660** | **81,567** | **18,531** | **146,758** |
| **EBITDA** | **3,850** | **5,440** | **1,081** | **10,371** | **3,771** | **1,660** | **1,028** | **6,459** |
| EBITDA margin | 9% | 7% | 4% | 7% | **8%** | **2%** | **6%** | **4%** |
| Depreciation and amortization | 3,555 | 4,104 | 2,702 | 10,361 | **4,566** | **5,085** | **628** | **10,279** |

A reconciliation of EBITDA to profit before tax:

| | 2017 | 2016 |
|---|---|---|
| **EBITDA** | 10,371 | 6,459 |
| Other segments EBITDA | (92) | (1,016) |
| **Total segments** | **10,279** | **5,443** |
| Depreciation and amortization | (10,361) | (10,279) |
| Non-recurring expenses | - | (153) |
| Loss from disposal and impairment of non-current assets | 670 | (506) |
| Finance expenses | (8,960) | (31,242) |
| Finance income | 1,130 | 13 |
| **Loss before tax** | **(7,242)** | **(36,724)** |

## 5 Balances and transactions with related parties

For the purposes of these financial statements, parties are considered to be related if one party has the ability to control the other party, is under common control or can exercise significant influence over the other party in making financial or operational decisions as defined by IAS 24 "Related Party Disclosures". During the reporting period the company had related party transactions with ultimate shareholder, key management and companies under common control.

Group's transactions with its related parties for the years ended 31 December were as follows:

| *Entities under common control:* | 2017 | 2016 |
|---|---|---|
| Administrative expenses | 1 | - |

The outstanding balances due from related parties as of 31 December were as follows:

| | Balance at | Transactions value | Balance at |
|---|---|---|---|
| ***Entities under common control:*** | **2017** | **2017** | **2016** |
| Trade accounts receivable | - | (281) | 281 |
| Other financial assets: | 555 | (2,709) | 3,264 |
| Other accounts receivable | 53 | (171) | 224 |
| **Total trade and other receivable** | **608** | **(3161)** | **3,769** |
| Other accounts payable | **842** | 786 | 56 |
| **Total trade and other payable** | **842** | **786** | **56** |

### Key management compensation

Key management includes Board of Directors. The short-term employee benefits paid or payable to key management for employee services is EUR 183 thousand (2016: EUR 299 thousand).

## 6 Cash and cash equivalents

Cash in bank is available for demand and earns interest at floating rates based on daily bank deposit rates.

| | 31 December 2017 | 31 December 2016 |
|---|---|---|
| Short term deposits | 436 | - |
| Cash in bank and cash on hand | 980 | 1,044 |
| **Total cash and cash equivalents** | **1,416** | **1,044** |

An analysis of the Group's cash and cash equivalents by currency is provided in note 32.

## 7 Trade and other accounts receivable

| | 31 December 2017 | 31 December 2016 |
|---|---|---|
| Trade accounts receivable | 9,757 | 13,386 |
| Other financial assets | 8,247 | 10,752 |
| Allowance for doubtful debts | (8,960) | (9,707) |
| **Total financial assets within trade and other receivables** | **9,044** | **14,431** |
| Advances issued | 1,934 | 1,318 |
| Advances issued for non-current assets | 11 | - |
| Other receivables | 9,035 | 4,873 |
| Allowance for doubtful debts | (618) | (580) |
| **Total trade and other accounts receivable** | **19,406** | **20,042** |

As at 31 December 2017 trade receivables of EUR 3,540 thousand (2016: EUR 2,762 thousand) were past due. Total trade accounts receivable are individually determined and to be impaired in the amount of EUR 8,960 thousand (2016: EUR 9,707 thousand). Based on historic information, that includes past due period and estimated recoverability value, the Group creates the allowance for doubtful debts against trade receivables past due.

The other financial assets include EUR 555 thousand (2016: EUR 3,264 thousand) due from related parties.

The analysis of credit quality of trade and other financial receivables is as follows:

| | 31 December 2017 | | 31 December 2016 | |
|---|---|---|---|---|
| | Trade receivables | Other financial receivables | Trade receivables | Other financial receivables |
| Customers with no history of default | 6,217 | 8,247 | 10,624 | 10,752 |
| **Total current and not impaired** | **6,217** | **8,247** | **10,624** | **10,752** |
| Individually determined to be impaired | | | | |
| - less than 30 days overdue | 675 | - | 165 | - |
| - 30 to 60 days overdue | 47 | - | 28 | - |
| - 60 to 90 days overdue | 17 | - | 10 | - |
| - 90 to 360 days overdue | 356 | - | 166 | - |
| - over 360 days overdue | 2,445 | - | 2,393 | - |
| Customers with history of default | - | - | - | - |
| **Total individually determined to be impaired** | **3,540** | - | **2,762** | **-** |
| **Less impairment provision** | (1,996) | (6,964) | (2,221) | (7,486) |
| **Total** | **7,761** | **1,283** | **11,165** | **3,266** |

Management have assessed the credit quality of clients which whom the Group have outstanding balances and have come to the conclusion the credit quality is mostly depended on the current economic and political crisis. In cases where credit quality is poor management have made a provision.

According to the National Bank of Ukraine Resolution dated 28 August 2015 № 562 "On revocation of the banking license and liquidation of PJSC" UKRAINIAN PROFESSIONAL BANK "executive directorate of the Deposit Guarantee made a decision № 158 regarding "The beginning of procedure of liquidation JSC" UKRAINIAN PROFESSIONAL BANK".

As at 31 December 2017 Other financial assets include balances previously classified as Deposits in PJSC UKRAINIAN PROFESSIONAL BANK in the amount of EUR 6,964 thousand for which 100% allowance for doubtful debts was accrued (note 7).

The carrying amounts of the Group’s trade and other receivables approximate their fair value.
Maximum exposure to credit risk at the reporting date is the carrying value of each class of receivable.

Movements on the group provision for impairment of trade receivables are as follows:

| | 2017 | 2016 |
|---|---|---|
| **Balance 1 January** | **2,221** | **2,114** |
| Provided by during the year | 42 | 320 |
| Unused amount reversed | - | (53) |
| Receivable written off during the year as uncollectible | - | (144) |
| Exchange difference | (267) | (16) |
| **Balance 31 December** | **1,996** | **2,221** |

The movement on the provision for impaired receivables has been included in other expenses, net line in the consolidated statement of comprehensive income.
Other classes of financial assets included within trade and other receivables do not contain impaired assets.
An analysis of the Group's trade and other receivables classified as financial assets by currency is provided in note 32.
The Group does not hold any collateral as security.

## 8 Inventories

| | 31 December 2017 | 31 December 2016 |
|---|---|---|
| Raw and other materials | 4,970 | 4,902 |
| Finished goods and work in progress | 3,516 | 7,445 |
| Agriculture produce | 227 | 531 |
| **Total inventories** | **8,713** | **12,878** |

At 31 December 2017 bank borrowings are secured on inventories the value of EUR 3,321 thousand (2016: 3,900 thousand) (note16).

As at 31 December 2017 inventories are stated net of provision for obsolescence at the amount of EUR 389 thousand (2016: EUR 553 thousand).

## 9 Other taxes receivable

| | 31 December 2017 | 31 December 2016 |
|---|---|---|
| VAT recoverable | 4,907 | 6,286 |
| Payroll related taxes | 92 | 75 |
| Other prepaid taxes | 195 | 378 |
| **Total other taxes receivable** | **5,194** | **6,739** |

VAT receivable as at 31 December 2017 is shown net of provision at the amount of EUR 1,379 thousand (31 December 2016: EUR 995 thousand). The provision for VAT is created for part of VAT balances due to complexity of reimbursement of VAT in Ukraine and is estimated at 17% (2016: 19%) of VAT refund claimed from the Ukrainian Government based on previous statistics of VAT recoverability.

## 10 Goodwill

| | 2017 | 2016 |
|---|---|---|
| Balance at 1 January | 1,558 | 1,746 |
| Foreign currency translation | (84) | (188) |
| **Balance at 31 December** | **1,474** | **1,558** |

Goodwill is initially recognized as an asset during the primary evaluation. As the goodwill relates to foreign subsidiaries, it is translated each year as part of the translation of the foreign operation.

Goodwill has been allocated for impairment testing purposes to the following cash-generating units:

- Milk production operations – represented by Ostankino Dairy Company located in Russia.
- Agricultural operations – represented by four agricultural companies located in Ukraine that were purchased by the Group during the years ended 31 December 2012 and 2013.

The carrying amount of goodwill was allocated to cash-generating units as follow:

| | 31 December 2017 | 31 December 2016 |
|---|---|---|
| Milk production operations | 1,381 | 1,490 |
| Agricultural operations | 93 | 68 |
| | **1,474** | **1,558** |

*Impairment test for goodwill*

Impairment testing of goodwill is performed annually.

The recoverable amounts of the cash-generating units are based on value in use calculations based on cash flow projections from formally approved budgets covering a five year period to 31 December 2017.

Management determined budget revenues based on past performance and its expectation of market development. Discount rates used are pre-tax and reflect specific risks relating to the relevant operating segments. Management expectations and other input to the calculation such as discount rate, market size and market shares reflect the current economic climate and market developments relevant to the segments.

The values assigned to the key assumptions represent management's assessment of future trends in the business and are based on both external and internal sources.

The outcome of the impairment tests is that the recoverable amounts exceed the carrying amounts of the cash-generating units and accordingly no impairment charge has been recorded in 2017 and in 2016. In addition to the impairment test, the principal assumptions were subject to sensitivity analyses, which led to the conclusion that no impairments would arise from reasonable possible changes in a key assumption.

## 11 Property, plant and equipment and intangible assets

| | Land and Buildings | Plant and equipment | Other assets | Constructions in progress | Intangible assets | Total |
|---|---|---|---|---|---|---|
| **At 1 January 2016** | | | | | | |
| Revalued cost | 84,575 | 27,880 | 5,655 | 5,093 | 3,051 | 126,254 |
| Accumulated depreciation and amortization | (1,145) | (4,111) | (159) | - | (1,358) | (6,773) |
| **Net book value** | **83,430** | **23,769** | **5,496** | **5,093** | **1,693** | **119,481** |
| **Year ended 31 December 2016** | | | | | | |
| Opening net book value | 83,430 | 23,769 | 5,496 | 5,093 | 1,693 | 119,481 |
| Additions | 1,145 | 3,662 | 308 | 4,421 | 784 | 10,320 |
| Depreciation and amortization | (3,721) | (5,637) | (1,562) | - | (248) | (11,168) |
| Transfers | 1,551 | 388 | 36 | (1,974) | - | - |
| Revaluation | 368 | (5,018) | (3,428) | - | - | (8,078) |
| Disposals | (10,943) | (149) | 211 | (113) | (75) | (11,069) |
| Exchange rate difference | (1,042) | 1,795 | (662) | 1,338 | 172 | 1,602 |
| **Closing net book value** | **70,788** | **18,810** | **399** | **8,765** | **2,326** | **101,088** |
| **At 31 December 2016** | | | | | | |
| Revalued cost | 74,880 | 25,873 | 1,746 | 8,765 | 3,363 | 114,627 |
| Accumulated depreciation and amortization | (4,092) | (7,063) | (1,347) | - | (1,037) | (13,539) |
| **Net book value** | **70,788** | **18,810** | **399** | **8,765** | **2,326** | **101,088** |
| **Year ended 31 December 2017** | | | | | | |
| Opening net book value | **70,788** | **18,810** | **399** | **8,765** | **2,326** | **101,088** |
| Additions | 489 | 1,361 | 163 | 759 | 183 | 2,955 |
| Depreciation and amortization | (3,420) | (5,479) | (1,099) | - | (363) | (10,361) |
| Transfers | 8,868 | (3,623) | 62 | (5,307) | - | - |
| Revaluation | 3,747 | 11,200 | 6,525 | 594 | - | 22,066 |
| Disposals | (1,902) | (2,450) | (80) | (421) | (91) | (4,944) |
| Exchange rate difference | (8,070) | 40 | (248) | (792) | (62) | (9,132) |
| **Closing net book value** | **70,500** | **19,859** | **5,722** | **3,598** | **1,993** | **101,672** |
| **At 31 December 2017** | | | | | | |
| Revalued cost | 72,874 | 28,433 | 5,946 | 3,598 | 3,303 | 114,154 |
| Accumulated depreciation and amortization | (2,374) | (8,574) | (224) | - | (1,310) | (12,482) |
| **Net book value** | **70,500** | **19,859** | **5,722** | **3,598** | **1,993** | **101,672** |

The Company conducted valuation of assets with effective date 31 December 2017 and indicated the increase of the value of the Ukrainian assets of the Group.

Weighted average cost of capital (WACC) for Ukrainian production assets impairment was calculated using the following most significant variables:

- Country risk at the rate of 4.2%
- Equity risk Premium at the rate of 4.1%
- Cost of Debt for Ukrainian Hryvnia at the rate of 13.1%

The calculation resulted with WACC at the level of 20.0%.

At 31 December 2017 bank borrowings are secured on properties for the value of EUR 68,321 thousand (2016: EUR 76,231 thousand) (note16).

At 31 December 2017 bank borrowings are secured on Intangible assets the value of EUR 211 thousand (2016: EUR 739 thousand).

At 31 December 2017 the gross carrying value of fully depreciated property, plant and equipment is EUR 1,123 thousand (2016: EUR 1,021 thousand).

The Group engaged independent appraisers to determine the fair value of land and buildings, plant and equipment and other assets of Ukrainian segment. Fair value as at 31 December 2017 was determined with reference to depreciated replacement cost or market-based evidence, in accordance with International Valuation Standards. Valuation of property, plant and equipment is within level 3 of the fair value hierarchy.

As a result of the revaluation, a revaluation deficit net EUR 5,305 thousand was debited to other comprehensive income and is shown in Revaluation reserve in shareholders equity (note 18). The revaluation loss of EUR 1,433 thousand was debited to Other (expenses)/income (note 26).

Should there be no revaluation the net book value of property, plant and equipment and intangible assets as at 31 December 2017 would be:

| | Land and buildings | Plant and equipment | Other assets | Constructions in progress | Intangible assets | Total |
|---|---|---|---|---|---|---|
| **31 December 2017** | 66,753 | 14,363 | 2,125 | 3,004 | 1,993 | **88,238** |

## 12 Investment property

| | Land and buildings | Constructions in progress | Total |
|---|---|---|---|
| **Year ended 31 December 2017** | | | |
| Opening balance value | 13,265 | 6,706 | 19,971 |
| Net gains or losses from FV adjustments | (1,395) | (1,844) | (3,239) |
| **Closing balance value** | **11,870** | **4,862** | **16,732** |
| **At 31 December 2017** | | | |

| | Land and buildings | Constructions in progress | Total |
|---|---|---|---|
| **Year ended 31 December 2016** | | | |
| Opening balance value | 13,097 | 6,968 | 20,065 |
| Additions | 168 | (262) | (94) |
| **Closing balance value** | **13,265** | **6,706** | **19,971** |
| **At 31 December 2016** | | | |

At 31 December 2017, there were no restrictions on the realization of investment property or the remittance of income and proceeds of disposal (2016: none).

There are no contractual obligations to purchase, construct or develop investment property for repairs, maintenance or enhancements on responding year.
The investment property was passed through appraisal on 31 December 2017 (2016: on 31 December 2016) using multiple appraisal methods, including cost and income based approaches, carried out by external independent qualified appraisal companies with recent professional experience in the locations of the Group business.

The fair value of the investment property has not been adjusted significantly for the purposes of financial reporting. The fair value of investment property is categorized as a level 3 recurring fair value measurement.

## 13 Biological assets

The Group is engaged in agricultural activities mainly for the following purposes:

- Development of livestock in order to create own base for raw milk supply.
- Grow of maize and winter wheat, with the main purpose to sale to the external customers
- Grow fodder cultures.

Non-current cattle are represented by dairy livestock with an average yearly lactation period of nine months. Current cattle comprise immature cattle and cattle intended for sale.
To estimate the fair value of biological assets, a valuation, which conforms to International Valuation Standards, was performed by the Group, fair value is estimated as the present value of the net cash flows expected to be generated from biological assets discounted at a current market discount rate.

Fair values of biological assets were based on the following key assumptions:

- crops are accounted on historical costs. As for now the Company restores plant growing for fodder with growth cycle about 5 years;
- Dairy cattle are accounted on the minimum amount of
  1) projected discounted cash flows based on the expected milk produced during their productive life after the reporting date and expected volume of meat at the date of slaughter;
  2) actual market price updated quarterly for the same biological assets;
- the average productive life of a cow is determined based on internal statistical information and stated as 8 years for milk producing forecast purposes;
- comparative prices for milk and meat are obtained from market resources as at the end of the reporting period;
- pre-tax discount rate of 14% is applied in determining fair value of biological assets. The discount rate was applied given the discount rate stated by the NBU effective at the reporting date.

The key assumptions represent management's assessment of future trends in agriculture and cattle farming business and are based on both external and internal sources of data.

As at 31 December biological assets comprise the following groups:

| | 31 December 2017 | | 31 December 2016 | |
|---|---|---|---|---|
| **Current biological assets of animal breading** | Units | Amount | Units | Amount |
| Cattle | 2,499 | 1,127 | 3,078 | 956 |
| Other | - | 1 | - | 4 |
| | **2,499** | **1,128** | **3,078** | **960** |

| **Current biological assets of plant growing** | Hectares | Amount | Hectares | Amount |
|---|---|---|---|---|
| Other | - | 174 | - | 136 |
| | **-** | **174** | **-** | **136** |
| **Total current biological assets** | **-** | **1,302** | **-** | **1,096** |

| **Non-current biological assets** | Units | Amount | Units | Amount |
|---|---|---|---|---|
| Cattle | 1,676 | 1,251 | 1,996 | 1,383 |
| Other livestock | - | - | | |
| | **1,676** | **1,251** | **1,996** | **1,383** |

Changes in key assumptions used to estimate biological assets would have the following effect on biological assets as at 31 December 2017 and 2016:

| | **2017** | **2016** |
|---|---|---|
| 1 % increase in discount rate | 3 | 3 |
| 1 % decrease in discount rate | (3) | (3) |
| | | |
| 10 % increase in price for milk | | |
| 10 % decrease in price for milk | 1 | 1 |
| | | |
| 10 % decrease (increase) in price for meat | (114) | 104 |
| 10 % increase (decrease) in price for meat | 104 | (114) |

Law elasticity on milk price changes is due to the fact that most of the cows are accounted at the market price as the less amount comparatively to discounted cash flows (DCF) of expected milk and meat sales revenue.

The following represents the changes during the year ended 31 December 2017 and 31 December 2016 in the carrying amounts of non-current and current biological assets:

| | Current biological assets of animal breading | Current biological assets of plant growing | Non-current biological assets |
|---|---|---|---|
| **As at 1 January 2016** | **1,600** | **21** | **1,507** |
| Purchases | 866 | - | 219 |
| Gain arising from changes in fair value attributable to physical changes and to changes in market prices | (16) | - | (36) |
| Investments into future crops | - | 115 | - |
| Transfers | (521) | - | 521 |
| Decrease due to harvest | - | - | - |
| Disposals | (797) | - | (752) |
| Currency translation difference | (172) | - | (76) |
| **As at 31 December 2016** | **960** | **136** | **1,383** |
| Purchases | 235 | - | - |
| Gain arising from changes in fair value attributable to physical changes and to changes in market prices | 317 | - | 154 |
| Investments into future crops | - | 235 | - |
| Transfers | (390) | - | 390 |
| Decrease due to harvest | - | (197) | - |
| Disposals | (274) | - | (461) |
| Currency translation difference | 280 | - | (215) |
| **As at 31 December 2017** | **1,128** | **174** | **1,251** |

**Risk management in agricultural business**

The Group is exposed to a number of risks related to its biological assets:

***Price fluctuation risk***

The Group is exposed to financial risks arising from changes in wheat, barley and milk prices. The Group does not anticipate that prices for its main products will decline significantly in the foreseeable future and, therefore, has not entered into derivative or other contracts to manage the risk of a decline in prices. Management reviews its outlook for prices regularly in considering the need for active financial risk management.

***Climate and other risks***

Biological assets are exposed to the risk of damage from climatic changes, diseases, fires and other natural forces. The Group has extensive processes in place aimed at monitoring and mitigating those risks, including regular field and farm inspections and industry pest and disease surveys.

## 14 Trade and other payables

| | 31 December 2017 | 31 December 2016 |
|---|---|---|
| Trade payables | 14,872 | 16,076 |
| Accounts payable for fixed assets | 23 | - |
| Interest payable | 14,340 | 11,511 |
| Other financial payables | - | - |
| **Total financial liabilities within trade and other payable** | **29,235** | **27,587** |
| Wages and salaries payable | 1,445 | 1,798 |
| Advances received | 1,048 | 7,682 |
| Other accounts payable | 8,176 | 5,088 |
| Accruals for employees' unused vacations | 874 | 899 |
| **Total trade and other payables** | **40,778** | **43,054** |

Financial liabilities are normally settled within 60-days period.

The fair values of trade and other accounts payable approximate their carrying amounts.

An analysis of the Group's trade and other payables classified as financial liabilities by currency is provided in note 32.

## 15 Other taxes payable

| | 31 December 2017 | 31 December 2016 |
|---|---|---|
| VAT payable | 1,102 | 1,355 |
| Payroll related taxes | 3,137 | 2,119 |
| Other taxes payable | 1,235 | 656 |
| **Total other taxes payable** | **5,474** | **4,130** |

## 16 Interest bearing loans and borrowings

| | 31 December 2017 | 31 December 2016 |
|---|---|---|
| **Current** | | |
| Interest bearing loans due to banks | 74,012 | 85,448 |
| Loans from non-financial institutions | 1 | - |
| Bank overdrafts | 9 | 435 |
| Finance leases | 1,778 | 1,410 |
| **Total current borrowings** | **75,800** | **87,293** |
| | | |
| **Non-current** | | |
| Interest bearing loans due to banks | 10,632 | 14,919 |
| Finance leases | 124 | 74 |
| **Total non-current borrowings** | **10,756** | **14,993** |
| **Total borrowings** | **86,556** | **102,286** |

At 31 December 2017 current borrowings of the Group stood at EUR 75.8 million. Out of this amount, bank loans in the amount of EUR 1,694 thousand (2016: EUR 13,054 thousand) are classified as a short-term as a part of the indebtedness of the Group under long-term credit lines from several banks, which is due in 2018.

As at 31 December 2017, the Group has not met requirement in respect of covenants to syndicate loan stated in Note 31. Management is in process of loan restructuring negotiation with lenders as at the date of these financial statements approval. The total sum of the Group's indebtedness to syndicate as at 31 December 2017 stood at EUR 48,845 thousand, including an overdue amount of EUR 48,845 thousand is classified as current interest bearing loans due to banks (note 16).

The exposure of the Company's borrowings to interest rate changes and the contractual repricing dates at 31 December are as follows:

| | 2017 | 2016 |
|---|---|---|
| 6 months or less | 63,273 | 62,070 |
| 6-12 months | 12,527 | 25,223 |
| 1-3 years | 9,380 | 14,993 |
| 3-5 years | 1,376 | - |
| | **86,556** | **102,286** |

Principal terms and the debt repayment schedule of the Group's loans and borrowings as at 31 December are as follows:

| | 31 December 2017 | | | | | 31 December 2016 | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | **USD** | **UAH** | **RUB** | **PLN** | **Total** | **USD** | **UAH** | **RUB** | **PLN** | **Total** |
| **12 months or less** | | | | | | | | | | |
| Outstanding balance, thousand EUR | 50,133 | 8,636 | 13,950 | 3,081 | **75,800** | 70,667 | 298 | 14,534 | 1,793 | **87,293** |
| Average interest rate, % | 9.53 | 1.30 | 15.32 | 1.94 | **9.35** | 7.70 | 22.10 | 15.26 | 9.00 | **9.04** |
| **1-5 years** | | | | | | | | | | |
| Outstanding balance, thousand EUR | 8,920 | 550 | 1,286 | - | **10,756** | 2,894 | 11,249 | 850 | - | **14,993** |
| Average interest rate, % | 3.00 | 19.50 | 12.87 | - | **5.02** | 3.00 | 17.2 | 13.53 | - | **14.25** |

At 31 December 2017 bank borrowings are secured on properties, plant and equipment (note 11), inventories (note 8).

At 31 December 2017, due to the difficult economic and political situation in Ukraine (note 1), the Group has overdue amount of EUR 48,845 thousand in respect of Facilities agreement with the Syndicate. Management is in process of negotiation of new repayment terms for the above mentioned and other loans (note 35).

Milkiland EU (as a guarantor for the leasing contracts of Ostrowia) and Pekao Leasing signed the prolongation agreement on 16 November 2016 regarding the original contracts term prolongation till 31 December 17. As of today, the Group is in negotiations with this Creditor in order to agree about the restructuring of this indebtedness until 31 December 2018. Five production equipment objects are leased according to the original leasing contracts 37/0868/13, 37/0869/13, 37/0922/13, 37/0935/13, 37/0936/13. The total amount of the respective debt under the leasing contracts stood at EUR 1.6 million as of 31 December 2017.

First of all, payments of the guarantor will cover the liability under the leasing agreement No. 37/0869/13 and further on the longest liabilities. In case Guarantor breaks any obligation under compromise agreement including delay at least one payment or its part exceeding 7 days, the Creditor may restart the enforcement process in court without additional notices and calls. The terms and conditions of further prolongation of leasing contracts should be discussed and agreed between Pekao Leasing and Debtor until 31 December 2018. Any special restrictions concerning dividends payment, additional debt obtaining and further leasing operations are applicable according to the signed prolongation agreement dated 16 November 2016 and other possible further restructuring agreements between the Parties.

## 17 Share capital

Share capital as at 31 December is as follows:

| | 31 December 2017 | | 31 December 2016 | |
|---|---|---|---|---|
| | Number | EUR 000 | Number | EUR 000 |
| **Authorized** | | | | |
| Ordinary shares of 10c each | 50,000,000 | 5,000 | 50,000,000 | 5,000 |
| **Issued and fully paid up** | | | | |
| *Ordinary shares of 10c each* | | | | |
| At beginning of the year | 31,250,000 | 3,125 | 31,250,000 | 3,125 |
| **At end of the year** | **31,250,000** | **3,125** | **31,250,000** | **3,125** |

## 18 Revaluation reserve

The revaluation reserve arises on the revaluation of properties, plant and equipment. When revalued properties, plant and equipment are depreciated or sold, the portion of the revaluation reserve that relates to that asset is transferred directly to retained earnings. During 2017 EUR 7,109 thousand was transferred to retained earnings (2016: EUR 6,263 thousand).

Change of Revaluation reserve as a result of the revaluation of property, plant and equipment in 2017 in the amount of EUR 12,286 thousand.

## 19 Currency translation reserve

Exchange differences relating to the translation of the results and net assets of the Group`s foreign operations from their functional currencies to Group`s presentation currency are recognized directly in other comprehensive income and accumulated in the currency translation reserve.

## 20 Dividends per share

During the year ended 31 December 2017 the Group had not declared dividends. Last payment of dividends was made by the Group in 2014, the respective amount of payment stood at EUR 2,187 thousand (EUR 0.08 per ordinary share).

## 21 Revenue

Sales by product during the year ended 31 December was as follows:

| | 2017 | 2016 |
|---|---|---|
| Cheese & Butter | 42,247 | 46,660 |
| Whole-milk products | 73,248 | 81,567 |
| Ingredients | 24,916 | 18,531 |
| **Total revenue** | **140,411** | **146,758** |

Regional sales during the year ended 31 December was as follows:

| | 2017 | 2016 |
|---|---|---|
| Russia | 87,567 | 94,282 |
| Ukraine (including export) | 40,352 | 38,264 |
| Poland | 11,466 | 10,190 |
| Other | 1,026 | 4,022 |
| **Total revenue** | **140,411** | **146,758** |

## 22 Change in fair value of biological assets

Change in fair value of biological assets at the amount of EUR 269 thousand (2016: EUR (52) thousand) represents the revaluation of cattle at fair value less costs to sell.

## 23 Cost of sales

| | 2017 | 2016 |
|---|---|---|
| Raw and other materials | 88,307 | 92,107 |
| Depreciation | 8,404 | 9,138 |
| Wages and salaries | 6,668 | 7,101 |
| Electricity | 3,005 | 3,501 |
| Gas | 3,005 | 3,088 |
| Transportation costs | 2,359 | 2,263 |
| Social insurance contributions | 1,544 | 1,678 |
| Repairs of property, plant and equipment | 914 | 1,728 |
| Water | 189 | 266 |
| Changes in finished goods and work in progress | (206) | 464 |
| Other | 2,530 | 4,258 |
| **Total cost of sales** | **116,719** | **125,592** |

## 24 Selling and distribution expenses

| | 2017 | 2016 |
|---|---|---|
| Transportation costs | 5,639 | 6,160 |
| Wages and salaries | 2,903 | 2,769 |
| Social insurance contributions | 715 | 722 |
| Depreciation and amortization | 440 | 350 |
| Security and other services | 436 | 592 |
| Marketing and advertising | 69 | 1,105 |
| License fees | 24 | 43 |
| Rental costs | 4 | 179 |
| Other | 1,342 | 1,159 |
| **Total selling expenses** | **11,572** | **13,079** |

## 25 Administrative expenses

| | 2017 | 2016 |
|---|---|---|
| Wages and salaries | 4,585 | 4,249 |
| Taxes and other charges | 1,526 | 1,166 |
| Social insurance contributions | 1,337 | 886 |
| Consulting fees | 1,332 | 1,837 |
| Depreciation and amortization | 591 | 662 |
| Security and other services | 548 | 673 |
| Transportation costs | 458 | 665 |
| Rental costs | 214 | 266 |
| Repairs and maintenance | 190 | 318 |
| Representative charges | 180 | 683 |
| Bank charges | 157 | 350 |
| Other utilities | 141 | 201 |
| Communication | 125 | 156 |
| Property insurance | 31 | 365 |
| Office supplies | 26 | 33 |
| Other | 763 | 485 |
| **Total administrative expenses** | **12,204** | **12,995** |

## 26 Other income/(expenses), net

| | 2017 | 2016 |
|---|---|---|
| Gain/(Loss) from disposal of non-current assets | 1,800 | (5) |
| Rental income | 561 | - |
| Operational foreign exchange results, net | 233 | 1 554 |
| Government grants recognized as income | 52 | 1,158 |
| Gain from write off of accounts payable | 2 | 190 |
| Change in provision and write off of trade and other accounts receivable | (87) | (27) |
| Change in provision and write off of VAT receivable | (131) | (500) |
| Loss from disposal and write off of inventories | (175) | (818) |
| Penalties | (478) | (702) |
| Depreciation | (926) | (129) |
| Loss from revaluation of non-current assets | (1,130) | (501) |
| Other income/(expenses) | 951 | (755) |
| **Total other (expenses)/income, net** | **672** | **(535)** |

## 27 Finance income

| | 2017 | 2016 |
|---|---|---|
| Finance foreign exchange income, net | 1,080 | 15 |
| Bank deposits | 50 | 3 |
| **Total finance income** | **1,130** | **18** |

## 28 Finance expenses

| | 2017 | 2016 |
|---|---|---|
| Bank borrowings | 6,785 | 11,960 |
| Discounting of loans | 2609 | (3,167) |
| Other borrowings | 182 | 200 |
| Finance leases | 49 | 58 |
| Finance foreign exchange expenses, net | (665) | 22,174 |
| Other finance expense | - | 17 |
| **Total finance expenses** | **8,960** | **31,242** |

## 29 Income tax

| | 2017 | 2016 |
|---|---|---|
| Current income tax expense | (777) | (848) |
| Deferred income tax benefit | 673 | (1,334) |
| **Income tax expense** | **(104)** | **(2,182)** |

The Group operates in several tax jurisdictions, depending on the residence of its subsidiaries (primarily in Ukraine, Russia and Poland). In 2017 Ukrainian corporate income tax was levied on taxable income less allowable expenses at the rate of 18% (2016: 18%), Russian profit tax was levied at the rate of 20% (2016: 20%), Poland profit tax was levied at the rate of 19% (2016: 19%). In 2017 the tax rate for Panama operations was 0% (2016: 0%) on worldwide income.

Reconciliation between the expected and the actual taxation charge is provided below.

| | 2017 | 2016 |
|---|---|---|
| **Profit/ (Loss) before taxation, including** | **(7,242)** | **(36,724)** |
| Profit/ (Loss) of companies levied a single agricultural tax (Ukrainian operations) | (147) | (764) |
| Profit/ (Loss) of Ukrainian companies | 451 | (21,581) |
| Profit/ (Loss) of Russian companies | (673) | (4,000) |
| Profit/ (Loss) of Poland companies | (2,066) | (3,090) |
| Profit/ (Loss) of Dutch companies | 233 | 1,077 |
| Profit/ (Loss) of Cyprus companies | (4,005) | (4,552) |
| Profit/ (Loss) before income tax of other companies | (1,035) | (2,400) |
| Declaration of dividends within the Group | - | (1,414) |
| | | |
| Income tax charge at statutory rate of 18% (Ukrainian operations) | (81) | 3,895 |
| Income tax charge at statutory rate of 20% (Russian operations) | 135 | 747 |
| Income tax charge at statutory rate of 19% (Poland operations) | 393 | 587 |
| Income tax charge at statutory rate of 25% (Dutch operations) | (58) | (275) |
| Income tax charge at statutory rate of 12.5% (Cyprus operations) | 501 | 455 |
| Change in deferred income taxes resulting from reduction in tax rate | - | - |
| Provision in respect of irrecoverable deferred income tax asset | 3,807 | (1,133) |
| Tax effect of items which are permanently not deductible or assessable for taxation purposes | (4,801) | (6,458) |
| **Income tax expense** | **(104)** | **(2,182)** |

At the existing Group's structure tax losses and current tax assets of one company cannot be offset against current income tax liabilities of another company. Correspondently, taxes may be accrued even if there is a net consolidated tax loss. Thus, deferred income tax assets of one company of the Group are not subject to offsetting against deferred income tax liabilities of another company of the Group. The deferred income tax liabilities and assets reflected in the consolidated statement of financial position as at 31 December are as follows:

| | 2017 | 2016 |
|---|---|---|
| Deferred income tax liability | (13,760) | (11,771) |
| Deferred income tax asset | 2,472 | 2,223 |
| | (11,288) | (9,548) |

**Unrecognized deductible temporary differences, unused tax losses and unused tax credits**

As at 31 December 2017 Milkiland EU Sp. z o.o. presents deferred tax assets in the amount of 2 350 thousand EUR (2016: 2 193 thousand EUR). This amount is mostly presented by the tax losses from the prior periods. The company has a history of tax losses and the calculated deferred tax asset, net of deferred tax liabilities are mainly a result of prior period losses.

The deductible temporary differences, unused tax losses, and unused tax credits for which no deferred tax asset is recognized in the statement of financial position presented below:

| | 2017 | 2016 |
|---|---|---|
| Deductible temporary differences, unused tax losses and unused tax credits for which no deferred tax assets have been recognized are attributable to the following: | | |
| - Tax losses (revenue in nature) | 2,876 | 7,369 |
| - Tax losses (capital in nature) | - | - |
| - Unused tax credit | - | - |
| - Deductible temporary differences | - | - |
| Total | **2,876** | **7,369** |

Differences between IFRS and the national tax legislations result in temporary differences between the carrying amount of assets and liabilities with the purpose to prepare financial statements and a tax basis for the income tax calculation. The following tables summarize the components of temporary differences that give rise to deferred income tax assets and liabilities:

| | 1 January 2017 | Deferred income tax income or expense recognized in profit or loss | Deferred income tax expense recognized in other comprehensive income | Tax effect in revaluation of PPE | 31 December 2017 |
|---|---|---|---|---|---|
| **Recognized deferred income tax assets attributable to the following elements:** | | | | | |
| Trade and other receivables | 2,568 | (1,767) | (170) | - | 631 |
| Inventories | 107 | 23 | (7) | - | 123 |
| Property, plant and equipment | 23 | 86 | (13) | - | 96 |
| Trade and other payables | 1,216 | (631) | 130 | - | 715 |
| Advances received | (3) | | 3 | | |
| Tax losses carried forward | 9,572 | (3,386) | (518) | - | 5,668 |
| Less accrued provision | (7,370) | 3,809 | 685 | - | (2,876) |
| Deferred income | 16 | - | (5) | - | 11 |
| Other | (27) | - | (17) | - | (44) |
| Netting with deferred income tax liabilities | (3,879) | 1,996 | 31 | - | (1,852) |
| **Deferred income tax assets** | **2,223** | **130** | **119** | **-** | **2,472** |
| **Recognized deferred income tax liabilities attributable to the following elements:** | | | | | |
| Trade and other receivables | (2,908) | 986 | 151 | - | (1,771) |
| Advances paid and prepaid expenses | (597) | - | (57) | - | (654) |
| Property, plant and equipment | (12,144) | 1,794 | 749 | (3,513) | (13,114) |
| Netting with deferred income tax assets | 3,878 | (1,876) | (223) | - | 1,779 |
| **Deferred income tax liabilities** | **(11,771)** | **904** | **620** | **(3,513)** | **(13,760)** |
| **Total deferred income tax assets and liabilities** | **(9,548)** | **1,034** | **739** | **(3,513)** | **(11,288)** |

Comparative information for 2016:

| | 1 January 2016 | Deferred income tax income or expense recognized in profit or loss | Deferred income tax income or expense recognized in other comprehensive income | Tax effect in revaluation of PPE | 31 December 2016 |
|---|---|---|---|---|---|
| **Recognized deferred income tax assets attributable to the following elements:** | | | | | |
| Trade and other receivables | 2,542 | (29) | 55 | - | 2,568 |
| Inventories | 121 | (5) | (9) | - | 107 |
| Property, plant and equipment | 29 | (3) | (3) | - | 23 |
| Trade and other payables | 1,416 | 17 | (217) | - | 1,216 |
| Advances received | (3) | - | - | - | (3) |
| Tax losses carried forward | 8,678 | 1,134 | (240) | - | 9,572 |
| Less accrued provision | (6,855) | (1,134) | 619 | - | (7,370) |
| Deferred income | 9 | - | 7 | - | 16 |
| Other | 96 | (113) | (10) | - | (27) |
| Netting with deferred income tax liabilities | (2,874) | (939) | (66) | - | (3,879) |
| **Deferred income tax assets** | **3,159** | **(1,072)** | **136** | **-** | **2,223** |
| **Recognized deferred income tax liabilities attributable to the following elements:** | | | | | |
| Trade and other receivables | (1,825) | (1,167) | 84 | - | (2,908) |
| Advances paid and prepaid expenses | 2 | (570) | (29) | - | (597) |
| Property, plant and equipment | (15,757) | 64 | 1,293 | 2,256 | (12,144) |
| Netting with deferred income tax assets | 2,874 | 938 | 66 | - | 3,878 |
| **Deferred income tax liabilities** | **(14,706)** | **(735)** | **1,414** | **2,256** | **(11,771)** |
| **Total deferred income tax assets and liabilities** | **(11,547)** | **(1,807)** | **1,550** | **2,256** | **(9,548)** |

Management assesses whether valuation allowances should be established against deferred tax assets based on consideration of all available evidence, both positive and negative. This assessment considers, among other matters, the nature, frequency and severity of recent losses, forecasts of future profitability, the duration of statutory carry forward periods, the experience with tax attributes expiring unused and tax planning alternatives. In making such judgments, significant weight is given to evidence that can be objectively verified. The Company's ability to realize deferred income tax assets depends on the ability to generate sufficient taxable income within the carry back or carry forward periods provided for in the tax law for each applicable tax jurisdiction.

As at 31 December 2017 deferred income tax assets are shown net of provision for irrecoverable deferred income tax assets at the amount of EUR 5,348 thousand (2016: EUR 9,591 thousand).

## 30 Contingent and deferred liabilities

### *Litigation*

The Group from time to time participates in legal proceedings. However, none of the legal proceedings either separately or in aggregate had significant negative material effect on the Group.

The litigation case with PJSC "Bank Forum" mentioned in the annual report for the year ended 31 December 2016 was solved without penalties.

The legal proceedings of the Group have a positive decrease tendency. During the last year the total credit indebtedness which should be collected from the companies of the Group was decreased from EUR 9,661 thousand as 31 December 2016 to EUR 1,071 thousand as of 31 December 2017.

### Taxation

The taxation system in the Russian Federation is relatively new and is characterized by frequent changes in legislation, official pronouncements and court decisions, which are often unclear, contradictory and subject to varying interpretations by different tax authorities. Taxes are subject to review and investigation by a number of authorities, which have the power to impose severe fines, penalties and interest charges. A tax year remains open for review by the tax authorities during the three subsequent calendar years; however, under certain circumstances a tax year may remain open longer. Recent events within the Russian Federation suggest that the tax authorities are taking a more assertive position in their interpretation and enforcement of tax legislation and it is possible that transactions and activities that have not been challenged in the past may be disputed.

The changes include, *inter alia,* the article 54.1 of Russian Tax Code with increasing attention and requirements to subcontractors relations in terms both of VAT and Profit tax calculations. Still there are no legal cases of applying the new approach to business.

These changes may create tax risks for the business in the Russian Federation.

### *Insurance policies*

The Group applies reasonable approach to risk management and assets safeguarding and mitigate key risks with insurance services.

One of significant insurance contract covers Directors and Officers liability insurance for reimbursement for losses or advancement of defense costs in the event an insured suffers losses as a result of a legal action brought for alleged wrongful acts by Directors and Officers. The insurance contract signed with Allianz Global Corporate & Specialty SE with limit liability of EUR 25 million.

The Company also engaged in the other types of insurance contracts, including property, cargo and civil liability insurance.

The choice of the insurance services providers is usually made based at their high business reputation and rates.

## 31 Capital management policy

Main objectives of the Group's capital management policy are as follows: management of accounts receivable and payable, raw materials and finished goods stocks, as well as healthy capital structure.

The Group has external requirements to the capital in respect of Loan facility to the Syndicate and other loans received by the Company.

According to the most significant Facilities agreement with the Syndicate the following covenants are applied:

- Tangible net worth should not at any time be less than EUR 105,000 thousand;
- the ratio of borrowing to EBITDA in respect of any relevant period will not exceed 3.5 to 1;
- the ratio of EBITDA to interest expenses in respect of any relevant period will not be less than 3.25 to 1.

Borrowing, EBITDA, interest expenses and tangible net worth shall be calculated and interpreted on a consolidation basis in accordance with the IFRS and shall be expressed in EUR.

Capital structure of the Group as of 31 December:

| | **2017** | **2016** |
|---|---|---|
| Total borrowings | 86,556 | 102,286 |
| Less: cash and cash equivalents | (1,416) | (1,044) |
| **Net debt** | **85,140** | **101,242** |
| Total equity | 12,922 | 6,914 |
| **Total capital** | **98,062** | **108,156** |

## 32 Financial risk management

The Company's activities expose it to a variety of financial risks, including foreign exchange, interest rate risks and also market, credit and liquidity risks. The overall risks management program focuses on the minimizing of the potential unfavorable influence of the different kind of risks to the Group's business and operations.

***Market risk***
The Group is exposed to market risks, including the volatility of the global commodity markets, as well as local raw materials markets. Milkiland's management is constantly seeking for the opportunities of establishment of long-term relations with the clients and suppliers in order to mitigate those risks.

***Foreign exchange risk***
Foreign currency risk is a risk of losses resulting from adverse movements in different currency exchange rates against the Group's reporting currency, namely EUR. Foreign currency risk arises from potential future commercial transactions in foreign currencies, and recognition of assets and liabilities denominated in a currencies, other than reporting currency of the Company.

The Group primary exposure to foreign currency risk is related to borrowings, the majority of which are denominated in US dollars, while the lions share of the Groups revenues come in RUB and UAH. The Group's management made several steps in order to mitigate this risk, including by partial transfer of the indebtedness previously denominated in US Dollars to UAH.

As of 31 December 2017 the Group's financial assets and financial liabilities were denominated in the following currencies:

| | EUR | USD | RUB | UAH | PLN | Total |
|---|---|---|---|---|---|---|
| **Financial Assets** | | | | | | |
| Financial receivables trade and other receivables | - | 349 | 4,154 | 4,163 | 378 | 9,044 |
| Cash and cash equivalents | 16 | 58 | 706 | 573 | 63 | 1,416 |
| **Total financial assets** | **16** | **407** | **4,860** | **4,736** | **441** | **10,460** |
| **Financial Liabilities** | | | | | | |
| Loans and borrowings | 8 | 58,580 | 15,236 | 9,651 | 3,081 | 86,556 |
| Financial payables within trade and other payables | 4 | 14,783 | 13,182 | 7,462 | 1,980 | 37,411 |
| **Total financial liabilities** | **12** | **73,363** | **28,418** | **17,113** | **5,061** | **123,967** |

**Comparative information for 2016:**

| | EUR | USD | RUB | UAH | PLN | Total |
|---|---|---|---|---|---|---|
| **Financial Assets** | | | | | | |
| Financial receivables trade and other receivables | - | 3,144 | 5,569 | 5,344 | 374 | 14,431 |
| Cash and cash equivalents | 4 | 122 | 107 | 783 | 28 | 1,044 |
| **Total financial assets** | **4** | **3,266** | **5,676** | **6,127** | **402** | **15,475** |
| **Financial Liabilities** | | | | | | |
| Loans and borrowings | - | 70,237 | 16,309 | 12,596 | 3,144 | 102,286 |
| Financial payables within trade and other payables | - | 9,156 | 10,985 | 9,943 | 2,492 | 32,576 |
| **Total financial liabilities** | **-** | **79,393** | **27,294** | **22,539** | **5,636** | **134,862** |

The following table presents sensitivities of post-tax profit for the year to reasonably possible changes in exchange rates applied at the statement of financial position date relative to the functional currency of the respective Group entities, with all other variables held constant:

| | 2017 | 2016 |
|---|---|---|
| USD strengthening by 10% (2016: 10%) | (934) | (1,725) |
| USD weakening by 10% (2016: 10%) | 934 | 1,725 |
| Euro strengthening by 10% (2016: 10%) | 1 | 665 |
| Euro weakening by 10% (2016: 10%) | (1) | (665) |
| PLN strengthening by 10% (2016: 10%) | 4 | - |
| PLN weakening by 10% (2016: 10%) | (4) | - |
| UAH strengthening by 10% (2016: 10%) | 12 | - |
| UAH weakening by 10% (2016: 10%) | (12) | - |

The exposure was calculated only for monetary balances denominated in currencies other than the functional currency of the respective entity of the Group.

***Credit risk***

Credit risk refers to the risk exposure that a potential financial loss to the Company may occur if counterparty defaults on its contractual obligations. The maximum exposure to credit risk is the value of the assets which might be lost.

Credit risk arises from cash and cash equivalents and credit exposures to accounts receivable. The Company does not have derivative financial assets and available-for-sale investments.

**Cash and cash equivalents.** Cash and cash equivalents are placed in major multinational, Ukrainian, Russian and Polish banks. Analysis by credit quality of bank balances is as follows:

| | 2017 | 2016 |
|---|---|---|
| Ratings by Moody's | | |
| Ba2 | 8 | 45 |
| B1 | - | 38 |
| B2 | 677 | - |
| Caa1 | 29 | - |
| Caa2 | 10 | - |
| E | - | 66 |
| Unrated | 650 | 868 |
| Cash on hand | 42 | 27 |
| **Total cash and cash equivalents** | **1,416** | **1,044** |

**Trade and other financial receivables.** The monitoring and controlling of credit risk is performed by sales department and analyst department of the Company. The credit quality of each new customer is evaluated before the Company provides it with the standard terms of supply, including credit limit and payment delay. The credit quality of customers is assessed taking into account their financial position, past experience and other factors. Customers that do not meet the credit quality requirements are supplied on a prepayment basis only. The Company controls following the credit limits of all existing customers as well as timely settlement of trade and other accounts receivable (note 7). Credit risk exposure mainly depends on the individual characteristics of customers, more particularly customers' default risk.

Trade and other accounts receivable are mainly represented by receivables from customers, which are not aiming to obtain the credit rating in their operating activity.

Quantitative disclosures of the credit risk exposure in relation to financial assets are set out below. Further disclosures regarding trade and other receivables, which are neither past due nor impaired, are provided in note 7.

| | 31 December 2017 | | 31 December 2016 | |
|---|---|---|---|---|
| ***Financial assets*** | **Carrying value** | **Maximum exposure** | **Carrying value** | **Maximum exposure** |
| Cash and cash equivalents | 1,416 | 1,416 | 1,044 | 1,044 |
| Trade and other receivables | 9,044 | 9,044 | 14,431 | 14,431 |
| | **10,460** | **10,460** | **15,475** | **15,475** |

### *Interest rate risk*

Borrowings issued at variable rates expose the Group to cash flow interest rate risk. The Group has no significant interest-bearing assets.

Interest rate risk arises from movements in interest rates which could affect the Company's financial results or the value of the Group's equity. A change in interest rates may cause variations in interest income and expense. The primary objective of the Group's interest rate management is carried out by the corporate finance department.

Monitoring of current market interest and analysis of the Group's interest-bearing position is performed as a part of interest rate risk management procedures. Monitoring is performed taking into consideration refinancing, renewal of existing positions and alternative financing.

At the end of 2017 the Group had approximately 40% (2016: 44%) of its borrowings in fixed rate instruments and 60% (2016: 56%) in variable rate instruments.

### *Liquidity risk*

Liquidity risk is a risk, when the Group is not able to pay all liabilities after maturity date. The Group manages and controls over the liquidity. The Group uses procedures for preparation of budget and forecasting cash flows that provides availability of necessary funds for fulfillment its payment liabilities. Based on the estimated cash flows a decision is made to invest cash funds or attract financing, if necessary. Performance of the credit risk policy management gives the Group sufficient cash to repay its debts on time.

The table below analyses the Company's financial liabilities into relevant maturity groupings based on the remaining period at the statement of financial position to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows, which approximate their fair value:

| | **Up to 6 months** | **6-12 months** | **1 - 3 years** | **3 - 5 years** |
|---|---|---|---|---|
| Trade and other accounts payable (note 14) | 29,235 | - | - | - |
| Borrowings | 63,273 | 12,527 | 9,380 | 1,376 |
| **Total** | **92,508** | **12,527** | **9,380** | **1,376** |

Comparative information at 31 December 2016 is as follows:

| | **Up to 6 months** | **6-12 months** | **1 - 3 years** | **3 - 5 years** |
|---|---|---|---|---|
| Trade and other accounts payable (note 14) | 27,587 | - | - | - |
| Borrowings | 62,070 | 25,223 | 14,993 | - |
| **Total** | **89,657** | **25,223** | **14,993** | **-** |

***Financial instruments carried at fair value***. The Group does not have available-for-sale investments. Cash and cash equivalents are carried at amortized cost which approximates current fair value.

***Financial assets at amortized cost***. An estimated fair value of instruments at fixed interest rate is based upon the method of discounted estimated future cash flows applying interest rates effective at the borrowed funds market for new instruments that provide for the same credit risk and the same maturity term. Discount rates depend on the credit risk from a contractor. The carrying amount of buyers and customers' accounts receivable equals to their fair value.

***Financial liabilities at amortized cost***. Fair value is evaluated based upon market quotations, if any. An estimated fair value of instruments with fixed interest rate and defined maturity date that do not have market quotation, is based on the discounting estimated cash flows applying interest rates for new instruments with the same credit risk and defined maturity date. The carrying amount of financial liabilities equals to their fair value.

## 33 Earnings per share

| | 2017 | 2016 |
|---|---|---|
| *Numerator* | | |
| Earnings used in basic and diluted EPS | (7,672) | (38,804) |
| *Denominator, in thousand* | | |
| Weighted average number of shares used in basic and diluted EPS | 31,250 | 31,250 |
| Earning per share, EUR | (0.25) | (1.24) |

## 34 Audit fees

The fees listed below relate to the procedures applied to the company and its consolidated group entities by BDO Audit & Assurance B.V., the Netherlands, the external auditor as referred to in Section 1(1) of the Dutch Accounting Firms Oversight Act, as well as by other Dutch and foreign-based BDO individual partnerships and legal entities, including their tax services and advisory groups. Remuneration to BDO Audit & Assurance B.V. was accrued in 2017 for audit services of the financial statements 2016.

**Information for 2017, EUR thousand:**

| | BDO Audit & Assurance B.V. | Member firms/affiliates | Total |
|---|---|---|---|
| **Charged to administrative expenses** | | | |
| Audit annual accounts | 100 | 106 | **206** |
| **Total** | **100** | **106** | **206** |

**Comparative information for 2016, EUR thousand:**

| | BDO Audit & Assurance B.V. | Member firms/affiliates | Total |
|---|---|---|---|
| **Charged to administrative expenses** | | | |
| Audit annual accounts | | | |
| Tax advisory fees | 52 | 106 | **158** |
| **Total** | **52** | **106** | **158** |

## 35 Subsequent events

***Restructuring of the Group's indebtedness***

Since the beginning of 2014 the Group has been continuing the negotiations with a main creditors of Milkiland, namely UniCredit Bank Austria AG and ZAO Raiffeisenbank, aimed at signing of long-term Restructuring agreement of debt under Syndicated Loan Facility Agreement provided by those banks.

Accept that, Milkiland has a conformation of engagement with Alvarez and Marshal Capital LLC including the scope of services: A&M shall provide consulting and advisory to the Company in connection with their efforts in seeking to the restructure its Syndicated Loan Facility.

***Entering of the new markets***

In 2018 Milkiland Ukraine with the support of Milkiland Intermarket, both the subsidiaries of Milkiland Group, has continuing the efforts aimed at searching of new export markets for Milkiland's products. In particular, new products are promoting in the market of Israel, China, Arabian countries markets.

# COMPANY FINANCIAL STATEMENTS AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2017 /Milkiland N.V./

(All amounts in euro thousands unless otherwise stated)

| | Notes | 31 December 2017 | 31 December 2016 |
|---|---|---|---|
| **ASSETS** | | | |
| **Current Assets** | | | |
| Cash and cash equivalents | | 78 | 64 |
| Amounts due from group companies | 5 | 76,849 | 79,502 |
| Other receivables and prepayments | 5 | 63 | 48 |
| Other taxes receivable | 5 | 5 | 3 |
| | | **76,995** | **76,617** |
| **Fixed assets** | | | |
| Goodwill | 3 | 1,381 | 1,490 |
| Investments in subsidiaries | 4 | 17,544 | 11,777 |
| | | **18,925** | **13,267** |
| **TOTAL ASSETS** | | **95,920** | **92,884** |
| **LIABILITIES AND EQUITY** | | | |
| **Current liabilities** | | | |
| Amounts due to group companies | 7 | 22,457 | 21,833 |
| Loans and borrowings | 8 | 48,845 | 55,573 |
| Other payables | 7 | 12,926 | 9,672 |
| Other taxes payables | | - | 1 |
| | | **84,228** | **87,079** |
| **Non-Current Liabilities** | | | |
| Loans and borrowings | | - | - |
| | | **-** | **-** |
| **TOTAL LIABILITIES** | | **84,228** | **87,079** |
| **Shareholder's equity** | | | |
| Issued and paid-up share capital | 6 | 3,125 | 3,125 |
| Share premium | 6 | 48,687 | 48,687 |
| Revaluation reserve | 6 | 79,403 | 69,208 |
| Currency translation reserve | 6 | (38,042) | (34,297) |
| Retained earnings and inappropriate result | 6 | (81,481) | (80,918) |
| **Total equity** | | **11,692** | **5,805** |
| **TOTAL LIABILITIES AND EQUITY** | | **95,920** | **92,884** |

(All amounts in euro thousands unless otherwise stated)

| | Notes | 2017 | 2016 |
|---|---|---|---|
| Revenue from Group companies | | 1,132 | 247 |
| Administrative expenses | 9 | (1,083) | (957) |
| Other expenses | | - | - |
| **Operating loss** | | **49** | **(710)** |
| Finance income | 10 | 5,429 | 5,302 |
| Finance expenses | 11 | (5,245) | (5,255) |
| Dividends from subsidiaries | | - | - |
| **Profit / (loss) before income tax** | | **233** | **(663)** |
| Income tax | | - | (87) |
| Share of profit of participating interests, after income tax | | (7,905) | (38,057) |
| **(Loss) / profit for the year** | | **(7,672)** | **(38,807)** |

## Notes to the company financial statements

### 1. General

Reporting entity Milkiland N.V. (the “Company”) was incorporated on 13 July 2007. It changed its Articles of Association on 23 May 2008 amending its legal form to public limited liability company. The financial statements of the Company are included in the consolidated statements of Milkiland N.V.

### 2. Significant accounting policies

***Basis of preparation***

The Company financial statements have been prepared in accordance with the provisions of Part 9, Book 2, of the Dutch Civil Code. The Company uses the option of Article 362.8 of Part 9, Book 2, of the Dutch Civil Code to prepare the Company financial statements, using the same accounting policies as in the consolidated financial statements. Valuation is based on recognition and measurement requirements of accounting standards adopted by the EU (i.e., only IFRS that is adopted for use in the EU at the date of authorization) as explained further in the notes to the consolidated financial statements.

***Foreign currency***

Assets and liabilities in foreign currencies are translated at the official rates of exchange ruling on statement of financial position dates. Transactions in foreign currencies are translated at the applicable exchange rate on the transaction dates. The resulting exchange differences are accounted for in the statement of comprehensive income.

The financial statements of the foreign subsidiaries are translated at the rates of exchange prevailing at the end of the accounting periods. Differences resulting from the translation of assets and liabilities of the group of companies at the rates prevailing at the beginning and at the end of the year are shown as a separate item in shareholders' equity.

***Financial fixed assets***

Subsidiaries and other participating interests in which significant influence may be exerted are stated at net asset value, using the equity method. The net asset value is calculated on the basis of the accounting policies included in these financial statements. Participating interests whose figures cannot be brought in line with these policies due to insufficient information, are valued based on the financial statements of the participating interest involved. Participating interests with a net asset value of less than nil are carried at nil. If the investing company is liable for the participating interest's debts, a provision will be formed.

***Receivables***

Accounts receivable are shown after deduction of a provision for bad and doubtful debts where appropriate.

The accounts receivable have a maturity date due within one year.

***Cash and cash equivalents***

Cash and bank balances are freely disposable, unless stated otherwise.

***Current liabilities***

The short term liabilities are due within one year.

***Bank borrowings***
Bank borrowings are initially recognized at fair value net of any transaction costs directly attributable to the issue of the instrument. Such interest bearing liabilities are subsequently measured at amortized cost using the effective interest rate method, which ensures that any interest expense over the period to repayment is at a constant rate on the balance of the liability carried in the statement of financial position.

***Profit of participating interests***. The share of profit of participating interests consists of the share of the Company in the results of these participating interests. Results on transactions, where the transfer of assets and liabilities between the Company and its participating interests and mutually between participating interests themselves, are not recognized.

## 3. Goodwill

The goodwill of EUR 1,381 thousand (2016: EUR 1,490 thousand) is a result of a subsidiary acquisition and recognized as an asset. Goodwill is initially recognized as an asset during the primary evaluation. Impairment testing is performed annually.

For details see note 10 in consolidated financial statements.

## 4. Investments in participating interests

| | **31 December 2017** | **31 December 2016** |
|---|---|---|
| JSC Ostankino Dairy, Russia | 30,682 | 25,870 |
| LLC Milkiland Ukraine, Ukraine | 1,755 | (5,207) |
| LLC Milkiland RU, Russia | 2,972 | 3,410 |
| LLC Milkiland N.V, Ukraine | (1,799) | (1,962) |
| Milkiland Intermarket (CY) LTD, Cyprus | (2,477) | (2,824) |
| MLK Finance Limited, Cyprus | (7,867) | (3,919) |
| Milkiland EU sp. z.o.o., Poland | (5,722) | (3,591) |
| **Total investments in participating interests** | **17,544** | **11,777** |

Movement during the year is the following:

| | **2017** | **2016** |
|---|---|---|
| At 1 January | 11,774 | 41,907 |
| Profit for the year | (7,905) | (38,057) |
| Currency translation differences | (3,630) | 15,885 |
| Acquisition of minority shares in Ostankino Dairy, Russia | - | - |
| Dividends declared by subsidiaries | - | (1,738) |
| Revaluation of PPE | 17,305 | (6,220) |
| Investments into subsidiaries | - | - |
| **At 31 December** | **17,544** | **11,777** |

For the period from 1 January 2017 to 31 December 2017 the Company had the following direct subsidiaries:

| Name | Country of incorporation | Share of ownership<br>31 December 2017 | <br>31 December 2016 |
|---|---|---|---|
| MLK Finance Limited | Cyprus | 100.0% | 100.0% |
| Milkiland Intermarket (CY) LTD | Cyprus | 100.0% | 100.0% |
| Milkiland EU sp. z.o.o. | Poland | 100.0% | 100.0% |
| JSC Ostankino Dairy | Russia | 100.0% | 100.0% |
| LLC Milkiland RU | Russia | 100.0% | 100.0% |
| LLC Milkiland N.V | Ukraine | 100.0% | 100.0% |
| LLC Milkiland Ukraine | Ukraine | 100.0% | - |
| LLC Moloko-Kraina | Ukraine | 100.0% | - |
| LLC Milkiland Agro | Ukraine | 99.0% | - |
| DE Milkiland Ukraine | Ukraine | - | 100.0% |

## 5. Receivables

| | 31 December 2017 | 31 December 2016 |
|---|---|---|
| *Amounts due from group companies* | | |
| MLK Finance Limited | 63,508 | 67,121 |
| Milkiland EU sp. z.o.o. | 12,266 | 11,619 |
| LLC Uspih-Mena-Plus | 676 | 354 |
| JSC Ostankino Dairy, Russia | 288 | 288 |
| Milkiland Intermarket (CY) LTD | 110 | 120 |
| LLC Milkiland RU, Russia | 1 | - |
| **Total amounts due from group companies** | **76,849** | **79,502** |
| | | |
| *Other receivables and prepayments* | | |
| Advances issued | 64 | 48 |
| Other receivables | 39 | 40 |
| Allowance for doubtful debts | (40) | (40) |
| **Total other receivables and prepayments** | **63** | **48** |
| *Taxes and social security* | | |
| Payroll related taxes | 5 | 2 |
| **Total taxes receivable** | **5** | **2** |

At 31 December 2017 accounts receivable from MLK Finance Limited represented by EUR 50,442 thousand (2016: EUR 55,573 thousand) of loan issued to this company in October 2012 through transferring of loans previously issued to Ukrainian subsidiaries of the Group and accumulative accrued interests of EUR 13,066 thousand (2016: EUR 9,747 thousand).

## 6. Shareholder's equity

The authorized share capital of the company amounts to EUR 5,000,000 consisting of 50,000,000 ordinary shares with a nominal value of EUR 0.10 each.

Movements in equity during the year may be specified as follows:

| | Issued and paid-up share capital | Share premium | Currency translation reserve | Revaluation reserve | Retained earnings and unappropriated result | Total |
|---|---|---|---|---|---|---|
| **Balance as at 1 January 2016** | **3,125** | **48,687** | **(48,651)** | **79,866** | **(48,377)** | **34,650** |
| **Total comprehensive income for the year** | - | - | 14,354 | (4,395) | (38,804) | (28,845) |
| Realised revaluation reserve, net of income tax | - | - | - | (6,263) | 6,263 | - |
| **Balance as at 31 December 2016** | **3,125** | **48,687** | **(34,297)** | **69,208** | **(80,918)** | **5,805** |
| **Total comprehensive income for the year** | - | - | (3,745) | 17,304 | (7,672) | 5,887 |
| Realised revaluation reserve, net of income tax | - | - | - | (7,109) | 7,109 | - |
| **Balance as at 31 December 2017** | **3,125** | **48,687** | **(38,042)** | **79,403** | **(81,481)** | **11,692** |

## 7. Trade and other payables

| | 31 December 2017 | 31 December 2016 |
|---|---|---|
| *Amounts due to Group companies* | | |
| Milkiland Corporation | 22,451 | 21,826 |
| LLC Milkiland N.V | 6 | 7 |
| **Total amounts due to Group companies** | **22,457** | **21,833** |
| | | |
| *Other payables* | | |
| Other accounts payable | 163 | 18 |
| Trade payables | - | 130 |
| Interest payable | 12,466 | 8,995 |
| Wages and salaries payable | 297 | 529 |
| **Total other payables** | **12,926** | **9,672** |
| *Other taxes payable* | | |
| Payroll related taxes | - | (1) |
| **Total taxes payable** | **-** | **(1)** |

Accounts payable to Milkiland Corporation include a financial aid from Milkiland Corporation at the amount of EUR 22,451 thousand (2016: EUR 21,826 thousand). This financial aid to Milkiland Corporation is free of interest rates.

## 8. Loans and borrowings

Since the beginning of 2017 the Group has been continuing the negotiations with a main creditors of Milkiland, namely UniCredit Bank Austria AG and ZAO Raiffeisenbank, aimed at signing of long-term Restructuring agreement of debt under Syndicated Loan Facility Agreement provided by those banks.

The total sum of the Group's indebtedness to syndicate as at 31 December 2017 stood at USD 58,580 thousand, all amount due.

## 9. Administrative expenses

| | 2017 | 2016 |
|---|---|---|
| Wages and salaries | 497 | 358 |
| Tax advisory and audit fee | 405 | 1 |
| Consultancy fee | 61 | 477 |
| Other expenses | 120 | 121 |
| **Total administrative expenses** | **1,083** | **957** |

Audit fees are disclosed in note 34 to consolidated financial statements.

## 10. Finance income

| | 2017 | 2016 |
|---|---|---|
| MLK Finance Limited | 4,750 | 4,632 |
| Milkiland EU sp. z.o.o. | 679 | 670 |
| **Total finance income** | **5,429** | **5,302** |

## 11. Finance expenses

| | 2017 | 2016 |
|---|---|---|
| Bank borrowings | 4,822 | 5,492 |
| Finance foreign exchange loss, net | 423 | (237) |
| **Total finance expenses** | **5,245** | **5,255** |

## 12. Remuneration of Board of Directors members

Remuneration of Board of Directors members is disclosed in Corporate Governance Report included in Annual report.

**Board of Directors of Milkiland N.V.**

**Amsterdam, 27 April 2018**

| | | |
|---|---|---|
| **A. Yurkevych** | **O. Yurkevich** | **O. Rozhko** |
| **V. Rekov** | **W.S. van Walt Meijer** | **G.C. Logusch** |
| **P. Sheremeta** | | |

## INDEPENDENT AUDITOR'S REPORT

To: The shareholders and Board of Directors of Milkiland N.V.

### Report on the audit of the financial statements 2017 included in the annual report

OUR OPINION

We have audited the financial statements 2017 of Milkiland N.V., based in Amsterdam. The financial statements include the consolidated financial statements and the company financial statements.

In our opinion:

- the accompanying consolidated financial statements give a true and fair view of the financial position of Milkiland N.V. as at 31 December 2017, and of its result and its cash flows for 2017 in accordance with the International Financial Reporting Standards as adopted by the European Union (EU-IFRS) and with Part 9 of Book 2 of the Dutch Civil Code.
- the accompanying company financial statements give a true and fair view of the financial position of Milkiland N.V. as at 31 December 2017, and of its result for 2017 in accordance with Part 9 of Book 2 of the Dutch Civil Code.

The consolidated financial statements comprise:

1 the consolidated statement of financial position as at 31 December 2017;
2 the following consolidated statements for 2017: the consolidated income statement, the consolidated statements of comprehensive income, the consolidated statement of cash flows and the consolidated statement of changes in equity; and
3 the notes to the consolidated financial statements comprising a summary of the significant accounting policies and other explanatory information.

The company financial statements comprise:

1 the company statement of financial position as at 31 December 2017;
2 the company income statement for 2017; and
3 the notes to the company financial statements comprising a summary of the accounting policies and other explanatory information.

BASIS FOR OUR OPINION

We conducted our audit in accordance with Dutch law, including the Dutch Standards on Auditing. Our responsibilities under those standards are further described in the 'Our responsibilities for the audit of the financial statements' section of our report.

We are independent of Milkiland N.V. in accordance with the EU Regulation on specific requirements regarding statutory audit of public-interest entities, the Wet toezicht accountantsorganisaties (Wta, Audit firms supervision act), the Verordening inzake de onafhankelijkheid van accountants bij assurance-opdrachten (ViO, Code of Ethics for Professional Accountants, a regulation with respect to independence) and other relevant independence regulations in the Netherlands. Furthermore we have complied with the Verordening gedrags- en beroepsregels accountants (VGBA, Dutch Code of Ethics).

We believe the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.



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MATERIAL UNCERTAINTY RELATED TO GOING CONCERN

We draw your attention to note 1 of the consolidated financial statements regarding the going concern assumptions.

Milkiland N.V. conducts significant part of its operations in Russia and Ukraine. The closure of the traditional Russian export market for the Ukrainian and Polish subsidiaries, deep devaluation of Russian Ruble and Ukrainian Hryvnia, decline of the demand for dairy in Russia and Ukraine had an adverse effect in Milkiland's financial position and performance in previous years. As from 2017 the economies of Russia and Ukraine started to recover. Both the timing and the dynamics of this process are uncertain, therefore this may adversely affect Milkiland's operations and financial performance.

As a significant amount of the external loans are in US Dollar and due to the earlier deterioration of the Hryvnia and Rubble against the US Dollar the company is no longer able to meet the covenants from the banks and scheduled loan repayments. Given the breach of covenants the bank is entitled to exercise certain rights among acceleration repayments of the loans. This could materially affect the ability of Milkiland to continue as a going concern. The company is dependent on the willingness of the banks to allow time for refinancing of the debts and not enforce early repayment. Also, in the course of 2017 Milkiland has initiated the voluntary liquidation procedure for its OJSC "Ostankino Dairy" factory. The reason for this is that OJSC Bank "Vozrogdenie" has started a bankruptcy petition against OJSC "Ostankino Dairy".

The ability of the company to continue its operations there is dependent on coming negotiations during the bankruptcy procedures and finding a mutually acceptable solution of the settlement of the indebtedness to Ostankino's Creditors.

These conditions indicate the existence of material uncertainties which may cast significant doubt about the company's ability to continue as a going concern. Our opinion is not modified in respect of this matter.

MATERIALITY

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 financial statements. The materiality affects the nature, timing and extent of our audit procedures and the evaluation of the effect of identified misstatements on our opinion.

Based on our professional judgement we determined the materiality for the financial statements as a whole at EUR 1.400.000. The materiality is based on 1% of total revenue as reflected in the 2016 financial statements and we have reassessed the materiality based on the final figures for 2017. We have applied this benchmark based upon our analysis of the mutual interests of the users of these financial statements. Based upon our analysis we conclude that revenue is an important key figure to determine the financial performance of Milkiland N.V. We identified - amongst others - the shareholders and loan holders as important group of users. We have also taken into account misstatements and/or possible misstatements that in our opinion are material for the users of the financial statements for qualitative reasons.

We agreed with the Board of Directors that misstatements in excess of EUR 35.000, which are identified during the audit, would be reported to them, as well as smaller misstatements that in our view must be reported on qualitative grounds.

SCOPE OF THE GROUP AUDIT

Milkiland N.V. is at the head of a group of entities. The financial information of this group is included in the consolidated financial statements of Milkiland N.V.

Our group audit mainly focused on significant group entities. We consider a component significant when:

- it is of individual financial significance to the group; or
- the component, due to its specific nature or circumstances, is likely to include significant risks of material misstatement, whether due to fraud or error of the group financial statements.

To this extent we:

- used the work of component auditors in the Ukraine, the Russian Federation and in Poland. Given the location of the representative office of Milkiland N.V. being situated in Kiev, Ukraine, the Ukrainian component auditor included this in their scope upon our request. Given the significance of the Ukrainian, Russian and Poland entities we have performed file reviews on site on the work of the component auditor in order to obtain sufficient assurance to be able to rely on the work of the component auditor; and
- performed review procedures or specific audit procedures at other group entities.

By performing the procedures mentioned above at the components, together with additional procedures at group level, we have been able to obtain sufficient and appropriate audit evidence about the group's financial information to provide an opinion about the consolidated financial statements.

### OUR KEY AUDIT MATTERS

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements. We have communicated the key audit matters to the Board of Directors. The key audit matters are not a comprehensive reflection of all matters discussed.

These matters were addressed in the context of our audit of the financial statements as a whole and in forming our opinion thereon, and we do not provide a separate opinion on these matters. In addition to the matter described in the *Material uncertainty related to going concern* section of our report, we have determined the matters described below to be the key audit matters to be communicated in our report.

The key audit matters are:

- Occurence and cutoff of revenue;
- Valuation of Property, Plant and equipment; and
- Transition as auditors including the audit of the opening balances.

The key audit matters are detailed below.

| Description of the Key Audit Matter | Our audit response regarding the Key Audit Matter |
|---|---|
| ***Occurrence and cutoff of revenue***<br><br>Revenue amounts to € 140 million (2016: € 147 million).<br><br>We consider revenue recognition and in particular occurrence and cutoff to be a key audit matter as revenue is one of the key factors for the performance of Milkiland. In accordance with the Auditing Standards we identified a fraud risk related to the tenancy to overstate revenue and/or understate the amount of discount earned by customers. The revenue accounting policies are specified in note 2 to the financial statements. | In order to obtain sufficient audit evidence our audit procedures included and our component auditors performed, amongst others, the following procedures:<br>- Evaluation of relevant internal controls and determine existence of internal controls relating to the revenue and receivables process;<br>- Performing inventory counts at year end;<br>- Performing substantive audit work on the appropriate allocation of revenue to the correct period (cut off testing);<br>- Performing reconciliation between delivery of goods and revenue recognized;<br>- Performing analytical work on revenue per |

<table>
<tr><td></td><td>month and per customer;<br>- Performing sample tests on contracts with supermarkets and retailers in order to assess the completeness of discounts recognized;<br>- Performing post balance sheet date testing on any credit invoices issues or amounts paid to verify whether these related to discount arrangements for 2017;<br>- Performing substantive work whether intercompany sales transactions are at arm’s length and whether profits are properly eliminated when unrealized;<br>- Performing details tests on manual journal entries posted around yearend in relation to recognized revenue.</td></tr>
<tr><td>Valuation of property, plant and equipment<br><br>The account property, plant and equipment amounts to € 100 million, being 62% of the total assets.<br><br>Property, plant and equipment is stated at fair value in accordance with IAS 16 Property, plant and equipment and IFRS 13 Fair value measurement. Fair value is determined by external appraisers who use either the market or cost approach for determining fair value.<br><br>Valuation of property and equipment is performed frequently enough to ensure that the fair value of a revalued asset does not differ materially from its carrying amount. Fair value is based on the valuations by external independent appraisal agencies.<br><br>Management’s estimates are required in order to determine the compensation amount for a cash generating unit. These estimates are complex and require significant judgement of management, such as:<br>• identification of the cash generating unit;<br>• the model used calculating the fair value;<br>• the applied interest and cost of capital (hereafter: WACC).<br><br>The estimations including the applied methodology may have significant effect on the fair value and impairment amount of property, plant and equipment. Based upon the size of the property, plant and equipment and significant judgements underlying the fair value calculation, we identified the valuation of property, plant and equipment as a key audit matter.</td><td>We have – together with our component auditor – applied a substantive audit approach regarding the valuation of property, plant and equipment.<br><br>To mitigate the audit risk we held a robust discussion with management relating to their point of view on the valuation of property plant and equipment and:<br>• tested the appropriate choice for determining the cash generating unit;<br>• tested the applied model including the appropriate use of formulas;<br>• agreed the input variables relating to the future cash flows with audited 2017 financial information;<br>• evaluated the cash flow forecasts based upon:<br>  o back-testing prior forecasts; and<br>  o challenging the cash flow forecast based upon available information, such as market developments;<br>• tested the parameters used, such as while determining the WACC based upon publicly available market information;<br>• included a valuation expert to validate the appropriate valuation method and consistent use of the discount rate, the long term growth percentage and other assumptions used with available market data; and<br>• compared the outcome of the valuation to the value per the financial statements..</td></tr>
</table>

| | |
|---|---|
| We refer to Note 11 to the financial statements for further disclosure on the valuation of Property, Plant and Equipment. | We evaluated the disclosure in the financial statements, in particular note 2 (Summary of significant accounting policies) and 11 (Property, plant and equipment and intangible assets) for compliance with IAS 16 *Property, plant and equipment* and IFRS 13 *Fair value measurement*. |
| ***Transition as auditors including the audit of the opening balances***<br><br>**During an initial audit the auditor is required to perform certain** additional **procedures to obtain a** sufficient **level of knowledge of the entity and to** enable the auditor to adequately determine the audit planning and audit approach.<br><br>**The procedures are also aimed to obtain sufficient and appropriate audit evidence related to the opening balance** and accounting policies applied and whether changes have be**en properly processed and disclosed.**<br><br>**As a consequence of the change of auditor the risk exists that insufficient** audit evidence is obtained relating to the opening balance. As a result, this is defined as a key audit matter. | Prior to becoming the company's auditors, we performed the following procedures, among other:<br>- Close interaction with the previous auditor, including a process of file review and formal hand over procedures as prescribed by our professional standards;<br>- Performed audit procedures to test the opening balances;<br>- Evaluation of key accounting positions and audit matters from prior years;<br>- Review of management's control documentation to assist us in obtaining and understanding of the company's financial reporting and business processes.<br><br>We discussed and agreed our audit plan with the Board of Directors. |

**Report on the other information included in the annual report**

In addition to the financial statements and our auditor's report thereon, the annual report contains other information that consists of:

- Five year summary on financial highlights and ratios;
- CEO and Chairman's statement;
- Report of the board of directors on operations for the year 2017;
- Corporate governance report;
- the other information as required by Part 9 of Book 2 of the Dutch Civil Code; and
- the other information as included in the table of contents of the annual report 2017.

Based on the following procedures performed, we conclude that the other information:

- is consistent with the financial statements and does not contain material misstatements;
- contains the information as required by Part 9 of Book 2 of the Dutch Civil Code.

We have read the other information. Based on our knowledge and understanding obtained through our audit of the financial statements or otherwise, we have considered whether the other information contains material misstatements.

By performing these procedures, we comply with the requirements of Part 9 of Book 2 of the Dutch Civil Code and the Dutch Standard 720. The scope of the procedures performed is substantially less than the scope of those performed in our audit of the financial statements.

The Board of Directors is responsible for the preparation of the other information, including the management board report in accordance with Part 9 of Book 2 of the Dutch Civil Code and other information as required by Part 9 of Book 2 of the Dutch Civil Code.

**Report on other legal and regulatory requirements**

ENGAGEMENT

We were appointed by the Board of Directors as auditor of Milkiland N.V. on November 10, 2017 for the audit for the year 2017.

NO PROHIBITED NON-AUDIT SERVICES

We have not provided prohibited non-audit services as referred to in Article 5(1) of the EU Regulation on specific requirements regarding statutory audit of public-interest entities.

**Description of responsibilities regarding the financial statements**

RESPONSIBILITIES OF THE EXECUTIVE MEMBERS OF THE BOARD OF DIRECTORS AND THE NON-EXECUTIVE MEMBERS OF THE BOARD OF DIRECTORS FOR THE FINANCIAL STATEMENTS

The executive members of the Board of Directors is responsible for the preparation and fair presentation of the financial statements in accordance with EU-IFRS and Part 9 of Book 2 of the Dutch Civil Code. Furthermore, the executive members of the Board of Directors is responsible for such internal control as the executive members of the Board of Directors determines is necessary to enable the preparation of the financial statements that are free from material misstatement, whether due to fraud or error.

As part of the preparation of the financial statements, the executive members of the Board of Directors is responsible for assessing the company's ability to continue as a going concern. Based on the financial reporting frameworks mentioned, the executive members of the Board of Directors should prepare the financial statements using the going concern basis of accounting unless the executive members of the Board of Directors either intends to liquidate the company or to cease operations, or has no realistic alternative but to do so.

The executive members of the Board of Directors should disclose events and circumstances that may cast significant doubt on the company's ability to continue as a going concern in the financial statements.

The non-executive members of the Board of Directors is responsible for overseeing the company's financial reporting process.

OUR RESPONSIBILITIES FOR THE AUDIT OF THE FINANCIAL STATEMENTS

Our objective is to plan and perform the audit engagement in a manner that allows us to obtain sufficient and appropriate audit evidence for our opinion.

Our audit has been performed with a high, but not absolute, level of assurance, which means we may not detect all material errors and fraud during our audit.

A more detailed description of our responsibilities is set out in the appendix to our report.

Zaltbommel, April 30, 2018

accon avm controlepraktijk B.V.

On behalf:

w.s.

W.J. Warmerdam MSc

Registeraccountant

**APPENDIX TO OUR AUDITOR'S REPORT ON THE FINANCIAL STATEMENTS 2017 OF MILKILAND N.V.**

In addition to what is included in our auditor's report we have further set out in this appendix our responsibilities for the audit of the financial statements and explained what an audit involves.

We have exercised professional judgement and have maintained professional scepticism throughout the audit, in accordance with Dutch Standards on Auditing, ethical requirements and independence requirements. Our audit included among others:

- identifying and assessing the risks of material misstatement of the financial statements, whether due to fraud or error, designing and performing audit procedures responsive to those risks, and obtaining 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;
- obtaining 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 company's internal control;
- compiling a team with sufficient specialized knowledge and expertise. In the component auditor team a valuation specialist is included;
- evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Board of Directors;
- concluding on the appropriateness of the Board of Directors 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 company'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 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 a company to cease to continue as a going concern;
- evaluating the overall presentation, structure and content of the financial statements, including the disclosures;
- evaluating whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

Because we are ultimately responsible for the opinion, we are also responsible for directing, supervising and performing the group audit. In this respect we have determined the nature and extent of the audit procedures to be carried out for group entities. Decisive were the size and/or the risk profile of the group entities or operations. On this basis, we selected group entities for which an audit or review had to be carried out on the complete set of financial information or specific items.

We communicate with the Board of Directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant findings in internal control that we identify during our audit. In this respect we also submit an additional report to the Board of Directors in accordance with Article 11 of the EU Regulation on specific requirements regarding statutory audit of public-interest entities. The information included in this additional report is consistent with our audit opinion in this auditor's report.

We provide the 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 the key audit matters: those matters that were of most significance in the audit of the financial statements. 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, not communicating the matter is in the public interest.

# CORPORATE INFORMATION

## The Netherlands

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